

**Steam and Hot Water Plant Renovation  
Update Number 3 as of September 30, 2011  
26 Lewis Street**

OVERVIEW

Several months ago the Board of Directors of East River Housing Corporation announced it had begun a project to upgrade and modernize its heat and hot water plant located at 26 Lewis Street. The 50+ year old plant produces heat and hot water for three different Cooperatives, East River, Hillman Houses and Amalgamated Dwellings. Costs related to the operation of the plant have been shared by the three Corporations based on proportionate square footage; this arrangement had been entered into when the facility was first opened and was based on a good faith agreement.

As stated, the facility is over fifty years old and can only burn number 6 fuel oil, a dirty fuel. Testimony to the maintenance and care given the equipment, it still works. However, it is not as efficient nor is it as clean burning as it could be. By changing to natural gas, with an alternate of number 2 fuel oil, the plant will be capable of burning the cheapest, cleanest, most dependable sources of fuels available.

STATUS

With contracts in place with two companies to address asbestos abatement and the demolition of a previously decommissioned boiler, the next step was to select a company to implement the actual plant renovation, including purchase and installation of a new boiler, purchase and installation of new burner tips on two existing boilers and installation of all specified controls, connections and safety equipment to complete the conversion and modernization. A pre-qualified list of 9 possible vendors was established by the two Engineering firms hired by the Corporation. Five and four companies with the experience, reputation and financial condition were recommended respectively by our two separate engineering firms. A Request for Bid (RFB) was developed by our legal counsel; the engineering specifications were developed by our engineer design firm and signed off by our quality control engineer. The RFB was distributed to all companies on the pre-qualified vendor list. Two walk-thru meetings were held, each with two groups of vendors in attendance; space and vendors' schedules did not allow for one meeting with all vendors present at the same time. All questions which were asked by any vendor were collected and answered in writing, with copies of the questions and answers going to each prospective vendor. This was done so as not to give any vendor an advantage over a competitor and ensure the best proposal from each vendor.

Seven proposals were received and were evaluated by the engineers for technical compliance with the specifications. Proposers were encouraged to recommend alternatives to the specifications in the RFB where they felt warranted. In all such cases they were asked to justify their recommendations.

The engineers evaluated the proposal and the best three proposers were given several opportunities to reduce the costs of their proposals. Eventually Dynamic Energy Group, Inc. was selected as the winning bid and a contract entered into. The boiler demolition and rubbish removal contract was assigned to Dynamic to ensure the work is done in compliance with Dynamic's needs, but it now appears that the demolition work will be separately contracted to ensure its timely completion. Dynamic and East River have made application for all necessary permits from various government entities. The burner tips and new boiler have been ordered.

The maintenance staff and boiler room staff have been working diligently for almost a year doing necessary work preparing the Lewis Street site for the project.

GAS SUPPLY

When purchasing gas used for heating, it is bought in two distinct parts, the delivery service and the natural gas commodity itself.

Con Edison has a monopoly on the delivery of gas to a user in New York City. East River contracted with Con Ed for delivery service that involved a significant extension of their existing system to be able to deliver the gas to the plant. Con Ed completed their part of the project: bring the gas line to East River's property line. This was completed during the summer so as to not interfere with the kids while school is in session.

There are 71 companies qualified to sell gas in Con Ed's territory and are known collectively as ESCOs (Energy Service Companies). Request for Qualifications was sent to each company in early August. Of the 9 companies who responded, seven (7) were deemed qualified by the special gas counsel hired by East River Housing Corporation.

These seven were sent Requests for Proposals (RFP) and six (6) responded with proposals by the deadline for submission. Following a series of opportunities for vendors to reduce their bid, including a request for “best and final,” Castle Energy Solutions was awarded the contract. The contract calls for gas to be provided under two separate circumstances; the first period (December 1, 2011 to April 1, 2012) during implementation which will be done over a period of several months when one boiler with a new burner tip will be implemented, then the second boiler with the new burner tip will be implemented and finally the new boiler will be implemented. The second period will be post conversion and the contract will run for two years from April 1, 2012 to March 31, 2014. Castle Energy Solutions also allows the Corporation an annual opportunity to lower the price and extend the term if the gas market reflects significantly lower prices than when the contract was set. No other bidder put this option in writing

## FUNDING

After exploring several alternatives options for funding the project, it was concluded that increasing the amounts of East River’s and Hillman’s mortgage loans was the cheapest and most cost effective option available for funding this project. Both East River and Hillman had their own mortgage and unsecured loans.

East River’s previous mortgage and unsecured loans were for just under \$15 million in the aggregate, at an interest rate of 4.4%. They had approximately two years remaining on the term. Management successfully negotiated a new mortgage loan for \$25 million at a rate of 4% for the first 5 years and 4.5% for the next five years; the loan also provides for a third term of five years, at a not yet determined interest rate (fixed or variable) but, before that third term commences, the loan may be paid off or refinanced without premium or prepayment charge during a two-month period at the end of the tenth year.

The new mortgage loan is of a type (often called an “interest-only” or a “balloon mortgage” loan) where East River, as borrower, is required to pay only the interest for a specified period of time, 10 years in this instance, at one interest rate for the first five years and a slightly higher rate for the next five years; during the term of the loan, the borrower is not required to make any payment on the principal, the actual amount borrowed. At the end of the time period, the borrower must pay off the principal in total. A common practice at that time is for borrowers on this kind of loan to negotiate a new mortgage loan and use the newly borrowed money to pay off the previous mortgage loan.

A critical aspect to the new mortgage loan is that, although no principal payments are required during the term, it allows East River, the borrower, to make a once each year payment on the principal, the amount borrowed, of up to \$2 million per year. It is hoped that the funds for such payments will come from the savings realized from the change in fuel from number 6 Fuel Oil to gas, with number 2 Fuel Oil as a back up, and the upgrade to the boiler plant.

The total amount of the mortgage loan was increased to \$25 million to cover the projected inspection of the exteriors of our four buildings over 6 stories tall and the costs of repair of any deficiencies discovered. These periodic inspections are mandated by the City under Local Law 11 and are considered a capital improvement. A copy of a preliminary report is available for review at the management office. As a note, Seward Park is in the process of addressing their Local Law 11 compliance.

## AMALGAMATED DWELLINGS

At the end of the first week in September, East River’s attorney Ezra Goodman, received a letter expressing the desire of Amalgamated Dwellings Board to withdraw from the project and to stop discussing the agreement among East River, Hillman and Amalgamated that would set forth the terms on which the parties long standing arrangement would continue. This caught management, our attorney, and the Board’s of East River and Hillman by surprise. Not only had Amalgamated participated in the drafting of a three party agreement between the three coops formalizing our existing “hand shake gentlemen’s agreement,” this agreement had been modified several times to address their President’s concerns; he had actually signed a version of the agreement which then underwent additional negotiation. Their President had attended many meetings on the actual implementation of the project, and decisions sometimes modified to address his concerns. Without prior warning or notice, he now stated that they will no longer require East River provide heat and hot water within six months. However, anticipating their estimate may be unrealistic; they have requested a three month extension. In the spirit of cooperativeness, East River has agreed to all of these requests and our lawyer sent them an agreement stating such. For several weeks they have been in possession of this agreement but have not signed it. East River and Hillman have had to repeatedly change plans for the boiler plant, delaying the project and incurring Engineering expense, Legal expense, and recalculated funding requirements. The Boards and Management of East River and Hillman continue to pursue this turn of events in the interests of our Coops.

Sincerely yours,

Leonard Greher  
President of the Board of Directors