NEW MARKETS TAX CREDIT PROGRAM:

PART 1: THE BASICS

FOR THE FINANCING OF REAL ESTATE, EQUIPMENT, AND BUSINESS/NONPROFIT OPERATIONS

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Introduction

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Community Reinvestment Associates, LLC is a national boutique financial consulting firm, which specializes in filling financing gaps by identifying and securing community and economic development subsidies on a contingent fee basis.

Phone: (312) 881-0966
Email: scott@crassociates-LLC.com

We have facilitated over $4.2 billion of community and economic development financings, including $1.1 billion of new markets tax credits, historic tax credits and preservation easements, low-income housing tax credits, opportunity zone financing, USDA programs, CDFI Fund programs, taxable bonds, tax-exempt bonds, and various federal, state and local grants and subsidies, as well as facilitating private-public partnerships, including securing traditional debt, equity, and donations.

Outline of NMTC Financing

Part 1: The Basics

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Outline of NMTC Financing

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Intent of the NMTC Program

- The intent of the federal new markets tax credit program (the **"NMTC Program"**) is to provide investment capital to low-income communities which have traditionally lacked access to financing.

- The NMTC Program particularly focuses on the benefits to the residents in such low-income communities and targeted populations (such as low-income persons, minorities, women and other populations who lack access to quality jobs, and community and consumer goods and services).
- NMTCs are equal to 39% of the NMTC financing, which is known as a "qualified equity investment" (a **"QEI"**).
- The NMTC Program subsidy is provided from a NMTC Investor's effective purchase of the NMTCs (which are dollar-for-dollar offset against federal income taxes).
- The Community Development Financial Institutions Fund, which is a division of the U.S. Treasury Department (the **"CDFI Fund"**), administers the NMTC Program.
- Borrowers do not apply to the CDFI Fund for NMTC financing but rather they apply to those who have received NMTC allocation awards from the CDFI Fund.

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Good Borrower and Project Candidates for NMTC Financing

Each of the following are good types of for-profit's and nonprofit's operations and projects for the NMTC financing:

- manufacturing facilities/operations;
- health care facilities/operations;
- grocery stores/operations;
- charter and independent schools/operations;
- qualified mixed-use projects (*i.e.*, those that satisfy the "80/20 Test");
- community facilities/operations; and
- renewable energy and recycling facilities/operations.

Economic Benefits of NMTC Financing

- NMTCs are equal to 39% of the NMTC financing, which is a “qualified equity investment” (a **“QEI”**).
- None of the Borrower, its affiliates or owners recognize the NMTCs.
- NMTC Investors are typically financial institutions (or large corporations, which is less common).

- A NMTC Investor effectively “purchases” the NMTCs based on:
  - current market pricing;
  - desirability of participating in the particular NMTC financing; and
  - whether or not other NMTC Investors are competing to participate in the particular NMTC financing.

Economic Benefits of NMTC Financing

Generally, with respect to the **Forgivable NMTC Loan**:

- the principal is provided by the proceeds of the NMTC Investor's "purchase price" for the NMTCs;
- it only requires approximate 1.5% interest-only payments during the 7-year NMTC compliance period; and
- it is forgiven at the end of the 7-year NMTC compliance period.

Generally, with respect to the **Non-Forgivable NMTC Loan**:

- a portion of the principal and the favorable terms of which are the provided by, or the result of, the NMTC Investor's "purchase" of the NMTCs;
- it only requires below-market interest-only payments during the 7-year NMTC compliance period; and
- after the 7-year NMTC compliance period, the loan amortizes through its maturity date of up to 40 years (which can be beyond the useful life of any secured assets).

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Economic Benefits of NMTC Financing

Generally, the economic benefits of the NMTC Program subsidy (whether in the form of the Forgivable NMTC Loan or the Non-Forgivable NMTC loan) include:

- gap financing;
- with approximate 1.5% interest-only payments during the 7-year NMTC compliance period;
- subordination to other creditors;
- nontraditional and favorable terms, and flexible underwriting criteria, such as:
  - the Forgivable NMTC Loan being forgiven at the end of the 7-year NMTC compliance Period, or
  - the Non-Forgivable NMTC Loan with a below-market interest rate and a term up to 40 years (and beyond any secured asset's useful life);
- ability to obtain additional financing;
- ability to "leverage" other sources of financing for a multiplier economic benefit;
- "softer" foreclosure and enforcement rights if there is a default;
- if applicable, state NMTCs provide additional subsidy; and
- substantial community and economic impacts to residents in "Low-Income Communities" and "Targeted Populations," including "Low-Income Persons."

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NMTC Financing Facilitated by "Allocatees" and "CDEs"

- Each year, the Community Development Financial Institutions Fund (the **"CDFI Fund,"** which administers the NMTC Program) provides <u>non-monetary</u> NMTC allocation authority awards (**"NMTC Allocation Awards"**) to "qualified community development entities (**"CDEs"**), after an extremely competitive process.
- If a CDE receives such an award, it becomes an **"Allocatee."**
- A NMTC Allocation Award authorizes an Allocatee to designate its NMTC financings as entitled to NMTCs.
- Borrowers must compete to obtain a "sub-allocation" of NMTC Allocation Awards from one or more Allocatees, which is also an extremely competitive process.
- Each Allocatee (a) has a service area, which is national, regional, multi-state or local; and (b) targets certain types of borrowers and projects, which provide substantial community impact in its service area.
- In the case of the Forgivable NMTC Loan (or pool of smaller Non-Forgivable NMTC Loans), each Allocatee spins off a separate CDE for the applicable NMTC financing.

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Legal Requirements

- There are many statutory and regulatory requirements as well as specific guidance provided by the IRS and the CDFI Fund (which administers the NMTC Program).
- Such requirements, include but are not limited to:
    - the project or operations, as applicable, must be "predominantly" located in a "Low-Income Census Tract" or otherwise benefit "Targeted Populations;"
    - there must be a gap in available financing (*i.e.*, satisfaction of the so-called "But For Test");
    - the borrower must be a "Qualified Active Low-Income Community Business;"
    - the borrower's trade or business (or the nonprofit's purpose and operations) must be a "Qualified Business;"
    - the NMTC financing proceeds must be used for "Permitted Uses" and not for "Prohibited Uses;" and
    - there cannot be a "Recapture Event" during the 7-year NMTC compliance period.

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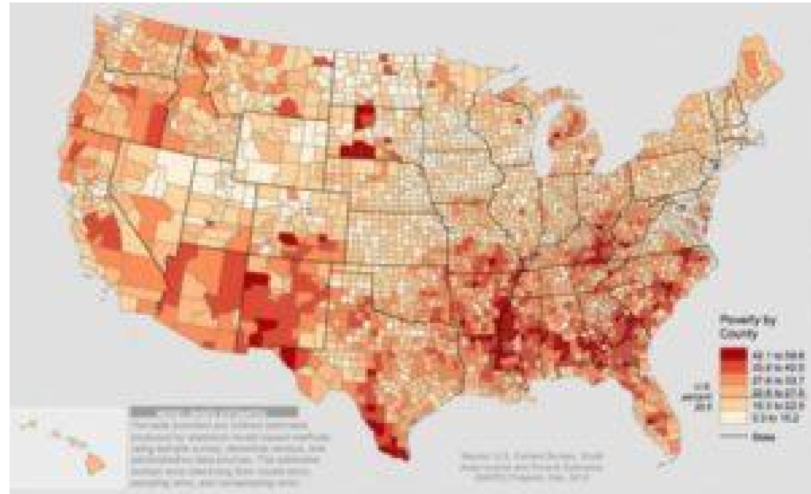
Low-Income Census Tract



The borrower or the project, as applicable, must be predominately located in a "low-income community" (a "**LIC**"), which is defined by U.S. Census data as a census tract with:

- a poverty rate of at least 20%, or
- either:
  - in the case of a tract located in a metropolitan area, the median family income (**"MFI"**) for such metropolitan census tract does not exceed 80% of the greater of (x) the statewide MFI or (y) the metropolitan area MFI, or
  - in the case of a tract in a non-metropolitan area, the MFI for such non-metropolitan census tract does not exceed 80% of the statewide MFI.

Alternative Test: Targeted Populations

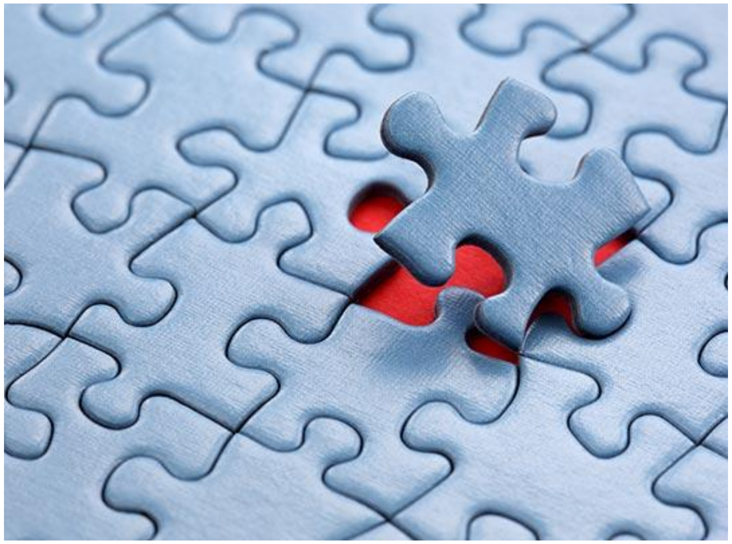
Alternatively, if a Borrower or a project is not predominantly located in a "Low-Income Community," it can be **deemed** to be in a "Low-Income Community" if it otherwise benefits "Low-Income Persons" (as "Targeted Populations") throughout the 7-year NMTC compliance period.

This Targeted Populations alternative is satisfied if:

- 1 of the following 3 tests is satisfied during the 7-year NMTC compliance period (the **"Targeted Populations Alternative Test"**):
- at least 50% of total its **gross income** is derived from sales, rentals, services or other transactions with "Low-Income Persons;"
- at least 40% of its **employees** are "Low-Income Persons;" or
- at least 50% of its **owners** are "Low-Income Persons;" and
- the applicable census tracts may only have median family income (**"MFI"**) that is (a) at or below 120% of the statewide MFI for non-metropolitan area tracts, or (b) the greater of statewide or metropolitan area MFI for tracts located within a metropolitan area.

"But For" Test

- A borrower must show that it cannot otherwise obtain a significant amount of its financing needs in the traditional marketplace.
- Specifically, the **"But For Test"** is applied as follows:
  - the overall financing will not proceed;
  - the project or operations will be significantly reduced in scope;
  - the project or operations will be substantially delayed;
  - there will be unrealized substantial community impacts; and/or
  - the project or operations would not otherwise be predominantly located in a "Low-Income Community."



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Borrower Must be a "Qualified Active Low-Income Community Business"

The borrower must be a "qualified active low-income community business" (a **"QALICB"**), which is a corporation, partnership, or limited liability company (or division of any of the foregoing), and has a trade or business (or, in the case of a nonprofit, any activity that furthers its charitable purpose), which is a "Qualified Business."

Additionally, it must satisfy each of the 5 requirements during the term of the NMTC financing. First,

- at least 50% of its total **gross income** must be derived from the active conduct of a "Qualified Business" within one or more "low-income communities;"
- at least 40% of the use of its **tangible property** (whether owned or leased) must be located within one or more LICs; and
- at least 40% of the **services performed by its employees** must be performed within one or more LICs.

Note: If a borrower cannot satisfy these requirements (such as not having any employees, there are alternative percentage tests and financing structures that can be used).

These 3 requirements are not required if the Targeted Populations Alternative Test is being used.

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"Qualified Active Low-Income Community Business"

During the term of the NMTC financing, the Borrower must also have:

- less than 5% of the average aggregate unadjusted bases of its property can only be attributable to **"collectibles"** (such as antiques) other than collectibles that are held primarily for sale to customers in the ordinary course of business; and
- less than 5% of the average of the aggregate unadjusted bases of its property can only be attributable to **"nonqualified financial property"** (such as holding cash or cash equivalents, or owning debt, stock, and partnership interests; <u>however</u>, reasonable working capital and construction reserves are permitted above this threshold).

“Qualified Business”

- A **“Qualified Business”** generally includes the acquisition, construction, and renovation of a real estate project, and the purchasing, refurbishing retrofitting, or leasing of equipment, as well any business or nonprofit operations (such as the funding of working capital).
- If a **for-profit** business, it must be reasonably expected to generate revenues (as opposed to net income) within 3 years of the funding of the NMTC financing.
- If a **nonprofi**t organization, it must be reasonably expected to engage in an activity that furthers one or more of its charitable purposes within 3 years of the funding of the NMTC financing.

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Non-Qualified Business

However, a Qualified Business does not include:

- **“**residential rental housing**”** (unless part of a qualified mixed-use project (*i.e.*, if the “80/20 Test” is satisfied));
- farming;
- a business that consists "predominantly" of the development and holding of intangibles for the purpose of sale or licensing; or

- any of the following so-called “Sin Businesses:” (a) a private or commercial golf course; (b) country club; (c) a gambling facility; (d) a racetrack; (e) a hot tub facility; (f) a suntan facility; (g) a massage parlor; or (h) any store the principal purpose of which is the sale of alcoholic beverages for consumption off premises.

If a borrower leases a NMTC financed project, no tenant may be a “Sin Business” (although the other types of businesses listed above may be tenants). However, there are ways to structure the NMTC financing to satisfy this prohibition.

Permitted Uses of NMTC Financing

NMTC financing may only be used by a "Qualified Business" to:

- acquire, construct, renovate and expand bricks and mortar projects (including those relating to healthcare, education, manufacturing, retail, qualified mixed-use (*i.e.*, if the "80/20 Test" is satisfied), cultural, community, renewable energy, recycling etc.); and

- finance business and nonprofit operations (such as those in the nature, as described above), including the purchasing, refurbishing, retrofitting or leasing of equipment, and/or funding working capital, inventory, and staffing etc.

Prohibited Uses of NMTC Financing

NMTC financing may not be used to:

- generally, refinance or prepay existing debt (with certain exceptions), or

- participate in any "abusive transaction" (*i.e.*, any transaction or series of transaction which are contrary to the intent of the NMTC Program).

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Recapture of NMTCs

- The 39% NMTCs are recognized by the NMTC investor over the 7-year NMTC compliance period as follows: 5% in each of the first 3 years, and 6% in the remaining 4 years.
- Unlike other tax credits, if there is a "Recapture Event" during the 7-year NMTC compliance period, 100% of the NMTCs are:
  - "recaptured" from all prior years; and
  - "disallowed" for all remaining years of the 7-year NMTC compliance period.

- However, to date, there has never been a "Recapture Event" in connection with approximately $42 billion of NMTC financings because these transactions are carefully underwritten and monitored, and there are cure periods to remedy certain Recapture Events, depending on the facts and circumstances.

Recapture Events

Subject to certain cure periods, with respect to a borrower, a **"Recapture Event"** includes, but is not limited to, each of the following:

- failure to maintain a "Qualified Business;"
- failure to be a "Qualified Active Low-Income Community Business;"
- using NMTC financing proceeds for a "Prohibited Use;"
- prepayment of any portion of the NMTC financing (including foreclosure proceeds, subject to a cure period);
- if applicable, the "Targeted Populations Alternative Test" is not satisfied; and/or
- participation in any abusive transaction in connection with the NMTC financing.

Recapture Events

- A Recapture Event does <u>not</u> include a foreclosure unless the CDE does not timely redeploy the foreclosure proceeds for another project or to another borrower predominantly located in a "Low-Income Community."
- Each of the NMTC Investor and the CDE (and its related Allocatee) is motivated to work with a borrower during the 7-year NMTC compliance period because:
  - the NMTC Investor has "purchased" the NMTCs (which is the sole source of the Forgivable NMTC Loan; therefore, the NMTC Investor does not expect a return of its capital, which is the "purchase price" of the NMTCs); and
  - the CDE merely facilitates the NMTC financing without using its own funds (*i.e.*, none of its own capital is at risk).

Underwriting Requirements

- Each year "qualified community development entities" ("**CDEs"**) apply to the CDFI Fund (which administers the NMTC Program) for a NMTC allocation authority award (a **"NMTC Allocation Award**"), which is an extremely competitive process.
- If a CDE receives a NMTC Allocation Award, it becomes an **"Allocatee."**
- To be competitive, each potential Allocatee generally commits to satisfy certain high benchmarks in order to demonstrate that the intent of the NMTC Program will be maximized (over and above the minimum standards required by the CDFI Fund, such as targeted and specific types of substantial community impacts and expeditious deployment of its Allocation Award to borrowers and projects).
- Such high benchmarks result in an Allocatee having high underwriting standards relating to borrowers and projects.

Underwriting Requirements

Accordingly, the for-profit's or non-profit's operations or project should satisfy several underwriting requirements, including but not limited to, the following:

- being "Shovel Ready;"
- being located in not only a "Low-Income Community" but also one that is "Highly Distressed" (especially if located in a rural community);
- providing or retaining substantial community impacts to residents in "Low-Income Communities" and "Targeted Populations" (such as "Low-Income Persons," minorities, women and veterans);
- have strong local support; and
- often it is beneficial to be located in an "underserved state," which can include: Alabama, Arkansas, Florida, Georgia, Indiana, Kansas, Nevada, Tennessee, Texas, West Virginia, Wyoming, Puerto Rico, American Samoa, Guam, Northern Mariana Islands and U.S. Virgin Islands.

"Shovel-Ready"

To be **"Shovel Ready,"** a borrower must show that:

- all other sources of financing are otherwise committed (or close to being committed);
- all other conditions are satisfied (or close to being satisfied), such as having site control, zoning approvals, permits, and good title etc.;
- if a for-profit, revenues (as opposed to net income) are reasonably expected to be generated within 3 years;
- if a nonprofit organization, one or more of its charitable purposes are reasonably expected to be furthered within 3 years; and
- substantial community impacts will be timely achieved.

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“Highly Distressed” Low-Income Census Tract

- NMTC financing is much more likely to be provided to a borrower or project, which is located in a “Highly Distressed” “Low-Income Community” (**“LIC”**), which includes a census tract that has either:
  - at least 1 of 4 “primary distress criteria” (such as a poverty rate greater than 30% (compared to the statutory minimum 20%), or being located in a rural community), or

  - at least 2 of several “secondary distress criteria” (such as poverty rates greater than 25% (compared to the statutory minimum of 20%), or satisfying any of the several other secondary criteria etc.).

- The more “Highly Distressed” the LIC, the more likely an “Allocatee” and a NMTC Investor will be interested in participating in the NMTC financing.

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Substantial Community Impact

- A borrower must qualitatively and quantitatively provide support of substantial community impact to the residents of the "Low-Income Community" in which the borrower and/or project is located, surrounding communities and "Targeted Populations" (including "Low-Income Persons," minorities, women and veterans), and execute a "Community Benefits Agreement."
- Such community impact includes any of the following:
  - direct and indirect full-time and part-time job creation, job retention, and construction jobs;
  - jobs that provide living wages, healthcare benefits, retirement plans, life insurance, job training, and/or continuing education;
  - access to public transportation;
  - consumer and/or community goods and services;
  - below-market lease rates and favorable terms to tenants;
  - affordable housing (only if part of a qualified mixed-use project);
  - "green" type benefits (such as satisfying LEED standards); and/or
  - any other community benefits.




Strong Local Support

A borrower must be able to show that the NMTC financing has and will receive strong local support. For example, this can be shown by:

- the project, business or nonprofit being a part of an economic development plan;
- providing letters of support from local officials, community leaders, and/or local businesses and nonprofits;
- receipt of governmental subsidies and private sources of capital; and/or
- there is an expected subsequent catalytic investment in the "Low-Income Community" and surrounding areas.

Good Borrower and Project Candidates for NMTC Financing

Each of the following are good types of for-profit's and nonprofit's operations and projects for the NMTC financing:

- manufacturing facilities/operations;
- health care facilities/operations;
- grocery stores/operations;
- charter and independent schools/operations;
- qualified mixed-use projects (*i.e.*, those that satisfy the "80/20 Test");
- community facilities/operations; and
- renewable energy and recycling facilities/operations.

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Recap of Economic Benefits of NMTC Financing

Generally, the economic benefits of the NMTC financing (whether in the form of the Forgivable NMTC Loan or the Non-Forgivable NMTC loan) include:

- gap financing;
- with approximate 1.5% interest-only payments during the 7-year NMTC compliance period;
- subordination to other creditors;
- nontraditional and favorable terms, and flexible underwriting criteria, such as:
  - the Forgivable NMTC Loan being forgiven at the end of the 7-year NMTC compliance Period, or
  - the Non-Forgivable NMTC Loan with a below-market interest rate and a term up to 40 years (and beyond any secured asset's useful life);
- ability to obtain additional financing;
- ability to "leverage" other sources of financing for a multiplier economic benefit;
- "softer" foreclosure and enforcement rights if there is a default;
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- substantial community and economic impacts to residents in "Low-Income Communities" and "Targeted Populations," including "Low-Income Persons."

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Our Services

- We have facilitated closing approximately $1.1 Billion of NMTC financings over the past 20 years.
- Our financing, legal and accounting backgrounds as well as significant experience in community and economic development enables us to strategically underwrite, structure and close these complex financings on behalf of our clients.

- Generally, all of our fees are contingent upon the securing the NMTC financing.
- Upon engagement we will:
  - promptly provide our Comprehensive NMTC Financing Intake Form, complete application sections with respect to those relating to our services described below, and answer any questions relating to the questions in such form;
  - identify, profile and solicit (a) NMTC Investors (for best pricing and terms); (b) Allocatees (for maximum NMTC Allocation, low fees, maximum forgiveness of the Forgivable NMTC Loan, and other favorable terms); and (c) providers of Leverage Loans needed for the NMTC financing (to create a maximum economic multiplier effect);

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Our Services

- underwrite the NMTC financing to satisfy each of the unique underwriting requirements of each applicable NMTC Investor, Allocatee, and each provider of a Leverage Loan;
- identify and secure other sources of financing (including traditional financing, state NMTCs, and other federal, state and local subsidies);
- structure the overall financing (including not just the NMTC financing) to satisfy specific underwriting, legal and tax requirements of the NMTC Program, and as otherwise required;
- draft detailed and strategic marketing executive summaries of the borrower's operations and project, including but not limited to: (a) a census tract distress analysis; (b) detailed analysis to support the quantification and qualification of community impacts; (c) support that all legal and tax requirements are satisfied; (d) support that all underwriting requirements are satisfied; and (e) support that any other requirements that are unique to the particular overall financing and the structure are satisfied;

Our Services

- prepare financial projections required for the overall financing;
- timely and strategically complete all intake forms from targeted NMTC Investors, Allocatees, and providers of Leverage Loans (as well any intake forms from any other sources of financings or subsidies);
- negotiate term sheets provided by NMTC Investors, Allocatees, providers of Leverage Loans, and any other debt or equity providers;
- provide an efficient timeline with benchmarks through the targeted closing date of the NMTC financing;
- facilitate each closing by collecting due diligence materials and creating a drop box;
- manage the closing and funding;
- provide ongoing asset management, compliance and reporting services; and
- provide such other services as set forth in our Consulting Agreement in order to "quarterback" the facilitation of the overall financing.

Questions

If you would like to apply for NMTC financing, please click on the green tab, entitled "Apply for NMTC Financing," which is located in each our New Markets Tax Credit web pages with respect to borrowers.

If you have any questions regarding this presentation, please click on the green tab, entitled "Contact/Initial Intake Form," which is located at the top right side of Community Reinvestment Associates' main website page.

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