December 5, 2024

Ms. Cherisse Vickers, Executive Director
City of Newburgh IDA
City Hall, Third Floor
83 Broadway
Newburgh, NY 12550

Re: Test of Reasonableness Findings – "1 Lafayette"
50-72 Liberty Street LLC

Dear Cher,

The City of Newburgh Industrial Development Agency (the "IDA") is considering providing assistance to a real estate development project in the City of Newburgh (the "City") as proposed by 50-72 Liberty Street LLC (the "Developer"). The proposed project is located at 50-72 Liberty Street, near 1 Lafayette, in the City of Newburgh (the "Site") and includes the construction a mixed-income, mixed-use development that includes a total of 145 units of affordable, workforce, and market-rate housing, and up to 11,000 square feet of retail space on 1.3 acres of land (the "Project"). The IDA engaged MRB Group to provide certain advisement and analysis including the completion of a cost-benefit analysis (CBA) of the Project that conforms to the requirements of Section 859-a(5) of General Municipal Law and the completion of a "reasonableness test" of the assistance being requested by the Developer.

Scope of Analysis

To conduct this test of reasonableness, the IDA required the Developer to submit to MRB Group a pro forma financial analysis of the Project. MRB Group analyzed the Developer's submitted information and requested level of assistance. We compared the assumptions used in that pro forma analysis against other sources. As necessary, we adjusted the pro forma assumptions. Of important note is that, due to the nature of this Project, MRB Group made significant adjustments to the framework of analysis, as explained more fully below.

While this is a mixed-income, mixed-use development, the large majority of the Project is affordable, rent-controlled, income-restricted units: only 18 units of the 145 total units are market rate. Furthermore, as an affordable housing development, the Project is not being funded by a conventional private loan and the investors in the Project (the "Investors") are not investing in exchange for future cash flows from the Project's operations. Instead:

Unit Breakdown by Income Limit	
(% AMI)	Unit Count
30%	8
50%	47
60%	50
70%	11
80%	11
Market Rate	18
Total	145

Source: Developer

- The Project is supported by a combination of sources of different types from the New York State Housing Finance Agency[1] (HFA) and certain local grants.
- The Investors in the Project are referred to "tax credit equity investors", which are entities that act as passive participants in the development, providing cash equity infusions to the Project in exchange for State and Federal Low Income Housing Tax Credits (LIHTC). The Investors become part of the ownership of the Project, but typically exit the Project at the end of the required 15-year compliance period (the "Compliance Period") required by the LIHTC program.
- Distinct from the Investors is the Developer, the active participant in the pre-development and construction of the Project. While the Developer maintains a small equity position in the Project during the Compliance Period, the Developer's main source of return on the Project is the "Developer Fee", the amounts of which are reviewed and approved by HFA, a portion of which is paid upfront and a portion of which is deferred (the "Deferred Development Fee" or DDF), meaning it is paid over the course of the Compliance Period.

Therefore, our typical Test of Reasonableness analysis must be modified to meet Project specifics, and includes the following tests:

- Whether the Project would meet HFA financing conditions, such as meeting minimum Debt Service Coverage Ratios (DSCR), (the "DSCR Test") and
- Whether the Deferred Developer can reasonably be paid out of free cash flow during the Compliance Period (the "DDF Test"), and

[1] "The New York State Housing Finance Agency is a public benefit corporation created in 1960 to finance low- and moderate-income rental housing. HFA issues taxable and tax-exempt bonds to provide mortgage loans to developers of affordable multifamily rental housing. HFA's mission is to create and preserve high quality affordable multifamily rental housing that serves communities across the State of New York." Source: HFA website.

- Whether there is any excess free cash flow beyond what is required to meet the DSCR Test and the DDF Test (the "Excess CF Test").

Because the amount of the Developer Fee is controlled and approved by HFA, we do not independently test the reasonableness of the Developer Fee. Because financial items such as the interest rate, DSCR, loan-to-value, etc. are also stipulated by HFA and other public bodies, we did not evaluate those items or benchmark them against market data, as MRB Group would typically do for a private project.

Discussion

MRB Group requested certain pro forma financial projections, which the Developer provided in spreadsheet format (the "Projections"). The Projections included comprehensive details on the Project's:

- Sources of capital, including financing terms and conditions.
- Construction budget, including hard, soft, carrying and other costs.
- Operating revenues and expenses[2], including proposed PILOT terms.
- Cash flows and debt service requirements.

MRB Group reviewed the above, asked for and received certain clarifications and amendments, and participated in several email consultations and phone calls with the Developer. To preserve confidentiality, we do not disclose the exact figures provided by the Developer and the discussions therein. However, we took the information and assumptions contained within the Projections, as amended, evaluated them and applied the various tests described above.

We examined a number of factors used in the Projections, including the assumed:

- Operating expenses, and escalation rate thereof,
- Hard, soft and other costs in the construction budget.

Of note, the Developer made certain representations regarding the treatment of operating expenses by HFA, including the assumed escalation rate, as well as deal terms that HFA required or that the presumed Investors might require. It should be noted as well that the Projections provided to MRB Group

[2] Because the rental revenues are regulated by HFA, we did not evaluate them.

are the same Projections provided to the underwriters at HFA, providing further assurances that the figures used within represent realistic assumptions.

Using the pro forma Projections model received from the Developer, as amended, we conducted the DSCR Test, the DDF Test and the Excess CF Test.

DSCR Test Findings

The Developer represented that HFA requires a minimum of a 1.15 DSCR for each year of operations of the Project. The Projections show that the Project meets this requirement under the current PILOT agreement being requested by the Developer.

DDF Test Findings

The Developer represented that the HFA and Investors require that the entire DDF be paid out of the free cash flows of the Project within the 15-year Compliance Period[3]. The Projections show that the Project meets this requirement under the current PILOT agreement being requested.

Excess CF Test

Initially, the Developer's Projections included a schedule of proposed PILOT payments that escalated payments at 3% each year of the PILOT. The initial Developer Projections did not meet the Excess CF Test, as there was cash flow in certain years that exceeded the amount necessary to meet the DSCR Test and the DDF Test.

To address this issue, the Developer made adjustments to its proposed PILOT terms so that PILOT payments would:

- Escalate 3% each year from years 1-17 of the PILOT, then
- Jump 50% in year 18,

[3] The reason for this is that the value of the State and Federal Low Income Housing Tax Credits is pegged to the total capital budget of the Project, including the Developer Fee paid out during the Compliance Period. If the Developer Fee is not fully paid out, there could be a recapture of some of the tax credits.

- Escalate 3% from year 19-25, and then,
- Jump again 50% in year 26, and
- Escalate 3% from year 27-32.

This new set of PILOT terms allows for a larger portion of the excess cash flow to be diverted to PILOT payments.

Summary of Findings

We find that the Applicant's requested PILOT abatement terms, amended as described above, appear to be adequate to achieve the Project under the strictures of an HFA funded project. We further find that the schedule of PILOT payments allows for a majority of the free cash flow to be used for PILOT payments. As such, and given the requirement of this deal structure, MRB finds that this request meets the Test of Reasonableness.

Thank you for this opportunity to assist the Newburgh IDA.

Sincerely,

R. Michael N'dolo, CEcD
Director / Practice Lead – Economic Development