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Historic Renovation of the Russel Erskine

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Financial Challenges and Structure

At the time that New Russel Erskine, L.P., the current owners of the Russel Erskine building, initially started pursuing the property, it was on the verge of foreclosure, occupancy had fallen to historic lows, the rental subsidy provided by the United States Department of Housing and Urban Development (HUD) was due to expire, and the future of the building itself appeared to be in jeopardy.

If that wasn't enough, the apartments had become functionally obsolete, the heating and air conditioning system was in dangerously poor condition, roofs leaked and the reserve for replacement, a fund set up to pay for capital improvements, had been depleted. In addition, it was necessary to bring the property into conformance with current fire codes and to mitigate asbestos, lead-based paint, and other environmental hazards.

The total cost to perform the work necessary to renovate the apartments, cure deferred maintenance, bring the property up to code and mitigate the environmental hazards was estimated to be in excess of $4 million. However, those costs did not include over $1 million in improvements that New Russel Erskine, L.P. felt were necessary to compete effectively in the marketplace for the long term, provide for the specific needs of its tenancy, and preserve the historical significance of the property.

In order to acquire the property, complete the planned historic renovation, and ensure the long-term viability of the development, New Russel Erskine, L.P. needs to secure over $11 million in debt and equity financing. Ultimately, the financing plan involves four federal, two state, and one city agency, each with its own set of unique requirements and approvals. It is estimated that, when complete, it will have taken nearly eighteen months to put it all together.

The first and most complicated piece of the financing plan was to restructure the existing Section 8 contract and government-insured debt. Working closely with the Jefferson County Assisted Housing Corporation in its capacity as the agent for HUD's Office of Multifamily Housing Assistance Restructuring (OMHAR), a restructuring proposal was submitted under OMHAR's Mark-to-Market Program in January 2004. The key aspects of that proposal include a new twenty-year, site-based Section 8 contract at post-renovation market rents and a new, cash flow second mortgage, the proceeds of which will be exactly the amount needed to pay off the existing debt encumbering the property. In June 2004, OMHAR's Production Office Loan Committee approved the restructuring proposal. The proposal had its last hurdle in front of the OMHAR Headquarters Loan Committee in early July 2004.

With the cash flow generated by a new Section 8 contract at post-renovation market rents, the development will be able to safely support a new first mortgage. Because a government-insured loan will provide the most proceeds for the property, New Russel Erskine, L.P., in conjunction with Highland Mortgage in Birmingham, Alabama, recently submitted an application for mortgage insurance to the HUD field office in Birmingham.

In early June 2003, New Russel Erskine, L.P. submitted an application for federal low-income housing tax credits under a program administered by the states in which awardees receive federal tax credits based on certain qualified acquisition and rehabilitation costs. Successful applicants are then able to raise equity capital for affordable housing developments by selling those tax credits to corporations.

The Alabama Housing Finance Authority, in October 2003, allocated $5,934,350 in low-income housing tax credits for the acquisition and historic renovation of the Russel Erskine building. Subsequent to receiving that award, New Russel Erskine, L.P. was able to raise in excess of $4.5 million in equity capital by selling those tax credits to a nationally known syndicator.

In addition to the low-income housing tax credits, New Russel Erskine pursued an allocation of historic tax credits for the property. Mike Holbrook from the firm of Fuqua Osborn Architects, the project architect, working in close consultation with Chloe Mercer of the Alabama Historical Commission, the state historic preservation office (SHPO), prepared the Part II submission, which was delivered to SHPO in February 2004. SHPO approved the application in March 2004 and the National Park Service provided a contingent approval of the Part II submission in April 2004.

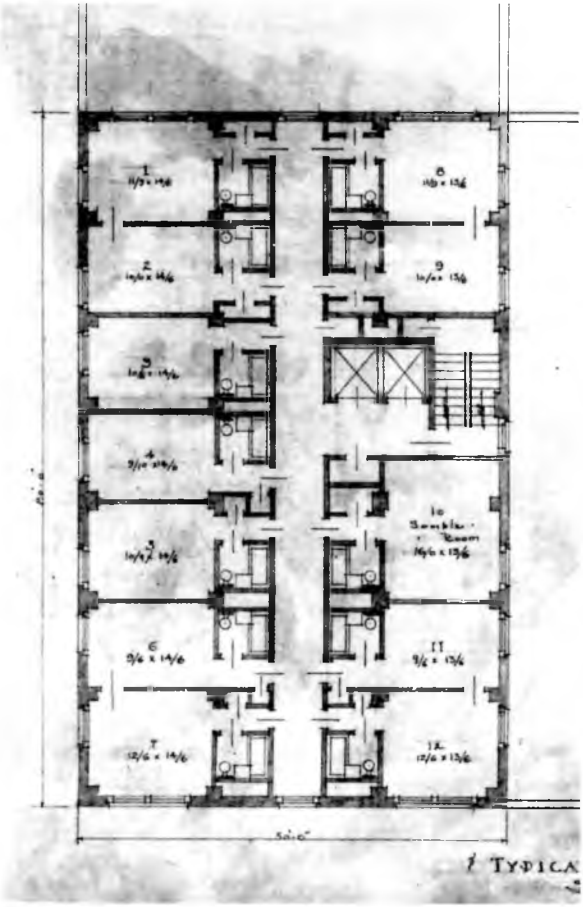
The entire approval process for the Part II application took less than two months, allowing New Russel Erskine, L.P. to secure nearly $1.5 million in additional equity capital for the renovation. The additional equity raised from the sale of the historic tax credits was the key to the financial viability of the rehabilitation effort.

New Russel Erskine, L.P. estimates that the additional work required to obtain the Part II approvals was less than $400,000, primarily due to a requirement to keep and repair, rather than replace, the windows. However, the benefits of utilizing the historic credits far outweighed the cost, a testament to the completeness of the owner's overall concept and the architect's design.

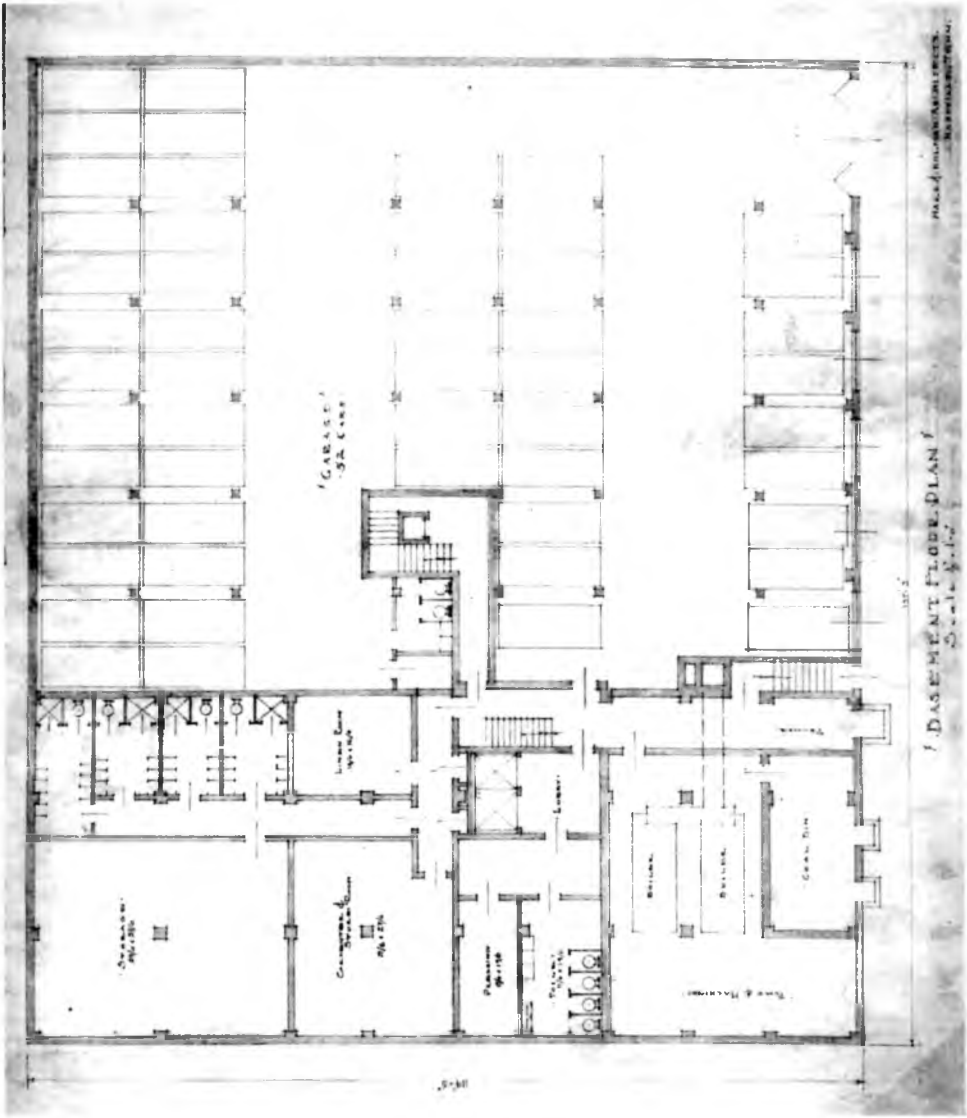
Last, and certainly not least, the City of Huntsville, through Jerry Galloway and the Office of Community Development, has played an instrumental role in helping New Russel Erskine, L.P. save and improve the Russel Erskine building. New Russel Erskine, L.P. believes that the city's strong support of the development and desire to preserve the property as affordable housing for senior citizens played a pivotal role in its ability to secure a significant portion of the financing described above. In addition, the city has agreed to provide a small loan to assist in the renovation. Without the city's support and timely response to code and fire issues that arose during the planning stages, New Russel Erskine would not have been able to get where it is today.

As of this writing, New Russel Erskine, L.P. hopes to close all of its financing and commence construction later this year with the hopes of unveiling a "new" Russel

Erskine building a year later. The owners and development team are excited about their plans for the building and look forward to working together with the city, SHPO, the building's residents and other interested parties in returning the Russel Erskine building to its former glory.



Detail, working drawings of Marr & Holman floor plans for typical guest rooms. Courtesy Fuqua Osborn Architects



Working drawings of Marr & Holman floor plans for basement. Courtesy Fuqua Osborn Architects

Ballroom entrance, 2004. Courtesy Fuqua Osborn Architects