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An Investor's Perspective of the LIHTC Industry

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Mark Dean is the National Production Manager for Citi Community Capital with over 28 years of experience providing investment banking and mortgage banking services to real estate developers and corporate sponsors.

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Agenda

- Introduction
  - "An Investor's Perspective of the LIHTC Industry Post Tax Reform"
  - Coverage and Objective of today's Webinar
  - Participants and Perspective

- Webinar Mechanics \ Participant Input

- LIHTC Update Topics
  - Perspective on post 2017 tax reform
  - Operating in 2018
    - Is there Certainty in Today's Market?
    - Current Depth and Breadth of Market
    - Pricing
    - CRA versus Economic Investors / What does CRA get you?
    - Impact of Fannie Mae and Freddie Mac in the market
    - Structuring / Credit Trends

- Q&A – AskCitiCommunityCapital@citi.com

Panelist

Greg Voyentzie

Boston Financial Investment Management, Executive Vice President, Production

Mr. Voyentzie joined Boston Financial in 1999 and has over 23 years of experience in the affordable housing industry. Mr. Voyentzie currently co-leads Boston Financial's equity syndication efforts with Sarah Laubinger. Together, they have joint responsibility for the strategic direction of the syndication practice, including the identification and marketing of new capital sources, the structuring and pricing of new fund offerings, and the selection of property-level investments. Prior to joining Boston Financial, Mr. Voyentzie represented LIHTC investors while at Ernst & Young and was also a manager in the Real Estate Accounting practices at PricewaterhouseCoopers. Mr. Voyentzie holds a Bachelor of Science and a Masters in Business Administration from the University of Connecticut.

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Panelist

Thomas Morton

Pillsbury Winthrop Shaw Pittman, Partner

Tom represents corporate investors, financial institutions, developers and syndicators in projects and transactions throughout the U.S. that qualify for low-income housing, historic rehabilitation, energy investment, energy production and new markets tax credits. He provides federal income tax and financing advice, and structures projects that combine various types of credit programs. Tom is also experienced in advising large corporations, airlines and financial institutions on leveraged, operating and synthetic lease transactions involving aircraft, railcars, computer systems and other equipment

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Panelist

Mark Sherman

Citi Community Capital, Director, Structured Lending and Investing

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Mark Sherman works in the Structured Lending and Investing group of Citi Community Capital (CCC). He is responsible for the management of CCC's low income housing tax credit equity platform, CRA-qualifying structured lending origination initiatives, various municipal structured products, securitizations and agency executions.

Prior to serving in his current role, Mark worked in Citi's Municipal Capital Markets Financial Products and Accounting Policy Groups. Before joining Citi, he served a one-year fellowship at the Financial Accounting Standards Board and worked as an assurance and advisory associate at Deloitte. Mark received his BS in accounting from the Pennsylvania State University.

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Discussion Points

1. LIHTC Update Topics

   – Perspective on post 2017 tax reform
   – Operating in 2018
     - Is there Certainty in Today's Market?
     - Current Depth and Breadth of Market
     - Pricing
     - CRA versus Economic Investors / What does CRA get you?
     - Impact of Fannie Mae and Freddie Mac in the market
     - Structuring / Credit Trends

2. What should our audience be considering relative to LIHTC transactions in 2018?

Q&A – AskCitiCommunityCapital@citi.com

Q&A

Question: **On a typical 9% LIHTC tax credit backed deal (say $10 million), what would we typically be looking at as far as equity injection amount vs. leveraged loan?**

Greg V: At this point, I think this is still in a bit of flux as the market settles on pricing and will vary widely based on the specific deal structure (amount of soft money, sub debt, etc). It will also be influenced by whether State Agencies will allocate additional LIHTC to projects to help plug the equity gap that would otherwise result from the decline in tax rates.

Q&A

Question: **Can you go over the changes to depreciation? Are they choices/new elections or is 27.5 year no longer an option.**

Tom M**:** Going through all of the phase-outs and special rules would be quite detailed. Briefly, though, “qualified property” that previously qualified for 50% bonus depreciation now qualifies for 100% depreciation in the taxable year in which such property is placed in service. Generally, “qualified property” is depreciable property with a recovery period of 20 years or less (i.e., personal property and site improvements for LIHTC properties) that is placed in service after September 27, 2017 and prior to January 1, 2023.

The bonus depreciation is phased out for qualified property placed in service during 2023 through 2026. An additional change is bonus depreciation may now apply to property acquired by a taxpayer by purchase from an unrelated prior user. Bonus depreciation is the default; however, a taxpayer may elect out of bonus depreciation and use the standard MACRS depreciation. (The taxpayer may also elect to use the alternative depreciation system, as under prior law, but this will disqualify the property from bonus depreciation.)

Residential rental property retains its recovery period of 27.5 years. However, the alternative depreciation system cost recovery period for residential rental property was shortened from 40 years to 30 years for property placed in service after December 31, 2017. (The cost recovery and alternative depreciation system recovery period for nonresidential real property remains at 39 years and 40 years, respectively.) The Legislation also creates a new category of “qualified improvement property”, which is internal improvements to (but not enlargements of) existing nonresidential property, excluding elevators and internal structural framework. The intend was to provide such property with a cost recovery period of 15 years. However, the Legislation failed to assign this recovery period to qualified improvement property, so that will require a technical correction or other guidance from Treasury to fix.

Q&A

Question: **What is the potential pricing impact of 100% expensing? What items can be expensed?**

Tom M: As it relates to LIHTC properties, qualified property for which 100% bonus depreciation may be claimed is depreciable property with a recovery period of 20 years or less (i.e., personal property and site improvements for LIHTC properties) that is placed in service after September 27, 2017 and prior to January 1, 2023. Note, however, that bonus depreciation is not available for property subject to the alternative depreciation system under Code Section 168(g) (such as tax-exempt use property or property for which the taxpayer elects the alternative depreciation system). While this will help yield, most, if not all, new properties will need to make the election out of the business interest limitation, which will require the use of 30-year depreciation. While extending the depreciation period for the real property by 2.5 years will not significantly impact yield, it will cut against some of the benefit provided by the 100 bonus depreciation.

Question: **Are the proposals that were pending in Congress to expand the LIHTC program dead? Or is there a chance that those proposals could still come to fruition?**

Tom M: They are not dead. However, whether an appropriate vehicle can be found to attach the LIHTC program improvements legislation during 2018 remains to be seen. The industry lobbyists are meeting with folks on the Hill, though, pushing for this proposed legislation.

Question: **With the reduction in the federal tax rate, can we expect that state LIHTC be priced higher since the tax hit at the federal should be less?**

Tom M: Under prior law, with a 35% federal income tax rate, a dollar of state tax credit reduced the federal deduction by one dollar, yielding a net benefit of 65 cents. With a 21% rate, the net benefit is increased to 79 cents. Due to other pressures on pricing and yield, though, whether this will actually translate into higher prices being paid for state tax credits remains to be seen.

Q&A

Question: **How much a reduction in pricing for federal historic tax credits should developers expect?**

Tom M: At this point, I would think there is too much uncertainty about how the program will operate due to the fact that Congress was unclear in its drafting and failed to make conforming amendments. For example, the statute says that the historic tax credit must be claimed over the 5-year period beginning with the taxable year in which the building is placed in service "allocated ratably to each year during such period." Under prior law, 100% of the credit was claimed as of the date of placement in service. There is no guidance on what Congress meant by claiming ratably over the 5-year period. Does this mean 20% of the credit is claimed in the year of placement in service ad in each of the following four taxable years? Or, if the project is placed in service on, for example, July 1, does that mean only 10% is available in the year of placement in service and the balance in year 6? Is it allocated ratably on a daily basis? Monthly? Nobody knows – Treasury will need to provide guidance so that the timing of the credit can be determined and priced appropriately. Similarly, Congress made no changes to the provisions requiring a basis adjustment for the amount of the historic tax credit determined for the project. If the credit is claimed ratably over five years, does this mean that depreciable basis is similarly reduced over a 5-year period, or is it reduced by the full amount of the credit in the year of placement in service? (Administratively, this is clearly the simplest answer, and is not necessarily inconsistent with claiming the credit over a five-year period – the amount of the credit is still "determined" in year one.) Accordingly, until Treasury provides guidance on these issues (or, in the absence of such guidance, the historic tax credit bar gravitates towards a unified interpretation), it is difficult to pinpoint what the ultimate pricing impact will be.

Your Webinar Speakers

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Thank you for your participation!

- Your feedback is very important to us. Please go to the survey and let us know how we did. Survey – https://www.citibank.com/icg/homepage/forms/citi_community_capital/form.jsp
- Listen to the playback - https://www.citibank.com/icg/sa/citicommunitycapital/resource_center.html
- Our next Webinar is coming soon. More information to come! We look forward to having you join us!
- www.citicommunitycapital.com

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