

Rehabilitation of vacant property at 1179 East Seventh Street, St. Paul for commercial or mixed-use

Goals: (1) Estimate development costs and potential sources of funds for a community center/church tenant of 3,000 to 3,500 square feet and either commercial or housing use for the rest of the building

(2) Identify next steps and timeline if owner decides to pursue the rehabilitation

The Building

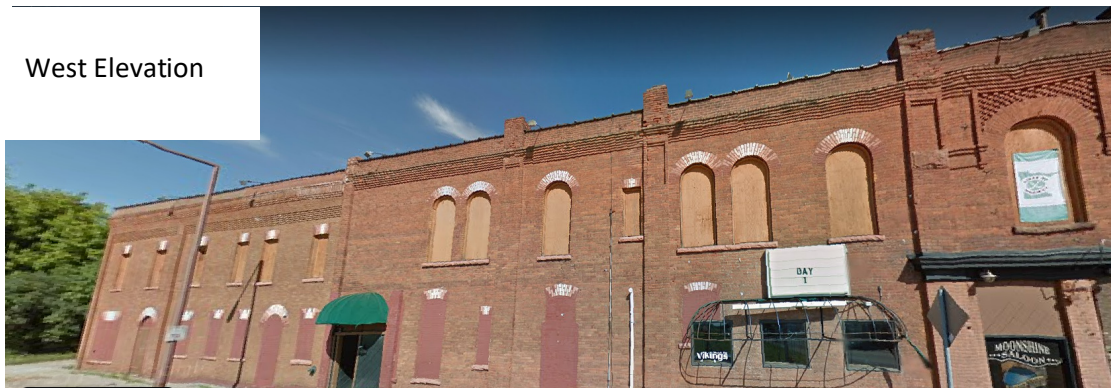
- Two-story brick and masonry building built in 1890 with commercial on the first floor and apartments above, occupied most recently (until 2013) as a bar.
- In the Dayton's Bluff neighborhood, one mile north and east of downtown St. Paul.
- The City of St. Paul is considering demolition of the building if no development plan is supplied. Full code compliance is required.
- The City of St. Paul Historic Preservation Commission has written a report deeming the property worthy of designation; the State Historic Preservation Office concurs.
- The building contains 3,900 square feet on each level plus full basement, on a lot of 4,661 square feet (.11 acre), with 14 surface parking spaces.



The Report

<i>Options Explored</i>	<i>1</i>
<i>Development Issues</i>	<i>2</i>
<i>Development Costs</i>	<i>2</i>
<i>Revenue</i>	<i>3</i>
<i>Funding Sources</i>	<i>5</i>
<i>Timelines</i>	<i>6</i>

West Elevation



Options Explored

The current owner will transfer the building to a new nonprofit corporation, The Emem Community Center, who will become the major tenant of 3,000 to 3,500 square feet. Options explored for the remainder of the space included the following uses.

<i>Use</i>	<i>Recommendation</i>
<ul style="list-style-type: none"> First floor restaurant to utilize the existing vent hood and other salvageable equipment; community center on second floor with elevator. 	Location is surrounded by residential and low-density commercial uses and is off the main route to Metropolitan State University. With a very limited local market, a strong destination restaurant would be required. In addition, local community development lenders have recently expressed concern about their restaurant exposure so potential loans for tenant improvements would likely be difficult to obtain.
<ul style="list-style-type: none"> Community center use and minimally rehabilitation of either floor for light manufacturing or other production use. 	Difficult to find credit worthy tenants when there is ample similar space, often with loading docks and other industrial amenities. Rent for warehouse/industrial spaces in this market are only \$4 to \$6 per square foot, inadequate to carry enough of the building rehabilitation costs, including an elevator that would be required for either second floor use. Property taxes would also be due on for profit tenant space.
<ul style="list-style-type: none"> First floor community center with one office tenant and second floor office space 	Even if the office space was on the first floor, demand for Class B/C space, particularly on a second floor, is not strong regionally or in this neighborhood and lenders will require a credit worthy tenant with a multi-year lease. This option is presented as a net lease option.
<ul style="list-style-type: none"> First floor community center and office tenant and family housing upstairs 	The second floor could accommodate 4 two-bedroom units or 3 three or (small) four-bedroom units and a financial analysis was done. Although the need for affordable family housing is immense and subsidies are available, outdoor play space is limited and the immediate area has moderately high traffic and adjoins commercial uses, making it a relatively undesirable environment for the number of children who would be in occupancy in subsidized housing.
<ul style="list-style-type: none"> First floor community center with one office tenant and one accessible apartment and SRO housing upstairs 	The second floor can accommodate 9 SRO (single-room occupancy) units containing approximately 215 square feet each with a small kitchenette with sink and shared bath and shower facilities. This is the housing option analyzed in this report. Based on owner feedback, there is preference for six or seven studio units with their own baths; very preliminary analysis indicated that the studio unit option would produce similar net operating income as the SRO option; higher rents, even with higher operating expenses, would defray the additional construction cost. Further work will be done on this option. SRO option. An accessible unit could be included on the first floor to eliminate the need for an elevator.

Development Issues

Zoning	Property is zoned T2-Traditional Neighborhood. Commercial and multifamily housing are permitted. Rooming house use requires a conditional use permit, which entails an application and public hearing at the City Planning Commission. The FAR (floor area ratio) of 1.67 is within the permitted ratio for rooming house use.
Neighborhood and District Council Approval	Vacant, the building is an eyesore, so a substantial rehabilitation should be able to get approval from the adjacent property owners and from the District Council. There is a recognized need for affordable housing. A strong commitment to tenant selection and property management standards will be required.
Historic Designation	A 2019 report by the St. Paul Preservation Commission staff indicates the building is historic and supports the historic fabric of the neighborhood. The SHPO office encouraged preservation.
Prevailing Wage Requirement	The City of St. Paul and the State of Minnesota now impose the federal requirement for prevailing wages.
Public bid, Section 3 and Vendor Rules	Public funding requires meeting St. Paul requirements for bidding, vendor selection and employment.
Sales Tax Refund	Contractors working on nonprofit construction projects must retain material receipts to submit to MN Revenue for refund of sales taxes paid. Refunds are paid twice yearly, so a bridge loan is required.

Development Costs

Construction costs are estimated by the owner's architect and general contractor, Kroll & Associates. The column marked public includes the prevailing wage rates from the May 1, 2020 schedule. The commercial option assumes the community center and two nonprofit office tenants. The housing option assumes 10 units – 9 SRO units and 1 one-bedroom.

	Community Center/ Office Space		Community Center / SRO Housing	
	private	public	private	public
Purchase	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Construction	\$ 732,909	\$ 951,538	\$ 725,861	\$ 952,408
Contingency-15%	\$ 109,032	\$ 109,032	\$ 107,982	\$ 140,287
Architect & Engineering	\$ 28,320	\$ 28,320	\$ 36,341	\$ 36,341
Other Soft Costs	\$ 26,003	\$ 38,404	\$ 26,003	\$ 38,403
Financing Fees	\$ 33,728	\$ 33,728	\$ 32,319	\$ 32,319
Operating Reserve	\$ 25,000	\$ 25,000	\$ 25,000	\$ 25,000
Total Development Cost	\$ 1,154,992	\$ 1,386,022	\$ 1,153,506	\$ 1,424,758

Per Gross Leasable Square Foot: \$ 148 \$ 178

Per Housing Unit (9 SRO +1 apt.) \$ 144,125 \$ 169,359

Notes on Development Costs

Construction	with sales tax, permit, P&P bond with public option
Contingency-15%	recommended for historic properties
Architect	4.5%
Other Soft Costs	Historic Preservation, Development consultants, legal (some pro bono), fees
Financing Fees	Origination, appraisal, survey, title, construction interest

Revenue and Funding Sources

Commercial

Pro forma income is net rent: tenants pay their own utilities, trash removal, groundskeeping and repairs to the interior of their space. The owner pays for exterior repairs.

The all-commercial option can support a mortgage of \$ 669,630 at 6% interest with a 25-year amortization. The LISC mini-perm loan would have a balloon payment to be refinanced within 6 years, with a lower interest rate and a lower payment or equity to use for other purposes.

			Year		1	2	3	4	5	6
	square feet	Annual rate	increase							
1st floor-community center	2,700	\$	10.00	2%	27,000	27,540	28,091	28,653	29,226	29,810
1st floor - commercial tenant	500	\$	10.00	2%	5,000	5,100	5,202	5,306	5,412	5,520
2nd floor commercial tenant	3,900	\$	10.00	2%	39,000	39,780	40,576	41,387	42,215	43,059
10% vacancy -(commercial tenants only)					(4,400)	(3,978)	(4,058)	(4,139)	(4,221)	(4,306)
Total Commercial Income					66,600	63,342	64,609	65,901	67,219	68,563
Total Commercial Expenses (20% increase yr 2, 3% thereafter)					4,500	4,890	5,343	5,870	6,487	7,210
Net Operating Income					62,100	58,452	59,266	60,031	60,732	61,353
Mortgage Payment -6%, 25-year amortization					51,750	51,750	51,750	51,750	51,750	51,750
Neighborhood Star Loan-3%, 20-year amortization					3,328	3,328	3,328	3,328	3,328	3,328
City of St. Paul 2% business loan program					1,272	1,272	1,272	1,272	1,272	1,272
Cash Flow to Owner					5,751	2,103	2,917	3,682	4,383	5,004

Housing

Rents for the SRO units are projected at \$525 per month, affordable at 30% of the median for one person - \$21,000 per year or \$10 per hour for full-time work. The one-bedroom unit at \$ 900 is affordable at the 50% of median income level These rents include all utilities. Tenant selection criteria will include adequate income and credit; background checks will be conducted.

The operating expenses assume professional property management and daily cleaning of the shared toilet and shower rooms. Utility cost (gas heat, electricity, water & sewer and trash) are based on the St. Paul Public Housing Authority schedule. Each SRO unit includes a kitchenette with a sink, countertop, upper and lower cabinets and a refrigerator.

Housing revenue as projected will support a mortgage of \$ 306,940 at 6% interest, 25-year amortization.

For both housing and commercial uses, the projections include common standards for vacancy rates, income and expense increases and debt service coverage ratios.

Minnesota requires nonprofit-owned housing to pay property tax, but at a 25% reduced rate. Property tax estimate is based a housing market value of \$600,000, using the Ramsey County Tax Calculator.

		Year:	1	2	3	4	5	6
	Rent	# units	increase					
SRO Units	\$ 525.00	9	56,700	57,834	58,991	60,170	61,374	62,601
One bedroom	\$ 900.00	1	10,800	11,016	11,236	11,461	11,690	11,924
Vacancy @ 5%			(3,375)	(3,443)	(3,511)	(3,582)	(3,653)	(3,726)
Total Housing Income			64,125	65,408	66,716	68,050	69,411	70,799
Total Housing Expenses			35,647	36,685	37,752	38,852	39,983	41,148
Net Operating Income			28,478	28,723	28,963	29,198	29,428	29,651
Mortgage Payment - 6%, 25-year amortization			23,731	23,731	23,731	23,731	23,731	23,731
Cash Flow to Owner			4,746	4,991	5,232	5,467	5,696	5,920
Debt Service Coverage Ratio			1.20	1.21	1.22	1.23	1.24	1.25

Combined Commercial and Housing

First floor commercial with housing above generates a mortgage of \$ 622,204 at 6%, 25-year amortization.

	Rent	Year:		1	2	3	4	5	6	7
		# units	increase							
SRO Units	\$ 525.00	9	2%	56,700	57,834	58,991	60,170	61,374	62,601	63,853
One bedroom	\$ 900.00	1	2%	10,800	11,016	11,236	11,461	11,690	11,924	12,163
Vacancy @ 5%				(3,375)	(3,443)	(3,511)	(3,582)	(3,653)	(3,726)	(3,801)
Total Housing Income				64,125	65,408	66,716	68,050	69,411	70,799	72,215
1st floor-community center	2,700	\$ 10.00	2%	27,000	27,540	28,091	28,653	29,226	29,810	30,406
1st floor - commercial tenant	500	\$ 10.00	2%	5,000	5,100	5,202	5,306	5,412	5,520	5,631
10% vacancy -(commercial tenants only)				(500)	(510)	(520)	(531)	(541)	(552)	(563)
Total Commercial Income				95,625	97,538	99,488	101,478	103,508	105,578	107,689
Total Expenses				37,897	39,002	40,139	41,310	42,516	43,756	45,034
Net Operating Income				57,728	58,535	59,349	60,168	60,992	61,821	62,656
Mortgage Payment - 6%, 25-year amortization				48,106	48,106	48,106	48,106	48,106	48,106	48,106
Cash Flow				9,621	10,429	11,242	12,061	12,886	13,715	21,155
Debt Service Coverage				1.20	1.22	1.23	1.25	1.27	1.29	1.51
First Loan Balance at Year 6:									546,655	
New Loan payment -4.5%, 20-year term										41,501

With the public loans, the first-year cash flow would look like this:

Total Net Operating Income	57,728
Suppoorts 6% interest, 25 year loan of	622,204
First Mortgage Payment	48,106
Neighborhood STAR loan-of taken	3,328
St. Paul 2% loan - if taken	1,272
Total Debt Service	52,706

Refinance at year 7 is conservative, if the property is operating well, the refinance could be earlier. The model shows refinancing only first loan balance, without refinancing costs.

Funding Sources

Potential funding sources are listed as **Probable** or **Possible**

All Commercial			Requirements & Notes
	private	public	
Owner Equity	\$ 50,000	\$ 50,000	3 full time jobs highly competitive National Register nomination small projects difficult,discounted highly competitive participation with LISC loan appraised value must support
NENDC CDBG Grant		100,000	
State Legacy Grant		100,000	
18% historic credits-MN	150,464	150,464	
Discount Federal Credits	115,000	115,000	
Neighborhood STAR		100,000	
2% loan	25,000	25,000	
LISC mini-perm Loan	669,330	669,330	
Total Sources	1,009,794	1,309,794	
Total Uses	\$ 1,154,992	\$ 1,386,022	
surplus (deficit)	\$ (145,198)	\$ (76,228)	

Commercial & Housing			Requirements & Notes
	private	public	
Owner Equity	50,000	50,000	committed
Legacy Grant		40,000	more likely at smaller amount
18% historic credits-MN	149,015	149,015	National Register approval
Discount Federal Credits	115,000	115,000	small projects difficult,discounted
Neighborhood STAR		100,000	highly competitive; 50% as loan
2% loan	25,000	25,000	participation with LISC loan
St. Paul CDBG/HOME		300,000	competitive, some amount likely
Federal Home Loan Bank	200,000	200,000	50% of AMI & tenant categories
LISC mini-perm	622,204	622,204	appraised value must support
Total Sources	1,161,220	1,601,220	
Total Uses	1,153,506	1,424,758	
surplus (deficit)	7,714	176,461	

At a 7 or 8% cap rate, the housing + commercial option provides sufficient value to meet LISC loan/value requirements.

Funding Timelines

	Application	Decision	Notes:
NENDC CDBG Grant	anytime	60 days	All other funds to be committed
State Legacy Grant-small	10-Apr-20	mid-June 2020	Write Register nomination
State Legacy Grant-capital	29-May-20	Oct-20	Requires Register status
18% historic credits-MN	on Register	Oct/Nov 2020	Nomination-90 days state review, 45 federal; credits -30-60 days(?)
Discount Federal Credits	on Register	same as above	
Neighborhood STAR	March 18,2020	fall 2020	
2% loan	anytime	30-60 days	participation loan with LISC
St. Paul CDBG/HOME	anytime/June	anytime/Nov.	requires discussion
Federal Home Loan Bank	1-Jun-20	Nov. 2020	
LISC mini-perm Loan	this week	60-90 days	soft letter for St. Paul -avert demo

Project Timeline

Task:	Completed by:
	2020
Final housing design evaluation and decision	February 28
Design Development Drawings and updated construction bid	April 10
Preliminary decision on need for public funding	April 17
Submit Historic Register Nomination to MN SHPO	April 17
Determine if local buyer exists for federal tax credits	May 4
Submit FHLB application	June 1
Submit housing and/or 2% loan application to St. Paul if needed	Mid-June
MN SHPO decision	July 20 (latest)
Complete Construction Drawings/ Final bid & Contracts	July 31
National Park Service Decision	September 10 (latest)
Federal Home Loan Bank decision	Mid-November
Final LISC loan commitment; final City funds if needed	Mid-November
Construction Closing and Construction Start	Mid-December
	2021
Construction Completion	Mid-June

Zimny, Joanna (CI-StPaul)

From: Lisa Kugler <lisa@lisakuglerconsults.com>
Sent: Thursday, February 20, 2020 2:50 PM
To: *CI-StPaul_LegislativeHearings
Cc: Kenneth Udoibok; Dennis Kroll; Olufemi Badejo (feranmibadejo@gmail.com)
Subject: Feasibility Study for 1179 Seventh Street East
Attachments: Feasibility Study - 1179 East 7th Street, St. Paul - 2.19.20.pdf

Ms. Moermond and Ms. Zimny,

Attached please find the feasibility study I was commissioned to provide for this property. A letter from LISC-Twin Cities will be forwarded to you as soon as possible.

Please let me know if you have questions or need additional information.

Thank you for your consideration.

Lisa Kugler
612-718-5954 or 612-827-2189

Zimny, Joanna (CI-StPaul)

From: Naylor, Racquel (CI-StPaul)
Sent: Monday, February 24, 2020 2:58 PM
To: *CI-StPaul_LegislativeHearings
Subject: 1179 Seventh Street, RLH RR 19-23 - Lisa Kegler, 612-827-2189

FYI: Lisa Kegler called our office and talked to Janis. Somehow they got disconnected. I called her back. She said that she wrote the feasibility study on 1179 Seventh Street. She will not be at the Legislative Hearing tomorrow, but the owners will be there along with the architect. She said to call if you have questions on the feasibility study.

-Racquel, 6-8573