



Memo

To: Bill Neuendorf, Edina Economic Development Manager
From: Nick Anhut, Ehlers & Associates
Date: February 9, 2018
Subject: 70th & France Affordable Housing Assistance

The City of Edina requested that Ehlers review an initial development pro forma from Aeon (the "Developer") from a proposal to construct a \$24.8 million project consisting of 90 units of Mixed-Income multifamily housing. The Developer intends to make an application to Minnesota Housing to seek Low Income Housing Tax Credits (LIHTC) and primary financing this Spring, as well as its zoning application to the City. The Developer has identified a gap in financing of \$6.8 million and is seeking financial assistance the Edina Housing and Redevelopment Authority and Edina Housing Foundation for the affordable project.

We have reviewed the preliminary project financing and two scenarios of proforma assumptions provided by the Developer, and prepared an estimate of the potential Tax Increment the 90-unit project may generate. Both scenarios' development pro forma assumptions were generally reasonable and within industry standards expected for LIHTC projects. This memo focuses on the 9% Tax Credit project which contains greater variety of mixed income units. Below are initial thoughts as the entities consider the request:

1. **Acquisition Costs:** The acquisition and demolition costs of over \$37,000 per unit are high as compared to similar residential projects. High acquisition costs are expected in Edina and have been demonstrated within the immediate area, but are difficult for affordable project rent levels to overcome.
2. **Mixed-Income Rents:** The apartment building includes a mix of studio, one-bedroom, two-bedroom, and three-bedroom units. The market rate rents range from \$1,066/month (\$2.13/sf) for a studio to \$2,125/month (\$1.74/sf) for a three bedroom. The estimates are slightly below recent new apartment developments in the vicinity but appear within market expectations.

The Developer has elected to provide 90% of the apartments (81 units) with rents that are affordable to households at various levels: 30%, 50% and 60% of the area median income (AMI). The income and rent limits along with the proposed distribution are as follows:

Rents by Unit Type				
Type	Market Rate Units	30% AMI Units	50% AMI Units	60% AMI Units
0 BR / SRO	3	2	1	1
1 Bedroom	2	3	4	7
2 Bedroom	2	3	5	24
3 Bedroom	<u>2</u>	<u>2</u>	<u>5</u>	<u>24</u>
Total:	9	10	15	56

Rent Comparison versus 100% Market Rate				
Unit Type	# of Units	Average Unit Market Rate Rent Difference	Per Unit Annual Revenue Difference	Total Annual Revenue Difference
30% AMI	10	(640)	(7,680)	(76,800)
50% AMI	15	(657)	(7,882)	(118,224)
60% AMI	56	(510)	(6,115)	(342,432)
Market Rate	<u>9</u>	<u>0</u>	<u>0</u>	<u>0</u>
Totals:	90	(498)	(5,972)	(537,456)

Per City of Edina's Affordable Housing Policy, new multi-family developments of 20 or more units must provide a minimum of 10% rentable area at 50% affordable rents or 20% at 60% affordable rents. The annual "cost" of a 50% affordable unit is \$7,882 and that of a 60% affordable unit is \$6,115.

The annual revenue difference of \$537,456 reduces the amount of a first mortgage the project can support and contributes to the gap in financing after LIHTC equity and other sources. The supportable mortgage is estimated to be \$8.2 Million with net revenue providing debt service coverage of 115% at MN Housing minimum standards based on a 40-year level amortization at 4.75% interest.

- Tax Increment:** Currently, the property is valued at approximately \$2.7 million and the City's portion of the existing taxes is \$10,308 (assuming preliminary pay 2018 property tax rates). The expected taxable value of the affordable project at completion is \$16.1 million. Minnesota allows a special classification (4d) for qualifying affordable housing units which lowers its tax capacity compared to market rate units. Assuming 90% of units qualify, we estimate that the project could generate \$102,570 of incremental taxes annually which can help offset the gap. TIF assistance is typically provided on a "pay-as-you-go" basis after property taxes are paid by the property. A maximum 21-year TIF cashflow could support up to \$1.3 million in additional mortgage proceeds, reducing the remaining gap to \$5.5 million.
- Other Private Gap Sources:** The project may also fill a portion of the financing gap by deferring a portion of the Developer's Fee (total Fee presented as \$2.0 million or 8.8% of development costs) or by securing a subordinated note payable from any free cashflow after annual operating and financing expenses.
- Other Public Gap Sources:** The HRA's Southdale 2 TIF District has received special legislative authority to pool its TIF funds towards affordable housing. We estimate Southdale 2 TIF Funds could provide up to \$3.54 million in remaining authority to grant

or loan to qualifying projects like the Aeon project. Historically, the HRA has also partnered with the Edina Housing Foundation to provide low interest loans on a case-by-case basis. The project will also seek additional funding this Spring from Hennepin County and/or Metropolitan Council grants.

If the City's HRA and Foundation choose to partner and provide assistance for this project, we recommend further understanding of potential public and private partner contributions toward the affordable project. The HRA's commitment should require revisiting an updated review of the updated project proforma based on general industry standards for development costs; market rate and affordable rents; operating expenses; developer fees; financing criteria; and resulting project cash flow. The detailed analysis will help policy-makers understand to what extent the apartment project demonstrates financial feasibility.

Please contact Nick at 651-697-8507 with any questions.

		AMOUNT (\$)	% of TDC	Per Unit
TOTAL Project Costs		\$24,823,548	100%	275,817
Less:	First Mortgage	-8,204,000	33.0%	91,156
Less:	Tax Credit Equity	-9,399,060	37.9%	104,434
Less:	Misc. Rebates	-357,448	1.4%	3,972
	Gap:	\$6,863,040	27.6%	76,256
Potential:	Deferred Developer Fee	??		
Potential:	Cash Flow Note	??		
Potential:	Public Grants	??		
Potential:	TIF Mortgage	1,300,000	5.2%	14,444
Potential:	Southdale 2 Pooling	??		