

Evaluating Affordable Housing Development Projects

Housing Production Unit (HPU)



SESSION OVERVIEW

- **Review of Evaluating Projects by HPU**
- **Project Proforma Overview**
- **Sustainability of Projects Over the Long Term**

HPU PROJECT REVIEW

- Time of constrained resources
- Moving towards competitive applications
- Provides framework for ensuring successful project completion
- Full review of projects and proformas works to ensure project success and sustainability over the affordability period

HPU PROJECT REVIEW

- Ability to fully complete required application
- Municipal project support
- Site Control
- Leveraging of other funds- having the needed capital stack
- Planning and Zoning
- Market Information
- Operating costs over the period of affordability
- Developer capacity

Project Feasibility and Readiness



Understanding the Project Pro Forma



Overview

- **Development Budget**
- **Funding Sources**
- **Debt Services**
- **Unit Mix**
- **Operating Pro-Forma**
- **Analysis**


Development Budget-Acquisition & Construction Highlights

AHTF Application: Development Budget			
New Jersey Best Affordable Housing Project			
ACQUISITION	AHTF	Other Sources	Total
Land	\$0	\$0	\$0
Structures	\$0	\$0	\$0
Total Acquisition	\$0	\$0	\$0
CONSTRUCTION	AHTF	Other Sources	Total
Building Permits	\$0	\$0	\$0
Water Supply Connection Fees & Permits	\$0	\$0	\$0
Sewer Connection Fees & Permits	\$0	\$0	\$0
Performance Bond	\$0	\$0	\$0
Demolition	\$0	\$0	\$0
Environmental Remediation	\$0	\$0	\$0
Site Work	\$0	\$0	\$0
Construction Material & Labor Cost	\$0	\$0	\$0
Electric Service Connection Fees	\$0	\$0	\$0
Gas Service Connection Fees	\$0	\$0	\$0
Other (Specify on Additional Costs Tab)	\$0	\$0	\$0
Subtotal	\$0	\$0	\$0
Contractor General Requirements	\$0	\$0	\$0
Contractor Overhead	\$0	\$0	\$0
Contractor Profit	\$0	\$0	\$0
Construction Contingency	\$0	\$0	\$0
Total Construction	\$0	\$0	\$0




- Acquisition may be land only or include structures.
- Line items in the Construction section should be reflective of the type of project. Example: New construction projects have different cost items than rehabilitation projects.
- Contractor General Requirements are indirect costs incurred by the General Contractor to successfully construct the project. Examples: project management, temporary office trailers, Porta Potties, safety fencing, waste removal, etc.
- Contractor Overhead are the costs incurred by the General Contractor that are not related to the project. Examples: office rent, salaries, insurance, equipment, vehicle cost, etc.
- Construction Contingency is a “just in case” budget item that is used for unexpected construction costs.

Development Budget-Professional Services Highlights

AHTF Application: Development Budget			
New Jersey Best Affordable Housing Project			
PROFESSIONAL SERVICES	AHTF	Other Sources	Total
Accountant	\$0	\$0	\$0
Appraisal	\$0	\$0	\$0
Architect	\$0	\$0	\$0
Attorney	\$0	\$0	\$0
Construction Cost Certification	\$0	\$0	\$0
Energy Star Consultant	\$0	\$0	\$0
Engineer	\$0	\$0	\$0
Environmental Consultant	\$0	\$0	\$0
Market Study (3rd Party)	\$0	\$0	\$0
NJ Housing Affordability Service (HAS) Fee	\$0	\$0	\$0
Marketing & Advertising	\$0	\$0	\$0
Planning & Zoning Fees	\$0	\$0	\$0
Planner	\$0	\$0	\$0
Realtor	\$0	\$0	\$0
Security	\$0	\$0	\$0
Surveyor	\$0	\$0	\$0
Other (Specify on Additional Costs Tab)	\$0	\$0	\$0
Subtotal	\$0	\$0	\$0
Professional Services Contingency	\$0	\$0	\$0
Total Professional Services	\$0	\$0	\$0

- Professional Services costs are often called Soft Costs which are costs unrelated to construction.
- All projects will have many of Professional Services costs listed.
- A Construction Cost Certification is prepared by an independent accountant after construction is completed and provides a detailed review and comparison of the Development Budget to actual costs incurred and which sources of funds were used to pay for the costs.
- All HPU funded projects that are new construction must be built and certified to Energy Star standards.
- All DCA Affordable Housing Trust Fund projects must be marketed through NJ Housing Affordability Service for a fee.
- Professional Services Contingency is a “just in case” budget line item that is used for unexpected costs.

Development Budget-Carrying & Financing Highlights

AHTF Application: Development Budget			
New Jersey Best Affordable Housing Project			
CARRYING & FINANCING	AHTF	Other Sources	Total
Interest	\$0	\$0	\$0
Real Estate Taxes	\$0	\$0	\$0
Electric & Gas Charges	\$0	\$0	\$0
Water Usage Charges	\$0	\$0	\$0
Sewer Usage Charges	\$0	\$0	\$0
Lender & Funder Fees	\$0	\$0	\$0
Property Insurance (Liability & Builder's Risk)	\$0	\$0	\$0
Title Insurance	\$0	\$0	\$0
Recording Fees	\$0	\$0	\$0
Other (Specify on Additional Costs Tab)	\$0	\$0	\$0
Subtotal	\$0	\$0	\$0
Carrying & Financing Contingency	\$0	\$0	\$0
Total Carrying & Financing	\$0	\$0	\$0

- Carrying & Financing costs are related to the cost of maintaining the project and the cost of obtaining financing or funding during the acquisition and construction phase.
- All projects will have many of Carrying & Financing costs listed.
- Carrying & Financing Contingency is a “just in case” budget line item that is used for unexpected costs.

Development Budget-Working Capital & Project Reserves Highlights

AHTF Application: Development Budget			
New Jersey Best Affordable Housing Project			
WORKING CAPITAL	AHTF	Other Sources	Total
Operating Deficit Reserve (Up to 18 Months)	\$0	\$0	\$0
Supplemental. Mgmt. Fee & Marketing	\$0	\$0	\$0
Purch. of Maintenance & Other Equipment	\$0	\$0	\$0
Other (specify on Additional Costs Tab)	\$0	\$0	\$0
TOTAL WORKING CAPITAL	\$0	\$0	\$0
PROJECT RESERVES	AHTF	Other Sources	Total
Capitalization of Operating Reserve	\$0	\$0	\$0
Capitalization of Replacement Reserve	\$0	\$0	\$0
TOTAL PROJECT RESERVES	\$0	\$0	\$0



- Working Capital costs are related to the costs incurred for negative cash flow due to partial occupancy during lease up, supplemental marketing if needed, purchase of specialized equipment or furniture.
- Working Capital costs are very common for Special Needs or Supportive Housing projects, less so for other projects.
- Project Reserves in the Development Budget are for capitalized reserves to cover projected cash flow shortfalls or anticipated capital repairs. This is common in existing housing that has significant rehabilitation needs and Special Needs or Supportive Housing projects serving populations with little income.

Debt Service Highlights

AHTF Application: Debt Service

New Jersey Best Affordable Housing Project



Funding Source Type	Funding Source Name	Permanent Amount	Lender & Funder Fees	Term Length (Months)	Interest Rate % or Cash Flow %	Amoritized Monthly Debt Service	Actual Monthly Debt Service	Terms of Repayment	Notes for Debt Service
AHTF	AHTF	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
0	0	\$0.00				\$0.00			
	Total	\$0.00	\$0.00			\$0.00	\$0.00		

- Understanding a project’s funding sources and how firm the funding commitments are is critical to determining if a project is financially feasible and will start and finish construction in a reasonable time frame.
- It is important to review funding source term sheets, commitment letters, or loan documentation to understand the terms of financing and repayment which impacts the project’s cash flow and profitability.
- Loans for rental projects may have fixed or variable interest rates, may be short term, intermediate term, or long term loans requiring monthly principal and interest payments. Other loans may be interest only loans and require a balloon payment at the end of the loan term or be structured as a cash flow loan paid annually based on the net cash flow of the project after mandatory debt service is paid.

Operating Pro Forma – Income & Expense Highlights

AHTF Application: 20 Year Operating Pro Forma						
		YEAR OF OPERATION				
INCOME	Annual % Increase	1	2	3	4	5
Annual Net Rent	2.50%	165,804	169,949	174,198	178,553	183,017
Vacancy Rate	7.00%	-11,606	-11,896	-12,194	-12,499	-12,811
Net Residential Income		154,198	158,053	162,004	166,054	170,205
Ancillary Income (ie. Laundry, Vending)	0.00%	0	0	0	0	0
Other Rent (ie. Commercial, Parking)	0.00%	0	0	0	0	0
Total Effective Income		\$154,198	\$158,053	\$162,004	\$166,054	\$170,205
ANNUAL EXPENSES						
Administration	% Increase	1	2	3	4	5
Property Manager Payroll & Fringe	0.00%	0	0	0	0	0
Management Fee	3.00%	9,252	9,529	9,815	10,110	10,413
Accounting and Audit	3.00%	8,000	8,240	8,487	8,742	9,004
Legal	0.00%	0	0	0	0	0
Advertising	0.00%	0	0	0	0	0
Office Supplies & Equipment	0.00%	0	0	0	0	0
Other:	0.00%	0	0	0	0	0
Other:	0.00%	0	0	0	0	0
Other:	0.00%	0	0	0	0	0
Total Administration		\$17,252	\$17,769	\$18,303	\$18,852	\$19,417
Maintenance & Operations	% Increase	1	2	3	4	5
Maintenance & Repair Payroll + Fringe	0.00%	0	0	0	0	0
Maintenance & Repair Materials	3.00%	2,800	2,884	2,971	3,060	3,151
Maintenance & Repair Contracts	3.00%	2,070	2,132	2,196	2,262	2,330
Garbage & Recycling	3.00%	4,920	5,068	5,220	5,376	5,538
Pest Control	3.00%	740	762	785	809	833
Landscaping	3.00%	1,240	1,277	1,316	1,355	1,396
Snow Removal	3.00%	750	773	796	820	844
Security	0.00%	0	0	0	0	0
Other: Janitorial	3.00%	4,200	4,326	4,456	4,589	4,727
Other: Fire Alarm Monitoring Service	3.00%	600	618	637	656	675
Other:	0.00%	0	0	0	0	0
Total Maintenance & Operations		\$17,320	\$17,840	\$18,375	\$18,926	\$19,494


- The Development Budget Operating Pro Forma projects the anticipated income and expenses of the project and provides a good estimate of how the project will work financially.
- Because rents increase over time due to market conditions as well as the costs to operate the building increase, the pro forma calculations are done with an annual percentage factored in.
- Projects will have their own unique mix of expenses as it depends on the ownership structure of the project, how much staff is required to manage the project, and the costs of goods and services.

Operating Pro Forma – Reserves & Debt Service Highlights

Reserve Contribution		1	2	3	4	5
Operating Reserve		0	0	0	0	0
Replacement Reserve		2,500	2,500	2,500	2,500	2,500
Total Reserve Contribution		\$2,500	\$2,500	\$2,500	\$2,500	\$2,500
TOTAL EXPENSES		\$74,172	\$76,395	\$78,687	\$81,051	\$83,490
Net Operating Income		\$80,026	\$81,658	\$83,317	\$85,003	\$86,715
Debt Service		1	2	3	4	5
Mandatory		65,517	65,517	65,517	65,517	65,517
Percentage of Cash Flow		7,254	8,071	8,900	9,743	10,599
Soft		0	0	0	0	0
Miscellaneous Debt:		0	0	0	0	0
Total Debt Service		\$72,771	\$73,588	\$74,417	\$75,260	\$76,116
DSCR - Mandatory		1.22	1.25	1.27	1.30	1.32
DSCR - Total		1.10	1.11	1.12	1.13	1.14
Cash Flow		\$7,254	\$8,071	\$8,900	\$9,743	\$10,599
Other Cash Flow to Operating Reserve:		0	0	0	0	0
Net Cash Flow		\$7,254	\$8,071	\$8,900	\$9,743	\$10,599
Operating Reserve		1	2	3	4	5
Beginning Balance		\$0	\$0	\$0	\$0	\$0
Interest Earned	1%	\$0	\$0	\$0	\$0	\$0
Payment to (draw from) cash flow		\$0	\$0	\$0	\$0	\$0
Ending Balance		\$0	\$0	\$0	\$0	\$0

- The Development Budget Operating Pro Forma projects the anticipated income and expenses of the project and provides a good estimate of how the project will work financially over time.
- An Operating Reserve contribution helps cover loss of income due to high vacancies, market conditions, etc. This is common with Supportive or Special Needs Housing projects.
- A Replacement Reserve contribution helps the project cover major capital improvements a project may need as the project ages or due to a catastrophic event such as a fire or flood.
- The Debt Service calculation is based on the information entered on the Debt Service tab and a Debt Service Coverage Ratio calculation is made by dividing Net Operating Income by the Mandatory Debt Service. Generally, a 1.2 or higher ratio is desirable.

Underwriting Analysis - Highlights

AHTF Application: Underwriting Analysis					
					
Contingency Analysis		Result	Maximum	Minimum	Acceptable
1	Is the Construction contingency within the standard?	2.84%	5.00%	2.00%	Yes
2	Is the Professional Services and Carrying & Financing contingencies within the standard?	4.41%	5.00%	2.00%	Yes
Development Budget Analysis		Result	Maximum	Minimum	Acceptable
3	Is the developer's fee within the standard?	2.85%	8.00%	2.00%	Yes
4	Is the Profit, Overhead & General Requirement cost within the standard?	6.55%	14.00%	6.00%	Yes
5	Are the "soft" project costs within the standard?	9.83%	28.00%	0.00%	Yes
6	For projects utilizing Low Income Housing Tax Credit Financing, is the net equity received greater than or equal to the minimum?	\$0.00	-	\$0.85	Yes
Operating Pro Forma Analysis		Result	Maximum	Minimum	Acceptable
7	Are the annual operating expenses within the standard of 35% to 50% Total Effective Income?	\$7,417.19	\$7,709.89	\$5,396.92	Yes
8	Is the percentage change in net income within the standard?	2.04%	3.00%	1.00%	Yes
9	Is the percentage change in operating expenses within the standard?	3.00%	3.00%	1.00%	Yes
10	Does the project have a debt coverage ratio of 1.20 or greater on <u>mandatory debt</u> ?	1.22	-	1.20	Yes
11	How much additional debt can the existing cash flow support?	\$51,937.00	-	\$0.00	Yes
12	Is the vacancy rate within the standard?	7.00%	7.00%	4.00%	Yes
13	Is the annual management fee less than \$80.00 per unit per month?	\$77.10	\$80.00	\$0.00	Yes
14	Is the annual management fee less than 8.00% of Total Effective Income?	6.00%	8.00%	0.00%	Yes
Reserve Analysis		Result	Maximum	Minimum	Acceptable
15	Is the annual contribution to the replacement reserve per unit a minimum of \$250.00?	\$250.00	-	\$250.00	Yes
16	Is the initial operating deficit reserve less than 18 months of operating expenses plus debt service?	\$0.00	\$220,414.85	-	Yes

- HPU has underwriting guidelines specific to each of its funding programs that are based on a combination of statutory and regulatory requirements and best practices.
- Other lenders and funders may use different criteria and standards. If the criteria or standards conflict, HPU works with other lenders and funders to resolve differences.
- It's important to remember that all projects are unique in their own way. What works for one project may not work for a different project.
- Ultimately, the goal is creation of safe, decent, affordable housing for low- and moderate-income households that can operate with positive cash flow and be maintained in good repair for the duration of its affordability period.

HPU Rental Portfolio

371 Projects · 16,588 Units · \$517.6M Invested

An estimated **15–25% of the portfolio is distressed** — spanning the full spectrum of sponsor types, from for-profit to nonprofit, experienced to inexperienced operators

The Capital Cliff: Year 20–25



Most affordable housing assets require major capital reinvestment between years **20 and 25**. Replacement reserves alone rarely cover the gap.

Initial deal structure can either position a project for this moment — or make recovery far more difficult.

Refinance

Leverage existing equity and improved cash flow

New Capital

Equity infusion, subsidies, or public financing

Why Distressed Properties Can't Be Ignored

Neighborhood Blight

Drag on surrounding property values and community reinvestment

Tenant Safety Risk

Deferred maintenance creates hazardous living conditions

Predatory Buyers

Targeted by speculators who prioritize extraction over preservation

Self-Reinforcing Decline

Without intervention, distress compounds and recovery costs escalate



Most Distress Is Preventable

The root causes of portfolio distress are rarely sudden — they develop over years. Two disciplines, applied early, prevent the majority of failures.



Underwriting

Realistic budgets, quality, sponsor capacity

Monitoring

Early intervention, trends, site visits

Compliance

Covenants and performance oversight

Applying both pillars from acquisition through the full hold period is the most effective strategy for preserving asset value and protecting residents.



Know Your Developer (KYD) (KYD)

Portfolio Experience ≠ Property Management

A strong development track record does not guarantee operational competence. Assess asset management and property management capabilities separately.

How Do They Handle Problem Projects?

Look for a pattern: Do they ignore issues, sell at a loss, inject capital, or work through problems systematically? Behavior under stress is the true test.

Underwriting the Operating Budget



→ Are Costs Reasonable?

Benchmark against industry standards for Maintenance and administrative expenses

→ Long-Term Cost Trajectory

Model inflation, component replacement cycles, and utility escalation

→ Replacement Reserve Discipline

Are contributions adequate and consistent — or deferred to boost short-term cash flow?

→ Controllable vs. Fixed Costs

Projections reflect which line items management can actively influence

Underwriting the Development Budget

Material Durability

Construction quality determines the timing and cost of future capital needs. Lower upfront costs often mean earlier, larger reinvestment.

- Roof, envelope, and mechanical system lifespan
- Interior finish quality and replacement cycles
- Accessibility and code compliance standards

Energy Efficiency

Efficiency investments reduce operating costs and extend reserve runway — a critical factor for long-term affordability.

- HVAC, lighting, and water heating systems
- Building envelope and insulation



Developers New or "New to You": Due Diligence Essentials



Background Checks

Verify track record with restricting entities — Section 8 experience does not equal LIHTC or UHAC competency.
Efficient due diligence research establishes baseline identity verification, confirming names and aliases, reviewing addresses, and uncovering instances of negative press that reflects public experience and opinion



Competency

Portfolio of comparable projects at similar scale and restriction type
Assessing or creating records of property ownership, transaction history, and property management in order to assess capacity for taking on similar or more complex projects.



Capacity

Staff or consultant bandwidth — how many new projects are they absorbing, and what is the operational plan?
Due diligence research, conducted through public records or research platforms, identifies business affiliations and corporate structures to uncover involved parties and conflicts of interest, which may affect an organizations capacity for compliance.



Track Record

Ask the restricting entity directly about history, compliance, and responsiveness
Through sufficient research, one can compile litigation history, liens, judgments, and bankruptcies to further evaluate financial stability and possible trends of noncompliance.



Essential Resources

Due diligence research can be conducted through **FREE**, easily accessible means, including but not limited to: **Bankruptcy & Litigation: PACER, NJ eCourts**, and other **county court records**.
Google to find news articles about a person/organization of interest.
In-depth research can be conducted through paid search engine platforms, such as **LexisNexis+** and **Thomson Reuters** products, including **CLEAR**.

Monitoring: The Key to Early Intervention

Desk Monitoring

- **Financial statements** — 2–3 years of trends; auditor flags signal accounting or management issues
- **Debt service coverage** — confirm operating expenses including debt are fully covered
- **Replacement reserves** — verify consistent contributions
- **Receivables & payables** — large balances signal cash flow stress
- **Vacancy rates** — may indicate market or management problems
- **Uncollected rents** — typically a management issue
- **Affordability controls & insurance** — compliance and coverage status

Site Visits

Every 3 years, someone should physically inspect the property. Leverage local building departments, BHI (4+ units), Section 8, and tax credit monitors. Use public records and online sources where available.

- **Life safety issues**
- **Routine maintenance conditions**



POLICY LEVERS

What Municipalities Can Do

Local governments have enforceable tools to protect affordable housing assets — outcomes are optimized and costs are minimized if they actively monitor and act on early warning signs.



Enforce Default Conditions

Tie funding, PILOTs, and redeveloper agreements to upkeep standards and timely municipal payables



Right to Replace Management

Reserve contractual authority to change property management when performance deteriorates



Monitor Actively

Early detection is the prerequisite for effective intervention — you can't fix what you can't see

THANK YOU

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