

**PENDERBROOK APARTMENTS
FAIRFAX, VIRGINIA**

**Potomac Realty Advisors, Inc.
1010 North Glebe Road, Suite 800
Arlington, Virginia 22201**

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APPENDIX A: FLOOR PLANS

I. INTRODUCTION

POTOMAC REALTY ADVISORS

1010 NORTH GLEBE ROAD
SUITE 800
ARLINGTON, VIRGINIA 22201
703-522-6200

June 17, 1988

Real Estate Investment Committee Members
United States Fidelity & Guaranty Company
100 Light Street
Baltimore, Maryland 21202

**Re: Penderbrook Apartments
Fairfax, Virginia**

Dear Sirs:

Enclosed for your review is the complete investment report on the Penderbrook Apartments, a 424-unit rental community in Fairfax, Virginia, which was presented at the Real Estate Investment Committee meeting on June 15, 1988. The proposed investment is a debt/equity joint venture with National Housing Partnership Real Estate Corporation and is composed of a fixed rate mortgage of \$20,000,000 and an equity commitment of \$15,350,000 for a total investment of \$35,350,000. Exhibit I-1 is the Application Letter which summarizes the proposed investment.

The Property — Penderbrook Apartments is a 424-unit garden apartment community located in the Fair Oaks area of Fairfax County, Virginia. The project is on an 18.9-acre tract of land and is comprised of 55% one-bedroom and 45% two-bedroom units housed in 19 buildings. Penderbrook Apartments is part of a larger master development which contains the Penderbrook Golf Course and when completed will be an 1,800-unit master planned community encompassing 294 acres.

The subject property has excellent accessibility, location, and complementary adjacent land uses. Penderbrook Apartments is strategically located on Route 50, one-eighth of a mile north of Interstate 66, directly adjacent to the Fair Oaks Mall, the largest mall in Fairfax County. Both Interstate 66 and Route 50 are major east-west arterials servicing the metropolitan Washington area. The subject property is just northwest of the intersection of Interstate 66 and Route 50.

The project will consist of 424 units in 19 buildings of wood frame construction, face brick veneer on the ground and second floors, and cedar siding on the top floors. The project will feature a 3,000 square foot concrete pool, two hot tubs, an exercise room, and a clubhouse with kitchen facilities, and male/female bath and shower facilities. Additionally, since the project is located within a larger Planned Use Development (PUD), residents of Penderbrook Apartments will have access to all the amenities of the PUD, including Golf Course membership privileges, clubhouse, pool, and tennis courts. Individual units average 735 square feet of net rentable area, and feature wall-to-wall carpeting,

patios/balconies, under-cabinet microwave ovens, refrigerators with ice makers, fireplaces, dishwashers and washer/dryers in all units, and pitched ceilings in all top floor units.

The Market — The metropolitan Washington, D.C. region has experienced substantial growth in the current decade, and Fairfax County has accounted for almost half of this recent increase. While the entire region experienced almost a doubling in population during the 1950 through 1975, Fairfax County's population increased over five times. Fairfax County's labor force is one of the most educated and skilled in the region, explaining why Fairfax County also has one of the highest median family income in the nation. The labor force is primarily white collar (77% in 1980).

The rental housing availability in Fairfax County has been very tight historically. During the past five years the vacancy rate for rental housing in Fairfax County has averaged 2.8%, and during the past three years the average vacancy rate has been 3.0%. Because of condominium conversion and apartment zoning policies of the county, the supply of apartment units has actually declined during the past twelve years. This has been reflected in the average rental rate increases in the county, with average rental rate increases of 8.8% for the past five years, and 9.7% for the past three years. During the past twelve years the average vacancy rate has never exceeded 4.4%, and has been as low as 2.1%. The Penderbrook Apartments are strategically located in the heart of this strong market.

The Partner/Borrower — The Partner/Borrower in the proposed transaction is NHP Real Estate Corporation (NHPREC), a wholly owned subsidiary of National Housing Partnership, Inc. (NHP). NHP has become one of the largest owners, developers and managers of residential housing in the United States, with 77,840 units in 44 states. NHPREC was formed in early 1987 to conduct the ongoing multi-family market rate and commercial development business of NHP.

The property will be managed by NCHP Property Management, Inc., a wholly owned subsidiary of NHP. NCHP Property Management, Inc. presently manages 423 properties totalling 63,985 units.

The Risk and Return — This debt/equity joint venture is structured as two separate financing transactions: \$20,000,000 fixed rate first mortgage and a \$15,350,000 equity contribution to a general partnership. The mortgage earns a 9.5% annual interest rate, has a 10-year term, and provides for a five-year lock-in period and a yield maintenance provision if prepayment occurs between the sixth and tenth years. The equity investment earns a 9.5% annual cumulative preferred return and receives 50% of the cash flow after the preferred return and 50% of the residual cash proceeds at sale. At closing, \$15,350,000 of the equity capital is paid to the general partnership, with \$1,500,000 placed into escrow as a

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USF&G
June 17, 1988
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rent achievement holdback. The escrowed monies are disbursed as the project achieves its proforma rent and occupancy levels.

The expected yields (or internal rate of return) assuming a 5% growth rate in income and expenses are as follows:

	<u>Expected Yield</u>
Total Capital (\$35,350,000)	11.57%
Mortgage Capital (\$20,000,000)	9.5%
Equity Capital (\$15,350,000)	13.61%


The proforma cash return on the total investment is 7.7%, and the pro forma cash return on equity capital is 5.13%.

The major risk in this investment is the lease-up or market risk. The investment structure addresses this market risk specifically in two ways. First, the seller must achieve 80% economic occupancy before the property can go to closing. The use of economic occupancy will completely eliminate any effects of concessions or giveaways used in the lease-up period. Second, the seller will be required to earnout the top \$1,500,000 of the purchase price, and will not completely earnout the \$1,500,000 until the seller has achieved 95% economic occupancy. The initial funding gives USF&G proper security and yield based on occupancy at closing.

The financial risk in this investment is minimized for several reasons. The pro forma projected debt coverage ratio in the first year is 1.43, and NHPREC will provide a two-year negative cash flow guarantee (limited to \$1,900,000). In addition, there is an 11.5% yield maintenance provision, which states that NHPREC does not receive its share of net sales proceeds until USF&G has received an 11.5% overall annual yield (IRR) on its total investment (debt and equity).

In conclusion, we feel that the risks in this investment are acceptable, and that the expected returns are attractive. Therefore, Potomac Realty Advisors recommends that the Real Estate Investment Committee approve the commitment of \$35,350,000 to a debt/equity joint venture under the terms and conditions outlined in Exhibit I-1.

Sincerely,


James E. Davis
Vice President

APPLICATION LETTER

POTOMAC REALTY ADVISORS

1010 NORTH GLEBE ROAD
SUITE 800
ARLINGTON, VIRGINIA 22201
703-522-6200

June 14, 1988

Mr. Richard A. Vinci
Director-Project Finance
National Housing Partners
1225 Eye Street N.W.
Washington, D. C. 20005

Re: Penderbrook Apartments
Fairfax, Virginia

Dear Richard:

Potomac Realty Advisors is prepared to recommend to its clients Investment Committee to issue a commitment for a fixed rate first mortgage loan ("the "Loan") subject to the terms and conditions described below.

Property:	Penderbrook Apartments. A 424-unit garden apartment in 18 buildings of 2-story and 3-story split level design. Project also includes a 4,000 foot club house with fireplace, a community house with a spa and an olympic size swimming pool, an exercise room, lighted tennis courts and jogging trails.
Location:	Penderbrook Apartments is located within the Penderbrook Master Plan Development which is built around Penderbrook Golf Course in Fairfax, Virginia.
Site:	Approximately 18.9 acres.
Borrower:	A to-be-formed general partnership, the partners of which will be NHP Real Estate Corporation or an affiliate ("NHPREC") and United States Fidelity & Guaranty Company or an affiliate ("USF&G").
Lender:	USF&G
Loan Amount:	\$20,000,000 (See Exhibit B)
Interest Rate:	9.5%


Richard A. Vinci
June 14, 1988
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Amortization: Not applicable, interest only.

Term: 10 Years

Prepayment: No prepayment before the 5th anniversary of initial funding and a prepayment fee of the greater of (a) 1% of the outstanding loan balance in year 6 and thereafter, or (b) a yield maintenance fee, as calculated in accordance with the procedure described in Exhibit F, based on the reinvestment of the loan proceeds into U.S. Treasury Notes of a like maturity.

Cure Provision: Borrower shall not, under the Loan Documents, be given notice of or be permitted any curative or grace period to correct any monetary default thereunder, except for a five (5) day grace period after which a late charge of five percent (5%) of the amount due shall be payable. If payment is not received within the 5-day grace period, Lender shall have the right to accelerate the Loan after (i) providing Borrower with five (5) business days written notice of Lender's intention to so accelerate the Loan, and (ii) Borrower's failure to cure such default within such five (5) business day period. If Borrower fails to cure such default within such five (5) business day period, interest at the default rate shall be payable on the Loan from the date payment was due until the date paid. The Loan Documents shall provide for written notice of default to Borrower and thirty (30) days to cure non-monetary defaults, except for defaults relating to (A) institution of bankruptcy or other proceedings relating to creditor's rights, except that Borrower shall have sixty (60) days within which to have a court dismiss an involuntary bankruptcy proceeding brought against Borrower, (B) ~~dissolution of the Borrower,~~ (C) ~~prohibited~~ transfers of the management or control of Borrower or the creation by Borrower of additional material encumbrances on the Property, (D) failure to pay taxes when due subject to the right to contest such taxes, provided Lender receives a bond or other security therefore acceptable to Lender, (E) failure to pay a final judgement as required, and (F) material variation from NHPREC's representations and warranties. **IN THE LOAN COMMITMENT.**



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Recourse: The Loan will be non-recourse to Borrower and its partners.

Commitment Fee: \$707,000; \$353,500 to be paid in cash which is earned upon acceptance of the Commitment; all of which will be returned to NHPREC in the event that Lender fails to close on the Loan when it is required to do so, and a \$353,500 letter of credit, which letter of credit will be returned to NHPREC at closing or in the event that Borrower does not acquire the Property due to an inability or unwillingness of the seller of the Property to close on the sale of the Property in accordance with the terms of the purchase agreement for the Property.

Funding: \$20,000,000. Closing on the Loan will occur simultaneously with the acquisition by Borrower of the Property and USF&G's initial equity capital contribution (described in Exhibit A). Closing on the Loan is to occur no later than December 31, 1988; provided, however, that if the purchase contract is in full force and effect, NHPREC shall have the right to extend the date of closing on the Loan for two additional 90-day periods by delivering written notice to Lender of such extension and by paying Lender an extension fee of \$176,750 for each extension period by not later than 10 business days before the extension period begins.

Lender Approval: This application and the transaction contemplated herein must be approved by Lender's Investment Committee by not later than June 22, 1988.

Additional Loan Provisions: The following provisions will be included in USF&G's loan documents, however, Lender will waive these provisions for the Loan if NHPREC has already complied with them under the Borrower's Partnership Agreement.

- A. Leases:** Lender shall have the right to review and approve the standard form of lease for the Property and shall be deemed to have approved of all existing and future leases for the Property apartments which conform to such standard lease form and to the agreed-upon rental rates, attached hereto as Exhibit C.
- B. Secondary Financing:** Secondary financing is not permitted without Lender's prior written approval.
- C. Budget Approval:** During the term of the Loan, Borrower shall submit to Lender annual operating and capital budgets for the Property for Lender's reasonable review and approval.
- D. Callable on Sale:** If the Property is sold or substantial partnership interests owned by either of the partners are sold (other than sales of partnership interest to affiliated parties), the Loan shall be callable and payable along with any applicable prepayment fees or yield maintenance fees.
- E. Management:** Lender approves Parkford Companies, Inc. as the initial Property Manager until the release of the Rental Achievement Holdback described in Exhibit A. Thereafter, Lender approves of NCHP Property Management, Inc. as the Property Manager.
- F. Accountant:** The Partnership will engage an accounting firm satisfactory to Lender who shall perform an annual audit of the Partnership. Lender approves of Resnick, Fedder & Silverman or Touche, Ross & Co. as the accounting firm.

Contingencies: The Commitment shall have the following contingencies:

- A. Economic Due Diligence:** The Commitment will be contingent upon Potomac Realty Advisors satisfactorily completing its Economic Due Diligence by not later than June 22, 1988.

B. Engineering:

NHPREC will engage an engineer approved by the Lender to perform an inspection of the mechanical, electrical, and structural components of the Property. Lender reserves the right to review and approve the scope and substance of the inspection by not later than June 22, 1988 provided Lender receives the complete inspection report by June 18, 1988. The cost of the engineering study will be paid by NHPREC. USF&G must be satisfied with, and approve of, the results of the inspection by not later than June 22, 1988. Lender approves Merrit & Harris, Inc. as engineers. NHPREC will be reimbursed at closing for engineering fees subject to the \$350,000 aggregate maximum amount.

C. Environmental:

Lender shall have received an environmental study of the Property by a reputable engineering or environmental firm acceptable to Lender which demonstrates to Lender's reasonable satisfaction that there are not environmental hazards or hazardous or toxic materials existing upon or affecting the Property. Lender shall have approved of such study by not later than five (5) business days after its receipt of such study from NHPREC. The analysis will involve a physical inspection of the Property and a historic review of the previous uses of the land. In the event that the historic review indicates that toxic materials may exist in the soil, soil borings will be conducted and the results will be analyzed by a laboratory. All costs associated with the environmental study will be paid by NHPREC. Lender approves ICF/Clement, Inc. as the environmental surveyor. NHPREC will be reimbursed at closing for the environmental report costs subject to the \$350,000 aggregate maximum amount.

D. Leases:

Lender reserves the right to review and approve the standard form of lease for the Property and shall be deemed to have approved of all existing and future leases for the Property apartments which conform to such standard lease form and to the agreed-upon rental rates attached hereto as Exhibit C.

- E. Equity Joint Venture:** NHPREC's acceptance of USF&G's Partnership Agreement and other documents relating to the equity joint venture portion of this transaction, the terms of which are outlined in Exhibit A.
- F. Committee Approval:** This Recommendation Letter must be approved by Lender's Investment Committee on or before June 22, 1988.
- G. Due Diligence:** The Commitment will be contingent upon Potomac Realty Advisors being satisfied with the results of its due diligence with respect to the Property by not later than June 22, 1988.
- H. Market Value Appraisal:** By not later than June 22, 1988, Lender will receive and approve of a market value appraisal of the Property from an MAI-designated appraiser approved by USF&G stating that the market value of the Property assuming stabilized occupancy is at least \$36,000,000. The cost of the appraisal will be paid by NHPREC. Lender approves Joseph Blake & Associates as the appraiser. NHPREC will be reimbursed at closing for the appraisal costs subject to the \$350,000 aggregate maximum amount.
- I. Title and Survey** Lender reserves the right to review and approve the condition of the title, title insurance and the Property survey. All costs associated with the title, title insurance and survey will be paid by NHPREC. Lender approves the Chicago Title Insurance Company as the title insurer. NHPREC will be reimbursed at closing for the title and survey costs subject to the \$350,000 aggregate maximum amount.
-
- J. Management and Leasing:** Execution of a Management and Leasing Agreement satisfactory to Lender and NHPREC providing for (i) the management by Parkford Companies, Inc. until the release of the Rental Achievement Holdback described in Exhibit A, and (ii) thereafter, the management of the Property by NCHP Property Management, Inc.


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K. Closing Costs:

All costs associated with the closing on the Property, including Lender's reasonable attorney's fees will be paid by NHPREC. NHPREC will be reimbursed at closing for all third party closing costs up to an aggregate maximum amount of \$350,000.

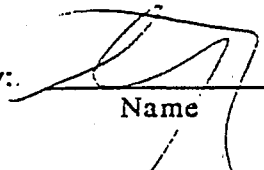
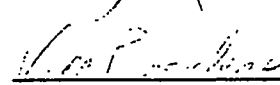
If the terms outlined in this letter are acceptable, please sign below and return this letter with a check in the amount of \$75,000, as an application fee, by June 14, 1988. The application fee will be returned to Borrower (less reasonable documented out-of-pocket expenses incurred to date by Lender and/or Potomac Realty Advisors) if Lender does not issue a commitment according to the terms outlined in this letter. The application fee will be earned by Lender upon issuance of a commitment according to the terms outlined in this letter, and the \$353,500 cash Commitment Fee to be paid by NHPREC will be reduced by \$75,000.

Sincerely,


Daniel B. Kohlhepp
President

Accepted:

NHP REAL ESTATE CORPORATION

By: 
Name

Title

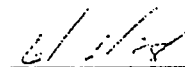

Date

Exhibit A

Penderbrook Apartments Fairfax, Virginia

This Exhibit summarizes the terms on which Potomac Realty Advisors is prepared to recommend to its client's Investment Committee that it enter into a general partnership (the "Partnership") with NHP Real Estate Corporation and/or affiliates ("NHPREC") which shall acquire the Penderbrook Apartments (the "Property"), subject to the terms and conditions described in this letter.

Property: Penderbrook Apartments

Location: 3905 Penderview Drive, Fairfax, Virginia

Real Property:

- * Land Area: 18.9 Acres, zoned PDH-8 (Residential Planned Community).
- * Building Description: 424-Unit Garden Apartment in 18 Buildings.

Personal Property: All personal property owned by the Partnership and used in connection with the Property.

Fixed Rate Debt (USF&G):

- * Mortgagor -- A to-be-formed general partnership
- * Mortgagee -- United States Fidelity & Guaranty Company and/or affiliates ("USF&G").
- * Term -- 10 years
- * Prepayment Prohibition -- through year 5
- * Loan Amount -- \$20,000,000
- * Interest Rate -- 9.5%
- * Annual Payment -- \$1,900,000

Parties: NHPREC and USF&G.


Basic Responsibilities:

USF&G

- (1) Provide equity capital in the amount of \$15,350,000.

NHPREC

- (1) Responsibilities Prior to Acquisition of the Property by the Partnership:

- (a) Prepare and submit to USF&G an operational plan acceptable to USF&G for the management and leasing of the Property. The plan shall include (1) a budget for the operation of the Property for the twelve (12) month period immediately following acquisition of the Property to the Partnership and (2) a projected capital and operational budget for the Property thereafter.
 - (b) Coordinate with USF&G regarding formation of the Partnership, acquisition of the Property by the Partnership, and otherwise generally be responsible for organizing the Partnership.
 - (c) Satisfy the requirements and contingencies of the Permanent Loan.
- (2) Cause the Property to be acquired by the Partnership.
- (3) Responsibilities After Conveyance of the Property to the Partnership:
- (a) Property Management - Property management fees shall not exceed 5.0% of collected rents for management of the Property apartments. Until the release of the Rental Achievement Holdback (described in this Exhibit A), Parkford Companies, Inc. shall receive a management fee of 4% of collected rents and NHPREC shall receive an asset management fee of 1% of collected rents. Thereafter, NHPREC Property Management, Inc. shall serve as the Property Manager and shall receive a management fee of 5% of collected rents.
 - (b) NHPREC shall oversee and report to USF&G on a monthly basis a progress and leasing report.
 - (c) NHPREC shall market, coordinate, and supervise the sale of the Property. NHPREC shall receive a disposition fee which is equal to the difference between (A) 3% of the ^{Gross} sales price and (B) all third party selling expenses.
- 

USF&G's Invested Capital:

1. Concurrently with the acquisition of the Property by the Partnership and closing on the Loan (the "Closing"), USF&G shall contribute \$15,350,000 ("Initial Capital Contribution") to the Partnership.
2. **Rent Achievement Holdback:**

Of the \$15,350,000 to be contributed by USF&G, a portion of such amount shall be paid into an escrow account at Closing in an amount equal to the product of (i) the difference between 95% and the actual percentage of Property units in regard to which tenants are paying rent at the agreed upon rental rates attached as Exhibit C (the "Economic Occupancy"), times (ii) \$100,000. Thereafter, for a period of twelve (12) months, \$100,000 shall be released from the escrow account for each one percent increase in Economic Occupancy, or portion thereof.* Any amounts paid by USF&G into such escrow account not released by the end of such twelve (12) month period shall be returned to USF&G and shall be a reduction to the equity capital contributed by USF&G. All interest earned on such amounts paid by USF&G shall be paid to the Partnership. * PROVIDED THAT ALL FUNDS REMAINING IN SUCH ESCROW ACCOUNT SHALL BE RELEASED TO THE

Subsequent Contributions: SELLER OF THE PROPERTY IF THE PROPERTY ACHIEVES 95% OCCUPANCY OR ACHIEVES A 3,838,836 ECONOMIC OCCUPANCY, OR APPROVED USF&G LEASES, BEFORE THE END OF SAID TWELVE(12) MONTH PERIOD.

Contribute 50% of all cash flow deficits and capital shortfalls from operations (or a percentage which corresponds to its percentage interest in the Partnership if its interest in the Partnership has been increased or decreased pursuant to the dilution provisions contained herein) following earlier to occur of (i) the second anniversary of initial funding, or (ii) such time as NHPREC has contributed \$1,900,000 or more to the Partnership ("Subsequent Capital Contributions").

NHPREC

Contribute 100% of all cash flow deficits and capital shortfalls from operations until the earlier to occur of (i) the second anniversary of initial funding, or (ii) such time as NHPREC has contributed \$1,900,000 or more to the Partnership. Thereafter, NHPREC shall contribute 50% of all cash flow deficits and capital shortfalls from operations (or a percentage which corresponds to its percentage interest in the Partnership if its interest in the Partnership has been increased or decreased pursuant to the dilution provisions contained herein)("Subsequent Capital Contributions").

Closing:

The parties intend that the execution of the Partnership's Partnership Agreement and the acquisition of the Property by the Partnership shall occur simultaneously, and such events shall occur on or before the earlier to occur of December 31, 1988 (unless NHPREC has exercised its right to extend such date for two (2) ninety-day periods or when the Property reaches 80% Economic Occupancy.

**Percentage
Interest in the
Partnership:**

USF&G: 50%

NHPREC: 50%

Percentage interests, capital contribution and distribution percentages shall be adjusted in accordance with the Dilution Formula set forth below.

**Distribution of
Cash Flow:**

Distribution of cash flow shall be made quarterly and shall be in the following order of priority:

USF&G

First Priority -- Payment of a 9.5% cumulative preferred return on its Invested Capital (i.e., Initial Capital Contribution less disbursements which are returned to USF&G from the Rent. Achievement Holdback);

Second Priority -- Pro rata with NHP's Second Priority, payment of a 9.5% cumulative preferred return on its Subsequent Capital Contributions, if any;

Third Priority -- 50% of the remaining cash flow after payment of First and Second Priority cash flow distributions.

NHPREC

Second Priority -- Pro rata with USF&G's Second Priority, payment of a 9.5% cumulative preferred return on its Subsequent Capital Contributions, if any;

Third Priority -- 50% of the remaining cash flow after payment of USF&G's First Priority capital distribution and both partners' Second Priority cash flow distributions.

All unpaid cumulative preferred returns will be compounded annually at the rate of 9.5%.

**Distribution
of Capital
Proceeds:**

Distribution of capital proceeds^{*} shall be in the following order of priority:

USF&G

First Priority -- Payment of its Invested Capital (i.e. Initial Capital Contribution less disbursements which are returned to USF&G from the Rent Achievement Holdback);

Second Priority -- Payment of any earned but unpaid cumulative preferred return on its Invested Capital (i.e. Initial Capital Contribution less disbursements which are returned to USF&G from the Rent Achievement Holdback);

Third Priority -- Pro rata with NHP's Third Priority, payment of its Subsequent Capital Contributions, if any;

Fourth Priority -- Pro rata with NHP's Fourth Priority, payment of any earned but unpaid cumulative preferred return on its Subsequent Capital Contributions, if any;

Fifth Priority -- Any remaining distributions of capital proceeds shall be paid to USF&G until such time as USF&G's overall annual yield (IRR) on initial total investment (Invested Capital, excluding any Subsequent Capital Contributions) is equal to 11.5%. Exhibit D shows the mathematical calculation of this amount.

Sixth Priority -- Pro rata with NHP's Sixth Priority, an amount, if any, necessary to bring the overall annual yield (IRR) on Subsequent Capital Contributions up to 11.5%. Exhibit E shows the mathematical calculation of this amount.

Seventh Priority -- 50% (or as adjusted) of any remaining cash after payment of First, Second, Third, Fourth, Fifth and Sixth Priority capital distributions.

* i.e., FUNDS REMAINING FROM THE SALE OF THE
PROPERTY AFTER PAYING ALL NORMAL COSTS INCIDENT
TO SUCH SALE INCLUDING, WITHOUT LIMITATION,
NHPREC'S DISPOSITION FEE, IF ANY.

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NHPREC

Third Priority -- Pro rata with USF&G's Third Priority, payment of its Subsequent Capital Contributions, if any;

Fourth Priority -- Pro rata with USF&G's Fourth Priority, payment of any earned but unpaid cumulative preferred return on its Subsequent Capital Contributions, if any;

Sixth Priority -- Pro rata with USF&G's Sixth Priority, an amount, if any, necessary to bring the overall annual yield (IRR) on Subsequent Capital Contributions up to 11.5%. Exhibit E shows the mathematical calculation of this amount.

Seventh Priority -- 50% (or as adjusted) of any remaining cash after payment of USF&G's First, Second and Fifth Priority capital distributions and both partners, Third, Fourth and Sixth Priority capital distributions.

Required
Partnership
Provisions:

The following are provisions that shall be incorporated into the Partnership's Partnership Agreement.

A. Dilution of
Ownership:

If either USF&G or NHP fails to make any required contribution, then (i) the Partnership, upon consent of all partners, may borrow such amount, or (ii) the contributing party may make the required contribution on behalf of the noncontributing party and the dilution formula outlined below shall apply.

B. Dilution
Formula:

For every \$2,000 (or increment thereof) of required but unfunded contribution, the noncontributing partner's percentage interest in the Partnership shall be reduced by one-fourth percentage point (.25%) and the contributing partner's percentage interest shall increase correspondingly.

C. Partnership
Term and Sale
of Partnership
Interests:

The term of the Partnership is 50 years. Either party may implement a mutually agreed upon buy/sell provision for Partnership interests. However, USF&G has the right to approve the transfer or sale of any partnership interests.

- D. Leases: USF&G shall have the right to review and approve the standard form of lease for the Property and shall be deemed to have approved of all existing and future leases for the Property apartments which conform to such standard lease form and to the agreed-upon rental rates, attached hereto as Exhibit C.
- E. Secondary Financing: Secondary financing is not permitted without USF&G's prior written approval.
- F. Budget Approval: USF&G shall have the right to review and reasonably approve all operating and capital budgets for the Property.
- G. Right of First Offer: If the Partnership desires to sell the Property, USF&G shall have the Right of First Offer to purchase the Property.
- H. Accountant: The Partnership will engage an accounting firm satisfactory to USF&G who shall perform an annual audit of the Partnership. USF&G approves Resnick, Fedder & Silverman or Touche, Ross & Co. as the accounting firm.
- I. Major Decisions: Major partnership decisions^{*} shall require the prior consent of all partners until such time as either partner's percentage interest exceeds 75% of the total percentage interest in the Partnership.
- If at any time either partner's percent interest in the Partnership equals or exceeds 75%, that partner shall be authorized, to the extent permitted by applicable law, to make all Partnership decisions and to take all actions on behalf of the Partnership without the approval of the other partner.

Contingencies: The following are conditions precedent to USF&G's obligation to enter into the Partnership:

- A. Engineering: NHPREC will engage an engineer approved by the Lender to perform an inspection of the mechanical, electrical, and structural components of the Property. Lender reserves the right to review and approve the scope and substance of the inspection by not later than June 22, 1988 provided Lender receives the complete inspection report by June 18, 1988. The cost of the engineering study will be paid by NHPREC. USF&G must be satisfied with, and approve of, the results of the inspection by not later than June 22, 1988. Lender approves Merrit &

** WHICH SHALL BE MORE FULLY DESCRIBED IN THE PARTNERSHIP AGREEMENT*

Harris, Inc. as engineers. NHPREC will be reimbursed at closing for engineering fees subject to the \$350,000 aggregate maximum amount.

- B. Environmental:** Lender shall have received an environmental study of the Property by a reputable engineering or environmental firm acceptable to Lender which demonstrates to Lender's reasonable satisfaction that there are not environmental hazards or hazardous or toxic materials existing upon or affecting the Property. Lender shall have approved of such study by not later than five (5) days after its receipt of such study from NHPREC. The analysis will involve a physical inspection of the Property and a historic review of the previous uses of the land. In the event that the historic review indicates that toxic materials may exist in the soil, soil borings will be conducted and the results will be analyzed by a laboratory. All costs associated with the environmental study will be paid by NHPREC. Lender approves ICF/Clement, Inc. as the environmental surveyor. NHPREC will be reimbursed at closing for the environmental report costs subject to the \$350,000 aggregate maximum amount.
- C. Leases:** USF&G reserves the right to review and approve the standard form of lease of the Property and shall be deemed to have approved of all existing leases and future leases which conform to such standard lease form and to the agreed-upon rental rates attached hereto as Exhibit C. As a contingency for USF&G to enter into the Partnership, all leases listed in Exhibit C must be in full force and effect.
- D. Loan:** NHPREC's acceptance of USF&G's commitment to make the Loan.
- E. Committee Approval:** This Exhibit must be approved by USF&G's Investment Committee not later than June 22, 1988.
-
- F. Due Diligence:** The Partnership Agreement will be contingent upon Potomac Realty Advisors being satisfied with the results of its due diligence with respect to the Property not later than June 22, 1988.
- G. Market Value Appraisal:** By not later than June 22, 1988, Lender will receive and approve of a market value appraisal of the Property from an MAI-designated appraiser approved by USF&G stating that the market value of the Property assuming stabilized occupancy is at least \$36,000,000. The cost of the appraisal will be paid

by NHPREC. Lender approves Joseph Blake & Associates as the appraiser. NHPREC will be reimbursed at closing for the appraisal costs subject to the \$350,000 aggregate maximum amount.

H. Title and
Survey:

Lender reserves the right to review and approve the condition of the title, title insurance and the Property survey. All costs associated with the title, title insurance and survey will be paid by NHPREC. Lender approves the Chicago Title Insurance Company as the title insurer. NHPREC will be reimbursed at closing for the title and survey costs subject to the \$350,000 aggregate maximum amount.

I. Management
and Leasing:

Execution of a Management and Leasing Agreement satisfactory to USF&G and NHPREC providing for (i) the management of the Property by Parkford Companies, Inc. until the release of the Rent Achievement Holdback described in this Exhibit A and (ii) thereafter, the management of the Property by NCHP Property Management, Inc.

J. Closing Costs:

All costs associated with the closing on the Property, including Lender's reasonable attorney's fees will be paid by NHPREC. NHPREC will be reimbursed at closing for all third party closing costs up to an aggregate maximum amount of \$350,000.

Exhibit B

SOURCES AND USES OF FUNDS

Sources of Funds:

First Mortgage (USF&G)	\$20,000,000
Equity Capital (USF&G)	<u>15,350,000</u>

Total Sources of Funds	\$35,350,000
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Uses of Funds:

Unconditional Purchase Price	\$33,150,000
Rent Achievement Holdback	1,500,000
Third Party Closing Costs - Up to	350,000
Commitment Fee to USF&G	<u>350,000</u>

Total Uses of Funds:	\$35,350,000
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Exhibit C

RENTAL SCHEDULE

UNIT MIX

Unit Type	No. of Units	Square Footage	Total
The Gleneagle (1BR/1Bath)	126	519 564	65,394
The Turnberry (1BR/1Bath)	108	664 720	71,712
The Prestwick (1BR/1Bath/Den)	40	821 846	32,840
The Prestwick (1BR/1Bath/Den)	72	850 876	61,200
The St. Andrews (2BR/2Bath)	78	1,031 1070	80,418
Total			311,564

RENTAL INFORMATION

Unit Type	No. of Units	Monthly Rental	Monthly Unit Potential
The Gleneagle (1 BR/1 Bath)			
Terrace Level	42	\$675	\$28,350
Mid Level	42	\$685	\$28,770
Vaulted Ceiling	42	\$700	\$29,400
	126		
The Turnberry (1 BR/ 1Bath)			
Terrace Level	36	\$750	\$27,000
Mid Level	36	\$765	\$27,540
Vaulted Ceiling	36	\$780	\$28,080
	108		
The Prestwick (1 BR/1Bath/Den)			
Terrace Level	40	\$850	\$34,000
Mid Level	32	\$860	\$27,520
Vaulted Ceiling	40	\$845	\$33,800
	112		
The St. Andrews (2 BR/2Bath)			
Terrace Level	26	\$915	\$23,790
Mid Level	26	\$925	\$24,050
Vaulted Ceiling	26	\$940	\$24,440
	78		

Gross Monthly Rent Potential
Gross Annual Rent Potential

\$336,740
\$4,040,880

Exhibit D

FIFTH PRIORITY
DISTRIBUTION OF CAPITAL PROCEEDS CALCULATION

The amount of the fifth priority in the distribution of capital proceeds to USF&G, to the extent funds are available at a specific time ("n" years) is calculated in the following manner:

	\$35,350,000
less:	Present Value of Interest Payments @ 11.5%
less:	Present Value of Cash Flow Priority 1 @ 11.5%
less:	Present Value of Cash Flow Priority 3 @ 11.5%
less:	Present Value of Mortgage Balance @ 11.5%
less:	Present Value of Capital Proceeds Priority 1 @ 11.5%
less:	<u>Present Value of Capital Proceeds Priority 2 @ 11.5%</u>
equals:	Present Value of Capital Proceeds Priority 5 @ 11.5%
times:	<u>Compound Amount of \$1, 11.5%, n years</u>
equals:	Amount of Capital Proceeds Priority 5 Due

Exhibit E

SIXTH PRIORITY
DISTRIBUTION OF CAPITAL PROCEEDS CALCULATION

The sixth priority distribution of capital proceeds at a specific time ("n" years) will be calculated in the following manner:

	Present Value of Subsequent Contributions @ 11.5%
less:	Present Value of Cash Flow Priority 2 @ 11.5%
less:	Present Value of Capital Proceeds Priority 3 @ 11.5%
less:	<u>Present Value of Capital Proceeds Priority 4 @ 11.5%</u>
equals:	Present Value of Capital Proceeds Priority 6
times:	<u>Compound Amount of \$1, 11.5%, n years</u>
equals:	Amount of Capital Proceeds Priority 6

Exhibit F
MORTGAGE YIELD MAINTENANCE FEE CALCULATION

The Mortgage Yield Maintenance Fee at a specific time ("n" years) will be calculated as follows using a Treasury Note Rate which will be the yield on U.S. Treasury Notes that mature when the mortgage would have matured, i.e. Notes that mature in 10-n years:

times:	Mortgage Balance in year n <u>Compound Amount of \$1, 9.5%, 10-n years</u>
(A)	Compound Amount at Interest Rate
times:	Mortgage Balance in year n <u>Compound Amount of the Treasury Note Rate, 10-n years</u>
(B)	Compound Amount at Treasury Note Rate
less:	(A) Compound Amount at Interest Rate <u>(B) Compound Amount at Treasury Note Rate</u>
times:	(C) Lost Interest from year n to year 10 <u>Present Value of \$1, Treasury Note Rate, 10-n year</u>
	(D) Yield Maintenance Fee Due at year n

II. THE PROPERTY

II. THE PROPERTY

A. INTRODUCTION

Penderbrook Apartments is a 424-unit garden apartment community located in the Fair Oaks area of Fairfax County, Virginia. Penderbrook Apartments is in a larger master development which contains the Penderbrook Golf Course, and when completed will be an 1800-unit master planned community encompassing 294 acres. In addition, the master plan development will contain a par 71 championship golf course with a community center, private swim club, and running trails. The project is on a 18.9 -acre tract of land, and is comprised of 55% one-bedroom and 45% two-bedroom units housed in 19 buildings.

The buildings are for the most part 3-2 split level with one 2-story building. The complex contains the following unit mix: 126 1-Bedroom/1-Bath units of 564 square feet with an average rental rate of \$685 or \$1.21 per square foot; 108 1-Bedroom/1-Bath units of 664 square feet with an average rental rate of \$765 or \$1.09 per square foot; 112 2-Bedroom/1-Bath units of 875 square feet with an average rental rate of \$860 or \$.98 per square foot; and 78 2-Bedroom/2-Bath units of 1,031 square feet with an average rental rate of \$925 or \$.86 per square foot.

B. LOCATION

Penderbrook Apartments is strategically located on Route 50, one-eighth of a mile north of Interstate 66 in the heart of the Dulles Business Corridor. It is directly adjacent to the Fair Oaks Mall, which is one of the largest (1.4 million square feet) in Fairfax County and is within 15 minutes of the Dulles International Airport. The development in the Dulles corridor includes the Westerfields and the International Corporate Center at Dulles, which will have corporate headquarters of national and international firms, research and development facilities, warehousing, restaurants, and at least one hotel.

The subject property has excellent access from the full interchange of Interstate 66 and Route 50. Both Interstate 66 and Route 50 are major east-west arterials servicing the metropolitan Washington area. Interstate 66 runs east to the Capital Beltway (I-495) and through Arlington, Virginia into Washington, D.C. Route 50 runs east into Fairfax City, to the Capital Beltway and through Arlington, Virginia into Washington, D.C. (see Exhibits II-1, II-2 and II-3). The subject property is just northwest of the intersection of Interstate 66 and Route 50.

C. ADJACENT LAND USES

Exhibits II-4A and II-4B are aerial photographs of Penderbrook Apartments and the surrounding area. The site is located in the southwest corner of the Penderbrook master planned development which will ultimately consist of 1,800 units built on 294 acres by regional home builders including Pulte, Richmond American, NV Homes, and Hooker Barnes Homes.

At the southeast quadrant of the intersection of West Ox Road and Route 50, a 21-story high-rise office building was recently completed. In the southwest quadrant, a 255,000 square foot office is planned.

Approximately one mile to the west of the site is the Fair Lakes development which, when completed, will have in excess of 6.7 million square feet of mixed use office, retail, and commercial space on its 628-acre site.

Directly east of the site is the Penderbrook Golf Course which is a part of the planned unit development. North of the site within the planned unit development are the Pulte and NV Townhome developments. West of the site along Route 50 is a commercial corridor with single family homes in the \$200,000 plus range.

All total, the Route 50/Interstate-66 intersection business area has recently completed or has under construction over 13 million square feet of commercial office space.

D. THE SITE

The irregularly-shaped site consists of 18.9 acres. On an adjacent 3.3 acres there are two buildings which contain 48 units which were presold to the Fairfax County Housing Authority as a requirement for final zoning approval. The site has frontage along a future highway loop which will be built to access the Lee-Jackson Highway (Route 50) and also has a 282-foot frontage along West Ox Road (see Exhibit II-5). The 18.9-acre represents a net site area computed after land has been deducted for the road dedication and the presold units. Frontage at the intersection of Route 50 and West Ox Road is approximately 8 to 10 feet above street grade while the major road frontage along West Ox Road is level with the street grade. The topography is rolling, sloping downhill in an easterly direction.

Access to the subject site is via Penderbrook Drive, which begins as a 90-foot wide right-of-way at West Ox Road and narrows to a 52-foot wide right-of-way along the subject frontage. All paving within the project is bound by concrete curbs and gutters.

E. THE IMPROVEMENTS

Penderbrook Apartments consists of a total of 19 buildings including one clubhouse, 17 three-story buildings, and 1 two-story building. Building exteriors consist of wood framed construction with face brick veneer on the ground and second floors. Top floors have cedar siding. Exterior walls have 1-1/2 inch gypsum sheathing as a backup. The ground floor slabs are 4 inch poured concrete. Windows are single hung, double pane, aluminum clad. Sliding glass doors are doubled pane insulated. The roof system is of gable variety with asphalt shingles and batt insulation. Prefab trusses and truss joints constitute the structural framing. Gutters and downspouts are aluminum. Exhibit II-6A, 6B, and 6C are exterior photographs of the improvements.

Apartment floors have wall-to-wall carpet in all areas except the kitchens and baths. Upper level units have 3-1/4 inch gypcrete over a 3-1/4 plywood sub-floor. Soundproofing is 3-1/4 inch gypcrete. The ground floor units have carpeting on concrete. Bathrooms and kitchens have vinyl floor coverings. Interior walls and ceilings consist of painted sheetrock. Plumbing consists of PVC supplied drain lines. Each one-bedroom unit has one full bath with a shower and each two-bedroom unit has two full baths.

The kitchens have stainless double-sink basins with disposals. Each unit has a dishwasher and washer/dryer. Domestic hot water is supplied by individual 46-gallon units. Each unit is individually equipped with an electric heat pump. Individual units have 125-amp circuit breaker systems and are metered individually. Each unit has either a balcony with a 1-1/2 inch poured concrete over wood deck or a concrete patio accessible by sliding glass doors. Additional unit amenities include: undercabinet microwave ovens, refrigerators with ice makers, fireplaces in all units, and pitched ceilings in all top floor units. Exhibits II-7A, 7B and 7C are interior photographs of the apartments, and Exhibit II-8 is a summary of building specifications. Appendix A shows the floor plans for the four different unit styles.

Project amenities include one 3,000 square foot concrete pool, and two hot tubs, one of which is enclosed. The clubhouse houses rental offices as well as a club room and kitchen facilities. In addition, the clubhouse has an exercise room, with male/female bath and shower facilities. The clubrooms have vaulted ceilings and fireplaces. The complex is serviced by ample parking of 649 surface spaces or 1.53 spaces per unit.

F. SOURCES AND USES OF FUNDS

The sources and uses of funds statement is presented in Exhibit II-9. USF&G will provide the capital sources of \$35,350,000 which will be broken down between a fixed rate mortgage of \$20,000,000 and an equity joint venture of \$15,350,000 with a cumulative preferred return feature.

G. CONCLUSIONS

Penderbrook Apartments is a soon to be completed 424-unit garden apartment complex near the intersection of Interstate Highway 66 and Route 50 in Fairfax County, Virginia. Penderbrook's best marketing tool and greatest advantage over the competition is its highway accessibility and its proximity to the Fair Oaks Mall. In addition, Penderbrook Apartments is part of a larger golf course community with townhomes and single family homes ranging from \$130,000 to \$380,000 and up. The immediate area is fast becoming a significant employment center, and is projected to have unsurpassed growth in the next few years.

Exhibit II-1
REGIONAL LOCATION MAP

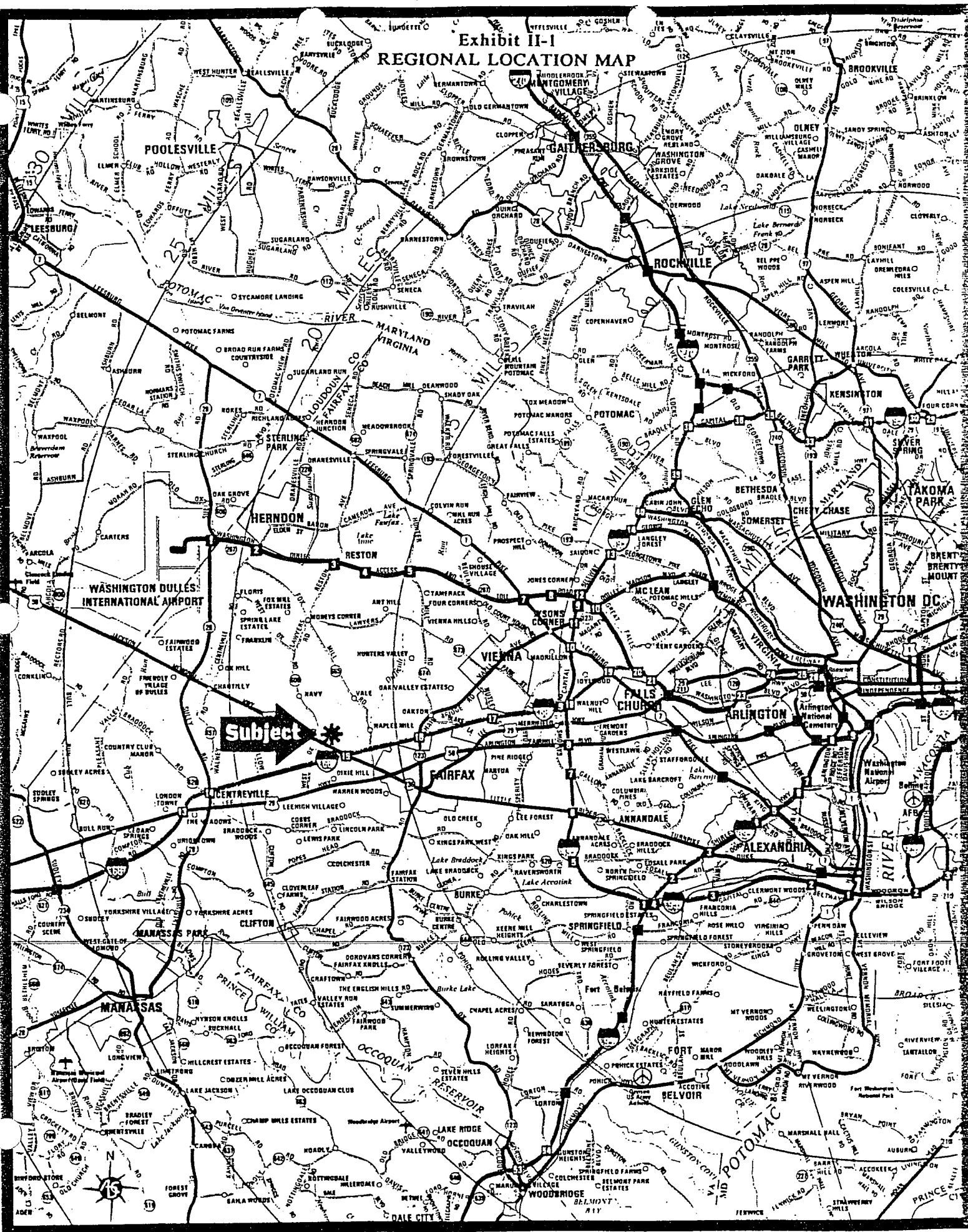
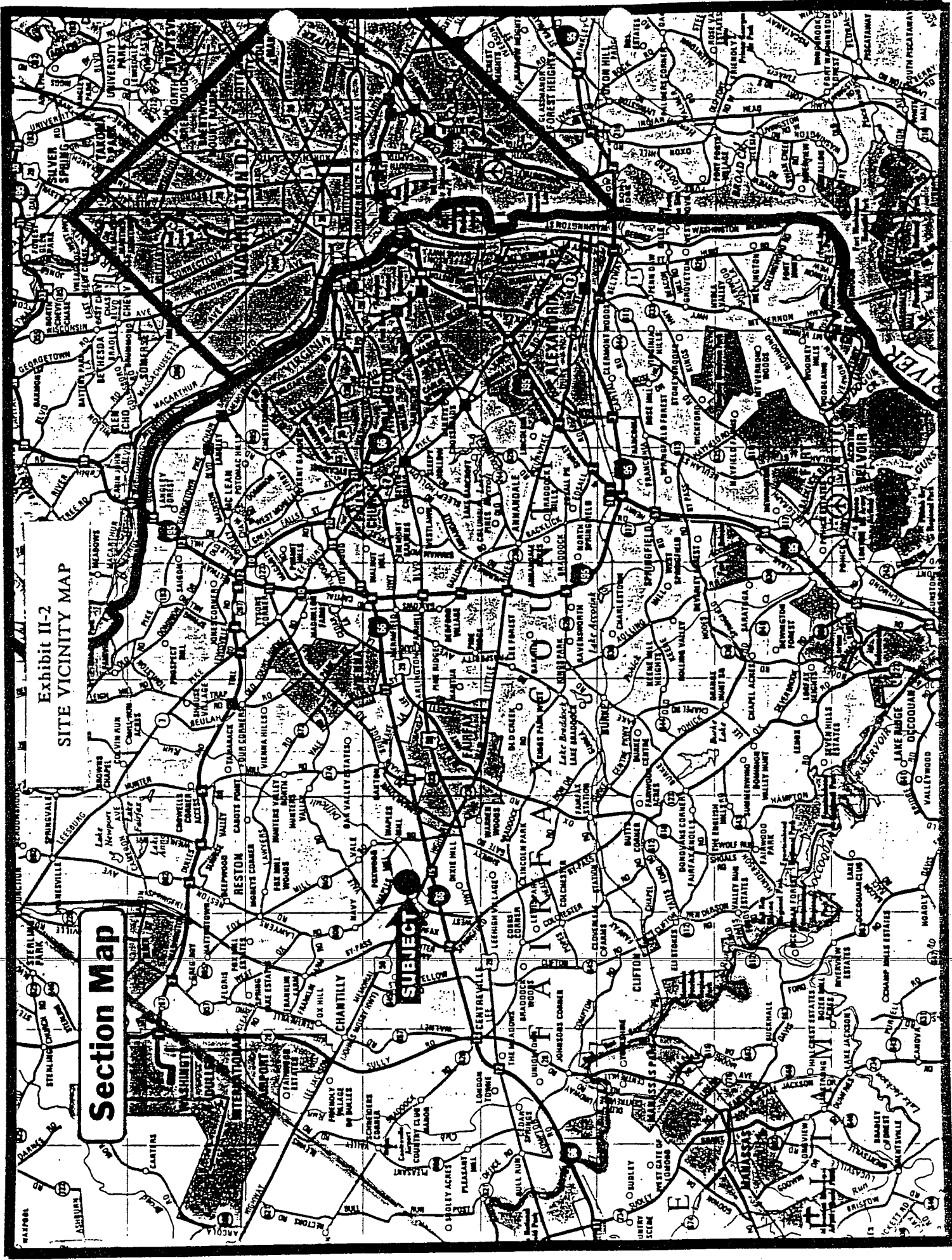


Exhibit II-2
SITE VICINITY MAP

Section Map

SUBJECT



Location Map

Exhibit II-3
SITE ACCESS MAP

SUBJECT

22030

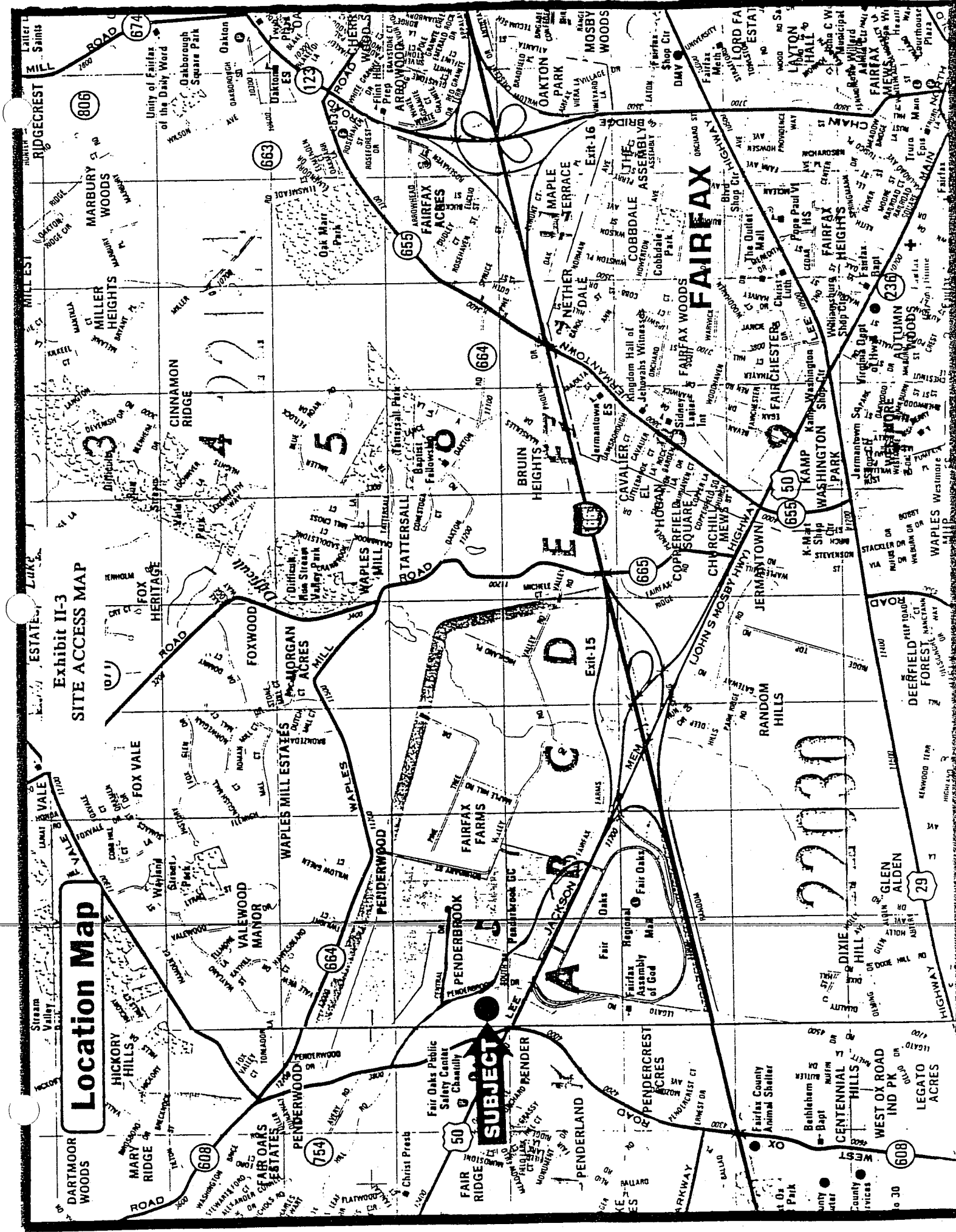


Exhibit II-4A
AERIAL PHOTOGRAPH LOOKING EAST

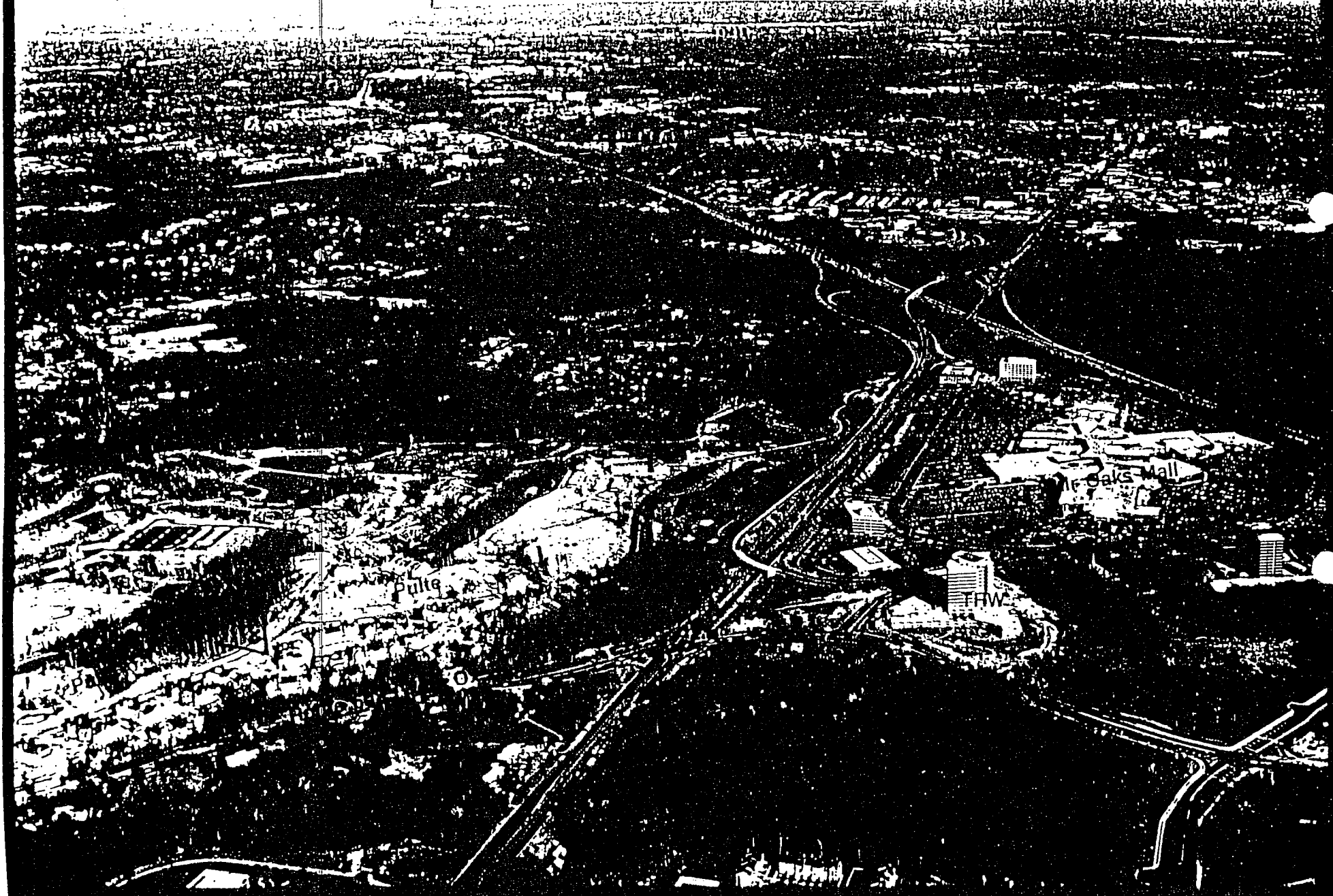


Exhibit II-4B
AERIAL PHOTOGRAPH LOOKING SOUTH

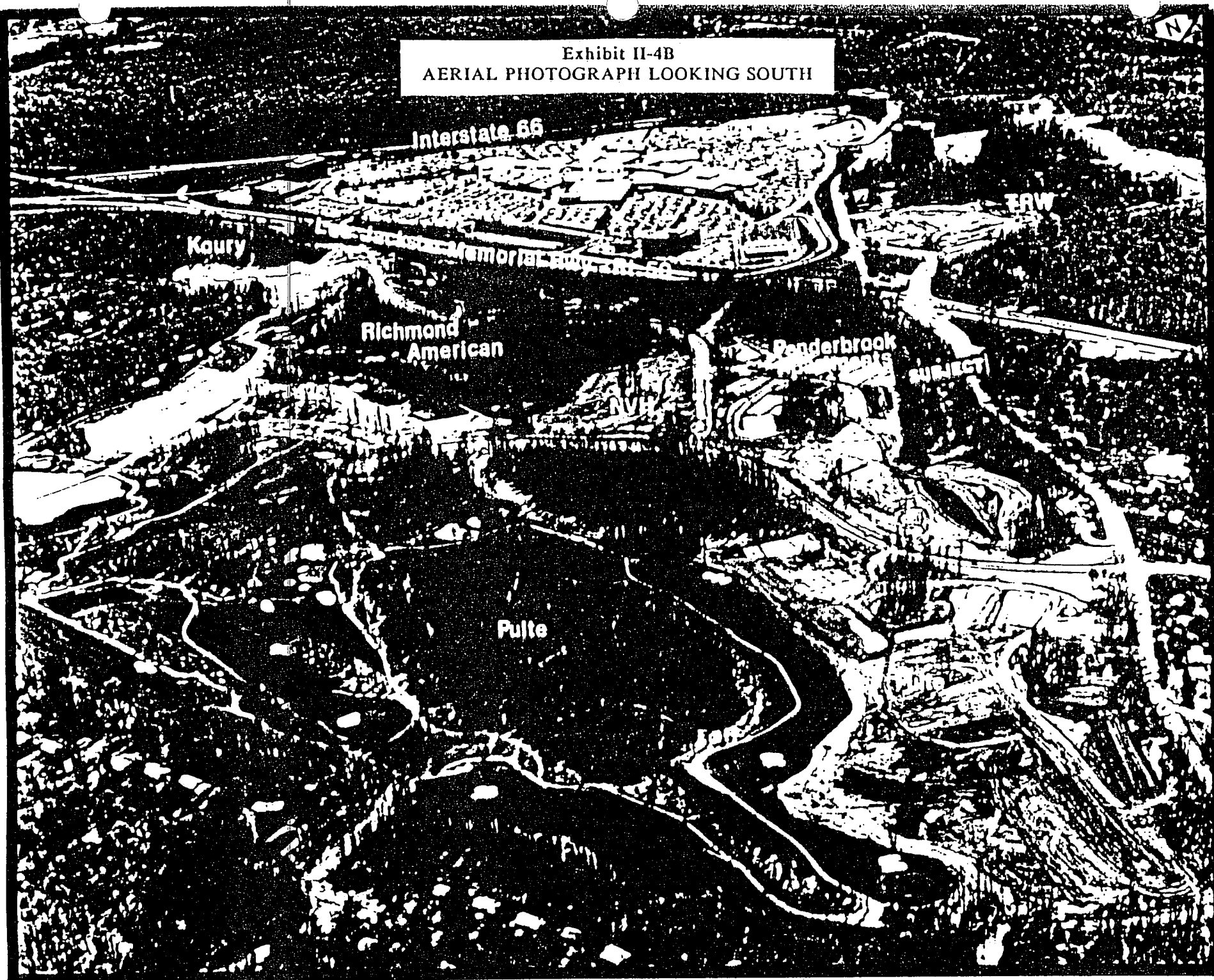


Exhibit II-5
SITE PLAN

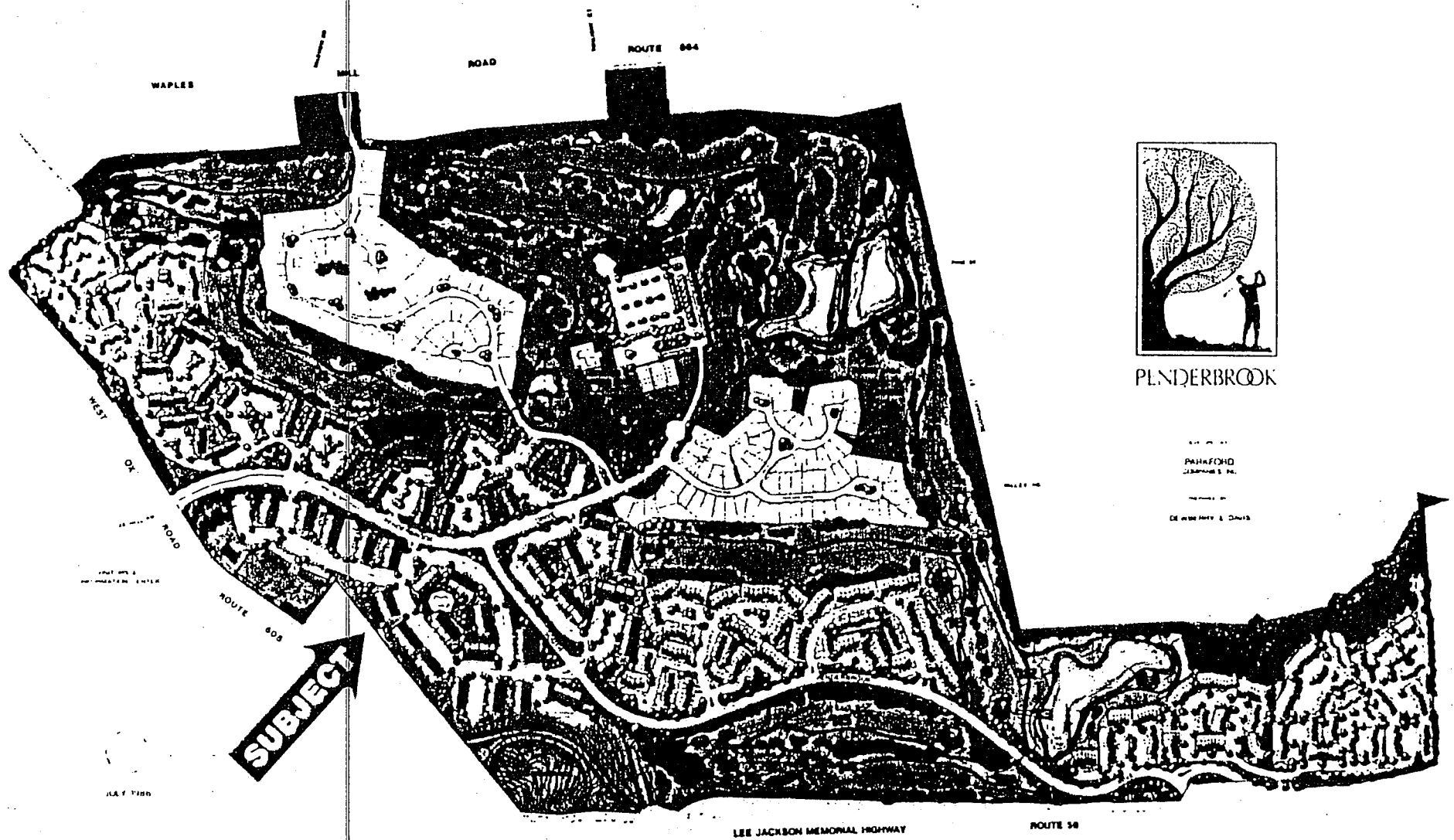


Exhibit II-6A
BUILDING PHOTOGRAPH



Exhibit II-6B
BUILDING PHOTOGRAPH



Exhibit II-6C
BUILDING PHOTOGRAPH



Exhibit II-6D
BUILDING PHOTOGRAPH



Exhibit II-7A
INTERIOR PHOTOGRAPH - ST. ANDREWS



Exhibit II-7B
INTERIOR PHOTOGRAPH - TURNBERRY

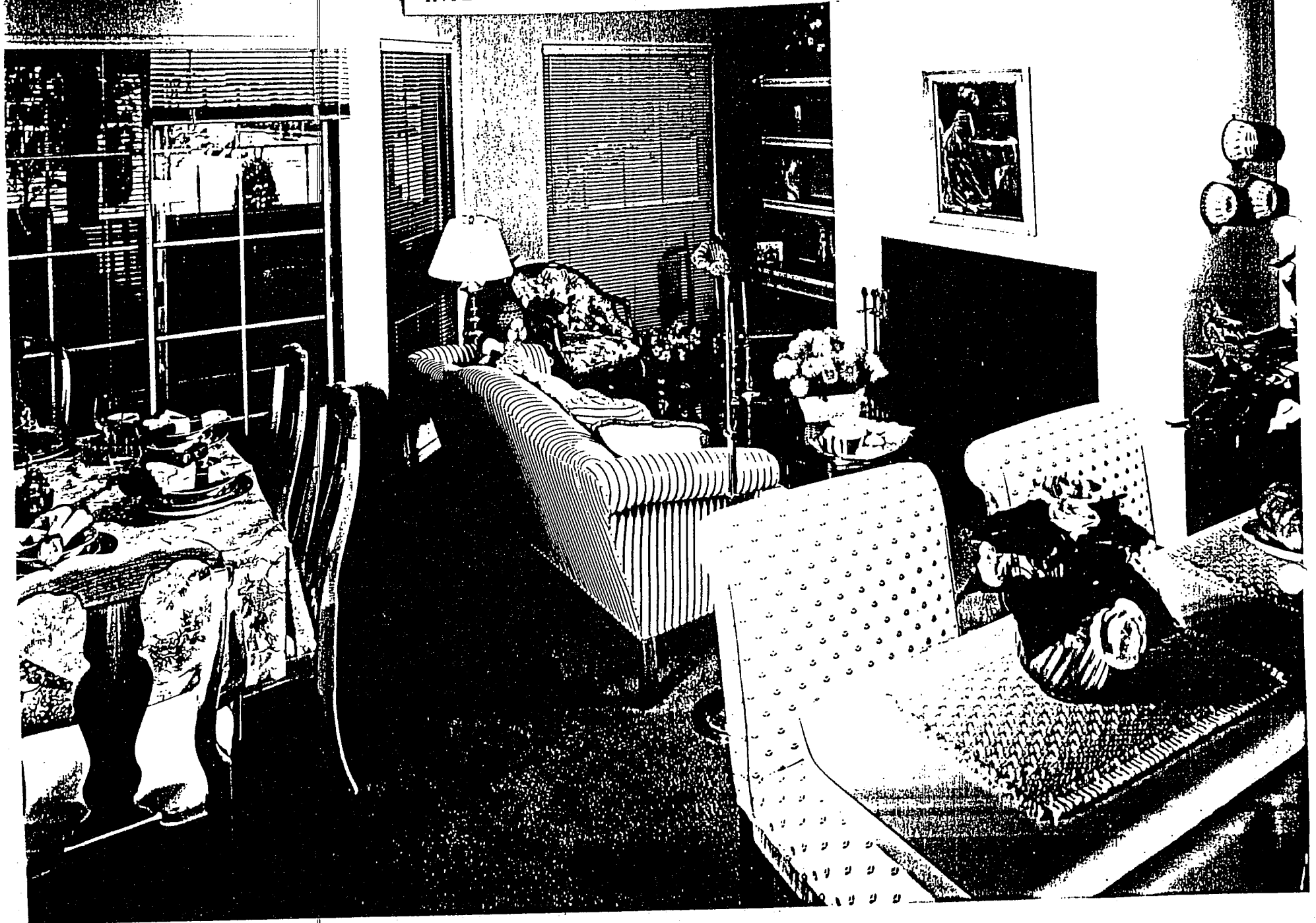


Exhibit II-7C
INTERIOR PHOTOGRAPH - CLUBHOUSE



**Exhibit II-8
CONSTRUCTION SUMMARY**

Construction:	Wood frame
Foundations:	Concrete slab on grade and masonry.
Exterior:	Rough cedar with partial face brick and beveled-edge siding and surfaces.
Roofs:	Composition roof shingles with felt paper over 1/2 inch plywood sheathing over wood trusses.
Structures:	Four-inch concrete slab on vapor barrier; upper levels are wood frame.
Windows and Patio Doors:	Pre-finished aluminum frames with insulating double planes; windows are double hung.
HVAC:	Individual heat pumps.
Insulation:	Batt insulation on walls (R-11) with vapor barrier; blown-in attic ceiling insulation (R-30).
Fireplaces:	Prefab units in all units and the clubhouse.
Electric:	Each unit is individually metered.
Interiors:	Plywood floors with 1-1/2 inch lightweight concrete topping with wall-to-wall carpeting; vinyl in kitchen and bathroom.
Interior Finish:	Walls and ceilings are painted drywall over studs; ceilings are standard flat white paint; ceiling height is 8 to 9 feet clear; wallpaper accents are provided in all units.
Appliances:	Continuous cleaning oven, dishwasher, disposal, range, microwave, washer and dryer and frost-free refrigerator.
Entrance Doors:	Fire-rated hollow metal with viewers and combination deadbolt locks.
Interior Doors:	All prefinished wood hollow core; all frame and trim prefinished wood.

Site Improvements:	Landscaping, concrete curbs, gutters and sidewalks, paved driveways and concrete swimming pool with deck; the recreation building includes an exercise room with exercise equipment, leasing office, meeting area with kitchen, reception area, men's and women's locker and rest rooms, aerobics area and spa.
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Exhibit II-9
SOURCES AND USES OF FUNDS

Sources of Funds:

First Mortgage (USF&G)	\$20,000,000
Equity Capital (USF&G)	<u>15,350,000</u>

Total Sources of Funds:	\$35,350,000
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Uses of Funds (See Exhibit V-2A)

Land	\$ 8,500,000
Structures	21,087,000
Site Improvements	848,000
Entrepreneurial Profit to Seller	4,215,000
Closing Costs to Third Parties	350,000
Commitment Fee to USF&G	<u>350,000</u>

Total Uses of Funds	\$35,350,000
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III. THE MARKET OVERVIEW

III. THE MARKET OVERVIEW

A. INTRODUCTION

The Metropolitan Washington, D.C. region has experienced substantial growth in the current decade. Over the seven-year period from 1980 to 1987 the estimated increase in population for the region was 340,000, greater than the 127,000 increase that occurred over the ten-year period from 1970 to 1980. Fairfax County has accounted for almost half of this recent increase. Fairfax County received a significantly higher share of Virginia's population growth in the 1980's than other jurisdictions in Virginia. The catalyst for this continuing population increase is found in the continued dominance of the services sector as well as the magnitude of federal, state, and local governments. Currently Fairfax County is growing faster than any other locality in the area. Current projections indicate that Fairfax County will be the most populated jurisdiction in the metropolitan area by the year 2000.

B. FAIRFAX MARKET OVERVIEW

Fairfax County is situated in the northeast corner of Virginia and is a part of the Metropolitan Washington MSA. The county consists of 399 square miles and holds the Virginia portion of the Capital Beltway (Interstate 495). Major arterial highways within Fairfax County include Interstates 395, 95, and 66, and US Routes 1 and 50. The Washington/Dulles International Airport is located in the north central region of Fairfax County and serves in excess of 3 million passengers per year.

Fairfax County has grown at a faster rate than the Washington area as a whole. While the entire region experienced almost a doubling in population during the 1950 through 1975 period, Fairfax County's population increased over five times. By the year 2000, Fairfax County is projected to be the largest Washington area jurisdiction in terms of population. Twenty percent of the MSA's population is expected to reside in Fairfax County. The projected annual growth for Fairfax will add over 7,000 new residents each year until the year 2000 (see Exhibit III-1A).

Fairfax County's labor force is one of the most educated and skilled in the region, which explains why Fairfax County has one of the highest median family income in the nation. Approximately 42% of Fairfax County's adult population are college educated as compared to 16% nationwide. Nearly 90% of Fairfax adult residents are high school graduates as compared to 67% nationally. The labor force is primarily white collar (77% in 1980) with concentrations in major business centers such as Tysons Corner, Merrifield, Reston, the Dulles business corridor, and Fairfax Center. Forecasts indicate that by the year 2000 the emerging business centers at Fairfax Center, Dulles and Chantilly will exceed employment now found at Tysons Corner (see Exhibits II-1B and 1C).

Fairfax County offers a residential environment that is among the best and most expensive in the nation. This is a result of the area's pleasing climate and a deliberate effort to preserve and encourage traditional residential communities while promoting economic development. Approximately 175,000 of the county's 244,000 zoned acres are zoned for residential use. This gives the area its primarily residential character. Of the county's total housing stock, approximately 56% are single family detached units, 18% are garden apartment units, 16% are townhomes, and 6% are low, mid, and high-rise apartments or condominium buildings. Duplex and multi-plex units comprise approximately 3% and mobile homes make up less than 1%.

Historically, Fairfax County rental housing availability has been very tight. During the past five years the vacancy rate for rental housing in Fairfax County has averaged 2.8% and during the past three years the average vacancy rate has been 3.0% (see Exhibit III-2A). During the past 12 years the average vacancy rate has never exceeded 4.4%, and has been as low as 2.1%. Predictably, average rental rate increases in the county for the same period of time have responded to this tight vacancy situation. During the past five years the average rental rate increase in the county was 8.8% and during the past three years the average increase was 9.7%. During the past twelve years, the highest rental rate increase was 10.9% in 1985 and the lowest increase was 5.6% in 1978 (see Exhibit III-2B). Because of condominium conversion and the apartment zoning policies of the county, the supply of apartment units has actually declined during the past twelve years. In 1975, the total number of units was 43,005. From that point it peaked at a level of 44,555 in 1979 then dipped to a level of 38,950 in 1985 and was estimated to be 40,003 at year end 1987 (see Exhibit III-2A). Note that when the number of rental units peaked in 1979 at a level of over 4,000 units higher than the supply today, the vacancy rate was never pushed higher than 4.1%.

C. COMPETITIVE APARTMENT PROPERTIES

The selected market comparables for the proposed project have occupancy rates ranging from 92% to 99% for those comparables not currently in a lease-up mode (see Exhibits III-3, III-4 and III-5). This range would seem to be explained by locational considerations. The 92% occupied comparables are located in Reston and the western extremes of the county, while the higher occupancy comparables are located closer into the Fairfax City/Vienna area. In particular, the 99% occupied comparable is located in Oakton, which is a very good locational comparable for the Penderbrook project.

There are several significant attributes which make the Penderbrook Apartments a superior property to its competitors. Penderbrook Apartments has the most accessible and visible location of all its competitors. Located at the intersection of Route 50 and Interstate 66 which are the two most frequently travelled highways in northern Virginia, Penderbrook occupies a location unmatched by its competitors.

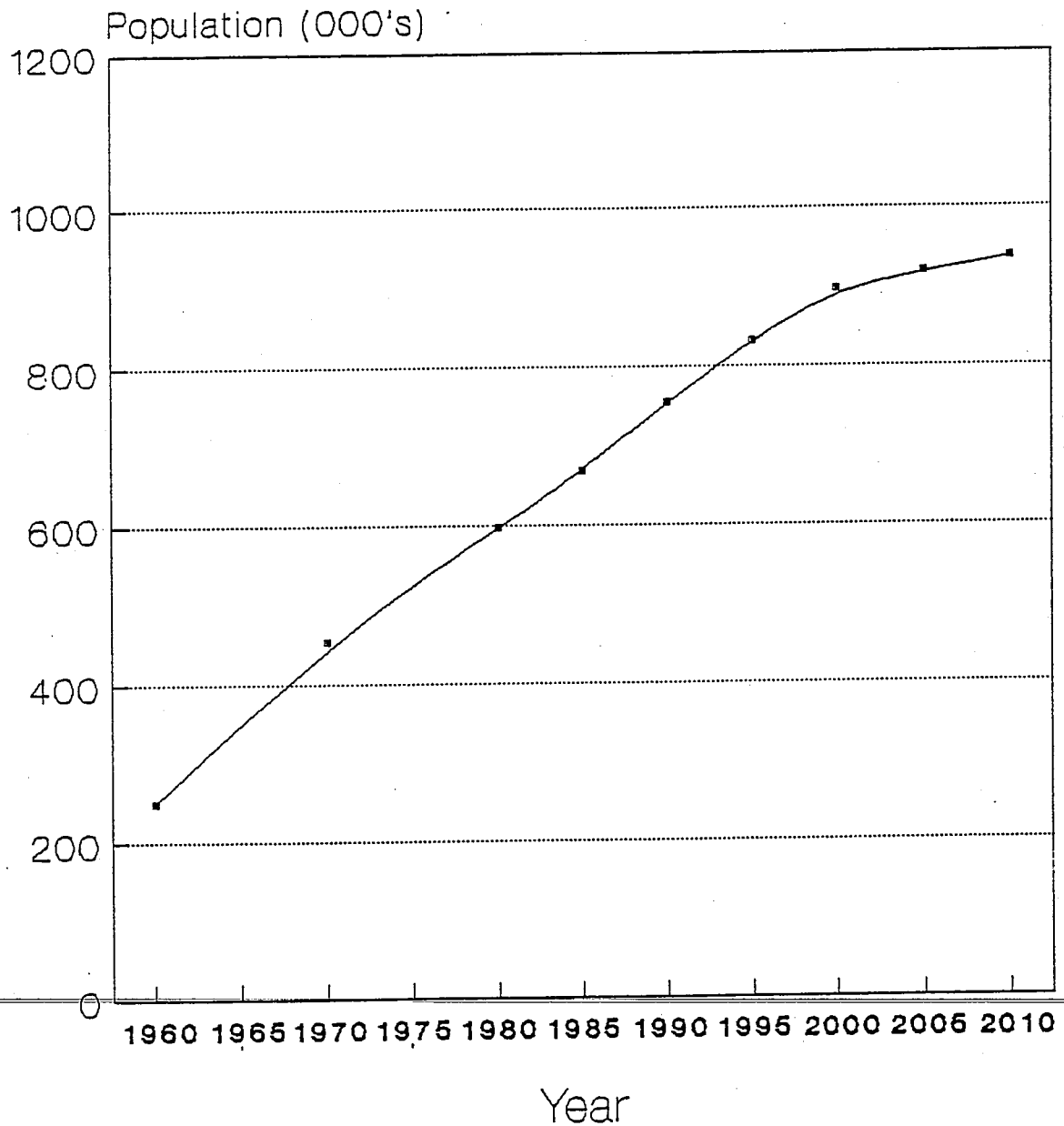
Located at the center of the Fair Oaks commercial office market, which currently has more than 2 million square feet of office space completed and an additional 11 million square feet proposed or to-be-delivered in the near future, the Penderbrook Apartments is strategically located within an area with a very strong employment base. Penderbrook also strikes a unique balance between proximity to commercial development and planned residential land use. As part of a larger Planned Use Development (PUD), residents of Penderbrook Apartments will have access to all the PUD's amenities, including Penderbrook Golf Course membership privileges, clubhouse, pool, tennis courts and centrally monitored individual unit security systems. Clearly, the Penderbrook Apartments are at the top of the apartment market with respect to amenities and location.

The rental rates for the Penderbrook Apartments reflect the premium nature of the product within its market as measured by either rent per square foot or total rent. The rates for Penderbrook are near or at the top of the scale within the market area. This premium is most clearly reflected in the one-bedroom/one bath rental rates which range from \$1.21 to \$1.30 per square foot, significantly above the \$1.00 to \$1.15 per square foot range at the high end for the competitors. This difference is largely due to the smaller average size of the one bedroom/ 1 bath units and is not so nearly pronounced when considered on a per unit basis. The total rent for the one bedroom/ one bath units at Penderbrook is \$780 compared to rates of \$800 to \$910 at the high end of the range among the competitors. For the two bedroom/ one bath and the two bedroom/ two bath units, the premium still exists but is not as large.

D. CONCLUSION

Fairfax County's apartment market has been exceptionally strong over the past twelve years. The county's strong economy, with the highest median family income in the entire country and its many suburban white collar business centers, is projected to remain strong through the year 2000. Given the property's superior amenities and location, the property is expected to further benefit from these favorable market conditions.

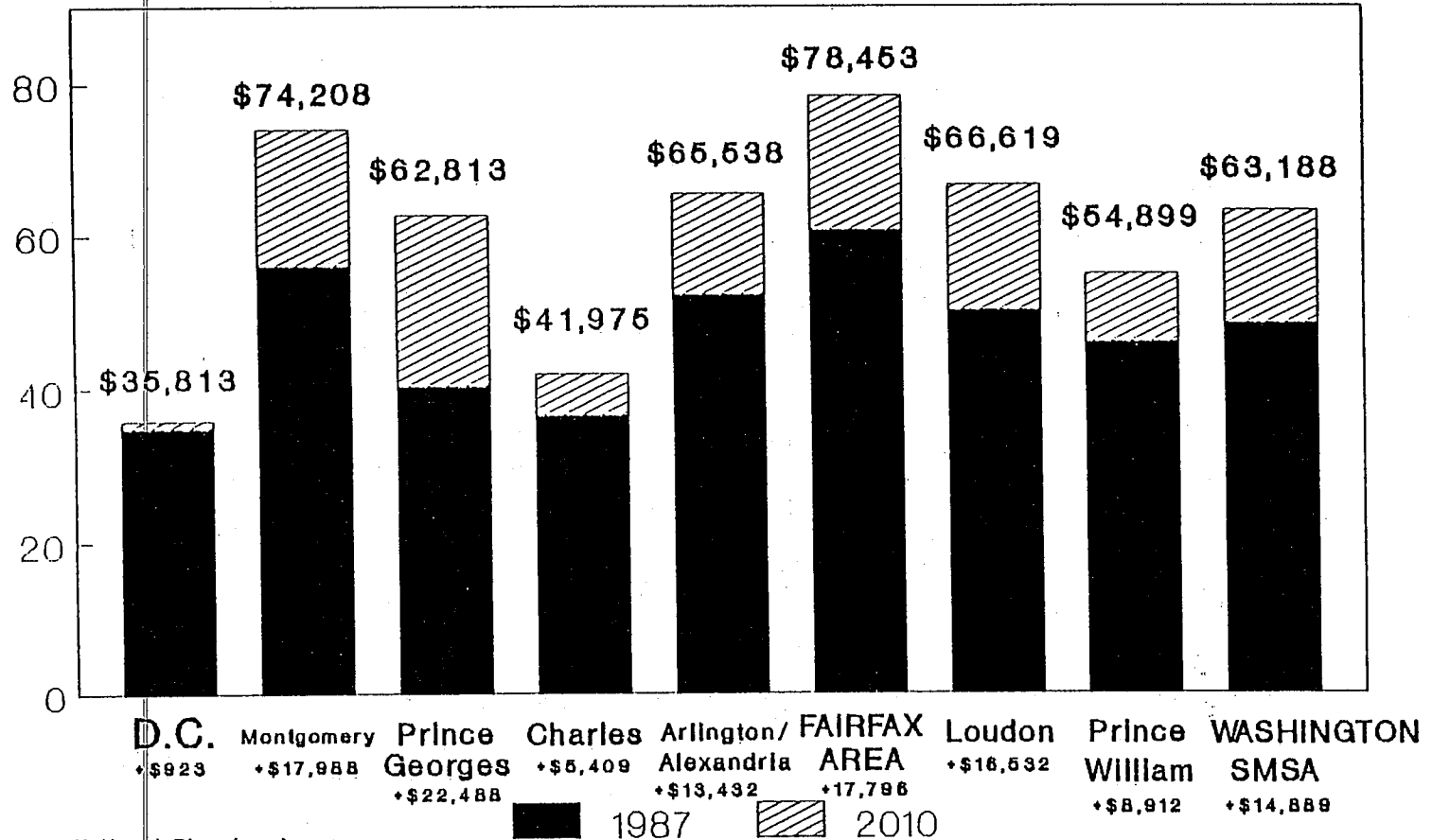
EXHIBIT III-1A
SUMMARY OF POPULATION GROWTH
FAIRFAX COUNTY, 1960 - 2010



Source: Fairfax County Economic Development Authority
Potomac Realty Advisors

Exhibit III-1B Average Household Income Washington SMSA Jurisdictions 1987 to 2010

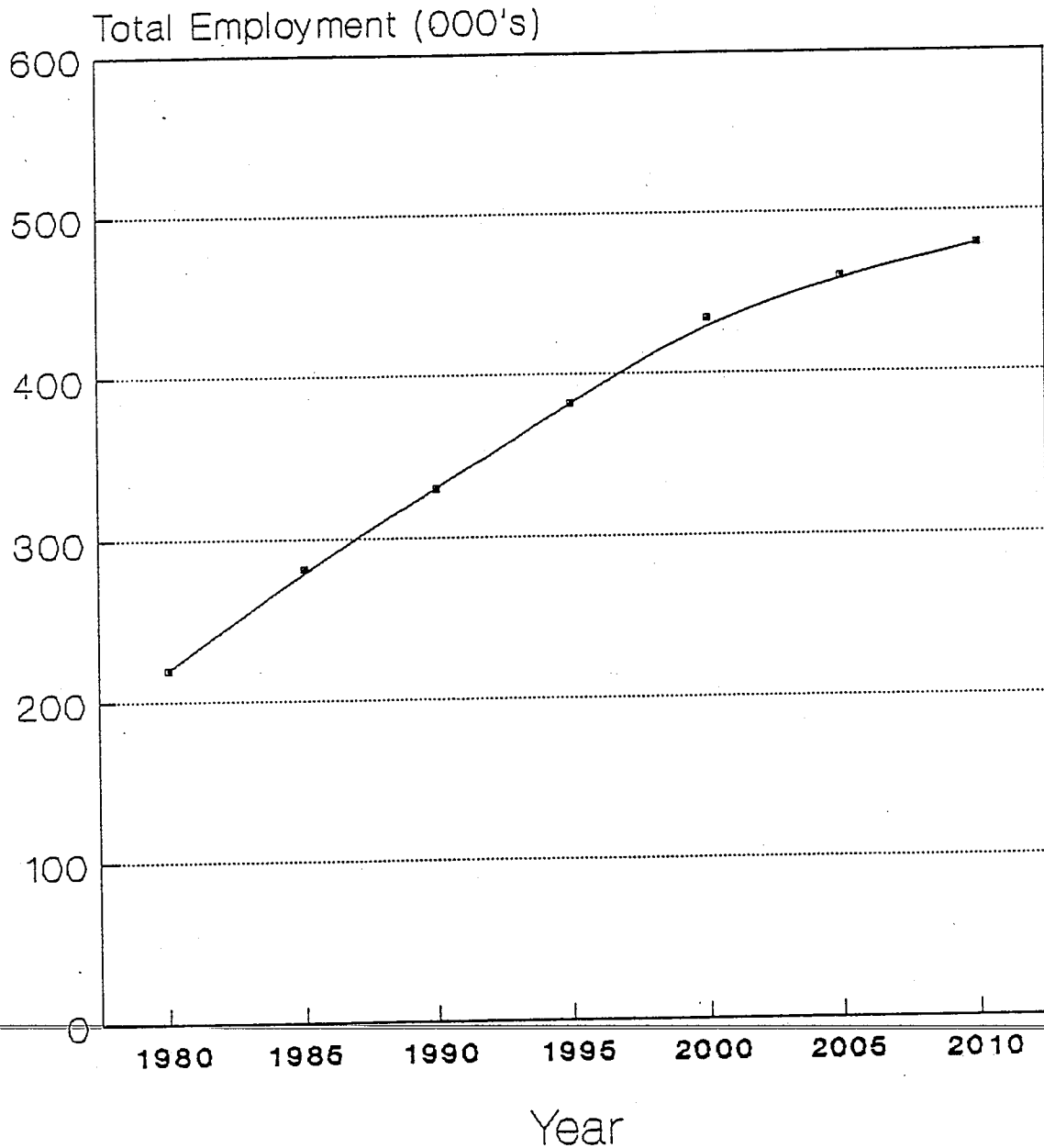
Average Household Income (000's)



Source: National Planning Assoc.
Potomac Realty Advisors

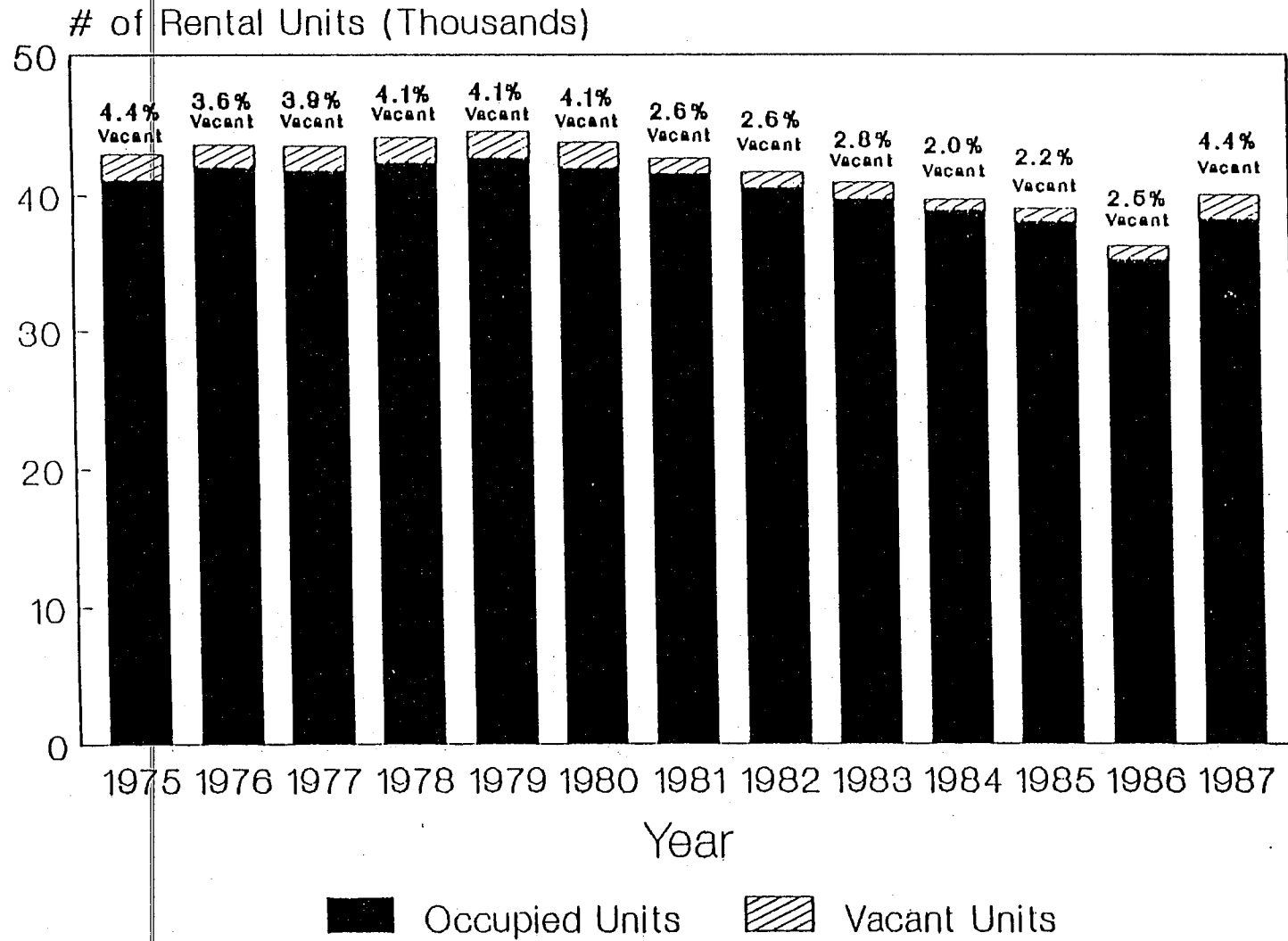
1982 Constant Dollars

EXHIBIT III-1C
FAIRFAX COUNTY EMPLOYMENT FORECAST
(EXCLUDING MILITARY AND SELF EMPLOYED)



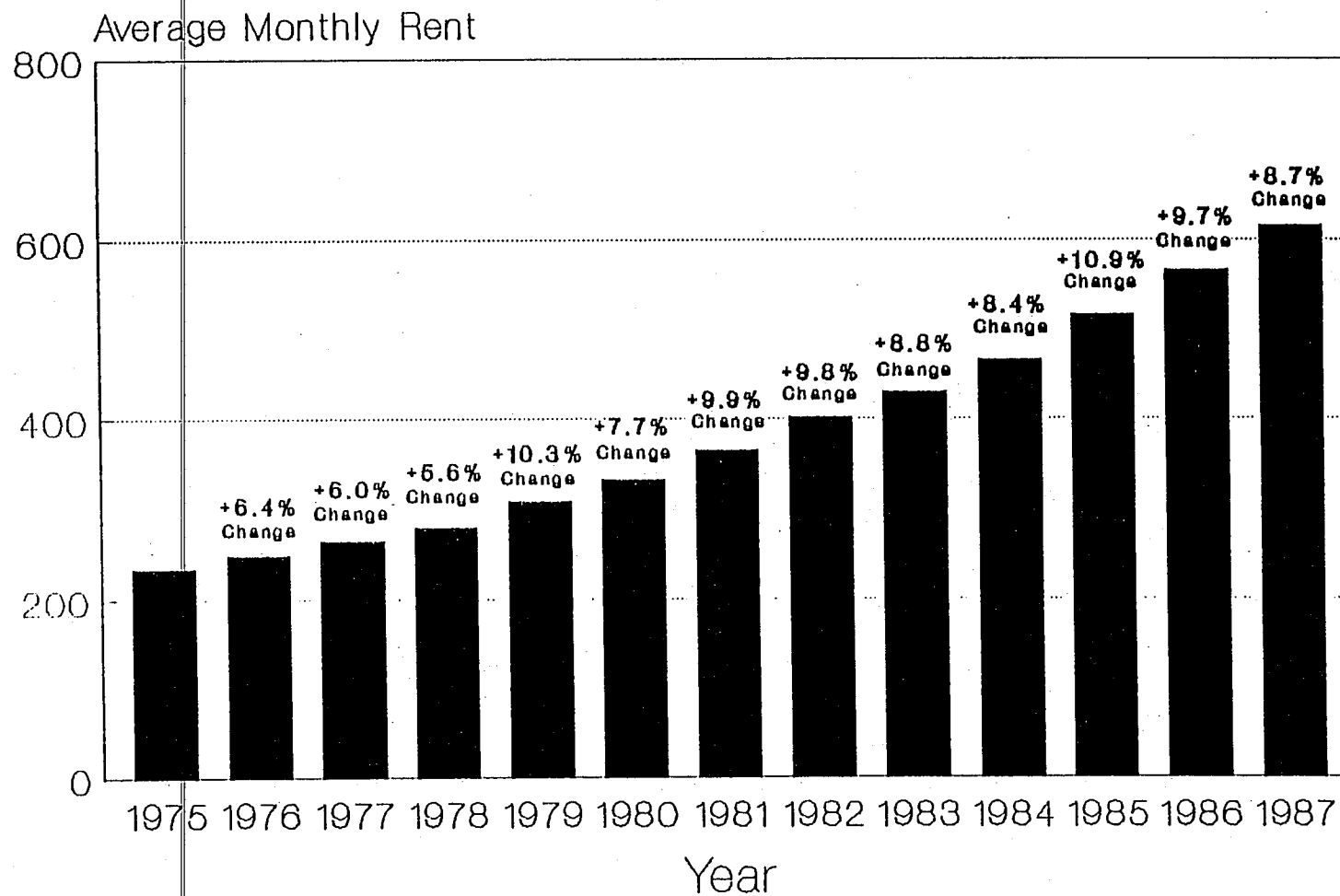
Source: Fairfax County Economic Development Authority
Potomac Realty Advisors

Exhibit III-2A Fairfax County Apartment Market



Source: Fairfax County Office of Research and Statistics
Potomac Realty Advisors

Exhibit III-2B
Average Monthly Rent for Rental Housing
Complex Units by Year
Fairfax County, 1975 to 1987



Source: Fairfax County Office of Research and Statistics
Potomac Realty Advisors

Exhibit III-3
COMPETITIVE PROPERTY SURVEY

Map Code	Project Name and Address	Developer or Mgmt. Co.	Completion Date	Total # Units	1 Bedroom/1 Bath			2 Bedroom/1 Bath			2 Bedroom/2 Bath		
					Size S.F.	Rent	\$/P.S.F.	Size S.F.	Rent	\$/P.S.F.	Size S.F.	Rent	\$/P.S.F.
1	Oaks at Fair Lakes Fairfax, VA	Hazel/Peterson	1988	282	699-817	\$745-800	\$.98-1.07	945	\$825	\$.87	1059-1092	\$900-925	\$.85
2	Waterside Reston, VA	Artery	1985	273	697	\$685-715	\$.98-1.03	880	\$775-790	\$.88-.90	937-1015	\$830-850	\$.84-.89
3	The Hermitage Fairfax, VA	PCA	U/C	488	601-820	\$675-790	\$1.12-1.15	934	\$825	\$.88	1040	\$890	\$.86
4	Providence Place Fairfax City, VA	BEW	1988	140	804	\$770-825	\$.96-1.03	855-905	\$1060-1100	\$.81-.82			
5	Old Centreville Gable Centreville, VA	NV Properties	U/C	252	788-987	\$720-830	\$.84-.91	920-1148	\$760-910	\$.79-.83	1017	\$805-840	\$.79-.83
6	Shenandoah Crossing Fairfax, VA	Oxford	1984	640	718	\$690-720	\$.96-1.00	840-880	\$740-810	\$.90-.95	934	\$790-825	\$.85-.88
7	Oakton Gables Fairfax, VA	NV Properties	1987	313	788-987	790-890	\$.90-1.00	960-1148	\$840-990	\$.88-.97	1017	\$890-985	\$.84-.88
8	Summit Square Oakton, VA	Calibre	1986	366	863-1109	\$750-790	\$.67-.92	870-1250	\$750-850	\$.66-.91	1083-1088	\$860-920	\$.79-.85
9	Chase Commons Burke, VA	Trammell Crow	1987	360	703-938	\$655-745	\$.79-.93				1097	\$798	\$.72
10	Peachtree of McLean Falls Church, VA	GHA	1970	340	801	\$740-775	\$.92-.97	793-960	\$760-830	\$.87-.96	1108	\$860-920	\$.78-.83
11	Summit Village Arlington, VA	Calibre	1987	198	856	\$835-910	\$.98-1.06	874-1044	\$865-1070	\$.95-1.08	950-1072	\$995-1195	\$.93-1.12
12	Jonathan's Keep Reston, VA	Oxford	1985-87	418	690	\$710	\$1.03	837-850	\$770-810	\$.91-.95	950-1050	\$830-860	\$.82-.87
	Subject	Parkford	1988	424	564-644	\$675-780	\$1.11-1.24	850	\$850-845	\$.99-1.00	1031	\$915-940	\$.89-.91

**Exhibit III-4
COMPETITIVE PROPERTY AMENITY MATRIX**

Map Code	Project Name	Children	Pool	Exercise Room	Jacuzzi	Tennis Courts	Laundry	Washer Dryer	Clubhouse	Racquetball Court	Fireplace
1	Oaks at Fair Lake	X	X		X	X		X	X		X
2	Waterside	X	X								
3	The Hermitage	?	X	X	X	X		X	X	X	X
4	Providence Park	?	X	X		X		X	X		A
5	Old Centreville Gable	?	X	X	X	X		X	X		A
6	Shenandoah Crossing	X	X	X	X	X		X	X	X	X
7	Oakton Gables	?	X	X	X	X		X	X	X	A
8	Summit Square		X	X	X			X	X		A
9	Chase Commons	X	X	X	X	X	X	C	X		A
10	Peachtree	X	X				X	A			
11	Summit Village		X		X			X			A
12	Jonathan's Keep	X	X	X				X	X		A
	Subject		X	X	X	X		X	X		X

CODES AND NOTES

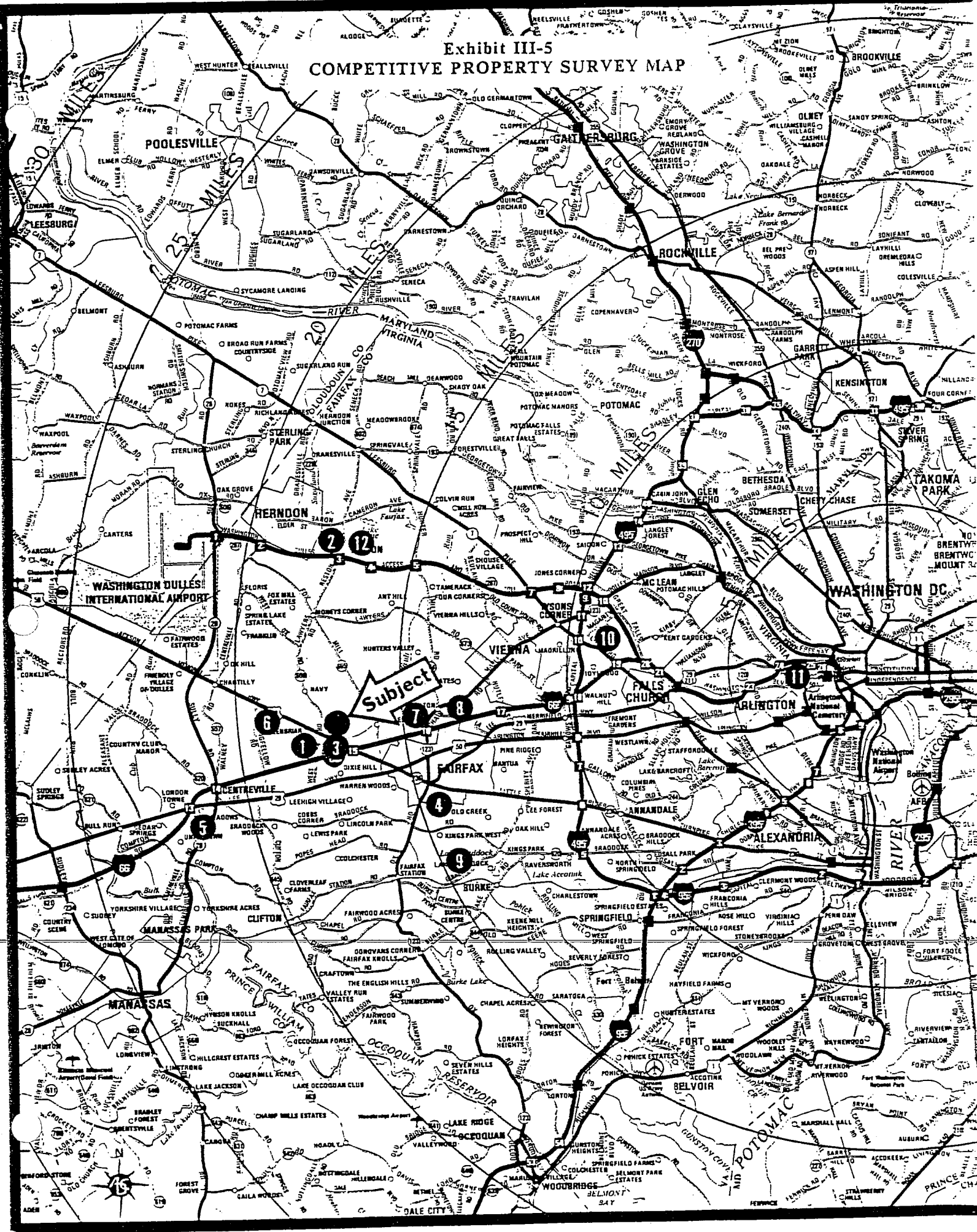
X Property offers this amenity or rental policy.

A Available in some units

All of the above properties have patios and/or balconies.

Source: Potomac Realty Advisors

Exhibit III-5
COMPETITIVE PROPERTY SURVEY MAP



IV. THE JOINT VENTURE PARTNER/BORROWER AND DEVELOPER

IV. THE JOINT VENTURE PARTNER/BORROWER AND DEVELOPER

A. INTRODUCTION

The Joint Venture Partner/Borrower will be NHP Real Estate Corporation (NHPREC), a wholly owned subsidiary of National Housing Partnerships, Inc. (NHP). NHPREC will act co-general partner with USF&G. NHP and subsidiaries have a combined net worth of approximately \$75,000,000, and NHPREC has a net worth of approximately \$18,000,000 (see Exhibit Iv-1 and IV-2).

B. NHPREC

NHPREC is wholly owned by NHP, a Washington, D.C.-based developer and manager of residential housing nationwide. NHP was organized in 1968 through an act of Congress to meet a growing nation's housing needs. Committed to the creation of quality rental communities, NHP has become one of the largest owners, developers and managers of residential housing in America. NHP now owns 77,840 units in 44 states. NHP is the central holding company, with operating companies comprised of The National Housing Partnership (the general partner in most of NHP's projects), The National Corporation for Housing Partnerships (the operating arm of the company, including the property management company) and NHPREC. NHPREC was formed in early 1987 to conduct the ongoing multi-family market rate and single family housing and commercial development business of NHP.

The property will be managed by NCHP Property Management, Inc., a subsidiary of National Corporation for Housing Partnerships. NCHP Property Management, Inc. presently manages 423 properties totalling 63,985 units. NHP is a general partner in 383 properties and 55,901 units managed by the subsidiary. The subsidiary manages 40 properties totalling 8,084 units for owners other than NHP. NCHP Property Management, Inc. is an Accredited Management Organization as designated by the Institute of Real Estate Management. The field staff is headquartered in four regional offices and 12 district offices across the country in order to provide constant hands-on management of the properties. Exhibit IV-3 is a listing of NHP-managed properties in the Washington metropolitan area.

C. DEVELOPMENT TEAM

1. Developer/Seller

The Developer/Seller of the project is The Parkford Companies. The Parkford Companies was founded in 1985 by Mr. Bart McEntire, formerly with the Vantage Companies of Dallas, Texas. The primary emphasis of Parkford Companies is multi-family development. It has projects underway in four states and maintains offices in Dallas and Maryland.

Exhibit IV-4 shows the projects that The Parkford Companies and their principals have been directly involved in since 1981. The Parkford Companies will also be managing the project during the rent achievement holdback earnout period.

2. General Contractor

The general contractor for the project is VRI Builders, one of Texas' largest multi-family builders. For the past several years, Builders Magazine has listed VRI Builders among America's top 40 multi-housing builders in contract volume. VRI Builders has completed over 12,700 units to date and has another 2,200 units under construction or in planning.

3. Golf Course Management

The golf course is managed by Penderbrook Golf Management, Inc., an affiliate of the Parkford Companies. Penderbrook Golf Management, Inc. has managed the Penderbrook Golf Course as a public golf course since its inception in 1980.

D. CONCLUSION

NHP, Inc., the parent company of NHPREC (the joint venture partner/borrower for this transaction), is a leading full service real estate company primarily engaged in the development, acquisition, and management of multi-family rental housing. NHP is also one of the largest property managers of multi-family housing, and is a demonstrated leader in property management. The associated professional firms will form an effective development team.

EXHIBIT IV-1
NHP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

	February 29, 1988	February 28, 1987
ASSETS:		
Cash	\$ 1,454,089	\$ 2,872,807
Receivables (Note 3):		
Due from housing partnership investors	35,438,178	71,971,101
Other	7,883,894	8,922,193
Single family housing (Note 2):		
Net investments in joint ventures	10,223,119	6,412,833
Land and homes in process	-	27,255,625
Multifamily rental housing (Note 4):		
Land and development costs	6,041,786	11,135,862
Investments in and advances to partnerships	56,598,372	50,185,554
Other investments	8,351,219	8,351,219
Investment in HPI, Limited (Note 5)	3,259,595	1,725,142
Other assets (Note 6)	8,710,183	10,878,679
	<u>\$137,960,435</u>	<u>\$199,711,015</u>
LIABILITIES:		
Accounts payable and accrued liabilities	\$ 6,662,828	\$ 15,561,051
Mortgage notes payable (Note 2)	-	19,270,064
Notes payable to banks (Note 7)	24,010,000	40,936,347
Balance due - rental housing acquisitions (Note 8)	13,981,055	35,788,868
Deferred income taxes (Note 13)	6,870,035	627,268
	<u>51,523,918</u>	<u>112,183,598</u>
COMMITMENTS AND CONTINGENCIES (Note 9)		
DEFERRED INCOME (Note 3)	<u>11,257,345</u>	<u>19,993,926</u>
STOCKHOLDERS' EQUITY (Notes 1 & 10):		
Common stock, \$.01 par value;		
Authorized, 1,000,000 shares:	2,744	2,743
Issued 274,375 and 274,250 shares	59,819,816	59,980,698
Additional paid-in capital	15,578,424	7,550,050
Retained earnings	(221,812)	-
Treasury stock, at cost, 875 shares	<u>75,179,172</u>	<u>67,533,491</u>
	<u>\$137,960,435</u>	<u>\$199,711,015</u>

EXHIBIT IV-2
NHP REAL ESTATE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

FEBRUARY 29, 1988
(unaudited)

ASSETS:

Cash	\$ 158,108
Net investment in single family joint ventures	10,223,119
Net investment in commercial joint venture	418,519
Multifamily rental housing: Land and development costs	3,952,197
Investment in and advances to partnerships	10,070,303
	<u>-----</u>
Total assets	\$24,822,246
	<u>=====</u>

LIABILITIES AND EQUITY:

Balance due on real estate projects	\$ 3,284,527
Due to NHP, Inc.	3,130,978
	<u>-----</u>
Total liabilities	6,415,505
	<u>-----</u>
Common stock issued and outstanding	100
Additional paid-in capital	18,319,828
Retained earnings	86,813
	<u>-----</u>
Total equity	18,406,741
	<u>-----</u>
Total liabilities and equity	\$24,822,246
	<u>=====</u>

EXHIBIT IV-3
NHP PROPERTIES IN THE METROPOLITAN
WASHINGTON, D.C. AREA

NHP has a very strong presence in the multi-family real estate market in metropolitan Washington, D.C. NHP owns 9,097 units in Maryland, Virginia and the District of Columbia. NCHP Property Management, Inc., a subsidiary of NHP, manages a total of 8,931 units in this marketplace, as follows:

<u>Maryland</u>	<u>Number of Units</u>
Avalon Apartments, Hillside	272
Branchwood Towers, Clinton	180
Brunswick House, Brunswick	52
Chapel NDP, Baltimore	175
Clay Courts, Baltimore	144
Copperstone Circle, Columbia	108
Grosvenor House, Bethesda	404*
Grosvenor Tower, Bethesda	237*
Franklin Square School #100, Baltimore	65
Hampton Hollow, Silver Spring	240
Hanover Square, Baltimore	199
Hickory Hill, Frederick	162
Hunters Crossing, Baltimore	168
Johnston Square, Baltimore	218
Kimberly Gardens, Laurel	172
Lester Morton Court, Baltimore	70
Locust Park, Columbia	160
Meadowood Townhouses I, Edgewood	130
Meadowood Townhouses II, Edgewood	161
Meadowood Townhouses III, Edgewood	238
Orchard Mews, Baltimore	101
Ruscombe Gardens, Baltimore	151
Stafford Towers, Gaithersburg	96
Village House, Gaithersburg	149
Waters Towers, Baltimore	204
Westminister Courts, Suitland	<u>115</u>
	4,416

Virginia

Number
of Units

The Ashby (McLean House), McLean	250
Evergreen House, Annandale	246**
Foxchase of Alexandria, Alexandria	2,113
Lockwood, Arlington	100**
Loudoun House, Leesburg	248
Marywood, Manassas	129**
Olde Towne West I, Alexandria	172
Olde Towne West II, Alexandria	72
Olde Towne West III, Alexandria	75
Stonegate Village, Reston	240
Strawbridge Square, Alexandria	<u>128</u>
	3,773

District of Columbia

Campbell Heights	171
Congress Park	163
Congress Park II	238
Fairmont I Apartments	114
Fairmont II Apartments	104
Garfield Hill	94
The Latrobe	176
Portner Place	48
Trinity Towers	122
Wah Luck House	<u>153</u>
	1,383

* Owned but not managed by NHP

** Management for Others

Exhibit IV-4
PARKFORD COMPANIES TRACK RECORD

Listed below are projects throughout the country that the Parkford Companies have been directly involved in and are currently involved in since 1981.

<u>Project Name</u>	<u>Location</u>	<u>No. of Units</u>
Barton's Landing	Raleigh, NC	208
Glen Oaks	Dallas, TX	142
High Oaks	Austin, TX	220
Highlands of Valley Ranch	Irving, TX	216
Highwood	Plano, TX	196
Huntington Ridge	Denver, CO	204
Meadow Road	Dallas, TX	138
Oakhaven	Dallas, TX	208
River Ranch	Ft. Worth, TX	272
Woodbridge Townhomes	Arlington, TX	189
Woodland Oaks	Tulsa, OK	228
Highland of Preston	Plano, TX	220
Highland Ridge	Plano, TX	240
Highland Trace	Plano, TX	160
Barton's Ridge	Raleigh, NC	184
LaTour Condominiums	Amarillo, TX	54
Condominiums of Bent Trail	Plano, TX	126
Parkford Oaks	Dallas, TX	174
Barton's Point	Durham, NC	192
Trails of Valley Ranch	Irving, TX	216
William's Run	Dallas, TX	252
Hampton Hollow	Silver Spring, MD	240
Penderbrook Apartments	Fairfax, VA	472
Hampton Point	Silver Spring, MD	184
Hampton Point North	Silver Spring, MD	168
Barton's Crowwing	Alexandria, VA	532
Regency Woods	Minnetonka, MN	282
Daniel's Run	Adelphi, MD	144
Penderbrook Development	Fairfax, VA	
	Total Units	6,061

V. THE RISK AND RETURN

V. RISK AND RETURN

A. INTRODUCTION

The proposed investment is structured as two separate financing transactions, a fixed rate first mortgage, and an equity joint venture which will be a general partnership between NHP Real Estate Corporation ("NHPREC"), an affiliate of NHP, Inc., and an affiliate of Fidelity & Guaranty Life Insurance Company. The fixed rate mortgage would be in the amount of \$20,000,000 which would be funded at closing. The interest rate on the mortgage would be 9.5% with a ten-year term, a five-year lock-in period, and a yield maintenance provision if a prepayment occurs between the sixth and tenth year of the loan. The equity investment amount would be \$15,350,000, of which \$13,850,000 would be invested at initial funding and the remaining \$1,500,000 would be held in escrow as a rent achievement holdback. USF&G will receive a 9.5% annual compounded cumulative preferred return on the equity capital as well as 50% of the net cash flow after its preferred return. Upon sale of the property, USF&G will receive 50% of net sales proceeds after any unpaid preferred return, an 11.5% yield maintenance payment, (equal to the amount necessary to bring USF&G's overall annual yield on total investment (IRR) to 11.5%), and repayment of its equity capital.

B. VALUATION

1. Pro Forma Income and Expenses

The proforma income and expenses for Penderbrook Apartments are presented in Exhibit V-1 and are based on the proforma rental schedule contained in the Letter of Application (Exhibit I-1), Exhibit C. The annual cash flow projections are based on the assumptions described in Exhibit V-3. The economic projections assume a 5% vacancy allowance, 5% growth on income and expenses, and a negligible lease-up period, making 1989 the estimated year of stabilization. The operating income in 1989 is projected to be \$2,720,257 which would provide a comfortable 1.43 debt coverage ratio.

2. Market Appraisal

Potomac Realty Advisors has reviewed an appraisal performed by Joseph J. Blake and Associates which estimated the market value of Penderbrook Apartments to be \$36,000,000. The valuation calculations and comparables used by Joseph J. Blake and Associates are summarized in Exhibits V-2A through V-2D. The ratio of total cost (\$35,350,000) to market value is 98%. The ratio of loan (\$20,000,000) to market value is 56%.

C. RETURN

The returns for this investment are calculated over a ten-year holding period. The mortgage provides for a five-year lock-in period and yield maintenance premium if the mortgage is repaid in year 6 through 10. It will also have a due-on-sale provision. Any partnership decision to sell

or refinance the property requires the consent of USF&G and NHPREC, and if the partners disagree, USF&G will have the Right of First Offer to purchase the property. In this manner USF&G can control the duration of both the mortgage and equity investment.

1. Annual Returns

The estimated annual cash returns to USF&G are presented in Exhibit V-4 and V-6. The cash returns are stated in two ways: annual cash returns on the equity investment and combined cash returns on the total investment (the annual cash return on the mortgage is a constant 9.5%, and therefore is not included on the exhibit). The estimated total return to USF&G (debt and equity) in the stabilized year (1989) is 7.7%. The total returns fluctuate between 7.94% and 10.34% through the remaining holding period. During the investment holding period, the difference between the actual equity cash return and the 9.5% preferred return rate is accrued and compounded annually.

2. Cash Proceeds at Sale

At the time of sale, net proceeds are first used to pay off the outstanding mortgage balance, second to return the equity capital, third to pay the unpaid cumulative preferred return, and fourth to pay an 11.50% yield maintenance payment to USF&G. Any remaining cash after the above disbursements are split 50-50 between USF&G and NHPREC. Using conservative assumptions, the amount of unpaid cumulative preferred return is estimated to be \$2,391,560 and the yield maintenance payment is estimated to be \$11,874,003. Because of the cumulative preferred return and the yield maintenance payment, USF&G receives 97% of the cash proceeds remaining after repayment of USF&G's total invested capital (\$35,350,000). See Exhibit V-7.

3. Yield Analysis

The estimated nominal yield on total capital (internal rate of return) assuming 5% growth in income and expenses is 11.57%. This represents a 6.57% real or inflation-adjusted return. The estimated nominal yield on total capital is derived by taking USF&G's total investment and USF&G's total annual cash flow and sales proceeds and capital repayments over the ten year holding period (see Exhibit V-5). The sensitivity of USF&G's yield to changes in inflation and terminal capitalization rates is demonstrated in Exhibit V-8A. The nominal yield on total capital varies from a low of 9.09% under low inflation and high capitalization to a high of 12.87% under high inflation and low capitalization. The 11.57% yield on total capital represents a 9.5% yield on the mortgage capital and a 13.61% yield on the equity capital. The sensitivity of the equity yield to changes in inflation and the capitalization rates is also shown in Exhibit V-8A. Exhibit V-8B shows the sensitivity of USF&G's yield to the holding period of the property at various terminal capitalization rates. The yield at the higher capitalization rates increases as the holding period increases, while the yield at the lower capitalization rate remains relatively constant over time.

D. RISK

In the proposed debt-equity joint venture investment, USF&G is exposed to all of the risks associated with a real estate investment plus the additional risks of being both the lender and general partner in the borrowing entity. The risks in this investment have been reduced to acceptable levels by careful and conservative underwriting as well as by specific provisions in the deal structure. Generally the risk can be divided into four categories: market, operational, financial, and partnership.

1. Market Risk

This risk arises if the Fairfax County apartment market fails to perform adequately with regard to rent levels and occupancies. The investment structure addresses this market risk specifically in two ways. First, the property will not go to closing until the seller achieves 80% economic occupancy. The use of economic occupancy will completely eliminate any effects of concessions or giveaways used in the lease-up period. Second, the seller will be required to earn out the top \$1.5 million of the purchase price, and will not completely earn out the \$1.5 million until seller has achieved 95% economic occupancy. The initial funding gives USF&G proper security and yield based on occupancy at closing; any additional funding must be earned. Effective rent (net of all concessions) will be used for the earnout calculation thereby assuring USF&G that actual (not projected) performance will determine the investment level. Parkford has only 12 months to earn the \$1,500,000 holdback. At the end of 12 months any monies not earned will be returned to USF&G and treated as a reduction to equity.

There is a risk to USF&G if rents actually decrease from today's level. However, the Fairfax County apartment market has performed exceptionally well over the past ten years, a period of rapid growth in Fairfax County. During the past 12 years, the supply of rental housing in Fairfax County has actually declined and occupancy levels have remained high. The strong economy of Fairfax County and the superior location of the property should provide a favorable climate for this investment.

2. Operational Risk

The operational risk in this investment is considered minimal. Management and leasing will be provided initially by the Parkford Companies, who will manage during the earnout period. Management and leasing will then be provided by NCHP Property Management, Inc., a subsidiary of NHP, who successfully manages and leases over 8,900 units in the metropolitan Washington, D.C. area. As additional protection, USF&G will have the right to review and approve annual operating and capital budgets.

3. Financial Risk

The financial risks in this investment are acceptable because USF&G will hold back \$1,500,000 of the equity funding, which will be disbursed as the property progresses from 80% to 95% economic occupancy. The \$20,000,000 loan is well secured, with a projected debt coverage ratio in the first year of 1.43. NHPREC has also provided a 24-month cash flow deficit guarantee (up to a limit of \$1,900,000). The equity investment also has good security with a 9.5% cumulative preferred return feature and an 11.5% yield maintenance provision. NHPREC's 50% interest in annual cash flow is fully subordinated to USF&G's cumulative preferred return. NHPREC's 50% interest at sale is fully subordinated to USF&G's equity repayment, unpaid cumulative preferred return and 11.5% yield maintenance payment. In other words, NHPREC does not share in net sales proceeds until USF&G has received an 11.5% overall annual yield (IRR) on its total debt and equity investment.

4. Partnership Risk

While NHPREC is the managing general partner, USF&G has the right to approve all major partnership decisions. If partnership problems should occur, a buy-sell agreement can quickly remove NHPREC from the partnership. Also, if NHPREC does not contribute its pro-rata share of capital contributions, its ownership position would be quickly diluted. If USF&G should own more than 75% of the partnership, NHPREC would not have partnership control.

E. CONCLUSIONS AND RECOMMENDATIONS

Penderbrook Apartments is a new, 33% pre-leased, 424-unit garden apartment in 19 buildings of two-story and three-story split level design in Fairfax County, Virginia. The project was developed, leased and managed by the Parkford Companies, who will continue to manage and lease the property during the earnout period. After the earnout period, NCHP Property Management, Inc., an affiliate of NHPREC will manage and lease the property, and NHPREC will serve as the managing general partner of the partnership. The Fairfax County apartment market has been exceptionally strong over the past decade and is projected to maintain that strength through the year 2000. The expected return on total capital for this investment provides an adequate return for the risks involved. Therefore, Potomac Realty Advisors recommends that the Real Estate Investment Committee for the United States Fidelity & Guaranty Company approve the commitment of \$35,350,000 for a debt equity joint venture under the terms and conditions outlined in Exhibit I-1.

Exhibit V-1

PRO FORMA INCOME AND EXPENSES

Gross Potential Income	\$4,141,902
Quarters Allowance	(36,000)
Other Income	67,600
Vacancy Allowance	<u>(207,095)</u>
Effective Gross Income	\$3,966,407
Payroll	\$ 202,537
Renting and Leasing Expense	18,732
Management Fee (@ 5% of EFI)	198,165
Administrative Expense	186,229
Utilities	112,292
Repairs and Maintenance, Service Contracts	137,951
Real Estate Taxes, Insurance and Other Fees	<u>390,244</u>
Net Operating Income	\$2,720,257
Mortgage Payment	<u>(1,900,000)</u>
Cash Flow	820,257
Cumulative Preferred Return to Equity	<u>820,257</u>
Cash Flow to Split	0
USF&G's Share	50.00%
USF&G Cash Flow (Operations)	0
USF&G Cumulative Preferred Return	<u>820,257</u>
Total USF&G Cash Flow	<u>820,257</u>
Indicated Debt Coverage Ratio:	1.43

**Exhibit V-2A
VALUATION SUMMARY**

The market value of the subject property was estimated by Joseph J. Blake and Associates as of April 5, 1988 to be \$36,000,000. Potomac Realty Advisors has reviewed Blake's appraisal dated April 5, 1988 and concurs that the market value of the subject property is \$36,000,000. The following is a brief summary of the appraisal:

Cost Approach to Value

Cost of Improvements (See Exhibit V-2B)	\$21,933,198
+ Value of Land (See Exhibit V-2C)	8,500,000
+ Developer's Profit @ 15%	<u>4,564,980</u>
= Estimated Value	\$34,998,178
Rounded to	\$35,000,000

Direct Sales Comparison Approach

Effective Gross Income (See Exhibit V-2D)	\$ 3,836,210
X Gross Income Multiplier (See Exhibit V-2D)	<u>9.0</u>
= Estimated Value	\$34,615,890
Rounded to	\$34,600,000

Capitalized Income Approach

	<u>Lease-Up</u>	<u>Stabilized</u>
Present Value of Net Operating Income @ 12%	\$16,743,221	\$18,416,787
+ Present Value of Net Sales Proceeds @ 12%	<u>17,762,467</u>	<u>17,762,467</u>
= Estimated Value	\$34,505,688	\$36,179,254
Rounded to	\$34,500,000	\$36,000,000

Value Reconciliation

Present Value -- As Stabilized (as of April 5, 1988)	\$36,000,000
Indicated Ratio of Total Costs to Value	98.19%
Indicated Ratio of Loan to Value	55.56%

Exhibit V-2B
COST OF IMPROVEMENTS

The following is a summary of the method in which Joseph J. Blake and Associates computed the estimated replacement cost of improvements. Potomac Realty Advisors has reviewed and concurs with this methodology.

Building Improvements: A 424-unit garden apartment complex having 18 3-story buildings. The gross building area will be 327,008 square feet and the net rentable space 311,564 square feet. There will be a 4,000 square foot Clubhouse and surface parking spaces.

Building Component:	<u>Apartments</u>	<u>Clubhouse</u>
Building Class:	C	C
Building Quality:	Excellent	Excellent
Basic Structure:	\$40.24*	\$73.26*
Exterior Wall:	\$14.88*	\$ 0
HVAC:	\$ 5.98*	\$ 0
Total Base Cost:	\$61.10	\$73.26
Size/Shape Multiplier:	\$.99	\$ 1.03
Current Cost Multiplier:	\$ 1.00	\$ 1.00
Local Cost Multiplier:	\$ 1.05	\$ 1.05
Final Base Cost:	\$63.51	\$79.23

Replacement Cost New

GROSS BUILDING AREA X FINAL BASE COST = REPLACEMENT COST NEW

Apartment:	327,008 SF	X	\$63.51	=	\$20,768,278
Clubhouse:	4,000 SF	X	\$79.23	=	<u>316,920</u>

Total Replacement Cost New: \$21,085,198

Site Improvements:

The depreciation of site improvements is classified as short-lived items, being subject to physical incurable obsolescence. After carefully examining components, as they relate to the subject property, the following was concluded:

Landscaping, Concrete Curbs and Pads, Macadam Paving, Etc. @ (\$2,000/unit)	<u>848,000</u>
--	----------------

Total Improvements: **\$21,933,198**

* Source: Marshall Valuation Service

Exhibit V-2C
LAND VALUATION

Joseph J. Blake and Associates conducted an extensive search for sales of properties similar in character to the Penderbrook site. The following is a summary of the comparable land sales compiled by Blake in their analysis. Based on their research, Blake assigned a value of approximately \$20,000/unit to the Penderbrook site. Potomac Realty Advisors has reviewed the land sale analysis and concurs with Blake's conclusions.

<u>Sale #</u>	<u>Date</u>	<u>Sale Price</u>	<u>Acres</u>	<u># of Units</u>	<u>Price/Unit</u>
1	Early '88	\$22,425,000	58.00	1,150	\$19,500
2	12/87	\$ 5,400,000	4.14	344	\$15,698
3	10/87	\$ 8,885,000	10.20	540	\$16,454
4	12/86	\$ 4,560,000	10.89	228	\$20,000
5	12/86	\$ 4,625,000	10.00	250	\$18,500
6	9/86	\$ 7,296,000	36.48	584	\$12,493
7	7/86	\$ 2,856,000	8.37	313	\$17,000

Exhibit V-2D
DIRECT SALES COMPARISON APPROACH

Joseph J. Blake and Associates conducted extensive research for sale of improved properties comparable to the Penderbrook Apartments. The following table summarizes the results of their research:

<u>Sale #</u>	<u>Date</u>	<u>Year Built</u>	<u>Price*</u>	<u># of Units</u>	<u>Price/Unit</u>	<u>EGIM</u>	<u>OCR*</u>
1 (Subject)	Asking 4/88	1988	\$34,650,000	424	\$81,722	8.47	8.18%
2	Offering 4/88	1988	\$22,000,000	316	\$69,620	9.44	7.10%
3	12/87	1970	\$24,500,000	443	\$55,305	6.32	8.61%
4	9/87	1987	\$11,550,000	192	\$60,156	7.29	8.50%
5	12/86	1986-87	\$20,550,000	352	\$58,380	7.78	8.55%
6	12/86	1980	\$11,130,000	185	\$60,162	7.65	8.09%
7	10/86	1985	\$10,400,000	190	\$54,737	7.72	8.48%

* Adjusted for cash equivalency.

Blake adjusted the above results for factors such as time of sale, financing, location, physical characteristics and occupancy rate, and determined the appropriate "Effective Gross Income Multiplier" (EGIM) for valuation purposes to be 9.0. Potomac Realty Advisors has reviewed this analysis and these adjustments and has determined that this approach is reasonable.

Exhibit V-3

ASSUMPTIONS TABLE

Mortgage Amount:	\$20,000,000
Interest Rate on Mortgage:	9.50%
Amortization Period:	NA
Payments per Year:	12
Equity Investment:	\$15,350,000
Cumulative Preferred Return on Equity:	9.50%
Equity Ownership %:	50.00%
Required USF&G Yield Before 50-50 Split at Sale:	11.50%
Capitalization Rate in Year of Sale:	8.50%
Sales Expense (% of Sales Price)	3.00%
Growth Rate - Income	5.00%
Growth Rate - Expenses	5.00%
Vacancy Rate	5.00%

**EXHIBIT V-4
PROJECTED PROPERTY CASH FLOW**

	No. of units	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Gleneagle:												
Terrace level	42	348,705	366,140	384,447	403,670	423,853	445,046	467,298	490,663	515,196	540,956	568,004
Mid-level	42	353,871	371,565	390,143	409,650	430,132	451,639	474,221	497,932	522,829	548,970	576,419
Vaulted ceiling	42	361,620	379,701	398,686	418,620	439,551	461,529	484,605	508,836	534,277	560,991	589,041
Turnberry:												
Terrace level	36	332,100	348,705	366,140	384,447	403,670	423,853	445,046	467,298	490,663	515,196	540,956
Mid-level	36	338,742	355,679	373,463	392,136	411,743	432,330	453,947	476,644	500,476	525,500	551,775
Vaulted ceiling	36	345,384	362,653	380,786	399,825	419,816	440,807	462,848	485,990	510,289	535,804	562,594
Prestwick:												
Terrace level	40	418,200	439,110	461,066	484,119	508,325	533,741	560,428	588,449	617,872	648,765	681,204
Mid-level	32	338,496	355,421	373,192	391,851	411,444	432,016	453,617	476,298	500,113	525,118	551,374
Vaulted ceiling	40	415,740	436,527	458,353	481,271	505,335	530,601	557,131	584,988	614,237	644,949	677,197
St. Andrews												
Terrace level	26	292,617	307,248	322,610	338,741	355,678	373,462	392,135	411,742	432,329	453,945	476,642
Mid-level	26	295,815	310,606	326,136	342,443	359,565	377,543	396,420	416,241	437,053	458,906	481,851
Vaulted ceiling	26	300,612	315,643	331,425	347,996	365,396	383,666	402,849	422,991	444,141	466,348	489,665

Gross Potential Income	424	4,141,902	4,348,997	4,566,447	4,794,769	5,034,508	5,286,233	5,550,545	5,828,072	6,119,476	6,425,449	6,746,722
- Quarters Allowance		(36,000)	(37,800)	(39,690)	(41,675)	(43,758)	(45,946)	(48,243)	(50,656)	(53,188)	(55,848)	(58,640)
+ Other Income		67,600	70,980	74,529	78,255	82,168	86,277	90,590	95,120	99,876	104,870	110,113
- Vacancy Allowance		(207,095)	(217,450)	(228,322)	(239,738)	(251,725)	(264,312)	(277,527)	(291,404)	(305,974)	(321,272)	(337,336)
= Effective Gross Income		3,966,407	4,164,727	4,372,964	4,591,612	4,821,192	5,062,252	5,315,365	5,581,133	5,860,189	6,153,199	6,460,859
- Operating Expenses		1,246,150	1,308,458	1,373,881	1,442,575	1,514,703	1,590,439	1,669,961	1,753,459	1,841,131	1,933,188	2,029,847
= Net Operating Income		2,720,257	2,856,269	2,999,083	3,149,037	3,306,489	3,471,813	3,645,404	3,827,674	4,019,058	4,220,011	4,431,011
- Mortgage Payment		(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	(1,900,000)	
= Cash Flow (Deficit)		820,257	956,269	1,099,083	1,249,037	1,406,489	1,571,813	1,745,404	1,927,674	2,119,058	2,320,011	
+ Deficits Paid by Remaining Loan \$		0	0	0	0	0	0	0	0	0	0	0
+ Deficits Paid by Equity		0	0	0	0	0	0	0	0	0	0	0
= Cash Flow Before Cum. Pref. Return		820,257	956,269	1,099,083	1,249,037	1,406,489	1,571,813	1,745,404	1,927,674	2,119,058	2,320,011	
- Cum. Pref. to Equity		820,257	956,269	1,099,083	1,249,037	1,406,489	1,571,813	1,685,448	1,685,448	1,685,448	1,685,448	
= Cash Flow to Split		0	0	0	0	0	0	59,956	242,226	433,610	634,563	

Cash Distribution on Sale in Year 10

Projected Sales Price												\$52,129,546
- Selling Expenses												(1,563,886)
- Unpaid Mortgage Balance												(20,000,000)
- Prepayment Penalty												0
= Cash Proceeds From Sale Before Equity Repayment												30,565,660
- USF&G Equity Repayment												(15,350,000)
- Unpaid Cum. Pref.												(2,391,560)
= Cash Proceeds For Yield Maintenance												12,824,100
- Yield Maintenance to USF&G (11.5% Yield)												(11,874,033)
Cash Proceeds to Split												950,067
x USF&G's Percent of the Split												50.00%
= USF&G's Share												\$475,033

USF&G Equity Yield Analysis:

USF&G Equity Contrib. (15,350,000)	0	0	0	0	0	0	0	0	0	0	0	0
USF&G Cumulative Preferred	820,257	956,269	1,099,083	1,249,037	1,406,489	1,571,813	1,685,448	1,685,448	1,685,448	1,685,448	1,685,448	
USF&G Split of Cash Flow	0	0	0	0	0	0	29,978	121,113	216,805	317,281		
Return of Capital	0	0	0	0	0	0	0	0	0	0	15,350,000	
Unpaid Cum. Pref.	0	0	0	0	0	0	0	0	0	0	2,391,560	
Equity Yield Maintenance Payment	0	0	0	0	0	0	0	0	0	0	11,874,033	
USF&G Residual Sales Proceeds	0	0	0	0	0	0	0	0	0	0	475,033	
Equity Cash Flow	(15,350,000)	820,257	956,269	1,099,083	1,249,037	1,406,489	1,571,813	1,715,426	1,806,561	1,902,253	32,093,356	
Estimated Yield on Equity		13.61%										
Cash on Cash Return (Equity)		5.13%	5.78%	6.46%	7.18%	7.97%	8.86%	9.67%	10.18%	10.72%	11.29%	
Cash on Cash Return (Combined)		7.70%	7.94%	8.21%	8.51%	8.84%	9.22%	9.58%	9.82%	10.07%	10.34%	

EXHIBIT V-5
INVESTORS YIELD SUMMARY

Year	Annual Debt Service	Unpaid Mortgage Balance (1)	Cumulative Preferred Return (2)	Cash Flow - Operations (3)	Unpaid Equity Balances (4)	Unpaid Cum Pref	Yield Maintenance (5)	Cash Flow - Sale (6)	Total Cash Flow - USF&G
1	1,900,000		820,257	0					2,720,257
2	1,900,000		956,269	0					2,856,269
3	1,900,000		1,099,083	0					2,999,083
4	1,900,000		1,249,037	0					3,149,037
5	1,900,000		1,406,489	0					3,306,489
6	1,900,000		1,571,813	0					3,471,813
7	1,900,000		1,685,448	29,978					3,615,426
8	1,900,000		1,685,448	121,113					3,706,561
9	1,900,000		1,685,448	216,805					3,802,253
10	1,900,000	20,000,000	1,685,448	317,281	15,350,000	2,391,560	11,874,033	475,033	53,993,356

Estimated Yield: 11.57% (7)

(1) Original Loan Balance = \$20,000,000.

(2) USF&G receives a 9.5% Cumulative Preferred Return on its Outstanding Equity Balance.

(3) USF&G receives 50% of Cash Flow from operations after payment of (a) Debt Service and (b) a 9.5% Cumulative Preferred Return.

(4) USF&G's Equity Commitment is \$15,350,000.

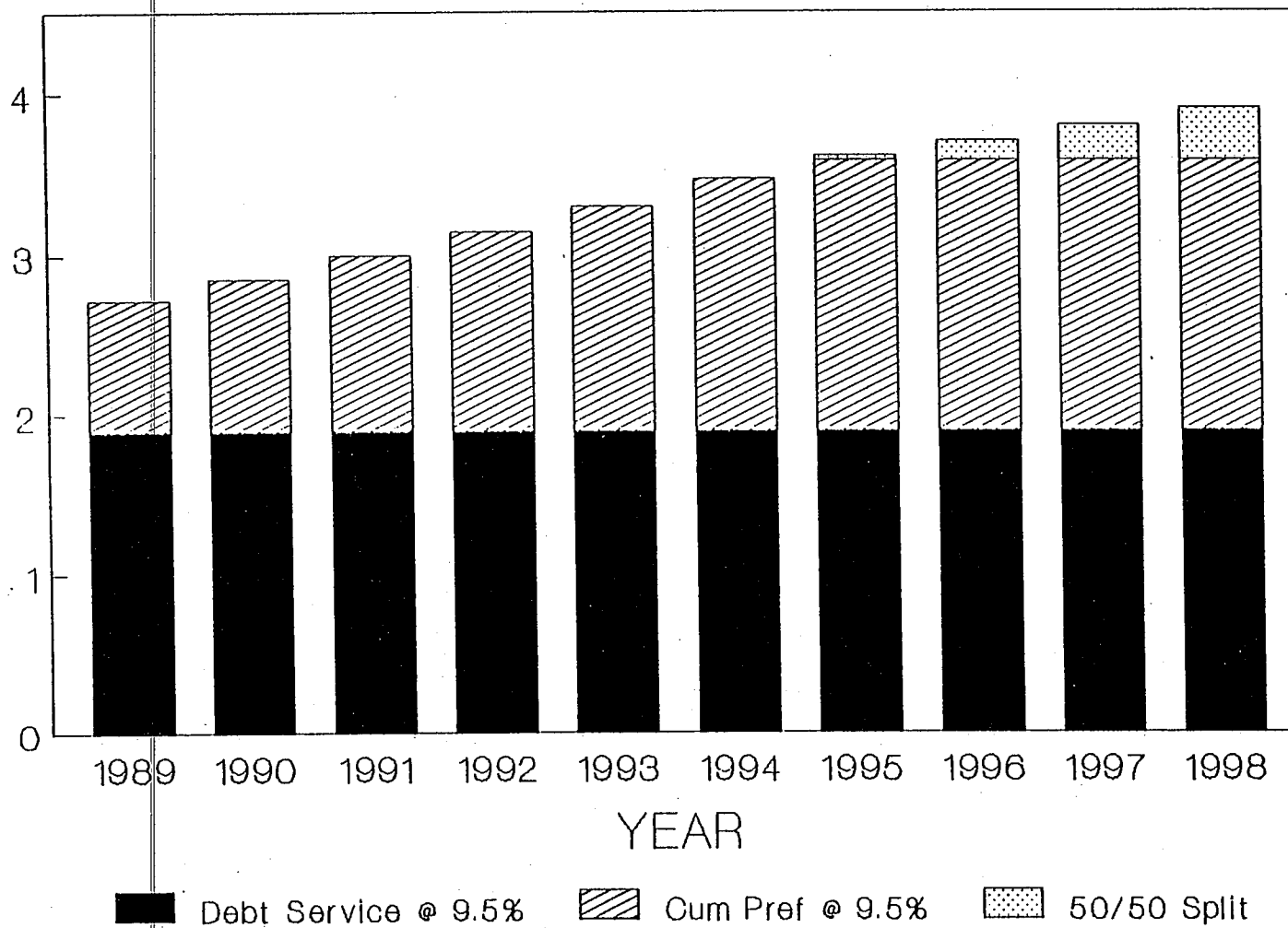
(5) USF&G receives a Yield Maintenance payment equal to the amount necessary to bring USF&G's annual yield on total investment to 11.5%.

(6) Equal to Net Sales Price of \$50,565,660 less the outstanding loan balance of \$20,000,000, less USF&G's Equity Repayment of \$15,350,000, less USF&G's unpaid cum. pref. of \$2,391,560, less USF&G's Yield Maintenance payment of \$11,874,033 split 50/50 with Borrower.

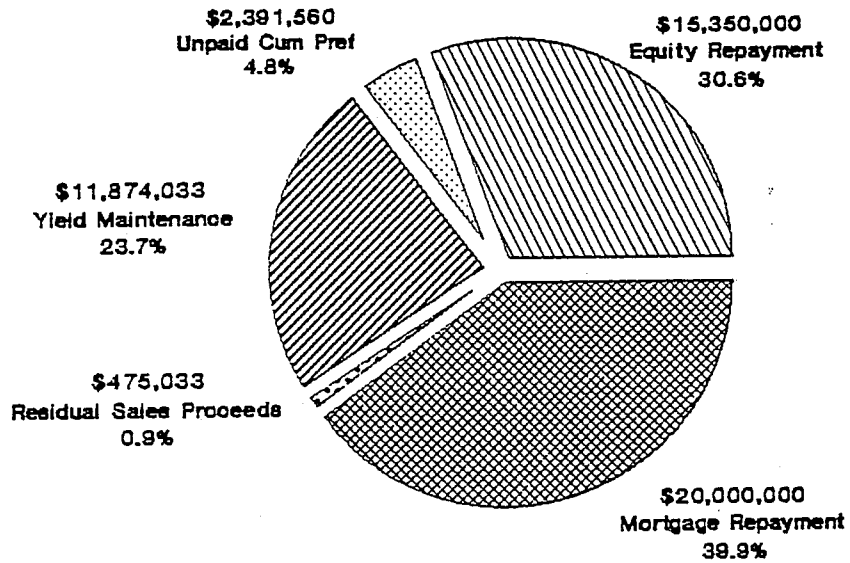
(7) Internal rate of return assuming cash investment (debt and equity) of \$35,350,000 made in year 0.

EXHIBIT V-6 TOTAL USF&G CASH FLOW

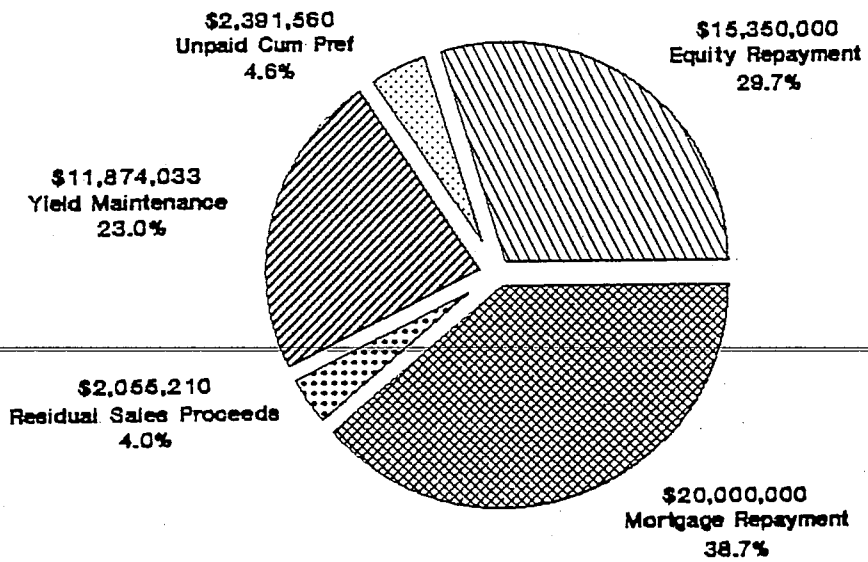
CASH FLOW ON DEBT AND EQUITY (Millions)



**EXHIBIT V-7A
COMPOSITION OF USF&G'S
PROCEEDS AT SALE - 8.5% CAP**



**EXHIBIT V-7B
COMPOSITION OF USF&G'S
PROCEEDS AT SALE - 8.0% CAP**



**EXHIBIT V-8A
SENSITIVITY ANALYSIS
CAP RATES AND INFLATION**

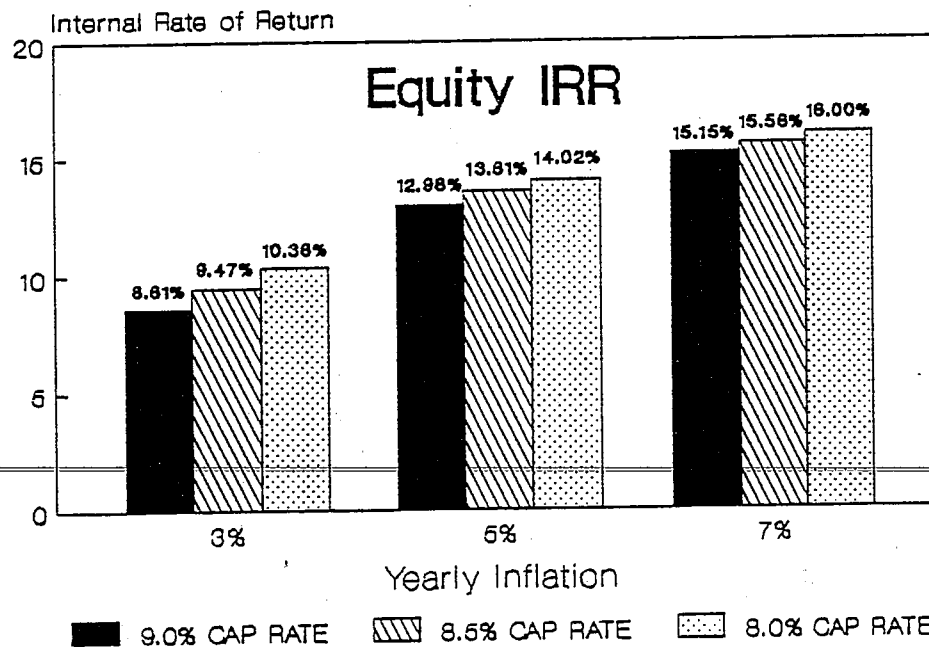
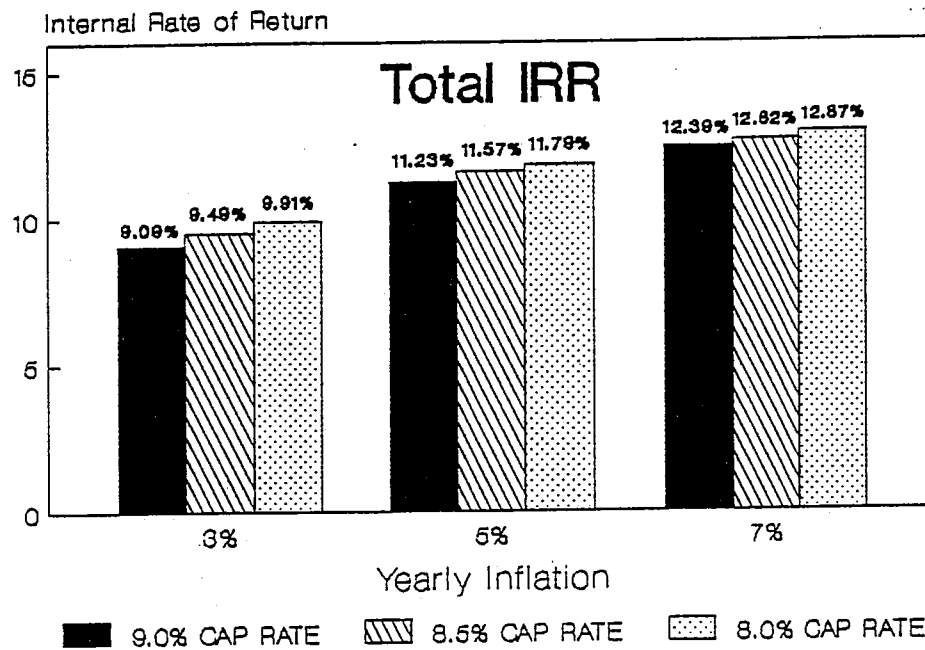
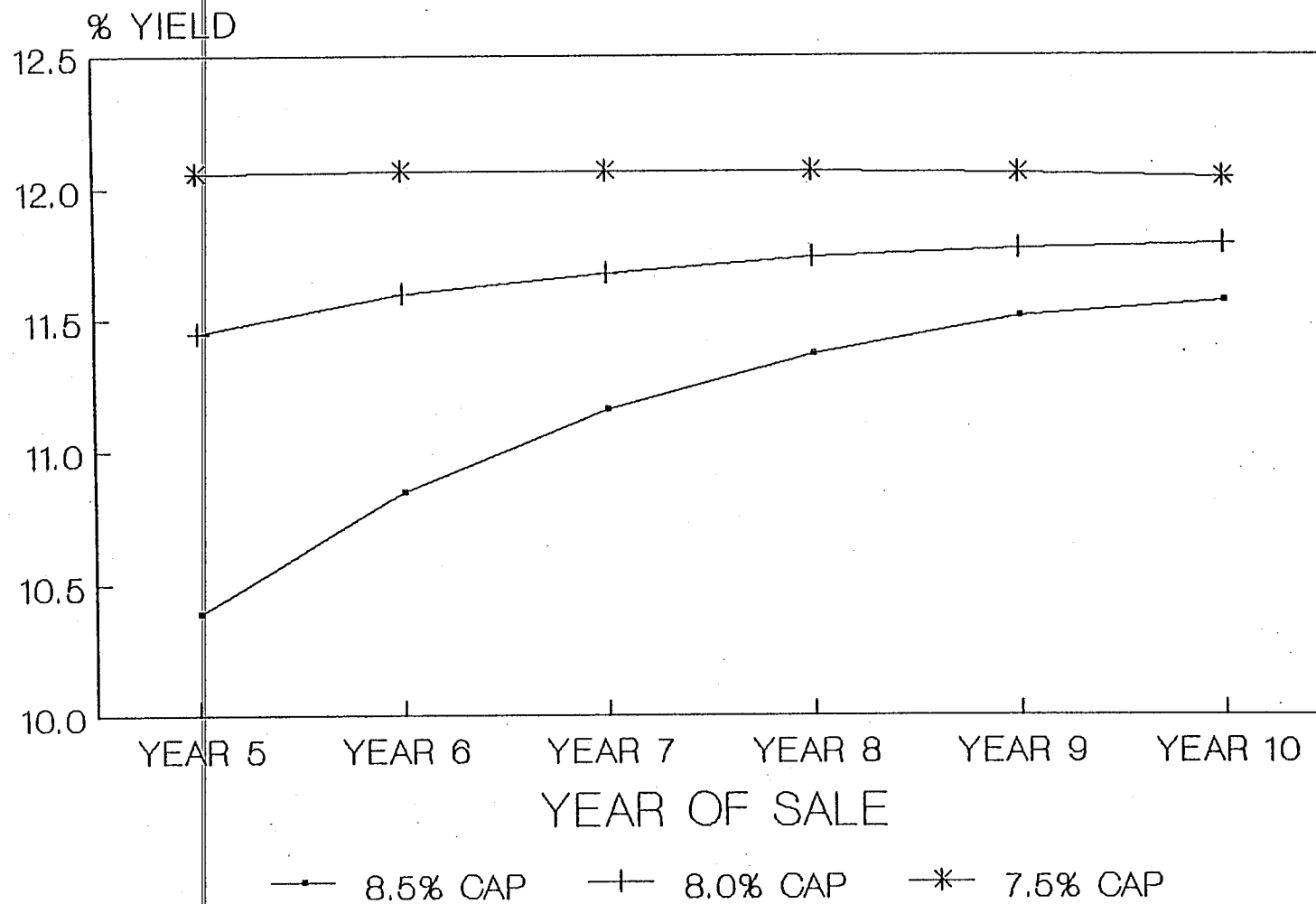


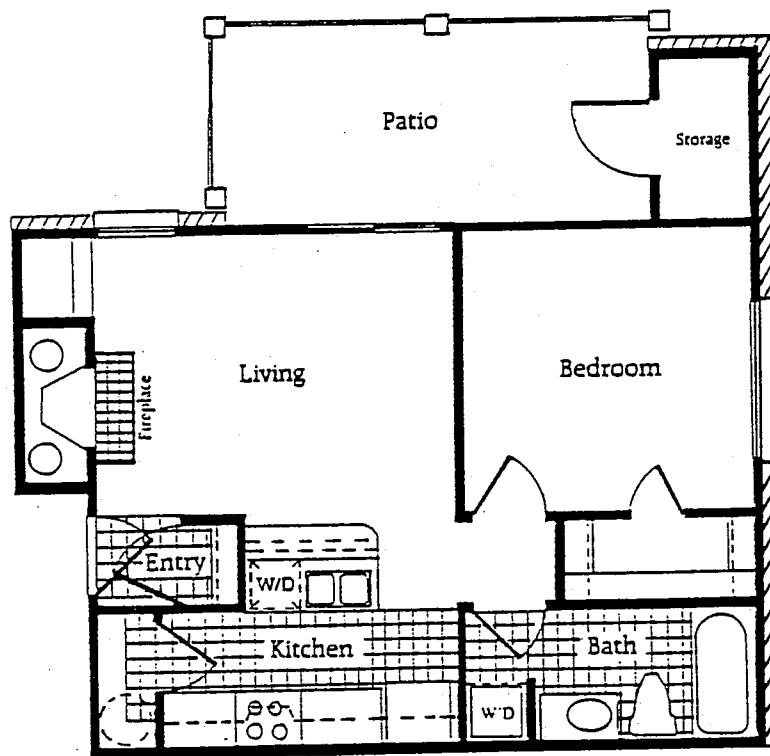
EXHIBIT V-8B
SENSITIVITY ANALYSIS
YIELD VS HOLDING PERIOD



APPENDIX A
FLOOR PLANS

THE GLENEAGLE

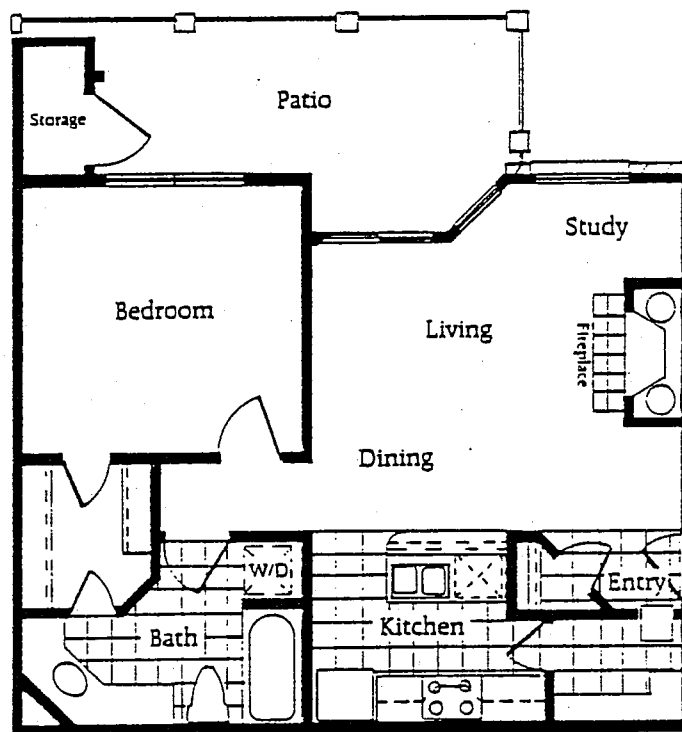
1 Bedroom,
1 Bath



564 SQUARE FEET

THE TURNBERRY

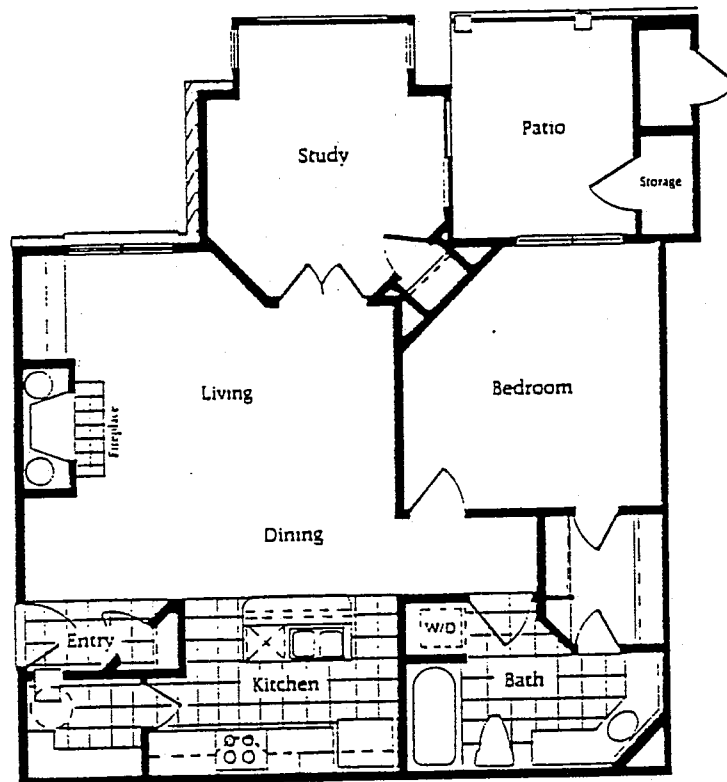
1 Bedroom,
1 Bath



665 SQUARE FEET

THE PRESTWICK

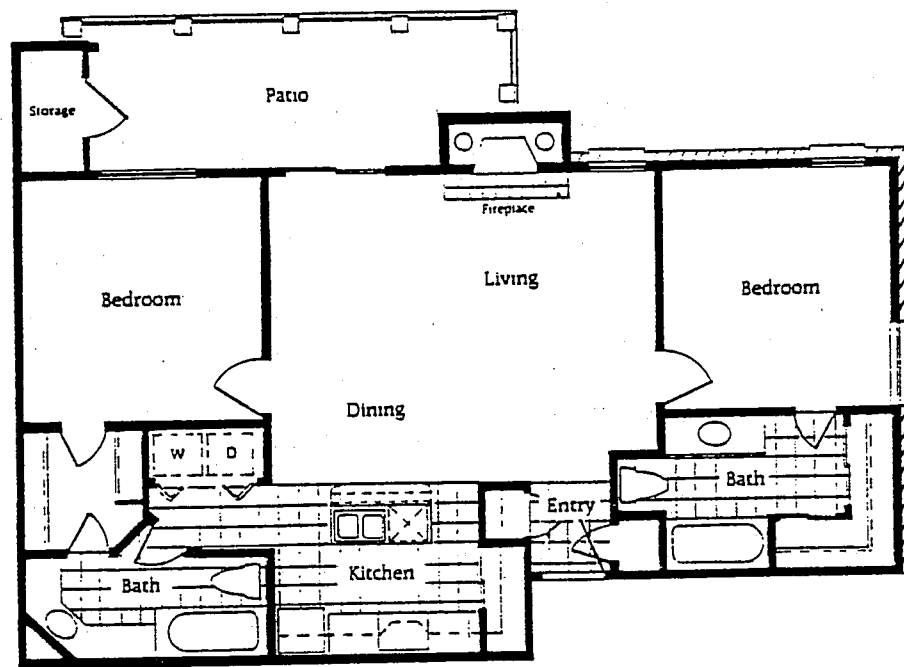
1 Bedroom/Den.
1 Bath



821 AND 851 SQUARE FEET

THE ST. ANDREWS

2 Bedrooms,
2 Baths



1,031 SQUARE FEET

NO. 052597

COUNTY OF FAIRFAX, VIRGINIA
DEPARTMENT OF ENVIRONMENTAL MANAGEMENT
DIVISION OF DESIGN REVIEW
RESIDENTIAL USE PERMIT
02/26/88

P. 3/3
DEPT. (TX): 9320
Use - Emergency Permit

STREET
NUMBER

03905

STREET NAME

PENDerview

ST
TY

DR

ACT
NO.

001

LEVEL

UNIT

ACT
NO.

01

LOT
NUMBER

SUBDIVISION NAME

PENDERBROOK

MAP REFERENCE NUMBER

044- /01/ /0071-

INSP
AREA

4

DATE

~~2-22-88~~

2-25-88

2-16-88

2-26-88

2-29-88

2-29-88

ELECTRICAL

PLUMBING

MECHANICAL

BUILDING

PUBLIC UTILITIES

APPROVED

REMARKS

INS
Emergency Permit
~~Cy Retzle~~
~~Don Brax~~
~~R.C. Wilt~~
~~Ronald Hosh~~
~~Mike Ernst~~
~~Mike Ernst~~

THE FOLLOWING REQUIREMENTS, IF CHECKED, ARE BEING WAIVED IN
ACCORDANCE WITH CHAPTER 112 ARTICLE 18 PART 704 OF THE FAIRFAX
COUNTY CODE TO OBTAIN A RESIDENTIAL USE PERMIT:

- ☒ FINAL GRADING, SODDING, SEEDING OF LOT
- ☒ COMPLETION OF LANDSCAPING AND SCREENING REQUIREMENTS
- ☒ COMPLETION OF SIDEWALKS
- ☒ BITUMINOUS CONCRETE STREET/DRIVEWAY SURFACE
- ☒ ADEQUATE STAND OF GRASS

***** ATTENTION *****
***** NO TREES OR SHRUBS MAY BE PLANTED IN THE DEDICATED *****
***** RIGHT-OF-WAY WITHOUT FIRST OBTAINING A PERMIT FROM *****
***** FAIRFAX COUNTY. FOR FURTHER INFORMATION CALL 691-3431. *****
***** WHEN EXCEPTIONS FOR FINAL GRADING, SODDING AND/OR *****
***** SEEDING ARE GRANTED DURING THE WINTER, THE BUILDER IS *****
***** OBLIGATED TO COMPLETE THIS WORK BY THE FIRST DAY OF MAY. *****
***** HOMEOWNER *****
***** BUILDER *****
***** ZONING *****

USF&G

P.O. Box 1138 • Baltimore, Maryland 21203 • (301) 547-3000

Realty

Gary L. Burke
Real Estate Investment Officer

Handwritten notes:
Penderbrook
1/13/89

January 13, 1989

Mr. Michael W. Jones
Potomac Realty Advisors
1010 W. Glebe Road
Suite 800
Arlington, VA 22201

Dear Mike:

Attached is a letter for Fairfax County which indicates that Penderbrook Apartments have no outstanding code violations. Please keep a copy for your files.

Very truly yours,

Handwritten signature of Gary L. Burke

Gary L. Burke

GLB/rlj

Attachment



INTEROFFICE CORRESPONDENCE

File - Penderbrook Apartments JAN 06 1989

JAN 12 1989

Ron Hughes

TO: H.O. Administrative Services - Michael B. Casey, Vice President

DATE: 1/5/89

FROM: H.O. Field Operations - Richard L. Nauman, Assistant Secretary

SUBJECT: Penderbrook Apartments
Fairfax, Virginia

Dear Mike:

Attached please find correspondence on the above which was somehow received in the Richmond Branch Office. If the correspondence does not concern something about which your department is involved, I would appreciate you forwarding it on to the correct party.

Sincerely,

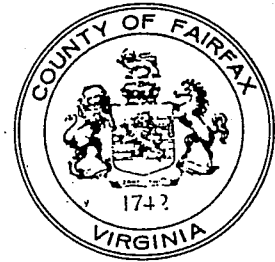
Richard L. Nauman

RLN/kf
Attachment





COMMONWEALTH OF VIRGINIA
COUNTY OF FAIRFAX
4100 CHAIN BRIDGE ROAD
FAIRFAX, VIRGINIA 22030



Telephone: 352-0863

DATE: November 8, 1988

Arent, Fox, Kintner, Plotkin & Kahn
ATTN: Kelli D. Moss
Washington Square
1050 Connecticut Ave., NW
Washington, DC 20036-5339

Subject: Penderbrook Apartments, 3905 Penderview Drive,
Fairfax, VA, 22033, Tax Map 046-3- /01/ /0071-

Dear Ms. Moss:

Pursuant to your request of November 4, 1988, inquiring of the status of any outstanding code violations for Buildings 1 through 20 of the above complex, the Code Enforcement Branch does not have any record of violations or complaints in reference to this project.

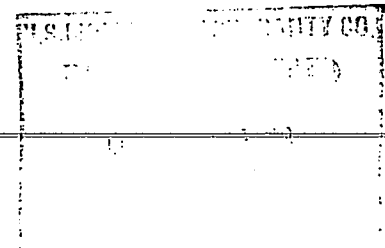
Any building or fire code discrepancies which were discovered in the course of construction would have been required to be corrected prior to the issuance of use permits for the buildings. A computer check of the Use Permit File shows all the use permits appear to be in order. Any inspection records generated during construction would not be in the custody of this branch, but would be retained by the Division of Inspection Services, Building Inspections Branch, Critical Structures Section.

If you have any questions on the above, or require clarification, please call Mr. Ed Harris of the Code Enforcement Branch, at 703-352-0863.

Sincerely,

Catherine Riley-Hall

Catherine Riley-Hall
Chief, Code Enforcement Branch
Department of Environmental Management
10555 Main Street, 2nd Floor
Fairfax, VA 22030



cc: Fidelity and Guaranty Life Insurance Co., 100 Light Street,
Baltimore, MD 21202
NHP Real Estate Corporation, 1225 Eye Street, NW,
Washington, DC 20005