BOSTON FINANCIAL
INVESTMENT MANAGEMENT

Housing Credits & Opportunity Zones – Strange Bedfellows

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Housing Credits & Ozones – Is There a Match?

- In theory, there should be a perfect match since affordable housing is needed in every one of the 8,700 designated opportunity zones

- When we look at the list of all the developments in the country that have qualified for 9% allocations and/or for 4% credits, roughly 30% of these projects are located in qualified opportunity zones (Ozones)

- Unfortunately, there is a serious mismatch between these opportunities and the LIHTC equity market. 85% of the equity for housing credit projects comes from commercial banks. Banks are not permitted to own equity investments, which means they do not have the capital gain income required to benefit from Ozone incentives

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- Another cause for mismatch arises from the fact that acquisition/rehab projects do not qualify for Ozone benefits unless the cost of the rehabilitation exceeds the property's income tax basis. Substantial rehab & historic credit developments will qualify

- To further complicate the formation of capital for LIHTC/Ozone projects, the IRS issued regulations in March that effectively put LIHTC projects at a serious disadvantage to "conventional" Ozone developments. The industry has worked hard to convince IRS and Treasury to "fix" their regulations…and we are cautiously optimistic that we will see amended regulations in November.

Has any Ozone/LIHTC investments closed?

- The short answer is “yes”… but the reality is that the potential Ozone benefits available to most LIHTC projects syndicated in 2019 have, due to the mismatch and IRS issues, effectively been frittered away.

- My best guess is that no more than a dozen or two Ozone/LIHTC investments have been syndicated this year.

- Boston Financial has placed two such investments with a West Coast bank in Gunnison, Colorado and Tigard, Oregon. We currently expect to close three additional opportunity zone investments with a MidWest life insurance company before year end.

Garden Walk of Gunnison

- 36 units in Gunnison, CO for families
- Developed by Belmont Development (OK City, OK) in partnership with Gunnison Valley Regional Housing Authority
- 11% hard debt ($34k/door)
- Significant soft funding from state and local agencies
- OZ Pricing likely provided between 3-4 additional cents of equity, which turned out to be crucial when the GP encountered a lack of GC bids (2 total) and cost escalation of 15%
- Closed in September 2019, completion in October 2020

Red Rock Creek Commons

- 48 units in Tigard, OR (part of Portland MSA) for families and households experiencing mental illness
- Developed by the Community Partners for Affordable Housing (CPAH)
- 27% hard debt, despite being a 4% transaction, thanks to significant soft funding by the city and state ($5.6M or 38% of capital stack)
- OZ pricing provided between 1-2 additional cents of equity, but more importantly, gave the sponsor Y15 comfort given our understanding of exit tax treatment under OZ investment rules (Federal tax is not charged to OZ investments), as due to the large soft funding, the capital account is negative in Y11 and grows significantly by Y15
- Closed in Sept 2019, completion in October 2020