MANSERMAR DEVELOPMENT

May 12, 2023

Ms. Marisa Button
Director of Multifamily Programs
Florida Housing Finance Corporation
227 N. Bronough Street, Suite 5000
Tallahassee, FL 32301

Dear Marisa:

We are writing today to submit comments for the current Rule Development for the upcoming 2023-2024 RFAs, specifically related to our efforts to redevelop Magnolia Gardens and other properties assisted with HUD Project Rental Assistance Contracts (PRACs) in Florida.

Magnolia Gardens is an 88-unit property in Daytona Beach, Florida that was originally developed utilizing the HUD Section 202 Capital Advance program with PRAC. It was first occupied in 1995, once construction was complete on the 3-story elevator structure. The property was developed to serve very low-income seniors (62+), earning 50% or less of the AMI. The 202 Capital Advance was, essentially, a grant from HUD which is forgiven 1/40th each year if the strict compliance is met. The community was developed under HUD's "Cost Containment & Modest Design" era with a very tight construction budget and currently has many capital needs due to HUD's tight restrictions on the annual budget and very limited rent increases over the years.

This development has never had a rehabilitation nor any major capital infusion, primarily due to the financing structure with limited reserves and no cashflow to the owner. The building has aged prematurely due to the lack of necessary funding for repairs and upgrades. It needs a substantial rehabilitation to keep the community in good shape and to maintain the affordability to its very low-income residents for at least the next 20 years. It is critical to preserve Magnolia Gardens and similar PRAC properties as they serve Florida's most vulnerable residents, very low-income seniors.

We would like to propose a few changes to the current Preservation and/or SAIL RFAs through which FHFC can offer greater support to RAD for PRAC properties, as we feel the rehabilitation and preservation of these properties is a worthwhile policy objective for Florida Housing, especially in light of recent changes in HUD's RAD program meant to facilitate the preservation of these assets.

1. **SAIL RFA for Preservation of Senior Properties: We request FHFC to consider increasing the amount of SAIL funds available in this RFA.** In 2023, the funding amount available was approximately $2.1 million. Due to the restrictions of the PRAC program, these properties need a larger amount of SAIL funds than what was offered this year. PRAC properties have historically been unable to make requisite capital improvements and major maintenance upgrades due to

the program parameters, described in further detail in this letter. The result is that these properties are aging faster than most properties of a similar era and are constantly patching up instead of doing proper replacements of major building components. The corresponding higher amount of capital needs required simply cannot be supported with $2 million in SAIL. We request that FHFC consider increasing the funding amount in this Preservation RFA to an amount similar to what is available in the general SAIL RFA for rehabilitations, so PRAC properties can compete for the amount of funding required to perform the substantial rehabilitation that both FHFC and the owner want to see happen.

2. **FHFC's Preservation RFA: We request that the Age of Development Funding Preference be changed from 30 years or older to 20 years or older for PRAC properties.** Properties that are subsidized by the PRAC program have a limited amount of funds available towards capital expenditures, described in further detail in this letter. Therefore, these properties cannot be as well maintained as other HUD-subsidized properties, causing the need for a substantial rehabilitation to be sooner than 30 years. Therefore, we request that FHFC consider allowing PRAC properties that are 20 years or older to automatically qualify for the Age of Development Funding Preference, so that these properties do not continue to deteriorate while waiting to meet the 30-year mark.

3. **General SAIL RFA: We request that FHFC consider adding a goal to fund RAD for PRAC applications in the Preservation RFA**, so that the state of Florida can start to make a dent in the backlog of preservation of these properties. Rehabilitation properties, which include PRAC properties, are only eligible for funding if there is enough SAIL funds available after all the goals are met. It is very difficult to be competitive in this RFA without a property meeting a stated goal. Furthermore, PRAC projects specifically are not able to support as much permanent debt, putting them at a disadvantage in leveraging. We request that FHFC consider adding a goal of funding two RAD for PRAC properties spread among the different county sizes in the SAIL RFA. This would put these valuable preservation opportunities on equal footing with New Construction applications, while recognizing the importance of preserving these very challenged assets.

With these proposed changes, FHFC can offer greater support to the rehabilitation of these properties that allows us to serve Florida's most vulnerable low-income seniors.

Furthermore, in this letter, we have outlined some of the specific challenges that PRAC properties face as they are trying to rehabilitate their properties and preserve their affordability.

1. The current financial structure of the properties

A Project Rental Assistance Contract ("PRAC") is a rental subsidy that covers the operating expenses and the reserve deposits of the property minus the residents' portion of the rent. This financing structure was funded by HUD only to a 501c3 non-profit owner, through the HUD Section 202 Capital Advance program, and it is designed to have a breakeven operating budget each year with no net cashflow whatsoever to the owner. Please note that it does not include debt service. With the conversion of the HUD Section 202 program to the Capital Advance program, the rental subsidy was reduced by the amount of the debt service and the loan was forgiven instead of being paid back to HUD. This resulted in an initial rent amount that was much lower than contract rents for other HUD-assisted properties.

The PRAC is a blessing to the residents of the property, however, it also creates a very tight budget for the property management team, and securing HUD approval for rent increases to cover capital items is a very difficult and subjective process. Since the PRAC does not cover debt service, there is no way to traditionally refinance and rehabilitate the property due to the low rents. This is what led to HUD's creation of the new HUD Rental Assistance Demonstration (RAD) for PRAC process, described in further detail below.

2. **Challenges in Obtaining Rent Increases = Less money to maintain the properties**

Obtaining rent increases for operations are particularly challenging at PRAC properties where rents are limited. Properties submit proposed budgets based on expected operating costs for review by a HUD project executive each year to establish the rent increase for the year. HUD generally limits the increase to cover the prior year audited expenses with no greater than a 5% increase or current year actual expenses on an annualized basis, unless substantial support is provided that would demand a larger increase. Obtaining a larger increase is very difficult. Even in recent years when the cost of living and inflation causes increased costs, unless a contract is in place or the utility has published their increase before the budget is submitted, the increased funds for higher rents are not approved. These budgets are designed to breakeven and the non-profit only has reserves for capital items at an amount approved by HUD. The typical rent increase approved by HUD is usually between 1 to3% a year and does not consider aging equipment that requires increasingly more maintenance each year. Therefore, even if the non-profit owner needs higher rents in order to fund operations, it does not have the funds to spend. In order to increase rents, the non-profit would have to fund the additional operating expenses and maintenance to support the higher operating expenses, with no mechanism for reimbursement for those costs.

3. **Challenges to Increased Replacement Reserves and Capital Improvements/Major Maintenance Projects**

To obtain an increase in the rents to support additional reserves for replacement requires submission of a 20-year schedule of capital items and replacement needs, which is then subject to the same subjective review as the annual rent setting process. This also results in approved reserves below what the property requires, causing the Owner to make choices as to what systems can be repaired or replaced.

Furthermore, HUD requires that the property maintain a reserve fund of a minimum of $1,000 per unit as a contingency in case of a significant issue at the property, further limiting the amount of reserves available for ongoing capital needs. As the building ages, the cost and needs for maintenance quickly outpace the funding available in the reserves. Because of the limited funding available from HUD and the inability to obtain outside funding, repairs and improvements must be made piecemeal or as bandage to keep systems working rather than being able to fund a complete replacement to any specific area.

Due to the difficulties noted above and the pressure on the HUD field staff to keep rent increases to a minimum, it is often difficult to obtain increases in the reserve deposits sufficient to support the level of capital improvements that need to occur. Since the property is also limited in its ability to fund preventative maintenance from operations, even the funds for major emergencies are insufficient to truly solve the problem, like when a roof leaks and needs to be replaced or an elevator or boilers fail and must be replaced. The owner is then left to repair versus replace systems. Apartments are turned when residents leave, but the work is typically limited to cleaning and painting due to having limited funds. Appliances and systems are replaced only when they fail, as funding is not available to complete a proactive replacement program. Pipe leaks are often repaired as opposed to replacements, that may need to occur.

For example, Magnolia Gardens has requested at least three times for a roof replacement to be funded on the building and has been denied all three times. It was suggested that only part of the roof should be replaced because the cost was too great to replace the entire roof. The roof structure on this building does not permit partial replacement, therefore the only option was to repair. Unfortunately, that repair did not solve the issue and the project continues to struggle with a damaged roof in need of replacement.

4. **Challenges in the PRAC to RAD Conversion Process**

i. **The rent increase process:** Until the announcement of the new HUD Rental Assistance Demonstration (RAD) for PRAC process, none of the Capital Advance/PRAC properties were able to refinance/restructure. The RAD for PRAC process allows PRAC properties the possibility of increasing their rents and securing a new Section 8 Project-Based Rental Assistance (PRBA) Contract, which automatically renews every 20 years. With these higher rents and long-term Contract, HUD created this process with the hope that these properties across the country would be able to secure new financing to allow them to undertake the substantial rehabilitations they desperately need. While the housing industry is grateful for this relatively new program, our experience is that it is a challenging process with relatively limited rent increases available.

The RAD for PRAC rent increase process requires owners to submit a Capital Needs Assessment (CNA) to their local HUD field offices, so that HUD staff can determine the appropriate annual replacement reserve deposit to address the 20-year capital needs schedule in a CNA. Once this amount is determined by the local HUD staff, the HUD RAD office will set the RAD rents to the sum of the current PRAC rents plus the additional replacement reserve deposit amount determined by the local HUD office, on a per unit per month basis. From our experience, the challenge with this process is that each local field office staff evaluates this replacement reserve amount based on its interpretation of the validity of the capital needs depicted in the CNAs. It should also be noted that the reserve deposit increase allowed as a part of the rental increase process is limited to the lesser of the 5 year or 20-year calculation which can produce substantially different results, and no rent increase is allowed as a part of the conversion process, which contributes to the difficulty in securing rents sufficient to support debt on the project.

The rent-setting for these RAD for PRAC properties is different than typical Section 8 PBRA Contracts from the 1970s and 1980s, which have been allowed to increase their rents to be comparable to other similar properties in the market area. As a result, many of these PBRA properties have been able to secure substantial rent increases if their surrounding neighborhoods have appreciated in value. In addition, HUD allows certain PBRA properties to base their rent increases on comparable properties to the PBRA property after it undertakes a substantial rehabilitation (often called "post-rehab rents"). In contrast, the RAD for PRAC properties' rents are not influenced by market comparable rents and therefore PRAC property owners are not able to secure any rent increases based on the appreciation of values in their market areas. This has typically meant that the RAD for PRAC rents are not as high as other Section 8 PBRA properties undertaking similar rehabilitation work scopes.

In addition, the rent-setting for RAD for PRAC properties is different than public housing properties that convert to a RAD Section 8 Contract. The RAD rents for public housing properties are based on a public housing authority's (PHA's) current public housing subsidies it receives from HUD. Those public housing subsidies often are higher than the existing PRAC subsidy, and therefore their RAD rents are sometimes higher than the RAD rents for PRAC properties. In addition, PHAs have several possible options to increase their initial "base" RAD rents by transferring a portion of rents from one property to another, or being located in a federal Opportunity Zone, or implementing energy efficient improvements that decrease units' Utility Allowances, or adding funds to the RAD rents from its own pool of HUD funds if the PHA is a Moving to Work agency. None of these options are available for RAD for PRAC properties.

ii. **Lower Permanent Mortgages:** As a result of these low RAD for PRAC rents, and the resulting lower Net Operating Income to service debt, RAD for PRAC properties' commercial first mortgages must typically be sized lower than mortgages on other types of Section 8 and RAD properties. Therefore, RAD for PRAC properties need a greater amount of LIHTC equity and/or soft gap financing (such as the SAIL program) in order to achieve a feasible rehabilitation. The reality of lower rents and a lower first mortgage means that RAD for PRAC properties have a greater need for 9% LIHTCs or a greater need for soft gap financing in 4% LIHTC/tax-exempt bond executions. The lower first mortgages also put these properties at a competitive disadvantage for some of FHFC's financing resources because their debt leveraging ratios are lower than other types of projects that can support greater debt. The ongoing interest rate environment and construction cost/supply chain challenges just exacerbates the difficulties for RAD for PRAC properties to achieve financial feasibility.

The unique rent-setting constraints and the resulting limited first mortgages is one of the main reasons we ask FHFC to understand that RAD for PRAC properties are unique and therefore, we ask FHFC to consider adding special goals and/or other methods of specifically supporting RAD for PRAC properties in your upcoming RFAs.

As mentioned previously, we are in the process of trying to renovate Magnolia Gardens, which is a PRAC property located in Daytona Beach, Florida.

The proposed new owner and borrowing entity is Magnolia Gardens, LLLP. Its General Partner is Christian Towers, Inc., which is a 501c3 non-profit. Its Board of Directors is the same Board as Rebuild America of Florida, Inc., and brings all of its experience to the non-profit. Rebuild America of Florida, Inc. is a not-for-profit public benefit corporation specializing in LIHTC preservation properties. To date, Rebuild America of Florida, Inc. has closed on the financing for the rehabilitation of 11 properties, all of which are affordable senior housing properties utilizing LIHTC and encompassing 6 states. They are very mission-driven and currently in the process of working on the preservation and conversion of three PRAC properties. It is important to them to figure out a way to continue to provide safe and decent affordable housing to these seniors through the rehabilitation of these properties.

Thank you for the opportunity to provide public comments during the Rule Development process. We have provided specific examples of how RAD for PRAC properties are a unique category of developments and therefore, we ask that FHFC consider specific relief to these redevelopments. There are many PRAC properties in Florida that serve thousands of very low or extremely low-income senior citizens. All PRAC properties are currently or will face the same challenges that we are facing at Magnolia Gardens. Our team is available to answer any questions that you or other FHFC staff may have about the issues I have raised. If helpful to you, I would be happy to provide data points from our pre-development work on Magnolia Gardens and/or our recent experience rehabilitating PRAC properties throughout the country.

Thank you very much for your consideration!

Sincerely,

Celia C Watson

Celia "Cissy" C. Watson

CEO