Agency Financing for Non-Profits:

Why You Should Consider HUD's 232, And Other Financing Options

Section 1

Capital Markets Update

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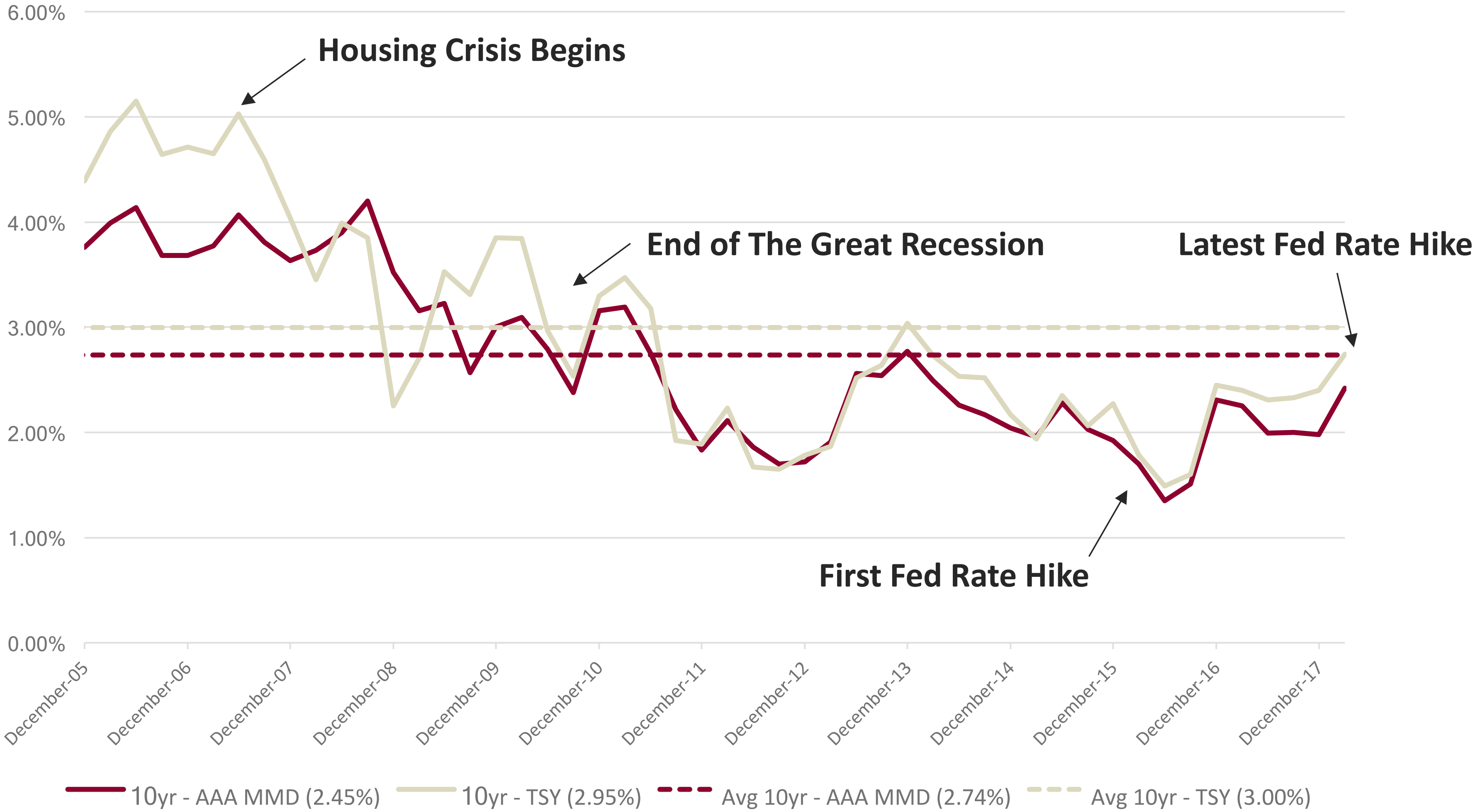
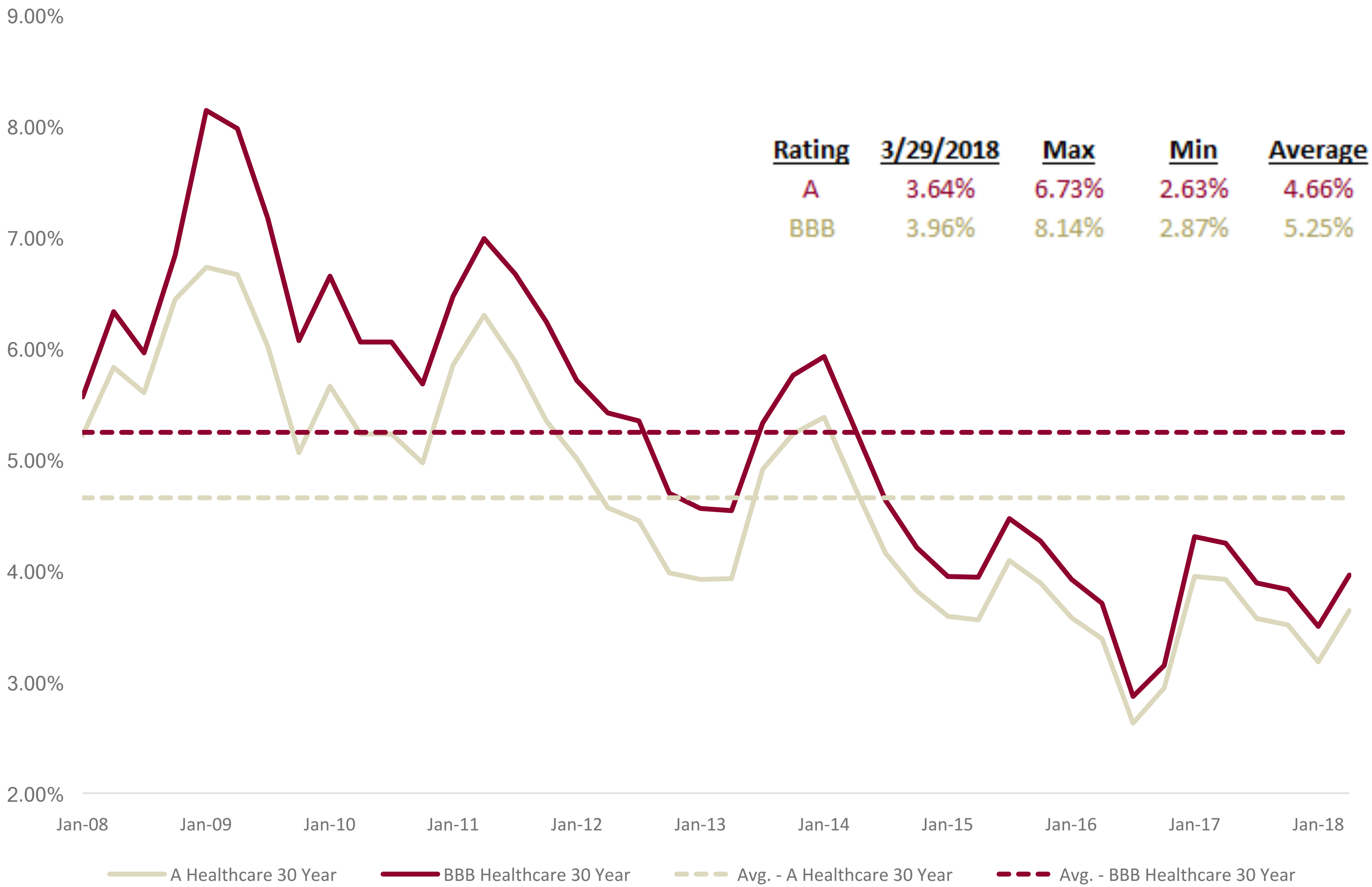
Historical Interest Rates



Sources: Thompson Reuters; Securities Industry & Financial Markets Association Index

Healthcare Yields



Rating	3/29/2018	Max	Min	Average
A	3.64%	6.73%	2.63%	4.66%
BBB	3.96%	8.14%	2.87%	5.25%

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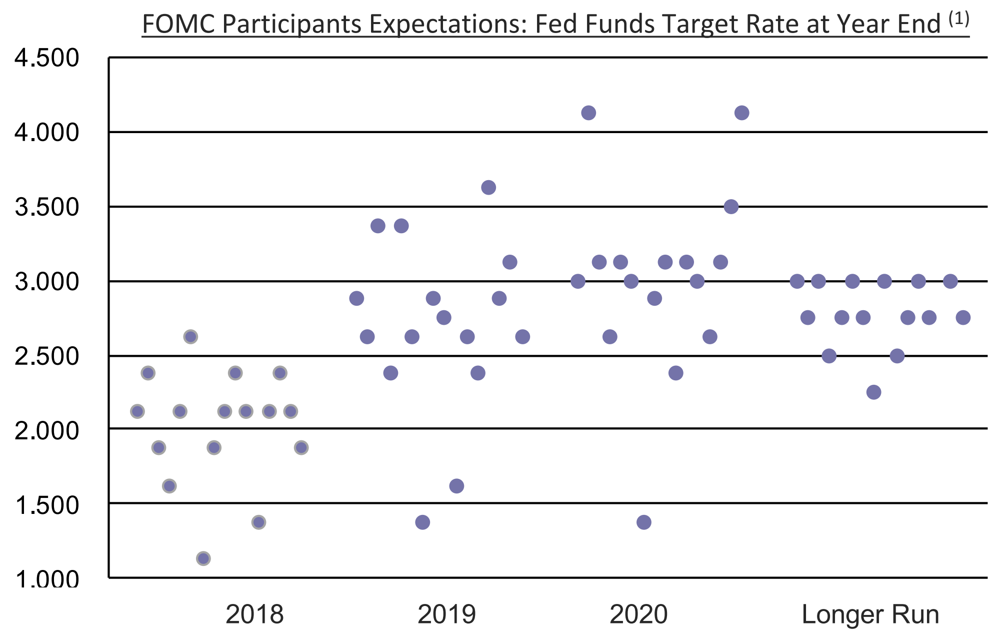
Sources: Municipal Market Monitor (TM3) – Data as of 3/29/2018
Not intended to be viewed as indicative pricing

Interest Rate Forecast



Interest Rate Forecast (2)						
Metric	**1Q2018**	**2Q2018**	**3Q2018**	**4Q2018**	**1Q2019**	**2Q2019**
2YR UST	2.15%	2.30%	2.40%	2.54%	2.65%	2.75%
10YR UST	2.75%	2.87%	3.00%	3.00%	3.15%	3.22%
FFR (Upper Bound)	1.75%	2.00%	2.00%	2.25%	nm	nm
FFR (Lower Bound)	1.50%	1.75%	1.75%	2.00%	nm	nm

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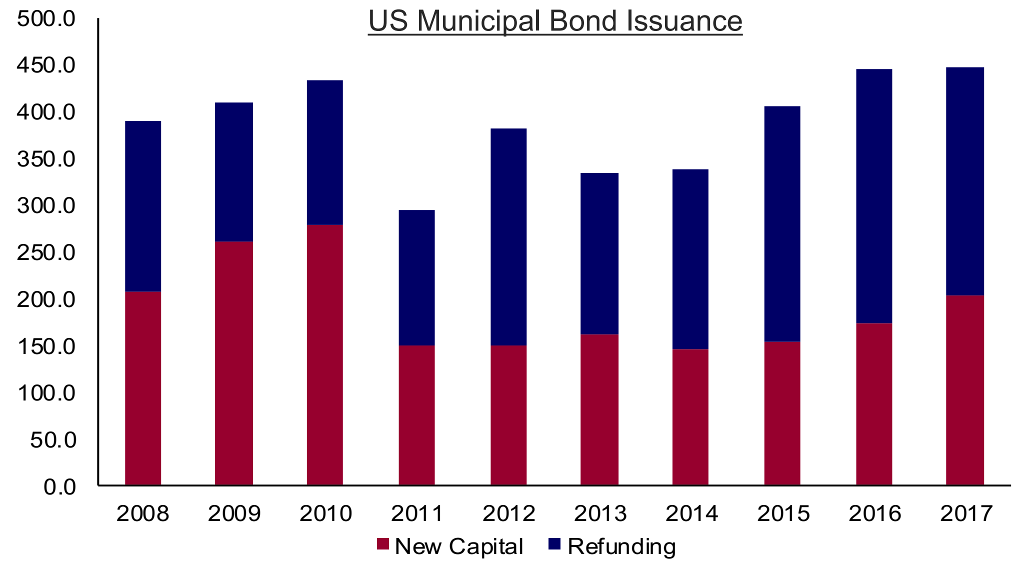
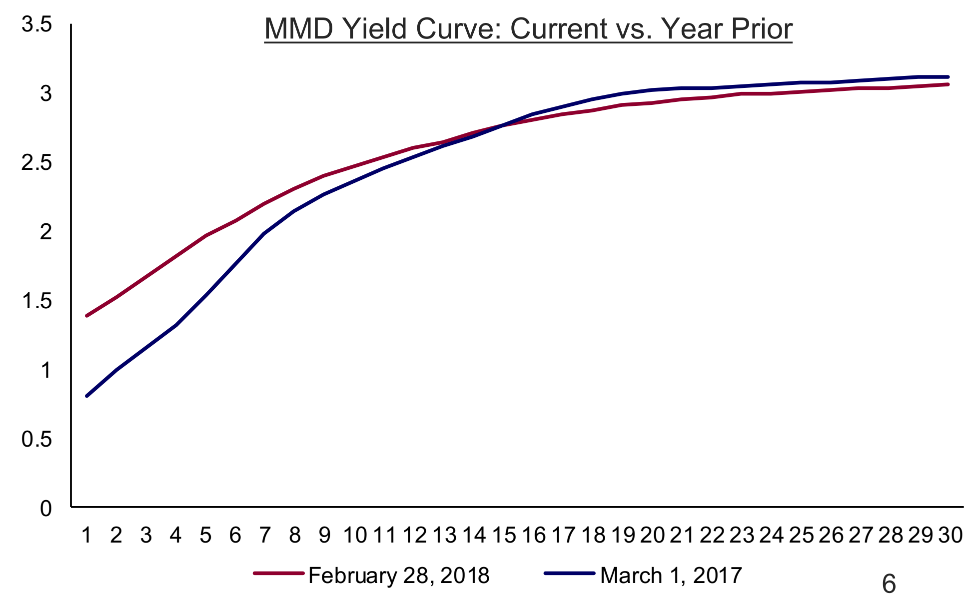
Sources: 1) FOMC December 13, 2017 and 2) Bloomberg composite forecast as of 2/27/2018

Municipal Bond Market

- Private Placements continue to grow in popularity
- Refundings outpacing new construction
- Public issuance in 2017 exceeded 2016 slightly
- Current Muni/Treasury ratio is 88%
- Yield curve continues to flatten





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Sources: 1) SIFMA Municipal Bond Issuance through 2/28/18; 2) TM3 data as of 3/1/2018

Section 3

Sources of Capital - Housing

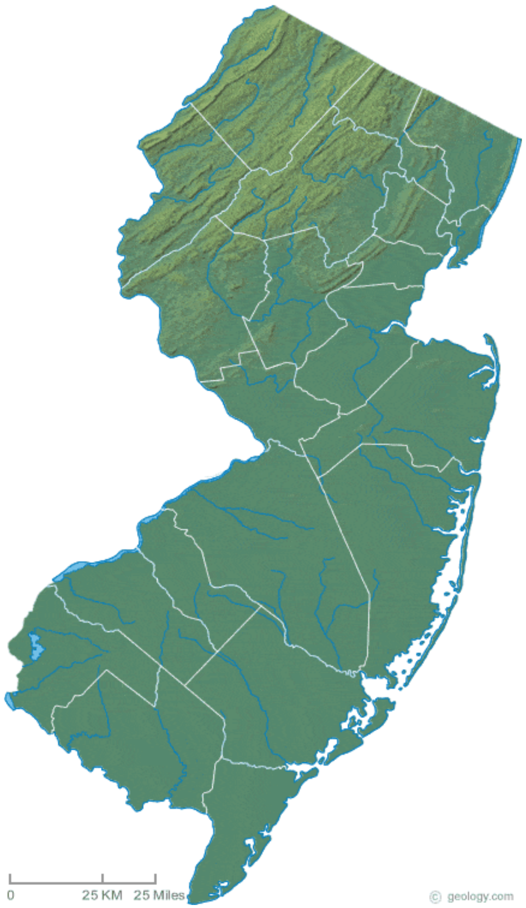
Senior Housing Overview

- **Key Challenges**
  - **Aging Population**
    - 832,198 65+ Population
    - 425,688 75+ Population
    - 212,971 85+Population

    Total # of Senior in 2017: 1,470,857
    16.2% of NJ is over 65+

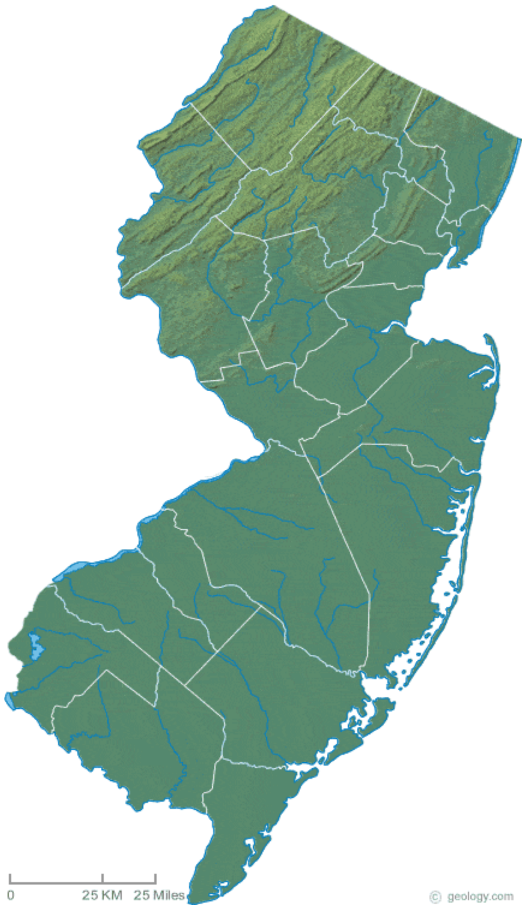
  - **Demand is Projected to Increase**
    - The 65+ Population will grow 15.7% to 962,945
    - The 75+ Population will grow 21.5% to 517,292
    - The 85+ Population will grow 2.5% to 218,354

    Total # of Senior in 2022: 1,698,591
    18.7% of NJ will be over 65+



Senior Housing Overview

- **Key Challenges**
  - **Properties Are Also Aging While Costs Are Rising**
    - Deferred maintenance
    - Energy efficiency retrofits
    - Accessibility requirements
    - Seismic repairs
    - Obsolete design
    - Supportive services



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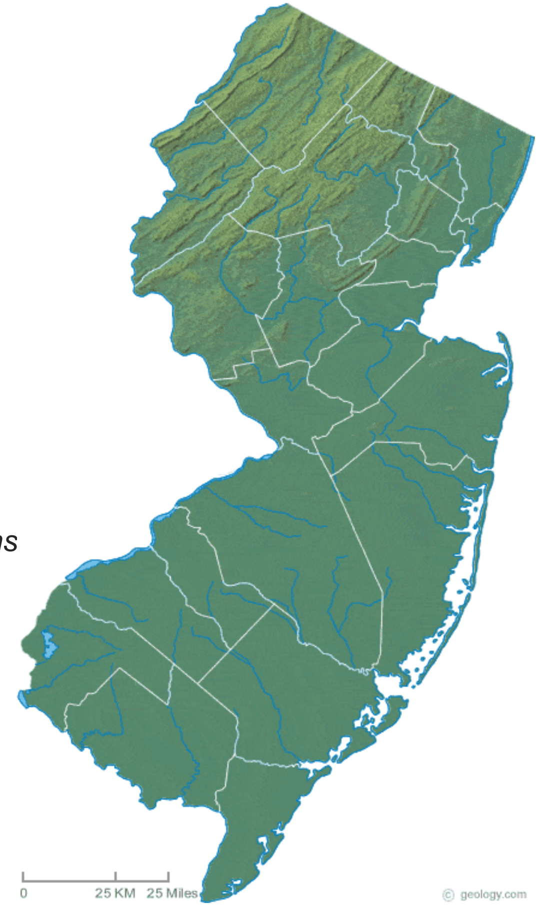
Senior Housing Overview

- **Limited Capital for Projects**
  - **HUD**
    - Rental Assistance
    - Subsidy Assistance
    - HOME / CDBG
    - Services Coordinator Grant Program
    - FHA Mortgage Insurance
  - **Fannie Mae**
    - Affordable Housing Preservation
    - Healthy Housing/Enhanced Resident Services
    - Green Preservation Plus
  - **USDA**
    - *https://www.rd.usda.gov/programs-services/programs communities-nonprofits*



Most likely, multiple funding sources will be leveraged-- federal, state, local and private investment will need to collaborate.

FHA – 202 Program

- Benefits
  - Recapitalize the Property to maintain affordability
  - Often completed to address repairs or deferred maintenance
  - Stable Cash Flows
  - Developer Fee (15% of refinance costs including repairs)
  - Reduce the interest rate
  - Long term & amortization (up to 35 years)
  - Client can borrow 100% of the cost to refinance
  - Recast annual deposit to replacement reserves
- Considerations
  - HAP Contract Considerations (20 Year Extension)
  - Third Party Report Costs (Appraisal, PCNA, Environmental, ALTA, etc.)
  - If repairs exceed 15k/unit, a General Contractor and Architect are required
  - Max repairs are ~40k/unit for a HUD 223(f)
  - HUD Application Fee .30%
  - Prepayment Penalty schedule reset (typically 10,9,8,7,6….1)
  - Refundable Repair Escrow Contingency (10% of Non Critical Repairs)
  - Can be funded with deferred developer fee

FHA – MAP Program

- **Attractive Low Cost Financing**
- **Customized Loan Structuring to Meet Client Needs**
    - Standard or Structured Loan Programs
    - Long Term Fixed Rate
- **Supplemental Loans**
- **Non-Recourse Financing**
- **Cash-out of Equity**

Section 2

Sources of Capital - Healthcare

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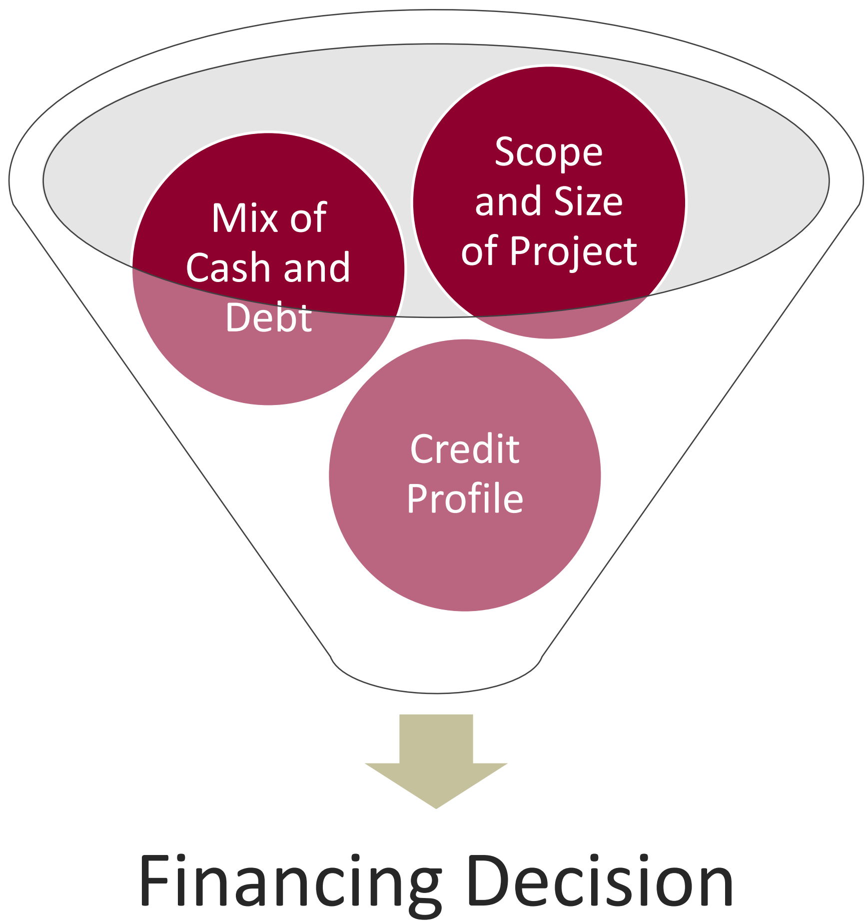
Financing Decisions

There are various options to finance progress within a community, but the decision on which path to pursue is based on several criterion.



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Decision-making Criteria

Scope and Size of Project

- Where are opportunities to improve?
- What are the demand expectations for improvements?
- What is competition doing?

Mix of Cash and Debt

- How much cash or endowment should be invested?
- What is cost of capital at different mixes?

Credit Profile

- How does the financing structure impact credit profile – both current and future?
- What collateral can be offered?
- What is current liquidity position?
- What is maximum affordable debt amount?

Traditional Financing Options

Criteria	Public Offering	Bank Execution
Rate Type	Fixed	Fixed and/or Floating
Term & Amortization	Commonly 30 year term and amortization	Commonly 5-10 year term with a 20-25 year amortization
Prepayment Penalty/ Lockout Period	Yes	Negotiated
Debt Service Reserve	Yes	No
Financing Timeline (days)	60 - 120	60 - 90
Transaction Costs	2% - 3%	1% - 2%
Ratings Agency	Commonly Yes	No

Bank Qualification ("BQ"):

- Both structures are feasible with or without BQ status.
- State-wide issuers allow opportunity to avoid local-issues related to $10 million cap.
- BQ value generally limited on larger bond issues

Structure Comparison

Issue	Public Offering	Private Placement
Guarantor	▪ Limited market for projects not guaranteed by a Parent organization. ▪ May structure a guarantee burn-off	▪ Generally required by Commercial Banks.
Construction Draw-Down	▪ Not available. ▪ As a result, projects must fully fund project at closing, resulting in negative arbitrage.	▪ Standard with Commercial Banks. ▪ Only pay interest on funds drawn for construction.
Loan-to-Value Constraints	▪ Not applicable.	▪ Commercial banks are required to have MAI appraisals completed for projects. ▪ As of March 2018, commercial banks are generally seeking loan-to-values at or below 75% for new construction.
Ongoing Covenants	▪ Generally require Debt Service Coverage and Days Cash on Hand. ▪ Ongoing (quarterly) <u>public</u> disclosure to Bond Trustee	▪ Generally require Debt Service Coverage and Days Cash on Hand. ▪ Ongoing (quarterly) <u>private</u> disclosure to Commercial Bank

Agency-Backed Financing for Projects

Alternative structures are becoming more popular to unlock value and improve an organization's overall credit profile

FHA/HUD Insured Debt

- Non-recourse
- Long-term low fixed rates
- Matching term and amortization
- Restrictions on number of IL units

Fannie Mae Insured Debt

- Non-recourse
- Long-term, low fixed or variable rates
- Balloon Structure
- Restrictions on number of SNF beds

USDA Insured Debt

- Non-recourse
- Long-term low fixed rates
- Matching term and amortization
- Rural eligibility requirements

FHA Section 232 Healthcare Facilities Program

Eligible Projects	• Skilled nursing ,assisted living and memory care (with de minimis independent living)
Uses	• New construction, renovation, refinance, acquisitions • New options for cash out
Non-Recourse	• Except for standard carve-outs for fraud and other "bad acts"
Loan Sizing	• Key Criteria: ▪ Maximum 80% Loan-to-Value* ▪ Non-profit adjustments
Loan Terms	• Up to 35 years for refinance or acquisition • 40 years for New Construction
Interest Rate Options	• Fixed only (taxable)
Timing	• Typically about 6 months
Other	• Loans are assumable, subject to lender review and approval • Supplemental loans available • No typical "bank like" loan covenants for standard loans • Entity structure considerations • Fully amortizing – no interest rate or refinance risk and no costs associated with regular refinancing

FHA Section 232 Healthcare Facilities Program (cont.)

The Federal Housing Administration, generally known as "FHA", provides mortgage insurance on loans made by FHA-approved lenders throughout the United States. Below is a brief summary of possible restrictions for possible FHA borrowers:

Facility Type	Potential Restrictions/Issues	Solutions
CCRC Campus	▪ Limited to 25% IL units ▪ Type A entry fee projects are restricted	▪ Waiver up to 30% ▪ Type C projects are typically approved (though IL needs to be financed separately)
Skilled Nursing	▪ *Non-Profit* – Expenses are higher due to quality of care focus and quantity of staffing relative to for-profit entities ▪ Heavy Medicaid payor mix facilities may require a debt service reserve	▪ FHA underwriting allows for market adjustments to expenses to determine appraised value ▪ DSRs may be funded with a letter of credit rather than cash
Assisted Living and Memory Care	▪ New construction development of facilities requires Davis Bacon wages	▪ Any increased costs are reimbursable through mortgage proceeds ▪ If project is already FHA-insured, a 241 loan is not subject to Davis Bacon wages unless prior campus construction was subject to them
Independent Living	▪ HUD 232 program does not fund stand alone IL senior living projects	▪ HUD does fund these via its traditional Housing program ▪ If campus is already FHA-insured, a 241 can fund IL units up to 30% of total units/beds

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FHA Section 232 – Post Closing

Servicing	• The new HUD loan will be serviced by the lender, or in some cases a third party servicing company.
Reporting Requirements	• Quarterly financials (internally prepared) are submitted to servicer • Annual audit for the borrowing entity is required and submitted to servicer • There are no public reporting requirements
Capital Needs Draws	• When facility repairs or updates are needed, the Asset Management group within the servicing firm will review and approve draws (with occasional HUD input)
Financial Covenants	• Once the loan is closed, there are no financial covenants associated with the HUD loan • The servicing firm will monitor performance and may ask for corrective action if needed (i.e. below 1.00 debt service coverage, facility becomes special focus, etc.)

FHA Section 232 – Not-For-Profit Considerations

Long Term Nature	• As most not-for-profit organizations plan well into the future, the long term financing of a FHA loan can be very appealing
Low Interest Rate	• Since the debt is guaranteed by the U.S. Department of Housing and Urban Development, the pricing is extremely advantageous and removes risk premiums often paid in other financing structures.
Non-Recourse	• A lack of recourse or parental guaranty allows facilities to be pulled out of an obligated group freeing up the parent organization to finance other needs.
Replacement Reserves	• A Capital Needs Assessment will guide a reserve schedule that is put in place at the onset of the new financing. This active account will be partially funded upfront and continuously funded throughout the life of the loan. • This is a dynamic account meant to be used regularly for capital projects and improvements. • Allows for easier budgeting process related to facility updates and improvements.
Leverage	• While 80% is standard, in some instances HUD will allow not-for-profit borrowers to borrow up to 85% of the value of the facility. However, certain restrictions are applicable in the case of higher leverage loans.

Fannie Mae Senior Housing

Eligible Projects	• Independent Living, assisted living, memory care and any combination thereof
Uses	• Refinance, cash out, acquisition, partner buyout, moderate rehab
Non-Recourse	• Except for standard carve-outs for fraud and other “bad acts”
Loan Sizing	• Underwritten Debt Service Coverage ▪ Minimum 1.30x for independent living, 1.40x for assisted living and 1.45x for memory care fixed rate loans ▪ Maximum 75% Loan-to-Value (80% for tax exempt loans)
Loan Terms	• Minimum of 5 years and up to 30 years fully amortizing; Interest only considered on a case-by-case basis
Interest Rate Options	• Fixed and floating rate options available
Timing	• Typically close within 60 days of loan application
Other	• Cash out loans permitted • Loans are assumable, subject to lender review and approval • Supplemental loans available after 12 months from loan closing • Structured loan programs, such as the Structured ARM and Master Credit Facility Programs, are available for large loans or crossed loan pools • No typical “bank like” loan covenants for standard loans

Fannie Mae Senior Housing (Cont.)

- **Attractive Low Cost Financing**

- **Speed and Certainty of Execution**
    - Delegated model
    - Loans typically close within 60 days of executed loan application

- **Customized Loan Structuring to Meet Client Needs**
    - Standard or Structured Loan Programs
    - Fixed and Floating Rate options, including combination thereof available
    - Speed to rate lock to help minimize interest rate uncertainty

- **Supplemental Loans**

- **Non-Recourse Financing**

- **Cash-out of Equity**

USDA Community Facilities (CF) Program

Certain rural projects qualify for USDA financing through the CF program.

USDA seeks to partner with eligible capital providers to finance non-profit organizations in rural communities. A portion of the financing is provided by a lender in the form of a 90% guaranteed loan while the other portion is a direct loan from the USDA.

Criteria	Terms
Rates	- **Guaranteed**: fixed or variable (quarterly resets) - **Direct**: 3.875% fixed (as of 4/1/2018)
Term	Up to 40 years
Loan Guarantee	Up to 90% of P&I to investors; financing is totally non-recourse to the borrower
Core Requirements	- Population of less than 20,000 - Half of financing must be 'new money' - Non-Profit entities only
Restriction	Does not fund new construction, so BANs or a bank loan may be used to fund actual construction
Prepayment	No prepayment penalties on direct debt

Section 4

Credit Analysis

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HUD 232 Underwriting Criteria

HUD will tend to be conservative in the underwriting process due to the fact the financing is long term with no financial covenants.

Criteria	Terms
Loan-To-Value*	80% of HUD-approved appraised value
Term	Up to 35 years for refinance Up to 40 years for new construction
Debt Service Coverage	Minimum 1.45x underwritten debt service coverage ratio
Guaranty	Non-recourse except standard “bad-boy” carveouts
Assumable	Loans are assumable with lender review and approval.
Prepayment	Typically 10 year prepayment penalty stepping down one percent each year from 10% - 1% (customizable).

Section 5

Sample Deals

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FHA Section 232 – Example 1

Facility	• New Jersey non-profit with assisted living, memory care and skilled nursing units.
In-Place Debt	• NJ EDA tax-exempt bonds • Interest rate 5.25%+ • $2.1 million annual debt service • Debt service coverage and days cash on hand covenants • Approached the end of 10-year lockout period
HUD Refinance Details	• Secured HUD-insured mortgage to refinance outstanding debt • 35 year fully amortizing loan with attractive fixed rate just over 3.50% • Separated several parcels to remove mortgage encumbrance
HUD Benefits	• Reduced annual debt service by more than $750,000 • Provided stable, long-term financing • Improved capital structure to allow more flexibility for parent organization

FHA Section 232 – Example 2

Facility	• Rhode Island non-profit with assisted living, memory care and skilled nursing units.
In-Place Debt	• RI Health Facility tax-exempt bonds • Interest rate 8.25%+ • $3.7 million annual debt service • Debt service coverage and days cash on hand covenants • Four years until lockout period ends
HUD Refinance Details	• Secured HUD-insured mortgage to refinance outstanding debt • Proceeds used to advance refund bonds since not callable at time of closing • 35 year fully amortizing loan with attractive fixed rate under 3.25%
HUD Benefits	• Reduced annual debt service by more than $1.1 million • Provided stable, long-term financing • Bond reserves used to pay down outstanding debt

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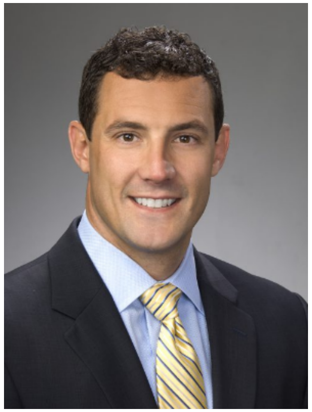

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