

Approval Loan Recommendation Summary – THE PARAGON MILL HOUSING

Preliminary _____

Firm X

Date: March 10, 2021

1. OVERVIEW AND SUMMARY OF CHANGES FROM PRELIMINARY APPROVAL

This Credit Committee request is for Firm Approval of a reservation of up to \$1,108,117 of 2020 Low-Income Housing Tax Credits (“LIHTC”) for the Paragon Mill (the “Development”), a 101-unit rental housing development located in Providence. The developer is The Alexander Company, Inc. (“TAC” or the “Developer”), a Wisconsin based for-profit developer with a portfolio of mixed-use housing and historic redevelopments in Maryland, Virginia, Iowa, Missouri and Wisconsin.

TAC proposes an adaptive reuse and environmental clean-up of the historic Earncliffe & Paragon Worsted Mills located adjacent to the Woonasquatucket River in the Olneyville neighborhood of Providence. The Development would create a total of 101 new residential units of which 44 units would be restricted for households at or below 60% of the area median income (“AMI”) and the remainder of the units would be restricted to 120% AMI. The Development notably incorporates an array of public and private sources including:

- Private equity investment for federal and state tax credits
- A construction to permanent loan from Citibank
- Private investment into the State of Rhode Island Opportunity Zone program
- The Providence Redevelopment Authority’s (“PRA”) contribution of the real estate, tax stabilization agreement and soft debt.

Since preliminary approval, the total development cost (“TDC”) has increased 20% from \$29,365,383 to \$35,294,310. TRAC Builders, Inc. (the “general contractor” or “TRAC”) was selected after competitively bidding the project and then TRAC competitively bid each trade of the construction budget. Three bids were received for each trade as required by RI Housing guidelines. The resulting increase of \$4.3 million in construction and contingency costs were attributed to:

- Increased environmental remediation of the subsurface soil contaminants
- Materials and labor cost increases
- Additional requirements to meet National Historic standards
- Higher soft costs related to additional design work

- Increased deferred developer fee to generate more historic tax credits (the amount of developer fee eligible for LIHTC basis remained the same. The developer fee was increased to general additional historic tax credits and the additional fee was deferred back into the transaction)
- A change in lead architect from DBVW Architects, Inc., to TAC to control the design process and predictable project delivery. DBVW, Inc is the locally licensed architect. TAC has provided a qualification statement demonstrating their experience as lead architect on previous projects. The contractual relationship between TAC and DBVB has been reviewed and approved by RIHousing. This change in architect has resulted in higher soft costs.

Since the appraisal was completed in August 2020, the projected market rents have been discounted by approximately 10% resulting in lower net operating income which resulted in a reduction of the Citibank permanent by \$1.6 million. The availability of the lesser expensive PRA loan at 1% interest was also a factor in the reduction of the Citibank permanent loan. The amount of LIHTC equity decreased due to a reduction in pricing from \$0.91 to \$0.89 attributed to an industry wide increase in the supply of tax credits as a result of the recent 4% LIHTC legislation and the risk associated with market rate units.

The resulting \$5.93 million gap in financing was resolved with the following changes:

- The PRA contributed a subordinate loan of \$5 million at 1% interest.
- The PRA will stabilize the property taxes with a limitation of 6% of gross income as may be enacted by an Affordable Housing Covenant (“AHC”). Apart from the LIHTC regulatory agreement restricting 44 units to 60% AMI, the AHC requires all units to be restricted to 120% AMI, effectively restricting 57 units to workforce rents. In the event the tax stabilization is lost or cancelled voluntarily by TAC, the managing member will guarantee the potential tax liability.
- The state and federal historic equity proceeds increased by \$2.2 million via a combination of increased pricing and, for the state historic credits, the elimination of capital gains tax through a non-profit pass through structure created with the PRA.
- The developer deferred increased by \$525,678

2. EXECUTIVE SUMMARY

Property Address: 39 Manton Avenue
Providence, RI 02909

Developer: The Alexander Company, Inc.

Amount(s) Requested: \$1,108,117 of 2020 Low-Income Housing Tax Credits

Loan to Value (LTV) Test:

	Appraisal	Per Unit	Variance	Current UW	Per Unit
NET OPERATING INCOME	\$630,619	\$6,244	(\$4,495)	\$626,124	\$6,199
Appraisal Cap Rate	6.00%			6.00%	
Valuation	\$10,510,317	\$104,063	(\$74,918)	\$10,435,398	\$103,321
Loan Principal	\$6,500,000	\$64,356		\$6,500,000	\$64,356
LTV	61.84%		0%	62.29%	

Citibank Permanent Loan Terms:

- 16-year term
- 35-year amortization
- 3.5% estimated interest rate; 3% over LIBOR and locked in at conversion

PRA HTF Loan Terms:

- 35-year term and amortization
- 1% interest rate
- Interest only payments for the first 5 years

Proposed Sources and Uses:

Sources	Preliminary		Delta	Firm	
	Amount	Per Unit		Amount	Per Unit
Citibank 1st Mortgage	\$8,100,000	\$80,198	(\$1,600,000)	\$6,500,000	\$64,356
PRA HTF 2nd Mortgage	\$0	\$0	\$5,000,000	\$5,000,000	\$49,505
LIHTC Proceeds	\$10,080,707	\$99,809	(\$219,451)	\$9,861,256	\$97,636
Fed. Historic Tax Credit Proceeds	\$4,366,351	\$43,231	\$812,095	\$5,178,446	\$51,272
State Historic TC Proceeds	\$5,858,471	\$58,005	\$1,404,710	\$7,263,181	\$71,913
Opportunity Zone Investment	\$144,502	\$1,431	\$5,895	\$150,397	\$1,489
Deferred Development Fee	\$815,352	\$8,073	\$525,678	\$1,341,030	\$13,278
Total Sources	\$29,365,383	\$290,746	\$5,928,928	\$35,294,311	\$349,449

Uses	Amount		Delta	Per Unit	
	Amount	Per Unit		Amount	Per Unit
Construction	\$20,502,424	\$202,994	\$3,785,706	\$24,288,130	\$240,477
Contingency	\$1,956,192	\$19,368	\$489,178	\$2,445,370	\$24,212
Acquisition	\$25,000	\$248	(\$10,000)	\$15,000	\$149
Soft Costs	\$2,787,619	\$27,600	\$487,508	\$3,275,127	\$32,427
Financing	\$1,392,497	\$13,787	\$47,229	\$1,439,726	\$14,255
Paid Developer Fee	\$1,915,200	\$18,962	\$0	\$1,915,200	\$18,962
Incentive Developer Fee	\$0	\$0	\$1,229,601	\$1,229,601	\$12,174
Replacement Reserve Year 1 Deposit	\$35,350	\$350	\$0	\$35,350	\$350
Total Uses	\$29,365,383	\$290,746	\$5,928,927	\$35,294,310	\$349,449

Deviations from standard underwriting: None. The increased developer fee is not included in LIHTC basis. It was added to generate additional historic credits and equity.

Recommendation: Firm Approval of a Reservation of Low-Income Housing Tax Credits.

3. OPPORTUNITY (BENEFITS) / CHALLENGES

3.A Benefits

This transaction will allow for the addition of 44 new affordable housing units, 57 workforce housing units and the preservation of a blighted and historic vacant mill in the Olneyville neighborhood of Providence.

3.B Risks/Challenges

The Paragon Mill rehabilitation faces a higher level of construction risk than other developments due to unforeseen issues that may be exposed in the weathered structure during the construction process as well as environmental site work and hazardous material abatement. As programmed in the Remedial Action Work Plan (“RAWP”), currently filed and awaiting

approval by RIDEM, the developer will mitigate soil contamination below the structure with the installation of a sub slab mechanical ventilation system. Additional geotechnical test pits were ordered at the end of February to mitigate the risk associated with the installation of new underground utilities in the parking area. The TAC principals will personally guaranty the construction completion and loan repayment through conversion. Since RIHousing is not the lender, it bears no financial risk.

Additionally, a portion of the property is also located in Flood Zone AE which is defined as the base floodplain. The majority of the development is located within Flood Zone X, an area of minimal flood hazard above the 500-year flood level. While the survey provided indicates the flood zone elevation is 22 feet above sea level and the first floor of the building in question is located at 26 feet above sea level, the portion of the building in the Zone AE will require flood insurance. A letter of map amendment will be pursued by TAC upon completion of the project to remove the flood insurance requirement.

3.C Affordability

The target population for the Development includes 44 households restricted to 60% AMI for the LIHTC units and the remaining 57 units are targeted for households earning less than 120% AMI. RIHousing will require the standard 30-year Tax Credit Restriction Agreement and a 30-year Regulatory Agreement for the LIHTC units. The 57 non-LIHTC units will be subject to the AHC between the developer and the PRA.

3.D Pertinent risk factors for this development are:

Market – Moderate Risk; RIHousing commissioned a market study and Citibank commission an appraisal and another market study. Both reports indicate strong demand for the LIHTC and market rate units. The market study suggests a lease-up period of six to twelve months. All of the units were underwritten with a 7% vacancy. Income is inflated at 2% per year and expenses are trended at 3% per year. The resulting debt coverage begins at 1.51 and ends at 1.31 in year 15.

Construction – Moderate Risk as identified above in Section 3B; TAC, DBVW, and TRAC are all experienced with this type of construction. RIHousing's Design and Construction group has reviewed the proposed plans and specifications. Contingencies are budgeted to cover unforeseen issues or unanticipated cost inflation.

Developer – Low Risk; TAC is a for-profit corporation with extensive experience rehabilitating historic mixed income buildings throughout the nation. TAC has an identify of interest property management team that will manage the Development. TAC has 1,303 total units under management, of which 821 are rent-restricted (LIHTC) and 482 are market rate.

Both TAC principals provided personal financials to Citibank for underwriting of the completion and repayment guarantee.

Community Opposition – Low Risk; The Paragon Mill has been vacant since 2008 and is an impediment to future development in the neighborhood.

Financing - Low Risk; The primary source of financing will be a construction to permanent loan from Citibank. AHP is a subsidiary of Berkshire Hathaway and has a lengthy track record of funding equity to low-income and historic tax credit projects.

Underwriting Assumptions – Low Risk; except as noted previously, the transaction is underwritten to RIHousing’s standard underwriting guidelines with negative trending and Citibank is absorbing the financial risk. The Development represents appropriate loan-to-value risk and there is sufficient cashflow to support the property’s debt service associated with the Permanent Loan. Initial capitalization of reserves meets or exceeds our underwriting guidelines.

Other – NA

4. UNDERWRITING

4.A Rent Assumptions

Bedrooms	AMI Restriction	Units	Gross Rents			Underwriting Rents		
			Under-writing	LIHTC or 120% AMI	Market	% of Max	Discount from Market	Effective AMI
1	60%	34	\$954	\$978	\$1,618	98%	-41.0%	59%
2	60%	4	\$1,145	\$1,174	\$1,804	98%	-36.5%	59%
2	60%	4	\$1,155	\$1,174	\$1,904	98%	-39.3%	59%
3	60%	2	\$1,335	\$1,357	\$2,372	98%	-43.7%	59%
1	120%	47	\$1,443	\$2,088	\$1,618	69%	-10.8%	83%
1	120%	1	\$1,668	\$2,088	\$1,718	80%	-2.9%	96%
2	120%	3	\$1,804	\$2,349	\$1,804	77%	0.0%	92%
2	120%	3	\$1,904	\$2,349	\$1,904	81%	0.0%	97%
2	120%	2	\$2,254	\$2,349	\$1,954	96%	15.4%	115%
3	120%	1	\$2,387	\$2,610	\$2,372	91%	0.6%	110%
Total		101	\$131,814	\$166,984	\$169,756	79%	-22.4%	74%

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

4.C Vacancy Loss and Bad Debt – 7% of Gross Potential Rent

4.D Other Income – \$23,284 includes:

- \$993 per month of commercial income at \$4 per sq. ft. on a triple net basis
- \$947 per month for pet and application fees

4.E Operating Expenses – \$7,199 per unit, inclusive of Replacement Reserve deposits

4.F RE Taxes – \$85,761; 6% of Gross Revenue Potential per the tax stabilization agreement.

4.G Proposed Replacement Reserve Deposit – Initial deposit of \$35,350 (\$350 per unit); annual deposits of \$350/unit per year

4.H Proposed Operating Reserve Deposit – \$650,806, or greater than six months of operating expenses and debt service on first mortgage.

4.I Other Proposed Reserves - NONE

4.J Resulting NOI for Debt Service – \$626,124 in Year 1 which increases steadily with negative trending to \$696,620 in year 15.

5. PROPERTY DESCRIPTION

The proposed development contains 119,995± square feet of gross building area spread across 9 total buildings (8 buildings are interconnected). Upon completion, the plans include the renovation and conversion of the property to 101 LIHTC and workforce dwelling units. There will be 112,832± square feet of gross building area and 76,779± square feet of gross living area. 44 units will be designated as LIHTC restricted to 60% AMI and the remaining 57 units will be designated as workforce restricted to 120% AMI. There will also be 2,755± square feet of commercial space in building #9. The site supports parking for 160± vehicles.

The apartment mix will include 81 one-bedroom units of 675 sq. ft, 15 two-bedroom units of 860 sq. ft., 2 two-bedroom/2-bathroom units of 882 sq. ft, and 3 three-bedroom units of 1,367 sq. ft. All apartments will feature elevated finishes, historic character, in-unit washers and dryers, and expansive windows to maximize natural light. Each unit will contain a refrigerator, range/oven, dishwasher, microwave, washer, dryer, carpet, blinds, coat closet, stainless steel appliances and granite countertops. Select units will also contain hardwood or wood composite flooring, exposed brick, walk-in closet and patio. Project amenities include a meeting room, exercise room, lounge, courtyard, extra storage, package receiving, rooftop terrace, on-site management, on-site maintenance, intercom/electronic entry, video surveillance and common area Wi-Fi.

6. DEVELOPMENT ENTITY AND CAPACITY

6.A Prior Developments and Current Operational Capacity – The Alexander Company, Inc. (“TAC”), which was founded 36 years ago, is a Wisconsin-based real estate developer and manager involved in the acquisition and development of multi-family rental communities and for-sale projects throughout the Midwest and Mid-Atlantic states. They have completed both mixed-use and historic projects. TAC and its team have successfully acquired or completed nearly 7,628 residential units, including several historic and affordable housing developments in Virginia, Washington D.C., Wisconsin and North Carolina. As a vertically integrated company, TAC provides its own property management. Over the past 30 years, they have managed over 7,000 units including residential, commercial and mixed-use properties. Their expertise lies in marketing and leasing, affordable housing compliance, market-rate property management, asset management, and preventative maintenance.

TAC has experience with state and federal affordable housing programs, real estate transactions utilizing low-income housing tax credits, historic tax credits and other housing and urban development programs. TAC is led by principal Joseph Alexander (President). David Vos, who has been with TAC for nearly 30 years, and Christopher Day are overseeing the project management for the Development.

6.B Financial Strength - RIHousing has reviewed the Borrower’s financials and determined they are financially stable; the organization is well capitalized and represents a minimal credit risk.

6.D Guarantees - Citibank will require a construction completion and repayment guarantee from TAC. The General Contractor will also be required to provide a Payment and Performance Bond.

7. LOCATION AND MARKET DYNAMICS

Brief Description of the Neighborhood – The Development is located in the eastern most section of Olneyville adjacent to the Woonasquatucket River and directly west of the Federal Hill and West Broadway areas which are more established with vibrant residential and retail sections. The neighborhood is defined as the area bound by Manton Avenue to the west, Atwells Avenue the north, Routes 6 and 10 to the east, and Westminster Street to the south. Surrounding uses include single and multifamily properties, Dunkin’ Donuts, AutoZone, United Way of Rhode Island, a Bank of America branch, Rent-A-Center, Sam’s Food Stores, Citizen’s Bank branch, William D’Abate Elementary, Joslin Park & Playground, various retail stores, various industrial buildings, and the Nickerson House Community Center, a not-for-profit with a sizeable day care, after-school care programs, and recreational fitness programs.

8. ADDITIONAL CONSIDERATIONS

Approval would be subject to:

- The approval of the RAWP currently under review by the RI Department of Environmental Management
- Receipt of an executed commitment letter from the PRA for the HTF loan as previously described.

9. CONCLUSION

Staff recommends firm approval of a reservation of up to \$1,108,117 of 2020 Low-Income Housing Tax Credits.

10. ATTACHMENTS

A) Proforma

Attachment A - Proforma