

## Housing Initiative Clinic Briefs

### Hunters View and Certificates of Participation

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This Housing Initiative Clinic Brief summarizes the Hunters View housing project's use of Certificates of Participation and examines the structure, advantages, and disadvantages of Certificates of Participation as an affordable housing financing tool.

#### **The Hunters View Project**

Hunters View (the "Project") is a housing project located in San Francisco. It was originally constructed in 1956 as a 267-unit public housing project but is currently being constructed as a mixed-income community with 800 new housing units, neighborhood retail, community facilities, and parks and playgrounds.<sup>1</sup> Hunters View sits above an old naval shipyard and is less than a mile away from the Third Street commercial corridor and rail line.<sup>2</sup> Hunters View is the first public housing project to be revitalized under San Francisco's HOPE SF Program.<sup>3</sup> Hope SF is a partnership between the San Francisco Housing Authority and the Mayor's Office of Housing. The aim is to revitalize distressed public housing developments.<sup>4</sup>

#### **Hunters View Financing**

The three phases of the Project are expected to cost \$450 million. Hunters View is being financed through affordable housing funds, City investments, funding from the state of California, federal support for capital and operating funds, philanthropic funds, proceeds from

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<sup>1</sup> [http://onesanfrancisco.org/wp-content/uploads/HOPESF\\_COP\\_CPC\\_Memo.pdf](http://onesanfrancisco.org/wp-content/uploads/HOPESF_COP_CPC_Memo.pdf)

<sup>2</sup> <http://hope-sf.org/hunters.php>

<sup>3</sup> <http://huntersview.info>

the sale of market rate homes, and the use of Certificates of Participation (“COPs”).<sup>5</sup> The Project’s use of COPs is the focus of this brief.

### **Certificates of Participation Overview**

Certificates of Participation are used as a financing method for real estate projects including prisons, parks, and office buildings. They are tax-exempt government securities sold to investors. The capital raised from the sale of COPs is used to raise funds for building construction and equipment while the purchasers receive COP payments derived from lease revenues that include tax-exempt interest.

### **The Structure of COPs**

COPs are structured so that ownership of the project being financed is vested in a third-party entity that leases the project back to the public agency conducting the financing.<sup>6</sup> The public agency gets to use or occupy the project while the investors in the COPs receive lease payments. The lease payments are assigned to a trustee who remits the payments to the investors in the COPs. Payments are made to the investors for the duration of the project based on the percentage of share the investor has in the lease agreement. Consequently, the investor does not have to wait for the bond to mature before receiving a return on the investment, which can be the case for general bonds. When the payment schedule to investors is complete, the public agency retains ownership of the project. In the event of default, the investors may be able to assume control and ownership of the project.

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<sup>4</sup> <http://huntersview.info>

<sup>5</sup> [http://onesanfrancisco.org/wp-content/uploads/HOPESF\\_COP\\_CPC\\_Memo.pdf](http://onesanfrancisco.org/wp-content/uploads/HOPESF_COP_CPC_Memo.pdf)

<sup>6</sup> [http://www.oregon.gov/DAS/CFO/docs/capital\\_investment/aboutcops.pdf](http://www.oregon.gov/DAS/CFO/docs/capital_investment/aboutcops.pdf)

## **Certificates of Participation and Hunters View**

In terms of Hunters View, the City of San Francisco is the corresponding public entity. The City will be required to make rental payments during the term of the Project to the trustee who will eventually make payments to the investors.<sup>7</sup> An unidentified non-profit is the assigned trustee. The collateral in this instance are the Mission Police Station and the Bayview Police Station. The collateral secure the repayment obligations in the event of default. Of the expected \$450 million cost of the Project, COPs are expected to contribute \$25 million.

## **Advantages of COPs**

One advantage of financing is that it spreads the capital costs of projects over several years. COPs allow governmental entities to finance projects without issuing long-term debt, which can be viewed as advantageous since the taking on of long-term debt is often subject to voter approval.<sup>8</sup> Because the financing occurs through leases, the agreements do not constitute state indebtedness and are not subject to State constitutional debt limitations or other statutory requirements that can apply to other bonds.<sup>9</sup> COPs are also transferable which makes them a tradable security.

In California, the required voter approval proportion for the government's use of long-term bonds increased from a simple majority to two-thirds.<sup>10</sup> This increase in the necessary approval fraction can be difficult to obtain and makes COPs look even more desirable for those wishing to

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<sup>7</sup> [http://onesanfrancisco.org/wp-content/uploads/HOPESF\\_COP\\_CPC\\_Memo.pdf](http://onesanfrancisco.org/wp-content/uploads/HOPESF_COP_CPC_Memo.pdf)

<sup>8</sup> <http://www.sbcgj.org/2001/2001certpart.htm>

<sup>9</sup> [http://www.oregon.gov/DAS/CFO/docs/capital\\_investment/aboutcops.pdf](http://www.oregon.gov/DAS/CFO/docs/capital_investment/aboutcops.pdf)

finance projects. Illinois has not made heavy use of COPs. This lack of COP usage may be the result of robust statutes that allow for the authorization and issuance of bonds to finance long-term projects. For example, Illinois has the “Build Illinois Bond Act” that authorizes the state of Illinois to issue, sell and provide bonds to finance long-term capital needs for projects that “foste[r] economic development and increased employment”. See 30 ILCS 425.

### **Criticisms of Certificates of Participation**

One criticism of the use of Certificates of Participation is also one of the advantages—their use is not subject to voter approval. Even though COPs are not counted as debt for states, it is important for there to be some type of central management system in place that makes sure that the financings are consistent with approved budgets. Although government-backed securities are typically viewed as safe, there is still a chance of default and it is necessary to take risk exposure into account.

### **The Future of COPs**

COPs will likely continue to be used as an alternative method of financing because they provide benefits for both public agencies and investors. The tax-exempt status of the COPs is favorable for the COP purchasers who benefit from the tax exemption. Projects financed through COPs are not subject to the same voter approval requirements and may mean that the process moves quicker. However, the absence of voter approval may cause concern by reducing oversight. In states like Illinois that have strong allowances for the issuing of bonds to finance long-term projects, it does not seem likely that COPs will be needed as a substitute for other types of bonds.

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<sup>10</sup> <http://www.sbcgj.org/2001/2001certpart.htm>