Gap Financing Analysis for Mixed-Use Development at 815 Vermont Street

Collaborative Architects, PC

Defining the "Financing Gap"

- **A project's financing gap is defined as the difference between projected costs (uses) and the debt and equity (sources) it can reasonably attract as follows:**

Total Project Costs

- Bank Loan

- Equity

= Financing Gap

Defining the Financing Gap (cont.)

Project Costs – are they reasonable & adequate?

- Bank Loan – maximized given lender terms?
- Equity – fair return without undue enrichment?

Gap – are there public sources available to close?

815 Vermont: Requested Gap Financing

- **NDC's analysis (memo dated October 3, 2016) of the request for a 75% NRA rebate for 10 years and an IRB sales tax exemption found the request to be reasonable given:**
  - **The projected debt has been maximized per bank underwriting criteria and market conditions**
  - **Projected sales proceeds from the residential condominiums are reasonable given the offered product and current market.**
  - **Developer returns on invested equity are reasonable with approval of the requested NRA and IRB incentives.**

815 Vermont: Returns on Invested Equity

	Amount	% of Total
Total Project Costs	**$9,275,979**	**100.00%**
Project Sources		
Projected Bank Loan	$3,404,489	36.70%
Net Condo Sales Proceeds	$3,616,086	38.99%
Required from Developer	$2,255,404	24.31%
Total Sources	**$3,622,795**	**100.00%**

- **Projected Internal Rate of Return:**
  - **With NRA and IRB incentives: 7.94%**
  - **With just NRA incentives: 7.23%**
  - **With Just IRB incentive: 6.36%**
  - **With no incentives: 5.78%**

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815 Vermont: Returns (cont.)

- **Developers and Investors demand a return on their money given their perception of Risk, Inflation and Opportunity Costs**
- **These three factors determine the discount rate (e.g., 10%, 12%, 15%, etc.)**
- **The discount rate converts future Project benefits - from cash flow, tax deductions and appreciation - to a present value and equals the Developer's desired Internal Rate of Return (IRR)**

815 Vermont: Returns (cont.)

- **Risks can be categorized as:**
  - **Predevelopment Risks – Project never makes it to construction due to a lack of adequate financing, regulatory processes and political opposition**
  - **Construction Risks – Project cannot be completed within budget due to cost overruns and change orders.**
  - **Operating Risks – insufficient revenues to pay operating expenses and debt service due to:**
    - **Lower than projected rents**
    - **Higher than anticipated vacancy rates**
    - **Higher than expected operating expenses**

815 Vermont: Returns (cont.)

- **Cost overruns during construction can lower returns by increasing the need for invested equity.**
  - **For example – a $500,000 increase in project costs for 815 Vermont would lower projected returns from 7.94% to 6.69%**
- **Higher vacancy rates, escalating expenses, and slower growth in rents can also reduce developer returns.**
  - **For example: increasing commercial vacancies from 2.6% to 10%, combined with 4% growth in expenses and 2% growth in rents (versus 3.0% for both), lowers the Developer's projected IRR from 7.94% to 6.24%.**

815 Vermont: Returns (cont.)

- The Project can also outperform projections through project cost savings, accelerated rent increases, and/or lower rates of expense escalation.
- Any of these outcomes, separately or together, could raise the projected IRR over 7.94% or could partially of fully offset adverse trends.

Conclusion

- **NDC's analysis concluded that projected benefits for the proposed mixed-use project at 815 Vermont Street - including the requested NRA and IRB incentives – provide the Developer with a reasonable 7.94% Internal Rate of Return on the equity that needs to be invested to close the gap between anticipated project costs, available debt and projected condominium sales proceeds.**

Comparison of 50-year Net Property Tax Revenue Projections

- **The numbers below compare projected net property tax collections over 50 years for the proposed project and an alternative project that includes only the commercial/retail component of the proposed project (no residential condos, no underground parking)**

50 Year Property Tax Projections		
	Project as Proposed	Alternative Scenario
Total Property Tax Revenues (Projected for 50 years)	$14,402,412	$6,271.713
Less Incentives (75% NRA Rebate for 10 Years)	$1,206,052	$0
Net Property Tax Revenues	$13,196,360	$6,271,713

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For more information

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