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Quick Takes

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Quick Takes: Projects - Money Comes Knocking

"If opportunity doesn't knock, build a door." Milton Berle.

Don't worry, Uncle Miltie. Money is knocking at the door. But you have to actually open the door, or build one. This issue of *Quick Takes* will tell you how.

FOREIGN MONEY

Owners or developers of many types of economic development projects (**manufacturing; film and TV production; tourism, recreation, and hospitality; etc.**) have benefitted from foreign capital invested through the EB-5 program. This program has been subject to concerns each year about whether Congress would renew it or not.

On September 28, 2012, the President signed S. 3245, which includes a three year re-authorization of the EB-5 Regional Center Program through September 2015. A foreign investor who invests, through a Regional Center, at least $500,000 in a Targeted Employment Area (TEA) and, within a certain time (usually 2 years), creates at least 10 direct and/or indirect jobs, can obtain a temporary "green card" that opens a path to permanent residency. An individual offering is conducted for each project, with amounts raised ranging from a few million dollars to hundreds of millions of dollars.

Here are the first steps to determine if you can tap this capital for your project-

1. Determine if it is located in a TEA. (This is based on either high unemployment or the rural nature of the site).
2. Find (or create) a Regional Center with "geographic jurisdiction" and "economic sector jurisdiction."
3. Determine if the Regional Center's "business model" matches your needs. The types of business models are:
    a) loan model
    b) equity model
    c) hybrid model
    d) "lease" model (actually referred to as an "affiliate", "consulting", etc., relationship)
    e) proprietary model.

“FREE MONEY”

Equity is, of course, the most expensive part of a project’s capital stack. But tax credit equity is basically “free money” that is raised through “monetizing” tax credits. Now the federal government has generously opened, or at least kept open, one important door to tax credit equity- New Markets Tax Credits (NMTC).

In December 2012, the New Markets Tax Credit Coalition reported that “…between 2003 and 2010, the NMTC generated over $20 billion in private investment in communities with high poverty rates, low incomes and high unemployment rates. This $20 billion leveraged an additional $25 billion in capital from other public and private sources, financing almost 3,000 projects ranging from **urban health care centers to rural factories and small business loan funds**.”

In the world of industrial development revenue bonds (IDBs) that finance private activities, a local public body like a development authority is the “conduit”, and the “gating” is receiving from the appropriate state agency (in Georgia, the Department of Community Affairs) an allocation of federal “volume cap.” In the NMTC world, a Community Development Entity (CDE) is the conduit, and the Community Development Financial Institutions (CDFI) Fund is the gatekeeper for the credit allocations.

Now- more good news! On January 2, 2013, the President signed into law the American Taxpayer Relief Act of 2012. This Act was known mostly for postponing the “fiscal cliff”, but it also did some good things for the NMTC program:

1. Provided $3.5 billion of NMTC allocation authority for calendar years 2012 and 2013. Applications by CDEs competing for allocations in the 2012 round were due in September 2012. The CDFI Fund will announce those awards in April 2012. But- If you are a developer or owner, now is the time to try to get a CDE to commit allocation to your project!
2. Extended, for two years (through 2018), the carryover of unused limitation.

MONEY FOR RENEWABLE ENERGY PROJECTS

Renewable energy got its own renewal under the American Taxpayer Relief Act of 2012. It extended the availability of the electricity production tax credit (PTC) for qualifying facilities that “start construction” (not defined in the Act) before January 1, 2014. Facilities that qualify include **wind** (sunset date extended until that date, to line up with other types of facilities), **closed-loop biomass facilities, open-loop biomass facilities, geothermal electricity facilities, landfill gas facilities, municipal solid waste facilities, qualified hydroelectic facilities, and marine and hydrokinetic energy facilities**. This extension also preserves the owner’s option to elect the electricity investment tax credit (ITC) in lieu of the PTC.

What this means to a developer or owner is the potential for tax credit equity- more “free money.” The PTC generates, over a 10-year period, a tax credit equal to a certain amount per kilowatt-hour of electricity produced by a qualified renewable energy facility that is sold to unrelated third parties. The ITC tax credit is equal to 30% of qualifying capital expenditures for the construction of the renewable energy facility.

These tax credits have to be monetized in a proper structure (there was an outright grant program, the

"1603 grant" in lieu of the ITC, but it has expired, except in certain "grandfathered" cases). The ITC is easier to monetize, because it is available one-time when the property is placed in service; thus, there are no uncertainties over a prolonged period as with the PTC.

However, the Act has a retroactive provision that has caused some anxiety about qualification (*e.g.*, "80/20 rule" issues) for facilities with used components.

Depreciation can also be monetized, and this Act also extended the 50% "bonus depreciation" for qualified property (includes most renewable energy property) that is acquired and placed in service before January 1, 2014. Certain long-production-period property, that is acquired before January 1, 2014, will qualify if it is placed in service before January 1, 2015. However, if tax-exempt bonds are used to finance qualified property, then the deduction for depreciation for such property must be determined using the straight-line method.

For **manufacturers** of a range of clean energy products, $150 million in tax credits were made available on February 7, 2013. Examples of eligible projects include property designed to be used to produce energy from the sun, wind, geothermal deposits, or other renewable resources; property designed to refine or blend renewable fuels or to produce energy conservation technologies (including energy-conserving lighting technologies and smart grid technologies); and more. This is Phase II of the Qualified Advanced Energy Project Credit authorized under the American Recovery and Reinvestment Act. These credits are being redeployed since they were not used by the original recipients. The credit is an investment tax credit of up to 30 percent of the qualified investment (as defined) in a qualifying advanced energy project (as defined).

Allocations of these manufacturing tax credits are competitive. Special rules apply to a sale or transfer of the project. Let me know if you would like to have more information about application criteria and what projects are eligible.

<u>BOND MONEY</u>

Bonds are often part of the capital stack of a **renewable energy project**. Sometimes they are industrial development revenue bonds and are federally tax-exempt as solid waste disposal or "small issue" manufacturing bonds. (Sometimes the bonds are just federally taxable bonds and are issued directly by the project company instead of through a public body like a development authority.)

Some renewable energy projects, typically biomass-to-electricity, are encountering "used equipment" issues. Generally, used equipment can't be financed with these tax-exempt bonds, although there can be an exception when the equipment is integrated into a facility and the "rehabilitation" rules are satisfied.

There is good news if the project is taking advantage of the investment tax credit (ITC) in addition to tax-exempt bond financing. The ITC is not subject to the reduction of up to 50% like the production tax credit (PTC) if combined with subsidized energy financing or tax-exempt bonds.

And more good news is in the offing. A new program will provide a source of long-term, cheap capital to certain financial institutions that specialize in community lending. This program is not final, but on January 31, 2013, the CDFI Fund released the interim rule for the CDFI Bond Guarantee Program. CDFIs include **banks, thrifts, credit unions and loan and venture capital funds**. Qualified CDFIs will issue guaranteed bonds and loan the proceeds to other eligible CDFIs who will use or in turn re-loan the proceeds to secondary borrowers, all for "Eligible Purposes" including, but not limited to, **community or economic development purposes** in Low-Income Areas or Underserved Rural Areas, as defined. Up to 10 bonds will be guaranteed per year, each at a minimum of $100 million, with a total of up to $1 billion in bonds guaranteed per year, through fiscal year 2014. The interim rule provides that the guaranty is lost if the bonds or a loan of their proceeds is effectively subordinated to tax-exempt obligations.

CONCLUSION

So, now that you know where the doors are, it's up to you to open them.. or build them!

If you have questions, just let me know.

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General note: This issue of *Quick Takes* is a quick-reference guide for elected and appointed officials, economic developers, community developers, owners and developers, participants in the real estate and financial industries, company executives and managers, and their advisors. The information in this issue is general in nature. Various points that could be important in a particular case have been condensed or omitted in the interest of readability. Specific professional advice should be obtained before this information is applied to any particular case. Any tax information or written tax advice contained herein (including any attachments) is not intended to be and cannot be used by any taxpayer for the purpose of avoiding tax penalties that may be imposed on the taxpayer. (The foregoing legend has been affixed pursuant to U.S. Treasury Regulations governing tax practice.)