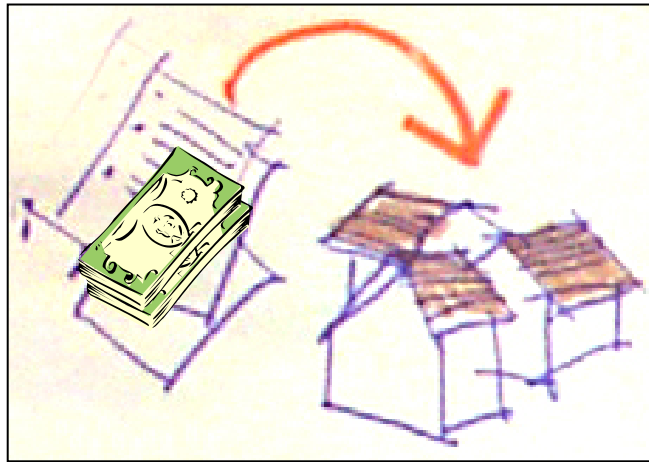




CITY OF SANTA CRUZ AFFORDABLE HOUSING TRUST FUND



Administrative Guidelines

*Department of Economic Development
Housing Division*

As adopted by the City Council on October 28, 2003 by Resolution No. NS- 26,410

As revised by City Council on April 25, 2006 (adding Section 5.4.i) by Resolution No. NS-27,214

Minor Revisions on May 2, 2014 updating organization change to Economic Development.

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City Of Santa Cruz Affordable Housing Trust Fund

Chapter 1: Statement of Purpose

The purpose of the City of Santa Cruz Affordable Housing Trust Fund, (AHTF), is to assist in the creation and preservation of affordable housing in the City of Santa Cruz for the benefit of low and moderate-income households.

Chapter 2: Definitions

1. “Area median income” or “AMI” is established for metropolitan areas or non-metropolitan counties by the U.S. Department of Housing and Urban Development (HUD), pursuant to 42 U. S. C. Chapter 1437 et seq., to establish local income classification levels. These classifications are also used in California housing law with respect to income eligibility limits.
2. “Affordable Housing” for purposes of these Guidelines shall mean rental housing that is affordable to low and/or very-low income households and for sale housing that is affordable to moderate, low and/or very-low income households.
3. “Extremely low income household” shall mean a household having an income not exceeding thirty (30) percent of AMI adjusted for household size.
4. “Very low income household” shall mean a household having an income not exceeding fifty (50) percent of AMI adjusted for household size.
5. “Low income household” shall mean a household having an income not exceeding eighty (80) percent of the AMI adjusted for household size.
6. “Moderate income household” shall mean a household having an income not exceeding one hundred twenty (120) percent of the AMI adjusted for household size.
7. “In-Lieu Fees” are fees paid by a market rate developer in lieu of building affordable units within the development as a means of satisfying the City’s inclusionary housing requirement as specified under Chapter 24.16.030 of the City of Santa Cruz Municipal Code (Municipal Code). Under these Guidelines, the In-Lieu Fees will henceforth be dedicated to the AHTF as stipulated below.
8. “Permanent Local Housing Allocation (PLHA) Program” is a State program established by the Building AHTFs and Jobs Act of 2017. Funding is provided by a \$75 recording fee on real estate documents with 70% of these fees being set aside for PLHA programs. Jurisdiction funding amounts are annually defined by the State Department of Housing and Community Development (HCD), who administers the program. Jurisdictions must annually apply for these allocated PLHA funds.

Chapter 3: Housing Trust Fund Established.

1. By Resolution No. NS-26,410, the City Council established a trust fund for a special revenue account under the name of the “Santa Cruz Affordable Housing Trust Fund”.
2. Accumulated and future Moderate, Low or Very-Low Income Housing Fund In-Lieu Fee dedications under Chapter 24.16.030(b) of the Municipal Code shall become AHTF property and shall be deposited directly into the AHTF. In-lieu fee dedications are allowed under Chapter 24.16.030 of the Municipal Code to be made by a market rate developer, upon application by the developer, to meet its inclusionary housing requirement. Accordingly, In-lieu fee dedications collected under Chapter 24.16.030 of the Municipal Code shall be deposited into the AHTF account.
3. Accumulated and future Permanent Local Housing Allocation (PLHA) Program funds shall become AHTF property and shall be deposited directly into the AHTF.
4. The AHTF may accept donations from individuals or organizations other than the City of Santa Cruz. Such donations may be designated for a specific project or purpose.
5. All moneys remaining in the AHTF at the end of any fiscal year, whether or not expended by the City, remain AHTF property.

Chapter 4: Management

1. The Housing Division Manager under the Department of Economic Development shall serve as the Manager of the Affordable Housing Trust Fund. The responsibilities of the Manager, subject to direction of the City Council, shall include:
 - a. Maintaining all records of the AHTF.
 - b. Assisting prospective applicants requesting AHTF support in the preparation and presentation of their applications.
 - c. Monitoring the use of monies distributed to successful applicants for AHTF support to assure ongoing compliance with the purposes of the AHTF and the conditions under which these monies were granted or loaned.
 - d. Reporting annually to the City Council regarding the operation and activity of the AHTF.
2. The Director of the Department of Finance, or designee, in coordination with the Manager of the Affordable Housing Trust Fund shall be responsible for the following:
 - a. Disbursing and collecting AHTF monies.
 - b. Maintaining and managing a separate account or accounts for AHTF monies.
 - c. Maintaining financial records for the AHTF.

Chapter 5: Distribution and Use of Housing Trust Fund Assets

1. Distributions may be made to individuals and/or private or public, profit or non-for-profit entities.
2. The types of investments the fund may make include: gifts, grants, loan guarantees, letters of credit or other forms of credit enhancement, or other disbursements deemed necessary and appropriate to fulfill the purposes of the AHTF.
 - a. AHTF funds used to provide construction loans and/or deferred payment permanent financing loans shall be at simple interest rates of no higher than 3 percent per annum, for payment of predevelopment costs, acquisition, construction, or rehabilitation of Eligible Projects.
3. Organizations or individuals bestowing a gift or grant to the AHTF may specify how such a gift or grant may be used. If the gift or grant has not been used for such purpose within a reasonable amount of time, or a time period specified as a condition of the gift or grant, the gift or grant shall be returned upon the request of the donor.
4. Types of projects in which the AHTF shall invest include:
 - a. Creation of new affordable units.
 - b. Preservation of existing affordable housing.
 - c. Assistance with multi-family rehabilitation programs.
 - d. Conversion of market rate units to affordable housing units.
 - e. Construction, conversion, or rehabilitation of accessory dwelling units (ADUs), or junior ADUs as defined in the Municipal Code.
 - f. Acquisition and rehabilitation of potential limited equity housing cooperatives.
 - g. First time Homebuyer loans.
 - h. Predevelopment loans/grants to assist non-profit and for-profit developers with project feasibility studies, site acquisition and preliminary design studies for potential affordable housing projects.
 - i. Administrative costs for affordable housing programs and projects for up to 5% of the AHTF.
5. Priority in all disbursements shall be given first to housing projects that guarantee the perpetual affordability of such housing and, second, to housing projects that guarantee a term of affordability of at least 55 years together with eventual recapture of the AHTF investment.
6. The following categories identify income groups that the AHTF will serve. The percentages shown are minimum target amounts or maximum allowed amounts of funding that will be expended in each category. If eligible projects are not found for a particular category within one year after funds have been deposited, funds targeted for that category may be moved into the contingency category to be allocated to other areas. Target set aside amounts and other restrictions are as follows:

- a. Extremely low-income (at or below 30% of AMI): Target 30% of AHTF funds.
 - b. Lower-income (at or below 80% of AMI): Up to 70% of AHTF funds.
 - c. Moderate-income (80% to 120% of AMI): Maximum of 20% of AHTF funds.
 - d. Contingency: Target 15% of AHTF funds. These funds can be allocated to provide for any of the identified categories above.
7. Projects will be evaluated with respect to criteria that are consistent with City goals and policies. In addition, projects that provide the following will be viewed favorably and when ranked against other projects, shall be given additional merit points:
- a. Projects that provide the greatest benefit per dollar of funds spent.
 - b. Projects that demonstrate higher equity in the project and/or a lower loan to value ratio.
 - c. Rental projects that have other funding sources identified and committed.
 - d. Rental projects which benefit the highest percentage of low and moderate income persons, provide the lowest rents, include a greater percentage of affordable units, or will maintain longer periods of affordability.
 - e. Rental projects that use program funds as a match or leveraging tool to stimulate the use of conventional and below-market resources, including tax credits, state and federal funding programs, and/or other funding sources.
 - f. Rental projects proposed by an applicant with a successful history of project development and/or property management, as appropriate.
8. When appropriate, the AHTF shall use existing City guidelines for homebuyer, homeowner Rehabilitation, or Accessory Dwelling Unit Programs. Guidelines providing for loans and/or grants for the development of multi-unit rental projects shall be as follows:
- a. A Nonprofit Community or Government Organization receiving an AHTF grant and/or loan must be a legally established tax-exempt nonprofit community organization recognized by the Internal Revenue Service and the Franchise Tax Board, a public agency, or other governmental agency.
 - b. Permanent financing shall be secured by a deed of trust against the land or a security agreement against physical improvements. A promissory note may be used for pre-development costs for up to 15% of the estimated project cost.
 - c. There must be at least 10% equity in the property after completion of a project. This value may be established by AHTF staff and/or an appraiser. Exceptions may be approved by the City Council.
9. Loan and Underwriting Guidelines for the AHTF are provided as an attachment to these Program Guidelines:

ATTACHMENT I

AHTF Loan and Underwriting Guidelines and Procedures

For purposes of the AHTF Program, underwriting involves the analysis of project assumptions and risks to determine if the public investment is reasonable and the project can be expected to meet all applicable program requirements. The following are core components of the City’s underwriting and subsidy layering review of an AHTF project. Required actions/procedures are noted at the end of each section.

1. **Sources and Uses Statement and Pro Forma** - An examination of the sources and uses of funds for the proposed project and a determination that all project costs are reasonable. Before committing AHTF funds the City shall evaluate a proposed project to ensure that funds are invested such that the project is likely to succeed over time. City shall assess all of the assistance that has been, or is expected to be, made available to that project, and take into account all the factors relevant to project feasibility, which may include, but are not limited to total development costs and available funds; impacts of restrictions from AHTF and/or other sources of funding such as eligible costs, maximum subsidy limits, cost allocation, and rent/utility allowance limitations; rates of return to owners, developers, sponsors, or investors; and the long-term needs of rental projects and tenants. The following elements shall be reviewed and analyzed in forecasting project success:

- a. **Sources and Uses Statement** – the sources and uses document shall include the following:
 - i. **Sources** - all sources, both private and public, of funds with dollar amounts and timing of availability for each source must be identified.

DOCUMENTATION: The following documentation is required in support of the sources and uses statement:

- Commitment letters with all terms and conditions for all mortgages, grants, bridge (interim) loans and investment tax credits.

Acceptable documentation of firm financing include award letters, offer letters, final term sheets or commitments which are conditioned upon receipt of AHTF funds. For projects with low income housing tax credits (“LIHTC”) a reservation from the credit allocator and a good faith offer of equity investment from an investor is required.

- If the developer is a partnership or limited liability corporation, a copy of the partnership agreement or operating agreement which will indicate the cash contributions by the partners or members.
- If equity is committed by the developer or owner, evidence of available equity funds.

ACTION TO BE TAKEN: City shall determine whether funding sources are adequate and timely in their availability to cover costs at all phases of the project.

- ii. **Uses** - All uses of funds (acquisition costs, site preparation and infrastructure costs, rehabilitation/or construction costs, financing costs, professional fees, developer fees and other soft costs) associated with the project and their costs. All costs must be necessary and reasonable.

DOCUMENTATION: The following documentation shall be required:

- Acquisition documentation such as purchase agreement, option or closing statement and appraisal or other documentation of value.
- Construction cost estimate, construction contract, or preliminary bids.
- Contracts, quotes or other agreements substantiating key professional costs and the basis for estimating other soft costs and working capital items, including capitalized reserves.
- Agreements governing the various reserves which are capitalized at closing (to verify that the reserves cannot be withdrawn later as fees or distributions).
- A third-party appraisal to substantiate the value of the land and the value of the property after rehabilitation or the structure being built.
- If low income housing tax credits are utilized, documentation on the syndication costs (legal, accounting, tax opinion, etc.) from the organization/individual who will syndicate and sell the offering to ensure that the project can support the fees necessary to syndicate/fund the project.
- Project schedule.

ACTION TO BE TAKEN: City shall determine that the all of the proposed costs for the project are necessary and reasonable by considering costs of comparable projects in the same geographical area and costs published by recognized industry cost index services.

b. Operating Pro Forma

DOCUMENTATION: Developer shall submit an operating pro forma (project income and expense statement) for the length of the Affordability Period pertaining to the project.

ACTION TO BE TAKEN: City shall evaluate the pro forma for the following:

- Reasonableness of the financial assumptions of the project to establish minimum total per unit operating costs.
- Sufficiency of specific line item and total operating costs.
- Determination that long-term operating projections over the Affordability Period are based on reasonable assumptions.
- Demonstration that project can cover expenses and debt service throughout the affordability period.
- Ensuring that cash flow projections are realistic in light of economic conditions.

- Determination that long-term operating projections are based on reasonable assumptions about how revenues and operating costs are expected to change over time.
- Determination that long-term operating projections over the affordability period are based on reasonable assumptions.
- Demonstration that project can cover expenses and debt service throughout the affordability period.
- Ensuring that cash flow projections are realistic in light of economic conditions.
- Determination that long-term operating projections are based on reasonable assumptions about how revenues and operating costs are expected to change over time.
- That non-residential revenue from fees/late charges, commercial income, interest, laundry/vending are projected conservatively.
- That vacancy projections reflect local market conditions and account for physical vacancies and collections loss.
- That the rate of projected growth for rental income and other revenues are appropriate and that in projects with deeply targeted rents, lower than average rate of revenue increases are used for comparison when possible.

ACTION TO BE TAKEN: City shall determine that Projected Income assumptions as provided in the pro forma are reasonable based on the following that:

- Non-residential revenue from fees/late charges, commercial income, interest, laundry/vending are projected conservatively.
- Vacancy projections reflect local market conditions and account for physical vacancies and collections loss.
- The rate of projected growth for rental income and other revenues are appropriate.
- For projects with deeply targeted rents, lower than average rate of revenue increases are used.
- Net operating income is sufficient to cover debt service obligations and mandatory replacement reserve funding.
- Reasonable but not excessive cash flow is generated throughout the affordability period.
- The rate of annual increase in project income is reasonable.

ACTION TO BE TAKEN: City shall determine that Projected Expenses are reasonable as provided in the pro forma submittals, including:

- Operating costs given the scope and size of the project.
- Management fees and other fees to the owner.

- Adequate replacement reserve deposits.

2. Market Assessment

DOCUMENTATION: Developer shall provide data that supports unit absorption rates used in the Operating Pro Forma. Data submitted to City in support of the project market assessment shall be no more than four months old. In the event that AHTF funds are not committed to the project within that timeframe, updated data must be submitted to the City for review.

ACTION TO BE TAKEN: The City shall assess the current market demand in the area to confirm the need for the project and that the type and number of units in the project. Given the housing shortage in the City, it is assumed that there will be high demand for housing in general. The goal is encourage the projects that reflect current community needs for size, price, and other factors affecting the projects marketability.

- Assess the market for the project and determine if there is sufficient demand to sell or rent the housing units within one year of construction completion.
- Identify recent real estate trends that indicate demand for types and sizes of units.
- Estimate the absorption period by determining how many units can be successfully leased or sold each month and how long it will take to achieve initial occupancy/sale of the AHTF units and stabilized occupancy for the project as a whole.

3. **Developer Capacity Assessment:** There are two elements of underwriting analysis related to the developer: 1) the experience and the capacity of the developer (including the staff and project team) to implement the project and 2) the fiscal soundness of the developer to meet its financial obligations and risks of the project. The City shall use the following procedures shall determine what constitutes acceptable experience and financial capacity of the developer based on the size, scope, and complexity of the project.

a. Experience

DOCUMENTATION: The Developer is required to provide information on their experience and provide references in the funding application including:

- Corporate or organizational experience of the developer.
- Experience of the staff assigned to the project and overall quality of the development team.
- Prior experience of the developer's team members compared to their roles in the proposed project.
- Skills and capacity including property management, asset management, service provision (as applicable), and financing.

ACTION TO BE TAKEN: The City shall consider prior experience and the current capacity of the developer and determine if the developer has the technical and managerial experience, knowledge, and skills to successfully complete the development.

- b. **Developer Financial Capacity** – The following elements shall be analyzed to determine developer financial capacity:

ACTION TO BE TAKEN: The City will review the following information taken from the developer’s operating pro forma and information provided in the funding application (audit, references, prior projects) to determine that the developer’s experience and financial capacity are adequate to implement the project and meet financial obligations and risks of the project. The following information will be analyzed for this purpose:

- Financial management systems and practices.
- Sufficient financial resources to carry the project to completion.
- Financial statements and audits to determine the developer’s net worth, portfolio risk, pre-development funding, and liquidity.

4. **Developer Profit and Return** –

ACTION TO BE TAKEN: The City shall require that any profits or returns on the owner’s or developer’s investment are not excessive. The City shall conduct an analysis that reviews profit expected to flow to the developer as operating cash flow from rental projects and any other professional fees being paid to the developer or related entities. The analysis shall focus on the following areas to determine that developer fees, cash flow, equity appreciation, and profit associated with the project are reasonable:

- a. **Developer Fee** – For LIHTC projects, the developer fee may not exceed the limits established by the awarding state or federal agency. The developer fees must reflect the local market and shall be reviewed with respect to the following:
- i. The scope and complexity of the project.
 - ii. The size of the project.
 - iii. The relative risk the developer is taking.
 - iv. The costs a developer will incur from the fee as compared to those being charged as project costs.
 - v. The fees that are regularly and customarily allowed in similar programs and projects.
 - vi. Other fees the project is generating for the developer and its related entities.
- b. **Cash-Flow** – Reasonableness of net cash flow assumptions and distribution of same to developer/owner and lenders.
- c. **Equity Appreciation** – Reasonableness of projected equity position over time.
- d. **Identity of Interest Roles**
- i. If the developer owns a construction company that will be working on the project, the City shall determine that the profit and overhead of the contractor is reasonable.

- ii. If the owner of a rental property assisted with AHTF funds also operates a property management company contracted to service the property, the City shall determine that the management fees are reasonable.

- e. **Profit From Rental Operations** – The City shall conduct an evaluation of the cash flow return on the investment in order to determine if the return is reasonable. The following types of cash flow analysis will be used by the City dependent on project type:
 - i. Cash on cash rate of return.
 - ii. Internal rate of return.