**ROSS FINANCIAL**

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March 9, 2023

Ms. Stacey Kurz
Director, Department of Housing and Homeless Services
City of Chula Vista
276 Fourth Street, Building A
Chula Vista, CA 91910

**Re: Otay Ranch Apartments**

Dear Ms. Kurz:

This analysis is provided in connection with the proposed issuance by the Chula Vista Housing Authority (the "Housing Authority") of a $4,000,000 tax-exempt multifamily housing revenue note (the "2023 Series A-1 Note") and an $870,000 taxable multifamily housing revenue note (the "2023 Series A-2 Note" and with the 2023 Series A-1 Note, the "2023 Notes") for the Otay Ranch Apartments currently known as the Encelia Apartments (the "Development"). The 2023 Notes will supplement the Housing Authority's prior issuance of a tax-exempt $35,000,000 multifamily housing revenue note on December 17, 2020 (the "2020 Note"). Citibank, N.A. ("Citi") in its capacity as construction and permanent lender purchased the 2020 Note and has agreed to purchase the 2023 Notes. Citi also made a subordinate taxable loan to the Borrower at the same time it purchased the 2020 Note.

This analysis updates the one prepared by Ross Financial, dated October 28, 2020 (the "Original Analysis"), for the Housing Authority in connection with its approval of the 2020 Note. The Original Analysis is attached.

## BACKGROUND

The Development is to consist of the new construction of three buildings providing an aggregate of 173 one, two and three-bedroom apartments to be rented to households earning 50% and 60% area median income (AMI) plus two managers' units. The Development is in a Planned Community or Sectional Planning Area identified as Village 8 West. The Developer, Meta Housing Corporation ("Meta"), anticipated a construction start date of March 1, 2021 based on the projected completion date of the site work that the master developer, HomeFed Corporation, needed to perform. That sitework included the relocation of a City of San Diego pipeline located beneath the Development site – which needed to occur before construction could commence on two of the three proposed residential buildings. Due to COVID-19 impacts, HomeFed was not able to complete the sitework until January 2022 – a ten month delay. While Meta was able to start construction of the residential building not affected by the pipeline relocation, the construction start of the other two buildings was delayed. As subcontractors could not hold their original pricing under volatile market conditions for construction materials, the Development was faced with higher costs.

The increased costs, in turn, created another problem. The higher costs caused the transaction to no longer qualify for low-income housing tax credits, which was a needed source of funding for the Development. Under Federal tax rules, to qualify for such tax credits, the tax-exempt obligations must exceed 50% of the Development's depreciable costs plus land (the "50% Test"). When the 2020 Note was issued in December 2020, the projections supported the conclusion that the 50% Test would be met. With higher costs, additional tax-exempt financing is needed. As many other projects in California experienced a similar situation, the California Debt Limit Allocation Committee ("CDLAC") created a special process to allow issuers to seek a "supplemental allocation" for purposes of the 50% Test.

On September 27, 2022, the Housing Authority on behalf of the Borrower, Otay Affordable I V8, LP, created by Meta, applied to CDLAC for a supplemental private activity bond alocation of $4,000,000. On November 30, 2022, CDLAC awarded the Housing Authority the requested Supplemental Allocation.

## PROPOSED FINANCING

***Project Costs and Funding***. According to most recent projections provided by Meta, the revised total cost of the Development, including construction and all soft costs, is now estimated at $80,362,757 – up from Meta's estimate of $73,407,980 contained it the Original Analysis. As with the Original Analysis, the estimated sources of funds will differ during the construction period and following construction and lease-up ("at permanent"). The current sources and uses are shown in the following table:

| Sources of Funds | Construction | Permanent |
|---|---|---|
| 2020 Tax-Exempt Note | $35,000,000 | $33,090,000 |
| 2020 Taxable Note | 17,420,000 | 2,900,000 |
| 2023 Tax-Exempt Note (Supplemental) | 4,000,000 | 0 |
| 2023 Taxable Note (Supplemental) | 870,000 | 0 |
| Seller Carryback | 3,000,000 | 3,000,000 |
| General Partner/Meta Loan | 1,732,658 | 0 |
| Low Income Housing Tax Credit Equity (Federal) | 6,380,981 | 29,341,440 |
| State Tax Credit Equity | 902,414 | 3,281,000 |
| Deferred Operating Reserve | 1,319,419 | 0 |
| Deferred Developer Fee and Costs | 9,737,285 | 8,750,317 |
| **Total** | **$80,362,757** | **$80,362,757** |
| **Uses of Funds** | | |
| Construction Costs (including site work) | $46,402,876 | 46,402,876 |
| Acquisition Costs | 279,933 | 279,993 |
| Contingency Costs | 1,000,000 | 1,000,000 |
| Impact and Permit Fees | 7,892,483 | 7,892,483 |
| Architectural & Engineering | 3,273,586 | 3,273,586 |
| Construction Interest and Fee | 5,682,628 | 5,682,628 |
| Legal and Miscellaneous Soft Costs | 5,013,780 | 5,013,780 |
| Reserves | 1,319,419 | 1,319,419 |
| Developer Fee* | 9,498,052 | 9,498,052 |
| **Total** | **$80,362,757** | **$80,362,757** |

*Cash portion of the developer fee is $747,735

***The Financing Approach***. The 2023 Notes will consist of a tax-exempt note and taxable note evidencing a loan to be made by Citi on a parity with the 2020 Note.

***The 2023 Notes***

Housing Authority will issue the tax-exempt 2023 Series A-1 Note in the estimated amount of $4,000,000 and the taxable Series 2023A-2 in the estimated amount of $870,000 (but not to exceed $1,000,000) to finance a portion of the increased costs of constructing the Development. The 2023 Notes will have the following features:

- The 2023 Notes will be purchased and funded by Citi on a draw down basis;
- The 2023 Notes will be issued in a separate series – one tax-exempt and the other taxable;
- The 2023 Notes will bear a variable rate based on the SOFR[1] index plus a spread (currently estimated at 7.92% for the 2023 Series A-1 Note and 8.42% for the 2023 Series A-2 Note;
- The 2023 Notes will be repaid after construction and lease-up (at “Conversion”) anticipated to occur in June 2024;
- The Note is expected to close on April 1, 2023.

[1] SOFR is an acronym for “Secured Overnight Funding Rate”, which is the primary successor index to LIBOR.

Citi will execute an investor letter in which it will represent that it has sufficient knowledge and experience to evaluate the risks and merits associated with making the loans evidenced by the 2023 Notes and has indicated its intention to hold the 2023 Notes for its account. Citi may transfer all or a portion of the 2023 Notes only to transferees that execute a document with similar representations.

***Housing Authority Financial Involvement***. The Housing Authority does not have any financial involvement with the Development. However, it previously executed an Inclusionary Housing Agreement with the Borrower that contains affordability restrictions that mirroring those contained in the tax-exempt Amended and Restated Regulatory Agreement and Declaration of Restricted Covenants (the "Tax-Exempt Note Regulatory Agreement").

***Affordability Restrictions***. The Development will continue to be subject to the following regulatory restrictions (collectively, the "Regulatory Agreements") and terms:

- Tax-Exempt Note Regulatory Agreement requirements (including voluntary elections made to CDLAC) for a 55-year term – which will be amended and restated to incorporate the 2023 Notes.
- Tax Credit Regulatory Agreement requirements under which all units must be affordable at 60% AMI for a 55-year term to remain eligible for tax credits; and
- Inclusionary Housing Agreement requirements which contain similar restrictions as contained in the Tax-Exempt Note Regulatory Agreement.

***Development Cash Flow***. The Borrower provided updated pro forma cash flows for the Development, reflecting changed revenue and expense assumptions.

| | |
|---|---|
| **Assumptions** | |
| Vacancy | 7% |
| Revenue Escalation | 2.5% |
| Expense Escalation | 3% |
| **Cash Flow and Coverage** | |
| Stabilized Net Income – First Full Year[1] | $3,166,806 |
| Expenses (includes Housing Authority monitoring fee and reserves) | (848,114) |
| Net Operating Income Available for Debt Service | $2,318,692 |
| Tax-Exempt Note Debt Service[2] | (1,629,786) |
| Taxable Loan Debt Service[3] | (151,561) |
| *Debt Service Coverage[4]* | *1.30x* |
| Cash Flow after Debt Service | 537,365 |
| LP Fee | (15,000) |
| AGM Fee | (20,000) |
| MGP Fee | (12,000) |
| Estimated Net Project Cash Flow | $490,365 |
| Deferred Developer Fee (Priority Payment) | (490,365) |
| Available Cash Flow after Deferred Developer Fee | $0 |

[1] Conversion is projected to occur in June 2024
[2] Assumes an initial permanent tax-exempt note par of $33,090,000 @ 3.83% interest and 40 year amortization
[3] Assumes initial permanent taxable loan par of $2,900,000 @ 4.28% interest and 40 year amortization
[4] Net operating income divided by total tax-exempt and taxable debt service

The following table shows the Borrower's most recent projected cash flow for the Development during first full five years following stabilized occupancy:

| | | Year | | | | |
|---|---|---|---|---|---|---|
| ***Escalation*** | **Revenues** | 1 | 2 | 3 | 4 | 5 |
| 2.50% | Gross Scheduled Rent | 3,322,462 | 3,405,524 | 3,490,662 | 3,577,928 | 3,667,376 |
| 2.50% | Other Income | 80,964 | 82,988 | 85,063 | 87,189 | 89,369 |
| | **less 7% vacancy** | (232,572) | (238,387) | (244,346) | (250,455) | (256,716) |
| 2.50% | **Other Vacancy Loss** | (4,048) | (4,149) | (4,253) | (4,359) | (4,468) |
| | **Total Net Income** | **3,166,806** | **3,245,976** | **3,327,125** | **3,410,303** | **3,495,561** |
| | | | | | | |
| | | | | | | |
| 3.00% | **Total Expenses** | **(848,114)** | **(875,030)** | **(902,875)** | **(931,664)** | **(961,428)** |
| | | | | | | |
| | **Net Operating Income** | **2,318,692** | **2,370,946** | **2,424,250** | **2,478,639** | **2,534,133** |
| | | | | | | |
| | Tax-exempt 2020 Note | (1,629,766) | (1,629,766) | (1,629,766) | (1,629,766) | (1,629,766) |
| | Taxable 2020 Note | (151,561) | (151,561) | (151,561) | (151,561) | (151,561) |
| | **Total Debt Service** | **(1,781,327)** | **(1,781,327)** | **(1,781,327)** | **(1,781,327)** | **(1,781,327)** |
| | | | | | | |
| | **Debt Service Coverage** | 1.30x | 1.33x | 1.36x | 1.39x | 1.42x |
| | | | | | | |
| | **Available Cash Flow after Bond Debt Service** | **537,365** | **589,619** | **642,923** | **697,312** | **752,806** |
| 3.00% | LP Fee | (15,000) | (15,450) | (15,914) | (16,391) | (16,883) |
| 3.00% | AGP Fee | (20,000) | (20,600) | (21,218) | (21,855) | (22,510) |
| 3.00% | MGP Fee | (12,000) | (12,360) | (12,731) | (13,113) | (13,506) |
| | **Project Cash Flow after GP and LP Fees** | **490,365** | **541,209** | **593,061** | **645,954** | **699,907** |
| | Deferred Developer Fee (Priority Payment) | (490,365) | (541,209) | (593,061) | (645,954) | (699,907) |
| | **Project Cash Flow after Priority Deferred Developer Fee** | 0 | 0 | 0 | 0 | 0 |
| | *Most expenses escalate at 3%; other expense components may vary | | | | | |

## PUBLIC PURPOSE

The 2023 Notes will provide needed additional funding to complete the Development, which is expected to result in the long-term affordability of 173 one, two and three-bedroom units in the City of Chula Vista: 53 units will be restricted and affordable to households earning 50% AMI; 120 units will be restricted and affordable to households earning 60% AMI; 2 units will be occupied by resident managers.

The Regulatory Agreements will require that these affordability levels be maintained for a period of 55 years.

## BENEFITS AND RISKS TO THE HOUSING AUTHORITY

The 2023 Notes provide a vehicle for funding the increased costs of the Development. As proposed, the 2023 Notes will enable the Borrower to complete the Development, which will result in the long-term affordability of 173 one, two and three-bedroom units in the City of Chula Vista with units restricted to income levels described in "Public Purpose" above.

The 2023 Notes do not pose undue financial risk to the Housing Authority. The 2023 Notes are not direct obligations of the Housing Authority or the City of Chula Vista. The 2023 Notes will evidence loans to be funded by Citi, which has indicated its intention to hold the 2023 Notes for its own account. All of the 2023 Notes will be repaid after construction and lease-up, expected in June 2024.

If the Housing Authority issues the 2023 Notes, it will receive an issuer fee at closing of $15,000 – equal to the larger of the minimum fee required under the Housing Authority's policy ($15,000) or 0.20% times the initial aggregate par amount of the 2023 Notes ($4,870,000) based on current projections ($9,740). The Housing Authority will continue to receive an annual monitoring fee of $17,000.

Costs of issuance will be funded by the Borrower from a source other than tax-exempt Series 2023A-1 Note proceeds.

## RECOMMENDATIONS

Ross Financial recommends that the Housing Authority proceed with the issuance of the 2023 Notes based on the following findings:

- The 2023 Notes will enable the completion of the Development, which will achieve a public purpose by providing 173 affordable units, with all units restricted to income levels at 50% and 60% of AMI.
- The 2023 Notes will evidence tax-exempt and taxable loans funded by a well-established, highly capitalized bank that is active in affordable housing lending. The 2023 Notes will be always subject to restrictive transfer limitations.

- The Borrower will pay issuance costs from sources other than tax-exempt Series 2023A-1 Note proceeds.
- Based on revised estimates provided by the Borrower, there should be sufficient funds to complete the Development and the Development provides adequate cash flow to cover debt service on the 2020 Note and the subordinate 2020 Taxable Loan made by Citi.

If there is any additional information you require concerning the Development, Ross Financial will be pleased to provide a supplemental analysis.

Very truly yours,

Peter J. Ross
Principal