Financial Modeling for Affordable Housing – Post HR-1

Jon Peterson, Winthrop & Weinstine, P.A.
Amy Broadwater, RubinBrown LLP

October 3, 2018
Agenda

- The importance of financial projections
- Common pitfalls encountered when a complete set of financial projections are not utilized
- What’s in a financial model?
- How have financial models for low-income housing tax credit deals changed post HR-1?
The Importance of Financial Projections

- Document the expectations of the deal for all parties
- Identify issues prior to closing
  - Eligible basis issues
  - 50% test issues
  - 704(b) issues
  - Placement in service issues
  - First-year credit issues
Common Pitfalls

- Incorrect split between land and building
- Including bond issuances costs in eligible basis
- Not discussing relocation costs
- Not thoroughly discussing first-year and second year credits in an occupied rehab project
- Not looking at the 50% test
- Not identifying capital accounts issues during the credit period
What’s in a financial model?

- Deal assumptions
- Sources and uses
- Credit calculations
- Rent analysis and operating expenses
- Lease up assumptions
- Amortization and depreciation
- Loan Amortization
- Taxable income and cashflow schedules
- Benefit / IRR schedules
How have financial models changed since HR-1?

- Corporate investor tax rate changed
  - The corporate federal rate is now 21% versus 35%.

- Limitations on interest expense deductibility
  - Net interest expense deduction will be limited to 30% of adjusted taxable income
    - The definition of adjusted taxable income changes after 2021.
  - The disallowance of interest expense occurs at the partnership level.
  - Effective for all deals for tax years beginning after December 31, 2017
How have financial models changed since HR-1?

- **Limitations on interest expense deductibility (cont.)**
  - Real Property Trade or Business election can be made
    - Requires the partnership to use the ADS life for depreciating the residential real property.

- **Depreciation changes**
  - Bonus depreciation percentage increased to 100% for qualified property placed in service after September 27, 2017 and before 2023.
  - Developers are being asked to better identify qualified property (personal property and land improvements) in the financial models.
  - Depending on the deal, you may want to elect out of bonus.
How have financial models changed since HR-1?

- **Historic rehabilitation credit changes**
  - Repeal of the 10% credit for pre-1936 buildings
  - 20% credit remains, but the credit will be claimed ratably over 5 years
  - Transition rule for QREs incurred with respect to a certain historic structure that was owned or leased at all times on or after January 1, 2018

- **Opportunity Zones**

- **Repeal of technical terminations**
  - This may impact syndicated fund models.
Contact Information

- Jon L. Peterson
  - Winthrop & Weinstine, P.A.
  - Email: Jpeterson@Winthrop.com
  - Phone: 612-604-6736

- Amy L. Broadwater
  - RubinBrown LLP
  - Email: amy.broadwater@rubinbrown.com
  - Phone: 615-480-2871