DAVID LETTERMAN'S LIGHTNING ROUND
BIG TOP FOUR DEVELOPMENTS ON TAX EXEMPT BONDS

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Presented by:

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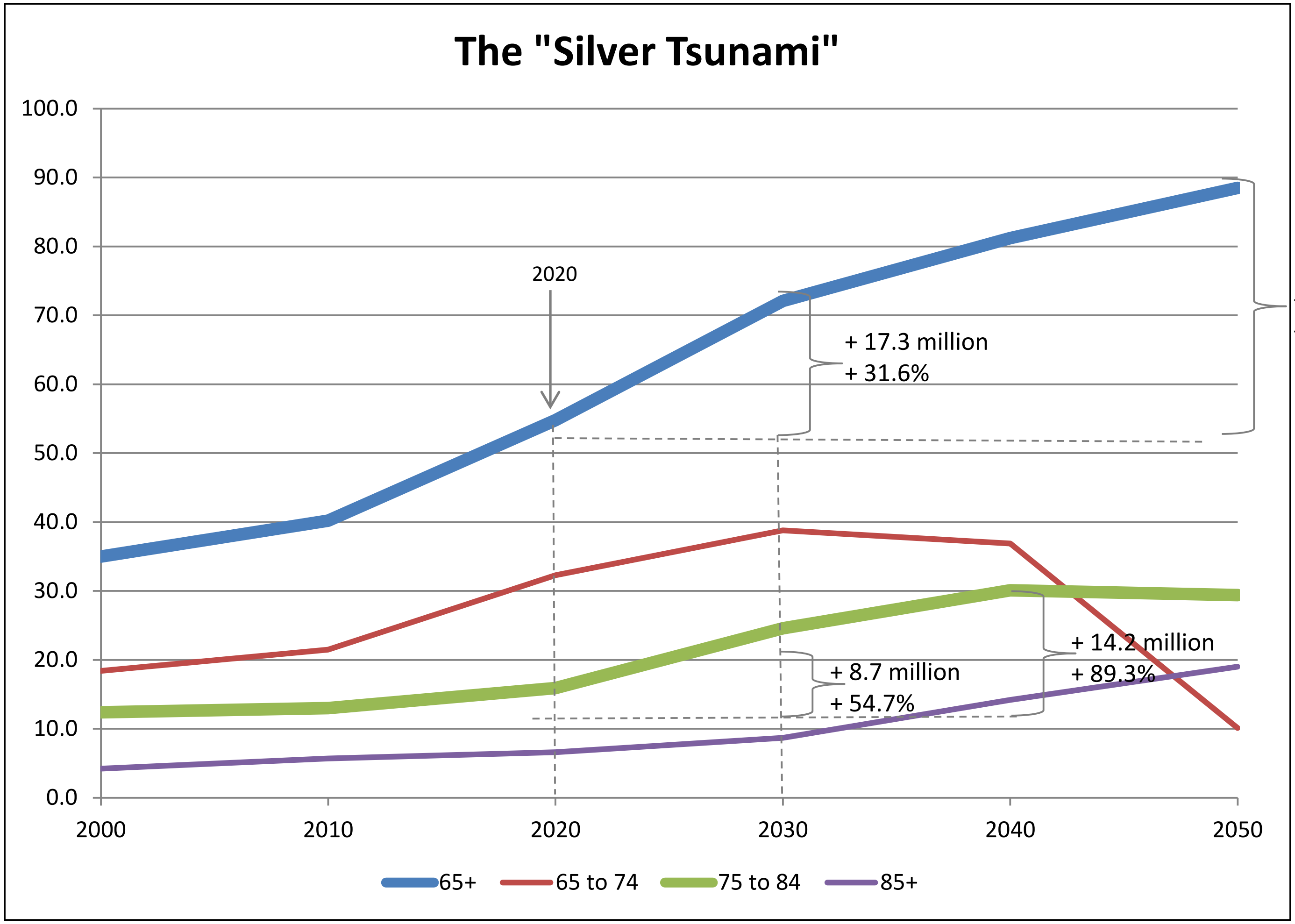
1. RECENT IRS PRONOUNCEMENTS CAST CLOUD OVER ALLOCATING UNITS TO VETERANS

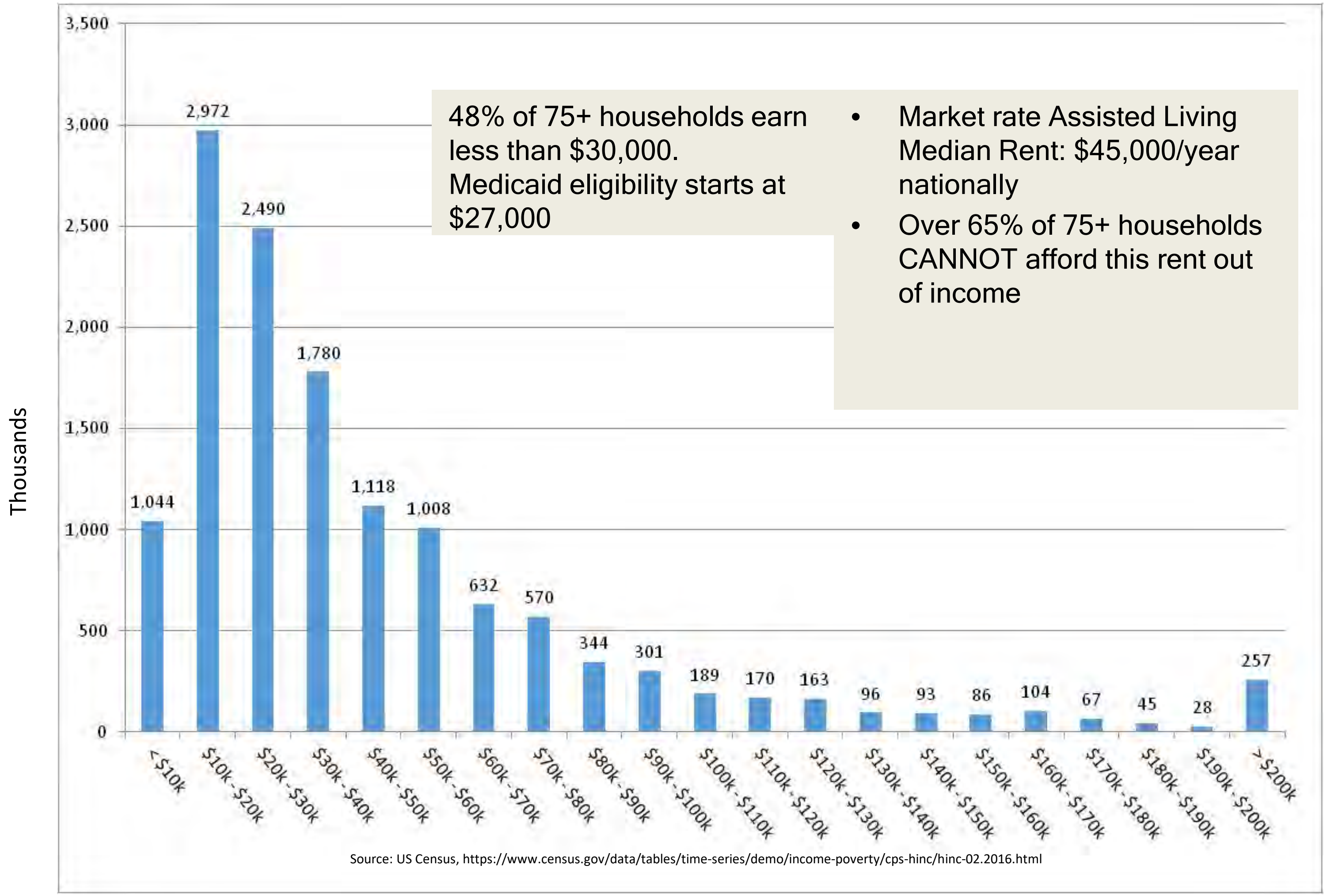
- A recent announcement by the **IRS questions whether setting aside units for veterans**, as a number of projects now do, **is consistent with** the requirement under Section 142(d) that unit be **available for occupancy by the general public.**
- Section 42(g)(9) of the Code, relating to the LIHTC, treats Group Preferences, including those for veterans, as meeting the public use requirement for purposes of the LIHTC, **but Congress did not address Group Preferences in the Section 142(d) Multifamily Bond provisions.** This fall the Office of Chief Counsel of the **IRS publicly stated that** in the absence of a statutory change, **they could not give comfort** that such a preference satisfies Section 142(d).
- As a result, **almost all bond counsel have put opinions on hold** until this can be fixed.
- **A statutory fix** was proposed in December and has bi-partisanship support. According to **Dave Gasson at Boston Capital**, the fix is included in the pending Cantwell-Hatch legislation, which is closing in on a final review, but he thinks this **will take some time**.
- NABL has urged the IRS to address this in a Field Notice, but the IRS is resisting that approach.
- Stay tuned for further updates. **Everyone hopes this will be fixed this spring or summer.**

2. THE COMING TSUNAMI OF ASSISTED LIVING/MEMORY CARE FINANCINGS – INCREASING USE OF 4% LIHTC; DEFINITION OF "COMPLETE LIVING UNIT"

- We are seeing a **rapidly accelerating interest** in the use of **tax exempt debt to finance assisted living facilities**, **including** those with **memory care facilities**.
- Basic demographic factors will drive a **huge surge in assisted living financings over the next 10-20 years**.
- The **75 to 84 age group** will grow by **870,000 per year**, **or ≈ 55%**, **through 2030**, and by **710,000 per year**, **or ≈ 89%, through 2040**.



- Emerging medical issues and physical limitations combined with low income levels and limited net worth will **force many 75-85 year old seniors into an affordable assisted living alternative.**



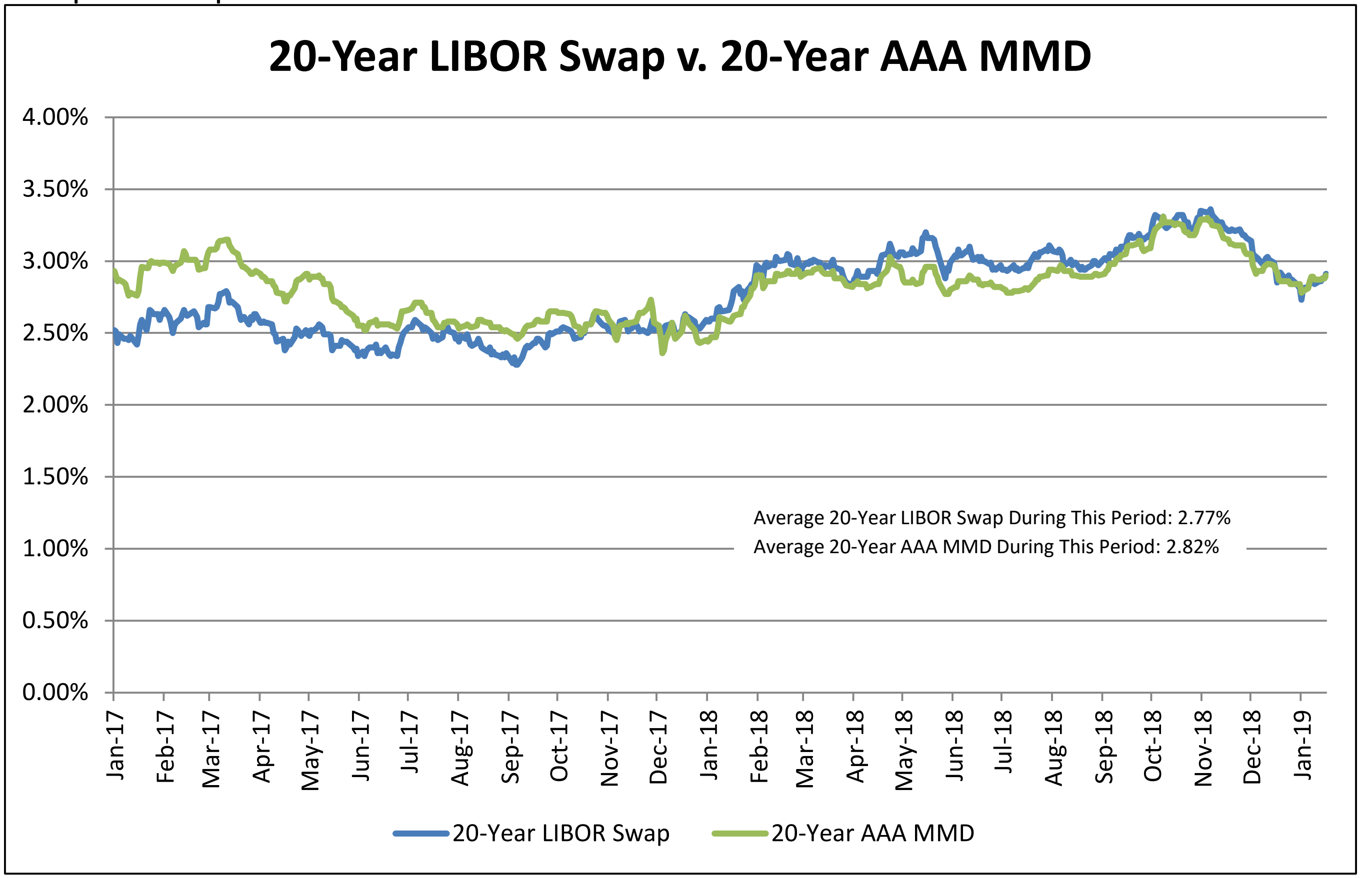
- A rapidly increasing number of assisted living projects are now financed with **tax exempt bonds under Section 142(d)**, and there are **now several major syndicators who will buy the 4% LIHTC** on these financings where an **experienced operator** is on board.
- For **memory care units** included in some of these facilities, there is a question of **whether the kitchens can be configured to meet the "complete living unit" standards** of Section 142(d).
  - Some bond counsel will allow a **half refrigerator, microwave and sink, with the microwave activated only when supervision is present.**
  - Some **assistance in taking medications, etc., is permitted**, including by nurses, but **one cannot have 24/7 licensed nursing care** or other arrangements which would constitute **"continual or frequent nursing, medical, or psychiatric care"** that would disqualify units from Section 142(d) financing (and 4% LIHTC).

3. FHA AND RD FINANCINGS AND SHORT TERM CASH BACKED TAX EXMPT BONDS – MR. LETTERMAN HAS GOOD NEWS AND BAD NEWS

- **Good News:**
  - **HUD affordable volume continues to grow – up $500 million or 18.5%** in **FY 18** v. FY 17 – $3.2 billion v. $2.7 billion.
  - HUD introducing a **new §221(d)(4) Pilot program** to speed loan underwriting.
  - **For West Coast developers, no negative arbitrage** on short term cash backed bonds. **All** of the **West Coast bond counsel firms will now give a clean "reallocation opinion" permitting investment in a fixed portfolio of U.S. Treasuries**, which now yield 40-50 basis points more than bond coupons. Only handful of East Coast bond counsel firms are not on board. **If in doubt, ask before selecting issuer** and applying for bond volume. **Can be $100,000's of losses** if no reallocation opinion on an FHA §221(d)(4) or comparable RD deal.
- **Bad News:**
  - The GNMA buy side is scared of rising rates – **GNMA spreads have risen** and **all-in borrowing rates now closer to those on other executions** – **4.35%** (223(f)) **to 4.65%** (221(d)(4)).

4. PUBLICLY OFFERED TAX EXEMPT BONDS, INCLUDING FANNIE MAE M.TEBS, CONTINUE TO GAIN MOMENTUM

- The following chart shows the relationship over the **past two years** of the **20-year LIBOR swap rate**, a widely used index of highly rated taxable rates, to the **20-year MMD** – the most widely used index for highly rated publicly offered 20-year tax exempt municipal bonds:



- As can be seen above, **two years ago** at the beginning of 2017, the **taxable 20-year LIBOR swap rate** was about **40 basis points lower than the 20-year MMD** (LIBOR at 2.50% versus the MMD at 2.90%); **today they are virtually the same**, at about 2.90%.
- If rates continue to rise and this trend continues, we expect to see an **increasing use of publicly offered tax exempt bonds** in affordable multifamily rental housing financings.

FANNIE MAE M.TEBS CONTINUE TO GAIN MOMENTUM

- M.TEBs bond coupons are **still 70 to 80 bps over the 10-year** U.S. Treasury.
- **All-in borrowing rates of 4.50% to 4.60%.**
- **"Forwards" M.TEBs** structure for new construction/sub rehab entails about **2.0 to 2.5% of negative arbitrage.**
- **But, having two sets of debt outstanding** during the construction period on a "Forwards" M.TEB **can increase tax credit basis and thus 4% LIHTC syndication proceeds. This almost offsets the negative arbitrage deposit** required.
- **Net result is – a permanent lending rate equivalent of about 4.70% –** a very competitive rate in the current market when compared to other executions.
- We can now save costs by **combining short term cash backed tax exempt bonds with M.TEBs in one Indenture and OS** where extra tax exempt bonds needed to meet the 50% Test.

SUMMARY OF BORROWING/ UNDERWRITING RATES
PRINCIPAL TAX EXEMPT DEBT PRODUCTS FOR 100% AFFORDABLE PROJECTS

	Estd. Actual All-In Borrowing and Underwriting Rate
1. Bank Private Placement	
-Mod Rehab	**4.10% to 4.50%**
-Sub Rehab/New Cons	
Cons Period	**4.10% to 4.50% Floating**
Perm Period	**4.50% to 5.10%**
2. Freddie Mac "TEL" Program (Mod Rehab, Sub Rehab, New Cons)	**Similar to Bank Private Placements above**
3. Fannie Mae "M.TEBS" Structure – mod rehab	**4.55%**
or "Forwards" (new cons / sub rehab)	**4.70%***
4. Short-Term Cash Backed Tax Exempt Bonds with Taxable Loan Sale	
FHA/ GNMA §223f (Mod Rehab)	**4.35%**
FHA/ GNMA §221(d)(4) (Sub Rehab / New Cons)	**4.65%**
Fannie Mae Mod Rehab	**4.65%**

*Taking into account 2-2.5 years of negative arbitrage during the pre-conversion phase, which is typically almost offset by a bump in tax credit basis and 4% LIHTC proceeds from two sets of construction period debt.