

## ***Multifamily Report Card***

The California Housing Finance Agency (CalHFA) has developed an efficient risk assessment tool, the Multifamily (MF) Report Card to compare the underwriting pro forma to the actual operating cost of a new construction property during the initial five-to-seven years of operation. The MF Report Card provides a quick one-page summary for senior management and staff to assess the overall financial condition of the property. The MF Report Card allows CalHFA to assess the financial performance of a project as compared to the underwriting assumptions. The MF Report Card can be used as leverage to determine if the agency would like to maintain or adjust its working relationship with a sponsor and/or management agent for future endeavors. The data that supports the MF Report Card provides substance to the relationship between the agency's Asset Management and MF Program staff.

An underwriting pro forma developed by the MF Programs division and the sponsor is a year-by-year projection of a project's income and expenses. The actual operating data (income and expenses) are derived from the Audited Financial report that is submitted by each property in the agency's portfolio. The MF Report Card shows the projected and actual debt coverage ratio (DCR), revenues and expenses of the property, and allows staff to quickly determine if the DCR is met. The DCR is the ratio of net operating income to debt payments on a property. DCR is used as a benchmark to measure a property's ability to generate enough revenue to pay the monthly mortgage payments. The DCR is calculated by dividing the property's annual net operating income (NOI) by a property's annual debt service. Annual debt service is the annual total mortgage payments; the principal and accrued interest, but not the escrow payments. A DCR of less than 1.0 (e.g. .80) indicates that there is not enough revenue to pay the property's expenses and monthly mortgage payments. A DCR of 1.0 is considered the breakeven point. Any project with a DCR less than 1.10, which is the agency's minimum standard, receives additional oversight by agency staff.

## **Background**

CalHFA's mission is to provide affordable housing to the families and individuals in California. The MF Programs division provides permanent financing for new construction rental housing and the acquisition, rehabilitation and preservation of existing rental housing. The oversight and monitoring of the property is the responsibility of the Asset Management division for the duration of the mortgage. The two divisions are tasked to work together to provide the best end product: a viable and thriving multifamily development.

The MF Report Card reviews the financial condition of a multifamily property during the initial years of operation. Over the years, more complex and diverse financial deals were crafted by the MF Program division. The loan complexity compounded the need for the asset manager to provide more detailed oversight on each property. A multifamily developer's desire to close the deal can often cloud the reality of what it costs to operate a multifamily development.

Another issue is the staffing level in Asset Management has not kept pace with the growing portfolio. The Asset Manager's portfolio has increased over the years which resulted in less oversight for each property. State compensation has not kept pace with the private sector.

As a result, it is difficult to attract qualified staff. This coupled with the increase number of staff that have retired, has directed our attention to using technology to manage more assets with less staff. The need to monitor the properties in a more efficient manner was identified. The MF Report Card helps direct staff to where their time would be best spend monitoring properties.

### **MF Report Card Elements**

An Excel template with formulas and links was created to generate the MF Report Card with simplicity. The MF Report Card captures the revenue generated, expense cost, reserve amount and debt service information from the pro forma and audited financial information for a property. It automatically calculates the NOI and DCR for the property and the variance by dollar and percentage of the pro forma cost versus the audited cost. The template contains formulas that will automatically populate years two through seven for some of the cost items after the first year of information is entered. If a cost item differs from the pro forma assumption, the Asset Manager can input the correct amount, thereby reducing the amount of time to takes enter the financial information for each year. Please refer to Exhibit A.

Once the financial information is entered, a graph and summary are automatically generated to produce the MF Report Card. The MF Report Card provides general property information: property location, sponsor name, total number of units, property type, loan amount, interest rate and loan terms. It also allows for comments for any special conditions or notes about the property. The DCR, Revenue per Unit per Year and Expense per Unit per Year is depicted on a graph to clearly show the trend over time. This summary illustrates the property's long-term viability and earnings and the actual operating cost to determine the accuracy of the projections. Please refer to Exhibit B.

### **MF Report Card Application / Achievement**

The MF Report Card was developed to achieve the following goals:

- ❖ Provide a risk assessment tool to identify at-risk properties at an early stage so the agency can intervene to remedy the problem.
- ❖ Provide a concise one-page summary of the pro forma versus the actual income and expenses to determine the accuracy of the underwriting projections and provide a succinct picture of the financial condition of the property.
- ❖ Chart the DCR to illustrate the property's performance.
- ❖ Provide actual income and expense cost and revenue trends to the MF Program division that will result in improved underwriting projections going forward.
- ❖ Communicate property performance information to agency staff, the sponsor and/ or management agent.
- ❖ Ability to review a sponsor's track record with the agency to determine the property's performance and allows CalHFA to discuss future properties with sponsor.

California Housing Finance Agency  
Entry Description: RENTAL HOUSING: Multifamily Management

The MF Report Card is a risk assessment tool the agency will use to identify the financial strengths and weaknesses of a specific property and provide valuable information when comparing similarly situated properties. Despite using a simple Excel application instead of expensive software, it permits a robust, proactive approach the agency can use to reduce the likelihood of a property default and anticipate potential financial risks in the long term.