



## ***Atascadero City Council***

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### ***Staff Report – City Manager***

#### **Inclusionary Policy Equity Sharing Program Loan Document Revision**

#### **RECOMMENDATIONS:**

Council:

1. Authorize staff to hire the law firm of Goldfarb Lipman LLP at an estimated cost of \$10,000 to revise the Inclusionary Policy Equity Sharing Loan Program; and,
2. Authorize the Director of Administrative Services to appropriate \$10,000 from the In Lieu Low/Moderate Housing Fund for Revision of the Inclusionary Housing Loan Documents.

#### **DISCUSSION:**

On or about November 2005, the City Council approved the Inclusionary Policy and Equity Sharing Loan Program. The loan program allows a qualified buyer(s) to buy a home at a price that is affordable to moderate-income households but is less than the home's fair market value. In exchange for this opportunity, the buyer(s) owe the City the difference between the home's fair market value and the affordable price paid for the home. This is the City Loan, or Second Trust Deed. To date, 21 units are under the loan program.

Staff has been contacted by a couple of buyers under the program that used adjustable rate loans to finance their original purchase. These loans have either adjusted or will soon do so. The homeowners have attempted to refinance to lower fixed rate loans, only to learn that the value of their home has declined such that the loan to value (LTV) with both the first and second trust deeds in place makes it unattractive to lenders to provide a new loan. As a result, staff has received notice from one homeowner of their intent to put the property on the market for sale, which could lead to the loss of that affordable unit. These homeowners and their lenders have approached staff with the request that the City consider reworking the "City Loan" so as to improve the possibility of obtaining a new fixed rate loan.

Staff consulted with Barbara Kautz from Goldfarb Lipman LLP, who believes that it may be possible to revise the structure of the City's loan to allow a new loan to meet the lender's 90% LTV requirement. The City would essentially lower its value in the second trust deed to meet the requirement, and in exchange would receive a higher percentage of contingent interest. This approach is intended to give the City the same amount as the original loan upon sale of the property. There is potentially more risk to the City using the revised loan structure in the event of default, however, staff believes that the exposure is not significant and the value to the community of keeping the affordable units available to homeowners outweighs the risk.

Conclusion: Should the Council approve, it will take Goldfarb Lipman LLP two to three weeks to draw up the new loan documents.

### **FISCAL IMPACT:**

\$10,000 from the In Lieu Low/Moderate Housing Fund.

### **ALTERNATIVES:**

1. Take no action.
2. Direct Staff to investigate other alternatives as identified by the City Council.
3. The Council may choose to refer the item back to staff for additional analysis.

### **ATTACHMENTS:**

Exhibit A - Example worksheet

## EXHIBIT A

### Example Worksheet

**Current Loan Structure Example:**

Market Value at time of purchase:	\$500,000
Affordable Purchase Price:	\$300,000
Second Trust Deed (City Loan):	\$200,000
City's interest in the property:	40%

Under the current loan structure and in accordance with the affordable housing program, the developer sells the home to the applicant for a specified affordable price which is under market value. In this case, if the market value at the time of purchase was \$500,000, the sales price of the home might be \$300,000. The applicant would qualify for a first trust deed loan of \$300,000. The City's principle share in the property under the program would be \$200,000, or 40%.

Once the homeowner decides to sell the home, they may sell the home at market value. The proceeds from the sale would be distributed as follows:

1. First the homeowner (and thus the first deed lender) would receive proceeds up to the original affordable purchase price of the home
2. In second position, the City would receive any remaining proceeds up to the original amount of the City's second trust deed in the home
3. Finally, any proceeds above the original market value of the home would be split based on the % equity in the property at the time of the original purchase of the home. (In this example, the homeowner would receive 60% or remaining proceeds and the City 40%)



**Proposed Revised Loan Structure Example:**

Revised Agreement

Market Value at time of refinance:	\$400,000
Affordable Purchase Price (Refinanced Loan):	\$300,000
Second Trust Deed (City Loan):	\$60,000
Loan to Value ratio (LTV)	90%

Under the proposed loan structure, if the home was appraised at \$400,000 today for the purpose of refinancing, the total amounts of the loans on the home can only equal 90% of the value of the home in order to qualify to refinance. If the homeowners maintain their current loan amount of \$300,000, the City would need to drop the amount of the second trust deed to \$60,000, but would earn 100% of the net gain up to the value of the old loan amount.

In this case, at a later date when the homeowner decides to sell, the proceeds from the sale would be distributed as follows:

1. First the homeowner (and thus the first deed lender) would receive proceeds up to the original affordable purchase price of the home
2. In second position, the City would receive any remaining proceeds up to the original amount of the City's new revised (lower) second trust deed in the home
3. The City would then receive any remaining proceeds up to the original market value of the home as contingent interest.
4. Finally, any proceeds above the original market value of the home would be split based on the % equity in the property at the time of the original purchase of the home. (In this example, the homeowner would receive 60% or remaining proceeds and the City 40%)

Sales price	
\$0 to \$300,000 Homeowner / 1st Deed Trust	Homeowner/ 1st Deed Lender receives 100% of the proceeds up to the original affordable purchase price
\$300,001 to \$360,000 City's 2nd Deed Trust	City receives 100% of the proceeds between the original affordable price and the new revised 2nd Deed Trust amount
\$360,001 to \$500,000 City contingent interest	City receives 100% of the proceeds between the 90% LTV amount at refinancing and the original market value as contingent interest
\$500,001 and above 60% to Owner 40% to City as contingent interest	Homeowner and City split proceeds exceeding the original market value of the home. The split is based on % share at the original purchase date