

THE CALIFORNIA DEBT LIMIT ALLOCATION COMMITTEE
July 17, 2013

Consideration of a Request for a Waiver of Negative Points for The Horizons at Olive Street
Apartments (07-205)
Qualified Residential Rental Project Program
(Agenda Item No. 4)

ACTION:

Consider the approval of a Waiver of Negative Points for The Horizons at Olive Street Apartments (07-205, the "Project"). The Project received an award of allocation from the Committee at the meeting held on December 5, 2007.

BACKGROUND:

An Applicant bears the risk of forfeiting all or part of their performance deposit and receiving negative points if the Allocation is not used in accordance with the conditions and timeframes set forth in the California Debt Limit Allocation Committee ("CDLAC") Resolution. As provided for under the Government Code, CDLAC permits an Applicant to request the waiver of the forfeiture of the performance deposit and negative points if the allocation is not used to issue the bonds within the set timeframe given. For a waiver to be approved, the CDLAC Executive Director subjects the request to two tests: 1) was the issue or event that prevented the issuance of the bonds unforeseen; and 2) was the issue or event wholly outside the control of the Applicant and Project Sponsor. A request must pass both tests.

On December 5, 2007 the Horizons at Olive Street Apartments Project ("Project") was awarded \$9,100,000 in tax-exempt bond allocation. The Project's bonds were issued March 20, 2008 and a minimal amount of proceeds were placed in a guaranteed investment contract (GIC); essentially as a "Dry Closing". CDLAC's program regulations and related scoring criteria emphasize the readiness of a project to deploy the issued bond's proceeds and move forward with construction. While CDLAC strongly recommends against Dry Closings, it is not a prohibited act under the Internal Revenue Code or the CDLAC Regulations. Nevertheless, negative points were assessed against Hesperia Housing Investors, L.P. (including its owners and principals, the "Project Sponsor") for failure to use bond proceeds and deliver the public benefits as required by the approved and accepted CDLAC Resolution. The penalty was assessed on October 18, 2011 (when CDLAC first learned of the non-compliance), and is set to expire on October 18, 2014.

DISCUSSION:

On January 19, 2006, the Project Sponsor entered into a Land Purchase Agreement to acquire the Project site in Hesperia. In October of 2007, the City of Hesperia Community Redevelopment Agency (and the successor parties, the "City") adopted a resolution committing \$7.25 million in Housing Set-Aside Funds to the Project. That same month, the Project Sponsor applied for a tax exempt bond award from CDLAC; issuing the bonds in March 2008. At the time, the City voiced no issues with the Project.

In June of 2009, the Hesperia City Council approved and later executed an Owner Participation Agreement ("OPA") with the Project Sponsor. The OPA included the provision of the \$7.25 million in funding for the construction of the Project. However, on March 15, 2011, the City terminated the OPA, claiming that certain conditions were not met. The Project Sponsor disputed this, and subsequently submitted a claim against the City in May of 2011 for damages in the amount of \$5,669,000. With the

claim pending, and without the \$7.25 million available for the construction of the Project, the Project Sponsor was forced to redeem the bonds in July 2011.

On November 4, 2011, the Project Sponsor filed a complaint against the City in San Bernardino County Superior Court charging breach of contract amongst other actions. Through mediation, the parties agreed to tentative terms for settlement on June 19, 2013. In essence, the City has agreed to purchase the Project site from the Project Sponsor for nearly the amount of the complaint's damages; \$5,650,000. The City has also acknowledged that the events that led to the litigation will not affect the future business of the Project Sponsor and its affiliates in and with the City of Hesperia.

While there is no admission of fault by the City here, the terms of the settlement agreement would make the Project Sponsor nearly whole. Further, the Project Sponsor would be free to do business with the City in the future without prejudice. Based upon these facts, CDLAC staff believes it is fair to conclude that the OPA termination was an unforeseen act by the City, and that the Project Sponsor was not demonstrably at fault. Therefore, CDLAC staff believes that the Project Sponsor's waiver request satisfies both waiver tests, and staff recommends approval by the Committee.

RECOMMENDATION:

In light of the circumstances described, staff recommends the approval of the Waiver of Negative Points for The Horizons at Olive Street Apartments (07-205).

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