RAD CASE STUDY

SPOKANE HOUSING AUTHORITY

The Spokane Housing Authority (SHA) serves Spokane, Lincoln, Pend Oreille, Stevens, Ferry, and Whitman counties in Washington State. SHA has completed its RAD portfolio conversion of 125 public housing units to Section 8 project-based assistance. SHA is working on selling its scattered site inventory to use the proceeds to develop over 250 units of affordable housing. SHA annually provides housing assistance to over 5,500 families of low income through a combination of tenant-based rental assistance, project-based rental assistance, SHA-managed apartment communities, and scattered-site housing.

We talked with Pam Tietz, Executive Director of the Spokane Housing Authority, regarding The Parsons property. This interview has been lightly edited for clarity.

What brought you to the PHA? What were your goals when arriving?

Having worked at small and mid-size PHAs, the opportunity to lead a large PHA was just too good to pass up.

SHA provided the considerable challenge of creating a plan to transform a stereotypical housing authority with limited reserves and programming into an innovative and progressive housing provider; a provider focused on meeting community needs ranging from providing options for those experiencing homelessness to helping those ready for homeownership. It was also critically important to strengthen our balance sheet and control the ongoing risk of SHA's property portfolio by repositioning SHA's real estate assets. Since 2013, we have successfully helped to create more than 500 permanent supportive housing units with non-profit partners, created two new statewide rental assistance programs, and recapitalized and repositioned SHA's entire real estate portfolio. This has taken the agency from a 2013-14 negative unrestricted net position to $77 million in unrestricted net position today.

What were your goals for this particular property? What were the long- standing issues with this property? Physical, Occupancy Rates, and Financial?

The Parsons was originally built as a hotel in the early 1900s and then rehabilitated in the 1980s. Occupancy rates were always close to 100% for the property; however, the future financial risk of the physical condition of the property was a major concern with limited available public housing capital funds and the inability to accumulate funds for several years to tackle large capital projects.

How did you hear about RAD? What convinced you it was time to move forward with RAD for this property?

News about RAD is widespread in our industry. Most PHAs were looking for a creative and innovative way to prolong the life of their aging public housing portfolios. As Executive Director at the Peninsula Housing Authority (PHA) back in 2013, we explored RAD as an option for our aging portfolio. At that time, we determined RAD to be financially infeasible due to the RAD rent levels and obsolete condition of the structures at PHA. At Spokane Housing Authority, the analysis reflected a much different picture. SHA's considerable real estate assets, combined with a different rental revenue picture made the decision to use RAD relatively easy.

Interior Rehabilitation Results

You decided you wanted to reposition your property using RAD, what other elements were in your strategy to recapitalize your property?

SHA initially did an agency-wide analysis of our real estate portfolio rather than just looking at our public housing properties. This strategy was key to assess our options, identify risk and provide direction as to our final development strategy. Our assessment included the following specific guiding principles:

- Preserve and enhance existing physical housing stock by addressing deferred maintenance and critical life safety issues.
- Stabilize the project's physical and financial hurdles to ensure that an acceptable living environment was maintained for the residents.
- Minimize SHA's long-term capital needs liability.
- Maximize utilization of existing real estate assets to create development, acquisition or preservation opportunities; or to increase SHA's liquidity.
- Solve debt uncertainty by repaying the existing private indebtedness and public funder debt with a longer-term, lower interest rate facility.
- If possible, create an opportunity for both cash lump sum payments to the Authority and/or a long-term annuity through distributable cash flow in order the maximize SHA's ability to develop new affordable housing for the community.

The repositioning plan looked at a sampling of specific market data, typical development assumptions and basic historic property information to form a general opinion of feasibility. The specific guidance in SHA's plan was based on an analysis considering the tenant mix, historic operations, regulatory agreements, basic equity and debt underwriting, general development cost assumptions, current financing obligations, and expected renovation needs based on the PCNAs.

Ultimately, our repositioning strategy included a portfolio RAD conversion, including the Parsons and our scattered site Public Housing.

Have you dealt with mixed finance multifamily transactions before this project? What were the steps taken to organize your funding sources (in addition to RAD)?

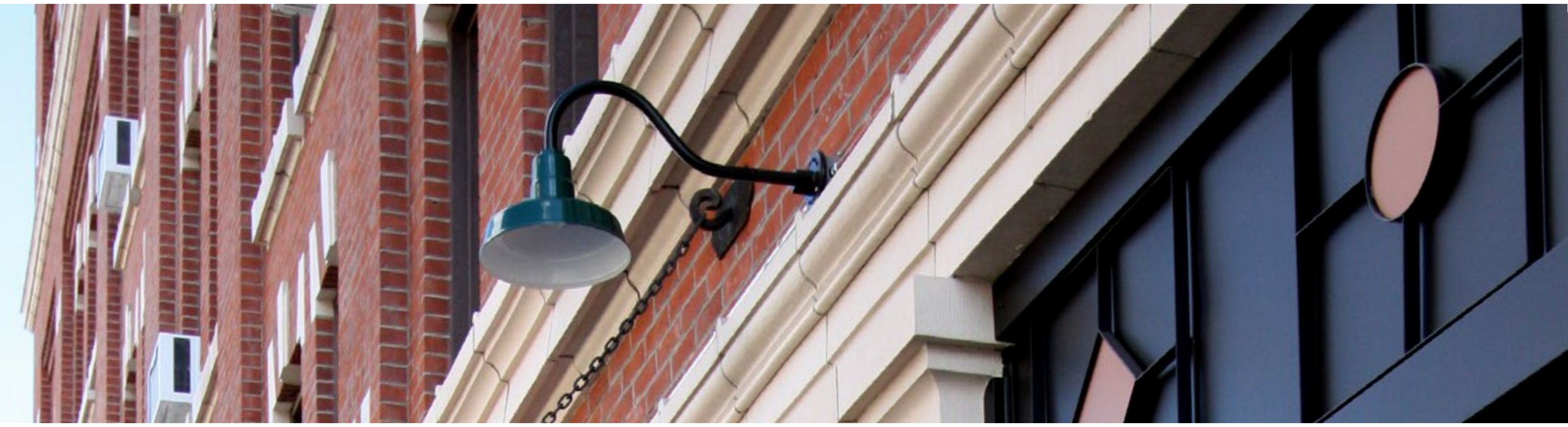
SHA had not dealt with a mixed finance multifamily transaction related to Public Housing, however had substantial experience with developing tax credit projects.

JH Brawner & Co., as financial consultant on SHA's portfolio repositioning plan, assisted SHA in developing project feasibility models to include the Parsons. The process began by performing an initial inspection of the Parsons in order to estimate immediate capital needs that must be addressed during the rehabilitation. Later a formal Physical Capital Needs Assessment (PCNA) was completed to fully identify current and future capital needs and inform the final project scope. Operating proformas were compiled utilizing RAD rents and existing per unit costs to determine cash flow available to leverage hard debt on the project. SHA then issued a request for proposals for both tax credit investors and hard debt lenders and carefully evaluated each proposal for both pricing, terms, and negotiable items such as required reserves and covenants for the best possible outcome for the project. SHA was fortunate that the Parsons did not have any existing hard debt, and appraisals indicated substantial existing equity was available to loan back into the project, eliminating the need for additional project sources beyond tax credit equity, hard debt, and sponsor related soft debt.

Who was part of your team to complete the conversion (consultants, local developers)? What steps did you take to form your team?

SHA contracted with JH Brawner & Co. to provide its portfolio analysis, financial feasibility and construction management for both RAD and non-RAD transactions. JH Brawner & Co was with SHA from initial project concept through construction. Their expertise was key in guiding the SHA team through a financing strategy that addressed numerous conditions, both fiscal and intangible, that helped shape the overall financial impact on the agency long-term.

SHA utilized a Request for Qualifications process to procure architectural/engineering services, a general contractor/contract management (GCCM), audit services related to the transactions, bond, HUD RAD, and tax credit legal counsel, and a Request for Proposal process for tax credit equity investor and construction/permanent lender.



What challenges did you need to overcome to complete the property conversion?

Using the GCCM method, the team's approach was a room-by-room analysis of conditions that led to a detailed understanding of what improvements would be made. Not all units required the same renovations, however this approach led us to a very clear understanding of the budget required to do the conversion. The biggest challenge was performing the renovations while the structure was occupied. This required extensive communication early on with tenants and establishing acceptable paths to renovation for the contractor and subcontractors. Our entire team was very hands on and this helped the project succeed.

Please describe how the property is performing now. Physical, Occupancy rates, Financial? Good DSCR?

The Parsons is financially performing extremely well after its conversion with an average occupancy of 98% and a steady debt service coverage ratio of 2.30. The property on average generates $50K - $70K in cash flow and will have fully paid its deferred developer fee loan by the end of 2020. Capital Replacement Reserves are fully funded as per lender/investor requirements and are expected to be sufficient to cover future capital needs.

How is on-site staffing managed?

SHA provides the property management for its portfolio. Both management and maintenance staff assigned to the Parsons are shared with other SHA properties located in downtown Spokane. By allocating staff between properties, SHA is better-able to hire quality full-time staff.

What comments have you received from tenants before & after the conversion?

Before the conversion tenants were most concerned about:

- The rent staying affordable.
- Being able to stay or return to their same units.
- How the rehabilitation work might affect them and for how long.

During or after the conversion tenants have expressed that:

- They are relieved that they are able to continue to live in a place where the rent is affordable.
- It was difficult to be out of their units during the day during an occupied rehabilitation but grateful the community spaces were available for them during this time.
- They have appreciation for new cabinets, carpet and fixtures and the upgrades to the common spaces.

What would you say to Executive Directors, other PHA senior staff, and Board members that are considering RAD or other public housing repositioning methods? Do you have any particular advice you would like to share?

For SHA, operating the Public Housing program with just 125 total Public Housing units just did not make a great deal of sense. By completing our RAD conversion, we have one less set of regulatory hoops to jump through. By focusing our real estate assets in the tax credit/bond arena, we have streamlined our regulatory and financial reporting environment considerably. In addition, by the end of 2020, by choosing the option to transfer assistance and dispose our 75 scattered site Public Housing units, SHA will accumulate approximately $13 million in sales proceeds to be used for future development. The end result will be transforming 125 aging Public Housing units into 50 updated project-based units and 250+ other affordable housing units for our community, a net increase of 275+ units.

I would also like to point out that HUD RAD staff now have a broad set of experiences guiding PHAs through the conversion process. We have found the HUD Office of Recapitalization to be flexible, innovative and dependable. SHA's journey through a RAD portfolio conversion was certainly not a walk in the park; however, if you take an organized approach and listen to the guidance provided by your transaction manager, it is definitely worth the effort.

What are current and future goals for your PHA? Do you expect to complete more public housing repositioning?

I am pleased to say that SHA has completed not only its Public Housing repositioning, but the repositioning of 96% of our real estate portfolio identified in our original portfolio analysis.

Next on our agenda is to complete the sale of scattered site units removed from our public housing inventory and look for development opportunities to use the proceeds to develop 250+ new affordable housing units.