



# FINANCING MIXED USE DEVELOPMENT- A SURVEY OF FINANCING SUBSIDIES

**CNU XIV**

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## FINANCING VEHICLES

- Conventional financing/ local banks etc.
- Federal Government
- Contemporary financiers
- Tax Credits



## TAX CREDITS

- Tax credit reduces income tax
- Some states have their own state tax credit
- Tax credits serve as a yield substitute instead of cash flow, or to boost yield to owners
- Tax credits are often sold to generate equity



## HISTORIC TAX CREDITS

### How Old Does the Building Have to Be?

- **Certified Historic Structure - 20% Credit**  
Age generally doesn't matter: building must be either in a historic district or listed (or eligible for listing) on the national register of historic places
- **Non-Historic Structure - 10% Credit**  
Age matters - location doesn't matter: building must have been originally used before 1936.



## 10% Credit

- Must satisfy exterior, interior and structural framework retention requirements
- May be no Parts I, II and III to file
- Multifamily rental property is **NOT** eligible for the 10% credit
- For-sale property is **NOT** eligible
- Commercial use does qualify
- Must have a minimum 5-year hold
- Credit is 10% of QREs



## 20% Credit

- Must file Parts I, II and III with State Officer and National Park Service - This is a Third-Party Architectural Review
- Multifamily property is eligible for the 20% credit
- For-sale property is **NOT** eligible
- Commercial use does qualify
- Must have a minimum 5-year hold
- Credit is 20% of QREs



## Calculating the Credit What is Not a QRE?

- Land & Interest Carry on Land
- Building Acquisition & Interest Carry on Acquisition
- Acquisition-Related Costs
- Site Improvements & Landscaping
- Enlargements & Demolition
- Personal Property
- Tax Exempt Use Property



## Limitations on Use of the Credit

- Passive loss rules
- At-risk rules
- Alternative minimum tax



## Who Can Claim the Credit?

### **Timing of Ownership is Critical**

- Owned during rehab & sold prior to placed in service = **CAN'T CLAIM**
- Bought into ownership just prior to and owned the day placed in service = **CAN CLAIM**
- Bought into ownership after placed in service = **CAN'T CLAIM**



## Downside of the Credit

# What is the Risk of Recapture?

- **Triggering Recapture**
  - Disposition of the Property
  - Disposition of at Least 1/3 Partnership Interest
  - Noncompliance with Secretary's Architectural Standards
- **Amount of Recapture**
  - 100% in the First 12 months from Placed in Service
  - Declines 20% Every 12 months thereafter



## Downside of Taking The Credit

- Potential for reduced depreciation
- Potential for additional rehab costs
- Architectural requirements may not meet needs of the market
- Potential third-party architectural review
- May require partners in ownership
- Transaction costs



## Façade Donations

- Charitable contribution (v. A tax credit) that is earned by placing **permanent** restrictions on an owner's ability to make changes
- What is it worth? Foregone value determined by an appraisal
- Be aware of inherent conflicts between historic credits and façade donations



## New Markets Tax Credit Program

- Another yield subsidy, in this case to encourage investment in businesses (and real estate) located in low-income census tracts.
- Enacted on December 21, 2000 as part of Community Renewal Tax Relief Act of 2000.
- Competitively allocated tax credits are used to induce equity capital into CDEs.



## KEY FACTS

- New Construction Can Qualify for New Markets Tax Credits, or
- Historic and New Markets Tax Credits *CAN* be combined
- Residential Rental Property **DOES NOT** qualify, that is, a mixed-use building that has commercial income that is less than 20% of total collections from all income sources **DOES NOT** qualify for New Markets Credits



## Process Overview For a Project Seeking NMTCs

Step 1: Determine that the project is in a qualified census tract

[cdfifund.gov](http://cdfifund.gov) or [ffiec.gov](http://ffiec.gov)

Step 2: Find a CDE that can serve this census tract

[cdfifund.gov](http://cdfifund.gov)

Step 3: Among these CDEs, find one that can make real estate investments (loans or equity)

Step 4: Discuss transaction with prospective CDEs to determine if there are unused NMTCs and gauge their interest

Step 5: Hire experienced advisors

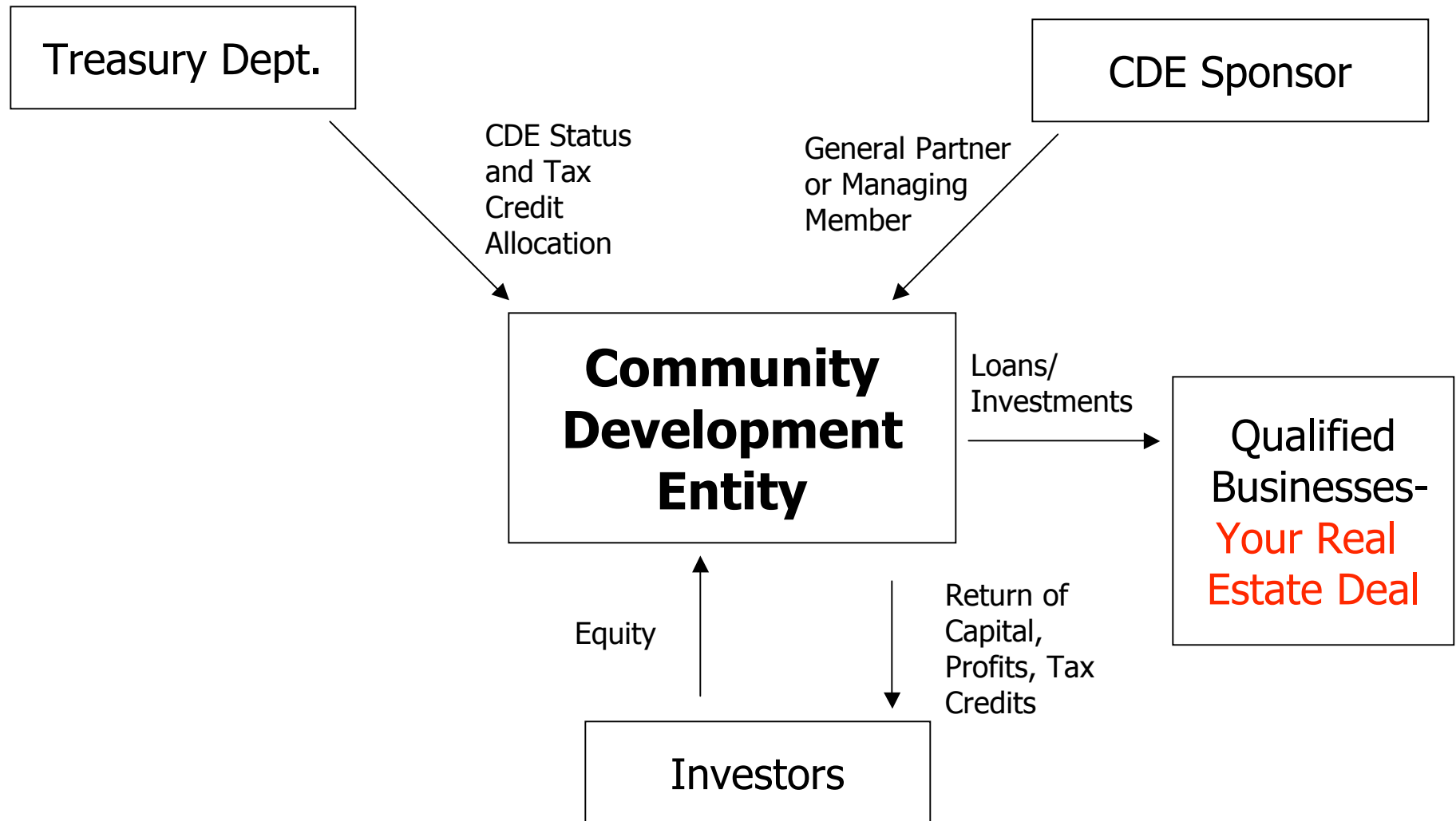


## The New Markets Credits is All About Location Location Location

- To qualify for New Markets Tax Credits, the property must be in a qualified census tract, which has:
  - Poverty rate of at least 20%, or
  - Median Income not more than 80% of Area Median Income
- Approximately 35-40% of the census tracts in the country qualify.



# How NMTC Programs Work





## DEBT PRODUCTS-HUD 221(d)4

### ■ PLUSSES

- Non Recourse construction and permanent loan
- 40 year amortization
- No balloon risk
- Automatic conversion to permanent, with no stabilization requirement

### ■ MINUSES

- Generally limited to commercial being 10% of space and 15% of income
- Slow closing
- Rates slightly higher than market
- Cost limits sometimes an issue
- Fees higher
- Mortgage can be lowered by cost limits



## DEBT PRODUCTS-HUD 220

- For projects in Urban Renewal Zones, projects can have an increased amount of commercial, up to 20% of space or 30% of income, otherwise with the same features as the 221(d)4 loan



## LOW INCOME HOUSING TAX CREDIT

- Another yield subsidy
- Applies to rental properties only
- Doled out by state agencies-somewhat limited availability
- Works in mixed-income buildings, but usually only in certain areas
- Highly regulatory and complex



## Green Building Credits

- State programs most prevalent
- Modest federal subsidy



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