

City of Los Angeles

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Council File: 12-0049-S25
Council Districts: CD 6
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Honorable Members of the City Council
City of Los Angeles
c/o City Clerk, City Hall
200 N. Spring Street
Los Angeles, CA 90012

COUNCIL TRANSMITTAL: LOS ANGELES HOUSING DEPARTMENT REQUEST FOR AUTHORITY TO MODIFIED TERMS FOR THE PREVIOUSLY APPROVED STRATHERN PARK APARTMENTS LOCATED AT 11040 W. LORNE STREET AND 11111 W. STRATHERN STREET

SUMMARY

The General Manager of the Los Angeles Housing Department (LAHD) respectfully requests authority to approve the modified terms and conditions of the previously approved loan modification for the Strathern Park Apartments, a 241-unit affordable housing development located at 11040 W. Lorne Street and 11111 W. Strathern Street in Sun Valley. Although the City Council approved the transaction in 2022 (C.F. No. 12-0049-S25), the transaction was placed on hold.

The original approved transaction did not occur on its planned timeline due to delays in securing environmental and other underwriting clearances required under the HUD 223(f) mortgage insurance program. Specifically, based on the location of the property, HUD required an environmental review and a No Further Action letter from LA County Fire Department; an 18 to 24-month process. During that time there were changes in the construction and lending environments, which reduced the loan amount and the stipulated shared Net Capital Proceeds to zero dollars from the anticipated \$5 million for both the borrower and LAHD. Construction costs for labor and materials have increased significantly and rising interest rates have lowered the amount that can be borrowed. LAHD considers this a significant change to the original approved transaction.

Key changes since the 2022 approval include a reduction in the HUD 223(f) loan amount from \$23 million to approximately \$17.5 million, resulting in no Net Capital Proceeds (ie. Borrower and LAHD will no longer be receiving the originally estimated amount of \$5M each). The amount to be used for property rehabilitation and capital needs has increased from \$10 million to \$14.1 million due to construction cost escalations. And the construction approach has shifted from a 12-month General Contractor-led rehab to a 36+-month phased rehab using a large upfront deposit to the project's lender-controlled Replacement Reserves account, which will reduce

the impact on the residents and also permit the Owner to right-size the subcontractor type for the project so the funds to improve the property are spent more efficiently.

RECOMMENDATIONS

- I. That the City Council, subject to the approval of the Mayor:
 - A. AUTHORIZE the General Manager of LAHD, or designee, to reaffirm and reapprove the previously authorized loan modification for the Strathern Park Apartments, to subordinate the loan, extend the loan maturity date, and to modify the residual receipts split for the affordable housing project located at 11040 W. Lorne Street and 11111 W. Strathern Street;
 - B. AUTHORIZE the General Manager of LAHD, or designee, to execute any necessary loan documents required to amend the loan and related documents to clarify the net capital proceeds, modify the interest rate, and establish a minimum allocation for hard costs for the affordable housing project located at 11040 W. Lorne Street and 11111 W. Strathern Street; and,
 - C. AUTHORIZE any other technical adjustments to the property ground lease, loan, and other documents as deemed necessary by the City Attorney to implement the changes outlined in this transmittal.

BACKGROUND

In 2022, the City Council approved a loan modification for the Strathern Park Apartments to facilitate a HUD 223(f) refinance and rehabilitation of the property. The approved financial structure included a \$23 million HUD loan, a 50/50 Net Capital Proceeds split (originally estimated at \$5M for the borrower and \$5M for LAHD), and a 12-month rehabilitation led by a General Contractor. Since that time, interest rates have increased and construction costs have escalated. Taking into account these factors, the Owner has proposed a revised approach to accommodate the lower amount of financing, which covers the increased cost and also actually increases the amount the Owner will use to address property capital needs by \$4,100,000 for future renovations and phased construction. This will ensure the upkeep of the affordable project without having to come back to LAHD and/or other sources for additional funding in the future. The funds in the Replacement Reserve will require the Owner to get LAHD’s authority and approval for use of the money on the project.

The revised transaction now has a \$17,500,000 HUD loan, reduced from \$23,119,395. As such, the borrower and LAHD will now each receive \$0. But the borrower has agreed to ramp up the amount that will go be used for property improvements from \$10M to \$14.1M to handle rehabilitation and work on the project well into the future and, thus, provide affordability for a very long extended period without having to come back to the City for additional funding in the future. This, and other revisions, can be seen on Table 1 (below).

TABLE 1, ORIGINAL APPROVED REQUEST VS. CURRENT REQUEST			
Financing Category	Current Loan	2022 Approval	2025 Revised Transaction
First Mortgage**	\$1,278,335*	\$23,119,395 (HUD 223(f))	\$17,500,000 (HUD 223(f))
Net Capital Proceeds to Borrower	N/A	\$5,000,000	\$0
Net Capital Proceeds to LAHD	N/A	\$5,000,000	\$0
First Mortgage Interest Rate	6.25%	2.50%***	5.65%***
Hard Costs and/or Reserve Deposits	N/A	\$10,000,000	\$14,100,000

LAHD Simple Interest Rate	5% to 7%	3%	8% to 10%****
LAHD Loan Maturity Date	2032	2062 to 2063	2062 or 2063*****
LAHD Residual Receipts	40%	Reduced to 20% for 15 years, thereafter, reverts to 40%.	Reduced to 20% for 15 years, thereafter, reverts to current 40%.
<p><i>*First mortgage balance per 11/2025 balance sheet.</i></p> <p><i>**Estimated amounts based on current market conditions and expected underwriting. Final amount subject to underwriting.</i></p> <p><i>***Estimated Interest Rates. Rate lock will occur at issuance of HUD Firm Commitment.</i></p> <p><i>****Interest Rate will increase to the simple interest equivalent to LT AFR compounded as determined by tax counsel and CPA prior to closing.</i></p> <p><i>***** 2062 if closing is in 2026, 2063 if closing is in 2027.</i></p>			

The revised transaction terms reflect current market realities, yet maintains or improves the affordability and rehabilitation goals of the original approved transmittal.

Current Request

- To amend, revise, combine and clarify the affordability covenants to correct certain ambiguities regarding their terms, including the termination date, and include current City standard requirements and City ADA requirements, among other things.
- Extend the loan terms and clarify and revise the CRA/LA affordable regulatory agreement for a new 35-year period to co-terminate with the new HUD 223(f) senior loan.
- Change the net capital proceeds language so that the net capital proceeds be split 50/50 between the borrower and the City with the borrower waiving (writing off) its \$8MM+ balance of the preferred return (original investment).
- Approx. \$14 million of the loan proceeds from the HUD 223 (f) financing are to be deposited to a replacement reserve and used to upgrade the property.
- Change the residual receipts split from the current 60/40 (Borrower/LAHD) to 80/20 for the first 15 years and then back to 60/40 for the remaining years respectively.
- Include language in the loan agreement that, should a capital transaction occur at any time, then residual receipts split shall change to 50/50. This enables the City’s residual receipts split to automatically be increased from 20% to 50% during the first 15 years and go from 40% to 50% after the first 15 years.
- LAHD to change the loan simple interest rates from 5% and 7% to approximately 8-10% moving forward.
- LAHD to subordinate its existing loans to the new senior loan. LAHD to use the current City contract provisions as applicable to loan documents and related agreements.

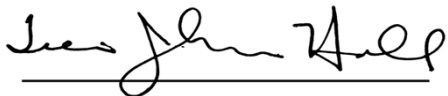
- The LAHD affordable housing covenant referenced above shall remain senior to the HUD FHA loan and shall survive any foreclosure of the HUD FHA loan. This ensures that affordability will be protected and will continue at the property in the event of a foreclosure action.
- Borrower be allowed to admit a 501 (c) (3) subject to LAHD’s approval as the New MGP.

Any other technical adjustments which may be required or deemed appropriate by the Office of the City Attorney

FISCAL IMPACT

There is no impact to the General Fund.

Approved By:

A handwritten signature in black ink, appearing to read "Tiena Johnson Hall", is written over a horizontal line.

TIENA JOHNSON HALL
General Manager
Los Angeles Housing Department