Unit III–Case Studies: Applying Community Development Finance Skills to Come up with the Money

Case Study One

Directions: Read this case study carefully. On Page 47, you will be asked to evaluate the unmet needs, assets and opportunities of the imaginary community. Then, you will have the opportunity to work through three scenarios to finance a community development project. You can compare your answers with the suggested answers that start on Page 60. Keep in mind, there is no single way to approach community development finance; so, there is no one right set of answers or opinions with regard to this case study. Be aware, also, that this is a simplified approach to such financing; in real life, other factors might also need to be considered in drawing up such a plan.

Main Street Mixed-Use Development in the City of Windsong

Background

The city of Windsong (population 12,500) is located just outside of Plateau City (population 354,805). Both are in Arrowhead County, which is in the state of Jefferson. Before World War II, downtown Windsong was the community's primary commercial hub. Downtown buildings usually had several tenants—typically a ground-floor retailer and several upper-floor offices or apartments. Together, these tenants provided enough rent for property owners to keep their buildings in good condition. Not only was downtown the center of the community's commercial life, it was also an important part of its social life. People thronged the streets on Saturday nights to meet friends, see a movie and window-shop.

In the 1960s, downtown Windsong sank under the weight of its own apathy. Neglected buildings, boarded-up storefronts and empty, trash-strewn streets gradually reinforced the public perception that nothing was happening downtown and that nothing in downtown was worth saving. With the economic boom of the 1980s, Windsong also saw increased development occurring outside traditional areas.

A building on Lemp Street in downtown Windsong housed until recently a 30-year-old pub called Annie Oakley's. When the building's owner allowed the property to go into foreclosure, Jack King, proprietor of Annie Oakley's, was disappointed to see his successful business close. So, he bought the two-story building for $250,000 and decided to redevelop it. He has an additional $50,000 available for the project. Mr. King envisions a project that would provide affordable rental housing and help revitalize the downtown area by providing retail stores. Mr. King's plan is to renovate the property, which he will call the Annie Oakley Building, to include 10 one-bedroom, affordable apartments and seven commercial storefronts. The Annie Oakley pub will reopen as part of the redevelopment. Rents are expected to range from $400 to $525 a month. Mr. King has identified commercial tenants who are interested but only if small-business financial assistance is available.

Your challenge is to put together a community development finance package that will enable Mr. King to realize his goal by applying the three principles of people, process and money. Let's walk through these principles one-by-one.

People

The main people who would be involved in this project initially are Mr. King and the members of the newly formed Main Street Windsong, a downtown revitalization group. You will act as if you are a board member of this group.

Mr. King, the developer, is an entrepreneur who not only operated Annie Oakley's but also owns and continues to operate other restaurants and other small, successful development projects in the area. His most recently completed project is in a nearby town and contains a family-style restaurant/bar, 18 efficiency apartments that rent at market rates and bed-and-breakfast accommodations.

Main Street Windsong is comprised of downtown merchants and property owners, among others who have an interest in the success of the area. They view downtown Windsong as a neighborhood commercial district and believe it is important to the economic health of the community and to the quality of life in the community. Main Street Windsong is affiliated with the National Main Street revitalization program.

Although Main Street Windsong has just begun its work, it has already made the following observations:

Storefront vacancies. Although the group doesn't know exactly how many businesses there are, the general perception is that most of the Main Street storefronts are vacant.

Resident population. The 2000 census indicates the population in the downtown census tract has a total of 24 people.

Ownership. Of the few businesses that occupy downtown buildings, most do not own the building. The actual number of tenants and owners is unknown, as are names and addresses of all building owners.

Jobs. No one knows the exact figures, but Main Street Windsong believes that a lot of people work downtown.

Deteriorating facades. An architect in town just completed an assessment and noted that nearly every original facade on downtown buildings was in need of substantial rehabilitation. The condition of the others couldn't be determined because aluminum facades had been installed on them in the early 1970s.

Deteriorating buildings. The majority of downtown buildings have had no new paint, tuckpointing or roofs in many years. Some of the buildings' tenants have closed upper levels for fear of unsafe conditions. Most tenants are responsible for completing roof patches.

Poor public infrastructure. Public works—including streets, curbs, sidewalks, drainage and sewers—were last updated in the early 1960s. Parking is inadequate. Pedestrian crossings don't accommodate the handicapped. Landscaping is nonexistent.

Process

Here are some of the sources where you can start your search for financing and for other help for Mr. King.

Sadie Hawkins Bank has been located in Windsong for 70 years. Its loans include both residential and commercial mortgages, with a lending limit of $250,000. The bank usually does not make construction loans, preferring to originate permanent debt-financing. For those who can persuade the bank to make a construction loan, the current rate is prime plus 3 percent, and the term is generally for 12 months. Mr. King believes that the bank will give him a construction loan because he has been a long-time customer. Once the construction is done, he assumes that the bank will give him permanent financing—a mortgage of anywhere from 15 to 30 years.

The Community Preservation Corp. is a nonprofit, mortgage-lending consortium established in 1974 by Plateau City banks and insurance companies to finance affordable housing. Fifty commercial banks, savings institutions and insurance companies participate in CPC activities in the Plateau City region. CPC offers all of the interlocking pieces of a public and private support system to serve as a one-stop intermediary. It makes mortgages and offers credit enhancements and forward commitments. A new product offered by CPC is a statewide Small Building Loan Program that provides rehabilitation financing for owner/occupants of buildings with 20 units or fewer. The maximum loan is one-third of the total project cost. The term is 12 months. The program offers faster, simplified loan processing and extensive technical support. (For example, the program's experts advise owners about government agency filings that are required to obtain real estate tax benefits. The program's experts also provide information about experienced local architects and contractors.) In addition, while CPC construction loans typically are 2 percentage points above prime, the loans through the Small Building program are 1 point above prime.

The Main Street Windsong program shouldn't be counted on for funds just yet. After all, it is just getting off the ground. But its organizers firmly believe that the four areas of concentration of the National Main Street program—organization, promotion, design and economic restructuring—are vital for the successful revitalization of downtown Windsong. The organizers intend to raise $1.5 million for a small-business fund, which should help Mr. King attract tenants.

In the meantime, the director of the Main Street program did some investigating and discovered that Arrowhead County has federal HUD funds available from the Home Investment Partnership Act program, commonly called HOME. This money is available through a competitive application process. The loans are limited to $150,000 per application. The good news is that HOME loan funds charge no interest; in addition, the loan may be forgiven after 15 years if the apartments maintain their affordability to low- and moderate-income occupants.

When the director of Main Street Windsong shared the information about the HOME program with the Main Street board, one board member suggested that federal Community Development Block Grant (CDBG) money may also be available for this type of activity. A CDBG loan could be made by the city of Windsong for up to $170,000 at no interest for 20 years if the project meets economic revitalization guidelines of the program.

The Main Street program also has access to a historic preservation grant program that offers grants up to $50,000 with a 50 percent match. There are strict rules to satisfy design standards and building codes.

Now that you have identified the people and the process, how will you come up with the money? That's your challenge. But before you start analyzing this case study, review Mr. King's basic budget on the next page.

Annie Oakley Budget Exhibits

The interplay of financial and non-financial information will be useful when thinking about coming up with the money for the Annie Oakley project. The exhibits are provided for informational purposes only. They include the type of information a lender, for example, would need to have to calculate if operating income will cover the debt payments on the project. Consider the following question: What is the monthly operating budget and how may it be matched to the project development budget? Keep in mind that your net operating income would have to cover all of your financing and other costs.

Table 1. Development Budget

Hard Costs	
Building acquisition	$250,000
Renovation	485,000
Contractor fee	50,000
Total	***785,000***
Soft Costs	
Contingency 9%*	$45,000
Architectural 3.5%*	17,500
Disbursing fees 1.5%*	7,500
Legal fees	5,000
Other fees	5,000
Total	80,000
Hard & soft costs subtotal	865,000
Financing cost (to be determined)	
Total Project Cost	

* These are percentages of renovation costs. These percentages are approximations of those that are sometimes used in the industry. The dollar amounts that go with these percentages have been generously rounded off to make calculations easier

Table 2. Projected Monthly Operating Budget (Income and Expense Statement)

Rental Income	
3 units at $400/month	$1,200
6 units at $450/month	2,700
8 units at $525/month	4,200
Rent revenue	8,100
Less 10 percent vacancy	810
Total Rental Income	***7,290***
Operating Expenses	
Leasing and administrative	
Property manager/ leasing agent	$1,000
Maintenance contract	500
Advertising	40
Office supplies	30
Telephone	20
Insurance	300
Property taxes	100
Utilities	900
Replacement reserve	500
Total operating expenses	3,390
Net Operating Income	***3,900***

Coming up with the Money

Let's start identifying financing sources.

As a board member of Main Street Windsong, you are responsible for assisting small-business owner Jack King in obtaining the initial financing for the rehabilitation of the mixed-use downtown property. How much money is really needed, where will it come from and how may it be used? (Assume the prime rate is 7 percent, and don't worry for now about long-term financing.)

Case Study Analysis: Evaluating Finance Projects

Instructions: After reading the case study, complete this step-by-step evaluation of the project. Then, compare your answers with the suggested answers on Pages 60-70.

Step 1. Define Unmet Finance Needs

- What is going on in Windsong that warrants attention?

- Is there an unmet need the project is attempting to address?

- What exactly is Annie Oakley's?

- What type of project will this turn out to be?

- What are the goals of the project?

Step 2. Recognize Assets (either in the community or available to the community)

- What is the management capacity of the initiative?

- What skills or resources could be brought to the initiative to improve performance?

Step 3. Identify Types of Funding Choices

Our case study mentions several financing sources that are available. Fill in the table on the next page with the name of each funding source, the type (equity, construction loan, grant, etc.), the rate, the term (length of loan) and conditions or restrictions on the money. Include Mr. King's investments on your list. Then, compare your answers with those on Page 63.

Mr. King's List of Possible Financing Sources

Source	*Type*	*Rate*	*Term*	*Amount and Conditions*

Calculating Financing Costs

When money is borrowed, interest is charged. How interest is calculated is usually complicated. This exercise will only give you a taste of how it's done in real life. This exercise serves as a reminder that the cost of borrowed money must be included in any community development finance project.

In the following example, the lender calculates the interest charge by multiplying the entire loan amount by the interest rate.

Example:

Loan Amount	Interest Rate	Term	Financing Costs
$10,000	5%	12 months	$500

Formula:

10,000 x .05 = 500

Now it's your turn.

What will be the financing cost for each of the following? Fill in the blank space with your answer.

Loan Amount	Interest Rate	Term	Financing Costs
$50,000	5%	12 months	
$50,000	8%	12 months	
$50,000	9%	12 months	
$150,000	10%	12 months	
$250,000	10%	12 months	
$500,000	12%	12 months	

Answers: $50,000 x .05 = $2,500; $50,000 x .08 = $4,000; $50,000 x .09 = $4,500; $150,000 x 0.10 = $15,000; $250,000 x 0.10 = $25,000; $500,000 x 0.12 = $60,000

Step 4. Determine Financing to Cover the Cost of the Project

The goal of this step is to review the project costs and the sources of money that are available to pay for the uses. You should work toward balancing the two. The costs can equal the sources of money or total less than the sources but can't exceed them.

Scenario 1

As you can see, there are three blank spaces in the Uses table that have yet to be filled in: the subtotal, the financing costs and the total project cost. You can add up the hard and soft costs to get the subtotal—a preliminary idea of how much money you need to come up with. The financing cost will have to be filled in later—you can't do it now because you don't know yet if you will be tapping into sources of money that charge interest. Only after you go through this process will you be able to come up with a total project cost.

Uses

Project Costs	***$ Amount***
Hard Costs	
Building acquisition	250,000
Renovation	485,000
Contractor fee	50,000
Total Hard Costs	785,000
Soft Costs	
Contingency 9%	45,000
Architectural 3.5%	17,500
Disbursing fees 1.5%	7,500
Legal fees	5,000
Other fees	5,000
Total Soft Costs	80,000
Total Hard Costs	785,000
Hard & Soft Costs Subtotal	
Financing costs	
Total Project Cost	

How would you start to decide which sources of funding to use? Which sources are the most attractive?

Sources

Use the list of possible financing sources that you developed for Mr. King (or see the list provided on Page 63) to fill in the Sources table to determine how to come up with the money for this project. (Hint: You'll want to turn first to the sources of money that cost the least and carry the least-restrictive conditions.)

So that you don't have to flip back and forth, you may want to remove the page with your list of financing sources from this binder and place next to this page.

Don't worry about the "$ Adjusted" column for now; you will see what that is for in a minute.

Sources

Sources	***$ Amount***	***$ Adjusted***
1.		
2.		
3.		
4.		
5.		
6.		
7.		
Total		

Once you determine the sources, calculate your financing costs (if any) and write this figure in at the end of the "Soft Costs" on the Uses table. ("Scratch paper" is provided on the next page for your calculations.)

Scratch paper

■ Is the total of uses equal to or less than the total of sources? ☐ Yes ☐ No

If "No," then you still have a funding gap. Rework your sources to cover the total project cost. Use the "Adjusted" column for your next attempt. Remember to adjust financing costs accordingly.

When you balance uses and sources, answer the following questions:

■ Why did you choose the sources that you did?

■ Did you remember to follow any terms or conditions tied to the sources?

Scenario 2

You recently learned that CDBG financing is not available for this project. Refer to the list of possible financing sources to fill in the Sources table to determine how to finance this project. You may not use CDBG funds for this scenario.

Sources

Sources	***$ Amount***	***$ Adjusted***
1.		
2.		
3.		
4.		
5.		
6.		
7.		
Total		

Once you determine the sources, calculate your financing costs and write this figure in at the end of "Soft Costs" on the Uses table on the next page.

Scratch paper

Uses

Project Costs	***$ Amount***
Hard Costs	
Building acquisition	250,000
Renovation	485,000
Contractor fee	50,000
Total Hard Costs	785,000
Soft Costs	
Contingency 9%	45,000
Architectural 3.5%	17,500
Disbursing fees 1.5%	7,500
Legal fees	5,000
Other fees	5,000
Total Soft Costs	80,000
Total Hard Costs	785,000
Hard & Soft Costs Subtotal	
Financing costs	
Total Project Cost	

- Is the total of uses equal to or less than the total of sources? ☐ Yes ☐ No

If "No," then you still have a funding gap. Rework your sources to cover the total project cost. Use the "Adjusted" column for your next attempt. Remember to adjust financing costs accordingly.

When you balance uses and sources, answer the following questions:

- Why did you choose the sources that you did?

- Did you remember to follow any terms or conditions tied to the sources?

Scenario 3

In this scenario, bank financing is not available. CDBG is available, but with a maximum of $50,000. (Round off the CPC loan to $300,000.) Begin making your selection of sources from your own list of possible financing sources or from the list provided in the answers section. This time, feel free to adjust your "soft costs" on the Uses table, pretending that you might be able to get some of the professional services donated or at a reduced price.

Sources

Sources	***$ Amount***	***$ Adjusted***
1.		
2.		
3.		
4.		
5.		
6.		
7.		
Total		

Once you determine the sources, calculate your financing costs and write this figure in at the end of "Soft Costs" on the Uses table.

Scratch paper

Uses

Uses	***$ Amount***	***$ Adjusted***
Hard Costs		
Building acquisition	250,000	
Renovation	485,000	
Contractor fee	50,000	
Total Hard Costs	785,000	
Soft Costs		
Contingency		
Architectural		
Disbursing fees		
Legal fees		
Other fees		
Total Soft Costs		
Total Hard Costs	785,000	
Hard & Soft Costs Subtotal		
Financing costs		
Total Project Cost		

- Is the total of uses equal to or less than the total of sources? ☐ Yes ☐ No

If "No," then you still have a funding gap. Rework your sources to cover the total project cost. You may need to reduce uses. Use the "Adjusted" columns for your next attempt.

When you balance uses and sources, answer the following questions:

- Why did you choose the sources that you did?

- If you altered uses, what was your rationale for doing so?

- Did you remember to follow any terms or conditions tied to sources?

- Were there any new resources or techniques used to adjust uses and sources?

- What other resources or ideas could have been used?

Suggested Answers to Annie Oakley Case Study

Step 1. Define Unmet Finance Needs

- What is going on in Windsong that warrants attention?

  Windsong has a distressed downtown area with at least one business owner/developer asking the downtown development organization for help to redevelop his property.

- Is there an unmet need the project is attempting to address?

  Possible responses include:

  - Need for economic health
  - Better quality of life in downtown
  - Downtown housing
  - Storefront businesses/reduce vacancies
  - Improved appearance of downtown
  - Improved public utilities
  - Small-business financing
  - Second-story development or rehab
  - Need for financing to assist small-business owner Jack King in developing second-story housing over rehabilitated retail storefronts in downtown Windsong
  - Need for a grant or loan fund for small-business development

- What exactly is Annie Oakley's?

  The building is named for the pub that once occupied part of the space. When renovated, the mixed-use property will include second-story housing and street-level businesses, including the reopened pub.

- What type of project will this turn out to be?

  Responses may include a range of types, but generally it is a project that requires a mix or blend of approaches to develop housing and retail storefronts. Specifically, it is a downtown revitalization project focusing on second-story housing and commercial storefront rehabilitation.

- What are the goals of the project?

  Possible responses include:

  - Housing
  - Revitalize downtown
  - Small business
  - Economic development
  - Community development
  - Rural development
  - Microenterprise development
  - Jobs in downtown
  - Attract downtown shoppers
  - Devise a finance plan
  - Organize a grant or loan fund

  Specifically, the housing-storefront goals of the project are:

  - Ten units of housing
  - Seven retail storefronts

Step 2. Recognize Assets (either in or available to the community)

- What is the management capacity of the initiative?

  The new owner of the building, Jack King, is a for-profit entrepreneur who appears to have a strong track record in owning and operating mixed-use developments. Mr. King has a recently completed project in a nearby community that includes a family-style restaurant and 18 efficiency apartments.

  Main Street Windsong is a recently formed, nonprofit organization that has the goal of improving the downtown—bringing businesses back to its Main Street. It is participating in the National Main Street program, which has a reputation for providing excellent management consulting services.

- What skills or resources could be brought to the initiative to improve performance?

  Mr. King, who bought the building for $250,000, has an additional $50,000 available for the project. His management skills will also be useful in leveraging other investments.

Those familiar with the National Main Street program know that it makes expert consultants available to participating downtowns. Main Street Windsong will be able to bring the management resources of the program to the table. In addition, Main Street Windsong plans to raise $1.5 million for a small-business fund. This fund will help finance small businesses that may be housed in this proposed development.

There is local government support (County HOME or City CDBG programs).

Community Preservation Corp. (CPC) has a strong record. CPC is a consortium, or partnership, among 50 banks, savings institutions and insurance companies to finance affordable housing. It has first mortgage underwriting capacity and offers credit enhancements and forward commitments.

Step 3. Identify Types of Funding Choices

Here's the list of specific funding sources that we've already identified as being available for Mr. King's project.

Mr. King's List of Possible Financing Sources

Source	*Type*	*Rate*	*Term*	*Amount and Conditions*
Jack King • Purchase of building • Additional owner equity	Equity			$250,000 already committed. Maximum $50,000 cash if required.
Sadie Hawkins Bank	Construction loan	Prime + 3%	12 mos.	Maximum lending limit of $250,000.
CPC-Small Building Loan Program	Construction loan	Prime + 1%	12 mos.	Maximum loan no greater than one-third total cost. Owner-occupancy required. 20-unit maximum.
County HOME funds	Loan	0%	15 yrs.	Limited to $150,000 per application, forgiven after 15 years. Affordability restrictions.
City CDBG funds	Loan	0%	20 yrs.	Maximum per project of $170,000 if project meets economic revitalization guidelines.
Historic preservation	Grant	0%		Up to $50,000. Requires 50% match. Strict design standards and building code restrictions.

Step 4. Determine Financing to Cover the Cost of the Project

Scenario 1

This is our first possible alternative for financing the project.

Uses

Project Costs	***$ Amount***
Hard Costs	
Building acquisition	250,000
Renovation	485,000
Contractor fee	50,000
Total Hard Costs	785,000
Soft Costs	
Contingency 9%	45,000
Architectural 3.5%	17,500
Disbursing fees 1.5%	7,500
Legal fees	5,000
Other fees	5,000
Total Soft Costs	80,000
Total Hard Costs	785,000
Hard & Soft Costs Subtotal	865,000
Financing costs	**42,000**
Total Project Cost	**907,000**

Financing costs: Prime = 7%.

The formula below is much simpler than what is actually used by lending institutions. This formula will only yield an approximation of what interest charges will really total in a year. We are calculating simple interest, not compound interest.

$$\begin{array}{rcl} \$180{,}000 \ \text{x} \ .10 & = & \$18{,}000 \\ \underline{\$300{,}000 \ \text{x} \ .08} & \underline{=} & \underline{\$24{,}000} \\ & & \$42{,}000 \end{array}$$

On the next page, see the sources of funding we chose.

Sources

Source	***$ Amount***	***$ Adjusted***
King	250,000	
CDBG	170,000	
CPC	300,000	
Bank	180,000	
Total	900,000	

First attempt (Refer to figures under "Amount.")

King–Only used his initial investment of $250,000 that he spent on the building. Saved his additional $50,000 to cover unexpected expenses.

CDBG–Used maximum available because there is no interest and are minimal conditions.

CPC–Used maximum available. Less interest than bank loan.

Bank–Due to relatively high interest rate, used minimum amount to fill gap.

HOME–Didn't use because even at no interest rate it has strict occupancy income restrictions.

Historic Preservation–Didn't use because of strict design standards and restrictions.

In our first attempt, we came up with $900,000. That covered all of our expenses as far down as the "subtotal." But then we added financing expenses. When we did that, our total expenses were $907,000. We had to try again.

Second attempt (Refer to "Adjusted" figures.)

Uses

Uses	***$ Amount***	***$ Adjusted***
Hard Costs		
Building acquisition	250,000	250,000
Renovation	485,000	485,000
Contractor fee	50,000	50,000
Total Hard Costs	785,000	785,000
Soft Costs		
Contingency 9%	45,000	45,000
Architectural 3.5%	17,500	17,500
Disbursing fees 1.5%	7,500	7,500
Legal fees	5,000	5,000
Other fees	5,000	5,000
Total Soft Costs	80,000	80,000
Total Hard Costs	785,000	785,000
Hard & Soft Costs Total	865,000	865,000
Financing costs	42,000	**43,000**
Total Project Cost	907,000	**908,000**

Financing costs: Prime = 7%.

Remember: The formula below is much simpler than what is actually used by lending institutions. This formula will only yield an approximation of what interest charges will really total in a year.

$$
\begin{array}{lcccr}
\$190{,}000 & \times & .10 & = & \$19{,}000 \\
\underline{\$300{,}000} & \underline{\times} & \underline{.08} & \underline{=} & \underline{\$24{,}000} \\
 & & & & \$43{,}000
\end{array}
$$

See how we adjusted our sources of funding on the next page.

Sources—Refer to the "Adjusted" amounts.

Sources	***$ Amount***	***$ Adjusted***
King	250,000	250,000
CDBG	170,000	**168,000**
CPC	300,000	300,000
Bank	180,000	**190,000**
Total	900,000	**908,000**

We took out an extra $10,000 in the loan from the bank. That slightly increased our financing costs, but we were also able to lower the CDBG contribution by $2,000. Everything else remained the same.

Scenario 2

Everything is the same, except CDBG financing is not available.

Sources

Sources	***$ Amount***	***$ Adjusted***
King	268,000	
CPC	300,000	
Bank	190,000	
HOME	150,000	
Total	908,000	

Rationale:

HOME–Have to use despite restrictions on occupants' income. Plus, like CDBG, there are no financing fees associated with HOME funds. Therefore, we didn't have to adjust our financing costs.

King–Used $18,000 of his additional $50,000 to fill the gap.

Historic Preservation Grant–Didn't use, again because of restrictions.

Scenario 3

Bank financing is not available. CDBG is available, but with a maximum of $50,000. Feel free to adjust your soft costs. For example, pretend that you might be able to get some of the professional services donated or at a reasonable price.

Uses

Uses	***$ Amount***	***$ Adjusted***
Hard Costs		
Building acquisition	250,000	
Renovation	485,000	
Contractor fee	50,000	
Total hard costs	785,000	
Soft Costs		
Contingency	**24,250**	
Architectural	**0**	
Disbursing fees	7,500	
Legal fees	5,000	
Other fees (estimates were too high)	**4,000**	
Total Soft Costs	**40,750**	
Total Hard Costs	785,000	
Hard & Soft Costs Subtotal	**825,750**	
Financing costs	**24,000**	
Total Project Cost	**849,750**	

Rationale:

We started by using the maximum amount of sources we had—$850,000. Because that is less than the subtotal of expenses we have been using, we knew we had to start cutting uses. The new numbers for some of these uses appear in boldface on the uses table. Here is why we cut those figures:

Contingency–Lowered from 9% to 5% and hope for the best.

Architectural–Services were donated through Main Street.

Other fees–Actual fees for licensing and for applications were lower than anticipated.

Financing costs–Reduced to $24,000, which is the CPC loan of $300,000 x prime + 1. Lowered because we have no bank financing to cover.

Sources–possible solution

Sources	***$ Amount***	***$ Adjusted***
King	300,000	
CPC	300,000	
HOME	150,000	
CDBG	50,000	
Historic preservation grant	50,000	
Total	850,000	

Rationale:

King–Once we found out bank financing was not available, we had to use his additional $50,000.

HOME–Have to use despite restrictions on occupants' income. Plus, no financing fees.

Historic preservation grant–Straight grant because we had the match (CDBG and King's money) and we decided to meet the design standards and code restrictions.

In real life, you'd also have to plan for long-term financing. You'd need a permanent loan to replace the one-year construction loan.

Update

This case study is loosely based on a real community development project in Port Jervis, N.Y. The real "Main Street Windsong" and "Jack King" assumed that a local bank would make a loan in downtown. They were wrong! Not one bank that "Mr. King" approached was willing to make such a large loan. The banks considered the venture to be a speculative project, and they said that the downtown area did not have a recent track record in either housing or small business start-ups or expansions.

The Main Street organization in the real town brought the project to that area's CPC program, which, in that county, could combine the county's HOME allocation with CPC financing in a one-stop annual request for proposals. The city also provided a subsidy to the project from its small cities' CDBG funds.

In coordinating the three funding sources, the CPC program required that the developer use county funds first and then city CDBG funds before drawing on CPC money. This lowered the project's long-term financing cost because the public funds were interest-free. Therefore, the major portion of construction work could take place without incurring the expense of interest payments.

See financing charts on next page.

Financing Sources for Actual Project

Development Financing

Sources	Amount	Type	Rate	Term
Owner	293,055	cash		
CPC	300,000	construction loan	prime plus 1%	12 months
County HOME	150,000	loan	0%	Forgiven after 15 years
City CDBG funds	175,000	loan	0%	20 years

Permanent Financing

Sources	Amount	Type	Rate	Term
Owner	293,055	cash		
State Retirement Fund	300,000	1st mortgage	9.75%	30-yr. fixed rate
County HOME	150,000	co-2nd	0% mortgage	Forgiven after 15 years
City CDBG	175,000	co-2nd mortgage	0%	20 yrs.

Small-Business Development Financing

In the actual case, the Main Street program made a concerted effort to help small businesses. At first, the Main Street program wanted to get legislation passed to create a Small Business Improvement District. But then the program's organizers realized that the tax base of downtown was in such poor condition that not much money would have been raised anyhow. So, they forgot about that idea for a while. (Remember business cycle and timing?)

The Main Street officials believed that the funding goal of $1.5 million could be more realistically attained if the city were to partner with the county and banks in the area to raise the seed capital. A public-private partnership was formed among the city, county and seven local banks. Low-interest loans were made available to service-oriented, light manufacturing, wholesale and retail businesses. Each business was required to create or retain permanent jobs for low- and moderate-income persons.

A loan review committee and the participating banks were involved in the loan approval process. This procedure resulted in a high-quality loan portfolio with a very low default rate. Jobs were created for low- and moderate-income residents. In the county, loans to 19 businesses resulted in the creation or retention of 81 jobs for low- and moderate-income persons. In the city itself, there were six loans and the creation or retention of 23 jobs in the downtown area.

The funding goal of $1.5 million was not quite reached, but a significant amount of dollars was secured: $420,200 from block grant funds and $622,800 from private sources.

Several lessons were learned in this process. Federal resources were leveraged through the public-private partnership. Sixty percent of each loan was composed of bank funds, and 40 percent was made up of federal funds. CDBG dollars were more effectively used and were stretched further by forming public-private partnerships. Seeking the participation of as many local banks as possible paid off.

The Federal Reserve Bank of St. Louis gratefully acknowledges the National Association of Affordable Housing Lenders (NAAHL) for permission to base this case study on the actual project located in Port Jervis, N.Y., and described in the NAAHL publication “Building Sustainable Communities: Best Practices in Community Development Lending,” 1997.