Unlocking the Power of New Markets Tax Credits

2016
Agenda

- Goals:
  - Understand the basics of how NMTCs can benefit projects in your community
  - Understand the process for obtaining NMTC Allocation

- Agenda:
  - NMTC Basics
  - Program descriptions and project examples
  - Questions
Panelists

- Kelsey Hamory, LISC
- Elaine DiPietro, Enterprise
- Shirley Boubert, DC Housing Enterprises
NMTC Background

• Financing tool to spur economic investment in low-income communities by providing equity to fill a capital gap

• Created by Congress as part of the Community Renewal Tax Relief Act of 2000

  • Codified in Section 45D of the Internal Revenue Code
  • Administered by the Community Development Financial Institutions (CDFI) Fund of the US Treasury Department
Pearl Foods – Dorchester, MA

Total NMTC Financing - $14,000,000
LISC NMTC Financing - $10,000,000

Community Demographics:
- Unemployment rate 2 times the National Average
- 23.6% Poverty Rate
- Family income 40.8% area median
- CHOICE Neighborhood

Project Basics:
- Dorchester Bay Economic Development Corporation (DBEDC) partnered with Commonwealth Kitchen to utilize NMTC financing for an exciting new concept that uses commercial kitchen space as a means of building small businesses, creating jobs, and encouraging asset building and wealth creation.
- Redevelopment of 36,000 square foot former Pearl Meats Factory, located in the Grove Hall section of Dorchester, into a shared-use and multi-tenant food production facility.
- Integral part of DBEDC’s Quincy Corridor Initiative, which will bring $80 million of public and private investment into a four-block stretch of Quincy Street to revitalize the community, including the rehab of 129 homes for low-income families.
- In 2011, initiative was awarded a HUD CHOICE Neighborhoods grant of $20 million.
### Financing:

**NMTC Leverage Sources:**

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>CDFI Debt</td>
<td>$3,060,000</td>
</tr>
<tr>
<td>HUD 108 Loan</td>
<td>$3,200,000</td>
</tr>
<tr>
<td>CHOICE Grant</td>
<td>$500,000</td>
</tr>
<tr>
<td>Other Grants</td>
<td>$3,035,800</td>
</tr>
<tr>
<td><strong>Total Leverage Sources</strong></td>
<td><strong>$9,795,800</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>NMTC Net Equity</td>
<td>$3,761,700</td>
</tr>
<tr>
<td>Sponsor Direct Equity</td>
<td>$1,273,152</td>
</tr>
<tr>
<td><strong>Total Financing</strong></td>
<td><strong>$14,830,652</strong></td>
</tr>
</tbody>
</table>

Total Development Costs $14,830,652

### Community Impact:

- 64 Construction Jobs Created
- 23 new jobs created in first six months of operation
- 40% of jobs filled by community residents

**NMTC Investor:** PNC Bank

**CDEs:** LISC, PNC
### NMTC: Overview

<table>
<thead>
<tr>
<th><strong>Purpose:</strong></th>
<th>Encourage the investment of private &amp; patient capital in low-income communities.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>What is it:</strong></td>
<td>39% tax credit (.39 for every $1) on the capital invested in a Community Development Entity (CDE), over 7 years (5% in yrs 1-3; 6% in yrs 4-7) 7 year compliance period</td>
</tr>
<tr>
<td><strong>Who is eligible for the credit?</strong></td>
<td>Only a CDE can apply for an allocation of federal tax credits. Only investors who make a qualified investment can claim the credit.</td>
</tr>
<tr>
<td><strong>Who benefits from the credit?</strong></td>
<td>Investors get return through tax credits CDEs further mission Businesses / projects get financing in form of loans or equity</td>
</tr>
<tr>
<td><strong>Eligible Property Types:</strong></td>
<td>Low-income community businesses Commercial, community or mixed-use projects</td>
</tr>
</tbody>
</table>
Community Development Entity (CDE) applies for and receives NMTC “allocation authority” from CDFI Fund - $3.5 billion annually
- $43.5 billion total allocation awarded to date

Investors form partnerships with CDE

Investor’s capital contributions and loans are used to make investments in qualified projects

Qualified projects result in new or rehabbed facilities, job creation and/or other benefits
NMTC Deal Structure: Simple (Unleveraged)

NMTC Investor

Qualified Equity Investment

GP in CDE

Community Development Entity

Loan / Equity

Qualified Project (Borrower)
NMTC: Overview

- NMTCs can finance a wide range of real estate and business activities:
  - Commercial real estate (i.e. office, retail etc.)
  - Community facilities (i.e. health centers, charter schools, rec centers etc.)
  - Industrial/Distribution
  - Business financing

- Type of Construction
  - New Construction or Substantial Rehab
  - Avoid refinancing of existing buildings (can do take-out)
  - Can be combined with Historic Tax Credits
  - Cannot be combined with LIHTC (unless a separate condo regime)

- Ownership & operation of rental housing is specifically excluded BUT
  - Mixed-use projects are permissible if less than 80% of gross revenue is from dwelling units (or if the project is separated into residential and non-residential components)
  - At least 20% of the units must be affordable to tenants earning no more than 80% of the area median income
What do NMTCs do for projects?

- NMTC leveraged financing can fill a 15% - 25% gap in a project’s capital budget, with the percentage filled depending upon:
  - Amount of financing provided
  - Pricing of NMTC equity
  - Whether ongoing NMTC fees & expenses are reserved at closing or paid out from project operating income

- The funding sources for the 75 – 80% of leveraged capital must be willing to accommodate the requirements of a NMTC financing

- Compared to 9% LIHTC projects, where the tax credit equity can be as much as 50% of the total development cost, NMTCs are a relatively shallow subsidy

- Unlike LIHTC and HTCs, NMTCs are generated by enhancing other project sources, rather than being based on project expenditures (“uses”)
How the NMTC Works

Credits are earned on a “Qualified Equity Investment” (QEI) in a “Community Development Entity” (CDE) which uses substantially all of the QEI proceeds to make “Qualified Low-Income Community Investments” (QLICIs) in “Qualified Active Low-Income Community Businesses” (QALICBs) located in Low-Income Communities (LICs)
NMTC: Key Definitions

- **Allocatee**: A CDE that has received an allocation of NMTC authority from the CDFI Fund.

- **QEI**: Qualified Equity Investment - $ contributed to the CDE to acquire equity in the CDE. Investor is able to take NMTCs in an amount equal to 39% of the QEI.

- **QLICI**: Qualified low-income community investment – a loan or investment by a CDE to/in a QALICB.

- **LIC**: Low Income Community - a census tract with (1) poverty rate more than 20% or (2) median family income less than 80% of area median income.
What is a Qualified Active Low-Income Community Business (QALICB)?

- Borrower/Investee that receives loan or equity investment from CDE

- A QALICB is a corporation or partnership (including a nonprofit corporation) engaged in the “active” conduct of a qualified business that meets 5 separate requirements and is not engaged in an excluded business or activity

- “Active” means the business can reasonably be expected to generate revenues within 3 years after the QLICI is made (or for a nonprofit to generate funds to further support its mission)
What are Excluded Businesses?

- Liquor store
- Racetrack or other gambling facility
- Massage parlor
- Hot tub facility
- Suntan facility
- Country club
- Golf course

Restrictions apply to QALICB and Tenants of QALICB
What are Other QALICB Restrictions?

• Can’t be a business which develops or holds intangibles for sale or lease
• Can’t be certain farming businesses

STOP!
This means YOU.

• Can’t be residential rental property (at least 20% gross rental income must be from commercial uses)
Why Leverage?

- **Limitation**: NMTC earned only on equity investments

- **Goal**: structure that allows NMTC to be earned on debt as well as equity, reduce investor’s risk and increase return

- **Solution**: create an intermediate entity (“Investment Fund”) that pools debt and equity from multiple sources before making QEIs into a CDE

- Can be used to NMTC-enhance debt, developer equity, grants & fundraising
$10M QEI x 39% = $3.9M NMTC

NMTC Deal Structure – Leveraged with Cash Down-Flow

- **NMTC Investor**
  - $3M Equity

- **Leverage Lender**
  - $7M Loan(s)

- **Investment Fund**
  - $10M QEI

- **Community Development Entity**
  - Allocatee
  - $10M QEI x 39% = $3.9M NMTC
  - $3M (“B” Loan)
  - $7M (“A” Loan)

- **Qualified Project**
  - (Borrower)

- Multiple Sources

---

NMTC: New Markets for Community Development
LISC: Local Initiative Service Corporation
Enterprise: Housing Enterprises
NMTC Deal Structure – Leveraged with Cash Up-Flow

NMTC Investor

Leverage Lender

Investment Fund

Equity

Loan(s)

Debt service

Cash Flow Distributions

Allocatee

Community Development Entity

Tax Credit

Qualified Equity Investment

“B” Loan

“A” Loan

Debt service

Qualified Project (Borrower)
## Example of the numbers...Gross Equity

<table>
<thead>
<tr>
<th></th>
<th>Example 1</th>
<th>Example 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>QEI</td>
<td>$ 10,000,000</td>
<td>$ 10,000,000</td>
</tr>
<tr>
<td>NMTC Rate (over 7 years)</td>
<td>39%</td>
<td>39%</td>
</tr>
<tr>
<td>Total NMTCs Generated</td>
<td>$ 3,900,000</td>
<td>$ 3,900,000</td>
</tr>
<tr>
<td>Equity Price per NMTC</td>
<td>$ 0.77</td>
<td>$ 0.85</td>
</tr>
<tr>
<td>Gross NMTC Equity Generated</td>
<td>$ 3,003,000</td>
<td>$ 3,315,000</td>
</tr>
</tbody>
</table>
### Example of the numbers…Net Equity

<table>
<thead>
<tr>
<th>Description</th>
<th>Example 1</th>
<th>Example 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross NMTC Equity Generated</td>
<td>$3,003,000</td>
<td>$3,315,000</td>
</tr>
<tr>
<td>Less: Placement Fee (% of QEI)</td>
<td>$(300,000)</td>
<td>$(300,000)</td>
</tr>
<tr>
<td>Less: NMTC Transaction costs</td>
<td>$(300,000)</td>
<td>$(300,000)</td>
</tr>
<tr>
<td>CDE Asset Management Fee (% of QEI)</td>
<td>$(350,000)</td>
<td>$(350,000)</td>
</tr>
<tr>
<td>CDE Audit / Tax Return Expense</td>
<td>$(70,000)</td>
<td>$(70,000)</td>
</tr>
<tr>
<td>Investment Fund Management / Expenses</td>
<td>$(175,000)</td>
<td>$(175,000)</td>
</tr>
<tr>
<td>Total Ongoing Annual Expenses</td>
<td>$(595,000)</td>
<td>$(595,000)</td>
</tr>
<tr>
<td><strong>Net NMTC Equity for Project</strong></td>
<td><strong>$1,808,000</strong></td>
<td><strong>$2,120,000</strong></td>
</tr>
</tbody>
</table>
NMTC Deal Structure - **Unwind**

**NMTC Investor**
- $3M Equity
- $10M QEI

**Leverage Lender**
- $7M Loan(s)
- $7M ("A" Loan)
- $7M ("B" Loan)

**Investment Fund**
- $10M QEI

**Community Development Entity**
- GP in CDE

**Qualified Project (Borrower)**
- $3M ("B" Loan)
- $7M ("A" Loan)

- Investor gets $0 cash back
- Hard leverage loans repaid
- Equity / soft leverage sources
  - May not be repaid

**Multiple Sources**
NMTC: Pros & Cons

Pros:
- “But for” projects are completed
- Focus on creating substantial community benefits
- Efficient use of taxpayer dollars

Cons:
- Limited access to credits; strong competition
- Strict compliance issues
- Transaction structures can be costly & complex
- Program renewal risk

Significant Recapture Risk:
The compliance period is 7 years from date of QEI
Amount of recapture = NMTC (39% of QEI) + interest + penalty
NMTC: Participant Roles

**NMTC Allocatee** (Enterprise, LISC, DCHE)

- Applies to CDFI Fund for NMTC allocation
- Utilizes allocation to finance projects for the direct benefit of the NMTC Investor and the indirect benefit of the borrower
- Role: Ongoing Compliance, accounting, asset management, and investor reporting for seven years

**NMTC Investor / Lender**

- **Economic investors** typically focus on cashflow and depend on project performance to receive a return on capital
  - Construction/permanent lender (“leverage lender”)
  - Equity investors (sponsor, preferred equity)
- **Tax credit investors** typically focus on the receipt of tax credits and depend on regulatory compliance to ensure a return on capital.
NMTC: Participant Roles

**Sponsor / Developer**

- Articulate community impact
- Specify level of commitment of all funding sources
- Develop a pro-forma that articulates NMTC allocation required and appropriate fees
- Begin conversations with NMTC allocatees / CDEs and Investors
  - Allocatees control their own credits
  - Investors control the $$$
NMTC: Participant Risks

Key risk categories

Real estate risk (leverage lender, sponsor)
  - Project performance
  - Effect of market-based conditions

Compliance risk (tax credit investor, CDE)
  - Following IRS guidelines
  - Complying with Allocation Agreement with CDFI Fund

Management of risk allocation (sponsor, tax credit investor, CDE)
  - Transaction structuring to ensure appropriate party bears risk

Reputation risk (CDE)
  - Ability to receive future NMTC allocations
    (maintain track record)
Transaction Selection

- Does it meet CDE’s strategy & commitments?
  - Geography
  - Investor relations
  - Project type, community impact, but-for
  - Located in highly distressed census tract?
  - Strong community support?
  - Environmental sustainability, etc.

- Does it meet the requirements of applicable Allocation Agreements?

- Does it meet the investment guidelines for investors?

- Is it a Qualified Active Low Income Community Business?
Transaction Selection

Filters: Community Impact

CDEs consider benefits to low-income community/end-users

- Job creation/retention
- Quality jobs: wages / benefits
- Brings commercial or community goods and services to underserved areas
- Flexible financing for business operations
Transaction Selection

Filters:

Project or other benefits would not be achieved “but for” NMTC

- Targeted towards investments that have a funding gap
- Demonstrate that all other sources of subsidy have been exhausted
- Commercial projects in “low-rent” areas
- Cannot access market rate capital
- Goal: Efficient use of taxpayer money
Timing

- Application cycle is important to both CDEs and project sponsors...
  - Typically, CDFI Fund announces new awards in Summer
  - Projects then take 3-6 months to close on average
- How to be prepared as a project sponsor:
  - Clearly defined funding gap that can be closed with a straightforward leveraged structure
  - Sources of Leverage and other financing committed
  - Project defined, construction drawings complete and costs estimated with a GMP Contract with general contractor
  - Site control and real estate issues in order
How to find a CDE?

- List of CDEs - Cdfifund.gov
  - Geographic Footprint
  - QEI Issuance Report
- NMTC Consultants
- Banking relationships
- Call one of us!
NMTC Compliance - Recapture

Events of recapture:

- CDE ceases to be qualified
  - Change of primary mission or non-accountable board

- “Substantially All” requirement is not met
  - 85% of QEI must be invested in a QLICI “at all times”

- QEI is redeemed or cashed out by CDE
  - Cash in excess of “net operating income” is distributed to investment fund / investor

Recapture = loss of all tax credits + interest & penalties
Not Recapture…

Recapture is not triggered if:

- CDE goes bankrupt
- QALICB goes out of business
- Mortgage is foreclosed upon
  - Any QLICI proceeds repaid are still subject to reinvestment requirements
DC Housing Enterprises

Enterprise

LISC
DC Housing Enterprises (DCHE) is a subsidiary of the District of Columbia Housing Authority (DCHA). DCHE is one of a few housing authority Instrumentalities that is certified by the Community Development Financial Institutions Fund (CDFI Fund) as a Community Development Entity (CDE).

Accomplishments:
- DCHE has received $83 million New Markets Tax Credit allocations since 2009 and has invested over $400 million in community real estate and business development.
- NMTC Investments has created over 500 construction and permanent jobs. 124 of jobs created were set aside for public housing residents.
- DCHA has received 7 HOPE VI awards and 1 Choice Neighborhood Planning Grant and lead the revitalization efforts in low income communities across the District of Columbia.
How DCHE uses NMTC

DCHE’s Strategy:
DCHE prioritizes investments that reinforce DCHA and other partner agencies targeted development activities therefore, we make investments in projects that meet the various demands of economically challenged communities.

- Types of projects include:
  - Educational
  - Mixed-Use Commercial
  - Community Facility
  - Recreational/Entertainment
  - Fresh Foods
  - Health Care Facilities
  - Employment Training Center
Educare DC – Kenilworth Parkside Community

Early Childcare Educational Program:
- Serves 175 very low income students ages 6 weeks – 5yrs old.
- Technical support to parents to assist with job training and employment.
- Offers innovative approach towards educating low income children beginning at 6 weeks old.
- 65 permanent jobs created.

Leveraged Model
NMTC Equity: $3,000,000 ( $15.6 Million Allocation )
Total Development Cost: $24,300,000
NMTC Investments at Kenilworth Parkside
CNI Planning Grant Recipient

- Educational Facilities
- Educare DC
- Unity Health Care – Medical Clinic
- Parkside Parcel
- Kenilworth Courts Parcel
- Kenilworth Ave.
Progression Place & Howard Theatre
DCHE Project Example

Progression Place (Office, Retail & Residential)
- 205 residential (51 workforce/affordable units)
- 24,343 GSF storefront retail & 103,083 GSF office space /UNCF Headquarters
- 194 parking spaces underground parking structure

Leveraged Model
NMTC Equity: $3,971,000 ($18 Million Allocation)
Total Development Cost: $157,654,244
- Highly Distressed:
  - Median Income < 60% of statewide
  - Unemployment > 1.5 times national average
- Community Impact:
  - 232 Construction and 66 Permanent Jobs Created
  - Real estate tax increase over $1.2 mill from 2012 – 2014
  - Scholarship Opportunities/ College of Knowledge Center
  - Job Training & Employment Opportunities
Enterprise Overview

- Enterprise is a national non-profit organization seeking to end housing insecurity. Enterprise’s mission is to create opportunity for low- and moderate-income people through affordable housing in diverse, thriving communities.
  - Loans, Grants, and Equity Investments
  - Local, State, and National Policy Support
  - Technical Assistance

- Since inception, Enterprise has invested $18.6 billion, investing in over 340,000 homes and millions of square feet of commercial and community facility space.

- Enterprise has received $830 million in NMTC allocation and invested $803 million to date
How Enterprise uses NMTC

- Enterprise invests NMTC allocation in severely distressed neighborhoods in the 10 areas where Enterprise has a local office.

- We focus on projects that will complement affordable housing investments and provide access to:
  - Health care
  - Better education
  - Healthy food and
  - Jobs

- Average NMTC investment is $10 million per project
- We partner with other CDEs and
- Provide compliance / asset management services for others as needed
Miller’s Court – Baltimore, MD

BECORE

$21M TDC
$19M of NMTC allocation
State and Federal HTC
38% Poverty Rate / 66% AMI
1.5 x national unemployment rate
Baltimore Enterprise Zone
Brownfield
Perception of crime & danger

AFTER
Miller’s Court - Impact

**GOALS**

- Quality Affordable Housing for Baltimore Teachers
  - Positive Financial Changes
  - Improved Resident Quality of Life
  - Increased Commitment & Positive Teaching Experience

- Provide a Collaborative Environment for Nonprofits
  - Strengthened Collaboration Between Tenants
    - Increased Professionalism & Opportunities for Growth

- Spark Revitalization in Distressed Neighborhood
  - Increased “Sense of Place”
    - Reduction in Crime
      - Increased New Investment
        - Greater Long-Term Neighborhood Commitment

- Create New Economic Opportunity
  - Increased Economic Activity & Local Spending
    - Job Growth
      - New Tax Revenue Generated

**PROJECT IMPACT**

- Enterprise
Asian Health Services – Oakland, CA

• $10.7M TDC
• $10.5M NMTC allocation
• AMI 34.8% / Poverty 21.6%
• Federal medically underserved area
• High unemployment

New NMTC facility is having a tremendous impact on the 9,800 patients seen annually:
• 87% of patients have their blood sugar under control, compared to 73% nationally
• 75% have blood pressure under control, compared to 52% nationally
• 97% have an asthma action plan, compared to 81% nationally
LISC Overview

- LISC is a national non-profit organization dedicated to transforming distressed neighborhoods into healthy, sustainable communities.
  - With 30 local programs and a national rural program, LISC helps to mobilize support to local community development organizations with:
    - Loans, Grants, and Equity Investments
    - Local, State, and National Policy Support
    - Technical and Management Assistance
- Since its inception in 1980, LISC has invested $15 billion which has generated $44.1 billion in total development.
- LISC has received $908 MM in NMTC allocation and invested $854 MM in 100 projects to date
- LISC NMTC Program is managed by its affiliate, New Markets Support Company
How LISC uses NMTC

- LISC brings NMTCs to communities served by LISC by financing transactions that advance the community development strategies of LISC’s local programs, National Rural Program, & other national programs and affiliates.
- LISC generally uses $5-$15 million in NMTC financing per transaction and can partner with other CDEs on larger transactions.
- LISC has also developed two structured NMTC products:
  - Small Business Loan Fund – provides advantageous first mortgage, real estate financing in connection with the SBA 504 Program.
  - Healthy Futures Fund – provides favorable financing for Federal Qualified Health Centers (FQHCs).
Paseo Verde TOD - Philadelphia, PA

Total NMTC Financing - $30,000,000
LISC NMTC Financing - $10,000,000

Community Demographics:
- Unemployment rate 4.4 times the National Average
- 61% Poverty Rate
- Family income 23.6% area median

Project Basics:
- Developers Asociación Puertorriqueños en Marcha (APM) and Jonathan Rose Companies received NMTC financing for the new construction of a mixed-use, transit-oriented, green development that provides affordable, workforce and supportive housing and space for a health center, pharmacy, and a nonprofit that provides social services dedicated to improving the outcomes for children.
- The NMTC project includes 67 residential units and 29,400 SF of commercial space. The health center relocated and expanded into new space in order to offer low-cost medical care to 2,000-2,900 uninsured people annually.
- The project utilized environmentally responsible construction and remediated a brownfield site, which had been underutilized for years, with a modern LEED Certified building.
Paseo Verde TOD - Philadelphia, PA

**Financing:**

<table>
<thead>
<tr>
<th>NMTC Leverage Source(s):</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>TRF Energy Leverage Loan</td>
<td>$3,000,000</td>
</tr>
<tr>
<td>Chase Senior Loan</td>
<td>$9,010,000</td>
</tr>
<tr>
<td>Sponsor Leverage Loan</td>
<td>$9,046,286</td>
</tr>
<tr>
<td><strong>Total Leverage Sources</strong></td>
<td><strong>$21,056,286</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Equity Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>NMTC Net Equity</td>
<td>$7,897,264</td>
</tr>
<tr>
<td>Deferred Developer Fee</td>
<td>$1,130,415</td>
</tr>
<tr>
<td><strong>Total Financing</strong></td>
<td><strong>$30,083,965</strong></td>
</tr>
</tbody>
</table>

| Total Development Costs          | $30,083,965 |

**Community Impact:**

- 112 Construction Jobs Created
- 139 Permanent Jobs Created
- 2,900 patients served
- 1,000 children served

**NMTC Investor:** Chase Community Equity, LLC

**CDEs:** LISC
Corporation for Supportive Housing
Building America
WNC
LISC and Enterprise Communities

Enterprise Footprint

LISC Footprint
Contact Information

- Shirley Boubert, DC Housing Enterprises
  - Sboubert@dchousing.org

- Elaine DiPietro, Enterprise
  - edipietro@enterprisecommunity.com

- Kelsey Hamory, LISC New Markets Support Company
  - khamory@newmarkets.org