

# Midwest Lenders Panel



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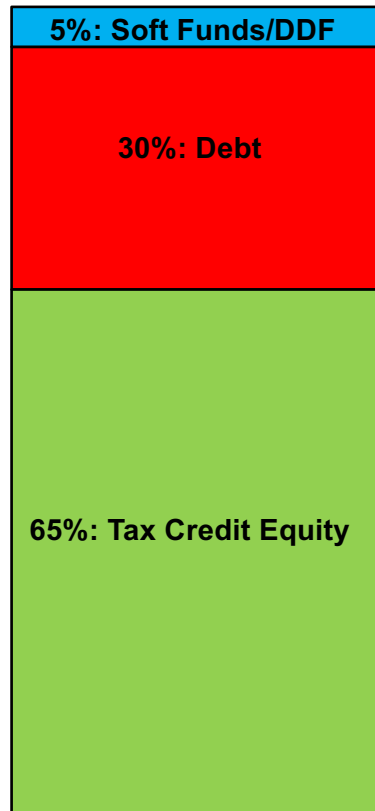
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# What are Low Income Housing Tax Credits (LIHTCs)?

# 4% vs 9% Deals Comparison

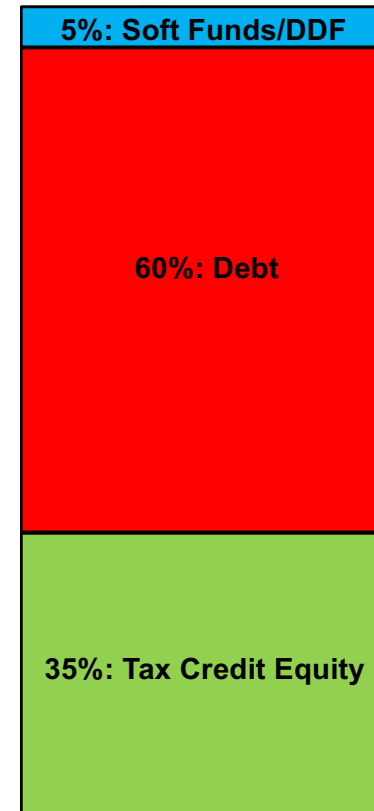
## 9% Deals



### 9% LIHTC Deals:

- Competitive
- Tax-Exempt Bonds are not permitted

## 4% Deals

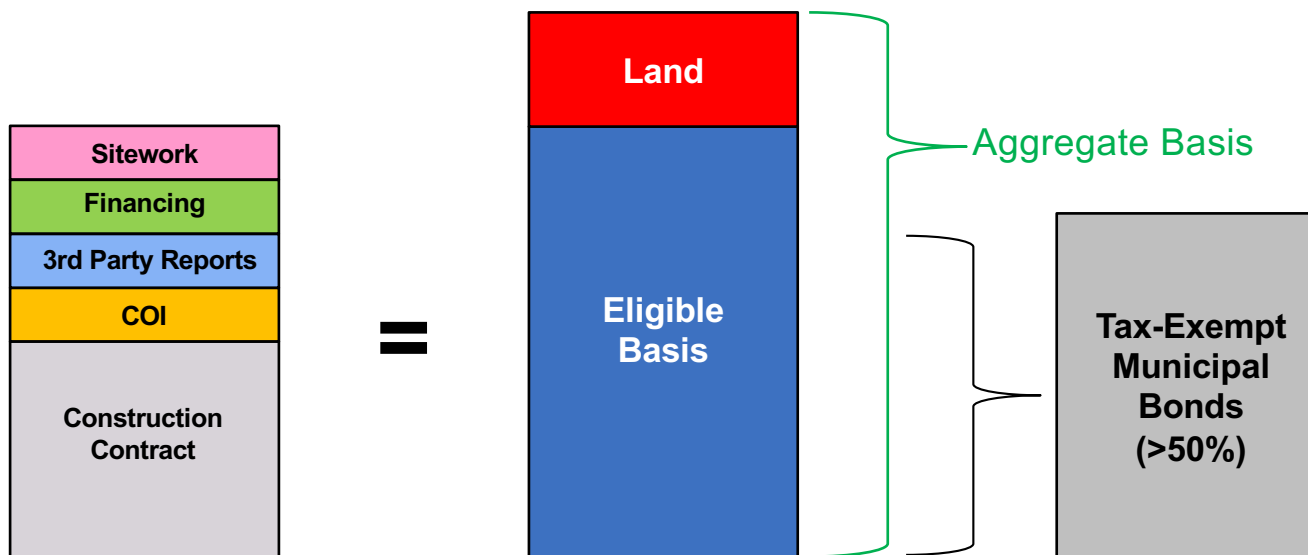


### 4% LIHTC Deals:

- Noncompetitive
- Tax-Exempt Bonds are required

# 50% Test

To qualify for 4% Tax Credits, the Project must utilize Private Activity Bonds greater than 50% of **Aggregate Basis** (which equals **Eligible Basis** plus **Land**)



Ex: If a Project has \$20mm in **Aggregate Basis**, the Borrower should request greater than \$10mm in Tax-Exempt Municipal Bonds

# What are Tax-Exempt Municipal Bonds?

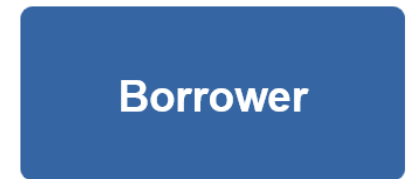
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Bond Investor



Issuer



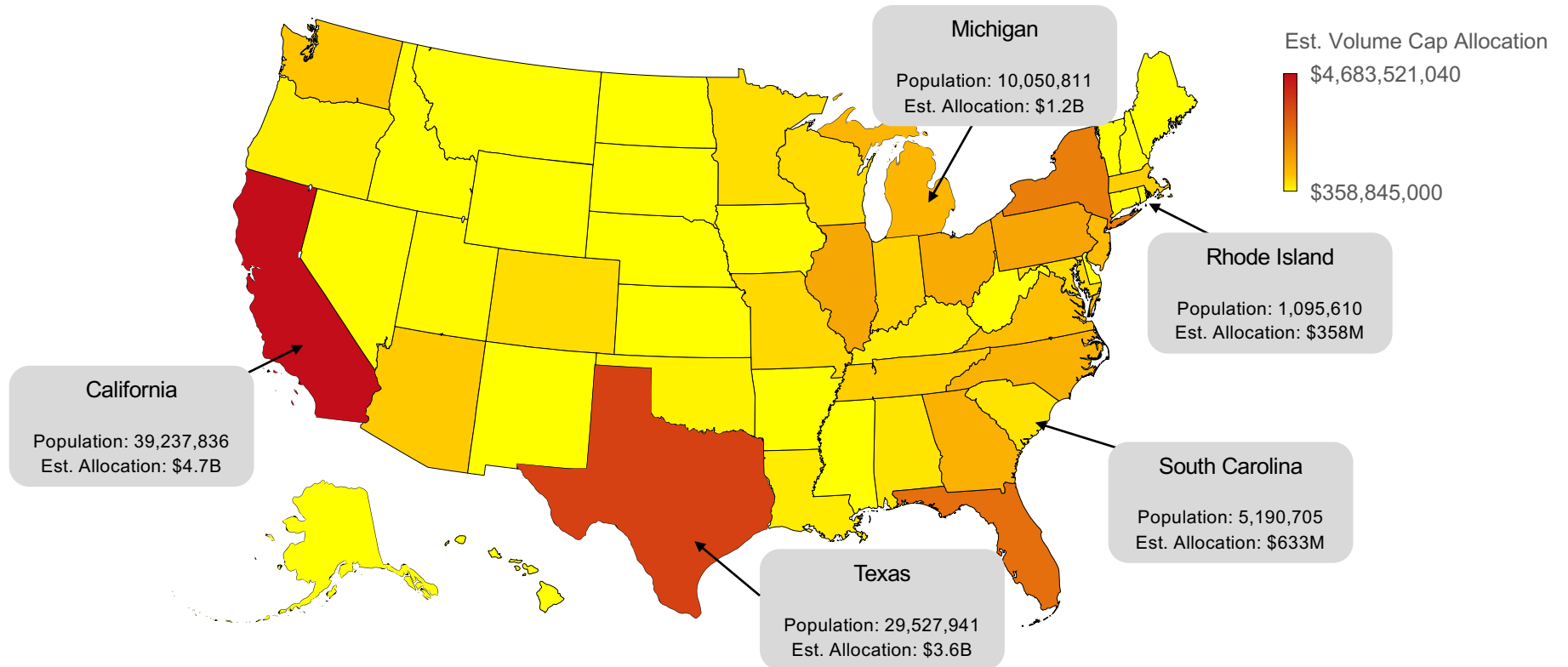
Project

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# Volume Cap and State Tax Credit Programs

# Private Activity Volume Cap Allocation By State

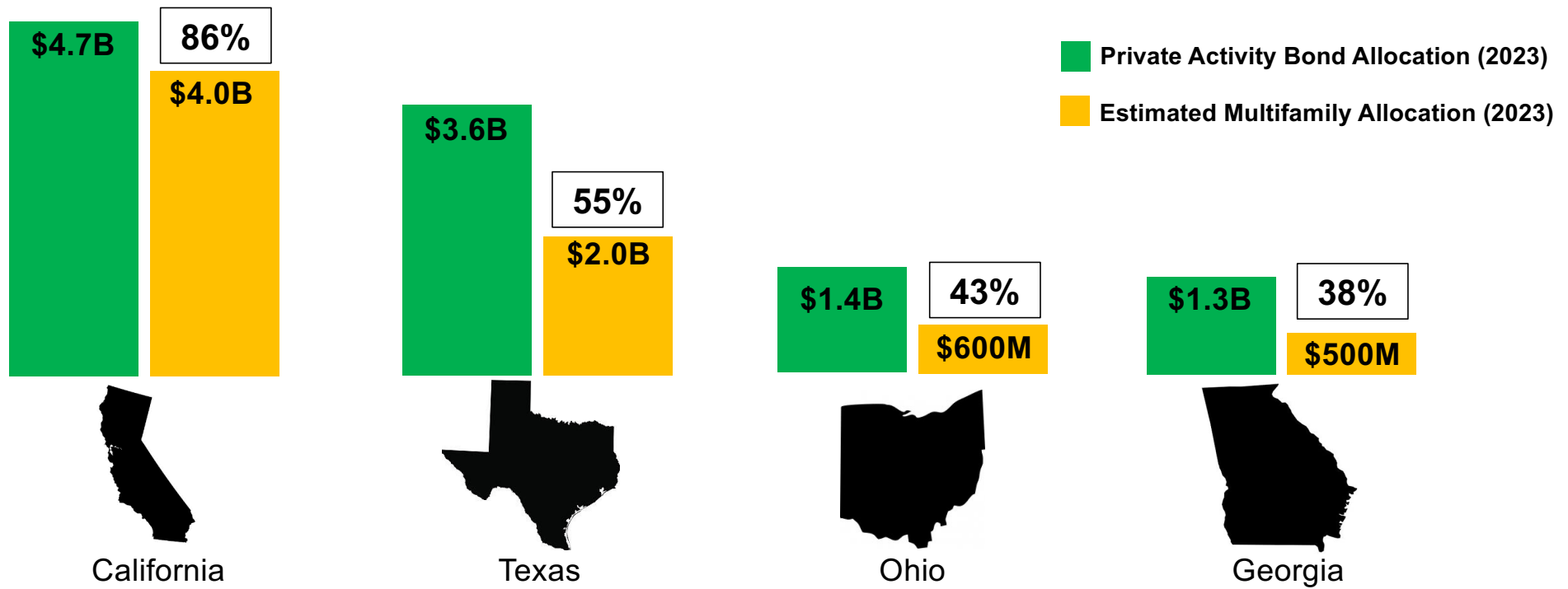
*2023 Volume Cap: \$120 per capita or  
\$358,845,000 minimum for small states.*



# Allocation of Volume Cap For Multifamily

Only a portion of the overall allocation for a state is earmarked for Multifamily use.

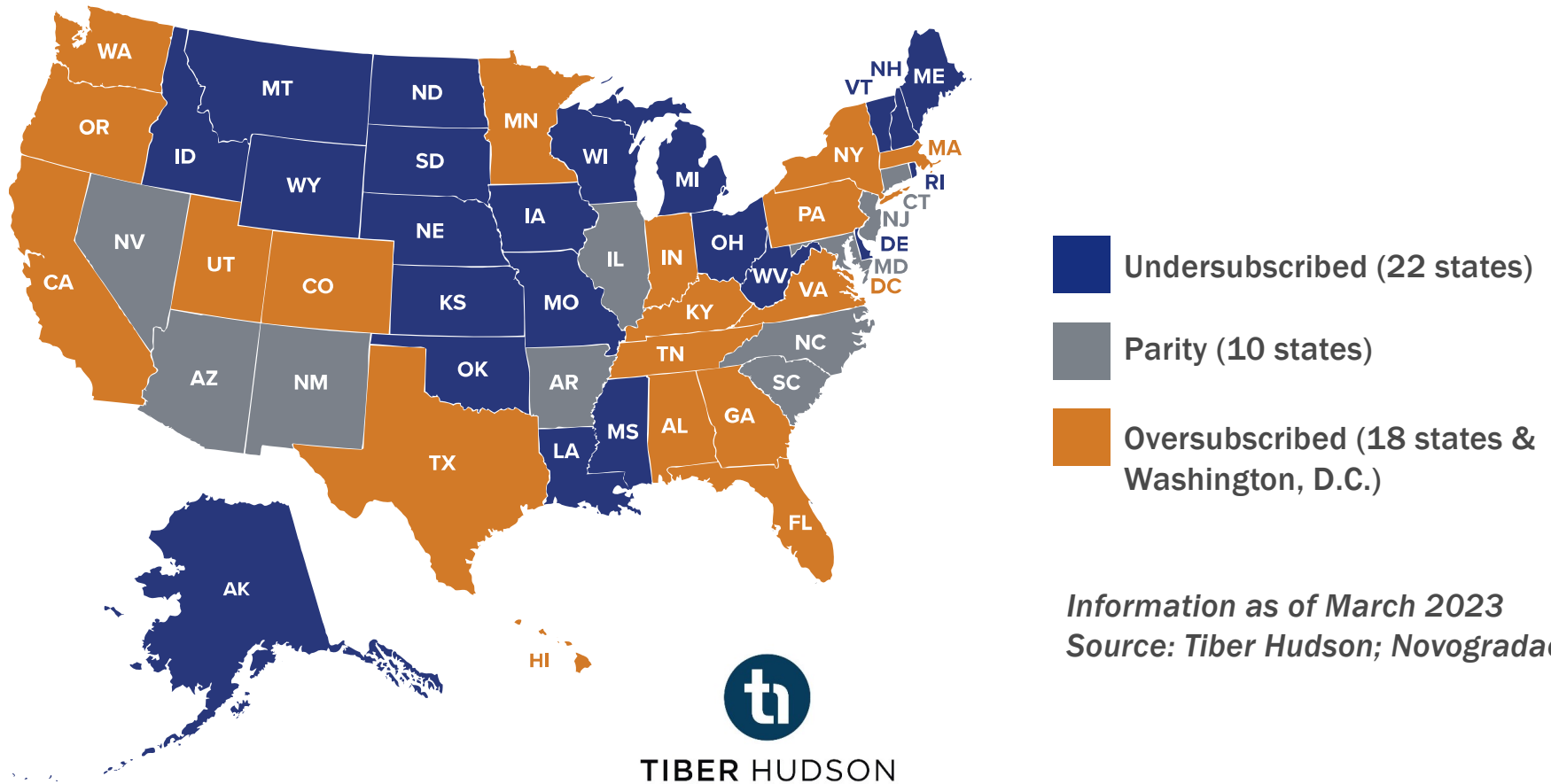
Each state has their own statutory guidelines on how to allocate these funds.



**BIG PICTURE: Important to work with local attorneys who know the area well**



# Multifamily Volume Cap Scarcity



# Preserving Volume Cap

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- Limit volume cap to 55-60% of aggregate basis
- Bifurcate transactions that are less than 100% affordable
- Obtain forward or multi-year volume cap allocation
- Twinning 4% and 9% deals
- Use recycled bonds for additional supportable debt above amount needed for 50% test

# State Subsidy Programs

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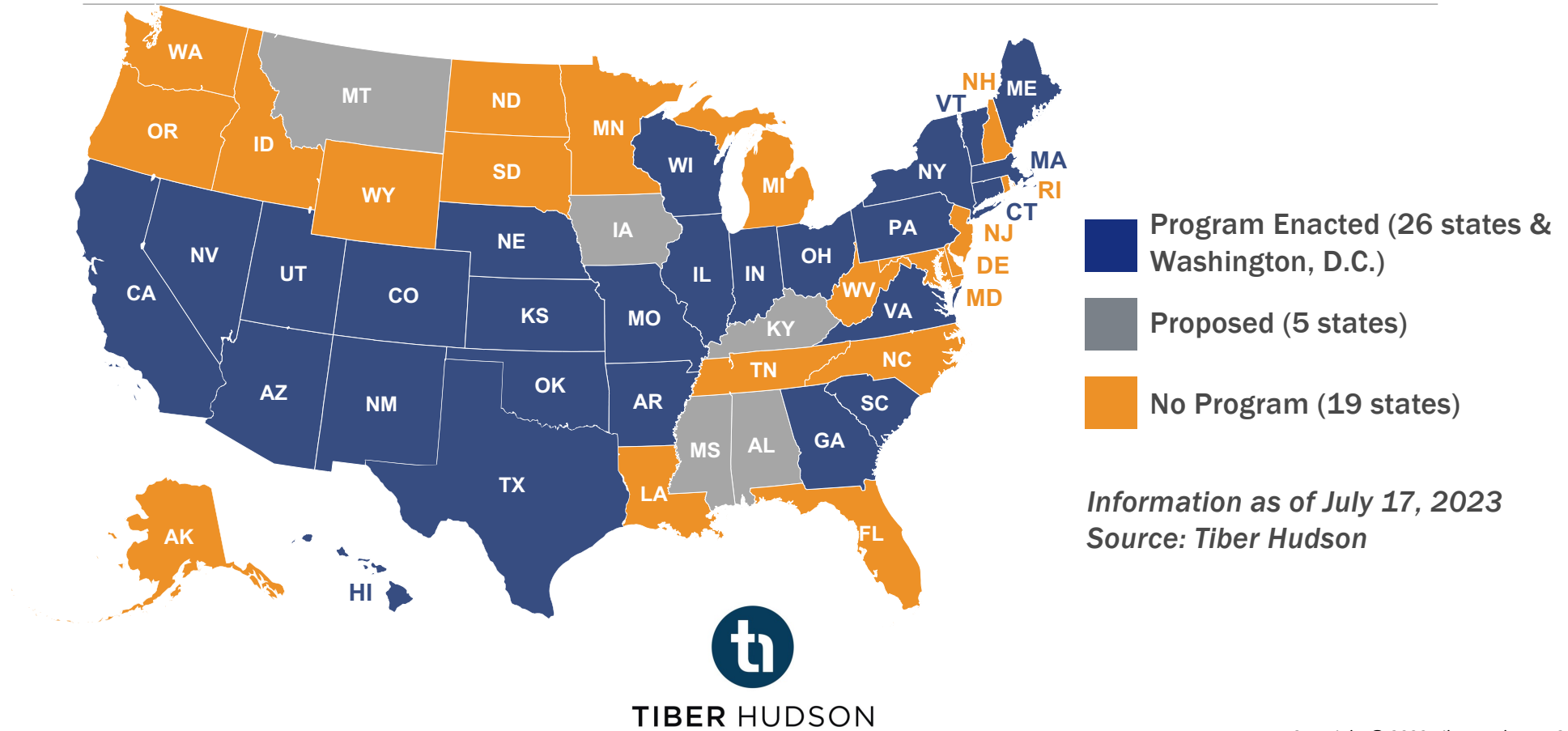
## Real Estate Tax Abatement (varies by jurisdiction)

- Non-profit ownership
- Local urban renewal designation
- Certain forms of local debt

## State and Local Subsidy Programs:

- Payment in Lieu of Taxes
- Soft funds

# State Tax Credit Programs



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# FHA Programs & Short-Term Cash-Backed Execution

## Short Term Cash-Backed Bonds with Taxable Perm Loan

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Taxable construction and/or perm loans still available in the current market at competitive rates including:

- FHA/GNMA (221(d)(4) / 223(f))
- Rural Development (538 / 515)
- Fannie loans (mod/light in-place rehab)
- Other (taxable) State and/or Local loan programs

## Short Term Cash-Backed Bonds with FHA Credit Enhancement

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### **Favorable Underwriting Terms for FHA loans (223f/221d4) include:**

- 35/40-year full term / amortization
- No resizing at conversion
- Non-recourse & integrated construction and perm
- Taxable mortgage loan is funded as needed for sub rehab / new construction deals
- FHA debt qualifies for 10-year hold exemption (for acquisition credits)
- Competitive rates still available
- Davis Bacon wages triggered for sub rehab / new construction deals

## Bond Executions with FHA Credit Enhancement

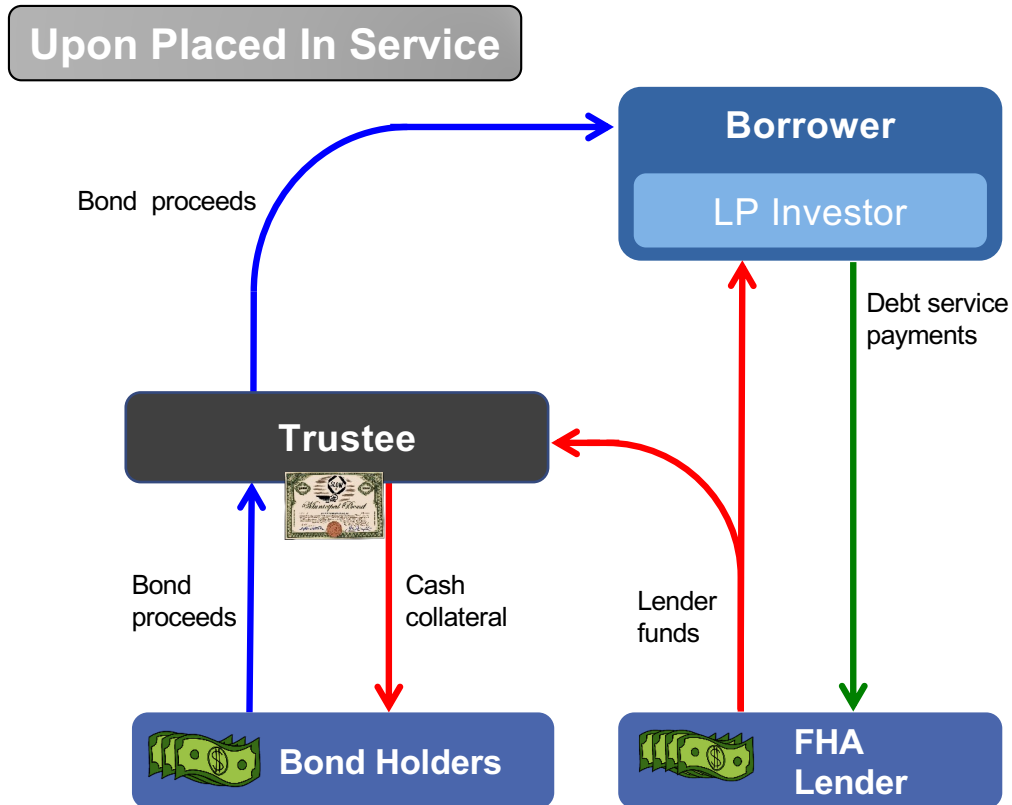
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### **4% Low Income Housing Tax Credits: The 50% Test**

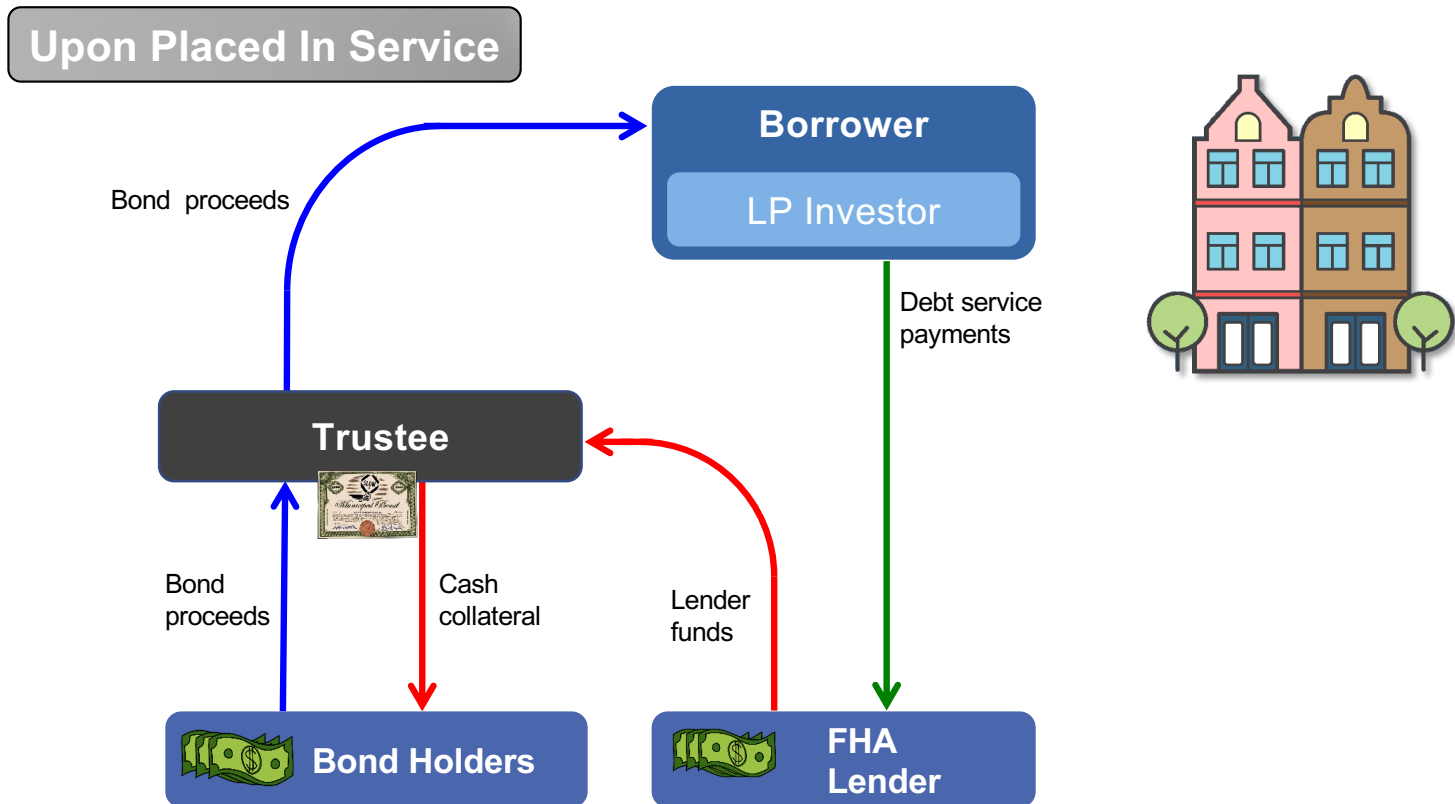
- Project still need tax exempt bonds to qualify for 4% Low Income Housing Tax Credits
- At least 50% of aggregate basis (including building and land) must be financed with tax exempt bond proceeds
- Provides a significant (~30% or higher) additional source of funds for affordable housing transactions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



# Short-Term Cash Backed Bonds – 221(d)4



# Short Term Cash Backed Bonds – 223(f)



# Short Term Cash-Backed Bonds

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## **Bond Amount to meet 50% test < Taxable Loan Amount**

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 Bridge

# Other Cost Saving Features/Options

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## **Methods to reduce transaction costs and generate more proceeds:**

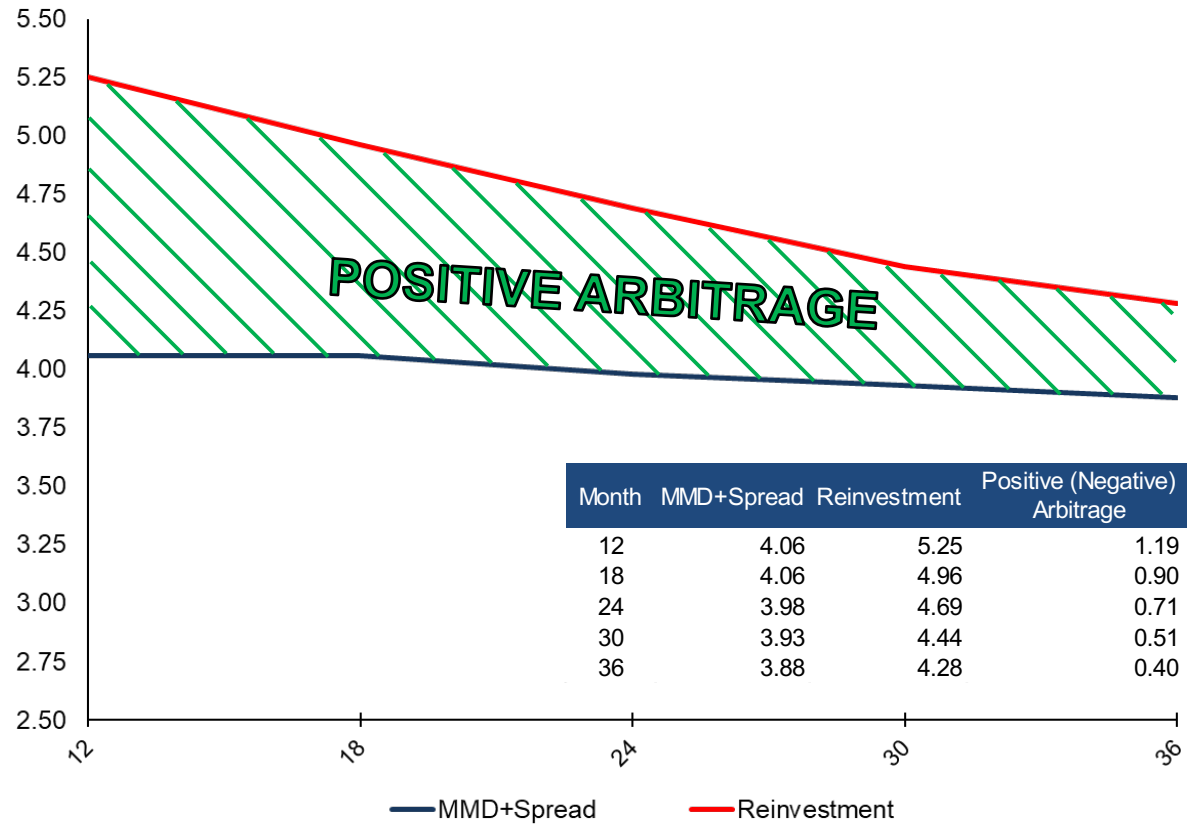
- Pooled financings – multiple projects w/ one aggregate bond issuance
- No long-term bond related fees
- Several investment strategies by Tiber Hudson have helped to mitigate negative arbitrage

# Potential Structure Benefits

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- Subject to approval by the developer's accounting firm, bond interest can often be included in basis in addition to construction loan interest.
- Subject to bond counsel approval, a portion of tax-exempt debt can be recharacterized as a long-term tax-exempt seller note, which can often allow for the retention of excess earnings

# Short-Term Rates vs. Reinvestment Rates – 12 to 36 Months



Source: Bloomberg, Thomson Reuters  
 Reflects market conditions as of June 22, 2023  
 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

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# Tax-Exempt Seller Note

# Tax-Exempt Seller Note\*

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- If deal contemplates a long-term seller note or other subordinate loan as part of the capital stack, ability to potentially convert all or some to tax-exempt financing to meet 50% test by running through issuer
- Can allow blending of yields between short- and long-term bonds as fixed yield issuance
- This increases the tax-exempt bond yield above the investment yield for the term, creating excess earnings that can often be retained instead of being rebated to the IRS

*\*Subject to bond counsel approval*



# Case Study: VA Park Shirlington

Project Overview	
Project Type	Acq/Rehab
Mortgage Lender	National Bank
Issuer	IDA of Arlington County
Location	Arlington, Virginia
Tax-Exempt Allocation	\$75,800,000
Maturity Date	30 Months
Units	294



# Case Study: VA Park Shirlington

Under the typical short-term bond structure, pricing would have been:

Tax-Exempt Proceeds:	\$75,800,000
Term Length:	30 Months
Short Term Bond Yield:	3.40%

Current market yields would generate roughly \$675,000 in positive arbitrage, which under the traditional short-term structure would need to be returned to the IRS:

Tax-Exempt Bond Yield	3.40%
Reinvestment Yield:	3.75%
Est. Excess Earnings:	\$675,000
Est. Retainable Earnings:	\$0

# Case Study: VA Park Shirlington

Instead of keeping 100% of the bond allocation as tax-exempt short-term bonds, \$6mm was recategorized as a long-term tax-exempt seller note:

	Short Term Bonds	Tax-Exempt Seller Note
Tax-Exempt Amount:	\$69,800,000	\$6,000,000
Term Length:	30 Months	42 Years
Yield:	3.40%	5.00%

By recategorizing a portion of the tax-exempt debt, the blended bond yield increases to 4.00%. This now exceeds the investment yield, so excess earnings in the amount of \$650,000 can be retained.

	Original Structure	With Seller Note
Tax-Exempt Bond Yield	3.40%	4.00%
Reinvestment Yield:	3.75%	3.75%
Est. Excess Earnings:	\$675,000	\$650,000
<b>Est. Retainable Earnings:</b>	<b>\$0</b>	<b>\$650,000</b>

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# FHA Refinancing to Re-syndication (R2R)

# FHA Refinancing to Resyndication (R2R)

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- Allows the ability to retain an existing FHA loan (if it has favorable terms) rather than pre-paying into higher interest rate.

## When ready for Bonds/4% Credits

- **Step 1: TPA** (transfer of physical asset) process
- **Step 2:** Supplemental **FHA 241(a)** loan
- **Step 3:** Use short term tax-exempt bonds to qualify for 4% tax credits

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