Atascadero City Council
Management Report – Community Development Department

Inclusionary Housing Policy
Moderate Income Unit Equity Sharing Policy
Resale Restriction Waiver Option

RECOMMENDATION:

Council adopt Draft Resolution A giving the City Manager the authority to waive the requirement to record a silent second for moderate income units upon sale to a qualified buyer when the sales price and appraised value are at or below the maximum applicable moderate income sales price.

DISCUSSION:

Background:

The City Council adopted an equity sharing policy for moderate income inclusionary housing units in November 2005. The equity sharing program allowed deed restricted, moderate income units to convert to market rate units prior to the end of the 30-year affordability term. The program was designed to encourage long term homeownership of affordable units and provided some protections for buyers against drops in affordable sale prices.

When the original 2003 inclusionary policy and the 2005 equity sharing program were created, San Luis Obispo County was in the midst of a housing boom with record increases in housing prices. As a result, moderate income units were being sold at more than $100,000 below appraised values. For this reason, it was very important to restrict the resale prices of these units so that buyers could not quickly resell the units and realize a huge windfall profit.

Since that time, the housing market has collapsed and the price range for some affordable moderate income units are at, or above the market rate appraisals.
Summary:

The City’s resale restrictions and silent 2\textsuperscript{nd} trust deed were created to provide a moderate-income qualified buyer the opportunity to own their own home. The program allows the moderate income buyer to share in the profits upon sale if the price of the home goes up and insulates the buyer from large losses upon sale if the price goes down. The program also allows the City to share in the profits when the unit sells for the unrestricted price. Although the City “loses” the affordable unit, the amount received in original equity and in profits can then be used to assist another moderate-income buyer in purchasing a home. This system is intended to provide additional funding to replace those affordable units that are converted to market rate units.

Since 2002, the City has approved nearly 1800 dwelling units of which about 600 have been completed. Of these units, 103 were required to be moderate income units. About a third of these moderate income units have been completed, leaving about 70 moderate income units still to be built and sold.

Under the City’s current policies, the following requirements apply to the original sale of a moderate income unit:

1. Set maximum sales price consistent with SLO County’s Affordable Housing Standard (March 2010: three bed moderate income unit max price $295,000).
2. Sell unit to a qualified moderate income buyer verified by HASLO.
3. Record a silent second mortgage covering the difference between the appraised value and the sales price including:
   - Deed of trust in favor of City of Atascadero
   - Promissory note (secured by deed of trust)
   - Resale and refinancing restriction agreement
   - Request for Notice of Default for 1\textsuperscript{st} trust deed
4. Record release of the original developer affordable housing deed restrictions for Moderate Income Units.
This bulletin summarizes the county's affordable housing standards including maximum household incomes, home purchase prices and rents. It applies to new projects in both the Coastal and Inland portions of the County.

**Income limits:**
The state defines family income groups as follows: "**Extremely Low Income**" is defined by Health and Safety Code Section 50106 as 30% of county median income; "**Very Low Income**" is defined by Health and Safety Code Section 50105 as 50% of county median income; "**Lower Income**" is defined by Health and Safety Code Section 50079.5 as 80% of county median income; "**Moderate Income**" is defined by Health and Safety Code Section 50093 as 120% of county median income; "**Workforce**" is defined by Title 22 of the County Code as 160% of county median income. The following income limits are effective as of April 3, 2009.

<table>
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<tr>
<th>Persons in Family</th>
<th>Extremely Low Income</th>
<th>Very Low Income</th>
<th>Lower Income</th>
<th>Median Income</th>
<th>Moderate Income</th>
<th>Workforce</th>
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**Sample maximum sales prices:** (see footnotes)

<table>
<thead>
<tr>
<th>Unit Size (Bedrooms)</th>
<th>Extremely Low Income</th>
<th>Very Low Income</th>
<th>Lower Income</th>
<th>Moderate Income</th>
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<tr>
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<tr>
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<td>$59,000</td>
<td>$110,000</td>
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</table>

**Note 1:** Homeowner association due (HOA) assumption per month is 150.00

**Note 2:** Mortgage financing assumed at a fixed rate for 30 years (per HSH Associates) is 5.28%

**Note 3:** Prices shown are preliminary estimates and may be revised. Round to the nearest 1000th.

**Note 4:** Actual sales price limits will be determined by the County on a case-by-case basis.
As a result of the housing market collapse, many of the uncompleted housing projects have fallen into bankruptcy. As the bankruptcies are resolved, new owners have been acquiring projects or sometimes individual lots within these projects. City Staff has seen cases of this occur in developments throughout the City.

One of these cases is Andy Fetyko’s Regio Place planned development project on north El Camino Real past Carrizo Road. The project was originally conditioned to provide six moderate income units (see following map). All of the affordable units have been partially constructed, but none have been finaled. The unit at 5419 Regio Place has been acquired by Consolidated Properties Group, LLC and is being represented by Paul Bischoff. Mr. Bischoff has been in contact with City staff over the past six months regarding completing the unit and the affordable housing requirements. Mr. Bischoff has reactivated the building permit and has passed the drywall inspection.

On January 29, 2010, Mr. Bischoff submitted a letter to the City asking to remove the affordable housing restriction from the property due to hardships resulting from the actions of the previous owner and lender (see Attachment 1).
Analysis:
The staff Housing Committee has met and reviewed Mr. Bischoff’s letter. Staff is sympathetic to financial hardships that his clients have experienced as an investor in the project. However, staff is opposed to waiving the affordable housing restriction for this individual property for the following reasons:

1. The project received additional units and approval as a result of providing affordable units.
2. Most real estate investors in the City, if not the State, have experienced some level of financial hardship over the past few years.
3. Waiver of this unit would set a precedent to waive affordable requirements on all un-built affordable units, potentially over 100 moderate, low and very low income units.
4. City housing policies must be applied uniformly and cannot provide individual exceptions.

However, staff thinks that a solution exists that will address Mr. Bischoff’s underlying concern, which is that the deed restriction and resale requirement would create a disincentive for a buyer. Because a buyer could purchase a market rate unit for the same cost as a deed restricted affordable unit, there appears to be a disincentive to purchase the affordable unit if there are a number of deed restrictions and resale requirements. Therefore, staff is recommending that the deed restrictions be dropped when the value of market rate units is below the moderate income sales rate.

Staff is recommending that the Council adopt a policy that authorizes the City Manager to waive the third requirement of the moderate income housing program at close of escrow, when the sales price/appraised value of a unit is below the Affordable Housing Standard for a moderate income unit and the unit is sold to a qualified buyer. This policy would continue to require the unit to be sold at an affordable moderate income price and guarantee the buyer had a qualifying income, which is the intent of the inclusionary housing policy. This policy change would be applied to all unbuilt / unsold moderate income units. This policy change would not affect low and very low income units because they are not subject to the equity sharing program.

1. [no change]:
   Set maximum sales price consistent with SLO County’s Affordable Housing Standard.
2. [no change]:
   Requirement to sell unit to a qualified moderate income buyer verified by HASLO.
3. [change]:
   City Manager authorized to waive the requirements to record the following at close of escrow:
o Deed of trust in favor of City of Atascadero
o Promissory note (secured by deed of trust)
o Resale and refinancing restriction agreement
o Request for Notice of Default for 1st trust deed

4. [no change]:
City Manager authorized to release:

- Original developer affordable housing deed restriction for Moderate Income Units

CONCLUSION:

Significant changes in the housing market have created new conditions that affect the City’s affordable housing program. The City’s inclusionary housing program has required the construction of over 200 affordable moderate, low and very low income units in nearly 50 different housing projects across the City. While the City should continue to implement its inclusionary housing program, some adjustments are warranted by economic conditions. The proposed changes would be consistent with the intent of the inclusionary housing program while removing unnecessary barriers to the sale of affordable housing units.

The proposed policy refinements would:

1. Meet the intent of City’s affordable housing policy by insuring the unit is originally sold to a qualified buyer. The developer will be required to have HASLO certify the buyers. (The current cost is $300).

2. Eliminate the large disincentive to potential purchaser by removing any future restrictions or cloud on the deed once it is sold to a qualified buyer.

3. Protect the City’s future interest in affordable housing by not removing the restrictions until the unit is sold to a qualified buyer. (If the unit is held by the developer until the market turns around, the City’s existing policy remains in place.)

FISCAL IMPACT:

No immediate fiscal impact, however this change in policy will reduce future amounts available for investment in moderate income housing.
ALTERNATIVES:

- The Council may choose to refer the item back to staff for additional analysis. Clear direction to staff should be provided on additional information or policies that are desired.

ATTACHMENTS:

Attachment 2: Draft Resolution A
January 29, 2010

Mr. Warren Frace
Community Development Director
City of Atascadero
hand delivered

Mr. Frace,

Please accept this letter as notice that I would like to start the process to be heard before the City Council regarding the Affordable Housing agreement for Tract 2577, signed by the developer Doya Partners II, LLC (Doya), and the City.

My company, Bischoff Properties, Inc., is completing the construction at 5419 Regio Place, and is the local representative of Consolidated Properties Group, LLC (Consolidated). Consolidated, which has two individual owners, now owns the property by virtue of its completing a foreclosure sale.

With respect to this affordable housing agreement, we request that the City Council remove the restrictions on the particular property at 5419 Regio Place. Consolidated makes this request because (i) its interests appear to pre-date the City’s affordable housing restriction, (ii) the affordable housing restriction will make the property impossible to sell (and will not effectuate its purpose to increase workforce housing), and (iii) Consolidated, like many others, is a victim of Estate Financial and its principals, Karen Guth and Joshua Yaguda, and a removal of the restriction will get the home sold and occupied and will reduce Consolidated’s significant loss on the property.

The master Deed of Trust encumbering the entirety of Tract 2577, including 5419 Regio Place, was originally recorded on February 8, 2005 (Instrument No. 2005-009951). Consolidated was to receive 100% of the beneficial interest in the master deed of trust 5419 Regio Place. To effectuate that, on July 25, 2005, EFI recorded an Assignment of Construction Deed of Trust (Instrument No. 2005-060618), which was intended to assign to Consolidated 100% of the beneficial interest in the master Deed of Trust for the subject property. Instead of making the assignment out properly, EFI assigned 100% beneficial interest in the entire master Deed of Trust (encumbering the entire subdivision) to Consolidated without reference to the subject property. Other investors in the subdivision also received a similar assignment. Regardless of the error, however, it is my understanding that Consolidated owned, at least equitably, the entire beneficial interest of the deed of trust effective in July 2005.

We believe that both the master deed of trust and the assignment giving Consolidated the beneficial interest in the deed of trust predate the City’s recorded Affordable Housing Agreement dated June 21, 2007 (Instrument No. 2007-042142). Certainly, Consolidated was not aware of any affordable housing restrictions when it agreed to provide nearly $300,000 to EFI to make the loan. In looking at the Affordable Housing Restrictions, it does not appear to be signed by the lender, either EFI on its own behalf, by EFI on behalf of the beneficiaries (i.e. Consolidated), or by Consolidated itself. Instead, it was only signed by the owner, Doya Partners II. As such, I do not believe that the master deed of trust or Consolidated’s assigned interest in it was ever “subordinated” or made subject to the Affordable Housing Restrictions.
EFI's fraud in dealing with Consolidated was significant. While I won't belabor the point by giving all of EFI's misrepresentations, two of them are significant and important for the City to consider. First of all, EFI never disclosed to Consolidated that its principals took a significant equity interest in Doya Partners II. Indeed, after the loan defaulted and EFI flatly refused to enforce the terms of the deed of trust (as servicer for Consolidated), Consolidated initiated an arbitration against EFI as required under the servicing agreement. Perhaps it was not surprising that EFI, run by Guth and Yaguda, was reluctant to foreclose on Guth and Yaguda's ownership interests in the project. Still, it was surprising and disconcerting for Consolidated to learn of the direct conflict of interest between servicing the loan and acting as a borrower under the loan. Second, as mentioned above, Consolidated had no idea that the lot might be subject to affordable housing restrictions. It should be noted that at the time of entering into the Affordable Housing agreement, a moderately affordable, 3-bedroom unit would be able to be sold for $261,131 under the agreement. As the loan amount for the property in which Consolidated had beneficial interest was $299,250, it is clear that Consolidated had no knowledge of this agreement, as no one would be willing to offer a 115% loan-to-value construction loan, with no opportunity for property appreciation.

Instead of just letting the property sit vacant, contributing to another unsightly ghost town in the City, Consolidated has been aggressive in trying to complete the partially-constructed home and to obtain clear title so that it can be sold. Among other things, Consolidated has:

1. Filed the arbitration against EFI in October 2007 to take over servicing of its loan;
2. Filed an action in San Luis Obispo Superior Court (Case No. CV 071107) in November 2007 against EFI, Guth, Yaguda, and Doya for fraud and against all 200 other investors in the project in order to obtain clear title to foreclose on 5419 Regio Place;
3. Settled the arbitration and lawsuit with the settlement requiring EFI to correct the deed of trust assignment of the master trust deed;
4. After EFI entered bankruptcy, moved for relief from stay in order to be given the right to foreclose against the property;
5. Obtained relief from stay in the bankruptcy court and agreed to pay the EFI Trustee $10,000 to foreclose on the property and convey insurable title to Consolidated as high bidder;
6. Completed the foreclosure of the property;
7. Hired me, as contractor, to complete construction of the home at 5419 Regio Place; and
8. Advanced (or is in the process of advancing) $90,000 to complete the construction.

As indicated in No. 3 above, EFI was required by the settlement to correct the deed of trust assignment to allow Consolidated to foreclose. Instead of recording the correction as required and without Consolidated's knowledge or approval, EFI recorded recissions of the master deed of trust and the assignment and recorded a new deed of trust against 5419 Regio Place on January 16, 2008. This recording was unlawful (as Consolidated never approved it), but required Consolidated to either file additional lawsuits against EFI and all of the 200 other investors in Tract 2577 to quiet title or continue with the foreclosure of the 2008 trust deed. If EFI had not recorded the 2008 documents unlawfully,
Consolidated could have foreclosed on its 2005 deed of trust and removed the 2007 affordable housing restrictions by virtue of the foreclosure. Unfortunately, due to the 2008 recordings, no title company will insure that the affordable housing restrictions have been eliminated without a document confirming that from the City.

Not only does Consolidated believe that they have the right to title without affordable housing restrictions, but application of the City's affordable housing restrictions in this instance is counterproductive. In February 2009, Consolidated obtained a property appraisal on the subject property from Jerald W. Jecker showing the completed home to be worth $280,000 assuming that the affordable housing restriction did not affect the property. Now, a year later, this value is likely lower.

Currently, in January 2010, the home's maximum price under the moderately affordable designation would be $289,000. Since the maximum price is higher than what the home would likely sell on the open market with no restrictions, Consolidated will have to greatly reduce the price to garner any interest (if any qualified buyers are even out there), as a potential buyer would be foolish to purchase a deed-restricted home for anywhere near the same price as he would pay for a non-deed-restricted home.

A potential buyer will also have to jump through the hoops to purchase the deed-restricted home, including qualifying for the purchase. The potential buyer also would know that, when it came time for him to sell the property, his potential buyer pool will be reduced as well. Coupling that with the elimination of almost all market appreciation, it likely will make the home unsalable due to these exceedingly negative factors. What is more likely to happen, if the City refuses to remove the affordable housing restrictions, is that the home will remain vacant and remain part of the City's unsold inventory and Consolidated will be victimized again (notwithstanding its years of effort and additional expense since making the $300,000 loan -- i.e. nearly $150,000 in construction costs and attorneys' fees).

To close, please take this narrative as introduction to the discussion we will hopefully have at the City Council meeting. There have been many parties harmed by the actions of the principals of EFI. The members of Consolidated are indeed victims of the fraudulent actions of EFI, and I view this as an opportunity to correct some wrongs that were unjustly put upon my clients. I look forward to discussing this with you and the Council at the appointed City Council meeting.

Yours sincerely,

Paul Bischoff, President
Bischoff Properties, Inc.
DRAFT RESOLUTION A

RESOLUTION OF THE CITY COUNCIL OF THE CITY OF ATASCADERO, CALIFORNIA, REVISING THE REQUIREMENTS FOR THE SALE OF DEED RESTRICTED, MODERATE INCOME UNITS WHEN THE SALES PRICE AND APPRAISED VALUE ARE AT OR BELOW THE MAXIMUM APPLICABLE MODERATE INCOME SALES PRICE

WHEREAS, the Atascadero General Plan and Housing Element recognize the importance of providing a range of affordable housing units for the residents and employees of Atascadero; and,

WHEREAS, the City of Atascadero has adopted an inclusionary housing policy that requires certain development projects to provide 20% of the dwelling units as deed restricted affordable units; and,

WHEREAS, the City has approved projects with over 200 inclusionary units as a condition of development; and,

WHEREAS, the City created an equity sharing program for moderate income inclusionary housing units that permit the units to be converted to market rate units; and,

WHEREAS, a severe national recession occurred in 2008 with significant impacts on the value of housing and the construction industry; and,

WHEREAS, due to the recession, the value of market rate homes have dropped to levels at or below the maximum sales prices identified for moderate income housing units; and,

WHEREAS, the City’s standard deed restrictions and resale restriction for moderate income units are unnecessary and cumbersome when the appraised value of market rate housing units is equal or below the maximum sales prices of moderate income units; and,

NOW, THEREFORE, BE IT RESOLVED, by the City Council of the City of Atascadero:

The City Council hereby authorizes the City Manager or designee to waive the requirement to record the following documents for moderate income units upon sale to a qualified buyer when the sales price and appraised value are at or below the maximum applicable moderate income sales price:

1. Deed of trust in favor of City of Atascadero
2. Promissory note (secured by deed of trust)
3. Resale and refinancing restriction agreement
4. Request for Notice of Default for 1st trust deed

On motion by Council Member _______________________ and seconded by Council Member ________________________, the foregoing Resolution is hereby adopted in its entirety on the following roll call vote:

AYES:

NOES:

ABSENT:

ADOPTED:

CITY OF ATASCADERO

By: ______________________________
   Roberta Fonzi, Mayor

ATTEST:

Marcia McClure Torgerson, C.M.C.,
City Clerk

APPROVED AS TO FORM:

_____________________________
Brian A. Pierik, City Attorney