



## HOUSING PRESERVATION NEWS

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## **Kern Villa: Preserving At-Risk Housing By Leveraging Project-Based Section 8**

In the last issue of Housing Preservation News we described Christian Church Homes' successful use of an innovative acquisition loan program to preserve Plaza de las Flores, a 101-unit senior Section 8 property in Sunnyvale. This month we take a look at East LA Community Corporation's (ELACC) successful acquisition of a family Section 8 property in Los Angeles using another creative method of financing, leveraging additional income from the project-based Section 8 contract.

### ***Project Background***

ELACC is an experienced community-based nonprofit housing developer created in 1996 that produces and preserves quality affordable housing and nurtures economic development opportunities for low-income residents of Boyle Heights and unincorporated East Los Angeles. ELACC has a five person development staff and a substantial track record of developing for sale and rental properties. In 2003, ELACC began searching to acquire and preserve at-risk properties in the East Los Angeles area. CHPC provided ELACC with a list of at-risk properties from our database of federally subsidized apartments. Kern Villa was one of the properties on the list as its Section 8 contract was set to expire at the end of January 2004.

Located in unincorporated East Los Angeles, Kern Villa is a 49-unit garden-style walk-up apartment complex that was constructed in 1982 using a HUD Section 221(d)(4) mortgage and 100% project-based Section 8 contract. The complex consists of a mix of three-bedroom townhouse apartments, two-bedroom flats that are fully handicapped accessible and two-bedroom townhouse apartments.

In March 2005, ELACC acquired Kern Villa with the goal of continuing to serve large low-income families in the East LA community for another 55 years. The property was in need of extensive rehabilitation, which was completed in January 2006. The rehabilitation included architectural treatments, new exterior and interior paint, new appliances and cabinets, and a new children's playground. The project also incorporated green building methods.

### ***Using Section 8 Increment to Leverage Additional Financing***

It is well known that project based Section 8 is an important housing subsidy as it allows very low and low income renters to pay only 30% of their income for housing. What is not as well known is that Section 8 rent subsidies can be used to leverage private capital for the acquisition and rehabilitation of existing affordable housing. The difference between the market rent paid by the Section 8 program and the underlying rent used by the affordable housing industry to estimate the capacity of property to pay debt service is called the Section 8 increment. Section 8 increment can be used to support additional debt, establish a transition reserve for tenants and in some cases investors may want the increment used for a reserve for the property. In this case the Section 8 increment is being used to service a permanent "B" loan in addition to the standard loan underwritten based on the Net Operating Income (NOI) from the tax credit rents. The term of the "B" loan depends on the type and term of Section 8 and lender and investor underwriting criteria and project economics.

## Financing Details

### CHPC Preservation Clearinghouse

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The total development cost for Kern Villa was \$8,650,064. To acquire and rehabilitate the property, CHPC helped ELACC assemble a variety of funding sources, including private loans and equity proceeds from the syndication of 9% low income housing tax credits,

ELACC purchased Kern Villa for \$3,328,400 million. Adding in other acquisition-related expenses, the total acquisition cost came to \$3,600,900, which was financed by a \$2,800,900 acquisition loan at 7.75% interest from US Bank and an \$800,000 loan at 6% interest from Enterprise Community Investment. Construction financing included a \$6,783,608 loan at 7.75% interest from US Bank and \$853,400 in equity from Enterprise and a \$49,100 grant from Enterprise's Green Communities program. The remainder of the construction financing included \$411,405 in income from operations during the rehabilitation.

The permanent financing includes two loans from US Bank: a 30-year first loan of \$973,000 at 7.52% interest supported by the tax credit rents, and a 20-year second loan of \$3,048,900 at 7.19% interest, supported by the Section 8 increment from a new 20-year Section 8 contract. In addition, Enterprise Community Investment paid \$4,097,000 to purchase the 9% tax credits.

SOURCES:	Acquisition Amount	Permanent Amount
US Bank Acquisition	2,800,900	
ESIC Acquisition Loan	800,000	
US Bank Permanent – Note A		973,000
US Bank Permanent – Note B (Section 8)		3,048,900
<b>Subtotal 3<sup>rd</sup> Party Financing</b>	<b>3,600,900</b>	<b>4,021,900</b>
Income from Operations (during rehab)		411,405
Deferred Developer Fee		70,659
General Partner Contributions		49,100
Limited Partner Contributions		4,097,000
<b>Total Equity Financing</b>		<b>4,628,164</b>
<b>TOTAL SOURCES:</b>	<b>3,600,900</b>	<b>8,650,064</b>
USES:	Acquisition Amount	Permanent Amount
Acquisition	3,328,400	
Acquisition/Construction Loans Take Out		3,609,900
Rehabilitation		3,275,309
Loan Fees, Interest and Expenses	196,450	432,533
Title, Recording & Escrow	38,733	30,000
Contingency	31,317	55,000
Local Fees		10,000
Architectural & Engineering Fees		116,700
Taxes & Insurance (during construction)	15,000	133,000
Legal Fees		82,500
TCAC Fees, Financial Consultant & Other		133,700
Costs		
Reserves		771,422
<b>TOTAL USES:</b>	<b>3,609,900</b>	<b>8,650,064</b>

## About the California Housing Partnership Corporation

The California Housing Partnership Corporation was created by the state in 1988 to assist nonprofit and government organizations to create and preserve affordable housing while providing leadership on housing policy. CHPC is unique in combining transaction-based technical expertise with deep experience in affordable housing policy work. To date, CHPC has helped preserve and create more than 10,000 affordable apartments for low-income households in California. CHPC also provides affordable housing finance training to nonprofit and government organizations across the state.

*This newsletter made possible with support from:*

