ARLINGTON COUNTY, VIRGINIA

County Board Agenda Item
Meeting of February 20, 2010

DATE: February 3, 2010

SUBJECT: Consideration of the conversion and re-subordination of loans to three (3) AHC Inc. multifamily residential properties to new ownership entities to facilitate the planned renovations of Ashton House, Key Gardens, Taylor Square Apartments and North Ashton.

RECOMMENDATIONS:

1. Approve the consolidation of the existing Affordable Housing Investment Fund (AHIF) and Community Development Block Grant loans and deeds of trust on the Ashton House, Key Garden, and Taylor Square Apartments to new first deeds of trust covering the same properties plus North Ashton under new ownership affiliates as detailed in the staff report and subordinate the County loans to new primary loans in the aggregate amount of up to $9.0 million.

2. Authorize the County Manager to approve the new ownership affiliates and to execute, subject to approval by the County Attorney, replacement AHIF and CDBG loan Agreements and deeds of subordination, which will subordinate the County's existing loans for the Ashton House, Key Garden and Taylor Square Apartments to new first deeds of trust as detailed in the staff report and subject to the conditions set forth in the report and to amend or execute other related contract and loan documents, subject to approval by the County Attorney.

3. Authorize the County's Manager, with the concurrence of the County Attorney, to act as the County's representative in approving financing and revisions that are described in this report or are necessary to remove any ambiguity or inconsistency or which improves the County's financial security or financial position, and which changes do not adversely affect the County financially prior to execution of the County's financing documents.

ISSUE: County Board action is needed to allow re-subordination of existing County loans to new first deeds of trust to allow the proposed financing and renovation of AHC's North Ashton, Ashton House, Key Garden, and Taylor Square Apartments.

SUMMARY: AHC is requesting that the County re-subordinate its existing AHIF and CDBG loans to new primary financing packages for four properties to be held under two new consolidated limited partnerships. The new financing packages would each need support from a successful 2010 tax credit award from the Virginia Housing Development Authority (VHDA).

County Manager: BMD mnr

County Attorney: SAM

Staff: David Cristeal and Anne Venezia, DCPHD

20.

AHC will apply for competitive 9% tax credits in March through the nonprofit pool. AHC is submitting two separate packages of two properties each in order to limit the credit request per application to the maximum amount of tax credits allowed for the nonprofit pool. The County AHIF and CDBG loans, now estimated to total approximately $1.2 million with accumulated interest as of the projected October 1, 2010 closing date, will be subordinate to up to $9.0 million in new primary financing. Successful tax credit applications and refinancing would result in the substantial renovation of 103 units of committed affordable housing (CAF's) of which 93 are currently income restricted. After renovation, all 103 units will be income restricted, or a 10-unit increase. It is possible that AHC may be awarded credits for only one of the two applications this year, and may need to resubmit next year for credits for the other two properties. In this latter event, the outstanding County loan balances on the properties that are unsuccessful in 2010 would be re-subordinated at that future date.

BACKGROUND: The sponsor for the proposed financing is AHC Inc., a Virginia not for profit 501(c) (3) corporation. Each property is owned by a separate AHC non-profit affiliate whose sole purpose is to own and operate the properties, individually. Three of the four properties are currently cross-collateralized, in that, they secure each other collectively. North Ashton is separately financed with a VHDA loan.

The current tenant population is predominantly households earning less than 60% of area median income (AMI) and AHC anticipates that they would return to the units after being required to temporarily relocate during renovation. In 2003, the affordable housing compliance period was extended for 25 years or until the County loans are paid in full, whichever is longer.

AHC acquired Ashton House, North Ashton, Key Gardens, and Taylor Square between 1983 and 1991 and completed minor renovations at the time of purchase. On August 8, 1995 the Arlington County Board approved the issuance of $7.5 million of Revenue Bonds by the Industrial Development Authority (IDA) to refinance the primary debt of the cross-collateralized properties, which also initially included Key Boulevard and Jordan Manor. Jordan Manor has been removed from the package and is now being redeveloped and financed separately.

In 2003, the County approved additional refinancing for these properties using bonds issued by the IDA. This refinancing allowed AHC to complete minor renovations (approximately $3,000 to $4,000/unit). The County's AHIF and CDBG funds were re-subordinated to the bond financing package. As a condition of both the 1995 and 2003 refinances, AHC agreed to increase residual receipts payments that would result in a faster repayment of County loans. To date, the cash flow and, therefore, the repayments of the County loans have not increased as anticipated. AHC indicates that the high cost of utilities at these properties is a primary driver of escalating operating costs and, thus, lower residual receipt payments. County staff are awaiting financial documents and operating statements from AHC to verify this information.

DISCUSSION: The balance of AHIF and CDBG loans on the properties as of February 1, 2010, is approximately $1.1 million and is expected to be approximately $1.2 million at the projected closing date (see summary table on the following page). While AHC does not require additional County funds for this renovation, loan repayments would be suspended during the 2-year construction period, which staff estimates at approximately $10,000/year.

Total Outstanding Balances on County Loans

Property	Funds	Principal	Interest Earned	Total Payments	Current Balance
Ashton House	AHIF	$328,065	$72,326	-$28,353	$372,038
Key Gardens	CDBG	$354,783	$77,526	-$33,884	$398,425
Taylor Square	CDBG	$267,767	$59,621	-$4,297	$323,091
TOTAL		**$950,615**	**$209,473**	**-$66,534**	**$1,093,554**

AHC currently owns and manages through separate 501(c)(3) affiliates, Taylor Square, Key Gardens, Ashton House, and North Ashton. They plan to establish two for-profit tax credit partnerships to acquire and refinance all four properties with a total of 37 and 66 affordable units respectively. AHC is asking the County to re-subordinate its existing loans on three of these properties and for a County Manager CEO letter of support to VHDA for each project to enable AHC to claim an additional 50 points to strengthen the projects' scoring in the highly competitive tax credit competition.

Major elements of AHC's proposal are as follows:

- The new limited partnerships, with AHC affiliates as the general partners, would acquire the properties from the existing affiliates for approximately $11 million (value is based on 2010 County assessments plus transaction costs). This $11 million is part of the larger acquisition/rehab budget and is part of the basis for tax credits from VHDA (total development cost = $25 million, or $245k/unit). See the Sources and Uses table below.

Permanent Financing Sources and Uses

SOURCES AND USES	Ashton House / North Ashton			Taylor Square / Key Gardens			Total
SOURCES		**Per Unit**					
Senior Permanent	$2,400,000	$64,865	25%	$5,000,000	$75,758	31%	$7,400,000
Bridge bonds	$0	$0	0%	$0	$0	0%	$0
Tax Credit Equity	$4,212,306	$113,846	44%	$5,700,000	$86,364	35%	$9,912,306
AHC Loan	$0	$0	0%	$0	$0	0%	$0
Deferred Developer Fee	$436,847	$11,807	5%	$742,999	$11,258	5%	$1,179,846
Seller Note	$2,181,892	$58,970	23%	$4,334,465	$65,674	27%	$6,516,357
County Loans	$399,493	$10,797	4%	$758,095	$11,486	5%	$1,157,589
Interim Income	($19,912)	($538)	0%	($189,580)	($2,872)	-1%	($209,492)
		$0	0%		$0	0%	$0
Total Sources	**$9,610,626**	**$259,747**	**100%**	**$16,345,979**	**$247,666**	**100%**	**$25,956,605**
USES		$0			$0		
Acquisition	$3,962,700	$107,100	41%	$7,068,600	$107,100	43%	$11,031,300
Construction	$3,487,950	$94,269	36%	$5,847,750	$88,602	36%	$9,335,700
Soft Costs	$1,033,733	$27,939	11%	$1,594,881	$24,165	10%	$2,628,613
Development Fee	$873,693	$23,613	9%	$1,485,998	$22,515	9%	$2,359,691
Tax Credit & Loan Fees	$252,550	$6,826	3%	$348,750	$5,284	2%	$601,300
		$0			$0		$0
Total Uses	**$9,610,626**	**$259,747**	**100%**	**$16,345,979**	**$247,666**	**100%**	**$25,956,605**

- AHC is requesting that the County recommit the current AHIF and CDBG loans totalling approximately $1.1 million and re-subordinate the projected balance to new senior debt of approximately $9.0 million.

- A County Manager letter of support for AHC's tax credit application could allow AHC to either win 9% competitive credits in the non-profit pool, or, if they did not score well enough, their application would then roll over into the 2010 Northern Virginia pool and therefore could compete with Buchanan Gardens for 9% competitive tax credits. If successful, their application would generate approximately $10 million in tax credit equity, roughly 38% of their total budget. It appears there may be insufficient credits in the Northern Virginia pool this year to fund both Buchanan Gardens and the AHC scattered-site projects. If both AHC projects were unsuccessful in the nonprofit pool and rolled into the 2010 Northern Virginia pool, this may put the County's investment in Buchanan Gardens and the corresponding units at risk. If outscored, Buchanan Gardens would then have to re-apply next year for tax credits.

- Currently, four units at Key Garden and six units at Ashton House are not income restricted (though the rents are affordable). AHC would convert these 10 units to be income-restricted units at the 60% AMI level. This would make all 103 units across the four properties income-restricted/committed affordable units for 60 years.

- AHC would spend approximately $70,000/unit for renovations (new roofs, kitchens, baths, high-efficiency HVAC systems and other upgrades, with a particular emphasis on improving energy efficiency. The renovations will enable the projects to achieve EarthCraft certification. The renovations would also include the addition of approximately eight ADA units since none of the units are currently accessible. The renovations, which include the transition from central utilities to individually metered utilities, would also allow AHC to achieve substantial savings in operating costs. AHC indicates that these savings would be used, in part, to pay off the County loan more quickly.

- Tenant relocation would be necessary to complete the renovations. AHC intends to phase the renovations and vacate each property on a building-by-building basis during renovations. The project budget includes $1,000/unit to support tenant relocation.

- AHC proposes a 9% development fee on each project's total development budget of which 50% will be deferred -- paid from cash flow over time. When acquisition costs (the sales price paid by one AHC affiliate to another) are removed from the budget, the total developer fee equates to 16% of the renovation and other non-acquisition -related costs of which 8% will be paid and 8% deferred.

- AHC's proposal is comparable to their Board-approved 1995 and 2003 requests to re-subordinate County debt and increase residual receipts loan payments to the County. In a staff analysis, however, average annual residual receipts saw little or no increase following either the 1995 or 2003 refinancing. As a condition of this report, staff is recommending that 100% of residual cash flow be used to repay County loans.

Loan Terms and Conditions: Staff recommends that the County Board approve the consolidation of the existing County loans on these properties into two new loans, the re-subordination of these County loans under two new subordination agreements and two County Manager CEO letters of support to VHDA, subject to the following terms and conditions:

1. The applicant shall execute a generally standard AHIF/HOME Program Agreement and loan instruments for the County loan in a form acceptable to the County Manager and the County Attorney.

2. The County financing assistance will be in the form of a subordinated residual receipts loan, secured by the property, and repayable from the cash flow from the property. This loan will be made at an interest rate of 4%, compounded annually, over a term of 35 years. This loan will be subordinate to the primary mortgages in the aggregate amount of up to $9 million.

3. The County shall receive 100% of residual cash flow until all the County loans are paid in full. These payments will be subordinate to any cash flow payments required to comply with Low Income Housing Tax Credit program parameters, including payment of the deferred developer fee.

4. The term of affordability shall be 60 years. However, if at any time in year 35 or later (but prior to the end of the full 60-year commitment period), AHC desires to refinance the property and is unable to refinance because the units are income-restricted, AHC may return to the County Board with a request to consider a recommendation to allow the units (or a portion thereof) to be rented at levels necessary for the financial feasibility of the refinance.

5. The applicant must comply with the affordable housing set-aside for the rental units as follows: All 103 or 100% of the units shall remain affordable at rents established in accordance with 60% AMI LIHTC rents as published annually by VHDA for the unit size, minus a utility allowance (if applicable) as per the schedule annually approved by HUD for apartments in Arlington for 60 years. In addition, all units which were previously committed at rents and incomes at or below 50% of the AMI shall remain committed at these levels through the duration of the affordability term.

6. Future payment on notes taken back by AHC for the acquisition proceeds shall be committed as part of the new Agreement for use in future Arlington affordable housing projects undertaken by AHC.

7. The applicant, its designated ownership entity, heirs or assigns shall provide a purchase option including a right of first refusal to the County or its designee, if the developer decides to sell the property to an unrelated third-party purchaser any time prior to or at the end of the 60-year affordability term, wherein the County or its designee shall have the right, but not the obligation, for a period of up to 180 days, to purchase the property at 90 percent of its then-appraised fair market value. If the owner's appraiser and County's appraiser do not concur on the fair market value of the property, the two appraisers shall select a third appraiser using the industry-standard three appraiser method to determine the fair market value.

8. This loan consolidation shall be subject to AHC's submittal of a Tenant Relocation Plan for the project, for consideration and also subject to approval by the Tenant Landlord Commission not later than March 31, 2010.

9. AHC agrees to diligently pursue the feasibility of making up to eight (8) of the units accessible to persons with disabilities and to work with the County's Department of Human Services (DHS) on including up to eight (8) units for DHS supportive housing program consumers.

FISCAL IMPACT: While additional County funds are not needed to support this renovation, repayment of County loans will be delayed until the renovation is complete.