(R-84-831)

RESOLUTION NUMBER R- 259655

Adopted on NOV 21 1983

BE IT RESOLVED, by the Council of The City of San Diego, as follows:

That the concept of a potential $50 million bond issuance to provide low interest mortgage funds to purchasers of single family residences originally approved by Council Resolution No. 222450 on December 19, 1978, is hereby again ratified and the San Diego Housing Commission is hereby authorized to proceed with the development and implementation of a $50 million single family mortgage revenue bond program, the design and concept of which are described in the report attached hereto and by this reference incorporated herein.

BE IT FURTHER RESOLVED, that the final proposed documents for implementing the program and selling the bonds are subject to final approval by this Council.

BE IT FURTHER RESOLVED, that the selection of the firms of E. F. Hutton & Company, Inc., and Stone & Youngberg as the lead underwriters for the bonds, with Goldman, Sachs & Co. and Newman and Associates, Inc. serving as co-managers, is hereby approved subject to a condition that payment to such firms shall be made solely and exclusively from bond proceeds and pursuant to a bond purchase agreement to be submitted to the Council for approval and that unless and until bonds are sold, the City shall incur no obligation for any payment to said underwriters.

APPROVED: John W. Witt, City Attorney

By [signature]
Harold O. Valderhaug
Deputy City Attorney

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SAN DIEGO
HOUSING COMMISSION

BEN MONTIJO • EXECUTIVE DIRECTOR

REPORT TO THE HONORABLE MAYOR AND CITY COUNCIL

DATE: November 2, 1983 REPORT NO: 83-

ATTENTION: Council Docket of November 21, 1983

FROM: Ben Montijo, Executive Director

SUBJECT: Single Family Mortgage Revenue Bond Program

SUMMARY

Issue - Should the City Council adopt a resolution which (1) authorizes the Housing Commission to proceed with the development and implementation of a $50,000,000 Single Family Mortgage Revenue Bond Program, the design and concept of which are described in this report, and (2) approve for this program the selection of the firms of E.F. Hutton & Company Inc. and Stone & Youngberg as the lead underwriters, with Goldman, Sachs & Co. and Newman and Associates, Inc. serving as co-managers?

Recommendation - It is recommended that the City Council adopt a resolution (1) authorizing the Housing Commission to proceed with the development and implementation of a $50,000,000 Single Family Mortgage Revenue Bond Program, the design and concept of which are described in this report, and (2) approve for this program the selection of the firms of E.F. Hutton & Company Inc. and Stone & Youngberg as the lead underwriters, with Goldman, Sachs & Co. and Newman and Associates, Inc. serving as co-managers.

Fiscal Impact - These bonds are not general obligations of the City. All costs associated with the bond sale will be paid with bond proceeds. A potential cash flow will be generated from the bond proceeds. The precise amount will be determined as the program is structured.

BACKGROUND

On December 19, 1978, the City Council adopted Resolution No. 222450 authorizing the City Manager to solicit proposals from qualified firms interested in assisting the City to develop a program to provide low interest mortgage funds through issuance of tax-exempt bonds. The City Manager was in the process of forwarding a report to the City Council describing the contemplated $50,000,000 bond program when on

April 26, 1979, a bill (HR 3712) was introduced into the U. S. House of Representatives to remove tax exemptions from State and local subsidy bonds. Accordingly, the City suspended its activity on the single family bond program, and redirected its efforts instead toward obtaining bond funding for the development of multifamily rental units.

HR 3712 became the Mortgage Subsidy Bond Tax Act of 1980. Its effect was to restrict the use and limit the number of tax exempt bond issuances available for single family purchase after April 1979, and to authorize state legislatures to provide for their own method of allocation. AB 1618 created the Mortgage Bond Allocation Committee (MBAC) to allocate the authority to issue tax exempt single family issues within the state. On May 2, 1983, Resolution #258393 was passed, authorizing the City Manager to submit an application to the MBAC for a $50,000,000 allocation of mortgage bonds for the purpose of single family home purchases. The status of that application is pending; the MBAC will meet next in February 1984.

According to Orrick Herrington & Sutcliffe (bond counsel), the tax-exempt funding which the City intended to pursue prior to April 1979 is still available through a grandfather clause in the Mortgage Subsidy Bond Tax Act. This funding ~~has~~ does not carry the restrictions of the Mortgage Subsidy Bond Tax Act and does not require application to the MBAC. The intention is to develop a program for this $50,000,000 in tax-exempt bonds.

On October 18, 1983, Housing Commission staff consulted with Commissioners Hedenberg and Robinson and financial consultant Gene Slater of Caine Gressel Midgley and Slater to form guidelines for the Single Family Bond Program. The resulting program description and recommendations were approved at the Housing Commission meeting of October 28, 1983.

DISCUSSION OF DESIGN AND CONCEPT OF PROGRAM

Types of Loans Bond funds would provide permanent first mortgages for owner-occupants. This bond issue cannot be used for construction financing or rental developments.

Size of Units Loans can only be made for one unit properties. These include attached and detached single family homes, townhouses and condominiums.

Owner-Occupants Borrowers must certify that they intend to occupy the property as their principal residence for at least two years. Subsequent purchasers (meeting the eligibility requirements) must also certify as owner-occupants. Violation would result in the loan becomming due and payable immediately.

Income Limits The borrower's total household income is limited to 150% of the area median income. This figure, as determined by HUD, is currently $39,500. This is one of the key restrictions in the program, and assures that loans will not go to upper middle income buyers who could afford conventional financing.

Location All units must be located within the City of San Diego.

Interest Rate and Loan Term Loans will probably be fixed rate, fully-amortizing, 30 year mortgages. In today's market, the loan interest rate would be approximately 10¼ to 10½% (plus mortgage insurance). Flexibility exists to provide graduated payment mortgages or growing equity mortgages if developers demonstrate a strong preference for these loans.

Loan-to-Value Ratio The maximum loan-to-value ratio would be 95%, and mortgage insurance would be necessary on all loans.

Role of Private Lender Private lenders would originate and service all loans on behalf of the City, using their normal underwriting criteria.

Total Amount of Loans The maximum size bond issue is $50 million ("grandfathered" as pre-Ullman). After considering reserve funds and other costs, the maximum amount of mortgages is approximately $45 million.

Loan Assumption A loan made under this program would be assumable by an eligible certified buyer only. Violation would result in the loan becomming due and payable immediately.

Affirmative Marketing Projects selected for funding must include an effective Affirmative Marketing Plan.

Selection Criteria Consideration will be given to projects meeting program requirements, submitted by developer/lender teams able to originate loans. Priority will be given to projects on Housing Authority or City owned land. In the event of over-subscription, the goal will be to select those projects which help achieve an overall diversification of projects, a dispersion of sales prices, and a positive impact on potential bond rating. Also, in the event of over-subscription, priority will be given to projects furthest along in development.

Fees An initial fee of ½ of 1% will be required with all commitments. Total fees due from developer prior to bond sale, in a combination of cash and letters of credit, will not exceed 4 points. It is anticipated that upon the origination of each individual loan, a substantial portion of this will be refunded to the developer.

Attachment A includes a time schedule for the Single Family Bond Program.

RECOMMENDATIONS

1. Previous Tenure of Borrower It is recommended that the City not establish a restriction of first-time homebuyers.

This bond issue is not subject to any federal or state requirement on borrowers being "first-time homebuyers". Although such a requirement would seem to have the commendable purpose of only helping those who were first entering the market, it has raised problems in other bond issues. In practice it has:

a. had unintended consequences; for example, for divorced persons, neither party can buy a new home, even if the previous home has been sold to meet the divorce settlement;

b. been extremely complicated to administer, requiring copies and verification of 3 previous years' tax returns, and various owner certifications; bond loan closings have often taken two to four weeks longer as a result;

c. substantially narrowed the market for bond loans, particularly where they are linked to specific new construction projects. It becomes more difficult for a developer to anticipate the amount of bond financing needed.

Even without a restriction, it is likely that a large proportion of borrowers will be first-time homebuyers simply because of the income and purchase price limits.

2. New vs. Existing Units It is recommended that all the bond funds be used for new homes, rather than existing homes.

a. AB 1355 requires that at least 3/5 of all loan funds be used for new construction (or substantial rehabilitation).

b. New construction would add to the housing supply and provide tangible, specific results of the bond issue.

c. In order to cover the "non-asset bonds" (underwriter's discounts, costs of issuance, etc.) someone must provide three to four points in cash and/or letter of credit, at the time of bond closing.

Developers have generally been the only parties willing to do this. Lenders (and realtors) have not been willing to take this risk simply to have 10½% loans available for existing homes. The City, to reserve funds for existing housing, might have to use some of its own money.

The bond issue would be limited to units which have not been previously sold. For rating agency purposes the bond issue should not be used to bail out foreclosed projects owned by private lenders.

3. Price Limits It is recommended that the City establish a purchase price limit of $120,000.

Although we are not required to have a purchase price limit, a ceiling of $120,000 would generally be consistent with bond issues under the Mortgage Subsidy Bond Tax Act, and would appear to be workable for the Site 18 Collins project. In addition, it would:

a. Prevent program abuses. A purchase price limit is desireable if the program is not limited to first-time homebuyers. Otherwise, owners could use very large down payments from their old homes to buy very expensive new homes.

b. Be consistent with the maximum borrower income limit of $39,500; few borrowers could normally qualify for more expensive homes.

4. Commitment Requests It is recommended that developers be required to submit commitment requests jointly with their preferred lender, listing each individual project and putting up a ½ point good faith deposit (refunded if their allocation is reduced). Before the actual bond sale, the developers will be required to increase their deposit by approximately another 1% in cash and 1½% in Letter of Credit.

This approach helps the City to avoid the problem of having to match lenders and developers. It assures that each developer has talked to a lender who is willing to originate and service loans for the project. It allows the Commission to focus on the types of projects to be financed, rather than on choosing between alternative lenders.

5. Lender Eligibility It is recommended that there be minimum standards for lenders, including having a loan origination office in the City, and having a track record in originating single family loans and servicing them for the secondary market.

The Commission would establish a maximum origination and servicing fee for loans under the bond issue; this maximum would be based on average fees charged by lenders on similar issues throughout the State.

6. Criteria for Project Approval Generally, priority will be given to those projects furthest along in the development process -zoning approvals, off-site improvements, working drawings, already under construction, etc. -- and which are likely to produce loans at the earliest time. This is relevant since the City might be able to issue additional bonds in future years. There would be a minimum commitment size to help to focus on larger projects and save administrative time, e.g., $500,000; similarly a maximum amount per developer or project (e.g., $5 million, except for Site 18) might be used.

Recommendation #6-A It is recommended that first priority in the selection of projects be given to projects on Housing Authority or City owned land. (This would ensure adequate funding for Site 18.)

Recommendation #6-B It is recommended that, in the event of over subscription, additional criteria would be considered in the selection of projects. Such criteria would include consideration of:

i. Designated target areas, such as the CDBG neighborhoods;

ii. An equitable dispersion of sales prices (and thus borrower income), taking into account the type, square footage, and quality of proposed units.

iii. Diversification of projects and their impact on potential bond rating. This can affect very large projects, ones which are all in the same area, or ones which are primarily condominiums.

The developer survey may yield information on additional criteria to be considered in the selection of projects.

DISCUSSION OF SELECTION OF UNDERWRITING TEAM

On October 28, 1983, the Housing Commission approved the selection of the firms of E.F. Hutton & Company Inc. and Stone & Youngberg to act as lead underwriters for the Single Family Bond Program, and Newman and Associates and Goldman Sachs to act as co-managers.

The Multifamily Bond underwriting team for San Diego has consisted of Goldman Sachs as lead underwriter with Lehman Brothers and Newman and Associates as Co-Managers. Staff is recommending a different underwriting team for the Single Family issue. The change is suggested because (1) a single family issue is structured differently, has different governing legislation, and requires different expertise, and (2) staff is striving to develop the best team to meet San Diego's needs.

The process for considering the underwriting team consisted of soliciting written proposals from bond underwriting firms, followed by an hour long discussion with representatives of these firms. The firms interviewed included Shearson/American Express Inc., E.F. Hutton & Company Inc., Stone and Youngberg, Miller & Schroeder Municipals, Inc., A.G. Becker Paribas Inc. and Dean Witter Reynolds Inc. Because staff has previously worked with Goldman Sachs, Lehman Brothers, Paine Webber, and Newman and Associates, these firms were not interviewed but were under consideration. Also, Kidder-Peabody and Solomon Brothers were given invitations to interview, but declined the invitation. Ben Montijo, Hal Kuykendall, Phil Rush and Gene Slater (Commission financial consultant) served as the interviewing panel. The criteria considered in evaluating the firms included: (1) competence, experience and responsiveness of the firm's representative assigned to liason with the Commission, (2) estimates on costs and pricing, (3) ideas on (a) marketing strategy (b) structuring the program, and (c) structuring the Bond issue.

E.F. Hutton has an excellent reputation for handling issues in an expedited fashion and excellent marketing capability. This firm took over the CCDC single family bond issues after several failures to market them and purchased/sold these within two weeks of taking over. Stone and Youngberg presented the lead person with the most experience. Goldman Sachs and Newman and Associates have performed effectively on the multifamily underwriting team, and it is proposed that they act as co-managers to add continuity to the underwriting team. These four firms appear to have an excellent working relationship between themselves.

Respectfully submitted,

Ben Montijo
Executive Director

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Attachment A: Time Schedule

ATTACHMENT A

Timeline for Single Family Bond Program

November - Advertise to developers.

November 21 - City Council approval of the program design.

December - Receive Commitment Requests from developers.

January 6 - Select projects.

January 23 - City Council approval of financing documents and Preliminary Official Statement.

January 31 - Bond sale.

February 22 - Bond closing.

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NOV 21 1983

Passed and adopted by the Council of The City of San Diego on NOV 21 1983, by the following vote:

Councilmen	Yeas	Nays	Not Present	Ineligible
Bill Mitchell	☑	☐	☐	☐
Bill Cleator	☑	☐	☐	☐
Gloria McColl	☑	☐	☐	☐
William Jones	☐	☐	☑	☐
Ed Struiksma	☑	☐	☐	☐
Mike Gotch	☑	☐	☐	☐
Dick Murphy	☐	☑	☐	☐
Uvaldo Martinez	☑	☐	☐	☐
Mayor Roger Hedgecock	☐	☐	☑	☐

AUTHENTICATED BY:

ROGER HEDGECOCK,
Mayor of The City of San Diego, California.

(Seal)

CHARLES G. ABDELNOUR,
City Clerk of The City of San Diego, California.

By Maybell L. [illegible], Deputy.

Office of the City Clerk, San Diego, California

Resolution Number R-259655 Adopted NOV 21 1983

CC-1276 (REV. 6-83)

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