First Housing

**To:** Todd Fowler, Special Assets Director
Florida Housing Finance Corporation

**From:** Scott M. Eberhard, Senior Credit Underwriter
First Housing Development Corporation

**Date:** July 10, 2009

**Subject:** The Gardens Apartments (HOME Rental 92HR-009 & 9% HC 91L-024)
Assign Existing First Mortgage to a Conventional Lender, Renewal/Restructure of Existing HOME Loan, and Extension of the HOME Affordability Period

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At the request of the Florida Housing Finance Corporation ("FHFC"), First Housing has reviewed the request from Creative Choice Homes II, Ltd. ("Borrower") to assign the existing first mortgage to a conventional lender, renew and restructure the existing HOME loan in the principal amount of $3,000,000, and an extension of the HOME affordability period. The original HOME loan note, dated March 25, 1993, matured on March 24, 2008 and was extended for one (1) year to March 25, 2009. The HOME affordability period in the LURA was also extended by one year.

The restructure of the HOME loan would provide for a reduction in the current interest rate from 7.03% to 1.5%. Monthly "Hard-Pay" payments will be required for a fifteen (15) year term with a maturity date of 2024, at which time a balloon payment of the balance would be due based upon a twenty-five (25) year amortization period. The HOME affordability period in the LURA will also be extended for an additional fifteen (15) years.

The Borrower has indicated that it anticipates applying to FHFC for tax exempt bond refinancing. If that should become the case, then another underwriting of the Development will be required.

The scope of the analysis includes the following items:

1. Overview
2. Economics
3. Financing
4. Status of the Property Compliance
5. Recommendation
6. Conditions

This report shall address each of the items in turn following a brief synopsis of the transaction.

## Overview

The Development, known as The Gardens Apartments, is located at 13180 Port Said Road, Opa Locka, Miami-Dade County, FL 33054.

The Development is a 328 unit, multifamily rental apartment complex. The unit mix is as follows:

| Bedrooms | Baths | No. of Units | Unit Size (Sf) |
|---|---|---|---|
| 1 | 1 | 55 | 708 |
| 2 | 2 | 211 | 936 |
| 3 | 2 | 54 | 1,134 |
| 4 | 2 | 8 | 1,613 |
| **Total** | | **328** | **310,576** |

## Economics

The development averaged 95% occupancy in 2008. As of May 31, 2009, there were 14 vacant units (9 vacant unrented and 5 vacant rented).

The existing set asides are as follows:

**HOME** – 16 years affordability period
48 HOME units
20% (10 units) @ 50% AMI
80% (38 units) @ 80% AMI

**Housing Credits** – 30 years affordability period
328 HC units
20% (66 units) @ 40% AMI
80% (remaining units) @ 60% AMI

The Development receives project based rental assistance through the Housing Assistance Payments Program ("HAP Contract" No. FL29E000012) established by the U.S. Department of Housing and Urban Development ("HUD") that provides funding to landlords who rent a specified number of affordable units to low income families or individuals. The assistance is tied directly to the properties so tenants can generally not move without losing their assistance. The existing HAP Contract with HUD expired in August 2008. The Borrower has indicated that HUD is working to process the renewal of the contract and that the assistance is currently still available. Confirmation that the HAP Contract has been renewed shall remain a condition of this report.

The Underwriter reviewed 2006, 2007, and 2008 audited financial statements for the Borrower. The summary is described below.

**Creative Choice Homes II, Ltd.**

| Audited Financial Statements December 31, 2008 | |
|---|---|
| Cash | $14,873 |
| Total Assets | $16,955,606 |
| Total Liabilities | $17,732,057 |
| Total Equity (Deficit) | ($776,451) |

| Audited Financial Statements December 31, 2007 | |
|---|---|
| Cash | $13,689 |
| Total Assets | $16,439,255 |
| Total Liabilities | $17,480,273 |
| Total Equity (Deficit) | ($1,041,018) |

| Audited Financial Statements December 31, 2006 | |
|---|---|
| Cash | $18,222 |
| Total Assets | $18,503,267 |
| Total Liabilities | $17,144,953 |
| Total Equity | $1,358,314 |

The audited financial statements were prepared assuming the Borrower will continue as a going concern. The Borrower is currently in default on the 3rd and 4th mortgage notes, the 2nd mortgage HOME loan note matured in March 2009 but is being renegotiated as part of this underwriting report, the HAP contract expired in August 2008, and the Borrower continues to incur significant operating losses.

The audited financial statements indicate net losses of $2,399,330 and $1,614,018 were incurred in 2007 and 2006, respectively. These losses include non-cash line items of depreciation, amortization, loss on impairment of long-lived assets and related party transactions which are required by Generally Accepted Accounting Principles. The Underwriter has adjusted the 2006 and 2007 audited financial statements pro forma to reflect the development's cash-only operating expenses. The 2008 audited financial statements indicate net income from operations before depreciation of $752,975.

The rent roll unit mix below is based upon an approval letter dated September 22, 2008 from HUD increasing the rents effective November 1, 2008. Please note that the HOME restricted units are broken out using the low and high HOME rents in the chart below. These units also qualify under the HC program which is more restrictive.

| Beds | Baths | No. of Units | Unit Size (SF) | HC Median Income % | Low HOME Rents | High HOME Rents | Gross Max HC Rents | Utility Allowance | Net Max HC Rents | Net HUD Rents | Underwriter Rents | Annual Rents |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1 | 1 | 2 | 708 | 40% | $631 | - | $631 | $63 | $568 | $731 | $731 | $17,544 |
| 1 | 1 | 6 | 708 | 60% | - | $801 | $1,011 | $63 | $948 | $731 | $731 | $52,632 |
| 1 | 1 | 11 | 708 | 40% | N/A | N/A | $505 | $63 | $442 | $731 | $731 | $96,492 |
| 1 | 1 | 36 | 708 | 60% | N/A | N/A | $758 | $63 | $695 | $731 | $731 | $315,792 |
| 2 | 2 | 6 | 936 | 40% | $758 | - | $758 | $80 | $678 | $834 | $834 | $60,048 |
| 2 | 2 | 24 | 936 | 60% | - | $963 | $1,214 | $80 | $1,134 | $834 | $834 | $240,192 |
| 2 | 2 | 43 | 936 | 40% | N/A | N/A | $607 | $80 | $527 | $834 | $834 | $430,344 |
| 2 | 2 | 138 | 936 | 60% | N/A | N/A | $910 | $80 | $830 | $834 | $834 | $1,381,104 |
| 3 | 2 | 1 | 1,134 | 40% | $876 | - | $876 | $102 | $774 | $1,048 | $1,048 | $12,576 |
| 3 | 2 | 7 | 1,134 | 60% | - | $1,105 | $1,402 | $102 | $1,300 | $1,048 | $1,048 | $88,032 |
| 3 | 2 | 11 | 1,134 | 40% | N/A | N/A | $701 | $102 | $599 | $1,048 | $1,048 | $138,336 |
| 3 | 2 | 35 | 1,134 | 60% | N/A | N/A | $1,051 | $102 | $949 | $1,048 | $1,048 | $440,160 |
| 4 | 2 | 1 | 1,613 | 40% | $977 | - | $977 | $125 | $852 | $1,134 | $1,134 | $13,608 |
| 4 | 2 | 1 | 1,613 | 60% | - | 1,213 | $1,564 | $125 | $1,439 | $1,134 | $1,134 | $13,608 |
| 4 | 2 | 2 | 1,613 | 40% | N/A | N/A | $782 | $125 | $657 | $1,134 | $1,134 | $27,216 |
| 4 | 2 | 4 | 1,613 | 60% | N/A | N/A | $1,173 | $125 | $1,048 | $1,134 | $1,134 | $54,432 |
| **Total** | | **328** | **310,576** | | | | | | | | | **$3,382,116** |

## The Gardens Apartments Operating Pro Forma

| Description | 2006 Audited Financial Statement | 2007 Audited Financial Statement | 2008 Audited Financial Statement | 2009 Budget | Underwriter Annual | Per Unit |
|---|---|---|---|---|---|---|
| **Revenue** | | | | | | |
| Gross Potential Revenue | $3,193,147 | $3,225,749 | $3,216,780 | $3,421,476 | $3,382,116 | $10,311 |
| Other Income | | | | | | |
| Miscellaneous | $62,502 | $463,795 | $591,962 | $12,900 | $12,900 | $39 |
| Gross Potential Revenue | $3,255,649 | $3,689,544 | $3,808,742 | $3,434,376 | $3,395,016 | $10,351 |
| Vacancy and Collection Loss | ($432,619) | ($16,786) | ($65,144) | ($99,098) | ($169,751) | ($518) |
| **Total Effective Gross Revenue** | **$2,823,030** | **$3,672,758** | **$3,743,598** | **$3,335,278** | **$3,225,265** | $9,833 |
| | | | | | | |
| **Expenses** | | | | | | |
| Fixed | | | | | | |
| Real Estate Taxes & Insurance | $736,945 | $844,633 | $765,863 | $499,200 | $499,200 | $1,522 |
| Insurance | $0 | $0 | $0 | $256,800 | $256,800 | $783 |
| Variable | | | | | | |
| Management Fee | $115,106 | $131,379 | $0 | $128,800 | $161,263 | $492 |
| General and Adminstrative | $80,826 | $196,787 | $146,362 | $65,242 | $65,242 | $199 |
| Payroll Expenses | $189,871 | $274,863 | $209,014 | $421,314 | $421,314 | $1,284 |
| Utilities | $311,685 | $345,761 | $362,464 | $375,600 | $375,600 | $1,145 |
| Marketing and Advertising | $0 | $0 | $0 | $0 | $0 | $0 |
| Maintenance and Repairs | $341,042 | $746,621 | $1,024,762 | $229,500 | $229,500 | $700 |
| Reserve for Replacements | $0 | $0 | $0 | $81,984 | $81,984 | $250 |
| Security | $0 | $0 | $0 | $278,400 | $278,400 | $849 |
| **Total Expenses** | **$1,775,475** | **$2,540,044** | **$2,508,465** | **$2,336,840** | **$2,369,303** | $6,375 |
| | | | | | | |
| **Net Operating Income** | **$1,047,555** | **$1,132,714** | **$1,235,133** | **$998,438** | **$855,962** | $3,458 |
| | | | | | | |
| **Debt Service Payments** | | | | | | |
| First Mortgage | $1,143,408 | $1,143,408 | $1,361,388 | $0 | $0 | $0 |
| Second Mortgage | $90,000 | $90,000 | $0 | $210,900 | $234,257 | $714 |
| **Total Debt Service Payments** | **$1,233,408** | **$1,233,408** | **$1,361,388** | **$210,900** | **$234,257** | $714 |
| | | | | | | |
| **Cash Flow After Debt Service** | **($185,853)** | **($100,694)** | **($126,255)** | **$787,538** | **$621,705** | $2,744 |

| | | | | | |
|---|---|---|---|---|---|
| **Debt Service Coverage Ratios** | | | | | |
| Debt Service Coverage - 1st Mtg | | | | N/A | N/A |
| Debt Service Coverage - 2nd Mtg | | | | 4.73 | 3.65 |
| Debt Service Coverage - All Mtgs plus Fees | | | | 4.73 | 3.65 |
| **Financial Ratios** | | | | | |
| Operating Expense Ratio | | | | 70% | 73% |
| Break-Even Ratio | | | | 74% | 77% |

Notes to the Operating Pro Forma:

1. The Underwriter has utilized the HUD project based rental assistance rents although the development is income restricted by both the HOME and HC programs.

2. A 5% vacancy and collection loss rate has been used to reflect the historical vacancy rates. In October 2005, the development suffered property damage and business

interruption due to a severe hurricane. The impact affected the vacancy and collection loss through 2006. The development received a grant in 2007 in the amount of $245,500 for flood mitigation which impacted 2007 miscellaneous income.

3. A 5% management fee has been utilized.

4. The audited financial statements indicate actual net operating income for 2008 was $752,975. This does not include below-the-line expense for depreciation of $488,408.

5. The first mortgage is currently held by BVS Solutions, Inc., an affiliate of the Developer, Creative Choice Homes, Inc. A Mortgage and Note Modification Agreement dated March 5, 2009 was submitted for review. The revised terms include all principal and interest payments on the unpaid principal balance shall accrue and be deferred until the maturity date of February 1, 2010. BVS Solutions, Inc. intends to assign the first mortgage to Regions Bank at or before closing on the renegotiated HOME loan.

6. The second mortgage HOME loan annual debt service payment is based upon a principal balance of $3,000,000 plus accrued, deferred interest in the approximate amount of $1,881,129 at a 1.5% interest rate, for a 15 year term and 25 year amortization period. However, the Borrower may choose to pay off the accrued, deferred interest amount prior to or simultaneous with the closing of the restructured HOME loan.

**Financing**

The Underwriter reviewed the 2008 audited financial statements for the Borrower. The following information is based upon the 2008 audited financial statements for the Borrower.

The first mortgage note dated November 3, 1993 in the original amount of $9,500,000 payable to the Federal Home Loan Mortgage Corporation, which purchased the note from the First Housing Development Corporation of Florida, is payable in monthly principal and interest installments of $95,284 through February 1, 2009. The note bears interest at the rate of 8.81% per annum. The amount outstanding on the mortgage at December 31, 2008 was $557,300. First Housing assigned the mortgage to BVS Solutions, Inc. in January of 2009.

The second mortgage note dated February 1, 1994 in the original amount of $3,000,000 is payable to the Florida Housing Finance Corporation. The note bears interest at the rate of 7.03% per annum, of which 4.03% of interest is deferred and added back to principal as allowed by the Note. Payments of interest only at 3% are payable quarterly through the maturity date of the note on March 24, 2008 which was extended by the FHFC Board to March 24, 2009. There is a balloon payment due of principal and all accrued interest at maturity. Included in the mortgage payable balance of $4,859,930 at December 31, 2008 is $1,859,930 of deferred interest.

The third mortgage note dated January 1, 1994 in the original amount of $543,759 is payable to Sailesh Shah, Trustee, an affiliate of the general partner, in annual installments of $59,702, including interest at 7% through 2009. No payments were made during 2008. Due to technical default, the entire principal balance is included in current liabilities and interest has been compounded on the interest outstanding in arrears. The principal amount outstanding on the third mortgage at December 31, 2008 is $479,770. Accrued interest on the note totaled $676,401 at December 31, 2008. The note is not secured by the property so it is not included in the pro forma analysis. The note is currently in default.

The fourth mortgage note dated January 1, 1994 in the original amount of $500,000 is payable to Dilip Barot, an affiliate of the general partner, in annual installments of $73,412, including interest at 12% through 2009. No payments were made during 2007. Due to technical default, the entire principal balance is included in current liabilities. The principal amount outstanding on the third mortgage at December 31, 2007 is $500,000. Accrued interest on the note totaled $773,469 at December 31, 2008. The note is not secured by the property so it is not included in the pro forma analysis. The note is currently in default.

**<u>Status of Property Compliance</u>**

First Housing is currently the Compliance Monitoring Agent for the development. Based on the most recent program reports, the development is in non compliance with the Land Use Restriction Agreement requirements. The recommendation is conditioned upon this development and all other developments affiliated with the Borrower being in compliance at the time of the loan restructure contemplated herein.

First Housing performed an Annual Management Review on the development on December 11, 2008. The Development was found to be not in compliance for the physical condition of the units. Of the twenty-two (22) occupied units inspected, fifteen (15) had deficiencies. Twenty-two (22) resident files were examined. Eight (8) files contained discrepancies; one (1) was corrected on the day of the review. The laundry rooms are not in working order. Currently, they are locked and used for maintenance.

A closeout letter dated May 7, 2009 prepared by First Housing indicated that all noted discrepancies have been satisfactorily corrected.

**Does the Development team have any FHFC financed developments on the Past Due/Non-Compliance Report?**

According to the FHFC, May 15, 2009 Asset Management Non-Compliance Report, Creative Choice Homes, Inc. has the following non-compliance item(s):

- Coral Gardens - failure to annually recertify eligibility.
- Hamilton Gardens a/k/a Azalea Gardens – failure to meet Uniform Physical Condition Standards.

According to the FHFC Past Due report, dated June 23, 2009, Creative Choice Homes, Inc. has the following past due item(s):

- Andros Isle – (Bond) – Borrower past due for the 5/15/09 and 6/15/09 debt service payment in the cumulative amount of $150,458.52. Trustee initiated a transfer from debt service reserve i/a/o $80,000 on 12/2/08. On 5/18/09 Trustee sent notification to the borrower for the required amount of $71,874.93 as repayment/replenishment to the debt service reserve pursuant to the Loan Agreement and original demand on 1/13/09. Trustee filed Claim for Loss with the FHFC Guarantee Program on 6/16/09.
- Caribbean West – (HOME) – Loan matured on 5/26/09. Borrower is in credit underwriting for renegotiated HOME loan terms and extension of affordability period.
- The Gardens – (HOME) – Loan matured on 3/24/09. Borrower is in credit underwriting for renegotiated HOME loan terms and extension of affordability period.
- Heron Cove a/k/a Tuscan Isle – (Bond) – Payments due 4/15/09 i/a/o $143,590.94 and 5/15/09 i/a/o 143,590.94. Interest began accruing at the rate of $71.80 per diem on 4/30/09 on the April balance and on 6/1/09 i/a/o $71.80 per diem on the May balance. Received notice from trustee; has not received the June monthly payment due 6/15/09.
- Woods of Vero Beach – (Bond) – Payment due 5/1/09 i/a/o $63,846.42 and a payment due 6/1/09 i/a/o $63,846.42. Interest began accruing at $31.92 per diem on 5/15/09 for the May balance and on 6/15/09 on the June balance.
- Andros Isle - the 2007 and 2008 Audited Financial Statement contains a Going Concern comment.
- Heron Cove a/k/a Tuscan Isle – the 2008 Audited Financial Statement contains a Going Concern comment.
- Marina Del Ray - the 2007 and 2008 Audited Financial Statement contains a Going Concern comment.
- Mariner’s Landing - the 2008 Audited Financial Statement contains a Going Concern comment.

- Peacock Run - the 2006, 2007 & 2008 Audited Financial Statement contains a Going Concern comment.
- Woods of Vero Beach - the 2006, 2007 & 2008 Audited Financial Statement contains a Going Concern comment.

Closing of the loan is conditional upon verification that any outstanding past due, and/or non-compliance items noted at the time of closing, have been satisfied unless otherwise approved by Florida Housing.

## Recommendation

Based upon the review of the information submitted by the Borrower, and within the scope of this analysis as described herein, First Housing recommends the renewal and restructure of the existing HOME loan providing for a 1.5% simple interest rate, a 25 year amortization with a 15 year term, monthly principal and interest payments with a balloon payment at maturity, and an extension of the HOME affordability period in the LURA for an additional 15 years subject to the following conditions:

## Conditions

The following is a summary of conditions outlined in this report:

1. Applicant shall agree that so long as the HOME LURA is outstanding, Florida Housing and their Compliance Monitoring Agent shall have access to the property to perform their compliance audits.

2. Confirmation at closing that all costs, interest and fees due to FHFC, its legal counsel and FHDC have been paid.

3. The Borrower and/or its affiliates shall have no outstanding past due and/or non-compliance issues at the time of closing unless otherwise approved by Florida Housing.

4. Review, approval, and execution of all loan documents as required by Florida Housing and its legal counsel.

5. Borrower has committed to extend the current HOME loan set asides for an additional 15 years from the date of the current HOME loan LURA expiration.

6. Verification of approval of the modification from all subordinate lenders and the limited partner of the Borrower prior to FHFC execution of modification documents.

7. Verification that the HAP Contract has been extended.

8. Verification that the defaulted status of the 3rd and 4th mortgage loans is brought current.

9. Development cash flow in excess of 1.50 debt service coverage on the HOME loan will be deposited into a reserve account held by FHFC and be used to fund repairs or if unexpended after 24 months from closing, will be used to pay-down the HOME loan. Starting as of March 1, 2009, the Borrower is required to make monthly deposits in the amount of $42,000 into the reserve account. This will be tested on an annual basis and will be adjusted for any excess or shortfall. This account will be re-evaluated for appropriateness if the development applies for refinancing in the future.

10. The HOME loan restructuring and extension shall not occur prior to the closing of the assignment on the existing first mortgage to Regions Bank.

11. FHFC, the Servicer, and FHFC legal counsel must approve the terms of the assigned first mortgage to Regions Bank. All assignment and/or modification documents must be acceptable to FHFC in its sole discretion.

12. No future advances shall be allowed on the assigned first mortgage loan.

13. Any other reasonable request of FHFC, its legal counsel and Servicer.