

TAPPING INTO BOND FINANCING

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Ideas to build on.™

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Combining Tax Exempt, Short-Term Bonds with Taxable GNMA Sale for Affordable Apartment Financings

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- ❑ In the fall of 2008 the world of long-term debt investors fled to the safety of U.S. Treasury bonds.
- ❑ At the same time, yields on tax exempt municipals soared to new heights as concerns about credit quality and liquidity mounted.

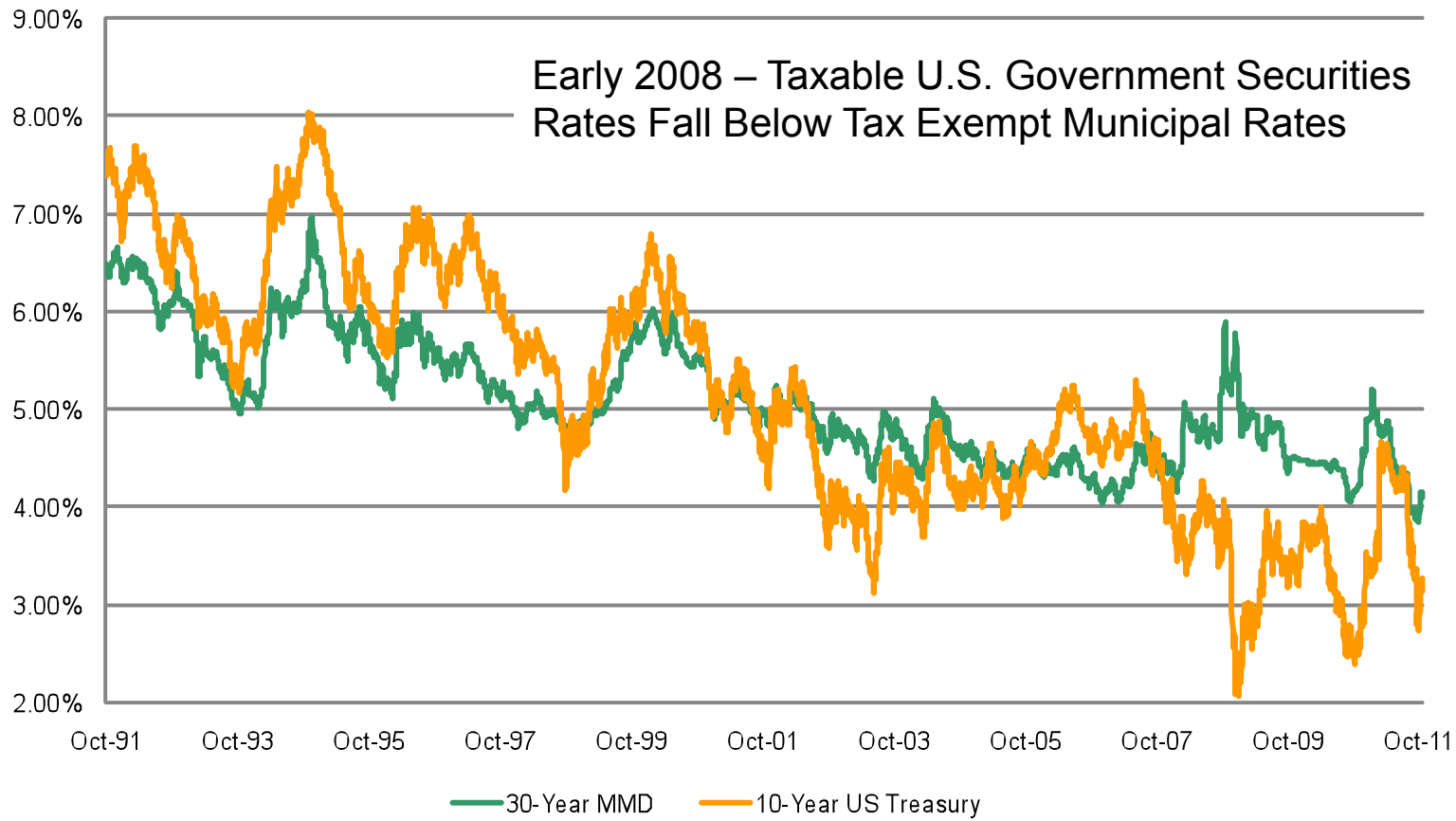
- ❑ Long-term AAA rated bonds rates soared above the rates of federally taxable US Treasury Bonds
- ❑ We are in an upside down world today with continuing economic uncertainty in Europe
- ❑ And with the uncertain future of municipal bonds

WHY TAXABLE GNMA'S? THE POST 2008 WORLD OF UPSIDE DOWN RATES

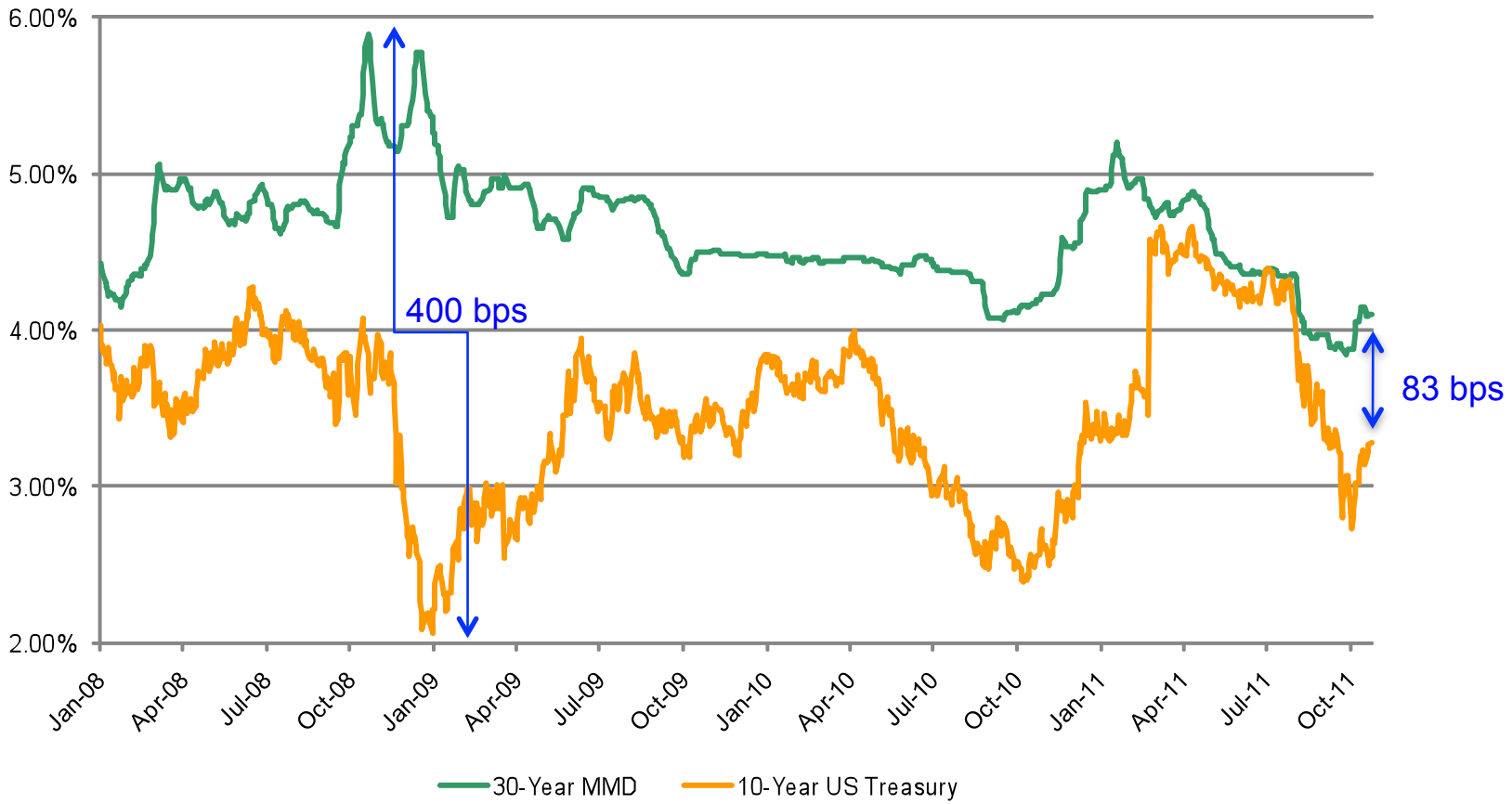


- Following charts show long-term tax exempt municipal yields (30-year MMD) have been significantly higher than comparable taxable U.S. Treasury yields
- At peak (early 2009), 400 basis points “upside down,” today, still 83 basis points upside down

**Long Term Rate Comparison: 30-Year MMD (Tax Exempt)
(Green Line)
versus 10-Year Constant Maturity Treasury (Taxable)
(Yellow Line)
October 1, 1991 - Present**



**Long Term Rate Comparison: 30-Year MMD (Tax Exempt)
(Green Line)
versus 10-Year Constant Maturity Treasury (Taxable)
(Yellow Line):
Jan 1, 2008 - Present**



COMBINING TAXABLE GNMA SALES WITH TAX EXEMPT BONDS AND 4% LIHTC

- ❑ Why not just borrow in the taxable markets through the sale of Taxable GNMA securities?
- ❑ Dilemma: Owner is required to finance 50% of project's land and depreciable basis with tax exempt bonds, and keep these tax exempt bonds outstanding until Project's placed in service date

- ❑ Solution: Issue Short-Term GIC (“Guaranteed Investment Contract”)-backed tax exempt Bonds; Sell GNMA’s into taxable market, cross proceeds (discussed next); pay off TE Bonds on placed in service date
- ❑ Structure originally developed on HOPE VI Financings, where there is no permanent debt, but short term tax-exempt bonds issued to get full value for critically important 4% LIHTC.

Bond Side:

- Underwriter Sells TE Bonds to TE Bond Purchaser
- Bid two AA- or AAA-rated Guaranteed Investment Contracts with same provider at same rate (0.25%): One (GIC “A”) for investment of Bond proceeds until disbursed and second for (“GIC B”) for replacement cash collateral when received
- At closing, Bond Proceeds deposited into GIC A, \$0 in GIC B

FHA Loan Side:

- ❑ FHA Lender (also GNMA Issuer) sells GNMA Securities (Construction Loan Certificate, “CLC”) to be issued with respect to FHA insured 221(d)(4) loan to Institutional GNMA Purchaser on “forward delivery” basis

Post Closing:

- ❑ As each “CLC” is issued by FHA Lender to each insured loan advance and delivered to GNMA Purchaser, “CLC” purchase price paid is deposited into GIC B under Indenture, against withdrawal of equal amount of Bond proceeds from GIC A, which is delivered to FHA Lender to retire its warehouse credit line draw, which funded the corresponding FHA loan advance
- ❑ TE Bonds still 100% cash collateralized and AAA rated

- ❑ Upon final endorsement of FHA insured loan, FHA Lender issues GNMA in form of Permanent Loan Certificate (“PLC”) against delivery to it by Institutional GNMA Purchaser of purchase price in form of previously issued CLC’s plus cash in amount of final FHA Loan advance
- ❑ Tax-Exempt Bonds kept outstanding until Placed in Service Date, when proceeds in GIC B used to redeem Bonds

Result:

- ❑ TE Bond proceeds spent on qualified Project costs as contemplated by Section 142(d) of Internal Revenue Code
- ❑ Bonds rated same high investment grade rating as GIC Provider – AA or AAA, with no separate credit enhancement

Net Results – Borrower:

- ❑ 100+ BPS Savings in Permanent Borrowing Rate, resulting in a lower cost of capital over the life of the loan
- ❑ Negative Arb. reduced from 6-8 points or more to 1-2 points
- ❑ Full syndication value of 4% LIHTC equity on affordable units achieved

Net Results – IRS:

- ❑ Tax-Exempt Bond proceeds used to fund Qualified Project Costs – significantly lower TE Bond amount than if FHA loan had been funded with long-term tax exempt bond issue
- ❑ No arbitrage “artifice or device” - all TE Bond Proceeds (and replacement proceeds in GIC B) invested at far below TE Bond yield
- ❑ No “over issuance” of bonds or “overburdening” of market - only enough TE Bonds to meet 50% test, and outstanding 2 yrs. versus 42.5 yrs!

Why Does It Work?

- ❑ Structure exploits the much greater efficiency of huge market for sale of taxable REMIC-eligible GNMA's (100 BPS lower rates with no neg arb) versus much, much smaller specialty market for Tax-Exempt Multi-Family housing bonds
- ❑ Also reflects recent “upside down” relationship of tax exempt long-term municipal rates and long-term taxable U.S. Treasury rates