

Mitchell-Lama Refinance Redevelopments

Father Finian Sullivan Towers, Yonkers, New York

Steven J. Weiss, Esq., Cannon Heyman & Weiss, LLP
Tim Favaro, Esq., Cannon Heyman & Weiss, LLP

April 4, 2008

I. Background

A. Mitchell-Lama Housing

- i. Housing owned by a limited-profit housing company formed under Article II of the Private Housing Finance Law and supervised by the New York State Division of Housing and Community Renewal (DHCR) or the City of New York Department of Housing Preservation and Development (HPD).
- ii. Mitchell-Lamas generally have state subsidized mortgages held by the New York State Housing Finance Agency, Urban Development Corporation (now Empire State Development Corporation), or the State of New York.
- iii. Real Property Tax exemption is generally available to Mitchell-Lama project under §33 of the Private Housing Finance Law (PHFL).
- iv. Mitchell-Lama projects aided by loans made after May 1, 1959 are entitled to opt out of the program after twenty (20) years by satisfying all outstanding government-assisted mortgages and by following certain procedural requirements set forth in *9 NYCRR Part 1750*.
- v. PHFL §33(1)(a) authorized the local legislative body of a municipality to grant real property tax exemptions to the extent specified in the statute if for so long as the mortgage loans of the company, including any additional mortgage loan the proceeds of which are used primarily for the residential portion of the project are outstanding.
- vi. The enactment of Chapter 389 and 449 of the Laws of 2003 was an effort to provide an incentive to the owners of the privately-owned developments to remain in the Mitchell-Lama program.
- vii. New subdivision (6) to PHFL §33 to provide that:

Any project that received a tax exemption under paragraphs (a), (c) and (d) of subdivision one, and

subdivision four of this section may, upon the expiration of the tax exemption period, be granted an additional tax exemption period of up to fifty years, or until such time as the project is no longer operated under the restrictions and for the purposes set forth in this article, whichever is sooner.

- viii. This required the local legislative body to revisit the exemption.

B. Section 236 Program

- i. Section 236 of the National Housing Act works in conjunction with Mitchell-Lama program.
- ii. Affords a project interest reduction payments (IRP) in addition to a real property tax exemption to preserve affordability.
- iii. Provides IRP in an amount that reduces the effective interest rate on 40 year subsidized mortgage to 1%.
- iv. Section 236 program terminated in 1973.
- v. All 236 mortgages are now eligible to prepay and leave the program.
- vi. Occupancy in 236 Projects restricted to 80% or less of AMI.
- vii. Rents structure has a minimum basic rent and maximum market rent. Generally, tenants are required to pay 30% of adjusted gross income but in no event will this amount be less than the basic rent or greater than the established market rent.
- viii. HUD delegates oversight functions to state agencies.

C. Decoupling of the IRP

- i. Incentive for projects to remain affordable.
- ii. Section 236(e)(2) of the National Housing Act allows an owner to make application to HUD to decouple the IRP from the original mortgage and continue those stream of payments to assist in refinance and redevelopment.
- iii. Section 236(b) of the National Housing Act allows an approved State or local agency Section 236(b) mortgagee to purchase the insured Section 236 mortgage, terminate the FHA insurance, and keeps the Section 236 mortgage intact.
- iv. Application made to HUD pursuant to the requirements enumerated in HUD Notice H 2000-8.
- v. Must maintain housing affordability for the term of the continued assistance plus an additional five years.
- vi. To be eligible for a 236(e)(2) decoupling, a project must currently receiving Section 236 IRP assistance, with FHA insured, HUD-held, or non-recourse public agency mortgages. [HUD Notice H 2000-8, Section 8].
- vii. The eligible mortgagor entities in a 236(e)(2) transaction are: nonprofit mortgagors; builder-seller mortgagors; limited

- distribution mortgagors; and cooperative and investor sponsor mortgagors. [HUD Notice H 2000-8, Section 6].
- viii. In some cases, rent increases may be necessary to meet new debt service requirements in a Section 236 transaction.
 - ix. The owner may request a budget-based rent increase in conjunction with the Section 236(b) or (e) transaction to cover debt service on any new financing (for acquisition, rehab, or equity takeout). In general, the new basic rent cannot exceed the market comparable rent decreased by the value of the IRP subsidy.
 - x. The budget-based rent computation must include an allowance for the owner's return on equity. HUD has calculated this component as (total equity ó paid developer fee) multiplied by 6%.
 - xi. A state or local public agency must perform the regulatory oversight functions required by the IRP contract (including administration of IRP subsidy payments, rent increase processing, physical inspections, and monitoring to ensure owner compliance). [HUD Notice H 2000-8, Section 5].
 - xii. Benefits of decoupling include:
 - a. carry more debt, moderately increase rents, and obtain a lower interest rate on the project mortgage;
 - b. lender will underwrite against project net operating income but also against the continued IRP with low coverage ratios (1.05 or less);and
 - c. projects receiving a project based Section 8 HAP may markup-to-market in lieu of enhanced vouchers and a budget based rent increase.
 - xiii. Project receives a HUD approval letter.

II. Father Finian Sullivan Tower, Yonkers, New York

A. Generally

- i. Father Finian Sullivan Towers (the "Project") located in Yonkers, New York, was originally built in 1975 under the Mitchell-Lama and HUD 236 programs.
- ii. The Project contains 149 one bedroom units and 1 supervisor unit.
- iii. The original mortgage amount on the Project was equal to \$4,550,000 maturing in 2016 with an interest rate of 8.5%, with IRP assistance that reduced the effective rate down to 1%.
- iv. As of September 18, 2006 the following financing was in place:
 - i. \$287,739 HUD Flexible Subsidy loan;
 - ii. \$2,162,215 First Mortgage Loan Serviced by Capmark (sold several times on the secondary market);
 - iii. \$642,161 Second Mortgage from HFA; and
 - iv. \$634,134 Hudson Valley Line of Credit.
- b. Rental Assistance Payment contract covering 60 units in the Project.

- c. Project in need of capital improvements.
- d. Decoupling plan devised whereby tax-exempt bonds would be combined with low-income housing tax credits, a rent increase and enhanced vouchers that would allow a related for-profit partnership to acquire the beneficial interest in the Project, refinance existing debt, provide funds for capital improvements, and allow the seller to contribute acquisition proceeds to related charitable entity to establish a scholarship fund.
- e. Project desired to take advantage of the continued tax exemption under Mitchell-Lama, however, due to local politics opted to enter a PILOT with the local jurisdiction.

B. Scope of Work

- i. Site Work: upgrading the plumbing system, roof exhaust fan replacement, kitchen and bathroom renovation, emergency generator system installation, renovation of the community room, enhanced security system, parking lot restoration, replacement of compactors, landscaping and interior painting.

III. Transaction Structure

A. Legal Structure Issues (see attached chart).

- i. percentage interests relating to syndication;
- ii. Related party purchaser;
- iii. Limited Partner and Special Limited Partner; and

B. Real Estate Issues (see attached chart)

- i. Declaration of Interest and Nominee Agreement;
- ii. Lease of the Mitchell-Lama and the Partnership to the IDA;
- iii. Installment Sale Agreement as a Financing Document;

C. Financing Issues (see attached chart)

- i. 50% Bond Test;
- ii. Promissory note and tax exempt bonds;
- iii. Tax credit structuring, importance of acquisition credits;
- iv. Bond Costs 95/5 limitation and good costs / bad costs; and
- v. IRP Payments to Trustee as a tax credit issue;
- vi. Traunch "A" and Traunch "B"; and
- vii. FHA Insured Mortgage pay-off process;

D. Operating Subsidies

- i. Enhanced Vouchers, not available during construction on non-RAP units.

IV. DHCR Review and Approval Issues

- A. Approval
 - i. DHCR Standards and Procedures for Processing Requests to Refinance by Mitchell-Lama Housing Companies (assuming continuation as a Mitchell-Lama;
 - ii. Approval Letter;
 - iii. DHCR Control of Replacement Reserves in Operating Escrow Fund;
 - iv. Party to the IRP Agreement; and
 - v. 2530 Clearance.

B. Design Approval

C. Credit Determination Role

D. Continued Supervisory Role

V. Attorney General and Supreme Court Approval

- A. Petition to dispose of substantially all the Mitchell-Lama's assets

VI. Relevant Documents

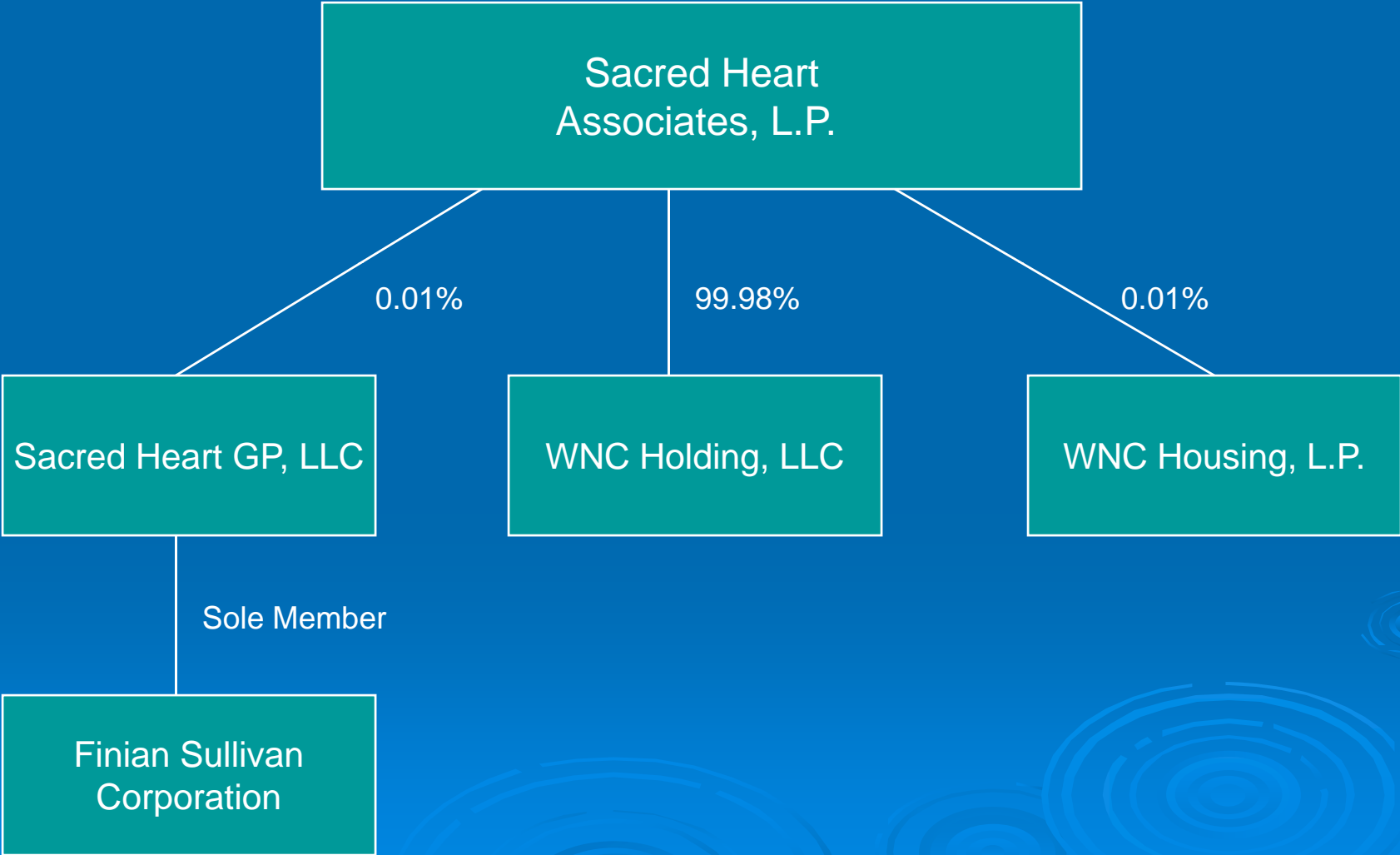
- A. Partnership Agreement ó memorializes the terms and conditions by which the Limited Partner contributes capital to the project and sharing of future revenues.
- B. Declaration of Interest and nominee Agreement ó bifurcates interests in the real property into the nominal fee interest and all beneficial and equitable rights to the property.
- C. Company Lease and Fee Owner Lease ó Conveys the necessary interest in the underlying real estate to the IDA necessary for the project to avail itself of IDA benefits.
- D. Installment Sale Agreement ó Financing document and conveyance document conveyed, by installment sale, the leasehold interest conveyed to the IDA in the Company Lease.
- E. Letter of Credit ó Construction ó Credit enhancement is essential for attracting purchasers of tax exempt bonds. SONYMA will not take construction risk.
- F. SONYMA Commitment ó provides permanent credit enhancement on the bonds.
- G. Trust Indenture ó Between IDA and The Bank of New York, as trustee on behalf of bond purchasers, sets forth the terms of the bonds and flow of funds relating thereto.
- H. IRP Agreement ó Memorializes the terms and condition under which the Interest Reduction Payments will continue to be made to the Project.

- I. Use Agreement ó Regulatory Agreement covering the Project proving that the Project will comply with the regulatory framework of the 236 program until the final IRP payment plus five years.

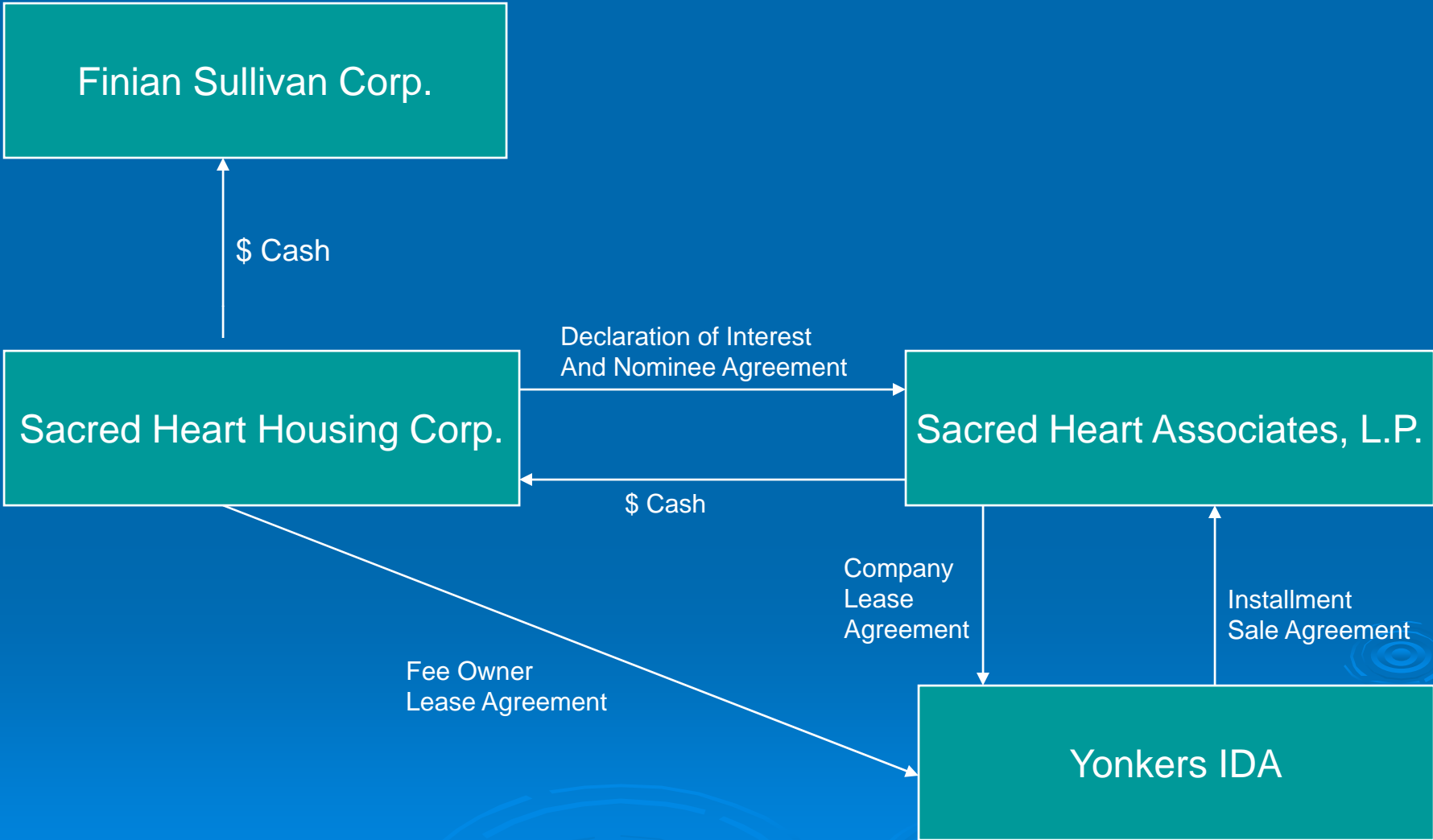
Mitchell-Lama Refinance Redevelopments



Father Finian Sullivan Towers Legal Structure



Father Finian Sullivan Towers Real Estate Structure



Father Finian Sullivan Towers Bond Financing Structure

