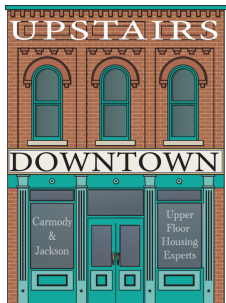


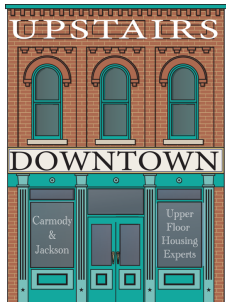
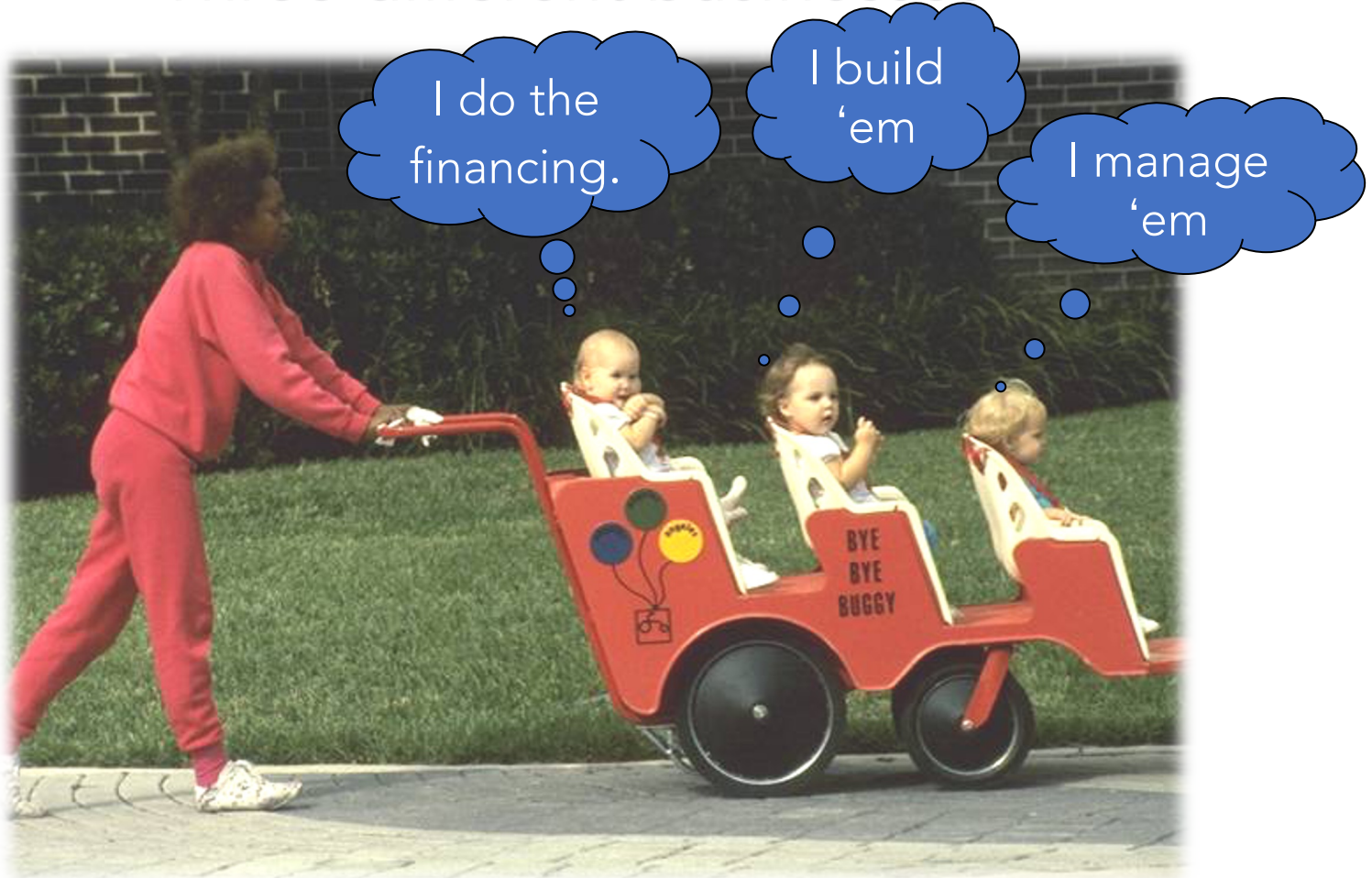
# Understanding the Numbers

## Of upper floor development



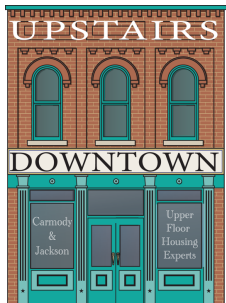
# Real Estate Development

Three different businesses



# Real Estate Financial Analysis

Two key financial statements



# Developing Sources and Uses

Due diligence to understand capital requirements

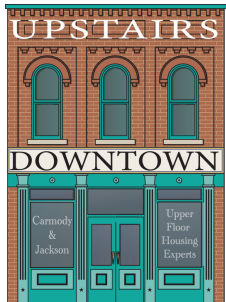
## Uses

### Soft Costs

- ✓ Accounting
- ✓ Legal
- ✓ A & E
- ✓ Loan application
- ✓ Building permits

### Hard Costs

- ✓ Construction Costs
- ✓ Contingency



# Developing Sources and Uses

Due diligence to understand capital requirements

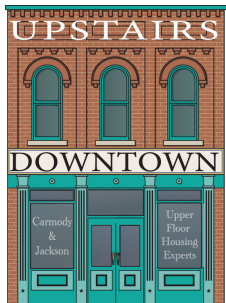
## Sources

### Equity

- ✓ Owner Capital
- ✓ Relatives & Friends
- ✓ Partners
- ✓ Frequent Flier Miles

### Debt

- ✓ Conventional Debt
- ✓ Banks
- ✓ Credit Unions
- ✓ Insurance Policies

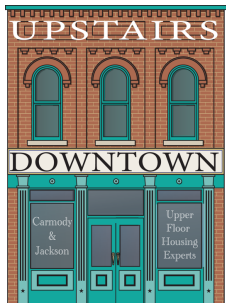


# Develop a realistic budget

Always include a generous contingency!

Which of you wishing to construct a tower does not first sit down and calculate the cost to see if there is enough for its completion? Otherwise, after laying the foundation and finding himself unable to finish the work the onlookers should laugh at him and say, 'This one began to build but did not have the resources to finish'.

Luke 14: 27-30



# Project Pro Forma

Annual Income and Expenses of a project

## Income

Rent Roll

How much rent for each unit

Tenant Contributions

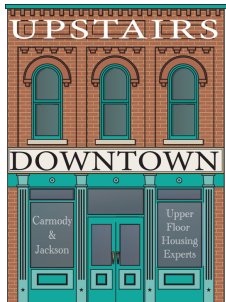
Utilities

Laundry

Parking

Vacancy Factor (5 -10%)

How long will vacant unit take to rent?



# Project Pro Forma

Annual Income and Expenses of a project

## Expenses

Taxes

Likely impact of upstairs investment?

Utilities

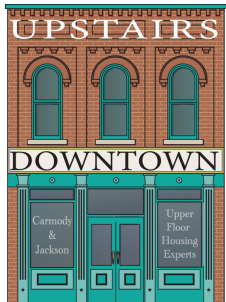
Separate meters or not?

Insurance

Varies greatly in not familiar to agency

Maintenance

Common areas and site





# Project Pro Forma

Annual Income and Expenses of a project

## Expenses

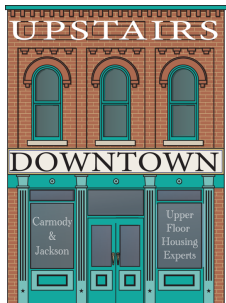
Management

By owner or by third party?

Other

Special assessment district levees

Annual rental unit inspection fee



# Simple Operating Pro Forma

## Income

Gross Rent	Rent Collected at 100% Occupancy
<u>Tenant Contributions</u>	<u>Tenant Contributions towards operating expenses</u>
Gross Income	Total Income at 100% Occupancy
<u>(Vacancy Rate)</u>	<u>Adjustment for Vacancy and Collections Loss</u>
Effective Gross Income	Anticipated Cash Actually Collected

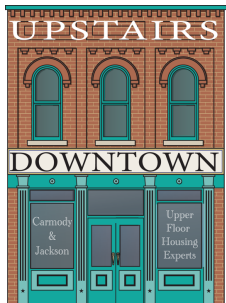
## Expenses

Taxes	Research and negotiate with assessor
Insurance	Discuss your project with your provider
Maintenance	Snow removal, window washing, common area
Utilities	Are utility expenses paid as part of rent?
Management	Manage the project yourself or pay someone?
<u>Reserves</u>	<u>Appliances replaced, units painted, etc.</u>
Total Expenses	
<u>Net Operating Income</u>	<u>Cash generated by the project</u>
Debt Service	Interest, principal payments to lender
Cash Flow	Return to owner

# Net Operating Income

Helps Determine Debt Service

- NOI is the number that drives project financing.
- Banks lend mostly to cash flow
- Debt service is the annual cost to pay off the loan determined by loan interest and amortization  $\times$  a constant.



# Case Study Sources & Uses

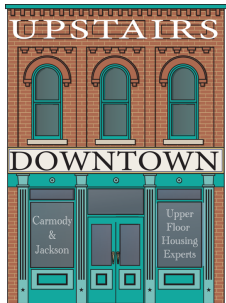
Two residential units above the business

## Uses

Acquisition	0
Arch / Engineer	10,000
Permits	500
Hard Construction	119,500
Appliances	5,000
Contingency	15,000
<hr/>	
Total	150,000

## Sources of funds

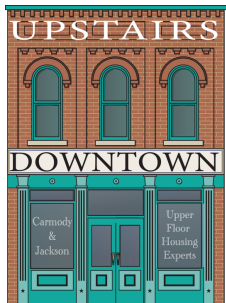
Owner Equity	20,000
Bank Financing	130,000
<hr/>	
Total Sources	150,000



# Case Study Pro Forma

Two residential units above the business

Gross Rent	$800 \times 2 \times 12 =$	19,200
Less Vacancy Rate 10%		(1,920)
Less Expenses		
Utilities	1,200	
Taxes	2,400	
Insurance	1,200	
Maintenance	1,000	
	<hr/>	
Total Expenses		(5,800)
Net Operating Income		11,480

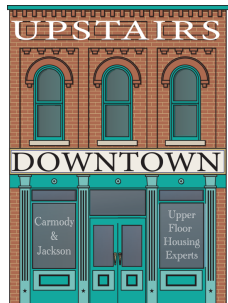


# Debt Service

Annual amount needed to pay off or service loan

## Debt Coverage Ratio

$$\text{DCR} = \frac{\text{Net Operating Income (NOI)}}{\text{Debt Service}}$$

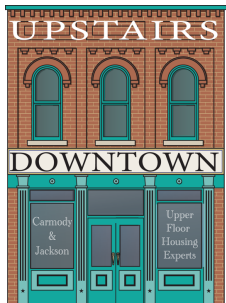


# Debt Coverage Ratio

Using the debt coverage ratio formula

$$\text{DCR} = \frac{\text{Net Operating Income (NOI)}}{\text{Debt Service (D/S)}}$$

$$\text{Case study project: DCR} = \frac{11,480}{11,037} = 1.04$$



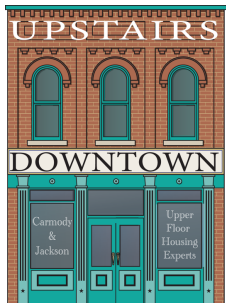
# How Much Will the Bank Lend?

This lender requires a DCR of 1.2

The largest loan this bank would make given NOI of \$11,480 is

$$D/S = \frac{NOI}{DCR} = \frac{11,480}{1.20} = \$9,567$$

$$\text{Loan } \$ = \frac{D/S}{c} = \frac{9,567}{.08481} = \$108,685$$





# Project Funding Gap

Capital costs exceed available funds

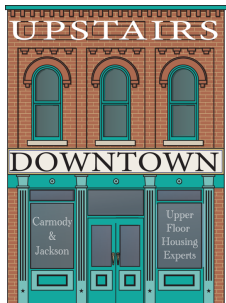
Difference between how much you can raise between owner equity and conventional financing and the cost of the project.

## Use of funds

Acquisition	0
Arch / Engineer	10,000
Permits	500
Hard Construction	119,500
Appliances	5,000
Contingency	15,000
<hr/>	
Total	150,000

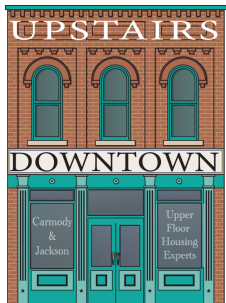
## Sources of funds

Owner Equity	20,000
Bank Financing	108,000
<hr/>	
Total Sources	128,000
Gap	22,000



# Minding The GAP

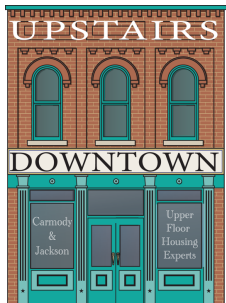
Fist rule when encountering a project gap



# Minding The GAP

Almost every project starts with a gap

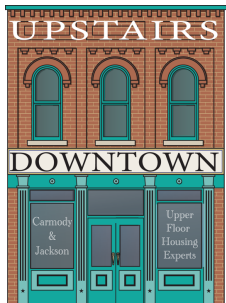
- ✓ Expected income does not provide enough cash flow to service debt and/or provide a return on investment to owner.
- ✓ The amount of conventional debt a unit can service provides a good measure of when and what level of public intervention is needed to assist with upstairs development.



# Project Funding Gap

Many ways to fill the gap

- ✓ Additional owner equity
- ✓ Wide variety of incentives
- ✓ Subordinated loan or grant – importance of local, simple solutions
- ✓ Tax credits including Historic, New Markets, and LIHTC.
- ✓ Reduce the scope of the project



# More than Cash Flow

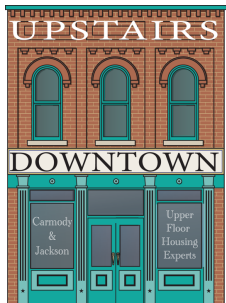
Other benefits from owning real estate

All real estate projects:

- ✓ Tax Benefits
- ✓ Appreciation

Unique upstairs project benefits:

- ✓ Improving the value of first floor retail
- ✓ Lowers first floor utility costs



# Revised Project Funding

Subordinated debt moves the deal forward

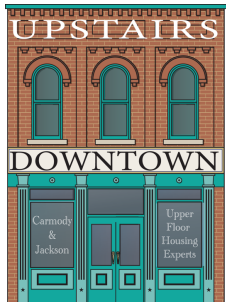
Subordinated debt allows first position lender to meet underwriting requirements.

## Use of funds

Acquisition	0
Arch / Engineer	10,000
Permits	500
Hard Construction	119,500
Appliances	5,000
<u>Contingency</u>	<u>15,000</u>
Total	150,000

## Sources of funds

Owner Equity	17,000
Bank Financing	108,000
<u>City TIF Program</u>	<u>25,000</u>
Total Sources	150,000

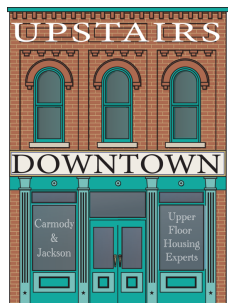


# Rule of Thumb

How much debt per unit can you service at different rent levels.

Based upon a loan with a 7% interest rate and a 20 - year amortization

Unit Mo. Rent	Allocation to Exp.	Monthly Net NOI	Annual NOI	Loan 7% 20 Yr Amort (c = .0931)
400	40%	240	2,880	30,934
450	40%	270	3,240	34,801
500	40%	300	3,600	38,668
600	40%	390	4,680	50,268
650	35%	422	5,064	54,458
700	35%	455	5,460	58,646
750	35%	488	5,856	62,836
800	35%	520	6,240	67,025
900	35%	585	7,020	75,403
950	35%	617	7,404	79,592
1000	30%	700	8,400	90,225
1050	30%	735	8,700	94,737
1100	30%	770	9,240	99,248
1200	30%	840	10,080	108,270
1300	30%	910	10,920	117,293
1400	30%	980	11,760	126,315
1500	30%	1,050	12,600	135,338
1600	30%	1,120	13,440	144,360

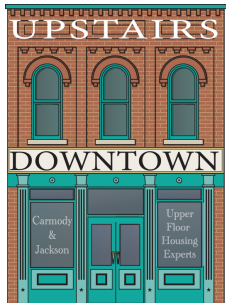


# Getting Started

## Next Steps

- ✓ Main Street has embraced upper floor and in fill development as keys to success and has a basic understanding of market dynamics.
- ✓ Main Street has begun to advocate for upper floor development as is building a team of advisors to assist early DIY developers and is seeking funding to advance the cause.
- ✓ Main Street has a good working knowledge of its building stock

Next Step: Finding a source of funding for pre-development expenses.





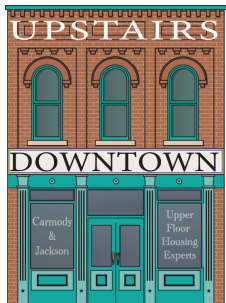
Helping DIY  
Developers  
with  
feasibility  
analysis is  
important  
tool to get  
projects  
moving  
forward.

**Upper-story Redevelopment  
Real Estate Feasibility Study**

3 & 4 Old Capitol Plaza  
Springfield, IL



August 10, 2021



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## The Upstairs Downtown Program for Successful Housing

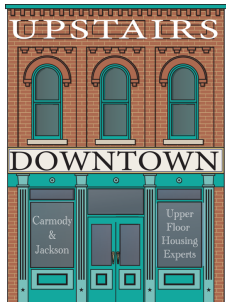
In our work, we strive to find design solutions for older buildings that create spacious yet affordable housing in the buildings along America's Main Streets. We focus our skills on the small-scale (two to three-story) brick buildings that are the commercial and architectural core of older downtowns. These buildings have great architectural amenities and tall ceilings that can be transformed into new housing units that have character and appeal for today. By adding contemporary building systems we greatly improve their safety. We utilize an open planning concept that converts under-utilized buildings into desirable living spaces. All of this is done while meeting the challenges of modern building codes and competing against other newer housing projects.

The Upstairs Downtown approach carefully assesses the architectural character found in historic buildings and matches these with contemporary amenities. High ceilings are a starting point for designs that also maximize natural lighting, vintage materials, and contemporary kitchens and baths. Full laundry facilities are provided in each unit. When space allows, a home office or an outdoor deck or terrace adds another amenity.

Our housing program guidelines:

- Unit size: 1 or 2 BR units of approx. 1,000 sq. ft.
- Open-plan kitchen and living rooms
- Retention of tall ceilings
- Natural lighting for living and bedrooms
- Laundry facilities in each unit
- All new building systems - HVAC, electric, plumbing
- Retain and enhance historic character-defining features
- Safety upgrades based upon the International Existing Bldg Code

The Upstairs Downtown real estate feasibility studies are an integrated design and financial assessment that helps owners understand what is needed to convert under-utilized spaces into contemporary housing. Property owners will need to assess their financing options and work with local professionals to move projects from these preliminary designs to more detailed construction documents for building permits and construction.



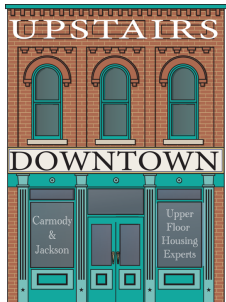
## Upper-story Redevelopment Real Estate Feasibility Study

This project is a combination of two different buildings that have been combined into a single parcel. The first floor of 4 OSC is a separate commercial condominium. The property was converted to office use in the 1980s including all new systems, finishes. A elevator and fire suppression system were also installed at that time. The building was vacant for several years and suffered from serious structural damage to the rear portion of 3 OSC which has been stabilized with new second floor structure.

The proposed project will create nine new residential units including one on the rear of the first floor. The commercial storefront will be maintained as the residential lobby to provide access to the elevator and front means of egress. A new egress stairs will be needed at the rear of 4 OSC. The 1980s renovation removed virtually any contributing historic features. The front windows in both buildings were changed in the previous renovations. The building has a very narrow and deep floor plate, so the residential units are designed with lower interior walls to allow "borrowed light and air" into the interior rooms. The building will maintain the full fire suppression system. There is an interior light well that also provides some additional natural light and air into the units.

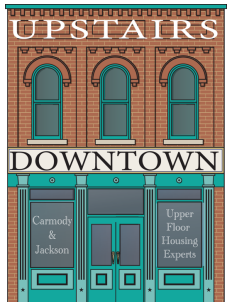
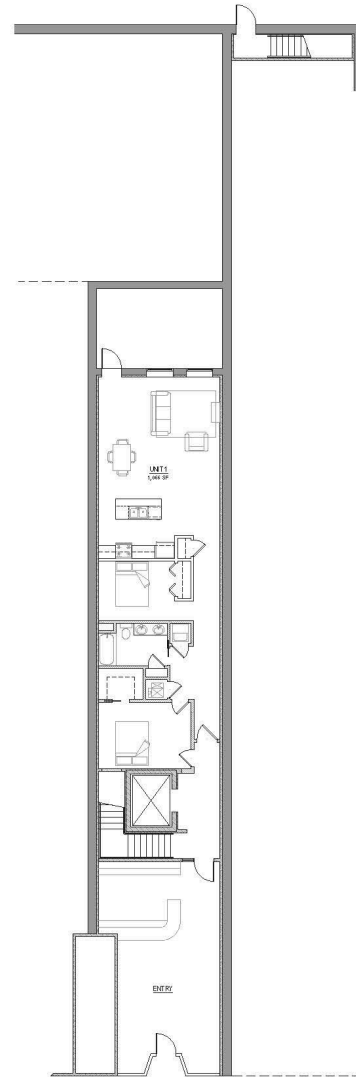
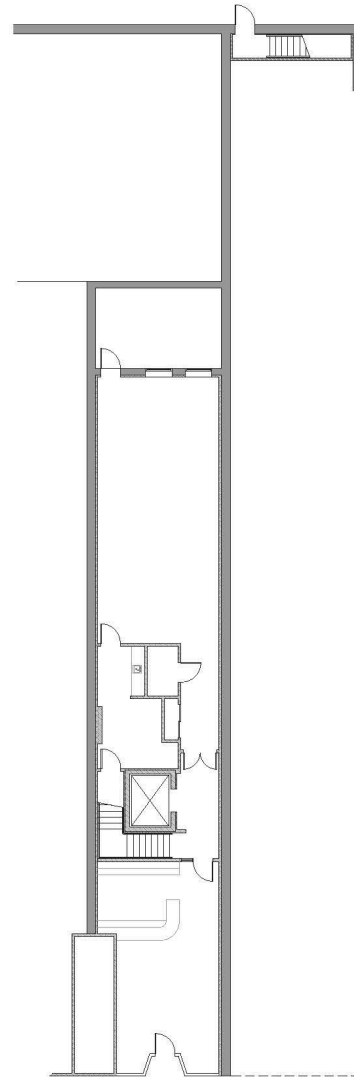
### Unit Summary

First Floor	Unit 1	1-bedroom	1086 sf	Outdoor courtyard
Second Floor	Unit 2	1-bedroom	616 sf	View of Old State Capitol
	Unit 3	2-bedroom	1,181 sf	Potential office in second BR
	Unit 4	2-bedroom	948 sf	View of Old State Capitol
	Unit 5	1-bedroom	857 sf	
Third Floor	Unit 6	1-bedroom	516 sf	View of Old State Capitol
	Unit 7	2-bedroom	952 sf	Potential office in second BR
	Unit 8	1-bedroom	966 sf	View of Old State Capitol
	Unit 9	1-bedroom	709 sf	Outdoor terrace

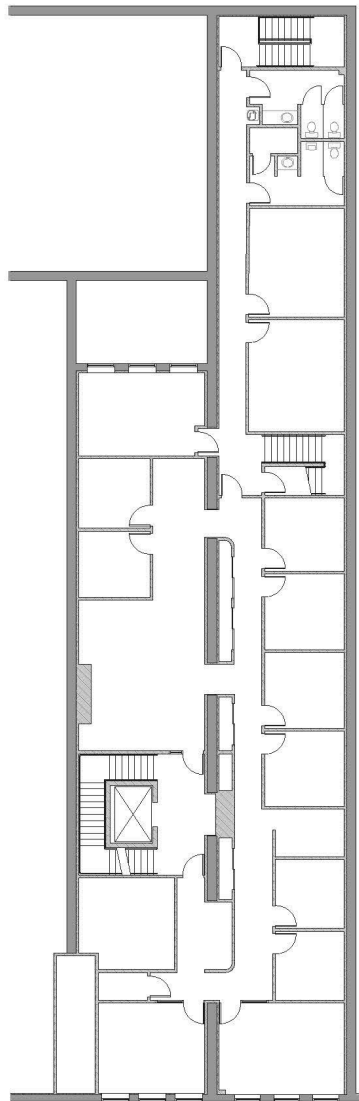


### Existing First Level Floor Plans

### Proposed First Level Floor Plans



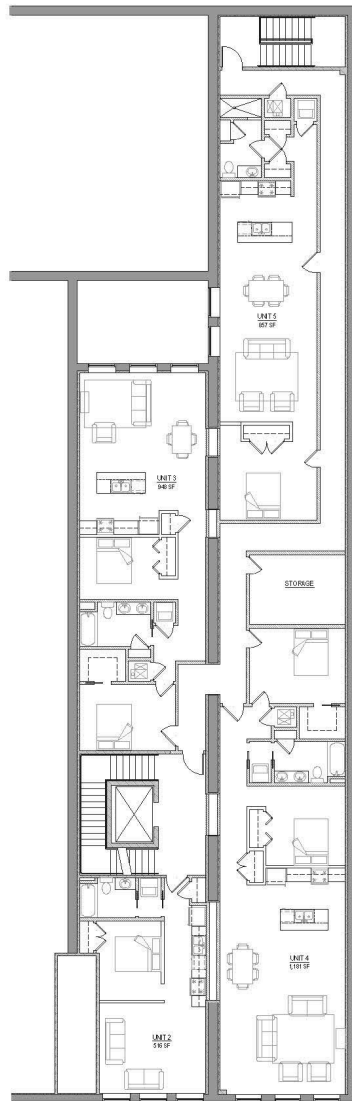
### Existing Second Level Floor Plans



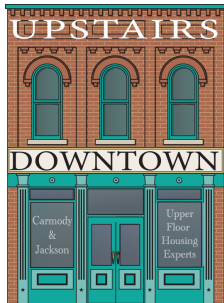
- EXISTING FULL-HEIGHT WALL
- FULL-HEIGHT WALL FROM PREVIOUS BUILD-OUT



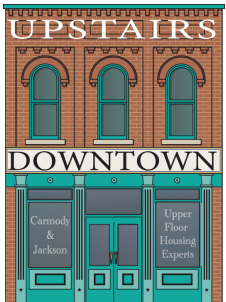
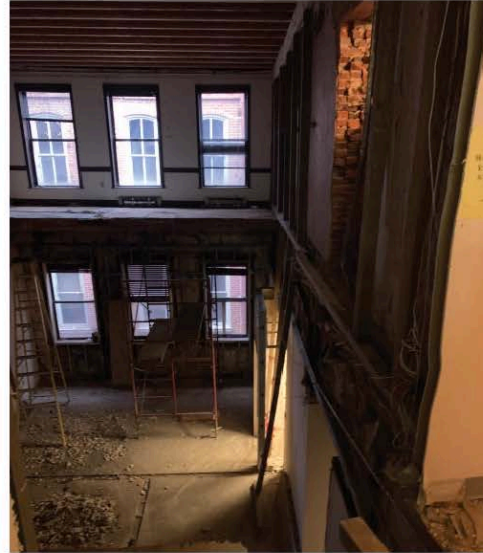
### Proposed Second Level Floor Plans



- EXISTING FULL-HEIGHT WALL
- FULL-HEIGHT WALL FROM PREVIOUS BUILD-OUT
- NEW FULL-HEIGHT WALL
- NEW PARTIAL-HEIGHT WALL



Existing Condition Photos



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## Real Estate Development Pro Forma

### 3 & 4 Old Capitol Plaza Assumptions

#### Proforma

Rental rates of \$1.25 per square foot

Property management by management firm at 5% of gross revenue

Operating expenses at 39%

#### Sources and Uses

Owner capital of 10%.

First position financing at 3.5% interest with a 25-year amortization.

Hard construction costs \$95 p.s.f. based on pricing from contractor/owner.

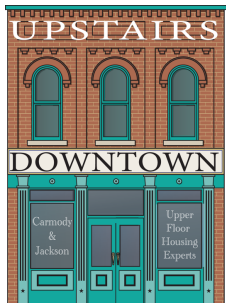
Soft costs \$20 p.s.f. due to contractor forgoing usual overhead fees and simple transaction costs but added cost to form LLC to make use of Federal tax credits.

Gap financing in the form of a CDFI loan with interest only payments for seven years at 1.5% interest allows for shorter term first mortgage (15 years) to pay down debt faster.

Refinancing in year eight to payoff original first position loan and CDFI loan .

Federal historic tax credit enables lower owner equity less debt.

Gap financing in the form of Federal Tax Credits purchased by CDFI at closing valued at 12% of total capitalized costs net present value.



## Real Estate Development Pro Forma

### Annual Income and Operating Expenses

		Unit Mix	Unit Mix	Sq.Ft.	Cost Range	\$100 - 150	Rent @ \$1.25
Project Name:	Springfield	1	2 bed	1039	103,900	155,850	1,300
Location	3 & 4 Old Capitol Plaza	2	1 bed	504	50,400	75,600	650
# of Units	9	3	2 bed	924	92,400	138,600	1,150
		4	2 bed	1157	115,700	173,550	1,450
		5	1 bed	828	82,800	124,200	1,050
		6	1 bed	530	53,000	79,500	650
		7	1 bed	941	94,100	141,150	1,175
		8	1 bed	935	93,500	140,250	1,175
		9	1 bed	690	69,000	103,500	850
				7,548	754,800	1,132,200	9,450

### Operating Expenses

#### Administrative

Advertising	500
Management Fee @ 5 %	5,670
Other	

**Total Administrative** 6,170

#### Operating

Elevator Maintenance	2,400
Fuel - Heating	1,800
Fuel - Hot Water	0
Electric	1,800
Water / Sewer	1,800
Trash Removal	1,200
Security	1,800
Payroll	0
Misc. _____	500

**Total Operating** 11,300

#### Maintenance

Decorating	900
Repairs	1,500
Exterminating	500
Insurance	10,000
Grounds	500
Other _____	

**Total Maintenance** 13,400

**Replacement Reserves (@\$200)** 1,800

### Total Operating Expenses

(Before RE Taxes)

#### Taxes

RE Taxes	12,000
Personal Property	0
Employee Payroll	0
Other _____	0

**Total Taxes** 12,000

### Annual Income

Gross Potential - Residential (8775 X 12)	113,400
(Less Residential Occupancy @ 7 %)	-7,938
<b>Subtotal</b>	<b>105,462</b>

Gross Potential - Commercial	N.A.
Less Commercial Occupancy @ ___%	
<b>Subtotal</b>	

Effective Gross Income	105,462
(Less Operating Expenses)	-44,670
<b>Net Operating Income</b>	<b>60,792</b>

#### Expense Ratio

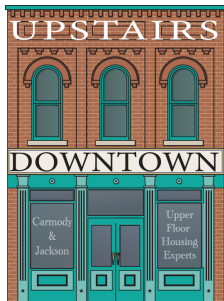
Gross Revenue:Operating Expenses 39%

#### Option A - Without Subordinated Debt

NOI	60,792
Option A Debt Service	-62,919
<b>Cash Flow after Debt Service</b>	<b>-2,127</b>

#### Option B - With Subordinated Dept

NOI	60,972
Option A+B Debt Service	-59,846
<b>Cash Flow after Debt Service</b>	<b>1,126</b>





You can start filling the gap until you know what it is.

## Real Estate Development Pro Forma

### Sources and Uses of Capital

Project Name:	Springfield	
Location	3 Old Capital Plaza	
# of Units	9	
Gross Sq. Ft.	11,400	
<b>Use of Funds</b>		
Land Improvements		0
Parking		0
Storm Water Management		0
Total Land Improvements		0
<b>Structures</b>		
Renovation	\$95	1,083,000
Additions or New Construction		0
Solar		0
Geo Thermal		0
Elevator		0
Contingency (10%)		108,300
Total Structures		1,191,300
Land Improvements and Structures		1,191,300
General Requirements @ 5 %		NA
Sub Total		
Builder's Overhead & Profit 7 %		NA
Subtotal		
Bond Premium		NA
Building Permits (1.5%)		16,245
Total Construction Costs		16,245
<b>Design and Construction Administration</b>		
Architect's Design Fee (5%)		54,150
Construction Administration Fee (3%)		32,490
Total Design and Construction Admin		86,640
Legal		5,000
Operating Reserve		10,000
<b>Total Capitalized Costs \$115.00 p.s.f.</b>		<b>1,309,185</b>

### Source of Funds Without Subordinated Debt or Federal Tax Credit

Owners Equity (20%)		261,837
Other Equity A:		
Other Equity B		
Debt Source A: <u>First Mortgage</u> (80%)		1,047,348
Debt Source B		
Debt Source C		
Other Debt or Equity:		
<b>Total Debt &amp; Equity</b>		<b>1,309,185</b>

### Debt Service

Debt Source A		
Amount 1,047,348 @ 3.5% X 25 years		62,919
Net Operating Income		60,792
<b>Debt Coverage Ratio</b>		<b>0.97</b>

### Source of Funds With Subordinated Debt and Federal Tax Credit

Owners Equity (5%)	5%	65,459
Other Equity A:		
Other Equity B		
Debt Source A: <u>First Mortgage</u> (60%)	47%	615,317
Debt Source B - CDFI Loan	36%	471,307
Debt Source C: Federal Tax Credit	12%	157,102
Other Debt or Equity:		
<b>Total Debt &amp; Equity</b>		<b>1,309,185</b>

### Debt Service

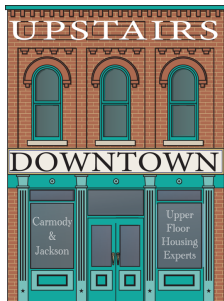
Debt Source A		
Amount \$615,317 @ 3.5% X 15 years		52,776
Debt Source B CDFI Loan		
Amount Interest Only 7 years @ 1.5%		7,070
Total Debt Service A+B		59,846
Net Operating Income		60,792
<b>Overall Debt Coverage Ratio</b>		<b>1.03</b>

### First Position Debt Coverage

Amount \$615,317 @ 3.5% X 25 years		52,776
Net Operating Income		60,792
<b>Revised Debt Coverage</b>		<b>1.15</b>

### Year 8 Refinance

First Position Balance		361,191
CDFI Loan		471,307
New Loan 5.5% X 25 years		832,498
Net Operating Income		64,047
<b>Debt Coverage Ratio</b>		<b>1.04</b>

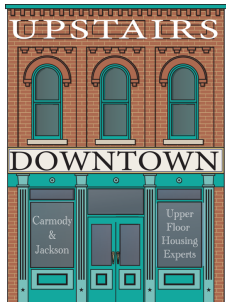


# How Others Got Started

## Hastings, NE



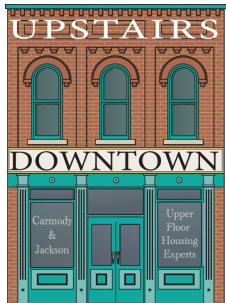
Randall Chick was the exceptional leader that enabled Hastings (population 24,000) to build 85 upper floor units over the last ten years.





## Hastings, NE

- Established both a business improvement district (BID) and a community revitalization area (CRA) to fund Main Street initiatives
- Attended NDC training early on
- First project was 100% funding by the BID/CRA

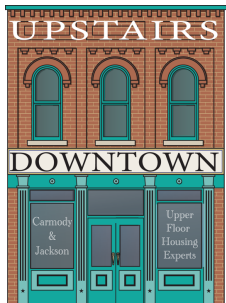


# How Others Got Started

## Galesburg, IL



Jay Matson is the exceptional leader that made Seminary Street a landmark.



# How Others Got Started

Here are more from the vault of Upper Floor Success



Welcome Back Mike!

