TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

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GOVERNOR

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RE: Appeal of Underwriting Recommendation - Braniff Lofts (24166)

Ms. Krochtengel:

The Department received the above-listed Application on March 1, 2024. The Application proposes the acquisition and rehabilitation of an existing building in Dallas. An appraisal was included with the Application that indicates that the building itself has no value, and instead contributes all value of the existing site to the land value. Because land value is not eligible to be included in the Eligible Basis used to determine the amount of Housing Tax Credits for which the Application is eligible, the Department's Real Estate Analysis Division limited the eligible building acquisition costs to the appraised "as-is" value of the buildings in accordance with §11.302(e)(1)(A):

> "(C) Eligible Basis on Acquisition of Buildings. Building acquisition cost included in Eligible Basis is limited to the appraised value of the buildings, exclusive of land value, as determined by an appraisal that meets the requirements of §11.304 of this chapter (relating to Appraisal Rules and Guidelines). If the acquisition cost in the Site Control documents is less than the appraised value, Underwriter will utilize the land value from the appraisal and adjust the building acquisition cost accordingly."

The property is an existing office building that will be adapted into apartments, therefore §11.304(c)(10)(D) applies, which requires that the appraisal must include the "as-is" value. The appraisal dated February 29, 2024 contributes no value to the buildings, as is noted in various parts of the Appraisal:

> "It is noted, due to the subject's existing improvements and their respective age/condition as of the effective date of this appraisal, the cost approach is not utilized. Instead, the "as is" value is based on the land value, as if vacant." (p. 6)
>
> "The property is pending contract of sale in the amount of $8,000,000. As noted, the subject improvements require significant renovations and currently provide minimal contributory value in their current state. The parties involved appear to be interrelated parties, however an arm's length transaction." (p. 6)
>
> "The subject property is an existing office building, originally built in 1967, that is vacant with significant deferred maintenance." (p. 67)
>
> "As of the date of the inspection, the property comprises of a vacant office building with significant deferred maintenance…The interior of the building has since been demolished, allowing for an immediate redevelopment opportunity." (p. 72)

Value Conclusions

Value Type & Appraisal Premise	Interest Appraised	Date of Value	Value Conclusion
Market Value As Is	Fee Simple	February 21, 2024	$5,230,000
Prospective Market Value As Completed	Fee Simple	January 1, 2026	$4,960,000
Prospective Market Value As Stabilized	Fee Simple	July 1, 2026	$5,100,000
Present Value of Tax Credits		January 1, 2026	$19,160,000

The appraisal states the "as-is" value at the time of Application is $5,230,000, which is entirely attributed to the land value.

> "To develop an opinion of the subject's "as is" value, it is necessary to estimate the land value, as though vacant and available to be developed to its highest and best use. As discussed, the subject improvements are in poor condition with significant deferred maintenance. As such, we have valued the subject's "as is" value conclusion utilizing only land sales" (p. 83)

Land Value Conclusion

Prior to adjustments, the sales reflect a range of $83.02 - $168.22 per square foot. After adjustment, the range is narrowed to $120.00 - $128.27 per square foot, with an average of $124.70 per square foot. To arrive at an indication of value, equal weight is given to all sales.

Based on the preceding analysis, the land value conclusion for the subject is presented as follows:

Land Value Conclusion	
Indicated Value per Square Foot	$125.00
Subject Square Feet	41,841
Indicated Value	$5,230,125
Rounded	$5,230,000

Reconciliation and Conclusion of Value

Reconciliation involves the weighting of alternative value indications, based on the judged reliability and applicability of each approach to value, to arrive at a final value conclusion. Reconciliation is required because different value indications result from the use of multiple approaches and within the application of a single approach. The values indicated by the preceding analyses are as follows:

Summary of Value Indications

	Market Value As Is	Prospective Market Value As Completed	Prospective Market Value As Stabilized
Cost Approach	Not Used	Not Used	Not Used
Sales Comparison Approach	$5,230,000	$5,140,000	$5,280,000
Income Capitalization Approach	Not Used	$4,950,000	$5,090,000
Reconciled	$5,230,000	$4,960,000	$5,100,000

The Application assumes the full sales price of $8,000,000 as building acquisition and $3,686,400 as acquisition to be included in Eligible Basis. The Development Cost Schedule did not attribute any acquisition cost to land value, which does not meet the QAP requirements listed above. Based on the appraisal, the Department underwrote the Application with no eligible building acquisition costs, which decreased Eligible Basis by $3,686,400. This resulted in a $931,772 decrease to equity. The assumed increase in Deferred Developer Fee to fill the gap cannot be repaid within 15 years, leaving a negative $705,306 15-year cash flow. The Application was determined to be financially infeasible per 10 TAC §11.302(i)(2), which states that a Development will be determined to be infeasible if:

> "(2) Deferred Developer Fee. Applicants requesting an allocation of tax credits where the estimated Deferred Developer Fee, based on the underwritten capitalization structure, is not repayable from Cash Flow within the first 15 years of the long term pro forma as described in subsection (d)(5) of this section."

The Applicant timely appealed this determination on July 1, 2024. The appeal states that the appraisal that was submitted with the Application did not represent the building values clearly, and therefore a revised appraisal, dated July 1, 2024, was submitted with the appeal. The appeal letter and untimely-submitted "updated appraisal" are relying on an assumed value of $7,590,000 (inclusive of land value) based on the calculated present value of the assumed future historic tax credits. Historic tax credits are calculated on actual eligible costs incurred and are calculated after the rehab of the property is completed. This is not an "as-is" value as required by the QAP.

Based on the valuation analysis in the accompanying report, and subject to the definitions, assumptions, and limiting conditions expressed in the report, the concluded opinions of value are as follows:

Value Conclusions

Value Type & Appraisal Premise	Interest Appraised	Date of Value	Value Conclusion
Market Value As Is	Fee Simple	February 21, 2024	$5,230,000
Prospective Market Value As Completed	Fee Simple	January 1, 2026	$4,960,000
Prospective Market Value As Stabilized	Fee Simple	July 1, 2026	$5,100,000
Present Value of Low Income Tax Credits		January 1, 2026	$19,160,000
Present Value of Historic Preservation Tax		January 1, 2026	$7,590,000

The appeal letter also states that the original appraisal did not include a separate value for favorable financing of the historic tax credits. Historic tax credits are not considered favorable financing; they are a source of equity like Housing Tax Credits, which also do not contribute to current "as-is" value. Per §11.304(c)(10)(E):

> "(E) For any Development with favorable financing (generally below market debt) that will remain in place and transfer to the new owner, the appraisal must include a separate value for the existing favorable financing with supporting information."

The Application was correctly underwritten using the "as-is" values contained in the QAP-compliant appraisal that was submitted with the Application. The revised appraisal submitted with the timely appeal does not meet the requirements of the QAP. Accordingly, the appeal is denied.

In anticipation that you will want this matter presented to the Department's Governing Board, this appeal has been placed on the agenda for the meeting to be held on July 11, 2024. If you have any questions, please contact Cody Campbell at cody.campbell@tdhca.texas.gov.

Sincerely,

Bobby Wilkinson
Executive Director