PARTNERS FOR
HOUSING SOLUTIONS LLC

May 5, 2015

Sally Stang, Director
Housing & Community Development Department
City of Tucson
310 N. Commerce Park Loop
P.O. Box 27210
Tucson, AZ 85726-7210

Re: Downtown Motor Apartments, Tucson, AZ

Dear Ms. Stang:

The Downtown Motor Apartments (the "Project") was awarded a 2014 allocation of Federal Low-Income Housing Tax Credits ("LIHTC") by the Arizona Department of Housing (the "ADOH"). This allocation was based on the Project's score received from the ADOH through its competitive scoring process as outlined in the 2014 Qualified Allocation Plan (the "2014 QAP"). At the request of the City of Tucson, I am providing my opinion about the financial feasibility of the Project if the number of residential units were reduced to 19, and the effect of any unit reduction to the ADOH's allocation and their determination of financial feasibility.

In order to evaluate the financial feasibility, a project alternative or model ("Model") was provided by the Owner that included the number of units, projected rental schedule, projected revenue and operating expenses, and a development budget. This Model deviates from the approved LIHTC Project and illustrates a proposed rehabilitation project with only 19 residential units.

Reducing the number of Project units would be considered a significant change to the original project description as submitted to the ADOH during the 2014 LIHTC application process and, therefore, would be deemed a "Complex Material Change" by the ADOH. Any Complex Material Change requires the ADOH's written approval (see page 66-68, 2014 QAP). Failure to obtain this approval may result in the recapture or reduction of all or a portion of the allocation of LIHTCs.

The ensuing comments and analysis are only to determine if the Model would be considered financially feasible by the ADOH. In completing this analysis, some of the Owner's assumptions have been revised to correlate with the ADOH Underwriting Standards as stated in the 2014 QAP.

In an effort to facilitate understanding of the ADOH's underwriting process, I have utilized some of the pages from the ADOH's 2014 Form 3, and filled in only the necessary information (see attached forms).

1. Page 1 of Form 3. Identification of the proposed project and type of project (Acquisition/Rehabilitation).

2. Rental Analysis. Competitive scoring points were given to the Project because the Developer committed to setting aside units that target households considered Very Low Income and below. In this Model, the original percentages are used for targeting of 40% of the Area Median Income ("AMI") households and 50% of AMI households. These percentages equate to the following unit mix:

7 units (37% of all units) set-aside for households at or below 40% of AMI;
9 units (47% of all units) set-aside for households at or below 50% of AMI.

In March 2015, HUD increased the imputed incomes and allowable rental limits. These most current limits were used in the pro forma cash flow analysis for the Model project. The ADOH will also use the most current rents and income limits during their final underwriting process.

ADOH allows an additional $20 per month per unit to be included in the project revenue. This additional income is not included in unit rental amounts. The Model pro forma includes this additional income. Additionally, the ADOH will allow a maximum 10% as a vacancy/loss provision from rental income. The Model reflects a 7% vacancy/loss provision, which is within ADOH guidelines.

Results: The projected first year Gross Annual Income for the Model project is anticipated to be $113,180.

3. Page 5 of Form 3 - Annual Operating Costs.

The ADOH requires, at a minimum, the projected operating expenses are $4,500 per unit per year. THIS MIMIMUM DOES NOT INCLUDE TENANT UTILITIES THAT ARE PAID BY THE OWNER. The Model indicates $6,493 in operating expenses per unit per year.

To determine the cost of tenant utilities paid by the Owner, the City of Tucson, Section 8 Program, 2015 Utility Allowance Schedule was utilized. The weighted average per unit of owner paid tenant utilities equates to $156.89 per unit per month. Using this average, multiplied by 12 months equals an additional expense to the owner of $1,882.68 per unit per year. The annual per unit operating expenses are therefore adjusted to $6,382.68.

$4,500.00	ADOH Underwriting Standards minimum per unit per year
$1,882.68	Owner paid tenant utilities per unit per year
$6,382.68 ========	Anticipated operating expenses per unit per year
$6,493.00 ========	Owner projected operating expenses per unit per year for Model project. Projection is within ADOH guidelines.

Annual Replacement Reserve per unit is $350 x 19 units = $6,650. Replacement Reserve amount satisfies ADOH 2014 Underwriting Standards.

4. Development Budget. Costs reflected in the Development Budget have been modified from the Owner's projections. Categories revised include:

a. Acquisition Cost was reduced to reflect land value only (per purchase and sale agreement).
b. Syndication Cost were increased to cover anticipated and usual organizational costs.
c. Developer Fee was increased per ADOH formula.
d. Total Development Cost is $4,097,545. Total eligible basis (9% and 4% combined) is $2,919,845,with Total Annual Tax Credits of $281,289.

5. Page 6 of Form 3 - Sources and Uses of Funds.

a. The Model project would be eligible for $281,289 in annual LHITC that would generate $2,226,964 in equity. This assumes current 7.5% applicable rate; $.87 pricing per credit. Credit pricing was obtained from a Syndicator and reflects current market conditions. The Syndicator also disclosed that they would probably not participate in the Model project because the number of units would render the project "challenging" and questioned how supportive services would be covered even if the project receives rental assistance.

b. ADOH HOME loan in the amount of $750,000. Assumes 2% interest only payments with any outstanding interest and principal deferred to note maturity.

c. City of Tucson, HOME funds. Assumes 2% interest only payments with any outstanding interest and principal deferred to note maturity. City of Tucson HOME loan amount $600,000.

d. Permanent debt in the amount of $300,581; 5.5% interest, fully amortized over 30 years, term 18 years. Annual payment of $20,480.

6. 15-Year Cash Flow Proforma.

ADOH Underwriting Standards requires all operating costs, including replacement reserves, increase at 3% per year during the Compliance Period. Additionally, revenue must increase at a rate of 2% annually.

Gross Annual Income is $113,810 less Total Operating Expenses (including Replacement Reserves) of $130,020, renders a Net Operating Deficit of $16,210 after the first year of operations. This deficit is BEFORE any debt service on the permanent loan, the ADOH HOME loan, the City of Tucson HOME loan, payment of supportive services, or Asset Management Fees.

The Total Cash Flow **DEFICIT** after FIRST YEAR of operations is $81,190.

CONCLUSION: With a first year cash flow deficit of $81,190, the Model project is not feasible and in all likelihood would not be approved by the ADOH for the LIHTC Program.

Additionally, equity (from LIHTC) and ADOH HOME funds represents 78% of the total development costs. If these sources of funds were eliminated, even if the Model project received market rate rents for its residential units, the project would not cash flow (would not be financially feasible).

Naturally, my comments and conclusions are my opinions and are not a determination by the ADOH. My comments are based on my past experience as the Underwriting Manager and Risk Assessment Officer for the ADOH with the LIHTC and HOME Programs. I was also the person responsible for developing the Underwriting Standards in the 2013 QAP. Most of those standards have carried forth to the 2014 and 2015 QAPs.

Please contact the undersigned with any questions or further explanation of comments in this analysis.

Sincerely,

PARTNERS FOR HOUSING SOLUTIONS

Julie Culver

Julie Culver, President

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