Panelists

- **Mark Stivers** – Tax Credit Allocation Committee
  TCAC’s Hybrid Rules/Requirements

- **Matt Grosz** - Red Stone Equity Partners
  Investor Underwriting, Demand & Pricing Considerations

- **Amy DeVaudreuil** - Goldfarb & Lipman
  Hybrid Legal & Tax Considerations

- **Q & A**
What is a 9%/4% Hybrid?

• Development using **BOTH** 4% and 9% credits simultaneously

• Formally recognized in 2016 QAP
  • Mitigate LIHTC pricing slump post November ‘2016
  • Regs updated for 2018 rounds

• Captures & generates 4% credit with excess basis from the 9% project
  • Net result is increased credits & equity
  • In theory, reduces need for state / local gap financing

• 9% & 4% developments be separate: ownership, legal parcels, financing, etc.
### Basic Math – Hybrid Example

<table>
<thead>
<tr>
<th>9% Only Project</th>
<th>9%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eligible Basis</td>
<td>48,352,420</td>
</tr>
<tr>
<td>Unused Basis</td>
<td><strong>(26,944,237)</strong></td>
</tr>
<tr>
<td>Resulting Basis</td>
<td>21,408,183</td>
</tr>
<tr>
<td>DDA/QCT Boost</td>
<td><strong>130%</strong></td>
</tr>
<tr>
<td>Adjusted Basis</td>
<td>27,830,638</td>
</tr>
<tr>
<td>Credit Rate</td>
<td><strong>9.00%</strong></td>
</tr>
<tr>
<td>Federal Credits</td>
<td>2,504,757</td>
</tr>
<tr>
<td>Total 10 year credits</td>
<td>25,000,000</td>
</tr>
<tr>
<td>Pay rate</td>
<td><strong>0.98</strong></td>
</tr>
<tr>
<td>Equity</td>
<td>24,500,000</td>
</tr>
</tbody>
</table>
## Basic Math – Hybrid Example

<table>
<thead>
<tr>
<th>Hybrid Example</th>
<th>9%</th>
<th>4%</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eligible Basis</td>
<td>48,352,420</td>
<td>26,944,237</td>
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</tr>
<tr>
<td>Unused Basis</td>
<td>(26,944,237)</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Resulting Basis</td>
<td>21,408,183</td>
<td>26,944,237</td>
<td></td>
</tr>
<tr>
<td>DDA/QCT Boost</td>
<td>130%</td>
<td>130%</td>
<td></td>
</tr>
<tr>
<td>Adjusted Basis</td>
<td>27,830,638</td>
<td>35,027,508</td>
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<tr>
<td>Credit Rate</td>
<td>9.00%</td>
<td>3.27%</td>
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<tr>
<td>Federal Credits</td>
<td>2,504,757</td>
<td>1,145,400</td>
<td>3,650,157</td>
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<tr>
<td>Total 10 year credits</td>
<td>25,000,000</td>
<td>11,453,995</td>
<td>36,453,995</td>
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<tr>
<td>Pay rate</td>
<td>0.98</td>
<td>0.98</td>
<td>0.98</td>
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<tr>
<td>Equity</td>
<td>24,500,000</td>
<td>11,224,915</td>
<td>35,724,915</td>
</tr>
</tbody>
</table>
Top 5 Considerations for Going Hybrid

• Does 9% project have excess eligible basis?
  • Drivers: TBL’s, voluntary basis reduction, $2.5M credit limit, geographic limit

• Does extra basis generate significant equity (threshold likely +/- 20MM total) to be desirable to an investor?

• The two projects will need separate parcels. Possible?

• Can you score full points for projects in key areas?
  • Housing type
  • Service & site amenities (by component)
  • Affordability (in the aggregate)

• Strong organizational capacity? These are complicated!
Hybrid Tiebreaker Benefit

• Qualified “hybrid” developments receive the following benefits:

  ➢ Tax credit units from the 4% project are included in the 9% project’s size factor.

  ➢ The 9% project’s first tiebreaker ratio shall utilize the combined amount of leveraged soft resources defraying residential costs and the combined total residential project development costs from both the 9% and 4% applications.

  ➢ The second tiebreaker ratio shall also utilize the combined total residential project development costs from both the 9% and 4% application.
Hybrid Tiebreaker Benefit

• To be qualified for tiebreaker credit:

  ➢ The owner must have submitted the 4% application to CDLAC and the components must be “simultaneous phases.”

  ➢ The 4% project must be eligible for maximum points in the 9% housing type, service amenity, sustainability, and lowest income points categories, except that the income targeting can be met across both the 4% and 9% projects.

  ➢ Any amount of the combined 4% and 9% developer fees in cost that are in excess of the specified limit must be deferred or contributed as equity to the projects.
**Hybrid Cost and Basis**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>9% Total Basis Reduction</td>
<td>$0</td>
</tr>
<tr>
<td>4% Residential Project Development Cost</td>
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</tr>
<tr>
<td>4% Commercial Project Development Cost</td>
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<tr>
<td>4% Total Project Cost</td>
<td>$0</td>
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</tbody>
</table>
Hybrid Tiebreaker Page in Application

<table>
<thead>
<tr>
<th>SIZE FACTOR CALCULATION</th>
<th>4% Tax Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Construction: No</td>
<td>Units:</td>
</tr>
<tr>
<td>9% Tax Credit</td>
<td>0</td>
</tr>
<tr>
<td>Units:</td>
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<tr>
<td>Size Factor: 1.00</td>
<td>Total Tax Credit</td>
</tr>
<tr>
<td></td>
<td>Units: 0</td>
</tr>
</tbody>
</table>
# Hybrid Financing Mechanics

## Traditional 9% Structure

<table>
<thead>
<tr>
<th>Units</th>
<th>100</th>
<th>per DU</th>
<th>9% Credits</th>
<th>$2,230,000</th>
<th>$22,300</th>
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</thead>
<tbody>
<tr>
<td>Tiebreaker</td>
<td></td>
<td></td>
<td>48.08%</td>
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<tr>
<td>Equity</td>
<td>$21,118,500</td>
<td>$211,185</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Soft Sources</td>
<td>$12,000,000</td>
<td>$120,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hard Debt</td>
<td>$1,500,000</td>
<td>$15,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Development Costs</td>
<td>$34,618,500</td>
<td>$346,185</td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>

## Hybrid 4% Condo

<table>
<thead>
<tr>
<th>Units</th>
<th>30</th>
<th>per DU</th>
<th>4% Credits</th>
<th>$379,665</th>
<th>$12,656</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tiebreaker</td>
<td></td>
<td></td>
<td></td>
<td>N/A</td>
<td></td>
</tr>
<tr>
<td>Equity</td>
<td>$3,595,496</td>
<td>$119,850</td>
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<tr>
<td>Soft Sources</td>
<td>$6,340,054</td>
<td>$211,335</td>
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<tr>
<td>Hard Debt</td>
<td>$450,000</td>
<td>$15,000</td>
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<tr>
<td>Total Development Costs</td>
<td>$10,385,550</td>
<td>$346,185</td>
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<td></td>
</tr>
</tbody>
</table>

## Hybrid 9% Condo

<table>
<thead>
<tr>
<th>Units</th>
<th>70</th>
<th>per DU</th>
<th>9% Credits</th>
<th>$1,850,335</th>
<th>$26,433</th>
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</thead>
<tbody>
<tr>
<td>Tiebreaker</td>
<td></td>
<td>96.60%</td>
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<tr>
<td>Equity</td>
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<td>Soft Sources</td>
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<td>$80,856</td>
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<tr>
<td>Hard Debt</td>
<td>$1,050,000</td>
<td>$15,000</td>
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</tr>
<tr>
<td>Total Development Costs</td>
<td>$24,232,950</td>
<td>$346,185</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

## Analysis

- **100 d/u**
  - 9% Condo
  - Total Development Costs: $346,185
- **30 d/u**
  - Hybrid 4% Condo
  - Total Development Costs: $346,185

**Conclusion:** There is a **> 17% reduction** in costs when moving from a traditional 9% structure to a hybrid 4% condo approach.
When and Where is this Effective?

- High amounts of public subsidy (cash as opposed to in kind contributions i.e. land donations)
- Large voluntary basis reductions
- Projects which are naturally exceeding the maximum annual allocation
- Projects with real estate that can reasonably be subdivided
When Doesn’t it Work?

- Smaller deals (less than 40 units)
- Little to no basis reduction
- Complex subdivisions of real estate
- Deals without a basis boost and/or state credits
- Timing constraints
Take Aways and What Next?

- Leverages an “unlimited” federal resource
- Not a one size fits all solution
- Execution takes an experienced team
- Not twice but probably 150% of the work to finance, close and manage
9%-4% HYBRID LIHTC TRANSACTIONS - TAX AND LEGAL ISSUES

AMY DEVAUDREUIL
GOLDFARB & LIPMAN LLP
MAY 22, 2018
SCANPH
OVERVIEW

- Real Estate/Corporate Considerations
  - 2 Partnerships
  - Separate legal parcels
  - Shared Space

- Tax/Financial Considerations
  - Inclusion of Costs in Eligible Basis
  - Cost Allocation
  - Credit Period

- CASE STUDY: Madison Palms
2 PARTNERSHIPS

- 4% Partnership
- 9% Partnership
- General Partner Structure
- 2 separate projects
  - Separate loan documents
  - Separate regulatory agreements
  - Separate LPAs
  - Separate escrow accounts
Each partnership must own its project
- 4% Partnership owns 4% project
- 9% Partnership owns 9% project

Create distinct legal parcels for each project
- Subdivision Map Act
- Public Agency Conveyance
- Air Rights Parcels
- APNs
SEPARATE LEGAL PARCELS

- Ownership Issues
  - Land
  - Rooftop
  - Walls/Windows
  - Gaps between floors
SHARED SPACE

- Landscaping
- Driveways
- Lobby
- Elevator Shafts/Stairwells
- Systems
- Equipment
- Hallways
- Common Areas
- Community Room
- Pool
- Parking
SHAREO SPACE

- Reciprocal Easement Agreement
  - Exclusive vs. Mutual Use
- Common Interest Development/Condoization
- Master Association/HOA
INCLUSION OF COSTS IN ELIGIBLE BASIS

- Owner must incur expenses to include in Eligible Basis
  - Must pay for costs without reimbursement
  - Must benefit its project
- Expenses onsite (on its owned parcels)
- Offsite expenses (on other parcels)
  - Dedicated public improvements
  - Exclusive Use
COST ALLOCATION

- Owner can only include costs it incurs for its project in Eligible Basis
  - Construction Contract Structuring
  - Cost Allocation Memo
  - Methodology
    - Actual/Direct
    - Pro Rata (Units vs. Square Footage)
  - Reimbursement Agreement
Recommend having different credit periods for 9% and 4% projects

- Different placed in service years
- Defer 1st year for one project
MADISON PALMS

- 3-story building
- 126 units
- Parking lot
- Pool
- Landscaping
MADISON PALMS

9% Project
- 72 units on 1st and 2nd floors
- Land under building footprint
- Portion of driveway and landscaping
- 78 parking stalls
- Common Area on 1st and 2nd floors
- Gap b/t 1st and 2nd floors

4% Project
- 54 units on 2nd and 3rd floors
- Roof
- Portion of driveway and landscaping
- 79 parking stalls
- Pool
- Common Area on 3rd floor
- Gap b/t 2nd and 3rd floors
MADISON PALMS COST ALLOCATION

- **9% Project**
  - 72/126 (57.14%) cost to construct residential units
  - 100% cost to construct driveway and landscaping on its parcel
  - 78/157 (49.68%) cost to construct parking stalls

- **4% Project**
  - 54/126 (42.86%) cost to construct residential units
  - 100% cost to construct roof improvements (including PV)
  - 100% cost to construct driveway and landscaping on its parcel
  - 79/157 (50.32%) cost to construct parking stalls
  - 100% cost to construct pool
LAND
1ST FLOOR
2ND FLOOR
3rd Floor