



CITY OF MORGAN HILL

CITY COUNCIL STAFF REPORT

MEETING DATE: June 3, 2020

PREPARED BY: Christie Thomas,
APPROVED BY: City Manager

APPROVE RE-SUBORDINATION OF EXISTING JASMINE SQUARE APARTMENTS CITY LOANS

RECOMMENDATION(S)

Approve re-subordination of existing City affordable housing loans necessitated by refinance of senior project loan, allowing developer to pay off balloon payment, lower interest rate, and pay \$150,000 towards City loans.

COUNCIL PRIORITIES, GOALS & STRATEGIES

Ongoing Priorities

Supporting Our Youth
Seniors
and Entire Community
Preserving and Cultivating Public Trust
Enhancing Diversity and Inclusiveness

2020-2021 Strategic Priorities

Financial Sustainability

GUIDING DOCUMENTS

General Plan/Housing Element

REPORT NARRATIVE:

Background

In 2005 and 2006, the Redevelopment Agency of the City of Morgan Hill provided two affordable housing loans of \$3,250,000 and \$156,350, respectively, (collectively, the City Loans) to the partnership Church & Monterey Road Associates, controlled by Eden Housing, Inc. (the Developer) for the development of Jasmine Square Apartments. Jasmine Square is a 72-unit affordable housing complex, of which 71 units benefit low and very-low income households, with 1 unit as the manager's unit (collectively, the Project). The City Loans and Regulatory Agreements that income-restrict the Property have an initial term of 55-years from completion of the Project. The City Loans mature in 2045 and 2046, respectively. The Project financing also consists of a senior bank loan in the amount of \$3,473,741, which matures on October 1, 2020.

In 2005, the Developer completed the Project and since that time has been managing the Project in accordance with the terms and conditions of all lenders who provided financing. In March 2020, the Developer notified the City (Attachment 1) of their intent to refinance the Project's senior loan in order to accomplish several goals including; 1) repayment of the senior loan which matures on October 1, 2020, at which point a balloon payment of \$3,391,627 is required, 2) securing a lower interest rate of 3.54%,

rather than the current loan of 6.9%, on a new loan, and 3) making a payment on City loans in the amount of \$150,000 to reduce existing debt on the Project.

Developer Proposal

As a subordinate lender for the Project, the City must consent to the transaction before the Developer may take steps to refinance. Through the refinance process, the Developer will seek to lower the Project's interest rate from 6.9% to 3.54%. This rate reduction will result in approximately \$147,000 in additional annual cash flow from avoided debt service payments. The Developer proposes to set aside this additional cash flow in the replacement reserve account to make necessary short-term capital improvements to the Project.

Through the refinance process, the Developer seeks to secure a new loan of \$4,000,000, with an interest rate at 3.54%, which requires monthly payments of \$18,051, and a 10-year term with 30-year amortization. Of this total amount, the Developer proposed the following allocations: 1) approximately \$3,473,741 would pay off the existing first mortgage in its entirety, 2) other transaction related costs estimated at \$109,000, 3) secure Capitalized Replacement Reserves in the amount of \$255,259, 4) Contingency in the amount of \$12,000, and 5) \$150,000 disbursed to City for partial repayment of City Loans. The Developer is not requesting cash-out proceeds from the refinance. The new financing is proposed to be underwritten at a 1.5 debt service coverage ratio.

City Staff Recommendation

City staff supports the Developer's intent to refinance in order to secure a lower interest rate, preserve property level cash flow for capital improvements and enhance the ability to fund rehabilitation. Most notably, the Developer is proactively trying to preserve the condition of the Project.

Refinancing and restructuring of debt for affordable housing projects is common, and the City has significant experience with charting subordination policy which protects the affordable housing assets. This request is consistent with that policy goal. The proposed refinancing is beneficial for the City and the Project because the annual savings from debt service will be used for physical improvements to the Project, to repay a portion of the City Loans, and to support affordable housing developers like Eden Housing.

The terms proposed allow for shared benefits for both City and Developer and are included in the table below:

The table below reflects this proposed breakdown of the Developer's new financing. All numbers are preliminary and subject to change due to potential changes in financing terms.

<u>USES</u>	New First Mortgage	% of Total
Total	\$4,000,000	100%

Repayment of Existing First Mortgage	\$3,473,741	86.8%
Transaction related costs	\$109,000	2.7%
Partial Repayment of City Loans	\$150,000	3.8%
Capitalized Replacement Reserve	\$255,259	6.4%
Contingency	\$12,000	0.3%
Surplus/(Deficit)	\$0	

Staff recommends City Council approve re-subordination and City loan payment in the amount of \$150,000 of existing Jasmine Square Apartments City loans so that Developer has the ability to refinance Senior Loan to pay off balloon payment, lower interest rate, and contribute to the project's Capitalized Replacement Reserve fund.

COMMUNITY ENGAGEMENT:

This report is intended to inform the Morgan Hill Community of the proposed refinancing.

PRIOR CITY COUNCIL AND COMMISSION ACTIONS:

No previous actions have been taken regarding this loan consideration.

FISCAL AND RESOURCE IMPACT:

With execution of the refinance, the City's Housing Successor Fund (255) will receive \$150,000 during Fiscal Year 2020-21. Additional funds may be received in coming years through residual receipts payments required of the underlying loan terms. The better the project performs financially, the better the prospects are for some residual receipts income.

CEQA (California Environmental Quality Act):

Project.

This project is Categorical Exempt pursuant to Section 15301 of CEQA Guidelines as proposed repairs, maintenance, and minor alteration of existing facilities involving no expansion of existing use will not have a significant effect on the environment.

LINKS/ATTACHMENTS:

1. Jasmine Square - Letter to City of Morgan Hill