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High Yield Tax-Exempt Issues for Workforce Housing: 501(c)3 and Essential Function Bonds

501(c)(3) Bond Basics

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501(c)(3) Bonds – Financing Overview

- **Non-Profit Tax Exempt Bond Financing**
  - Non-Profits are automatically eligible to use Tax Exempt Bond Financing for their mission as specifically called out in their 501(c)(3) Letter from the IRS and authorized in Section 145 of the IRC
    - Common structure used by non-profit Hospitals, Universities, Healthcare Providers and Affordable Housing providers
    - Cannot be used for space dedicated to non-charitable purposes (i.e., retail or office space leased to outside tenants) with certain other limits on uses (working capital and transaction costs). These so called ‘bad’ costs can be financed with sponsor funds or taxable bonds
    - Verify eligibility for projects based on 501(c)(3) Letter, articles of incorporation, bylaws and form 990
  - No automatic property tax abatement, but many states provide for abatement under defined conditions
  - May contract with private business in several ways, but must avoid “Private Inurement”
  - Dispersed properties can be financed in multiple locations / states by using a Master Trust Indenture Structure
  - Various financing structures are available to provide fixed rate, variable rate or hybrid debt
  - Can accommodate various credit profiles (i.e., both rated and unrated executions are viable)

Source: Internal Revenue Code

501(c)(3) Bond Structuring

Permitted Uses / Transaction Characteristics:

- Real Estate
  - Acquisition – No rehab requirement (if affordability meets the Donnelly rule), proceeds must be spent expeditiously
  - New Construction
- Asset Categories
  - SRO (must follow LIHTC rules)
  - Multifamily
  - Income Qualifying Age Restricted
- Markets: MSA's 250k+ with ~10% minimum rent differential
- Total Individual financing size
  - Minimum: ~$10,000,000
  - Maximum: None
- Income targeting based on IRS Revenue Procedure 96-32, which defines the "Safe Harbor" for affordability as:
  - 20% @ 50% AMI or 40% @ 60% AMI
  - Total of 75% at 80% AMI income restricted. Remainder of units can be market rate or quality for property tax abatement / exemption
- Costs for which the use of Tax Exempt Bond Proceeds is limited:
  - No use for commercial space or space which is unrelated to mission
  - No working capital (broadly defined)
  - Maximum of 2% of proceeds for Costs of Issuance and 3% of Bond Proceeds for "Bad Costs" (i.e., those which are otherwise restricted or non capitalized)

Investment Structure:

- Low cost debt with smaller equity requirement (non-profit)
- Requires strong economic fundamentals of the project or strong backing from a highly creditworthy entity
- Property Tax Abatement not automatic, but may be available based on local rules
- 35 – 40 year amortization
- Potential for Interest Only with amortization based on a proportion of cashflow
- Reserve funds for Debt Service, Capitalized Interest, Capital Replacements and operating needs (funded with equity or 'taxable tail')
- Requires approved 3rd party reports (appraisal, property needs assessment, plan & cost review, etc.)

Benefits:

- Not impacted by LIHTC rules or long application processes
- Bonds are available by right for a non-profit's mission
- Very strong demand for Tax Exempt Investments, especially in California, provides attractive cost of capital and structuring flexibility

Source: Internal Revenue Code

Non-Profit Bond Structure Summary

- Non-profit must be 100% owner
- Not volume cap limited
- Owned by a non-profit but can contract with private developers for services at fair market rates
- IRS Revenue Procedure 96-32 provides safe harbor affordability of (20% of units at 50% AMI or 40% of units at 60% AMI and a total of 75% @ 80% AMI – remaining units may be market rate

Source: Internal Revenue Code

West Virginia Portfolio Acquisition

501(c)(3) Case Study

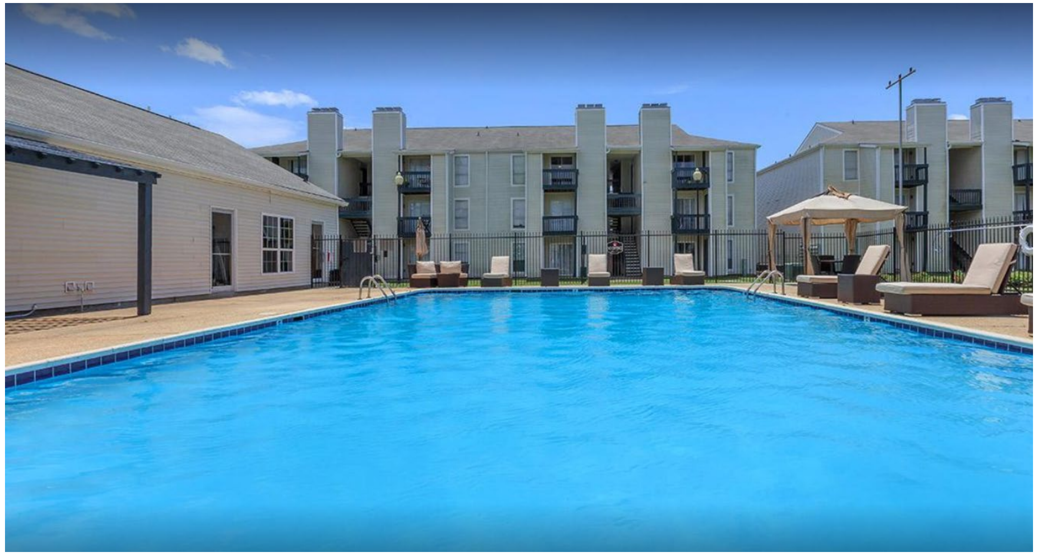
- $62,700,000 acquisition of 23 multifamily properties consisting of 991 units in Charleston, WV area
- The portfolio of properties was acquired and operated by a single investor over a period of approximately 50 years
- A private developer assisted the non-profit sponsor with pre-development financing, due diligence, guarantees and asset management
- $10 million in bond proceeds is funding rehabilitation (including roofs, HVAC, water heaters, plumbing, electric etc.)
- Acquisition and rehabilitation was financed under a single master trust indenture allowing for cross collateralization
- Non-Rated Institutional Bond structure allowed for early partial bond redemption if the borrower intends to pursue a tax exempt bond/ 4% LIHTC execution
- LURA requires 40% of units to serve households at or below 60% of Area Median Income ("AMI") and 35% of units to serve households at or below 80% AMI

Source: Placement Memorandum, Borrower

4 Property Restructure

501(c)(3) Case Study

- $95,005,000 financial restructuring of 4 multifamily properties located in 3 states consisting of 1,105 total units
- Worked with the 3 separate issuers
- Portfolio was financed under a single master trust indenture allowing for cross collateralization which strengthened the credit
- LURA requires 40% of units to serve households at or below 60% of Area Median Income ("AMI") and 35% of units to serve households at or below 80% AMI



Source: Placement Memorandum, Borrower

Highly Experienced Team

Team of Senior Professionals with Deep Housing Expertise and Execution Experience

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Experience
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- Leads Multifamily coverage of West / Midwest
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