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Refi at Sky 55

Rental market forces 'tremendous concessions' at South Loop building

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By MICAH MAIDENBERG

Editor

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The battered economy has a prominent development group seeking permission to restructure the financing behind Sky 55, a glassy, 40-story tower that was one of the first rental buildings to go up in the South Loop during the boom years.

Central Station Development Corporation, a firm that has invested deeply in South Loop residential projects, built the tower, located at 1255 S. Michigan, and was helped in that effort with more than \$83 million in multi-family housing bonds the city issued in 2004.

Multi-family housing bonds do not create a financial liability for taxpayers; city governments merely serve as the conduit for their issuance, as they offer federal tax subsidies meant to encourage below-market rate housing development. At Sky 55, that means 83 of the 411 rental units are let out at what the city considers affordable rates.

But now the Central Station group is worried the rents produced by the building won't be enough to meet loan obligations.

"The current net income from the rental of the building — while it's fine right now — we are concerned with what's happening in our economy, what we're all dealing with every day," Tim Desmond, a principal with Central Station, told aldermen at a Feb. 8 Committee on Finance hearing. "We're concerned that our rents will not be sufficient to pay the debt on the senior mortgage."

That note, held primarily by Citibank, is worth \$68 million. But because of the building's cash flow, the developers need to lower that amount, said Bruce Weisenthal, who served as outside counsel for the 2004 bond issue, at the Feb. 8 hearing.

The Central Station group is asking the city to issue up to \$20 million in secondary bonds so it may drop the senior mortgage down to \$48 million. The firm's junior mortgage on the property would then increase from \$13 million to \$33 million.



Sky 55
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Weisenthal analogized the deal to a homeowner facing the loss of income.

“Say JPMorganChase has a mortgage on your home, and as a requirement of the mortgage you needed to be able to prove on an annual basis that your income was sufficient to cover the debt-service payments on your mortgage,” he said. “If your income was not able to do that, you would agree to make a pre-payment on the mortgage so that your mortgage loan amount would remain in balance with your ability to pay.”

The firm’s worries about Sky 55 illustrate how the roiled housing market has reset assumptions about the South Loop.

Molly Sullivan, a spokeswoman for the Department of Community Development, said that no builder wanted to put up rental units when the Sky 55 bond deal was struck six years ago. The real estate market at the time instead motivated a stream of proposals for new condo buildings and conversions.

Today, on the other hand, rental is a common part of the South Loop scene.

Some of those units, like AMLI 900, on Clark south of Polk, were planned. Other projects, like Burnham Pointe at Clark and Polk, and the Roosevelt Collection, were converted to rental after the developers that put them up failed to sell stories of condos as the recession started to hit.

Ron DeVries, a vice president for the real estate analysis firm Appraisal Research Counselors, also pointed to a “shadow market” of condos being used as rentals right now.

An Appraisal report released in January said there were 1,739 more occupied rental units in the downtown area in the fourth quarter of 2009 versus the same time in 2008 — “the highest year over year gain since we began formally tracking the downtown rental market,” the report says. And 2,234 new rentals in six different downtown buildings will be delivered this year. Appraisal’s definition of downtown stretches from Old Town to Cermak Road, and includes the West Loop.

In short, that means competition for renters is fierce.

At the Feb. 8 hearing, Desmond said that Sky 55 was 90 percent occupied but that reaching that mark hadn’t been easy. The firm was forced to offer renters “tremendous concessions,” he said at the time, such as up to three months of free rent and breaks on utilities and other fees.

The worst-case scenario, Desmond acknowledged, would be default on the loan. The long-term hope is that a better economy will allow rents to rise in the building in accordance with projections made years ago.

Brian Anderson, the manager of policy and education for the Council of Development Finance Agencies, a national organization, couldn’t speak to the specifics of Sky 55. But he said it wasn’t uncommon to see bond refinancings right now.

Seven or eight years ago, when such deals were first coming together developers “were probably using assumptions that were perfectly valid at the time,” Anderson said. But they’re not at the moment.

At the Feb. 8 hearing, Ald. Leslie Hairston (5th) asked Desmond about his firm’s calculations for the building.

“I would say we thought our finance work was fairly conservative,” Desmond answered. “It wasn’t conservative enough.”

The finance committee did not vote on the restructuring on Feb. 8.



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