affordable housing

Developers Gain Welcome Boost

New firm launches alternative financing for developments that reserve at least 20% of their units for low-income residents. **By Donna Kimura**

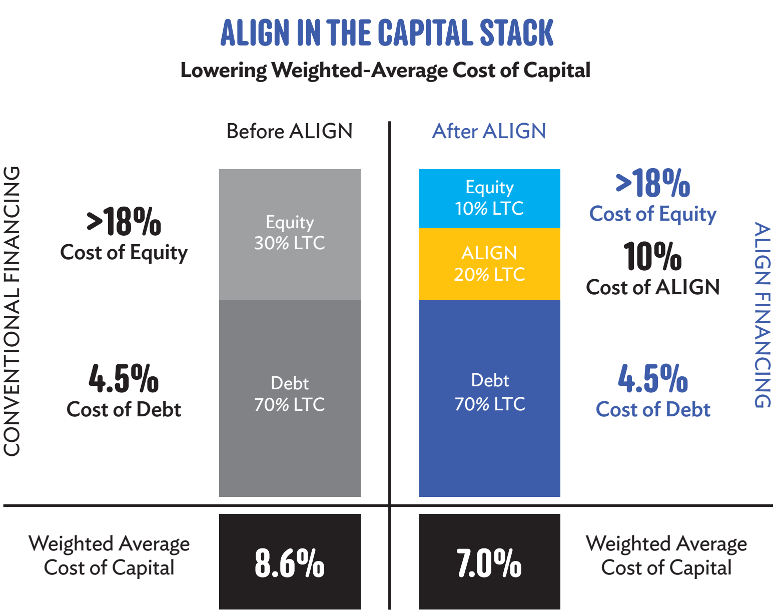
THERE MAY BE A NEW WAY TO FINANCE APARTMENT PROJECTS THAT INclude affordable housing.

Align Finance Partners, a recently formed private commercial real estate finance firm, plans to provide subordinate gap financing for the acquisition, renovation, and development of multifamily properties in the West.

The financing will be structured as a tax-exempt private-activity housing bond or 501(c)(3) bond, secured by a second deed of trust on the property or interest in the ownership entity.

"We've created something new that hopefully benefits the industry in a big way," says Michael Costa, president of Highridge Costa Cos. and one of the founders of Align. A veteran affordable housing developer, Costa says he saw a need for an additional financing vehicle at a time of rising interest rates and changes brought on by tax reform.

As a first step, Align is creating a bond fund with the goal of investing $100 million to $150 million in tax-exempt subordinate bonds. So far, the company has raised about $50 million and expects to hit its fund-raising target by Q1'19. The goal is to create a financing platform that will lead to increasing the number of affordable units leased by low-income families.



Source: Align Finance Partners

Align's founders also expect the fund to be attractive to investors for two reasons: It offers federally tax-exempt returns (and, in some cases, state tax exemptions), and it meets the criteria for impact investing by promoting more affordable housing.

For high–net worth investors, the 10% tax-exempt bond has a tax-adjusted effective yield of 14% and aligns with the firm's mission to have a double–bottom line investment opportunity. The subordinate bonds are intended to provide financing for the portion of the capital stack between 60% and 90% loan to value. Loan amounts will be between $5 million and $15 million.

"[The] program will provide the second-position B bond to an A-position tax-exempt bond financing," says Costa. This is unique because traditional sources of funding usually only provide the A piece.

Qualifying projects must reserve a minimum of 20% of the units for low-income residents. The fund will be designed to provide investors with a stable, tax-exempt cash flow while providing affordable housing with needed mezzanine capital, say Align's leaders.

Costa says potential borrowers include nonprofit organizations that are general partners of exiting low-income housing tax credit properties in years 10 to 15 of their cycles and want to buy out their tax credit partners. These owners can create a 501(c)(3) tax-exempt bond A piece, and then Align can attach a B piece that's 501(c)(3) bond as well. The new fund's subordinate financing can help the nonprofits facilitate the early purchase of the limited partner in their existing partnerships, says Costa.

Other potential borrowers include large, market-rate multifamily developers who face inclusionary zoning requirements. The new fund looks to save these developers money by switching them to a tax-exempt bond financing structure. "We're working with a borrower that has a Los Angeles project fully entitled to include 18% affordable units," notes Costa. "We proved that moving the affordable unit count to 20% would yield the borrower greater financial returns to their investors and produce more affordable units the city truly needs."

The objective is to replace a large chunk of what normally is very expensive "profit participating" mezz and/or equity above a typical first loan, at 70% of cost, with a fixed-rate "B" loan up to 90% of cost, according to Costa.

Other founding partners of the company are Robert Tetrault, CFO and senior vice president at Highridge Costa, and Michael Potter and Dani Evanson, managing directors of Regis Metro Associates, a real estate investment management firm. MFE