# CDFA Brownfields Redevelopment Financing Webinar Series:
# New Investments in New Markets Tax Credits

THE BROADCAST WILL BEGIN AT 2:00PM (EDT)

- Submit your questions in advance using the GoToWebinar control panel
- View previous webcast recordings online at www.cdfa.net

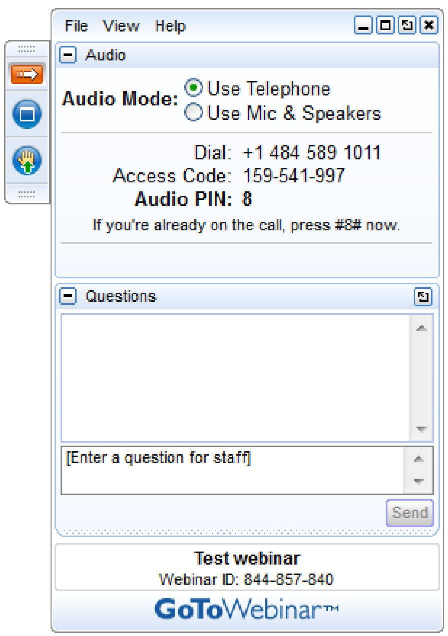
# Welcome & Overview

Emily Moser, Program Manager

Council of Development Finance Agencies

Columbus, OH

# Welcome & Overview




Using your telephone will give you better audio quality.

Submit your questions to the panelists here.

Join the Conversation

**Technical Questions?**
Contact Kevin White at CDFA: 614-705-1317

# Panelists

Jon Ades
Manager, CohnReznick LLP

Colin Rowan
Principal, United Fund Advisors

**CDFA connects the public and private development finance sectors.**

# CDFA's 5 Focus Areas:

- *Education*
- *Advocacy*
- *Research*
- *Resources*
- *Networking*

# CDFA Training Institute

## Training Courses:

- Fundamentals of Economic Development Finance Course
- Bond Finance (Intro and Advanced)
- Tax Increment Financing (Intro and Advanced)
- Intro Tax Credit Finance Course
- Intro Revolving Loan Fund Course
- Intro Energy Finance Course
- Intro Public-Private Partnership (P3) Finance Course
- Intro EB-5 Finance Course
- Intro Food Systems Finance Course
- Seed & Venture Capital Course
- Intro Brownfield Finance Course

# CDFA Online Resource Database

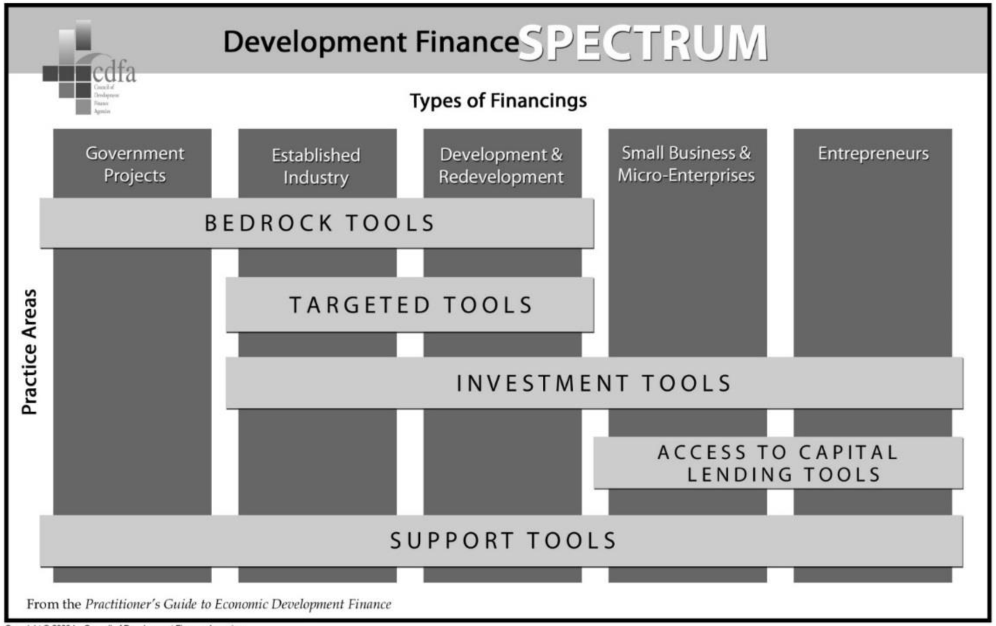
The CDFA Online Resource Database (ORD) is the nation's only electronic resource collection dedicated exclusively to development finance.

- CDFA Online Resource Database – 5,000 categorized resources
- Federal Financing Clearinghouse – 150+ federal program overviews
- Resource Centers – Bond, TIF, RLF
- Development Finance Review Weekly – newsletter to 20K+ subscribers
- 5 Targeted Newsletters – Tax Increment Finance Update, Bond Finance Update, Clean Energy + Bond Finance Initiative, Legislative Front Update, State Small Business Credit Initiative Update
- Targeted State Financing Roundtable Newsletters
- Daily Headlines

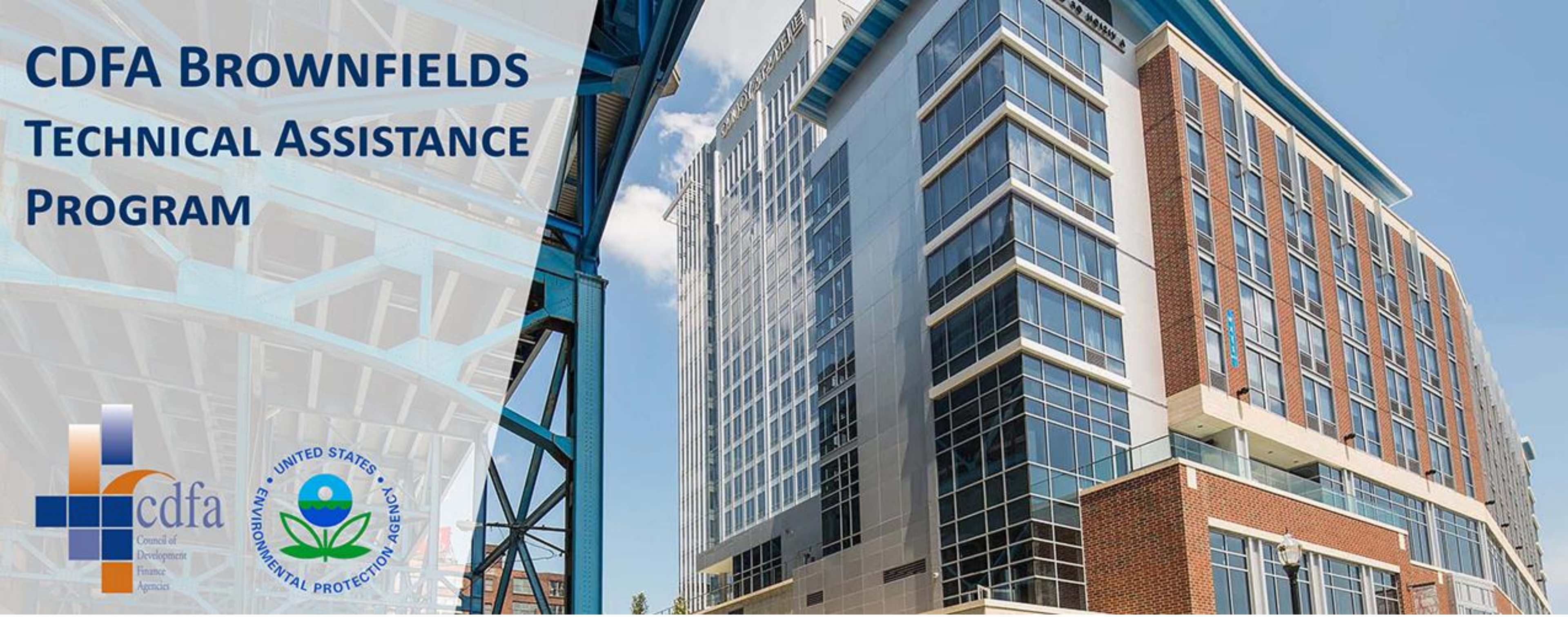
# CDFA Toolbox Approach

- *Bedrock Tools:  Bonds*
- *Targeted Tools: TIF and SAD*
- *Tax Credits/Investment Tools*
- *Lending/Access to Capital*
- *Support Tools: Federal Grants, Tax Abatements*

# CDFA Toolbox Approach



# CDFA Brownfields Technical Assistance Program



**Online Resources:**

- Monthly Brownfields Financing Update
- Brownfields Financing Toolkit
- Online Resource Database

**Technical Assistance:**

- Brownfields Project Marketplace
- Project Response Team Visits

# Jon Ades

Manager, CohnReznick LLP

# Using New Markets Tax Credits to Build Stronger Communities

Presented to: **CDFA Brownfield Financing Webinar**

COHN REZNICK

FORWARD THINKING.

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August 13, 2015

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# COURSE OUTLINE

- **Overview of the New Markets Tax Credit (NMTC) Program**
- Process Overview and Deal Structure
- Players in a NMTC Deal – Risks and Benefits at each level
- Project Eligibility
- Compliance Requirements

# HISTORY AND OBJECTIVES OF NMTC PROGRAM

- Enacted on December 21, 2000 as part of the Community Renewal Tax Relief Act of 2000 to revitalize low-income communities.

- New Markets Tax Credits (NMTCs) are federal, dollar-for-dollar tax credits to assist in the funding of neighborhood changing/job creating <u>commercial</u> real estate projects and businesses located in low-income census tracts.

- Low-income communities have trouble attracting investment, leading to dormant or vacant buildings and businesses, inadequate access to healthcare and education, lower property values, leading to low-income communities becoming distressed communities.

## Example Projects:

Charter schools, health care facilities, timberlands, child care providers, supermarkets, restaurants, museums, hotels, performing arts centers, pharmacies, convenience stores, manufacturers, processors, distributors, trucking companies, printing companies, waste management, renewable energy projects, sporting goods, office buildings, shopping centers, substance abuse treatment facilities, recording studios, movie studios, parking garages, etc., etc.

# CURRENT DEVELOPMENTS

| Round (Year) | Total Allocation | Amount Finalized | Amount Remaining |
|---|---|---|---|
| Round 1 (2001-2002) | $2,485,699,042 | $2,485,699,042 | $0 |
| Round 2 (2003 – 2004) | $3,493,786,205 | $3,493,786,205 | $0 |
| Round 3 (2005) | $1,964,688,856 | $1,964,688,856 | $0 |
| Round 4 (2006) | $4,099,765,000 | $4,099,765,000 | $0 |
| Round 5 (2007) | $3,892,249,021 | $3,892,249,021 | $0 |
| Round 6 (2008) | $4,964,500,010 | $4,964,500,010 | $0 |
| Round 7 (2009) | $5,000,000,000 | $4,987,649,999 | $12,350,001 |
| Round 8 (2010) | $3,475,000,000 | $3,454,471,927 | $20,528,073 |
| Round 9 (2011) | $3,622,919,753 | $3,610,908,147 | $12,011,606 |
| Round 10 (2012) | $3,500,000,000 | $3,333,581,479 | $166,418,521 |
| Round 11 (2013) | $3,501,392,113 | $2,502,754,587 | $998,637,526 |
| Round 12 (2014) | $3,512,350,000 | $0.00 | $3,512,350,000 |
| Total | **$43,512,350,000** | **$38,790,054,273** | **$4,722,295,727** |

- Round 13 applications are expected to be awarded in Spring/ Summer 2016; however, only if Congress extends the program.
- For Round 12, there were 263 applications, requesting $19.9 billion. Round 12 awards were made to 76 applicants for $3.512 billion.
- Allocation awards ranged from $15 million to $75 million per allocatee, and the average being $46.2 million.

# Allowance of Credit

- General business credit under Section 38.
- Claimed on "anniversary" date of QEI (credit allowance date).
- Subject to AMT.
- Can combine with other Federal and State subsidies and credits, except LIHTC.
- Can be used to offset passive income.

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# PROCESS OVERVIEW

Step 1: Entities apply to the CDFI Fund for CDE certification *(rolling basis)*.

Step 2: CDEs apply competitively to the CDFI Fund for a NMTC allocation.

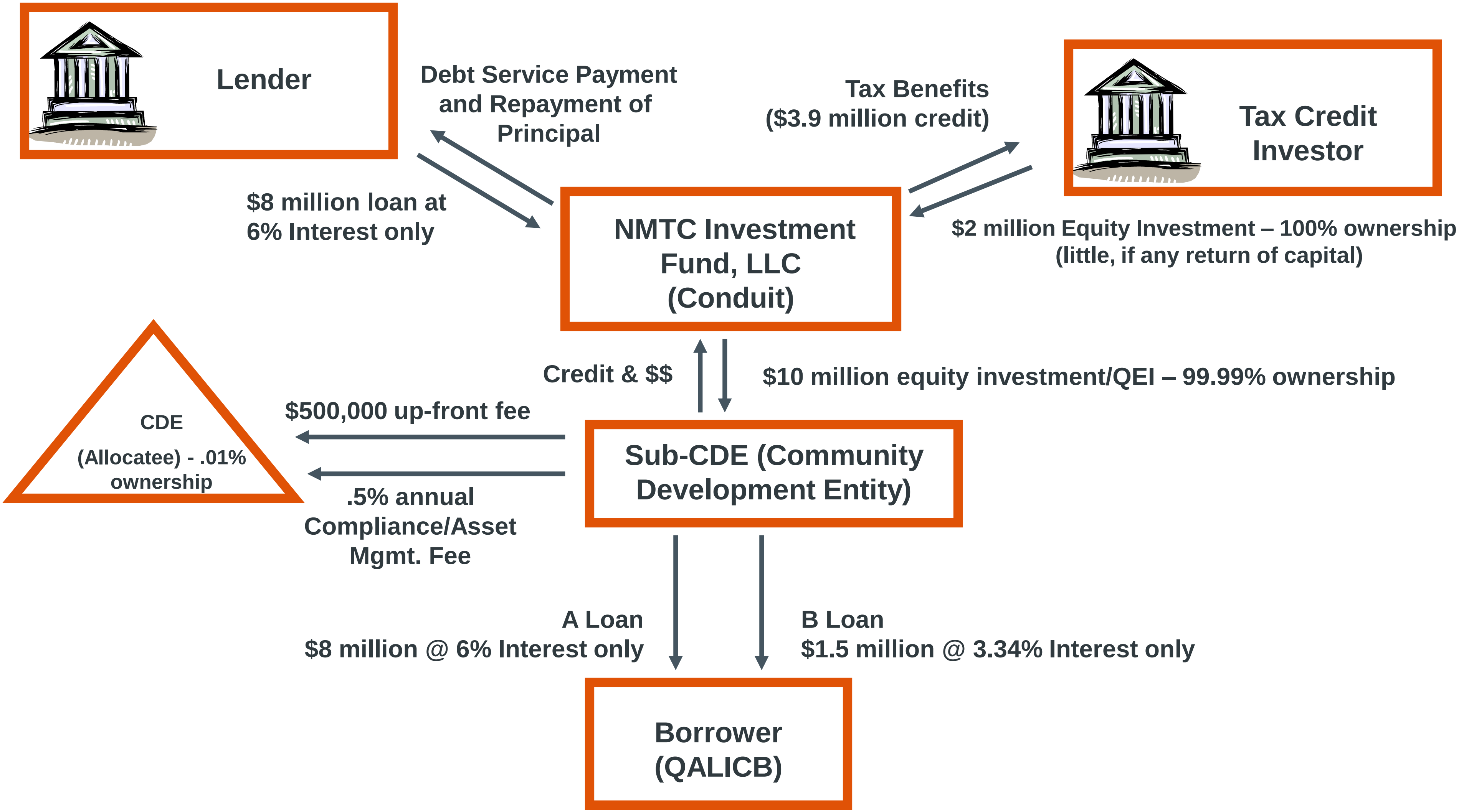
Step 3: The CDFI Fund allocates NMTCs to CDEs that are selected.

Step 4: CDEs use allocations to offer NMTCs to investors for cash investments called a Qualified Equity Investment(“QEI”).

Step 5: CDEs use proceeds to make Qualified Low-Income Community Investments (“QLICIs”) in QALICB.

Projects are chosen VERY CAREFULLY – they must meet the “But-For Test” – meaning that “but-for” the assistance of the tax payer dollars, the project would never come to fruition

# Leveraged NMTC Structure



# TIMING AND CALCULATION OF THE CREDIT

- NMTCs are offered to investors for Qualified Equity Investments (QEIs) in the CDE.

- Credit equals 39% of amount of QEIs.

- Credit claimed over 7 Years:
  - *5% in each of the first three years, and*
  - *6% for each of the final four years.*

- QEI must remain invested in the same CDE for a seven year credit period ("compliance period").

- Full year of credit claimed regardless of when during the year the QEI is made.

# EXAMPLE

- CDE receives a $10 million allocation of NMTCs. This is only allocation authority!

  This means that the CDE can raise $10 million of equity from investors.

- $10 million of allocation x 39% credit = $3.9 million of federal tax credits to be received by the investor.

If a single investor made the $10 million investment into the CDE today then the investor will receive tax credits over time equal to…

| | |
|---|---|
| Year 1 | @ 5% = $.5 million |
| Year 2 | @ 5% = $.5 million |
| Year 3 | @ 5% = $.5 million |
| Year 4 | @ 6% = $.6 million |
| Year 5 | @ 6% = $.6 million |
| Year 6 | @ 6% = $.6 million |
| Year 7 | @ 6% = $.6 million |
| 7 Years | @39% = $3.9 million |

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# PLAYERS IN A NMTC DEAL

- Community Development Financial Institution Fund (CDFI Fund)
- Internal Revenue Service (IRS)
- Community Development Entity (CDE)
- Investor
- Leveraged Lender
- Qualified Active Low-Income Community Business (QALICB)

# COMMUNITY DEVELOPMENT ENTITIES (CDE)

- Domestic corporation or partnership that is an intermediary vehicle for the provisions of loans, equity investments, or financial services to qualified businesses in Low-Income Communities of the CDE's service area.

- CDEs are required to demonstrate that they:

- Have a primary mission of serving, or providing investment capital for, Low-Income Communities or Low-Income Persons, and

- Are accountable to residents of the Low-Income Communities they serve through a minimum 20% representation on their governing or advisory board (annual feedback to CDE management).

- Extremely competitive process to get an award!

## Investor benefits

- 39% tax credit over 7 years
- Being the 1st in a new, unsaturated market
- Recognition/CRA credit for helping underserved populations
- Increased investment volume
- Great public relations
- Project control
- Using the leveraged model to diversify risk (allow the leveraged lender to carry the economic risk, while the investor only carries the low credit risk)

## Leveraged Lender Obstacles

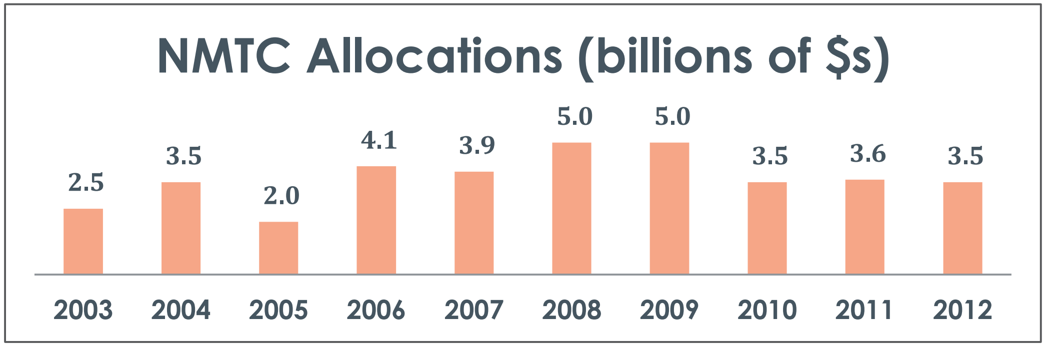
- 7 year stand-still on calling the loan
- No direct security in the real estate of the project

# Qualified Active Low-Income Community Business (QALICB) benefits

- Access to non-conventional, non-conforming financing
  - Lower than market interest rates
  - Subordinated debt
  - Lower or no origination fees
  - Higher LTV
  - Lower DSCR
  - Fixed rate debt
  - Typically, the 7 years with little to no amortization (interest only)
- Gap financing (equity as approx. 20% of capital stack)

# Overall benefits

- Between 2002 and 2015, the federal government has provided New Markets Tax Credits (NMTC) allocations to more than 350 Community Development Entities (CDEs), totaling $43.5 billion in tax credit authority.
- The NMTC program has created or retained 358,000 jobs, supported construction of 17.1 million square feet of manufacturing, 49.4 million square feet of office space and 42.7 million square feet of retail space.




- For every $1 invested by the federal government, it is estimated that $8 of private investment is generated, making it 1 of the most efficient use of tax dollars of any government program.

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- Reporting

# THE QLICI MUST BE MADE IN A QUALIFIED AREA

- There are generally two hurdles
- Hurdle #1—QALICB in an LIC
- LICs are census tracts with…
  - *Poverty of at least 20%, or*
  - *Median family income at or below 80% of the area median family income,*
  - *Median family income at or below 85% of the area median family income, and designated as a high outmigration rural county*
  - *2,000 or less population, designated an empowerment zone and contiguous to an LIC*

# THE QLICI IS ALMOST ALWAYS MADE IN A HIGHLY DISTRESSED COMMUNITY

- Hurdle #2—QALICB in a "highly distressed" community

- Highly distressed LICs are :

  - *Poverty of at least 30% of the national average, or*

  - *Median family income at or below 60% of the area median family income, or*

  - *Unemployment at least 1 ½ times the national average*

  - *Other options as defined in section 3.2 (h) of the Allocation Agreement*
    - Brownfield site
    - Hope VI Redevelopment Plan
    - Native American or Alaskan American area
    - Federally designated medically underserved area (if investment supports health services)
    - Non-metro census tracts
    - Food desert

# WHAT IS A QUALIFIED ACTIVE LOW-INCOME COMMUNITY BUSINESS?

- 50% or more of the total gross income is from active conduct of a qualified business in a Low-Income Community; and
- 40% or more of the use of the tangible property is located in a Low-Income Community; and
- 40% or more of the services provided by the business' employees are performed in a Low-Income Community; and

**Exceptions:**

1. **The gross income test is met if either the tangible property or the services test is met at 50% or higher.**
2. **A business venture with no employees (e.g., real estate partnership) meets the services and gross income tests if it meets the tangible property test at 85% or higher.**
3. **"Active conduct" includes start-ups (for profit and not-for-profits) if the entity is reasonably expected to generate revenue (receive donations) within three years of the date of the QLICI.**

# WHAT IS A QUALIFIED ACTIVE LOW-INCOME COMMUNITY BUSINESS (CONTINUED)

- Less than 5% of the average aggregate unadjusted bases of the property is attributed to;
  - *Collectibles (e.g., art and antiques, other than for sale in the ordinary course of business), and*
  - *Non-qualified financial property (e.g., debt instruments with a term in excess of 18 months OR unreasonable levels of working capital in cash and cash equivalents [QLICI made to support construction activity within twelve months of investment is considered reasonable working capital]).*
- Ineligible business activity;
  - *Operation of residential rental property which derive 80% or more gross rental income from dwelling units*
  - *Rental of real property where no substantial improvements are made*
  - *Rental of real property where any tenant is not a qualified business*
  - *Operation of golf courses, race tracks, gambling facilities, certain farming businesses, and liquor stores (referred to as "sin businesses").*

# What Constitutes Real Estate

- Loans or investments to qualified businesses who's primary function is the development and leasing of real property are considered Real Estate

- Non Real Estate refers to loans or equity investments to businesses who, for example, will build their own facility and will be the principal tenant of the property. In order to be considered the principal tenant, they have to lease more than 50% of the total square footage, without regard to the % gross rent.

- 80/20 Rule (residential vs. commercial)

- Real Estate Exceptions (no straight acquisitions or refinancing)
  - Cost in connection with new construction
  - Cost in connection with substantial rehabilitation
  - Cost in connection with acquisitions and substantial rehabilitation
  - Cost in connection with acquisitions and new construction
  - Take out financing, if the original financing was used for any of the above

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# ALLOCATION AGREEMENT RESTRICTIONS

- Must honor allocation agreement terms (more restrictive than IRS)

- Must use allocation on QEI within 5 years of allocation agreement

- Must use substantially all of QEI as QLICIs within 12 months, for duration of 7 years after QEI (substantially all test)
  - *85% for first 6 years*
  - *75% for last year*
  - *Must reinvest returns on capital within 12 months*

# RECAPTURE

Cumulative NMTC's claimed may be recaptured, with penalties and non-deductible interest, from investors during the 7-year tax credit period if:

- The "substantially all" requirement is not met; or
  - *E.g., Failure to meet 85% threshold;*
  - *Failure to meet QALICB requirements; or*
  - *Failure to meet the twelve month investment and/or reinvestment requirement.*
- The CDE ceases to qualify as a CDE; or
  - Primary mission directed to low-income community
  - Accountability to low-income community
- The CDE redeems the investment through distributions.
  - Each year you need to ensure distributions made during the year are equal to or less than tax-basis net operating income for the year.
- **Recapture cliffs from 100% to 0% after 7 years.**

***If a CDE and/or QALICB files for bankruptcy, this is not a recapture event.***

# Colin Rowan

Principal, United Fund Advisors

# INVESTMENT TOOLS: NMTC FINANCE

## CDFA: BROWNFIELDS REDEVELOPMENT FINANCING WEBINAR SERIES

**August 13, 2015**

UFA UNITED FUND ADVISORS℠

# UFA – Background

- Fund manager and financial services company that provides tax-advantaged investment capital and advisory services for community development and renewable energy projects throughout the country

- 3BL Mission: "To create opportunities for profitable investments which enhance social and environmental yields"

- Over $2 billion of assets under management

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# UFA – Tax Credit Experience

- Closed over 155 investments: >$4.8 billion of project costs
- Direct NMTC Financing:  Over $500 million
- Client CDEs:  Over $1 billion including institutional investors, developers, CDFIs and major cities
- Syndicated over $80 million of HTC investments
- Manage UFA Renewable Energy Fund I, LLC

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# UFA – NMTC Clients

- **Financial Institutions:** Prudential, American Savings Bank
- **Agencies:** Honolulu, Las Vegas, Los Angeles, New York City, Portland, San Francisco, San Diego
- **Nonprofits:** Raza Development Fund, Montana Community Development Corporation, Ecotrust, Genesis LA
- **Developers:** Gerding/Edlen Development Company, Sage Hospitality, Urban Holdings

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# UFA – Services

- **Prepare NMTC Applications**
  - Develop strategy
  - Secure investor commitments
  - Analyze community impacts
  - Draft application

- **Structure & Close Tax Credit Transactions**
  - Outline financing options and select most appropriate based on overall cost and projected impacts
  - Prepare investment materials, source tax equity, secure additional allocations, and guide negotiations with investors and lenders
  - Manage structuring, negotiation and closing process from start to finish

- **Develop Compliance & Asset Management Systems**
  - Incorporate tax credit compliance requirements into policies and procedures
  - Review tax credit filings and reports

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# NMTC BENEFITS

- Approximately 20% of the “capital stack” can be derived from NMTC financing
- NMTC financing is low-cost, flexible capital
- NMTC flexibility comes in the form of flexible terms, underwriting and covenants
- NMTC financing is typically debt but can be structure as equity

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# NMTC CONSIDERATIONS

- 7-year credit/compliance period
- Requires 80% of funding in the structure to come from another source – the "leverage"
- Challenges combining NMTC equity with commercial financing
- Highly competitive program
- "Lumpy" funding cycle
- Congressional re-authorization beyond 2015

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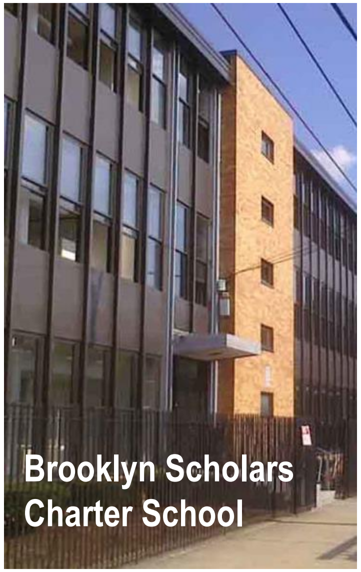
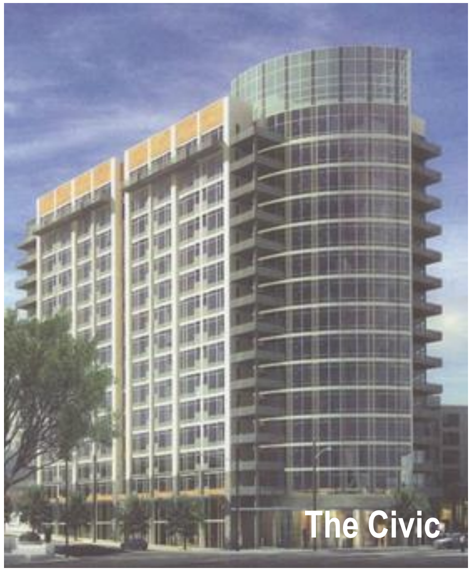
# NMTC EXAMPLES

**Schools | Cultural Centers | Healthcare Facilities | Office & Retail**



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# RENEWABLE ENERGY EXAMPLES

**Rooftop Solar | Community Wind | Biogas/Fuel Cells | Solar Highway**





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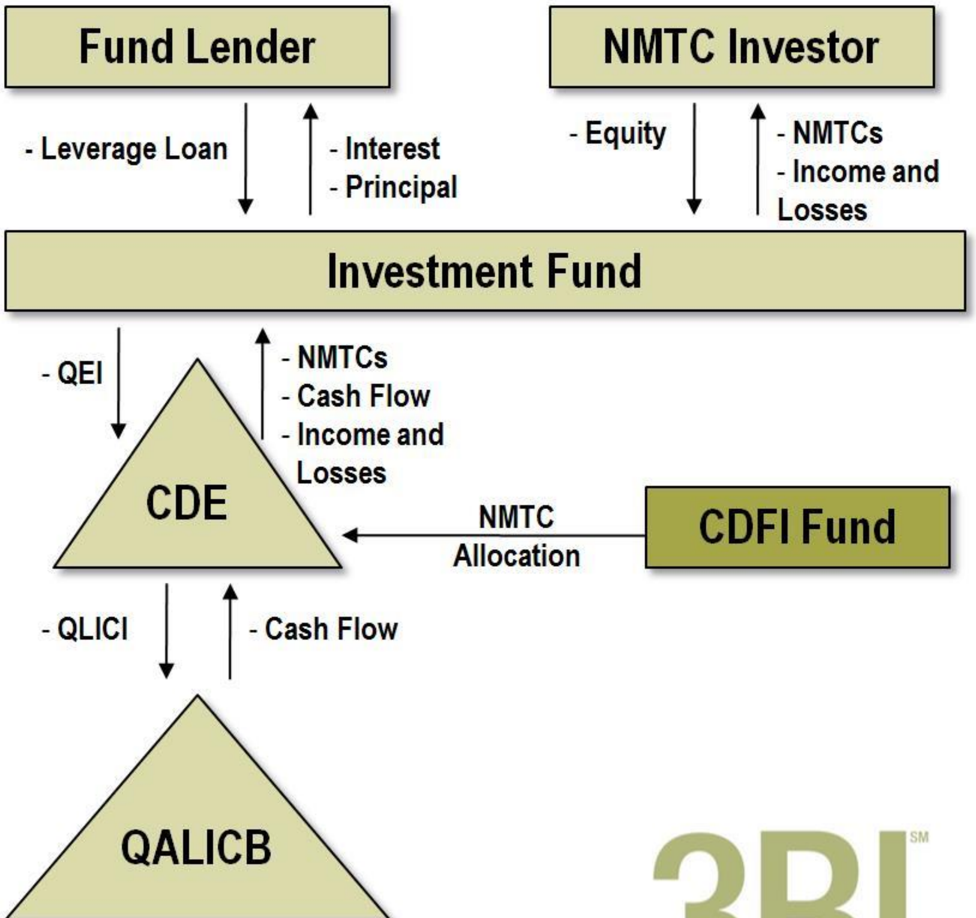
# NMTC BASICS – Structure

## Leverage Structure

- Investment Fund is the intermediary for the debt and equity contributions
- QLICI is typically separated into "A" and "B" notes, corresponding to debt and equity portions of QEI
- Fund Lender receives interest and principal paid to the CDE, which flows up through the Investment Fund
- NMTC investor receives tax credits



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# ISSUE WITH PAIRING HTC/ITC/NMTC

- Is the project a good fit for NMTCs?
  - Create or maintain quality jobs
  - Provide needed goods and services
  - Provide housing units at below-market rates
  - Provide demonstrable benefits for residents of a low-income community and/or low-income persons
  - Provide environmentally sustainable outcomes
- Is there investor appetite for both credits?
- Are there tax issues that need to be addressed?

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# CASE STUDY #1: COASTAL ENERGY

- Location: Coastal WA
- Renewable Energy Type: Wind
- Capacity: 6 MW
- Configuration: 4 1.5 MW Turbines
- Output: +/-13,500,000 kWh
  clean energy annually

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# COASTAL ENERGY COMMUNITY IMPACTS

- Increased operating income for social service agency
- Coastal provides:
  - Food bank services
  - Health care services
  - Job training and placement services
  - Housing services: transitional, rental assistance

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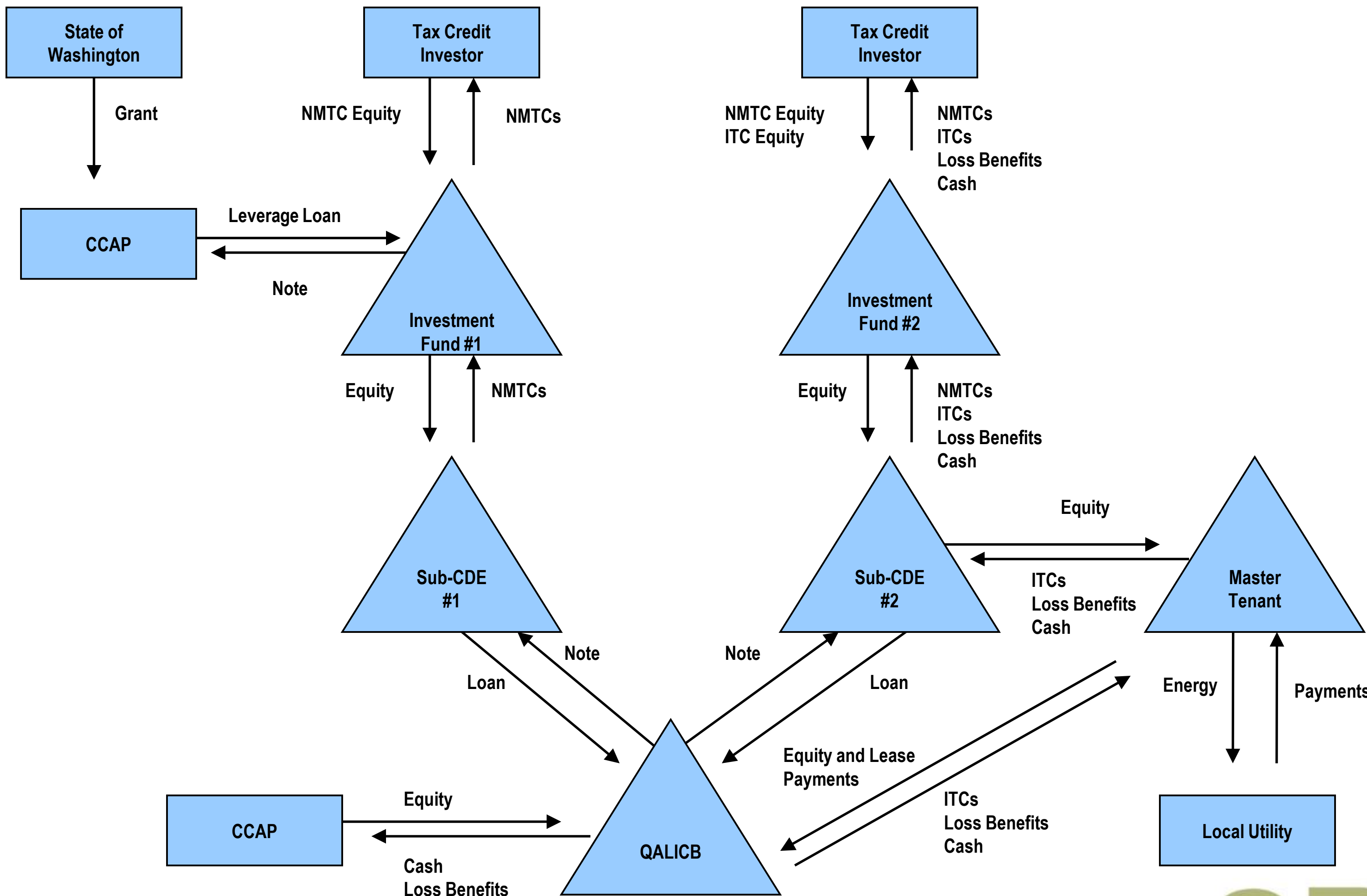


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# CASE STUDY #2: ROSHEK BUILDING

- Location: Dubuque, IA
- LEED Gold Commercial/Retail
- Sponsor: Dubuque Initiatives
- Project cost: $45.5mm
- Financing:
  - Commercial debt
  - New Markets Tax Credits
  - Historic Tax Credits
  - City guarantee

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# ROSHEK BUILDING COMMUNITY IMPACTS

- Job creation: 1,600 living wage jobs
- Environmental: historic preservation, LEED gold facility
- Goods and services: below market space for local non-profits, new retail, support for local job training program
- $9.0mm of NMTC equity, $9.8mm federal HTC equity and $10.7mm state HTC equity, allowing for no up-front public funding

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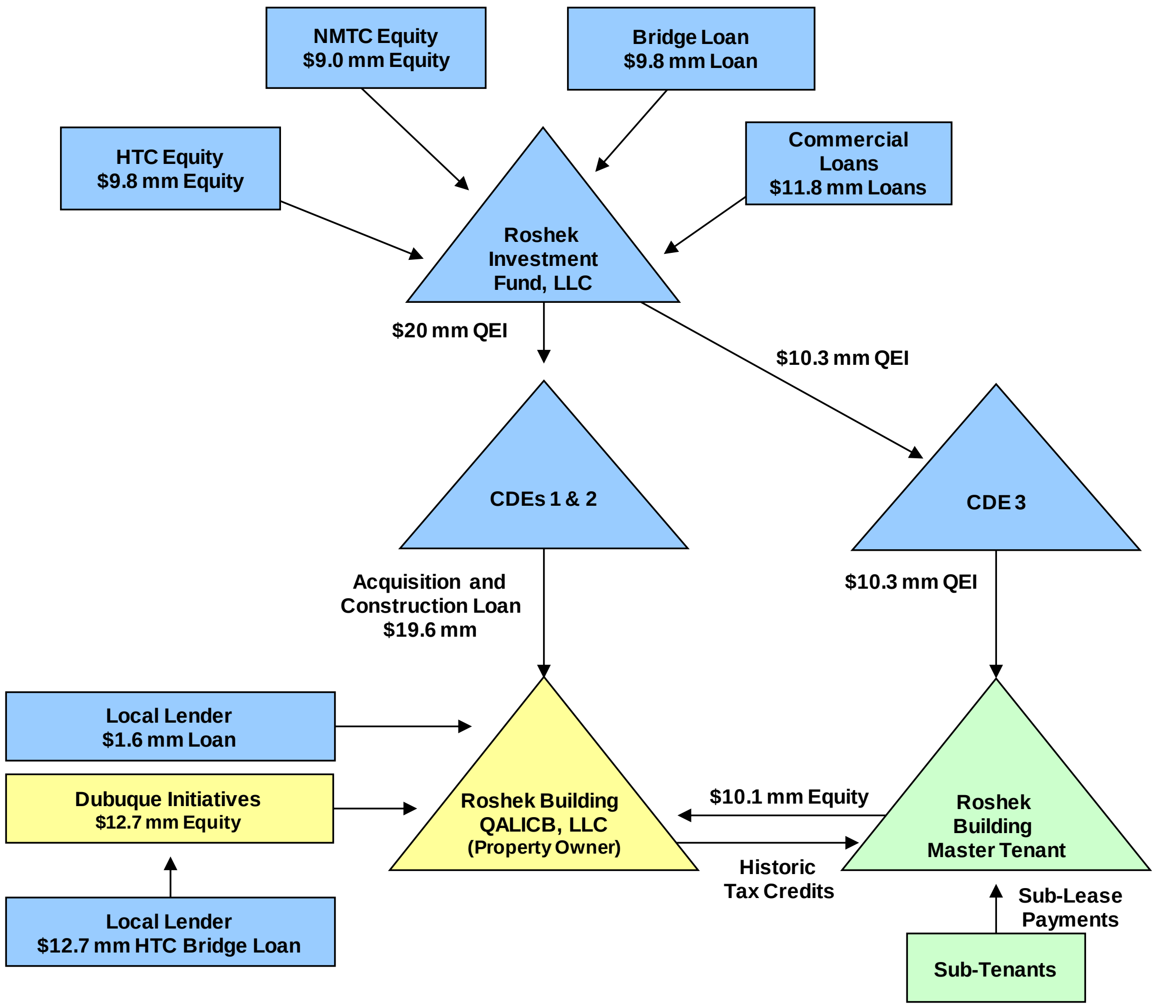


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# HTC CONSIDERATIONS

- "Pricing" hard to pinpoint given all of the variables
- Need for bridge financing
- Investor market is narrow
- State credits often available
- Technical elements of program need to be considered early

# ITC CONSIDERATIONS

- Ongoing extension of legislation
- 1-year credit w/5-year compliance period
- Choppy TC market, especially for non-utility scale projects
- Gap filler for projects that face challenging economics
- Need for bridge financing to tax credit capital

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# CONCLUSIONS

- NMTC financing can deliver up to ~20% of the capital needed for a project
- Brownfields are attractive to NMTC allocatees, but additional community benefits need to be articulated
- NMTC financing is true gap financing - typically the last money in
- All none NMTC capital must be identified
- Closing NMTC financing requires full project-readiness

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# CDFA Brownfields Technical Assistance Program

# Questions?

**Contact:**

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# CDFA Upcoming Events


Brownfields2015
SUSTAINABLE COMMUNITIES START HERE

EPA United States Environmental Protection Agency

ICMA Leaders at the Core of Better Communities

# Join us in Chicago: Save the Date!


## 2015 NATIONAL BROWNFIELDS TRAINING CONFERENCE

**Chicago • Hilton Chicago • September 2-4, 2015**

Visit www.brownfieldsconference.org for more information.

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