

RESOLUTION NO. _____

A RESOLUTION OF THE COUNCIL OF THE CITY OF SAN JOSE APPROVING CHANGES AND ADDITIONS TO THE UNDERWRITING GUIDELINES DEVELOPED BY THE HOUSING DEPARTMENT FOR USE IN UNDERWRITING AND STRUCTURING AFFORDABLE HOUSING TRANSACTIONS AND ADOPTED BY RESOLUTION NO. 78761 TO ADD SECTIONS CLARIFYING POLICIES REGARDING RESYNDICATION AND REFINANCING, CITY AND COUNTY LAND ACQUISITION FOR AFFORDABLE HOUSING AND COMMUNITY ENGAGEMENT; AND CHANGES TO POLICIES REGARDING RESIDUAL RECEIPTS AND FORECLOSURE AND LOSS OF SUBSIDY

WHEREAS, the City of San José (“City”) Housing Department uses its the Underwriting Guidelines to communicate with developers, borrowers, and other lending institutions regarding the expectations of the City with respect to key project financing, development and operating parameters and to evaluate project proposals that are submitted to the City in response to the Housing Department’s Notices of Funding Availability, when issued; and

WHEREAS, the Director of Housing normally adopts the Department’s Underwriting Guidelines, but since the current Underwriting Guidelines were approved by Council, these amendments are also presented for Council approval; and

WHEREAS, the City’s Underwriting Guidelines were last updated in August 2018 to establish clear requirements regarding risks and project feasibility related to underwriting affordable housing development; and

WHEREAS, the proposed changes and additions to the Underwriting Guidelines, attached hereto as Attachments A and B, are intended to provide the changes and additions needed to clarify policies regarding resyndication and refinancing, City and

County land acquisition for affordable housing and community engagement, and changes to policies regarding residual receipts and foreclosure and loss of subsidy; and

WHEREAS, the proposed changes and additions to the Underwriting Guidelines will provide greater clarity and consistency in the negotiation of transactions, reducing the time spent on negotiations, and will help isolate terms that will need to be brought to the City Council for approval;

NOW, THEREFORE, BE IT RESOLVED BY THE COUNCIL OF THE CITY OF SAN JOSE THAT:

The additions and changes to the Housing Department Underwriting Guidelines previously adopted by Council Resolution 78761, attached hereto as Attachments A and B, are hereby approved.

ADOPTED this _____ day of _____, 2020, by the following vote:

AYES:

NOES:

ABSENT:

DISQUALIFIED:

SAM LICCARDO
Mayor

ATTEST:

TONI J. TABER, CMC
City Clerk

ATTACHMENT A
UNDERWRITING GUIDELINES UPDATES

| 2018 Update | Current Language | Proposed Language |
|--|---|---|
| <i>Policy Update</i> Category: Loan Terms and Condition Section 3: Subordination of Affordability Restriction | In lieu of subordinating the affordability restriction, the City may allow a 60-day standstill and a float-up of affordability levels up to 60% Area Median Income (AMI) upon foreclosure (as required for feasibility). | At the discretion of the City Council, the City may allow the float up of affordability levels, to a maximum of 60% AMI, if necessary, for feasibility, in such cases where there is a loss of subsidy or foreclosure. The City's float-up language to apply to "New Tenants" in case of loss of subsidy only. |
| <i>New Policy</i> Category: Financing Options and Fees Section 2: Refinance, Resyndication/ Rehabilitation, Cash-out Policy | No Policy in last underwriting update | Explicit Policy (Attachment B) |
| <i>Policy Update</i> Category: Permitting Adjustments Section 9: Residual Receipts Update | The City shall require a payment of fifty percent (50%) of Net Cash Flow as a Residual Receipts payment per the calculation. However, if there is additional soft financing, the City may require the total share of Net Cash Flow for Residual Receipts payments to all Residual Receipts lenders to increase up to two-thirds ($\frac{2}{3}$). Of this $\frac{2}{3}$ of Net Cash Flow, the portion of Residual Receipts payments going to the City will be determined on a pro rata basis of the total gap financing. | California Department of Housing and Community Development (HCD): Projects that include funding from HCD, the calculation of residual receipts will need to adhere to HCD UMR 8314(a2). The City will not allow for 100% of residual receipts to pay any deferred developer fee in a priority to the City. |

| 2018 Update | Current Language | Proposed Language |
|--|---|---|
| <p><i>Policy Update</i> Category: Ground Lease Policy</p> <p>Section 8: City/County Acquisition Policy Section</p> | <p>This policy clarifies the guidelines on determining which agency will hold the ground lease.</p> | <p>In cases when the development is seeking funding from both the City and the County, one of the two agencies will hold the ground lease, ensuring long-term affordability. The City of San José will purchase the land if:</p> <p>The land was originally owned or financed by the City of San José</p> <p>The County of Santa Clara has not assisted the developer with acquisition and does not intend to own the land</p> <p>The City of San José has more soft funding in the development than the County of Santa Clara</p> |
| <p><i>New Policy</i> Category: Underwriting Guidelines Operations</p> <p>Section 5: Community Engagement Plan</p> | <p>No Policy in last underwriting update</p> | <p>All project sponsors are recommended to develop a community engagement plan to include the followings but not limited to: identify communities with diverse cultural and linguistic needs in various neighborhoods in San José, develop culturally and linguistically relevant communication materials, engage with the proposed community, its residents, and surrounding businesses that may be affected by the proposed development to adequately address their concerns. Track the engagement progress to report and refine engagement strategies as needed.</p> |

ATTACHMENT B

CITY OF SAN JOSE POLICY RESYNDICATION, REFINANCE, REHABILITATION & CASH-OUT POLICY

| RESYNDICATION, REFINANCE, REHABILITATION POLICY | |
|---|---|
| 1.1 Purpose | The purpose of this Policy is to establish guidelines for how the City will assess requests to Resyndication, Refinancing, and/or the Rehabilitation of developments where the City has a financial or non-financial interest in the development. In any of these cases, the City's Cash-Out Policy will apply. |
| 1.2 Eligible Projects | This policy will apply to any project currently being managed by the City of San José's Asset Management team, where the City has a City Loan, City Issued Bond with a Bond Regulatory Agreement, City Affordability Restriction, and City Ground Lease. All Sponsor loans must be in fully compliant in order for the City to consider any refinance or resyndication/rehabilitation projects. An application will be required to be completed for all transactions. |
| 1.3 City Council | Staff has a limited authority through the Director's Delegation of authority. Therefore, many request will have to be brought before City Council for approval. Transactions that require the subordination of the City affordability restriction, cash-out, or material changes to a current loan may require that the request be heard by City Council. |
| 1.4 Consideration | The City expects consideration for all transactions, specifically when there is a request for a transaction that does not meet the requirements of the City's underwriting guidelines. |
| 1.5 Examples of When Policy Applies | <ul style="list-style-type: none">• The City of San José is the Issuer of the Bond• City has a Construction, Permanent, or Acquisition Loan• There is an Enforceable Bond Regulatory Agreement in place, but there is no longer an outstanding Bond.• There is an Enforceable City Affordability Restriction in place, but there is no longer a Construction, Permanent, or Acquisition Loan. |
| 1.6 Developer Fee | <ul style="list-style-type: none">• The City will only allow for a Developer fee to be taken out that is proportional to the amount of rehabilitation. Developer fee should be no more than 10% of total construction cost of the rehabilitation. |

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| 1.7 Rent Burden | <ul style="list-style-type: none"> • For Developments that are taking on additional debt to the property, the Developer will need to assure that the additional debt that will not cause additional rent burden to its current tenants. • The Developer will need to provide a plan of action that will address “Rent Burden” if any of their current residents are paying 50% or more of their gross income in rent. • The action plan should include, solutions such as: <ul style="list-style-type: none"> ○ Lowering of AMI to meet the income level of current tenants ○ The creation of a rent reserve to help cover rent burdened tenants ○ Property management plan that demonstrates a clear effort to address rent burdened tenants. |
| 1.8 Affordability Restrictions | For request for refinance or resyndication, the City will require a minimum of an additional 15 to 25 years extension of the affordability restriction, based on the nature of the transaction. |
| 1.9 Bond Redemption | The City of San José shall be the issuer of all bonds financing for multifamily housing rental projects within the City. Please refer to City Council Policy for Bond Issuances for more information about this policy. |
| 1.10 Outside Issuer | In general, the City does not allow for the outside issuance of any multifamily Bond Issuance without City Council approval. |
| 1.11 CASH-OUT POLICY | |
| <p>In general, The City of San José will allow a Sponsor to secure new loans for financing or refinancing the acquisition/rehabilitation of a Project, but only if the City of San José determines in its sole discretion, that such financing/refinancing is necessary to ensure the viability of the Project. Under City Documents, a Sponsor must obtain The City of San José prior written consent for such new financing/refinancing, encumbrance of a leasehold estate, subordination of any City of San José existing liens, and/or prepayment of existing debt. Therefore, to ensure the financial viability and sustainability of a Project, a Sponsor is generally not permitted to obtain a loan in an amount that exceeds the amount necessary to acquire/rehabilitate a Project, which is commonly known as a “Cash Out.”</p> <p>If Sponsor would like to seek the City’s consent in obtaining a new loan for conducting an</p> | |

RESYNDICATION, REFINANCE, REHABILITATION POLICY

acquisition/rehabilitation, resyndication or refinancing, and will be taking “cash out”, the proceeds will be subject to a split between City and Developer 50/50, with the City’s portion being applied to outstanding interest and the project must meet three criteria:

Cash-Out Requirements:

- 1) The City has performed a satisfactory analysis of the financial health of Developer/Sponsor. Three years of Audited Financial Statements will be required.
- 2) The Development must be analyzed for rent burdened and this analysis must be reviewed, addressed, and approved by the City
- 3) A Physical Needs Assessment must be completed, and approved as satisfactory, by the City of San José.

| Waiver Type | Cash-Out 50/50 Waiver |
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| Reinvestment in Future Developments | <ul style="list-style-type: none">• The City of San José may consider a waiver to the 50-50 split of “Cash-Out” by allowing the Sponsor to take a greater portion of the Cash-Out, if the Sponsor can demonstrate that Cash-Out proceeds will be used by the Sponsor to invest in future affordable housing developments in the City of San José, currently being planned by the Sponsor within the next five years.• Subject to review by the City, the Sponsor will need to provide a copy of all current and proposed developments where the Cash-Out will be used. The Sponsor will also be required to assure that the Cash-Out appears on the audited financials of the Sponsor as a development loan. |
| Reinvestment in Proposed Development | <ul style="list-style-type: none">• The City of San José may also consider waivers, subject to City of San José’s review of supporting documentation, that result in an increased net public benefit to the subject property, where a Sponsor commits to reinvest all Excess Proceeds into the development. Such requests must demonstrate that the proposed uses justified by recent Capital Needs Assessments (“CNA”) approved by City of San José, feasible underwriting, Sponsor capacity, and long-term cash flow projections. |