

NEWSLETTER

New Developments in USDA's Rural Development Multifamily Program

Changes to the Section 515 Program Affect Transactions of Rural Properties

In the past, recapitalization options have been very limited for owners of USDA-subsidized multifamily properties. However, legislation passed over the past two years has created new opportunities for owners. USDA's increased interest in preserving their ageing portfolio has led the agency to be more responsive to owners of Section 515 properties that are in need of physical rehabilitation or may opt-out of the program.

The average age of projects in the USDA Rural Development (RD) portfolio has been steadily increasing over the years, as new construction has dropped off significantly since it peaked in the late 70s, early 80s (see Figure 1). The ageing of the portfolio, coupled with restrictive regulations on Section 515 mortgages, has left many properties with extensive capital needs, limited options, and limited resources for rehabilitation. Demand for Section 515 rehabilitation loans far outweighs the supply that RD has committed for physical improvements. Additional sources of funds, such as the Low Income Housing Tax Credit,

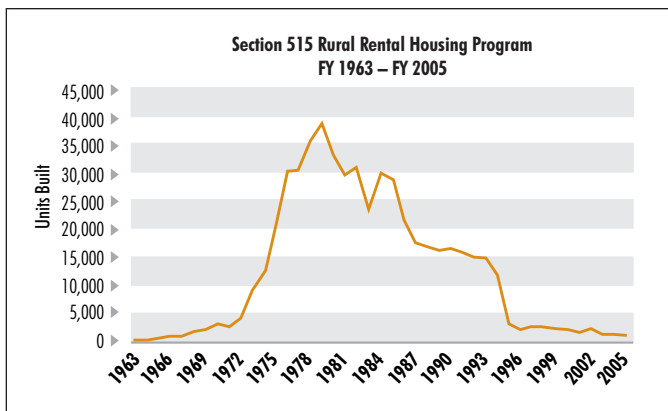


Figure 1

HOME and CDBG programs are also oversubscribed, or are too costly for the typically small size of a Section 515 project to pursue.

Areas with relatively high rent growth, such as properties located in metro, or metro-adjacent, counties have rents that have been restricted and are often significantly below market. If owners were able to opt out of the program, rents could be increased to market, increasing cash flow and equity in the property. Because of recent legislation and legal decisions, many projects are no longer bound by constrictive prepayment prohibitions, and owners may opt out of the program if they feel it is in their

best economic interest: more than two thousand Section 515 projects have already prepaid their mortgages and converted to market rate properties. In response to the prospect of projects opting-out, RD has begun offering financial incentives to owners who are willing to stay in the program and preserve affordability at their projects for an extended period of time.

Conversely, many 515 properties are located in very rural locations that have experienced little or no rent growth over the years. While many of these properties are desperately in need of rehabilitation, they cannot generate sufficient cash flow over and above their first mortgage debt service to support increased debt used for rehabilitation.

For many owners of USDA-subsidized apartment properties, a recapitalization involving a sale of some or all of their RD holdings has become a very viable option, given the legal and regulatory events of the past 2–3 years. Owners that are considering a sale of their property should consider the following benefits:

- Frees up equity to be redeployed at market rates of return.
- Alleviates burden of portfolio and property management in smaller, less profitable assets.
- Receive preservation incentives, which can be passed on to buyers and incorporated into the sales process.
- Availability of prepayment options and incentives coupled with historically low interest/cap rates creates great opportunities for sale.

CB Richard Ellis' Affordable Housing Group specializes in the sale of federally-subsidized projects across the country and has worked with many owners of portfolios of USDA-subsidized projects, helping them to achieve their goals of disposing their RD multifamily assets. Their access to a national pool of real estate capital investors, developers, and experts in regulatory issues and legal council specializing in specific RD matters is unmatched in the industry.

For assistance evaluating the options available for recapitalization of your portfolio, contact a member of the Affordable Housing Group.

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WHO WE ARE

The Affordable Housing Group of CB Richard Ellis specializes in consulting, acquisition, sales and refinancing of HUD subsidized, insured properties, Section 42 LIHTC Properties, and RD Section 515 Multifamily Properties. In recent years, our services have resulted in the repositioning or resale of over \$250 million in federally subsidized apartment properties, at true market rents. Contact us to see how we can help you.

OUR EXPERIENCE

We offer a wealth of resources and expertise to help you.

- Experience with USDA-RD subsidized properties throughout the United States
- Thorough knowledge of RD regulations and standards
- Former HUD Senior Director available in advisory capacity
- Asset recapitalization strategies
- Market evaluation & risk analysis
- Government agency coordination
- Local Market Analysis

PLEASE FAX TO: 206.292.6152 OR 206.292.6033

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