Financing Structures for Affordable Housing Transactions in the current Market

- **Irena Edwards**, Deutsche Bank, 212-250-8749
- **Patrice Mitchell**, Wells Fargo Securities, 212-214-6731
- **Dale Giffey**, Red Capital Group, LLC, 614-857-3162
- **Patricia Marinilli**, Bank of America Merril Lynch, 617-346-0935
- **Kent Neumann**, Tiber Hudson LLC, 202-973-0107
- **Adam Stein**, WinnDevelopment, 617 239-4554

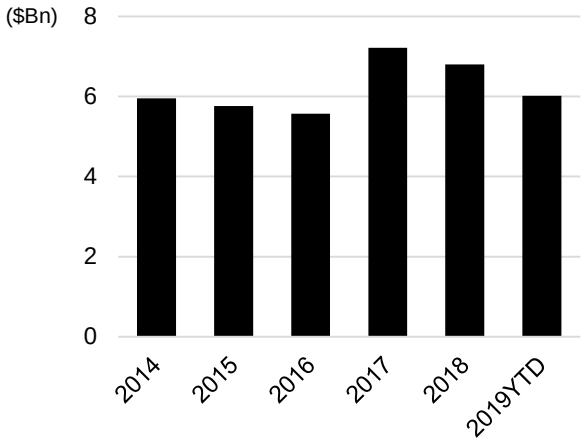
NH&RA | NATIONAL HOUSING & REHABILITATION ASSOCIATION

Fall Developers Forum
October 15-16, 2019

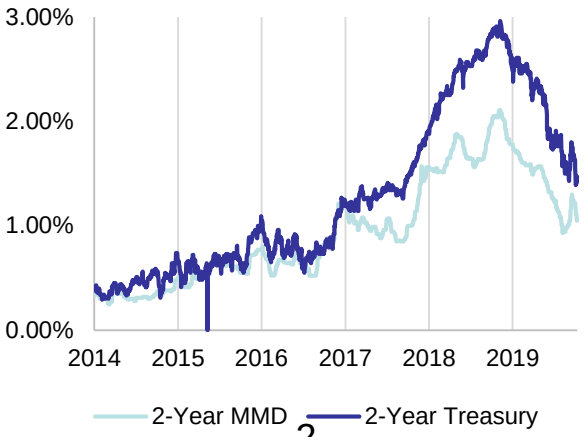
Market Trends for 4% Bond Executions

- Demand for tax-exempt municipal bonds has been high for most of 2019 due to supply and demand dynamics
- 4% bond activity in general continues its upward trend
- Securitization structures have become more widespread
- Increasing investor appetite for unenhanced bond structures
- In general, Interest in affordable housing bonds has grown substantially across a wide variety of investors
- State HFA use of HFA Risk Share product continues to grow
- An increasingly common approach is to pair bank construction loan with Risk Share perm
- Recent rundown in interest rates has decreased positive arbitrage on cash-collateralized bonds; small amount of negative arbitrage possible
- Volume cap is becoming scarce in more jurisdictions
- **Key Takeaway**: developers have more 4% bond executions options available than at any other point in the program's history

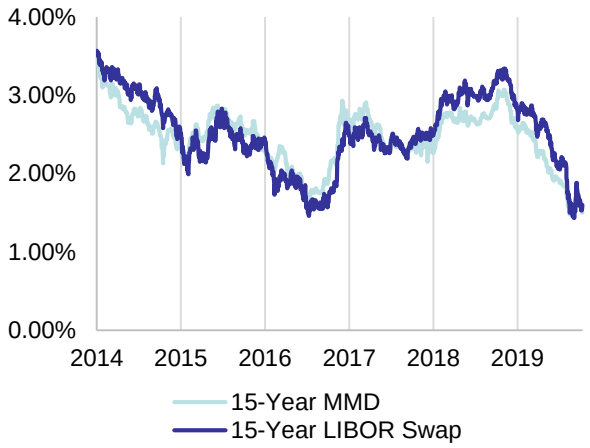
Multifamily Housing
Publicly Offered Bond Issuance Since 2014



2-Year MMD and UST Rates Since 2014

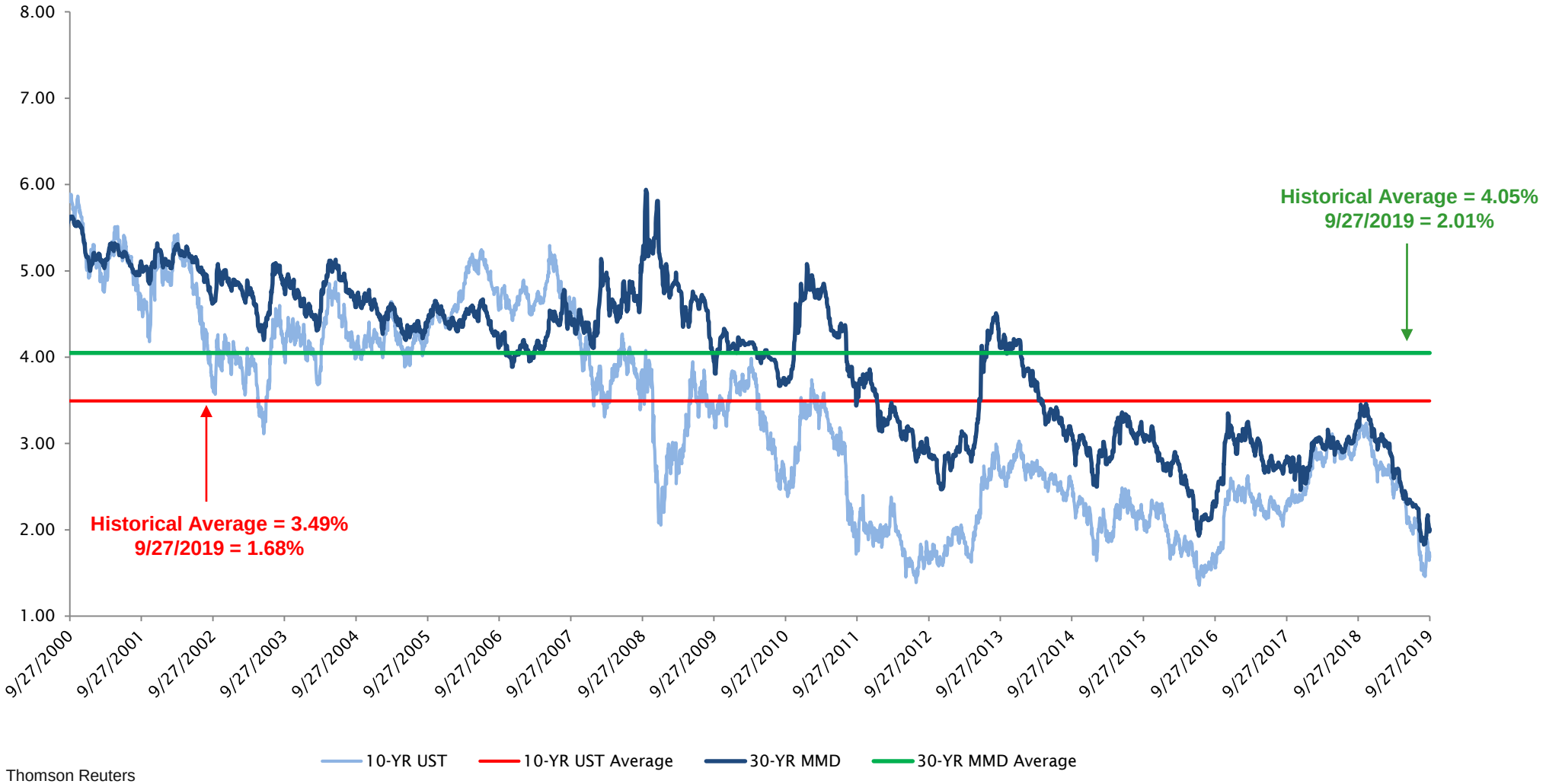


15-Year MMD and LIBOR Swap Rates Since 2014



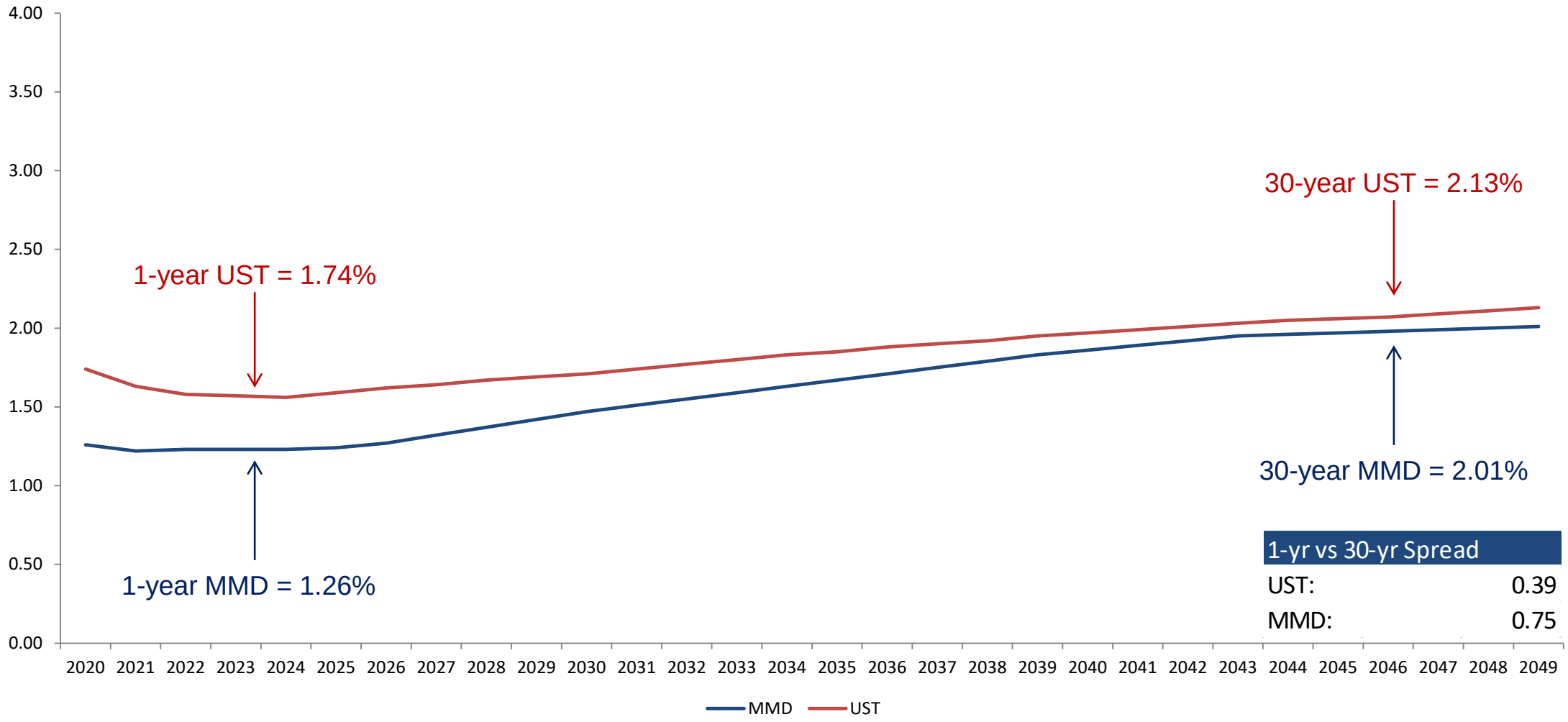
Source: Thomson Reuters SDC, as of 10/10/2019

Long Term Yield Curves (as of 09/27/19)



Source: Bloomberg. Thomson Reuters
Reflects market conditions as of September 27, 2019
Thomson Reuters Municipal Market Data (MMD) AAA curve is a proprietary yield curve that provides the offer-side of AAA rated state general obligation bonds

Historically Flat Yield Curve (as of 09/27/19)



1-yr vs 30-yr Spread	
UST:	0.39
MMD:	0.75

Source: Bloomberg. Thomson Reuters
Reflects market conditions as of September 27, 2019
Thomson Reuters Municipal Market Data (MMD) AAA curve is a proprietary yield curve that provides the offer-side of AAA rated state general obligation bonds

Bond Costs of Issuance – Know Your Options!

Issuer Fees*:	0.10% - 1.50%
Bond Counsel*:	$35,000 - $100,000
Underwriter's / Purchaser Fee:	0.50% - 1.00%
Underwriter's / Purchaser's Counsel:	$30,000 - $50,000
Miscellaneous:	$10,000 - $20,000
Negative Arbitrage*:	0.00% - 0.75%

Tax Exempt Multifamily Housing Financings in the Current Market

- Short Term Cash-Backed Bonds with Taxable Perm Loan
- Tax-Exempt Seller “take back” Bonds (for 50% test)
- Taxable Financing Structures For Future LIHTC Deals
- Private Placement / Forward Commitment TE Bond/Loan Deals (including new Cash Backed Forward Structure)
- Long Term Bond deals with Credit Enhancement (including Fannie M-TEM and 542(c) Risk Share).

Short Term Cash-Backed Bonds with Taxable Perm Loan

- Taxable construction and/or perm loans still available in the current market at historically low rates including:
  - FHA/GNMA (221(d)(4) / 223(f))
  - Rural Development (538 / 515)
  - GSE loans (mod/light in-place rehab)
  - Other (taxable) State and/or Local loan programs

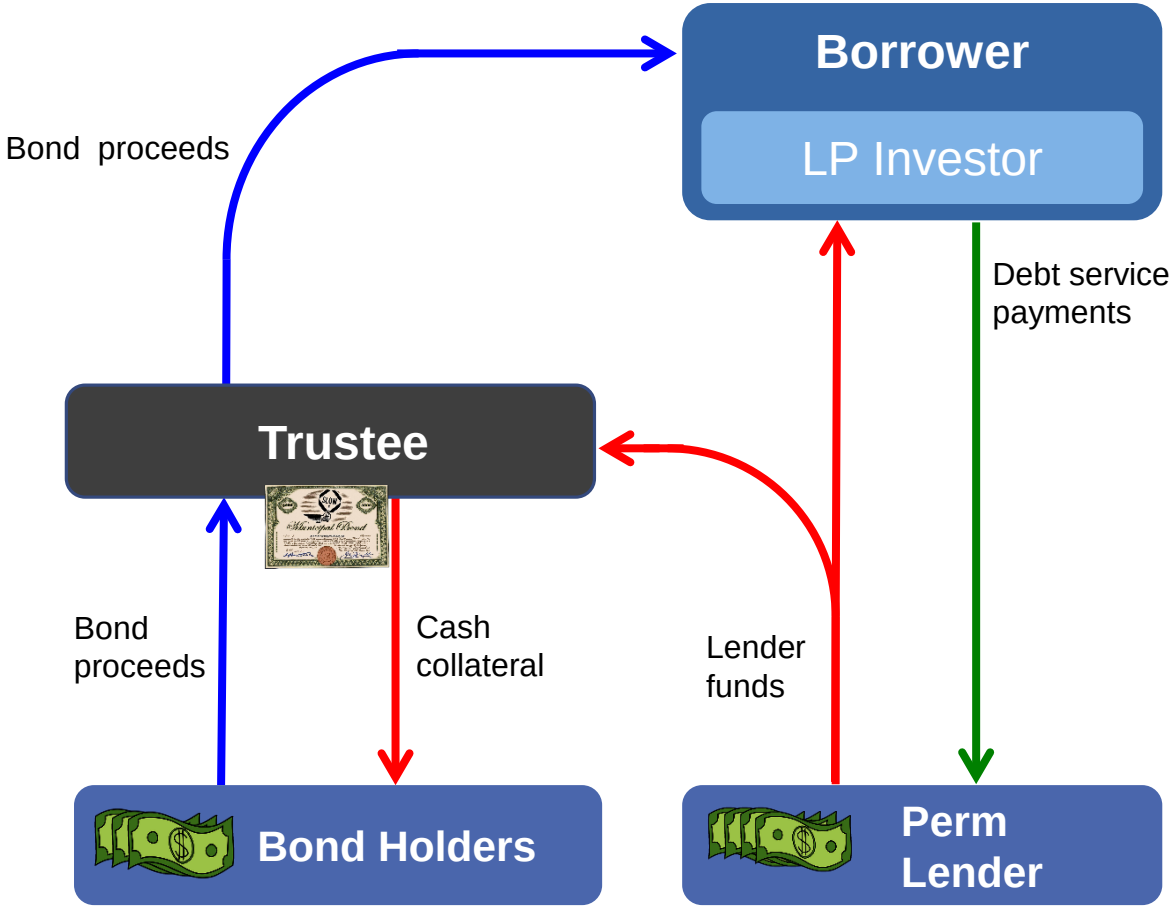
Short Term Cash-Backed Bonds with Taxable Perm Loan

- Favorable Underwriting Terms (vary by product) include:
  - 35 to 40-year amortization
  - Fully amortizing debt / no resizing at conversion (FHA/RD)
  - Non-recourse & integrated construction and perm
  - Davis Bacon wages triggered if federal funds used for sub rehab / new construction deals
  - Most are structured as draw-down loans to avoid neg arb
  - FHA debt qualifies for 10-year hold exemption (for acquisition credits)
  - Historically low mortgage rates still available

4% Low Income Housing Tax Credits: The 50% Test

- Project still need tax exempt bonds to qualify for 4% Low Income Housing Tax Credits
- At least 50% of aggregate basis (including building and land) must be financed with tax exempt bond proceeds
- Provides a significant (~30% or higher) additional source of funds for affordable housing transactions
- Can be used with other “longer term” bond structures to meet 50% test

Short Term Cash Backed Bonds



Short Term Cash Backed Bonds

Bond Amount to meet 50% test < Taxable Loan Amount (see prior slide): No additional collateral needed!

Bond Amount to meet 50% test > Taxable Loan Amount: Need other collateral sources of funds including:

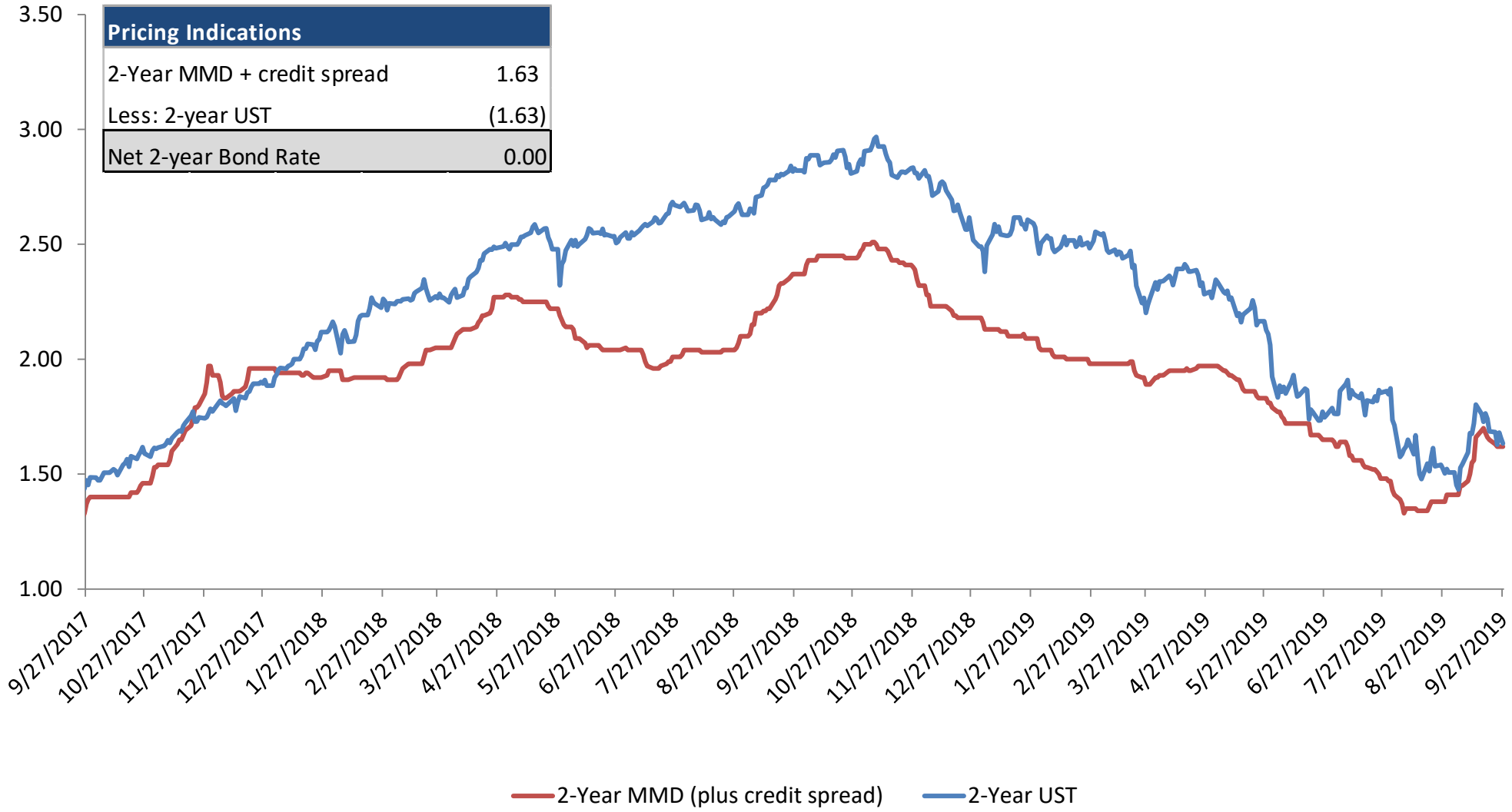
- Subordinate Loan Proceeds
- Seller Note
- Tax Credit Equity

Other Cost Saving Features/Options

Methods to reduce transaction costs and generate more proceeds:

- Pooled financings – multiple projects w/ one aggregate bond issuance
- No long-term bond related fees
- Potential for additional tax credit equity due to increased basis
- No net interest cost on bonds and in some cases, additional investment earnings can be used for other project costs

Short Term Yield Curve (as of 09/27/19)



Pricing Indications	
2-Year MMD + credit spread	1.63
Less: 2-year UST	(1.63)
Net 2-year Bond Rate	0.00

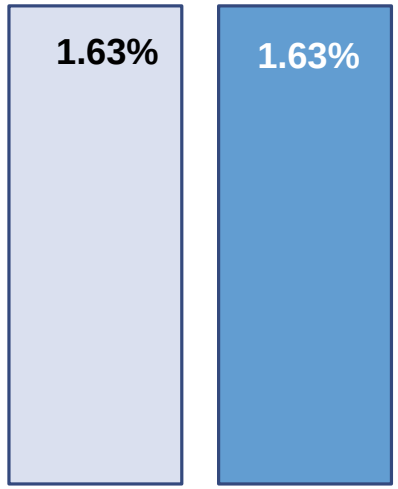
Source: Bloomberg. Thomson Reuters
Reflects market conditions as of September 27, 2019
Thomson Reuters Municipal Market Data (MMD) AAA curve is a proprietary yield curve that provides the offer-side of AAA rated state general obligation bonds

Negative/Positive Arbitrage

Trustee

Treasury Investment

- Cash collateral can be invested in treasury while held with the Trustee



Bond Holders

- Bondholders are receiving (tax exempt) interest while bonds are outstanding

Avg Investment Yield

Bond Rate

Tax Exempt Seller “Take Back” Note & Bonds

- Many 4% preservation deals include seller financing in the form of a subordinate “take-back” note (common in RAD transactions)
- Due to the LIHTC 50% test, tax-exempt bonds in excess of the permanent financing are often required in these deals
- Several ways to address this issue with various bond structures (often with a positive result)

Taxable Financing Structures for future LIHTC Deals

GOALS:

(1) Using taxable longer-term loan to lock in today's rates for future tax credit deals (R2R) and/or

(2) Qualify for exemption to 10-year hold rule (for acquisition credits) using FHA

Taxable Financing Structures for future LIHTC Deals

- **NEW LOAN**: FHA or GSE loan to refinance existing debt or purchase project. Keep rehab to a minimum.

When ready for Bonds/4% Credits

- **Step 1**: **TPA** (transfer of physical asset) process
- **Step 2**: Supplemental loan for additional debt
- **Step 3:** Use short-term tax-exempt bonds to qualify for 4% tax credits

Private Placement / Forward Commitment Tax Exempt Loan / Bond transactions

Popularized over a decade ago in “steep” yield curve environment.

- Draw Down structure to reduce interest cost
- Reduced upfront fees due to fewer participants
- Attractive loan terms and ease of execution

Tax Exempt Bond Direct Purchase Program

Description	National, not location or CRA specific, balance sheet direct purchase of tax-exempt debt for new construction or acq/rehab of 4% LIHTC properties
Additional Uses	Construction debt can bridge tax credit equity and/or other pay-ins
Sizing	• Minimum 1.15x DSC on a 40 year amortization • Maximum 90% LTV • Typically $15mm and above; smaller deals on a case-by-case basis
Interest Type	Fixed
Interest Rate	• Typically, fixed rate determined at closing based on current 17 or 18 yr MMD + spread • Pricing based on term, location, leverage, project and Borrower (inquire for specific pricing)
Loan Term	17 or 18 years; Borrower optional redemption after year 16 or 17; Bondholder optional tender after year 17 or 18
Interest Only Period	2-3 years during construction/rehab, with the potential for 1-3 additional years after stabilization on a case-by-case basis
Amortization	Up to 40 years

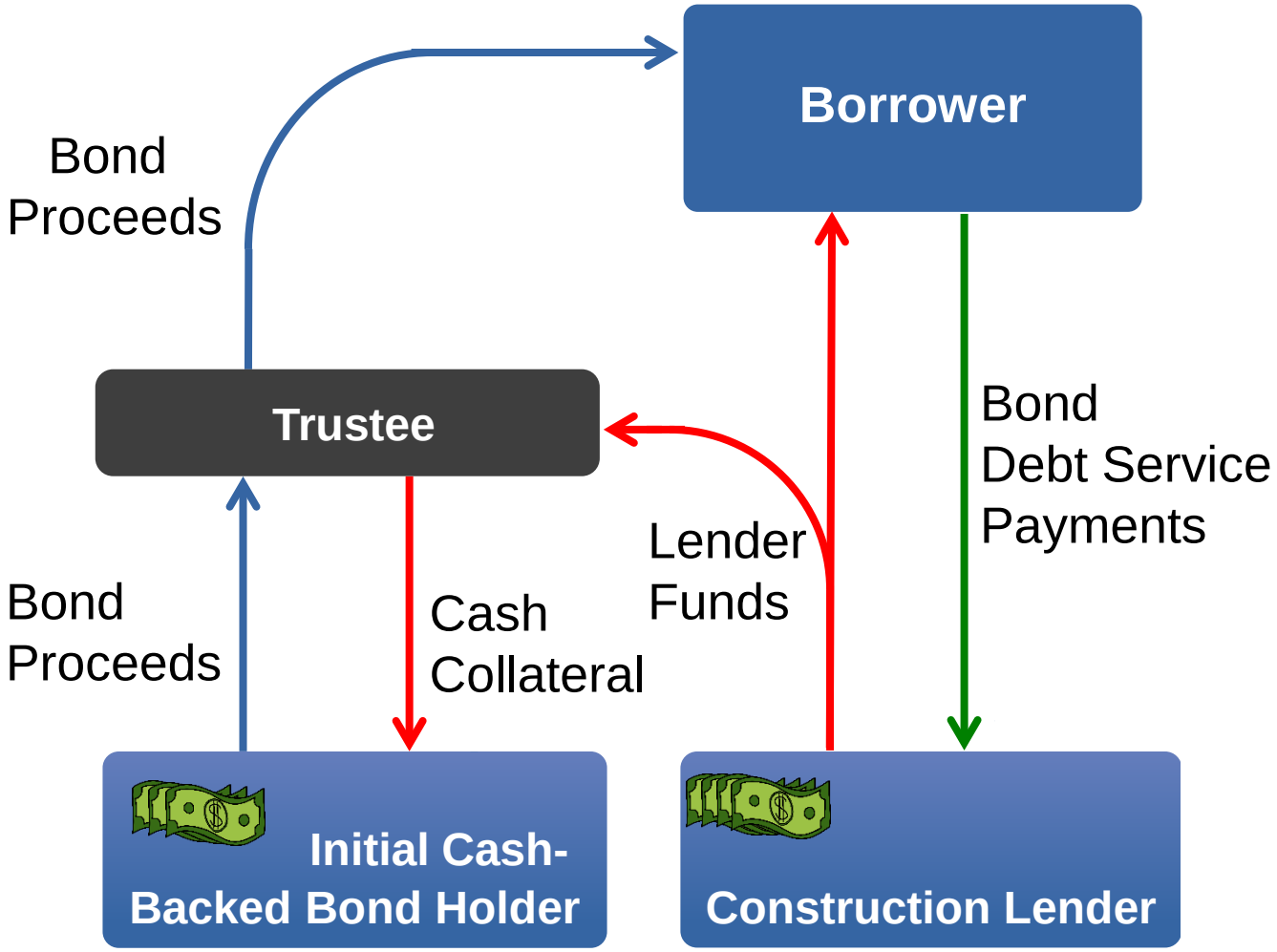
Tax Exempt Bond Direct Purchase Program

Lock-Out Structure	10-15 years from Stabilization Date
Drawdowns	Quarterly draws to limit negative arb during construction
Security / Collateral / Recourse / Guarantees	• First mortgage lien and assignment of rents on the property being developed • Assignment of all construction documents and third party contracts • New construction will require stabilization guaranty from creditworthy guarantor, or a LOC • Full recourse for completion and stabilization • Upon stabilization, non-recourse except typical bad boy acts • Guarantor must have acceptable liquidity/net worth
Origination Fee	Typically between 0.50%-1.50% of Loan Amount
Closing Timeframe	Typically 60-90 days
Due Diligence Scope	Standard due diligence process including the ordering of third party reports
Due Diligence Costs	Borrower covers all customary closing costs and third-party fees

Cash Backed Forward – New Const/Sub Rehab

- New Structure Developed by TIBER HUDSON for New Construction or Substantial Rehabilitation Projects
- Works with any Tax-Exempt Financing that involves a Forward Commitment from a Permanent Lender to Purchase the Tax Exempt Debt at Conversion – including Freddie Mac TEL, Barings, Redstone, Fallbrook and others.
- Takes Advantage of Flat Yield Curve and provides other significate benefits – particularly in Texas.

Cash Backed Forward



Cash Backed Forward

Advantages:

- Potential for positive Earnings During Cash Backed Mode
- Additional Equity (subject to accountant approval)
- Allows Equity Investor to also serve as Construction Lender without certain tax implications
- If Bonds > Perm Loan, allows other funds to be used as collateral (reduced construction loan)
- In Texas, significantly reduces interest costs on construction loan due to draw down structure

Disadvantages:

- Additional Costs of Issuance for Cash Backed Bonds
- Construction Loan is Taxable (if not already due to relationship of parties)

Long Term Bond deals with Credit Enhancement

Long term bonds (16+ years) sold via underwriter to capital market backed by credit enhancement:

- Locks in very low tax-exempt rates resulting in additional loan proceeds
- Low negative arbitrage due to very flat yield curve
- Monthly pass through structure can be used to match taxable MBS market for additional efficiency.
- Used with Fannie Mae MTEB/MTEM and 542 Risk Share

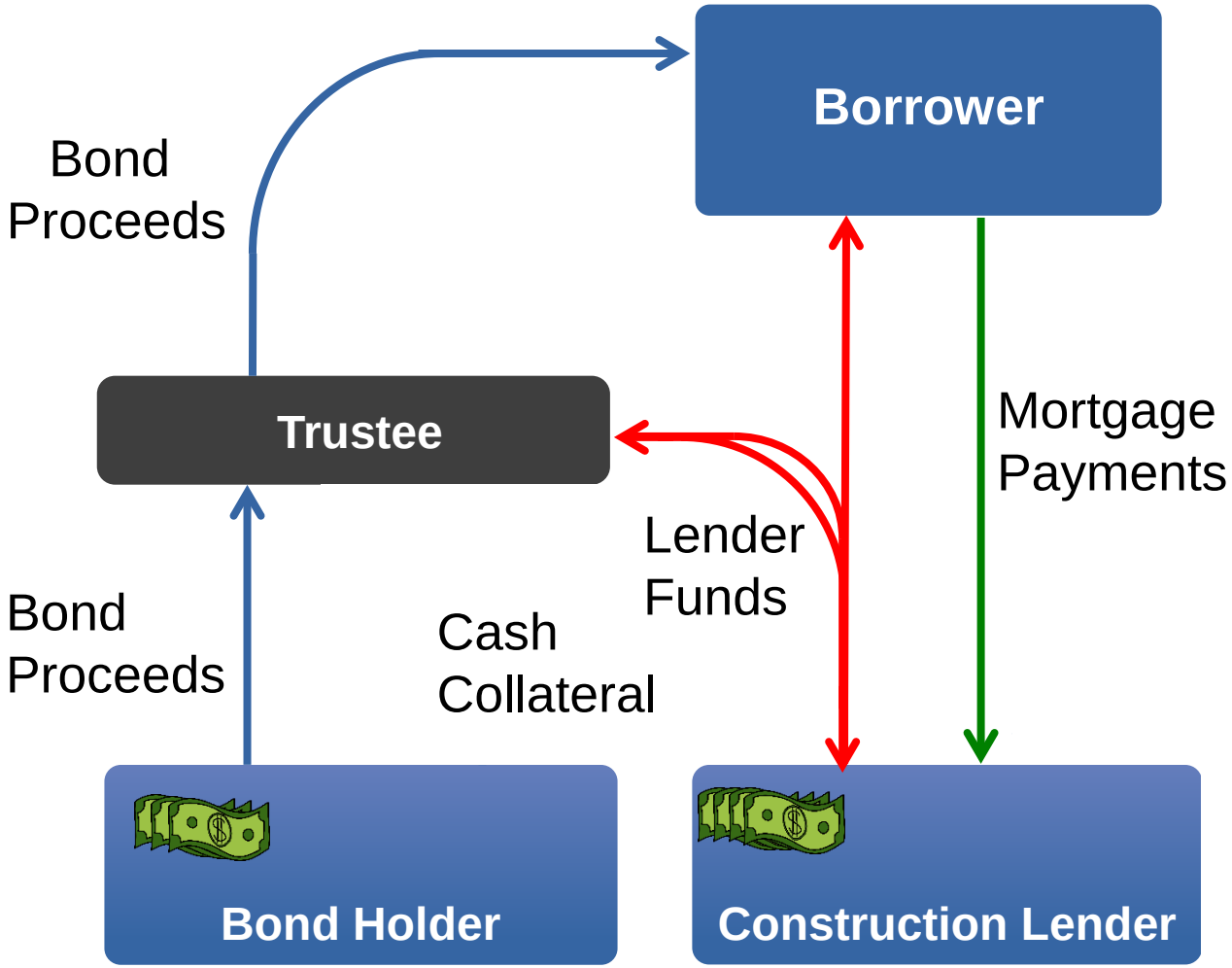
Fannie Mae Forward MTEB/MTEM

- Fannie Mae provides commitment
- Taxable Construction Lender required before conversion (new construction/sub rehab)
- Bond initially secured by cash collateral and replaced at conversion with MBS
- Fannie to credit 75 bps for Bond related costs (paid upon conversion)
- Negative Arbitrage prior to conversion (~0.75% per year)
- Low Mortgage Rates Often results in additional net loan proceeds despite some additional upfront costs

Fannie Mae MTEB/MTEM

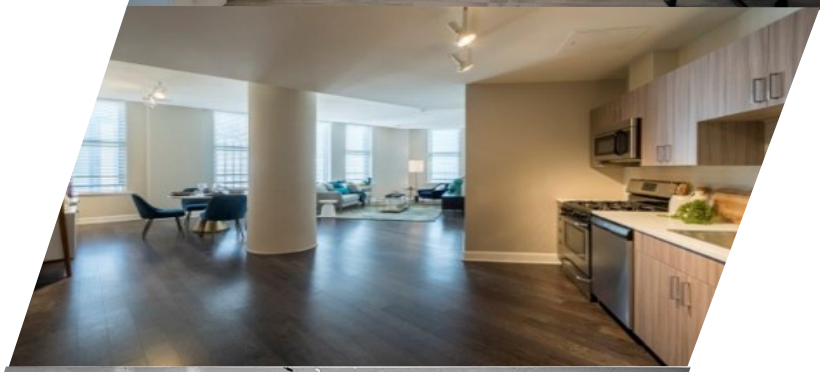
- Flexible interest only period; 35-year amort (40 for some deals)
- Hybrid structure (immediate/forward) available for some mod/sub rehab deals
- Can be structured with Taxable or Tax Exempt Earn-Out
- Total Bonds issued in the amount equal to the greater of:
  - Permanent Loan – (no other series of tax-exempt Bonds needed)
  - 55% of aggregate basis – (second cash-backed or other series of tax-exempt bonds needed)

Fannie Mae Forward MTEB/MTEM



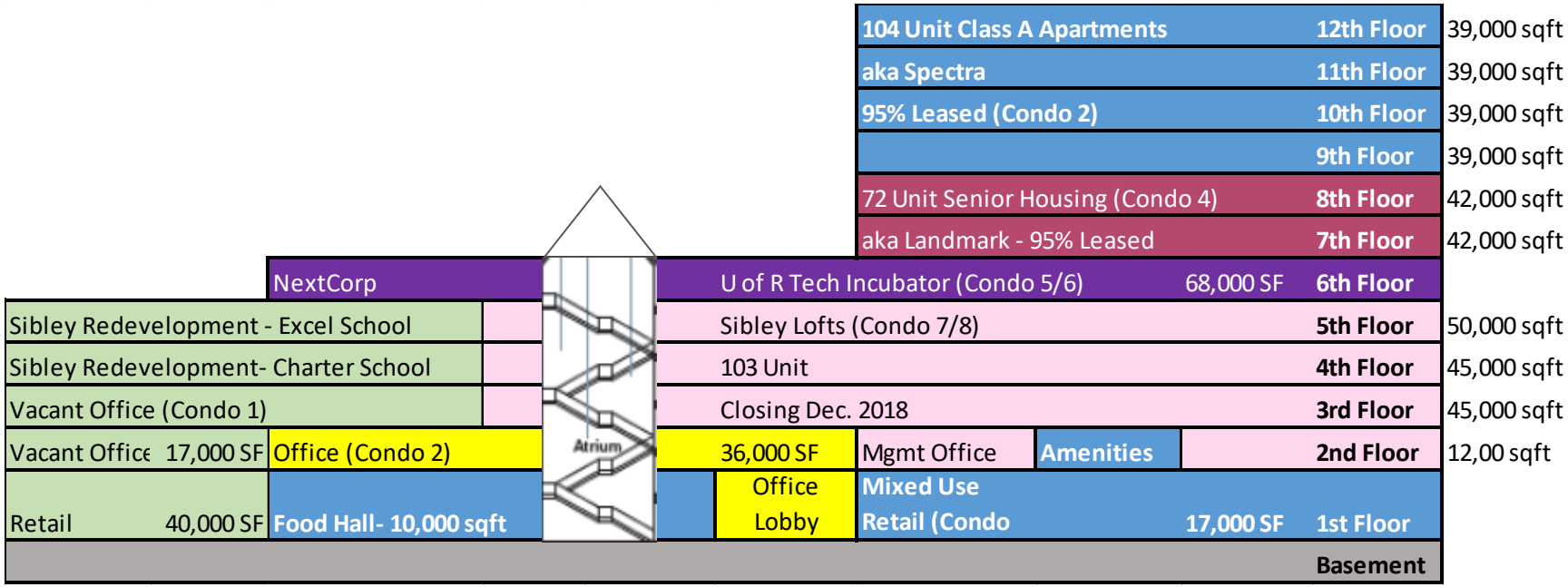
Sibley Lofts- Rochester, NY

- Sibley Building: historic adaptive reuse of former 1.1 million square foot department store into a mixed-income and mixed-use development.
- Condominium structure approved by NY AG's Office.
  - **<u>Sibley Lofts:</u>**
    - Fifth phase of Sibley redevelopment
    - 104 units of affordable and workforce housing
    - 53 LIHTC units and 51 workforce units at 110% AMI
    - Financed with 4% LIHTC, HTCs, City of Rochester funds, Restore NY, and NYHFA subordinate financing
    - 1 investor, 1 perm lender (HFA), separate AFS, reqs, cost centers etc.



WinnCompanies
Development | Residential | Military

Sibley Lofts – Rochester, NY



3 Phases of Residential

- Spectra. 104 unit market rate (blue)
- Landmark. 72 unit senior affordable (red)
- Lofts. 103 unit workforce/affordable (pink)
- Represents 35% of project sq footage

WinnCompanies
Development | Residential | Military

Sibley Lofts- Rochester, NY

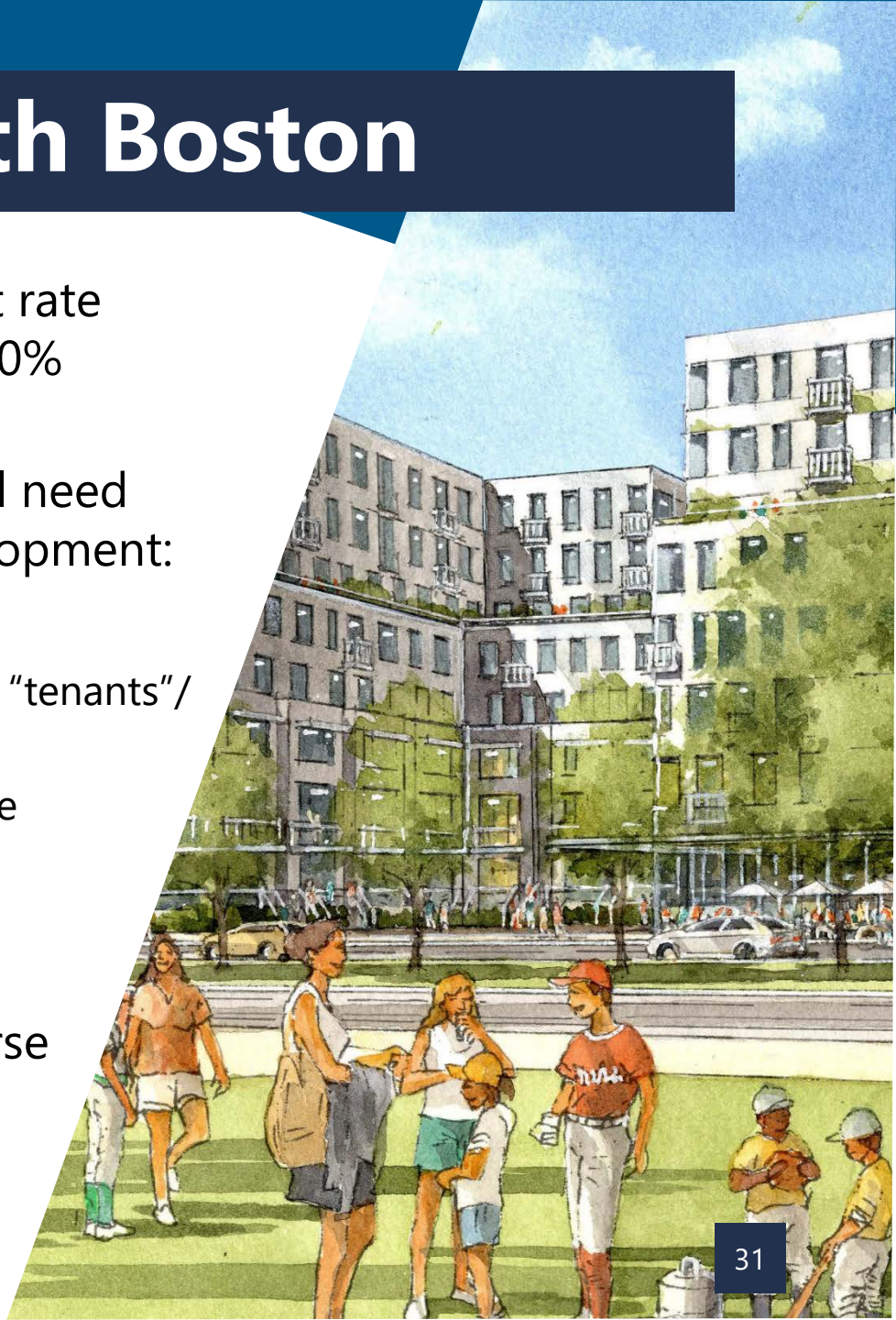
Sibley Building

SIBLEY LOFT CONDO UNIT 7 & 8 - LEVEL 5

- $30.4 million total TDC
- Split deal into two condominiums with limited common elements
- $15.8 million LIHTC deal and $14.6 million workforce deal
- Condos defined unit by unit- equitably dispersed
- Met 50% test only on LIHTC condo unit transaction
- Recycle bonds utilized in workforce deal= saved NYHFA ~$7 million in scarce volume cap resources

Mary Ellen McCormack – South Boston

- Replacement of affordable housing units through market rate unit creation and cross-subsidization in mixed-income, 80% market, 20% affordable buildings.
- Proposed deal structures aimed at minimizing the overall need for volume cap allocated, tax exempt debt in the redevelopment:
- Master Lease Structure:
  - Borrower = Master Landlord with Affordable and Market "tenants"/ co-borrowers. Single loan, one note, one mortgage.
  - The tax-exempt bond proceeds would be allocated to the affordable units on a pro rata basis.
- This structure preserves limited tax-exempt resources. For the first 80/20 building, this structure will save $60MM in TE resources, and over $660MM over the course of the overall redevelopment.



WinnCompanies
Development | Residential | Military

Harbor125 – East Boston

- Two separately financed projects, existing Boston Housing Authority site, sub-divided to accommodate mix of uses:
  - **Harbor125:**
    - 22 affordable rental units with ground floor retail and amenity spaces.
    - 4% LIHTCs, Brownfields, TEB financing from MassHousing, and off-site Inclusionary Development Funds (Lendlease).
    - 99-year ground lease with BHA.
  - **Harborwalk Residences:**
    - 30 mixed-income condominium units.
    - Fee simple purchase of project parcel from BHA.
- Complex allocation of site costs between the projects. Demolition, soil remediation, site improvements (roadway), utilities.

WinnCompanies
Development | Residential | Military