



THE CITY OF SAN DIEGO

## Redevelopment Agency's Report

DATE ISSUED: June 20, 2007

REPORT NO.: RA-07-20  
RTC NO.: 07- 100

ATTENTION: Honorable Chair and Members of the Redevelopment Agency  
Council President and City Council  
Docket of June 26, 2007

SUBJECT: Line of Credit with San Diego National Bank for the Affordable Housing  
Opportunity Fund and the City Heights and Naval Training Center Project  
Areas

REFERENCE: Redevelopment Agency Report (RA-06-18) issued July 19, 2006  
Redevelopment Agency Report (RA-06-43) issued September 26, 2006

REQUESTED ACTION: Approve the Redevelopment Agency Execution of a Credit  
Agreement to establish separate lines of credit for the Affordable Housing Opportunity Fund and  
the City Heights and Naval Training Center Redevelopment Project Areas.

STAFF RECOMMENDATION: That the City Council approve the execution of a Credit  
Agreement with San Diego National Bank for \$70,000,000 by the Redevelopment Agency.

That the Redevelopment Agency:

1. Authorize the Executive Director or designee to enter into a Credit Agreement for six separate lines of credit between the Redevelopment Agency of the City of San Diego ("Agency") and San Diego National Bank in an aggregate amount not to exceed \$70 million for the City Heights, Naval Training Center, North Bay and North Park Redevelopment Project Areas.
2. Authorize the City Attorney to enter into an agreement with Best Best & Kreiger to provide bond counsel services for the \$70 million line of credit, in an amount not to exceed \$40,000.

SUMMARY: On December 6, 2006, a Request for Proposals was distributed to 20 commercial and investment banks for six separate non-revolving lines of credit or private placement in an aggregate amount of \$70 million for the City Heights, Naval Training Center, North Bay, and North Park Redevelopment Project Areas. The proposed lines of credit will be supported by either 20% low and moderate income housing set-aside funds ("Housing Set-aside") or 80% discretionary ("Non-housing") tax increment ("TI") revenue from each of the four project areas

in the following amounts:

<b>Project Area</b>	<b>Housing Set-aside TI</b>	<b>Non-housing TI</b>	<b>Total</b>
City Heights	\$11.0 million	\$20 million	
Naval Training Center	\$7.1 million	\$16 million	
North Bay	\$8.6 million		
North Park	\$7.3 million		
<b>Total</b>	<b>\$34.0 million</b>	<b>\$36 million</b>	<b>\$70 million</b>

**Line of Credit Structure and Financing Terms**

Two proposals were received from commercial banks: Bank of America and San Diego National Bank. After review of the proposals, the Agency’s financial advisor, Kitahata & Company, recommended the lines of credit with San Diego National Bank as the preferred lender, in terms of lower costs and greater flexibility.

The Summary of Terms and Conditions as negotiated with San Diego National Bank is provided as Attachment 1, together with the proposed Credit Agreement reflecting this information provided as Attachment 2. The lines of credit in the aggregate amount of \$70 million carry terms of three years and are secured by a subordinate pledge of the tax increment revenues generated within and received by the respective Project Areas, excluding those revenues required by law to be set-aside for tax-sharing purposes, and the amounts needed to service the outstanding tax allocation bonds for City Heights, North Bay and North Park. Interest-only payments are required on a quarterly basis, in arrears, and are expected to begin in September 2007. The proceeds of any future tax allocation bonds issued for the four project areas must first repay the respective lines of credit.

The lines of credit will be available as taxable borrowing. Funds will be drawn down on an as-needed basis. The interest rate is the lower of the 3-year U.S. Treasury plus 190 basis points or 30-day LIBOR<sup>1</sup> plus 110 basis points. As of May 2, 2007, the rate would be 6.65% based on the 3-year U.S. Treasury rate and 6.46% based on the 30-day LIBOR rate.

Independent Fiscal Consultant Reports were prepared for the project areas (Attachments 3 through 6) which show that sufficient tax increment revenue is available and is expected to be generated on an annual basis to support payments on each line of credit and existing bond obligations, and could support future bond issuances to ultimately pay off the lines of credit. These reports were provided to the banks as part of the Request for Proposal process for their evaluation to determine the ability of the Agency to commit funds for this purpose.

**Community Reinvestment**

San Diego National Bank received a rating of Outstanding by the Comptroller of the Currency in its August 2006 Community Reinvestment Act Performance Evaluation. The rating was based

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<sup>1</sup> London Interbank Offered Rate. The rate of interest at which banks offer to lend money to one another in the wholesale money markets in London. A standard financial index used in U.S. capital markets to set the cost of various variable-rate loans.

on tests of lending, investment and service. The Performance Evaluation is provided as Attachment 7.

**Uses of the Line of Credit Funds**

Affordable Housing Collaborative Opportunity Fund

In August 2002, the Comprehensive Affordable Housing Strategy was approved by the Redevelopment Agency, the Housing Authority and the City Council. The strategy was to leverage and aggregate the Redevelopment Agency’s Housing Set-aside funds to create up to \$55 million in affordable housing financing to fund the Affordable Housing Collaborative Program (“Affordable Housing Program”). Of the \$55 million, \$40 million was provided by proceeds from Centre City and Horton Plaza tax allocation bonds; the remaining \$15 million would be provided by the Redevelopment Division’s project areas’ Housing Set-aside funds. In January 2003, the Agency issued a Notice of Funding Availability (“NOFA”) to seek proposals for the development of new affordable housing units within the City of San Diego. The City’s Redevelopment Division, the Centre City Development Corporation (“CCDC”), the Southeastern Economic Development Corporation (“SEDC”) and the San Diego Housing Commission have been working together as the Affordable Housing Program to review and recommend projects for funding. The Affordable Housing Program has provided the four entities with an opportunity to work more efficiently and collaboratively on affordable housing projects.

To date, approximately \$52 million of the original \$55 million has been approved by the Agency for projects that have created a total of 831 affordable units. There are eight projects currently submitted for funding consideration and under review for an additional \$40 million. The demand for affordable housing funding assistance exceeds the original \$55 million Program funding by \$37 million. In July 2006, the Redevelopment Agency authorized the issuance of a Request for Proposals to secure a bank line of credit to provide funding for an Affordable Housing Collaborative Opportunity Fund (“Housing Opportunity Fund”). In addition, the Agency approved the treatment of the Housing Set-aside funds from the Redevelopment Division’s project areas as a revenue pool for the Housing Opportunity Fund.

The proposed lines of credit supported by the Housing Set-aside from the City Heights, NTC, North Bay and North Park Project Areas total \$34 million. Of that total, \$29 million will be available to the Housing Opportunity Fund for affordable housing projects including those currently under review. Approximately \$5 million of the borrowed funds would be dedicated to existing City Heights programs and the NTC Homeless Assistance Agreement remaining obligation.

<b>Allocation of Borrowed Funds</b>	<b>Amount</b>
Housing Opportunity Fund	\$29.0 million
City Heights Home in the Heights	\$2.0 million
City Heights Housing Rehabilitation	\$1.0 million
NTC Homeless Assistance Agreement	\$2.0 million
<b>Total</b>	<b>\$34.0 million</b>

The demand for affordable housing funding assistance exceeds the initial funding capacity of the

Redevelopment Division’s contribution to the Housing Opportunity Fund. If the current affordable housing projects under consideration proceed, an additional \$11 million will need to be raised in order to fund these projects.

City Heights Projects

In the City Heights Project Area, the following projects are proposed for funding by the City Heights Non-housing line of credit:

<b>Project/Obligation</b>	<b>Amount</b>
Purchase of surplus SR-15 parcels from City	\$5.0 million
Property acquisition (41 <sup>st</sup> and University)	\$2.0 million
Community Enhancements	\$5.0 million
Opportunity Property Purchase Fund	\$5.0 million
SDRC Loan Repay for City Heights Square Project/business relocation	\$3.0 million
<b>Total</b>	<b>\$20.0 million</b>

The total amount of the City Heights line of credit supported by Non-housing funding is \$20 million. It is anticipated that funds would be drawn down as needed within the next 12 to 18 months.

Draws on City Heights Line of Credit

The first draw on the City Heights line of credit is estimated at \$10 million which will be used for the purchase of the State Route 15 surplus parcels from the City, for property acquisition at 41<sup>st</sup> and University Avenue and for community enhancement projects.

Future draws on the line of credit will be used for additional community enhancement projects and a City Heights Opportunity Purchase Fund which will enable the Agency to purchase property as it comes on the market. With land costs expected to increase over time, securing funds now for property acquisition will reduce project costs. Future draws will also be used for repayment of the loan from San Diego Revitalization Corporation (“SDRC”) for the City Heights Square Project. The term of the SDRC loan is 20 years; however, the interest on the loan will be reduced from 8% to 6% if it is paid off no later than five years following disbursement. Interest on the \$3,000,000 developer loan is scheduled to begin at the start of construction.

Naval Training Center (“NTC”) Projects

The NTC Non-housing line of credit would be used for the following proposed projects:

<b>Project/Obligation</b>	<b>Amount</b>
Consultant Contract – Matrix Environmental Services	\$250,000
McMillin Loan	\$5.25 million

Public Improvements	\$6.0 million
Proposed Rosecrans/Midway Traffic Improvements	\$500,000
Proposed NTC Foundation Grant Agreement	\$4.0 million
<b>Total</b>	<b>\$16.0 million</b>

The total amount of the NTC line of credit supported by Non-housing funding is \$16 million. It is anticipated that funds would be drawn down as needed within the next 12 to 18 months.

Draws on the NTC Line of Credit

A portion of the first draw on the NTC line of credit will be used to fund a consultant contract with Matrix Environmental Services, the Agency’s consultant in negotiations with the Navy for the Early Transfer Conveyance and cleanup of the NTC boat channel. The NTC boat channel is the last remaining parcel of property to be conveyed from the Navy to the City. Staff had been in negotiations with the Navy in 2004 when the Agency’s credit ratings were suspended. Since all available tax increment revenue is pledged to the NTC master developer, McMillin-NTC, LLC (“McMillin”), for the costs described below, there has been no funding available to cover consultant costs for negotiating the transfer and clean up of the boat channel. With the NTC Park improvements underway, the transfer and cleanup of the boat channel can no longer be delayed.

In July 2003, the Agency entered into the Third Implementation Agreement to the Disposition and Development Agreement with McMillin which requires Agency reimbursement up to \$8.5 million, plus interest for additional City-imposed requirements for water, storm drain, and streetlight improvements. The actual cost of the improvements was estimated to be \$10.5 million. Repayment of these costs is to come from the “Pledged Revenues” which are defined as: 1) the Agency’s Share of Cash Available for Distribution pursuant to the Participation Agreement (which is currently projected to be zero dollars), and 2) available tax increment from the Naval Training Center project area, less amounts required to be set-aside for housing and tax-sharing purposes. The Third Implementation Agreement dedicates the NTC tax increment as a Pledged Revenue to repay McMillin, subject only to the off-sets described above.

To date, the Agency has reimbursed McMillin over \$4.7 million. All claims/invoices by McMillin are submitted to the Agency’s audit engineering consultant, David Taussig and Associates, who reviews the documentation for payment approval and then submits the request to the Agency for payment processing. The Agency has received the invoices for the remaining amount; however there is insufficient tax increment revenue for payment.

The Third Implementation Agreement requires the Agency to make good faith efforts to issue bonds by December 2005 with provisions for an extension to December 2006. Without the issuance of bonds, and without sufficient tax increment, the Third Implementation Agreement imposes an obligation on the Agency and McMillin to “meet and confer in good faith concerning revisions to the terms of repayment of the McMillin Loan without diminishing or otherwise reducing the rights, duties and obligations of the parties.”

In addition, Section 3. j.(7) of the Third Implementation Agreement states:

Except for Pledged Revenues, no funds or assets of the Agency shall be pledged to, or otherwise liable for, the satisfaction of the McMillin Loan under this Agreement. Nothing contained herein shall prevent the Agency from refinancing the McMillin Loan or making any payment to Master Developer from any other funds or assets of the Agency which may be legally used for such purpose. Master Developer agrees to subordinate its rights to the Pledged Revenues to the extent necessary for the Agency to issue the Agency Bonds or obtain other financing in order to repay in full the McMillin Loan.

The Agency and McMillin have met, and McMillin has agreed in writing to release the tax increment as a pledged revenue source for repayment of incurred costs in exchange for being reimbursed from the proposed line of credit. The tax increment would then be available as a dedicated source of revenue to repay SDNB for the draw-down on the NTC line of credit.

Other projects to be funded from the proposed line of credit include traffic improvements in the area served by the project area, NTC Park and shoreline enhancements and a proposed second rehabilitation grant agreement with the NTC Foundation, which will be brought to the Agency for consideration in the coming months. In February 2004, the Agency approved a Rehabilitation Grant Agreement (“Grant Agreement”) with the NTC Foundation which provided \$5.85 million from a HUD Section 108 loan. Annual payments of approximately \$509,000 on the loan are made from NTC tax increment revenue. The Grant Agreement provides for the Foundation to request further funding not to exceed \$6.0 million and matched at least dollar-for-dollar with other Foundation funding. The funding is to be used for the rehabilitation of buildings in the NTC Civic, Arts and Culture Center. Section 1.8 of the 2004 Grant Agreement, which refers to further funding requests, is provided as Attachment 8.

### **Financing Team**

The engagement of SDNB as the lender for this transaction was made through a competitive process. San Diego National Bank was selected based on the most competitive bid and flexible structuring options offered. Kitahata & Company has served as the Agency’s financial advisor since October 2002 and has proposed a fee not-to-exceed \$30,000 plus \$1,000 for out of pocket expenses for this transaction. The City Attorney’s Office has selected Best Best & Kreiger (“BB&K”) to serve as bond counsel on this transaction due to their previous experience serving in the same capacity on the Agency’s Series 2003 bond issuance and the 2006 Credit Agreement with Bank of America for the North Park line of credit. BB&K has proposed to provide such services for a fee in an amount not to exceed \$40,000.

FISCAL CONSIDERATIONS: There is no fiscal impact to the City or the City’s General Fund by this action to implement separate lines of credit borrowing for the Redevelopment Agency. All payments will be made from tax increment generated by the respective Redevelopment Project Areas.

Based on the projected uses of funds, estimated maximum debt service on the line of credit is

approximately \$165,000 per month, or \$1.97 million for a twelve-month period. Assuming \$47 million is drawn down in the next twelve months, the effective annual rate of borrowing is estimated at 4.20%, based on LIBOR rates or 4.32% based on US Treasury rates as of May 2, 2007. The Agency paid a \$10,000 Application Fee upon acceptance of the terms of the proposal. The fees related to consultants for this transaction will be pro-rated among the four project areas. These fees include (i) the bond counsel fees in an amount not to exceed \$40,000; (ii) the financial advisory services in an amount not to exceed \$30,000; and (iii) the SDNB counsel fees of approximately \$34,000, to which the \$10,000 Application Fee will be applied.

PREVIOUS COUNCIL ACTION: On May 23, 2006, the Agency authorized CCDC to issue \$79 million in tax allocation bonds and \$35 million in tax allocation housing bonds secured by tax increment revenue from the Centre City Redevelopment Project Area. The ratings and bond insurance received by the Centre City Project Area reflects the continued strength of downtown's economic growth and its corresponding tax revenues. Unfortunately, these same characteristics do not exist throughout all of the Agency's project areas, and it appears infeasible for the Agency to issue bonds within the City's Redevelopment Division Project Areas at this time. Because of this, it is recommended that a short-term line of credit be obtained to provide the funds to meet these needs and commitments, until a long-term bond issuance can be successfully completed. The Agency intends to fully repay and terminate the line of credit with a public offering of long-term tax allocation bonds within one year. Should the Agency be unable to issue such debt when the line of credit expires in three years, the Agency would have to renew the line of credit, or negotiate with a bank for a new line of credit, or repay the line with a private placement.

On July 25, 2006, the Agency authorized the issuance of an RFP to secure a bank line of credit in the amount of \$35 million to provide funding for an Affordable Housing Opportunity Fund. In September 2006, the Agency and the City Council authorized a \$10,000,000 line of credit with Bank of America secured by Non-housing tax increment revenues from the North Park Project Area. The line of credit was issued on October 31, 2006, with the first quarterly interest payments made in January 2007.

COMMUNITY PARTICIPATION & PUBLIC OUTREACH EFFORTS: On February 12, 2007 the City Heights Project Area Committee ("PAC") adopted a motion (9-1-1-2) to support the line of credit; there were two recusals. On March 13, 2007 the North Park PAC adopted a motion (8-0-0) to support the use of North Park Housing Set-aside tax increment revenue for the Housing Opportunity Fund line of credit. On April 11, 2007 the North Bay PAC adopted a motion (11-1-0) for the Agency to move forward on the line of credit. On March 15, 2007, the Peninsula Community Planning Board was notified of this action. No vote was taken; however, members requested that any proposed projects to receive funding from the line of credit be presented to the Board.

KEY STAKEHOLDERS AND PROJECTED IMPACTS: Business entities involved in this transaction are – San Diego National Bank (lender); Kathleen C. Johnson, Attorney at Law (Bank's counsel); Best Best & Kreiger (bond counsel); and Kitahata & Company (financial advisor).

Respectfully submitted,

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Janice Weinrick  
Deputy Executive Director  
Redevelopment Agency/  
Assistant Director  
City Planning & Community Development

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Approved: James T. Waring  
Assistant Executive Director  
Redevelopment Agency/  
Deputy Chief Operating Officer  
Land Use & Economic Development

Attachments:

1. Summary of Terms and Conditions
2. San Diego National Bank Credit Agreement
3. City Heights Redevelopment Project Area Fiscal Consultant Report
4. Naval Training Center Redevelopment Project Area Fiscal Consultant Report
5. North Bay Redevelopment Project Area Fiscal Consultant Report
6. North Park Redevelopment Project Area Fiscal Consultant Report
7. Community Reinvestment Act Performance Evaluation
8. Rehabilitation Grant Agreement Section 1.8