

HallKeen Management, Inc.

320 Norwood Park South, Norwood, Massachusetts 02062

Tel: 781.762.4800 Fax: 781.762.4841

November 15, 2012

Reginald Johnson
City of Durham
City Hall, City Hall Plaza
Durham, NC 27701

Re: Durham Hosiery Mill, FHA Project No. 053-35525-PM-SR

Dear Mr. Johnson,



Durham Hosiery Mill Limited Partnership is currently in the process of obtaining HUD's commitment to refinance FHA insured First Loan for the above referenced project. The proposed refinance will allow the partnership to capitalize approximately \$330,000 of necessary repairs and provide approximately \$79,000 of additional cash flow annually. The detailed analysis is provided in the attached Exhibit A. The additional cash flow should also allow the Partnership to begin payments on the subordinate City of Durham loans in the amounts of \$2,265,000 and \$550,000, payable solely from surplus cash flow.

We are now seeking the City of Durham's agreement, as the holder of the subordinate City Loans, to subordinate the City Loans to the proposed FHA First Loan refinancing.

Thank you for your consideration. Mark Hess, at HallKeen Management, Inc., who can be reached at 781-915-3022, is available to discuss this matter further, or if you need additional information.

Sincerely,

DURHAM HOSIERY MILLS LIMITED PARTNERSHIP

By: Allen & Company, Inc., its general partner

By: Andrew P. Bowers
Name: Andrew P. Bowers
Title: President

Exhibit A - Durham Hosiery Mill Apartments

Durham Hosiery Mill Apartments is comprised of 151 one- and two- bedroom apartments in one historic mill building in the City of Durham, originally built in 1898 (the “**Project**”). Durham Hosiery Mill Limited Partnership (the “**Partnership**”) was organized in 1986 to redevelop the Project. The Project was first renovated and converted into apartments in 1987, and was financed with a 221(d) (4) FHA insured loan in the amount of \$5,370,800 (the “**FHA First Loan**”). The Project was also financed with two additional subordinate mortgage loans from the City of Durham, in the amounts of \$2,265,000 and \$550,000, respectively (the “**City Loans**”), which City Loans are payable solely from Project surplus cash flow, prior to maturity.

As a result of the Partnership’s participation in the HUD Mark-to-Market program in 2002, the FHA First Loan was restructured, whereby a prepayment of \$2,627,583 was made on the FHA First Loan, leaving an outstanding principal balance of \$2,281,627.52 on such loan, and (under HUD’s OMHAR program) the \$2,627,583 prepayment amount became a second mortgage loan (the “**OMHAR Loan**”), payable to HUD, and payable solely out of Project surplus cash flow. At the time of the OMHAR restructuring, the Partnership requested, and the City of Durham agreed, to subordinate the City Loans to the OMHAR Loan. This restructuring enabled the Partnership to avoid Bankruptcy.

We are now seeking the City of Durham’s agreement, as the holder of the subordinate City Loans, to subordinate the City Loans to the below-described proposed FHA First Loan refinancing.

The Partnership is currently applying to HUD for a commitment to refinance the FHA First Loan, under the 223(a)(7) program, to reduce the interest rate and lower the debt service due under the FHA First Loan. Under the proposed refinance, the outstanding principal balance of the FHA First Loan will be increased from its current balance of approximately \$1,869,655, to approximately \$2,274,700, which amount is approximately equal to the original principal balance of the FHA First Loan at the time of the OMHAR restructuring. This will result in approximately \$404,000 of net refinancing proceeds, of which approximately \$330,000 will be escrowed pursuant to HUD closing conditions and used to pay for needed capital improvements to the Project¹, and the balance will be used to pay for HUD approved refinancing costs. No refinancing funds will be distributed to, or otherwise made available to, the Partnership or its partners.

The Partnership believes that a refinancing under the current conditions will provide both immediate and substantial capital improvements to the Project, and also put the Project in a strong financial position for the long term. The refinancing will allow for additional replacement

¹ The Project is currently in fair physical condition. However, according to the latest Project CNA report, which has been reviewed by HUD in connection with this proposed refinancing, the Project will require significant additional capital expenditures for repair and maintenance in the near future, which capital needs will be funded by proceeds from the proposed refinancing.

reserves to accumulate, which will allow the Partnership to complete necessary capital repairs, and will also have a positive effect on net cash available for debt service. In addition, the refinancing will improve the subordinate loans' cash flow position, and the debt service savings on the first mortgage loan should allow the Partnership to begin payments on the subordinate OMHAR Loan and the City Loans.

The results of the Partnership's analysis are summarized in the following table, which compares cash flow waterfall for the Project, projected 2012, 2013 projection with current loan structure, and 2013 projection with refinanced first mortgage.

Durham Hosiery Mill Apartments - Cash Waterfall

	2012 Projections	2013 No Refinance	2013 Proposed Refinance
Total Income	1,379,038	1,422,374	1,422,374
Total Operating Expenses	1,014,429	1,075,434	1,075,434
Net Operating Income	364,610	346,940	346,940
<u>Operating Waterfall:</u>			
Net Operating Income	364,610	346,940	346,940
First Mortgage	210,123	210,123	131,405
Replacement Reserve Deposits	101,896	105,992	101,880
Capital Recovery (projected to be paid off in 2012)	7,962	-	-
Incentive Performance Fee	39,716	30,825	40,964
Surplus Cash	4,912	0	72,691
85% - Restricted Surplus Cash (HUD Mortgage Restructuring Note)	4,175	0	61,787
15% - City of Durham Loans	737	0	10,904
Balance	0	0	0

In summary, the Partnership believes that the proposed refinancing offers the following benefits to the Project: (i) it provides for immediate needed capital improvements for the Project; (ii) it stabilizes the Project for the long term by reducing monthly first loan debt service; and (iii) it frees up additional cash flow for payments on the subordinate loans. Therefore, the Partnership requests that the City of Durham agree to the proposed refinance of the FHA First Loan, and subordinate the City Loans to the refinanced FHA First Loan.