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ROUTE TO:


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MEMORANDUM

RETURN INSTRUCTIONS:

TO: Herman D. Parker
Community Services Director

DATE: August 2, 2013

FROM: Mark S. Manion 

FILE NO.: 20222-29

SUBJECT: Pescadero Lofts Isla Vista

This memorandum has been prepared pursuant to a request by Mr. John Polanskey, Director of Housing Development for the Housing Authority of the County of Santa Barbara. The purpose of this memorandum is to describe the necessary changes to the terms and conditions of the acquisition of real property owned by the County of Santa Barbara ("County") located at 761 Camino Pescadero, Isla Vista, CA ("Property") by the Housing Authority of the County of Santa Barbara ("Housing Authority"). The Housing Authority intends to develop a 33 unit affordable housing apartment complex on the Property ("Project").

The County and the Housing Authority entered into an Option Agreement ("Option") on March 5, 2013. The Option provides the Housing Authority with the right to purchase the Property for the amount of \$2,900,000 pursuant to the Purchase Agreement and Escrow Instructions ("PSA") attached to the Option. As a condition of the sale of the property the County is also requiring the recordation of a regulatory agreement that will mandate that the Property is used for affordable housing purposes only. The regulatory agreement has a term of 55 years.

Pursuant to the Option and PSA the entire purchase price is due when the Property is transferred at the close of escrow. As was discussed with County staff prior to the approval of the Option and was discussed during the Board of Supervisors' hearing on this item, in order for the Project to be financially feasible it will be necessary that the County finance the entire purchase price of the Property. The County financing will be secured by a subordinated deed of trust. If the County does not agree to finance the acquisition of the Property then the Project will not be financially feasible and the Project will not be constructed. Housing for Isla Vista's homeless, including veterans, and over \$3.8 million in tax credit equity will be lost to the County.

The Housing Authority proposes that the County's land financing have a term of 55 years, an interest rate of three percent simple interest and be paid from residual receipts from the operation of the Project. In the context of affordable housing developments, this is a typical structure for the financing of land acquisition costs and will allow the Project to be financially feasible.

Further, and as the County is aware, the Project is being financed with Low Income Housing Tax Credits, which were awarded to the Project on June 12, 2013. The tax credits will

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result in approximately \$3,835,644 of equity being contributed to the Project for construction purposes in exchange for the tax credits. As County staff is aware, in order to exchange the tax credits for the equity, the Property must be transferred into a California limited partnership.

In order to accomplish this requirement, the Housing Authority formed Pescadero Lofts Isla Vista, L.P., a California limited partnership ("Partnership"). The Partnership is a "pass through" entity which allows the benefit of the low income housing tax credits and losses resulting from depreciation to accrue to the investor as a limited partner. Control of the land and buildings within the Partnership remains with the general partners. In this case, the Housing Authority and Surf Development Company, a California nonprofit public benefit corporation, are the general partners. Union Bank has committed to providing construction and permanent financing to the Project. In addition, Union Bank has committed to purchasing the tax credits allocated to the Partnership.

For low income housing tax credit transactions, the Internal Revenue Code ("IRC") requires a 15 year compliance period. At the conclusion of the compliance period, the equity investor desires to exit the Partnership. To accomplish this, the Partnership Agreement will include a purchase option agreement that allows the general partners to acquire the Project in accordance with the requirements of the IRC. The acquisition of the Project at the conclusion of the compliance period by the general partners will allow the Project to remain affordable in perpetuity.

The Project is also expected to generate excess cash flow based upon preliminary Project estimates. The equity investor is not interested in receiving any of the excess cash flow. Accordingly, to the extent cash flow is available for repayment of the County loans, the payments will be applied first to the County Home Loan until paid in full and then applied to the County Land Loan.

Finally, because the Property will be owned by the Partnership rather than the Housing Authority, the Housing Authority requests that the County transfer the property directly to the Partnership. In the event the County agrees to these requests, the Housing Authority will terminate the Option and execute a quitclaim as may be necessary.

Please feel free to contact John Polanskey or me should you have questions or wish to discuss this matter further.