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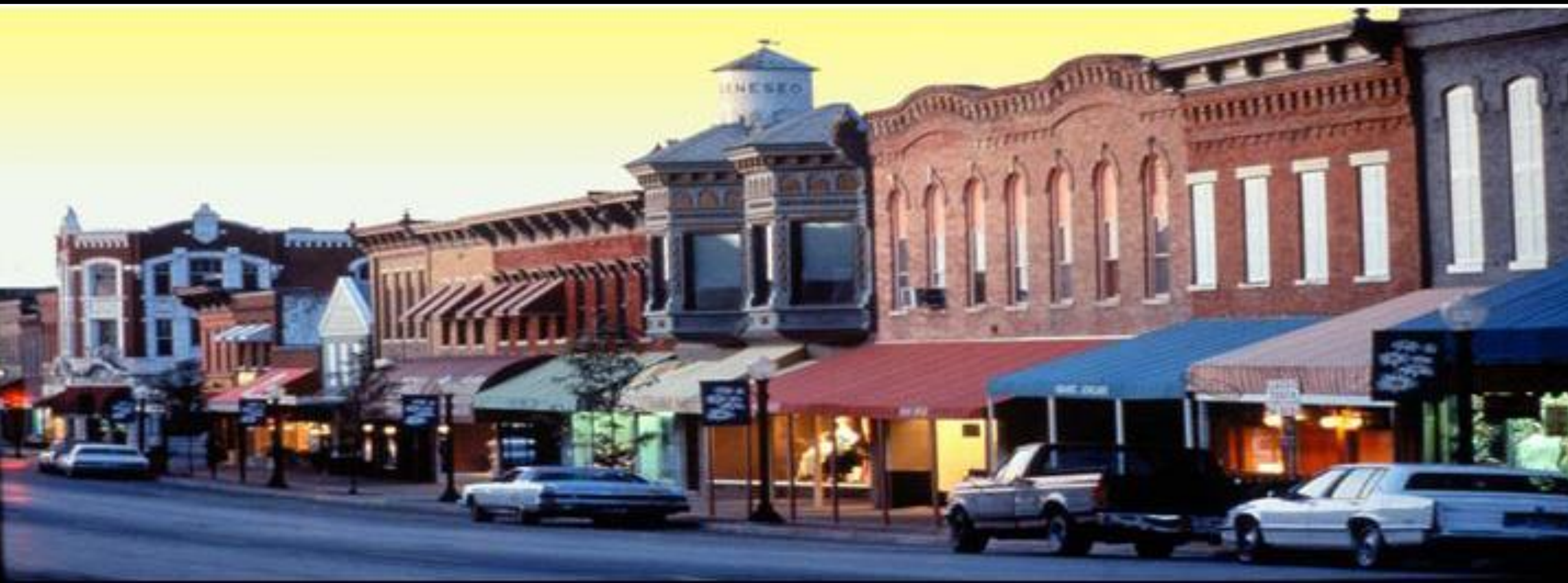


2005 NALHFA Spring Conference

New Markets Tax Credits
And Affordable Housing

Common Misunderstandings About New Markets Tax Credits

- Commercial real estate development is the best use of NMTCs.
- NMTCs cannot be used to finance multifamily housing.
- NMTCs and LIHTCs are mutually exclusive tax credits.
- Using NMTCs in for-sale housing projects is a prescription for recapture.

Questions to Consider

- Does the business the CDE will be lending to or investing in qualify as a QALICB?
  - Restrictions on residential rental property.
- What are the statutory or regulatory prohibitions regarding low-income housing?
  - Restrictions on use with LIHTCs.
- What concerns are there about NMTC compliance?
  - Reinvestment risk.

Four Common Ways to Finance Housing with NMTCs

1) "Mixed-use" developments
   - 20% or more commercial revenue
   - Potentially in combination with LIHTC
2) Developers of residential rental property (including LIHTC)
3) For-sale housing
4) In combination with other subsidies
   - Historic Tax Credits
   - Other "soft" financing

(1) “Mixed-Use” Developments

- QALICBs must be engaged in the active conduct of a qualified business.
- **Rental** of real estate qualifies only if the property is <u>not</u> depreciable as residential real estate and there are substantial improvements on the property.
- Residential real estate is defined in section 168(e)(2)(A) of the Code as “any building or structure if <u>80 percent</u> or more of the gross rental income from such building or structure is rental income from dwelling units.”

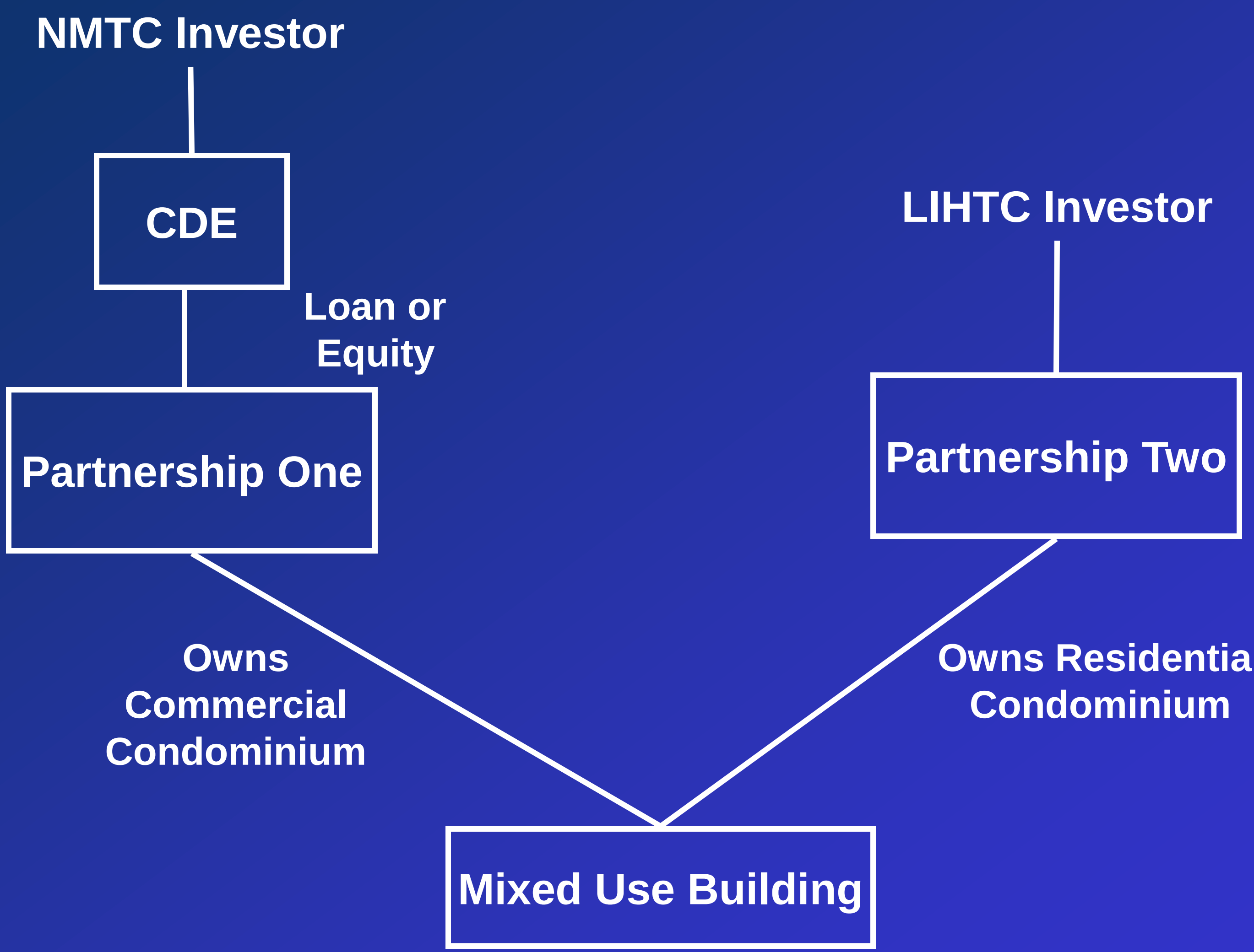
“Mixed-Use” (cont’d)

- Mixed-Use must have less than 80% of income from rental housing plus 20% or more of income from:
  - Office space
  - Retail
  - Other commercial space

Can Mixed Use Projects Combine NMTCs and LIHTCs?

- Generally speaking, not allowed
  - CDE's loan/investment will not be a QLICI to the extent it finances building's eligible basis under Section 42(d)
- Solutions
  - Use condominium structure
  - Finance non eligible basis items

Condo Structure: NMTCs and LIHTCs



NMTCs and LIHTC: Eligible Basis

- NMTCs cannot finance eligible basis items
- Can finance
  - Land
  - Infrastructure/sitework
  - Commercial portion of building
- Importance of tracing funds, no cross-collateralizing, no cross-defaults

Multiple Buildings and “Part of a Business” Rule

- CDE may treat any trade or business (or portion thereof) as a QALICB if it would meet the QALICB requirements if separately incorporated
  - Must maintain separate books and records.
  - Typical example – grocery store
- Multiple buildings, commercial and residential

(2) NMTCs Financing Housing Developers

- Developers of housing may qualify as QALICBs
- Must ensure all QALICB tests are met, including:
  - Tangible property test
  - Gross income test
  - Employee Test
- Beware of developers who own the property
- Reinvestment risk

(3) NMTCs and For-Sale Housing

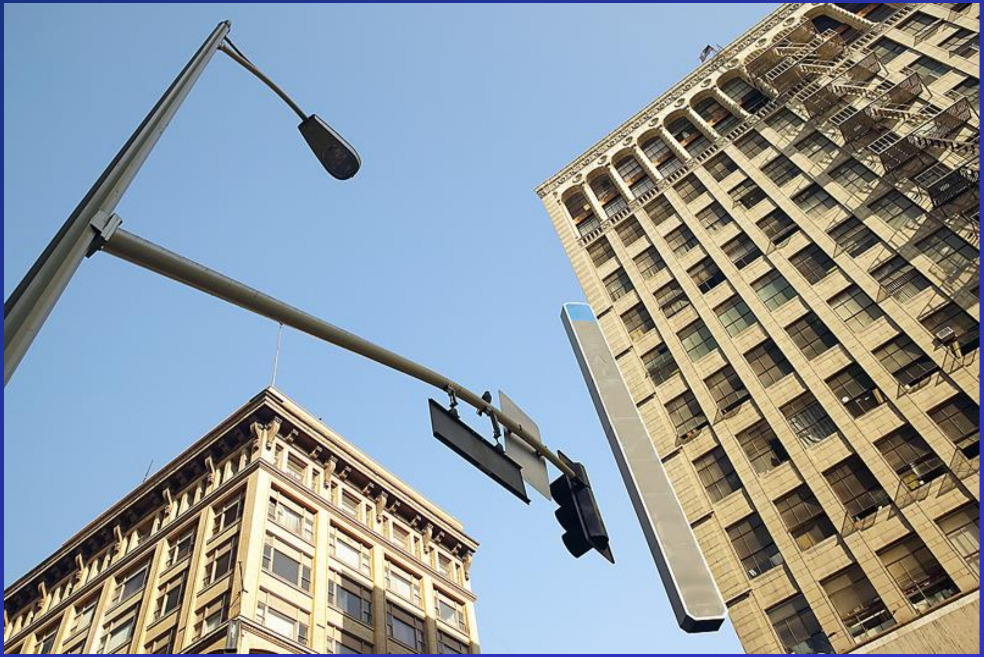
- QALICBs can include developers of for-sale housing
- No requirements for low-income residents
- Concerns include reinvestment risk
- Better suited for phased projects where sales proceeds can be recycled into subsequent phase of development.

(4) Sources of Financing HTCs as Other Subsidy

- NMTCs can be paired with HTCs
- Other housing sources as leverage
  - CDBG
  - HUD 108
  - Tax-exempt bonds
  - Tax Increment Financing

Other Possibilities

- Live/Work space
  - NMTCs finance commercial portion of apartment



More Information?

Merrill Hoopengardner

401 9th Street, NW

Suite 900

Washington, DC 20004

202.585.8169

202.585.8080 (Fax)

mhoopengardner@nixonpeabody.com

NIXON PEABODY LLP