Real Property Implications of LIHTC and 105(l) Leasing Under the ISDEAA

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Topics Covered

- Low Income Housing Tax Credits (LIHTC) A housing subsidy program for rental housing
- Section 105(l) leasing under the ISDEAA
- Both programs have been important to Indian Country, growing in scope and impact

LIHTC CREDITS

- Low Income Housing Tax Credits (LIHTC) A housing subsidy program for rental housing
- Created within Section 42 of the Internal Revenue Code
  – Modified by 2008 and 2009 Legislation

LIHTC CREDITS

Real Property Aspects of the Program

- Investor will want to examine title report, Title Status Report, on property
- Property can be owned, leased, assigned
- Must be site control
- Use restriction for 30 years required per Code (income and rent limits)
- Enforced through Land Use Restriction Agmt.

LIHTC CREDITS

What do LIHTC finance?

- New construction and rehab projects
- Acquisition in some cases
- Housing for families, special needs tenants, single room occupancy and the elderly
- Urban, rural and suburban locations
- Additional tax incentives for projects in high-cost or difficult-to-develop areas

LIHTC CREDITS

How Do LIHTCs work?

- Rental units with tenants earning no more than 60% of area median income
- Investors earn dollar-for-dollar credits against their federal tax liability

LIHTC CREDITS

How Do LIHTCs work?

- Investors also get tax benefits from losses
- Generally, tax credits are received over the first 10 years of operation
- Some tax credits are recaptured by the IRS if the project does not comply for 15 years

LIHTC CREDITS

Generally used in a limited partnership structure

- General partner owns just 0.01%, but controls and operates the project

- Passive limited partner invests equity in return for 99.99% ownership

LIHTC CREDITS
Key Questions

- **Can the project be completed in the time and within budget**
  - What will it cost to build the project?
  - How much is needed to place it in service?
  - What are reasonable timelines?

- **What are the key risk areas to lenders and equity investors and how can the risks be ameliorated?**

ISDEAA and Section 105(l)
Leasing for BIA/IHS Facilities

- What is the program?
- How does it work?
- What are some tips for proposal submission?
- Funding and Finance Issues and Opportunities

History of Funding for BIA/IHS Facilities

- If BIA/IHS provide services directly they generally have adequate facilities.
- Tribal facilities used for BIA/IHS FA programs are badly underfunded.
- Chronic problem that BIA/IHS created by not asking for enough appropriations.
- Section 105(*l*) has been law since 1994; until 2016 it was not used as a means to fund facility needs.

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Section 105(l) of the ISDEAA

(1) Upon the request of an Indian tribe or tribal organization, the **Secretary shall enter into a lease with the Indian tribe or tribal organization** that holds title to, a leasehold interest in, or a trust interest in, a facility used by the Indian tribe or tribal organization for the administration and delivery of services under this Act.

(2) The Secretary **shall compensate each Indian tribe** or tribal organization that enters into a lease under paragraph (1) for the use of the facility leased for the purposes specified in such paragraph. Such compensation **may include rent, depreciation based on the useful life of the facility, principal and interest paid or accrued, operation and maintenance expenses, and such other reasonable expenses that the Secretary determines, by regulation, to be allowable.**

Implications of Maniilaq I and II

- Cases litigated in 2014 and 2016.
- Section 105(*l*) leases are mandatory upon request of Indian tribe or tribal organization.
- Regulations set out 3 options for calculating compensation; they do not allow IHS to fund $0 compensation.
- Leases must be fully funded.
- IHS may decline unreasonable or duplicative costs.
  - Potential duplicative costs include M&I and CSC.
- IHS did not appeal the ruling.

IHS Implementation of Maniilaq I and II Decisions

http://bit.ly/IHSLeaseSupportingDocumentation

- Requirements for Section 105(l) to apply:
  - (1) Tribe must hold title to, have a leasehold interest in, or a trust interest in, a facility.
  - (2) The facility must be used for the administration and delivery of services under ISDEAA
- Options Available For Proposed compensation at 25 C.F.R. § 900.74:
  - FMR
  - Costs incurred
  - Combination of FMR and cost incurred
- Reasonable and non-duplicative

Cost/Appraisal Methodologies

- **Fair Market Rental**
  - Generally carried out by a third party appraiser
  - Often uses comparable properties (if there are any) to valuate space rental estimates
  - Involves the expense of hiring an expert, but an be worth the investment
- **Cost Basis/Costs Incurred**
  - This could be an important method to use if the costs for a certain facility far outweigh what a fair market rental appraisal would estimate
  - Could be high cost of principal and interest, construction costs, operation costs
- **Combination FMR and Costs Incurred**
  - Perhaps the appraisal is very close, but there are unique cost elements that the Tribe wants to include
  - Ideally, each methodology would be examined if possible for optimization

Recent Developments

- **Space needed for the "Federal Program"**
  - IHS limits lease compensation to portion of facility IHS deems necessary to serve IHS beneficiaries, not portion IHS deems as serving non-beneficiaries.
  - IHS has been reducing lease compensation to reflect the facility's % of non-beneficiaries served.
  - Supportable space in BIA and IHS leases is also a factor in potential reduction of compensation.
  - Issue was litigated by the Jamestown S'Klallam Tribe.
- **Appropriation Issues**
  - Funding is part of discretionary appropriated funding but Congress has appropriated ***such sums as necessary*** to fully fund all leases
  - Congress is actively considering changing the funding from discretionary to mandatory, which would be beneficial to tribes/tribal organizations

Miscellaneous Issues

- Leases are funded from date of Letter of Intent, not the date a lease is finally negotiated.
- Practically, this means it is important to prepare a “Proposal” package efficiently and submit the LOI early.
- The LOI can be submitted prior to completion of new space, though the agency may not fund the lease until the building is substantially complete or otherwise occupied by the Tribe
- Lease funds have become potentially important revenue streams to finance facility construction costs.
- The tax question of “private business use” and 105(l) lease revenues

Proposal Contents

- Generally, the 105(l) lease proposal will include: 1) cover letter/LOI; 2) fair market rental appraisal (if completed and that methodology utilized); 3) floor plan, potentially, showing program use of space, etc.; 4) any additional narrative explanation of space use; and 5) if known, any knowledge of whether the space is already receiving funding through indirect costs or other funding
- The agency generally wants to know what space is used for what portions of the FA scope of work, whether there is any double recovery of funding, whether there is any space that is excluded within the building

Proposal Contents (cont.)
Floorplan Example

QUESTIONS?

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