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ATTORNEYS AT LAW

By Email

To: Howard Leventhal
From: Ezra N. Goodman, Esq.
Date: October 1, 2010
Re: PRHC / Reconstitution

Howie: Enclosed is a revised memo that can be distributed to the PRHC shareholders. It is the same as the prior one, except for the introduction and ending and some minor textual changes. Let me know of any questions and, more importantly, please consider how PRHC is going to handle the questions that may come from the shareholders in response to the memo. We will not respond to any communications from individual shareholders on this matter, as that would not be feasible and would create chaos.

E.N.G.



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The following is a summary of the presentation made by Ezra N. Goodman and Karol S. Robinson of the law firm Norris, McLaughlin & Marcus, P.A., at the informational meeting of shareholders of Park Reservoir Housing Corporation (PRHC) held on September 26, 2010 at 10:00 a.m. at the Van Cortlandt Jewish Center on the issue of “going private” by leaving the Mitchell-Lama program. Please note that the information presented is based on the statutes of the State of New York and the regulations of the New York State Division of Housing and Community Renewal (DHCR) as they now exist. If there are changes, then the information may also change and be materially different.

A. PRHC as a Mitchell-Lama

Today, PRHC is a Mitchell-Lama cooperative under the regulatory jurisdiction of the DHCR, and subject to Article 2 of the NYS Private Housing Finance Law. This means that there are certain restrictions and benefits:

1. Shareholders are restricted in the sale of their apartments to the next person on a waiting list at a price that is equal to what the shareholder paid plus some additional amount for mortgage amortization and capital assessments.
2. There are restrictions on the allowable income for people purchasing apartments (7 or 8 times the maintenance, depending on family size) and the co-op has very little control over who can buy an apartment at PRHC, because the purchasers come off a waiting list.
3. No subletting of apartments is allowed, so that is a restriction.
4. Apartments cannot be left to relatives by a will or given to relatives as a gift. If the shareholder passes away or moves out, the apartment can pass to a relative by succession, but that person must qualify under DHCR rules.
5. And, PRHC’s operations are restricted by the rules of the DHCR. PRHC needs to obtain DHCR’s approval for contracts, maintenance increases and many other aspects of its operations, and this can lead to bureaucratic delay and even increased costs when bidding out work.
6. The major benefit under Mitchell-Lama is that PRHC receives shelter rent tax abatement which greatly reduces the amount of real estate taxes that PRHC pays, and that

keeps the maintenance low. The abatement would continue for so long as PRHC remains Mitchell-Lama.

7. Another major benefit is that PRHC has a low interest mortgage from the State, but that mortgage will be fully paid on January 1, 2012, so the benefit will end then.

8. Another benefit, at least in the eyes of some shareholders, is that DHCR does provide supervision and oversight with respect to PRHC's operations.

9. Finally, there is the benefit of providing affordable housing to new persons of the kind that PRHC and its residents have enjoyed for many years, which is important in a City where the amount of affordable housing seems to decline every year.

B. Going Private

Under the law, PRHC is eligible to leave the Mitchell-Lama program, provided that the DHCR rules are complied with (as discussed below). At first, DHCR took the position that PRHC could not leave Mitchell-Lama, but after PRHC's attorneys pushed back, DHCR changed its position and said that PRHC could leave the Mitchell-Lama program if the shareholders chose to do so.

This process is sometimes called "going private" or "reconstitution". The end result of this process would be for PRHC to become a private market, unregulated co-op like most co-ops in the City. If this process actually took place, here is what PRHC would look like after reconstitution:

1. There would no longer be any regulatory supervision by the DHCR.
2. Shareholders will not be required to "buy" the shares of the private co-op; they will simply exchange their existing shares for new shares of stock, and their existing occupancy agreements for new agreements or proprietary leases.
3. Shareholders will be able to sell their apartments for a market price to any willing purchaser, provided that the purchaser is approved by the Board. The Board of Directors will have the authority to accept or reject applicants, so long as they are not rejected for illegal reasons, such as discrimination based on race or sex. There will no longer be any waiting lists; all apartments will be sold and bought on the open market.
4. Shareholders will be permitted to sublet, with certain restrictions to be determined by the Board.
5. Shareholders will be able to give their apartments or, at the least, the economic value, to relatives by will or by gift, but actual occupancy will still be subject to Board approval.

6. The co-op will function largely as before reconstitution. A Board will be elected by the shareholders, but the Board will now be able to act without DHCR regulation, but still subject to corporate law.

7. The major impact of going private will be economic. PRHC will lose its tax abatement; will lose its surcharge income, which PRHC receives as a Mitchell-Lama; will lose its exemption from certain State taxes, and may have to pay a large transfer tax. PRHC will also have to pay off its existing mortgage, if it reconstitutes prior to January 1, 2012, but the current amount owed is not large. The result could be a significant increase in operating expense. The way that expense has been handled by other co-ops that have reconstituted is to charge a fee, called a "flip tax", on the sale of the apartments, which is retained by the co-op and used to offset the increase in operating costs. It is set at a higher percentage on first sales after reconstitution, usually between 20-30% of the sales price, because those are the sales in which the sellers are receiving a large windfall, which is the difference between the Mitchell-Lama equity they paid for the apartment, and the market price they are receiving. But, if the flip tax is not permitted to apply to operating costs by the Attorney General's office, or if the flip tax is insufficient to cover the entire operating deficit, there could be increases in the maintenance.

C. Procedures

That is a brief rundown of what PRHC is now and what it would be as a private co-op. The final point is the procedure that has to be followed if PRHC wants to reconstitute, or if the PRHC shareholders want to obtain more specific information, including dollar estimates, about going private. It is important to keep in mind at all times that PRHC is a co-op, so the decision of whether or not to go private is in the hands of the shareholders; they make the decisions, and no one can force PRHC to go private.

Briefly, the steps are as follows:

1. First shareholder vote is to authorize the preparation of a preliminary feasibility report to explore and explain the specific consequences of going private, economic (with dollar projections) and legal, and to authorize an appropriation of up to \$50,000 to cover the cost. The study would be prepared by a team consisting of an attorney, an accountant, a real estate appraiser and an engineer. Approval requires the affirmative vote of a majority of all PRHC apartments, on the basis of one vote per apartment, taken at a shareholders meeting called for that purpose. No proxies are permitted. The report would be distributed to all the shareholders.

2. Second shareholder vote, if PRHC chooses to continue, is to authorize the preparation of a Plan of Reconstitution (Offering Plan) to be submitted to the Attorney General's office and DHCR for approval, and to authorize an appropriation, estimated to be \$125 – 150,000, to cover the cost. Approval requires the affirmative vote of a majority of all the PRHC apartments taken at a shareholders meeting, on the basis of one

vote per apartment; proxies are permitted. The Plan would be a much more detailed explanation of the proposed privatization, and would contain the actual documents to be used in the reconstitution (new Bylaws, etc.). The Plan would require the same kind of team as for the feasibility report. The Plan would have to go through several drafts; be submitted to the shareholders for a comment period; and receive approval from the Attorney General's office and DHCR.

3. Final shareholder vote, if PRHC chooses to continue, is to approve the final Plan, and to take the final steps to conclude the privatization. Approval requires the affirmative vote of two-thirds of all the PRHC apartments taken at a shareholder meeting, on the basis of one vote per apartment; proxies are permitted.

4. The entire process could take up to two years (or longer), and many decisions will have to be made along the way, often by the Board, which is deemed to be the sponsor of the reconstitution. If the original monetary appropriation, at any step, proves to be insufficient because the process is taking longer than budgeted or because of unexpected issues, there may have to be another shareholder vote to supplement the appropriation.

The above sets out the issues in general terms and, necessarily, leaves many questions unanswered at this preliminary stage. If a feasibility study is approved by the shareholders, then more specific facts and figures would be developed and presented. The purpose of the meeting, which was very well attended, and this memo, is to alert the PRHC shareholders of the options available to them, and to introduce them to this complex topic.