



NEW YORK CITY  
HOUSING DEVELOPMENT  
CORPORATION

## MEMORANDUM

**To:** The Chairperson and Members

**From:** Eric Enderlin *EE*  
President

**Date:** May 29, 2018

**Subject:** HDC Neighborhood Pillars Loan Program & New York City Acquisition Fund LLC (NYCAF) Senior Term Loan

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I am pleased to recommend two proposals related to the Mayor's Neighborhood Pillars Program ("NPP") of the Housing New York 2.0 Plan, an effort by the Corporation and the New York City Department of Housing Preservation and Development ("HPD") to aid in the acquisition and moderate rehabilitation of multifamily buildings of fewer than approximately 50 residential units that have proved difficult to finance under existing HPD and HDC financing programs. Specifically, the Members are requested to authorize the following:

1. The use of the Corporation's unrestricted reserves to make certain loans, described herein, in an aggregate amount not expected to exceed \$100,000,000 for the HDC Neighborhood Pillars Loan Program ("NPLP") to provide secured senior financing coupled with subordinate debt originated by the Corporation and funded with grants from HPD for the acquisition and moderate rehabilitation of existing affordable buildings that have received no previous City investment.
2. The use of the Corporation's unrestricted reserves to make an interest-only loan to the New York City Acquisition Fund LLC ("NYCAF") in an amount not to exceed \$15 million (the "Senior Term Loan") in order to facilitate an increase in the volume of loans generated by NYCAF.

### Background

The Mayor has recently announced the Housing New York 2.0 Plan, an expansion on the previous plan that aims to create or preserve an additional 100,000 affordable units by 2026 through various initiatives. The Plan announced that HPD's Neighborhood Pillars Program would serve 1,000 units annually and be designed to respond to surging demand for multifamily apartment buildings that threaten to greatly reduce the number of affordable units that occur

outside of current city funding programs. Market changes have led to aggressive real estate speculation in rent-stabilized buildings, including those smaller than 50 units that are difficult to finance with existing HPD or HDC loan programs. The Neighborhood Pillars Program works to respond to these market developments by creating a coordinated approach that supports non-profit and mission-driven organizations in the acquisition of existing buildings and preservation of affordability. Specifically, the NPP would aid qualified organizations in the acquisition/rehabilitation of eligible buildings by offering tools during each of the three distinct stages of an acquisition/rehabilitation project: 1) Predevelopment, 2) Acquisition, and 3) Rehabilitation.

- 1) The NPP tools during the predevelopment stage will require no HDC involvement, and are expected to include a \$10-12 million revolving equity fund that is expected to be administered by a third party that would also be contracted by the City to provide technical assistance to eligible organizations for all stages of the acquisition process. The equity fund is expected to provide nonprofits with funds that will assist in paying for down payments on acquisition contracts and pre-acquisition costs involved in acquisition due diligence and in the securing of an acquisition loan from the NYCAF.
- 2) During the acquisition stage, the City proposes to use the existing NYCAF in order to finance the acquisition of a significant proportion of the units served by NPP. It is expected that in order to meet this increased demand the NYCAF will need to roughly double from its current size to \$275 million. As described in further detail below, the Corporation proposes to bolster this expansion by providing a Senior Term Loan to NYCAF that is not to exceed \$15 million for a term of up to 5 years.
- 3) Lastly, in order to finance the rehabilitation and stabilization of eligible buildings, the City proposes to create a Neighborhood Pillars Loan Program further described below that combines low-interest loans from HPD, and tax exemptions, with construction and permanent financing from eligible lenders, including HDC and CPC.

#### New York City Acquisition Fund LLC (NYCAF)

The NYCAF, which was created in 2006, offers acquisition, predevelopment and moderate rehabilitation loans to experienced, for-profit and not-for-profit real estate developers of affordable, supportive, and mixed income rental housing in the five boroughs of New York City. Its members are Enterprise Community Partners (50%) and the Local Initiatives Support Corporation (50%), and the Fund has been managed by Forsyth Street Advisors since its inception. Made possible through a partnership between the City of New York, major philanthropic foundations, and New York's public and private investment groups, the NYCAF provides loans at capital advance rates of up to 130% loan-to-value for non-profit borrowers with loan terms of up to three years and limited recourse.

#### Neighborhood Pillars Loan Program

The Members are being asked to authorize the making of loans, in an aggregate amount not expected to exceed \$100,000,000, to projects currently outside of the Corporation's portfolio and in an individual loan amount less than \$25,000,000. All, or a portion, of the permanent loans may be initially funded with the unrestricted funds of the Corporation and would be secured by REMIC, SONYMA, or HUD, as determined at the time of loan closing.

The terms of the Neighborhood Pillars Loan Program are consistent with the Corporation's conservative underwriting standards as detailed in the attached Neighborhood Pillars Loan Program Term Sheet (as approved and/or amended by the Corporation's Credit Committee). All loans will require the Corporation's Credit Committee approval. Any loans greater than or equal to \$25,000,000 would be presented to the Members for authorization.

HDC's Neighborhood Pillars Loan Program combines a secured HDC first mortgage with a subordinate mortgage originated by the Corporation and funded by HPD to finance the preservation of existing multifamily apartments that do not currently have regulatory agreements and either are rent-stabilized or are willing to restrict rents going forward. Projects may have a range of affordability tiers depending on the existing rent levels at an eligible project. For HPD projects that close with an alternative senior lender such as CPC, the Corporation's involvement would be as a conduit lender to originate the subordinate mortgage loan that is funded with money granted by HPD, pursuant to conduit lending authorization from the Members in November, 2013.

In the interest of establishing conservative and transparent terms, this memorandum proposes a \$100,000,000 limit on the loan volume delivered under NPLP. Under this proposal, the Corporation's staff would be required to seek additional loan authority from the Members to originate and deliver conforming loans in an aggregate amount that exceeds \$100,000,000. For further transparency, the Corporation's Audit Committee will be notified of the number of loan closings, as well as the total volume of originations made under the Neighborhood Pillars Loan Program annually at the end of Corporation's fiscal year.

### Risks and Risk Mitigation

The primary risks associated with the Neighborhood Pillars Loan Program are construction risk and the risk of nonpayment of debt service. These risks and their mitigants are discussed below.

#### *Construction Risk*

Loans closed under the NPLP are expected to be primarily funding acquisition costs of stabilized assets and to address minor or moderate rehabilitation needs that will not typically require a separate construction period. Scopes will be determined in consultation with a mandatory Integrated Physical Needs Assessment (IPNA) from a firm that is on HDC's existing prequalified list of IPNA providers. All projects must comply with HPD's Master Guide Specifications for Rehabilitation Projects and Scope of Work (July 2014). Projects that require a construction period will receive enhancement via a stand-by letter of credit from a bank acceptable to HDC or, if approved by the Corporation's Credit Committee, be self-enhanced by the Corporation for a fee. All contractors will be required to secure either a 100% Payment and Performance Bond or a Letter of Credit equivalent to 10% of hard costs plus contingency.

#### *Debt Service Repayment*

Projects that have completed construction and reached stabilization are expected to have permanent mortgages enhanced by REMIC, SONYMA, or HUD depending on the specifics of a given project. Because vacancies have a disproportionate effect on buildings with less than 50

units, the NPLP program will have a standard capitalized operating reserve held at HDC in an amount equal to or greater than six months of expenses and debt service on all loans.

### Fees

The Corporation, at its discretion, would receive an upfront fee equal to 1% of the HDC senior loan amount and a cost of issuance fee as determined at the time of loan closing. For projects without a letter of credit, the Corporation may charge a construction monitoring fee of \$2,500-\$5,000 per month based on the total number of units and buildings, as well as a fee to cover HDC's enhancement of the construction loan.

### **NYCAF Senior Term Loan**

#### Economics

In support of the Mayor's Neighborhood Pillars Program goal of doubling the size of the NYCAF to \$275 million, the Corporation proposes to make an interest-only Senior Term Loan to the New York City Acquisition Fund LLC ("NYCAF") not to exceed \$15 million for a term of up to 5 years, which may be drawn periodically during the first 24 months. It is expected that the Senior Term Loan will bear an interest rate between 0.5% and 1% over the 5-year Treasury, which was 2.90% as of May 21, 2018. Principal repayment may occur at any time and is expected to occur over a two-year period to reflect the timing of the NYCAF's loan portfolio repayments.

The NYCAF is expected to use the Senior Term Loan proceeds in combination with other NYCAF funds to make unsecured loans to borrowers for acquisition and pre-development costs for projects that are simultaneously receiving secured financing for acquisition and pre-development costs. Together the Senior Term Loan proceeds comprise up to 35% of each individual project loan. Project loans fund acquisition and predevelopment costs, and are made to for-profit and not-for-profit developers seeking to create or preserve existing affordable or supportive multi-family rental housing in New York City. Acquisition and pre-development project loans are expected to be repaid by various construction and permanent financing sources including the Neighborhood Pillars Loan Program.

#### Risk Mitigants

The risk to the Corporation of the Senior Term Loan is default in repayment by NYCAF. The risk mitigation stems from the superior performance of the NYCAF and the senior position of the Senior Term Loan in relation to the other funds at NYCAF, as well as fund covenants and rigorous underwriting standards for individual deals. The NYCAF has a historical default rate of 0.8%. HDC holds a seat on the NYCAF Credit Committee and reviews all loan proposals. Senior Term Lenders to the Fund hold a senior position secured by the New York City Acquisition Fund LLC and its assets (but not by collateral that secures the Fund's project loans). There are currently three Senior Term loans to NYCAF with commitments totaling \$35 million, at terms varying from 2, 3, and 5 years. Additional subordinate funds include \$11 million funded by

philanthropic foundations, which is senior to subordinate debt and equity, a subordinate lender (the City of New York) who has provided an \$8 million subordinate loan for a 10-year term, and finally by NYCAF equity which consists of surplus cash generated and maintained by the NYCAF in an amount of \$4.5 million as of March 2018.

The NYCAF operates under financial covenants regarding liquidity, leverage, annual operations, project loan delinquencies, project loan defaults, and net loss rate. As of its latest financial report dated December 31, 2017, NYCAF is in compliance with its fund financial covenants.

#### **Action by Members**

The Members are requested to approve i) the making of senior loans to eligible projects under the terms of the HDC NPLP in an aggregate amount not to exceed \$100,000,000, funded with the unrestricted reserves of the Corporation, ii) the execution by an Authorized Officer of the Corporation of mortgage-related documents and any other documents necessary to accomplish the financing and iii) the use of unrestricted reserves of the Corporation in order to make an interest-only Senior Term Loan to the New York City Acquisition Fund LLC ("NYCAF") not to exceed \$15 million for a term of up to 5 years.

#### **Attachments**

- A. HDC Neighborhood Pillars Loan Program Term Sheet