Case Study – Seattle

Summary

The Seattle Housing Authority (SHA) owns and operates 5,443 conventional public housing units subsidized by the U.S. Department of Housing and Urban Development and nearly 1,000 additional units for seniors and people with disabilities as part of the Seattle Senior Housing Program. These properties are widely scattered throughout the city in strategically well-placed locations in garden apartment and townhouse communities, as well as 28 high-rise structures. SHA provides affordable housing to more than 27,000 low-income individuals in Seattle. Of these residents, approximately 23,500 have incomes below 30 percent of the Area Median Income (AMI) and the remaining 3,500 residents have incomes between 30 and 80 percent of the AMI. Many residents of SHA housing are elderly or disabled. In 1999 HUD recognized SHA's accomplishments by approving the authority's request to be designated as one of 30 Moving to Work (MTW) Authorities. The authority's MTW status has provided the flexibility needed for SHA leadership to implement significant operational changes that have further improved operating efficiency, the quality of residents' lives, and the livability of public housing.

As a result of a thorough and rigorous 30-year Physical Needs Assessment, the Seattle Housing Authority determined that 21 of the authority's 28 high-rise buildings were in need of significant capital repairs. Most of these buildings were constructed between 1967 and 1971 and in total required $70 million in repairs to windows, façades, and essential building systems. SHA quickly recognized that the size of the investment needed would require use of a Mixed-Finance Modernization approach that included Low Income Housing Tax Credits. Since the 4% LIHTC allocation associated with private activity bonds would only provide half of the required investment, additional bonds authorized under HUD's Capital Fund Financing Program, in addition to other smaller grants and loans, were needed to close the funding gap. This Mixed-Finance Modernization program was then named *homeWorks*.

SHA realized that because of the scope of the work, and the need to meet the "placed-in-service" requirements of the LIHTC program, the work would have to be completed in three phases as indicated in the table below.

Phase	**Buildings**	**Construction**	**LIHTC and Other $**	**CFFP**	Total
1	7	2006-2007	$24,000,000	$12,000,000	$36,000,000
2	7	2008-2009	$28,000,000	$16,000,000	$44,000,000
3	7	20010-2012	$18,000,000	$9,000,000	$27,000,000
Total	**21**		**$70,000,000**	**37,000,000**	**$107,000,000***

*Includes the LIHTC partnerships' purchase of the properties from SHA using financing leases.

Recognizing the immediate needs of Phase 1, SHA obtained HUD approval for its Mixed-Finance Modernization program and a Capital Fund Finance Program bond issuance of $12 million. The CFFP bond is payable over 20 years, with a fixed interest rate of 4.86% and a level of debt service that represents approximately 9.5% of SHA's estimated adjusted annual capital grant. [Note: in a CFFP proposal, the authority needs to adjust its most recent capital grant allocation to account for future removal or the addition of ACC units from its inventory.]

<u>Project Concept - *homeWorks* - Phase I</u>

Capital Needs Planning

The Seattle Housing Authority has adopted an innovative plan for tracking the physical condition of its inventory. Most of this inventory was built between 1939 and 1985 and is now more than 20 years old. The result is an aging portfolio with some functional obsolescence and large, escalating capital needs. To track the status of its units, SHA has developed a Microsoft Access database that includes all of the units in each development and their specific status. Every site manager provides regular updates to this system and performs an annual evaluation to insure its completeness and accuracy. This information allows the Asset Management team to evaluate the relative capital needs of the various properties and focus the use of capital funds where they will be most effective.

The Work

Over the years, SHA maintenance teams observed the deterioration of the galvanized iron water lines used throughout its properties. Whenever possible they replaced any accessible piping with copper lines, but only a complete replacement of the water supply lines would eliminate the problem. Eventually, leaks also caused significant water damage and many units had to be taken off line. However, all of these buildings were otherwise in very good condition and were not candidates for demolition or redevelopment programs such as HOPE VI. Over time, some window replacement and other façade repairs were implemented using local programs to defray the total costs. Some repairs to elevators and other essential building systems were also made on an emergency basis.

Eight high-rise sites were initially identified as needing immediate repairs to their water distribution systems. Architectural and engineering firms were then procured to perform comprehensive evaluations of all of the building systems. The eight sites selected for Phase I of *homeWorks* contain a total of 809 units, of which only 704 benefit from CFFP financing. The eight sites include: Olive Ridge[1]; Harvard Court; Ballard House, Green Lake Plaza; Capitol Park; Lictonwood; Beacon Tower; and International Terrace.

The scope of work includes:

<u>Building</u>

- Full replacement of domestic water supply lines
- Full replacement of domestic hot water boilers
- Upgrades to entrances and common areas, including community rooms and kitchens
- Repairs to the building shell including:
    - Roofing
    - Window caulking

[1] Olive Ridge was excluded from the M-F Mod, because of the modest needs of that site. The needs of Olive Ridge were met exclusively through the annual capital fund, but it was still included in the overall homeWorks revitalization effort.

    - Masonry and brick re-pointing and façade repair
    - New rooftop fans and ventilation systems
- Elevators and elevator controls
- New security systems

Units
- Closet doors
- Laminate shower surrounds
- Kitchens as needed

Ownership Structure

The Seattle Housing Authority formed an affiliated Limited Partnership, High Rise Rehabilitation Phase I Limited Partnership, with the Authority acting as the General Partner. This Partnership then acquired a leasehold interest in the eight scattered-site multi-family locations containing 704 units that make up the Seattle *homeWorks* Apartments.

The regulatory requirements of this transaction required SHA to obtain a Demolition/Disposition approval from HUD in order to permit the lease/purchase of the former public housing sites to an affiliated Limited Partnership. The Partnership, on behalf of its investors, will then rehabilitate, own and operate these units. The parties have also entered into a Regulatory and Operating Agreement that will make the modernized units available to SHA during the lease period as public housing units, in return for a portion of the authority's HUD operating subsidy. SHA, however, retains the option to buy back the property at the end of the 15-year tax credit holding period, at Fair Market Value. Other repurchase options include an early buy-back option if the General Partner's capital account is reduced to a negative value and a Right of First Refusal to purchase the property based upon an offer by an unrelated third party non-profit entity.

Financial Structure

This partnership raised $11,693,117 in investment capital from two funds managed by Boston Capital, based upon the anticipated LIHTC return to the investors. Since this tax credit equity will be paid in over four years, the authority used its independent bonding authority to issue $10.8 million in bonds to serve as a bridge loan, not secured by public housing assets. This bridge loan is secured by a pledge of the LIHTC equity as it is paid into the authority's general fund pursuant to the lease/purchase agreement. This arrangement is typical of a 4% LIHTC transaction and allows the partnership to benefit from the authority's lower cost of borrowing. SHA then raised $12 million from the sale of the CFFP bond that will be loaned to the partnership to fund the rehabilitation costs. A second $10.8 million bond issue, secured by SHA's non-ACC assets, provides long-term financing while an additional $150,000 in MTW Block Grant funds, $100,000 in Energy Rebates, and $127,000 in interest income related to the CFFP bond issue brings the total project funding to $36,070,117.

Considering all public housing funds available during and after construction, there is a nearly 2 to 1 ratio of private funds to public funds. This leverage is achieved through a conventional Mixed-Finance Modernization format using tax credits and CFFP bond proceeds. The authority has also loaned the partnership the monies it receives from the developer fees, and executed lease/purchases of the properties, specially crafted to maximize the tax benefits to the tax credit investor. These structured elements allow SHA to maximize the benefits from this program and maintain its inventory at the highest possible level.

The authority considered the use of 9% credits, but the uncertainty of the competitive process was a significant disincentive to the authority based upon the urgency of the repairs. The chart below shows a simplified example of the Seattle 4% LIHTC and CFFP transaction in comparison to a 9% LIHTC transaction and a straight loan. This shows the relative savings that Seattle achieved in using 4% LIHTC credits.

Comparison of Leveraged to Unleveraged

Seattle CFFP Example

Loan or Bond	**Bond**	**Leverage (9%)**	**Leveraged (4%)**
Amout of Borrowing/Loan	$ 12,000,000	$ 4,132,397	$ 8,630,928
Less:			
Cost of Issuance	$ (249,960)	$ (127,402)	$ (438,710)
Debt Service Reserve	$ (951,514)	$ (327,669)	$ (696,096)
Capitalized Interest	$ (145,800)	$ (50,209)	$ (104,866)
Reserve for Replacement	$ -	$ (161,800)	$ (161,800)
Net Proceeds	$ 10,652,726	$ 3,465,317	$ 7,229,457
Tax Credit Equity	$0	$ 7,474,223	$ 3,200,618
Total Development Costs	$ 10,652,726	$ 10,939,540	$ 10,430,075
Interest Costs over Life of Borrowing	$ 7,030,277	$ 2,420,991	$ 5,290,987
Total Capital Funds Expended	$ 19,030,277	$ 6,553,388	$ 13,921,915
CFP Savings + Additional Development		$ 12,763,702	$ 4,885,710

Construction/Relocation

The Seattle Housing Authority has procured W. A. Clark Construction Company to complete the work in Phase I of the *homeWorks* program. Both the hard and soft construction costs associated with this contract are outlined in the budget below. Special care was taken during the design process to avoid crossing the 50% improvement cost barrier [that is, the total improvements would exceed 50% of the post-rehab value of the property], which would have required additional work to bring the buildings into conformance with all current building code requirements.

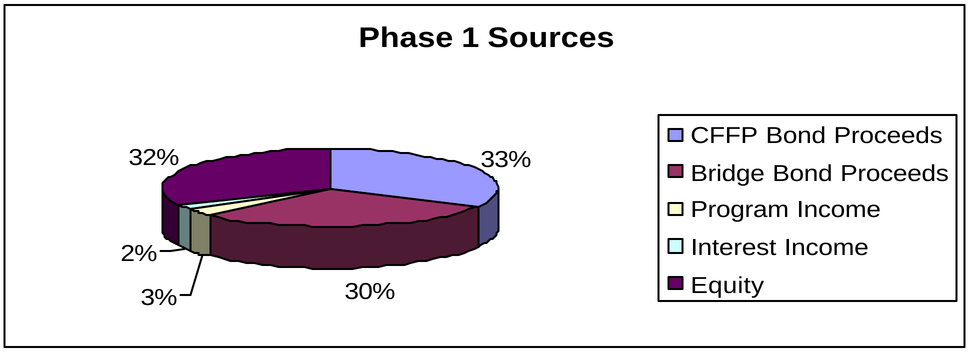
Resident participation during the design and planning stages resulted in a high level of acceptance by the residents.

Construction crews are scheduled to move from unit to unit on each floor until the work is complete. This shortens the construction period for each unit and permits the residents to remain in their units unless the repairs are extensive or involve hazardous materials. During the replacement of water lines, the construction crews can complete the majority of work, including the removal of asbestos pipe insulation, in just a few days before they move on to the next unit. Many of the buildings in Phase I also contain a high percentage of fragile seniors and handicapped residents with limited mobility who also receive special treatment while construction crews are working in their units so that they too can remain in their units. This special effort allows the residents to return to their units after only a few nights in a motel and keeps overall relocation costs to slightly more than $500 per unit, well below the typical amount for similar projects.

Once projects are identified, they are managed by a team made up of SHA staff from every major department. This staff meets on a bi-weekly basis and reviews every aspect of the project, rendering immediate decisions and assigning responsibilities for the completion of various tasks. Changes in the scope of construction work, delays in scheduling, and changes in materials are reviewed not only for their cost implications, but also for their impact on resident relations and how the finished work will be perceived. Careful attention to the needs and concerns of the residents permitted the contractor to perform disruptive work in occupied units with the full cooperation of the residents.

Sources and Uses (Phase 1)

Phase I Sources	
CFFP Bond Proceeds	$ 12,000,000
Bridge Bond Proceeds	$ 10,800,000
Program Income	$ 1,200,000
Interest Income	$ 858,592
Equity	$ 11,676,400
Total Sources	**$ 36,534,992**
Uses	
Acquisition	$ 11,434,750
Construction/Rehab	$ 17,133,857
A/E and Other Fees	$ 1,802,800
Interim Costs (insurance, construction interest, etc.)	$ 1,625,196
Permanent Financing Costs	$ 332,985
Financing Soft Costs (Market Study, Appraisal, LIHTC Fees, Etc.)	$ 306,570
Relocation	$ 400,000
Developer Fee	$ 1,900,000
Financial Consultant Fees	$ 130,000
Operatiing Reserves	$ 1,468,834
Total Expenses	**$ 36,534,992**



Phase I Conclusion
Phase I rehabilitation is 90% complete. All the buildings were placed in service on January 1, 2007. The SHA did not spend the contingency for unforeseen construction items and as a result, the SHA has been able to add backup generators to the buildings without generators and upgrade capacity for the buildings with pre-existing generators. This became particularly important after some outages experienced in December 2006.

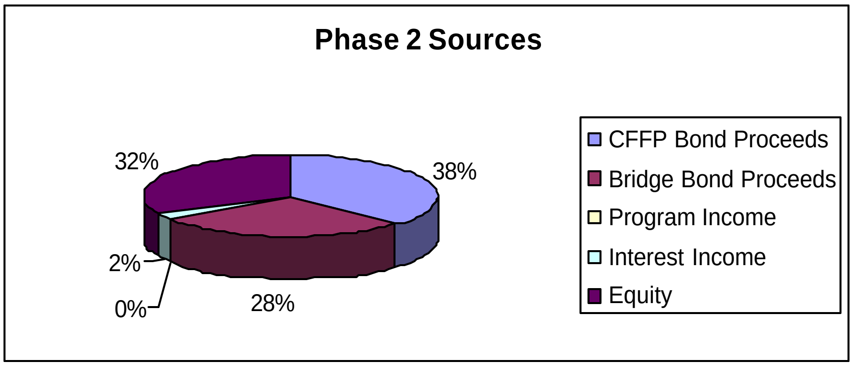
Phase II Overview

Phase II began rehabilitation in February 2007 in three buildings – Cedarvale House, Cal-Mor Circle, and Lake City House. Work on Queen Anne Heights will begin later in May. The work consists of the rehabilitation of 21 of the 28 high-rise public housing buildings over a six year period. The project is broken into three phases with each phase containing seven buildings. The second phase of the project mirrors Phase 1. SHA is performing the same scope of work in each of the buildings and will be using the same contractors , design team, lawyers, financial advisors, underwriters and bond insurers. The SHA will be using private activity bonds and four percent tax credits to finance the improvements. The second phase of the project will have a maximum debt service payment amount of $1,206,225.00 and the second phase payment is 11.49 % of the current Capital Fund allocation. The combined phase I and II payments will equal 20.43 %.

Sources and Uses (Phase 2)

Phase II Sources		
CFFP Bond Proceeds	$	16,051,551
Bridge Bond Proceeds	$	12,000,000
Program Income	$	-
Interest Income	$	1,053,737
Equity	$	13,812,289
Total Sources	$	42,917,577
Uses		
Acquisition	$	12,130,203
Construction/Rehab	$	21,837,234
A/E and Other Fees	$	2,320,874

Interim Costs (insurance, construction interest, etc.)	$ 1,998,500
Permanent Financing Costs	$ 331,995
Financing Soft Costs (Market Study, Appraisal, LIHTC Fees, Etc.)	$ 343,464
Relocation	$ 207,000
Developer Fee	$ 2,000,000
Financial Consultant Fees	$ 110,000
Operatiing Reserves	$ 1,638,307
Total Expenses	$ 42,917,577



Phase III Projections

Phase III is still in the planning stages and it is uncertain as to when SHA will undertake this phase and whether their may be some adjustments. The chart below is based upon estimates only.

Sources	Phase III - Est.
CFFP Bond Proceeds	$ 11,000,000
Bridge Bond Proceeds	$ 10,000,000
Program Income	$ 1,500,000
Interest Income	$ 1,381,896
Equity	$ 11,413,341
Total Sources	$ 35,295,237
Uses	
Acquisition	$ 11,294,074
Construction/Rehab	$ 17,261,210
A/E and Other Fees	$ 1,871,900
Interim Costs (insurance, construction interest, etc.)	$ 1,689,396
Permanent Financing Co	$ 282,650
Financing Soft Costs (Market Study, Appraisal, LIHTC Fees, Etc.)	$ 297,647
Relocation	$ 200,000
Developer Fee	$ 1,000,000
Financial Consultant Fee	$ 60,000
Operatiing Reserves	$ 1,338,360
Total Expenses	$ 35,295,237

Lessons Learned

SHA noted that the 24/48 month window for commitment and expenditure of funds is challenging and has penalties that represent a risk for the authority and the investors and therefore must be managed carefully. In the ninth month of construction the project is three months ahead of schedule. They also noted that the extra cost and effort associated with creating both acquisition and rehabilitation (4%) credits increased the leverage to 4:1 at an estimated cost of $200,000 in additional transaction fees.

Although the MTW designation seemed to expedite some of the approval process times and made it easier to coordinate the various elements of the transaction, the planning and approval processes and matching the federal with the state deadlines made the task extremely challenging. An expedited Demolition/Disposition process, a streamlined OGC review, a regulatory or legislative change on the determination of DOFA, more standardized CFFP forms and/or additional technical assistance would also have helped make the process easier and faster.

Some of the Best Practices employed by the Seattle Housing Authority include:

- The use of a project committee with representatives from all of the departments that have a role in this project that meets weekly to discuss the progress of the work, the

schedule of upcoming activities and any open issues that must be resolved immediately.
- Resident meetings and involvement in the early planning stages of the work and throughout the entire process.
- On-site construction managers who work closely with the contractor to insure timely notice to residents of upcoming work.
- Extensive efforts to minimize resident inconvenience and to allow residents to remain in their units while construction work is ongoing.
- Creation and use of a capital needs tracking database.

Partners

Public Housing Authority	Housing Authority of the City of Seattle
State Government	Washington State Housing Finance Commission
Owner	High Rise Rehabilitation Phase I Limited Partnership
Developer (under contract)	Housing Authority of the City of Seattle
Property Manager	Housing Authority of the City of Seattle
LIHTC Equity Investor	Boston Capital
Bridge Bond Provider	Bank of America
General Contractor	W G Clark Construction Company
Bond Counsel and Partnership Counsel	Foster, Pepper & Shefelman PLLC
HUD and Partnership Counsel	Ballard Spahr Andrews & Ingersoll, LLP
Financial Advisor	CSG Advisors Incorporated
Underwriter	RBC Dain Rauscher Inc.
Underwriter's Counsel	Kutak Rock LLP
Rating Agency	Standard & Poor's Ratings Services
Trustee	J. P. Morgan Trust Company, National Association (now Bank of New York)

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