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## HISTORIC TAX CREDIT TOOL BOX

# Historic Tax Credits and the Community Reinvestment Act



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**F**For developers using historic tax credits (HTCs) as part of their funding, one critical challenge is finding their HTC investor.

For most larger projects, negotiations are project-specific—and in most marketplace negotiations, competition can and does make a difference. The more suitors, the better one's negotiating position.

Often, the negotiation is a nuts-and-bolt number crunch. But sometimes thinking outside the box can also help. One “outside the box” consideration is understanding whether your HTC project may be valuable to an investor's Community Reinvestment Act (CRA) responsibilities.

In 1977, in the face of growing urban decay and a lack of community investment, Congress enacted the CRA. In particular, the intent was to curtail the practice of redlining, where banks in the past had been accused of denying credit to minority and small-business borrowers in economically depressed neighborhoods, regardless of their credit-worthiness. The CRA is designed to encourage regulated financial institutions to help meet the credit

needs of their entire communities. CRA regulations establish the framework and criteria by which regulating agencies assess an institution's record of helping to meet the credit needs of its community, including low- and moderate-income neighborhoods, consistent with safe and sound operations. The regulations provide different evaluation standards for institutions of different asset sizes and types. Each bank then develops its own plan to comply with the CRA.

Investments using low-income housing tax credits (LIHTCs) or new market tax credits (NMTCs) are popular with investment institutions because both programs by statute target benefits to low-income areas. The same may be anticipated for projects located in opportunity zones where opportunity funds are used in conjunction with investments by financial institution.

continued on page 2



continued from page 1

Because of the clear statute requirements, for CRA purposes, combining HTCs with the 4 percent LIHTC is attractive. It is direct investment into a distressed community with clear and tangible results. These projects can take many forms. One example of an impactful CRA project is Spring Garden School No. 1 in north Philadelphia.

Built in 1928, the school was closed for nearly 40 years. Help USA, a New York-based nonprofit dedicated to housing and helping the homeless and people in need,

adapted the school into the Lural Lee Blevins Veteran Center with affordable housing units

*Image: Courtesy of David Sundberg*  
**The former Mechanics & Farmers Savings Bank in Bridgeport, Conn., was adapted into offices and apartments, using new markets tax credit and historic tax credit equity.**

with preference for veterans and on-site public health support service.

A substantially different, but also CRA-impactful, development can be found in Newburgh, N.Y. There, the Rural Ulster Preservation Company, in cooperation with the Newburgh Community Land Bank, acquired 15 individual buildings in the city's long-distressed East End Historic District and renovated them for affordable housing. Both the Spring Garden and Newburgh projects combined LIHTC with HTC to make the financing work.

Not every CRA impactful project needs to be affordable housing. Redevelopment in distressed areas that creates permanent jobs and economic development is

continued on page 3

continued from page 2

also valuable as direct investments in distressed census tracts. One good example here is the Mechanics & Farmers Savings Bank in downtown Bridgeport, Conn. The building had been vacant since the 1990s. Forstone Capital adapted the savings bank into offices for an architectural firm and 30 one-bedroom, market-rate apartments in an interconnected former office building, known as McLevy Square. Even further afield was the renovation of a 19<sup>th</sup>-century armory in Portland, Ore. Abandoned and derelict by the 21<sup>st</sup> century, Gerding-Edlen Development transformed the one-of-a-kind 56,000-square-foot building into a state-of-the-art multi-stage performance venue for Portland Center Stage. Both projects relied on HTC for funding but also NMTC.

Historically, however, stand-alone HTC projects—that is, projects that did not also use LIHTC or NMTC, did not have the same CRA impact—even though roughly two-thirds of all HTC projects are in low-to-middle-income census tracts. The primary reason is that unlike LIHTC and NMTC, where program regulations require LMI (low-moderate income) investment, the HTC program does not by statute specifically require investments in low-income communities. Thus, these projects on their own were not especially impactful to a bank's CRA record. That has recently changed.

In 2014, bank regulators prepared a questions-and-answers document aimed at helping financial institutions determine whether proposed financing counted toward their CRA obligation. With comment from the Historic Tax Credit Coalition, National Park Service, National Trust for Historic Preservation and others in the HTC community, the resulting Q&A document, issued in 2016, highlighted three types of HTC transactions:

- HTC investments in space leased to small businesses that provide permanent jobs to low-income persons,

in LMI communities, or in areas designated for economic development are CRA eligible;

- Transactions that provide direct benefits to LMI individuals—such as affordable housing or job training centers—can earn CRA credit; and
- HTC investments in projects that stabilize or revitalize LMI communities (as defined by the Department of Housing and Urban Development), disaster areas, certain rural census tracts, or designated economic development districts also qualify as CRA eligible.

The upshot is that under this revised guidance, many HTC projects that may not have previously qualified to earn CRA credits for bank investors will now qualify. There is the nexus with LIHTC and NMTC, but standalone commercial HTC projects may also qualify depending upon location and function.

John Leith-Tetrault, then president of the National Trust Community Investment Corporation, provided an update on the clarification in the September 2016 *Novogradac Journal of Tax Credits*. According to guidance issued by the Office of the Comptroller of the Currency in 2017, “Banks that finance or invest in HTC properties located within the bank's assessment area(s) may receive CRA consideration, to the extent that the activities meet the definition of community development. In addition, financing or investing in HTC properties located in the broader statewide or regional area that includes the bank's assessment area(s) and that meet the definition of community development may also be eligible for consideration. Examiners consider these activities even if they do not benefit the bank's assessment area(s), as long as the institution has been responsive to community development needs and opportunities in its assessment area(s).”

On a practical basis, there is no direct link between the CRA and securing financing for a possible HTC project. Nonetheless, as with any negotiation, having

continued on page 4



*Image: Courtesy of HUGH LOOMIS*  
**The former Spring Garden School No. 1 in North Philadelphia is now the Lural Lee Blevins Veteran Center.**

continued from page 3

full knowledge of how a project may or may not fulfill a funding institution’s CRA obligation is important. HTC projects, along with LIHTC and NMTC investments, are routinely highlighted. For example, the current U.S. Bank CRA performance evaluation for Cincinnati (the bank’s fourth-largest rated area of 39) led the investment section with “A \$12 million HTC investment relating to the acquisition and restoration. ... The building was rehabilitated into a hotel, art gallery, restaurant and conference meeting space.”

In seeking HTC investors, here are a few basic questions that every developer should know:

- Is my potential funder subject to CRA? If the institution is governed by the Federal Reserve Board, the Federal Deposit Investment Corporation or the Office of the Comptroller of the Currency, then the answer is “yes.” If the answer is yes, it would be a

good idea to ask for the funder’s CRA performance evaluation. These reports are often available online.

- Does my development use LIHTC or NMTCs? If so, by program regulations, the project is defined as contributing to a funding institution’s CRA.
- Is my project located in a low- or moderate-income area, or has it been designated as an economic development area? One good source is the Federal Financial Institutions Examination Council website ([www.ffiec.gov](http://www.ffiec.gov)), which includes a current spreadsheet of distressed and underserved tracts. You might also check with your community’s economic development office to see if the building is located in a designated economic zone and FEMA’s website for declared disaster zones.
- How does my project contribute to the institution’s CRA strategy or to the broader CRA goals? Does my project create new permanent jobs? Does it provide direct benefit to low-or-moderate households, such

continued on page 5

continued from page 4

as job training? Generally, the accepted threshold for defining such a contribution is 50 percent of the leasable space. Thus, a 5,000-square-foot service center in a 50,000-square-foot building would not be considered consequential, while a 25,000-square-foot space would.

The key point here is for the developer to think beyond the transaction with the HTC investor as just a question of financing. As with any negotiation, it is important to understand the benefits to the other side of the table.

CRA benefits do not inherently change the calculation, but with some due diligence, it may be possible to broaden the possible funder pool and/or convince possible funders of benefits beyond just the numbers. ❖

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