

Overview of LIHTC Market

The Low Income Housing Tax Credit (LIHTC) program was created in 1986 and encourages investors and developers to develop more low income housing, which without the tax credit, would likely not be financially feasible. The dollar-for-dollar credit can be used to construct new properties or renovate existing rental buildings and is claimed pro rata over a period of ten years, with a fifteen year compliance period. LIHTC guidelines, which are established by the IRS and administered by state housing agencies, require that higher tax credit allocations be given to projects that typically serve tenants which earn 60% or less than the area median income and maintain affordability for at least 30 years (the initial 15 year compliance period plus an extended use period of at least 15 years, depending on the state). The LIHTC program will either subsidize a project at 30% of the acquisition cost of existing buildings, or new construction that uses additional subsidies, or subsidize a project at 70% of new construction without any additional federal subsidies.

In response to bulging industry opportunity, CB Richard Ellis formed the National Tax Credit Advisory Group (NTAG) in mid-2006. The group is comprised of three LIHTC sector veterans with over 55 years of combined experience: Tom Fischer, Senior Vice President, and Tom Mangum and Sam Merkle, Vice Presidents. In tandem with CBRE|Melody, NTAG provides developers, investors, syndicators and lenders with complete brokerage and debt solutions, including expiring (Year 15) properties, workouts and stabilized LIHTC properties where the general partner is looking to monetize its investment.

While the market is ripe with LIHTC opportunity, buyers need to understand the unique compliance challenges the asset type offers. The properties' covenants with various federal and state agencies restrict the income profile of residents and rental rates. "Maintaining the rent restrictions required by LIHTC assets contradicts the prevalent industry goal of increasing rental rates to improve asset performance,"

says Merkle. "As the tax credit status means a compliance audit is unavoidable, maintaining a balance between asset performance and compliance is essential."

Developers seeking tax credits must initially secure a tax credit reservation, and then secure a conventional loan and gap financing, and exchange tax credits for equity from the syndicator or direct investor. Often billed as limited partnerships to minimize investor liability exposure, this complex transaction structure can be difficult to navigate. "The restrictions required to achieve and maintain tax credit status often bring several additional parties to the negotiating table," says Mangum. "Typically the tax credit investors, the syndicator, state or federal government agencies, lenders and those holding any soft debt all have a stake in and approval rights over the transaction."

LIHTC property owners are required to certify annually throughout the fifteen-year compliance period that they are renting to low-income tenants or risk losing future tax benefits and recapture of tax benefits previously claimed. This means that experienced LIHTC property management staff is essential to the success of an asset. "In addition to rental restrictions, the sheer volume of compliance paperwork requires a unique knowledge base and consistent efficiency, or else asset performance suffers," according to Fischer. "Often operators who lack such internal specialists will outsource to third party compliance companies."

Despite the unique operational challenges afforded by LIHTC, compliance capable investors and operators are seeking hot opportunities in large coastal markets like New York City, Boston, Washington, DC, and cities in Florida and California. And the future of the sector looks positive: "With an estimated 100,000 units reaching the end of the initial 15 year compliance period each year, and the demand for affordable housing and current investor appetite, LIHTC properties offer long-term appeal," concludes Merkle.

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