

New Jersey Governor's Conference on Housing

"Is There Really an Investor Behind Your Tax
Credit Deal?"

September 29, 2010

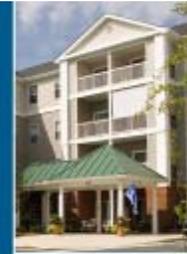


Leading with Ideas

DEMONSTRATING THROUGH ACTION

Transforming with Capital

SUSTAINING THROUGH POLICIES AND PARTNERSHIP



Enterprise



- LIHTC Syndication
 - \$10 billion under management
 - 1,700 projects, 100,000 units
- Multifamily Mortgage (FHA, Fannie Mae, RD 538)
- New Markets Tax Credits & Consulting
- Acquisition & Predevelopment Lending
- Development
- Green Communities Program

LIHTC Market Conditions



Today's Snapshot

- LIHTC industry volatility appears to be stabilizing
- “V” shaped pricing curve; high / low / high
 - Higher yields / new investors
- Areas of intense CRA need seeing highest pricing
- Investors resisting deterioration of terms – would rather pay higher price
- Pricing up but flight to quality remains largely in effect

LIHTC Market Conditions



In addition to location, the three focus areas are:

- Sponsorship
- Real Estate
- Underwriting

www.enterprisecommunity.org
www.enterprisecommunity.com





Tax Credits & the Elusive Investor

2010 Governor's Conference on
Housing and Community Development
September 28-29

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Role of Projections

- Allows developers to address potential problems
- Facilitates syndicator review
 - Optimum structure
 - Positive impression
 - Capital account issues
 - Good debt issues



Is There a Market for Bonds?

- Size
- Acquisition rehab vs. new
- Section 8 overhang
- Historic properties



Public Housing Revitalization

- Tax Exempt bonds for Construction
 - Federal Elements:
 - - Capital grant or replacement housing funds
 - - Section 8
 - - Section 9 subsidy (cannot fund debt service)
 - Debt Accumulation Issues
 -
 -
 -



Interface Solar into Transactions

- Calculating the credits
- Treasury program sunsets
- Basis reduction
 - How is it calculated?
 - Impact on 9% transactions
 - Impact on 4% transactions
 - Depreciation
- How a syndicator benefits
 - - First year credit to loss
 - - Impact on rate of return



Mixed Income

- **Most Difficult**
 - Concerns over market rents
 - Loss to credit ratios

- **Possible Solutions**
 - Master lease pass-through as a sale



Bank

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LIHTC Pricing, Market Dynamics, and Industry Issues

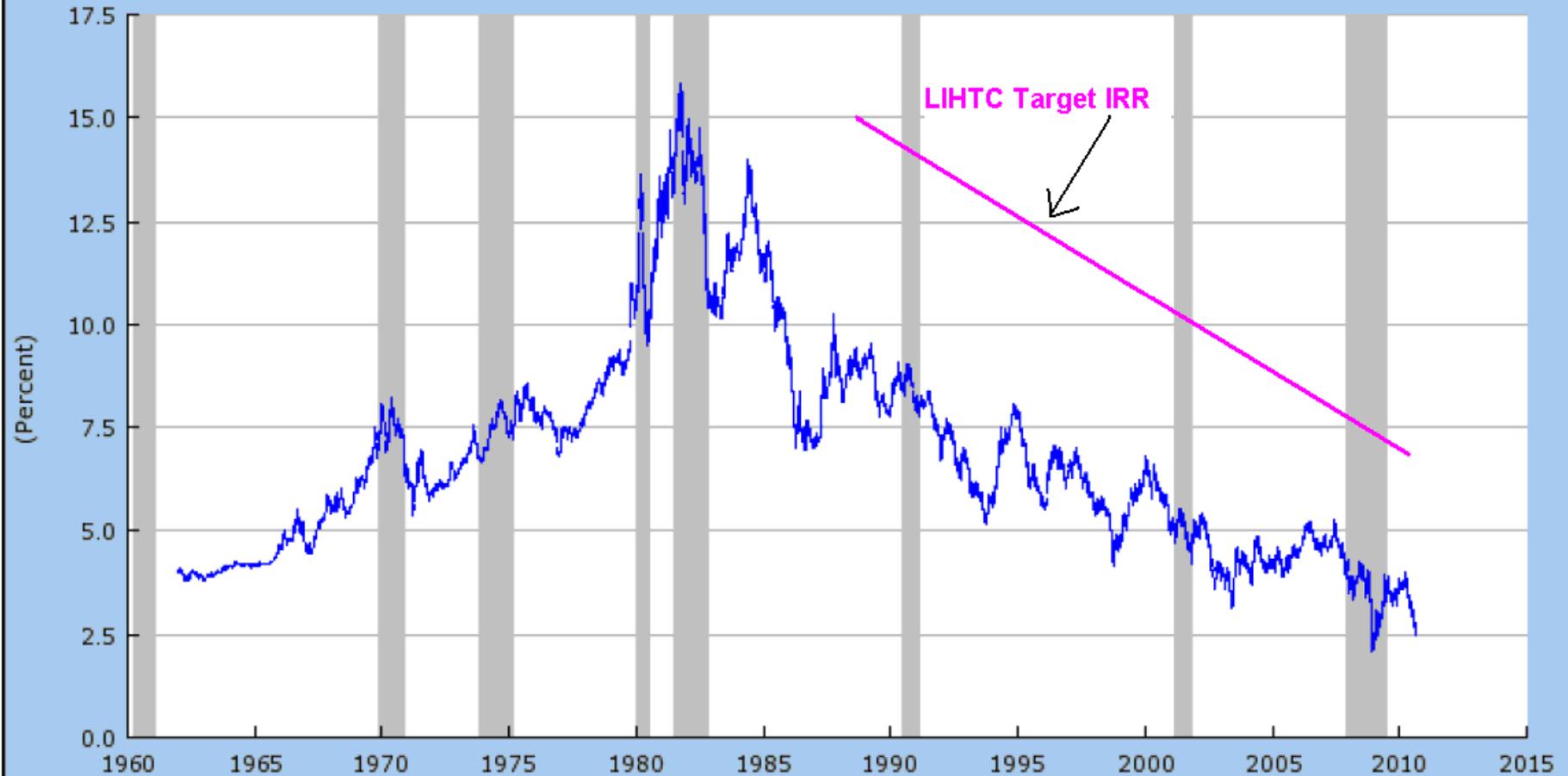
Mark McBride

TD Bank

Status of North American Banking Industry

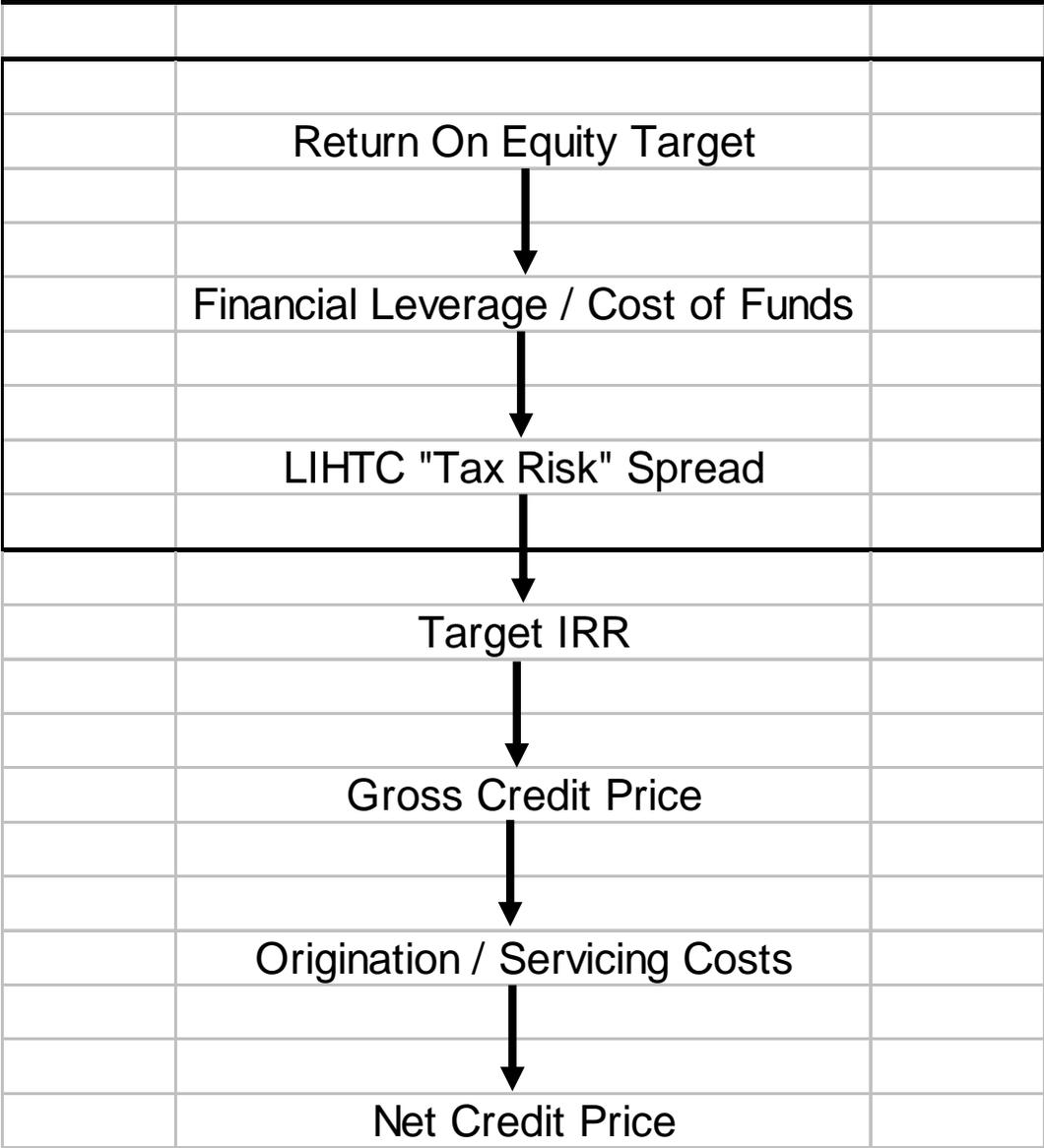
| <u>Ranked Size of Large Banks</u> | | | <u>Ranked Safety of Large Banks</u> | |
|---|--|---------------------------------|-------------------------------------|----------------------------|
| <u>Global Rank</u> | | <u>Total Assets (\$billion)</u> | <u>Global Rank</u> | |
| 6 | Bank of America | 2,223 | 10 | Royal Bank of Canada |
| 9 | JPMorgan Chase | 2,032 | 15 | Toronto-Dominion Bank |
| 10 | Citigroup | 1,857 | 22 | Scotiabank |
| 24 | Wells Fargo | 1,244 | 25 | Caisse centrale Desjardins |
| 30 | Goldman Sachs | 849 | 30 | BNY Mellon |
| 32 | Morgan Stanley | 772 | 36 | Bank of Montreal |
| 38 | Royal Bank of Canada | 608 | 37 | CIBC |
| 48 | Toronto-Dominion Bank | 517 | 40 | JPMorgan Chase |
| | | | 42 | Wells Fargo |
| | | | 47 | U.S. Bancorp |
| | | | 49 | Northern Trust |
| Combined assets of six largest US banks | | 8,977 | | |
| Market share of six largest US banks | | 68% | | |
| ● | <i>source: Global Finance Magazine, September 2010, Top 50 Global Banks</i> | | | |
| ● | <i>LIHTC activity is less than one tenth of a percent of total activity at these banks</i> | | | |
| ● | <i>The large US Banks will dominate LIHTC because of taxes and CRA</i> | | | |

10-Year Treasury Constant Maturity Rate (DGS10)
Source: Board of Governors of the Federal Reserve System



Shaded areas indicate US recessions.
2010 research.stlouisfed.org

Tax Credit Investor Pricing Model



Investor Return / Credit Price

| | Current Market |
|-----------------------------|---------------------------|
| Hurdle Rate | 7.00% |
| Tax Rate | <u>35%</u> |
| Hurdle Rate After-tax | 4.60% |
| LIHTC "Tax Risk" Spread | <u>2.40%</u> |
| Investor Required LIHTC IRR | 7.00% |
| Gross Credit Price | \$89.2 |
| Origination / Servicing | <u>10.0%</u> |
| Net Credit Price | \$80.3 |

Driving the Investment Decision

What Determines the "Tax Risk" Spread

- LIHTC is much less liquid than other securities also available to the investor.
- The impact of firm-wide operations on the ability to profit from LIHTC is very extreme; highly leveraged.
- The CFO has options, including:
 - invest in less "intrusive" tax-oriented investments.*
 - operate with higher leverage and avoid most taxes.*
 - buy a bank with loss-carryforward.*
 - just pay more taxes and keep things simple.*
- Overall economic climate; where are profits headed?
- Explicit or implicit federal support ("TBTF").
- Opportunity to cross-sell loans and deposits.
- Perceptions about underlying asset class performance.
- CRA enforcement and scope; impact of mergers.
- Supply and Demand equation.

| Investor Return / Credit Price | | | |
|---------------------------------------|--|----------------------|----------------------|
| | | Current | Weak |
| | | <u>Market</u> | <u>Market</u> |
| Hurdle Rate | | 7.00% | 8.00% |
| Tax Rate | | <u>35%</u> | <u>35%</u> |
| Hurdle Rate After-tax | | 4.60% | 5.20% |
| LIHTC "Tax Risk" Spread | | <u>2.40%</u> | <u>4.00%</u> |
| Investor Required LIHTC IRR | | 7.00% | 9.20% |
| Gross Credit Price | | \$89.2 | \$78.2 |
| Origination / Servicing | | <u>10.0%</u> | <u>10.0%</u> |
| Net Credit Price | | \$80.3 | \$70.3 |

| Investor Return / Credit Price | | | |
|---------------------------------------|----------------------|----------------------|--|
| | Current | Hot | |
| | <u>Market</u> | <u>Market</u> | |
| Hurdle Rate | 7.00% | 6.00% | |
| Tax Rate | <u>35%</u> | <u>35%</u> | |
| Hurdle Rate After-tax | 4.60% | 3.90% | |
| LIHTC "Tax Risk" Spread | <u>2.40%</u> | <u>1.30%</u> | |
| Investor Required LIHTC IRR | 7.00% | 5.20% | |
| Gross Credit Price | \$89.2 | \$100.5 | |
| Origination / Servicing | <u>10.0%</u> | <u>10.0%</u> | |
| Net Credit Price | \$80.3 | \$90.5 | |

Market Dynamics / Competition

How can the market remain healthy and fair?

- Investor Type: large bank, medium bank, insurer, non-financial.
- Multi-investor, proprietary or direct investment?
- Investor education is a priority; syndicators can diversify the investor base.
- Relationship; be sure to ask for "enough".
- Deal Characteristics and Terms
 - social impact*
 - reserves and coverage; should be "balanced"*
 - track record matters; but so does innovation*
 - focus on strong guarantors who are "in it for the long run"*
 - market study / demographics must tell the story*
 - keep politics (all types) out of the way*
 - it all comes down to "team synergy"*
- The US "taxpayer" is a stakeholder.
 - a 7% increase in the Credit Price creates another*
 - \$.5 billion in affordable housing annually.*

| | | | | | |
|---|--|-----------------------------------|---|--|--|
| | | Tax Credit Industry Issues | | | |
| | | | | | |
| | | | | | |
| FASB / SEC accounting rules are outdated | | | | | |
| | | | | | |
| | | ● | Asset is depreciated over ten years, resulting in a drop in pre-tax earnings. | | |
| | | ● | Credits are taken over ten years, resulting in a drop in federal tax obligation. | | |
| | | ● | The net result is favorable to the bottom line | | |
| | | ● | However, many performance benchmarks are based on pre-tax earnings. | | |
| | | ● | This accounting approach makes it difficult for firms to enter the asset class; difficult to get into the "budget". | | |
| | | ● | This accounting approach does not reflect how this assets class actually works; there are few "benefits to equity ownership. It is all about the tax benefits. | | |
| | | ● | FASB / SEC should change the rules so that all accounting is on the "tax line" in the income statement. Overall the Credit Price will increase; a savings to Uncle Sam. | | |

| | | | | | |
|---|--|----------------------------|--|--|--|
| | | Tax Credit Industry Issues | | | |
| | | | | | |
| | | | | | |
| <h2>CRA geo-targets are too narrow</h2> | | | | | |
| | | | | | |
| | | ● | CRA geo-target rules were written in 1977; community development needs and issues have changed. | | |
| | | ● | CRA Rules require that investment must map to location of deposits. This is an obvious mis-match. | | |
| | | ● | Large role of FNMA / FHLMC masked the problem. | | |
| | | ● | Today competition is too intense in "affluent" markets and too weak in other (non-metro) markets. | | |
| | | ● | AHIC has proposed a state-wide approach that banks can follow for CRA investments. | | |
| | | ● | Since the QAP is a measure of "need", full CRA credit should be provided so long as the bank operates somewhere in the state covered by the QAP. | | |
| | | ● | Federal regulators should change the "investment test" so that competition increases. Overall, the Credit Price will increase; a savings to Uncle Sam. | | |



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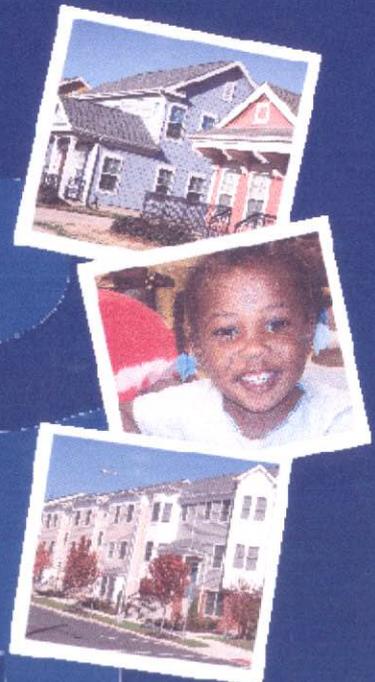
TD Bank

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Developing Solutions, Creating Value, Enhancing Lives

- Michaels Development Company
- Interstate Realty Management
- Michaels Military Housing
- Prestige Affordable Housing Equity Partners
- Prestige Renovations
- Continental Mortgage Corp.





Michaels Development Company

Joel Silver, Esq., Regional Vice President



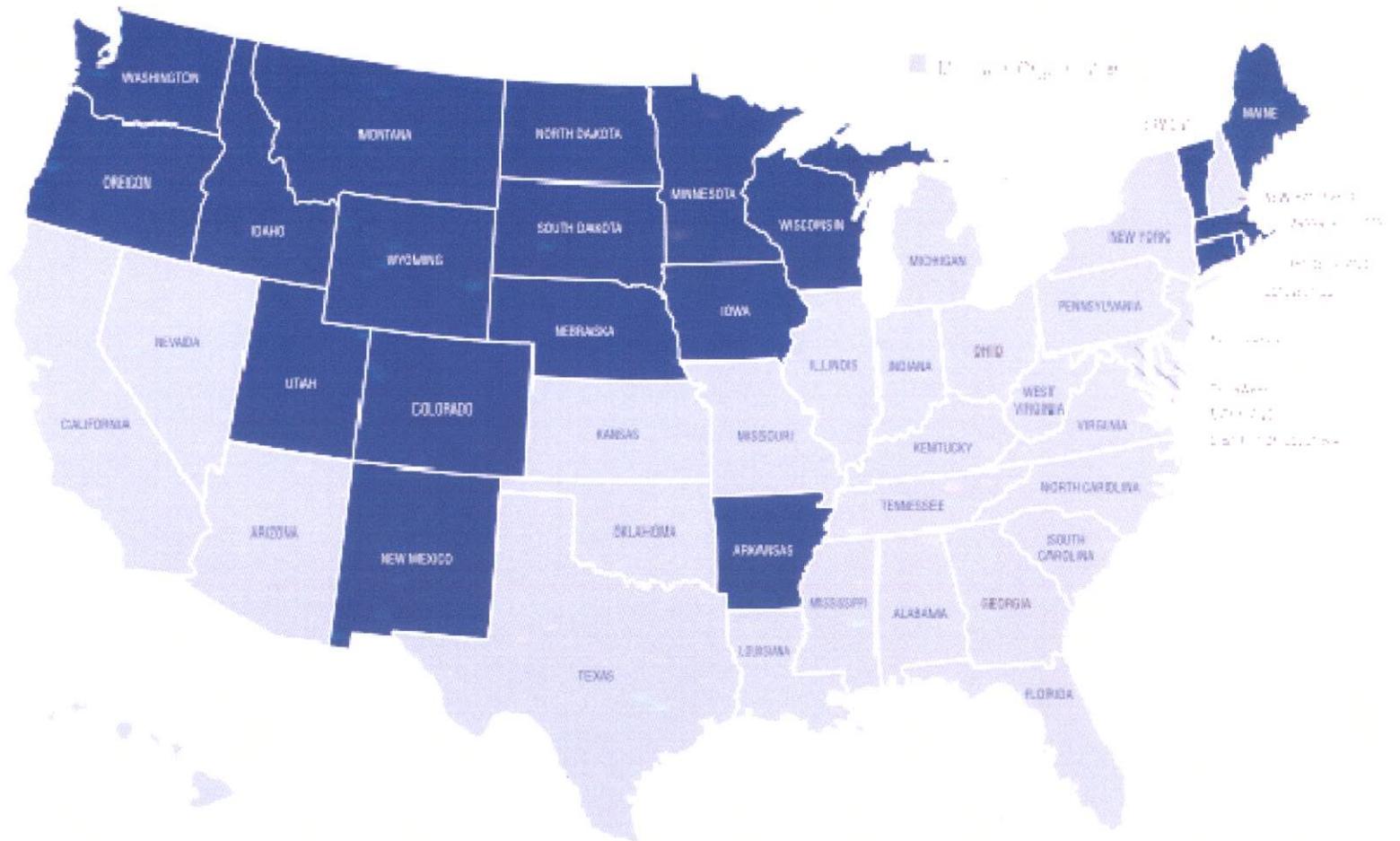
MDC Executive Leadership

- 45,000 units in 29 states, D.C. and the U.S. Virgin Islands.
- 100+ communities affordable to lower income families and seniors through project-based Section 8 and similar federal assistance
- 70+ communities affordable to working families through the low income housing tax credit program.
- 20 HOPE VI projects, representing an investment exceeding \$1.5 billion.

➤ No. 1 Affordable Housing Developer in the U.S., 2006-2010



National Strength, Local Expertise



The Michaels Organization is currently in 29 states, D.C., and the U.S. Virgin Islands





Resources for Long-term Success



Michaels Development Company



Our Goals:

- Create housing opportunities for families of all income levels
- Create sustainable, environmentally thoughtful new developments that are knitted into the fabric of the greater community
- Create communities that are financially self-sustaining



Neighborhood Revitalization/Mixed Income Community: A Case Study in Success in NJ

“Barbara Place beautifully realizes the goals of the HOPE VI program, which is a truly mixed-income community.”

--Joan Pollack, Development Director, NJMFA



Smart Growth
Award Winner!

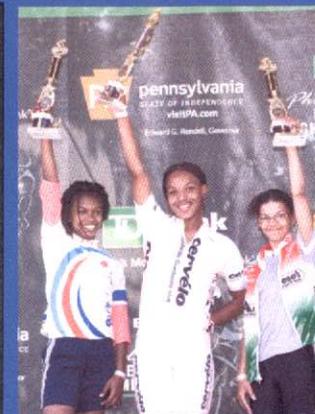


Managing for Lasting Value

Montgomery Townhouses – Philadelphia

“An Oasis in the City”

- The Michaels Organization has owned and managed for over 25 years
- Full slate of supportive social services, active community groups, and hub of activity for the wider neighborhood
- Physical maintenance of the property has been hailed as an example of excellence



➤ HUD Best Practices Award: “Best Neighborhood Network Center” in the country



Prestige Affordable Housing Equity Partners LLC

The Michaels Organization's In-house Tax Credit Syndication Company

We Reach Our Goals by Helping Investors Reach their Goals

- Cultivate long-term relationships with our investors
- Driven by the goal to provide equity to build or rehabilitate only the best quality affordable housing in the country and to provide safe and decent housing to all of the residents in whose communities we have invested.
- Focused on long-term value creation that help our investors reach their goals.

Prestige Affordable Housing Equity Partners services over 5,000 investors.

Proven Track Record

Total Equity Placed: \$252,020,000

8,457 UNITS

**Low- Income Housing Tax Credits*

BARBARA PLACE JERSEY CITY, N.J. \$13,000,000 *
BARLINVIS APTS ATLANTIC CITY, N.J. \$400,000
BENTLEYVILLE APTS BENTLEYVILLE, PA \$900,000
BROOM (TERRY) WILMINGTON, DE. \$2,000,000
CANEBRAKE ASSOCIATES FREDRICKSTED, ST. CROIX, V.I. \$1,000,000
CENTERVILLE SOUTH CAMDEN, N.J. 17,100,000 *
CLARIDGE (FILBERN MANOR) WEST NEWTON, PA. \$250,000
CRESTBURY APTS CAMDEN, N.J. \$ 1,400,000
CUMBERLAND (MALLARD RUN) CAMP HILL, PA. \$750,000
DWIGHT STREET JERSEY CITY, N.J. 10,570,000 *
EAST I PRESERVATION ATLANTIC CITY, N.J. \$1,600,000 *
GARRISON WOODS STAFFORD, VA. \$1,550,000
GLOUCESTER ELDERLY GLOUCESTER CITY, NJ \$3,500,000 *
HAGERSTOWN (ELIZABETH CT) HAGERSTOWN, MD. \$1,650,000
HARBISON (WOODS EDGE) COLUMBIA, S.C. \$1,600,000
HUNTINGTON (ADAMS LANDING) HUNTINGTON, W.V. \$500,000
LEGENDS SOUTH A-2 CHICAGO, IL. 30,100,000 *
LEHIGHTON ELDERLY LEHIGHTON, PA. \$800,000
LIVING SPRINGS DELANCO, NJ \$14,100,000

MT. SINAI PHILADELPHIA, PA. \$2,500,000 *
NIA APTS. (NIA ASSOCIATES) BRIDGETON, N.J. \$2,000,000
NORTHBRIDGE COURTS MONCK'S CORNER, S.C. \$1,100,000
NORTHLAND (COLONY NORTH) ST. LOUIS, MO. \$1,300,000
OCEAN MANOR (WATERSIDE) ATLANTIC CITY, N.J. \$2,600,000
OCEAN TOWERS JERSEY CITY, N.J. \$1,700,000
PARK SPRING SPRING CITY, PA. \$950,000
PINECREST MT. KISCO, N.Y. \$1,700,000
PLUMLEY VILLAGE WORCESTER, MA. \$13,200,000 *
ROOSEVELT GARDENS JACKSONVILLE, FL. \$1,500,000
ROSTRAVER APTS. BELLE VERNON, PA. \$950,000
ROWAN TOWERS (NIA ASSOCIATES) TRENTON, N.J. \$1,950,000
SCRANTON (VILLAGE PARK) SCRANTON, PA. \$900,000
SHARSWOOD APARTMENTS PHILADELPHIA, PA. \$8,000,000 *
SHARSWOOD APARTMENTS II PHILADELPHIA, PA. 12,000,000 *
SHERWIN WILLIAMS FUND MISSISSIPPI & ALABAMA \$8,000,000 *
SIMPSON (HUNTER'S RIDGE) BROWNSVILLE, PA. \$550,000
SOUTH PARK (PARKFORD APTS) LIBRARY, PA. \$2,450,000

SPRING GARDEN PHASE II PHILADELPHIA,
\$10,500,000 in Low Income Tax Credits





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The Michaels Organization's In-house Tax Credit Syndication Company

Discussion of Michaels View of the Equity Market

There is a wide disparity between markets

Financial institutions are paying premiums for Projects for which they will receive CRA credit when compared to Projects that do not impact the institution's compliance with the Community Reinvestment Act.

Expectations regarding investor yield are dropping in New York City and other prime markets in the United States.

The disparity between North and South Jersey continues

The preference for developments funded with 9% LIHTC relative to developments funded with 4% LIHTC is becoming less pronounced.