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MEMORANDUM

To:	**The Affordable Housing Trust**
From:	**Christopher Cotter, Housing Director**
	Anna Dolmatch, Housing Planner
	Janet Haines, Housing Planner
Date:	**August 6, 2020**
Re:	**Park View Cooperative Request for Additional Funding**

The Park View Cooperative is a twelve-unit limited-equity coop located at 24-26 Corporal McTernan Street in Cambridgeport. The coop was created in 1984 as part of the City program to assist tenants in purchasing their buildings during rent control. The coop was created without any public funding other than a second mortgage from CNAHS that was fully repaid.

We are attaching to this memo, material the Coop has submitted in support of its request to the Trust.

<u>Overview</u>

The building was built in 1908 and is considered historically significant. At the time of conversion to a limited-equity coop, very little rehab work was done. While the coop has completed some rehab projects over the years, they currently have significant rehab needs. As you may recall, the Trust approved a loan of up to $1,394,000 in March 2019 to assist the cooperative with this project.

The Coop is requesting additional funding to more than double the amount of Trust subsidy in the project. The Project Review Committee has reviewed the request. The PRC reviewed the details of the new request and changes in project costs, specifically reviewing increases in construction costs and available opportunities to leverage other funding sources to reduce the current funding gap. However, there were few concrete recommendations there beyond those suggested by staff, and discussion then touched on the principles the Trust should consider for this type of request, including:

- preservation of existing affordable housing;
- ensuring long term-financial viability, use of public funds and participation of residents in sustainable resident-controlled housing;
- promoting broad access to Trust-funded housing and ensuring diversity in resident selection processes.

As this discussion transcended the specific review of the funding request, the PRC suggested that the request be forwarded to the Trust without a recommendation for a broader discussion of the policy approach of the Trust to this request.

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Current Needs and Construction Costs

The scope of needed renovation work includes replacement of the roof, exterior stucco, and all windows with historically-appropriate materials; additional insulation throughout the building; new electrical service to the entire building and replacement of all knob-and-tube wiring; plumbing stacks; new kitchens and baths for most units; new sewer lines and required sitework; and installation of a sprinkler system. All work, other than kitchens and baths, is an immediate need; it is most efficient to do all the work in one phase. This rehab will address major capital items that were not updated when the building was converted to affordable housing.

The initial budget for this work was based on estimates and not a full bid with finalized design and mechanical drawings. The initial budget was $2,202,843 with hard costs at $1,900,000. With the aid of a contractor and architectural firm, the scope has been more fully developed and undergone a full bid process with confirmed subcontractor pricing. The revised budget is now $3,714,764. Staff have reviewed the scope and budget and feel it is appropriate for this work in the current market. The Coop is therefore facing a funding gap of $1,533.568.

We have requested that the Coop review a range of value engineering projects to reduce project costs. Some of these options would impact the historic elements in the building, reducing access to a $100,000 grant committed by the Cambridge Historical Commission. However, the potential savings would not be significant, and would change the exterior of the building significantly by removing much of the historic building envelope materials.

Staff have worked extensively with the Coop and their development consultant to leverage other funding sources to cover the costs. The coop ownership structure makes it difficult to use any form of tax credits, as the coop would need to transfer ownership to another entity, which would fundamentally alter the resident-ownership model. They also consulted with state funding sources including DHCD and CEDAC, who both stated they did not see a path for the project to receive funding.

Cambridge Savings Bank (CSB) has provided a letter of interest to provide conventional financing for the project. This would be a loan secured by a mortgage on the entire building. CSB has provided a letter of interest to provide the requested $500,000. Taking on new "blanket" mortgage financing to undertake rehab is an approach that has been successfully used by other coops.

We have reviewed the operating budget to determine if additional debt could be carried. An increase of $100,000 to a total of $600,000 is possible without increasing the number of shareholders who are cost burdened, discussed more below. The debt service coverage ratios for the increased loan would be sustainable at current revenue levels and would become more so over time.

Current sources and uses are:

Source	Amount	Use	Amount
First Mortgage	$ 500,000	Hard Costs	$2,723,771

Historic Grant	$ 100,000	Contingency	$ 408,565
Reserves	$ 148,000	Soft Costs	$ 582,427
MassSave	$ 39,106		
CAHT Commitment	$ 1,394,000		
CAHT New Request	$ 1,533,658		
TOTAL	**$ 3,714,764**	**TOTAL**	**$3,714,764**

The TDC per unit is $309,564.

<u>Issues and Recommendations</u>

Affordability and Carrying Charges

Current carrying charges are less than $650 for each units, which is affordable to households earning approximately $26,000 per year. Of the twelve shareholders, only one earns more than 80% AMI. The estimated median income is slightly less than 40% of AMI, with many shareholders living on Social Security. Even with low carrying charges, one-third of shareholders are cost burdened. Other shareholders pay low portions of their income for housing. This is similar to affordable ownership, where costs remain relatively fixed as incomes increase or decrease over time, compared to rental programs with annual recertifications and ongoing rent adjustments.

The coop has invested in ongoing maintenance, but the amount of work required to address rehab needs precedes the creation of the coop. Even if the coop had significantly higher reserves, the amount of work needed to preserve the building would require new subsidy.

The coop model does not support having income-based carrying charges, so that approach would require a shift towards a rental housing model and would be a significant change for the coop. This may also impact the operating revenue as shareholders retire or otherwise have lower incomes. The coop is concerned about changes to carrying charges causing displacement of very-low income residents, both current and future.

The 2019 Trust funding commitment required that the coop continue to increase carrying charges at a reasonable rate. However, carrying charges have not been increased for at least two years. Any additional funding could be contingent on benchmarked increases to the carrying charges to ensure that the coop is sustainable while minimizing the risk of displacement. Options could include a combination of the following:

- immediately increase carrying charges by 3% or CPI change for 2019 or some other reasonable increase;
- requiring an indexed increase annually as of a certain date (e.g. January 1 or July 1). Index could be straight percentage or tied to benchmark such as AMI or CPI;
- requiring an increase that aligns with median coop income;
    - a portion of increased revenue could be set aside to internally subsidize very-low-income shareholders who might otherwise be displaced by the increase;
    - when units turn over, new shareholders would need to have sufficient income to afford the charges at the higher level or have a voucher;

- this is not sustainable if too many residents require subsidy to pay the required carrying charges, and so could still result in residents being cost burdened.

<u>Shareholder Selection</u>

The 2019 Trust commitment is contingent on the Coop developing a shareholder selection plan that includes outreach to rental voucher holders. In previous conversations, the Trust members expressed a desire to increase the likelihood that future vacancies will be filled by voucher holders.

Other limited-equity coops have shareholder selection policies that align with this goal, while providing flexibility for the unique needs of housing cooperatives. Options include:

- requiring selection process to include preferences for voucher holders and/or certain income levels prior to offering share to next groups (e.g. voucher holders or households earning less than 50% AMI are highest priority);
- setting secondary preferences to align with Trust goals and/or additional equity goals;
- documenting required outreach and request assistance from CHA to ensure CHA voucher holders and CHA applicants are aware of new shareholder selection opportunities;
- including Trust representative (or designee) in shareholder selection process including interviews;
- lowering the maximum income from 95% AMI to 80% AMI, except in cases of surviving non-owner spouse or share transfer from deceased owner, to resident household member which would remain at 95% AMI;
- requiring coop to amend their by-laws as necessary to incorporate changes.

We recommend that the preference for voucher holders not be a strict requirement. Other coops with this preference use a model that provides that if they are not able to find an eligible shareholder with a voucher, they notify the City and the CHA. There would then be additional outreach, or the search would move to the next preference group. This process would incorporate feedback from both the City and the CHA. Other coop selection processes also have different requirements depending on how many units are currently occupied by "highest priority" households, with more stringent requirements when the ratio drops below a certain level, for example if fewer than 3 of 12 households are very low-income or have a voucher.

Demand for coop units has typically not been as robust as for housing in other affordable programs. The coop's consensus and shared work model requires a large investment of time and process. In addition, the low carrying charges may mean that as soon as a voucher holder buys in, they may no longer qualify for subsidy and could lose the safety net of the voucher. Park View members have raised concerns about the ability of a voucher holder to afford the buy-in price with or without a share loan. We continue to work internally and with the CHA to understand how best to support a voucher holder purchasing in a coop. The is shared desire and agreement between staff, CHA and coop residents to fully explore how voucher holders can be offered housing at Park View when units are available. However, there are currently no vacancies. Staff are working with CHA and residents to determine how this could be accomplished.

Share Transfer Appreciation

Currently, each share transfer price is estimated to be in the range of $35,000. The share appreciation formula currently has three factors:

- Initial share buy-in price adjusted by the change in CPI from date of purchase;
- Capital improvements in the unit, capped at $200 per year;
- Principal amortized on blanket mortgages paid by the corporation, based on the amount attributable to the unit.

The Coop is currently working with Cambridge Savings Bank to secure a $500,000 blanket mortgage with a thirty-year term. Under the current appreciation formula, this would add an average of $41,667 to each share price. Our analysis shows that the Coop could increase the loan to $600,000 with a small impact on monthly carrying charges. Coop residents are concerned about how an increase in the CSB loan would impact future affordability. We recommend that the CSB loan be increased so that the Trust request can reduced accordingly, and that the appreciation component relative to this loan be altered to reduce the impact on future affordability.

The current share appreciation formula is inverse to the depreciation of the work funded by the loan, giving the current shareholders more and more value for work (as the loan is repaid) that is closer to the end of its useful life. This is the opposite of how capital improvements are valued in affordable ownership units. The current model has no provision for improvements or maintenance funded through monthly charges or reserves but all costs other than interest for work funded through a repayable loan..

As we look at the impact of a new mortgage on share value, we agree with the concern about future affordability, and find these provisions from the 1980's counter to current best practices.

While some limited equity cooperatives use the principal amortization factor, none have taken on a mortgage of this size. Some coops use a portion of the carrying charges as a factor in the share price appreciation. This is intended to provide a partial reimbursement for what the portion of the carrying charge that is invested per share in the reserves and improvements.

For example, several other limited-equity coops use 8.34% of the monthly carrying charges. A change to a similar formula at Park View would shift a portion of the costs of the current rehab loan from future shareholders to the current occupants.

For example, at the end of 30 years under the current model, each share price would increase by $50,000 for payment of a $600,000 mortgage. Under the alternative model, assuming increased carrying charges each year, this factor would increase share prices by approximately $17,000.

Any additional funding commitment could be contingent on changes to the share price formula used by the coop. Options include:

- changing the principal amortization factor to either:
    - substitute a portion of the monthly charges;
    - cap the amount that can be recovered;
    - exclude all or a portion of the CSB loan for this project;
- capping the overall share price to be tied to a factor such as AMI or CPI; or
- depreciating value of any work completed.

Monitoring and Oversight

We recommend that any additional funding be contingent upon entering into a monitoring agreement with the Trust through the Community Development Department. In addition to participation in the shareholder selection process, we recommend that oversight include:

- regular review of Coop finances and budgets, including operating and capital reserves;
- approval of annual carrying charge amounts;
- requiring and reviewing updates to Capital Needs Assessment as requested to ensure sustainability;
- provision of any other information as requested.

We also recommend that the Trust require that a monitoring agreement include steps to be taken if the coop's finances are unsustainable, including requiring that the next vacant unit(s) be purchased by the coop and rented to a tenant with a mobile voucher paying Fair Market Rent; oversight by a non-profit housing provider; or in the case of financial infeasibility, transfer of the property to another entity for continued operation as affordable housing.

Summary

Limited-equity coops are a unique part of the affordable housing stock in Cambridge. Coop shareholders are not able to access individual mortgages or home equity financing. These units are also not eligible for most affordable housing subsidy programs without altering their very nature as cooperatives. The work on this building cannot be completed without significant public subsidy. As noted, this will be the only public subsidy invested in the project over almost 40 years. The rehab needs of the building are extensive and will require a significant amount of public funds given the limit of what the coop can afford based on the income of most residents there.

The Coop has committed to putting a new Affordable Housing Covenant on the building that will ensure an additional 50 years of affordability, with the ability to extend that restriction further

The Project Review Committee is requesting that the Trust review the issues raised by staff and in its discussion of this request and provide input on appropriate terms and conditions if the coop's request for additional funding from the Trust is approved.