TO:	Ayanna Wayner Executive Director, New Rochelle Industrial Development Agency
FROM:	Kevin F. Gremse, KFG
DATE:	November 3, 2015
RE:	165 Huguenot Street PILOT for Proposed Mixed-Use Mixed Income Development
CC:	Luis Aragon, Commissioner, Department of Economic Development Jeremy Schumer, New Rochelle Industrial Development Agency

SUMMARY

Per your request, the National Development Council (NDC) has reviewed the financial information for the proposed mixed-use, mixed-income redevelopment by East and Hudson New Rochelle, LLC (the "developer" or the "applicant"), a newly formed real estate entity comprised of experienced residential real estate executives, Anup Misra and Stanley Conway. NDC is a national not-for-profit economic development company which provides development finance advisory services to municipalities throughout the country. NDC is routinely asked to analyze financial structures of proposed developments in our client communities and determine the appropriateness of direct financial assistance or incentives such as payments in-lieu of taxes (PILOT).

NRIDA requested that NDC review the submitted financial information, including the development program, capital budget, and operating budget and make a determination on the financial need and sizing of the PILOT.

The $21.8 million project involves the construction of 71 mixed-income units and 3,000 square feet of ground floor commercial space at 165 Huguenot Street. The developer submitted two applications to the NRIDA, requesting benefits including a sales tax exemption, a mortgage recording tax exemption, and a payment in lieu of taxes (PILOT). In the first application filed in July 2015, the developer requested a 30-year PILOT commencing at $83,000 annually. In a second application, the developer requested a 15-year PILOT commencing at $101,000 annually (the current real estate tax), with 2.5% annual escalators. The recommended PILOT for your consideration is a ten year PILOT commencing at $128,000, with 3% annual escalators.

The justification for and the sizing of the PILOT will be further supported based upon the following sections of this memo. These sections include summaries of the proposed development program, sources and uses, and operating pro forma.

PROJECT

The developer currently has a purchase option for 165 Huguenot Street. The developer has proposed to demolish the six-story building on the property and construct 71 luxury apartments that are mostly intended for professional millennials. The program includes 84 market rate units and 7 workforce units. The workforce units will be leased at rents that are affordable to households earning less than 80% of area median income (AMI). The average market rate rent will be $2,175 and the average workforce rent will be $1,650. There will be 24 studios, 26 one-bedroom apartments, and 11 two-bedroom apartments. The development program will include high end finishes, extensive common area amenities for the residents, and on-site parking.

SOURCES AND USES

The sources and uses for the project include the following;

USES OF FUNDS	$	Per Unit
Acquisition	$2,832,000	$39,887
Construction Costs	$15,129,004	$213,085
Professional Fees and Soft Costs	$2,773,736	$39,067
Developer Fees	$760,950	$10,718
Carry Costs	$328,067	$4,621
TOTAL	$21,823,757	$307,377
CONSTRUCTION SOURCES OF FUNDS	**$**	**Per Unit**
Commercial Loam	$12,003,067	$169,057
JV Partner Equity	$8,838,622	$124,488
Partner Equity	$982,069	$13,832
TOTAL	$21,823,758	$307,377

The development cost is $21.8 million, equivalent to $307,000 per unit. While the costs are considered somewhat high, the higher costs are attributed to the demolition cost of the existing building as well as high-end finishes and the extensive common area amenities.

The capital structure involves the use of an institutional investor who will fund the majority of equity during the construction stage. After the project achieves stabilization, the developer plans to convert the construction loan to a permanent loan based upon the stabilized income stream and take out the investor. It is expected that the permanent loan proceeds will be approximately $19 million.

The developer reported the need to achieve a “cash on cost” ratio of 7%, defined as the stabilized net operating income (NOI) divided by project cost. While the proposed PILOT results in the cash on cost ratio falling short of the 7% targeted yield, the development with the proposed PILOT still allows the developer and investor to earn market rates of return. If the development were to be taxed at full assessment from the beginning, the developer and investor would not be able to achieve market rates of return and the development would likely not proceed.

OPERATING PROFORMA

		WITHOUT PILOT				WITH PILOT		
Market Residential Income		$1,680,210	$2,188	avg. rent		$1,680,210	$2,188	avg. rent
Affordable Residential Income		$140,045	$1,667	avg. rent		$140,045	$1,667	avg. rent
Retail Income		$72,000	$24	Sq. ft.		$72,000	$24	Sq ft.
Other Income		$97,284				$97,284		
Less Vacancy		($99,477)				($99,477)		
Effective Gross Income		$1,890,062				$1,890,062		
Operating Expenses Excl. of RE Taxes/PILOT		$319,500	$4,500	per unit		$319,500	$4,500	per unit
RE Taxes/PILOT		$216,701	$3,052	per unit		$127,692	$1,798	per unit
Total Op Expenses		$536,201	$7,552			$447,192	$6,298	
Net Operating Income (NOI)		$1,353,861				$1,442,869		
Debt Service		($1,196,314)				($1,196,314)		
Cash Flow		$157,547				$246,555		
Estimated As Complete Fair Market Value (FMV)		$24,615,657				$26,233,989	$369,493	
Reported Project Cost		$21,823,757	$307,377	per unit		$21,823,757	$307,377	per unit
Cash on Cost		6.20%				6.61%		
Cash on Cash Rate of Return		7.33%				11.48%		

PROPOSED PILOT

			SECOND DEVELOPER REQUEST				NRIDA COUNTER		
Year	Operating Year	Taxes at Full Assessment	PILOT Schedule	Escalator	Savings		PILOT Schedule	Escalator	Savings
1	Constr/Stab	**$101,142**	**$101,142**	0.00%	$0		**$101,142**	N/A	$0
2	Constr/Stab	**$101,142**	**$101,142**	0.00%	$0		**$101,142**	N/A	$0
3	1	**$225,369**	**$103,670**	2.50%	($121,698)	*	**$127,692**	N/A	($97,676)
4	2	**$229,876**	**$106,262**	2.50%	($123,614)		**$131,523**	3.00%	($98,353)
5	3	**$234,473**	**$108,919**	2.50%	($125,555)		**$135,469**	3.00%	($99,005)
6	4	**$239,163**	**$111,642**	2.50%	($127,521)		**$139,533**	3.00%	($99,630)
7	5	**$243,946**	**$114,433**	2.50%	($129,513)		**$143,719**	3.00%	($100,227)
8	6	**$248,825**	**$117,294**	2.50%	($131,531)		**$148,030**	3.00%	($100,795)
9	7	**$253,802**	**$120,226**	2.50%	($133,576)		**$152,471**	3.00%	($101,330)
10	8	**$258,878**	**$123,232**	2.50%	($135,646)		**$157,045**	3.00%	($101,832)
11	9	**$264,055**	**$126,312**	2.50%	($137,743)		**$161,757**	3.00%	($102,298)
12	10	**$269,336**	**$129,470**	2.50%	($139,866)		**$166,609**	3.00%	($102,727)
13	11	**$274,723**	**$132,707**	20.00%	($142,016)		**$274,723**	Full Taxes	$0
14	12	**$280,217**	**$136,025**	20.00%	($144,193)		**$280,217**	Full Taxes	$0
15	13	**$285,822**	**$139,425**	20.00%	($146,397)		**$285,822**	Full Taxes	$0
		$3,510,769	**$1,771,901**		($1,738,868)		**$2,506,895**		($1,003,873)

As previously mentioned, the developer originally requested a 30-year PILOT commencing at $83,000. This request was rejected, as the starting PILOT was less than current taxes ($101,000) and the term of the PILOT was considered too long. The developer amended the application to request a 15-year PILOT commencing at the $101,000, matching the current annual real estate taxes. The estimated annual real estate taxes at full assessment by the Tax Assessor is approximately $225,000 at stabilization, the third year after acquisition of the property.

The term for the counter PILOT proposed by the NRIDA term is 12 years, including the 2-year construction and stabilization period. At stabilization in year three, the NRIDA proposed PILOT commences at $127,692, an amount derived from the "revenue neutral" target of $83,000 (the costs of educating four new net students), divided by 65% (representing the percentage of each tax dollar allocated to the Board of Education). The four new students were projected based upon the formulas associated with the Rutgers University study on educational impact of rental residential development.

The proposed NRIDA PILOT results in $1,003,878 in savings to the developer during the 10-year PILOT term. This NRIDA proposed schedule results in $734,995 more in PILOT payments than what the developer requested.

The NRIDA is recommending that the PILOT be permitted to be transferred with the sale of the property if the transfer of IDA benefits conditions contained in the Resolution are met by the purchaser or assignee.

COST/BENEFIT ANALYSIS

The benefits to the City and NRIDA, measured in the form of estimated incremental taxes, impact fees, IDA fee, sales tax revenue, and value of the seven affordable units, total nearly $2.4 million over fifteen years. This is 77% greater than the costs borne by the City and IDA, or the benefits realized by the developer, in the form of tax savings through the PILOT, the mortgage recording tax exemptions, and the sales tax exemption on building materials. On a Net Present Value (NPV) basis using a discount rate of 3%, the benefits exceed the costs by a ratio of 1.12.

Gross Benefits	$2,389,563		NPV Benefits		$1,624,892
Gross Costs	$1,667,038		NPV Costs		$1,449,912
Gross Benefit/Cost Ratio	1.43		Benefit/Cost Ratio		1.12

The cost and benefits are summarized in the following two worksheets.

* *Building fees, etc. during construction*
** *To be confirmed*
*** *Assumption of $75,000 average household income, spending 10% of disposable income in New Rochelle, and 2.5% sales tax realized by City of New Rochelle*
**** *Difference between the value of the development with having 10% affordable units*

Costs (Benefits to Developer)				
Year	**PILOT Benefits**	**Sales Tax Exemption**	**Mortgage Recording Tax**	**Total Benefits**
1	$0	$507,124	$156,040	$663,164
2	$0	$0	$0	$0
3	$97,676	$0	$0	$97,676
4	$98,353	$0	$0	$98,353
5	$99,005	$0	$0	$99,005
6	$99,630	$0	$0	$99,630
7	$100,227	$0	$0	$100,227
8	$100,795	$0	$0	$100,795
9	$101,330	$0	$0	$101,330
10	$101,832	$0	$0	$101,832
11	$0	$0	$0	$0
12	$0	$0	$0	$0
13	$0	$0	$0	$0
14	$0	$0	$0	$0
15	$0	$0	$0	$0
TOTAL	$798,848	$507,124	$156,040	$1,462,012
NPV of Costs w 3% Discount Rate				$1,303,959