# New Markets Tax Credits

## Taking advantage of a new source of capital

**CALED Finance Workshop**
**Fairfield, CA**
**Oct. 8, 2003**

**Presented by**
**Frank Altman**
**President/Chief Executive Officer**
**Community Reinvestment Fund**

# What is CRF?

- **A national non-profit financial services organization based in Minnesota**
- **Provides capital to communities by purchasing economic development and affordable housing loans from community development lenders**
- **Helped establish New Markets Tax Credit as member of NMTC Coalition**

# CRF's track record

- **Has purchased more than $300 million in loans**
- **Has issued $208 million in debt securities**
- **Has privately placed $54 million in loans with individual investors**
- **Loss ratio is less than 0.5%**
- **Delinquencies currently 0.29%**
- **Loans from 103 sellers in 24 states**

# Community Reinvestment Fund Working with CDE Lenders

## The CRF NMTC Allocation

- $162.5 Allocation to be used nationally
- 50 community development lenders serving communities in 30 states joined in the application
- Key strategy:  CRF will purchase loans made to qualified active low income community businesses by community development entity (CDE) lenders

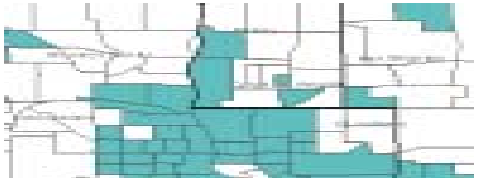
# Community Reinvestment Fund Working with CDE Lenders

## The CRF NMTC Business Theory

- NMTC works well for loans to businesses that are secured by real estate
- Many community lenders will want to use NMTC but won't want to apply for or won't receive NMTC allocation
- It will be costly and difficult to raise investor equity through NMTC

**Conclusion: Secondary market approach to NMTC addresses these issues**

# What's different this year

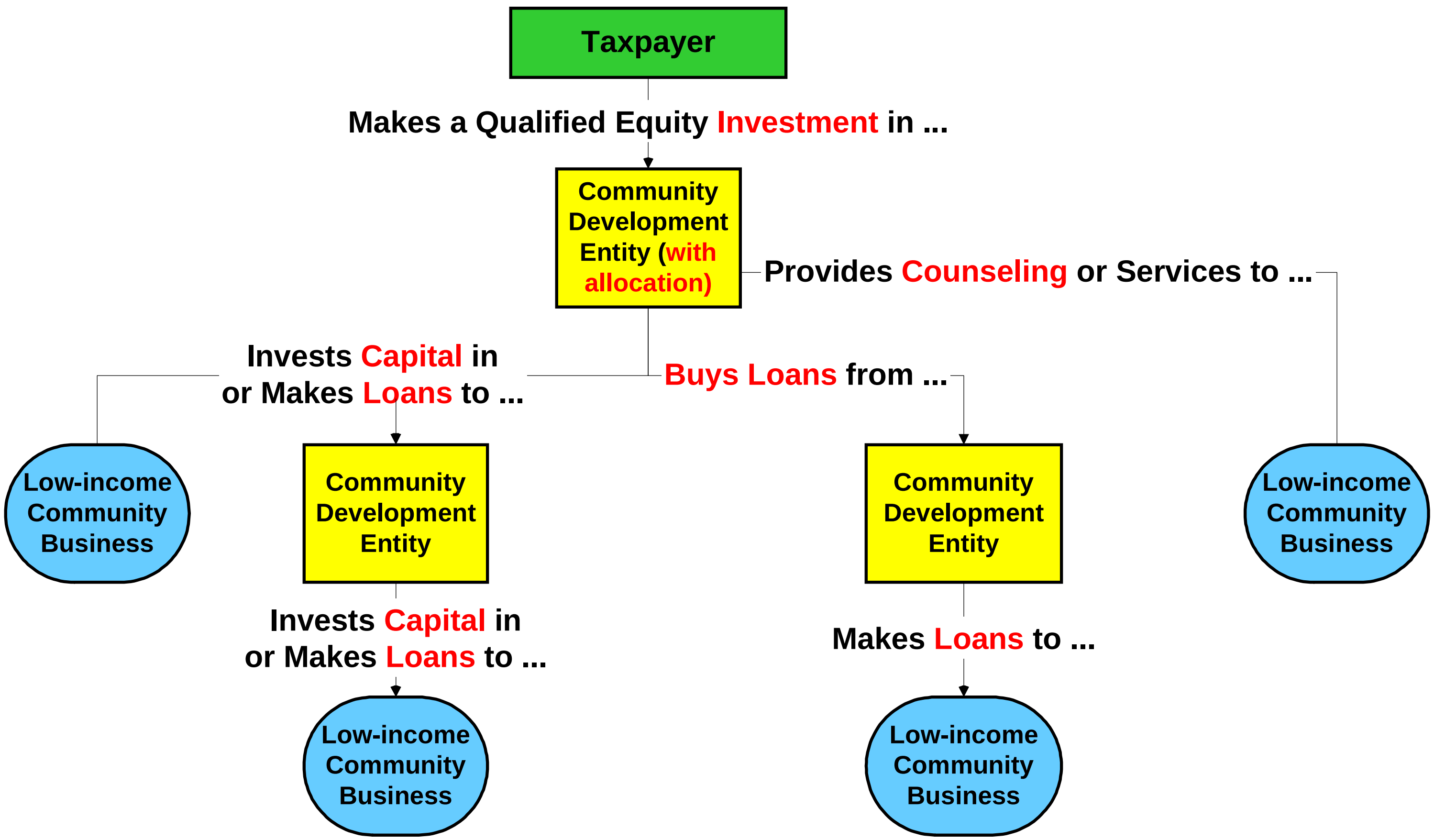


- **More credits available: $3.5 billion**
- **Again, though, it covers two years of allocations (originally would have been $1.5 billion in 2003, $2 billion in 2004)**
- **More applicants likely**
  - **Expectation is that 600 will apply**
- **CRF, along with others who won allocation last year, have up until March 5 to get 50% of our awarded allocation amount from our investors ($81.25 million)**
  - **If not, application will be thrown out**

# CRF applied for second allocation

- **66 lenders altogether joined us this year**
- **Seeking $350 million total**
- **California lenders and communities large part of application**

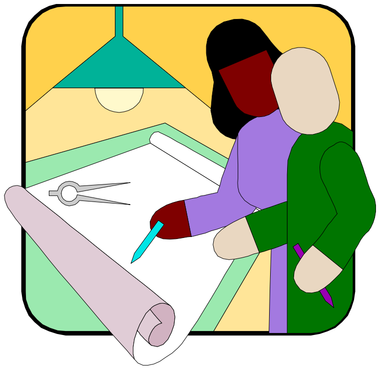
# NMTC Investment Options



# Community Reinvestment Fund Working with CDE Lenders

## The CRF NMTC Strategy

- Assemble a pool of loans originated by many CDEs
- Provide quality control for investors by careful review of QALICB eligibility and managing recapture risks
- Use the leveraged investment approach to minimize cost of capital and maximize investor interest
- Provide loans to QALICBs at rates 1.5% to 2% less than current rates for equivalent loans



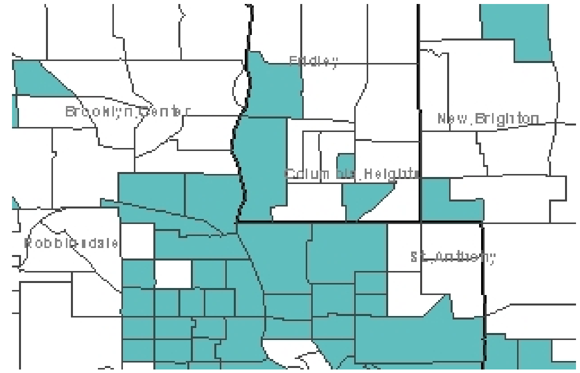
# Community Reinvestment Fund
# Working with CDE Lenders

## What kinds of loans will CRF buy?

- Loans to existing businesses (in business for at least two years) for acquisition, renovation or refinancing of real property or equipment
- Secured by first or second liens on real estate or first liens on equipment
- Maximum combined LTV of 90%
- Minimum debt coverage ratio of 1.20 to 1

# What's a low-income area?

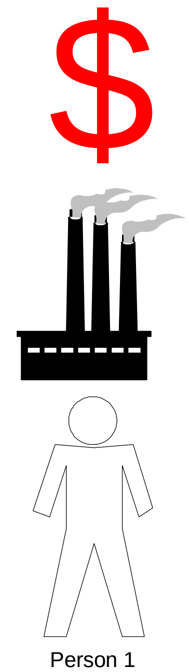
- **20% or higher poverty rate**
- **80% or less of median income for state or metro area (state for rural areas)**




- **1990 census tract vs. 2000 census tract**
  - **Changes posted late last year**
  - **Check to make sure you don't have earlier deals that qualified that maybe aren't part of it now**

# What qualifies as a low-income community business?

1. **At least 50% of revenue from business activity conducted within qualifying area AND**
2. **At least 40% of tangible property in qualifying area AND**
3. **At least 40% of business conducted by employees within area**
   – ***If #2 or #3 are 50% or more, #1 is deemed to have been met***



# Closer look: First test

1. **At least 50% of revenue from business activity conducted within qualifying area**

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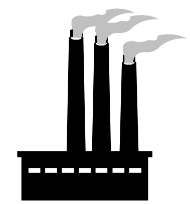
   - **What kinds of businesses might be on the line? Prime example: Poultry producer selling to high-end restaurants in Los Angeles.**

**<u>Look to tests 2 and 3</u>**

   - **If either property or employees exceed 50% level, you're okay. (Still need 40% for one not exceeding 50% level.)**

# Closer look: Second test

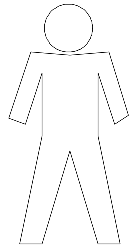
**2. At least 40% of tangible property in qualifying area**



- **Problem is multiple sites**
- **Question comes up with chains**
- **No clear direction yet on fencing off businesses that are chains, owned by separate entities**
- **What are examples of questionable groups?**

# Closer look: Third test

**3. At least 40% of business conducted by employees within area**


Person 1

- **What about businesses with traveling sales forces?**
- **What about businesses with off-site workers – e.g., home-based?**

# Reasonable expectations test

- **What if business moves to another locale two years after loan made?**
- **Raises "reasonable expectations test" – what did lender reasonably expect at time of loan?**
  - **If lender knew business was moving, big trouble.**
  - **If lender reasonably expected business to stay, okay.**

# Community Reinvestment Fund Working with CDE Lenders

**How can a community development lender do business with CRF?**

- **CRF will purchase loans from lenders (including CDFI banks and credit unions) that are committed to community development lending**
- **Lenders must enter into a Qualified Seller agreement with CRF to sell NMTC and/or non-NMTC loans to CRF**

# Community Reinvestment Fund Working with CDE Lenders

**How can a community development lender do business with CRF?**

- **Qualified Sellers must demonstrate to CRF their expertise in originating business loans, including underwriting and loan approval procedures**
- **Qualified Sellers may elect to service the loans they sell to CRF if they can demonstrate acceptable expertise and infrastructure**

# Community Reinvestment Fund Working with CDE Lenders

**What additional requirements will there be for NMTC loans?**

- **CRF will give a preference to the 50 lenders who joined its NMTC application**
- **Depending on the pipeline of these lenders and on targeting requirements of CRF's allocation agreement, CRF will likely seek additional CDEs to sell NMTC loans**
- **Lenders must demonstrate their ability to maintain compliance with NMTC requirements**

# Community Reinvestment Fund Working with CDE Lenders

## Loan Parameters and Pricing

- Loans secured by real estate or hard assets
- 25-year amortization with 7-year balloon or rate reset every 7 years
- Underwriting characteristics:  maximum CLTV of 90%; minimum debt coverage ratio of 1.20 to 1
- Priced at pre-agreed initial spread to index (7-year Treasury + 150 to 200 BP)
- Acquired by the CRF net of primary servicing and lender origination fees

# For More Information

**If you would like more information about the New Markets Tax Credit program, please contact us.**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# Now … the view from a lender

- **Jim Baird, CEO, Bay Area Employment Development Co.**
- **CRF lending partner**