California Local-State Bond Recycling Partnership

California Housing Finance Agency

Management Innovation: Financial

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Summary

Looking for innovative ways to finance more affordable housing in California's bond-constrained environment, CalHFA created a Bond Recycling program through partnerships with Apple and the State Treasurer's Office. In the past year, CalHFA's modest program has gone to the next level by entering truly first-of-their-kind partnerships with the cities of San Diego and San Francisco, so that CalHFA could not only preserve volume cap from their pipelines, but also deploy recycled bonds on their projects.

Background

Despite being used almost exclusively for multifamily housing, California's Federal Tax-Exempt Private Activity Bond Allocation has seen demand outpace supply since 2019, and the oversubscription continues to grow (see Figure 1). This situation has pushed the state housing finance delivery system, and particularly the California Housing Finance Agency – which is self-supported, allowing it to be more flexible and design programs quickly – to search for innovative debt financing alternatives.

Also in 2019, perhaps spurred on by Microsoft's affordable housing investment in Seattle, California's biggest tech companies announced investments of billions of dollars to address the state's affordable housing crisis. These investments went to a variety of state and nonprofit partners, but through negotiations with Governor Gavin Newsom, Apple chose to direct most of its $2.5 billion investment to a partnership with the state itself. A large portion of that partnership is with CalHFA, as Apple's funds are being used to finance homeownership and a $250 million revolving credit facility that makes CalHFA's first-of-its-kind-in-the-state Bond Recycling Program possible.

For additional background, California faces a challenge that most states do not – it has an extremely fragmented issuer base. Between the statewide issuer, CalHFA, and a variety of localities and Joint Powers Authorities, no one entity does anything close to a majority of the issuances in the state. The allocation is done by the California Debt Limit Allocation Committee, which is part of the State Treasurer's Office.

How it works

Bond Recycling, which was enacted into Federal law in the Housing and Economic Recovery Act of 2008 and pioneered by the New York City Housing Development Corporation, is the transfer of tax-exempt bond authority from an existing tax-exempt bond to a new unrelated project. This transfer, however, is done in two parts with CalHFA preserving the bond authority from the original project at the point when the construction loan is paid off, then warehousing it for up to six months until it can be used as part of the initial financing for a new construction project or a rehabilitation deal.

The key to this recycling is the warehousing, which is free to CalHFA and the project thanks to Apple's line of credit (see Figure 2).

Recycled bonds do not allow projects to access 4% Low-Income Housing Tax Credits but are extremely useful as additional tranches of low-cost debt in LIHTC/bond deals as well as the acquisition and rehabilitation of Naturally Occurring Affordable Housing, preservation of exiting regulated affordable housing, 80/20 mixed-income projects and more (see Figure 3).

The public-private partnership with Apple creates the mechanism with which CalHFA's Bond Recycling Program works, but it is CalHFA's public-public partnerships that allow the program to thrive. This includes working with the State Treasurer's Office so that they can help facilitate recycling by building recycling features into the bond documents for every project that receives allocation, by allowing California's State LIHTCs to be awarded without federal 4% tax credits and by building incentives for using recycled bonds into the bond allocation scoring system.

To make sure the program makes the most of the Apple credit line, CalHFA has recently entered groundbreaking partnerships with two of the state's largest local Private Activity Bond issuers, the cities of San Diego and San Francisco.

These collaborations required lengthy negotiations to create partnerships that would be mutually agreeable to both sides and maximize the use of recycled bonds. These negotiations led to individualized term sheets (see Figure 4) that are adapted to follow the city's issuance guidelines, with CalHFA being flexible to create alignment. Perhaps most eye-opening are the data-sharing agreements, each organization allow unprecedented access to pipeline information that allows CalHFA to create a mechanism to intercept the tax-exempt bond authority from city projects before it dissolves.

By leveraging our three large pipelines into one very large pipeline, CalHFA's Bond Recycling Program now has a much bigger pool of projects from which to preserve tax-exempt bond authority. This collaboration is especially meaningful in a state where the issuer base is so splintered. The MOUs, which were approved by the San Diego City Council and San Francisco Board of Supervisors on the same day back in October of 2021, further create special pools within CalHFA's collection of recycled bonds to ensure that bonds from those cities are used in that area whenever possible.

Results

CalHFA's Bond Recycling Program used $12 million to help finance a 96-unit project in 2020 – a new construction project (see Figure 5) that will provide much-needed affordable housing in Santa Rosa which lost thousands of homes in a devastating 2017 fire season – but recycling activities really took off in 2021 and 2022.

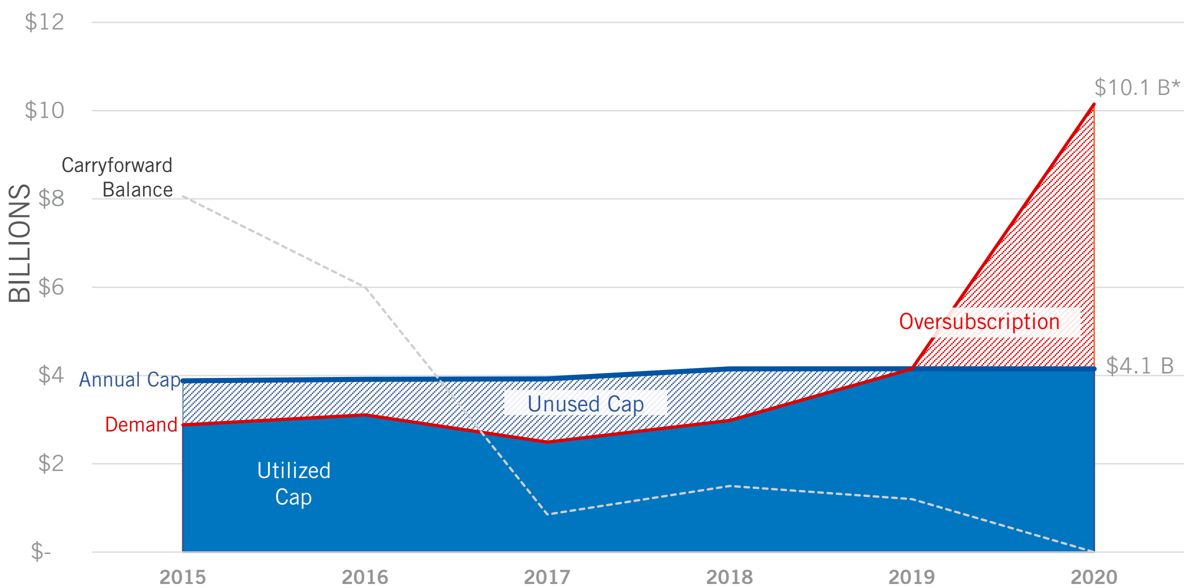
To date, CalHFA has used $200 million in recycled bonds to help finance 1,577 units across eight projects, including 1,061 units in developments that are being financed outside of the state's oversubscribed federal bond allocation.

Thanks to CalHFA's continued collaboration with Apple and the Treasurer's Office, the innovative state-local partnerships with San Diego (see Figure 6), San Francisco and possibly more local issuers, CalHFA expects to use the full capacity of the $250 million credit line in the next few years to finance up to 3,300 units per year.

FIGURE 1 OUTREACH FLYER SHOWING CA BOND CAP USE

MAXING OUT ON HOUSING BONDS

After decades of underutilization, California's bond cap is severely oversubscribed



*Based on Oct. 2019 California Debt Limit Allocation Committee Demand Survey and 2020 application trends

WHAT CONGRESS CAN DO

Lower 50% test for at least 6 years

(S. 1136 /HR 2573 of 2021, Sec. 313)

- Generates more Low-Income Housing Tax Credits with existing State bond cap
- Doubles program production: 17,000 additional homes in CA per year.

Improve bond recycling

- Recycled bonds can fill the gap in tax exempt financing produced by lowering the 50% test.
- Congress can expand this program by allowing issuers more time to recycle *(S. 1136 /HR 2573 of 2021, Sec. 601)*

09/21

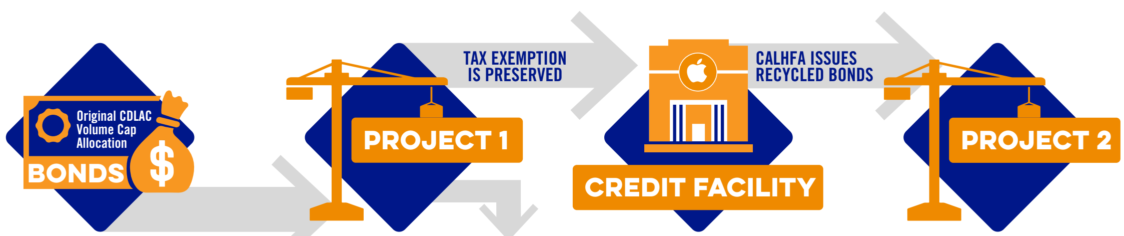
FIGURE 2 OUTREACH FLYER DESCRIBING BOND RECYCLING

CalHFA California Housing Finance Agency

MULTIFAMILY BOND RECYCLING

An innovative new housing finance tool for California

California must increase its housing supply to address the critical issues of homelessness and affordability, yet the $4.1 billion federal cap on tax-exempt housing bonds that can be issued in the State poses a critical bottleneck to ramping up production. Recycling previous bond allocations provides an innovative way to issue bonds outside of the $4.1 billion cap, grow the aggregate amount of resources available in California, and give developers a new financing option to allow projects to pencil.



HOW IT WORKS

The credit facility (Apple) is the key to bond recycling. Instead of bonds being retired after financing a single project, the credit facility pays off the construction loan to preserve those bonds. This allows us to "warehouse" the recycled volume until CalHFA can close on a new project that will deploy the new bonds. Thus, recycled bonds are made available to help finance more affordable housing.

PROJECT TYPOLOGY

- ✓ New financing vehicle outside of State volume cap: Recycled bonds can be paired with soft sources to create an alternative to the bond/ tax credit model
- ✓ 80/20 mixed-income projects that do not require tax credit equity
- ✓ Rental Assistance Demonstration (RAD) public housing rehab projects
- ✓ Additional tranche of low-cost debt in a LIHTC/bond deal
- ✓ Can be used for preservation and new construction

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FIGURE 3 CALHFA BOND RECYCLING PROGRAM TERMSHEET

CalHFA
California Housing Finance Agency

BOND RECYCLING PROGRAM

MULTIFAMILY HOUSING BONDS

Term sheet effective for applications submitted after January 1, 2021

The CalHFA Bond Recycling Program is designed to preserve and recycle prior year(s) tax-exempt private activity bond volume cap that would otherwise expire upon repayment of construction period financing (resulting in redemption of bonds) for multifamily affordable housing development. This program facilitates access to tax-exempt bonds by using preserved private activity bond volume cap ("Recycled Bonds"). In turn, the use of these Recycled Bonds will reduce the need for current year private activity bond volume cap managed by the California Debt Limit and Allocation Committee ("CDLAC"). This program is for developers seeking construction and/or rehabilitation financing for eligible projects that provide affordable multifamily rental housing for individuals, families, seniors, veterans, or special needs tenants ("Projects"). Please refer to the standard CalHFA Conduit Issuer Program Term Sheet for terms, conditions, and pricing related to the issuance of bonds. In the event that CalHFA is issuing Recycled Bonds pursuant to a Memorandum of Understanding ("MOU") with a local issuer, please refer to the CalHFA Conduit Local Issuer Program Term Sheet, which is specific to the terms of that MOU for terms, conditions, and pricing. In some instances, the MOU may provide that the standard CalHFA Conduit Issuer Program shall govern the bond issuance with regard to one or more of these items.

Qualifications	Available to for-profit, nonprofit or public agency sponsors. Rules of Recycling: • New loans utilizing Recycled Bonds must be made to an eligible project within 180 days of the effective date of the preservation of the construction bonds ("Original Bonds"). • The issuance of the Recycled Bonds ("Bond Refunding") must occur within 4 years of the issuance of the Original Bonds. • Typically, preservation of the Original Bonds occurs at conversion of construction financing to permanent financing (at which time the bonds funding the original construction debt will be preserved vs. redeemed/repaid). • Maturity of any Recycled bonds must be within 34 years of the Original Bond issuance date (generally construction loan closing date). • Recycled bonds are subject to public notice requirements (TEFRA). • Recycled bonds cannot generate 4% LIHTC. • Volume cap cannot be recycled more than once. • Recycled bonds can only be used for multifamily housing.
Eligible Projects	New construction and/or existing projects with the following financing structure: 1. 100% affordable projects pursuant to CDLAC requirements. • CalHFA Recycled Bonds may provide loan proceeds for up to 45% of the Project's total development costs. • The Project may apply to CDLAC for the remaining 55% of bond allocation needed to generate loan proceeds. The CalHFA Recycled Bonds are not included in the Project's 50% aggregate basis test. 2. Refinance of projects with expiring affordability restrictions or projects reaching the end of their tax credit compliance period. CalHFA Recycled Bonds will provide loan proceeds for up to 100% of the Project's total development costs. 3. Finance acquisition and substantial rehabilitation of existing market-rate units converting to affordable. CalHFA Recycled Bonds will provide loan proceeds for up to 100% of the Project's total development costs.

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BOND RECYCLING PROGRAM

Eligible Projects (Continued)	4. Projects restricted at less than 100% of the total units • A minimum of 20% of total units restricted at or below 60% of AMI. Projects may have up to 80% of their total units as unrestricted or market rate. ("80/20 Financing Structure") • CalHFA Recycled Bonds will provide loan proceeds for up to 80% of the Project's total development costs. • The Project may apply to CDLAC for the remaining 20% of bond allocation needed to generate loan proceeds. The CalHFA Recycled Bonds are not included in the Project's 50% aggregate basis test. See CalHFA standard Conduit Issuer Program Term Sheet for details. Note: Recycled Bonds are subject to availability.
Occupancy Requirements	Either (A) 20% of the units must be rent restricted and occupied by individuals whose incomes are 50% or less of the area median income as determined by HUD ("AMI") with adjustments for household size ("20% @ 50% AMI"), or (B) 40% or more of the units must be both rent restricted and occupied by individuals whose income is 60% or less of the AMI, with adjustments for household size ("40% @ 60% AMI"); however in the latter case, a minimum of 10% of the units must be at 50% or less of AMI ("10% @ 50% AMI"). Borrower will be required to enter into a Regulatory Agreement which will be recorded against the Project for the Qualified Project Period (as defined in the CalHFA Regulatory Agreement for the issuance of the conduit bonds). This includes the later of the federally-required qualified project period, repayment of the Bond funded loan, redemption of the Bonds, termination of Section 8 assistance, as applicable, or the full term of the CDLAC Resolution requirements.
Affordability Period	The affordability period shall generally be 55 years from the Recycled Bond closing, unless, the project is an existing CalHFA portfolio project not seeking additional allocation from CDLAC, then the affordability period shall be the longer of 1) 20 years from the new loan closing date, 2) CalHFA permanent loan term or 3) an additional 5 years beyond the expiration of the current affordability restrictions.
Fees (subject to change)	Bond Recycling Transaction Fee: $25,000, due at loan closing. Negative Arbitrage: Borrowers using CalHFA Recycled Bonds will be required to draw down the entirety of the Recycled Bonds within 180 days from the date those bonds were preserved ("Bond Preservation Effective Date"). See standard CalHFA Conduit Issuer Program term sheet for other applicable fees. The Borrower shall be responsible for all other costs of Bond issuance including fees of the underwriter, trustee, rating agencies, lender, compliance administrator, all Bond counsel legal fees, and any other parties required to complete the transaction.

Last revised: 4/2022

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FIGURE 4 CALHFA-SAN DIEGO BOND RECYCLING PROGRAM TERMSHEET

CalHFA California Housing Finance Agency

SAN DIEGO-CALHFA CONDUIT ISSUER AND BOND RECYCLING PROGRAM

MULTIFAMILY HOUSING BONDS

Term sheet effective for applications submitted after January 1, 2021

The Housing Authority of the City of San Diego and the San Diego Housing Commission (collectively "San Diego" or "SD") and CalHFA have worked together to create the SD-CalHFA Conduit Issuer and Bond Recycling Program ("SD-CalHFA Bond Program") is designed to preserve and recycle prior year(s) tax-exempt private activity bond volume cap which was originally issued by SD, and which would otherwise expire upon repayment of its related construction financing ("Original Bonds"). The SD-CalHFA Bond Program is designed pursuant to a Memorandum of Understanding ("MOU") between CalHFA and SD. This Program facilitates access to tax-exempt bonds by using preserved private activity bond volume cap ("Recycled Bonds"). The use of these Recycled Bonds may reduce the need for current year private activity bond volume cap managed by the California Debt Limit and Allocation Committee ("CDLAC"). This program is for developers seeking construction and/or rehabilitation financing for eligible projects located in the City of San Diego that provide affordable multifamily rental housing for individuals, families, seniors, veterans, or special needs tenants.

Qualifications	Available to for-profit, nonprofit or public agency sponsors. Rules of Recycling: • New loans to finance an Eligible Project (as defined in this Term Sheet) utilizing Recycled Bonds must be closed and funded within 180 days of the effective date of the preservation ("Preservation Date") of the Original Bonds. • The issuance of the Recycled Bonds ("Bond Refunding") must occur within 4 years of the issuance of the Original Bonds. • Typically, the Preservation Date of the Original Bonds occurs at conversion of construction financing to permanent financing (at which time the bonds funding the original construction debt will be preserved vs. redeemed/repaid). • Maturity of any loans to Eligible Projects funded with Recycled Bonds must be within 34 years of the Original Bond issuance date. • Recycled Bonds are subject to public notice requirements (TEFRA) by CalHFA. • Recycled Bonds cannot be used to qualify for 4% federal LIHTCs. • Volume cap cannot be recycled more than once. • Recycled Bonds can only be used for multifamily housing.
Eligible Projects	The SD-CalHFA Bond Program may provide Recycled Bonds to new construction multifamily projects ("New Construction Project") and/or existing multifamily projects ("Existing Project") with the following financing structures: 1. New Construction Projects that are 100% affordable projects financed pursuant to CDLAC's regulatory requirements. a) Recycled Bonds may be provided to finance any amount up to 45% of the New Construction Project's total development costs. b) The New Construction Project may apply to CDLAC for a new bond cap allocation sufficient to fund any portion of the remaining 55% of total development costs. Recycled Bonds are not eligible for inclusion in the New Construction Project's 50% aggregate basis test.

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BOND RECYCLING PROGRAM

Eligible Projects (continued)	2. Acquisition, Refinance, and/or Rehabilitation of existing multi-family projects ("Existing Projects") which will either preserve or increase, by a minimum of 20%, the number of units subject to affordable regulatory restrictions. a) The SD-CalHFA Bond Program may provide the refinance of affordable Existing Projects which are extending the affordability restrictions of 100% of total units (excepting any onsite manager's unit). The SD-CalHFA Bond Program will provide loan proceeds for up to 100% of the Existing Project's total development costs. However, any intent to include new bond cap for purposes of 4% federal tax credits, must be for at least 55% of the financing. b) The SD-CalHFA Bond Program may provide the acquisition and substantial rehabilitation of market-rate Existing Projects which are converting existing units to an affordability structure which meet the Minimum Occupancy Requirements outlined below. The SD-CalHFA Bond Program will provide loan proceeds for up to 100% of the Project's total development costs. Note: Recycled Bonds under the SD-CalHFA Bond Program are subject to availability.
Minimum Occupancy Requirements	Either (A) 20% of the units must be rent restricted and occupied by individuals whose incomes are 50% or less of the area median income as determined by HUD ("AMI") with adjustments for household size ("20% @ 50% AMI"), or (B) 40% or more of the units must be both rent restricted and occupied by individuals whose income is 60% or less of the AMI, with adjustments for household size ("40% @ 60% AMI"); however in the latter case, a minimum of 10% of the units must be at 50% or less of AMI (i.e., 30%@60% AMI; 10%@50% AMI). Any units restricted by CalHFA pursuant to this program, including those units restricted in addition to the minimum requirements set forth above, shall be rented at rents up to 30% of the applicable income restriction using the occupancy assumptions required in the Agency's Regulatory Agreement. Rents for all restricted units must be at least 10% below market rents as evidenced by a current market study or an appraisal current within 6 months. Borrower will be required to enter into a CalHFA Regulatory Agreement which will be recorded against the Project for the Qualified Project Period (as defined in the CalHFA Regulatory Agreement for the issuance of the conduit bonds). This includes the later of the federally required qualified project period, repayment of the Bond funded loan, redemption of the Bonds, termination of Section 8 assistance, as applicable, the full term of the CDLAC Resolution requirements or 55 years.
Affordability Period	The affordability period shall be 55 years from the Recycled Bond closing.
Fees (subject to change)	Negative Arbitrage: Borrowers accessing Recycled Bonds under the SD-CalHFA Bond Program will be required to draw down the entirety of the Recycled Bonds within 180 days from the date the Original Bonds were preserved ("Bond Preservation Effective Date"). • Bond Recycling Transaction Fee: $25,000, due at bond closing. • Annual Monitoring Fee: For bonds issued pursuant to this Term sheet, 12.5 bps of the total bond issuance amount due at construction loan closing and due annually thereafter until permanent loan conversion. After permanent loan conversion, billed annually in advance, 12.5 bps of principal amount of the CalHFA issued Bonds outstanding at permanent financing conversion regardless of any later reductions of the outstanding principal of the CalHFA issued Bonds. Minimum Annual Monitoring Fee shall be $10,000 for the entire term of the CalHFA Regulatory Agreement.

BOND RECYCLING PROGRAM

Fees (subject to change) (continued)	• For all other applicable fees, including upfront Issuer Fee, refer to San Diego Housing Commission (SDHC) BOND ISSUANCE AND POST-ISSUANCE COMPLIANCE POLICY: https://www.sdhc.org/wp-content/uploads/2019/04/Bond-Policy-300.301.pdf If used in conjunction with a CalHFA permanent loan product, the annual monitoring fee outlined on the CalHFA permanent loan program term sheet will not be charged. The Borrower shall be responsible for all other costs of Bond issuance including fees of the underwriter, trustee, rating agencies, lender, compliance administrator, all Bond counsel legal fees, and any other parties required to complete the transaction.

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FIGURE 5 REDWOOD APARTMENTS (SANTA ROSA) NEARING COMPLETION

FIGURE 6 ARTIST RENDERING OF CREST ON IMPERIAL (SAN DIEGO)

Crest on Imperial is projected to use funding made possible through the Local-State Bond Recycling Partnership between San Diego and CalHFA. It is expected to use $4.3 billion in recycled bonds to help finance 100 units of affordable housing.