CALIFORNIA HOUSING PARTNERSHIP CORPORATION

HOUSING PRESERVATION NEWS

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Turnagain Apartments: A case study in preserving affordable housing in San Diego County

Editor's Note: This case study examines the financing challenges of rescuing older HUD-assisted properties without the support of full Section 8 rents and highlights the complexity of refinancing LIHPRHA/Title VI properties and the need for new policies from HUD.

Project Background

Turnagain Apartments is an 80-unit family apartment development located in Fallbrook, California (San Diego County). Turnagain Apartments, originally called Turnagain Arms, was built in 1974 by Spieker Properties, a private, for-profit developer using a Section 236(j) subsidized mortgage.

In 1978, Turnagain was awarded a contract for 22 Section 8 units through the Loan Management Set Aside (LMSA) program, which was established to provide rent subsidies that can help prevent subsidized mortgage defaults. Despite the extra rent from the market rate payments HUD made for these 22 Section 8 apartments, Turnagain's financial and physical condition continued to decline. As the Section 8 contract neared the end of its initial 20-year term in 1998, Turnagain was at risk of converting to market rate rents as the Section 236 rents had dropped far below market and the owner was eying the prospect of obtaining market rents.

A few years earlier in 1992, Congress had established the Low-Income Housing Preservation and Resident Homeownership Act (LIHPRHA) to provide tools to preserve buildings in this situation. Also known as Title VI, LIHPRHA was designed to encourage partnerships involving residents and nonprofit housing developers and to incentivize owners to stay in the HUD programs. To take full advantage of the program's benefits, the Turnagain residents asked San Diego based Community HousingWorks (CHW) to help them establish the Turnagain Arms Community Housing Association (TACHA), a single-asset nonprofit. With assistance from CHW, TACHA succeeded in purchasing Turnagain Arms in 1995.

However, despite some rehabilitation work done following the 1995 purchase, TACHA found that Turnagain's budget-based Section 236 financing structure did not provide enough funding for it to adequately maintain the aging building. CHW helped the residents to realize that the property needed to be refinanced in order to rehabilitate the 30-year old building or they would risk losing their homes. They also pointed out that maximizing the chances for refinancing would require the residents to transfer full control to CHW.

Financing Challenges and Innovations

With help from CHPC and an experienced HUD attorney, CHW developed a tax-exempt bond financing structure that included a seller take-back loan from TACHA for the sale of the building, Low-Income Housing Tax Credits (LIHTC) and leveraged Section 8 rents. Two of the key elements of the financing structure were renewing the existing Section 8 contract with a rent increase and securing Enhanced Section 8 Vouchers (EVs) for the 58 apartments not already funded under the existing Section 8 contract.

Mark up to Budget - Using Section 8 Rents as Revenue to Service Bond Debt
For the 22 existing Section 8 units, CHW and CHPC used Chapter 15 of HUD's Section 8 Renewal Policy to secure a 20-year contract renewal with a budget-based rent increase for capital repairs. CHPC worked with staff from HUD's LA office to secure a Section 8 rent increase of approximately 35 percent for the 22 apartments covered by the contract. This additional income enabled CHW to secure a secondary loan of $791,000.

Enhanced Vouchers - Protecting Existing Tenants and Generating Income for Services
HUD provides EVs to protect residents of HUD-assisted properties when the owner decides to opt-out of a Section 8 contract or to prepay a subsidized loan. EVs enable the owner to increase rents while ensuring that residents receiving them pay no more than 30 percent of their income for housing. While CHW is a mission-driven organization committed to maintaining rents at affordable levels, it was essential to the financial viability of the property to find a way to raise the rents of the 58 apartments without Section 8 from the extremely low levels that had been maintained under the 236 mortgage regulations to Tax Credit rents ranging from 50 to 60 percent Area Median Income (AMI). EVs protected the residents against unaffordable rent increases and generated additional revenue to cover operating expenses and make payments on the seller take back note, which the residents had agreed would be dedicated to paying for tenant services.

Overcoming Obstacles

To obtain the EVs for the 58 non-Section 8 households, CHW first had to demonstrate that a nonprofit that purchases a for-profit Section 236 development has a right to prepay the mortgage and, in turn, receive EVs. While CHW felt they had the ability to prepay the Section 236 contract as a matter of right, HUD Headquarters staff initially argued that prepayment of the 236 contract required HUD Secretary approval and was subject to Section 250a of the National Housing Act (12 U.S.C. §1715z-15), which limits and conditions how units can be prepayed. After hearing from the offices of Senator Diane Feinstein and Congressman Darrel Issa, who represents the Turnagain residents, HUD relented and approved the release of the EVs.

Ultimately, CHW was successful in securing both the Section 8 budget-based rent increase and the Enhanced Vouchers. This funding combined with the other financing elements enabled CHW to acquire Turnagain Arms, now known as Turnagain Apartments, in October 2008. CHW noted that this project would not have been possible without the commitment of Union Bank of California and RED Capital. As of today, the rehabilitation of Turnagain Apartments is well underway.

Sources of Funds: Permanent	Amount		Uses of Funds	Amount
Union Bank -- TCAC Rent Loan	$3,200,000		Acquisition	$7,007,184
Union Bank -- Section 8 Loan	$791,000		Construction/Financing	$4,444,596
Seller Take Back Loan	$6,388,767		Architect, Survey & Engineering	$325,400
GP Loan (using NWA grant funds)	$200,000		Relocation and Marketing	$411,800
Income from Operations (during rehab)	$560,817		Reserves	$628,584
Tax Credit Equity -- RED Capital	$4,107,171		Costs of Issuance/Financing/Legal Fees	$404,871
--	--		Developer Fee	$1,057,530
--	--		Other Costs	$967,790
Total Sources	**$15,247,755**		**Total Development Costs**	**$15,247,755**

About Community Housing Works (chworks.org)
Community HousingWorks is a San Diego non-profit that helps people and neighborhoods move up in the world by providing a full range of housing options combined with training and support. CHW develops affordable apartments, offers first-time homebuyer loans and provides other community training and support services.

PRESERVATION SERVICES FOR NONPROFIT AND LOCAL GOVERNMENT STAFF

CHPC provides financial consulting, technical assistance, and training to help nonprofit and government agencies build and preserve affordable homes for California families and seniors. For more information, please contact our Housing Policy Manager, Marilyn Wacks at *mwacks@chpc.net* or (415) 433-6804 x313.

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