

2022 Management Report To Stakeholders

September 28, 2022

Welcome to Co-op City. For those of you who are here for the first time, you are in the largest affordable cooperative housing complex in the country. We have 15,372 apartments located in 35 high-rise buildings and seven (7) townhouse clusters. In addition, the complex has three commercial centers, eight parking structures and a 40 megawatt combined heat and power plant that produces and supplies all of the electrical, heating and cooling needs of the entire community. We also have a Public Safety Department that provides community policing to ensure the safety and security of Co-op City's residents, and our own garbage and recycling transfer facility. If we were an independent municipality, we would be the 10th largest in the state.

Since last we gathered in June 2020, we have continued to make progress to improve the infrastructure and operations of Co-op City, albeit during a challenging period. The community was hit hard by the pandemic. Many residents passed away. Management staff, in conjunction with multiple social service programs, operated weekly food banks that also included mask and hand sanitizer distribution. Working with the City government, we provided a vacant commercial space for daily Covid testing that was open for over a year. Once vaccines became available, we provided Dreiser Auditorium for a mass vaccination center thanks to then-Mayor de Blasio and Congressman Bowman. All this was going on while we continued to manage the day-to-day business of the corporation and provide services to the residents.

As the pandemic continues to recede, we now grapple with problems many other companies are facing. We are having difficulty filling vacant positions in all of our departments. We are subject to both supply chain shortages of necessary supplies and price increases for all goods and services we purchase. Most problematic and costly are the significant increases we are experiencing for natural gas, oil, water rates and insurance premiums. Together, these costs have created a \$14 million deficit in our current budget, requiring a 7.5% emergency carrying charge increase.

Capital Projects

Despite dealing with the operational challenges created by the pandemic, we were able to continue with the execution of our capital improvement program. In the last two years, we have completed the following capital projects:

1. Modernization of all 160 residential elevators.
2. LL 11 façade restoration work to 22 of our 35 high-rise buildings.
3. Installation of ADA-compliant lobby entrances in 15 Tower buildings (entrances in 10 Chevron buildings had been completed in 2020).
4. Renovation of Dreiser Auditorium and four restrooms to comply with the ADA.
5. Installation of a fire alarm system in Einstein Mall (Bartow was completed in 2019).
6. Concrete restoration in Garage #2.
7. Restoration and ADA compliance work to four public restrooms in Bartow Mall.

Current projects that are in progress or will be commenced this fiscal year include:

1. Local Law 11 Façade Inspections and Restoration. Work has begun on Buildings 1-8 and 15-19 and will be completed by the end of 2023. This will complete all repairs for Cycle 8 and all buildings will be filed as "Safe" for Cycle 9.

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Bob Klehammer



2. Replacement of Triple Core building entrances with ADA-compliant doors. Work will be completed in February 2023. These are the final buildings to receive this improvement.

3. Complete engineering review for the replacement and upgrade of exterior concrete areas and waterproofing at Einstein Mall. Similar work has been completed to the Bartow and Dreiser Malls in 2019.

4. Improvements in all building pump rooms, including replacement/repair of pump bases; pumps, where needed; improved lighting and reinsulating piping.

5. Complete engineering review for the replacement/improvement of the convector system.

6. Commence remedial concrete work in Garage 8.

7. Replace unsafe office trailers for the Power Plant and Construction Department.

In April 2022, we refinanced our HUD insured mortgage with Wells Fargo. This transaction provided \$124 million in proceeds that is available to pay for these ongoing capital projects and others identified in a Physical Needs Assessment over the next 10 years.

Projects that will be commenced next include:

Modernization of all garage elevators, façade restoration work of the townhouse units, installation of EV chargers in our garages, cement restoration at Einstein Mall and installation of a fire alarm system at the Dreiser Mall.

Operations

We also continued to make improvements to the daily operations of the community. Some highlights include:

- In late 2020, we completed the renovation of the 35 laundry rooms throughout the complex and increased our annual revenue by \$507,000, in addition to a \$750,000 payment we received upon signing the new agreement.

- We completed the installation of copper/silver ionization systems in every residential building that prevents the creation of legionella bacteria in the domestic hot water system.

- We completed the installation of new smoke detectors and CO2 detectors in every apartment. During the installation, we also gave the occupants a fire safety lecture and checked to ensure that the required fire safety plan was installed on the back of the apartment entrance door and that the door is self-closing.

- We invested in new floor cleaning equipment for the Janitorial Department that reduced the time for completing this work, thus increasing the productivity of the staff and allowing us to reduce the number of employees needed for this department.

- We continued to make physical improvements to our IT infrastructure that included: replacement of core switches in every building (which allows connectivity of computers, phones and cameras back to our main data center); replacement of all firewalls at multiple locations; core servers were added in the data center; replacement of obsolete physical towers and thin client servers at employees' desks with new

virtual server technology, which increased speed, performance and reliability while reducing overall cost; installation of a second UPS was installed in the data center to run alongside the main UPS providing a redundant power source in case of a failure in the primary UPS; the fire suppression system was replaced in the data center to be compliant with the current fire codes; a disaster recovery site was built that replicates the main datacenter.

- Software enhancements included: Installation of advanced malware and ransomware protection; we deployed multi-factor authentication for all employee email accounts; enabled DDoS attack protection on our internet pipeline serving the entire corporate network to prevent a denial-of-service attack and added Proofpoint protection to our email servers which prevents phishing and spoofing emails and other malicious viruses and attacks.

- We have continued to optimize the equipment at the Power Plant to improve reliability and increase the annual revenue we generate from monthly sales of excess power to Con Edison, participation in the summer Demand Response Program and sales to our commercial tenants.

- We conducted the required LL 87 Energy Audit and Retro-commissioning Report and are completing the recommended work, including pipe insulation and roof fan repairs.

- We are negotiating with Verizon for the installation of FIOS in all residential buildings, thus bringing an alternative provider of internet and TV services to the residents.

- We created a small park area in Section 5 using in-house staff that provides a relaxing space along the Hutchinson River for residents. We received a \$500,000 federal grant through Congressman Bowman's office to begin work for a similar space along the waterfront on Co-op City Blvd.

Future Challenges

Co-op City is now over 50 years old. It is large and its physical plant needs continuous maintenance and improvement.

Our Capital Program over the past six (6) years, since Douglas Elliman became the property manager, has improved critical elements of the infrastructure that will benefit the community for many years. Besides the components that have already been identified for improvement, there will be other significant challenges to be confronted by future Boards, Management staff and you, the stakeholders.

The most important challenge is our convector system and what should be done to either improve or replace it. The convector system provides both the heating and central air conditioning to the community. There are 75,000 convectors. The Power Plant sends tempered water to them; chilled in the summer, heated in the winter; through our underground distribution system. These units are original equipment. They have been a problem for years. We project spending \$1.3 million this fiscal year in ordinary repairs of the units. However, they cause even a larger expense during the summer when we get several thousand cases of water backing up onto the floors of apartments because the condensate lines become clogged. This damages floors, which often need to be replaced, while we are also required to use certified asbestos removal workers and conduct air monitoring for asbestos during the work. This alone costs us over \$15 million per year for labor, materials and environmental remediation.

One would think, well, why do they not just replace the system? Besides this costing hundreds of millions to accomplish, climate change and the governmental response to this issue has made this a difficult question to answer. In the past few years, climate change legislation has been enacted at all levels of government that significantly affects how we deal

with the convectors, but also will have a substantial financial impact on the community in other ways.

The New York State Climate Act seeks to eliminate the use of fossil fuels by 2050. New York City's LL 97 will impose monetary fines on buildings containing over 25,000 sq. ft. for failure to meet designated emissions standards. Fortunately for Co-op City and other Mitchell-Lamas, those LL 97 fines will not be imposed until 2035. All other buildings are facing them as early as 2024.

Because our Power Plant produces almost the entire heating, cooling and electrical needs for the community, using primarily natural gas, the State law would make the facility obsolete within 25 years, unless an alternative fuel such as hydrogen becomes commercially feasible. Our convector system also becomes obsolete as it is connected to the Power Plant. The current prevailing wisdom is to convert the HVAC system to electric heat pump technology.

If we are required to power the system with electricity, it will have to be purchased from Con Edison at much greater cost to the residents than what we produce it for now. There is no current technology that would allow us to replace our entire electrical needs with onsite generation. So what do we do to repair or replace the aged units we have now? In addition, while we try to figure this out, how do we also finance the installation of EV chargers for all 11,000 parking spaces in our garages in anticipation of gasoline-powered autos becoming obsolete? Also, our residents use gas stoves. Every resident will need to purchase an electric stove. If we have to use electricity for the heating, cooling and cooking in every apartment, this will only be possible with the installation of additional wiring and circuits to increase the transmission and load capacity in every structure.

These looming issues will be the single most important challenge for the community that will have an impact on our ability to maintain the affordability of the complex, but it is not the only one.

In the last several years, both the New York City Council and the State Legislature have enacted laws that increase the costs of managing residential real estate for all property owners. These unfunded mandates have already increased expenses for Co-op City and will continue to do so in the future.

The most expensive of these mandates is LL 11 requiring façade inspections every five (5) years and the remediation of any deficiencies identified. While this has been a requirement for 40 years, what has changed over this time is the additional requirements for the inspections and work that raises the cost of compliance seemingly with every cycle. The most recent changes were enacted by the City in 2020 that will increase just the inspection costs alone from an average of \$35,000 per building to approximately \$150,000 when we again must file our reports in 2027 for Section 5 of the complex and 2029 for the remainder of our buildings. One of the newer mandates is LL 152 requiring inspection of the gas distribution system every 4 years in each building by a licensed plumber specially certified to do gas inspections. We had to comply with this in 2020 and will have to do it again in 2024. It cost us \$400,000.

Recently, the City Council enacted LL 126, which requires inspections of all garages every six (6) years and repair of any noted conditions. Our compliance period is in 2026-27. We are trying to get ahead of this law by doing concrete repairs to the garages before then as part of the capital program.

Other legislation enacted in the last few years have increased our costs for mold remediation, installation of smoke and CO2 detectors in apartments, installation and maintenance of required fire safety signage and elevator inspections.

Additionally, the State Legislature enacted a law that eliminated our ability to collect late and legal fees from non-paying shareholders in Housing Court. This not only eliminated a tool that ensured prompt payment but the revenue we collected from these fees was worth over \$1.5 million. The initial law passed in 2019 applied to all rentals and co-ops. An amendment enacted in 2021, exempted most co-ops except those created pursuant to the Private Housing Finance Law. Why wealthy private co-ops were exempted and not affordable developments that rely on this income makes no sense. All this does is place the burden for this lost revenue on the backs of shareholders who comply with their occupancy agreement. We will once again be working with our elected officials to get a similar exemption and would hope that HCR would be supportive of this effort.

Conclusion

It is difficult to appreciate the complexity of operating Co-op City. You are usually dealing with smaller properties that may have similar issues as we are having, but the solutions are not as expensive or as challenging to plan, coordinate and execute as we encounter here.

We have accomplished much during my time here thanks to the conscientious efforts of our Executive Management team and the support of the Riverbay Board of Directors, but there is still much more to be done to preserve the development that has the distinction of being a symbol of affordable housing around the world. The path forward will require focused, comprehensive and inclusive discussions with the community, our legislators and stakeholders to ensure Co-op City remains a viable residential option for working families in our City.