



# Redevelopment Financing

HOW CITIES USE TAX CREDITS TO LEVERAGE REDEVELOPMENT

# Tax Credits & Municipal Government

- ▶ When a private developer owns property for redevelopment, the developer may receive allowable credits or may sell his interest in the tax credits to an investor in order to secure partial financing for a project.
- ▶ Tax credits enure to the developer or other tax-paying entity in a development or redevelopment project.
- ▶ A local government is not a tax-paying entity so cannot benefit directly from tax credits.
- ▶ When a local government owns property on which the redevelopment efforts could otherwise benefit from tax credits, it must surrender some property rights in the short run in order to gain a long-term benefit.

# Developer with long-term leasehold interest in a property

- ▶ When a local government owns the subject property, it may
  - ▶ Lease the property to a tax-paying entity (Master Tenant) for a term (often these are limited liability corporations formed under state law).
  - ▶ Allow a tax-paying entity separate from the owner, to serve as the Managing Member of the Master Tenant organization during the term of the lease.
  - ▶ The additional members of the Master Tenant may comprise a Federal Tax Credit Investor and a State Tax Credit Investor, both of whom contribute capital to the Master Tenant in an amount equal to the value of the tax credits (as much as 45% to 55% of the qualifying investment).
  - ▶ During the lease term, the Master Tenant may sub-lease the property to one or more subordinate tenants who will occupy the property, live or conduct business there, and pay rent.
  - ▶ In some cases, the subordinate tenants may include the local government or other governmental entity.
  - ▶ The rents paid to the Master Tenant are applied to project debt service and operating expenses, including lease payments to the property owner, with the remainder being net income that can be distributed to the members.
  - ▶ Once the Federal and State Tax Credit Investors' tax credits mature (5 years), the Master Tenant may repurchase the membership interests of the tax credit investors for nominal consideration and may sell the property and improvements.