

Memorandum



DATE January 15, 2010

TO Members of the Economic Development Committee: Ron Natinsky (Chair),
Tennell Atkins (Vice-Chair), Dwaine Caraway, Jerry R. Allen, Sheffie Kadane,
Ann Margolin, Linda Koop, Steve Salazar

SUBJECT **New Markets Tax Credit Program**

At your January 19, 2010 meeting, you will be briefed on the "New Markets Tax Credit Program." A copy of the briefing is attached.

Should you have any questions, please contact me at (214) 670-3314.



A.C. Gonzalez
Assistant City Manager

C: The Honorable Mayor and Members of the City Council
Mary K. Suhm, City Manager
Deborah Watkins, City Secretary
Tom Perkins, City Attorney
Craig Kinton, City Auditor
Judge C. Victor Lander, Administrative Judge Municipal Court
Ryan S. Evans, First Assistant City Manager
Forest Turner, Assistant City Manager
Jill A. Jordan, P.E., Assistant City Manager
Dave Cook, Chief Financial Officer
Jeanne Chipperfield, Director, Office of Financial Services
Karl Zavitkovsky, Director, Office of Economic Development
Hammond Perot, Assistant Director, Office of Economic Development
Theresa O'Donnell, Director, Development Services
Helena Stevens-Thompson, Assistant to the City Manager

New Markets Tax Credit Program

Economic Development Committee

January 19, 2010



Briefing Purpose

- Provide an update on Dallas Development Fund's Application for an allocation to the federal New Markets Tax Credit (NMTC) program
- Review guidelines of the NMTC program
- Present necessary bylaw and certificate of formation changes and seek committee approval to pursue next steps

New Markets Tax Credit (NMTC) Overview

- **NMTC attract private investment** for business and real estate developments in **Low Income Neighborhoods**
- NMTC is **federal tax credit program** created in 2000 and renewed through 2009
 - U.S. Treasury administers
 - Allocations made directly to local Community Development Entity (CDE)
 - Tax credit is **39% of original investment over 7 years** (5% first three years, 6% last four)
- NMTC program offers **additional financial tool** to achieve Dallas' development goals, particularly in southern Dallas (see Appendix B)

NMTC Overview (cont'd)

- Funds can be used for debt or equity financing in combination with Public Private Partnership and TIF subsidies
- Targets commercial, industrial, not-for-profit and operating businesses and mixed use (rental housing less than 80% of income)
- A **community development entity (CDE)** (non-profit or for-profit) must be **formed to apply** for the program and a for-profit CDE must be **formed to accept** the NMTC allocation.

NMTC 2009 Awards

- **Dallas' award is for \$55 million**
- In 2009, a total of \$5 billion in tax credit allocation was awarded
 - \$1.5 billion of this was stimulus funded
- 249 CDEs applied for an allocation; 99 were awarded funds (40%) (See Appendix C for historical data)
- Total request of funds was \$22.5 billion
 - 22% of total request was awarded
- Allocation size ranged from \$4 million to \$125 million.
 - Median award was \$50 million
- 16% (16) of awarded CDEs were government-controlled
 - Received \$790 million in allocation (average award \$49 million)

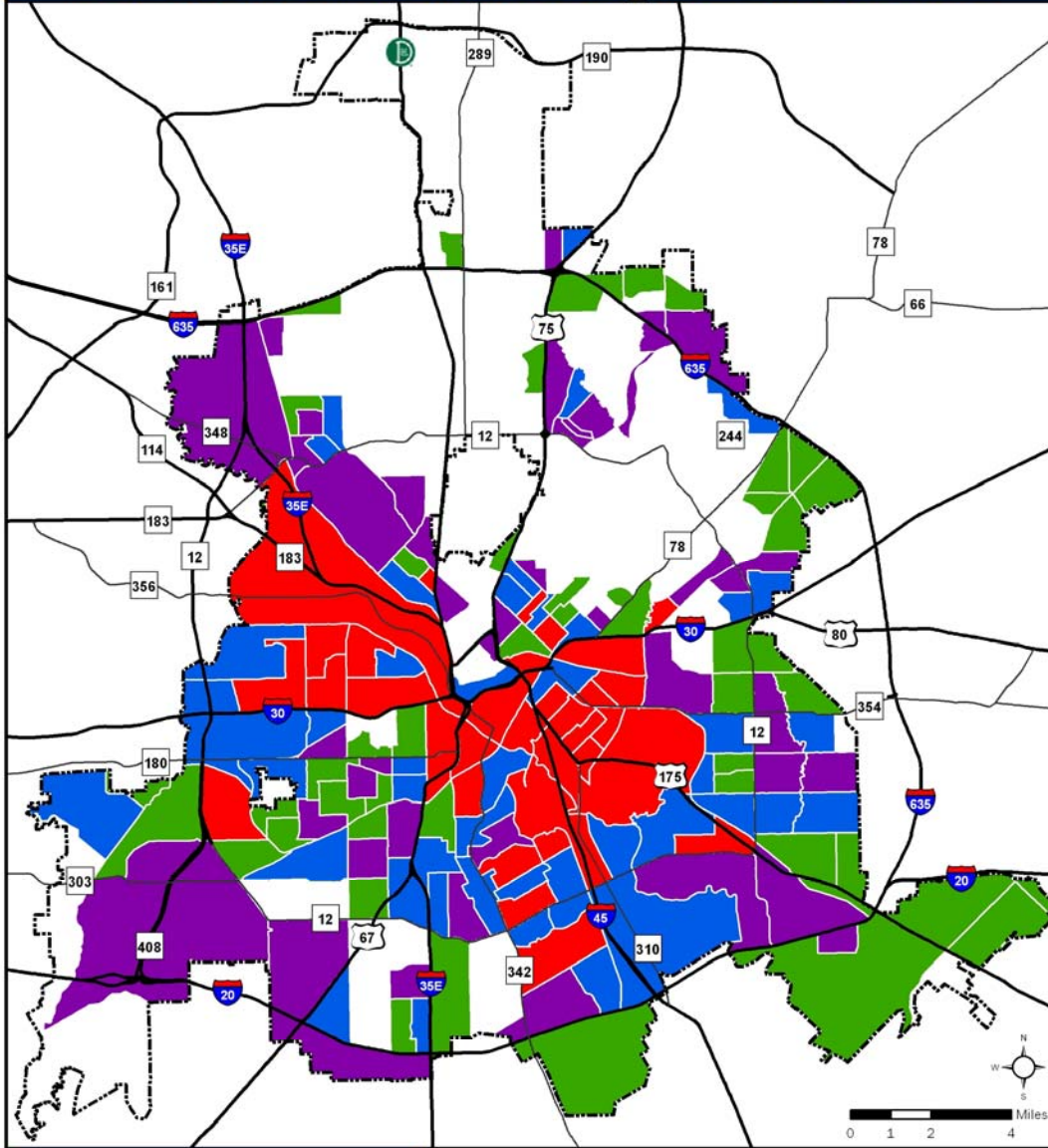
NMTC Net Award Less Than Allocation Amount

- Award amounts relate to the amount of investment that can receive a credit (not \$ value of credits awarded)
- The net dollar amount of the DDF \$55 million award is approximately \$14 million
 - $\$55\text{M} \times \$.39 \text{ credit amount} \times \$.72 \text{ (market rate of credits)} - 3\% \text{ QEI (DDF overhead)}$
- Private investors discount 39% tax credit to reflect net present value of a 7-year credit. Amount of discount varies with market conditions

Types of Eligible Projects

- Allocation award depends on applicant's strategy to use the tax credits to support eligible development projects
- **DDF's application highlighted** multiple types of projects for priority funding under the NMTC program:
 - **Transit-oriented development**
 - **Job training facilities**
 - **Mixed use (retail and housing)**
- Several types of projects are not eligible:
 - Those that derive more than 80% of gross rental income from rental dwelling units
 - Golf courses, race tracks, gambling facilities, country clubs, massage parlors, hot tub facilities, suntan facilities, liquor stores
- All projects must be in NMTC-eligible areas
 - Eligible areas determined by poverty rate, unemployment and median family income
 - Distress criteria: 1) a poverty rate of at least 30 percent; 2) a median family income at or below 60 percent of the applicable area median family income; or 3) an unemployment rate at least 1.5 times the national average.

New Markets Tax Credits: Eligible Census Tracts



City of Dallas
Office of Economic Development



Research & Information Division
(214) 670-1685
<http://www.Dallas-EcoDev.org>

Created 1/28/09. Last Updated 4/22/09 - NMTC_Final TCG

Legend

- Eligible, Not Distressed
- Eligible, Meets One Distress Criterion
- Eligible, Meets Two Distress Criteria
- Eligible, Meets Three Distress Criteria
- Not Eligible
- ⋯ City of Dallas
- Freeway
- Highway

Source: US Census Bureau, 2000

Benefits of the NMTC program

- An **additional financial tool** to achieve Dallas' development goals, particularly those in southern Dallas neighborhoods
 - Focuses on (federally defined) Low-Income Communities and Low-Income Populations (see Appendix A)
- Funds can be used for **debt, equity or “hybrid” financing**
 - Projects include commercial, industrial, institutional, not-for-profit
 - For-sale housing (challenging due to 7-year time frame)
 - Mixed-use projects, with rental housing less than 80% of income
 - Operating businesses
- An important **supplemental layer** that complements conventional debt and equity financing as well as existing city subsidy programs.

Potential Risks of NMTC Program

- A CDE that does not properly manage program compliance **can create additional tax liability** for investors related to credit previously claimed plus interest
- Three things can trigger a recapture event:
 - CDE ceases to be certified as a CDE
 - CDE does not satisfy the requirement to invest a minimum of 85% of their qualified equity investments within 1 year of receiving investment
 - CDE redeems the investment
- A Dallas CDE **will require experienced program administrators** that can be funded from **investor proceeds**

Risk Mitigation/Program Compliance

- Steps taken to address compliance and risk factors
 - In February 2009, the **Dallas City Council** created the **Dallas Development Fund (DDF)** as a non-profit corporation as the vehicle **to apply** for New Markets Tax Credits
 - **DDF was certified** as a Community Development Entity (**CDE**) and applied for \$125 million in NMTC allocation under the 2009 funding round
 - **DDF was awarded a \$55 million allocation** on October 30, 2009
- DDF is a community-based board approved by Council on February 9th and May 13th, 2009
 - See Appendix D for current board members

Risk Mitigation/Program Compliance

- DDF may enter into and make contracts, employ agents, employees and consultants as necessary to carry-out the purposes of the Corporation, solicit proposals from low-income businesses and from potential investors in the NMTC program for projects related to the City's NMTC program, and attain and maintain its status as a qualified CDE.
 - DDF remains independent from Dallas Council based on guidance from CDFI stating Governing Board of CDE must be autonomous in decision making
- Underwriting and project evaluation criteria are being developed by the DDF
 - Primary objectives for NMTC projects include job creation, Southern Sector projects, and the use of other City funds
 - Projects will be solicited and initially reviewed by City Staff, but underwritten by third party consultant with expertise in structuring NMTC deals
 - DDF will primarily be staffed by City Staff, but experienced third-party assistance will be needed for underwriting and deal structuring, accounting and compliance and legal counsel
 - \$1.65 million is available under the allocation for this outside assistance over a 7 year period

Creation of For-Profit Subsidiaries

- For-profit subsidiaries must be formed to accept any NMTC allocation
- For accounting purposes, it is recommended to form one subsidiary for each project
 - Project subsidiaries must be certified as CDEs
 - Recommend creating five for-profit project subsidiaries
- Two additional subsidiaries (management and holding) are created to form an LLC for DDF operations
 - The management and holding subsidiaries will each have a 50% ownership position in the for-profit CDE's until individual transactions close.
 - After the transactions close, the DDF subsidiaries will transfer ownership to individual project tax credit investors who become 99.9% owners of each for-profit CDE
 - DDF management subsidiary will retain a .01% ownership as well as management responsibility (see Appendix E for diagram)
- Under the Texas Constitution, these for-profits must be independent from the City of Dallas

Recommended Bylaw Changes

- To create the for-profit entities necessary to accept the NMTC allocation and remain in compliance with Texas law, changes to the DDF bylaws and certificate of formation are necessary
 - New Board Structure: Create two classes of directors with three (3) class I directors appointed by the City Manager and the remaining four (4) self-elected (no change to current board members)
 - Class I Directors must vote unanimously on matters related to investment/deal decisions, including project development agreements, and any changes to the DDF certificate of formation and/or bylaws which would change the Class I Directors' control over investment/deal decisions
 - In addition to the unanimous Class I vote, there must be at least one vote from Class II for matters listed above.
 - All other matters require a majority vote regardless of Class I or II
 - LIC representation changes from a minimum of 5 to 3 out of 7 board directors
- Council will no longer approve DDF's board members, bylaws and certificate of formation (and any amendments thereto), and the organizational documents for any for-profit CDE that the Corporation may create
- The City Council will approve all development agreements for projects.

Next Steps

- To be able to accept the awarded NMTC allocation, **DDF needs to create for-profit subsidiaries** (January)
 - Requires City Council approval to modify bylaws and certificate of formation to allow for the independent creation of up to seven for-profits
 - Five of these for-profits will be submitted for CDE certification, the other two are for management and holding purposes to facilitate DDF operations
 - The **for-profit CDEs** will eventually be aligned with an **individual DDF NMTC project**
- DDF needs ongoing professional and technical assistance to support City staff in operating the NMTC program (January/February)
 - OED issued **an RFP to solicit a consultant** to assist with initial deal structuring and FY2010 NMTC allocation request. Will seek Council approval on **February 24**
 - DDF will also need **outside legal and accounting assistance** which may require **additional RFPs**
 - Consultants will be **funded by DDF once DDF closes a deal** (has cash flow)
 - DDF will enter into a **contract with COD** to formalize relationship and create management control, including payment structure for bridge funding from PPP program (as needed for underwriting, compliance and legal assistance)

Next Steps (cont'd)

- DDF anticipates providing information about the Dallas NMTC program and application process and receiving initial applications for funds in February
- It is likely that 3-4 projects can be assisted through the FY09 allocation under the NMTC program
- An application for FY10 funds would potentially be due in June 2010.

Recommendations

- Approval by Economic Development Committee for consideration by City Council on January 27 to:
 - Amend current DDF by-laws and certificate of formation to allow DDF to independently create up to seven (7) for-profit DDF subsidiaries which will be submitted for CDE certification for the purpose of accepting the \$55 M NMTC allocation and facilitating the disbursement of tax credits and investment of proceeds

Appendix A

Acronyms and Definitions



Acronyms

- CDE– Community Development Entities
- CDFI– Community Development Financial Institutions Fund
- LIC– Low-Income Communities
- QEI-- Qualified Equity Investments

Definitions

- Low Income Communities:
 - Eligibility for Census tracts in Dallas
 - At least 20% poverty rate; OR
 - The median family income does not exceed 80% of the area median family income
- Low Income Persons
 - For Dallas, an individual (adjusted for family size) with an income no larger than the greater of
 - 80% of the statewide median family income OR
 - 80% of the metropolitan area median family income

Definitions

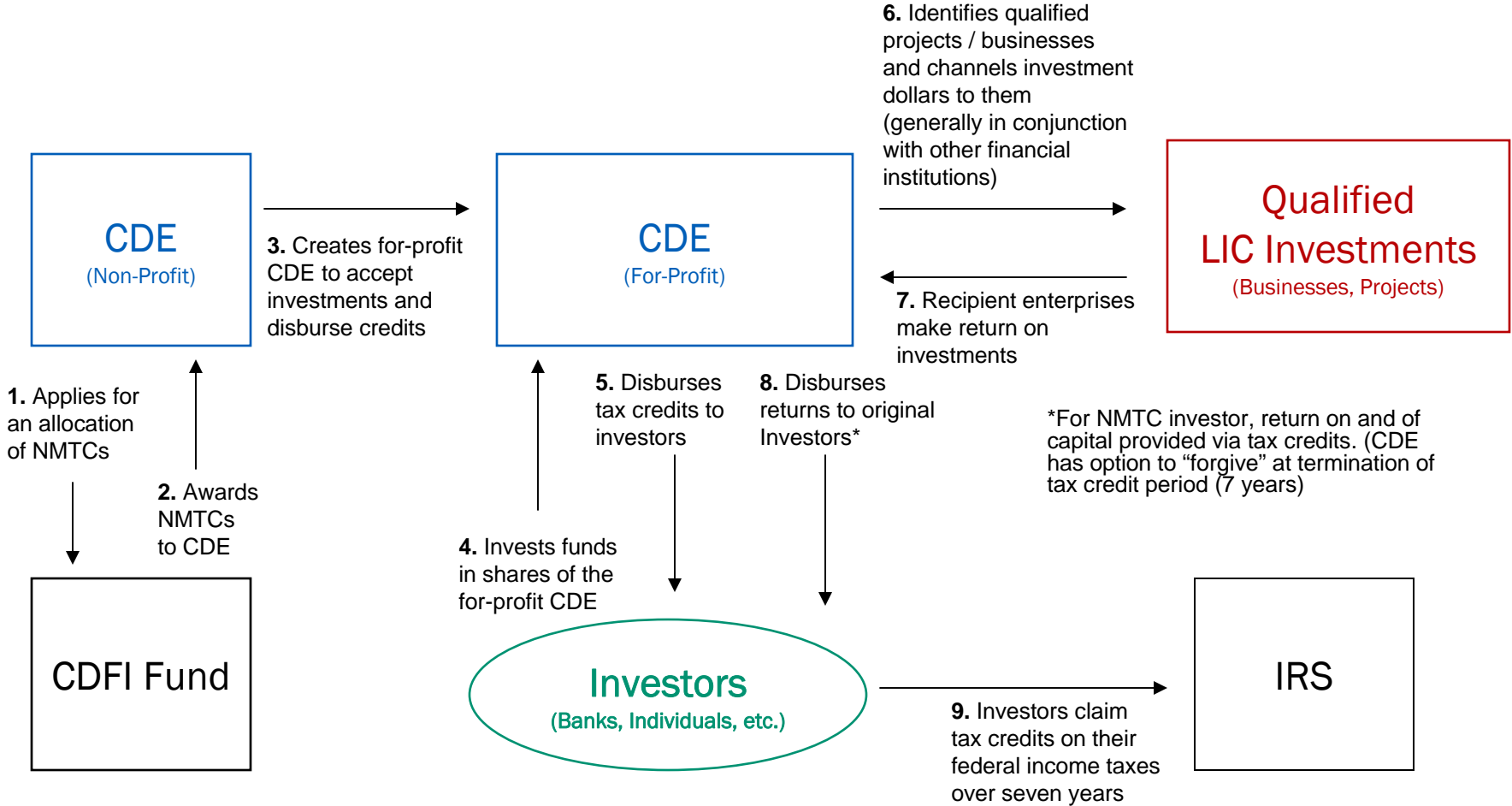
- Qualified Equity Investments
 - An equity investment (stock in a corporation or any capital interest in a partnership) in a CDE
 - The equity investment must be acquired by the investor at its original issue solely in exchange for cash
 - Must be designated by the CDE

Appendix B

Illustrative NMTC Use



Illustrative NMTC Use

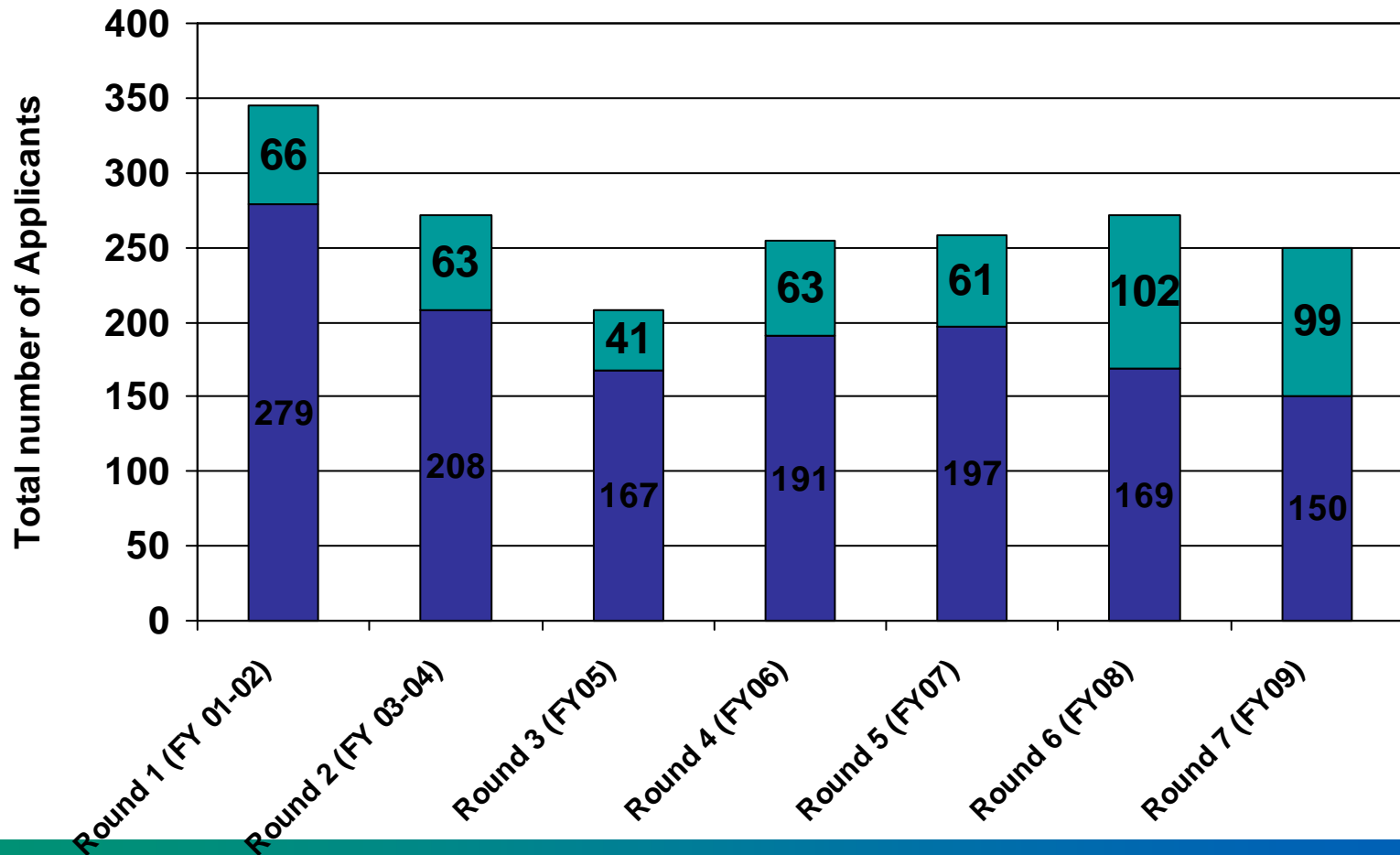


Appendix C

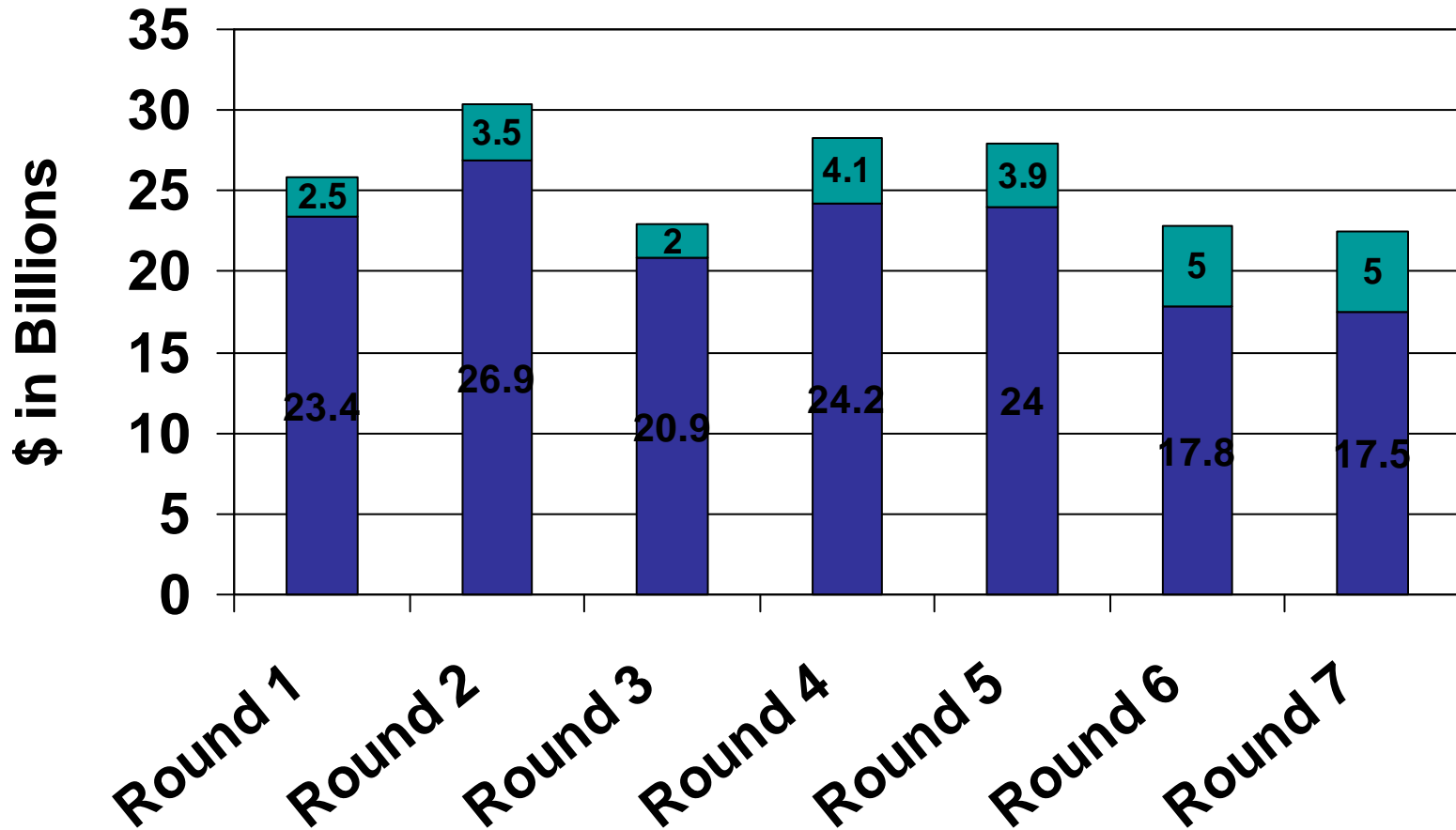
Historical Data on Award Recipients



Applicants and Number of Awards



Amount Requested v. Amount Awarded



Appendix D

DDF Board Members



Dallas Development Fund Board Members

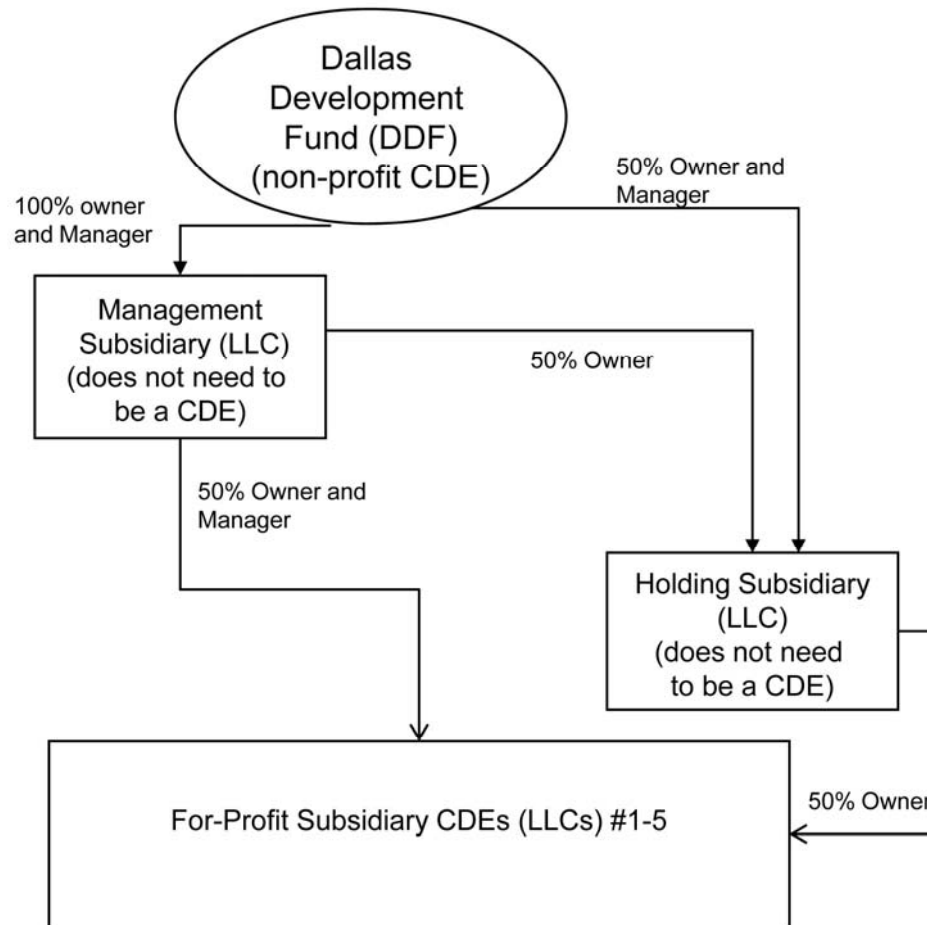
- Gilbert Gerst (President)
 - Vice President, JP Morgan Chase
- Brentt Shropshire (Vice President)
 - Partner, SDL Citadel Global, LLC (Renewable energy company)
- Zenetta Drew (Treasurer)
 - Executive Director, Dallas Black Dance Theater
- Anthony Pace
 - Executive Director, PLAN Fund (Community micro-lending institution)
- Bill Hall
 - Senior Director of Operations for Dallas Area Habitat for Humanity
- Edward Okpa
 - Principal of The OKPA Company, LLC, with appraisal and brokering commercial real estate experience
- Maria Gonzalez
 - Former Washington Mutual executive, with over 15 years experience in real estate industry and asset management experience

Appendix E

DDF For-Profits Structure



DDF For-Profit Structure Model (Before Transactions Close)



DDF For-Profit Structure Model (After Transactions Close)

