VIRGINIA ECONOMIC DEVELOPMENT PARTNERSHIP
THIRD WEDNESDAY WEBINAR

NEW MARKETS TAX CREDITS AND DEAL STRUCTURING

WEDNESDAY, March 18, 2015
2:00 P.M. - 3:05 P.M.

HOSTED BY:

BRENT SHEFFLER

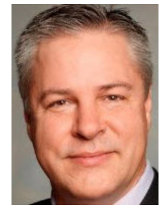
VIRGINIA ECONOMIC DEVELOPMENT PARTNERSHIP

901 EAST BYRD STREET

RICHMOND, VIRGINIA 23218

TELEPHONE: 804.545.5742

EMAIL: BSHEFFLER@YESVIRGINIA.ORG



PRESENTERS:

HOWARD GORDON, ESQUIRE

WILLIAMS MULLEN

DAWN DEHART, SENIOR VICE PRESIDENT

VIGINIA COMMUNITY CAPITAL INCORPORATED

Q & A SEGMENT:

CONNIE LONG

VIRGINIA ECONOMIC DEVELOPERS ASSOCIATION

INDEX

EXHIBITS

THIRD WEDNESDAY WEBINAR

WEDNESDAY, MARCH 18, 2015

2:00 P.M.

BRENT SHEFFLER: Hello everyone. Welcome to the Virginia Economic Department Partnerships Third Wednesday Webinar. Thank you for joining us today. Today is the 18th day of March, 2015. This third Wednesday Webinar is the third in our 2015 series and its titled "New Markets Tax Credits and Deal Structuring." We expect today's session to run a little over one hour.

My name is Brent Sheffler. I serve as Managing Director of Knowledge Transfer and Strategic Outreach on the Business Expansion division at the Virginia Economic Development Partnership. At the controls is Connie Long with the Virginia Economic Developer's Association, also known as VEDA. Connie is managing the dashboard and will moderate the Q and A part of today's webinar. The Virginia Economic Development Partnership is collaborating with Virginia Community Capital and Williams Mullen to present today's webinar.

In just a minute I will introduce our program for today, but before I do, I'd like to provide our listeners with a bit of webinar housekeeping. Those of you attending this webinar are in listen only mode for the duration of the program. Your mics and your telephones have been muted. We can't hear you but we can read what you write in the question panel. Usually this question panel is located in the upper right of your screen. We are taking questions and we want this webinar to be interactive. Those of you who have screens on their desktop, your laptop or your mobile device are invited to type your questions in the question panel window on your GoToWebinar dashboard at any time during the session. Connie Long is able to read the question submitted and communicate those questions to us as we proceed through today's session. Again, we want this to be interactive so please go ahead and drop a question in the question panel if you have one.

Several of our listeners ask us how can they receive a copy of the presentation. This session is being recorded. After we close today's session we will post the recorded webinar on the virginiaallies.org website. If you missed any of the webinars conducted so far in this year or like to revisit any of the sessions we held last year, you're invited to do to the virginiaallies.org website where each webinar conducted so far has been posted and is made available to you.

After we end today's session and once you've closed GoToWebinar you'll receive an e-mail with a few survey questions. This survey should arrive in your e-mail within 24 hours after the close of today's webinar. We encourage you to take a minute to respond to this survey and give us your feedback. This will help us to improve and to plan for future webinars.

Our Third Wednesday Webinars are part of the Virginia Economic Department Partnerships Ally Communication Strategy. The webinars we held in 2013, 2014, and the webinars we're showcasing this year are designed to being subject matter experts to address topics that are important to you and to share knowledge about available resources. It's our objective to keep you, our Virginia allies and partners well informed so that we can collectively accomplish our mission and to realize your economic development goals.

For those of you just not joining us, our topic today is titled "New Markets Tax Credits and Deal Structuring." Our speakers today are Dawn DeHart, with Virginia Community Capital and Howard Gordon, with Williams Mullen. What we plan to cover today are a number of items that we believe are important to you. Our speakers will share what new markets tax credits are all about. What a community development financial institution is. How will locality be determined. If it meets CDFI's definition of a low-income community, LIC. You'll also hear about what roles economic developers and local organizations can play. What are the pros and cons that should be considered before purposing new markets tax credits and where economic developers and community leaders can go for more information.

Our first speaker is Howard Gordon. Howard Gordon is Partner with Williams Mullen, a major law firm that has more than 200 attorneys, with ten offices in Washington D.C., Virginia, and North Carolina. Mr. Gordon's practice is focused on commercial and multi-family real estate, commercial leases, ground leases, land use planning, and permits and past-through entities. His experience includes representing owners and developers in the acquisition of land, development leasing, and financing of numerous shopping centers and multi-family housing projects as well as hotels and development of a traditional neighborhood. He also has represented borrowers in the closing of conventional FHA insured conduit and specialty loans secured by commercial and multi-family properties.

Mr. Gordon has represented developers of hotels which have used new market tax credits to reduce the equity required for development. Mr. Gordon is a fellow of American Bar Foundation, Virginia Law Foundation, and the American College of Real Estate Lawyers. He's a recipient of the Virginia State Bar's Travers Scholar award and listed in Best Lawyers in America and Virginia Business Magazine's legal elite among real estate practitioners. Additionally, Mr. Gordon has been made a super lawyer for real estate by Virginia Super Lawyers Magazine and in 2012 was recognized by that publication as a top 100 lawyer in Virginia. Martindale Hubbell has rated Mr. Gordon an AV attorney, its highest rating available.

Before joining the firm, Mr. Gordon was a partner with Hofheimer Nusbaum, PC, which merged with Williams Mullen in 2004. Mr. Gordon also served as law clerk to John A. MacKenzie, Judge of the U.S. District Court Eastern District of Virginia from 1972 to 1973. Mr. Gordon received his law degree from the University of Virginia School of Law and a bachelor of arts degree in economics from the University of

Virginia. Please join me in welcoming Howard Gordon.

Following Howard Gordon, you will hear from Dawn DeHart. Many in our audience know that Dawn DeHart served as a panelist during the third Wednesday webinar series in 2014, on the topic of Virginia Community Capital. She's back with us by popular demand. Dawn DeHart serves as Senior Vice President, Senior Loan Officer with Virginia Community Capital. Dawn's primary role with the organization is to make commercial loans at align with the Virginia Community Capital community development mission. Dawn has been with the Virginia Community Capital for eight and a half years.

Ms. DeHart works with small business owners, economic development, and government officials, housing authorities, and real estate developers and she has developed expertise in the new markets tax credit program to facilitate economic development goals. Dawn has worked in the banking finance sector for over 30 years and has worked for Bank of Virginia, Dominion First Union, and Crestar Suntrust. Prior to joining VCC in 2006, Ms. DeHart invested eight and a half years working as a loan officer with Business Finance Group where she made business loans under the SBA 504 program. Dawn holds a finance degree from Virginia Tech. Please join me in welcoming Dawn DeHart.

Now, for a moment I will go back to Howard Gordon and Howard your slide is up first, so please go ahead.

MR. GORDON: All right. Good afternoon everybody. I'm glad to be here with you. I'm going to lead off and go through some of the more technical side of the program and some of the background as to the definitions and the like. And Dawn is going to get us involved in the more practical side of the program.

So, as you can see on the slide the new markets tax credits program was signed into law by President Clinton in December of 2000. The real purpose of it is to generate private investment economic development in both urban and rural, what are defined as low-income communities. Since the inception of the program in excess of $30 billion of credit has been authorized and allocated out to various projects within those communities.

As I mentioned in order to understand the structure of the new markets tax credit deal, loan, equity, whatever phrase we want to use for it because it's really sort of a combination of both.

There's some magic or buzzwords that we really need to have a little bit of familiarity with. When this first one, I've got the acronyms, the words the CDE being a community development entity. Your CDFI, community development financial institution fund. LIC, being your low-income communities. QEI, the qualified equity investments. And the QALICB, is the way I think they pronounce it, as a qualified active low-income community business.

And as we flip to the next slide. It runs through the definitions really of those particular phrases. A community development entity, the CDE, can be a domestic corporation or partnership. Obviously for all of the discussions today where I use the word partnership it includes limited liability companies because for tax purposes they're the same. The mission of the community development entity is to secure provide investment capital, again, to these low-income communities and the low-income persons who live within those communities. In order to be a CDE you have to be certified as a qualified community development entity. And in essence the role of the CDE is that it serves as the vehicle to provide the loans or investments in the low-income communities. So, they sort of the keepers of the allocations of the credits and weigh those projects.

The community development financial institution fund was created by Congress to administer the new market tax credits program that through the department of the treasury. That's the entity which really sort of has control of the credit and allocates the credits out to qualifying CDE's. So, you've got the financial institutions fund that's sort of the governments side that says we've got X numbers of dollars of credits. The CDE's make application and say we've got projects or we want to utilize, say three million, five million, pick a number, of those credits within our community. And then they allocate, award the credits really to the community development entity which then allocates the credits out to particular projects.

Your low-income communities, in order to qualify as a low-income community you go by eligible census tracks. So, it's not the whole city, the whole area, the whole county. It's broken down by eligible census tracks. You qualify as an eligible census track, say that fast a lot of times. An eligible census track, if the poverty rate for that track that at least 20 percent of the residence of that census track are below the poverty level. The other definition is that the median family income within the particular census track does not exceed 80 percent of the area median family income adjusted for family size within the census track. There's a slight difference as to how you do that 80 percent comparison if you're in a metropolitan versus a non-metropolitan track.

All right, the qualified equity investments. I think you skipped a slide, there we go.

You're qualified equity investments basically is the equity investment, the stock in a corporation, a capital interest in a partnership in a CDE. The equity investment must be acquired by the investor at its original issue solely in exchange for cash and it must be designated by the CDE as a qualified equity investment. So, you've got your investor, your third party who wants to utilize the credits making that equity investment capital contribution into the QEI.

The next one on the list is this qualified active low-income community business and that's really your developer entity. That's the corporation or partnership that's engaged in the act of conduct of a qualified business within your qualified census track. In order to be a qualified business at least 50 percent of its gross income is earned in the low-income community. At least 40 percent or substantial portion of its properties owned or leased in that community and at least 50 percent of the services are performed in that community. That may sound like a difficult threshold but in reality you windup creating a single purpose or special purpose entity that just takes on this particular project so it's located within the community. In essence, again, if it's an operating business most of its income, again, is going to come from within that community and its going to own property within that community. So, again, the single purpose or special purpose entity makes those requirements not too difficult to meet.

And then there's another word that you'll hear and we'll go through which is the QUALICI, the qualici, which is the loan or the investment that the CDE makes into the QALICB. So, if you weren't confused before I'm sure you are now. But, anyhow, your QALICB is the developer, the person who is going to do the project.

And the next slide.

On how, again, your CDFI the fund allocates the new market tax credits authority to your community development entity, your CDE, and that's a competitive application process. So, Dawn's CDE, again, can apply and say we thing we can utilize and deploy so many dollars of the credits. And again, depending how many credits are available and how many other applicants there are that that's that allocation process.

Then once her entity has her allocation then the CDE decides which programs it's going to underwrite or assist by providing the credits to. So, they create a CDE or a Sub-CDE. The investor, again, the people who can utilize the tax credits, make a cash investment in exchange for the equity or capital. They earn the tax credits on the investment and that's your QALICB, the investment itself.

The CDE's use these proceeds to make loans or equity investments in real estate projects, community facilities, or businesses operating in a low-income community. And those businesses, that's your QUALICI, that's your qualified low-income community investment. Again, the investments are targeted toward commercial, industrial, mixed-use businesses. You can't use the credit for strictly residential. An apartment property will not qualify. Hotels are okay. Mixed-use are okay, as long as your residential component is not over, I think, 80 percent of the income. Some of the unique things that the tax credits can be used for though are timber foresting or harvesting. I think here one was done a local dry dock. They used new market tax credits to help finance that project.

Again, just by way of background the amount of the credit is 39 percent of the qualified equity investment. And the credits determined based on the cash investment to acquire the capital interest at the issuance in the qualifying community development entity. Again, these are tongue twisters to go through. Again, formed for that specific purpose, to make that qualified low-income investment. Typically the QUALICI is a, you know, a subordinate or discounted loan to the business that's going forward. The QEI may include borrowed money and we'll talk about the leverage model. I'll mention it and then Dawn will run though one in more detail.

So, again, if the investor puts in so many dollars they get credits, that's qualified equity investment. But the QEI, the entity, can also borrow the money, use that money for the project. That also counts as a qualified equity investment. So, you windup leveraging up and obtaining credits when a larger number then just the amount put in by the equity investor.

The timing of the credit, the first three years from the startup of the project, the tax credit is five percent of the qualified equity investment. And then for the following four years its six percent of the qualified investment credit and that's how you get to that total of 39 percent of the qualified equity investment. And just again for clarification we're talking about a tax credit here, not a deduction. So, it's a dollar for dollar credit.

If a corporation has $1,000 of income tax it has to pay and it gets a $1,000 credit, its tax liability would be wiped out. So, it's a dollar for dollar credit. So, it's more bang for the buck then just a deduction would be, like a depreciation deduction or charitable deduction or whatever other deductions you can think of. Again, it's a dollar for dollar credit against income taxes which are otherwise payable.

The specific restrictions, again, the borrower must reasonably be expected to satisfy the QALICB status throughout the tax credit recapture period. Which means operate the business within the community and so on. Again, there are five tests for

QALICB status, you know, the gross income test, the use of the property, the services performed, the collectables test, and non-qualified property test. So, we talked about this briefly above.

Recapture, that's the big gorilla if you will, because if you stub your toe part way through your seven year tax credit compliance period the credits get completely recaptured. It's as if the credit was never awarded to the investor. It's recaptured, the full amount is recaptured with interest, again, retroactively as if the credit had never been claimed. Because of the recapture and the seven year period there also some things to think about or structuring points that go into the avoidance of the recapture. If a loan goes into default then the credits can be recaptured.

So, again, the avoidance of the credit is basic to the program. So, some of those requirements the loan must be interest only and that's both the qualified equity investment that comes from the investor but also if you've got third party debt that's got to be interest only for the full seven year compliance period. In order to avoid an acceleration or default under these things typically within your documentation you'll have what we call a stand still period, where the lender agrees we'll stand still for some period of time until the QALICB developer can figure out a way to get us out of the box, so that there's not going to be a default. Because of the risk of recapture is paramount to the tax credit investor we've seen transaction where that tax credit investor in essence will come in and guarantee the loan of the real lender so that there, again, there's really no chance of a default during the seven year credit period. And again the length of the loans and the typical loans are, you know, a lot of them are structured as seven year loans and then at the end of the recapture period the properties are refinanced.

The next slide is a lot of text and a little bit hard to describe. So, I'll run through it quickly because the slide that follows will make these words I think a lot clearer. And, again, I'm going to sort of look at it from the upper level and Dawn is going to get into it from the lower and more practical level.

But, basically most of the new market tax credits deals are a leveraged transaction. So, you've got your limited liability company or borrower, being formed by the investor to borrow the leveraged loan which is the combination of the tax credit equity and your third party debt. And, again, in some situations where you've got banks involved in the transactions, the bank may have an allocation of the new markets tax credits and it may also be the lender on a more conventional type loan, but they at that point have more control over the transaction. Again, the CDE is typically an LL say formed as a Sub-CDE for the entity that controls the spigot of the tax credits. That CDE, you know, receives a .01 percent, so that the investor who's putting the money in in exchange for the credits gets the tax benefit of 99.99 percent of the tax credits.

The loans, the A loan being your more conventional loan, the B loan being your tax credit investors money goes to your developer, the QALICB. And that loan represents the economic investment in the B, that's the amount on which the credits are based.

At the end of the recapture period the QALICB will generally buyout the interest of the investor or the CDE will buy them out for a minimal amount of money, and we'll talk about that briefly on the next slide. Again, this is, I call this the funnel truck, the first time I got exposed to this thing and I saw that sort of the money coming in at the top and the money dropping out at the bottom to the borrower. I just said this is the funnel truck.

So, at the top right you got your new market tax credits equity investor who's putting in, we'll call it equity for purposes of the example. And that's their money, it winds up being debt by the time it goes through the funnel. At the top left is the bank or other debt. That's your real loan, that's your typical conventional loan. On conventional loan terms they can be a seven year loan, they can be long term money or whatever.

I'd say those two sources of funds become the funding of your investment fund, your conduit LLC or LLP. That money is then contributed as equity into your CDE. So, you then have the funds merge, I guess is a good a word as any, into the CDE. The senior CDE, the entity that put the deal together, generally pulls a fee out from that CDE for the placement of the loan and then from the CDE down to your QALICB is your debt. That basically has the seven year term to it. I'd say that's the quick view of that. Again, we're going to save time for Dawn to go through it in more detail.

The one comment I'd make instead of the last bullet point on the slide, where at the end of the seven year compliance period, the $7 million notice repaid or refinance and the 2.5 million here, 2.5 was the number, the assumed number for your tax credit investors through a put and call option. There's some substantial tax ramifications on that if you've got a $2.5 million debt and you pay it off for, you know, $250,000. There's a potential for substantial, what we call forgiveness of indebtedness income tax consequences. Now that we've lived with the program for more than seven years we've done some exit strategies and figured out ways to keep that new market note alive and to avoid the forgiveness of indebtedness.

I think the last slide on mine, are a couple of the risks associated with this thing. I think Dawn will go through more of the benefits from that side.

The risks, sort of overarching risks, is that the CDE does not properly manage the program compliance. So that can create a tax liability, the investors and, again, the liability is that those credits are recaptured and to the extent the investor has taken offset from its income taxes credit against the taxes paid. They're going to have to pay that money back. Four of the things that can trigger the recapture event, is the CDE ceases to be a certified as a CDE. I think that's rare. If the CDE does not satisfy the requirement to invest a minimum of 85 percent of their qualified equity investments within one year of receiving and really the allocation on that one the CDE would redeem the investment early and there's actually a way to avoid that one. Bankruptcy's not a recapture event as long as the loan itself doesn't get called.

So, you know, sort of the bottom line take away on that is that creating a new markets tax credit deal is not for the faint of heart or I guess for the rookies. You're going to need people who have done it before and a stable of professional advisors to be able to get you from the developer who says I want to do this project within your low-income community, your low-income census track, and getting the deal put together. That's I'd say sort of the high level view. I've got my disclaimer on there since I don't want anybody in the group to think that I've given them for real legal advice but, anyhow, that's what our ethics guru says we need to do.

Appreciate the opportunity of speaking with you and look forward to the questions.

BRENT SHEFFLER: Thank you very much, Howard. Those of you who just joined us, you've been listening to Howard Gordon with Williams Mullen. As a reminder to our audience we are taking questions at the end of the program in the Q and A session. We plan to address those questions following the speaker presentations.

If you have a question please pose it in the question panel and let us know which speaker your question is directed, either Howard Gordon or Dawn DeHart. Up next is Dawn DeHart with the Virginia Community Capital.

Dawn, we will get started here in just a second. Here we go.

DAWN DEHART: Thank you, Brent. Let's go to the next slide please. There we go.

I thought we ought to take just a brief moment to talk about community development financial institutions. These organizations really are the cornerstone of community development and they're very essential entities in the delivery of new market tax credits. There are about 800 CDFI's across the nation and there form takes a lot of different shapes. They can operate as banks, credit unions, and other types of loan funds.

In addition to that you can have a CDFI

that operates as a community development bank. There are about 75 across the country. They're regulated by various state and federal regulatory agencies. And you can also have a CDFI that operates as a non-profit bank holding company which is the business model that Virginia Community Capital utilizes. There are only about ten of those in the county regulated just like traditional banks are with state and federal regulatory agencies but the profits from the state charter bank are plowed right back into the organization and recycled into our mission lending admission investments.

Next slide, please.

All of the activities of a CDFI revolve around focusing on financing projects that are in low-income neighborhoods. It's social lending, which is what most of us call it in the industry. It's helping to being people out of poverty. It's creating economic developing opportunities that put people to work. It's removing blight from a neighborhood so it's a revitalization strategy. And it's basically brining capital into neighborhoods that would not ordinarily benefit from capital in other traditional ways.

So, the CDFI's are so important in the

new market tax credit arena because their missions are so aligned with one another. CDFI's have an enormous impact, very powerful impact across the country. They have about ten billion in assets collectively. Since inception they've made 31 billion in investments in distressed neighborhoods. They have funded 84,000 plus businesses across the country. They've created and preserved over 900,000 units of affordable housing. And CDFI's have been instrumental in funding over 9,000 community facilities in these underserved markets such as medical facilities and daycare and so forth.

Let's go to the next slide, please.

When we talk about new market tax credit eligibility, generally you're talking about a large real estate project. As Howard mentioned it could be industrial. It can be healthcare, it can be retail shopping center related. Generally it's going to be large dollars devoted to a real estate transaction of some sort. But the cornerstone of new market tax credits is that that project has to be in that designated census track. There's a map in our presentation that will show you in a moment that gives you an overview of all the eligible areas, census track areas, across Virginia. But the starting point is to make sure the project is indeed in a designated census track for new market tax credit eligibility. Because the new market tax credits are I'll say in short supply, there's a lot more demand for new market tax credits as the industry has grown than there is supply.

So it's very competitive to attract an investor. So, the project itself has to have a very compelling story around the community impact that project will have. And a compelling story can be something such as we'll create X number of jobs in that distressed neighborhood. It could be a project that provides critical services on the social side such as healthcare, daycare, senior citizen type services. The more compelling the story, the greater the ability to attract an investor to enter a new market tax credit transaction. You have to be able to attract the investors through the community impact. Very, very important item to underscore I think in new market tax credits.

Let's go to the next slide, Brent.

Types of businesses that can't be funded with new market tax credits. And this list is pretty consistent with other types of government loan programs. It can't be used to finance country clubs or gold courses. Massage parlors and suntan salons are off the list. Gambling casinos are not eligible. And Howard mentioned a few minutes ago something about the residential rental properties, new markets can fund a mix-use project that has residential component to it.

However, you have to be aware that there is a restriction on how much income is derived from the rental units, the residential rental units. The provision in new market tax credits provide that no more than 80 percent of that income stream can come from the rental revenue of the apartments themselves.

Next slide, please.

We have a real life case study here. This project you see here is a project that VCC financed with its allocation of new markets a couple of years ago. It's a medical facility in a rural area of Virginia, and you've got a construction budget here. This project started several years ago when we financed conventionally with our capital the acquisition of a medical facility.

The medical facility was operated for a couple of years, stabilized and then we put new market tax credits together in order to fund some significant improvements and modernization to that facility which would allow them to practice, I think, more current medicine as well as attract more patients and deliver better medicine and healthcare in their market area.

So this budget is for the most part a typical construction budget. You'll see that there's about 4.2 million in hard costs to renovate that facility. It's got architect and engineering in it. Contingencies, professional fees, interest during the construction stage. As well as the pay off of the existing mortgage that funded the original acquisition of that property.

Now what should standout to you are the large fees at the bottom of the uses section. You'll see new market tax credit legal and accounting for $200,030. It's not unusual for the legal fees and the accounting fees in the new market structure to be in excess of $200,000. There are a lot of professionals with the expertise that come into a transaction like this, the accountants, the specialized expertise from the lawyers. You have to utilize those professional services in order to get through a structure like this. This particular model of this project also has some fee reserves. In a new market tax credit project there are asset management and compliance fees and servicing fees and so forth. And in many cases you get those paid upfront and funded with loan proceeds which become part of the project.

So, you've got about 400, $500,000 in fees and professional services that you would not ordinarily have in a conventional project. So, roughly a $7 million budget. On the right-hand side you've got sources loan A and loan B. That's terminology consistent with new market tax credit language. And then you've got a very small portion of the sources being funded with borrower equity, 194,000, so it's a $7 million project.

And the next slide, I'm going to walk you through what Howard referred to as funnel concept. We'll follow the flow of money and this is the event that happens on the day of the new market tax credit closing when all the money gets funded. So, let's look at some of the players in a new market tax credit structure. Some of them Howard reference in his presentation. You have a CDE, community development entity. That's the entity that's awarded the new market tax credit allocation through a competitive process. You have a QALICB, which is the qualified active low-income community business. That's basically your borrower. If you want to relate it to a conventional loan, that's the project level.

You have a Sub-CDE in this case which is the single purpose entity that the CDE creates to facilitate this individual transaction. And the QEI, qualified eligible investment, which is $7 million. That's basically your project budget in new market tax credit acronym.

So, let's walk through how this $7 million flows down to the project level. At the top, on the left-hand side, you've got a leverage lender. On the right-hand side, you've got the investor equity. This is essentially the same chart that Howard reviewed just a moment ago. The funding process starts by the CDE selling $7 million of its new market tax credit allocation to an investor. And that's usually at a negotiated price per credit.

In this example I think it was 77 or 78 cents on the dollar. In today's world that's actually risen to about 82 or 83 cents per credit which shows you how popular the program is becoming. And unlike historic tax credit and low-income housing tax credits where the cash comes in after the project is completed. In new market tax credit world, the investor equity comes in cash on the day of closing.

So, in this case the investor equity, they purchased the allocation for roughly $2 million.

In this example, the investor was also paying a small origination fee to the leverage lender that's brining the debt capital into the structure. So the investors bringing in $2.1 million in cash equity. On the left-hand side the leverage lender, since this is a leverage model, it takes debt financing to make up the $7 million.

So you've got cash equity coming in and you've got debt capital coming in into an investment fund which is owned by the investor. The investment fund in this case then takes the $49,000 and pays the origination fee to the leverage lender for brining in the debt component. And from that point the $7 million from the investment fund flows down to the Sub-CDE, in this case a subsidiary of the CDE which was VCC.

We take out the three percent placement fee which is the fee that CDE's charge to cover essentially putting the deal together, brokering the deal in a lot of ways. So, we take out the $200,010, and in the industry that fees an average of three percent. Then the remainder of that funding comes down to the project level, which is the QALICB.

So, you'll see that once you take out the $200,010 placement fee to the CDE, you're left with $6,790,000. That takes the form of two loans, a loan A and a loan B. Loan A typically is going to mirror your leverage loan, $4,919,000. Loan B basically represents it's the soft debt in the deal.

It's basically the cash being brought in by the investor, less the fees. So, loan B becomes $1,870,000. And its soft debt, and Howard alluded to this earlier, it's the soft debt, it comes in as cash equity but it's treated as debt during the seven year compliance term of a new market tax credit loan. So, both of these loans are booked at a fixed rate of interest for seven years. And you have basically a seven year interest only loan. So, that's the flow of money on the day of closing and this is the typical structure that you'll see in a leverage model.

Let's go to the next slide.

So, I wanted to try to compare this with a conventional loan as best you can. It's not exactly apples to apples. And that's because most lenders aren't making a seven year loan. Typically you'll find a five year loan with some period of amortization.

And the other nuance here, as we talked earlier, you've got all of those professional fees and legal fees which amounted to upwards of $200,030 or more in the new market tax credit project budget that you would not have in a conventional budget. But for purposes of illustration, I left them constant just so we can have the discussion. Even if you adjusted the project budget or conventional loan without those additional fees you still can prove that there's a lot of value being brought to the table by using the markets. In a conventional loan structure it's the 80 20 rule.

A bank will finance 80 percent of a cost and it's expected that the borrower will bring in the other 20 percent. In this case you would have more of a traditional loan at about $5.6 million. That 20 percent that the borrower is expected to bring would be roughly $1.4 million. Usually lenders are going to fix that rate for five years. You could probably argue that 5.9 is a bit high but it depends on the nature of the deal.

The real example here or the real point under rate is that most banks are going to fix that rate for five years, whatever that rate may be. The term on a normal conventional loan is usually a five year balloon with a 20, maybe a 25 year amortization with a maximum loan to value of 80 percent. That payment on a conventional structure is roughly $40,000 a month. So, let's contrast that with the terms under a new market structure.

The loan is essentially 100 percent, the borrowers getting the benefit of $6,790,000. The equity being brought by the borrower to this deal is fairly nominal, it's about $194,000. The rate on this particular deal was charged at 5.92 percent, fixed for seven years. And the term is seven years interest only, no principal payment. Matter of fact principal payments are prohibited in a new market tax credit structure. The borrower's payment was going to be $33,000 a month, interest only and financing 100 percent essentially of the project costs. So, there's a big difference between conventional and new market tax credit structures.

Let's advance to the next slide.

The advantages of new markets in this particular case study, well right off the bat you can see that the borrowers saving about $6,300 a month because there's no principal payment requirements. One of the major selling points of the program to is that the borrower doesn't have to put in the 20 percent cash contribution. When you get into some of the larger projects that are 5 and $10 million, 20 percent of a project of that size is a big chunk of cash. Many of the borrowers that we work with in underserved markets simply don't have access to that kind of cash equity.

So, virtually no equity required in the new market tax credit world. The cash being brought in from the investors, which are normally institutional, typically they tend be large banks, like US Bank and Bank of America and so forth, but they're brining in their cash on the day of closing which is anywhere from 20 to 30 percent cash equity as part of the project.

One of the other features here, one of the benefits to the borrower I mentioned loan B is really soft debt in the deal, it's the cash equity being brought in by the investor less the fees that are paid to the CDE, the borrowers going to pay on that loan for seven years but at the end of seven years that debt gets cancelled.

And the reason its eligible for cancellation is because remember the investor came in, had an incentive, to be in this deal for seven years because of the significant tax break on the federal tax liability by participating in this program. That's the carrot that brings the investor into some of these underserved markets because there's no other capital flowing through these distressed areas.

So, the investor has already recognized seven years worth of tax benefit, there's no other reason to stay in the deal, and they're willing to cancel loan B. And the borrower refinances loan A, in this example $4.9 million, on a conventional amortizing basis. By the end of seven years that borrower is very seasoned and has a track record. And of course one of the other obvious benefits is that the new market tax credit loan finances 100 percent. The CDE lender in this case accepts a loan to value of 100 percent.

Let's go to the next slide.

There are benefits to all the parties in the transaction. To the borrower, seven years interest only. There aren't many lenders, traditional lenders that I know that offer those kinds of advantageous terms. The significant equity that comes in from the investor on loan B, 20 to 30 percent and then the ability to cancel some of that debt at the end of seven years and convert the loan to a traditional amortizing loan. To the investor that has come in, it's the tax break. It's that 39 percent federal tax credit over a seven year period that has lured them into this underserved market to begin with. And that's a huge incentive in this program and that's one reason it's so very popular.

The next slide.

The leverage lender in this case study that we used the VCC was both the CDE and the leverage lender. For VCC it gives us an opportunity to build our loan portfolio with a seven year earning asset and it's a mission oriented investment for us. And then at the end of seven years we have an opportunity to be the refinance lender on loan A and keep that loan in our portfolio. The CDE, which is the role that we played in that case study, the CDE is the entity that has a new market tax credit allocation and is trying to deploy it.

It gives us an ability to differentiate ourselves from other traditional lenders. It's a very unique product. It offers a lot of advantages to the borrower. And it's a very specialized program that really meets a lot of the social needs that we're trying to accomplish in these underserved markets. And it allows us to continue building the new market tax credit industry. So the more outcomes, favorable outcomes you have by deploying this type of capital the more popular the program becomes and the more Congress recognizes the need to renew it every year and provide more funding for mortgage and related work.

There's always a downside. So, we encourage all of the parties in the new market tax credit deal to go into these transactions with their eyes open. They are fairly complex and no one likes surprises.

So, to the borrower the downside is that there are large legal fees and accounting fees. It doesn't matter whether that's a million dollar deal or whether it's a $20 million deal. Legal fees are legal fees. Very specialized expertise is needed to put these deals together. Because of the cost the program is really geared towards the larger deals, five million, ten million, and up. We usually tell our borrowers that probably being to realize the benefits of a new market tax credit structure when a project hits about $3 million. Anything less than that you're paying a lot of professional fees and you're not maximizing the value of using the new market tax credit allocation wisely. And on smaller deals it's harder to attract investors.

There are very long lead times in a new market tax credit deal. So, we encourage folks that are speaking about a project that could be compatible with new markets to really plan it wisely and start early. Sometimes its nine months before a deal can close. There's just so many parties in a deal and the nuances that have to be worked out with some of the regulations and so forth.

And there's a downside to the investor of course which is the recapture issue that Howard discussed earlier. If a CDE is negligent, not maintaining the compliance aspect or if the transactions not being serviced properly or if the project just simply fails. There are consequences to the investor. If something catastrophic happens to this project in the seventh year the recapture to the investor goes back to day one. So, they have the potential to incur substantial fees to the IRS as well as penalties and so forth.

To the leverage lender, the leverage lender VCC in that particular example, if you looked at the model you could see that the leverage lender was not lending to the project, so there's no real estate collateral. The collateral is the investment funds assets which is the 99 percent interest in the Sub-CDE, so it's not real tangible collateral. A leverage lender can't foreclose during that seven year compliance period. If something goes awry with that project that leverage lender is stuck with a fixed rate for seven years. And in a volatile rate environment that earning asset, you know, could squeeze the earnings of the leverage lender for some time to come.

The CDE, the risk to the CDE, this is a very compliance intensive program. There's a lot of reporting to the CDFI fund as well as to the investors in a particular transaction. So, the CDE needs to have the personnel that's focused on servicing this portfolio and being on top of the reporting on a very timely basis.

Just a quick highlight of some of the deals funded by VCC, these have all been medical related. Some of these were deals that we funded with our allocation. Some of them we played a leverage lender role using another CDE's new market tax credit allocation. Most were rural facilities, some were metro. But, all of these are fairly well established and doing extremely well.

Next slide.

We included a map that I mentioned earlier. You can see all across Virginia. The dark green highlighted areas shows you, at least based on the 2012 map which is the period that's referenced in this map. That dark green area is all of the eligible, the new market tax credit eligible areas across Virginia. Its substantial, that's if it's rural of course. All of the rural is eligible. But, we thought you might want to take a look, I think it makes an impact of showing you all the opportunities across Virginia to deploy new market tax credits. The next slide will show you some other resources if you want to do some additional research.

Cdfifund.gov, remember the CDFI fund is the agency that allocates and awards the new market tax credits to the CDE's. CDFI fund is a wealth of information, there's program related information, there's an allocatee database. If someone is interested in learning who are the new market tax credit allocatees across Virginia, this will show you who's active in the program and when they got their last award and how much that award was for as well as contact information for that allocatee. And also gives you mapping software where you can just type in the address of a project and immediately determine if it's in an eligible area.

Two other accounting firms that are primary in this industry, CohnReznick and Novogradac. Their websites also contains mapping software where you can drop-in the address for eligibility purposes as well as upcoming conferences and events and webinars if one wants to learn more information about the industry.

And so with that, Howard and I have now given you a very high level global overview about the new market tax credit program and the value that it serves in brining capital into distressed areas. But, there's a lot more to learn about the program but hopefully this has peaked your interest.

BRENT SHEFFLER: Very well.

DAWN DEHART: Brent, I'll turn it back over to you.

BRENT SHEFFLER: Dawn DeHart, thank you very much. Those of you who joined us in the middle of the program, you have been listening to Howard Gordon and Dawn DeHart. Howard Gordon is with Williams Mullen and Dawn Dehart is with the Virginia Community Capital. Thank you very much Dawn.

We now have an opportunity to take some questions. Connie Long will communicate those questions to us. We'll take as many questions as we can before the close of the hour but since we are right up against it we will got over a little bit. And I know that Connie you have informed us you've received a number of questions, so let's jump right in on those.

CONNIE LONG: Thank you, Brent. First question, are allocations made to CDE's based on specific projects or simply a lump sum allocation that the CDE uses to fund eligible projects not decided at the time of allocation?

If the latter, can a potential borrower contract with the CDE to apply its allocation first to the borrowers project?

DAWN DEHART: Howard, I can address that if you'd like?

HOWARD GORDON: Yeah, I think that's one for you Connie, or Dawn, I'm sorry.

DAWN DEHART: Yeah, basically what was happening years ago is there was an allocation that basically was awarded in lump sum to a CDE and then they took that and found the projects and funded them, those particular projects. What's happening now because the popularity of the program and such now, that every year there's three and a half billion that's awarded across the country in allocation but there's 20 billion in aid.

It's so competitive now that CDE's now develop a pipeline of projects and they essentially are underwriting those projects before they ever apply to the CDFI fund for another award. You have to be able to demonstrate now that you've got projects that, to some extent, are shovel ready to support the amount that you're asking for.

But we all recognize, let's say that CDE gets an allocation award but that project is no longer viable, projects fall out of bid all the time, but the application process requires that you be able to demonstrate you've got projects of which you can deploy that allocation. If something falls out of bid later you simply go looking for another deal to replace it.

So, I hope that answers that question.

HOWARD GORDON: I would just add one brief thing and that is that sometimes, like Dawn said, when you've got a deal that falls out of bid, the CDE that has that money to use that money with another CDE within the same or similar, you know, neighboring community to help fund 100 percent of a deal that where the first CDE didn't have enough of the credits to be able to fund the entire deal.

CONNIE LONG: Okay. Our second question, can you provide an example of how local government has used the NMTC program?

HOWARD GORDON: I would just say

quickly on that, that it's a combination of things where the economic development person gets acquainted with a deal. And then says how can we make this deal happen and starts exploring the opportunities. And then you start looking at whether it's the new market tax credits or other incentives that the locality may have in order to be able to attract the business within, again, in your low-income community.

DAWN DEHART: Yeah, and I would add too, a specific situation in Roanoke there was a market building that contained a food court. And several years ago the city, the building by the way was owned by the city, and governmental entities are not eligible specifically for a new market tax credits.

In the case of that market building which drastically needed some renovation and upgrades. Although the city owned the building, they created a foundation, a non-profit foundation to take ownership of that building and that non-profit foundation became the beneficiary of the new market tax credits. So, the city indirectly benefited from the new market tax credits but they could not be a direct beneficiary of that allocation, of that award. So, that was one way the local government benefited from the program.

CONNIE LONG: Have any large scale manufacturing projects in Virginia taken advantage of the new market tax credit program?

Is time frame for decision too long for these?

HOWARD GORDON: I don't know for certain one way or the other, but I've got to believe that there's been some activates that were generated by virtue of the ability to fund a portion of the quote equity with the new market credits. I just don't know of anyone specific to do that. I think most of those, if it's a big enough capital investment it's going to have a long term or long lead time, you know, to sign a zoning, finding the right parcels. You know, there's a lot that goes into the development of something like that, to get it into the right place and then start looking for the financing. And I would think that when you start looking for financing, you know, exploring the option of using the new markets credits is something that, again, dependent on the type of business and the location is an option they would at least take a look at.

CONNIE LONG: Brent, I think this is our final question. What is the low to moderate threshold to qualify for a new market tax credits?

HOWARD GORDON: Connie, you want to talk about that? I think you mentioned it in your presentation, all that.

DAWN DEHART: I'm not sure I understood the question. What is the minimum? Repeat the question for me.

CONNIE LONG: Low to moderate threshold to qualify?

DAWN DEHART: Well, you know it's going to vary by area. And when you go in and use the mapping software on some of those websites that I referred you to, it's actually very easy. As opposed to creating a dollar threshold, when you use the mapping software, the mapping software will tell you whether or not it has hit the right threshold, is a 20 percent poverty rate or whether the area immediate income falls below the 80 percent. So, it's very easy because each community, each census track is probably going to have a different area immediate income dollar value. But, in mapping it and determining eligibility you don't have to worry about the actual dollar threshold.

HOWARD GORDON: And I think if the question was really, and I think Dawn answered it during her presentation, is that I think she said that a minimum of a $3 million project. Anything of a project that's smaller than $3 million is one that the costs you just don't get the benefit of all the fees and costs that it's going to take to be able to structure the deal.

BRENT SHEFFLER: Very good. Thank you very much. I think that's all the questions. I know that a number of you might have additional questions after this concludes. So, please let us know if your questions are still coming at us. Just send us a direct e-mail and we'll do what we can to respond to you on those. So, thank you very much Dawn DeHart with Virginia Community Capital, and Howard Gordon with Williams Mullen. Thank you very much for investing your time and energy you did share this information with us on new market tax credits.

I'd like to thank a number of people who made today's webinar possible. Here are just some of the names who have served. If you sound this webinar to be helpful please drop them a note of appreciation. If you have a complaint please don't tell them just tell me, so let me know. I'd also like to inform everyone that this session has been recorded. If you'd like to revisit this or forward it to a friend, please go to the virginiaallies.org webinars and you will find not only this webinar recording in the next 24, 48 hours but also the others that have been posted previously. Those of you who attended today's webinar, thank you for joining us today. We thank you for your participation.

This next webinar will take place on Wednesday, April 15th, 2015. For our Third Wednesday Webinar on the topic "SourceLink Virginia." During this next webinar we will provide you with an overview of what's taking place with SourceLink Virginia, and we will highlight the value this digital resource is designed to bring to you to serve Virginia businesses and those of us in the economic development profession.

Our speaker for the April 15th webinar will be Conaway Haskins the Third, who serves as Executive Director of the Virginia Community Economic Network. There's no cost for registration. We look forward to having you with us on April 15th for our fourth webinar in our 2015 Third Wednesday Webinar series.

Until then, good-bye everyone and have a great day! Thank you for joining us

(WHEREUPON, the Webinar was concluded at 3:05 p.m.)

STIPULATION

The foregoing matter was taken on the date, and at the time and place set out on the title page hereof.

It was requested that the matter be taken by the reporter and that the same be reduced to typewritten form.

CERTIFICATE OF REPORTER AND SECURE ENCRYPTED SIGNATURE AND DELIVERY OF CERTIFIED TRANSCRIPT

I, **ANDREA F. MIKUS**, do hereby certify that the forgoing matter was reported by stenographic and/or mechanical means, that same was reduced to written form, that the transcript prepared by me or under my direction, is a true and accurate record of same to the best of my knowledge and ability; that there is no relation nor employment by any attorney or counsel employed by the parties hereto, nor financial or otherwise interest in the action filed or its outcome.

This transcript and certificate have been digitally signed and securely delivered through our encryption server.

IN WITNESS HEREOF, I have here unto set my hand and delivered through encrypted server this 25th day of March, 2014.

Andrea F. Mikus

/s/ANDREA F. MIKUS

COURT REPORTER