COUNCIL AGENDA: 03/26/19
FILE: 19-117
ITEM: 4.2

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Jacky Morales-Ferrand

SUBJECT: SEE BELOW

DATE: March 15, 2019

Approved D.DSyL Date 3/15/19

SUBJECT: ELLIS ACT ORDINANCE RE-CONTROL PROVISIONS

RECOMMENDATION

Accept the verbal staff report on research on the Ellis Act Ordinance's re-control provisions including conversations with developers and lenders, potential alternatives for meeting re-control requirements and accept the ancillary staff report.

OUTCOME

City Council approval of the recommendation will result in staff conducting additional research and analysis to identify potential alternatives for re-control requirements.

BACKGROUND

On May 10, 2016, the City Council directed staff to develop a local Ellis Act Ordinance to address the removal of rent stabilized properties from the rental market. The City Council gave this direction as part of the policies adopted to strengthen the Apartment Rent Ordinance (ARO).

The City Council approved the Ellis Act Ordinance on April 18, 2017. This action established a process by which a property owner can remove their apartments from the rental market. The process included providing tenants with noticing timelines, relocation benefits, and the ability to return to the unit if it was returned to the rental market. It also included re-control provisions if the owner built new apartments. Upon approval of the Ellis Act Ordinance, the City Council provided direction to the City Manager to return with additional research regarding the impact of subjecting all "replacement" apartments to re-control by the Apartment Rent Ordinance. Replacement apartments are new apartments constructed on the site of the rent stabilized apartments removed from the market via the Ellis Act Ordinance. As part of that action, the City Council directed Housing Staff to 1) complete additional research regarding the impact of subjecting all replacement units to re-control by the Ellis Act; and 2) provide the City Council with additional research regarding existing Ellis Act Ordinances throughout California.

On April 24, 2018, the City Council amended the Ellis Act Ordinance to reduce the number of replacement apartments subject to re-control to the greater of: (a) the number of demolished rent stabilized units, or (b) half of newly constructed replacement apartments (rather than all the replacement units). In addition, non-ARO apartments with three or more units became subject to the Ellis Act Ordinance's notice requirements and relocation specialist fee. The City Council also approved an exemption from the re-control provisions if 20% of the new replacement apartments are deed-restricted affordable apartments (i.e. Inclusionary Housing Ordinance built on-site plus 5% of units at 100% of area median income). The goals were to 1) preserve rent stabilized apartments, 2) provide developers with viable options to meet the Ellis Act Ordinance requirements, and 3) provide new housing opportunities. This change became effective on June 6, 2018.

On February 5, 2019, the Housing Department provided an update to the City Council on the Rent Stabilization Program. The City Council directed staff to conduct analysis and return with a verbal update on:

- ***Developers and lenders:*** Findings from the interviews with developers and lenders regarding the impact of the Ellis Act re-control provisions;
- ***Threshold density increase resulting in a net positive for affordable housing:*** Return with a detailed analysis within six months including a threshold of the number of new units (for a build on-site development) which could create a net positive number of affordable housing units;
- ***Ellis Act re-control provision impact on new residential projects:*** Conduct updated research on the re-control provision in the Ellis Act to determine the extent to which makes new residential projects more difficult to build; and
- ***Other replacement formulations to encourage construction:*** Consider other formulations that maintain a minimum one-to-one replacement of rent stabilized or rent-restricted apartments to encourage construction of new housing.

The direction included an update on the progress to be provided as part of the Housing Crisis Workplan. The Ellis Act item was delayed to the March 26, 2019, City Council meeting in order to allow time to complete a conflicts analysis. The memorandum from the Mayor and Vice Mayor initiating this direction is included in **Attachment A**.

Ellis Act Ordinance

The Ellis Act Ordinance establishes a process by which a property owner can remove their apartments from the rental market. A summary of the Ellis Act Ordinance requirements is provided below:

For tenants of ARO and non-ARO apartments:

- **Noticing** – All households must be provided with a minimum of 120 days' notice prior to the removal of the property from the rental market. Upon request, special populations including residents over the age of 62, disabled, terminally/catastrophically ill, and residents with school-aged children must be given up to one-year notice to vacate.
- **Relocation Specialist Services** – All tenant households are entitled to relocation services through a specialist who assists tenants in the procedures, obtaining assistance, and developing a relocation plan.

For tenants of ARO apartments:

- **Relocation Benefits** – All tenant households are eligible to receive relocation benefits. Qualifying households include low-income residents, residents over the age of 62, disabled, terminally/catastrophically ill, and residents with school-aged children are eligible for additional relocation benefits.
- **Relocation Specialist Services** – All tenant households are entitled to relocation services through a specialist who assists tenants in the procedures, obtaining assistance, and developing a relocation plan.
- **Right to Return** – If the removed apartments return to the rental market within ten years, tenants have a right to return to their apartments.
- **Re-control** – If a property owner demolishes existing rent stabilized apartments and rebuilds apartments at the same location within five years, the greater of 50% of all new apartments or the number demolished will be subject to the City's Apartment Rent Ordinance. The owner sets the initial rent for these re-controlled replacement apartments.

ANALYSIS

Re-control Amendment by the City Council allows option for developer to rebuild affordable apartments instead of re-control

In response to concern about Ellis Act re-control provisions, a waiver of re-control provisions was introduced in April 2018. Developers moving forward with projects of 20 units or more may exceed the current Inclusionary Ordinance Provisions by providing an additional 5% affordable units at 100% AMI may apply for a waiver of re-control provisions. This means that instead of being subject to rent control, projects building twenty or more units and 20% of the rental units are dedicated as affordable to households in the following Area Median Income (AMI) categories of 9% affordable to 80% AMI, 6% affordable to 50% AMI, and 5% affordable to 100% AMI.

For example, if there are currently four apartments and there are 100 apartments being proposed for building, the following new units would be subject to the following re-control provisions:

- 9 apartments at 9% affordable to 80% AMI
- 6 apartments at 6% affordable to 50% AMI
- 5 apartments at 5% affordable to 100% AMI

As a result, of the 100 new apartments built, 20 apartments would be deemed affordable.

Re-control of Apartments

Alternatively, an owner who demolishes an ARO property and builds new apartments will be subject to the re-control requirements under the Ellis Act Ordinance if they choose not to build on-site affordable housing pursuant to the IHO. In this instance, the owner sets the initial rent to the current market rate and then any subsequent rent increase is subject to the ARO's annual maximum of 5%. All of the other provisions of the ARO would also apply to these units.

The 5% Rent Increase Limit Has No Empirical Impact on Financing New Apartments

The City engaged David Paul Rosen and Associates to evaluate the potential impact of ARO obligations resulting from the demolition of ARO properties on the development of new market rate housing. The consultant evaluated the difference in cash flows, property valuation, and supportable debt under alternative restrictions to determine the extent to which the financing of the new apartments is affected. The results of this work can be found in the report titled *Assessing the Potential Effect of the ARO on New Development*. The report is included in **Attachment B.** The report concludes that first lenders typically underwrite new development assuming 2 - 3% growth rates in rents. The 5% annual general increase in the ARO would not be a limitation to this financing.

Other Cities Require Re-control for All New Apartments

The Housing Department researched the different re-control provisions in cities with Ellis Act ordinances. The ordinances of San Francisco, Berkeley, West Hollywood, Los Angeles, and Santa Monica have provisions requiring all new housing developments following an Ellis Act withdrawal are subject to the rent control provisions of that jurisdiction. This is consistent with San José's current requirements. Los Angeles provides an exemption from rent control provisions to developers who replace the new units with 20% restricted affordable units. Table 1 summarizes these provisions.

Table 1: Summary of Cities with Ellis Act Provisions

	San Francisco	Berkeley	West Hollywood	Santa Monica	Los Angeles
What is covered by Ellis?	3 units or more	All	2 units or more & single family homes when tenant occupied	All	5 units or more
How many replacement units will be subject to re-control?	All	All	All	All	All
Are there exemptions to re-control?	N/A	N/A	N/A	N/A	Yes

Re-control has had Mixed Results in Preventing the Loss of Rent Stabilized Apartments

The Housing Department also looked at the impact of Ellis Act Ordinance provisions in these jurisdictions. The Department found that in some jurisdictions which require all new apartments to be covered by rent control provisions, the overall number of rent stabilized apartments erodes over time. Even if the jurisdiction requires re-control of all new units, the provisions may lead developers to make choices that avoid the Ellis Act re-control obligations. Santa Monica is a case in point. It has the longest standing Ellis Act in the State.

According to the 2016 Santa Monica Rent Control Board Consolidated Annual Report, Santa Monica has lost over 2,000 rent controlled apartments through Ellis Act removals Santa Monica requires that all newly constructed apartments built within five years are required to be covered by rent control. However, staff from Santa Monica have observed that properties do not always return to the rental market. One reason for this is because apartments are often replaced with for-sale housing, commercial use, and/or mixed use development. In addition, developers building rental housing sometimes do not bring the apartments into the rental market until the five-year re-control period required under the Ellis Act has lapsed. These factors have led to the net loss of apartments covered by Santa Monica' s rent control provisions.

Additional Research

The City Council directed staff to conduct additional analysis of the re-control provisions, including considerations of other formulations that maintain a minimum one-to-one replacement of rent stabilized apartments. Staff from the Housing Department and Office of Economic Development are holding interviews with developers with proposed projects impacted by the Ellis Act. This information along with additional research will be presented to the City Council as a verbal report for consideration.

Staff will be providing a verbal report on:

- Stakeholder meetings with developers, and lenders
- Interviews with tenants from proposed Ellis Act Ordinance projects
- Public Community meeting
- Other cities Ellis Act re-control provisions and impact on development

PUBLIC OUTREACH

The Housing Department has conducted community outreach in the past regarding the Ellis Act Ordinance and will continue to meet with a wide range of stakeholders while developing the proposed Ordinance. Staff will return to the City Council with a verbal update as directed by the City Council on March 26, 2019.

EVALUATION AND FOLLOW-UP

If directed by the Council, staff will return with further research and/or amendments to the Ellis Act Ordinance.

COST IMPLICATIONS

There are no cost implications.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office, the City Manager's Budget Office and the Office of Economic Development.

COMMISSION RECOMMENDATION/INPUT

The proposed amendments to the Ellis Act Ordinance were presented to the Housing and Community Development Commission (HCDC) at its special meeting on March 7, 2019. The Commission unanimously recommended against any amendments to the Ellis Act Ordinance and approved an Ad Hoc Subcommittee to draft a letter to the City Council. A summary of the Commissioners' concerns include:

- The current provisions of the Ellis Act Ordinance was enacted only ten months ago and after extensive community engagement and public comment was conducted.
- A compromise was already approved by the City Council on April 24, 2018. A developer could choose to dedicate twenty percent (20%) of the new units to income

restrictions. It was also a compromise from the original Ellis Act Ordinance which required 100% of new rental units to be rent-stabilized if they were built to replace buildings that were subject to rent stabilization.

- Weakening the Ellis Act Ordinance will only accelerate the crisis of affordable housing in San José.

CEQA

Not a Project, File No. PP17-009, Staff Reports, Assessments, Annual Reports, and Informational Memos that involve no approvals of any City action.

/s/
JACKY MORALES-FERRAND
Director, Housing Department

For questions, please contact Rachel VanderVeen, Deputy Director, at (408) 535-8231.

ATTACHMENTS:

Attachment A: Mayor and Vice Mayor Memorandum, Rent Stabilization Program Implementation Plan, dated February 1, 2019
Attachment B: David Rosen and Associates Report, "*Assessing the Potential Effect of the ARO on New Development*", dated March 28, 2018

ATTACHMENT A

City Council: 02/05/19
Item: 4.3

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

To: **CITY COUNCIL**

From: Mayor Sam Liccardo
Vice Mayor Chappie Jones

Subject: **RENT STABILIZATION PROGRAM IMPLEMENTATION PLAN**

Date: February 1, 2019

Approved: 2-1-19

RECOMMENDATION

1. Accept the Rent Stabilization Program Implementation Plan Update.

2. Direct the City Manager to conduct additional analysis of the re-control provision in the Ellis Act Ordinance to determine the extent to which it makes new residential projects infeasible.
    a. Consider whether other formulations—which still maintain a minimum 1-for-1 replacement of rent controlled or rent-restricted units—can improve feasibility of housing development.
    b. Return to Council with the results of this analysis at the next update on the Housing Crisis Workplan.

BACKGROUND

When the Ellis Act Ordinance was last updated in April 2018, Housing Staff acknowledged that the 50% requirement amounted to a "best-guess" strategy to avoid dis-incentivizing development of much-needed rental housing while maintaining our existing ARO housing stock. We expected that we would need to monitor the response of the housing market, and learn from feedback.

In the ten months since, we have seen very few Ellis-relevant housing development proposals emerge, and have heard anecdotally that the re-control requirement undermines the viability of several projects. If we have any intention of meeting our affordable and market-rate housing goals, Council must fully understand the impacts of the current requirement. We urge approval.

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March 28, 2018

To: Kristen Clements

From: Nora Lake-Brown, David Rosen

Subject: Assessing the Potential Effect of the ARO on New Development

This memo summarizes findings from DRA's analysis of the potential effect of ARO obligations on demolished ARO housing properties that are rebuilt with new market rate housing. DRA focused on the potential difference in cash flows, property valuation and supportable debt under alternative restrictions and the extent to which the financing of new market rate housing construction is affected.

To complete this assignment DRA conducted interviews with representatives of private debt and mezzanine debt/equity sources, using the interviewee list and interview questions outlined in DRA's memo dated February 9, 2018. DRA prepared a financial analysis of prototypical rental developments and calculated supportable first mortgage financing using financing terms and underwriting standards consistent with GSE multifamily loan programs. DRA also compared trends in San Jose apartment rents with the 5% cap on ARO units.

SUMMARY OF FINDINGS

In its lender and investor interviews and analysis, DRA focused on the following key questions regarding the effect of ARO restrictions on the financing of new multifamily housing development[1]:

1. How do the ARO restrictions affect the sizing of the senior first mortgage?
2. How do the ARO restrictions affect subordinate mezzanine debt/equity financing?
3. How do historical rent trends in San Jose compare to the 5% cap under the ARO?

[1] These interviews will inform DRA's middle income debt fund analysis as well as the ARO analysis.

DRA completed the following lender and investor interviews for this assignment:

- Andrew Ditton at Citibank;
- Stephanie McFadden at CBRE (formerly at Union Bank);
- Kenji Tamaoki at Prudential;
- Bob Simpson and Angela Kelcher at Fannie Mae.

Effect on First Mortgage Financing

In terms of first mortgage financing, the key underwriting factors affecting first mortgage sizing include the DSCR, mortgage interest rate, loan to value ratio, and escalation rates and cap rates used to determine projected value upon exit. Current term sheets for FreddieMac and FannieMae fixed-rate multifamily loans are attached to this memo.

Due to GSE underwriting standards of 2% escalation on revenues and 3% on costs for the purpose of the refinancing test, the 5% annual cap on rent increases imposed by the ARO does not affect the sizing of the first mortgage. Standard fixed-rate mortgage products for conventional multifamily properties from both FannieMae and FreddieMac require a loan-to-value (LTV) ratio of no more than 80% and a minimum debt service coverage ratio (DSCR) of 1.25. Based on our cash flow analysis, first mortgage financing on new multifamily construction in San Jose is currently constrained primarily by DSCR, rather than LTV requirements.

Our lender interviews confirmed that ARO rent caps would have no effect on first mortgage financing for new apartment construction. Lenders further confirmed that any effects ARO rent caps might have on subordinate mezzanine debt/equity financing would not affect senior mortgage financing.

DRA also confirmed through its interviews that mezzanine lenders and investors use similar escalators and refinancing tests in assessing the viability of mezzanine debt and equity investments as conventional lenders. Therefore, the sizing of mezzanine debt or equity is not directly affected by ARO rent caps. One lender mentioned that there may be a perception that ARO rent caps subject multifamily property owners to limitations on the "upside" while providing full exposure to "downside" risks. This is despite the fact that there is no 10-year period (the length of time typically used for the refinance test) since 1970 where market rents have increased by more than an average of 5% per year, as described in the next section.[1]

The perception of a limit on upside potential, however, may lead to ARO projects being viewed slightly less competitively by lenders and investors than projects without ARO restrictions, all other factors being equal. We uncovered no evidence of a lack of liquidity for such projects, however, ARO projects may receive slightly less competitive pricing. Given the number of economy-wide and project-specific factors that affect pricing and investment, it is not possible to isolate or quantify the amount, if any, of this pricing effect.

Historical Rent Trends in San Jose

Comparing historical trends in apartment rents in San Jose with the 5% annual cap imposed by the ARO sheds light on the potential effect of ARO restrictions on underwriting of subordinate debt and equity. **Table 1** and **Charts 1** and **2** on the following pages show the annual percentage increase in the average effective monthly rent per unit and average effective monthly rent per square foot[2], along with the Consumer Price Index for all urban consumers for rent (CPI-U Rent), from 2006 through 2017. Since 2009, the lowest point in the market during this period, the average annual increase in monthly rents has been 3.5%, well below the 5% ARO cap. Additional data on the CPI-U Rent back to 1970 indicates the average annual increase over the past 46 years has averaged 4.9%. With these rent trends, it would be difficult to support underwriting projected rent increases over 5% per year.

[1]Based on analysis of CPI-U Rent data since 1970 and CoStar rent data since 2006.

[2]For 4 and 5 star properties as rated by CoStar (5 stars is the highest rating).

Table 1 Annual Percentage Increase in Apartment Rents[1] and the Consumer Price Index 2006 to 2017					
	Effective Monthly Rent Per Unit[1]		Effective Monthly Rent Per Square Foot[1]		
Year	**$**	**Annual Change**	**$**	**Annual Change**	**CPI-U Rent)**
2006	$2,172	--	$1.83	--	--
2007	$2,348	8.1%	$2.00	9.3%	3.9%
2008	$2,379	1.3%	$2.06	3.0%	4.1%
2009	$2,171	-8.7%	$1.86	-9.7%	3.2%
2010	$2,278	4.9%	$1.95	4.8%	-0.1%
2011	$2,353	3.3%	$2.03	4.1%	2.3%
2012	$2,449	4.1%	$2.15	5.9%	4.1%
2013	$2,599	6.1%	$2.28	6.0%	4.5%
2014	$2,721	4.7%	$2.45	7.5%	5.5%
2015	$2,823	3.7%	$2.66	8.6%	6.1%
2016	$2,782	-1.5%	$2.68	0.8%	--
2017	$2,869	3.1%	$2.75	2.6%	--
2009 - 2017	**--**	**3.5%**	**--**	**3.3%**	**3.7%**

[1]Includes 4- and 5-star properties as rated by CoStar (5 stars is the highest rating).
Source: CoStar; City of San Jose, DRA.

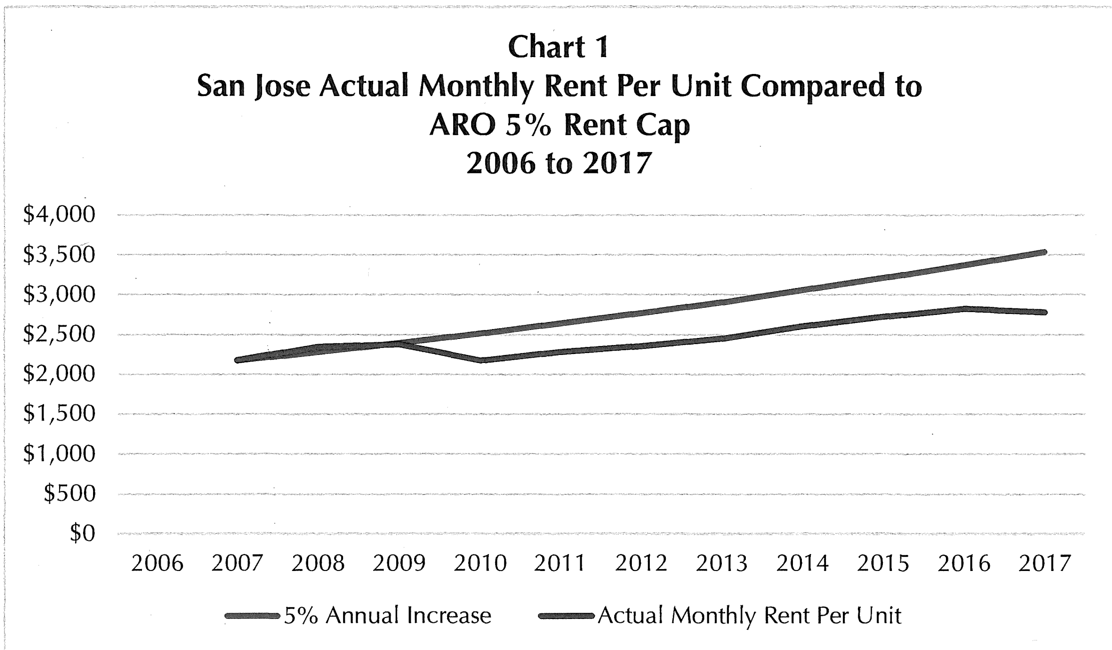
Chart 1
San Jose Actual Monthly Rent Per Unit Compared to
ARO 5% Rent Cap
2006 to 2017
$4,000
$3,500
$3,000
$2,500
$2,000
$1,500
$1,000
$500
$0
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017
5% Annual Increase
Actual Monthly Rent Per Unit

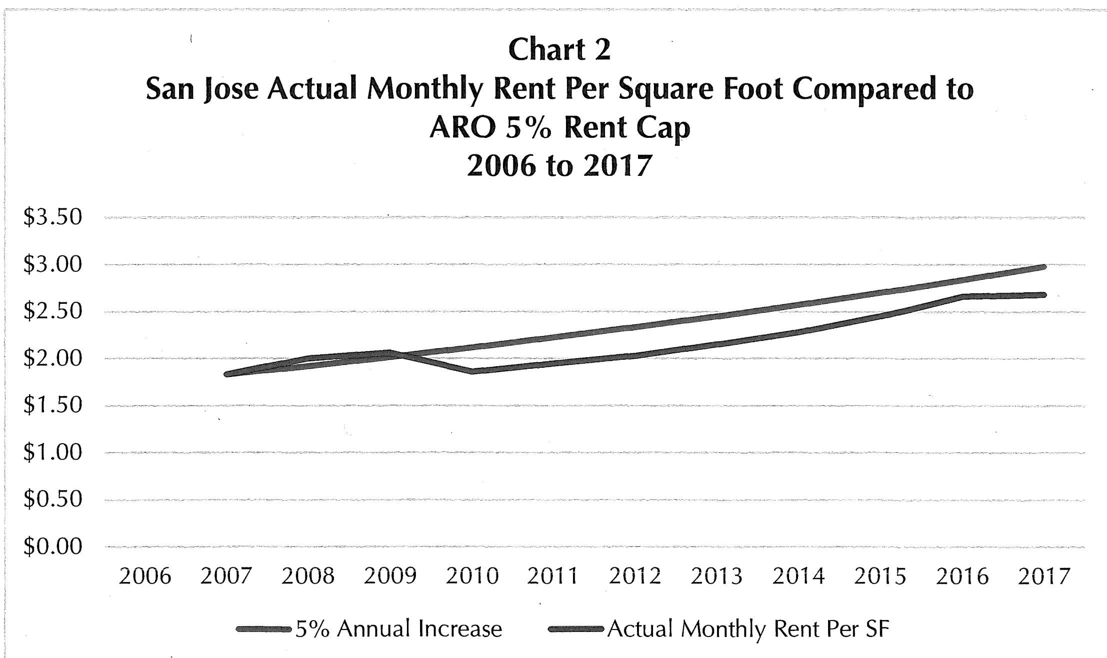
Chart 2
San Jose Actual Monthly Rent Per Square Foot Compared to
ARO 5% Rent Cap
2006 to 2017
$3.50
$3.00
$2.50
$2.00
$1.50
$1.00
$0.50
$0.00
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017
5% Annual Increase
Actual Monthly Rent Per SF

CASH FLOW ANALYSIS

DRA prepared a cash flow analysis estimating the supportable first mortgage financing from prototypical newly constructed multifamily apartment projects using:

- Loan terms (LTV, DSCR), escalation rates (2% on revenues; 3% on operating costs), and current interest rates[1] for multifamily fixed rate mortgages used by FannieMae and FreddieMac (estimated at 5% for 30-year amortization).
- Data from CoStar on average rents by unit bedroom count and subarea within the City of San Jose for apartment properties constructed since 2015, representing rents for newly constructed properties. CoStar data were used to create prototypical housing developments (in terms of total units, unit bedroom count distribution, square footages and rents) for the five geographic market subareas of San Jose defined by CoStar.
- Operating cost data for conventional apartment properties in San Jose from the Institute of Real Estate Management, by housing product type.

Table 2 on the next page summarizes the financing assumptions used in the analysis. **Table 3** on the following page summarizes rent and operating costs assumptions.

Since we have concluded that ARO restrictions have no effect on first mortgage sizing or refinance tests used by GSE lenders, the percentage of ARO replacement units (100%, or 200% of demolished AMO units) has no effect on these cash flow projections. The projections assume that the project's Citywide inclusionary housing requirement is met through an alternative compliance method, such as payment in lieu, and does not contain on-site inclusionary units.

Appendix A contains the detailed financial analysis, including **Table 4**, which describes the rental prototypes in terms of unit sizes and bedroom count distribution, cash flow projections for each prototype, followed by current FannieMae and FreddieMac fixed rate multifamily loan term sheets.

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[1] 5% interest rate for 30-year amortization, FannieMae fixed-rate loan, Feb. 16, 2018.

DAVID PAUL ROSEN & ASSOCIATES
DEVELOPMENT, FINANCE AND POLICY ADVISORS

Table 2
Cash Flow and Financing Assumptions
San Jose ARO Analysis

Escalation Rates: Underwriting and Refinance Analysis	
Unregulated Rents	2.0%
ARO Rents	2.0%
Inclusionary Rents	2.0%
Laundry/Misc. Income	3.0%
Retail Income	3.0%
Operating Costs	3.0%
Cap Rates	
Entry Cap Rate	5.0%
Exit Cap Rate	7.0%
Financing Assumptions	
First Mortgage Interest Rate	6.0%
Amortization Period	30 years
Debt Service Coverage Ratio (DSCR)	1.25
Loan to Value (LTV) Ratio	80%
Refinance Assumptions	
Interest Rate	7.0%
Amortization Period	30 years
DSCR	1.25
LTV	80%

Sources: Lender and investor interviews; GSE term sheets; DRA.

Table 3
Monthly Rent Per Square Foot and Annual Operating Cost Assumptions
San Jose ARO Analysis

	Downtown San Jose	West San Jose	Outer North San Jose	South San Jose	East San Jose
Studio	--	--	$3.60	$3.60	$3.95
One BR	$3.33	$3.33	$3.33	$3.00	$3.33
Two BR	$2.80	$2.80	$2.80	$2.60	$2.30
Three BR	--	--	$3.00	$2.45	
Average	$3.07	$3.13	$3.09	$2.80	$2.88
Operating Costs/SF	$14.20	$14.20	$14.20	$9.25	$9.25
Operating Costs/Unit	$12,894	$12,141	$13,362	$8,233	$7,770

[1]Rent assumptions from CoStar for properties built 2015 through 2017. Based on average monthly rent by submarket area and unit bedroom count.
[2]Total annual operating expenses per square foot, including property taxes, from Institute of Real Estate Management 2017 Income/Expense Analysis for San Jose.
Sources: CoStar; IREM; City of San Jose; DRA.

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Appendix A
Assessing the Potential Effect of the ARO on New Development
City of San Jose

3/28/18

List of Tables

San Jose ARO Analysis

Table 1
City of San Jose
Apartment Rent Trends
4 and 5 Star Properties (1)

	Inventory (Units)	Effective Monthly Rent/Unit	Annual Change	Effective Monthly Rent/SF	Annual Change	Annual Change in CPI-U-Rent
2006	21,887	$2,172		$1.83		
2007	22,774	$2,348	8.1%	$2.00	9.3%	3.9%
2008	23,606	$2,379	1.3%	$2.06	3.0%	4.1%
2009	23,849	$2,171	-8.7%	$1.86	-9.7%	3.2%
2010	24,119	$2,278	4.9%	$1.95	4.8%	-0.1%
2011	24,656	$2,353	3.3%	$2.03	4.1%	2.3%
2012	27,410	$2,449	4.1%	$2.15	5.9%	4.1%
2013	30,524	$2,599	6.1%	$2.28	6.0%	4.5%
2014	33,820	$2,721	4.7%	$2.45	7.5%	5.5%
2015	39,178	$2,823	3.7%	$2.66	8.6%	6.1%
2016	42,147	$2,782	-1.5%	$2.68	0.8%	--
2017	43,843	$2,869	3.1%	$2.75	2.6%	--
2006-2017 (2)			2.6%		3.8%	
2007-2017 (2)			2.0%			3.7%
2008-2017 (2)			2.1%		3.2%	3.7%
2009-2017 (2)			3.5%		3.3%	3.7%
2010-2017 (2)			3.4%		5.0%	3.7%
2011-2017 (2)			3.4%		5.0%	4.5%
2011-2017 (2)			3.2%		5.2%	5.1%

(1) The CoStar Building Rating System is a national rating for commercial buildings. The highest rating is 5 stars.
(2) For the CPI-U Rent, annual changes are through 2015 rather than 2017.

Sources: CoStar; City of San Jose; DRA.

Table 2
Cash Flow and Financing Assumptions

Escalation Rates: Underwriting/Refinance Analysis	
Unregulated Rents	2.00%
ARO Rents	2.00%
Inclusionary Rents	2.00%
Laundry/Misc. Inc.	3.00%
Retail Income	3.00%
Operating Costs	3.00%
Cap Rates	
Entry Cap Rate	5.00%
Exit Cap Rate	7.00%
Financing Assumptions	
Interest Rate	5.00%
Amortization Term (Years)	30
DSCR	1.25
LTV	80%
Refinance Assumptions	
Interest Rate	7.00%
Amortization Term (Years)	30
DSCR	1.25
LTV	80%

Source: FannieMae and FreddieMac fixed-rate multifamily mortgage term sheets; lender interviews; DRA.

Table 3
Net Operating Income from Apartments
San Jose ARO Analysis

	Prototype 1	Prototype 2	Prototype 3	Prototype 4	Prototype 5
	Downtown San Jose	West San Jose	Outer North San Jose	South San Jose	East San Jose
Tenure	Rental	Rental	Rental	Rental	Rental
Net Rentable SF of Apartment Space	227,000	513,000	376,400	356,000	168,000
Net Rentable SF of Retail Space	0	8,000	0	0	0
Parking Spaces	0	945	0	0	0
Approximate Building Stories	0	4 & 5 Stories	0	0	0
Total Units	**250**	**600**	**400**	**400**	**200**
Unit Size (Square Feet)					
Studio/Loft	-	-	660	550	550
One Bedroom	780	750	800	750	750
Two Bedroom	1,100	1,100	1,100	1,100	1,050
Three Bedroom	-	-	1,300	1,300	-
Four Bedroom	-	-	-	-	-
Average	*908*	*855*	*941*	*890*	*840*
Monthly Rent Per SF (1)					
Studio/Loft			$3.60	$3.60	$3.95
One Bedroom	$3.33	$3.33	$3.33	$3.00	$3.33
Two Bedroom	$2.80	$2.80	$2.80	$2.60	$2.30
Three Bedroom			$3.00	$2.45	
Four Bedroom					
Total Units					
Average Monthly Rent/Unit	$3.07	$3.13	$3.09	$2.81	$2.88
Monthly Rent Per Unit					
Studio/Loft			$2,376	$1,980	$2,173
One Bedroom	$2,597	$2,498	$2,664	$2,250	$2,498
Two Bedroom	$3,080	$3,080	$3,080	$2,860	$2,415
Three Bedroom			$3,900	$3,185	
Four Bedroom					
Average Monthly Rent/Unit	$2,790	$2,672	$2,904	$2,500	$2,416
Average Monthly Rent Per Square Foot	$3.07	$3.13	$3.09	$2.81	$2.88
Parking Income ($/Space/Month)	$0	$0	$0	$0	$0
Parking Usage Rate	100%	100%	100%	100%	100%
Miscellaneous Income ($/Unit/Year)	$120	$120	$120	$120	$0
Stabilized Rental Vacancy Rate	7.0%	7.0%	7.0%	7.0%	7.0%
Rental Operating Cost/Unit	$12,894	$12,141	$13,362	$8,233	$7,770
Rental Operating Cost/SF (2)	$14.20	$14.20	$14.20	$9.25	$9.25
Retail Income ($/NSF/Year)		$65.00			
Retail Vacancy Rate (% Gross Retail Income)		0%			
Retail Operating Cost ($ Per NSF)		$10			
Total Monthly Gross Rental Income, Apts.	**$697,610**	**$1,603,350**	**$1,161,760**	**$999,800**	**$483,150**
Annual Gross Income	**$8,371,320**	**$19,240,200**	**$13,941,120**	**$11,997,600**	**$5,797,800**
Less: Apartment Vacancy	($585,992)	($1,346,814)	($975,878)	($839,832)	($405,846)
Plus: Retail Income	$0	$520,000	$0	$0	$0
Plus: Parking Income	$0	$0	$0	$0	$0
Plus: Misc. Income	$30,000	$72,000	$48,000	$48,000	$0
Adjusted Annual Gross Income	**$7,815,328**	**$18,485,386**	**$13,013,242**	**$11,205,768**	**$5,391,954**
Operating Costs					
Less: Apartment Operating Costs (2)	($3,223,400)	($7,284,600)	($5,344,880)	($3,293,000)	($1,554,000)
Less: Retail Operating Costs	$0	($80,000)	$0	$0	$0
Net Operating Income	**$4,591,928**	**$11,120,786**	**$7,668,362**	**$7,912,768**	**$3,837,954**

(1) From CoStar for properties built 2015 through 2017. Average by submarket area and unit bedroom count.
(2) Total expenses from Institute of Real Estate Management 2017 Income/Expense Analysis, including property taxes.
Assumes elevator served buildings for Prototypes 1, 2 and 3 and Garden Apartments, High Cost, for Prototypes 4 and 5.
Sources: CoStar; IREM; City of San Jose; DRA.

Table 4
Development Prototypes
San Jose ARO Analysis

	Prototype 1	Prototype 2	Prototype 3	Prototype 4	Prototype 5
Market Subarea:	**Downtown San Jose**	**West San Jose**	**Outer North San Jose**	**South San Jose**	**East San Jose**
Total Housing Unit Count	**250**	**600**	**400**	**400**	**200**
Original ARO Units	**100**	**200**	**200**	**200**	**100**
Other Regulated Units	**0**	**0**	**0**	**0**	**0**
Tenure (Renter/Owner)	Rental	Rental	Rental	Rental	Rental
New Construction or Conversion	New	New	New	New	New
Total Site Area (Acre)		7.68 Acres			
Total Site Area (SF)		334,541			
Density (Units Per Acre)		78			
Construction Type		Type III-A			
Parking Type		1.5 Levels Partially Subt.			
Building Stories		4 & 5 Stories			
Net Residential Square Feet (NRSF)	**227,000 SF**	**513,000 SF**	**376,400 SF**	**356,000 SF**	**168,000 SF**
Net SF Retail	0 SF	8,000 SF			
Other Uses (NSF)	0 SF	0 SF			
Net SF Total	227,000 SF	521,000 SF	376,400 SF	356,000 SF	168,000 SF
Other Uses (NSF)					
Building Efficiency Ratio (%)	78%	78%	571%	571%	80%
Total Gross Building SF (Excl. Pkg.)	291,026	667,949	65,864	62,294	210,000
Unit Bedroom Count Distribution (1)					
Studio/Loft	0%	0%	10%	10%	15%
One Bedroom	60%	70%	45%	50%	45%
Two Bedroom	40%	30%	35%	30%	40%
Three Bedroom	0%	0%	10%	10%	0%
Four Bedroom	0%	0%	0%	0%	0%
Total	100%	100%	100%	100%	100%
Units by BR Count					
Studio/Loft			40	40	30
One Bedroom	150	420	180	200	90
Two Bedroom	100	180	140	120	80
Three Bedroom			40	40	
Four Bedroom					
Total Residential Units	250	600	400	400	200
Unit Size (Net SF) (1)					
Studio/Loft			660 SF	550 SF	550 SF
One Bedroom	780 SF	750 SF	800 SF	750 SF	750 SF
Two Bedroom	1,100 SF	1,100 SF	1,100 SF	1,100 SF	1,050 SF
Three Bedroom			1,300 SF	1,300 SF	
Four Bedroom					
Average Unit Size	*908 SF*	*855 SF*	*941 SF*	*890 SF*	*840 SF*
Underground Parking Spaces		945 Spaces			
Structured Parking Spaces					
Podium Parking Spaces					
Garage Parking Spaces					
Surface/Carport Parking Spaces					
Total Parking Spaces Provided		**945 Spaces**			
Actual Project:		The Reserve			

(1) From CoStar. Average by submarket area.
Sources: CoStar; DRA.

Table 5
Cash Flow Projections
Prototype 1 Downtown San Jose
100% ARO Replacement
San Jose ARO Analysis

Total Housing Units	250
Unregulated Units	112
ARO Units	100
Inclusionary Units	38
Other Regulated Units	0

Escalation Rates		**Cap Rates**		**Financing Assumptions**		**Refinance Assumptions**	
Market Rents (non-ARO)	2.00%	Entry Cap Rate	5.00%	Interest Rate	5.00%	Interest Rate	7.00%
ARO Rents	2.00%	Exit Cap Rate	7.00%	Amortization	30	Amortization	30
Inclusionary Rents	2.00%			DSCR	1.25	DSCR	1.25
Other Restricted Rents	2.00%			LTV	80%	LTV	80%
Laundry/Miscellaneous Income	3.00%						
Retail Income	3.00%						
Operating Costs	3.00%						

Year		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
CASH FLOW																
Revenues																
Gross Potential Rent																
Market-Rate Rental Income		$3,750,351	$3,825,358	$3,901,866	$3,979,903	$4,059,501	$4,140,691	$4,223,505	$4,307,975	$4,394,134	$4,482,017	$4,571,657	$4,663,091	$4,756,352	$4,851,479	$4,948,509
Inclusionary Units		$611,880	$624,118	$636,600	$649,332	$662,319	$675,565	$689,076	$702,858	$716,915	$731,253	$745,878	$760,796	$776,012	$791,532	$807,363
ARO Units		$3,348,528	$3,415,499	$3,483,809	$3,553,485	$3,624,554	$3,697,045	$3,770,986	$3,846,406	$3,923,334	$4,001,801	$4,081,837	$4,163,474	$4,246,743	$4,331,678	$4,418,312
Other Restricted Units		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous		$30,000	$30,900	$31,827	$32,782	$33,765	$34,778	$35,822	$36,896	$38,003	$39,143	$40,317	$41,527	$42,773	$44,056	$45,378
Retail Income		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Apartment Vacancy Allowance	7.00%	($539,753)	($550,548)	($561,559)	($572,790)	($584,246)	($595,931)	($607,850)	($620,007)	($632,407)	($645,055)	($657,956)	($671,115)	($684,538)	($698,228)	($712,193)
Retail Vacancy Allowance	5.00%	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Net Rental Income		$7,201,006	$7,345,326	$7,492,542	$7,642,711	$7,795,893	$7,952,149	$8,111,539	$8,274,128	$8,439,980	$8,609,159	$8,781,734	$8,957,772	$9,137,343	$9,320,517	$9,507,368
Operating Costs		($3,223,400)	($3,320,102)	($3,419,705)	($3,522,296)	($3,627,965)	($3,736,804)	($3,848,908)	($3,964,375)	($4,083,307)	($4,205,806)	($4,331,980)	($4,461,939)	($4,595,798)	($4,733,672)	($4,875,682)
Net Operating Income		$3,977,606	$4,025,224	$4,072,837	$4,120,415	$4,167,928	$4,215,344	$4,262,631	$4,309,753	$4,356,673	$4,403,354	$4,449,754	$4,495,832	$4,541,545	$4,586,846	$4,631,686
Debt Service--First Trust Deed		($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)	($3,182,085)
Debt Coverage Ratio		1.25	1.26	1.28	1.29	1.31	1.32	1.34	1.35	1.37	1.38	1.40	1.41	1.43	1.44	1.46
Net Cash Flow		$795,521	$843,139	$890,752	$938,330	$985,843	$1,033,259	$1,080,546	$1,127,668	$1,174,588	$1,221,269	$1,267,669	$1,313,747	$1,359,460	$1,404,761	$1,449,601

Capitalized Value, Cap Rate of:	5.00%	$79,552,124
MAX. 1ST MORTGAGE BASED ON DSCR		$49,396,994
MAX 1ST MORTGAGE BASED ON LTV		$63,641,699
PROJECT VALUE LESS FIRST MORTGAGE		$30,155,130

REFINANCE TESTS

	Refinance in Year 10	**Refinance in Year 15**
NOI	$4,403,354	$4,631,686
Cap Rate	7.00%	7.00%
Project Value	$62,905,051	$66,166,948
Max Loan Based on LTV	$50,324,040	$52,933,559
Max Loan Based on DSCR	$44,123,824	$46,411,834
Refinance Proceeds	$44,123,824	$46,411,834
Less: Outstanding Debt	$40,180,535	$33,532,611
Cash Out	$3,943,289	$12,879,224

Source: DRA

Table 6
Cash Flow Projections
Prototype 2 West San Jose
100% ARO Replacement
San Jose ARO Analysis

Total Housing Units	600
Unregulated Units	310
ARO Units	200
Inclusionary Units	90
Other Regulated Units	0

Escalation Rates	
Market Rents (non-ARO)	2.00%
ARO Rents	2.00%
Inclusionary Rents	2.00%
Other Restricted Rents	2.00%
Laundry/Miscellaneous Income	3.00%
Retail Income	3.00%
Operating Costs	3.00%

Cap Rates	
Entry Cap Rate	5.00%
Exit Cap Rate	7.00%

Financing Assumptions	
Interest Rate	5.00%
Amortization	30
DSCR	1.25
LTV	80%

Refinance Assumptions	
Interest Rate	7.00%
Amortization	30
DSCR	1.25
LTV	80%

Year		1	2	3	4	5	6	7	8
CASH FLOW									
Revenues									
Gross Potential Rent									
Market-Rate Rental Income		$9,940,770	$10,139,585	$10,342,377	$10,549,225	$10,760,209	$10,975,413	$11,194,922	$11,418,820
Inclusionary Units		$1,431,900	$1,460,538	$1,489,749	$1,519,544	$1,549,935	$1,580,933	$1,612,552	$1,644,803
ARO Units		$6,413,400	$6,541,668	$6,672,501	$6,805,951	$6,942,070	$7,080,912	$7,222,530	$7,366,981
Other Restricted Units		$0	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous		$72,000	$74,160	$76,385	$78,676	$81,037	$83,468	$85,972	$88,551
Retail Income		$520,000	$535,600	$551,668	$568,218	$585,265	$602,823	$620,907	$639,534
Apartment Vacancy Allowance	7.00%	($1,245,025)	($1,269,925)	($1,295,324)	($1,321,230)	($1,347,655)	($1,374,608)	($1,402,100)	($1,430,142)
Retail Vacancy Allowance	5.00%	($26,000)	($26,780)	($27,583)	($28,411)	($29,263)	($30,141)	($31,045)	($31,977)
Net Rental Income		$17,107,045	$17,481,626	$17,837,356	$18,200,384	$18,570,860	$18,948,941	$19,334,782	$19,728,547
Operating Costs		($7,284,600)	($7,503,138)	($7,728,232)	($7,960,079)	($8,198,881)	($8,444,848)	($8,698,193)	($8,959,139)
Net Operating Income		$9,822,445	$9,978,488	$10,109,124	$10,240,305	$10,371,979	$10,504,093	$10,636,589	$10,769,408
Debt Service--First Trust Deed		($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)
Debt Coverage Ratio		1.25	1.27	1.29	1.30	1.32	1.34	1.35	1.37
Net Cash Flow		$1,964,489	$2,120,532	$2,251,168	$2,382,349	$2,514,023	$2,646,137	$2,778,633	$2,911,452

Year	9	10	11	12	13	14	15
CASH FLOW							
Revenues							
Gross Potential Rent							
Market-Rate Rental Income	$11,647,196	$11,880,140	$12,117,743	$12,360,098	$12,607,300	$12,859,446	$13,116,635
Inclusionary Units	$1,677,699	$1,711,253	$1,745,478	$1,780,388	$1,815,995	$1,852,315	$1,889,362
ARO Units	$7,514,320	$7,664,607	$7,817,899	$7,974,257	$8,133,742	$8,296,417	$8,462,345
Other Restricted Units	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous	$91,207	$93,944	$96,762	$99,665	$102,655	$105,734	$108,906
Retail Income	$658,720	$678,482	$698,837	$719,802	$741,396	$763,638	$786,547
Apartment Vacancy Allowance	($1,458,745)	($1,487,920)	($1,517,678)	($1,548,032)	($1,578,993)	($1,610,572)	($1,642,784)
Retail Vacancy Allowance	($32,936)	($33,924)	($34,942)	($35,990)	($37,070)	($38,182)	($39,327)
Net Rental Income	$20,130,399	$20,540,506	$20,959,040	$21,386,177	$21,822,095	$22,266,978	$22,721,011
Operating Costs	($9,227,913)	($9,504,751)	($9,789,893)	($10,083,590)	($10,386,098)	($10,697,681)	($11,018,611)
Net Operating Income	$10,902,485	$11,035,755	$11,169,147	$11,302,587	$11,435,997	$11,569,297	$11,702,400
Debt Service--First Trust Deed	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)	($7,857,956)
Debt Coverage Ratio	1.39	1.40	1.42	1.44	1.46	1.47	1.49
Net Cash Flow	$3,044,529	$3,177,799	$3,311,191	$3,444,631	$3,578,041	$3,711,341	$3,844,444

Capitalized Value, Cap Rate of:	5.00%	$196,448,902
MAX. 1ST MORTGAGE BASED ON DSCR		$121,982,730
MAX 1ST MORTGAGE BASED ON LTV		$157,159,122
PROJECT VALUE LESS FIRST MORTGAGE		$74,466,172

REFINANCE TESTS

	Refinance in Year 10	**Refinance in Year 15**
NOI	$11,035,755	$11,702,400
Cap Rate	7.00%	7.00%
Project Value	$157,653,644	$167,177,139
Max Loan Based on LTV	$126,122,915	$133,741,711
Max Loan Based on DSCR	$110,583,834	$117,263,950
Refinance Proceeds	$110,583,834	$117,263,950
Less: Outstanding Debt	$40,180,535	$33,532,611
Cash Out	$70,403,299	$83,731,339

Source: DRA

Table 7
Cash Flow Projections
Prototype 3 Outer North San Jose
100% ARO Replacement
San Jose ARO Analysis

Total Housing Units	400
Unregulated Units	140
ARO Units	200
Inclusionary Units	60
Other Regulated Units	0

Escalation Rates		**Cap Rates**		**Financing Assumptions**		**Refinance Assumptions**	
Market Rents (non-ARO)	2.00%	Entry Cap Rate	5.00%	Interest Rate	5.00%	Interest Rate	7.00%
ARO Rents	2.00%	Exit Cap Rate	7.00%	Amortization	30	Amortization	30
Inclusionary Rents	2.00%			DSCR	1.25	DSCR	1.25
Other Restricted Rents	2.00%			LTV	80%	LTV	80%
Laundry/Miscellaneous Income	3.00%						
Retail Income	3.00%						
Operating Costs	3.00%						

Year		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
CASH FLOW																
Revenues																
Gross Potential Rent																
Market-Rate Rental Income		$4,879,392	$4,976,980	$5,076,519	$5,178,050	$5,281,611	$5,387,243	$5,494,988	$5,604,888	$5,716,985	$5,831,325	$5,947,952	$6,066,911	$6,188,249	$6,312,014	$6,438,254
Inclusionary Units		$975,144	$994,647	$1,014,540	$1,034,831	$1,055,527	$1,076,638	$1,098,171	$1,120,134	$1,142,537	$1,165,387	$1,188,695	$1,212,469	$1,236,718	$1,261,453	$1,286,682
ARO Units		$6,970,560	$7,109,971	$7,252,171	$7,397,214	$7,545,158	$7,696,061	$7,849,983	$8,006,982	$8,167,122	$8,330,464	$8,497,074	$8,667,015	$8,840,356	$9,017,163	$9,197,506
Other Restricted Units		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous		$48,000	$49,440	$50,923	$52,451	$54,024	$55,645	$57,315	$59,034	$60,805	$62,629	$64,508	$66,443	$68,437	$70,490	$72,604
Retail Income		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Apartment Vacancy Allowance	7.00%	($897,757)	($915,712)	($934,026)	($952,707)	($971,761)	($991,196)	($1,011,020)	($1,031,240)	($1,051,865)	($1,072,902)	($1,094,360)	($1,116,248)	($1,138,573)	($1,161,344)	($1,184,571)
Retail Vacancy Allowance	5.00%	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Net Rental Income		$11,975,339	$12,215,326	$12,460,127	$12,709,839	$12,964,560	$13,224,391	$13,489,436	$13,759,798	$14,035,584	$14,316,904	$14,603,868	$14,896,590	$15,195,187	$15,499,775	$15,810,475
Operating Costs		($5,344,880)	($5,505,226)	($5,670,383)	($5,840,495)	($6,015,710)	($6,196,181)	($6,382,066)	($6,573,528)	($6,770,734)	($6,973,856)	($7,183,072)	($7,398,564)	($7,620,521)	($7,849,136)	($8,084,611)
Net Operating Income		$6,630,459	$6,710,100	$6,789,744	$6,869,344	$6,948,851	$7,028,211	$7,107,370	$7,186,269	$7,264,850	$7,343,048	$7,420,796	$7,498,027	$7,574,666	$7,650,638	$7,725,865
Debt Service--First Trust Deed		($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)	($5,304,367)
Debt Coverage Ratio		1.25	1.27	1.28	1.30	1.31	1.32	1.34	1.35	1.37	1.38	1.40	1.41	1.43	1.44	1.46
Net Cash Flow		$1,326,092	$1,405,732	$1,485,376	$1,564,977	$1,644,483	$1,723,843	$1,803,002	$1,881,902	$1,960,482	$2,038,680	$2,116,429	$2,193,659	$2,270,298	$2,346,271	$2,421,497

Capitalized Value, Cap Rate of:	5.00%	$132,609,186
MAX. 1ST MORTGAGE BASED ON DSCR		$82,342,178
MAX 1ST MORTGAGE BASED ON LTV		$106,087,348
PROJECT VALUE LESS FIRST MORTGAGE		$50,267,007

REFINANCE TESTS

	Refinance in Year 10	**Refinance in Year 15**
NOI	$7,343,048	$7,725,865
Cap Rate	7.00%	7.00%
Project Value	$104,900,679	$110,369,495
Max Loan Based on LTV	$83,920,543	$88,295,596
Max Loan Based on DSCR	$73,581,041	$77,417,061
Refinance Proceeds	$73,581,041	$77,417,061
Less: Outstanding Debt	$40,180,535	$33,532,611
Cash Out	$33,400,506	$43,884,451

Source: DRA

Table 8
Cash Flow Projections
Prototype 4 South San Jose
Scenario 1: 100% ARO Replacement
San Jose ARO Analysis

Total Housing Units	400
Unregulated Units	140
ARO Units	200
Inclusionary Units	60
Other Regulated Units	0

Escalation Rates		**Cap Rates**		**Financing Assumptions**		**Refinance Assumptions**	
Market Rents (non-ARO)	2.00%	Entry Cap Rate	5.00%	Interest Rate	5.00%	Interest Rate	7.00%
ARO Rents	2.00%	Exit Cap Rate	7.00%	Amortization	30	Amortization	30
Inclusionary Rents	2.00%			DSCR	1.25	DSCR	1.25
Other Restricted Rents	2.00%			LTV	80%	LTV	80%
Laundry/Miscellaneous Income	3.00%						
Retail Income	3.00%						
Operating Costs	3.00%						

Year		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
CASH FLOW																
Revenues																
Gross Potential Rent																
Market-Rate Rental Income		$4,199,160	$4,283,143	$4,368,806	$4,456,182	$4,545,306	$4,636,212	$4,728,936	$4,823,515	$4,919,985	$5,018,385	$5,118,753	$5,221,128	$5,325,550	$5,432,061	$5,540,702
Inclusionary Units		$969,492	$988,882	$1,008,659	$1,028,833	$1,049,409	$1,070,398	$1,091,805	$1,113,642	$1,135,914	$1,158,633	$1,181,805	$1,205,441	$1,229,550	$1,254,141	$1,279,224
ARO Units		$5,998,800	$6,118,776	$6,241,152	$6,365,975	$6,493,294	$6,623,160	$6,755,623	$6,890,736	$7,028,550	$7,169,121	$7,312,504	$7,458,754	$7,607,929	$7,760,087	$7,915,289
Other Restricted Units		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous		$48,000	$49,440	$50,923	$52,451	$54,024	$55,645	$57,315	$59,034	$60,805	$62,629	$64,508	$66,443	$68,437	$70,490	$72,604
Retail Income		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Apartment Vacancy Allowance	7.00%	($781,722)	($797,356)	($813,303)	($829,569)	($846,161)	($863,084)	($880,346)	($897,952)	($915,911)	($934,230)	($952,914)	($971,973)	($991,412)	($1,011,240)	($1,031,465)
Retail Vacancy Allowance	5.00%	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Net Rental Income		$10,433,730	$10,642,885	$10,856,237	$11,073,871	$11,295,873	$11,522,331	$11,753,334	$11,988,974	$12,229,343	$12,474,538	$12,724,655	$12,979,794	$13,240,054	$13,505,539	$13,776,355
Operating Costs		($3,293,000)	($3,391,790)	($3,493,544)	($3,598,350)	($3,706,301)	($3,817,490)	($3,932,014)	($4,049,975)	($4,171,474)	($4,296,618)	($4,425,517)	($4,558,282)	($4,695,031)	($4,835,882)	($4,980,958)
Net Operating Income		$7,140,730	$7,251,095	$7,362,693	$7,475,521	$7,589,572	$7,704,841	$7,821,320	$7,938,999	$8,057,869	$8,177,920	$8,299,139	$8,421,511	$8,545,023	$8,669,658	$8,795,397
Debt Service--First Trust Deed		($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)	($5,712,584)
Debt Coverage Ratio		1.25	1.27	1.29	1.31	1.33	1.35	1.37	1.39	1.41	1.43	1.45	1.47	1.50	1.52	1.54
Net Cash Flow		$1,428,146	$1,538,511	$1,650,109	$1,762,937	$1,876,988	$1,992,257	$2,108,735	$2,226,415	$2,345,285	$2,465,336	$2,586,554	$2,708,927	$2,832,439	$2,957,073	$3,082,813

Capitalized Value, Cap Rate of:	5.00%	$142,814,607
MAX. 1ST MORTGAGE BASED ON DSCR		$88,679,120
MAX 1ST MORTGAGE BASED ON LTV		$114,251,686
PROJECT VALUE LESS FIRST MORTGAGE		$54,135,487

REFINANCE TESTS

	Refinance in Year 10	**Refinance in Year 15**
NOI	$8,177,920	$8,795,397
Cap Rate	7.00%	7.00%
Project Value	$116,827,431	$125,648,528
Max Loan Based on LTV	$93,461,945	$100,518,823
Max Loan Based on DSCR	$81,946,886	$88,134,315
Refinance Proceeds	$81,946,886	$88,134,315
Less: Outstanding Debt	$40,180,535	$33,532,611
Cash Out	$41,766,351	$54,601,705

Source: DRA

Table 9
Cash Flow Projections
Prototype 5 East San Jose
100% ARO Replacement
San Jose ARO Analysis

Total Housing Units	200
Unregulated Units	70
ARO Units	100
Inclusionary Units	30
Other Regulated Units	0

Escalation Rates		**Cap Rates**		**Financing Assumptions**		**Refinance Assumptions**	
Market Rents (non-ARO)	2.00%	Entry Cap Rate	5.00%	Interest Rate	5.00%	Interest Rate	7.00%
ARO Rents	2.00%	Exit Cap Rate	7.00%	Amortization	30	Amortization	30
Inclusionary Rents	2.00%			DSCR	1.25	DSCR	1.25
Other Restricted Rents	2.00%			LTV	80%	LTV	80%
Laundry/Miscellaneous Income	3.00%						
Retail Income	3.00%						
Operating Costs	3.00%						

Year		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
CASH FLOW																
Revenues																
Gross Potential Rent																
Market-Rate Rental Income		$2,029,230	$2,069,815	$2,111,211	$2,153,435	$2,196,504	$2,240,434	$2,285,243	$2,330,947	$2,377,566	$2,425,118	$2,473,620	$2,523,092	$2,573,554	$2,625,025	$2,677,526
Inclusionary Units		$474,132	$483,615	$493,287	$503,153	$513,216	$523,480	$533,950	$544,629	$555,521	$566,632	$577,964	$589,524	$601,314	$613,340	$625,607
ARO Units		$2,898,900	$2,956,878	$3,016,016	$3,076,336	$3,137,863	$3,200,620	$3,264,632	$3,329,925	$3,396,523	$3,464,454	$3,533,743	$3,604,418	$3,676,506	$3,750,036	$3,825,037
Other Restricted Units		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Laundry/Miscellaneous		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Retail Income		$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Apartment Vacancy Allowance	7.00%	($378,158)	($385,722)	($393,436)	($401,305)	($409,331)	($417,517)	($425,868)	($434,385)	($443,073)	($451,934)	($460,973)	($470,192)	($479,596)	($489,188)	($498,972)
Retail Vacancy Allowance	5.00%	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Net Rental Income		$5,024,104	$5,124,586	$5,227,077	$5,331,619	$5,438,251	$5,547,016	$5,657,957	$5,771,116	$5,886,538	$6,004,269	$6,124,354	$6,246,841	$6,371,778	$6,499,214	$6,629,198
Operating Costs		($1,554,000)	($1,600,620)	($1,648,639)	($1,698,098)	($1,749,041)	($1,801,512)	($1,855,557)	($1,911,224)	($1,968,561)	($2,027,618)	($2,088,446)	($2,151,099)	($2,215,632)	($2,282,101)	($2,350,564)
Net Operating Income		$3,470,104	$3,523,966	$3,578,439	$3,633,521	$3,689,211	$3,745,504	$3,802,399	$3,859,892	$3,917,977	$3,976,651	$4,035,908	$4,095,742	$4,156,146	$4,217,112	$4,278,634
Debt Service--First Trust Deed		($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)	($2,776,083)
Debt Coverage Ratio		1.25	1.27	1.29	1.31	1.33	1.35	1.37	1.39	1.41	1.43	1.45	1.48	1.50	1.52	1.54
Net Cash Flow		$694,021	$747,883	$802,356	$857,438	$913,128	$969,422	$1,026,317	$1,083,809	$1,141,895	$1,200,568	$1,259,825	$1,319,659	$1,380,063	$1,441,029	$1,502,551

Capitalized Value, Cap Rate of:	5.00%	$69,402,073
MAX. 1ST MORTGAGE BASED ON DSCR		$43,094,435
MAX 1ST MORTGAGE BASED ON LTV		$55,521,659
PROJECT VALUE LESS FIRST MORTGAGE		$26,307,638

REFINANCE TESTS

	Refinance in Year 10	**Refinance in Year 15**
NOI	$3,976,651	$4,278,634
Cap Rate	7.00%	7.00%
Project Value	$56,809,306	$61,123,338
Max Loan Based on LTV	$45,447,445	$48,898,670
Max Loan Based on DSCR	$39,848,054	$42,874,068
Refinance Proceeds	$39,848,054	$42,874,068
Less: Outstanding Debt	$40,180,535	$33,532,611
Cash Out	($332,481)	$9,341,457

Source: DRA