

Approval Loan Recommendation Summary – Harris House Apartments

Preliminary:

Firm: X

Date: May 6, 2020

1. OVERVIEW

Harris House Apartments is an existing 133-unit elderly affordable housing development located in Cranston, RI (“Harris House” or the “Development”) that is currently financed by RIHousing. The Development is owned by Harris House Partners, LP (the “Mortgagor” or the “Borrower”). 28 Harris Associates, LLC is the general partner and Cathedral Development Group, Inc. (“CDG” or the “Developer”) is the sole managing member of the General Partner and the developer. In 2018 (), an affiliate of CDG purchased the limited partner interest which had been held by a LIHTC investor. No change in either the general partner or a limited partner with greater than 25% ownership interest is anticipated.

The property is subsidized by a Section 8 Housing Assistance Payment (“HAP”) Contract that is effective through May 2031. The Developer is seeking to refinance the Development with a taxable first mortgage in the principal amount of \$16,560,000. The Developer will use the proceeds of the new financing to pay off the existing mortgage, undertake elevator, accessibility, energy efficiency and life safety upgrades to the Development, recapitalize the reserves and make an equity distribution to the partners. The proposed refinancing is consistent with RIHousing’s taxable loan program that was introduced to replace the Treasury-HUD Federal Financing Bank (“FFB”) HFA Multifamily Risk Sharing Loan Financing Initiative which was suspended by HUD in 2018.

As part of the approval process, staff has determined that the Development and owner meet RIHousing’s requirements for participating in the taxable loan program. Broadly, this review includes:

- Compliance with HUD’s requirements
- Demonstrated responsible long-term ownership and management of the property
- A 20-year HAP contract
- Well-funded reserves
- Low vacancy rates
- Consistency with RIHousing’s standard underwriting requirements
- Financially beneficial to RIHousing
- Execution of a new 40-year affordability agreement.

Specifically, under the taxable loan platform, RIHousing will agree to a refinancing if, at a minimum, all of the following additional conditions are met:

- The borrower has demonstrated responsible long-term ownership and management of the property;
- The property is in good physical condition and RIHousing is satisfied based on review of a current capital needs assessment that all capital needs are adequately funded during the life of our loan;
- The transaction conforms to RIHousing's Risk Share Underwriting Guidelines and the Taxable Loan Program Term Sheet.

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2. EXECUTIVE SUMMARY

Property Address: 28 Harris Avenue, Cranston, RI 02920

Developer: Property Advisory Group, Inc.

Amount(s) Requested: \$16,560,000

Loan to Value (LTV) Test:

	Appraisal	Per Unit	Variance	Current UW	Per Unit
Net Operating Income	\$1,086,281	\$8,168	(\$46,280)	\$1,040,001	\$7,820
Appraisal Cap Rate	5.90%			5.90%	
Valuation	\$18,400,000	\$138,346	(\$772,869)	\$17,627,131	\$132,535
Loan Principal	\$16,560,000	\$124,511		\$16,560,000	\$124,511
LTV	90.00%		3.95%	93.95%	

Loan terms (rate/term):

- Rate: 4.375%
- Term: 40-years with a balloon payment in Year 30 and a prepayment option in Year 15. The projected debt coverage in Year 30 with negative trending is 1.58.

Proposed Sources & Uses:

Sources	Firm	
	Amount	Per Unit
RIH First Mortgage	\$16,560,000	\$124,511
Operating Reserve	\$438,530	\$3,297
Replacement Reserve	\$729,373	\$5,484
Total Sources	\$17,727,903	\$133,293

Uses	Firm	
	Amount	Per Unit
Construction	\$192,500	\$1,447
Contingency	\$150,000	\$1,128
Acquisition	\$6,260,000	\$47,068
Soft Costs	\$304,201	\$2,287
Financing	\$484,700	\$3,644
Operating Reserve	\$215,816	\$1,623
Replacement Reserve	\$1,573,500	\$11,831
Other Reserves	\$112,238	\$844
Equity Takeout	\$8,434,947	\$63,421
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Other Reserves	\$112,238	\$844
Total Uses	\$9,292,956	\$69,872
Equity Takeout	\$8,434,947	\$63,421

Deviations from standard underwriting – YES:

- A 4% vacancy rate was applied to underwriting as the historical vacancy ranged from 1.2% to 3.4% since 2017. The appraisal used a vacancy rate of less than 3%.
- Operating reserves were sized to 3 months versus 6 months. The borrower and property have an excellent repayment history and the HAP rents provide additional debt coverage.

Recommendation: Firm approval of the first mortgage in the amount of \$16,560,000.

3. OPPORTUNITY (BENEFITS) / CHALLENGES

3.A Benefits: The proposed refinancing preserves 133-units of elderly and/or disabled housing and will extend the affordability period for the Development for 40 years, while allowing the Developer to perform necessary upgrades to the elevators, enhance accessibility, improve energy efficiency, upgrade life-safety equipment including additional fire safety, and adequately capitalize the renovation reserve to provide for future upgrades to the Development over the next 20 years.

3.B Risks/Challenges: The refinancing transaction assumes continuation of Section 8 assistance to support the new first mortgage debt, however, credit enhancement in the form of FHA Risk Share Insurance will be required

3.C Affordability: 40-year affordability restriction will be recorded at closing.

3.D Pertinent risk factors for this development are:

Market - Low Risk – The Development has historically low vacancy rates, and except for standard turnover, the Development is essentially 100% occupied with a waiting list. All the units are subsidized with a HAP Contract. The loan is underwritten to the market rents which are lower than the HAP rents.

Construction - Low Risk – The scope of work is small, and the Developer has demonstrated capacity to both self-perform and subcontract work. Completed architectural plans will be required before closing for ADA upgrades, life safety and other work as required by RIHousing and building code. A Capital Needs Assessment will be commissioned every five years to reassess needs.

Developer - Low Risk – CDG has had an ownership interest in the property and managed the Development since 1992.

Community Opposition - Low Risk – Not Applicable. The site is existing and has been operating since 1979.

Financing - Low Risk – This transaction assumes payoff of the existing RIHousing debt. The primary source of permanent financing will be a 40-year mortgage

supported by the lower of HAP or market rents which will be insured through the FHA Risk Sharing Program.

Underwriting Assumptions – Low Risk – The transaction is underwritten to RIHousing standard guidelines with negative trending and a 4% vacancy rate. The Development's debt coverage ratio is 1.19 in year 1 and increases annually thereafter. Capitalized reserves will equal RIHousing's required amounts.

Other – Not applicable.

4. UNDERWRITING

4.A Rent Comparison –

Bedrooms	Number of Units	LIHTC Max Rent	Gross Market Rent	Gross HAP Rent	Gross UW Rent
1	122	\$ 988	\$ 1,320	\$ 1,340	\$ 1,320
2	10	\$ 1,107	\$ 1,500	\$ 1,575	\$ 1,500
1	1	\$ 988	\$ 1,320	\$ 988	\$ 988
Total	133	\$ 132,594	\$ 177,360	\$ 180,218	\$ 177,028

The loan is underwritten to the Market rents which are lower than the HAP rents

4.B Trending – 2% income; 3% operating expenses

4.C Vacancy Loss and Bad Debt— 4%

4.D Other Income – 0%

4.E Operating Expenses – Forecasted at \$7,893 including the annual deposit to the replacement reserve

4.F RE Taxes – 8% of gross revenue trending at 2% per year to be consistent with income trending.

- **4.G Proposed Replacement Reserve Deposit** – \$1,573,500 initial deposit (\$11,831 per unit) plus annual deposits of \$300/unit/year. It is important to note that the borrower is capitalizing the Replacement Reserve with \$11,831/unit compared to standard 2000/unit. Out of an abundance of caution, the borrower intends to undertake work in the 12-18 months after closing due to COVID-19. The borrower will undertake the full scope of work when there is adequate time to get into the units and prepare plans and specs. Only the critical needs identified in the CNA are being done immediately.

4.H Proposed Operating Reserve Deposit – \$215,816 equals three (3) months of operating expenses and debt service, less the amount of the initial deposit into the replacement reserve.

4.I. Other Proposed Reserves – Not Applicable.

4.J Resulting NOI for Debt Service

- \$1,040,001 in the first year
- Model performs above 1.19 for 30 years with negative trending

5. PROPERTY DESCRIPTION

Harris House consists of one tax parcel containing 4.32 acres located at 28 Harris Avenue in Cranston, Rhode Island. The Development's site is improved with a single 4-story apartment building that originally operated as an industrial warehouse constructed in the early 1900s, renovated for its current use in 1979 and last upgraded in 2010. Harris House contains 123 one-bedroom and 10 two-bedroom apartment units, all of which are restricted to low income elderly and/or disabled residents. Of the total 133 units, 132 have the benefit of project-based rent assistance through a HAP Contract and a single one-bedroom unit is restricted to senior households with incomes less than 60% of area median income.

6. DEVELOPMENT ENTITY AND CAPACITY

6.A Prior Developments and Current Operational Capacity - CDG is a Rhode Island based real estate ownership. They control the general partner interest in approximately 10 Section 8 developments financed by RIHousing and they have proactively preserved most of their portfolio with RIHousing through its various preservation programs. Their identity of interest management company is Property Advisory Group ("PAG"). They are an experienced management agent providing services to its developments. CDG, and PAG own and operate other developments in Rhode Island, New York, Delaware, Wisconsin and Arizona.

6.B Financial Strength - RIHousing has reviewed the Borrower's audited financials for the preceding three years and has determined that they are financially stable and represent a reasonable credit risk.

6.C Guarantees – A construction completion guaranty will be required and 20% of the equity will be withheld until completion.

7. DESCRIPTION OF THE NEIGHBORHOOD

Harris House is well located within an urban location that has access to health care, senior focused services, shopping, restaurants, and entertainment all of which benefit the residents at the Development. The immediate neighborhood is developed with primarily commercial, two-family, and multi-family residential uses as well as retail, dining, and entertainment services including a Stop & Shop supermarket, Aldi supermarket, Lang's Bowlarama, Lowe's Home Improvement, a Rite Aid Pharmacy, Cranston Public Library's Arlington Branch, and multiple cafes. The Cranston Department of Senior Services is located within a quarter-mile to the south of the Development. RIPTA's bus line #4, which has a stop at the front entrance of the Development, provides transportation to the Cranston Department of Senior Services as well as additional locations primarily along Cranston Street.

8. CONCLUSION

Staff recommends firm approval of a taxable first mortgage loan in the amount of \$16,560,000.

9. ATTACHMENTS

A: Pro Forma