

Technical Memorandum: Preliminary Financial Feasibility Analysis Historic Restoration of Pennhurst



Prepared for:

Pennhurst Memorial & Preservation Alliance

and

Preservation Alliance for Greater Philadelphia

Prepared by:

Urban Partners

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Background

The Pennhurst Memorial & Preservation Alliance and the Preservation Alliance for Greater Philadelphia have great interest in securing the historic restoration of a significant portion of the former Pennhurst State School and Hospital Complex. This historic 112-acre campus of over twenty Jacobean Revival buildings is located in East Vincent Township, Chester County, Pennsylvania. The analysis included in this report focuses on assessing the financial feasibility of restoring a core grouping of 11 buildings within the overall complex. These 11 buildings include approximately 360,000 SF of gross building space and utilize about one-quarter of the total Pennhurst site. As a result, at least 75 acres of land would be available for other uses.

In preparing this report, Urban Partners conducted an initial scan of real estate market conditions in the trade area which includes East Vincent. This scan focused on office and residential uses which could (1) utilize a significant portion of the multi-story buildings in the complex; (2) generate sufficient income to support the historic restoration of those buildings; and (3) result in an ownership structure that could benefit from the likely equity investment that could be derived from utilization of historic tax credits.

Uses likely to meet these criteria include continuing care communities and other senior services complexes, rental housing, and office. The market for office space in the area does not appear to be sufficiently large to support any significant restoration of the Pennhurst buildings. CCRCs and other senior service facilities will require elevators in each building and substantial retrofits to the tunnel complex. These costs appear to be prohibitive. Rental housing, on the other hand, is expected to be a growing market within the Pennhurst Trade Area and could be readily accommodated within the key buildings in the complex.

As a result of this scan, the financial feasibility analysis included in this report assesses restoration for rental housing. We should note that the high quality of the residential product produced through this restoration would be attractive for conversion to condominium ownership after the five-year holding period required for use of historic tax credits.

Assumptions

This analysis is based on the following assumptions:

- Overall population and housing growth in the trade area surrounding Pennhurst will be consistent with the forecasts of the Delaware Valley Regional Planning Commission;
- The historic restoration of the eleven buildings identified in this analysis will provide a sufficient mass of restoration to qualify that effort for use of federal historic tax credits as well as for any benefits that might be derived from dedication of façade easements; and
- The portion of the complex utilized for the rental housing development can be separated from other activities on the site in a manner that provides a quality residential environment without undo noise, odor, dust, etc.

Rental Housing Market

East Vincent Township and the surrounding ten jurisdictions collectively had a population in 2010 of nearly 86,000 people (see **Table 1**). The Delaware Valley Regional Planning Commission (DVRPC) forecasts 16.8% population growth in these eleven jurisdictions through 2025. This growth will require the addition of approximately 6,800 housing units in the area, of which we anticipate 35% or 2,400 units will be for the rental market.

Table 1
Pennhurst Housing Trade Area
Population & Housing Demand Forecast 2010-2025

| Municipality | Population | | | | |
|----------------------------|------------|----------------|----------------|----------------|-------------------------|
| | 2010 | 2015 (Est.) | 2020 (Est.) | 2025 (Est.) | % Change (2010-2025) |
| Charlestown Township | 5,671 | 6,929 | 7,505 | 8,054 | 42.0% |
| Schuylkill Township | 8,516 | 8,748 | 9,258 | 9,739 | 14.4% |
| Phoenixville Borough | 16,440 | 16,323 | 16,748 | 17,153 | 4.3% |
| W. Pikeland Township | 4,024 | 4,768 | 5,023 | 5,267 | 30.9% |
| E. Pikeland Township | 7,079 | 7,905 | 8,414 | 8,899 | 25.7% |
| W. Vincent Township | 4,567 | 4,369 | 4,581 | 4,758 | 4.2% |
| E. Vincent Township | 6,821 | 7,496 | 8,047 | 8,573 | 25.7% |
| Spring City Borough | 3,323 | 3,522 | 3,690 | 3,851 | 15.9% |
| E. Coventry Township | 6,636 | 6,625 | 7,035 | 7,427 | 11.9% |
| Royersford Borough | 4,752 | 4,603 | 4,717 | 4,824 | 1.5% |
| Limerick Township | 18,074 | 19,304 | 20,590 | 21,802 | 20.6% |
| Total | 85,903 | 90,592 | 95,608 | 100,347 | 16.8% |
| Growth From 2010 | | 4,689 | 9,705 | 14,444 | |
| Incremental Housing Demand | | 2,200 | 4,600 | 6,800 | |
| Rental Housing Share (35%) | | 800 | 1,600 | 2,400 | |

Source: U. S. Census; Delaware Valley Regional Planning Commission; Urban Partners

Multi-family residential building permit activity in these eleven jurisdictions was minimal in the 2006 to 2010 period. Only 447 units were permitted—90% of which were in 2006 and 2007.

This information—anticipated population growth and low levels of recent investment—suggest that new rental housing product can be absorbed in the trade area at the rate of approximately 160 units per year for the next 15 years.

Urban Partners surveyed 18 rental housing complexes in these eleven jurisdictions for unit mix, rent levels, and availability. On **Table 2**, we detail current conditions at the five highest quality complexes in the area, representing over 1,000 apartment units. These five complexes include between 136 and 260 units each and provide a mix of one-, two-, and three-bedroom units. In general, these complexes are fully occupied with moderate monthly turnover.

**Table 2
 Pennhurst Housing Trade Area
 Competitive Rental Housing Developments**

| Property | Municipality | BR | BA | SF | Rent | Rent/SF | Availability 9-1-11 | # Units In Complex |
|----------------------|--------------|-------|---------|--------|---------|---------|---------------------|--------------------|
| Madison at Westridge | Phoenixville | 1 | 1 | 840 | \$1,124 | \$1.34 | Two | 136 |
| | | 1 | 1 | 840 | \$1,135 | \$1.35 | | |
| | | 2 | 2 | 1,026 | \$1,282 | \$1.25 | Zero | |
| | | 2 | 2 | 1,026 | \$1,296 | \$1.26 | | |
| | | 2 | 2 | 1,058 | \$1,311 | \$1.24 | | |
| | | 2 | 2 | 1,058 | \$1,325 | \$1.25 | | |
| | | 3 | 2 | 1,166 | \$1,508 | \$1.29 | Zero | |
| | | 3 | 2 | 1,166 | \$1,529 | \$1.31 | | |
| Oxford Riverwalk | Royersford | 1 | 1 | 808 | \$1,013 | \$1.25 | | 216 |
| | | 1 | 1 | 882 | \$1,298 | \$1.47 | | |
| | | 2 | 2 | 1,055 | \$1,227 | \$1.16 | | |
| | | 2 | 2 | 1,506 | \$1,442 | \$0.96 | | |
| | | 3 | 2 | 1,370 | \$1,775 | \$1.30 | | |
| | | 3 | 2 | 1,396 | \$1,775 | \$1.27 | | |
| Chestnut Pointe | Limerick | 1 | 1 | 800 | \$1,325 | \$1.66 | One or two | 192 |
| | | 1 | 1 | 865 | \$1,235 | \$1.43 | | |
| | | 1 | 1 | 865 | \$1,255 | \$1.45 | | |
| | | 2 | 2 | 1,100 | \$1,510 | \$1.37 | Some | |
| | | 2 | 2 | 1,100 | \$1,540 | \$1.40 | | |
| | | 2 | 2 | 1,166 | \$1,550 | \$1.33 | | |
| | | 2 | 2 | 1,166 | \$1,690 | \$1.45 | | |
| | | 3 | 2 | 1,350 | \$1,860 | \$1.38 | Some | |
| 3 | 2 | 1,350 | \$1,990 | \$1.47 | | | | |
| Walnut Crossing | Limerick | 1 | 1 | 750 | \$1,062 | \$1.42 | | 260 |
| | | 1 | 1 | 750 | \$1,170 | \$1.56 | | |
| | | 2 | 1 | 960 | \$1,330 | \$1.39 | | |
| | | 2 | 1 | 960 | \$1,350 | \$1.41 | | |
| | | 2 | 2 | 980 | \$1,284 | \$1.31 | | |
| | | 2 | 2 | 980 | \$1,390 | \$1.42 | | |
| | | 2 | 2 | 1,095 | \$1,302 | \$1.19 | | |
| | | 2 | 2 | 1,095 | \$1,430 | \$1.31 | | |
| | | 3 | 3 | 1,300 | \$1,730 | \$1.33 | | |
| Summer Chase | Limerick | 1 | 1 | 714 | \$1,090 | \$1.53 | | 198 |
| | | 1 | 1 | 910 | \$1,250 | \$1.37 | | |
| | | 2 | 2 | 975 | \$1,290 | \$1.32 | | |
| | | 2 | 2 | 1,099 | \$1,475 | \$1.34 | | |
| | | 2 | 2 | 1,157 | \$1,525 | \$1.32 | | |
| | | 2 | 2 | 1,244 | \$1,555 | \$1.25 | | |
| | | 2 | 2 | 1,327 | \$1,610 | \$1.21 | | |
| | | 3 | 2 | 1,400 | \$1,790 | \$1.28 | | |
| | | 3 | 2 | 1,495 | \$1,805 | \$1.21 | | |

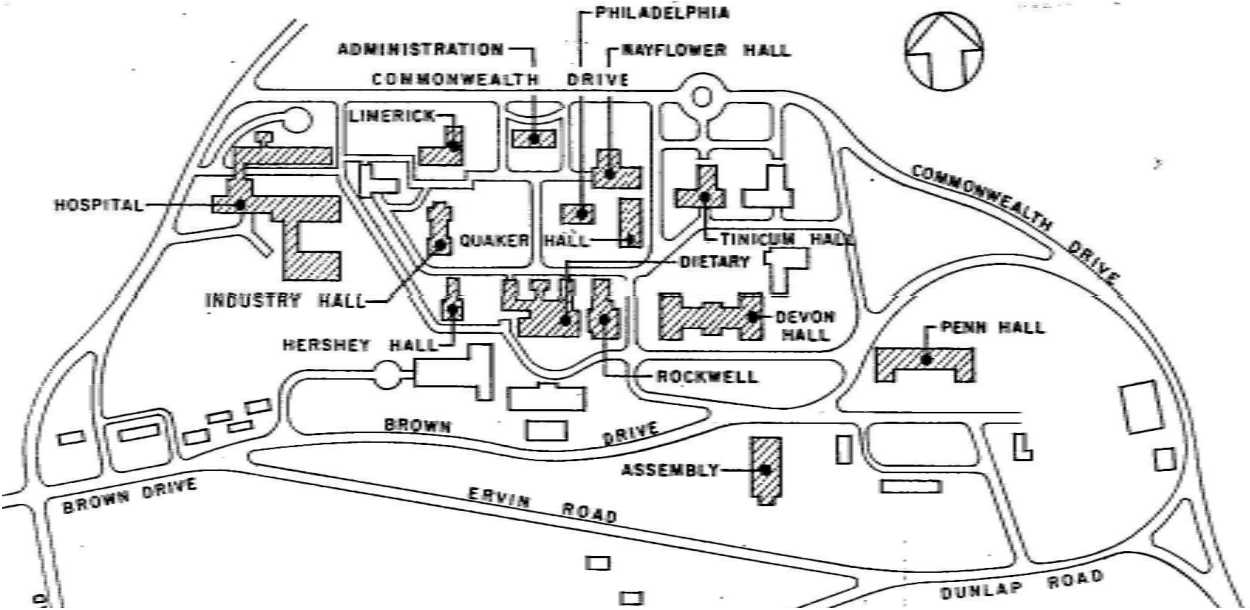
Source: Urban Partners

Current rent levels are generally \$1,100 to \$1,300 per month for 700 to 900 square foot one-bedrooms; \$1,300 to \$1,700 per month for 1,000 to 1,175 square foot two-bedrooms; and \$1,700 to \$2,000 per month for 1,300 to 1,400 square foot three-bedroom units.

Potential Rental Housing Development

A core cluster of 11 buildings have been identified as candidates for historic restoration as a rental housing complex. These eleven buildings include:

- Administration;
- Limerick;
- Mayflower;
- Industry;
- Philadelphia;
- Quaker;
- Tinicum;
- Hershey;
- Rockwell;
- Devon; and
- Penn.



On **Table 3**, we show the building characteristics for these 11 buildings as estimated by the Community Design Collaborative project team for its work in 2010. This data has been adjusted by Urban Partners from photographic documentation and floor plans to eliminate some redundancies and to estimate usable attic areas (those with sufficient ceiling heights and windows).

The gross floor space for the eleven buildings is 358,362 SF. Approximately 55% of the attic space appears to be usable for residential purposes, yielding a total usable space of 322,309 SF. No attempt has been made to layout individual apartments; however, we have assumed that 85% of first floor

space; and 88% of basement and second floor space is rentable for residential use. This yields 286,538 SF of rentable area in the eleven buildings.

Table 3
Pennhurst Historic Restoration for Rental Housing
Building Characteristics

| Building | Gross | Total Usable | Rentable-- 1st/2nd/Attic | Rentable-- Basement | Basement Gross | First Gross | Second Gross | Attic Gross | Attic Rentable |
|----------------|---------|--------------|--------------------------|---------------------|----------------|-------------|--------------|-------------|----------------|
| Administration | 29,272 | 24,082 | 14,862 | 6,376 | 7,246 | 7,246 | 7,390 | 7,390 | 2,200 |
| Limerick | 34,792 | 33,052 | 22,006 | 7,654 | 8,698 | 8,698 | 8,698 | 8,698 | 6,958 |
| Mayflower | 36,112 | 34,306 | 22,840 | 7,945 | 9,028 | 9,028 | 9,028 | 9,028 | 7,222 |
| Industry | 23,182 | 22,040 | 14,441 | 5,331 | 6,058 | 5,708 | 5,708 | 5,708 | 4,566 |
| Philadelphia | 14,448 | 12,436 | 7,849 | 3,179 | 3,612 | 3,612 | 3,612 | 3,612 | 1,600 |
| Quaker | 27,440 | 24,330 | 15,618 | 6,037 | 6,860 | 6,860 | 6,860 | 6,860 | 3,750 |
| Tinicum | 32,628 | 26,171 | 15,812 | 7,178 | 8,157 | 8,157 | 8,157 | 8,157 | 1,700 |
| Hershey | 26,560 | 25,232 | 16,799 | 5,843 | 6,640 | 6,640 | 6,640 | 6,640 | 5,312 |
| Rockwell | 25,200 | 22,200 | 14,199 | 5,544 | 6,300 | 6,300 | 6,300 | 6,300 | 3,300 |
| Devon | 83,072 | 72,804 | 46,429 | 18,276 | 20,768 | 20,768 | 20,768 | 20,768 | 10,500 |
| Penn | 25,656 | 25,656 | 14,795 | 7,526 | 8,552 | 8,552 | 8,552 | | |
| Total | 358,362 | 322,309 | 205,649 | 80,889 | 91,919 | 91,569 | 91,713 | 83,161 | 47,108 |

Source: Community Design Collaborative; Urban Partners

For purposes of estimating financial feasibility, we have assumed that a unit mix of approximately 40% one-bedroom/50% two-bedroom/10% three-bedroom would be desirable. We have further assumed that, given the high ceilings and attractive historic features, apartments on upper floors will achieve rents at or somewhat above the top of the current market. Therefore, our analysis assumes average rents of:

- \$1,325 per month for 800 SF one-bedroom units;
- \$1,650 per month for 1,075 SF two-bedroom units; and
- \$1,975 per month for 1,350 SF three-bedroom units.

As shown on **Table 4**, we estimate that the rentable space in the eleven buildings will allow for 196 units on the upper floors renting at these premium prices—46 one-bedrooms, 122 two-bedrooms, and 28 three bedroom units.

It appears that another 90 units—56 one-bedrooms and 34 two-bedrooms—can be accommodated in the basements of the 11 buildings. Due to the smaller, high-placed windows in these basement units, we believe they will rent at pricepoints near the bottom of the current luxury market:

- \$1,125 per month for 800 SF one-bedroom units; and
- \$1,425 per month for 1,075 SF two-bedroom units.

Table 4
Pennhurst Historic Restoration for Rental Housing
Housing Unit Potential

| Building | Total Units | Basement-- | Basement-- | Upper-- | Upper-- | Upper-- |
|----------------|-------------|------------|------------|-----------|------------|-----------|
| | | 1-BR | 2-BR | 1-BR | 2-BR | 3-BR |
| Administration | 21 | 4 | 3 | 3 | 9 | 2 |
| Limerick | 31 | 3 | 5 | 10 | 13 | 0 |
| Mayflower | 32 | 6 | 3 | 7 | 16 | 0 |
| Industry | 18 | 4 | 2 | 0 | 6 | 6 |
| Philadelphia | 10 | 4 | 0 | 0 | 1 | 5 |
| Quaker | 22 | 1 | 5 | 6 | 10 | 0 |
| Tinicum | 23 | 5 | 3 | 3 | 10 | 2 |
| Hershey | 24 | 6 | 1 | 5 | 12 | 0 |
| Rockwell | 17 | 3 | 3 | 0 | 2 | 9 |
| Devon | 66 | 16 | 5 | 11 | 30 | 4 |
| Penn | 22 | 4 | 4 | 1 | 13 | 0 |
| Total | 286 | 56 | 34 | 46 | 122 | 28 |

Source: Urban Partners

Financial Feasibility

On **Table 5**, we undertake a typical annual income and expense analysis for this development based on stabilized occupancy at 2011 pricing. For this analysis, we assume the 286 units detailed on Table 4 at the rent levels discussed above. This yields total gross rents of \$5.148 million annually. Adjusting for 4% vacancy and operating expenses, net operating income is estimated at slightly below \$3.7 million per year. This income stream will support \$46 million in first mortgage debt at 5% interest on a 30-year amortization and provide a 4.51% return on \$16 million in long-term invested equity seeking a cash return. This 4.51% return on economic equity would be expected to grow substantially from year-to-year as net operating income increases.

Table 5
Pennhurst Historic Restoration for Rental Housing
Income & Expense Analysis

| | Units | Rent | Income |
|--|-------|---------|-------------|
| One-Bedroom Upper Floors | 46 | \$1,325 | \$731,400 |
| One-Bedroom Basement | 56 | \$1,125 | \$756,000 |
| Two-Bedroom Upper Floors | 122 | \$1,650 | \$2,415,600 |
| Two-Bedroom Basement | 34 | \$1,425 | \$581,400 |
| Three-Bedroom Upper Floors | 28 | \$1,975 | \$663,600 |
| Total Gross Rents | | | \$5,148,000 |
| Vacancy | 4% | | \$206,000 |
| Taxes--\$2300 Per Unit | | | \$658,000 |
| Maintenance & Operation--\$2100 Per Unit | | | \$600,000 |
| Net Operating Income | | | \$3,684,000 |
| Debt Service (\$46 Million/5%/30 Year) | | | \$2,963,000 |
| Cash Flow | | | \$721,000 |
| Return on Economic Equity (\$16 Million) | | | 4.51% |

Source: Urban Partners

Table 6 details the expected development costs for these 11 buildings as rental housing.

Table 6
Pennhurst Historic Restoration for Rental Housing
Development Budget
August, 2011

Development Budget

| | | |
|--|-------------------|--------------|
| Site Acquisition | | \$2,000,000 |
| Construction | | |
| Demolition/Environmental Remediation | 358,362 SF @ \$15 | \$5,375,000 |
| Structure | 358,362 SF @ \$48 | \$17,200,000 |
| HVAC | 322,309 SF @ \$18 | \$5,800,000 |
| Interior Finishes | 322,309 SF @ \$30 | \$9,675,000 |
| Electrical | 322,309 SF @ \$13 | \$4,200,000 |
| Plumbing Systems | 322,309 SF @ \$15 | \$4,825,000 |
| Fire Suppression Systems | 358,362 SF @ \$5 | \$1,800,000 |
| Contractor Fee/Construction Management | | \$12,225,000 |
| Historic Street Lights | | \$1,000,000 |
| Parking & Landscaping | 600 Spaces | \$1,200,000 |
| Site Improvements | | \$1,500,000 |
| Contingency (10%) | | \$6,500,000 |
| Total Construction | | \$71,300,000 |
| Project Soft Costs | | |
| Architecture/Engineering | | \$5,000,000 |
| Legal | | \$400,000 |
| Accounting/Audit | | \$30,000 |
| Tax Credit Equity Legal/Accounting | | \$250,000 |
| Appraisal, Title & Closing | | \$30,000 |
| Taxes, Insurance & Utilities | | \$90,000 |
| Construction Interest | | \$3,000,000 |
| Financing Fees (1.5%) | | \$1,200,000 |
| Marketing | | \$50,000 |
| Soft Cost Contingency (7%) | | \$700,000 |
| Project Management/Development Fee | | \$4,000,000 |
| Total Soft Costs | | \$14,750,000 |
| Total Development Costs | | \$88,050,000 |

Sources of Financing

| | |
|---------------------------------|--------------|
| First Mortgage | \$46,000,000 |
| Tax-Credit Equity | \$15,600,000 |
| Economic Equity | \$16,000,000 |
| Total Economics-Based Financing | \$77,600,000 |
| Financing Gap Before Grants | \$10,450,000 |

Source: National Trust Community Investment Corporation; Urban Partners

We estimate **total development costs at slightly above \$88 million, or approximately \$308,000 per unit.** As noted above, the annual income and expense analysis suggests that \$3.7 million in net operating income can support \$46 million in first mortgage debt and \$16 million in economic equity.

Assuming federal historic tax credits are available for this development, another \$15.6 million can be expected to be raised from investors seeking the use of those tax credits. These three sources would yield **approximately \$77.6 million in funding sources.**

There remains a \$10.45 million financing gap that would need to be met through grant funding, real estate tax incentives, a state historic tax credit program, and/or other sources.

Based on this analysis, it appears that the historic restoration of these 11 core buildings as rental housing is feasible subject to:

1. the continued availability of federal tax credits and of investors desiring to utilize these tax credits;
2. the securing of \$10.45 million in grant or other funding to meet the identified financing gap; and
3. the identification of a substantial rental housing developer capable of undertaking a development of this scale.