



Preparing the Supportive Housing Project Proforma

There are three key financial components to the development of any supportive housing project:

1. *RENTAL INCOME*: How much rent will the project generate?
2. *OPERATING COSTS*: How much will it cost to operate the project, year in, year out, over a period of time?
3. *DEVELOPMENT COSTS*: How much will it cost to build the project?

Oftentimes, the financial analysis of a housing development project begins with an examination of the development costs, the first costs that the developer will incur. For supportive housing development, however, it often makes sense to first consider the operating financial feasibility first, including clearly identifying the prospective tenants and the rent levels they can afford. The question: “Who will be served in this project?” should be answered early in the development process and the answer should align with both organizational mission and community need. Analyzing operating feasibility first will also help predict whether the project can afford to pay debt service on any loans that might be considered as sources to pay for development costs.

The Project Proforma

The tool used to analyze and present the overall financial feasibility of a housing development project is a “project pro forma.” Documenting the projections for the costs to build a project and to operate it over time, a project proforma is both:

- A financial plan for Operating a project
- A financial plan for Developing a project

The project pro forma will document the answers to two fundamental questions about a project’s Operating Feasibility:

- How much rental income will be generated?
- What expenses will need to be paid to operate the building, including reserves for future repairs or projected deficits?

The answers to these questions will help you to complete your Rent Roll and Operating Budget.

The project pro forma will document the answers to two fundamental questions about a project’s Development Feasibility:

- How much money will it cost to develop the project?
- What sources of money will be used to pay the development costs?

The answers to these questions will help you complete your Development Budget (also referred to as the “Sources & Uses” budget.)

Note: This document is included within the *Development and Finance* section of CSH’s *Toolkit for Developing and Operating Supportive Housing*, which is available at www.csh.org/toolkit2.

Components of the Proforma

Organizations without significant development experience or with little in-house capacity should consider engaging the services of a financial consultant or development consultant to “run the numbers” for the project pro forma and to help create a plan for a financially feasible project. All organizations engaging in supportive housing development, however, should have an understanding of the basic components of a project pro forma, which include:

1. **The rent roll**
2. **The operating budget and cash flow analysis**
3. **The development budget or “sources and uses” budget**

1. The Rent Roll:

Also sometimes referred to as Tenant Mix and Rental Income, Unit and Affordability Mix, or several other names, the key components of the Rent Roll are:

- The Number of Units
- The Breakdown of Units by Number of Bedrooms/Size
- The Breakdown of Units by Affordability - documenting the income groups (usually shown as a percentage of Area Median Income [AMI]), to which the units will be affordable or restricted
- The Rents for Units – both gross, and after any utility allowance (utility allowance calculations are available through local public housing authorities)
- The Income from dedicated Operating Subsidies – such as Shelter Plus Care or Project-Based Section 8 subsidies dedicated to the project
- The Vacancy Allowance – the percentage of units expected to be vacant at any given time

The Rent Roll will project how much annual income the supportive housing development can be expected to generate from rental income and any operating subsidies. A slightly simplified rent roll for a mixed income development (with sample utility allowances) might look like the following table:

# of Units	BR Size	% AMI	Gross Rent per unit /month	Subsidy Payments per unit /month	Utility Allow.	Net Rent per unit /month	Total Rent /Year	Vacancy Allow.	Net Rent /Year
20	1	30%	\$345	\$405	\$50	\$700	\$168,000	10%	\$151,200
10	1	40%	\$460	\$290	\$50	\$700	\$84,000	10%	\$75,600
30	2	60%	\$880	\$0	\$75	\$805	\$289,800	5%	\$275,310
60			\$1,688			\$2,380	\$456,300		\$502,110

Setting rent levels is a key element in creating the project pro forma, and must address the following considerations:

- Rents will need to match the regulatory requirements of the capital and operating funding program(s) being utilized in the project;
- The rents being charged need to be affordable to the people who will be living in the project. Setting unrealistic expectations regarding what a tenant with a limited income and a disability (or disabilities) can pay can result in a project going under due to lack of adequate occupancy and rental income; and
- The rental income generated needs to be in an adequate amount to cover the cost of operating the project.

Calculating Rent Levels

The most common scenarios under which rents must be calculated to provide affordability in accordance with funder requirements are:

- a. Calculating Rents for Fixed Rent Programs
- b. Calculating Rents for Income-Based Programs
- c. Calculating Rents with Fair Market Rent-based Programs

a. Calculating Rents for Fixed Rent Programs

Fixed rent programs establish a maximum rent for each unit size at each affordability level. Such programs include tax credits and tax-exempt bonds.

Program Max Monthly Gross Rent (20%AMI 1BR unit)	\$310
Less: Utility Allowance per Month	- \$50
Maximum Net Tenant Rental Payment	\$260

Example assumes a one-bedroom unit in Contra Costa County, California

b. Calculating Rents for Income-Based Programs

Income-based programs require tenant rents be based on a percentage of each tenant household’s actual income. In practice, property management staff calculates actual rents on a tenant-by-tenant basis. For the purpose of operating rental income projections, a conservative estimate of what the average tenant has in income should be used. Income-based programs, such as the federal Supportive Housing Program (SHP), typically set the rent plus utilities at approximately 30% of household income.

Estimated monthly tenant income (SSI)	\$700
Program affordability standard	<u>x .30</u>
Est. Maximum Gross Rent	\$210
Less: Utility Allowance per Month	- \$50
Maximum Net Tenant Rental Payment	\$160

c. Calculating Rents with Fair Market Rent-based Programs

When using rental subsidy programs that base their payment standard on Fair Market Rents (FMRs), the rents included in the pro forma for those units with this subsidy reflect the FMR levels. FMRs are published annually by HUD at <http://www.huduser.org/datasets/fmr.html>. Rent levels are published according to location and unit size (number of bedrooms). The tenant typically only pays 30% of their income or a similar calculation as their share of the rent, with the rental subsidy source paying the difference between that amount and the FMR. (Note: In October 2005, HUD published its [Final Rule on Project Based Vouchers](#), which establishes regulations under which project based rent levels are determined, including limitations for subsidy rent levels in units financed with low-income housing tax credits.)

Section 8 and Shelter Plus Care are examples of FMR-based rental subsidies. When using these programs for a project, it is often best to obtain “project based” assistance which means that the rental subsidy (or voucher) stays with the project. However, these subsidies may only be guaranteed to a project for a short term - a Section 8 contract can usually be granted for ten years (subject to annual allocations), and a Shelter Plus Care contract normally only extends out for five years. In both cases, these sources of funding can be renewed beyond the term of the original contracts, subject to availability of funding.

2. The Operating Budget and Cash Flow Analysis:

The **Operating Budget** documents the costs to operate the project for one year. This includes costs such as the property manager’s salary, a property management fee, utilities for common areas, landscaping, maintenance, and other related costs. Deposits to reserves should also be included as an operating cost. Supportive services costs are not usually included within the Operating Budget. Projecting the costs of operating the housing development is a critical task, and should be based on comparables from other projects, or if possible, actual costs to come up with the most realistic budget possible.

The **Cash Flow Analysis** is a multiple year analysis (usually either 15 or 30 years) that projects the rental income and how much money is left each year after the costs of property operations, any debt service costs, and reserves. An important assumption in a cash flow analysis is the percentage by which rental income and operating costs will increase each year. This financial concept is called “trending.” Funders of supportive housing projects typically assume that costs are increasing at a greater percentage than income each year. A fairly standard rate of increase for rents is 2% per year and 4% per year for operating costs. The 2% difference between these two rates is called the “spread.” Depending on the location of the project, funders will have different requirements for the spread between the percentage increase for rents and operating costs, and the spread requirements can be as low as 1%.

Projecting Cash Flow

The math needed for developing a cash flow projection for one year is:

- 1) Total annual rental income (aka “Gross Potential Income”)
- 2) LESS Vacancy Loss (usually 5% or 10% - check with your funders)
- 3) EQUALS Effective Gross Income (aka EGI)
- 4) LESS Operating Costs + Reserves (based on your operating budget)
- 5) EQUALS Net Operating Income (aka “NOI”)
- 6) LESS Mortgage Payment (if any)
- 7) EQUALS Cash Available
- 8) LESS Partnership Management Fees and/or Asset Management Fees
- 9) EQUALS Cash Flow for Residual Receipts Debt, and/or for your agency

To develop the multi-year analysis, the trending factors identified are applied to the Gross Potential Income and the Operating Costs for each year that the analysis covers.

Taken all together, this analysis will project whether there is (and will be in the future) enough rental income to meet the costs of operating the project. This analysis will also help determine whether there will be adequate cash flow after meeting operating costs that could be used for any costs associated with financing that may be used to pay for the development costs.

3. The Development Budget – Sources and Uses

A project’s **Development Budget** documents all of the costs involved in developing the project, including buying the land/building, new construction or rehabilitation activities, finance charges, professional services and agency costs (which can be included as the developer’s fee). A development budget is often broken down into the three phases:

- Predevelopment/Acquisition – the activities that occur before construction starts;
- Construction – the construction or rehabilitation of the property;
- Permanent – upon completion of construction when all of the funding that will remain in the project is in place.

The Sources and Uses Budget

Projecting all of these costs will produce the project’s “Total Development Cost” or TDC. Equally important is identifying adequate sources to cover the project’s TDC - together, these two components are often referred to as the **Sources and Uses** budget. The Sources and Uses budget will document how much the project will cost to develop, and how those costs will be financed - and the sources must always equal the total development costs for a project to be feasible. It is also

very important to be sure that the sources identified can actually be used for the costs for which they are expected to pay. Further, some funding sources will only be available for certain of the phases of the development process identified above - when identifying sources of funding, it is essential to be sure that there are adequate resources available during each of these phases.

The sources of development funding should be identified as early as possible in the development process. There are different types of sources (debt, grants and equity) that can be used for the different phases of a project's development. Some types of funding are more commonly used at certain stages of a project, and for particular uses. For example, short-term loans from non-profit intermediaries are commonly used for predevelopment expenses, while long-term loans from conventional banks or government agencies are used to pay for construction and other development costs and remain invested in the project as permanent financing. Equity and grant funding do not require repayment, whereas debt requires that the funding be repaid at some point in time, in accordance with a repayment schedule and with interest.

Typically, projects are funded with a combination of local, State and Federal resources. While there are localities and States that provide considerable funding for supportive housing projects, the Low Income Housing Tax Credit Program is one of the biggest funders of affordable and supportive housing. Projects using tax credits are typically larger-sized projects (20 units or more in most locations, even larger projects in many places.). The tax credit program, which is authorized under the Internal Revenue Code, is complicated and most tax credit financed projects are developed by experienced developers. Using tax credits adds additional compliance regulations and requirements that will impact how the project's other sources of funding are structured as well.

9% tax credits have traditionally been the most widely used form of tax credits as they yield a substantial amount of equity funding. However, it is also possible to use 4% tax credits in supportive housing development, typically used in conjunction with tax exempt bonds, which act like low interest debt in a project. This structure is somewhat complex and requires the involvement of attorneys and financial advisors.

Note: CSH's *Toolkit for Developing and Operating Supportive Housing* contains many other documents that may be useful for understanding supportive housing financing issues. Please see the tools under *Assembling the Financing* in the *Development and Finance* section of the *Toolkit*, at www.csh.org/toolkit2development.