A GUIDE FOR DEVELOPING
CHILD CARE FACILITIES
WITH AFFORDABLE HOUSING

Financing

BRIDGE Housing

BUILDING SUSTAINING LEADING

FINANCING

Financing

Summary

For all but the large for-profit child care providers, financing is the largest hurdle today to building child care facilities in California. Since 1986, the Low Income Housing Tax Credit program has become the primary source of financing for affordable rental housing development. No comparable program exists that is specifically designed to finance child care facilities development. Each new child care facility faces the challenge of cobbling together scarce funds from a number of debt, equity, and/or grant sources from the public and private sector.

To significantly increase the number of child care spaces in California, it is necessary to develop products tailored to financing child care facilities development. The financing needs and the challenges of financing child care development, particularly for child care facilities serving low- and moderate-income working families, are very similar to affordable housing. Early access to predevelopment funds for site acquisition and due diligence are needed. Low operating cash flow limits a provider and a particular facility's ability to support debt. Additionally, like project-based Section 8, public subsidies are subject to annual state or federal legislative appropriations and subsidy levels are set by the government.

This chapter provides information to assist the developer and/or owner to finance child care facilities. This chapter contains a background on how child care facilities have been and can be financed, underwriting principles, a rudimentary understanding of the income and expenses of child care operators, and term sheets for frequently used capital sources.

How Child Care Facilities Have Been Financed

At the time of the writing of this handbook, most child care facilities co-located with affordable housing were financed with grants and public soft debt and/or equity available for the provision of affordable housing and related supportive services. Child care–specific funds were then used as gap financing, except in the case of Head Start facilities where Head Start capital funds provided significant initial financing. Since funds must be cobbled together and providers and developers have access to different sources of capital, providers and developers have typically collaborated in the fundraising effort. The fundraising responsibilities are typically allocated pragmatically, according to which party can access a particular source of capital and who has the capacity to secure the financing, or they are allocated by scope of work, the developer fund raising for the warm shell and the child care provider fund raising for the tenant improvements.

Many grants for child care facilities development are available solely to the provider; therefore, the provider often secures these funds and contributes the funds to the development. Few child care operators own their facilities. Funders typically require the facility to be operated as a child care facility for a designated number of years in order to ensure their investment results in the creation of an ongoing service to the designated service population. In many cases, a Memorandum of Understanding will suffice. However, a long-term lease or evidence of some form of ownership interest is frequently required.

Use of debt as a financing tool is relatively rare among providers and developers both, but is beginning to increase. This is markedly different from affordable housing, where financing is usually approached by first analyzing the amount of debt a project can support, then adding low income housing tax credit equity and public and private gap financing sources. Child care facilities financing has been approached by first analyzing available public and private sources of funding, primarily grants, soft debt and donations, and, only after these sources are exhausted, considering debt financing. In a few cases, the provider or owner has secured a small amount of debt that is repaid through the provider's cash flow directly or through rental payments from the provider to the owner. In the field, the low utilization rate for debt financing is generally attributed to provider's fear of the recourse nature of debt financing, the limited ability of facilities to support debt, lender's lack of knowledge of how to underwrite child care providers and operations, and lender's risk aversion given the contingent nature of child care operating funding and provider's limited track record with servicing debt.

In some cases, affordable housing developers and owners have secured loans on behalf of the provider. Developers and owners have taken on this role when necessary; most providers who serve low- and moderate-income families operate on such tight margins and cannot meet lender's underwriting requirements. Few providers have a proven track record in servicing debt. Conversely, as described in the preceding paragraph, many lenders do not know how to approach understanding and managing the risks associated with under-writing child care. Also, if housing funds are used, the housing developer usually must secure the financing in association with the housing; the provider may need to assist in meeting underwriting requirements of a lender or investor. However, this structure, where the developer is essentially the borrower, may create a recourse problem if the provider decides to vacate the premises or no longer offers child care services. Please refer to Chapter IV: "Partnering with the Provider" for legal and structuring information.

The ABCD Fund, a new portfolio of financing resources tailored to child care facilities development in California for all phases of development from planning through construction, was created in 2003 by the David and Lucile Packard Foundation. The Low Income Investment Fund (LIIF), a community development financial institution, designed and now administers the ABCD Fund. The Fund consists of a planning grant and loans for all phases of development including predevelopment, construction and permanent operations. The ABCD Fund is a valuable new resource and potentially represents the first step towards a creating a sustainable financing mechanism to fund child care facilities development in the long term.

Common Capital Sources

Common equity and debt sources used by developers and providers in California are listed in the chart below. Term sheets for these sources with common and somewhat static requirements statewide are included at the end of this chapter. Debt Financing is described in greater detail in the next section below. Additional sources whose availability or requirements differ significantly from locality to locality or from year to year are described briefly under Other Discretionary Funds. When pursing financing for a specific project, check with the Low Income Investment Fund (LIIF), local government child care facilities development staff, your local intermediary, or other sources of financing on the availability of funds and any changes to terms and requirements.

The chart below provides a list of common sources organized by type of financing. Term sheets are organized according to whether they are public or private since some sources can be structured as debt or grants.

COMMON CAPITAL SOURCES FOR CHILD CARE FACILITIES

	Equity	*Hard Debt*	*Soft Debt*	*Grant*
Public:			Community Development Block Grants	Community Development Block Grants
			Multifamily Housing Program NSSS Funds	Head Start One-Time Supplemental Funds
			Redevelopment Agency Tax Increment Funds	Proposition 10 Funds
			Local Child Care Funds	Local Child Care Funds
				Transportation Funds for Transit Oriented Development
Private:		Conventional Loan		
	LIHTC	ABCD Loans		ABCD Planning Grant
		Loans from Community Development Financial Institutions		Private foundations, corporations, individuals

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Debt Financing—Underwriting the Provider

In a situation in which the developer will provide a guarantee for financing on behalf of the provider, the developer should underwrite the provider. Just as with any commercial rental or turnkey development services contract, the level of underwriting that should be undertaken should be based on the degree of risk exposure the developer is taking on. At minimum, the lender(s) and/or investor(s) require certain guarantees and/or that underwriting requirements specific to the child care facilities be met.

BASIC UNDERWRITING GUIDELINES

In their "Guide to Underwriting Child Care," the Low Income Investment Fund (LIIF) has outlined the "Five C's of Credit" principles when considering the capacity of a child care business to carry debt.

Low Income Investment fund

A GUIDE TO UNDERWRITING CHILD CARE

Following the "Five C's of Credit" principles, this document is intended to be a guide when considering the capacity of a child care business to carry debt.

1. Cash Flow/Capacity to Repay

Will the child care business be able to meet its monthly payment?

This is typically determined by the debt service coverage ratio. When reviewing a child care business' cash flow statement remember their margins are usually very thin so small fluctuations to revenue or expenses will have big implications. When determining a child care business' capacity to carry debt, consider the following:

Revenue[41]

- When expanding or opening a new location, a conservative monthly phased ramp-up budget should be developed
- No more than 90% enrollment & collections should be assumed
- Remember that government reimbursements take 30–90 days
- Be sure to scrutinize sources for trends, future risks, local environment, and contingency planning
- Consider required staff/child ratios when adjusting enrollment if you're trying increase the revenue stream

[41] Revenue sources may include Parent Fees (non-subsidized tuition), Head Start/Early Head Start, California Department of Education (Child Care, State Preschool, and Alternative Payment), CalWORKs, USDA Food Program, CDBG, Corporate or Philanthropic Grants, and other locally administered subsidies.

Expense

- Public subsidies don't always cover expenses, especially in high cost areas
- Analyze expenses as fixed (rent, mortgage, insurance) and variable (staff, food) to determine a break even enrollment
- Expenses vary greatly due to several factors:
  - Location of the program and regional costs
  - Quality of child care provided
  - Age of the children being cared for (infants most costly)
  - Needs of the child (special needs children higher)
- Rules of Thumb:
  - Payroll 55%–80%, very labor intensive sector
  - Enriched programs tend to have more staff
  - Recruitment costs should be budgeted on-going
  - Occupancy 8%–25%[42]
  - Utilities tend to be high
  - Food 4%–10%
  - Full day programs have higher costs
  - Materials/Supplies, Professional Dev. 1%–6%
  - Replacement reserves, $0.50 to $1.50 per sq ft, depending on property condition[43]
  - Account for operating reserves when allowable by government funding sources

2. Character/Capacity to be a Responsible Borrower

Is this a sound child care business? Is there leadership and technical capacity to effectively operate the business?

There are many nuances to a child care business. Continual fundraising to cover the full cost of operations, compliance with facility licensing regulations, and managing public subsidy contracts to name just a few. In order to evaluate this type of business it's helpful to understand some sector-specific quality business indicators.

Evaluating the Business

- Is there evidence of lengthy child care experience, community involvement and support?
- Do they have experienced and engaged board members, management, and staff?
- Is there low staff turnover and commitment to professional development?
- Do they have experience and are in good standing with public subsidy sources?
- What is their track record with Community Care Licensing?[44]
- Has there been a high rate of avoidable liability insurance claims.
- Do they have a quality child care program (environment, staff/child interaction, parent involvement)?

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[42] Child care providers who serve low income families typically pay a maximum of 8% for occupancy costs.

[43] $0.50 to $1.50 per square foot should be deposited annually.

[44] Refer to Chapter III: Choosing a Provider: Criteria for Selecting a Provider—Licensing and Accreditation Record for details on how to obtain the track record of a center or provider.

- Have they prepared a detailed market analysis with current and reliable data? An analysis should describe supply and demand and include the following:
  - Target population growth and income trends
  - The impact of housing, jobs, education, and transportation on their market, site location and business operations
  - Evaluation of competition (openings, closures, location, slots, target market)
  - Subsidy sources and availability
  - Special market niche
  - Current waiting list
  - High rate of referrals and other successful marketing strategies

3. Capital/Equity Investment
What is the business' cash investment? What other equity sources are they investing?
Child care businesses are typically debt averse, historically relying on fundraising to cover the full cost of operations and to pay for capital improvements. However, some child care businesses can actually pay up to 40% of capital development costs with debt. Yet, in order to cover the entire cost of a capital improvement project, grants and equity investments are needed.

4. Collateral
What is the value of the property being pledged for repayment? If property isn't being pledged, what form of collateral will be used?
Determine the value of the property, leasehold improvement, and other business assets to insure it will meet a lender's minimum loan to value ratio. If there isn't sufficient collateral, a third party guarantor may be necessary and there are agencies that offer loan guarantees specifically for child care businesses.

5. Credit History
What is the credit history of the business (owner, principles, or nonprofit board)?
Inquire about recent credit reports. It is not unusual, however, for child care businesses to have no credit history, especially if they are debt adverse. But, these businesses can verify their ability to pay bills and manage their finances by documenting their relationships with vendors.

The principles "Cash Flow/Capacity to Repay" and "Market Study," described in the preceding exhibit, differ enough from the knowledge base of affordable housing developers that tools for understanding these principles are provided in the section that follows entitled "Sizing Debt and Rental Payments" and in Chapter II, "Assessing the Market."

SIZING DEBT & RENTAL PAYMENTS

As described in detail in Chapter I, "California Child Care System," subsidies from the federal or state government enable child care providers to serve very low- to moderate-income families. However, these subsidies frequently do not cover the full cost of care. Due to lack of knowledge or experience with the business of child care, housing developers frequently incorrectly expect that child care businesses can support debt or make rental payments like any commercial tenant. The business of providing affordable child care is much like the business of providing affordable housing–subsidies for child care spaces are low, and families are stretched in their ability to make up the difference if the subsidy program allows it. Older children whose care is less expensive than younger children, full-fee families, and a provider's larger centers can frequently cross-subsidize the cost of care for younger children. Providers who serve low-income families are usually looking for no or minimal rental payments and tend to be debt-adverse.

In some cases, a modest amount of debt can be supported by the center's operating budget. Modest rental payments are considered by all subsidy programs as a legitimate program services expense. The larger the center, the more likely it can achieve and maintain a positive cash flow due to the economies in staffing, marketing, and purchasing of consumables. A larger-size center is frequently difficult for developers to achieve since larger plots of land are increasingly rare in all but rural areas, and land costs are high in California. Also, the developer may have to reduce the number of affordable housing units in order to provide a child care center. Many providers say that at 48 to 62 child spaces centers begin to break even. A 48 to 62 child space center would require between 5,280 sq. ft. (if no space was allocated for use by adults for a 48-space center) and 10,850 sq. ft. (including adult offices, circulation space, etc., for a 62-space center). However, child care is an important and enabling resident and neighborhood service that can also be a great tenant for ground floor commercial space. Around and beyond this size, centers can make a rental payment or begin to support debt.

The three main subsidies, described in detail in Chapter I, "California Child Care System," are 1) Head Start (HS) and Early Head Start Program funds (EHS), 2) Alternative Payment vouchers (AP), and 3) center-based contracts. The first is administered by Head Start and the second and third are administered by the California Department of Education's (CDE) Child Development Department (CDD).

All three program subsidies may be used to support debt or pay rent as long as those expenses are characterized by the provider as program service expenses, i.e., expenses necessary to provide contracted child care services, unless the expense is specifically nonreimbursable or ineligible by regulation. Use of funds to support debt or pay rent may also be subject to approval by the administrating agency. The provider will know how much of their current program subsidies are being used to support debt or pay rent and may inquire at the agency that administers their program subsidies as to the amount that could be included for a new facility. Whether the subsidies can actually support debt or pay rent, and how much, depends on the particular provider and center. Determining factors for sizing debt are 1) amount of subsidy, which may differ from provider to provider and can frequently be less than the cost of care, 2) size of the child care center and number of children served, 3) staff costs, 4) size of the provider, and 5) availability of other sources to cover the cost of care.

When margins are slim, a rent residual calculation combined with a maintenance and management cost analysis may be the best approach. Using the LIIF "Guidelines to Underwriting Child Care," compare the total revenues to the total expenses for the proposed center and those for another of that provider's centers of a similar size and service population. Look at this comparison over a two-year period, if possible. Assuming there is a positive balance, the balance may be used to size the rental payment. If any revenue or expenses seem out of proportion, discuss them with the provider. Program decisions and design decisions will have a significant impact on the income and expense statement. For example, program decisions—such as if the center director will be counted in classroom staff-child ratios—have a significant impact on the income and expense statement. If the center director is counted towards maintaining classroom ratios, one less staff salary would be paid. Design decisions with respect to the center's insulation and heating, venting, and air conditioning system have a significant impact on the income and expense statement, since small children are especially sensitive to climate and utility costs for child care centers tend to be high. The results of the rent residual calculation should then be compared to the results of a maintenance and management cost analysis that assesses the cost for the owner to maintain and manage the child care facility space. These are the costs the owner bears for maintaining the outside of the building, major systems, etc. These costs will depend on the terms of the lease between the child care operator and the owner.

To determine supportable debt, a similar calculation can be used. The debt may be sized based on the residual cash flow less operating expenses less replacement reserves and other owner expenses for maintaining the property.

Each of the program subsidies' ability to support debt or pay rent is reviewed individually below. Some providers are able to creatively layer these subsidies and improve their centers' bottom line, e.g., using center-based contracts to subsidize the basic service and Head Start funds to subsidize ancillary services. Additional funds that appear on the balance sheet and can improve the bottom line include 1) Child Care and Adult Food Program administered by the U.S. Department of Education and funded by the U.S. Department of Agriculture to reimburse meals and snacks, 2) Head Start's Family Day Care Food and Summer Food program, which is the child care version of the National School Lunch Program, 3) Head Start Transportation allowances, and 4) other enhancements for special needs, the homeless, migrant workers, staff compensation or development. In addition, some programs also enroll full-fee families whose fees partially subsidize many overall program costs.

1. Head Start and Early Head Start Program Funds (HS or EHS)

   Debt service and rental payments are eligible uses for HS or EHS Program Funds. Since HS and EHS grants are negotiated individually, payment amounts vary significantly (e.g., $4,000 per year per child to $9,000 per year per child). A HS Grantee may independently determine how much debt their budget can support. A HS Delegate must seek approval from their Grantee as part of the 1309.1 application for One-Time Funds. Grantees seek approval from the Regional Office for their own and their Delegates' applications. The amount of rental payment depends largely upon the size of the program, the payment amount, and the ancillary HS or EHS services funded in addition to the base payment amount.

2. Alternative Payment vouchers

   AP vouchers have a very limited ability to support debt or be relied upon for rental payments, because 1) the vouchers are not contractually obligated for any set period of time to a child care provider, 2) the term of the vouchers is one year at best, and 3) the amount of subsidy per child can be low.

   CDE contracts with AP Agencies, e.g., Resource and Referral Agencies, other nonprofits, or departments of county government, in every county throughout the state to administer the program. Like Section 8 vouchers for housing, low-income families take these vouchers to any provider and the AP agency reimburses the child care provider at the same market rates charged to nonsubsidized families with children of the same age group who are cared for by the provider for a similar block of time, up to a ceiling. The ceiling is set by a state-sponsored study called the "Regional Market Rate Survey of California Child Care Providers" (RMR). For example, Alameda County market rates range between $75 and $200 per week, averaging $150 per week. Additionally, parents may choose to pay an additional amount without restriction for child care out of their own funds.

Some counties have contracted directly with providers for a specific number of AP spaces, but there has been some question of the legality of this practice since the voucher program was designed to create choice for low-income families. This practice could create an opportunity for supporting debt in the future or at least to provide some comfort that rental payments can be made.

The AP Program consists of a blend of federal, state, and county funds. Federal AP funds cannot be used for acquisition of sites or buildings.

3. Center-based contracts

   Center-based contracts have a very limited ability to support debt or be relied upon for rental payments. This is primarily due to the low level of subsidy per child that typically does not cover the cost of care. Center-based contract payments are typically lower than AP reimbursement rates per child. The 2006 "standard reimbursement rate" (SSR) paid to a center-based program is $32.89 per day per child for full time care for preschool child (age 3 and older).[45] The 2006 rate or "reimbursement ceiling" paid for subsidized child care which is provided through an alternative payment agency varies by county. For example, the 2006 rate for Alameda County is $50.81 and for Merced County is $37.83.[46] Additionally, providers with contracts must earn their payments based on the number of days a child is in the program. The larger the center with primarily Center-based contracts, the more likely that the center can support debt or make rental payments. For example, a number of providers have found that a center with a Center-based contract, needs 48 to 64 child spaces in order to be able to support any debt or make minimal rental payments.

The Head Start and Center-based contract funds also have modest capital pools available for new facilities development, which are described in the Capital Sources: Term Sheets section of this chapter.

RECOURSE CONSIDERATIONS

If the developer is required by a lender or public agency to provide child care services in the property for a specific term as a condition of funding, the developer may want to structure the relationship with the provider so that the developer's default and/or compliance risk is mitigated.

- Low Income Housing Tax Credit Program
  - A developer who has committed child care services as a resident service and has been awarded points for providing this service is required to provide the service for ten (10) years; compliance will be monitored by the California Tax Credit Allocation Committee (CTCAC). While CTCAC will allow the substitution of alternate services in unique circumstances, it has been challenging to acquire approval for this substitution.
  - If the developer has included the cost of constructing the child care facilities in tax credit basis as a "community facility," the developer is required to retain the space as a community-serving facility. The requirements under this designation are described in more detail in the CTCAC term sheet towards the end of this chapter.

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[45] http://www.cde.ca.gov/ls/cg/pp/documents/formi2.pdf. The location of this form changes each year. A search on the California Department of Education website for the "standard reimbursement rate" is an alternative method for finding the rate should the location change in the future.

[46] http://www.cde.ca.gov/fg/aa/cd/ap/index.aspx. This website contains an index by county of the rates for subsidized child care which is provided though an alternative payment agency. A search for the "reimbursement ceilings for subsidized child care" is an alternative method for finding the rate should the location change in the future.

- Loans and Grants
  - A developer who is the borrower or guarantor of a recourse loan for the construction of the child care improvements has assumed a true financial obligation on behalf of the provider. Larger lenders and/or the tax credit investor for the housing development may not allow the developer to provide the property as collateral for a comparably small child care improvement loan. Frequently, the child care improvements are owned outside of the tax credit partnership because of this issue or the developer is the guarantor of the loan outside of the tax credit partnership.
  - If the developer is the grantee for a grant that is non-recourse as long as the center continues to be operated as a child care facility, then the developer may have more leeway to negotiate with the foundation or community development financial institution for time to find a replacement provider. However, the developer has taken on a similar position to a borrower of a loan on behalf of the child care provider since the grant can become a recourse loan if child care services are not offered for the term of the requirement.

Recommendations: 1) ensure that there is adequate noticing time from the provider in the Termination provision of the Services or Lease Agreement to allow for transition to a replacement provider (as described in the Partnering with the Provider: Legal Agreements chapter), 2) have the provider as "borrower" for other sources of financing for the child care center, and/or 3) include some financial recourse to the provider as collateral.

Other Discretionary Funds

Other funds that have been used for child care facilities development include:

1. Proposition 10 Commission Facilities funds (First 5)
2. Redevelopment Agency Tax Increment funds
3. Local government funds for child care facilities development
4. Conventional loans & Community Development Financial Institution loans
5. Transportation funds for transit-oriented development
6. Private foundations

1. PROPOSITION 10 COMMISSION FACILITIES FUNDS (FIRST 5)

- California Voters approved Proposition 10 in the November 1998 election, resulting in a $0.50 tax per pack of cigarettes and comparable tobacco products, to be used to create the California Children and Families Commission as well as a comprehensive and integrated system of information and services to promote early childhood development and school readiness. Further information on Proposition 10 is available at http://www.ccfc.ca.gov/prop10facts.htm.
- Eighty percent of the projected $700 million annually is allocated to a community trust fund established by each county commission. Allocations are based on the number of births, according to the mother's county of residence.

- The availability of these funds for center development differs from county to county, according to the county commission's strategic plan. In some counties, either out of the commission's own priority setting or lobbying a pot of funds has been created for child care facilities development. If available, funds tend to be a small amount but can be valuable for gap funding. Many counties' strategic plans are available on the Web. Contact your county's commission to determine if funds are available for development.
- A list of county commissions is available at http://www.ccfc.ca.gov/countyinfo.htm and in the Appendix.

2. REDEVELOPMENT AGENCY TAX INCREMENT FUNDS

- Both Redevelopment funds set aside for affordable housing development and general tax increment funds have been used for child care facilities development.
- Requirements differ significantly locally. Payment of State prevailing wage may be required by the local Redevelopment Agency. The child care center would need to be in a redevelopment area if the project is using tax increment financing. The center would not need to be in the project area if the source is land sales proceeds or if the center is ancillary to housing and is using funds from the low-moderate income housing set-aside.
- The main challenge to accessing the housing set aside funds is that some redevelopment agencies and city councils consider child care facilities an ineligible use.
- The main challenge to accessing the general tax increment funds is that cities tend to protect these funds, and they may be allocated years in advance.

3. LOCAL GOVERNMENT FUNDS FOR CHILD CARE FACILITIES DEVELOPMENT

- Some cities, such as San Francisco, have set aside significant child care facilities funds. Check with the city child care coordinator or the local planning council or resource and referral agency for information.
- Some cities impose a child care impact fee to large housing and/or commercial developments.

4. CONVENTIONAL LOANS

- To finance the development of child care centers, banks occasionally have made construction loans to developers and permanent loans to providers. Whether a bank will originate the loan and the competitiveness of the terms will depend on their underwriting criteria, their need for Community Reinvestment Act credits, and their relationship with the borrower. An affordable housing developer can lend credibility to a provider with the bank. Some providers have accessed conventional debt through the relationship they have with their local bank.
- Typically the bank will want a security interest in terms of the land and the building. Additionally, the bank may require a guarantee. The Packard Foundation has a guarantee program for 50% of the construction and permanent loan for child care center development.
- Example: In recent years, the Bank of America has made two loans to finance child care center development. The Bank made a $2 million construction loan to a developer for a twelve-month term at an 80% Loan to Value and a $1 million permanent fully amortizing loan to the provider for a twenty-year term with a required 1.25 debt service coverage ratio at 75% Loan to Value.

5. COMMUNITY DEVELOPMENT FINANCIAL INSTITUTION LOANS (CDFI)

- CDFIs will frequently make loans that are considered too risky for a traditional bank. Contact the CDFIs in your area to determine if they will consider a loan for child care center development. The Low Income Investment Fund (LIIF), described earlier, is a CDFI.

6. TRANSPORTATION FUNDS FOR TRANSIT-ORIENTED DEVELOPMENT

- Federal Transit Administration Grant (FTA)
  - Administered federally by the U.S. Department of Transportation.
  - Funding is appropriated on the basis of legislative formulas or discretionary authority.
  - The recipient is a public entity with legal authority to receive and dispense federal funds designated by the governor, local officials, or publicly owned operator of transit services.
  - The recipient may grant the funds to projects, which are considered transportation improvements under the FTA's definition of eligible purposes.
  - Talk with the local transportation authority that you are working with about fund availability.
- Intermodal Surface Transportation Efficiency Act (ISTEA)
  - Administered by the U.S. Department of Transportation.
  - Reauthorization expired in February 2004. Congress has rescheduled reauthorization consideration for ISTEA (TEA-21) multiple times.
  - Projects should address safety, continued growth of traffic and travel, and its attendant congestion, environmental concerns, and demographic changes.[47]
- Metropolitan Transportation Commission (MTC)
  - The Transportation for Livable Communities' Capital Grants can be used to finance transit villages, including child care centers. Grants range from $150,000 to $2 million per project.
  - The Transportation for Livable Communities' Housing Incentive Program (HIP) can be used to finance affordable housing one-third mile from a major transit station or transit corridor. Projects must be a minimum density of 25 units per acre.
  - Check http://www.mtc.ca.gov/ for funding opportunities, then select Planning, then Smart Growth, then Transportation for Livable Communities (TLC).

[47] ISTEA Reauthorization Policy Statement and Principles.

7. PRIVATE FOUNDATIONS

- There are several avenues for gathering financial support and grants:
  - Foundations
  - Corporations
  - Events
- Due to the provider-based nature of grants for child care services, these funds are not often available to the developer for facilities development and must be applied for by the provider. For this reason, the provider is an excellent source of information in terms of up-to-date priorities of foundations and corporations in terms of child care facilities.
- Some foundations choose to fund only high-profile projects with prominent media coverage in their geographical areas of focus.
- Most of these sources are relatively small, best serving as funds for gap financing.
- A listing of foundations that make applicable grants is available at the Building Child Care in California website: http://www.buildingchildcare.org. However, the website does not have information on projects for which grants have been made. Providers usually have more up-to-date and insider information on foundation sources.

Term Sheets for Capital Sources

The pages that follow present a series of term sheets for common capital sources. These term sheets are provided in order to provide a general overview of these sources and considerations when using them for child care facilities development with affordable housing. The information contained in these term sheets should not be relied upon; refer to the administrator of the funds directly for up-to-date terms and considerations.

Public Capital Source Term Sheet

NAME OF SOURCE: COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

SUMMARY/OVERVIEW/BACKGROUND:

CDBG provides metropolitan cities and counties with annual direct grants that they can use to revitalize neighborhoods, expand affordable housing and economic opportunities, and/or improve community facilities and services. HUD's Office of Community Planning and Development administers the CDBG program and provides annual grants on a formula basis to many different types of grantees through several programs. Applicable programs include Entitlement Communities and State Administered CDBG. In the Entitlement Communities program, annual appropriations are split between and are managed by entitled cities and counties. In the State Administered CDBG, participating states award funds to units of general local government in accordance to the State's annual funding priorities and criteria. Seventy percent (70%) of funds per year must be used to benefit low- and moderate-income people. Additional information on the CDBG programs is available at http://www.hud.gov/offices/cpd/communitydevelopment/programs/index.cfm. The Code of Federal Regulations, Title 24, Volume 3 governs CDBG funds can be found at http://www.access.gpo.gov/nara/cfr/waisidx_04/24cfr570_04.html. Additional information on the State CDBG Program is available at http://housing.hcd.ca.gov/fa/cdbg/GenNatAmCol.html.

Administrator: City or County or State, whichever is appropriate for your development location. Every administrator has its own application and funding priorities with opportunities for input through a public hearing process.

Type of Financing: Can be structured as a Loan or a Grant

Who is Eligible to Use the Funds: Nonprofit developer or Provider for eligible activities. The developer does not need to be a Community Based Development Organization (CBDO) in order to utilize CDBG funds for construction costs.

Possible Structures: Nonprofit developer or provider may access funds from the City or County as a subrecipient.

How to Apply: Apply through the Administrator.

Basic Use Restrictions: The types of eligible activities that may be funded by the CDBG differs for entitlement and non-entitlement communities per the Code of Federal Regulations, Title 24, Volume 3. Child care facilities development has in practice largely been interpreted as an eligible activity under a different category (Public facilities and improvements) from affordable housing. CDBG funds may be used for child care facilities development as a basic eligible activity under the rubric of public facilities and improvements in entitlement and non-entitlement communities (Code of Federal Regulations, Title 24, Volume 3, 570.201 c) and under the rubric of housing new construction in non-entitlement cities and counties.

Public facilities and improvements. Acquisition, construction, or installation of public facilities and improvements. Current legal advice is that the funds may not be used for predevelopment or take out financing. Design features and improvements that promote energy efficiency and architectural features that enhance the aesthetic quality of facilities and improvements may be included. In certain cases, nonprofit entities and subrecipients may acquire title to public facilities as long as they are operated for use by the general public during all normal hours of operation. Additional requirements are outlined under the section on underwriting requirements below.

Housing new construction in non-entitlement cities and counties (State Administered CDBG). Construction for "a housing construction project which is assistance to a neighborhood-based nonprofit organization, . . . or nonprofit organization serving the development needs of a community in a non-entitlement area" (Section 105(a)(15) of Title 1 of the HCD Act of 1974).

TERMS AND CONDITIONS:

Minimum/Maximum Amounts (if any):	Not applicable.
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	By locality if structured as a loan.
Regulatory Term:	By locality.
Repayment Terms:	By locality. (Depends on if utilizing funds as an eligible activity under housing or public facilities and improvements)
Guarantees:	Generally not applicable.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability:
   At least 51% of the children served must come from low-income households. Low-income means 80% of area median income or below.
2. Underwriting requirements:

   Public Facilities and Improvements (570.200 b)

   a. Facilities containing both eligible and ineligible uses. A public facility in a multipurpose building is eligible for assistance under the CDBG program if:

      1. The facility, which is otherwise eligible and proposed for assistance as a public facility, will occupy a designated and discrete area within the larger facility; and
      2. Costs attributable to the facility proposed for assistance must be accounted for separately and distinct from the overall costs of the multiple-use building and/or facility. Allowable costs are limited to those attributable to the eligible portion of the building or facility.

b. Reasonable fees for use of facilities. Reasonable fees may be charged for the use of the facilities assisted with CDBG funds, but charges such as excessive membership fees, which will have the effect of precluding low- and moderate-income persons from using the facilities, are not permitted.

3. Prevailing wage or Davis Bacon: Davis Bacon wages must be paid for construction. If funds can be used for predevelopment or take out financing, this requirement may no longer apply. Current legal advice is that the funds may not be used for predevelopment or take out financing.
4. Lease or ownership: No requirements.
5. MOU or Services contract: No requirements.
6. Mandated design: No requirements.
7. Reporting: By locality.
8. Other: NEPA requirements.

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

1. CDBG funds require a fairly arduous application, and funds come with significant requirements. Funds should be of a significant amount to warrant the labor required to secure the funds and comply with the requirements.
2. If used for child care facilities development with affordable housing, the requirement that Davis Bacon prevailing wages be paid might be transmitted to the entire development. Developers should seek advice from legal counsel with regard to how best to manage this requirement.

CHALLENGES TO UTILIZING:

In most cities and counties, the application is labor intensive and highly competitive. In rural areas, the funds may be less competitive and administered in a more discretionary manner. Cycles tend to be only once a year and there tends to be a long wait for the award. National Environmental Protection Act clearance is required prior to accessing funds.

Recommended Lenders: Not applicable.

Public Capital Source Term Sheet

NAME OF SOURCE: MHP NONRESIDENTIAL SUPPORTIVE SERVICE SPACE (NSSS)

SUMMARY/OVERVIEW/BACKGROUND:

In 2002 California voters passed a bond measure that resulted in $2.1 billion of funding for the California Department of Housing and Community Development's affordable, supportive, and farm worker housing programs. Almost $1 billion of the $2.1 billion was allocated to the MHP program. At time of printing, nearly all of those funds had been encumbered. The Multifamily Housing Program's recent NOFAs have averaged about $70 million per round. It is unclear at the time of this publication if the program will be renewed. In addition, the California Department of Housing and Community Development has made about $8 million available in each round for Nonresidential Supportive Services Space. NSSS funds provide permanent financing for resident services space, including child care. They are awarded as an addition to MHP General Funds (residential) loans and, as such, are subject to MHP requirements and regulations. Regulations, NOFAs, and applications can be found at http://www.hcd.ca.gov/ca/mhp/.

Type of Financing: Permanent Soft Debt

Who is Eligible to Use the Funds: Affordable housing developers who apply for and are awarded MHP General Funds. A supplemental application for NSSS funds must be submitted with the application for General Funds. General Funds and NSSS funds are issued under the same loan.

Possible Structures: Developer as borrower; Provider as lessee. Rent is allowable for NSS space. If rent is charged, MHP will view the NSS space as commercial space, with a 50% vacancy rate, in operating budgets.

How to Apply: The NSSS application is a compact addition to the MHP General Fund application. MHP General Funds can be awarded without NSSS funds, but NSSS funds can only be awarded to successful MHP applicants.

Basic Use Restrictions: MHP General Fund restrictions apply. MHP NSSS funds provide permanent financing for new construction and rehabilitation of, and conversion to, space for supportive services for MHP project residents. The NSS space must be within, adjacent to, or directly across the street from the residential project. Changes to the use of the space must be approved in writing by the California Department of Housing and Community Development.

NSSS funds cannot be used for supportive services operations. Services must be appropriate for residents, who have priority, but they can be made available to the greater community. Not all of the child care spaces are required to match the income levels of the housing development. MHP loan officers are available for consultation on specific projects. See http://www.hcd.ca.gov/ca/mhp/ for contact information.

FINANCING

TERMS AND CONDITIONS:

Maximum:	The lesser of $25,000 per restricted residential unit or $500,000 *in addition to* MHP General Funds.
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	3%
Regulatory Term:	55 years. Subject to MHP General Funds Regulatory Agreement.
Repayment Terms:	55 years; 0.42% of outstanding principal balance required annually for debt service payment for the first 30 years. Debt service will be adjusted after year 30. After year 55, remaining principal and interest will be forgiven (if in compliance with the MHP Regulatory Agreement).
Guarantees:	MHP General Funds guarantee requirements apply.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability: MHP income and rent restrictions apply.
2. Underwriting requirements: MHP General Funds requirements apply. Applicant must demonstrate control of the NSSS site.
3. Prevailing wage.
4. Lease or ownership: Developer-owned or long term–leased (90 years; 65 if lessor is a public entity). Providers may lease space from developer.
5. MOU or services contract: Required if provider is leasing the space. If the provider will not lease the space, no MOU is required.
6. Mandated design: No design requirements by lender.
7. Reporting: MHP reporting requirements apply.
8. Other:
   a. At time of application, developer must indicate whether or not the space will be built if NSSS funds are not received.
   b. An interim financing source is needed to bridge the construction period since the MHP funds are a permanent source.

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

CHALLENGES TO UTILIZING:

Since NSSS funds are accessible only in conjunction with MHP funds, they will be increasingly difficult to access as MHP funds become more competitive or are exhausted. At the time of publication, it is unclear if this program will be available in the future.

Recommended Lenders: The State Department of Housing and Community Development is the sole provider of MHP NSSS money.

Public Capital Source Term Sheet

NAME OF SOURCE: HEAD START ONE-TIME SUPPLEMENTAL FUNDS

SUMMARY/OVERVIEW/BACKGROUND:

Head Start One-Time Supplemental Funds, also referred to as Facilities Funds or Quality Funds, are awarded as one-time grants from recaptured program monies. Each year, Head Start programs that are under-subscribed must return the excess program funds to the Regional Head Start Office, which then redistributes them to Head Start and Early Head Start Grantees for capital uses. Head Start One-Time Funds prioritize expenditures that maintain or prevent disruption of service to children, such as replacing a lost facility. The Code of Federal Regulations, Title 45, Subtitle B, Chapter XIII, Part 1309 details the regulations and application requirements for Head Start One Time Funds (http://www.acf.hhs.gov/programs/hsb/performance). Since Congressional approval in 1987, One-Time Funds can be used to purchase land and/or a facility.

Type of Financing: Grant

Who is Eligible to Use the Funds: Head Start Grantees. Head Start Delegates must apply through their grantee.

Possible Structures: Grantee receives funds. Grantees either use funds themselves or administer funds to a delegate.

How to Apply: The regulations and application requirements are listed in the Code of Federal Regulations, Title 45, Subtitle B, Chapter XIII, Part 1309.1, which can be found at http://www.headstartinfo.org/pdf/1309.PDF.

Applications are due annually to the Region IX Office. Program providers should initiate discussions about their application with the Regional Office as soon as possible.

Basic Use Restrictions: Funds can be used for "major renovations," including tenant improvements, the purchase of a facility, equipment, transportation needs, and program improvements. Grantees must indicate how they intend to use the funds when applying for the grant. In some cases, a Grantee may be permitted to use the funds in alternate ways after the grant has been approved. The purchase of modular units is an acceptable use but requires additional documentation, listed in the Code of Federal Regulations, Title 45, Subtitle B, Chapter XIII, Part 1309.3. Head Start New Facility Funds cover the purchase or construction of a new center related to program expansion (not program relocation) and are applied for separately from the National Head Start Office.

TERMS AND CONDITIONS:

Maximum:	Capped at 25% of total project costs. Region IX gives the guideline of 20% of costs but has historically been flexible. Shell and equipment can be included in total project budget. Funds must also meet the 15% limit on administrative costs. See narrative for details.
Minimum:	At least $200,000 or 25% of the annual direct, approved costs of the Grantee
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	Not applicable.
Regulatory Term:	For the term of the contract.
Repayment Terms:	If the Grantee gives up or loses their Head Start Contract, they must either repay the Head Start One-Time Funds or turn the facility over to Head Start.
Guarantees:	Not applicable.
Limits on amount that can go towards debt service or rental payments:	Subject to approval.

FINANCING

REQUIREMENTS:

1. Affordability: Head Start income levels apply.
2. Underwriting requirements: The Federal Government has an interest in all One-Time Funds work and purchases. This must be recorded as a Notice of Federal Interest. Federal interest can be subordinated to the project lender. The Code of Federal Regulations, Title 45, Subtitle B, Chapter XIII, Part 1309.1 lists the specific requirements related to underwriting included in the application.
3. Davis Bacon wages apply. Head Start funds are federal funds.
4. Lease or ownership acceptable. See Federal Register Title 45, Subtitle B, Chapter XIII, Part 1309.10 for lease requirements. Generally the Region IX Office expects a 15–20 year lease.
5. MOU or Services contract: Grantee must have a Head Start Program contract. Federal Register Title 45, Subtitle B, Chapter XIII, Part 1309.1 does not require a services agreement or MOU between the developer and provider. It does, however, require evidence of a long-term lease. An MOU may be submitted in addition to a lease, or, in some cases when a lease has not yet been executed, in place of a lease. Acceptance of an MOU instead of a lease is at the discretion of the Regional Office.
6. Mandated design: Must meet Head Start design requirements.
7. Reporting: No reporting is required during construction. A report must be filed at completion of the project, and the Regional Office may do a site visit. Accounting must carefully track how the One-Time Funds are used. The One-Time Funds acts as a mini-grant within the Grantee's overall budget, and its accounting and timeline must be included in the Grantee's annual report.
8. Other

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

Head Start funds are federal funds. As such, the Low Income Housing Tax Credit eligible basis must be reduced if Head Start funds are used for shell construction, or for build-out costs included in the housing project contract, if the project is not owned by the provider. If used for tenant-owned tenant improvements, under separate contract, they may not need to be subtracted out of tax credit basis. Keep in mind that Head Start Funds trigger Davis Bacon requirements, so they may be best used for tenant improvements if the entire project does not already have Davis Bacon requirements. Seek legal advice on this matter for your specific project.

CHALLENGES TO UTILIZING:

Competitive, and political. The application process is extensive, and the amount of funds and distribution of funds can be unpredictable. There is an annual, floating deadline, usually in late spring or the summer, which is set in early spring, shortly before the deadline. Grantees who are able to leverage other sources and have a good relationship with the Regional Office will be more likely to succeed.

Recommended Lenders: Available only through Head Start Regional Offices.

Private Capital Source Term Sheet

NAME OF SOURCE: THE AFFORDABLE BUILDINGS FOR CHILDREN'S DEVELOPMENT FUND (ABCD)

SUMMARY/OVERVIEW/BACKGROUND:

The ABCD Fund is the financing component of the ABCD Initiative, a program that provides a system of capital delivery for California child care centers. The ABCD Fund offers a continuum of three financial products for providers, taking into account today's current environment yet building toward an ultimate goal of an efficient delivery system of capital for the child care sector. Products include: planning grants, predevelopment loans, and flexible loans for acquisition, construction, and permanent uses. The ABCD Fund enables child care centers in California to meet the costs of facilities development and assists them with their long-term real estate financing needs. The ABCD Fund also provides technical assistance during each phase of the development process, helping borrowers navigate the financing market and providing referrals to facilities development resources. LIIF officially launched the ABCD Fund in January 2003. As of 2005, it committed 16 loans totaling $6.9 million from the Fund and 20 planning grants for $371,500. This financing will support over 2,710 quality child care spaces. The Packard Foundation has already committed $14.5 million to LIIF in grants and Program Related Investments to launch the Fund. An encouraging number of foundations and financial institutions have also expressed interest and in some cases made preliminary commitments to invest in the ABCD Fund. In total, the ABCD Fund envisions assembling $30–$40 million in a combination of private capital and philanthropic investments to finance nearly 10,000 spaces of child care in California over ten years.

Administrator: Low Income Investment Fund (formerly the Low Income Housing Fund)
100 Pine St., Suite 1800, San Francisco, CA 94111
415-772-9094
http://www.liifund.org

Type of Financing:
1. Planning Grant
2. Predevelopment, Acquisition, Construction, & Permanent Loans

Who is Eligible to Use the Funds: Developer or Provider with projects that will provide child care services within the state of California. Information is needed from both Developer and Provider.

Possible Structures: Flexible. Developer or Provider may be borrower.

How to Apply: Contact the ABCD Fund. Contact information available at http://www.liifund.org/. Select Program Areas, Child care, Loans or Grants.

Basic Use Restrictions: ABCD funds must be used for the development or preservation of child care facilities. Eligible costs are indicated under each grant or loan product type below.

1. PLANNING GRANT

TERMS AND CONDITIONS:

Minimum/Maximum Amounts (if any):	$10,000/$20,000
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	Not applicable.
Regulatory Term:	Not applicable.
Repayment Terms:	No repayment.
Guarantees:	Not applicable.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability: Grant must be used to develop new or preserve existing child care spaces serving at least 20% low-income households at or below 80% of Area Median Income.
2. Underwriting requirements:

   The grant review will evaluate:
   —an applicant's organizational capacity;
   —the long-term viability of the proposed project;
   —ability to obtain additional financing for the proposed project;
   —the borrower's financial position and track record.
3. Prevailing wage or Davis Bacon: Not required.
4. Lease or ownership: Both OK.
5. MOU or Services contract: MOU or Services agreement with provider or developer, whichever applicable, required.
6. Mandated design: No requirements.
7. Reporting: Use of Funds reports are due when the funds have been spent and a one-time final report.
8. Other:
   a. Eligible costs—Early stage project feasibility analysis. Grants may be used to cover expenses such as:
      - Architectural and development consulting services
      - Engineering analyses and other third party work to determine project feasibility and/or to develop proforma budgets and financing plans

   b. Match—The applicant must match some or all of the requested grant amount with funds from their own or other sources. The match requirement may be met by the applicant's allocation of staff resources committed to the project.

2. PREDEVELOPMENT LOANS

TERMS AND CONDITIONS:

Minimum/Maximum Amounts (if any):	$100,000 maximum
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	3% deferred interest
Fees:	Origination Fee: $2,000, plus $375 legal and closing fee. Fees may be financed from the loan.
Regulatory Term:	Not applicable.
Repayment Terms:	Up to 3 years. Principal plus accrued interest is due in full at maturity.
Guarantees/Collateral:	Unsecured with recourse to Borrower. The Borrower is fully responsible for repayment of the loan, even if the project does not go forward.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability: Serve at least 20% low-income households at or below 80% of Area Median Income.
2. Underwriting requirements: Underwriting requirements are similar to traditional lenders, but more consideration is given to the reputation of the borrower. Readiness to proceed is critical to a successful grant or loan application.
3. Prevailing wage or Davis Bacon: Not required.
4. Lease or ownership: Both OK.
5. MOU or Services contract: MOU or Services agreement with provider or developer, whichever applicable, required.
6. Mandated design: No requirements.
7. Reporting: Ongoing project progress reports are due for the term of the loan.
8. Other: Eligible costs—Typical predevelopment costs, including Phase I and II environmental assessment, inspections, architectural and consultant services, permits, loan and legal fees, as well as acquisition costs in some cases.

3. INTEREST-ONLY LOANS

TERMS AND CONDITIONS:

Minimum/Maximum Amounts (if any):	$1 million maximum based on the borrower and project's ability to repay.
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	6%–8%, nonamortizing
Fees:	Origination Fee: Up to 2% of loan amount. Borrower is responsible for legal costs, appraisal, environmental report, etc. Fees may be financed from the loan.
LTV:	Up to 90% if secured by real estate.
Regulatory Term:	Not applicable.
Repayment Terms:	Up to two years, considered interim loans while a project seeks permanent financing. Interest only during term, full principal repayment at loan maturity.
Guarantees/Collateral:	Loan guarantee may be required in some cases. Real estate, pledges, assignment of construction-related collateral, assignment of specific repayment sources, etc. Unsecured loans will be considered.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability: Serve at least 20% low-income households at or below 80% of Area Median Income.
2. Underwriting requirements: Requirements are similar to those of traditional lenders, but more consideration is given to the reputation of the mortgagee. Readiness to proceed is critical to a successful grant or loan application.
3. Prevailing wage or Davis Bacon: Not required.
4. Lease or ownership: Both OK.
5. MOU or Services contract: MOU or Services agreement required.
6. Mandated design: No requirements.
7. Reporting: Ongoing project progress reports are due for the term of the loan. The frequency of reporting depends on the type of loan.

8. Other:
   a. Eligible costs—Acquisition, construction, renovation, and bridge financing.
   b. Submit property appraisal, Phase I environmental report, property evaluation, and/or construction inspections.
   c. Conditions of financing may include
      - phased disbursement of the loan
      - pledge of identified repayment sources
      - periodic project, organization and financial reporting
      - provision of updated development budget
      - limits on additional borrowing
      - other covenants appropriate for the transaction

4. AMORTIZING LOANS

TERMS AND CONDITIONS:

Minimum/Maximum Amounts (if any):	$1 million maximum.
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	Average interest rate of 5.5%.
Fees:	Origination Fee: up to 2% of loan amount. Borrower is responsible for legal costs, appraisal, environmental report, etc. Fees may be financed from the loan.
LTV:	Up to 90% if secured by real estate, may be lower for land acquisition.
DSCR:	Will vary by project, but typically 1.15:1.00 net of replacement reserves.
Regulatory Term:	Not applicable.
Repayment Terms:	Up to 10 years, with up to 40-year amortization. Repayment terms will be based on the ability of the borrower to repay the loan.
Guarantees/Collateral:	Loan guarantee may be required in some cases. Real estate, pledges, assignment of construction-related collateral, assignment of specific repayment sources, etc. Unsecured loans will be considered.
Limits on amount that can go towards debt service or rental payments:	Not applicable. Subordination negotiable.

REQUIREMENTS:

1. Affordability: Serve at least 20% low-income households.
2. Underwriting requirements: Requirements are similar to those of traditional lenders, but more consideration is given to the reputation of the mortgagee. Readiness to proceed is critical to a successful grant or loan application.
3. Prevailing wage or Davis Bacon: Not required.
4. Lease or ownership: Both OK.
5. MOU or Services contract: MOU or Services agreement required.
6. Mandated design: No requirements.
7. Reporting: Annual project and borrower reporting.
8. Other:
    a. Eligible costs—Refinancing of existing debt and other permanent financing. Conditions of financing may include:
        1. Phased disbursement of the loan
        2. Pledge of identified repayment sources
        3. Periodic project, organization and financial reporting
        4. Provision of updated development budget
        5. Limits on additional borrowing
        6. Other covenants appropriate for the transaction

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

No conflicts.

CHALLENGES TO UTILIZING:

1. Meeting project readiness criteria for loans may be challenging for some providers.
2. Fewer planning-grant funds available outside of the San Francisco Bay Area.

Recommended Lenders: Not applicable.

Private Capital Sources Term Sheet

NAME OF SOURCE: NONPROFIT SPACE CAPITAL FUND— SAN FRANCISCO/ALAMEDA COUNTY PROGRAMS

SUMMARY/OVERVIEW/BACKGROUND:

Provides technical assistance, planning and capital grants to San Francisco- and Alameda-based nonprofits seeking to establish new permanently affordable nonprofit office or program space through capital expansion projects or the acquisition or long-term leasing of real estate. Preference is given to projects providing co-location opportunities to other nonprofits.

The Fund provides a portion of the equity needed. Applicants are expected to leverage these grants with other resources. The 2005 round of funding is made possible by a matching grant from the Evelyn & Walter Haas, Jr. Fund for the contributions received from The William and Flora Hewlett Foundation.

Since its inception, the Nonprofit Space Capital Fund has awarded 22 capital grants totaling over $3 million. Nine of these grants, totaling nearly $800,000 have been awarded to developers to fund community or nonprofit spaces.

Although this term sheet focuses on the capital grants, there are planning grants available for costs that might be incurred before buying, renovating, or building property, from feasibility studies and appraisals to environmental testing.

Administrator: Northern California Community Loan Fund (NCCLF)
870 Market Street, Suite 677
San Francisco, CA 94102
phone: (415) 392-8215
http://www.ncclf.org/
Contact: Sarah Abbe Taylor, Program Associate
Joshua Simon, Director of Consulting & Grants Program

Type of Financing: Grant

Who is Eligible to Use the Funds: Incorporated 501(c)(3) in good standing, or a sponsored project of a tax-exempt corporation that is operating for purposes consistent with Section 501(c)(3) status. Entity must demonstrate financial stability, technical capacity, experience, and ability to significantly leverage NCCLF's contribution with additional financing. Entity must also be located and serve citizens in San Francisco or Alameda Counties.

Possible Structures: Owner (developer) of property as grantee, and subsequently lease space to non-profit.

Basic Use Restrictions:

- Funds can be used only to fund the permanently affordable nonprofit office or program space component of proposed project.
- Project must provide affordable nonprofit space for at least fifty-five (55) years.
- Preference will be given to projects that result in co-location by nonprofits working in partnership with other community projects. In the case of co-locaton, 51% of the space must be used by nonprofit organizations.
- Preference will be given to projects that provide benefits to the neighborhood in which they are located.
- Preference given to projects that guarantee affordability beyond 55 years.

TERMS AND CONDITIONS:

Maximum Amounts (if any):	15% of the nonprofit space component of total project costs OR $500,000 per project, whichever is less. Most grants are between $50,000 and $100,000.
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	Not applicable.
Regulatory Term:	55 years
Repayment Terms:	This is a revocable grant if the affordability requirement is not met, or if the space is no longer used by a non-profit. The grant is secured by a Deed of Trust (or equivalent). If the nonprofit moves to another space, the nonprofit may take the grant with them or repay the grant. A new nonprofit utilizing the space may also take over the grant.
Guarantees:	All capital grants must be secured by a Deed of Trust, or other acceptable alternative instrument, to guarantee compliance with grant terms and conditions. In the case of funding projects on leased property, the grantee must record a Leasehold Deed of Trust and show evidence of a recorded lease. The Deed of Trust is typically subordinated to all other sources.
Limits on amount that can go towards debt service or rental payments:	Grant funds cannot be used for payment of back taxes, penalties, late charges, interest on late payments, or the repayment of existing loans.

REQUIREMENTS:

1. Affordability: No specific definitions of what constitutes affordability, however 51% of space must be used by nonprofits.
2. Underwriting requirements: NCCLF will evaluate both the project itself, and the experience, financial stability, and capacity of the entity executing the project.
3. Prevailing wage or Davis Bacon: None.
4. Lease or ownership: Most projects are expected to be ownership projects; however, if funds are used for capital improvements to leased space, the term of the lease will be considered in determining amount of grant. Minimum lease requirement is 55 years, and the longer the lease term, the larger the potential grant.
5. MOU or Services contract There are no restrictions on an owner/grantee leasing the space to a nonprofit.
6. Mandated design None.
7. Reporting:
   At project completion: Certificate of Occupancy and documentation that there are no mechanic liens on the property.
   For operations: Annual financial statements and statement that at least 51% of space is occupied by nonprofits.
8. Other: None.

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

1. For a project financed with tax credits, the General Partner may be the grantee and characterize the grant as a capital contribution to the project. However, the partnership (owner) must secure the General Partner's obligation through a Deed of Trust.
2. May be included in basis since no federal funds are used through the fund.

CHALLENGES TO UTILIZING

Source—The fund does not have a perennial source and requires fund raising for each round. The fact that this fund was started in 2001 in response to Bay Area rents driving out many local nonprofits and that office rents have since declined, has led many funders to perceive a lesser need for this grant program. As of January 2006, the fund had no funds available. NCCLF recommends that nonprofits check their websites for a updates at http://www.ncclf.org/nscf_sub.html?Id=236.

Highly Competitive—The application process starts with a letter of inquiry (LOI) which is reviewed by NCCLF program staff, who contact the applicant. If the project looks feasible and is within the program guidelines, the applicant will be asked to submit a formal application. In the December 2005 round, 15% of applicants who sent an LOI were asked to submit an application and are eligible for funding.

Recommended Lenders: Not applicable.

Private/Public Capital Sources Term Sheet

NAME OF SOURCE: LOW INCOME HOUSING TAX CREDIT PROGRAM (LIHTC)

SUMMARY/OVERVIEW/BACKGROUND:

Congress authorized the Federal Low Income Housing Tax Credit Program in 1986. The program is structured to raise project equity for affordable rental housing through the "sale" of tax benefits to investors. The LIHTC program, contained in Section 42 of the Internal Revenue Code, has become the primary source of financing for affordable rental housing. Each year, the amount of annual housing credit ceiling is set on a per-state-resident basis. Additionally, states may qualify for a prorated share of credits available annually in a national pool comprised of unused credits. Credits are allocated through a competitive point-based application, which is designed to award higher scores to projects that match the state's housing priorities and is based on assessment of eligible project costs. In terms of federal credits, the housing sponsor has available ten times the annual allocation amount, since investors can take the annual credit each year for a ten-year period. In terms of state credits, the full four-year state credit allocated to a project is deducted from the annual state credit ceiling.

Administrator: The IRS administers the federal LIHTC program. In California, responsibility for administering the federal tax credit program was assigned to the California Tax Credit Allocation Committee (CTCAC). Additionally, CTCAC administers a state low income housing tax credit program that supplements the federal tax credit program.

Type of Financing: Private equity leveraged by federal and/or state tax credits.

Who is Eligible to Use the Funds: Developer through a partnership entity comprised of an investor as limited partner and a developer as managing general partner. Developer secures an allocation of LIHTC to finance an affordable housing development and selects a tax credit investor as the equity partner. Can only be used in conjunction with an affordable housing development.

Possible Structures:

1. Developer utilizes LIHTC for development of child care facility as a community service facility, or
2. Developer utilizes LIHTC for development costs associated with the shell of the child care facility if housing units above are structurally supported by the shell.

How to Apply: Submit an application to CTCAC during one of the application rounds. Confer with a tax attorney for an opinion on the basis eligibility of child care facility development costs. Utilize the written opinion and IRS ruling 2003-77 to ensure auditors recognize the child care facility costs as basis eligible. Application and regulations are available at http://www.treasurer.ca.gov/ctcac/ctcac.htm. The IRS ruling can be accessed from the IRS website at http://www.irs.gov/irb/2003-29_IRB/ar05.html.

Basic Use Restrictions: Eligible project costs.

TERMS AND CONDITIONS:

Maximum Amount:	$2 million in federal credits on an annual basis per project for entire project (2006 regulations).
Amount of Subsidy (per child):	Not applicable.
Interest Rate:	Not applicable.
Regulatory Term:	Child care facility space must remain a community service facility for a minimum of ten years. The space can be converted to another community service use during the ten years with permission from CTCAC.
Repayment Terms:	Tax credits subject to recapture if use is ineligible.
Guarantees:	Probably, depending on the investor. If the child care facility supports debt, investor will likely impose additional guarantee requirements, beyond their standard requirements for the housing, on the developer.
Limits on amount that can go towards debt service or rental payments:	Not applicable.

REQUIREMENTS:

1. Affordability: Refer to Considerations for Using with Affordable Housing, Note 3.
2. Underwriting requirements: Depends on the investor.
3. Prevailing wage or Davis Bacon: At the time of this writing, the current interpretation of Senate Bill 975 by the Department of Industrial Relations is that some projects with LIHTC financing must pay prevailing wage. However, whether a project is subject to prevailing wage depends on the facts of the particular transaction.
4. Lease or ownership: Child care facility will be leased if LIHTC financing is utilized for the space.
5. MOU or services contract: Depends on the investor. Investor will probably require approval rights.
6. Mandated design: Investor usually has approval rights.
7. Reporting: Depends on the investor. Typically nothing beyond the requirements for the housing, unless rental income from a child care facility supports debt.
8. Other: None.

CONSIDERATIONS FOR USING WITH AFFORDABLE HOUSING:

1. If the total project costs exceed the 221(d)(3) limits, no additional funds may be requested for the child care facility.
2. If the housing project costs are below the 221(d)(3) limits, the child care facility costs can increase eligible basis.

3. If including the child care facility costs in basis under the community service facility allowance, the space must be retained as a community service facility for a minimum of ten years. To be considered a community service facility, the facility must be designed to serve primarily individuals whose income is 60% or less of area median income. There has been no clarification of the definition of "primarily." However, it has been opined by some tax attorneys that the term "substantially," which has been clarified to mean 85% or more, is stronger wording than "primarily." The following conditions must be met to satisfy this requirement:
   a. Provide services that improve the quality of life of community residents.
   b. Demonstrate that the services provided at the facility will be appropriate and helpful to individuals in the area of the project whose income is 60% or less of area median income. The required market study or a similar study can be used to demonstrate that this requirement will be met.
   c. Facility must be located on the same tract of land as one of the buildings that comprise the qualified low-income housing project.
   d. Fees must be affordable to individuals whose income is 60% or less of area median income. There is no definition of "affordable."
4. Child care can count as a service amenity if licensed child care services are provided to residents and all TCAC service amenity requirements are met. Child care should only be submitted in the TCAC application as a service amenity if:
   a. The service will be offered for a minimum of ten years, 20 hours or more per week, Monday through Friday.
   b. Child care services are appropriate for the housing population.
   c. The physical space can be available when the development is placed-in-service.
   d. The service is made available within 6-months of the placed-in-service date.
   e. The service will be provided on site unless the project is applying as a Small Development or within ½ mile of the development if providing the service on-site can be shown to be duplicative.

   The applicant must submit contracts with service providers, service provider experience, evidence that the physical space will be provided, and a budget reflecting how the services will be paid for in the application. [Section 10325, 5(B)]

CHALLENGES TO UTILIZING:

1. Beyond Ruling 2003-77, the IRS has not made any rulings on inclusion of child care facilities in eligible basis.
2. Ensuring all tax credit requirements for the child care facility as a community service facility or as a service amenity or as commercial space are met.
3. Ensuring the child care facility is completed at the same time that the affordable housing is placed in service and that the child care provider will offer the service within six months of the placed-in-service date.

Recommended Lenders: Not applicable.