

## Schochet Associates Affordable Housing Acquisition Fund

### Investment Objective:

The objective of the Schochet Associates Affordable Housing Acquisition Fund is to deliver a low risk, long term investment that offers total returns dramatically above comparable US Treasuries while simultaneously allowing investors to participate in the upside inherent in well located, well managed residential real estate. The Fund will invest in HUD-assisted projects in strong markets which are at or nearing the end of their contractual affordability period. Projects acquired will be those which are covered under expiring project based Section 8 Contracts and which have the potential to be renewed at very favorable terms by agreement between HUD and the Fund as project owner.

Under the terms of the contracts, each resident pays 30% of his/her income toward rent, with HUD providing the difference up to the market rent. **Typically, 80% to 85% of all rents collected at a property of this type will be paid by HUD. This government backing provides a high degree of safety and consistency of cash flow to the projects, and through the projects, to investors.**

**Project Based Section 8 contracts also deliver protection against operating cost increases while simultaneously providing opportunities to participate in changing market conditions.** Under HUD's "mark-up-to-market" (MUTM) program, established in 1999 as an incentive for owners to preserve Project Based Section 8 housing, projects covered under Section 8 contracts receive automatic cost of living (OCAF) adjustments annually. These annual rent increases are authorized and funded by HUD, thereby protecting projects of this type from short-term cost spikes which might not otherwise be able to be passed on to tenants. Moreover, the projects in which the Fund will invest will typically have waiting lists of at least six months (very often as long as two years), thereby ensuring minimum vacancies regardless of market conditions.

**The opportunity for owners to participate in increases in market value over time comes from the MUTM program's provisions allowing for adjustments of rents every five years to then-current market levels.** As with cost of living increases, any rent increases resulting therefrom are authorized and funded by HUD, with no adverse impacts on the residents. The potential for rising rents is especially strong in today's markets as the sub-prime debt crisis deepens, single family home building continues to lag, and demand for rental housing grows.

### The Challenge:

As construction costs rise, homebuilding slows, credit markets tighten thereby limiting new multifamily construction, and more and more individuals and families either lose their homes to foreclosure or are unable to borrow, apartment markets around the country are expected to tighten dramatically over the next several years. The result will likely be a return to rapidly increasing rents, putting ever larger numbers of senior citizens and low income families at risk of losing their housing. At the same time a growing number of federally subsidized housing units are reaching the end of their affordability periods and are at risk of being "taken to market," ultimately depleting the nation's stock of subsidized housing. This phenomenon is not limited to just a few selected markets, but is a nationwide problem that will grow worse due to the imminent expiration of Federal subsidies covering more than 1.5 million housing units across the nation. According to the National Housing Trust private owners have already taken to market more than 300,000 previously subsidized housing units which are lost to the affordable housing stock forever.

The National Low Income Housing Coalition has summed up best the current state of subsidized housing, "Like a high stakes game of musical chairs, the number of poor renters remains the same and they must compete for a diminishing number of affordable places to live." In fact, the situation may be worse than this, as the number of poor renters continues to increase.

### **The Opportunity:**

Against this backdrop, as owners opt out of project based Section 8 contracts these housing units are not being replaced. Since the early 1990's when the oldest contracts began to expire and owners in strong markets began to opt out, HUD has offered a series of increasingly generous plans to incent owners to maintain affordability.

Notwithstanding these efforts, more than 300,000 previously HUD assisted units have been taken to market over the last decade making the project based Section 8 contract a depleting resource, the value of which increases daily. **For those who understand the dynamics of this marketplace, the opportunity exists to identify, purchase, and preserve tens of thousands of units nationwide, while earning exceptional returns on a risk adjusted basis.**

### **Deal Structure:**

The fund seeks to raise \$50 million dollars in equity, which, when combined with the appropriate leverage will allow a total transaction value of up to \$250 million.

Investors in the fund will be entitled to all operating cash flow and all net proceeds from sales or refinancings until their entire investment has been returned to them along with a total return (IRR) of 10% per year (on a look back basis). At that time, investors will be entitled to 75% of all future project cash flows along with 75% of net proceeds from any subsequent sales or refinancings. It is estimated that investors will receive total returns over the entire holding period of more than 13%, with cash on cash pay rates starting at between 4.5% and 6% in the first year, and increasing annually to 10% to 12% in the tenth year.

**By taking advantage of the subsidies available as described above, the Fund can significantly minimize vacancy, collections, and operating risks while offering the upside associated with well located, well managed residential real estate.** As with many real estate investments, the Fund's returns will be partially sheltered from income taxes.

### **The Sponsor:**

The Fund is a to-be-formed Massachusetts entity which will be sponsored by Schochet Associates. Schochet Associates has over thirty five years experience developing, financing and managing multifamily residential projects, and currently owns and/or manages 3,750 apartments and 250,000 square feet of commercial space throughout New England. Since 2000, Schochet (and/or its affiliated companies) has completed affordable housing transactions valued at over \$250 million.

### ***For more information please contact:***

Richard J. Henken  
President  
Schochet Associates  
Richard.Henken@schochet.com  
617-398-5105

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