December 8, 2017

Mr. Ralph Mosley
Chairman
MDHA Board of Commissioners

Dear Ralph,

Organizations rarely face a single decision that reflects their overall strategy and values. MDHA’s Board of Commissioners’ decision to develop the Explore School as a centerpiece of its Envision Cayce master plan is one of these rare decisions. MDHA has tied its future to Envision Cayce. The success of Envision Cayce’s mixed income plan to remedy concentrated poverty is intrinsically linked to a new high performing elementary school for the larger Envision Cayce population. In preparation for the next Board meeting, and as approved unanimously by a Joint Meeting of the Finance and Development Committees on December 6th, this letter presents the program to develop and sell a new school building to the Explore School, the charter school approved for Envision Cayce adjacent to the Martha O’Bryan Center (MOB).

Prior to my appointment, MDHA collaborated with the residents of James A. Cayce Homes and the surrounding neighborhoods to plan for the revitalization of the 1937 era, obsolete Cayce apartments as a way to remedy its concentrated poverty. After 18 months of community planning, the MDHA Board approved the resulting Envision Cayce master plan to transform Cayce’s public housing into a mixed income, mixed use community that supports and improves opportunities for new and present residents. Based on strong resident desires expressed in extensive surveys, the plan places an education and services campus at the heart of the new mixed income community, whose focus is high quality educational opportunities for children. All evidence from the master planning process and other successful mixed income communities show that a commitment to high quality education for resident children is the key to neighbors of differing incomes living well, side by side, in harmony.

The leading model for mixed income redevelopment of concentrated poverty in the United States is the East Lake Community of Atlanta, where a very aged public housing site of concentrated poverty, high crime and low opportunity was transformed into a thriving mixed income, mixed use community. Purpose Built Communities developed and runs East Lake and is the Nation’s leading mixed income consultant. The President of Purpose Built Communities, Carol Naughton, addressed the Development Committee on December 6th and emphasized the critical importance of high quality early education to successful mixed income redevelopment of concentrated poverty.

As Carol specified, breaking the cycle of generational poverty can only be achieved through changing the lived environment from antiquated housing of concentrated poverty and limited opportunity, to new housing with mixed income residents and high quality educational opportunity for children. A new, superb elementary school is the foundation of educational opportunity and successful mixed income redevelopment. East Lake and Purpose Built Communities, as stated eloquently by their President to the Development Committee, fully endorse the residents’ desires and the Board’s decision to build the Explore School as Envision Cayce’s centerpiece.
During the search in 2013 for a new MDHA Executive Director, the Executive Search Committee's principal development question to candidates was: "how would you make the Envision Cayce master plan a reality, and what resources exist to fund Envision Cayce's construction?" My answer was the transformative nature of the U.S. Department of Housing and Urban Development's (HUD) Rental Assistance Demonstration (RAD) program whose fee simple land transfer to MDHA from HUD would allow a more business focused approach to development, operations and finances; full access to debt equity and tax credit financing; and better access to business partnerships. MDHA accepted this answer and since my appointment has pursued the RAD conversion of all MDHA public housing. We are 70% complete with James A. Cayce scheduled for conversion in March, 2018.

Post RAD, MDHA is freed from the HUD Public and Indian Housing model to function more efficiently, and to pursue the resources needed to build Envision Cayce and the Explore School. The school will be built using the construction management at risk with a guaranteed maximum price (CM at risk with GMP) project delivery method on a Fast Track schedule, allowing an early start for site preparation and subgrade utilities beginning April 2018, and enabling completion in July 2019. The project delivery team is led by MDHA's Recapitalization Division. The architect is Johnson, Johnson and Crabtree Associates (JJCA) of Nashville. The selection of the Construction Management firm is underway with evaluation this week of the responses to our CM at Risk with GMP Request for Proposal that was published in November.

The Explore School is chartered as a K – 8 elementary school with an anticipated student full occupancy population of up to 900 students, and will be built immediately adjacent to the Martha O'Bryan Center on 4 acres in one 90,312 gross square foot (gsf) building. This building will have 36 classrooms, minimal offices, a small faculty lounge and a resource room. When complete, the school will take advantage of the present Martha O'Bryan infrastructure, alleviating the need for a gymnasium and other supporting amenities. Its design includes designated expansion zones for future student body needs.

The Explore School presently is housed .5 miles from its future site and has grades K – 2 fully operating. It will add one grade per year. At its present pace, it will outgrow its current facility by the start of the 2019 – 2020 school year. It has, and will continue to have, a preference for Cayce resident children. The project is timed to deliver at the end of July 2019 to allow continuity of school operations. Any delay in project delivery complicates school operations.

Task sequencing on the program’s critical path is essential to project timing and success. Post Board review and approval, key next steps are completion of the RAD transfer of Cayce to MDHA fee simple ownership, the clearing of environmental review, and the start of resident relocation for the 9 existing buildings that are in the Explore School footprint. Detailed planning is ongoing for these tasks.

The project’s total budget is not to exceed $25,000,000 with architect and engineering fees at $1,549,404; construction at $19,630,108; MDHA developers’ fee at $429,393; furnishings, moveable equipment and telecommunication at $1,949,178; other soft costs, including impact and Metro review fees at $277,224; and owner contingency at $1,154,693.

Permanent financing will consist of New Market Tax Credits that will provide $5.3 million equity for the project, a loan of $14.7 million, and $5 million in equity to be raised by the Martha O'Bryan Center through a fund raising drive. At occupancy, MOB will execute a triple-net, 10 year lease for the building, paying rent equal to approximately 9.5% of the school’s annual gross revenues. MDHA will own the school and MOB will be our tenant until they can purchase the building from MDHA, or until the end of the 10 year lease period, whichever is earlier. Their rent will pay the majority of MDHA’s debt service requirement.
During the lease period, MDHA is responsible for any gap between MOB rent payments and debt service. The projected rent from the school may not cover all debt service on the loan, especially in the initial years as the school grows to a full K-8. After the school has been in operation, but not later than 10 years, MOB will purchase the school building and reimburse MDHA for any funding advanced to fill a debt service gap. Pro forma analysis indicates that the aggregate gap will not exceed $3M at the end of 10 years. $300,000 is estimated as the maximum amount of interest due to account for present value.

Not later than the conclusion of the 10 year lease, MOB will purchase the school from MDHA for a presently estimated maximum price of $18,000,000. This $18,000,000 estimate results from a $25,000,000 rough figure for MDHA costs, reduced by $5,300,000 in tax credits, reduced by $5,000,000 in MOB fund raising and increased by an estimate of $3,300,000 maximum in debt gap payments at 10 years, including escalation for present value. MOB will receive the value of the tax credits. As in the other parcels on Cayce where MOB buildings exist, MDHA will retain ownership of the land with MOB taking a long term ground lease concurrent with their building purchase.

MDHA has partnered with Atwater Infrastructure Partners of Los Angeles to finance the project. Atwater has secured new market tax credit pledges from nine Qualified Community Development Entities (CDE) in excess of the tax credit financing requirement. The new market tax credit process and full financing will not complete until October 2018. In order to meet the project delivery schedule and complete by July 2019, this project calls for development at risk until close of financing, estimated to be October of 2018. The funds for our development at risk are available in MDHA’s operational reserve and are estimated not to exceed $4.7M. MDHA will receive these funds back at loan close.

Cash equity requirements for an October 2018 loan close are estimated at $5M. MDHA also has these funds available in its operational reserve. MOB will raise $5M in a three year fund raising drive that begins in early 2018. As MOB receives funds in their campaign, they will provide them to MDHA. MOB anticipates providing $1.2M to MDHA by the end of 2018, an additional 1.3M to MDHA by the end of 2019 and the balance of $2.5M by the end of 2020. These estimated balances will be adjusted for present value as they are provided to MHDA. The Explore School will occupy the new building in August 2019.

In financing, there are three separate cash funding gaps for the project: an initial $4.7M for development at risk to loan close, which is reimbursed to MDHA at the October, 2018 close of financing; $5M equity to close financing, which is reimbursed to MDHA by MOB over a three year fund raising campaign and not later than the end of 2020; and a potential operating deficit between required debt service and collected rent, which is estimated not to exceed $3M in aggregate over ten years, should MOB not buy the school sooner, and will be reimbursed with interest at property sale, not later than ten years after initial occupancy.

As previously presented to, and approved unanimously by the Joint Meeting of the Finance and Development Committee, I am requesting Board approval of the Explore School project delivery program as described in this letter. Approval is requested for: the project’s location, scope, budget, schedule and project delivery team; not more than $4.7M in operating reserves to be expended for development at risk to loan close on or about October, 2018, when these funds will be reimbursed to the operating reserve; not more than $5M to be expended from the operating reserve at loan close for equity, with these funds being reimbursed from MOB fund raising over three years and not later than 2020; and not more than $3M total from operating reserves over a ten year period from 2019 to 2029, should the MOB lease go to full term, and only to pay any rent to debt service gaps if they develop, with these funds being reimbursed at Explore School building sale with interest to account for present value.
I will request subsequent Board approval for: the selection of the Construction Management firm; the loan and new market tax credits, as these documents are completed for financing over the course of the next year; the development agreement between MOB and MDHA; the lease agreement between MOB and MDHA; the final sale of the school building to MOB from MDHA; and the ground lease accompanying the sale for the parcel on which the Explore school building is built.

MDHA enjoys an 80 year partnership with the Martha O'Bryan Center who has an incredible bond of trust with our residents and joins us daily in our work to improve their lives and advance out of poverty. The Board chose wisely and boldly to plan Envision Cayce. This program provides a practical means to build the Explore School while mitigating the development risk of increased construction costs through a CM at Risk with GMP and Fast Track schedule project delivery method, and simultaneously mitigating the educational risk of delaying the Explore School's move to its new location. Approving this project delivery plan for the Explore School will establish the centerpiece of our Envision Campus, and Envision Cayce's mixed income redevelopment approach to alleviating concentrated poverty.

Sincerely,

James E. Harbison
Executive Director

cc: MDHA Board of Commissioners
    Chief Executive Officer, The Martha O'Bryan Center
    President, Atwater Infrastructure Partners
    President, Johnson, Johnson and Crabtree (JJCA) Architects
    President, Purpose Built Communities, LLC