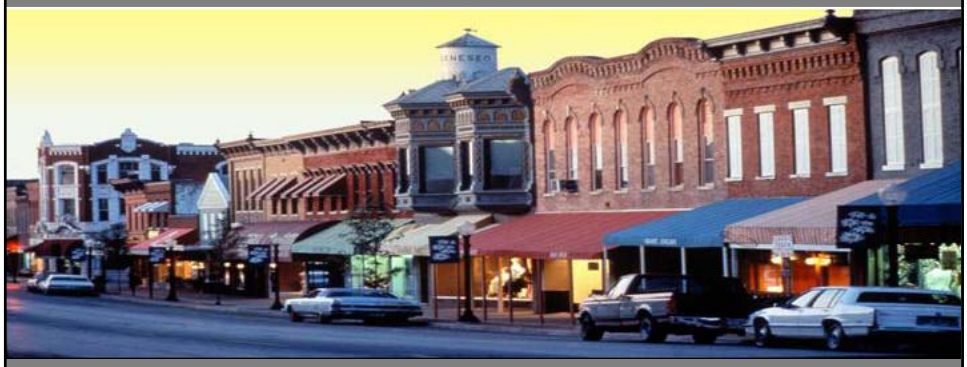

New Markets Tax Credits and Housing

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Common Misunderstandings About New Markets Tax Credits

- Commercial real estate development is the best use of NMTCs.
- NMTCs cannot be used to finance multifamily housing.
- Using NMTCs in for-sale housing projects is a prescription for recapture.

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Questions to Consider

- Does the business the CDE will be lending to or investing in qualify as a QALICB?
  - Restrictions on residential rental property.
- What concerns are there about NMTC compliance?
  - Reinvestment risk.

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Three Common Ways to Finance Housing with NMTCs

1) "Mixed-use" developments
   - 20% or more commercial revenue
2) Developers of residential rental property
3) For-sale housing

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(1) "Mixed-Use" Developments

- QALICBs must be engaged in the active conduct of a qualified business.
- **Rental** of real estate qualifies only if the property is not depreciable as residential rental property and there are substantial improvements on the property.
- Residential rental property is defined in section 168(e)(2)(A) of the Code as "any building or structure if 80 percent or more of the gross rental income from such building or structure is rental income from dwelling units."

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"Mixed-Use" (cont'd)

- Mixed-Use must have less than 80% of income from rental housing plus 20% or more of income from:
  - Office space
  - Retail
  - Other commercial space

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(2) NMTCs Financing Housing Developers

- Developers of housing may qualify as QALICBs
- Must ensure all QALICB tests are met, including:
  - Tangible property test
  - Gross income test
  - Employee Test
- Beware of developers who own the property
- Reinvestment risk

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(3) NMTCs and For-Sale Housing

- QALICBs can include developers of for-sale housing
- No requirements for low-income residents (see next slide)
- Concerns include reinvestment risk
- Better suited for phased projects where sales proceeds can be recycled into subsequent phase of development.

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NMTCs and For-Sale Housing (cont'd)

- Exception re: affordability/low-income residents:
  - If (1) Allocatee's activities are directed to developing or rehabilitating rental or for-sale housing, and (2) Allocatee committed to providing at least 20% of developed units as affordable housing units (i.e., affordable to persons with income less than 80% of AMI), then Allocatee may held to this minimum standard in the Allocation Agreement.

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More Information?

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Telesis Corporation
New Markets Tax Credits
And
For Sale Housing

Telesis Corporation

- Telesis Corporation plans, finances and builds urban communities that are affordable, beautiful, and safe.
- Community Development and Public/Private Partnerships for 25 years
- Master Planner and Developer
- National Footprint
- HOPE VI, LIHTC, HTC, NMTC, TE Bonds, 108, Brownfields, etc.
- $50 MM HTC/NMTC mixed-use project in Memphis with ESIC and NDC under construction now

Telesis CDE Corporation

- Round 3 Allocatee; $60 Million award
- Can do related party deals
- Round 6 applicant
- Created to further the mission of Telesis Corporation
- Focus on for-sale housing

CDE For-Sale Investments to Date

- Four for-sale QLICIs funded to date
- All land acquisition predevelopment loans with "A" and "B" structures
- Minimum 20% affordability
- Leverage "A" loans at 65% LTV
- NMTC equity funds used for"B" loans
- 18 month loan terms
- All "but for" financings

Benefits to developers and projects:

- "B" loans (NMTC equity) provide risk capital where others will not go; truly "but for" investments
- "B" loans lower first mortgage to levels acceptable in today's market
- Also provides capital at a price that is affordable for project feasibility in challenging locations
- Reduced cost of capital creates room for affordability and "green" costs

Benefits to communities:

- Most of the investment typically stays local – construction materials and labor
- Homeownership typically produces positive local long-term economic and social benefits
- Construction jobs are often great entry level jobs for low income persons
- Projects are short term, allowing funds to be rolled over once or twice over 7 years; this doubles or triples community impact

For-Sale QLICI issues, generally:

- Leverage debt interest clock never stops ticking
- Watch NQFP / "substantially all" like a hawk
- Administration of affordability requirements long term

Parkside Townhomes

- Anacostia, Washington, DC
- 118 townhouses, 20% affordable
- 1st phase of a large multi-phase project
- Will set new market standards; foundation for future phases
- Continuation of 20 year revitalization effort
- NMTC Benefits:
  - Other lenders unwilling to pioneer
  - Reduced lending costs supports affordability and green features

Parkside, Washington, DC

315 H Street: Washington DC

- 64 condominiums, 20% affordable
- Transit-oriented development 2 blocks from Union Station
- Part of Washington DC Great Streets Initiative
- Benefits:
  - Other lenders unwilling to pioneer
  - Reduced cost enables affordability and green features

SD Megablock: San Diego, CA

- 525 units, 20% workforce housing
- 315 for sale; 210 rental
- Office, retail and parking
- Benefits:
  Other lenders unwilling to pioneer

Jefferson Plaza: Memphis, TN

- 80 condominiums, 20% affordable
- Condominium market no longer strong enough
- Sale of property for adaptive reuse as a hotel now in process
- QLICI will need to be redeployed
- Benefits of NMTCs:
  Private loan capital not available

Jefferson Plaza:
Northwest Corner

Housing International Gulf Coast: Reserve, LA

- Manufacturer of panelized products made from recycled steel for use in housing construction
- Wall panels to varying degrees of finish; roof and floor trusses; knee walls
- Intended to help solve labor shortage problem post-Katrina
- Penetrating residential construction trade difficult
- Targeted population QALICB
- Benefits of NMTCs:
  Private loan capital not available

HIGC Arabella Site

Issues ahead for existing loans:

- Will projects close construction financing on schedule?
- Will additional interest reserves need to be funded?
- Where is the second generation of projects?

Virchow Krause & company

NH & RA
NMTC and Housing

Summer Institute
Santa Fe, New Mexico
July 23-26, 2008

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NMTC and Housing

- The common myth is that NMTC cannot be used to fund housing –
  - This is not true
    - It can fund projects that are
      - Mixed Use in nature
      - For-Sale property
      - Developer focused fundings

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Mixed-Use Properties

- In funding mixed-use properties
  - Significant levels of impact can be achieved
    - By providing for multiple types of impact
      - Achieving blends of targeted incomes in the housing units
      - Creating live/work environments
      - Redeveloping blighted urban core areas
      - Anchoring cornerstone properties in distressed neighborhoods

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Mixed-Use Properties

- Risks exist that should be considered and mitigated in the funding process
  - Recapture elements related to the percentage of residential rental income
  - Revolving principal requirements on for-sale components
  - Issues related to certain types of subsidies that may be used in financing the development as a whole
  - Timing related to drawing the proceeds down

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Case Study

Syndicate Building, St. Louis, MO

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Syndicate Building, Saint Louis, MO

- The property includes all of the risk elements mentioned prior
  - As this historic property has
    - For-Sale Condominiums
    - Market Rate Rental Units
    - Retail and Commercial Office Space
    - Affordable Rental Units

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Syndicate Building

- Financing sources included:
  - TIF proceeds
  - Brownfield credits
  - Federal and State Historic Credits
  - NMTC proceeds
  - Developer equity
  - Conventional debt
  - LIHTC funding

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Making the Funding Decision

- Stage One
  - Compliance with NMTC location requirements
    - Additional elements of distress
- Community Impact
  - Estimated level of community impact
    - Based on community involvement
    - Number of units developed/ affordability
    - Number of jobs (construction and permanent)
    - Additional impact

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Making the Funding Decision

- Basic Feasibility and Compliance
  - Initial compliance with NMTC program
  - But-for test
  - Basic Financial Viability
  - Readiness to Proceed

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Post-Closure Elements

- Substantially all testing
  - Draw down of principal on a timely basis
- Commercial rental income testing
- Placement of for-sale principal
- Actual community impact analysis

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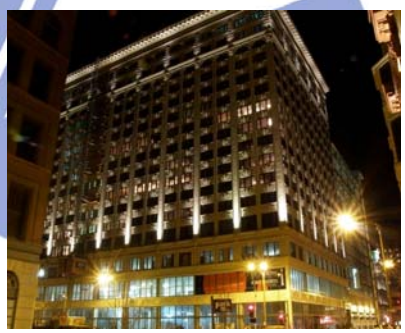
Syndicate Building



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Mixed-Use Properties

Thank you for your interest in serving our Nation's communities…

If you have any questions please feel free to contact me at:

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608 240 2456

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- **Using NMTCs to stimulate housing development for low income displaced families**
- **NMTC subsidy is deployed in support of small developers**
- **NMTC funds will be recycled over the seven year compliance period**

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Developed by Cypress Realty Partners

- 15 units: 100% affordable at 80% of median income
- **Katrina Cottage design**
- **Development area:**
  - **40% of residents below poverty level**
  - **49% of AMI**
- **Financing rejected by local, national and CDE lenders**
- Pilot program for small scale housing development
- Additional funds available for closing cost assistance

10

- **NMTCs used to support high leverage, flexible debt for acquisition, pre-development and development funding**

Benefits of financing:

- **Connected small developer with institutional capital**
  - **Developer lacked access to equity and debt**
- **Capacity and experience building with local developers**
- **Leveraged a local company's knowledge of community needs and organizations**

11


DEAD
END


DEAD
END