



10400 Detrick Avenue
Kensington, MD 20895-2484
(240) 627-9425



DEVELOPMENT AND FINANCE COMMITTEE

August 26, 2022

10:00 a.m.

YouTube Link: <https://youtu.be/a7Y-GwuZjHQ>

Approval of Minutes:

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Discussion/Action Items:

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Minutes

HOUSING OPPORTUNITIES COMMISSION OF MONTGOMERY COUNTY

10400 Detrick Avenue
Kensington, Maryland 20895
(240) 627-9425

Development and Finance Committee Minutes

July 22, 2022

For the official record of the Housing Opportunities Commission of Montgomery County, an open meeting of the Development and Finance Committee was conducted via an online platform and teleconference on Friday, July 22, 2022, with moderator functions occurring at 10400 Detrick Avenue, Kensington, Maryland beginning at 10:20 a.m., available for viewing [here](#). Due to administrative issues the meeting start time was delayed. Those in attendance were:

Present

Jackie Simon, Chair – Development and Finance Committee
Richard Y. Nelson, Jr. – Commissioner
Jeffrey Merkowitz – Commissioner

Also Attending

Chelsea Andrews, Executive Director
Aisha Memon, General Counsel
Marcus Ervin

Kayrine Brown, Deputy Executive Director
Zachary Marks

Also Attending Via Zoom

Jay Berkowitz
Matt Husman
Fozia Malik
Victoria Dixon
Terri Fowler
Eugenia Pascual
Timothy Goetzinger
Len Vilicic
Nathan Bovelie

Fred Swan
Gail Willison
Ellen Goff
Alex Torton
Gio Kavaladze
Jennifer Arrington
Leidi Reyes
John Broullire
Olutomi Adebo

IT Support

Aries Cruz

Commission Support

Patrice Birdsong, Spec. Asst. to Commission

Commissioner Simon opened the meeting with a welcome and introduction of the Commissioners participating on the Committee.

APPROVAL OF MINUTES

The minutes of the June 24, 2022 Development and Finance Committee open session meeting was approved upon a motion by Commissioner Merkowitz and seconded by Commissioner Nelson. Affirmative votes were cast by Commissioners Simon, Nelson, and Merkowitz.

DISCUSSION ITEMS

1. Westwood Tower Apartments: Approval to Draw on the PNC Bank, N.A. Real Estate Line of Credit (RELOC) to Provide Interim Financing for Westwood Tower Apartments

Marcus Ervin, Director of Real Estate, and Zachary Marks, Chief Investments and Real Estate Officer, provided a presentation requesting that the Development and Finance Committee recommend to the full Commission the following: 1) to authorize interim financing; and 2) to authorize a draw on the PNC RELOC as a source for the interim financing, for a term that is coterminous with the RELOC facility.

Commissioner Simon stepped away briefly during the discussion. Staff addressed the questions of the Commissioners during the absence of Committee Chair Simon. Staff addressed Commissioner Nelson's question regarding an emergency legislation related to the rental increase restrictions of the voluntary rent guidelines. Upon the return of Chair Simon, Commissioner Nelson confirmed that there was no additional discussion during her brief absence and was prepared for a vote. A motion was made by Commissioner Merkowitz and seconded by Commissioner Nelson to recommend to the full Commission for approval at the August 10, 2022 monthly meeting. Affirmative votes were cast by Commissioners Simon, Nelson, and Merkowitz.

After the vote there was discussion of upcoming legislation meetings that may be of interest to HOC.

Based upon this report and there being no further business to come before this session of the Development and Finance Committee, a motion was made by Commissioner Merkowitz

and seconded by Commissioner Nelson to adjourned. Affirmative votes were cast by Commissioner Simon, Nelson, and Merkowitz. The meeting adjourned at 10:42 a.m.

Respectfully submitted,

Chelsea Andrews
Secretary/Treasurer

/pmb

Discussion Items

HILLANDALE GATEWAY: UPDATE OF PRELIMINARY DEVELOPMENT PLAN AND APPROVAL OF ADDITIONAL PREDEVELOPMENT FUNDING

10100, 10110, 10120, AND 10140 NEW HAMPSHIRE AVE, SILVER SPRING, MD



CHELSEA J. ANDREWS, EXECUTIVE DIRECTOR

**Kathryn Hollister, Senior Financial Analyst
Gio Kaviladze, Senior Financial Analyst
Marcus Ervin, Director of Development
Zachary Marks, Chief Real Estate Officer**

August 26, 2022
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Executive Summary

Updated Predevelopment Plan

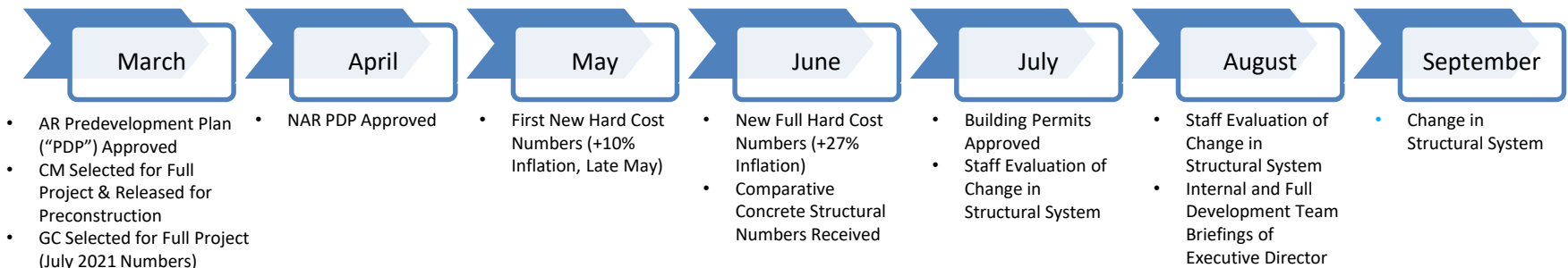
- Broad inflation in 2022 upset the normal relationship between structural systems and sent all project hard costs higher (by \$32MM total over July 2021 projections).
- Steel was disproportionately affected and has continuing geopolitical issues around processing/shipment.
- Concrete system is currently cheaper, is domestically available, and will be competitively bid to capture more of the pricing decline with inflation now abating.

Additional Predevelopment Funding

- Project is nearing the end of predevelopment and requires additional funds (\$1.7MM) on a short-term basis to complete design and secure financing.
- With the Updated Predevelopment Plan, an additional \$2.5MM (included \$309K of ground lease payment) will be needed on a short-term basis to convert design.
- Expending the additional \$2.5MM will lock in an immediate \$3.5MM savings on concrete over the Prescient structure based on most recent cost projections.
- Staff Recommendation: **Fund additional \$4.2MM in predevelopment from OHRF.**

Project Status & Current Development Path

At the March 2 and April 6, 2022, Commission meetings, the selection of the general contractor for the full project and the Preliminary Development Plans for the AR and NAR buildings were approved. Over the past year, staff had already been navigating inflation of specific materials and products due to factory closings and supply chain ruptures. By May, much broader inflation across all construction materials began appearing in our estimates. In June, the selected general contractor completed a new full cost estimation based on conversations with prospective subcontractors that yielded a 27% increase over the July 2021 proposed budget. Inflation was relatively evenly spread across all divisions. However, steel saw a notable four-fold run-up in comparison to the three-fold of lumber and more modest increase in already high concrete prices. The wide, reliable pre-COVID spread between the Precast and concrete structural systems had fully disappeared.



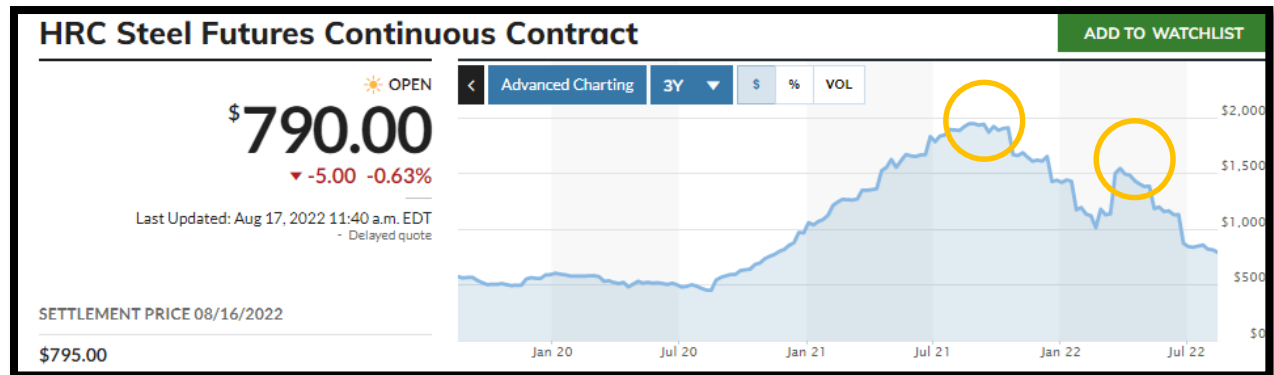
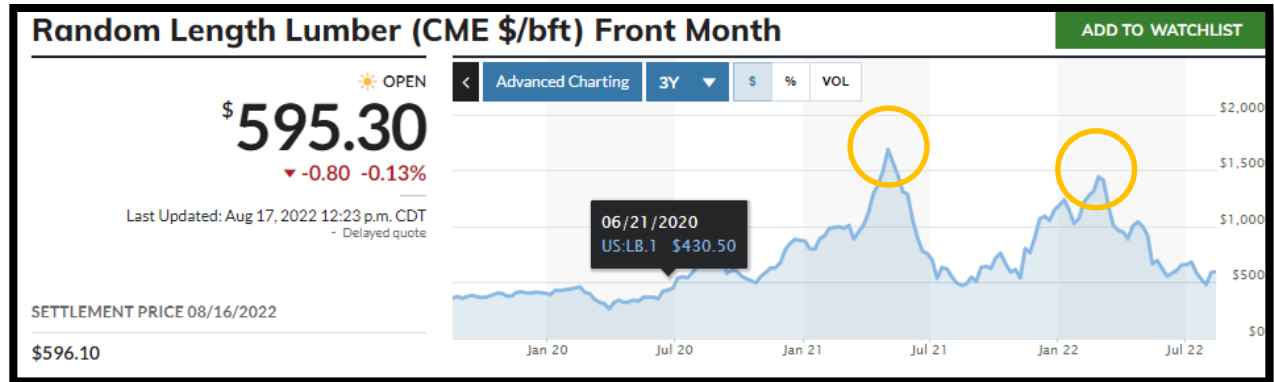
Though Hillandale Gateway has secured full permits for construction using the Precast structural system, the disappearance of its cost advantage to concrete drove staff to evaluate a change to a concrete structural system. This would require administrative amendments to current permits but would not incur any project delays and provides several benefits to HOC.

Inflation's Impact on Core Materials

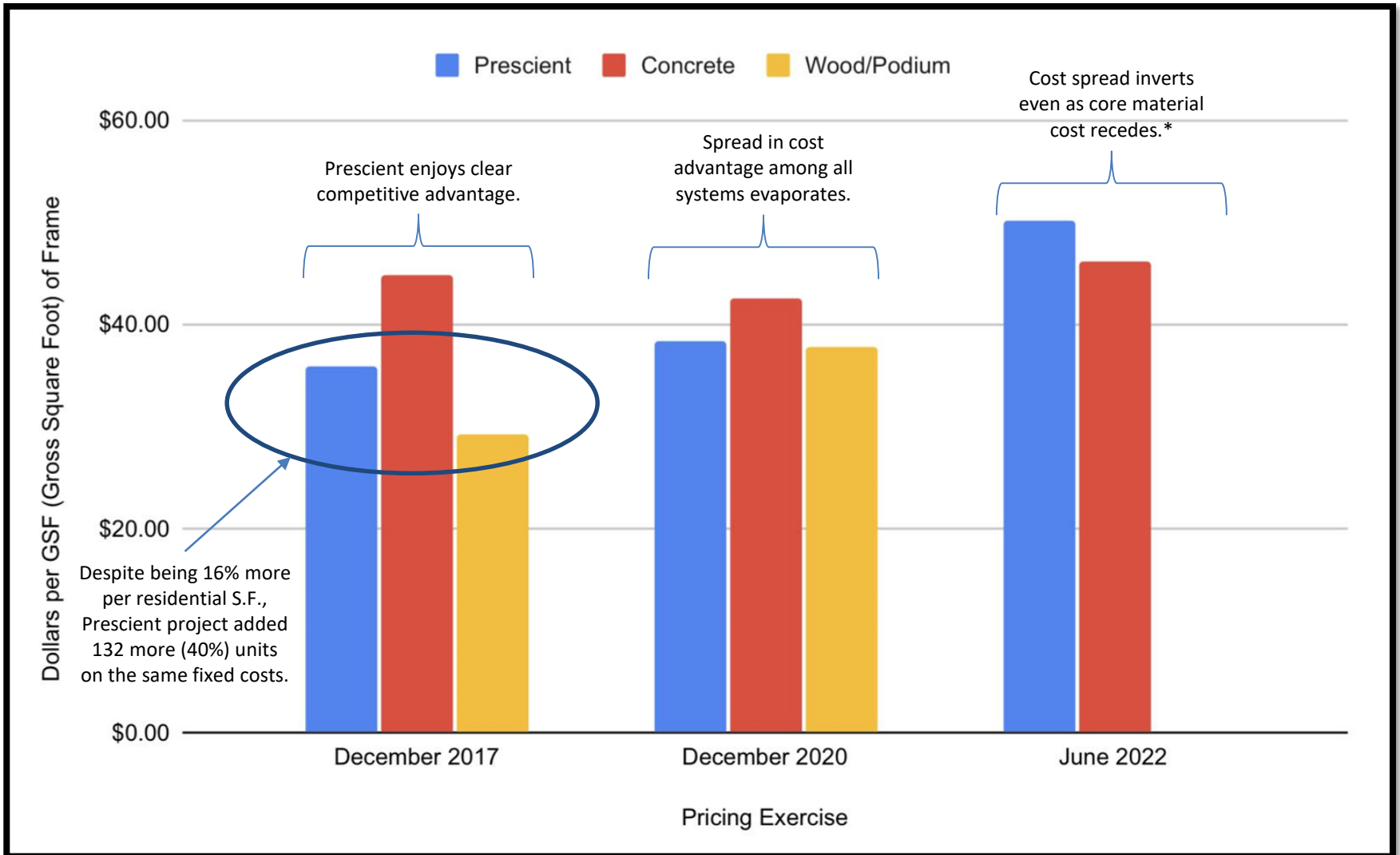
Before COVID, builders enjoyed relatively stable pricing of core structural construction materials. Staff originally evaluated the Prescient steel system in December of 2017. That analysis produced near-par per-unit pricing between the typical wood-over-podium product common to non-CBD, non-Metro-adjacent Montgomery County and the high-rise Prescient system proposed for Hillandale Gateway. The value relationship persisted for nearly three years, even beyond the onset of COVID. Lumber soared as mills shut down and shipping ground to a halt with workers out sick.

It tripled and retraced two separate, largely seasonal times – in the second instance, once single family household formation and secondary home demand exploded in late 2021.

Eventually, the same contagion spread to steel, which saw the most intense increases because of China's large role in steel production. It also endured a second spike with the advent of war in Ukraine, which is not only another world leader in steel production but is also the source of many chemicals key to steel processing. Had HOC been in position to start construction 12-18 months prior, Hillandale Gateway would certainly be using the Prescient steel system and have delivered on the thesis that MPDU bonus height and density can be achieved at per-unit parity to the height-limited wood frame-over-podium system.

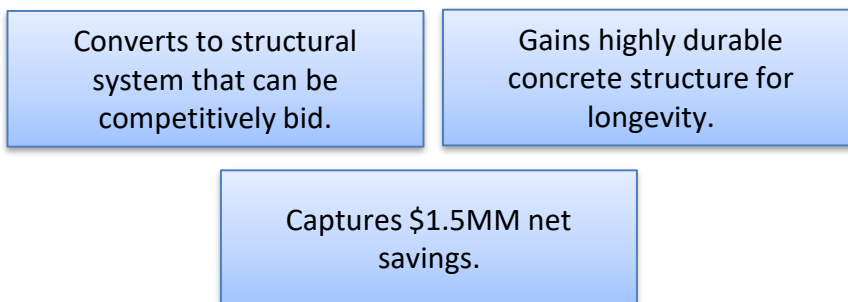


Inflation Wreaks Havoc on Structural Systems



Updated Preliminary Development Plan

Change in Structural System



Steel pricing has declined significantly from its recent inflationary peak. However, those decreases have still not been reflected in current price indications for Prescient.

With the additional demand destruction from several Federal Reserve rate increases this calendar year, all indications are that materials costs should continue to retrace their paths back to pre-COVID levels.

Reduction in steel pricing will inevitably make its way into steel systems pricing and restoring the cost advantages those systems enjoyed prior to the pandemic. Staff expects the broad inflation seen in all construction materials in June 2022 to be notably lower when hard bidding begins in 2023. However, staff is recommending a switch to concrete construction for the two Hillandale Gateway buildings both to best position HOC to reap savings from continued cost price decreases and to move to a more durable system while still improving the transaction economics.

Moving from the proprietary Prescient system to a generic concrete structure will reintroduce competitive bidding to that subcontractor role. This will be more likely to capture the effects of lower materials costs on the pricing of the structural system itself. As of June 2022, even with the cost of redesigning the building to accommodate a concrete structural system, staff projects an immediate net hard cost savings of \$1.5MM.

DPS has indicated that the building permits that were recently approved based on the use of the Prescient system can be amended administratively and at little additional fee. Because the project has 10 months of site work to be completed prior to going vertical, the nine month delay in permit issuance does not impact the start of vertical construction.

	<u>Site Work Start</u>	<u>Site Work End</u>	<u>Permit Issuance</u>	<u>Vertical Start</u>	<u>Vertical Start Delay</u>	<u>Vertical Finish</u>	<u>Vertical Finish Delay</u>
Stay with Prescient	1-2023	11-2023	9-2022	12-2023	0 Months	10-2025	0 Months
Switch to Concrete	1-2023	11-2023	6-2023	12-2023	0 Months	12-2025	2 Months

Updated Preliminary Development Plan

Fund Predevelopment through Full Close

As with all new construction developments in Montgomery County; design, entitlement, and permitting take place over several years. While staff sets out the most

accurate duration it can in its presentation of predevelopment budgets, there is nearly always a reconciliation period toward the end where a target date for full construction mobilization can be better relied upon. Often that date is a few months beyond previous estimates. Were staff not updating the preliminary development plan, that full closing date would be January of 2023; approximately six months beyond the June 2022 full closing date that had been the estimate. Staff estimates the additional predevelopment funding needed to achieve site plan certification, complete construction drawings, and pay financing costs prior to closing to be approximately \$1.72MM.

The staff proposal to change the structural system would move that full closing date back an additional six months and require additional predevelopment spending of \$2.40MM, most of which is for additional design professional work, but includes \$309K of ground lease payments.

	<u>Add</u>	<u>Savings</u>	
Change in Structural Frame	\$2,095,175	-3,500,000	Includes additional dev team time. Savings per CBG pricing update.
Continued Predevelopment Efforts	\$1,722,828		Universal team efforts for ongoing predev, LIHTC Fees, Contingency.
Ground Lease	\$308,895		
Total	\$4,126,898	-3,500,000	
Net Project Impact	\$626,898		

Cost Type	Amount
Land and Acquisition Costs	\$230,445
Site Studies & Reports	\$37,458
Government & Registration Fees	\$94,427
Design Consultants	\$1,557,229
Professional Consultants	\$595,160
Lease Costs	\$308,895
Construction	\$19,116
Furniture, Fixtures & Equipment	\$0
Financing	\$415,263
Misc.	\$520,351
General Contingency	\$348,554
	\$4,126,898

As noted above, the expenditure of the additional \$2.40MM will be more than offset by an estimated structural cost decrease of \$3.5MM based on the June 2022 general contractor's numbers.

Though the change in structural system pushes back by six months, to June 2023, County permission to fully mobilize construction, those changes do not alter Hillandale Gateway's current approval to begin site work. The design team has determined benefits to beginning site work in January as currently planned. Site work that must precede vertical construction is expected to take ten months. A six-month head start to full construction financing yield project timing and cost management advantages.

Staff is working to complete the analysis of cost and funding needs and expects to return to the Commission in November/December 2022 with a proposal to launch site work ahead of the full construction mobilization.

Raising Sources to Meet Higher Costs

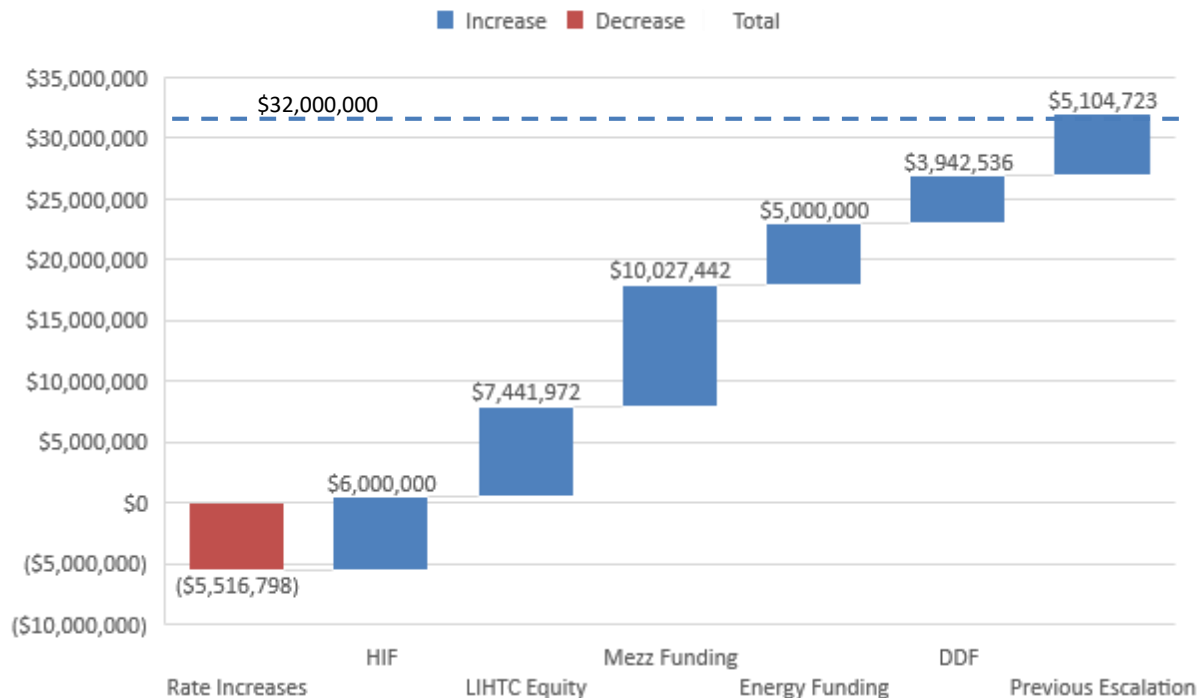
The broad construction cost inflation that appears to have peaked in June 2022 will likely recede from that peak. Material inputs have nearly completed a round trip in pricing since COVID.

Interest rates, however, have moved higher. Forward indications are beginning to suggest a future decline in rates, but staff is working from the most conservative estimates in ensuring project financial viability.

Per the regular process, staff will bring a Financing Plan later this year. Included here are the broad themes and approximate magnitude of the offsets to the June 2022 numbers, which staff is confident will be higher than the eventual real costs. Still, the analysis here does not assume any improvement in those costs including any value engineering.

These different offsets are the result of continuous financing management by staff that occurs throughout the predevelopment process. Solutions range among additional HIF funding (requested not as a cost offset, though the County is expecting that sort of additional request, but as an offset to the recent increase in project affordability), additional LIHTC equity driven by the higher hard cost numbers, increased 2022 AMI limits, cost escalation that staff had already assumed in its previous underwriting, deferring a portion of HOC's LIHTC development fee ("DDF"), and energy funding (both State and Federal). Of note is that the energy funding assumptions here were made prior to the passage of the Inflation Reduction Act.

Major Offsets to Cost Increases



Previous Approvals & Revised Budget

	Source	Resolutions	Amount
(A) Revised Predevelopment Budget			\$14,203,265
Predevelopment Installment 1	OHRF	Res 15-79	\$546,000
Predevelopment Installment 2	OHRF	Res 17-18	\$1,341,500
Predevelopment Installment 3	OHRF	Res 19-10	\$1,616,970
Predevelopment Installment 4	OHRF	Res 20-13	\$2,868,000
Predevelopment Installment 5	OHRF	Res 20-78	\$1,809,253
CONA Sale	HOC Share of Proceeds	Res 19-21AS	\$1,894,644
(B) Total Commission Funds Approved			\$10,076,367
(C) Additional Funds Needed		OHRF	\$4,126,898

Staff is requesting approval of additional predevelopment funds in an amount up to \$4,126,898 (as generally enumerated on Slide 7), in the form of a loan from the OHRF to Hillandale Gateway, LLC, to cover predevelopment costs through closing of vertical construction financing. Per the terms of the Hillandale Gateway, LLC, operating agreement, the loan would earn interest at the current Applicable Federal Rate (currently 3.14%).

The Commission has approved a total of \$10,076,367 (shown to the left) in predevelopment funding to date. As of July 15, 2022, \$7,864,275 has been spent; \$1,687,831 has been obligated; and \$524,261 was available. The additional predevelopment funding requested would not be drawn until all previously-approved funding is spent. All predevelopment expenditures will be reimbursed at closing of construction financing.

As full construction financing is expected to occur in June 2023 (assuming the change in the structural system), this additional predevelopment installment is expected to be outstanding for a short period of time. The full \$14,203,265 can be reimbursed at closing both through repayment to the OHRF and conversion to necessary and expected HOC equity contributions to the two-building development.

Those eventual contribution amounts will be presented to the Commission as part of the Financing Plan and are not expected to exceed the amount of the total predevelopment spending (current and proposed). The total predevelopment spending should be the Commission's maximum commitment of its own resources to the full financing of Hillandale Gateway.

Staff proposes funding this \$4,126,898 installment from the OHRF using the \$5,830,212 in proceeds from the sale of the Holly Hall property to the Duffie Companies.

Hillandale Gateway Predevelopment Funds as of 7/15/2022		
\$	10,076,367	Total Approved Funds
\$	7,864,275	Total Drawn
\$	1,687,831	Total Obligations
\$	524,261	Available Balance

Reference Notes to Previous Actions

Predevelopment Funding to Date

Installments 1: On October 7, 2015, the Commission authorized initial funding of \$546,000 that was sufficient for approximately 17 months of work.

Installments 2: On March 1, 2017, the Commission approved a revised 12-month predevelopment budget and additional funding in the amount of \$1,341,500. The second installment of funding was sufficient for approximately 22 months of work.

Installment 3: On January 9, 2019, the Commission approved a revised predevelopment budget, including approval to fund a third installment of \$1,616,970.

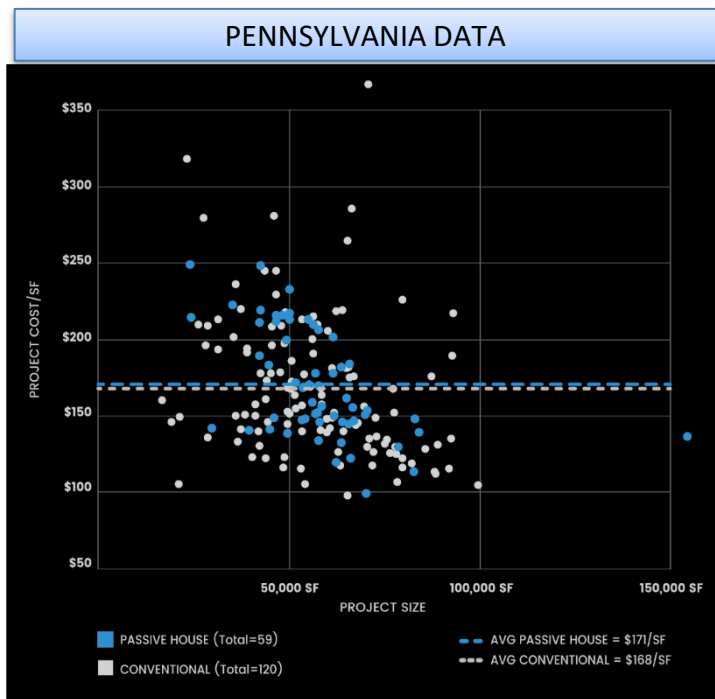
Installment 4: On February 5, 2020, the Commission approved a revised predevelopment budget, including approval to fund a fourth installment of predevelopment funding in the amount of \$2,868,000.

Installment 5: On November 4, 2020, the Commission approved a revised predevelopment budget, including approval to fund a fifth installment of predevelopment funding in the amount of \$1,809,253.

CONA Sale: On February 6, 2019, the Commission approved the sale of the Capital One, N.A. Site ("CONA Site", which HOC had acquired on July 11, 2014) to Duffie and authorized HOC's portion of the proceeds to remain with Hillandale Gateway, LLC to be used for future predevelopment and development activities. The CONA Site and Holly Hall are being entitled together as part of the Hillandale Gateway site plan.

Passive House Value is Net Positive

Both through analysis of substantial data from affordable Passive House transactions in Pennsylvania and a comparative analysis of Hillandale Gateway and other contemporary non-Passive House developments, the Hillandale Gateway development team has placed the upfront cost premium *at most* at between 2%-5%. Per a large scale study involving more than two dozen projects built in Pennsylvania between 2015 and 2016, the cost of Passive House was within 2% of the cost of non-Passive House projects on average, with cost premiums more prevalent on smaller-sized projects and cost savings more prevalent on larger scale projects. For reference, Hillandale Gateway's AR and NAR buildings are ~200,000SF and ~400,000SF, respectively – larger than any of the projects in the Pennsylvania data). As this is an older study, that premium has likely vanished because of purpose-built equipment and better implementation techniques. The comparative analysis conducted by the team in 2020 put the cost premium at less than 2% of the cost per SF of other non-Passive House buildings.



In 2015, Pennsylvania Housing Finance Agency added points into its LIHTC qualified allocation plan to encourage Passive House design.

Comparative Study			
	Hillandale Gateway (Prescient) PASSIVE HOUSE		GC ANALYSIS (Avg Wood over Concrete) NOT PASSIVE HOUSE
Items	Cost per Unit	Delta from Avg	Cost
Metal Panel /sf	-	-	\$ 45.50 /sf
Windows /sf	\$ 68.03	\$ 30.90	\$ 37.14 /sf
Appliances /unit	\$ 5,705.00	\$ 2,140.33	\$ 3,564.67 /unit
Plumbing /fixture	\$ 2,353.00	\$ 112.00	\$ 2,241.00 /fixture
HVAC /unit	\$ 6,999.78	\$ (2,361.88)	\$ 9,361.67 /unit
Electrical /unit	\$ 29,594.00	\$ 6,960.33	\$ 22,633.67 /unit
Finishes /unit	\$ 14,753.00	\$ 332.34	\$ 14,420.66 /unit
Cost / GSF	\$ 149.13	\$ 2.72	\$ 146.41 /sf
Variance from Average	1.86%		

Construction Typ.	Price PSF
Prescient	\$ 149.13
Wood over Concrete	\$ 146.41
Concrete	\$ 207.50

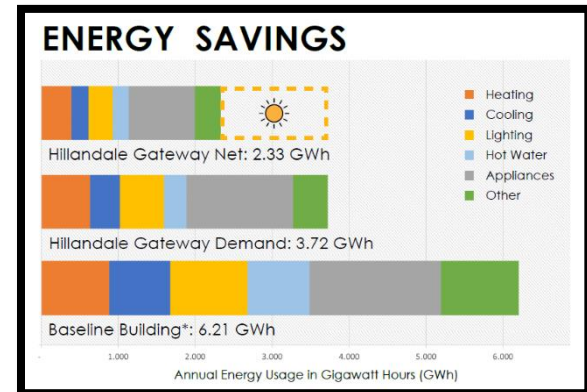
Passive House Value is Net Positive

Demonstrates leadership on County Climate Action Plan.

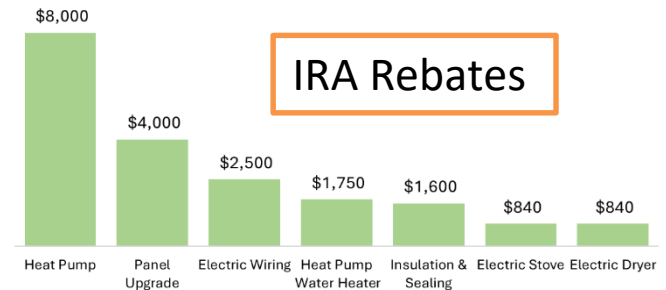
Reduces utility burden to residents.

Protects residents against extreme temperatures during prolonged outages.

Eliminates external drafts, smells, and noises.



<i>Premium and Payback Analysis</i>			
	463 units	308 Units	155 Units
Metric	Total HG	NAR	AR
Premium (@ 2% Hard Cost)			
Total Construction Cost (Buildings)	\$ 148,037,110	\$ 92,594,373	\$ 55,442,737
Indicated Passive House Premium	2%	2%	2%
Total Premium for High Performance	\$ 2,960,742	\$ 1,851,887	\$ 1,108,855
Premium per Unit		\$ 6,013	\$ 7,154
Return Analysis			
	463 units	308 Units	155 Units
Metric	Total HG	NAR	AR
Utility Savings Alone			
Utility Savings Per Annum	\$ 348,600	\$ 231,898	\$ 116,702
Return on Investment			
Simple ROI (Savings per Annum/Total Premium)		12.52%	10.52%
Simple Payback			
Simple Payback (Total Premium/Savings per Annum)		8.0	9.5
Capped Value of Savings (at indicated Cap)			
Capped Value of Savings per Annum	\$6,972,000.00	\$4,637,961.12	\$2,334,038.88
<i>Notes:</i>			
Hard cost excludes renewables.			
Hard cost is for buildings not including site, retail, garage.			
Estimated payback is irrespective of utility payer.			



With such minimal upfront costs, the payback period is relatively short and the return on investment high. On a present value basis, the value of the savings is nearly 2.5x the upfront investment (which itself is leveraged of course). As described above, these numbers do not take into account the significant new sources of funding and cost offsets authorized by the Inflation Reduction Act.

Summary and Recommendations

ISSUES FOR CONSIDERATION

Does the Development & Finance Committee join staff's recommendation that the Commission accept its Update of the Preliminary Development Plan, discussed herein?

Does the Development & Finance Committee join staff's recommendation to the Commission that it authorize:

1. Increasing the predevelopment budget to \$14,203,265?
2. Obtaining an additional predevelopment loan installment of \$4,126,898 from the Opportunity Housing Reserve Fund at the Applicable Federal Rate, which loan will be repaid at full construction financing?

BUDGET/FISCAL IMPACT

There is no adverse impact on the Commission's FY2023 Operating Budget. Current unobligated OHRF balance is \$11,349,789.

TIME FRAME

For discussion at the August 26, 2022, meeting of the Development & Finance Committee and formal action in open meeting of the Commission on September 14, 2022.

STAFF RECOMMENDATION AND COMMISSION ACTION NEEDED

As these changes would enable the full permitting and financing of the Hillandale Gateway development and better position the development team to manage construction cost risk, staff is recommending that the Development and Finance Committee join staff's recommendation to the Commission to accept its Update of the Preliminary Development Plan, discussed herein and that it authorize:

1. Increasing the predevelopment budget to \$14,203,265; and
2. Obtaining an additional predevelopment loan installment of \$4,126,898 from the Opportunity Housing Reserve Fund at the Applicable Federal Rate, which loan will be repaid at full construction financing.