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5 Reasons Why NMTC Participants Should Take a Second Look at HUD's Section 108 Loan Guarantee Program

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The U.S. Department of Housing and Urban Development (HUD) in March updated its current availability of financing for Community Development Block Grant (CDBG) entitlement communities and states to pursue a Section 108 guaranteed loan, a program offering low-cost, long-term financing for economic and community development projects.

With almost \$15 billion in Section 108 loan authority available for potential borrowers, local governments and states have ample opportunity to leverage part of their CDBG funds into federally guaranteed loans that can finance economic development, housing, infrastructure, public facilities and other projects. However, the Section 108 program is a vastly underused resource, with only about 300 active participants out of about 1,200 eligible recipients despite a \$300 million FY2021 appropriation.

HUD staff spoke with the Novogradac Journal of Tax Credits to discuss the following reasons new markets tax credit (NMTC) transactions can benefit from a Section 108 loan:

1. Commonalities in Persons and Communities Served

CDBG's national objective of principally benefiting low- and moderate-income people and areas is compatible with the objective of the NMTC. (Section 108 uses the CDBG National Objectives framework, which provides three possible objectives to meet.) Most NMTC developments qualify under geographic

eligibility by being located in a census tract where the poverty level is at least 20% and household incomes are 80% or less of the area median income. An alternative method of qualifying for the NMTC is for the development to directly benefit targeted populations where at least 40% of employees are low-income persons earning 80% of the area median income at the time of hiring (51% for the Section 108 national objective) or at least 50% of gross income is derived from sales, rentals or services to low-income persons (Section 108 activities principally benefit 51% low- and moderate-income persons).

1. Flexible Financing

Both Section 108 and the NMTC were created to provide gap financing for private developments that cannot attract conventional financing—Section 108 applicants must certify they made efforts to obtain financing without the federal guarantee and NMTCs are used for developments that could not be completed “but for” the NMTC. Combining Section 108 with the NMTC as a leverage loan or a leverage source loan can make the Section 108

loan interest-only for the seven-year compliance period of the NMTC. Section 108 loans that are interest-only during the NMTC compliance period cannot convert to permanent interest rates until the NMTC compliance period ends and the NMTC structure unwinds.

1. Section 108 is Self-Amortizing for Economic Development

HUD said one reason communities may be hesitant to use the Section 108 program is that applicants are required to pledge their current and future CDBG funds, as well as additional security. One benefit of pairing Section 108 with the NMTC is that qualified active low-income community businesses under the NMTC would theoretically generate enough revenue to pay off the Section 108 loan themselves.

1. Recently Reduced Application Review Periods

HUD says one of the misconceptions about the Section 108 program is the turnaround time for reviewing applications. Previously, HUD's application review period was approximately 90

days because a HUD field office would review an application before sending it to HUD headquarters for underwriting. Presently, HUD headquarters and field offices review Section 108 applications concurrently, reducing review times to about 45 days if the submission complies with all application requirements.

1. Technical Assistance

HUD provides technical assistance to applicants at any point of their project cycle, from brainstorming to implementation. Making use of technical assistance can help reduce commitment approval times.

Conclusion

The NMTC and Section 108 program are effective community development resources, each with its own program requirements and nuances. Contact a Novogradac professional at cpas@novoco.com to discuss structuring options, compliance requirements and other considerations. HUD offers additional information about the Section 108 program on its HUD.gov and HUD Exchange website. ❖

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