

TO: Thomas Dolan, Town of Babylon Industrial Development Agency

FROM: Kevin F. Gremse, National Development Council *KFG*

DATE: October 2, 2018

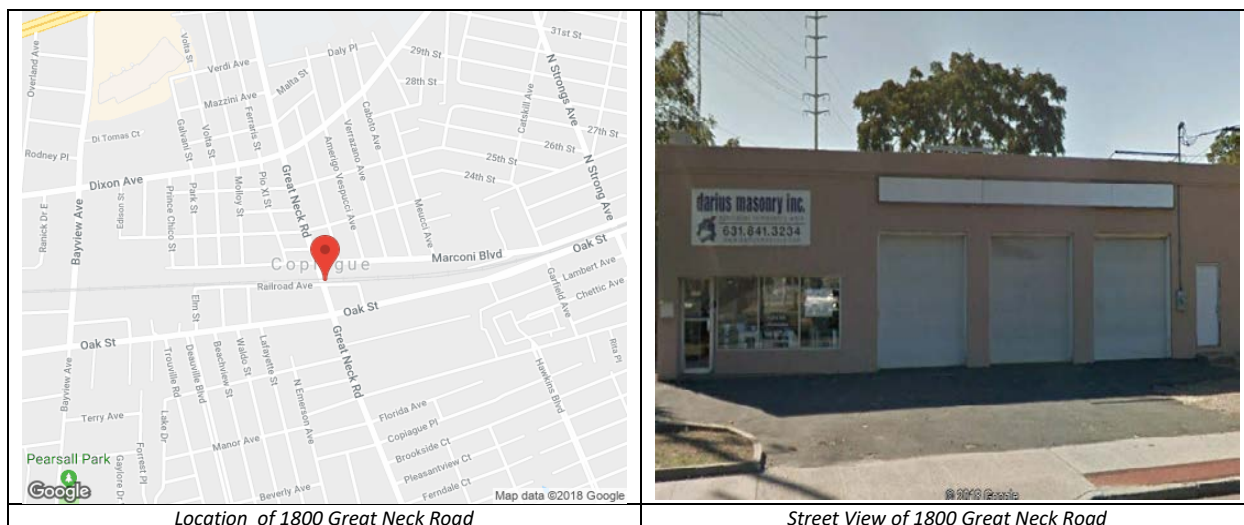
SUBJECT: Ardmore Place LLC  
PILOT for Mixed-Use and Mixed-Income development in Copiague

The National Development Council (“NDC”) has a limited engagement with the Town of Babylon Industrial Development Agency (the “IDA”) to review applications for tax assistance. NDC is a national economic development finance company that works on behalf of municipalities and public benefit corporations around the country. Among its services that it provides to its public sector clients is evaluating the need for and determining the appropriate mix and sizing of economic development incentives. The purpose of this memo is to describe NDC’s project understanding and findings of the above-referenced project.

**PROJECT SUMMARY**

Ardmore Place LLC (the “developer” or “applicant”), submitted a Uniform Joint Application for tax assistance in July, 2018. The application requests a sales tax and a mortgage recording tax exemption in addition to a payment in-lieu of taxes (“PILOT”). The developer is a single asset entity and an affiliate of a real estate investment, development, and construction firm. Dariusz Mroczkowski is the principal representing the applicant. The developer recently completed Marconi Villas, a 20 unit mixed income development in close proximity to the subject site on Marconi Boulevard in Copiague.

Ardmore Place is a proposed \$3.5 million mixed-use and mixed-income project involves the construction of twelve (12) residential units and approximately 7,700 square feet of ground floor commercial retail at the corner of Great Neck Road and Marconi Boulevard in Copiague. The building was formerly used as the home of a masonry business. Ardmore Place conforms with the Town of Babylon’s rezoning of the applicant’s property into the “Downtown Copiague Zoning District.”



Of the 12 units, 8 will be 2 BR units and 4 will be 1 BR units. The development will comply with the IDA’s new affordable housing policy, meaning that three (3), or 25% of the units, will be deed restricted as affordable to households earning less than 60% of area median income (AMI). With an AMI of \$116,700 (family of four) for the Nassau Suffolk labor market area, the affordable rents would generally be available and affordable to households earning between \$40,000 - \$56,000, depending on household size. There will be two 2BR affordable units priced at \$1,335 and one 1BR affordable units priced at \$1,084. The other eight (8) units will be market rate with rents projected to start approximately \$1,800 per month.

### SOURCES & USES

The development will be financed with a conventional debt and equity capital structure. The budget is approximately \$3.5 million.

USES OF FUNDS	Amount	
Acquisition	\$558,000	
Demo & Site Work	\$215,000	
Building Renovation	\$2,337,000	
Soft Costs	<u>\$390,000</u>	
TOTAL	\$3,500,000	
SOURCES OF FUNDS	Amount	%
Loan	\$2,430,000	69%
Equity	<u>\$1,070,000</u>	<u>31%</u>
TOTAL	\$3,500,000	100%

The budget seems modest for a development with 12 units and 7,700 square feet of retail.

### SUMMARIZED BENEFITS PACKAGE

The benefit package is summarized below. With the current 2018 tax rate applied, the estimated “as complete” taxes at full assessment would be \$82,609, almost a 3x multiplier. Taxes at full assessment at that level would render the rental residential development financially challenged or more appropriately, infeasible. This is especially the case with 20% of the units having restricted rents.

As such, the proposed financial incentive includes a 15-year PILOT in addition to the exemptions on mortgage recording tax and sales tax exemption on building materials. The PILOT schedule includes an 100% abatement on improvement in the first year. The abatement will burn off from years 2 – 15 at a rate of 6.67% annually.

TAX BENEFIT SUMMARY				
IDA RELATED PROPERTY TAXES		SALES TAX EXEMPTION		
Current Taxes	\$29,160	Construction Cost		\$2,552,000
As Complete Taxes	\$86,209	Value of Building Materials	50%	\$1,276,000
Multiplier	2.96	Sales Tax Rate		8.625%
PILOT and Non-Abated Tax Payment over 20 Years	\$881,490	Value of Exemption on Building Materials		\$110,055
PILOT Savings over 20 Years	(\$755,416)			
MORTGAGE RECORDING TAX				
Mortgage	\$2,430,000			
Mortgage Recording Tax	0.75%			
Value of Exemption	\$18,225			

The PILOT schedule is detailed in Appendix 1 to this memorandum.

## SUMMARY OF NDC ANALYSIS

NDC based its analysis on the revenue assumptions provided in the IDA application. For consistency with other IDA reviews, NDC adjusted the pro forma provided by the developer with the following assumptions:

- Permanent loan assumptions that are in line with the current market for similar projects
  - 20-year amortization
  - Rate of 5.50%
- Adjusting revenue growth to 3% annually
- Adjusting expense growth to 3% annually
- Projecting terminal value of project using a 6% cap rate

Rents and operating expenses are consistent with other comparable developments. Market residential rents are approximately \$1,800 per month and the affordable residential rents are at \$1,084 for a 1BR and \$1,335 for a 2BR.

Returns from the project, with the proposed PILOT schedule projected, are modest but reasonable enough to establish financial feasibility. The metrics used and determined for the project, cash on cash return, cash on cost, and internal rate of return, with the proposed schedule, are lower than what the market normally expects for a comparable residential development.

There is not an incidence of undue enrichment as a result of this financial incentive package. Without the proposed 15-year PILOT schedule, the development would not be financially feasible as the returns for the developer would be prohibitively low. More specifically, with taxes at full assessment, the rental income stream would not be sufficient to attract the necessary debt and equity to cover the development costs.

STABILIZED OPERATING PRO FORMA	without PILOT		w PILOT	
Gross Market Income	\$189,000	\$1,750 avg. rent per unit	\$189,000	
Gross Affordable Income	\$45,048	\$1,251 avg. rent per unit	\$45,048	
Gross Residential Income	\$234,048		\$234,048	
Commercial Income	\$169,488		\$169,488	
Vacancy	(\$17,924)		(\$17,924)	
Effective Gross Income	\$385,612		\$385,612	
Expenses	(\$70,000)		(\$70,000)	
RE Taxes	(\$82,609)	RE Taxes at full assessment	(\$15,250)	PILOT in second year
NOI	\$233,003		\$300,362	
Debt Service	(\$200,588)		(\$200,588)	
Cash Flow	\$32,415		\$99,774	
METRICS	without PILOT		w PILOT	Typical in Market
DCR	1.16		1.50	>1.25
Cash on Cash	3.03%		9.32%	>8%
Cash on Cost	6.66%		8.58%	> 7%
Unlevered Internal Rate of Return (IRR)			9.11%	> 7%
Levered IRR			13.74%	> 10%

## COST / BENEFIT ANALYSIS

The below analysis shows a positive net value to the taxing jurisdictions when taking into account the increase in total taxes received across all taxing jurisdictions.

In addition to the below benefits, the applicant expects 15 temporary construction jobs and approximately 8 full-time equivalent jobs at the retail stores. In addition, the project replaces underutilized and vacant building with an amenity-filled building that provides needed retail and quality affordable and market rate housing in close proximity to the rail station.

BENEFIT SUMMARY	
Sales Tax Exemption	\$110,055
Mortgage Recording Tax Exemption	\$18,225
RE Property Tax Savings through 20 year PILOT	<u>\$755,416</u>
Total Financial Benefit form IDA Package	\$883,696
PILOT and Non-Abated Tax Payment over 20 Years	\$881,490
PILOT Savings	(\$755,416)
Tax Income Over Developer Benefit	\$126,074





**APPENDIX 2: 15 YEAR OPERATING PROFORMA**

			1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gross Market Income	3.00%		189,000	194,670	200,510	206,525	212,721	219,103	225,676	232,446	239,420	246,602	254,000	261,620	269,469	277,553	285,879
Gross Affordable Income	3.00%		45,048	46,399	47,791	49,225	50,702	52,223	53,790	55,403	57,065	58,777	60,541	62,357	64,228	66,155	68,139
Commercial Income	3.00%		169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488	169,488
Gross Income			403,536	410,557	417,790	425,239	432,911	440,814	448,954	457,338	465,973	474,868	484,029	493,465	503,184	513,195	523,507
Vacancy			(\$20,177)	(\$20,528)	(\$20,889)	(\$21,262)	(\$21,646)	(\$22,041)	(\$22,448)	(\$22,867)	(\$23,299)	(\$23,743)	(\$24,201)	(\$24,673)	(\$25,159)	(\$25,660)	(\$26,175)
			5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Effective Gross Income			\$383,359	\$390,030	\$396,900	\$403,977	\$411,266	\$418,773	\$426,506	\$434,471	\$442,674	\$451,124	\$459,827	\$468,792	\$478,025	\$487,536	\$497,331
Expenses Excl of RE Taxes	3.00%		(70,000)	(72,100)	(74,263)	(76,491)	(78,786)	(81,149)	(83,584)	(86,091)	(88,674)	(91,334)	(94,074)	(96,896)	(99,803)	(102,797)	(105,881)
RE Taxes			(9,289)	(15,250)	(21,412)	(27,851)	(34,540)	(41,453)	(48,665)	(56,151)	(63,880)	(71,937)	(80,290)	(88,912)	(97,888)	(107,189)	(116,783)
Total Operating expenses			(79,289)	(87,350)	(95,675)	(104,342)	(113,326)	(122,602)	(132,249)	(142,242)	(152,554)	(163,271)	(174,364)	(185,808)	(197,691)	(209,986)	(222,664)
Net Operating Income			304,070	302,680	301,225	299,635	297,940	296,171	294,257	292,228	290,120	287,853	285,463	282,984	280,334	277,549	274,667
<b>UNLEVERED ANALYSIS</b>																	
NOI		(3,500,000)	304,070	302,680	301,225	299,635	297,940	296,171	294,257	292,228	290,120	287,853	285,463	282,984	280,334	277,549	274,667
Terminal value																	4,225,646
CF		(3,500,000)	304,070	302,680	301,225	299,635	297,940	296,171	294,257	292,228	290,120	287,853	285,463	282,984	280,334	277,549	4,500,313
Internal Rate of Return (IRR)		9.11%															
<b>LEVERED ANALYSIS</b>																	
NOI		(1,070,000)	304,070	302,680	301,225	299,635	297,940	296,171	294,257	292,228	290,120	287,853	285,463	282,984	280,334	277,549	274,667
Debt Service			(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)	(200,588)
Terminal Value																	3,295,636
CF		(1,070,000)	103,482	102,092	100,637	99,047	97,352	95,583	93,669	91,641	89,533	87,265	84,875	82,396	79,746	76,961	3,369,715
Internal Rate of Return (IRR)		13.74%															
Cash on Cash			9.67%	9.54%	9.41%	9.26%	9.10%	8.93%	8.75%	8.56%	8.37%	8.16%	7.93%	7.70%	7.45%	7.19%	6.92%