

THE CALIFORNIA DEBT LIMIT ALLOCATION COMMITTEE
July 18, 2012

Consideration and Approval of the Morgan Hill Retirement Residence Apartments
Waiver of the Penalties Forfeited
(Agenda Item No. 7)

ACTION:

Deny the Applicant's requests to return the Performance Deposit and reverse Negative Points accessed to the Project Sponsor for the Morgan Hill Retirement Residence Apartments (11-105) due to failure to issue tax-exempt bonds.

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.

DISCUSSION:

On September 28, 2011, the Morgan Hill Retirement Residence Apartments Project ("Project") was awarded \$16,309,539 in tax-exempt bond allocation. The Project's original issuance deadline was December 27, 2011; which the Executive Director extended to the January 18, 2012 allocation meeting. At the January allocation meeting, the Committee granted a second extension to March 19, 2012. In accordance with the CDLAC regulations for carryforward allocation the Executive Director granted a third extension to December 31, 2012. On April 24, 2012, the California Statewide Communities Development Authority (CSCDA), the Applicant, notified CDLAC the allocation would be reverted due to the Project's inability to maintain site control.

The Applicant first requested an extension on November 11, 2011 to March 19, 2012 due to IFG Capital's inability to find an upper tier investor to commit to the Project. The Project needed additional time to find a new syndicator to purchase the tax credits. At that time, the Project also requested that the Performance Deposit and Negative Points be waived. The requested was granted by the Committee at the January 18, 2012 allocation meeting. The next extension request was received and dated March 5, 2012 in which the Applicant stated that WNC's withdraw from the Project as the second tax credit investor was "unanticipated and unexplained". The March 5, 2012 letter requested a carryforward extension to December 31, 2012; which was granted by the Executive Director on March 9, 2012. The Project Sponsor also requested a waiver of the forfeiture of the performance deposit required under Section 5132 of the CDLAC Regulations for all carryforward extensions. Said waiver was approved by the Committee at the March 21, 2012 CDLAC Meeting.

On April 6, 2012, CDLAC staff received a phone call from the Nicolson Family Partnership, the current owner of the project site, stating that the Purchase and Sale Agreement, which expired on March 26, 2012, was not be extended. They went on to say that a new developer would apply for allocation at the July 18, 2012 CDLAC Meeting. Staff contacted the Applicant and requested clarification on the status of the Project. The Applicant responded with a April 24, 2012 letter requesting to revert the allocation, with

a letter attached from the Project Sponsor which stated that the seller chose not to extend site control due to the seller's uncertainty that an equity investor would be obtained. It should be noted that the original purchase and sale agreement expired on July 30, 2011 and had received three extensions by the time of application. The seller stated that at the time the parties negotiated the last extension, they specifically informed the Project Sponsor that they had no intention of extending the purchase and sale agreement again.

For consideration of a waiver of the assessment of the penalties for failure to issue bonds, staff 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. The Project Sponsor contends that both the seller's unwillingness to extend the purchase and sale agreement for the property and the notices of default from SunAmerica satisfy the two tests.

By its very nature, a purchase and sale agreement extension is not a guaranteed action. Neither a seller nor buyer is obligated to extend such an agreement; therefore, it is not reasonable to assume that an extension must be granted so that a project can continue through the development process. Given this, the possibility that an extension would not be granted by a seller cannot be defined as unforeseen.

To the Project Sponsor's second reason, the Project Sponsor's difficulties with SunAmerica may have contributed to the Project Sponsor's inability to find a tax credit investor for the project; delaying their ability to close on the bonds by the extended seller and CDLAC deadlines. By the Project Sponsor's own admission, the SunAmerica notices of defaults ("NODs") relate to a previously-negotiated May 2011 workout plan. The Project Sponsor also just recently informed us that the NODs were issued on February 9, 2012; well before CDLAC's consideration of the Project Sponsor's carryforward extension and related performance deposit waiver requests. Staff believes this critical information likely impacted the Project Sponsor's relationship with WNC and other potential investors (as an underwriting issue); jeopardizing the feasibility of the project. Had this been disclosed to CDLAC in the Applicant's March 05, 2012 CDLAC extension request, it may have influenced both the staff approval recommendation and ultimate decision of the Committee.

In reviewing the information provided, Staff is forced to conclude that the Project Sponsor was aware of the possibility that the purchase and sale agreement would not be extended, and that the Project Sponsor was aware of the potentially fatal issues associated with SunAmerica prior to requesting a carryforward extension and waiver of the required forfeiture of the performance deposit back in March. Given this, the subject waiver request does not meet the two waiver tests since the current circumstances cannot be considered unforeseen and wholly outside the control of the Project Sponsor.

RECOMMENDATION:

In light of the circumstances described, staff does not recommend Committee approval of the request for a waiver of penalties against the Project Sponsor for the Morgan Hill Retirement Residence Apartments (11-105).

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