EXHIBIT A-1

PDC PORTLAND DEVELOPMENT COMMISSION

Loan Review Committee Recommendation & Approval Form

☒ I am the Project Manager
☐ I am NOT the Project Manager

Project Name:	HAZELWOOD RETIREMENT COMMUNITY
Business Name:	THE HAZELWOOD GROUP, LLC
Address:	11933 NE Davis Street — City: Portland — Zip Code: 97220
Presenter:	John Marshall — Extension: 03232
Department:	Housing — Section: HDF

☐ **THIS IS A "NO ACTION" ITEM – INFORMATION ONLY**

ACTION REQUESTED: *(150 character limit)*
Recommend approval of extension of full tax abatment to Planning Commission

The exceptions/special requests are found on Page: ________ ☒ There are no exceptions.

Approved Loan Deferrals **START** Date: ________ Approved Loan Deferrals **END** Date: ________

Department Director's Endorsement: Komi P. Kalevor
I support and agree this item should go forward to the Loan Review Committee.
Director *or* Division Manager signature required before submitting to LRC for review and recommendation.

Loan Committee Members – initial for recommendation *(3 members required before sending forward)*

- ☑ **Approval Recommended** to Executive Director – move forward for signature
- ☐ **No Approval Recommended** to Executive Director – move forward for concurrence
- ☐ **Defer to Next Meeting** – Amendments/Corrections to be completed – return to Presenter
- ☐ **Approval Recommended to Commission** – forward for signature

JVC — Julie V. Cody, Chief Financial Officer & Loan Review Committee Chair
DRB — David Elott, Interim General Counsel
____ Bruce Allen, Sr. Development Manager (Special Projects)
____ Fred Atiemo, Business Finance Manager
____ Komi Kalevor, Interim Housing Director
AMB — Alfred Bookman, Division Manager, Asset Management & Credit Administration

☑ **APPROVED** ☐ **NOT APPROVED**

Bruce A. Warner, Executive Director [signature] (See Note Below!)

Date signed: 5/30/08

☐ *Check here if you are "Acting" for Executive Director.*

→ So long as we make clear that PDC's recommendation is based solely on the financial analysis. We are not making a determination on the project's eligibility for the abatement as a legal matter, leaving that issue to the City Attorney in advising the City Council.

Loan Committee Approval for:
HAZELWOOD GROUP, LLC

ACTION REQUESTED:

Recommend approval of extension of tax abatement to Planning Commission for Hazelwood Retirement Community

SUMMARY:

Hazelwood Retirement Community (Project) is a neighborhood mixed income housing project for seniors located at 122nd Avenue in northeast Portland. The Project has 120 units of congregate housing for people 62 or older. A 30-year PDC Regulatory Agreement restricts 96 units with 36 under 50% MFI, 4 under 60% MFI, and 56 under 75% MFI.

The owner has applied for an extension of the Section 3.103 Transit Oriented Development (TOD) tax abatement for the term of the Project's affordability requirement (11-15-29) because the 10 year property tax abatement expires in June 2008. The owner has provided financial projections showing the Project can not continue affordability, pay debt service of approximately $708,000, and pay an increase of approximately $143,000 in property taxes.

According to City Code, Section 3.103.45, PDC's role is limited to a financial analysis and a recommendation based on that analysis. PDC has reviewed financial projections from the borrower. It has not viewed tax returns from the borrower.

PDC's recommendation will be sent to the Planning Commission, who will review and make its policy recommendation. Abatement extensions are discretionary. Ultimately, the decision to grant the extension will be a policy decision for City Council. PDC staff and legal department have had more than a dozen conversations with the Bureau of Planning staff and the City Attorneys office. The Bureau of Planning states they will recommend a partial abatement as this is the policy position Planning took in 2006.

PDC must complete its recommendation prior to the biweekly Planning Commission hearing that is scheduled for June 3, 2008 to obtain approval from City Council by June 30, 2008.

FINANCING REQUEST:

Dollar Amount $0

PRIORITY TARGET

Family	24 two BRs
Special Needs	Congregate Care - 120 Units
Mixed Income	Yes
Mixed Use/ Commercial	No

PROPOSED UNIT BREAKDOWN:
(Count and affordability) **Restricted**

Studio	28	28 @ 50%,
One BR	8	8 @ 50%
One BR	4	4 @ 60%
One BR	56	56 @ 75%
Two BR	24	24 Unrestricted
Total Units	120	36 @ 50%, 4 @ 60%, 56 @ 75% and 24 unrestricted

COLLATERAL:

2007 Assessed Value *(Land/Improvements)* $11,649,010

RELATED DEBT:

Number of Loans	1
Dollars Outstanding	$700,000
Paid As Agreed	Yes
Deferral/Restructure	N/A
# of Projects on Watchlist	0

SPONSOR CAPACITY: Very Good

OWNERSHIP TEAM:

Senior Lender:	State of Oregon Elderly and Disabled Bond
Property Manager:	Retirement Housing Services
Owner:	The Hazelwood Group, LLC
Subordinate Lender:	PDC

COMMENT:

The abatement will not require any new PDC funds.

Investing in Portland's Future

PORTLAND DEVELOPMENT COMMISSION
INTERNAL MEMORANDUM

PDC
PORTLAND DEVELOPMENT COMMISSION

DATE: May 29, 2008

FROM: John Marshall, HDF - Team 3

TO: Loan Review Committee

SUBJECT: Recommend extension of tax abatement to Planning Commission for Hazelwood Retirement Community located at 11933 NE Davis Street in the Hazelwood neighborhood of Northeast Portland

PDC'S ROLE:

PDC coordinates with the Planning Bureau, which makes a presentation to the City Council after PDC completes a financial analysis when owners request a new tax abatement or extension. The threshold test is to ascertain whether the property needs the tax abatement to be financially feasible and the tax abatement should not result in the owner earning more than a 10% Internal Rate of Return.

PROJECT DESCRIPTION/BACKGROUND:

The Hazelwood Retirement Community is located in the Hazelwood neighborhood at NE Glisan and 122nd Avenue. It serves seniors 62 or older and is the residential component of a 17 acre mixed use shopping center development, which includes a Safeway supermarket, Target department store, and additional retail space. The Project is the upper three floors of a four story wood frame masonry building whose ground floor provides retail space for several small businesses located between the Safeway and Target stores. The Project was built in 1997-98 and has 28 studios, 68 one bedroom units, and 24 two bedroom units. The Project also provides additional services including: meals, on- site activity director, van transportation, 24 hour attendant, and 24 hour security. The site is on City bus lines and is three blocks from a MAX light rail stop.

The owner, Hazelwood Group, LLC, is a for-profit business comprised of J. Daniel Steffey; architects, Brian Carelton and William Hart; and general contractor principals, Hawkin Au, and John Bently. The property management agent is Retirement Housing Services.

The Project has three regulatory agreements. The ten year City Ordinance for the original Transit Oriented Development tax abatement mirrors the recorded PDC regulatory agreement that restricts 28 studios and 8 one bedrooms at 50% MFI, 4 one bedroom units at 60% MFI, and 56 one bedrooms at 75% MFI through July 2028. PDC's restriction lasts 15 years beyond the maturity of the PDC loan.

The remaining 24 two bedroom units are unrestricted. The state's recorded Regulatory Agreement and Declaration of Restrictive Covenants is less restrictive than PDC's affordability requirement since it restricts only 24 units at 50% MFI through November 15, 2029.

The owner's current equity investment of $848,907 or 8.4% of the development cost is much greater than the average non profit's contribution to affordable rental projects. The Project has an Oregon Elderly and Disabled loan of $8,000,000 with annual debt service of approximately $635,500, and a PDC $700,000 loan with annual debt service of approximately $72,400.

To date, this Project as many other affordable housing projects, (some of which have expiring tax abatements) has not performed as was initially projected. The current revenue is 1.6% lower than was estimated in 1998. One cause is HUD's three year freeze on rent increases in the Portland metro area. The 2008 budget shows operating expenses 6.8% higher than was projected in 1998. The bottom line is the 2008 cash flow after debt service will be approximately $120,000 lower than the original estimate. Moreover, this underperformance has been evident from the beginning.

The Project also competes against several projects that have received greater subsidy including the newly built The Heights at Columbia Knoll two miles northwest. The Heights has 208 units of senior congregate housing targeted primarily toward 60% MFI residents. It does not pay property taxes, has Low Income Housing Tax Credits, and below market financing from the state and PDC. Russellville Park, a market rate senior project less than a mile from Hazelwood, has a TOD property tax exemption. A third nearby property, Oregon Baptist Retirement Homes, is exempt from property taxes. The result is Hazelwood will be at a greater disadvantage with nearby senior housing projects if the tax abatement is not extended.

Property taxes on the improvements at Hazelwood are abated until June 30, 2008 at which point they will increase from $8,339 to an estimated minimum of $151,227 per year based upon last year's tax ratio, millage rate, and a 3% increase in value. The property taxes could be substantially higher if the property is reassessed after it loses the tax abatement.

FINANCIAL:

The 2008 proforma (Attachment 1) uses the 2008 budget developed by the owner and has been approved by Oregon Housing and Community Services (OHCS), the senior lender with an $8,000,000 Elderly and Disabled Bond. PDC has reviewed the financials presented by the borrower and it has not reviewed the tax returns of the borrower.

The income in the proforma is based upon the Hazelwood 2008 budget. The 2008 income is 7.7% higher than the 2006 audited financials. This conservative projection is only a 3.8% per year increase over 2006 actual income. Future income is increased at 2% per year because, higher rents will be implemented gradually because of the nearby competition, and Hazelwood currently has an 11% vacancy. Hazelwood's rents and service packages are below nearby newly constructed market rate projects and above the newly built 208 unit The Heights. Hazelwood's rent and service package are below the newer subsidized (Russellville Park) and unsubsidized market rate projects. This suggests Hazelwood's rents and service package are priced at a level to attract some slightly higher income residents than the Heights but are limited by newer projects.

The Hazelwood proforma has operating costs of $1,557,000 for the property and additional services including: meals, on- site activity director, van transportation, 24 hour attendant, and 24 hr security. This produces an Overall Debt Coverage Ratio of 1.05 in the first year with the full tax abatement. The 2008 budget is 3.9% higher than the 2006 audited financials, which indicates the budget is based upon small inflationary adjustments (2% per year). The operating expenses in the proforma are increased at 3% per year in the analysis.

The property management fee is 5%, which is priced at market considering the responsibilities of managing rentals and the congregate care services, and additional reporting requirements for the state and PDC. However, a small portion of the fee ($20,000) is attributed to the return to the owner in the investor analysis because the property is self managed.

FULL ABATEMENT:

The analysis of the full abatement utilizes the income and expenses from the state approved budget with the owner maintaining the existing restrictions on affordability for 80% of the Project through the affordability restrictions (November 15, 2029 for the state and through July 8, 2028 for PDC). The rent growth is 2 % per year, and expense growth is 3% per year. A 6% vacancy is projected because Hazelwood is experiencing a higher than normal vacancy, the Project is more than ten years old, and it competes with newer projects several of which have greater public subsidy.

The full tax abatement is needed for the Project to remain financially feasible and maintain the restricted units to seniors, while paying the nearly $708,000 annual debt service. The additional revenue from the market rate units and under 75% units is needed as much now as it was needed when the original full tax abatement was approved. These units offset the reduced income on the more affordable units. The best estimate of the internal rate of return with the full tax abatement for a ten year period is -1.55. Projecting beyond this period is considered to be speculative because there are too many market factors that can change considerably over time.

If the tax abatement is not extended, the project's cash flow will be negative in the year property tax payments resume and could require the owner invest additional equity to pay the state and PDC debt service. The Debt Cover Ratio (DCR) goes negative or is marginal under all scenarios of the partial or no abatement, which may create a default under the bond documents. Making the Project more affordable is not an option because this lowers revenues and the ability of the Project to pay the required debt service to the state and PDC.

The rents are at the maximum on the restricted units. The owner could raise service charges for the congregate care if the occupancy improved dramatically. There are limitations on the possible increases because the tenants consider the rent and service package cost compared to the amenities offered at other nearby projects. Hazelwood will be competing against other subsidized and newer unrestricted market rate projects.

A 10% internal rate of return to the owner could be exceeded if rents or the service package are increased significantly after the PDC debt is paid off in 2014 and the PDC debt service payments are not required. However, refinancing may be needed to pay for capital repairs. A projection of property operations more than six years from now is speculative, and traditionally is not part of IRR calculations. Moreover, changes in the property performance will be ascertained by the annual reviews PDC is required to perform. If substantially higher cash flows occur, PDC may determine that an Accrued Payment Liability obligation by the owner is applicable or an extension of the affordability period under an Extended Use Agreement may be necessary.

NO ABATEMENT:

The analysis with no abatement uses property taxes based upon the assessed value of the property increased by 3%. This produces total property taxes starting at $151,227 or $1,260 per unit. Since there is a possibility the property could be revalued if Hazelwood's tax exemption is terminated, the estimated taxes used for the analysis are at the low end of the potential range. Higher property taxes would result in even greater losses, which could further jeopardize the status of the 40 units that are restricted under 60% MFI by the PDC Regulatory Agreement.

Using the lower end of the property tax range increases operating expenses by a minimum of approximately $143,000 ($1,192 per unit) above current operating expenses. This produces a loss of $114,000 in the first year, and a first year Debt Coverage Ratio of -.85.

Considering the age of the property and its nearby competition, the Project would not be able to pass the increase entirely to the 24 market rate units. This would require a $595 per month increase and is not realistic. Passing the increase to the market rate units and the 56 units under 75% MFI would require an average increase of $147 per month. This would be unlikely to be successful because of the loss of existing tenants, the timing lag in increased cash flow from raising rents for new tenants if significant rent increases were possible, and Hazelwood's competitive market disadvantages (older facility, 80% of units have rent restrictions, and lower public subsidy than competitors). To offset this increase, the owner would more likely attempt to increase charges for the service package and spread them evenly, which is a $99 per unit per month increase. This would result in immediate turnover of many of the current very low income senior citizens.

Another option would be to request that the affordability agreements be terminated because the property can not pay the increased property taxes. A suspension of debt service obligations by PDC would not come close to offsetting the full increase in property taxes.

If the tax abatement is not extended, and rents remained at the same level to maintain the affordability, the owner would have to make equity contributions to fund the operating losses, debt service, and property taxes. This produces an internal rate of return that is too low to calculate because the losses are so severe. In addition, there would be no expectation of a positive return until the existing affordability agreements expire in 2028 and 2029.

PARTIAL ABATEMENT:

Partial abatements are not financially feasible. A 33% abatement based upon the portion of the Project considered to be low income (below 60% MFI) produces an internal rate of return that is too low to calculate because of the $95,258 increase in property taxes. An 80% abatement based upon the 96 long term restricted units (including the 56 under 75% MFI units) produces an internal rate of return of -8.64% because of the $28,600 per year increase in property taxes. It should be noted that an extension of partial tax abatement on a nearby multifamily project with a much greater portion of the project being at market (58% for Floyd Light versus 20% for Hazelwood) was not sufficient and the project was sold to a nonprofit.

CURRENT UNIT MIX AND AFFORDABILITY:

Studio	28	28 @ 50%
One BR	8	8 @ 50%
One BR	4	4 @ 60%
One BR	56	56 @ 75%
Two BR	24	Unrestricted
Total Units	120	96 are restricted with 40 under 60% MFI

DISLOCATION:

Many seniors with low and moderate incomes as well as market rate tenants may be displaced if the tax abatement is not extended because the owner will raise the rents or service charges to pay for the minimum $143,000 increase in operating costs. It is likely that many seniors will be forced to leave on short notice. (Many tenants are on month to month tenancies, so the displacement could be very rapid.) At a minimum, the City may also lose a large portion of the restricted under 75% MFI units. There is no requirement or funding to help the tenants relocate.

FEDERAL COMPLIANCE:

N/A - No federal funding exists and none is being requested.

GIVE AND RECEIVE:

Give	Get
Extend Transit Oriented Development tax abatement through the affordability term. November 15, 2029.	Preserve 96 restricted units for seniors with limited income through November 15, 2029.
NPV of property taxes = $2,189,166.	Protect state and city investment (almost $9,000,000).
	Preserve successful residential portion of mixed income project near the 122nd Avenue Max light rail station.
	Encourage efficient property owners/managers to participate in providing affordable housing.

CONDITIONS:

If the tax abatement extension is approved by City Council, the Borrower will execute an Extended Use Agreement that is required for all tax abatements after December 8, 2006.

EXCEPTIONS TO GUIDELINES:

None

SUMMARY:

An extension of the abatement is necessary for the property to remain financially feasible while serving very low/moderate income seniors because the cross subsidy of the 56 units under 75% MFI and market rate units are necessary to fund the Project's current debt service payments. The internal rate of return analysis shows a return to the owner is -1.55% over a ten year period with the full tax abatement.

This low return is caused by several factors:

1. Hazelwood Retirement Community has a larger capital investment ($848,907 = 8.4% of total development cost) than most affordable properties;
2. Hazelwood Retirement Community pays annual debt service of approximately $708,000 to the state and PDC;
3. rents are restricted/do not increase to market rents on 80% of the units during the period of analysis because of the PDC Regulatory Agreement/state restrictions until 2028 and 2029;
4. transfer prices from the past history in Portland indicates that purchasers of restricted affordable housing are nonprofits that pay the outstanding debt plus costs to ensure the seller does not incur tax obligations.

In essence, the PDC and OHCS affordable housing restrictions depress appreciation and prevent the owner from recovering more than the cash return in year 10 of the analysis because the owner will not be able to sell the property at market value until the affordability agreements expires in 2029. In addition, the owner will most likely have to fund major repairs from cash flow or unsecured credit lines that reduce cash flow because Regulatory Agreements limit equity that would be used as collateral to refinance capital repairs.

The net present value of the forgone property tax during the term of the tax abatement through 2029 is $2,189,166.

RECOMMENDATION:

Based on the financial analysis, PDC staff recommends an extension of the abatement through the affordability period (November 15, 2029) for the entire project. A full abatement appears necessary to preserve this affordable project and allow the owner to pay the project's debt. However, PDC staff recognizes the loss of revenues to local government and other policy considerations by the Planning Bureau and the City may lead the Council to grant only a partial abatement for the Project, which is within the City Council's discretion. PDC provides this financial analysis so City Council may be fully informed on the financial implications of the extension.

ATTACHMENTS:

1. Proforma- Full Abatement with Internal Rate of Return of = **-1.55%**
2. Proforma – No Abatement with Internal Rate of Return that is **too low to calculate**
3. Proforma- Partial Abatement for 40 units with Internal Rate of Return for Partial Abatement 40 units restricted at under 60% MFI = 33% abatement = **-too low to calculate**
4. Proforma- Partial Abatement for 96 units with Internal Rate of Return for Partial Abatement 96 units restricted at under 75% MFI = 80% abatement = **-8.64%**