

Seattle Housing Levy

Acquisition Opportunity Revolving Loan Fund

In order to take advantage of changing market conditions, OH is proposing a new Levy revolving loan program with the following two components:

- **Acquisition revolving loan fund** --- available to make strategic land purchases; for example, to facilitate TOD at key transit stops;
- **Equity loans for private market-rate projects** --- below market financing in return for below market rents or sales prices.

A. Market conditions/opportunities:

Dupre+Scott noted the following in August–October 2008 reports (Apartment Vacancy and Apartment Advisor):

- “It has been a great year—actually, three great years. But now there are signs of softening.”
- Vacancy rates are going up---usually that coincides with declining rents, but rents still rose 7% in the past 12 months;
- Condo conversions have dropped nearly to 0;
- New jobs are slowing;
- Capitalization rates are starting to go up;
- In addition, we are seeing and will continue to see increases in foreclosures.

These trends suggest the following opportunities potentially, particularly in the early years of the Levy term ahead:

- Land and building prices are moderating, cap rates going up---heading toward potential buyers market;
- Higher vacancy rates likely to eventually slow demand for land/building purchases;
- Financing becoming more difficult to obtain---may lead to very opportune time to acquire land/buildings;
- Private developer equity interest rates going up---an opportune time to offer low interest equity financing to help make market rate projects feasible and to lock in affordable units for 50+ years.

B. Program Components:

Acquisition revolving loan fund:

The existing real estate market is an important example of the fact that if the current Levy had flexible enough and sufficient acquisition dollars, there would be an opportunity now to purchase existing distressed properties to add to the city’s affordable housing stock. OH currently has a small amount of bridge loan authority that has enabled nonprofit housing developers to acquire property prior to being

able fully develop a proposal. However, it is not sufficient to purchase entire buildings and has numerous restrictions.

OH proposes a larger and more flexible revolving acquisition loan fund to be used and administered as follows:

- Funding to buy land or buildings at strategic locations; focus on areas where City is encouraging higher density development, for example TOD.
- Low interest loans in return for below market rents or sales process for as long a term as possible.
- Rather than having developers bring properties to the city, the city would be strategic in having an entity go out and find distressed properties or properties that meet strategic goals; the flexibility of an outside entity is needed to move quickly, responding to market conditions
- City will set criteria through Administration & Finance Plan, which is reviewed and approved by Council.
- Take out funds could be through OH or other public subsidies.

Equity loans for private market rate projects:

Over the last year equity has been increasingly difficult to obtain. (With current markets, debt is also nearly impossible, but we are presuming that the markets will moderate by the time Levy money is available in 2010). Although the product that we are proposing is actually a loan, because it would be subordinate to the primary debt, the creditor in first position would consider our loan product to be equity. If equity requires a 14%-20% return, we could provide much cheaper "equity" with a 3% interest loan. Based on the modeling done by Hal Ferris, we could "buy" affordable units in the building using the loan product based on the differential in the cost of the equity loan we would provide versus the cost of equity in the market. The following are the parameters modeled for the loan product:

- Low interest (3%) equity loans with funding available during construction and rent-up/sales period;
- Loans revolve after rent-up/sales period, out for 3 to 5 year period;
- Portion of units have long term affordability---focus on moderate-wage workers with income between 60% to 80% median;
- Loans subordinate to private financing, not to private equity contribution; City funding generally 25-50% of equity financing;
- Primary purpose to ensure affordable housing is developed in high density locations; engage private sector in developing housing affordable for moderate wage workers;
- Available for rental as well as homeownership projects;
- Works in conjunction with other incentive programs: Seattle Homes Within Reach---property tax exemption and Incentive Zoning.
- Could potentially work in conjunction with bond/4% tax credit deals.