DATE ISSUED: November 21, 2003 REPORT NO. 03-250

ATTENTION: Honorable Chair and Members of the Land Use and Housing Committee
Docket of December 3, 2003

SUBJECT: Redevelopment Agency Low- and Moderate-Income Housing Set-Aside Percentage

SUMMARY:

Issue - Should the Land Use and Housing Committee consider raising the percentage of Redevelopment Agency tax increment that is set aside for low- and moderate-income housing as suggested by the Affordable Housing Task Force?

Manager's Recommendation – That the Land Use and Housing Committee consider the issue of raising the tax increment that is set aside for low- and moderate-income housing after the expenditure of already available affordable housing Notice of Funding Availability (NOFA) funds, as need demands and no later than 2007.

Other Recommendation – On October 22, 2003 the Budget/Finance Committee of Centre City Development Corporation (CCDC) considered this issue and recommended the following: continue to spend the $55 million of funds committed to the Affordable Housing NOFA; use the increased 20% tax increment stream for additional funds for the NOFA; CCDC is not in a position to allocate any of the 80% tax increment revenue at this time; and to annually review CCDC's finances.

Fiscal Impact – None.

Environmental Impact – This activity is not a "project" and is therefore exempt from CEQA pursuant to the State CEQA Guidelines Section 15060 (c) (3).

BACKGROUND:

In December 2002, the City Manager initiated the Affordable Housing Task Force in response to the City Council's declaration of a "State of Emergency Due to the Severe Shortage of Affordable Housing in the City of San Diego" in August of that year. The Task Force included a wide variety of experts representing various interests and perspectives in the City and was asked to take a comprehensive look at the housing situation in San Diego and then make recommendations for specific actions the City Council could take to address the issue.

On June 18, 2003 the Land Use and Housing Committee accepted the Task Force's final report and on September 3 and 17 and October 1, 2003 considered the City Manager's response and accepted the recommendation that the Redevelopment Agency conduct an analysis of existing debt service obligations in order to determine the immediate and future impact of an increase in the Redevelopment Agency's housing set-aside percentage from 20% to 35% for a total of $17.5 million per year.

Redevelopment Agency affordable housing revenues have totaled $105.1 million through Fiscal Year 2003 (see Attachment 1). The Agency has contributed to the provision of 2,677 completed units of affordable housing in the City of San Diego using its Low and Moderate Income Housing Fund (LMIHF) (see Attachment 2). In addition to annual tax increment, the LMIHF includes other revenue sources such as interest income, developer loan repayments and bond proceeds. The completed units include not only new and rehabilitated homes, but also first time homebuyer assistance and the acquisition of affordability covenants. To accomplish this, the Agency has spent a total of $81.4 million, or an average of $30,407 per unit. Added to these already completed projects, CCDC has encumbered through Agency agreements an additional $16 million to assist 391 more units of affordable housing, an average of $40,921 per unit.

In January 2003, the Redevelopment Agency issued a Notice of Funding Availability (NOFA) for Affordable Housing throughout the City of San Diego, committing $55 million over the next three to five years with the goal of assisting in the development of 2,184 new affordable units. Out of nine proposals received so far, there are currently six potential projects in the pipeline at various stages of review. Together, these six projects under review would produce 578 new units, and their development teams have requested approximately $21.6 million of the NOFA funds (an average of $37,370 per unit). Located in City Heights, Barrio Logan, Bankers Hill, Downtown and Southeast San Diego, these projects include family, senior and special needs housing. At least two of these projects are expected to be presented to the Agency for funding consideration by end of this calendar year.

DISCUSSION:

The Affordable Housing Task Force has recommended raising the amount of tax increment set aside for low- and moderate-income housing from 20% to 35%. As the City Manager's response indicated other Redevelopment tax increment has already been committed or earmarked for priority development projects around the City, and an increase in the set-aside percentage could limit the bonding capacity necessary to carry out such major capital projects.

CCDC

Downtown=s redevelopment is highly successful due to increasing private development that has generated growth in assessed values and tax increment. Along with this growth, the Centre City Development Corporation (CCDC) has been able to increase its obligations and commitments providing for the enhancement of downtown and allowing for the continued private sector investment in downtown.

The schedule of projected tax increment and obligations includes revenues generated from projects under construction and planned (see Attachment 3). Tax increment is expected to grow between 30% and 40% over the next several years, however, during the same period obligations are expected to grow on the order of 50%. These obligations and commitments include: an accelerated sale of tax allocation bonds pursuant to the MOU and the Fourth Implementation Agreement with the Padres relating to property and possessory interest taxes; a funding commitment for the Downtown Main Library; a funding of CCDC=s and the City=s portion of the North Embarcadero Alliance for the related waterfront improvements; and a continuation of the development of public parking facilities enhancing the accessibility to downtown entertainment and business activities for the Gaslamp Quarter District, Convention Center and the Ballpark. Additional ongoing obligations include the Agency payments associated with the tax sharing agreements with the various taxing entities (San Diego Unified School District, County of San Diego, Community College District, and the Office of Education). These obligations have recently increased from approximately 8% to 13% of gross tax increment. In addition, the Acredits@ that the Agency has been applying against its tax sharing obligations will be depleted by Fiscal Year 2006, causing the payments to increase substantially. A significant obligation, with an unknown magnitude, is the State taking redevelopment funds for the Education Revenue Augmentation Fund (ERAF). In Fiscal Year 2003 approximately 3% of tax increment was transferred to the State. In Fiscal Year 2004 the amount will be approximately 5% of tax increment. In years thereafter the amount is unknown. Capital improvement programs (public improvements), which include street lights in the Cortez and Little Italy Districts, street enhancements and public improvements along Market Street, 10^{th}, 11^{th} and 12^{th} Avenues, the King Promenade extension from Park Boulevard to MTDB Station, and AC@ Street improvements, require continued public funding. Also, the Community Plan update includes several elements that need to be addressed financially such as the development of parks to serve the planned residential community.

The Centre City Redevelopment Project currently enjoys an A+ Rating from Fitch Ratings and an A3 from Moody=s Investor Service which allows for the Agency to facilitate lower interest rates when bonds are issued. The primary reasons for the favorable rating are that the Agency maintains excellent debt service coverage on outstanding bond obligations and is successful in attracting private development. In the next several years, CCDC will be fulfilling the above described obligations with additional bond issues from projected tax revenue increases. The financial planning and structuring needs to be done strategically and with financial prudence so that the Agency can continue its success in attracting private development in downtown for the long term.

Although it is anticipated that substantial growth in tax increment will occur over the next several years, the revenues generated may fall short with all the needs and expectations that are necessary to continue the redevelopment efforts of downtown. Any modification to the existing allocation of tax increment revenues in the next several years will inhibit our ability to meet our existing commitments and diminish the flexibility in the Agency=s financial structure.

SEDC

Southeastern Economic Development Corporation (SEDC) continues to see an increase in the amount of tax increment revenue generated by the approved redevelopment activities in its four (4) Redevelopment Project Areas (see Attachment 3). Between Fiscal Year 1995 and Fiscal Year 2004, the projected tax increment has increased by 252%, and SEDC's approach to redevelopment continues to yield positive results. As a result of continuing to repay debt incurred by the Agency prior to SEDC's incorporation, SEDC has very limited resources.

SEDC's major source of project financing has been the 80% of tax increment revenue coupled by bonds issued. Maintaining favorable debt service coverage on outstanding bond obligations is one of the primary reasons that the Mt. Hope 2002A tax allocation bond issuance enjoys an "AAA" and "Aaa" municipal bond ratings from Standard & Poor's Ratings Services and Moody's Investors Service, respectively. Any deviation from the current allocation of tax increment revenues in the next several years will constrain SEDC's ability to meet current obligations and limit the flexibility of future bond issuance to finance major redevelopment projects including street improvements or any infrastructure.

Redevelopment Division

The City's Redevelopment Division manages 10 project areas, most of which are relatively new and are still working to establish their first catalyst projects. In order to adequately begin removing blight and to re-invigorate these newly designated areas, commercial, mixed uses and public infrastructure are fundamental recipients of redevelopment money.

In spite of this clear need to create non-housing projects, such affordable housing developments as City Heights Office and Townhomes, Metro Villas, Renaissance at North Park and Veterans Village have already received Agency funding from the LMIHF to support upcoming affordable housing units. CCDC has also contributed to some of these projects. These units and others currently under consideration will be available for occupancy within the next few years.

The Division also has existing bond obligations stemming from the North Bay and North Park issuance of tax allocation bonds in 2000 and by the end of this calendar year will be issuing more bonds for City Heights and North Park (again) in order to facilitate both affordable housing and non-residential development.

Overall tax increment in Division project areas has risen from only $500,000 in 1999 to an expected $16 million in FY 2005, a 3,100% increase within six years (see Attachment 3). The success of catalyst projects in each area is likely to contribute to even more increases in tax increment revenues, and caution should be exercised in re-allocating limited amounts of funds away from such projects at this time.

As with CCDC and SEDC, the Redevelopment Division has tax sharing and ERAF obligations each year.

CONCLUSION:

Tax increment revenues are expected to increase as are obligations and commitments of the Redevelopment Agency. As the $55 million already designated by the Redevelopment Agency for the NOFA process is consumed over the next five years by new affordable housing development, the need for designating additional set-aside monies may be revisited. Until such time, if an urgent need arises, non-low/mod funds (i.e. those that are not in the LMIHF) can be used to subsidize affordable housing projects. However, it should be noted that, once set aside in the LMIHF, tax increment money may not be used to fund non-affordable housing projects, regardless of their priority.

Respectfully submitted,

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Note: The attachments are not available in electronic format. A copy is available for review in the Office of the City Clerk.

Attachments:
1. LMIHF Summary through Fiscal Year 2003
2. Redevelopment Agency Cumulative Low- and Moderate-Income Housing Units through Fiscal Year 2003
3. Projected Tax Increment and Obligations