

Approval Loan Recommendation Summary – BEACHWINDS

Preliminary _____

Firm X

Date: October 7, 2020

1. OVERVIEW AND UPDATE

This Credit Committee request is for Firm Approval of a tax-exempt construction to permanent loan for Beachwinds (the “Development”). Preservation of Affordable Housing, Inc. (“POAH”) is the “Developer”. Preliminary approval of Beachwinds was granted by the Board of Commissioners on March 19, 2020.

A. Overview

This is the refinance of two separate post year-15 low income housing tax credit (“LIHTC”) projects, South Winds and Beachwood, both of which are located in Narragansett and were constructed in 1977. South Winds Apartments contains three buildings and contains 42 one-bedroom units and 6 two-bedroom units. Beachwood Apartments contains one building with three wings linked by common corridors with 52 one-bedroom units and 4 two-bedroom units. In total the Development will have 104 units.

Both Beachwood and South Winds were refinanced in the early 2000’s with financing from Rhode Island Housing and Mortgage Corporation (“RIHousing”). The existing first mortgages for both sites will be paid off as part of this transaction. South Winds also has a Affordable Housing Trust Fund (“AHT”) loan that is payable from surplus cash. The original loan, made in 2001, was for \$1,400,000 and was made because at the time, the highest and best use for the property was as market rate condominiums rather than affordable housing. Payments are required annually in an amount equivalent to 50% of surplus cash (if any) generated by the property. Over the past 15 years the property has made regular payments, but they have not even covered the accrued interest. Staff is recommending that as part of this transaction POAH make a payment of approximately \$900,000 towards the AHT loan paying off 100% of the accrued interest and reducing the principal balance from \$1,400,000 to \$920,000.

When considering the current transaction, POAH weighed a refinance with RIHousing against a loan through the U.S. Housing and Urban Development’s (“HUD”) Multifamily Accelerated Processing (“MAP”) program. Under the MAP program, POAH’s interest rate would have been below 3.5% allowing POAH to leverage considerably more debt and repay the entire AHT loan, however, Beachwinds would no longer be part of RIHousing’s portfolio. POAH is mindful of overleveraging the properties. While the potential post rehab HAP rents are

quite high, they are dependent on HUD granting a waiver. Additionally, POAH recognizes that even if the waiver is granted, with market rent fluctuations, the HAP rents could decrease upon reset. Retaining good loans with strong owners is essential for the RIHousing portfolio and overall long-term financial health of the organization.

Therefore, staff has underwritten the permanent loan to the HAP rents that will be in place at closing which are equal to the current market rents. This does not fully repay the AHT loan, but does ensure a strong first mortgage with a healthy debt service coverage that will allow repayment over the first 6-7 years of the loan. The project will make annual payments equivalent to the greater of 50% or surplus cash or \$153,333 annually, with a cap of 60% of surplus flow. This will make certain that the loan can be repaid within seven years. This compromise will induce POAH to refinance with RIHousing and they will invest over \$90,000 per unit in the assets. RIHousing will also require the affordability period to be extended for an additional 40 years while the alternative HUD loan has no such requirement.

The total development cost (“TDC”) at the time of Preliminary Approval was \$33,496,179. The TDC has subsequently increased to \$36,550,154, an increase of 9.1%. This is a result of the following factors:

- The acquisition cost of the improvements increased from \$16,375,000 to \$17,540,000, an increase of \$1,165,000
- Construction/Contingency Costs increased from \$8,306,587 to \$9,908,601, an increase of \$1,602,014. This is due primarily to an increase in scope, but also due to escalating prices.
- Construction Loan Interest increased from \$700,000 to \$1,050,000, an increase of \$350,000. The increase is due to a longer construction period and an increase in the amount of the construction loan.
- Combined Base and Incentive Developer Fee increased from \$4,003,000 to \$4,620,066, an increase of \$617,066 which generates additional equity.

The increase in TDC is being offset by the following three increases to sources:

- An increased seller loan;
- Increased amount of LIHTC equity generated by the sale of additional credits and an increase in the credit pricing from \$.92 to \$.94; and
- An increase in the permanent mortgage.

The capital stack includes a deferred developer fee, seller loans, existing reserves, income from operations and rolling over a portion of the existing AHT loan. The preliminary approval included a tax-exempt loan of \$17,000,000, with a balloon payment of \$5,260,000 and the remaining \$11,740,000 converting to the amortizing permanent loan. In order to meet the required 50% test, POAH is now requesting a tax-exempt loan not to exceed \$17,500,000. At the end of the construction period POAH will make a balloon payment of \$5,250,000 with a permanent loan not to exceed \$12,250,000.

2. EXECUTIVE SUMMARY

Property Address: 30 Kingstown Road & 29 South Pier Road
Narragansett, RI

Developer: Preservation of Affordable Housing, Inc.

Amount(s) Requested: \$17,500,000 Tax-exempt loan

Loan terms (rate/term):

Tax-exempt Construction 4.125% / 18-month term, interest only

Tax-exempt Permanent 4.125% / 40-year Amortization/17-year Balloon

*** Note:** The RIHousing loans will be re-priced approximately two weeks prior to closing.

Loan to Value (LTV) Test:

NET OPERATING INCOME	\$1,053,923	\$10,134	(\$151,616)	\$902,307	\$8,676
Appraisal Cap Rate	5.50%			5.50%	
Valuation	\$19,162,236	\$184,252	(\$2,756,655)	\$16,405,582	\$157,746
Loan Principal	\$12,250,000	\$117,788		\$12,250,000	\$117,788
LTV	63.93%		11%	74.67%	

RIHousing funded Capital Stack Terms:

<u>Loan Type</u>	<u>Principal</u>	<u>Term</u>	<u>Rate</u>	<u>Comment</u>
RIH Loan	\$17,500,000 Construction \$12,240,000 Permanent	40 years	4.125%	Construction to Permanent New Mortgage

Existing Debt for Beachwood and South Winds

Beachwood

<u>Loan Type</u>	<u>Principal</u>	<u>Accured Interest</u>	<u>Rate</u>	<u>Comment</u>
First Mortgage	\$ 3,416,588	None	6.73%	Paid off at Closing

South Winds

Loan Type	Principal	Accrued Interest	Rate	Comment
First Mortgage	\$ 2,638,350	None	6.75%	Paid off at closing
AHT Loan	\$ 1,400,000	\$ 422,000	4.25%	Interest & partial principal repaid, remaining principal assumed by new owner

As part of the approval process, staff has determined that the Development and sponsor meet RIHousing's requirements for rollover of existing debt. Broadly, this review includes:

- Current on first mortgage or in compliance with forbearance agreement;
- No outstanding monitoring findings, no history of significant monitoring findings;
- Demonstrated responsible long-term ownership and management of the property;
- A satisfactory equity pay-in schedule to RIHousing;
- Maximize amortizing debt the property can support; and
- Borrower provide guarantees to cover any deficit shortfalls.

Proposed Sources and Uses:

Sources	Preliminary		Delta	Firm	
	Amount	Per Unit		Amount	Per Unit
RIH First Mortgage	\$11,740,000	\$112,885	(\$510,000)	\$12,250,000	\$117,788
Assumed Debt (Rollover)	\$950,000	\$9,135	\$30,000	\$920,000	\$8,846
Seller Loan	\$876,978	\$8,432	\$40,279	\$836,699	\$8,045
Seller Loan	\$730,800	\$7,027	(\$216,776)	\$947,576	\$9,111
Seller Loan	\$7,505,982	\$72,173	(\$1,263,119)	\$8,769,101	\$84,318
LIHTC Proceeds	\$9,086,639	\$87,372	(\$634,074)	\$9,720,713	\$93,468
CF From Operations During Construct	\$600,000	\$5,769	(\$89,043)	\$689,043	\$6,625
Deferred Developer Fee	\$2,005,780	\$19,286	(\$411,242)	\$2,417,022	\$23,241
Total Sources	\$33,496,179	\$322,079	(\$3,053,974)	\$36,550,154	\$351,444

Uses	Preliminary		Delta	Firm	
	Amount	Per Unit		Amount	Per Unit
Construction	\$7,550,587	\$72,602	(\$1,465,347)	\$9,015,934	\$86,692
Contingency	\$756,000	\$7,269	(\$136,667)	\$892,667	\$8,583
Acquisition	\$16,375,000	\$157,452	(\$1,165,000)	\$17,540,000	\$168,654
Soft Costs	\$1,846,069	\$17,751	\$157,023	\$1,689,046	\$16,241
Financing	\$1,594,550	\$15,332	(\$68,247)	\$1,662,797	\$15,988
Developer Fee	\$4,003,000	\$38,490	(\$617,066)	\$4,620,066	\$44,424
Operating Reserve	\$866,837	\$8,335	\$56,112	\$810,725	\$7,795
Replacement Reserve Year 1 Deposit	\$208,000	\$2,000	\$0	\$208,000	\$2,000
Other Reserves	\$296,136	\$2,847	\$185,217	\$110,919	\$1,067
Total Uses	\$33,496,179	\$322,079	(\$3,053,975)	\$36,550,154	\$351,444

Deviations from standard underwriting: None

This Development meets all applicable RIHousing underwriting guidelines, including the two tests in the RIHousing Bridge Loan Term Sheet. See Attachment A for analysis.

Recommendation: Staff recommends firm approval of a tax-exempt loan in the amount not to exceed \$17,500,000 of which \$12,250,000 will remain as permanent debt.

3. OPPORTUNITY (BENEFITS) / CHALLENGES

3.A Benefits

This transaction will preserve 104 existing affordable units and complete a moderate rehabilitation of the units and common areas. Many of the improvements are focused on upgrades to the exterior envelope and energy upgrades. The net result of the completed proposed scope of work will be completely refreshed buildings and a new affordability period that will extend the life of this affordable development an additional 40 years.

3.B Risks/Challenges

The proposed transaction is low risk and presents few material challenges. The loan is underwritten to the lower of HAP or market rents. The LTV is less than 75%. The Development will have a new 20-year HAP contract subject to annual appropriations. The permanent loan will be insured through the HUD Risk Share program.

3.C Affordability

The target population for the Developer is seniors with incomes below 50% AMI with a Section 8 HAP rental subsidy encumbering all units. A 40-year affordability extension will be recorded at closing.

3.D Pertinent risk factors for this development are:

Market – Low Risk; the proforma utilizes a 5% vacancy for underwriting consistent with the syndicator’s projections.

Construction – Moderate Risk; There is always a degree of uncertainty surrounding rehabilitation. However, this is partially offset by POAH’s long history of owning and managing the properties. The Developer and general contractor are both experienced with the rehabilitation of occupied units. In addition, the contingency is 10% of the construction budget.

Developer – Low Risk; POAH owns and operates a large portfolio of similar buildings and has substantial resources.

Community Opposition – None, the improvements are existing.

Financing - Low Risk; The primary source of permanent financing will be a 40-year tax exempt mortgage, with a 17-year balloon payment. Additional sources of funds include equity from the sale of 4% LIHTC generated by the issuance of tax-exempt bonds, seller loans, income from operations, the deferred AHT loan and a deferred developer fee.

Underwriting Assumptions – Low Risk; transaction is underwritten to RIHousing’s standard underwriting guidelines. The Development represents a conservative loan-to-value risk and there is sufficient cashflow to support the property’s debt service. In addition, the underwriting includes a full six-month operating reserve, plus an additional replacement reserve, both required by the syndicator.

Other – As a means of asserting greater control over LIHTC projects, in recent years POAH has utilized a ground lease structure. The to be formed limited partnership will have a fee interest in the improvements and a leasehold interest in the supporting site. Because any lease

payments will be “below” the line and made from POAH’s share of surplus cash this structure will not impact the underwriting or RIHousing’s collateral for the proposed financing.

4. UNDERWRITING

4.A

Unit	Rent Type	Number of Units	Gross Rent	Gross Rent as a		
				LIHTC Max Rent	% of LIHTC Max Rent	Discount from Market Rent
1	60%	42	\$ 1,575.00	\$ 922.00	171%	0.0%
2	60%	6	\$ 1,770.00	\$ 1,107.00	160%	0.0%
1	60%	52	\$ 1,560.00	\$ 922.00	169%	0.0%
2	60%	4	\$ 1,765.00	\$ 1,107.00	159%	0.0%
Total		104				0.0%

Note: Current HAP rents are equal to current market rents

4.B Trending – 2% rental income/3% expenses

4.C Vacancy Loss and Bad Debt – 5%

4.D Other Income – \$17,480 for laundry and other miscellaneous revenue.

4.E Operating Expenses – \$9,573 per unit, inclusive of Replacement Reserve deposits

4.F RE Taxes – \$158,352; 8% of Gross Revenue Potential.

4.G Proposed Replacement Reserve Deposit – Initial deposit of \$208,000 (\$2,000 per unit); annual deposits of \$325/unit per year

4.H Proposed Operating Reserve Deposit – \$810,725, or a full six months of operating expenses and debt service on first mortgage.

4.I Other Proposed Reserves - None

4.J Resulting NOI for Debt Service – \$902,307 in Year 1 which increases gradually despite negative trending to \$51,519 in year 15. DSC is 1.44 in year 1.

4.K Bridge Loan Tests: – See Bridge Loan Test “Attachment A”.

5. PROPERTY DESCRIPTION

South Winds and Beachwood are both located in Narragansett, were both built in 1977 and are both 100% subsidized by Section 8 HAP contracts. Each property has surface parking, a community room and community laundry room. South Winds Apartments contains three buildings located on one parcel of land. There are a total of 48 units; 42 one-bedroom units and 6 two-bedroom units. Beachwood Apartments contains one building. It is configured into three wings linked by common corridors. There are a total of 56 units; 52 one-bedroom units and 4 two-bedroom units.

6. DEVELOPMENT ENTITY AND CAPACITY

6.A Prior Developments and Current Operational Capacity

POAH is a not-for-profit corporation with a core mission of preserving at-risk affordable housing, often housing that is at risk of being lost due to market pressures or physical deterioration. Based in Boston, POAH now owns and operates more than 11,000 affordable homes in 11 states and Washington DC. One of POAH's core principles is that the real estate portfolio must be sustainable and that the organization should be sustained primarily by the portfolio. They have an identify of interest property management company called POAH Communities.

Aaron Gornstein has been the Executive Director for five years. From 2012-2015, Mr. Gornstein served as undersecretary for the Massachusetts Department of Housing and Community Development (DHCD) and executive director of Citizens' Housing and Planning Association (CHAPA). POAH has significant staff capacity with a development team, asset management group and a design and construction team that oversees their projects.

6.B Financial Strength

RIHousing has reviewed the Borrower's financials and has determined that they are financially stable, the organization is well capitalized and represents a minimal credit risk.

6.C Guarantees

RIHousing will require a construction completion guarantee from POAH. The General Contractor will also be required to provide a Payment and Performance Bond.

7. LOCATION AND MARKET DYNAMICS

The two projects are located at the eastern most edge of Narragansett and are located less than a mile apart. The neighborhood is developed primarily with single- and multi-family residential uses; and projects are located less than 0.25± miles west of the ocean. Beachwood is located across the street from Narragansett Pier Marketplace and northwest of the Towers and the Coast Guard House. South Winds is located west of Monahan's Clam Shack and Restaurant. The sites are primarily accessible from Ocean Road as well as from Route 1 and Route 108. There is bus transportation available in the area, but both projects are considered to be "car-dependent" locations.

Well managed market rate apartment projects throughout the state have averaged less than 5.0% vacancy for the last several years, although the impact of COVID is just starting to be seen in market statistics. In June 2020 the market rate vacancy rate in Washington County was 1.7, which is less than the 2.2% vacancy rate reported six months earlier. Consistent with the rest of the state, there is a shortage of affordable housing in Narragansett and Washington County, so strong demand is anticipated for the affordable units located within Beachwinds.

8. ADDITIONAL CONSIDERATIONS - None

9. CONCLUSION

Staff recommends firm approval of: a tax-exempt loan of \$17,500,000, with a balloon payment of \$5,250,000 at the end of construction and the remaining \$12,250,000 converting to an amortizing loan with a balloon payment in year 17.

10. ATTACHMENTS

- A) Bridge Loan Test
- B) Proforma

Attachment A - Bridge Loan Test

Test 1 The sum of the bridge loan (the “Bridge Loan”) and the Rhode Island Housing permanent loan cannot exceed 90% of the Total Development Cost (“TDC”) of the project. This includes transactions in which the Bridge Loan is bridging equity from the sale of Low Income Housing Tax Credits (“LIHTC”), federal and/or state historic tax credits.

Bridge Loan:	\$5,250,000
Permanent Loan:	<u>\$12,250,000</u>
SUM:	\$17,500,000
TDC:	\$36,550,154

MEETS REQUIRED TEST.

The sum of the Bridge Loan and the initial capital contributions may not exceed 90% of the gross syndication raise, subject to terms and conditions of the Limited Partnership Agreement (“LPA”) and all subsequent capital contributions.

Test 2 For tax-exempt transactions, the amount of the Bridge Loan in general, shall not exceed the minimum amount of loan proceeds necessary to ensure that over 50% of the aggregate basis of the project is funded with tax-exempt bond proceeds (the “50% Test”), as determined in accordance with applicable tax code provisions. Under certain circumstances, Rhode Island Housing will consider bridging historic tax credits, which exceed the minimum loan amount necessary to meet the 50% Test.

Bridge Loan:	\$5,250,000
Total LIHTC Equity:	\$9,720,713
B Gross Syndication Raise:	\$9,720,713
Initial Capital Contribution:	\$1,458,107
Initial Percent of Credits:	15.0%
A Bridge + Initial Contribution:	\$6,708,107
Test: A over B	69% <90% TRUE