MINUTES

Grand Junction Housing Authority
Board of Commissioners Special Meeting

June 23 & 24, 2003
Conference Room
1011 North Tenth: 11:30 a.m.

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1. Call to Order

At 11:33 a.m., a **special** June Board Meeting of the Grand Junction Housing Authority (GJHA) was called to order by Board Chair, Gabe DeGabriele. The following individuals were in attendance: Harry Butler, Erin Ginter, Steve Heinemann, Cory Hunt, Gi Moon, Jody Kole, Kristine Franz, Mary Gregory, and Becki Tonozzi. John Collier representing Collier Consulting Services and Rich Krohn representing Dufford, Waldeck, Milburn, & Krohn were also in attendance.

2. Review and Discuss Restructuring Commitment on the Refinancing of Ratekin Tower

The only agenda item for this special meeting is to review and discuss the Ratekin Tower Apartments (RTA) Refinancing Restructuring Commitment that was received recently from Heskin-Signet Partners (Heskin-Signet), who is representing the U.S. Department of Housing and Urban Development (HUD) in this transaction. Before starting the discussion, Jody Kole, Executive Director, distributed a revised Page 3 to her June 19, 2003, memo. She summarized Ratekin Tower's history as follows:

- The existing 40-year mortgage has been covered, up until now, by Housing Assistance Payments (HAP) from HUD under the 20-year funding contract. Now it is time to renew the funding commitment, and HUD would like to renew the commitment but at a much lower payment level. This is common across the country with properties that were financed 20-25 years ago at much higher interest rates.

- To answer Steve's question of, *"Through this restructuring, we are totally paying off the existing mortgage?"* Jody answered, *"The existing mortgage will be retired by the new transaction which will include 3 mortgages."*

- Jody further explained that the scenario is that the new HAP Contract will establish a contract rent, which is the tenant contributions plus the HUD subsidy, for a combined total starting at $500/month/tenant at Ratekin with the potential for annual increases, by HUD's operating cost adjustment factor.

- Next, a new 1st mortgage will be signed in the amount that can be supported by the new lower rents, which is roughly $1.8 million.

Steve asked the question, *"Why weren't we informed of what the appraisal numbers were earlier?"* to which Jody replied, *"The appraisal is nearly a year old and was done by an out-of-town appraiser selected by Heskin-Signet, which we had no control over, and at the time thought it wasn't a significant item to bring to the Board's attention."* Steve felt that if we owe $4.4 million on a building that appraised at $3.8 million, that's a problem and does affect the financing if that's the source document for the appraisal on the building and *"right or wrong, that is a ludicrous appraisal."*

Rich Krohn commented that this deal may be to our benefit because of the way this deal is structured. The Agency is getting a lower figure on the appraisal, but also getting a lower figure on the loan it's paying for at market rate, a higher figure on the loan it's paying 1% for, and it's paid only from available cash flow, plus it's a non-recourse note. Given the numbers, there are several benefits to the 2nd loan being a higher principal amount and the 1st loan being a lower principal amount.

Steve said, *"I personally have a problem entering into a 30-year agreement with this institution that's going to end up at the end of 30 years owing $2.0 million."*

Erin stated, *"I have some problems with this. I don't know where to begin."* She asked if we tried to negotiate with HUD on the Residual Receipts Account that has a balance of $793,000, to recapture some of the funds. Jody responded, *"No we did not. Under the original financing terms, that Residual Receipts Account belongs to HUD."* GJHA will receive 10% of the balance in the Residual Receipts Account at closing of the Mark-to-Market Transaction. Erin understood that but felt we should have tried to keep some of that money and was surprised that we didn't. She indicated when calculating the numbers, the results showed that over the course of 50 years, the Agency would be paying $187,000/unit and she felt that it wasn't fiscally responsible for the Agency to do this and, consequently, doesn't agree with this course of action.

Gi agreed with the rest of the Board that voiced their opinion and stated, *"At the end of this to have a $2.0 million loan with no principle reduction after we have already seen what 20 years of doing that has created, and for us to step back in and do that again – I agree."* Her additional concerns are that we have eliminated the ability to keep creating the Residual Receipts because of the lower payments, so that cushion is gone, plus can this project cash flow anymore than it is already to pay down the $2.0 million note?

Group discussion ensued regarding conventional loan options. Jody said the pay-off on the existing mortgage was $4.415 million and the projected operating costs for 2004 were $33,500/month. If the Agency doesn't finance the property through HUD, then the subsidy "goes away" since it is attached to the property, not the tenants. If we were to negotiate something where all 107 tenants received Vouchers, the tenants would become "portable" and could seek housing elsewhere. Then, we would have to try to fill the building with tenants at or below 50% of the area median income that could pay at least $500/month for rent. Voucher holders could choose to live at RTA; however, the administrative fees we receive on Vouchers are cut in half if GJHA owns the building the client lives in.

Erin addressed the possibility of selling the building but retaining the management of the facility. Jody thought this idea would have to be explored in greater depth and explained that because of the property's value as it is and the tenant income, there is a limited amount of debt than anyone could take on without very favorable terms like the ones presented today.

Jody further explained that the Colorado Housing and Finance Authority (CHFA) can't be part of this transaction because they hold the existing note, and Becki Tonozzi, Finance Director, recapped scenarios she and Jody have previously explored when looking at available options.

In response to Gi's question regarding the structure of the 2nd mortgage, Jody said that the 2nd mortgage is paid down partially in the Heskin-Signet Pro-Forma and nothing is paid on the 3rd during the 30-year term. Jody informed the group that a more realistic scenario actually looks better than demonstrated by the Heskin-Signet Pro-Forma because the cash flow generated from the rent of the commercial space, which is roughly $20,000/year, isn't included in the Pro-Forma. In the event there is cash flow left over at the end of the year, and we expect there to be, 25% of the amount goes to the Agency and 75% goes to pay down the 2nd and 3rd mortgages.

Erin asked if we could get a time extension, to which Jody explained this is an extension from June 16th with a request to fax the signed copy of the Restructuring Commitment and overnight the originals. We could try to get another but she understands this is a "limited-time offer and if not accepted, the offer goes away". Erin felt the timelines were unrealistic and that we needed time to look at other options. She asked if anyone in Washington, D. C. had been contacted to which Jody said, *"No, we worked with Heskin-Signet, as HUD's agent."* Gabe referred to the appeal referenced on Page 1 of the Heskin-Signet letter dated June 4, 2003, and wondered what that was concerning. Jody indicated that the appeal was referring to what a market rent amount is, and not the debt structure.

For clarification to Gi's question regarding this new Contract and participation in 25% of the annual net cash flow, which isn't the Replacement Reserves, Jody reiterated that the 25% we participate in is the net cash flow after debt service and an incentive to the Housing Authority for operating it. The new Replacement Reserves are held in trust for the property.

Jody explained the events that happened after the appraisal was done, which included Heskin-Signet site visits to RTA and meetings with the tenants. We didn't try to appeal the appraisal except that extensive discussions were held regarding the tenants' rent and operating expenses. Jody expressed a concern that HUD could, down the road, say "the rents are at market-rate rents and we just can't afford to subsidize all 107 units" and would only subsidize a certain number of units. Then, it would be up to the Housing Authority to rent the remaining unsubsidized units at market rate to whomever.

Becki explained Attachment 1, "Closing Sources and Uses for Ratekin Tower", to the GJHA's June 19th memo to the Board which identifies the funding sources and funding uses. She noted that the Agreement has been structured in a positive way to make it work and reminded everyone that this Agreement does help the Housing Authority Program overall. She pointed out that the Replacement Reserves of $419,288 will be reinstated to RTA, and the Residual Receipts are being used to help pay off the other mortgage. Jody stressed that with Ratekin Tower as part of the properties, the Agency has a broader base in which to spread the overhead costs.

John Collier felt that the Agency would loose over $100,000 in cash profit if we lost the Ratekin Tower building; therefore, if at all possible, the Agency can't afford to loose the building. Jody identified that the incentive performance fees and owner's share of cash flow would be affected.

Gi felt that the Board's overall concern was not with HUD's contract but with the fact that there is a 2nd and 3rd mortgage. She felt that the HUD contract needed to be attached to the overall package so administrative fees aren't lost and she understood the value of the flexible cash flow 2nd and 3rd mortgage payments, but was still hesitant of the overall commitment. If the loans are split as proposed, $1.8 million represents the 1st mortgage and roughly $2.850 million jointly represents the 2nd and 3rd mortgages.

Rich stressed that the Agency owes $4.4 million on an asset that appraises out at less than that so it is important to think about what the building is worth today. He explained that if the Board chooses not to accept the Agreement, $4.415 million is due and payable NOW as well as transaction costs incurred up to this point. Options include selling the building or refinancing it conventionally. That sparked a lengthy discussion pertaining to conventional refinancing requirements, a new appraisal, current market rents for similar 1-bedroom units, appraisal problems encountered due to the value of the building, cash flow, and the ability to generate cash flow.

Jody referenced Paragraph 18 of the Restructuring Commitment. It states that within the next 3 years, we have the ability to transfer the property to a non-profit (such as Grand Valley Housing Initiatives or a different non-profit) with room for debt forgiveness. Additional information states that the non-profit would need to be "at arms length" from the Housing Authority with the Authority having no control or ongoing relationship with the property, and Jody discussed how that might happen. The fact that this transaction must be completed within 3 years after the date of this Commitment complicated this opportunity.

Erin asked if it would be possible to hire a firm qualified to negotiate our position with HUD since we haven't pursued that option.

Steve asked for confirmation of his understanding that if this Commitment is signed, $500 is the amount of rent that is to be charged no matter what – subsidized or unsubsidized – and if HUD does pull partial funding, that's all the rent that can be charged for the units. Jody stated that by signing this Restructuring Commitment, the Agency is agreeing to the essence of this transaction in its entirely and all the other mortgage documents still will need to be signed. Jody further confirmed that the land usage restriction reads that we will rent 40% of the units at rents equivalent of 60% of the area medium income. The other 60% of the units would be unrestricted. Mary Gregory, Administrative Director, discussed her findings of the rent comparability done in August of 2002, for a 1-bedroom unit by citing location examples. The average rent was $461.

Gi asked if HUD would be giving a cost-of-living allowance for utilities any quicker than for the rent portion. Jody said the rents could be adjusted annually by the Operating Cost Adjustment Factor, and we should apply for that annually which would include utility expenses. Gi wondered if HUD could just forgive some of the debt now knowing it was structured so poorly in the beginning. Jody explained that so many Agreements were structured poorly and that HUD would rather not have a "big run" on the FHA insurance pool.

In response to Steve's question, Jody stated that the net cash flow on the building is currently at a loss because HUD has frozen the rents for the last 6 years. The rents are higher than market rate and HUD has changed the rules on when you can and can't ask for rent adjustments. One rule that we can't meet is if the rent is substantially above market rate, and unless you meet some extreme circumstances, you get no rent increase.

To answer Gi's question, Jody explained that the Office of Multifamily Housing Assistance Restructuring (OMHAR)/HUD regulations dictate how large a 2nd mortgage can be so that is why there is a 2nd and 3rd mortgage.

Erin expressed a desire to pursue more options – ask for extensions, request assistance to see if this is the best deal possible, and make telephone calls to Washington, D. C. Jody cautioned that during the in-between contract period, the mortgage payment of $54,000/month would have to be maintained. She also felt that if we are out-of-contract with the old Contract and haven't signed the new Contract, we wouldn't receive a HAP payment for the month of July.

Jody indicated that we have several 1st mortgage offers and explained in detail the particulars. Group discussion continued on offered interest rates, payment amounts, debt service, and cash flow amounts.

Jody requested that Becki immediately contact Mr. Chris Curran with Heskin-Signet for a possible time extension so Becki left the meeting. When asked, Rich stated that he had had limited conversation with the attorney representing Heskin-Signet. Becki returned stating that she was unable to talk with anyone, possibly due to the lunch hour, but that she left several messages. She was then asked to call the HUD office and again left the meeting.

It was suggested to table further discussion until tomorrow allowing time for the GJHA staff to make inquiries, ask for additional assistance, and explore other options through various avenues, as directed by the Board.

Gi made a motion for this special June Board Meeting to go into recess until tomorrow, June 24, 2003, at 11:00 a.m., thereby allowing the GJHA staff additional time for further research. The motion was seconded by Erin and it passed unanimously. The recess went into affect at 12:58 p.m.

At 11:12 a.m., on June 24, 2003, the special June Board Meeting reconvened. All individuals were present for the continuation of the meeting with the following exceptions: Cory Hunt was absent and Kathleen Belgard was in attendance.

Jody distributed her memo dated June 24, 2003 to the Board and reviewed the results of the Board's requested inquiries:

- There hasn't been a response from OMHAR/HUD to the request for a 30-day extension to consider this transaction.

- Mr. Chris Muhle of Heskin-Signet was contacted and was very reasonable to deal with. He reran the financial model, taking into account the lower interest rate, and was willing to work with us on whatever it takes. A number of scenarios were reviewed. The effect of obtaining a lower interest rate is that, with the same cash flow, RTA can handle a larger 1st mortgage. We will get $45,000 more higher-cost debt and $45,000 less 1% interest debt, keeping in mind that the lower-cost debt is non-resource and cash flow only. The impact of overlaying a Tax Credit transaction on this deal was evaluated, and it was discovered that the pluses and minuses are at least a wash and maybe make it less attractive. She further expounded on additional information pertaining to the Tax Credit. The 2nd and 3rd mortgages are sized according to a couple of different formulas. The FHA Insurance Fund is taking a hit. If we approve this deal financially, hoping to benefit GJHA, the majority of the benefit goes to HUD and we really don't improve things that much. Mr. Muhle's quote was, *"The deal would be no worse - no better."*

Jody referenced the attachments to her memo – a copy of the 30-day extension request to OMHAR/HUD and a spreadsheet created to show the first 30 years of the transaction. She noted that on the spreadsheet, and to the left of the shaded block area, the cumulative investable cash flow to the Housing Authority over the next 30 years is shown. She also reviewed each column on the spreadsheet for additional explanation. In summation, she stated that in the 1st year, the Agency should net $61,000 unrestricted money that could be invested to improve Ratekin Tower's financial picture. The cumulative cash flow, not including any investment income and only increasing where identified over 30 years, should total over $1.7 million. Jody felt that if the amount is invested prudently, the 2nd and 3rd mortgages could be paid off within the 30 years.

Becki acknowledged the Board's concern for the amount of debt we are assuming again. She informed the group that if this HAP Contract had continued for another 20 years, we would have paid $23 million for the property. Instead, this way, we will have paid $18 million for the property. She also illustrated another way to view this situation. Under the old Contract, we would have paid 2.42 times the purchase price and under the new Contract it would be 1.52 times the purchase price, because of a lesser interest rate.

John commented to the Board that the alternatives, such as tax credit, selling to a non-profit, or selling to the private market place, do exist. However, because of the way the building was originally financed, we are left with such a high mortgage on the property and that makes the alternatives negated.

Erin felt that if some of this information had been known 6 months ago, a more proactive approach could have been taken earlier on by everyone. Jody shared dialogue that the process was started a year ago and when the aggressive approach was tried, Heskin-Signet informed us that it's too early and to basically take your turn, and that to the extent that matters were negotiable, staff negotiated hard and improved the transaction considerably.

Gi felt that she, and possibly the entire Board, would be more comfortable if there was a more binding way to document the Board's intentions to pay off the 2nd and 3rd mortgages with the extra funds being designated as Restricted Funds and the purpose of this designation is to go towards debt reduction. She commented that just documenting the intentions in the form of a motion in the Minutes wasn't strong enough for a future Board to recognize and acknowledge.

Jody suggested some options to consider regarding restricting these funds.

- Adopt a Resolution.

- Consider not segregating the funds so that they can be used along with the Agency's current cash reserves for future investments. Try to invest the funds in ways that do not further restrict the use of the proceeds. For example, if the Board decides to invest these funds in a rental property, it would be best not to combine the funds with grant funds which restrict the property and its proceeds.

In response to that suggestion, Gi wondered if we could still designate the funds as being Restricted Funds with the intentions of investment purposes but keep these Restricted Funds separate from the rest. Jody indicated that could be done.

Kathleen asked for clarification on several items in the Restructuring Agreement since she was unable to attend Monday's meeting.

The group discussed the potential loan package benefits regarding lower interest rates, no prepayment penalties, 75% of the cash flow applying to the 2nd mortgage, potentially setting a 10-year goal to accumulate enough cash to pay off the debt, having the ability to acquire assets to later buy out the 2nd and 3rd mortgages, restructuring the Ratekin Tower financial picture with improved options for a future Board to inherit, and putting the GJHA in better overall financial condition.

Jody informed the Board that Friday, June 27, 2003, is the submittal deadline for the lenders to submit financing proposals for the 1st mortgage. If a decision is reached today on the Restructuring Commitment, the selection of the lender would need to be made during Monday's, June 30, 2003, Board Meeting. Heskin-Signet would then be notified of the lender selection and proceed with the Mark-to-Market Transaction.

There was some discussion as to the possibility of a higher interest rate going into affect shortly and how that would affect the repayment schedule.

In anticipation of a Board decision, Rich wrote and distributed a draft Resolution for Board review entitled "Authorizing Execution and Delivery of Documents and Other Actions to Participate in the Mark-to-Market Program with Respect to Ratekin Tower Apartments". After review and discussion, it was felt that additional language should be included as a record for the history of this transaction the Board is facing. The following additions were requested by Board Members to be incorporated into the Resolution:

- Gi requested that the amount of the current outstanding debt be listed.

- Steve requested that the reasons of "why" we are doing this be added.

Rich read aloud the incorporated changes to the Resolution. A motion was made by Steve, with a second by Gi, to accept Resolution 2003-12 as stated. There being no further discussion, a voice vote was taken with the following outcome:

4 – Approving the Resolution (Gabe, Steve, Gi, Kathleen)
1 – Opposed (Erin)
1 – Abstention (Harry)

Note: A copy of the Resolution is attached to these Minutes.

There being no further business, Erin made a motion to adjourn the meeting. With a second by Gi and a unanimous vote, the meeting was adjourned at 12:01 p.m.