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Chicago's Covent Apartments Makes Math Work with HTCs, LIHTCs

NICK DECICCO, SENIOR WRITER, NOVOGRADAC

When Veronica Gonzalez sought investors to rehabilitate a century-old hotel on a prized piece of North Side Chicago real estate, she had a surprisingly difficult time finding collaborators. The property has a large commercial component making it extraordinarily complex. Investors would need to factor in unusual depreciation assumptions.

Gonzalez spoke to investors who were initially intimidated by the complexity of the underwriting. "One investor flat out told me, 'No, girl, I can't do it,'" said Gonzalez, Midwest development director for nonprofit developer NHP Foundation.

Still, Gonzalez persevered, tapping longtime NHP collaborator R4 Capital to invest a combined \$7.9 million in low-income housing tax credit (LIHTC) and historic tax credit (HTC) equity to make The Covent Apartments a reality. The \$21.6 million renovation will turn the 64 single-room occupancy (SRO) Covent Hotel into 30 permanent supportive apartments for those earning up to 30% and 50% of the area median income (AMI).

Image: Courtesy of NHP Foundation

An artist's rendering looks southwest down West Drummond Place in Chicago's Lincoln Park neighborhood at a new construction apartment complex. Lincoln Park Drummond Group will construct the seven-story building atop parking lot.

The site includes ground-floor commercial space. Adam Cohen, senior vice president for R4 Capital, said balancing the depreciation assumptions for the commercial property with the permanent supportive housing component was the greatest challenge in making the transaction pencil out.

“Veronica and I sent spreadsheets back and forth,” Cohen said. “We know that NHP knows their stuff. We know that NHP stands behind their projects. Having a partner in this where we know they’re not going to close a deal and if we run into problems, they run away. ... You want somebody who isn’t going to leave you high and dry if something goes sideways.”

Construction began in September 2022 and is due for completion this September.



Image: Courtesy of NHP Foundation

A look at the exterior of the Covent Hotel building in the Lincoln Park neighborhood of Chicago from the northwest corner of North Clark Street and West Drummond Place. The site is being turned into permanent supportive housing with a capital stack that includes historic tax credits and low-income housing tax credits.

Got Angels All Around Me

The Covent Hotel was built in 1915. The classical revival-style hotel resides in Chicago’s Lincoln Park neighborhood, which has transformed from one of the Windy City’s poorest areas in the mid-20th century to one of its most affluent in modern times. Gonzalez knew what a rare opportunity she had.

“This is one of very few undeveloped pieces in Lincoln Park,” Gonzalez said. “An opportunity like this was not going to come quickly or come again any time soon. It was very opportunistic in that respect.”

Cohen agreed. “When you’re looking at housing, especially for homeless individuals in a neighborhood

like Lincoln Park where gentrification is such an issue and loss of affordable housing stock is such an issue, it’s an opportunity that you really want to jump at because there’s not that many opportunities to do projects like that,” Cohen said.

Maintaining the lifespan of SRO sites matches the goals of the city, which passed an SRO preservation ordinance in 2014.

The Illinois Housing Development Authority (IHDA) Supportive Housing Funding brought nearly \$3.1 million to The Covent Apartments.

“We call it a Frankenstein jokingly,” Gonzalez said. “We know these are difficult deals. When you come to [the city] and say you want to recapitalize an SRO, they know. IHDA knew. It’s not that it was us. It’s one of those deals. You can’t hide from them. Eventually everyone has to sit at the table and figure out how to get them done. It’s a challenge, but the will has to be there. We wouldn’t have got this done with \$5 million from soft debt and bonds, \$3 million from IHDA. Those are not small amounts.”

Gonzalez said because Lincoln Park is a high-market area and a neighborhood with many amenities, it raised the stakes for success for a property and a population served by permanent supportive housing.

“The minute you go out of that 30% to 60% AMI expertise, you’ve got to cut your teeth well and know you’re doing it the right way,” Gonzalez said.

Gonzalez said the partnership with the Corporation for Supportive Housing has been helpful to service providers in the Windy City to help people negotiate services and assistance.

“Even I wound up having a hard time navigating that on my own,” Gonzalez said. “Rental assistance is a key component of that.”

Gonzalez said timing also was a factor in securing an investor for Covent Apartments. When shopping the tax credits in 2020, the economic uncertainty

wrought by the COVID-19 pandemic gave potential financiers pause. As the economic fog began to burn off in 2021, R4 showed its willingness to grapple with the uncertainty as well as the complicated depreciation issues.

“A year earlier, it was crickets. Nobody was calling,” Gonzalez said. “We had other investors who walked away. I’m not mad at them. I understand why they did. But it was because we had to really get into it and think creatively around those depreciation issues, their yield and where the investor is looking at it and willing to go through with it.”

Embers Never Fade in the City by the Lake

Gonzalez said refashioning the ground-floor storefronts for contemporary use required a balance between those needs and honoring the historic regulations and rules. A further challenge came in adding an elevator to the site to comply with the Americans With Disabilities Act.

Longer-term plans for the site also include the construction of a new, 84-apartment building where a parking lot stood previously. Lincoln Park Drummond Group will develop that site, which is planned for almost exclusively market-rate households. Groundbreaking is anticipated later this year.

For Cohen, the complexity was the greatest challenge as well as the most rewarding part of the development.

“We jumped at the chance,” Cohen said. “These are the deals that we thrive on and I personally love doing because every one of these deals is a puzzle. None of them are going to be exactly the same. This one was a truly interesting puzzle working with NHP, who we love working with, working on a deal in Chicago. It’s where my grandma grew up, so it has a special place in my heart.”

Financing

The \$21.6 million capital stack for The Covent Apartments includes several state and city sources: \$1.5 million from the city’s Affordable Housing

Opportunity Funds, \$3.5 million in city HOME funds and \$3.1 million from IHDA Supportive Housing Funding.

R4 Capital provided \$5.6 million in 4% LIHTC equity and \$2.5 million in federal HTC equity. Cohen said continuing to work with NHP combined with the location made the deal too difficult to pass up. Cohen said the transaction was difficult, but necessary.

“If everyone ran away from every complex deal, the affordable housing crisis would be even worse,” Cohen said. “I love these sorts of complex deals. These are the ones that are the most important to get done because they’re the ones that serve the populations who need it the most.”

Gonzalez said despite all the challenges and complexity, the fact that construction was ahead of schedule as of early March was a sign of success.

“I’m at a comfort level with where we are that we’ll be able to meet what we committed to for R4,” Gonzalez said.

The next time she has a difficult transaction seeking an investor, Gonzalez has at least one investor eager to listen.

“If Veronica called me, I’d pick up the phone in an instant,” Cohen said. “This was a really great project to work on.” ❖

THE COVENT APARTMENTS

FINANCING

- ◆ \$5.6 million 4% low-income housing tax credit equity investment from R4 Capital
- ◆ \$4.9 million first mortgage
- ◆ \$3.5 million in city of Chicago HOME funds
- ◆ \$3.1 million in Illinois Housing Development Authority Supportive Housing Funding
- ◆ \$2.5 million in federal historic tax credit equity from R4 Capital
- ◆ \$1.5 million from the city of Chicago Affordable Housing Opportunity Funds
- ◆ \$84,675 in cash from operations
- ◆ \$84,675 deferred developer fee
- ◆ \$44,964 ComEd Energy Grant

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