Low-Income Housing Tax Credit Development Project

submitted by NAME
for Property Development, CPLN 666
December 17, 2009

Concept, Site and Location

The .56 acre parcel at 3161 Market Street, current site of Firestone Auto Care, presents a potential affordable housing development site. The concept is to create a 50/50 mix of 82 market rate and affordable units that range in size from 1-bedroom to 3-bedrooms. The market will be targeted to students and staff connected to the University of Pennsylvania and Drexel, while it is hoped that the affordable units will directly impact the needs of the surrounding community. The site, though oddly shaped, has many locational advantages. The site is ideally positioned along many bus routes and is close to trolley, El, regional and national train service through 30th Street Station.

The building will be three (3) stories with ceiling heights of 9 feet (floor heights of 11.5 feet) on top of a single-level parking podium 10 feet high. The total building height will be 44.5 feet. Construction is expected to last 18 months.

The project is expected to be financed primarily through use of the Low-Income Housing Tax Credit (LIHTC) program of the federal government and a combination of other sources as outlined in the following report.

Zoning

The site is currently zoned G2, General Industrial. This information was obtained through a search on the Philadelphia Zoning Overlay website and then getting a general idea for the characteristics of the zoning type through Philadelphia’s Zoning Matters website. Usage types were not appropriate for the product type I intend to market, so I am assuming that I will receive a zoning variance to change the zoning on the parcel to R-16. This zoning allows for residential construction of a building type commensurate with my overall plans. I plan to build 82 units on my .56 acre parcel, which creates a zoned density of 146 units/acre.

Should this project be increased in size, R-16 permits buildable area at 500% of lot size + bonus gross floor area percentage according to certain requirements. There are
no limits on height. The bonus requirement applicable to this project and site is 725%, which allows for a maximum building area of 1225% of floor area, which is 24,625 x 12.25 = 301,656 square feet.

For R-16 a 5% increase is given for each foot in excess of 60 feet that face the street. This project will have 205 feet facing Market Street. So, the calculation is 205 - 60 = 145 x 5% = 725%. 725% + the original allowance of 500% = 1225%.

The citation for this is buildable area is located in the zoning code titled “§ 14-1303. Additional Floor Area.” and states:

(1) Buildings Facing a Street More than Sixty (60) Feet in Width. Where a building faces upon a street which is more than sixty (60) feet in width, the gross floor area of the building may be increased by five percent (5%) of the area of the lot for each one (1) foot of width of the street over sixty (60) feet; provided, that where a building faces two (2) or more streets, it shall receive additional gross floor area for the width of the widest street, and that street only.

The full code can be found here: http://www.amlegal.com/nxt/gateway.dll/Pennsylvania/philadelphia_pa/title14zoningandplanning/chapter14-1300additionalgrossfloorarea?f=templates$fn=document-frame.htm$3.0#JD_Chapter14-1300

► Affordable Housing Appropriateness

This site is particularly well suited to an affordable development given its location in West Philadelphia and proximity to many modes of public transit, including Market St. and 30th Street Station. This development will provide high quality housing to lower income residents in the community while integrating market-rate units in the same building.

Moreover, median income for zip code 19104, which includes the vast majority of the target affordable housing market in West Philadelphia, stood at $17,640 as of 10/2007 according to bestplaces.net. While this number is certainly skewed because of the large number of students in the area, it is well below the maximum incomes permitted under the LIHTC Program (for one person, $27,250 at 50% AMI, and $32,700 at 60% AMI) and therefore presents a need for this type of housing.

► Floorplate and Envelope

Lot dimensions are 250ft x 140 ft x 70 ft x 205 ft x 50 ft. This creates a parcel size with buildable land area of approximately 24,625 square feet. According to the zoning code I must build 15 feet away from the back lot line that abuts the other high-rise on the north side of the lot. Taking this square footage away leaves a building footprint of 22,750 square feet.

► Tax credit rent limits

The target market for affordable units will be those with 60% of area median incomes. Though there are many low-income residents in West Philadelphia in the 19104 zip code who are appropriate for this program, the community overall has a higher ability to pay than a project focusing on 50% AMI.
Maximum Rents

<table>
<thead>
<tr>
<th>Unit Size</th>
<th>50% AMI</th>
<th>60% AMI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Studio</td>
<td>$681.25</td>
<td>$817.50</td>
</tr>
<tr>
<td>1-Bedroom</td>
<td>$729.38</td>
<td>$875.25</td>
</tr>
<tr>
<td>2-Bedroom</td>
<td>$875.00</td>
<td>$1050.00</td>
</tr>
<tr>
<td>3-Bedroom</td>
<td>$1011.25</td>
<td>$1213.50</td>
</tr>
<tr>
<td>4-Bedroom</td>
<td>$1127.50</td>
<td>$1353.00</td>
</tr>
</tbody>
</table>

Source: danter.com

► Building Program

Number of Units, Size, Mix and Rent Schedule
This project will have 82 units. The market/affordable mix
will be 50% according to the following rent schedule:

<table>
<thead>
<tr>
<th>Units</th>
<th>Size</th>
<th>Rent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-bedroom, market</td>
<td>13</td>
<td>715</td>
</tr>
<tr>
<td>2-bedroom, market</td>
<td>20</td>
<td>850</td>
</tr>
<tr>
<td>3-bedroom, market</td>
<td>8</td>
<td>1100</td>
</tr>
<tr>
<td>1-bedroom, affordable</td>
<td>13</td>
<td>715</td>
</tr>
<tr>
<td>2-bedroom, affordable</td>
<td>20</td>
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</tr>
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</table>

Source: market study and danter.com

► Pro Forma & Assumptions
Please see attached appendix for pro forma spreadsheets.

Common Area
A standard 10% of livable square footage has been allotted
to common area.

Parking Spaces
Extensive public transit exists within a 5-minute walking radius. As such, parking limits per zoning requirements are expected to be reduced from 1 to .5 per unit, necessitating 41 parking spaces.

► Land

Land, cost per square foot
The Board of Revision Taxes website was used to
determine the value of the land for the parcel. They quoted
in 2009 a market value of $565,000 which comes to
$23.45/sqft with a lot square footage of 24,625.
Wharton, there is a belief that trees increase neighborhood property values, so extra money has been allotted for additional tree planting. Also, a green roof will be installed. Budgeting in the concept allows for $60,000 in landscaping.

► Permanent Financing

**Interest, Term, Debt-Coverage Ratio and Points**
PNC Bank will be the lender for the permanent mortgage and the bank quoted a rate of 5.75% over a 30 year term. Debt to coverage was 1.3 and points were 2.

► Construction Lending

**Percent Financed**
The PNC LIHTC construction loan program will lend 100%.

**Interest rate**
PNC LIHTC Financing quoted an interest rate of 9%.

**Term**
The term is typically 24 months, but provisions allow for negotiation. My concept predicts 18 months construction.

**Drawdown Factor**
A drawdown factor of .55 is used for this project.

**Fees**
PNC Bank charges fees of .5% to 1% of the hard costs. This project assumes the maximum fee of 1%.

Source: [https://www.pnc.com/webapp/unsec/Requester?resource=/wps/wcm/connect/d777ee004e5c64d8f18ff6d630ad7?MOD=AJPERES&CACHEID=d777ee004e5c64d8f18ff6d630ad7](https://www.pnc.com/webapp/unsec/Requester?resource=/wps/wcm/connect/d777ee004e5c64d8f18ff6d630ad7?MOD=AJPERES&CACHEID=d777ee004e5c64d8f18ff6d630ad7)

► Rents & Incomes

**Rent**
The rent schedule for this project was determined by market studies and tax credit program rental limits. Please see above table.

**Other Income**
This project will generate no other income sources except for the 13 additional parking spaces at $75 per month, for ‘other’ monthly income of $975.

**Rent Inflation Factor**
The market study for this project predicts national inflation to remain constant according to historical trends and therefore the rental inflation factor will be set at 3%.

► Vacancy Rates

Because this project will include a 50% mix of affordable housing, the market study indicates that vacancy rates will be lower than typically seen in a building of this type. Initial vacancy in year one will be 4% and stabilized vacancy will be 2%.

► Expenses

**Utilities, Maintenance and Reserve, Insurance**
Utilities are estimated using data from bestplaces.net for the zip code 19104. Monthly utilities are quoted at $130. With 82 apartments, yearly utilities are estimated at $131,040.

Comparable new construction buildings of this size have yearly maintenance of $50,000, reserves of $35,000 and insurance costs of $30,000.

**Management, Contingency**
Comparable new construction buildings with this level of service will cost $25,000 per year and contingencies should be predicted at $40,000.

**Expense Inflation Factor**
The market study conducted for this project suggests a typical expense inflation factor of 3%.

**As Percentage of Rents**
It was found on IREM that dense urban areas typically experience expenses of 37.5 percent to 43.9 percent of rents. This project’s expenses as a percentage of rents is 40%.

► Tax Info

**Useful Life**
The IRS provides the benchmark for the depreciable building life. For a residential building that useful life is 27.5 years.
Amount of Personal Property
$3,000 per unit x 82 units amounts to personal property of $246,000.

Personal Property Life
The IRS sets personal property depreciable life at 7 years.

Potential Sources for Gap Financing
This project is estimated to need financing of $16,402,283 on development costs of $15,216,586 and faces a gap of $2,446,623.

Sales Cap Rate
I used a cap rate of 7.8%, which was obtained from a special report on Real Capital Analytics. For benchmarking purposes I also found a general, multifamily apartment building cap rate of 6.95% on the RCA website, and considered the advisement of Dr. Guillen from Econsult who said his developer friends suggest a cap rate of 10-12% given the current market situation.

Selling Costs
The industry standard of 6% selling costs is used in this model.

Capital Gains Tax Rate
The IRS has set the capital gains tax rate at 15%

Discount Rate
The discount rate has been set by the developer at 8%.

Syndication Details
Applicable Credit
The applicable credit for this project is 11.7%. The baseline LIHTC Program allows for 9% yearly for 10 years on new unit construction costing more than $3,000 per unit, but since this project is located in a ‘high-cost’ area as defined by HUD, the allowable credit is increased to 130%, providing for 11.7% yearly credits.

Limited Partner Share, Required IRR, Syndication Costs, Annual Ground Lease, Interest on Ground Lease and Years of Tax Credit Pay-in
The structure of deal in this project has determined the levels for these syndication components.

As is common in a deal such as this, the Limited Partner share is 99%. A reasonable IRR for investors interested in a project like this has been set at 14%. Syndication costs stand at $75,000. The annual ground lease is $0 and therefore interest payments will also be zero. The years of Credit Pay-In is 1.

1. The Federal Home Loan Bank (FHLB). This is a partnership of approximately 6,500 financial institutions around the United States. Each year the FHLB is required to grant 10 percent of its profits to help rehabilitate or create affordable housing. Annually, FHLB distributes about $150 million nationally. Awards generally range from $2,000 to $20,000 per unit. If these sources could be secured at the maximum level of $20,000 per unit this would provide $1,640,000 of the approximately $2,500,000 gap in financing. More on the FHLB and its funding programs can be found at www.fhlbanks.com.

2. Commercial Private Banks. Similarly, banks are required by the Community Reinvestment Act to divert a certain amount of their profits to community to meeting the credit needs of the community in which it is based. Given the recent controversy in bank regulation and high profits at some banks in the past year this might prove to be a fruitful area for funding.

3. Community Loan Funds. Although usually a source for predevelopment and construction loans, community loan funds may be convinced to provide a modest grant. Since most, if not all, of a community loan fund’s financing comes from contributions and loan commitments, these funds may be an excellent source for referrals to other public and private grantors.

4. HOME Funds. These funds may be used to help close part or all of the funding gap that remains for a LIHTC-funded project after the sale of tax credits and mortgage financing have been determined. However, the usage of this kind of financing triggers an analysis required of HUD federal regulations Title 24, Sec. 92.250, which can be found here:

The basic idea is that funding must not exceed what is needed to provide affordable housing. It is recommended that PJs coordinate with the LIHTC administering agency to obtain a complete understanding of the financing involved.

See more at:
http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/homefunds/gapfinancing.cfm

5. Special Appropriations. Revenue surpluses in the state may be earmarked for projects such as ours. With the current health of the economy, the state is unlikely at this point to have such surpluses, but should conditions change this may be an innovative method for gap financing.

6. Miscellaneous Federal Programs. Though this project would forego 9% credits (and instead receive 4%) if other federal programs were utilized this is an option.

7. Private investors. This source of financing will be difficult given my inexperience in the development world, but this avenue can produce financing with little of the restrictions found on other government sponsored programs.

The following website was helpful in considering various funding gap financing measures:

http://www.nhi.org/online/issues/104/fundraising.html

Thank you for your time and consideration.