



Affordable Housing Committee Staff Report

AGENDA TITLE: Consideration of the proposed loan application and Disposition and Development Agreement and Joint Escrow Instructions (DDA) with Elk Grove Old Town Mutual Housing Associates, L.P. (Developer), in support of the proposed senior affordable housing development project known as Old Town (APNs 134-0072-013, -014, -015, and -016)

MEETING DATE: April 15, 2025

PREPARED BY: Sarah Bontrager, Housing and Public Services Manager
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RECOMMENDED ACTION:

Staff recommends that the Affordable Housing Committee (Committee) perform an independent review of the affordable housing loan application and Disposition and Development Agreement (DDA) for Old Town project and provide direction to staff on whether to move forward with finalization of terms and conditions set forth in the DDA, including the proposed loan term sheet attached to the DDA.

BACKGROUND INFORMATION:

The City has an Affordable Housing Fund (AHF), which is generated by fees on new residential and non-residential development. The AHF must be used to support housing opportunities for low-income households, one option for which is to subsidize new affordable apartment construction. The City acquired the Old Town site (9220-9244 Elk Grove Boulevard) in 2023. The site is approximately two acres and consists of four undeveloped lots located in the historic Old Town neighborhood.

Request for Proposals and Proposal Evaluation

In April 2023, the City released a Request for Proposals (RFP) soliciting a development partner to build affordable multifamily housing on the Sheldon Farms North site. The RFP provided minimum criteria for proposals, with a focus on addressing community housing needs, maximizing funding sources, and innovation in project design. The City received 12 proposals from developers interested in partnering to develop the site.

On November 13, 2023, the Affordable Housing Committee (Committee) reviewed information related to the RFP and directed staff to work with Mutual Housing California (Mutual Housing), a nonprofit affordable housing developer, and their affiliated entity (Developer) to develop the Old Town site. Mutual Housing was selected based on their extensive development and operating experience, financial capacity, and alignment with the City's vision. Mutual Housing proposed an 89-unit senior project comprised of one building. The design included higher density (three stories) close to Elk Grove Boulevard and is oriented around multiple courtyards. Studio, one-, and two-bedroom units would serve

seniors earning 30% to 70% of the area median income.

Project Iteration

Since the Developer was selected, they have worked with City staff to refine their project and explore multiple funding options. The Developer also held three community meetings to obtain feedback on their site plan, design aesthetics, and community amenities.

The Developer proposes merging the parcels and constructing the project in a single phase. The Developer submitted an entitlement package to the City’s Development Services Group in 2024, and the entitlement submittal is expected to be approved in the coming months.

Letter of Intent

On February 14, 2024, the City Council authorized the City Manager to execute a Letter of Intent (LOI) with the selected Developer, thereby formalizing the commitment to partner in the development of affordable housing. The LOI was valid for a term of 12 months; however, the Developer requested a 12-month extension to allow more time to enhance funding competitiveness. On February 12, 2025, City Council authorized the City Manager to execute an Amended and Restated LOI with the Developer to continue collaboration toward the development of much-needed affordable housing. The LOI is included as **Attachment 1**.

The LOI offers the Developer the exclusive opportunity to pursue development of the Old Town property. The LOI is valid until February 11, 2026, or until replaced by a conveyance agreement executed by the City and the Developer. Staff has completed substantial work on a Disposition and Development Agreement and Joint Escrow Instructions (DDA), the preferred form of the conveyance agreement, which is described later in this report.

Loan Consideration and Timing

The LOI commits the City to consider an Affordable Housing Fund loan commitment of \$3,000,000, excluding land acquisition costs. The Developer has identified 4% tax credit/State bond financing through the California Tax Credit Allocation Committee (TCAC) as a viable funding source for the project. The application deadline is earlier than the entitlement approval process can be completed, but TCAC allows applications to be submitted when an entitlement process is underway. In order to apply for TCAC, the Developer may use the DDA as proof of site control and a conditional loan commitment from the City as proof of local funding.

In order to allow the Developer to pursue 4% tax credit funding in the May 2025 funding round, staff is bringing forward the DDA, including a loan commitment component, for the project. As is common in affordable housing project structures, Mutual Housing created a limited partnership entity: Elk Grove Old Town Mutual Housing Associates, L.P., a California limited partnership.

ANALYSIS/DISCUSSION:

Loan Application

The loan application serves as an important process for evaluating the feasibility of the proposed project, while ensuring alignment with the information submitted in the Developer’s proposal. Mutual Housing filed their loan application on October 18, 2024, and has worked with staff to refine elements of the loan application since its filing.

The components of the loan application are dictated by the Affordable Housing Loan Program Guidelines

(see copy of Developer’s loan application in **Attachment 2** and pro forma in **Attachment 3**). The following item was not submitted:

- *As-built property appraisal.* This appraisal identifies the “as is” value of the land, and prospective market values of the property when complete and when stabilized under both the restricted rent and unrestricted rent scenarios. The Developer indicated that this appraisal is typically initiated by the lender. As negotiated, the City requires the as-built appraisal as a condition of the loan closing, but the City’s conditional commitment cannot be tied to the value identified in the appraisal because that is not a factor within the Developer’s control.

The loan application provides additional information with which to consider a project. Central to this evaluation is the assessment of several key components, including the robustness of the development partners, the structure of the financing, and the overarching viability of the project itself. A summary of key project features is shown in **Table 1**.

Old Town Project Summary

Table 1

Old Town Senior Apartments						
Developer	Elk Grove Old Town Mutual Housing Associates, L.P., a California limited partnership A not- for-profit affordable housing developer with more than 20 affordable properties in Northern California. This is Mutual Housing’s first project in Elk Grove.					
Service Provider	Mutual Housing					
Location	9220-9244 Elk Grove Boulevard (APNs 134-0072-013, -014, -015, and -016)					
Nearby amenities	Adjacent uses are shopping centers, multifamily market-rate housing, and single-family homes. Excellent proximity to shopping, services, transit, and the future Elk Grove public library.					
Type of project	Senior					
Affordable unit description ¹	Affordability Level (% of AMI)	Total	Studio	1BD	2BD	3BD
	30%	16	1	12	3	-
	40%	10	-	8	2	-
	50%	21	-	19	2	-
	60%	41	-	35	6	-
	70%	-	-	-	-	-
	TOTAL	88	1	74	13	-
Total number affordable units	88					
Total residential square footage	55,125					
Total project cost	\$50,830,912					
Construction cost	\$33,119,109					
Cost per unit	\$571,134					
Cost per residential sq. ft.	\$922.10					

Developer fee ²	\$3,585,193 (7%)
Loan request	\$4,200,000 (\$1,200,000 land value + \$3,000,000 cash)
City subsidy per affordable unit	\$47,727.28 (8.36%)
Other financing/subsidy ³	\$20,993,005 – 4% tax credits \$15,185,727 – Tax-exempt bonds \$6,004,188 – Permanent debt \$1,085,193 – Deferred developer fee \$747,526 – Other \$376,633 – Sustainability incentives
Project amenities	Bike storage rooms, community clubrooms, BBQ/picnic areas, outdoor gathering decks, outdoor decks, office space for provision of resident services, elevators, laundry facilities, bike racks, benches, and lighted parking.
Social services offered	Minimum of 12 hours per week of on-site supportive services.

- 1 The project includes one three-bedroom manager unit, which is not income-restricted.
- 2 The developer fee is a total of \$5,984,466, of which the Developer is contributing \$2,399,273 as equity to the project, giving an effective developer fee of \$3,585,193.
- 3 As proposed, the City’s financing will be in a junior position, behind senior permanent financing in the amount of approximately \$6 million. “Other” funds include a mix of deferred interest and other tax credits.

Project Strengths

The Developer’s loan application demonstrates several notable project strengths that contribute to its potential for long-term success:

- *Experience.* Developer has significant experience designing, funding, constructing, and managing affordable housing projects in California. Since 1988, Developer has developed and placed in service over 20 affordable housing projects located in Northern California. This portfolio houses 3,500 residents and consists of approximately 1,300 homes in multifamily communities designated for extremely low- to low-income families, seniors and individuals. Developer’s track record demonstrates an ability to consistently obtain low-income housing tax credits (LIHTC) awards and the accompanying private and public financing to complete their projects.
- *Location.* The project is located in the historic Old Town neighborhood with close proximity to grocery stores, restaurants, and the future Elk Grove public library, which would be an off-site amenity for residents of the project. The project is also near shopping centers, a pharmacy and a credit union. The proposed building is predominantly facing Elk Grove Boulevard frontage and emulates the relationship to the street that is found throughout the historic district. The apartments are structured around the south-facing courtyards to optimize daylighting and outdoor areas adjacent to the units. There are many mature trees on the south side of the site. The building has been located to accommodate the preservation of as many trees as possible.
- *Unit affordability.* Overall, this project is more affordable than other affordable housing projects built in Elk Grove in recent years, with most units targeted to senior households earning 30% to 60% of the area median income. There are currently only a few projects in the City’s affordable housing stock (Vintage at Laguna I and II, Seasons, and Renwick Square) targeting senior

households, so this project adds a valuable resource for those households at a time when market-rate rents are increasingly unaffordable.

- *Unit mix.* The unit mix includes a greater percentage of one-bedroom units than two-bedroom units, making it particularly suited for seniors. The project also includes one studio unit.
- *Partnership to address homelessness.* The Developer is committed to partnering with the City to address homelessness, including by moving homeless Elk Grove households to the top of the waitlist for any unit for which they are qualified. A similar partnership on other affordable housing complexes has resulted in numerous Elk Grove homeless households being placed in units that they can afford.
- *Revenue and operating cost assumptions.* The project's revenue and operating cost assumptions are in line with TCAC guidelines and other affordable housing projects in the City. The pro forma reflects a vacancy rate of 5%, consistent with industry standards for similar affordable housing projects. Operating costs are projected to remain stable, with annual increases of approximately 3%.
- *On-site property management and social services.* The project accounts for on-site property management by setting aside one non-income-restricted three-bedroom unit for a member of the property management staff. The Developer maintains its own in-house property management services through Mutual Housing Management (MHM). MHM has experience managing market-rate and affordable multifamily units and is committed to partnering with the City throughout the lease-up process.

Project Weaknesses

A key goal of the City's affordable housing programs is ensuring that units remain an excellent resource for low-income households over the duration of a project's life. While the Old Town project has several strengths noted above, the project also has several weaknesses, mainly related to the financial assumptions of the project. These weaknesses may impact the project's ability to remain viable throughout the 55-year affordability period. Specifically, staff has identified the following weaknesses:

- *There is a disparity between the projected increases in rental revenue and the increase in operating expenses.* The Developer assumed that rents would rise at 2% annually, and that most operating expenses would rise at 3% annually, which is consistent with TCAC standards. In the current economic climate, a 2% increase in annual rents is likely, but in a weaker economic environment, increases in revenue may be dependent on increasing Section 8 receipts and/or maintaining a lower than standard vacancy rate. In the event that costs continue to increase at a rate outpacing revenue increases, the project's net operating income will decline, which may lead to a situation where the property cannot be adequately managed or maintained.
- *The proposed replacement reserve contribution of \$350 per unit per year is inadequate to maintain the project over the 55-year affordability period.* Although this contribution is within TCAC guidelines and greater than the reserve contribution the City has approved on past loans, the reserve is unlikely to ever accumulate enough funds before the replacement reserves equal the non-inflation-adjusted construction cost of the project. Additionally, while it is reasonably certain that construction costs will rise over time, the replacement reserve contributions are not adjusted, meaning the amount they will be able to cover will decline as the project ages.

Underfunding the replacement reserves creates a situation where the project may not be able to be maintained in line with the City’s standards during the entirety of the affordability period.

- *The likelihood of the City receiving significant loan repayment throughout the loan term is small.* A residual receipts payment structure is proposed, with payments to the City being made only after full payment of all deferred developer fees. Under this structure, the loan would not be amortizing and the annual payments to the City would not be equal to annual interest on the loan, creating a scenario where the loan balance continues to grow. If rents fail to increase at the predicted pace, if expenses are greater than estimated, and/or if vacancy is higher than anticipated, it is possible the City would not receive any payment at all. Historically, this has been the case for the majority of the City’s residual receipts loans.

Loan Negotiation

Staff dedicated considerable time and effort working with the Developer to negotiate loan terms, with the primary goal of obtaining a high-quality project, providing a reasonable level of competitiveness for other funding sources, and responsibly allocating public funds. Staff’s chief goals in loan negotiations included the following:

- Ensuring that the City is providing the minimum amount of “gap financing” needed by a project to make it financially feasible;
- Mitigating risk to the City;
- Ensuring the long-term affordability and maintenance of the project;
- Promoting affordable housing options for populations that have some of the most serious challenges securing and maintaining housing, including senior households; and
- Providing cost controls to improve transparency in usage of public funds.

Loan Term Sheet

The loan term sheet includes a summary of the key aspects of the loan such as the loan amount, interest rate, repayment schedule, and any conditions tied to the disbursement of loan funds. The term sheet is used to prepare the loan documents, including a Loan Agreement, Regulatory Agreement, Promissory Note, and Deed of Trust. The intention of the loan term sheet is to protect the City’s position and minimize risk, as well as to clarify the City’s expectations for the Developer and the senior lender.

Highlights of the Phase I loan terms include the following:

- Loan amount of \$4,200,000 in total;
- Interest rate of 4%;
- Project’s design and construction plans substantially conform with the terms of the DDA, and allows the Developer to work to secure funding through December 31, 2026;
- City has agreed to provide an initial disbursement of \$1.2 million at the closing of construction financing as part of the total loan amount, contingent upon the Developer’s simultaneous completion of the land purchase from the City. The remaining disbursements (\$3 million) are tied to project framing completion, construction completion, cost certification, and project stabilization;
- Provisions to assist the City in ensuring that the project’s costs are reasonable;
- Provisions to assist the City in ensuring the project’s amenities meet design guidelines and promote desirable living spaces for residents, which will be further elaborated in the DDA;
- A requirement to provide 12 hours per week of on-site social services;
- A definition to be used to calculate annual payments to the City, based on the project’s income and expenses;
- Requirements related to insuring and reporting on the property; and

- A Regulatory Agreement that will restrict the units as affordable for a period of 55 years.

The City and the Developer were able to reach mutually agreeable loan terms. A copy of the Old Town loan term sheet is provided in **Attachment 4**.

Conveyance of City-owned Land

Unlike traditional affordable housing arrangements, where developers come to the City with their own plans, the City has the ability to play a more active role as owner and lender of the Old Town site. The use of a DDA framework allows the City to accomplish this. A DDA is a legally binding agreement that governs the terms and conditions under which City-owned property is sold to the Developer. The DDA not only incorporates the loan terms, but also sets clear expectations for how the Developer will meet certain predevelopment activities and adhere to key project milestones, even after changes in ownership.

The DDA is not a Development Agreement as contemplated by California Government Code section 65864 et seq. Therefore, the DDA does not require an ordinance in the same way a Development Agreement does under these same provisions. While the DDA does not require an ordinance, it is subject to the Committee’s review and City Council approval. Pending the Committee’s recommendation, staff plans to present the loan and DDA to City Council for final approval.

Staff, in coordination with the Developer and the City Attorney’s Office, engaged in an extensive and collaborative process to draft the Old Town DDA.

Highlights of the DDA include the following:

- Memorializes the \$4.2 million total loan amount, including the purchase price of the land at \$1.2 million, and any other specific provisions related to the loan term sheet.
- Specifies the conditions that must be satisfied before the land is conveyed to the Developer, such as securing necessary financing, environmental reviews, obtaining permits required by local, state, or federal regulations, finalization of project plans, etc.
- Provisions to clarify City-land is conveyed “as-is” and the Developer assumes full responsibility for any environmental remediation or any other site-specific issues related to title.
- Provides the City with certain rights in case of default or any breach of the terms and conditions.
- Defines the scope of the affordable housing development, ensuring the project design aligns with the City’s long-term goals.
- Sets requirements for the Developer to meet key project milestones from the completion of predevelopment activities to lease-up.

The City and the Developer were able to reach mutually agreeable terms. A copy of the Old Town DDA is provided in **Attachment 5**.

Options

The Committee’s responsibility is to perform an independent review of the loan application and DDA (including loan term sheet) in support of the Old Town project and return to staff with their recommendation.

The Committee has the following options:

1. Make a recommendation for conditional loan and DDA approval by the City Council.

2. Make a recommendation for conditional loan and DDA denial by the City Council.
3. Provide direction to staff to collect additional information requested from the Developer and continue negotiation. If the Committee asks for additional information or continued negotiation, it will likely negatively impact the Developer's ability to apply for funding in 2025 and further delay the project.
4. Make such other recommendation as deemed appropriate by the Committee.

Next Steps

The Developer has submitted an entitlement application and is proceeding with the City's entitlement process. Staff expects that the Zoning Administrator will consider the approval of the Old Town Project for development and construction in the coming months. The loan term sheet and DDA will come before the Committee for a recommendation to Council.

If the Committee chooses to (1) recommend that the Council approve the conditional loan and DDA for the Old Town project, the Council is expected to consider this item on April 23, 2025. Staff also plans to propose declaring the land as exempt surplus for Council consideration as part of the DDA approval. If approved by Council, this timeframe will allow Mutual Housing to apply for apply for the 4% TCAC funding round due May 20, 2025. In the event the Committee chooses to (2) recommend that the Council deny the conditional loan and DDA, or chooses to (3) ask for additional information or continued negotiation, the Developer would not be able to obtain a loan commitment from the City in order to apply for financing. The next opportunity to apply for funding is expected to be in early to mid-2026.

Once all necessary funding for the project has been secured, staff will work with the Developer to draft a Regulatory Agreement and other loan documents. The Regulatory Agreement and loan documents will be brought before the Council for final approval.

ENVIRONMENTAL DETERMINATION:

The Committee's action only recommends financing and will not cause a direct physical change in the environment, nor a reasonably foreseeable indirect physical change in the environment. The Committee's action at this stage is merely a recommendation to Council and does not constitute approval of a commitment by the City to issue a loan for the project, nor does it constitute the approval of the project or a commitment to convey the City-owned property to the Developer. Environmental review on the project is underway and will be completed as a part of their entitlements processed through the City's Community Development Department's Planning Division. The Committee's action, therefore, does not constitute the approval of a project under the California Environmental Quality Act ("CEQA"), and it is exempt from CEQA. (Pub. Res. Code § 21065, CEQA Guidelines §§ 15060(c),(2)(3); 15061(b)(3); 15064(d)(3); 15352; 15378; *Laurel Heights Improvement Association of San Francisco, Inc. v. The Regents of the University of California*, 47 Cal.3d 376, 398 (1988))

FISCAL IMPACT:

The loan term sheet presented to the Committee includes a loan amount of \$4,200,000. Of that amount, \$3,000,000 is cash needed from the Affordable Housing Fund. The remainder (\$1,200,000) is the appraised value of the portion of the site anticipated to be used for the project and allows the Developer to purchase the land from the City, so this amount does not recommend an actual cash outlay.

If approved, the conditional loan commitment will reserve the monies for the length of the commitment period and preclude other projects from consideration. There is adequate fund balance in the Affordable Housing Fund to cover the cash loan amount for the project. Budget for the project is programmed for the upcoming fiscal year 2026.

Additionally, there is adequate budget in the Affordable Housing Fund to cover staff costs associated with making one or more loans, including the creation of loan documents to secure the City's investment. The cost of staff time to process loans is small in comparison to the value of the loans, and the cost of staffing to support the goals of the Affordable Housing Fund is budgeted annually.

The Developer will pay customary City processing fees associated with the entitlement plan approval, building permit fees, and required impact fees. This is typical, and each Developer budgeted for this cost in the financial projections provided to the City.

No General Fund contribution is anticipated for the loan or for the project monitoring and oversight.

ATTACHMENTS:

1. Letter of Intent
2. Loan Application
3. Project Pro Forma
4. Loan Term Sheet
5. Disposition and Development Agreement and Joint Escrow Instructions