

# Financing Multifamily Housing in Massachusetts



**Massachusetts  
Housing Partnership**

Moving affordable housing forward

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*March 8, 2018*

## **Benefits of Multifamily Housing**

- Provides housing for city employees, young families starting out (including those who grew up in the community and want to come back);
- Helps seniors to downsize and stay in their community;
- Directs economic benefits to the local community, such as increased jobs and sales taxes;
- Promotes economic and social integration while building a diverse community;
- Despite scarce resources, it presents excellent design and urban planning opportunities

### **Cutler Heights, Holliston**



Before



After

## Who occupies Multifamily Housing?

- Seniors, municipal workers, veterans and disabled that work for low-moderate wages or may be on a fixed income;
- Young families, millennials that have additional monthly expenses (i.e., day care, student loans) which constrains ability to afford housing.



# **Lenders -- Five C's of Credit**

**Gauges the creditworthiness of potential borrowers.**

1. Character

2. Capacity

3. Capital a/k/a Net Worth or Equity

4. Conditions

5. Collateral

# Character

Customers' willingness and determination to meet a loan obligation. Lender conducts interviews, obtains bank references, investigates borrowers payment habits and the way they manage their business affairs and may have responded to any adversity.



# Capacity

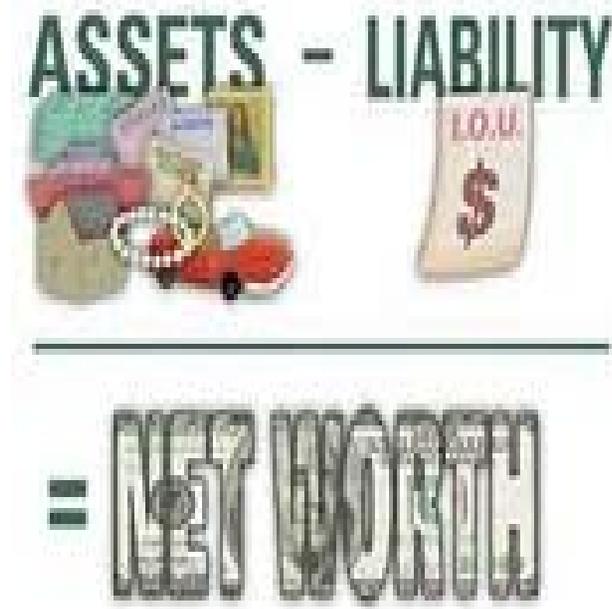
Measures a borrower's ability to repay a loan by comparing revenue against recurring operating expenses and sizing the mortgage payment to a % of net operating income.

Annual Property Operating Budget	
Rental Income	\$800,000
Less: Expenses	<u>- 500,000</u>
Net Operating Income	\$300,000
Mtg. Payment	<u>(\$240,000)</u>
Cash Flow	\$60,000
Debt Service Coverage	1.25x
(\$240,000/\$300,000 =80%)	



# Capital a/k/a Equity or Net Worth

Represents reserves a business or borrower has in the event of unforeseen problem. A lender investigates capital adequacy of a borrower and it also show a level of commitment by stakeholders of the company and mitigates moral hazard.



# Conditions

External variables that can affect credit such as its interest rate influence the lender's desire to finance the borrower. Conditions can also refer to how a borrower intends to use the loan.



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# Collateral

Are assets pledged to secure a loan (i.e. reserves, guarantees, etc.). Collateral provides the lender an alternative source of repayment if the primary source of repayment is not available.



# Putting it Together

- Who is on the “team” (developer, contractor, architect, manager, attorney) and what is their experience level in housing development and property management?
- How will the project compete in the marketplace to capture anticipated monthly rents and average occupancy?
- Are the project sources sufficient to cover costs contingencies?
- What are the risks and consequences of unexpected delays in either the construction schedule and/or financing commitments for the development?
- How does the project meet the developer’s need to cover its overhead, and to make a reasonable return?
- Does the project rely on operating subsidies that may discontinue during the financing term (Section 8)?

## **How does financing affordable and workforce housing differ from market rate housing?**

- Various additional sources are needed to fund affordable/workforce housing and rental subsidies (Section 8) support extremely low income households;
- Affordable and workforce housing requires households to be income eligible;
- For affordable and workforce housing investors and subsidy lenders conduct site visits and tenant file reviews confirming occupancy eligibility and property condition; and
- Affordable and workforce housing typically has use restrictions imposed by zoning (40B Comprehensive Permits, covenants running with the land), which do not terminate in the event of foreclosure.

Household eligibility for affordable and workforce housing is based on an income limit which is set annually by HUD for a particular community where the housing is located

<b>2017 Income Limits</b>			<u>Area Median Income (AMI)</u>	<b>Household Size</b>		
Boston-Cambridge-Quincy, MA				<u>1 PERSON</u>	<u>2 PERSON</u>	<u>3 PERSON</u>
	Extremely Low Income	30% AMI	21,700	24,800	27,900	
	Very Low Income	50% AMI	36,200	41,400	46,550	
	Low Income	60% AMI	43,440	49,680	55,860	
	Moderate Income	80% AMI(1)	54,750	62,550	70,350	
<b>2017 Maximum Rents</b>			<b># Bedrooms (People)</b>			
Boston-Cambridge-Quincy, MA			<u>Studio(1)</u>	<u>1BR(1.5)</u>	<u>2BR(3)</u>	
	Extremely Low Income	30% RENT	542	581	697	
	Very Low Income	50% RENT	905	970	1,163	
	Low Income	60% RENT	1,086	1,164	1,396	
	Moderate Income	80% RENT(1)	1,368	1,466	1,758	

**Note 1:** For example, a 2 bedroom apartment with occupancy restricted as moderate income (or 80% AMI) would have a monthly rent of \$1,758 ((\$70,350 x 30%) divided by 12 months).

# Analyzing the Pro-Forma

- Revenue:
  - **Residential rents must observe constraints of ...**
    - Market (Supply and Demand)
    - Monthly Rents of Competition
    - Affordability restrictions imposed by subsidy lenders
    - Use restrictions imposed by local permitting
  - **Commercial rents must observe constraints of...**
    - Market
    - Need for brokers' and tenant fit-up costs at turnover
- Expenses
  - **Expense budget must not understate the cost of operations**
    - Management Fees (% of collected rents)
    - Administrative (legal, accounting, office)
    - Operations and Maintenance
    - Utilities
    - Real estate taxes and insurance

## Sizing the First Mortgage (Market vs. Affordable)

<b>MARKET</b>	
<b>REVENUE</b>	
Rental Income	
10 -- 1-BR @ \$2,600/mo.	312,000
27 -- 2-BR @ \$3,500/mo.	1,134,000
18 -- 2-BR @ \$5,100 /mo.	1,101,600
	<b>2,547,600</b>
<i>less: vacancy 5%</i>	<i>(127,380)</i>
<b>EFFECTIVE RENTAL INCOME</b>	<b>2,420,220</b>
<b>EXPENSES</b>	
Management	76,428
Administrative	80,000
Maintenance	80,000
Utilities	75,000
Taxes and Insurance	100,000
	<b>411,428</b>
Per Unit Operating Costs \$7,480	
<b>NET OPERATING INCOME</b>	<b>2,008,792</b>
Target Debt Coverage ratio	1.20
Available for Debt Service (\$2,008,792/1.2)	<b>1,673,993</b>
Maximum Mortgage Amount based on 5% Int. Rate, 30 year term and amort.	<b>25,977,766</b>

<b>AFFORDABLE</b>	
<b>REVENUE</b>	
Rental Income	
10 -- 1-BR @ 50% AMI Rent \$970/mo.	116,400
27 -- 2-BR @ 50% AMI Rent \$1,163/mo.	376,812
18 -- 3-BR @ 50% AMI Rent \$1,344/mo.	290,304
	<b>783,516</b>
<i>less: vacancy 5%</i>	<i>(39,176)</i>
<b>EFFECTIVE RENTAL INCOME</b>	<b>744,340</b>
<b>EXPENSES</b>	
Management	47,011
Administrative	100,000
Maintenance	100,000
Utilities	120,000
Taxes and Insurance	84,575
	<b>451,586</b>
Per Unit Operating Costs \$8,210	
<b>NET OPERATING INCOME</b>	<b>292,754</b>
Target Debt Coverage ratio	1.10
Available for Debt Service (\$292,754/1.10)	<b>266,140</b>
Maximum Mortgage Amount based on 4.50% Int. Rate, 17 year term and 30 year amort.	<b>4,370,000</b>

# Workforce Housing?

Workforce housing is generally understood to mean affordable housing for households with income of up to 120% AMI that are too high for subsidized housing but are priced out of an areas market rents. For Newton, using the 2017 Income Limits (Boston-Cambridge-Quincy) with affordability targeted at 120% AMI for 3 persons is \$111,720/annually and assuming occupancy of 2BR the maximum rent would be \$2,793/mo.

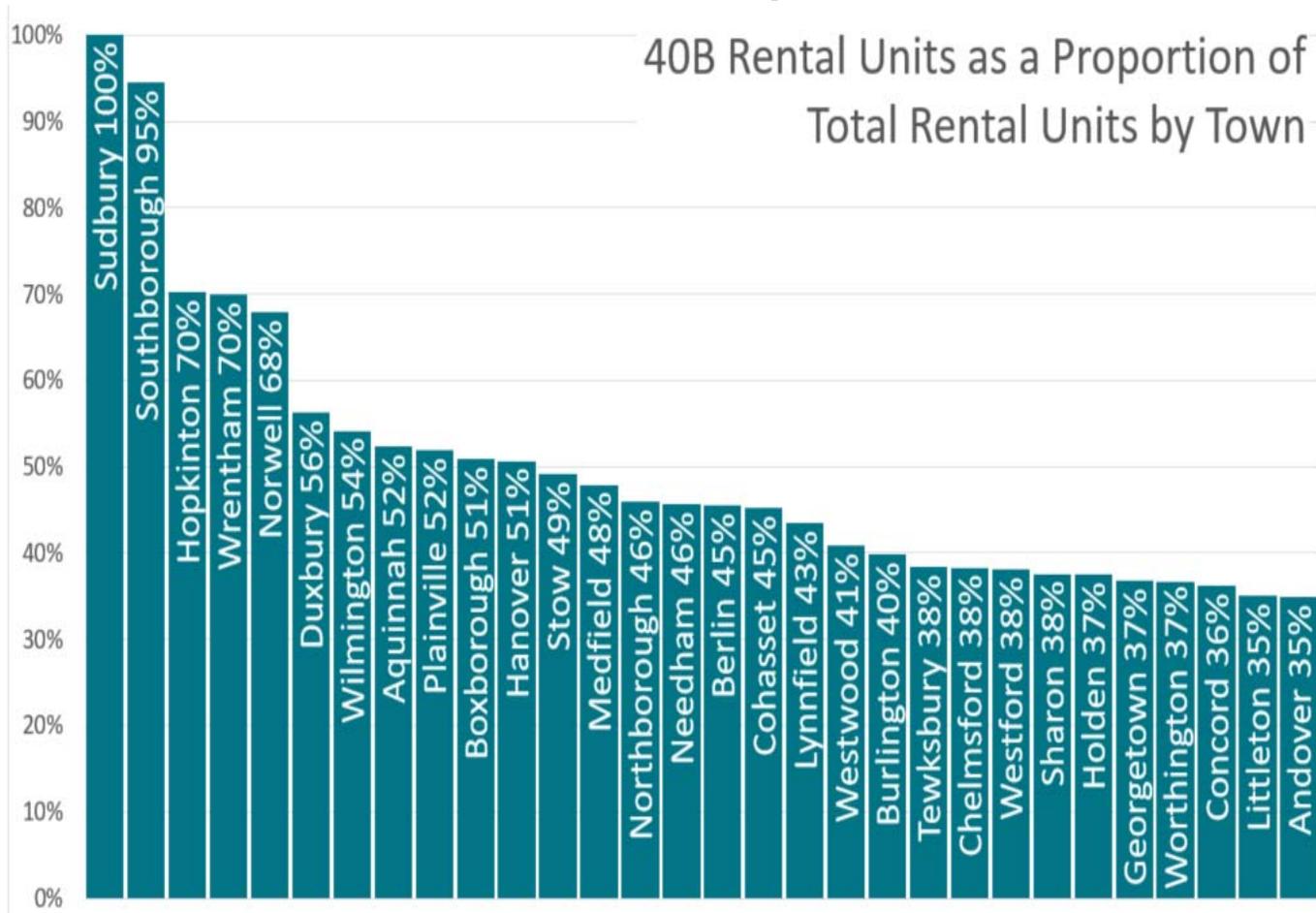
MassHousing's \$100 million Workforce Housing fund supports the creation of rental housing that is affordable for working families, program highlights are below:

- Provides up to \$100,000 of subsidy per workforce housing unit created;
- Leverages strategic opportunities to use state-owned land;
- Ensures workforce housing units are deed restricted as affordable for at least 30 years;



Gateway Residences on Washington in Lynn

40B is an effective tool to create housing, faster than changing local zoning. 30 communities have produced more than one-third of their rental units through Chapter 40B



Developers creating 40B communities in most cases offer and/or are required to provide mitigation \$\$ to a city or town to lessen adverse impacts (i.e., upgrade roads, add traffic lights, donate land for bike path, update police/fire station, etc.)

# Can you tell the difference between affordable, workforce and market rate housing?

