FINANCING MIXED-USE DEVELOPMENT

IN THE DELAWARE VALLEY REGION

Delaware Valley Regional Planning Commission

August 2008

Created in 1965, the Delaware Valley Regional Planning Commission (DVRPC) is an interstate, intercounty and intercity agency that provides continuing, comprehensive and coordinated planning to shape a vision for the future growth of the Delaware Valley region. The region includes Bucks, Chester, Delaware, and Montgomery counties, as well as the City of Philadelphia, in Pennsylvania; and Burlington, Camden, Gloucester and Mercer counties in New Jersey. DVRPC provides technical assistance and services; conducts high priority studies that respond to the requests and demands of member state and local governments; fosters cooperation among various constituents to forge a consensus on diverse regional issues; determines and meets the needs of the private sector; and practices public outreach efforts to promote two-way communication and public awareness of regional issues and the Commission.

Our logo is adapted from the official DVRPC seal, and is designed as a stylized image of the Delaware Valley. The outer ring symbolizes the region as a whole, while the diagonal bar signifies the Delaware River. The two adjoining crescents represent the Commonwealth of Pennsylvania and the State of New Jersey.

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Cover Photo: One Hancock Square, in the Northern Liberties neighborhood of Philadelphia, developed by Tower Investments, designed by Erdy McHenry Architecture, LLC. (Source: DVRPC)

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EXECUTIVE SUMMARY

Mixed-use development, a merging of multiple land uses into a single project, offers many benefits, including promoting efficient land use, community revitalization, and the creation of new residential and business opportunities. Despite its benefits, mixed-use is challenged by high complexity, development costs, and governmental regulation. These challenges create greater uncertainty and risk, and as a result, mixed-use can be difficult to finance.

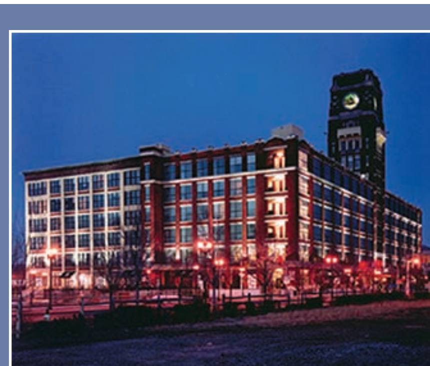
Many proven strategies exist for combating financing challenges, with the Delaware Valley's real estate developers using these strategies to create successful mixed-use projects. Such strategies include:

- Developing collaboratives that utilize public, private, and non-profit investment resources and the advantages of each.
- Utilizing government programs at the federal, state, and local levels to promote mixed-use as a goal or component of community and economic development initiatives.
- Finding real estate investors that seek longer-term opportunities, such as foundations, pension funds, and educational institutions.

Based on an assessment of mixed-use financing strategies and completed projects in the region, this report recommends:

- Streamlining municipal regulatory practices.
- Coordinating housing and economic development programs at the state and local levels.
- Developing new land assembly tools and financing techniques to facilitate approvals, construction, and financing.

This report is designed to aid municipalities and developers in effectively financing mixed-use projects. Chapter 1 provides a brief overview of the many benefits of mixed-use development, while Chapter 2 summarizes challenges to its implementation. Next, Chapter 3 outlines best practices in mixed-use financing, including specific financing mechanisms, different organizational structures for financing, and overall strategies for achieving success. Chapter 4



Left: East Passyunk Avenue in South Philadelphia contains a vibrant mix of retail and residential uses. (Source: DVRPC)

Above: The Victor Building in Camden, NJ combines 341 residential units with 25,000 square feet of retail space.
(Source: The State of New Jersey)

introduces some of the Delaware Valley's successful mixed-use projects and developers, as well as a discussion of funding sources that exist in the region. Chapter 5 discusses various public funding sources that exist in the region. Finally, Chapter 6 contains concluding lessons and a list of the report's critical recommendations.

INTRODUCTION

Mixed-use can be defined as an integrated real estate development which incorporates two or more different land uses. Such uses can include housing, retail, offices, hotels, entertainment facilities, and community institutions. Contemporary mixed-use projects take many forms and are located in communities ranging from older central cities to growing suburbs. Some of these forms include low-rise buildings with residential units above first floor retail, integrated towers that incorporate various uses on different floors, and entire town centers that combine entertainment, restaurants, retail, and housing.

Historically, almost all urban development has been mixed-use out of necessity, from the ancient cities of China and the Mediterranean to the medieval towns of Europe. Lacking access to inexpensive long-distance transportation, people depended on products and services that were located in close proximity to where they lived. Starting during the Industrial Revolution and continuing well into the twentieth century, mixed-use lost favor in the United States. The reasons for this were:

- Mass production resulted in large, single-use factories that utilized economies of scale. These replaced smaller operations that had often included housing.
- Increased industrialization led to pollution and unsanitary conditions. The nation's first zoning ordinances were meant to alleviate this problem by separating housing from heavy industry. The codes utilized by many municipalities today are an outgrowth of this method of land use regulation.
- A growing population after World War II created a strong demand in the housing market. This demand was generally fulfilled by detached, single-family homes.
- The rise in automobile usage made physical proximity less important and increased the feasibility of large, single-use development projects.
- Developers and financial institutions sought to simplify and increase profits. Single-use projects created a standardized approach to development that allowed for financials to be more easily evaluated. Many developers began to specialize in one

Left: The Hub on Chestnut, in West Philadelphia, a recently built condominium and retail development. It is located near public transit and developed by Teres Holdings.
(Source: DVRPC)

Below: Levittown, PA is a suburban development built in the 1950s that separates land uses.
(Source: National Archives and Records Administration)

specific use (e.g. residential, commercial, or office) and rarely incorporated multiple uses.

While single-use has become the dominant form of development in the United States, concern is growing about its negative effects. These effects include a built environment that lacks vitality and automobile dependence. Additionally, single-use often results in suburban sprawl, which fragments the landscape, and is ecologically unsustainable.

Concerns over these effects are leading to increased popularity of mixed-use development. However, traditional, single-use financing strategies are not suitable for mixed-use, and their application to such development has led to projects that are unsuccessful. Many development entities are currently ill-equipped to address this problem, limiting the number of mixed-use projects that are built. Additionally, current conditions in the real estate market make it even more important that projects meet strict financial criteria in order to be successful. This report describes the financing challenges that exist in more detail, and also provides strategies for overcoming these challenges.

DVRPC and Mixed-Use Development

As the Metropolitan Planning Organization for greater Philadelphia's nine-county area, the Delaware Valley Regional Planning Commission (DVRPC) serves in an advisory role to the region's municipalities. DVRPC is actively engaged in promoting a variety of objectives that mixed-use helps to accomplish. These include, but are not limited to, the following:

- Building according to smart growth guidelines to promote medium to higher densities in appropriate locations and the efficient use of limited land resources.
- Creating hubs of activity where people interact with each other and develop a sense of community.
- Fostering economic development through job generation, new business creation, and higher tax revenues for municipalities.
- Reducing traffic congestion and automobile infrastructure needs, both by shortening

Left: Governments, developers, and financiers can work together to create exciting, mixed-use environments, like Main Street, Manayunk, in Philadelphia.
(Source: DVRPC)

Above: Forrestal Village in Princeton, NJ combines a hotel, retail, restaurants, and office space as part of a mixed-use development.
(Source: DVRPC)

travel distances and decreasing parking requirements.

- Providing more diversity in housing stock, which enables more people to live near their jobs and remain in the same community even as their life circumstances and residential needs change over time.

Destination 2030, DVRPC's adopted long-range plan, supports further development of higher density, mixed-use projects by promoting reinvestment in core cities and older suburbs, advancing strategies for land use and transportation linkages, and advocating for the creation and maintenance of area centers - places of governmental, economic, or other significance that provide focal points in the regional landscape and offer nearby residents a sense of community. By incorporating multiple uses into a single development project, mixed-use construction often enhances the dynamism and walkability of the places where it is located.

Recommendations

In addition to outlining strategies for mixed-use development, this report recommends action steps that governments, developers, and financiers can take to improve the feasibility of mixed-use development in the future. A summary of these recommendations is provided below. See Chapter 6 for a complete listing.

For local government:

- Create mixed-use zoning overlay districts to streamline the permitting process.
- Implement outreach and education initiatives to provide developers, non-profits financiers, and the public with information about the benefits of mixed-use.
- Create additional subsidies and other financial incentives to promote the development of mixed-use.

For state and county governments:

- Encourage local governments to adopt mixed-use public financing programs that are available on the county, state, and federal levels, such as Pennsylvania's Mixed-Use Facility Financing Initiative.
- Coordinate the wide variety of housing and economic development programs and agencies, in order to make them easier to utilize.
- Strengthen existing community development programs, revising them to promote mixed-use when needed.

For developers:

- Use land acquisition and financing tools that facilitate the construction and financing of projects. Examples include land banks, vacant property initiatives, gap financing, tranching repayment[1], and credit enhancement tools such as loan pools.
- Build strong relationships with municipalities in order to determine the development needs of individual communities. Open conversation increases the ease of completing a project.
- Make realistic development projections by not overestimating market demand, having thorough financial analysis, and scheduling a realistic construction plan.
- Think outside the box to create innovative development techniques for mixed-use

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1 A tranching repayment plan divides financing opportunities into different lengths of time, allowing investors with both short-term and long-term investment goals to participate and choose based on their individual preferences and objectives.

which adhere to best practices in sustainability and good urban design.

- Outreach and dialogue with the pending neighbors of a mixed-use project, in order to minimize NIMBY responses and calls for project rejection.

For financiers:

- Become better acquainted with the basic concepts of mixed-use, as well as its benefits, feasibility, and the financial returns it provides.
- Reevaluate traditional investment and lending criteria to take into consideration the positive effects on value and property demand that mixed-use creates.
- Explore new investment opportunities in overlooked markets, especially with regard to infill and inner city development.

CHAPTER 1: WHY MIXED-USE?

Mixed-use benefits all of the many stakeholders in the development process. For private developers and financial institutions, these benefits are financial. For municipalities and non-profit developers, positive outcomes include both fiscal returns and achievement of social goals. For the general public, advantages include economic development, community revitalization and enhanced identity, efficient use of land, and an overall higher quality of life.

Benefits to Investors

Private Developers: In recent years, demand has grown for higher-quality projects among the residential, retail, office, and entertainment sectors. Rather than inexpensive, low-quality development, individuals and businesses are attracted to real estate based on such factors as amenities, walkability, and convenience. This bodes well for private developers, who can tap into a growing real estate market by building mixed-use. Developers can also benefit from the ability to use public programs, such as smart growth and mixed-use funding initiatives, to reduce financing costs.

Financial Institutions: Lenders are often less inclined to finance mixed-use projects, requiring developers of such projects to seek several financing sources for the various project components. However, the lending industry has much to gain by reevaluating its practices and investing in mixed-use. Mixed-use projects, with their attention to design and quality, yield better long-term returns. Lending to such projects increases the success of repayment, making it more profitable. Additionally, mixed-use creates demand for further development of stagnant real estate markets, creating new demand, and providing for more potential lending customers. Depending on the geographic area, this fact may increase the compliance with the Community Reinvestment Act for large lenders (see Chapter 3 for more details).

Non-Profit Developers: Community development corporations (CDCs) and other non-profit groups work to promote social justice and improve the overall quality of life in the neighborhoods they serve. Mixed-use can help achieve these goals through efficient land use and community and economic revitalization. A single project is often able to meet multiple

Above: The mixed-use environment of Palmer Square in Princeton, NJ creates a very desirable built environment. (Source: DVRPC)

Left: Mixed-use helps to create exciting street life, such as that found in various neighborhoods of Philadelphia. (Source: DVRPC) community needs comprehensively. For example, a mixed-use project may include affordable housing, retail, and community services that are all needed by the neighborhood.

Municipalities: In addition to improving quality of life standards and amenities, mixed-use can create jobs and provide new sources of tax revenue. The increased density and property value created by mixed-use projects raises the amount of property tax revenue a municipality can collect from a single property.

Public Benefits

Economic Development: Mixed-use can help to revitalize and extend commercial corridors by attracting new business next to existing commercial uses, thereby improving the customer base for both. The presence of a large anchor tenant makes a development a go-to destination, which benefits all other retail residually. Additionally, if retail is local, this expands the options available to nearby entrepreneurs, who may consider starting a new business. The proximity of additional jobs in a small area also encourages the employment of local residents. Indeed, placing multiple uses in close proximity to each other benefits local residents and business owners alike. For example residents of a housing unit create demand for retail and other services, and the proximity to those uses, in turn enhances the market demand for housing.

Community Revitalization: Mixed-use helps to revitalize communities in three ways. First, well-designed, mixed-use projects can be fundamental in fostering sense of place. In newer communities that have mostly new residents and lack social cohesion, mixed-use can plant the seeds of a new identity. In older communities, mixed-use can reinvigorate an area with new landmarks, businesses, and residences. For both, overlapping uses provide residents places to interact in their neighborhood. Second, mixed-use is an effective type of infill development for brownfield, vacant, or abandoned properties. Successful projects have a compounding effect, both raising property values and creating additional investment. Third, mixed-use can be part of efforts to expand upon existing residential units and variety. Diverse housing stock, as opposed to exclusively large, single-family detached homes is better at accommodating the needs of everyone who lives in an area as their needs and housing demands change. For example, many empty nesters move to smaller homes once their children are grown. The existence of varied housing stock allows them to age in place, rather than forcing them to leave.

Mixed-Use and Multiple Use

The term “mixed-use” has increased in popularity so much that it is often overused, with a resulting loss of its meaning. One outcome of this has been a blurring between the terms “multiple use” and “mixed-use.”

While all mixed-use projects are multiple use, the reverse is not always true. Mixed-use can be differentiated from multiple use through characteristics such as:

- Short distances between uses, with strong pedestrian connections.
- Different buildings that vary architecturally, but are also visually connected.
- A unity that psychologically links the entire project together.

While multiple use projects can promote smart growth, they do not do so as effectively as mixed-use. Many developments in the Delaware Valley are described as mixed-use but are in fact multiple use. While these projects incorporate many good design principles, they are not truly mixed-use.

Efficient Land Use: Increased concerns about pollution, stormwater management, infrastructure costs, and reduction in open space have raised awareness about the negative impacts of low-density sprawl. Because mixed-use is higher density, it consumes less land, provides for denser infrastructure networks, and helps reduce automobile pollution. Mixed-use is also a critical aspect of creating transit-oriented development, or projects that are compact, walkable, and intended to encourage transit ridership. Finally, mixed-use enables effective reuse of previously developed or underutilized property. This form of development is natural in older areas, where it is already the primary land use pattern. Vacant residential and industrial properties are often found in central cities, and have great potential to be developed as infill mixed-use.

An exceptional benefit of mixed-use is its ability to address multiple community needs within the development of one project. Just one successful project can produce jobs, increase housing options, generate a profit for private developers, provide community amenities, and create additional property tax revenues for local municipalities. Nonetheless, despite its many advantages, mixed-use projects often face opposition - including challenges from the local officials, residents, and investors that have the most to gain from the completion of such projects.

The next section of this report provides an overview of the challenges that are faced in the mixed-use development process.

CHAPTER 2: OVERCOMING THE CHALLENGES OF MIXED-USE DEVELOPMENT

Current real estate financing practices in the United States can create challenges for mixed-use. By utilizing the correct development strategies, however, these hurdles can be overcome. This section describes the challenges, categorizing them into financing, municipal regulation, and construction.

Financing

Securing financing for mixed-use projects poses a challenge for several reasons, including the higher complexity and risk, and difficulty in utilizing assistance programs.

Higher Complexity and Risk

Real estate investment decisions are primarily informed by risk assessment. High-risk projects have a reduced chance of success and require a higher potential rate of return in order to attract investors. Risk assessment is also performed by financial institutions when determining lending terms. Mixed-use carries more risk because:

- Incorporating multiple land uses into a single project increases the possibility of unforeseen construction difficulties.
- Market demand is more difficult to predict due to the presence of multiple uses and uncertainty about the presence of one use may affect demand for another.
- The generally large size and greater complexity of mixed-use projects often requires the use of several forms of financing. Uncertainty is higher, increasing the potential of an investor's equity being lost. When profit from the first phase of a project is used to finance later phases, it is even more critical that estimations are correct and that each phase is able to sustain itself separately.

Above: Wal-Mart is an example of single-use development that is relatively inexpensive and easy to finance.
(Source: DVRPC)

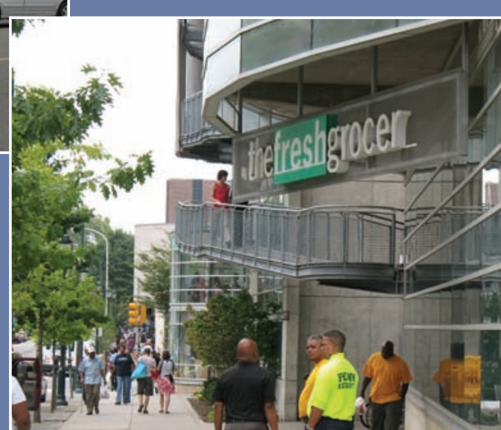
Left: Despite recent trends to build baseball stadiums in downtowns as mixed-use development, parking and community concerns resulted in the new Philadelphia Phillies' stadium being isolated and primarily single-use.
(Source: DVRPC)

- Underwriting standards vary for different land uses; thus, the expected returns for a residential development will be different than those for a retail project of the same size. As a result, combining two or more uses into a single development project creates a situation that many lenders, who have traditionally focused on single-use, are not prepared to handle.
- Pro formas, used to project the value of a development, are based on estimates of future costs and revenues. This requires projections on key variables such as future demand and construction costs. Potential lenders base their terms on the pro forma. Because traditionally each individual use has required its own pro forma, it has been difficult to assess the value of mixed-use through it.
- Mixed-use projects may contain components that require different amounts of equity and different lenders, may yield different cash flows, and may have different exit strategies. These factors require dedicated developers who have the skills to marshall the development disciplines associated with combining uses in a single project.
- Re-selling mixed-use projects can be challenging because of the smaller market for buildings with different types of components (residential, retail, hospitality, etc.). This issue may be overcome by dividing ownership for resale; however divided ownership entities have a different set of problems (e.g., sharing utilities, cross-easement agreements, etc.)
- Mixed-use projects may require public subsidies, such as grants, tax credits, and tax-increment financing. This fact requires developers to be willing to utilize non-conventional financing strategies.

Assistance Programs Do Not Fund Enough Mixed-Use

Most public and non-profit programs dedicated to community or economic revitalization have a narrow focus, making them difficult to apply to mixed-use. For example, many affordable housing programs do not provide funding or integration with commercial development, even though doing so could enhance the value of the housing and foster economic development. The Federal National Mortgage Association (known as Fannie Mae) is a financial organization that promotes mortgage lending by selling mortgage-backed securities. Fannie Mae limits mixed-use by requiring qualifying mortgages to be at least eighty percent residential.

Above: Grocery stores can require large tracts of land and parking, often resulting in single-use development. (Source: DVRPC)



Right: Fresh Grocer, at the corner of 40th and Walnut Streets in Philadelphia, overcomes the parking challenge through having a large public parking garage above the store.
(Source: DVRPC)

Municipal Regulations

Municipalities regulate development in order to ensure projects contribute positively to their communities. Zoning codes and permit processes for new construction are meant for this purpose. However, because many of these regulatory systems tend to separate development into single-use districts, they often function as a barrier to mixed-use. A few of the ways in which local development regulations can hinder the construction of mixed-use are described below.

Zoning Not In Place

While zoning can effectively separate conflicting land uses, improve standards of living, and raise property values, it can also contribute to the creation of sprawling, auto-oriented communities. Many municipalities in the Delaware Valley have zoning ordinances that ban mixed-use altogether. Zoning amendments to create overlay districts can be proposed to help address this issue; however, implementing proposed zoning changes can be a long and arduous process. From a developer's standpoint, the presence or absence of mixed-use zoning can make or break the feasibility of a project. This is especially true in the case of infill and smaller-scale projects, where a developer's potential profit tends to be relatively small.

Parking Requirements Too High

Zoning codes traditionally require a certain number of parking spaces based on the square footage of a project. For example, a municipality might require one parking space for every 300 square feet of retail, and two spaces for every residential dwelling unit. This can become problematic for mixed-use, when the ordinance requires parking spaces to be the sum of those for each use separately. An oversupply of parking can make a project uneconomical - it raises parking infrastructure costs. Additionally, it reduces the square footage that can be devoted to revenue-generating primary uses and amenities, such as green areas. These consequences can reduce the final quality of the project's design and its pedestrian friendliness.

Above: The construction process for mixed-use can be complex and time-consuming. (Source: DVRPC)

Right: The vast size of larger mixed-use developments, such as Eagleview in Exton, PA, can be overwhelming for many smaller suburban municipalities. (Source: The Hankin Group)

Separate Permitting Processes for Each Use

In addition to variances for land use and parking, building codes often require mixed-use to receive a set of permits for each use, making the process possibly twice or three times as complex. If there is considerable opposition to a project, the permitting process can be further hindered. Additionally, many permitting processes require higher standards for building materials when multiple uses are combined in a single structure. While this may improve the quality and safety of the project, it can also lead to increased costs and reduced feasibility.

Small Municipalities Lack Necessary Resources

The region's land use is generally controlled by local, municipal governments. These entities generally lack experience in handling the higher complexity of mixed-use development. Furthermore, smaller governmental bodies lack large full-time staffs, and are thus often unable to devote the necessary time to collaborating with private mixed-use developers. Without this collaboration, projects might not be as effective as they otherwise might, in terms of economic and community development.

Complexities of Construction

Mixed-use is more complex and expensive for several reasons, including:

- Developers usually specialize in projects with one type of use; however lenders and equity investors favor developers with proven experience when assessing a project's financial worthiness. This fact makes it especially difficult for many developers to secure financing for mixed-use projects. Developers inexperienced in mixed-use may need to bring in partners experienced in other use components.
- Each use has specific construction needs and practices that often are not compatible, such as the different structural support methods needed for retail and residential uses.
- Building systems must be duplicated or increased in quality, such as additional noise insulation between a restaurant and condos, separate sprinkler systems for each use to appease fire codes, and separate entrances for each use.
- Upfront costs are generally higher, as more infrastructure and construction must occur prior to operation. This is especially the case in vertical mixed-use, where the entire project must be completed before any uses can be functional.
- If a redevelopment project, especially one involving brownfields, cleanup and rehabilitation add to the project's complexity and cost.
- If using older buildings, extensive rehab is often required, especially if the structures have been sealed off or vacant for long periods of time. Floor plans in such buildings are often antiquated - modern office tenants want open floor plans and residential users want more space than are available in older buildings.

These complexities create a greater chance that unforeseen difficulties occur, raising potential risk and the cost of financing. Higher complexity also causes longer construction times, which increase risk by making it more possible that the market demand will change between a project's inception and its completion. While the increase in total costs is usually limited to between two and ten percent, perceived costs, on the part of developers and investors, are generally much higher.

Financing, regulating, and constructing mixed-use development can prove a challenge for developers. However, these barriers can be overcome provided the right financing tools are available. The following chapter provides information about some of the programs and organizations that support mixed-use development in the Delaware Valley and beyond.

CHAPTER 3: FINANCING STRATEGIES

While financing mixed-use development can be challenging, many strategies exist that make it possible. This chapter provides an overview of some of the investment tools available to support the construction of mixed-use projects. Information about financing techniques and public-private partnerships, and a project checklist are also provided.

Private Investment

The private sector is the driving force for real estate development and financing in the United States. While developers sometimes provide financing completely on their own, this reduces the size of a possible project and increases risk. Rather, most developers seek investment from sources such as banks, investment entities, and private investors. This has two key benefits. First, reduced equity is required on the part of the initial developer, who can leverage their equity more effectively by combining it with other sources. Second, tax structures and the nature of limited liability entities can also make partnerships less expensive and risky. However, despite these advantages, the developer must still provide the initial equity that is required for such things as feasibility and design studies. These first costs are incurred when there is high risk and little interest from other investors.

The ability to obtain project financing is improved through the Community Reinvestment Act (CRA), a Federal law requiring financial institutions to provide loans equally to all areas they service. Lending institutions are evaluated by the government's financial regulators and are required to provide evidence that they are lending in an equitable manner. In this manner, the CRA promotes lending to locally-owned projects that are located in low-income areas, giving more merit to mixed-use investment in such areas.

The different kinds of private investors all have their own priorities and financing approaches, which makes each more or less suitable for mixed-use projects. An understanding of the advantages and disadvantages of each is essential. Common sources of private investment include real estate investment trusts, commercial mortgage backed securities, pension funds, commercial banks, and life insurance companies.

The challenge of providing parking facilities that are contextual in urban areas can be solved by including ground-floor retail uses.
(Source: DVRPC)

In addition to these common sources of private investment, several financing tools exist to most effectively utilize different pools of money. These include:

- Mezzanine financing, also known as gap financing, is used to make up the difference between the amount of equity and debt available from lending institutions. While more expensive than equity and debt financing, mezzanine loans can be critical to a project's feasibility.
- A tranching repayment plan allows for incorporation of both short-term and long-term investors, by segmenting financing into different lengths of time. Investors interested in short-term investment can finance initial construction costs, such as infrastructure, and building of the first phases and uses.
- Separating financing by use can reduce the complexity and uncertainty faced by many investors when looking at mixed-use projects. For a multi-story building, this may be accomplished by separating uses and investors through a condo structure. While the building as a whole is still mixed-use, investors are able to analyze it using traditional strategies, focusing on a single component.

Public Sector Support

Public sector support is often critical to the creation of successful mixed-use projects. Local governments, in particular, play a vital role because they regulate land use and oversee municipal permitting processes. Many local governments also administer impact fees and manage public utilities that provide services to every occupied property within their jurisdiction. A wide variety of public programs that are administered at the federal, state, regional, and local levels may be utilized to support mixed-use development. More information about public funding sources can be found in "Chapter 5: Public Funding Programs."

Public-Private Partnerships

The public sector has always provided subsidies or other incentives, like those mentioned elsewhere in this report, to private development in the name of economic development. Public-private partnerships, however, go further, and can be defined as a situation in which the two sectors share risk, construction, and financing responsibilities to create joint development projects.

Sources of Equity Financing

Institutional Equity

- Pension Funds
- Colleges and Universities
- Life Insurance Companies

Private Equity

- Individual partners
- Private Equity Funds

Source: Urban Land Institute. *Mixed-Use Financing Handbook.* Second Edition. 2003

Public-private development has several benefits, which includes creating projects that are both socially progressive and financially profitable, and generating more economic development in traditionally stagnant or underperforming real estate markets. Public-private partnerships must incorporate strong collaboration and compromises on the part of government and the developer to create projects that are successful and efficiently implemented.

Construction and Operation Financing Strategies

Consideration must be given to a project's construction and operation costs. It is important to accurately estimate a project's long-term cash flows and operating strategies. The following are aspects of effective financing for mixed-use operating and construction costs.

Construction Loan

Long-term lenders often will not finance the higher-risk, short-term construction costs. A separate set of lenders are often needed for construction financing, to be repaid with longer-term loans. Construction lenders look at what kind of financing will be available in the permanent marketplace to guide the size of development loans. The gap between the project costs and construction loans must be plugged by additional equity capital.

Project Phasing

Developers must have a clear and organized schedule for implementing a mixed-use project. Well-planned phasing allows the cash flows of earlier phases to be used to fund later phases. Additionally, phasing allows for a contingency plan should the market change during construction - the project can be scaled back, with later phases not built. Critical to phasing is

Sources of Debt Financing

Commercial Banks

Pros: Provide sources of competitive equity and construction loans. Sometimes construction loans can be open-ended without a permanent loan commitment in place.
Cons: Cautious about financing mixed-use projects, and risk-sensitive to current economic conditions.

Life Insurance Companies

Pros: Long history of financing, strong track record and experience. Some provide both construction and permanent loans.
Cons: Financing is difficult to secure, and often requires a pre-leasing commitment. Stringent underwriting criteria.

Pension Funds

Pros: Good source of financing for larger projects in urban areas.
Cons: Often requires use of union labor that can increase construction costs.

Fannie Mae and Freddie Mac

Pros: Least expensive sources of permanent financing for multi-family rental properties.
Cons: Only provide permanent financing (no construction lending). Conservative debt service requirements.

Source: DVRPC, 2008

consideration of construction and operation realities. Generally, phasing is easiest in low-rise developments of multiple buildings, for which parcels can be split up and developed in different portions. Phasing in larger buildings is also possible, though this can be more complex - funding is not always secure for the entire building before construction starts, and the upper floors of a high rise might interfere with the operation of the lower portions. Regardless of the project, phasing is generally critical to financing success.

Debt Service Coverage Ratio (DSCR)

The amount of financing that a project can obtain is largely based on its expected net operating income, making this figure critical to developers in determining project feasibility. Net operating income is figured by subtracting all project operating expenses (utilities, maintenance costs, etc.) from revenues (rents, parking fees, etc.). Net operating income is divided by the amount of debt payment, accounting for a vacancy factor, to calculate the debt service coverage ratio (DSCR). Lenders use this ratio to precisely quantify the amount of financing they will provide. A larger DSCR means that less risk exists for the lender, because revenues are higher relative to the amount of financing, and a developer is more likely to successfully make their debt payments. Lenders generally have a minimum DSCR requirement of around 1.2 (or higher), meaning that net operating income must be 20% more than debt payments.

Permanent Financing Plan

Such a plan, which normally covers a time of at least ten to fifteen years into the future, is a critical first step to the physical implementation of a development.

Exit Strategy

The exit strategy carefully lays out the conditions for lenders and equity investors, including the planned schedule for investment and the time frame. The exit strategy is easy to manage when a project is financed based on its different uses. This allows a simple explanation of the conditions to investors.

Above: Avenue North, a development in Philadelphia that includes a movie theater and retail space, was spearheaded by Temple University and developed by Tower Investments.
(Source: DVRPC)

Right: Neighborhoods which are rapidly transforming, such as Northern Liberties in Philadelphia, have much to gain from mixed-use projects. Shown here is One Hancock Square, developed by Tower Investments and designed by Erdy McHenry Architecture, LLC.
(Source: DVRPC)

Utilize the Demand for Higher Quality

As discussed in Chapter 2, construction costs are generally higher for mixed-use, a result of challenges in combining different uses and increased standards for quality. However, these costs also create more desirable buildings, and can obtain higher returns than single-use development. Taking advantage of higher quality standards involves generating additional profit from the requirements. For example, energy efficient windows reduce energy costs and improve noise insulation between uses. Similarly, separate entrances for each use results in a building that has no front or back, but rather utilizes every building face. This can create more prominent and better designed buildings.

Consult an Independent Expert

Inexperience can often be a major inhibitor to success for the construction and operation of mixed-use because of the unique challenges attached to it. Private consulting firms exist that can provide assistance and recommendations for mixed-use projects to avoid some of these pitfalls.

CHAPTER 4: MIXED-USE IN THE DELAWARE VALLEY

Greater Philadelphia has the advantage of being one of the oldest and densest areas of the country, making mixed-use already prevalent in many communities throughout the region. In addition, new mixed-use construction can be found from core downtowns to emerging suburban areas. The challenge for individual municipalities and developers is to determine the appropriate scale and density for individual projects within the context of local market demand and the existing built environment.

Projects in the Region

Core cities are older, denser urban centers which often already contain a significant amount of mixed-use. New projects are usually successful in these areas because of the dense development context that already exists. Because only small amounts of undeveloped land exist in core cities, most construction projects require land to be reused. This often includes the rehabilitation of historic buildings as well as the remediation of contaminated, vacant industrial properties (brownfields). A few recently completed urban mixed-use projects in the Delaware Valley region are:

- The Broad Street Bank building in Trenton, New Jersey, a major landmark in the city, was purchased by Bayville Holdings in 2005 and converted into 125 rental apartments above eight ground floor retail spaces.
- Domus, completed in 2007, is located near the University of Pennsylvania at 34th and Chestnut Streets in Philadelphia. Penn contributed financial assistance to the 8-story, 290-unit rental apartment building which also includes a Starbucks and Eastern Mountain Sports.
- The Victor, a luxury loft rental apartment building in Camden, New Jersey, includes 341 rental units atop ground floor retail and restaurants. The first residents moved into the Victor in 2003. Formerly an RCA factory, the converted building brought Camden its first new market-rate housing in many years. Dranoff Properties owns, manages and oversaw the redevelopment of the Victor.

Above: Domus, near the campus of the University of Pennsylvania in Philadelphia, is a condominium and retail development.
(Source: DVRPC)

Left: The Broad Street Bank in Trenton, NJ, was recently renovated for condominiums and retail tenants.
(Source: DVRPC)

Older suburbs can also be excellent locations for mixed-use development. Many of the first generation suburban communities in the Delaware Valley are dense, walkable places with established downtowns and frequent transit service. Many older suburbs offer opportunities for redevelopment and infill construction; however, some greenfield sites - land that is currently undeveloped or used for agriculture - may also be available. Projects that are completed or under construction in the region's first generation suburban communities are:

- The LumberYard Condominiums, in Collingswood Borough, New Jersey, are a prominent example of vertical mixed-use redevelopment in an older suburb. Located near the PATCO high-speed rail line, this transit-oriented development contains 120 residential units and approximately twenty ground floor retail stores. The project is being developed primarily by the City of Collingswood, with assistance from Kanalstein Danton Associates, and construction by Costanza Builders.
- Lantern Hill in Doylestown Borough, Pennsylvania is a horizontal mixed-use project that is built on a former brownfield site. The project, built by Granor Price Homes and developed by Doylestown Investment Group, includes 117 units of housing, both detached and townhomes. There is also 62,400 square feet of office and retail space. Within walking distance of downtown Doylestown, Lantern Hill is easily accessible by rail transit.

In newer, growing suburbs, mixed-use usually occurs on greenfield sites. The built densities of mixed-use projects located in these areas are often less than in core cities or first generation suburbs. Nonetheless, these properties are much more compactly developed than traditional suburban subdivisions and shopping centers. In areas where low-density, auto-oriented development has long been the norm, the demand for single-family detached homes is generally high. Thus, mixed-use buildings in growing suburbs are commonly located in town centers that are surrounded by single-family homes.

- The Village at Valley Forge, in Upper Merion Township, Pennsylvania is a 136-acre development currently under construction by Realen Properties. Plans for the project call for up to one million square feet of commercial space, 2,000-3,000 residential units, and 500 hotel rooms in a town center setting. The first phase of the project will be complete in 2009.
- Washington Town Center, in Robbinsville, New Jersey was developed by Sharbell

Above: Townhomes at the Lantern Hill development in Doylestown, PA are densely built to promote walkability and mixed-use.
(Source: 10000 Friends of Pennsylvania)

Right: The LumberYard Condominiums project in Collingswood Borough, NJ is a large mixed-use, transit-oriented revitalization project.
(Source: New Jersey Future)

Development Company. It contains 47,000 square feet of retail, 35,000 square feet of office space, and 700 housing units on 400 acres. In the center of the development is The Lofts at Washington Town Center, condominium units located above retail. There is significant density which creates substantial public space as part of this traditional neighborhood development.

Local Private Developers

Private developers are the primary drivers of mixed-use. The Delaware Valley's diversity of communities results in a variety of developers, each with their own particular characteristics, and often working in a variety of contexts.

- Greenfield developers work with land that is undeveloped or used for agriculture. The Hankin Group, which created the 800-acre Eagleview community in Exton, Pennsylvania is an example of a large greenfield developer with a background in mixed-use.
- Infill developers are concerned primarily with redevelopment, building projects in core cities and older suburbs. Westrum Development is an example, having completed projects in Gloucester City, Burlington City, and the Brewerytown neighborhood of Philadelphia. Tower Investments, also an infill developer, recently completed a complex which includes a movie theater, as well as retail and residential uses next to Temple University's campus in North Philadelphia.
- New Urbanist developers adhere to the planning movement of the same name, creating designs that follow the design principles of traditional urban places. An example is Weatherstone in Ludwigs Corner, Chester County, Pennsylvania, created by the Hankin Group. The project combines 273 single family residences and townhomes, along with 240,000 square feet of office space.

Amongst all various types of developers, the size of the company has an impact on its priorities, abilities, and development strategy:

- Large developers have a substantial amount of capital that they can use to initialize the investment process. Their size and history give them strong records towards

Above: The Village at Valley Forge, in Upper Merion Township, PA, currently under construction.
(Source: Realen Properties)

Above Right: Townhomes at Weatherstone in Ludwigs Corner, Chester County, PA.
(Source: The Hankin Group)

Below Right: Urban infill projects, such as this development in the Brewerytown neighborhood of Philadelphia, are an excellent application for mixed-use.
(Source: Westrum Development)

financial institutions and investors, resulting in less financing difficulty. In addition, they have often already established strong relationships with financial institutions.

- Smaller developers do not have the advantages of their larger counterparts in that they do not have the same capital or alliances with financial institutions. However, this can be overcome by taking advantage of public funding programs to supplement their financing. Enterprise Heights is a real estate development firm based in West Philadelphia involved in rehabilitating blighted buildings and specific construction projects.

Concerns of Local Private Developers

Based on interviews completed with representatives from a variety of developers in the region, the following concerns and beliefs are apparent:

- Local governments tend to impede mixed-use by using zoning to restrict certain types of development. Citizens and governments alike often do not want additional density, concerned about the effects it will have on their quality of life.
- Mixed-use requires more investment and focus on detail, which can be difficult for inexperienced developers. The president of one large development company believes that his organization is able to create massive projects in desirable locations for two reasons - they have a proven track record and own a significant amount of land. For developers new to the process, starting small can be a critical step for success.
- The demand for retail is often overestimated. Many cities that pursue a mixed-use program are wildly optimistic about how much retail their project can sustain. Furthermore, relying on high retail rents is not favored by banks in pro-forma exercises.
- The private sector believes the public sector to be somewhat of a hurdle to creating mixed-use development. The regulations and local officials of many municipalities in Pennsylvania and New Jersey restrict attempts to create unique projects.
- Infill is easier because many of the key aspects of mixed-use are already in place, whereas a greenfield development requires all design elements that make a successful project to be created from scratch. One experienced developer believes that those new to the process should begin with infill development.

Financing Through Non-Profit Organizations

The region's non-profit organizations are actively involved in mixed-use development, especially in distressed communities. Non-profits finance mixed-use through loans, grants, equity investments, technical assistance, and community organizations. Many non-profit organizations, such as community development corporations, also have direct experience with real estate development and oversee the planning and construction of projects.

Colleges and Universities

Educational institutions are a major resource for obtaining equity financing for mixed-use. This is both because of their desire to realize long-term profit horizons, and also their promotion of social justice causes. Mixed-use near universities can be particularly practical and successful both because of their large property ownership, and the live-work-play functions they provide. Temple University and the University of Pennsylvania have both promoted mixed-use, using direct investment in projects and providing financial assistance to third-party developers.

The Reinvestment Fund (TRF)

Headquartered in Philadelphia, TRF invests in a wide range of community development projects, including housing, schools, and mixed-use. TRF's investment approach is data-driven and based on analysis of where investment funds will have the most impact. TRF has worked on over 2,000 projects and delivered over $650 million in capital to communities throughout the region. Their projects include residential and retail development in Philadelphia's Brewerytown neighborhood, residential and economic revitalization projects in East Camden, and the mixed-use 40th Street Promenade in West Philadelphia.

Local Initiatives Support Corporation (LISC)

As the nation's largest community development intermediary, LISC provides CDCs and other non-profit groups with loans, grants, lines of credit, training, technical assistance, and equity investments to help rebuild distressed neighborhoods. LISC operates several regional offices throughout the country, including in Philadelphia.

Community Development Corporations (CDC)

CDCs act as local development organizations, focusing in a small, targeted focus area. Unlike private developers, CDCs are primarily driven by social concerns rather than profit. This allows them to strongly advocate, finance, and build mixed-use, guided by concern for improving an area rather than heading projects that are simple to finance. A CDC umbrella organization, the Philadelphia Association of Community Development Corporations provides advocacy and education services to Philadelphia CDCs. Mt. Airy USA is an example of a local CDC that has developed mixed-use projects.

Community Development Financial Institutions (CDFI)

CDFIs are local, geographically-based lending organizations which provide both financing and development resources. The U.S. Treasury provides loans and investments to CDFIs through the CDFI Fund program. The Treasury also makes designated CDFIs eligible for New Markets Tax Credits (more information about NMTCs can be found in the next chapter). CDFIs can be credit unions, banks, or loan funds. Because they are local and serve the community immediately around them, CDFIs often quickly recognize the benefits of mixed-use and finance it. Additionally, there are organizations which provide support for CDFIs via advocacy and educational services. The Opportunity Finance Network, Philadelphia Neighborhood Housing, United Bank of Philadelphia, and the Reinvestment Fund are local examples of CDFIs.

CHAPTER 5: PUBLIC FUNDING SOURCES

Public funding to support mixed-use development is available at the federal, state, regional, and local levels. However, many public sector programs that promote mixed-use do so indirectly, through a variety of smart growth, economic development, and community revitalization programs. Funding programs with a specific purpose such as for affordable housing, infill, or brownfield remediation can often be used for a mixed-use development. It is important, however, that program funds are only used for their intended purpose and accounted for accordingly.

Selected public funding resources that may be applied to mixed-use development projects are summarized on the following pages. For more information about these and other programs that can potentially be utilized, DVRPC has published a variety of sources, such as the Municipal Resource Guide (2006).

Federal Funding

Federal initiatives that may be utilized to support mixed-use development include tax credit programs, affordable housing vouchers, and tax-abatement districts:

New Markets Tax Credit (NMTC): Tax credits are government programs that reduce the amount of taxes paid. Unlike a tax deduction, which only lowers the amount of pre-tax income,

Case Study: The LumberYard

Location: Collingswood Borough, Camden County, New Jersey

Developer: City of Collingswood, Kanalstein Danton Associates

The LumberYard Condominiums are a mixed-use development on a former lumberyard on Haddon Avenue, a main corridor in Collingswood. The project consists of 120 residential condos, twenty-one retail spaces, and an underground parking garage.

Collingswood, a middle-income suburb which borders Camden City, is well connected to the region via the PATCO high speed line. The Lumberyard Condos are four blocks from the PATCO station, making this a transit-oriented development.

The development is being completed in three stages. The project is developed primarily by the City of Collingswood, with assistance from Kanalstein Danton Associates, and construction by Costanza Builders.

This case study illustrates the importance of supportive municipalities and state government in fostering mixed-use development. The City of Collingswood has extensively developed plans to revitalize the retail and residential sectors of the city since the 1970s. The program was also sponsored by the State of New Jersey's Transit Village Initiative, which provides financial assistance to communities showing interest in developing around transit stations. The City was able to fund a smart growth study with these state funds. When it decided to undertake a redevelopment, the City also incorporated hundreds of community members into the implementation process. They had input into project characteristics such as layout, content, and density of the design.

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a tax credit is applied after taxes have been calculated, making it worth more than a tax deduction of the same amount. This makes tax credits a particularly valuable type of subsidy.

The Community Development Financial Institutions (CDFI) Fund, an arm of the U.S. Department of the Treasury, annually allocates New Markets Tax Credit equity to certified Community Development Entities (CDEs). Qualified CDEs include CDCs, loan funds, and other local development organizations. Private sector investors, such as banks, can utilize these credits by partnering with CDEs to develop projects in low-income communities. Examples of CDEs in the Delaware Valley are The Reinvestment Fund, the Local Initiatives Support Corporation, the Wachovia Community Development Enterprises LLC, and the Pennsylvania Housing Finance Agency.

Low Income Housing Tax Credit (LIHTC): The LIHTC program is administered through the state's housing credit agency: the New Jersey Housing and Mortgage Finance Agency or the Pennsylvania Housing Finance Agency. To obtain a LIHTC, an investor provides capital that will be used to support the development of low-income housing rental units. The investor need not be the developer or manager of the project. All LIHTCs are paid annually to investors over a period of 10 years. For projects without federal financing, the value of the tax credit is approximately nine percent of the development cost (excludes the value of the land). The value of tax credits for projects with federal financing is four percent. To be defined as low-income, a housing development project must meet one of the following criteria:

1) At least twenty percent of its units must be rented to households earning no more than fifty percent of the area median income; or
2) At least forty percent of its units must be rented to households earning no more than sixty percent of the area median income.

Historic Preservation Tax Credits: Current federal tax incentives for historic preservation include a twenty percent tax credit for the certified rehabilitation of registered historic structures, and a ten percent credit for the rehabilitation of non-historic, non-residential buildings built before 1936. The program is administered jointly through the National Park Service, Internal Revenue Service, and each state's State Historic Preservation Office. To be eligible for either credit, the planned rehabilitation must meet the program's standards, which include the reuse of a depreciable building. Federal historic preservation tax credits may be used in conjunction with LIHTCs and/or tax deductions for charitable contributions.

Housing Choice Voucher Program: The U.S. Department of Housing and Urban Development's Housing Choice Voucher Program, commonly known as Section 8, provides housing to low-income individuals. Those who qualify for the program are given a certificate, which they can use as partial payment to all landlords registered in the program. The landlords can in turn redeem the vouchers for money. While not directly promoting mixed-use, the program provides developers the ability to create mixed-use housing in low-income areas that is closer to market rate - the voucher subsidy makes such projects affordable to low-income residents.

Empowerment Zone Tax Incentives (EZ): Funded by the U.S. Department of Housing and Urban Development, the EZ program offers tax breaks in designated Empowerment Zones. These breaks take the form of employment credits, which reduces the amount of taxes that must be paid based on employing workers within the Empowerment Zone. This substantial reduction in taxes can make a key difference in the feasibility of mixed-use financing. Large areas of both Philadelphia and Camden are located in EZs, with exact boundary information available on the HUD website. Many non-profits exist that are dedicated to specific EZs, such as the American Street Financial Services Center, which provides financial investment and business consulting services to the area around American Street between Girard and Lehigh Avenues, and the North Central Philadelphia Financial Partnership which lends inside the North Central Philadelphia Empowerment Zone.

State Funding - Pennsylvania

Several programs administered by the Commonwealth of Pennsylvania also support mixed-use development. These initiatives include, but are not limited to, the following:

Building PA: Administered by the Pennsylvania Department of Community and Economic Development, Building PA serves as the state's real estate development fund. The program earmarks 150 million state dollars for the fund, an amount which is matched by non-profits and private investors. The public-private partnership program is targeted at small and mid-sized communities in the state.

Keystone Opportunity/Expansion Zones (KOZ/KOEZ): The KOZ and KOEZ programs are statewide Pennsylvania initiatives that provide state and local tax abatements to residents and businesses located in one of twelve designated economic development zones. KOZs/KOEZs are located in low-income areas that offer opportunities for redevelopment. Development projects in KOZs/KOEZs are given priority consideration for assistance under various community and economic building initiatives that are administered at the state level.

Mixed-Use Facility Financing Initiative (MUFFI): MUFFI, one of the Pennsylvania Housing Finance Agency's Homeownership Choice Programs, supports mixed-use development and the revitalization of commercial corridors by providing a mechanism to help close funding gaps that may exist between residential and commercial lenders. The program currently gives preference to projects involving the rehabilitation of existing structures. The Condos at Pelham, in the Mt. Airy neighborhood of Philadelphia, is an example of a project that utilized MUFFI funding.

Transit Revitalization Investment District (TRID): Pennsylvania's TRID program encourages cooperation between municipalities and public transit agencies to promote economic development around train stations. Once established, a TRID allows transit agencies to share in the real estate tax revenues generated by new development near a station. The transit agency, in turn, reinvests that revenue in capital projects at the specific transit station and/or the maintenance of the TRID area. So far, the Pennsylvania Department of Community and Economic Development has awarded four TRID planning grants to three municipalities in southeastern Pennsylvania: Marcus Hook Borough (SEPTA R2 Marcus Hook station), Bristol Township (SEPTA R7 Croydon station), and the City of Philadelphia (for SEPTA's Temple University Regional Rail station and the 46th Street station on SEPTA's Market-Frankford Line). A TRID study grant from the Pennsylvania Department of Transportation has also been provided to Ambler Borough (SEPTA R5 Ambler station). In addition, DVRPC has awarded a Transportation and Community Development Initiative (TCDI) grant to Lower Merion Township to support TRID planning in the area of the Bryn Mawr station on SEPTA's R5 line.

Tax Increment Financing (TIF): TIF programs provide for the funding of public projects by borrowing against the additional tax revenue (the "increment") the project is expected to create. Creating a situation in which the future users and beneficiaries of a project pay for its construction, TIFs are a valuable method of public investment that does not require raising general property taxes. The laws regulating TIFs are state run, with minor differences for Pennsylvania and New Jersey.

State Funding - New Jersey

State of New Jersey initiatives that can be utilized for mixed-use financing include, but are not limited to, the following:

New Jersey Redevelopment Investment Fund (NJRIF): Available to New Jersey municipalities, counties, non-profits, and corporations, the NJRIF is a flexible investment fund that provides debt and equity financing for business and real estate ventures. For more information, contact the New Jersey Redevelopment Authority at www.njra.us.

Smart Futures Planning Grants: These grants are to support planning initiatives that are consistent with smart growth objectives, and statewide and regional planning precepts. In 2007, the New Jersey Department of Community Affairs accepted applications falling within five general categories: main street design; rural sustainability; regional sustainability; transferable development rights real estate market analysis; and urban parking solutions. Smart Future Grants are for planning purposes only and may not be used to finance capital improvements or support general administrative costs.

Revenue Allocation Districts (RAD): RADs are New Jersey's legislation promoting tax increment financing. As in Pennsylvania, this provides for the funding of public projects by borrowing against the additional tax revenue they are expected to create. This results in the future users and beneficiaries of a project paying for its construction. In New Jersey, regulation

Case Study: WINSTON COMMONS

Location: Mt. Airy, Philadelphia, Pennsylvania

Developer: Mt. Airy USA

Winston Commons, developed by Mt. Airy USA, a community development corporation, shows how financing challenges can be overcome through creativity and innovation. The project consists of 20,000 total square feet, with six market-rate condominium units, ground floor commercial including a coffee shop, and 11 parking spaces.

Since the project involved infill, brownfield redevelopment, adaptive reuse, and historic preservation, Mt. Airy USA was able to procure funding from over 12 different sources. In total, $2 million in grants was secured for the $4 million project. The Reinvestment Fund (TRF) provided the acquisition loan as well as a demolition loan; the Philadelphia Industrial Development Corporation (PIDC) provided permanent financing.

The grants had many specific requirements. Many funding sources were for either residential or commercial, requiring all funding from a particular source to go to one use. For example, Mt. Airy USA received a grant from the Pennsylvania Department of Community and Economic Development (DCED) which stated that it could only be used for the commercial part of the project, and so these funds were used for such items as new windows and paint for the retail space. One of the commercial funding requirements was for façade work. Mt. Airy USA worked closely with the contractor to make sure the money met the grant requirements.

The Winston Commons project illustrates the complexity of mixed-use development. Omar Brownson, project manager of the development, lists several key lessons learned from the project which can be used to overcome these challenges.

- On a cash flow basis, funding streams vary, and it is important to be aware of the "when" and "where" cash flows are coming in and going out, so there is enough money to pay necessary expenditures.
- Political support is critical to success. Mt. Airy USA engaged a lobbyist to seek help from the Redevelopment Assistance Capital Program, a Pennsylvania-state program that offers grants to non-profits for economic development projects that have cultural, historic, or civic significance.
- Flexibility in the funding process and different sources greatly increases the feasibility of mixed-use development.

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requires that RADs not include more than fifteen percent of the total taxable property in the municipality. Governments financing RAD projects through the use of bonds have the option of designating the New Jersey Economic Development Agency (NJEDA) to act on their behalf as the redeveloper. This enables the municipality to take advantage of NJEDA's ability to condemn property and handle other technical components of the project.

Transit Village Initiative: The New Jersey Department of Transportation's Transit Village Initiative assists communities that demonstrate a strong commitment to revitalizing the area around their transit station. Municipalities are recommended for designation as a Transit Village by an interagency task force. The designated Transit Villages in the Delaware Valley include Burlington City, Riverside, and Collingswood, New Jersey. Designation brings prioritized funding and technical assistance from state agencies, as well as eligibility for other grants.

Case Study: Palmer Square

Location: Downtown Princeton Borough, Mercer County, New Jersey

Developers: Edgar Palmer, Collins Development Corporation / Palmer Square Management

Palmer Square is an example of a mixed-use development that has had a complicated evolution. Developed adjacent to Princeton University's campus by Edgar Palmer, initially the square had 107 residences situated above 37 retail stores. Princeton took ownership of the square after Palmer's death in the early 1940s. The square was not a financial success under Princeton's ownership, arguably attributable to maintaining outdated rent rates and not providing a mix of retail that would sufficiently provide enough foot traffic.

In 1981 Princeton sold the property to Collins Development Corporation, which undertook a $100 million expansion that involved converting original residences to condominiums, creating three four-story buildings of office, retail, and residential. Additionally, the original focal point of the square, the Nassau Inn, was expanded. The new buildings were integrated with surrounding development, providing context between old and new. However, the recession of the late 1980s caused the project to temporarily fail.

In the 2000s, there have been plans by Collins Development, which has retained the property but changed its organizational name to Palmer Square Management, to create approximately one hundred additional condominium units. The Borough of Princeton has generally backed this proposal, providing funding for site and infrastructure improvements, as well as expedition of the permitting process. However, the project has stalled, largely because of financial challenges resulting from state law that requires the project to incorporate affordable housing. Additionally, there is concern about the effect that more development will have on the character of nearby neighborhoods.

Palmer Square demonstrates the long-term nature of larger infill mixed-use projects. Such projects have considerable potential, often because of their attractive central locations. Palmer Square, despite its various setbacks, is a vibrant downtown commercial center for Princeton. However, such projects are also quite susceptible to economic conditions because of the long time they take to plan and build. It is likely that larger projects will encounter an economic downturn over the course of their construction. For this reason, it is critical to have a long-term mentality when financing larger projects.

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Princeton, NJ 08542
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Urban Enterprise Zones (UEZ): The UEZ program is a New Jersey initiative similar to Pennsylvania's Keystone Opportunity Zone program. Currently, thirty-two distressed commercial and industrial areas in New Jersey are designated as UEZs. Businesses that locate in one of New Jersey's UEZs may be eligible for tax incentives and other financial benefits provided they meet certain criteria and comply with hiring standards specific to the UEZ program.

Other Funding Sources and Resources

Land Banks: Maintained by the public sector, land banks serve to purchase, hold, and manage the redevelopment of tax-foreclosed property. Land banks allow for the acquisition of abandoned and vacant land for the purpose of selling to private developers for specific projects. As government can specify the type of project for which they will sell a developer property, they are in a strong position to control development and ensure that it becomes mixed-use.

Location-Efficient Mortgages (LEM): LEMs work on the principle that people living in mixed-use areas have less need to drive and thus spend less money on transportation. This means they are able to use a larger portion of their income to pay mortgage loans, and based on an LEM evaluation, allows them to borrow more money. Because LEMs provide mixed-use homebuyers with more borrowing power, they make the purchase of higher-cost, higher-quality mixed-use development more viable. While still a relatively new concept, LEMs provide an example of how the benefits of mixed-use can be financially utilized.

Municipalities and County Governments: Local governments offer an array of funding sources to promote smart growth and community economic development, similar to the type available at the state and federal levels.

Transportation and Community Development Initiative (TCDI): Administered by DVRPC, TCDI provides regional-level grant funding to support planning, design, and feasibility studies that encourage reinvestment and redevelopment in older communities. Because mixed-use promotes smart growth, walkability, and transit-oriented development, studies for its development are TCDI eligible.

Redevelopment Authorities (RDA): RDAs are government-affiliated entities that carry out acquisition and redevelopment of abandoned or tax-delinquent property, generally using condemnation powers. While most RDAs have a specific focus towards either economic or community development, it is important that they understand the significance and benefits of mixed-use towards both goals. Because they have eminent domain powers, RDAs are able to facilitate redevelopment in a way unique to the public sector and are thus very important.

Guides and Reports: A variety of financing resources are published by the non-profit, public, and private sectors. The following are some recommended publications, with a more extensive list of resources provided in the Appendix.

- Urban Land Institute's *Mixed-Use Development Handbook* (2005) provides a comprehensive introduction to all aspects of mixed-use, including construction, financing, planning, and design.
- DVRPC's *Municipal Resource Guide* (2007) lists general funding opportunities for community and economic development. Programs mentioned are for Pennsylvania and New Jersey and run on federal, state, county, and municipal levels.
- DVRPC's *Brownfields Redevelopment Guide* (2007) provides a list of government funding programs devoted to the rehabilitation and remediation of vacant industrial properties. Listed programs are for Pennsylvania and New Jersey and run on federal, state, county, and municipal levels.

CHAPTER 6: RECOMMENDATIONS

Success in financing has been realized through a variety of funding sources, ranging from private firms to non-profit organizations to the federal, state and local levels of the public sector. As mixed-use development continues to increase in popularity, the utilization of these resources will become more proven, successful, and established. Investors are also beginning to realize the long-term profits that can be generated from mixed-use. As the popularity of mixed-use increases, information and knowledge about how to underwrite this form of development also continues to develop. This enables investors to better assess a project's potential risks and determine whether it is worth financing.

Despite its increased popularity, mixed-use still faces significant financing challenges that require the participation and cooperation of multiple stakeholders. The following recommendations describe how municipalities, developers, investors, and other partners can provide a better financing environment for mixed-use, and thereby encourage smart growth in the Delaware Valley.

Local, County, and State Government

- Create mixed-use zoning overlay districts. Local governments are in a strong position to require private developers to implement good design, and requiring mixed-use can be one way to achieve this goal. Overlays should be focused in areas that can support additional density, such as near transit stations.
- Streamline the permitting process and other regulatory barriers. Municipalities must realize the benefits of mixed-use and develop codes that specifically address it, rather than applying single-use development laws.
- Incorporate shared or reduced parking measures into zoning ordinances. Requiring enough parking for each use separately results in an overabundance of parking. Additionally, when mixed-use projects are served by transit the need for parking may be further diminished.
- Provide additional incentives for mixed-use development. This can include tax incentives, density bonuses, and/or infrastructure improvements. Public-private partnerships can also create opportunities for mixed-use.

Winston Commons, developed by Mt. Airy, USA contains a mix of retail and condo units. (Source: Mt. Airy USA, photo by Hugh Loomis)

- Coordinate housing and economic development programs between different agencies at the local and state levels, with regards to program restrictions, application processes, and other caveats. All too often different funding programs work against each other, making it difficult to utilize multiple programs at the same time. However, when effectively coordinated, funding programs are leveraged, creating better, more profitable results.
- Work with private developers through open conversation to determine both socially and financially optimal solutions. This is important in order to signal that well designed mixed-use is wanted. Developers can also be solicited through the issuing of requests for proposal for specific sites.
- Implement outreach and education to the public to make them aware of the benefits of mixed-use through workshops, charrettes, newsletters, etc. It is largely up to local government, developers, and planners to provide this knowledge.

Developers:

- Utilize unique land assembly tools and financing techniques to facilitate the approval, construction, and financing of mixed-use projects. Examples of these include land banks, vacant property initiatives, and credit enhancement tools such as loan pools, and gap financing. As construction of mixed-use projects increases, their usage will become more relevant.
- Make realistic projections about potential development and refrain from overestimating market demand, especially for retail. Have a well thought-out pro forma and establish a realistic timeline for construction.
- Share experiences and best practices with colleagues through regional networking groups, such as the Urban Land Institute.

Financial Institutions:

- Reevaluate underwriting standards to ensure that they are not biased in favor of single-use only projects.
- Become better acquainted with the basic concepts of mixed-use, as well as its benefits, feasibility, and the financial returns it provides.
- Reassess investment and lending criteria to consider the positive effects mixed-use has on property demand.
- Explore new investment opportunities in traditionally overlooked markets, especially infill and inner city development.

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Financing Mixed-Use Development in the Delaware Valley Region

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Abstract: This report is designed to aid municipalities and developers in effectively financing mixed-use development. Included are an overview of the benefits and challenges to implementing mixed-use development, best practices in financing (including specific financing mechanisms), different organizational structures for financing, and strategies for achieving success. Case studies of successful mixed-use projects in the Delaware Valley region are presented, as well as funding sources that exist in the region.

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