

# HOUSING AND REDEVELOPMENT AUTHORITY OF THE CITY OF SAINT PAUL, MINNESOTA

REPORT TO THE COMMISSIONERS

DATE: May 8, 2013

**REGARDING: APPROVAL OF SUBORDINATION OF THREE HRA LOANS FOR REFINANCING OF THE SIBLEY PARK APARTMENT PROJECT, AMENDMENT TO \$750,000 HOME LOAN NOTE, and SALE OF \$750,000 HOME LOAN NOTE AND \$250,000 HRA LOAN NOTE TO SHERMAN ASSOCIATES Inc., District 17**

## **Requested Board Action**

The specific actions being requested of the HRA Board are as follows:

1. Approval of subordination of \$750,000 HOME loan.
2. Approval of subordination of \$250,000 HRA loan.
3. Approval of subordination of \$500,000 HRA loan.
4. Approval of an amended and restated \$750,000 HOME loan note.
5. Approval of execution of purchase agreement with Sherman Associates Inc. for the sale of the amended and restated \$750,000 HOME loan note and the \$250,000 HRA loan note.

## **Background**

The Sibley Park Apartments Limited Partnership (“Developer”) proposes to refinance a \$9,250,000 HUD-insured mortgage for the Sibley Park Apartments, a 114-unit, mixed-income housing project located at 7<sup>th</sup> and Wacouta. Built in approximately 2000, there are 54 affordable housing units within the project and 8,700 square feet of commercial space. Refinancing the HUD-insured mortgage will allow the developer to obtain a lower interest rate of 2.9%, thus reducing annual debt service by approximately \$300,000 per year. Per HUD requirements, no money is being taken out of the refinancing by the Developer.

The HRA has the following three loans on the project:

1. **\$750,000 HOME loan** with a 6.09 % interest rate. Payments are to be made from the project’s “cash flow”. To date the project has had no cash flow, so no payments have been

made on this loan. As of January 1, 2013 the outstanding principal and interest balance was \$1,523,015.56.

2. **\$250,000 HRA loan** (sourced with Enterprise Fund 117 funds) with 0% interest. At the time this loan was made, it was anticipated that there would be insufficient cash flow to make any periodic payments, so repayment was deferred to 2042.
3. **\$500,000 HRA loan** (sourced with Metropolitan Council funds) with 0% interest. Like the \$250,000 HRA loan, repayment on this loan was deferred to 2042.

In order to obtain new financing, the three current HRA loans that are subordinate to the current HUD-insured mortgage must also be subordinate to the new mortgage. The project has been operating at a deficit, and the developer has made general partner cash loan infusions into the project that are subject to repayment solely from cash flow and must be repaid at an interest rate of 9%.

In addition to the subordination of the three HRA loans, the following transactions are proposed:

- The \$250,000 HRA loan note will be sold by the HRA to Sherman Associates Inc.(an affiliate of the Developer) for the price of \$250,000. Payments to the HRA will be made as described in the Financing Structure section of this report below.
- The \$750,000 HOME loan note will be amended and restated to reduce the current 6.09% interest rate to 2.7%. This will reduce the project interest rate burden, make the project more financially viable, and help ensure affordability is maintained.
- The \$750,000 HOME loan note will be sold by the HRA to Sherman Associates Inc. for the price of \$1,250,000. Payments to the HRA will be made as described in the Financing Structure section of this report below.
- Staff negotiated the sale of the \$250,000 HRA loan so the HRA could receive flexible Fund 117 payments over the next two years as described in this report.
- The Sherman Associates Inc. general partner loan interest rate will be reduced from 9% to 0% and remain subject to repayment from cash flow. This will reduce the project

interest rate burden, make the project more financially viable, and help ensure affordability is maintained.

- The property management incentive fee will be reduced from 4% to 2%. This will enhance the project cash flow and help ensure affordability is maintained.

Sherman Associates Inc. proposes to purchase the \$750,000 HOME loan and \$250,000 HRA loan notes to reduce the interest rate burden and provide greater flexibility for the refinancing and re-syndication of the project in the future. The note purchase structure with Sherman Associates Inc. is being proposed instead of restructuring the existing loans with the Developer because any forgiveness of the loan principal or interest would result in unacceptable tax consequences for the tax credit investors; no debt can mature earlier than the HUD insured mortgage; and payments on the HOME loan can only be paid out of surplus cash flow. Projections indicate the project won't be generating surplus cash flow until 2021. Through the note purchase agreement with Sherman Associates, the HRA will be able to collect fixed guaranteed payments upon closing.

### **Budget Action**

NA

### **Future Action**

NA

### **Financing Structure**

Sherman Associates Inc. will execute one purchase agreement with the HRA to purchase the \$750,000 HOME loan note and purchase the \$250,000 HRA loan. Assuming a closing of June 1, 2013, the current outstanding balance of the \$750,000 HOME loan, including \$811,452 in accrued interest, is estimated to be \$1,561,452. Sherman Associates is paying \$1,250,000 for the loan reflecting a discount of \$311,452 of accrued interest. The HRA is being paid the full amount of the outstanding balance of the \$250,000 HRA loan which otherwise wouldn't have been repaid until 2042. Under the purchase agreement the HRA will receive guaranteed fixed payments much earlier than under the existing loan agreements.

Payments to be made by the Developer to the HRA are as follows:

1. At closing, \$100,000 to be applied to the \$250,000 HRA loan.

Payments to be made by Sherman Associates Inc. to the HRA are as follows:

1. Three payments of \$50,000 each on April 1, 2014, October 1, 2014, and April 1 2015 that will pay off, in its entirety, the \$250,000 HRA loan.
2. Twenty-five payments of \$50,000 each payable semi-annually beginning on October 1, 2015 and continuing through October 1, 2027, at which time the \$750,000 HOME loan note will have been purchased in full. With the execution of the note purchase agreement, Sherman Associates Inc. will be entitled to collect cash flow payments from the Developer under the amended and restated \$750,000 HOME note, provided that Sherman Associates Inc. is current on required payments on the notes purchase agreement. Current cash flow projections indicate there will not be any cash flow payments available under the amended and restated \$750,000 HOME loan note until about 2021.

At the time of loan origination, the \$750,000 HOME loan was risk rated Doubtful and the \$250,000 HRA loan was risk rated "Loss". With execution of the notes purchase agreement, the HRA will receive guaranteed fixed payments instead of payments of an unknown amount from excess "cash flow" on the \$750,000 HOME loan note and will receive payments on the \$250,000 HRA loan.

Collateral pledged to the purchase agreement will include Sherman Associates Development Inc. project deferred developer fees, and Sherman Associates Inc. general partner loan payments, which will be evidenced by a Collateral Pledge Agreement. The Collateral Pledge Agreement will require that the HRA approve any proposed change to the partnership agreement that would impact the collateral pledge. Sherman Associates Inc. will provide a corporate guarantee and George Sherman will provide a personal guarantee of the purchase agreement payments that are fixed at \$50,000 semi-annually through October of 2027.

Until the amounts due under the purchase agreement are paid in full, the HRA will hold the \$750,000 HOME and \$250,000 HRA loan notes and mortgages, and such loans will continue to

be a liability of the project. Once the payments are completed under the purchase agreement, the notes and mortgages will be conveyed to Sherman Associates Inc. Regardless of which entity holds the \$750,000 HOME loan note, the HOME Declaration of Restrictive Covenants will require that the HOME units be maintained until 2023.

### **PED Credit Committee Review**

The Credit Committee risk rated the proposed HRA \$250,000 note portion of the purchase agreement as “Substandard” because payments will be made within the next few years and the \$750,000 HOME note as “Vulnerable” since payments will be made over 14 years.

HRA policy requires notification of the HRA Board if a developer seeking additional HRA/City funding is on the adverse lending list. Sherman Associates/affiliates has not completed the Printers Row project due to the state of the condominium/townhome for-sale market and is on the adverse lending list.

The HRA will need to execute an amended and restated \$750,000 HOME loan note with the Developer, and notes purchase agreement with the Sherman Associates will incorporate terms consistent with those stated in this report.

### **Compliance**

NA

### **Green/Sustainable Development**

NA

### **Environmental Impact Disclosure**

NA

### **Historic Preservation**

NA

**Public Purpose**

Payments from the \$250,000 HRA loan and \$750,000 HOME loan notes purchase agreement will provide the HRA with funds to utilize for future HRA activities.

**Land Use Plan**

NA

**Recommendation:** Staff recommends approval of the attached resolution.

**Sponsored by:** Commissioner Dave Thune

**Staff:** Marie Franchett, 266-6702

**Attachments**

- **Attachment A -- Resolution**
- **Attachment B-- Map/Address of Project, should include libraries, parks, schools.**
- **Attachment C -- Census Facts (<http://www.mncompass.org/twincities/neighborhoods.php>)**  
\*\* Click the district on the map to access the profile. \*\*