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OAKLAND

2017 JUN 29 PM 1:06

# AGENDA REPORT

**TO:** Sabrina B. Landreth  
City Administrator

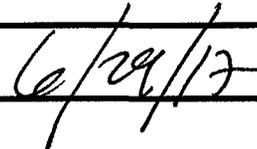
**FROM:** Michele Byrd  
Director, HCDD

**SUBJECT:** Purchase the HUD-Held Mortgage  
Loan Secured By E.C. Reems Garden  
Apartments

**DATE:** June 19, 2017

City Administrator Approval

Date:

## RECOMMENDATION

**Staff Recommends That The City Council Approve A Resolution (1) Authorizing The Purchase Of A HUD-Held Mortgage Loan Secured By E.C. Reems Garden Apartments Located At 2700 Alvingroom Court (The "Property") For A Purchase Price Of Up To \$4,000,000 Plus Accrued Interest, And (2) Authorizing The City Administrator To Take Actions To Facilitate The Preservation And Rehabilitation Of The Property, Including Contracting With An Interim Property Management Company, Foreclosing On City Loans Secured By The Property, And/Or Assigning City Loans Or Lien Rights On The Property To An Affordable Housing Entity.**

## EXECUTIVE SUMMARY

Authorization of the proposed resolution will accomplish the following:

- Prevent the Department of Housing and Urban Development (HUD) from foreclosing on the HUD-held mortgage loan and selling the property to a for-profit real estate developer with no interest and/or ties to the neighborhood and/or City of Oakland.
- Preserve affordability restrictions on the project for an additional fifty-five years.
- Preserve the City of Oakland's financial investment in the amount of \$4.1 million.
- Authorize the assignment of City loans or lien rights, including the loan purchased from HUD, to an affordable housing entity as needed to facilitate the preservation and rehabilitation of the property.
- Ensure that the new affordable housing entity that steps into the project agrees to make all the repairs within 24 months of assignment of lien rights (contingent on the ability to secure full financing or approval of an extension).
- Ensure that the new affordable housing entity and City-authorized property management company conduct a thorough file review, including tenant income re-certifications to ensure that each household meets the low-income requirements.

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## **BACKGROUND / LEGISLATIVE HISTORY**

The E.C. Reems Gardens Apartments (Alvingroom Court) is a 126-unit multi-family affordable housing complex located at 2600-2795 Alvingroom Court. The apartments were constructed in 1948, and consist of one, two and three bedroom units scattered throughout fifteen buildings. In the early 1990's, the then privately-held property had earned a reputation in the community as a site for drug traffic and violence. From there, it began to rapidly deteriorate and carry a high vacancy rate. In 1995, American Savings Bank foreclosed and took title to the property.

In 1996 Alvingroom Court L.P. (the "owner") (composed of the Corporation for Better Housing (managing general partner), Hope Housing Development Corporation (operating general partner), and KAVIGEM, Inc.) entered into negotiations to acquire, rehabilitate, and manage the deteriorated complex. The City provided the owner with financial assistance to acquire and rehabilitate the project as affordable housing.

Between 1997 and 2001, the owner received multiple loan funding awards from the City totaling \$2,939,500. The current outstanding balance on the City loans, including accrued interest, is \$4,134,762 (maturing on December 31, 2034 and subordinate to HUD's deed of trust). To date, no loan repayments have been made to the City from either available surplus cash flow or any other available project funds.

On September 9, 1997, the project was awarded a California Tax Credit Allocation (TCAC) of \$510,759 per year for a ten-year period. During 1997 and 1998, the property was renovated utilizing these tax credits. However, these credits have since expired.

On October 1, 1999, the property converted its construction financing to the current HUD-insured permanent mortgage, in the principal amount of \$4,208,200 (maturing on November 1, 2034). The HUD financing is in first position, senior in priority to the City loans. The unpaid principal balance on the HUD note is \$3,418,553.15.

As a condition of the 1999 HUD financial assistance, the owner entered into three separate recorded regulatory agreements with: (1) the City of Oakland (expires in 2026 and subordinate to HUD's regulatory agreement), (2) HUD (continues so long as the contract for mortgage insurance continues), and (3) the California Tax Credit Allocation Committee (TCAC). The tax credits expired but the TCAC Agreement is still in effect through 2028. The purpose of these agreements is to ensure that the owner complies with the conditions of financing, including but not limited to, restrictions on project rents, occupancy by individuals and families who are income qualified, operations, ownership and property management.

Alvingroom Court, L.P., is no longer properly managing the development per the terms of the HUD, State, and City regulatory agreements. This failure is due in part to years of financial hardship and on-going management turn-over issues (six different property management companies from the start of operations). This situation puts the City's regulatory agreement and financial investment of more than \$4.1 million in deferred loan balance at substantial risk.

Both the City and HUD have put the owner in default under their respective regulatory agreements. HUD's deed of trust is in senior lien position, and a foreclosure sale will wipe out the City's regulatory and financial interest in the property. The property would be sold at HUD's

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foreclosure free and clear of the HUD or City regulatory agreement. At this point, HUD is no longer willing to consider reviewing and approving a new financial partner. Nor do they want to give the present owner additional time to cure the default.

After months of lengthy discussions, the City submitted a proposal that allowed for the City to either assume the HUD loan or purchase the loan for \$1 million and then assign the loan to an affordable housing partnership or other affordable housing entity. The affordable housing entity would then foreclose on the City's deed of trust with the assurance that the City's security interest and affordability restrictions would survive the foreclosure. Unfortunately, HUD rejected the City's proposal and then countered with an offer for the City to purchase the HUD loan at the face value of its note of \$3,418,553.15 plus accrued interest and fees. The purchase price breakdown is as follows:

Principal Balance:	\$	3,418,553.15
Interest (through 5/31/2016):	\$	21,793.28
Servicer Administrative Fees	\$	300.00
Interest on Tax and Advances	\$	24,441.76
Late Charges	\$	2,279.34
Quote Revision Fee and Misc. Charges	\$ \$	74.00
Outstanding Escrow Advances	\$	416,523.26

Total Projected Due as of May 31, 2016: \$ 3,881,685.45

**ANALYSIS AND POLICY ALTERNATIVES**

In order to protect the project's 126 low-income residents from future rent increases and/or displacement, the City must take the following actions: (1) secure the HUD note and deed of trust, (2) engage a reputable interim property management company to manage the project, (3) release a Request for Proposals to identify an affordable housing entity that will be assigned one or more of the City's secured interests in the property, (4) support the foreclosure of the City's secured loans by the new affordable housing entity, while ensuring that City affordability restrictions remain on title for an additional 55 years, and (5) assist the new affordable housing entity to rehabilitate the project to restore it to decent, safe, and sanitary physical standards fit for human habitation.

The project has suffered from major cash-flow issues that have interfered with the owner's ability to comply with the regulatory requirements regarding replacement reserve set-aside funds to pay for (1) completion of the initial rehabilitation; (2) replacement of systems/appliances; and (3) abatement of deferred maintenance. This failure has negatively impacted the physical conditions and financial monitoring scores from HUD and the City over the years. This continuing non-compliance eventually led HUD to pursue loan foreclosure.

***Physical Inspection, Property Management and Misuse of Funds Issues***

Both the City and HUD have been concerned for several years about the overall management of the project, the condition of the project units, and the welfare of its residents, and have put the owners on concurrent notices of default under their respective regulatory agreements.

In the last several years, the project has failed its physical property inspection required by HUD's Real Estate Assessment Center (REAC). The REAC inspection reports cite repeated and serious deficiencies for items such as: missing/damaged/expired fire extinguishers; missing/damaged/inoperable range/stove/refrigerator; missing/damaged mailboxes; and broken/missing hand rails on walkways/step. In February 2014, HUD approved a disbursement from the Reserve Fund for Replacements in the amount of \$230,226 for the sole purpose of curing the physical deficiencies cited under the REAC. However, based on the HUD Auditor's report of FYE 2014 Audited Financial Statement, approximately \$219,000 of the \$230,226 was inappropriately used by the owner to pay for related services by BLH Construction, an affiliate of Corporation for Better Housing, for work completed in FY 2010 or earlier and not to cure the physical deficiencies under recent REAC inspections. This misuse of the Reserve Fund was unauthorized and deemed ineligible by HUD.

The HUD Auditor's report also recommended release of \$135,643 from the Operating Reserve Account to complete the repair of life safety items, property maintenance, and to make critical payments to vendors. However, these funds were used to pay CBH's Property Management fees in the amount of \$57,000 and \$65,000 for reimbursed payroll expenses. Again, the misuse of funds for this purpose was unauthorized and deemed ineligible by HUD.

In the last several years, the project repeatedly failed the City's physical and financial reviews under its asset monitoring inspection program. Despite numerous discussions between the parties around the on-going deficiencies and the approval of multiple requests to extend time to cure, these deficiencies remain outstanding.

After it became clear that the owners had no intention of curing the deficiencies or complying with their proposal to order a Capital Needs Assessment, the City engaged EMG Corporation Consultants to conduct such an analysis. A copy of EMG's report was sent to the respective owners for review and action. To date, the owners have failed to submit a plan of action to cure the health and safety items listed in the report.

In addition to the outstanding physical issues, the property file review identified major recordkeeping deficiencies, including but not limited to: (1) absence of executed residential leases, (2) absence of annual income re-certifications, (3) rent levels above the allowable income levels in the regulatory agreement, (4) tenant files for units listed as vacant on the Annual Rent and Tenant Income Report, (5) absence of tenant documentation, including initial rental application and financial verification, and (6) high vacancy rates.

The owners continue to disregard the fact that they are in default with both HUD and the City. Despite written and verbal requests to cure default items, no serious effort has been made to cure, and the owners continue to operate and manage the project well below the reasonable standard of care expected of a reputable affordable housing entity.

The fact that the owners maintain high vacancies at EC Reems at a time when there is an affordable housing shortage in Oakland and the surrounding Bay Area is incomprehensible and unacceptable. The City is committed to protect this critical housing resource and preserve the project as long term affordable housing for the benefit of its residents. The owners have simply failed at all attempts to make this project whole and operate it accordingly.

### ***Property Transition Plan***

To ensure an effective transfer of the property to a new affordable housing entity, ownership of the property must be delivered with clear title. At this point, the City must take the following steps: (1) secure the HUD loan for the purchase price of \$3,881,685.45, and (2) secure a contract for interim property management services.

The purchase price per-unit cost breakdown is as follows: \$3,881,685 / 126 affordable units = \$30,807.02/ 55 (55 years of affordability) = \$560 per unit per year. The annual anti-displacement cost of approximately \$560 per unit per year would be less expensive than allocating these funds to a new construction project with an equal number of units. Per figures in the NOFA 2015 report, the per unit cost for new construction averaged \$561,083 per unit. Moreover, given the construction boom in the Bay Area, the cost of new development projects has steadily increased every year.

If the \$30,807.02/unit is coupled with an average cost of \$90,000/unit for rehabilitation, the resulting cost/unit is still far below new construction costs and within the City's standard of \$150,000 subsidy /unit.

The City will solicit proposals from reputable property management companies that have experience working with troubled properties and at-risk tenant populations. The management company will be required to prioritize health and safety items identified in EMG's CNA report and perform an in-depth file review. The file review will include establishing: (1) current vacancy rate, (2) rent schedule, (3) re-certification of the legal tenants, (4) monthly operating budget review, and (5) review of the fair marketing and advertising plan.

To accomplish these steps, the City must first secure the HUD loan by HUD's deadline of July 31, 2017, or risk the project going through HUD's property disposition process and lose this valuable anti-displacement opportunity. The City is eager to purchase the HUD loan and transition the project to a responsible purveyor of affordable housing to avert the potential for displacement and relocation of vulnerable residents.

### ***Alternative to Assuming HUD-Held Mortgage***

As Noted, if the City Council chooses not to step in and assume the HUD Mortgage, this property would move to Foreclosure on the open market. The new property owner is not obligated to maintain the Regulatory Agreements, thereby erasing affordable rents and likely displacing some residents.

Staff believes that this option is unacceptable, given the severe shortage of deeply affordable housing and the current, substandard conditions of the property. Additionally, once this property

is stabilized and better managed, the surrounding community will benefit with regards to public safety and overall maintenance.

### **FISCAL IMPACT**

**SOURCE OF FUNDING:** The City will use funds from the Affordable Housing Trust Fund – Boomerang Funds (1870) and Low Moderate Housing Asset Fund (2830) to purchase the HUD loan.

**FISCAL IMPACT:** Funds used to purchase the HUD loan to prevent displacement and ensure preservation of EC Reems as an affordable housing development will reduce the amount of funds available for the production of new affordable housing units.

Staff recommends that the funds be allocated for the purchase of the HUD loan and for the rehabilitation of the project.

### **PUBLIC OUTREACH / INTEREST**

The ongoing issues around health and safety are complaint driven. When the City receives a health and safety complaint by a resident, it is then addressed by staff. In the last several years, the City received complaints for such things as mold and deferred maintenance items. The residents have been very vocal with the City about the overall condition of the project and their desire to see improvements made by the owner. The City is eager to facilitate these improvements once a new affordable housing entity is in place.

### **COORDINATION**

The preparation of this report was coordinated with HCD, the Building Department's Specialty Combination Inspectors, the Controller's Bureau of the Finance Department, and the City Administrator's Office; the legislation was reviewed by the City Attorney's Office.

### **SUSTAINABLE OPPORTUNITIES**

**Economic:** The project serves low to moderate income residents, and the potential loss of these units to a market-rate developer will negatively impact the residents. By the City purchasing the HUD loan, it will preserve these units as affordable for another fifty-five years under the regulatory agreement. The purchase will also preserve the City's financial interest in the project in the approximate amount of \$4.1 million.

**Environmental:** For most the residents the ability to walk or take public transportation is a key factor in their desire to remain at the property. The project is centrally located on the MacArthur Boulevard corridor that services buses and is near the 580 Freeway. The project is conveniently surrounded by local mom and pop storefronts and small food markets for easy access.

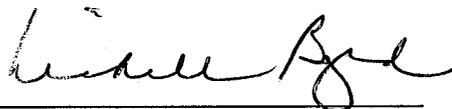
**Social Equity:** The goal is to properly select a suitable non-profit to purchase and rehabilitate the project. The project is in a low-income community of color and these residents are more likely to face the financial hardship and emotional distress associated with displacement and gentrification. In the event of a HUD foreclosure, the project will lose Federal, State, and City affordability restrictions and residents could be forced to relocate due to exorbitant market-rate rent increases and/or evictions. Due to financial pressures and low employment, most residents will have a harder time raising funds to cover their relocation costs. The approval to purchase the HUD note will balance the social equity impact versus allowing a market-rate developer purchase the note, raise the rent or serve eviction notices on the residents.

**ACTION REQUESTED OF THE CITY COUNCIL**

Staff Recommends That The City Council Approve A Resolution (1) Authorizing The Purchase Of A HUD-Held Mortgage Loan Secured By E.C. Reems Garden Apartments Located At 2700 Alvingroom Court (The "Property") For A Purchase Price Of Up To \$4,000,000 Plus Accrued Interest, And (2) Authorizing The City Administrator (Or His/Her Designee) To Take Actions To Facilitate The Preservation And Rehabilitation Of The Property, Including Contracting With An Interim Property Management Company, Foreclosing On City Loans Secured By The Property, And/ Or Assigning City Loans Or Lien Rights On The Property To An Affordable Housing Entity

For questions regarding this report, please contact Norma Thompson, Housing Manager, at 510-238-7137 or Antoinette M. Pietras, Housing Development Coordinator, at 510 238-6177.

Respectfully submitted,



Michele Byrd  
Director, Housing and Community Development  
Department

Reviewed by:  
Norma Thompson, Manager of Housing  
Development

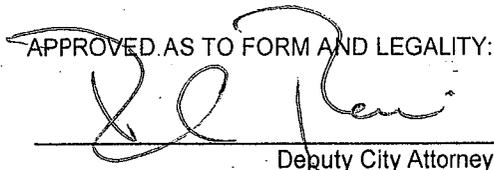
Prepared by:  
Antoinette M. Pietras, Housing Development  
Coordinator  
Housing Development Services

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APPROVED AS TO FORM AND LEGALITY:

  
Deputy City Attorney

## OAKLAND CITY COUNCIL

RESOLUTION No. \_\_\_\_\_ C.M.S.

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RESOLUTION (1) AUTHORIZING THE PURCHASE OF A HUD-HELD MORTGAGE LOAN SECURED BY E.C. REEMS GARDEN APARTMENTS LOCATED AT 2700 ALVINGROOM COURT (THE "PROPERTY") FOR A PURCHASE PRICE OF UP TO \$4,000,000 PLUS ACCRUED INTEREST, AND (2) AUTHORIZING THE CITY ADMINISTRATOR TO TAKE ACTIONS TO FACILITATE THE PRESERVATION AND REHABILITATION OF THE PROPERTY, INCLUDING CONTRACTING WITH AN INTERIM PROPERTY MANAGEMENT COMPANY, FORECLOSING ON CITY LOANS SECURED BY THE PROPERTY, AND/OR ASSIGNING CITY LOANS OR LIEN RIGHTS ON THE PROPERTY TO AN AFFORDABLE HOUSING ENTITY

**WHEREAS**, Alvingroom Court L.P., composed of the Corporation for Better Housing (managing general partner), Hope Housing Development Corporation (operating general partner), and Kavigem, Incorporated, is a housing development limited partnership; and

**WHEREAS**, Alvingroom Court L.P. owns an affordable housing rental housing project in Oakland known as E.C. Reems Garden Apartments, a 126-unit multi-family affordable housing complex located at 2600-2795 Alvingroom Court; and

**WHEREAS**, the City and/or the Redevelopment Agency has made affordable housing development loans to Alvingroom Court L.P. for the project; and

**WHEREAS**, the U.S. Department of Housing and Urban Development (HUD) has insured a permanent mortgage loan on the property; and

**WHEREAS**, the HUD financing is in first position, senior in priority to the City loans; and

**WHEREAS**, the project is subject to recorded long-term rent and occupancy restrictions enforceable by the City, HUD, and other funding agencies; and

**WHEREAS**, Alvingroom Court L.P. has ceased to own, manage and operate the project according to the terms and conditions of the City's and HUD's recorded regulatory agreements; and

**WHEREAS**, the City and HUD have both put the owner in default under their respective loans and regulatory agreements; and

**WHEREAS**, HUD forwarded the project file to its Property Disposition Department to expedite foreclosure under its deed of trust, which is in senior position to the City's deeds of trust securing the City's development loans; and

**WHEREAS**, HUD's imminent foreclosure action and subsequent sale to a market-rate developer will extinguish the City's financial interest and recorded regulatory agreement on the project; and

**WHEREAS**, the City wishes to purchase the HUD loan at the current face-value plus accrued interest; and

**WHEREAS**, the City wishes to take other actions necessary to facilitate the preservation and rehabilitation of the project, including foreclosing on the City's loans secured by the property or assigning City loans or lien rights to a responsible affordable housing entity chosen by the City Administrator; and

**WHEREAS**, per the CEQA Guidelines, this action is exempt from environmental review per Section 15301 of the CEQA guidelines (continuing operation of existing facilities); and

**WHEREAS**, funds are available from the City's Affordable Housing Trust Fund to purchase the HUD loan; now, therefore, be it

**RESOLVED:** That the City Council hereby authorizes the City Administrator or designee to purchase the HUD-held mortgage loan secured by E.C. Reems Garden Apartments for a purchase price of up to \$4,000,000 plus accrued interest; and be it

**RESOLVED:** That \$1,300,000 shall be allocated from the Affordable Housing Trust Fund (1870), Housing Development Organization (89929), Housing Development Program Project (P1000386) for this purchase; and be it

**RESOLVED:** That \$2,700,000 shall be allocated from the Low Moderate Housing Asset Fund (2830), Housing Development Organization (89929), Housing Development Program Project (P1000388) for this purchase; and be it

**FURTHER RESOLVED:** That the City Administrator or designee is authorized to select and contract with an interim property management company to manage and operate E.C. Reems Garden Apartments until the transfer to an affordable housing entity, without returning to Council; and be it

**FURTHER RESOLVED:** That the City Administrator or designee is authorized to take other actions to facilitate the preservation and rehabilitation of E.C. Reems Garden Apartments, including foreclosing on City loans secured by the property or assigning City loans or lien rights on the property to an affordable housing entity selected by the City Administrator, without returning to Council; and be it

**FURTHER RESOLVED:** That the City hereby appoints the City Administrator and/or designee to conduct negotiations, execute documents, and take any other action with respect to the purchase of the HUD loan and the preservation and rehabilitation of E.C. Reems Garden Apartments consistent with this Resolution and its basic purpose.

IN COUNCIL, OAKLAND, CALIFORNIA, \_\_\_\_\_

**PASSED BY THE FOLLOWING VOTE:**

AYES-           BROOKS, CAMPBELL WASHINGTON, GALLO, GIBSON MCELHANEY,  
                  GUILLEN, KALB, KAPLAN, and PRESIDENT REID

NOES-

ABSENT-

ABSTENTION-

ATTEST: \_\_\_\_\_

LaTonda Simmons  
City Clerk and Clerk of the Council  
of the City of Oakland, California