Rockville Housing Enterprises Rental Demonstration Program Financing Terms and Strategy

HUD RAD Program
Loan Term Requirement

- The HUD RAD application template required loan financing parameters of at least a 15 year term and a 30 year amortization with a maximum amortization of 40 years.
- The HUD RAD Program regulations allows for a Debt Service Coverage ratio (DSC) of 1.20 times net cash flow.
  - *A debt service coverage ratio of 1.2 means the property must net at least 1.2 times the amount of funds needed to pay the monthly loan note.*
- The RHE RAD financing terms will exceed the allowable DSC and will have a DSC that will exceed 1.60.

Citi Community Capital (Citi) Loan Terms

- The maximum loan amount cannot exceed $3,500,000
- The loan term is 15 years with a 30-year amortization
  - The extended amortization allows for the property to minimize debt service payments and maximize accumulated cash reserves to ensure the property has cash on hand to fund unexpected expenses.
  - *A more common term for a commercial loan of similar nature with Citi using a Freddie Mac product is 5 or 7 years.*
- The interest rate is 5.2%
  - The interest rate is reflective of a longer loan term and is competitive for the current market.

Replacement Reserve Payments

- The property will make annual replacement reserve payments of approximately $36,750.

- It is anticipated the replacement reserve account would have an approximate balance of **$551,250 at the end of the 15-year term**.

Accumulated Net Cash Flow

(Funds remaining after property expenses and loan payments are made)

- Anticipated accumulated net cash flow after debt service at the end of the 15 years is estimated at **$2,250,000.**
- The total of the accumulated net cash flow and replacement reserves in this scenario would be **$2,801,250.**
  - ***$551,250 in accumulated replacement reserve + $2,250,000 in accumulated net cash flow = $2,801,250***
  - *These funds would be used to fund any capital improvements and other property expenses in excess of budgeted costs over the 15 year loan term.*

Initial Loan Repayment Strategy

- The remaining principal balance due at the end of the 15-year loan is estimated at **$2,335,377**.
- The approximate total of the accumulated net cash flow and replacement reserves in this scenario would be **$2,801,250**.
- The remaining balance of the loan could be retired at the end of the 15-year term with approximately $465,873 remaining.
  - $2,801,250 - $2,335,377 = 465,873 remaining
- The loan repayment terms require payment of the entire amount of interest to be earned by Citi for 14.5 years of the 15-year term of the loan. While the property could pay down the loan early, there is no financial advantage to do so.

Projected Loan Retirement

Initial Loan Retirement Projection	
Principal Remaining at end of Initial 15 YR Period	$2,335,377
Amount of Accumulated Net Cash Flow and Replacement Reserves ($551,250 in accumulated replacement reserve + $2,250,000 in accumulated net cash flow)	$2,801,250
Amount remaining after balance of loan is paid (This amount could be reduced if capital repairs are made during the initial 15 YR period)	$465,873

Year 15 - 30

Attach B

Repair/Replacement Strategy

- Conservative repair/replacement expenses at the end of the 15-year term are estimated to be $10,000 a unit or $1,050,000.
- A Physical Needs Assessment will be completed to determine the extent of the capital repair/replacement required.
- Below are estimated work items to be completed at the end of the 15-year term based on product life cycle expectations.
  - New roofs will have a 20-25 year life cycle and will not have to be replaced at the end of year 15.
  - Siding and windows should not need replacement.
  - Interior and exterior doors are not anticipated to need replacement.
  - HVAC units and water heaters have a 20 year life cycle and will be replaced as needed.
  - Refrigerators and other appliances may need to be replaced after 15 years.
  - Cabinets in the kitchens and bathrooms should not need to be replaced after 15 years.

Two Options for YR 15 Capital Improvements

1. **RHE can pursue additional financing to complete the estimated $1,050,000 in repairs at one time**
   - An estimated loan amount would be approximately **$594,127**
     - Estimated loan amount based on amount remaining after the balance of the initial loan is retired ($1,050,000 of estimated work to be completed - $465,873 remaining after initial loan retired)
   - The estimated loan of **$594,127** could be financed with a 5 or 7 year loan term which could be paid off at the end of the loan term
     - The financing terms for a loan in year 2030 are based on assumptions and estimations; it is not possible to predict the market 15 years from now.
2. **RHE can complete the repairs over time using funds available from accumulated net cash flow and replacement reserve funds once the initial mortgage is retired; estimated at an additional $19,500 in monthly cash flow or ($234,000) annually**
     - $234,000 represents funds previously dedicated to debt service payments for the initial mortgage.

Deciding on a Strategy for YR 15 Capital Improvements

- RHE will make a final determination on which approach to take to complete property capital repair/replacement at the end of the initial 15-year loan.
- The financing approach will depend on market conditions, regulatory constraints and the financial position of the property at that time.