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**FINANCING COMMUNITY AND
ECONOMIC DEVELOPMENT:
PROJECT, INSTITUTIONS AND
SYSTEMS**

Karl Seidman
Senior Lecturer in Economic Development
MIT Department of Urban Studies and Planning

Class Overview



- Development finance practice framework
- Financing firms and projects
- Development finance intermediaries
- Local finance systems
- Class project discussion and applications

Development Finance Framework: Capital Availability and Market Failures



- Supply capital to firms and projects that advance local vision, plans and priorities
- Capital supply “gaps” and misalignment result from market imperfections:
 - Limited competition: monopoly or oligopoly
 - Lack of information or high information costs
 - High transaction costs
 - Non-rational decisions: risk aversion, discrimination
 - Regulatory distortions
 - Externalities: social benefits exceed private returns
- Fill gaps to expand capital and avoid “capital substitution”

Capital Markets in Practice

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- Capital markets: set of institutions that accumulate and channel savings to households, businesses and governments and provide a return to suppliers of capital
- Institutional structure and operation of capital markets shape supply gaps
- “Public” vs. “Private” capital markets
 - Public market imperfections: high transaction costs and sizes, non-rational behavior
 - Private market imperfections: high information costs and opacity, non-rational behavior and regulations

Race/Class/Gender and Capital Availability

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- History of disparity in access to capital/exclusionary policies
 - FHA mortgage policies
 - Red-lining of low-income neighborhoods
 - Segregated financial institutions and networks
- Inequality in income, wealth, & education limits access to informal and formal capital
- Institutionalized discrimination in financial institutions & products serving communities
 - Nexus of residential & financial segregation
 - Sub-prime loans 3X more likely in low-income area; 5X more likely in black neighborhoods, independent of income
- Racial disparities in lending decisions and pricing remain after 30 years of legal & regulatory changes

Community Development Implications

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- Common capital supply gaps from market imperfections:
 - Lack of institutional equity for most small businesses
 - Limited availability of small commercial loans
 - Limited availability of long term debt
 - Capital access disparity: geography, wealth, race & gender
 - Higher level of risk aversion in post-crisis environment
- Private intermediaries are key capital sources for community economic development
- Understand how market, regulatory and financial sector factors shape regional capital supply by private sector
- **Expand supply of small amount & higher risk capital**
- Proactive strategies to address class/race/gender biases

Triad of Development Finance Practice



- Financing projects and firms
- Creating effective intermediaries
- Improving development finance systems
 - Expand private market capital supply
 - Complimentary alternative development finance intermediaries
 - Aligning investment with vision and goals
 - Addressing demand side “pipeline”

Financing Businesses and Projects

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- Capital is only one component of viable enterprises and projects; other inputs must exist first
- Financial tools and building blocks:
 - Equity – owners' investment in business or project
 - Debt – contract to supply capital with fixed repayment terms, condition and interest rate
 - Project subsidies – funding without financial return from project or business income
 - Credit enhancement – reduce lender's risk to supply debt

Community Development Project Types

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- **Low-income/subsidized housing**
 - Largely built by private sector: for profit and non-profit
 - Receives the most subsidies and financial resources
- **Community facilities**
 - Health care, child care, charter schools, cultural facilities
- **Commercial real estate**
 - Grocery stores, retail centers, office buildings
- **Small businesses**
- **Infrastructure**
 - Largely built by state and local governments
- **Planning/district management**

Project Financing Equity

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- Major source for businesses –half of their capital
- Smaller role in real estate projects : 10% to 30%
 - Less for affordable housing and subsidized projects
- Business equity
 - Entrepreneur's personal wealth, family and friends
 - Business retained earnings
 - Angel investors/funds, venture capital funds
 - Stock markets
- Real estate equity
 - Developer's wealth, assets and cash resources
 - Institutional investors (pension funds, insurance companies)
 - REITs and private investment funds

Project Financing: Debt

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- **Federal programs:**
 - HUD 108 loan program
 - SBA 504 program for business financing
 - USDA Rural Development Authority loans
- **State authorities access private credit markets**
 - Long-term permanent debt via bonds
 - Predevelopment and interim loans with own capital
 - Interest rate subsidy: exempt from federal and state income tax
- **Community development financial institutions**
 - Specialize in financing for low-income communities
 - Supply higher risk predevelopment and long-term debt
 - Funded by mix of government, banks, foundations and individuals
- **Private banks and financial institutions**
 - Lower risk construction and permanent loans
 - Small business loans: often with federal and state guarantee
- **Foundation program related investments**

Project Financing: Subsidies

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- Federal and state tax credits attract private investment
 - Low-Income housing tax credits (LIHTC)
 - New market tax credits (NMTC)
 - Historic tax credits (HTC)
- State and local government, foundation grants
 - Funding levels and priorities vary by state and city
 - State governments set priorities for and allocate LIHTC
 - Local governments allocate federal block grants funds
 - Large variation in foundation funding across cities
- State and local tax incentives and abatements
- Tax-increment financing
 - Increase in local taxes used to fund projects and infrastructure
- Federal and some state rental housing subsidies

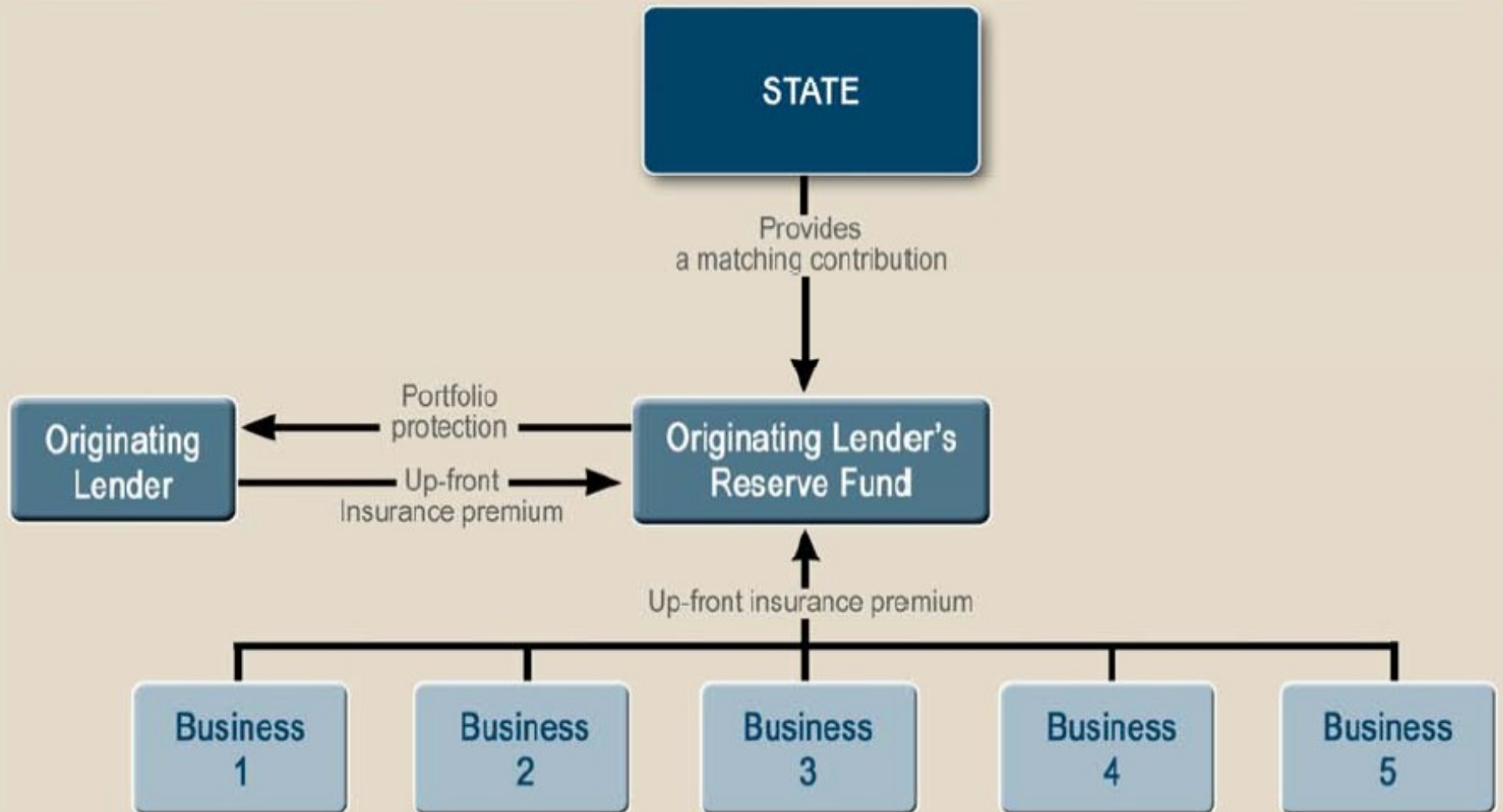
Project Financing: Guarantees

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- SBA 7(a) program for small business loans
 - One of the largest federal financing program: \$84 billion portfolio
 - Guaranteed 45,571 loans valued at \$18.9 billion in FY2017
 - Private lenders increase loan terms, lower equity required, serve more start-up, women and minority-owned firms
- State and local government loan guarantee programs
- Capital access program: portfolio guarantee via loan loss reserve
- Private bank letter of credit
- Guarantees by large government or quasi-government agencies, foundations

Capital Access Program Mechanics

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Delivery of Federal Funds Varies by Program

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CDBG, HOME, Rental Subsidies

Federal Government



City Government



Project or User

LIHC, Tax Exempt Bonds

Federal Government



State or Local Government



Developer



Investor to raise capital

New Market Tax Credits

Federal Government



Intermediary



Developer



Investor to raise capital

Historic Tax Credits

Federal Tax Entitlement



Developer based on project type

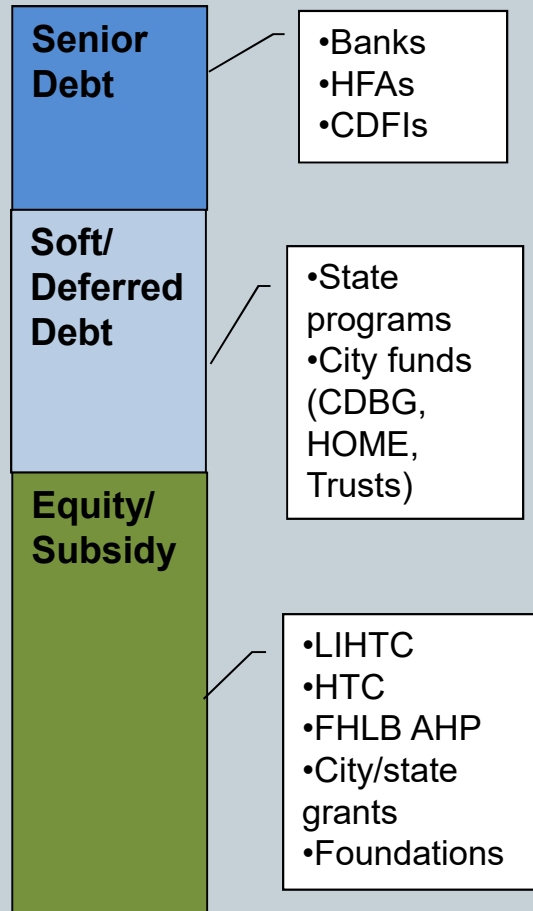


Investor to raise capital

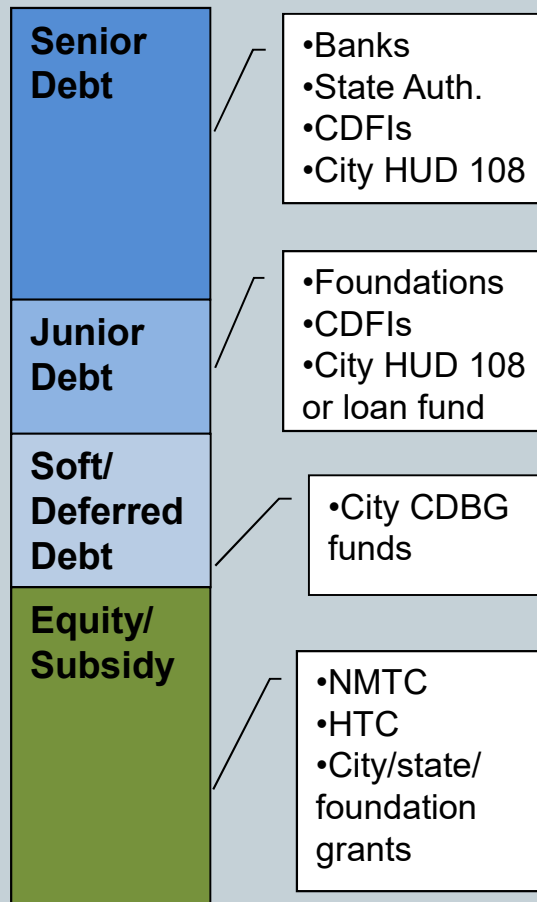
Project Financing by Type

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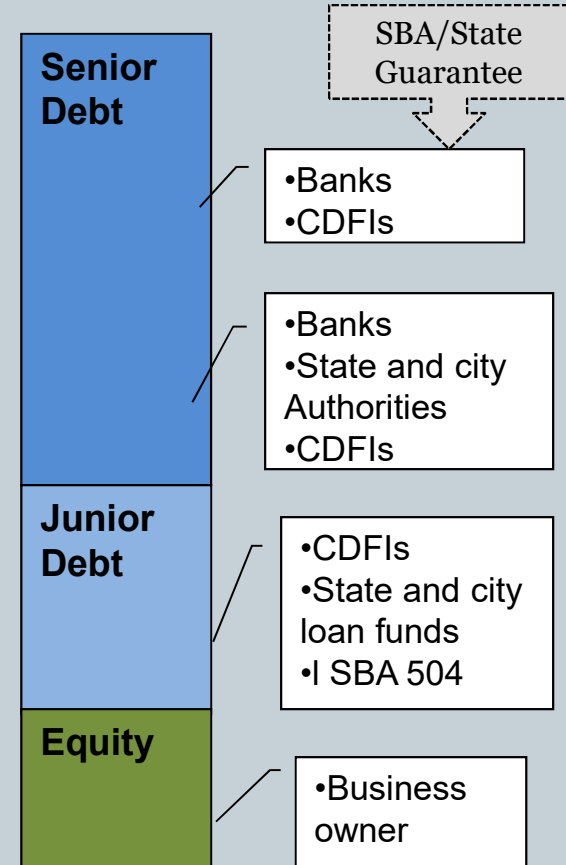
Low Income Housing



Commercial Real Estate



Small Business



Project Case Studies: Boston

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**ONE GREENWAY:
NEW CONSTRUCTION HOUSING**

**JP BREWERY:
COMMERCIAL REUSE OF HISTORIC
BUILDING**

Housing Project Example: One Greenway

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- Mixed income housing + commercial space and plaza
- Joint venture: nonprofit Asian Community Development Corporation (ACDC) and for profit New Boston Fund
- 10 year development period



One Greenway: Development Plan

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- **Mixed Income Residential with 363 units**
 - 217 market rate rental units
 - 95 affordable rental units
 - 51 affordable condominium units (separate building 2nd Phase)
 - 40% affordable units overall
- **Mixed Use and Transit Oriented**
 - 5,000 sf community space
 - 3,000 sf retail space
 - 13,000 sf open space restores street connections, creates civic plaza
 - Adjacent to South Station multi-mode transit station
 - Near Boston's financial district
- **420,000 square feet on 1.5 acre site**

One Greenway: Community Vision with Non-Profit/For Profit t Joint Venture

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- Vibrant area taken for highway construction in early 1960s
- New highway project in 1990s removed highway ramp creating new development site
- Community coalition led 2 year planning process to create vision for site
- ACDC organized and advocated to get vision incorporated into developer RFP issued by state Transportation Department
- ACDC and New Boston Fund formed Parcel 24 LLC
- Developer designation in April 2006; BRA approval Nov 2008
- 1st phase completed : June 2014 to August 2015
- 2nd phase construction completion: Fall 2017

One Greenway Financing: Private Debt and Public Subsidy

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- **TDC: \$135 million**
 - \$400,00 acquisition; state participates in condo sales revenue
- **\$46 million in public subsidies, most state allocated**
 - \$2 million state brownfield remediation grant
 - \$6.5 million state rental housing subsidies
 - \$3.5 million Boston HOME funds
 - Annual \$2 million federal and \$1 million state LIHTC award
 - \$3.9 million state AHT grant to support affordable condos
- **\$80 million phase 1 mortgage from PNC Bank**
- **\$27 million in construction financing from Property and Casualty Initiative and Boston Private Bank**

Jamaica Plain Brewery Reuse

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- Closed brewery complex acquired by neighborhood non-profit in 1983
- Renovated in phases over 25 years
- Final phase: difficult and costly
 - Interior demolition and entire reconstruction of 68,000 square foot
 - Reuse as fitness center, retail and office space
- Home to 50 small businesses



JP Brewery: Project Financing

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Total Dev Costs	\$12,105,000
Senior Debt (Life Ins. Fund)	\$4,700,000
Fed and State Historic Tax Credits (MHIC)	\$4,000,000
New Market Tax Credits (MHIC)	\$2,160,000
City of Boston Loan	\$150,000
Developer loan & deferred fees	\$1,095,000



Project Case Studies: Detroit

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**AUBURN PROJECT:
MIXED USED NEW CONSTRUCTION
ARGONAUT BUILDING:
EDUCATIONAL REUSE OF
HISTORIC BUILDING**

The Auburn Mixed-Use Development

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Part of multi-project and investment strategy to attract new residents to Midtown Detroit neighborhood

- Demolition and new construction project
- 58 market rate apartments
- 9,100 SF retail space
- Completed in 2012
- Hard to finance after Great Recession



The Auburn: Financing Sources

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Total Development Cost	\$12.3 million
CDFI Loan	\$3.7 million
New Market Tax Credits	\$7.6 million
State Grant	\$1.0 million

- 2nd local CDFI guaranteed retail rental income
- Market rate project needed 70% subsidy
- Due to low rents and low property values in Detroit

Argonaut Building Reuse, Detroit



- Adaptive reuse of large historic building
 - 11 stories, 760, 000 SF
- Part of former General Motors HQ complex
- Reuse as Design Education Center by College for Creative Studies (CCS)
 - Graduate & undergraduate programs
 - New middle and high schools
 - Student housing
 - Parking, gym, shared space

Taubman Center for Design Education

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- GM donated building to CCS
- CCS selected private real estate firm to develop project
- Completed in 18 month period , 2007 to 2009
- Complex financing with large gifts and subsidies

Building Program

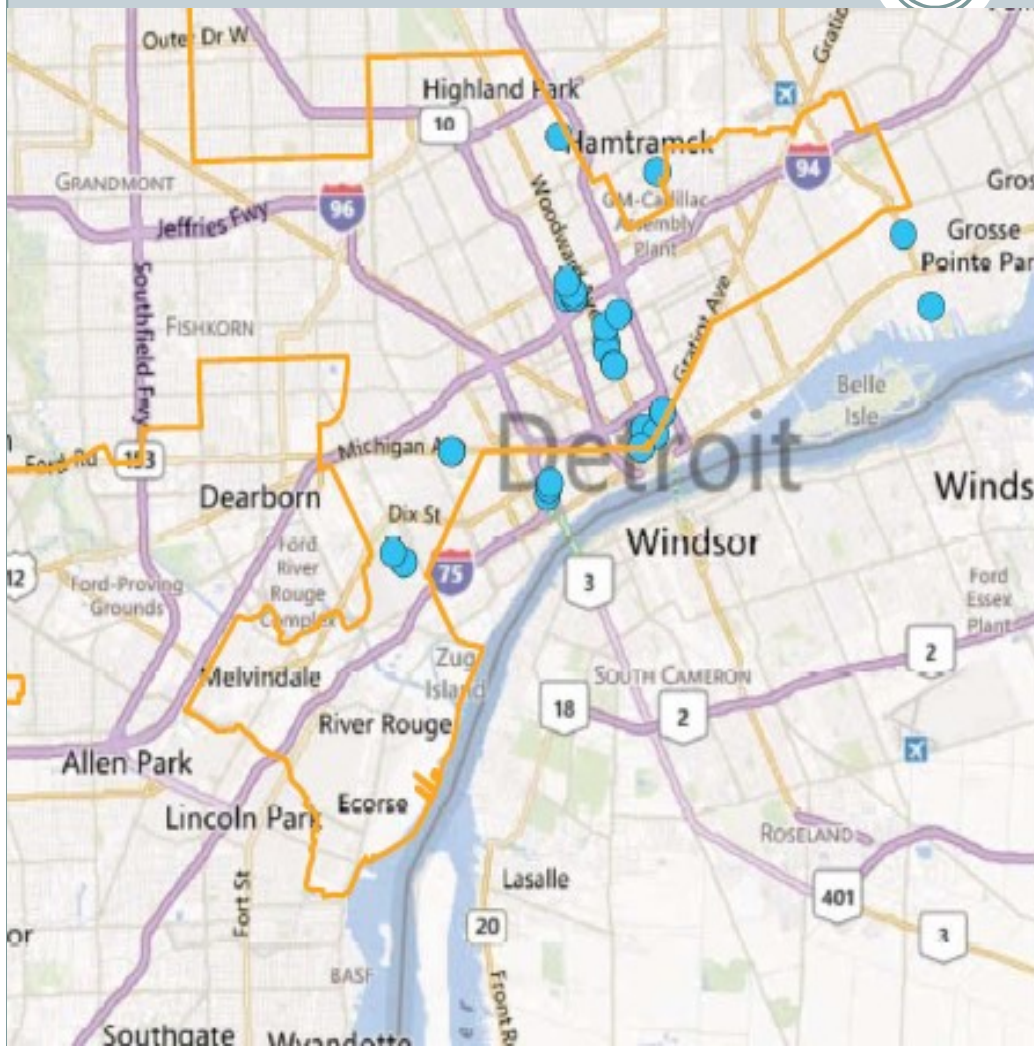
- 415,000 SF CCS Use
- 108,000 SF middle and high schools
- 84,000 SF to lease to CCS partners and other organizations
- 84,000 shared facilities

Taubman Center Financial Structure

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Use of Funds	\$ million	Sources of Funds	\$ million
Acquisition (Donated building)	\$0	NMTC	\$20.7
Construction and tenant improvements	\$119.6	Historic Tax Credits (federal and state)	\$31.8
Soft costs	14.6	Owner Equity	\$36.0
Financing costs for loans and equity	5.6	State brownfield tax credits	\$7.4
Total	\$139.8	Tax exempt bonds	\$26.0
		Gifts, grant and partner funds (CCS and high school)	\$17.9

NMTC Investments in Detroit Through 2010



- Critical subsidy source
- Funded 15 projects
- \$200 million in NMTC
- ~\$650 million in total investment
- Concentrated in downtown, Midtown, New Center along Woodward corridor

Financial Intermediaries: Function and Value

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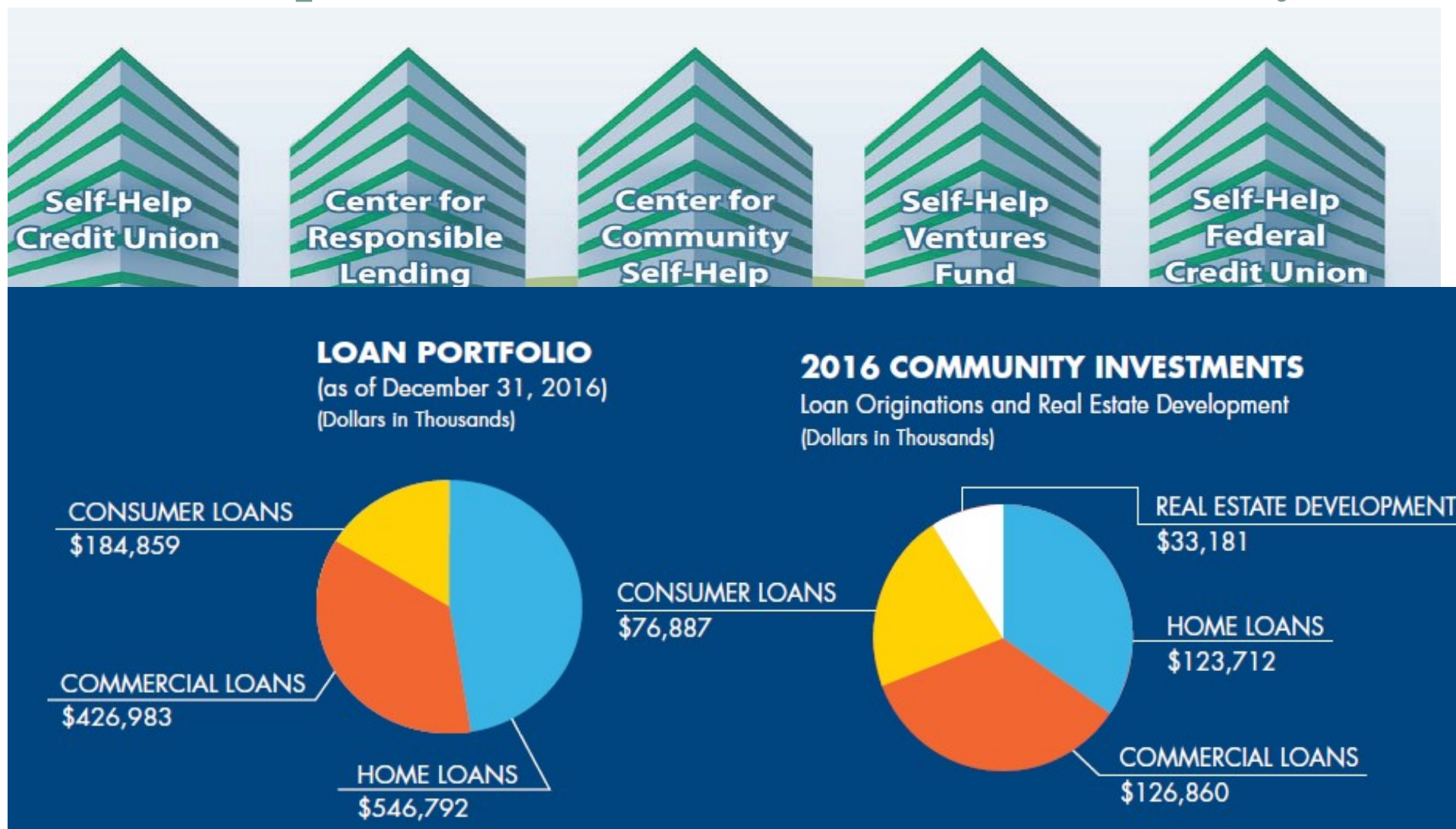
- Expertise in underwriting and structuring financing
- Capacity to raise and manage capital to support local vision and goals
- Specialized local knowledge & cultural competencies
- Link capital with development services to address demand side barriers and historic inequities
 - Outreach and trust-building
 - Training and technical assistance
 - Aligned real estate development
 - Planning and policy
- Innovation and product development to address new needs , opportunities and challenges

Alternative Financial Intermediary Models

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- **Public and quasi-public corporations**
 - State housing financing authorities
 - State and local economic development corporations
- **Revolving loan funds**
 - Can be public, private or non-profit
- **Venture capital and angel investment funds**
 - Private for profit fund with civic, public and social impact versions
 - Public pension funds target for social and economic goals
- **Community development financial institutions**
 - Serve low-income communities with financing + development services
 - Certified by US Treasury CDFI Fund
- **Microenterprise funds**
 - Small loans + training and technical to serve very small enterprise

Self Help Model of Multifaceted Intermediary



\$1.98 billion in total assets; 129,00 members in CA, Chicago, NC, FL

Intermediary Case Studies

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**MASSDEVELOPMENT:
EXPANDING ROLE OF STATE
DEVELOPMENT FINANCE
AUTHORITY**

**CAPITAL IMPACT PARTNERS:
IMPACT OF STRONG CDFI IN
DETROIT**

MassDevelopment History

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- Quasi-public authority governed by private sector board
- Formed in 1998 from merger two authorities:
 - Government Land Bank –managed and financed difficult real estate projects
 - Mass Industrial Finance Agency – issued bonds to finance businesses and non-profit organization
- Result: stronger intermediary to raise capital and deliver programs, assist communities
 - Used to manage multiple state grants and loan programs
 - NMTC Intermediary
 - Real estate technical assistance, development, management services
 - \$500 million in assets (2016) ;\$30 to \$40 million in annual loans & guarantees; \$1 to \$2 billion in bond issues

MassDevelopment Services

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- Manages 5 state grant programs for site clean-up, cultural facilities, health centers and manufactures
- 11 loan and loan guarantee programs for businesses, real estate redevelopment and non-profits
- Issues bonds for firms, infrastructure and RE projects
- Advises and assists communities with development properties and plans
- Leads state Transformative Development Initiative to stimulate investment and redevelopment in older industrial cities (“Gateway Cities)
- <http://www.massdevelopment.com/>

Capital Impact Partners

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- Formed in 1984 as outgrowth of National Consumer Cooperative Bank
- Initial focus on financing non-profit health centers
- Expanded into financing charter schools and housing in 1990s
- Becomes NMTC entity (2003) and CDFI (2011)
- National intermediary targeting specific sectors
- \$284 million in assets; \$131 million in annual loans

Capital Impact Partners and Detroit

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- Launched first “place-based” initiative in Detroit
- Recruited by Living Cities and local foundations to support Woodward Corridor Initiative
 - CDFI partner for national 5-city initiative
 - Received \$20 million in debt and grants for investment fund
- Attracted new capital via relationships and expertise
 - Opened Detroit office with full-time staff person
 - Raised \$30.5 million for 2nd investment fund for long term debt
 - Intermediary for JPMorgan Chase Detroit Neighborhood Fund (\$30 million); Ford Foundation Predevelopment Fund (\$3 million)
- Made \$47 million in loans to 13 projects creating 689 housing units (2011 to 2015)

Local Development Finance Systems

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- The set of private, public and non-profit financial intermediaries that work to deploy capital to advance local development vision, goals and priorities
 - Includes research and policy advocacy to shape policies, budgets, regulations and investment priorities
 - Includes “demand-side” to expand capacity to plan, undertake projects, create new enterprises, link investment to social and equity goals
- Institutional and resource ecosystem framework
- Capital absorption functional view of system

Finance System Operates and Varies at City Level

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- ❖ Common tools and policies yet different local systems
 - Politics + leadership
 - Varied state and city vision, leadership, policies and funding, coordination
 - Civic capacity, bank/corporate resources and role
 - Different private sector funding and institutions
 - Neighborhood level response and capacity
 - Extent/impact of non-profits; advocacy for public funding
 - Local philanthropy
 - Size and focus shapes support for neighborhood development
 - Human resources
 - Weak or strong market and economic conditions

Finance Ecosystem

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Resource Providers

Financial

- Banks
- Insur Cos.
- CDFI Fund
- Fed. Govt
- Foundations
- Capital Mkts
- Tax Credit Investors
- Local Govt/RDAs

Human

Knowledge

- Consultants
- Academics/Think Tanks
- OFN, SAHF, HPN
- Federal Reserve

Technology

Environmental Conditions

Financial Intermediaries

- CDFIs and SPEs
- Banks
- Local Government
- RE Equity Funds
- SBA Lenders

Complementary Orgs

- Anchor institutions
- Community groups
- Businesses

- Policy and Administration
- Economics and Market
- Geography and Infrastructure
- Cultural and Social Fabric

Borrowers

- Developers
- CDCs
- Non-profits
- Small businesses
- QALICBs

Problem-Makers

- Speculators

Living Cities Adapted from Stanford Social Innovation Review Article "Cultivate Your Ecosystem."

Impact: Increase economic opportunity and promote revitalization of low-income communities

Vision and Legitimacy

Ensure that investment meets recognized community needs, and is done with the support of community actors.

- Define needs
- Engage with community
- Convene stakeholders; “table-setting”
- Determine priorities

Enabling Environment

Build the policy and support tools that allow community investment to take place.

- Set and influence policy and regulatory environment
- Apply and enforce policies and regulations
- Generate and provide data
- Provide subsidy, first loss money, and training
- Ensure availability of diverse and capable actors

Pipeline

Generate deals and projects that contribute to defined community goals.

- Spot opportunities
- Pull together projects and deals
- Predevelopment and development
- Leverage public resources
- Assemble capital, including identification and blending of sources
- Structure and underwrite investments
- Align deals and projects with vision and goals

Management and Monitoring

Manage portfolio to ensure financial and social performance.

- Loan servicing
- Portfolio management
- Workouts and problem solving
- Data collection and evaluation
- Social impact monitoring
- Organizational capacity building

Innovation

Learn and apply the lessons of CI to create durable networks that can strengthen CI practice and carry it through to new areas.

- Identify and explore emerging needs/fields
- Create new products
- Build platforms for ongoing collaboration
- Identify and attack barriers

System Components

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Policy Advocates	Public Sector	Foundations	CDFIs	Banks	CDCs/ Non-profits	Entrepreneurs / Developers
Design and propose policies	Create and implement policies	Design and propose policies	Design and propose policies	Supply debt	Set local vision, plans and priorities	Start and manage businesses
Push for funding	Set vision, plans and priorities	Invest in and build capacity	Invest in and build capacity	Fund capacity building	Build and manage projects	Build and manage projects
	Deliver project subsidies	Supply subsidy and some debt	Supply debt		Organize /voice for residents	Manage districts
	Supply/guarantee debt				Manage districts	

CD System: Additional Tools and Policies

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- **Community reinvestment act**
 - Requires banks to serve banking and credit needs of low-income communities, small firms and small farms
 - Expanded bank investment and lending for neighborhood development
- **Inclusionary zoning**
 - Share of units in new projects must be for low income and affordable housing
- **Linkage fees**
 - Fee from non-residential projects to fund affordable housing
- **Dedicated tax revenues**
 - Local option extra tax dedicated to housing or other uses
- **Assessment districts**
 - Extra tax to fund infrastructure or services in designated area

Comparing Local Finance Systems

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**BOSTON:
STRONG MARKET, ACTIVE STATE
GOVERNMENT, HIGH LOCAL
CAPACITY**

**DETROIT:
WEAK MARKET, POOR LOCAL
CAPACITY, STRONG FOUNDATIONS,
GROWING PRIVATE INITIATIVE**

Boston: Strong Multi-Sector System

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1. State-led: high funding for housing and infrastructure
2. Dense system: many actors across sectors and roles
3. Strong non-profit developer capacity
4. Multiple state and CDFI intermediaries
5. Strong mayor; capable, activist city government
6. Advocacy groups sustain state funding and push innovations
7. Modest, supportive role for foundations
8. Complex project funding: many sources, high costs and long time frames
9. Entrenched system resistant to large-scale change
10. Tensions between state and community priorities

Historic System Drivers

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- State government leadership, policies and funding
 - Sustained AH funding, investment in CDC/non-profit capacity, public transit funding and focus on cities
 - Policy orientation to multiple intermediaries and funds
- Community-based activism and leadership matched with philanthropic, public and private sector support
- Mayoral priority on neighborhood reinvestment, CDCs and affordable housing
- Strong advocacy organizations
- Long-term commitment, innovation and leadership by many talented professionals
- Region's economic health enabled public and private investment and helped retain talent

Dense and Complex Housing Finance

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Specialization,
competition, &
overlapping
roles

Many state
subsidies
and funds

City linkage
fees, CPA,
CDBG, HOME
Funds

Coordinated
delivery of
LIHTC & state
subsidies



Three
Intermediaries
supply long-
term debt

CRA agreements:
MHIC; home
mortgages ; CDC
capacity building
support

CDFIs, CEDAC,
Insurance
Industry funds
predevelopment

Strong Affordable Housing Project Pipeline

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- Federal/state subsidies make projects feasible
- High capacity non-profit and for-profit developers
- Private development consultants add capacity for smaller CDCs and non-profit developers
- Open system: no preference for non-profit vs. for-profit
- CEDAC: state technical assistance provider and gatekeeper for predevelopment funding
- CDC-private developer partnerships for large projects

System Weaker for Commercial Projects

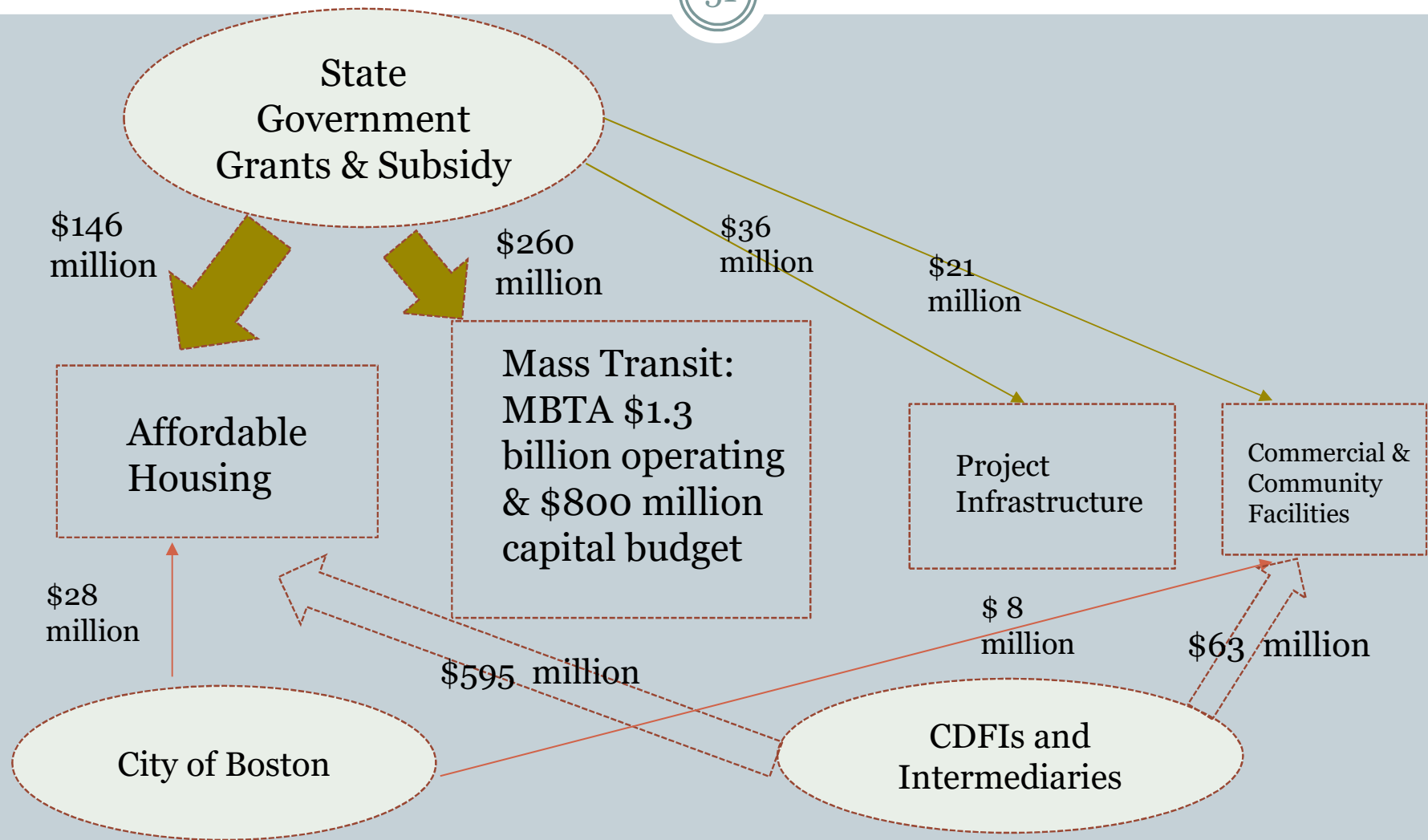
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- Fewer funding sources
 - NMTC, HTC, brownfield and modest state ED grants
- Several debt sources but with modest capital
 - MassDevelopment, HUD 108, local loan funds , LISC
- Lacks clear funding pathways and system
 - Projects typically one-off hunts to assemble funding



Boston System: Annual Funding Flows

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Boston Housing Subsidy: Federal, State and Local Funding Shares

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- State programs supply almost half of subsidies
- Declining local government share
- Declining federal share before ARRA

SOURCES OF GOVERNMENTAL GAP SUBSIDY FUNDING 2001-2013

YEAR STARTED	FED ENTITLEMENT % OF GOVT FUNDS		CITY FUNDS % OF GOVT FUNDS		STATE PROGRAMS % OF GOVT FUNDS		FED COMPETITIVE % OF GOVT FUNDS	
2001-2004	\$30,320,535	20.2%	\$31,197,056	20.8%	\$66,319,571	44.2%	\$22,319,894	14.9%
2005-2008	\$26,492,834	17.6%	\$29,255,771	19.5%	\$79,680,807	53.0%	\$14,976,700	10.0%
2009-2013	\$41,216,031	20.2%	\$36,191,339	17.7%	\$96,235,069	47.2%	\$30,432,900	14.9%

Source: Housing Boston 2020 Report

At Neighborhood Level: CDC Role

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- **Jamaica Plain Neighborhood Development Corporation:**
 - Develops affordable housing and commercial real estate
 - Provides technical assistance to local small businesses
 - Leads neighborhood planning
 - Partner for Main Street non-profits to manage commercial districts

Detroit: Weak System, Privately Led

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1. Disinvestment on a mammoth scale
 - 60% population loss: 1.8 million to 700,000; 38% in poverty
 - 71,000 blighted buildings and 90,000 vacant lots
2. Historically weak and ineffective local government
 - Dysfunctional city services and regulatory system
 - No city plan and policies to support neighborhood development
 - City files for bankruptcy in 2013; completed in late 2014
3. Philanthropic leadership and funding initiatives
 - Focus on downtown and Midtown neighborhoods
 - Impetus for recent Detroit Future City Plan
 - Advocate for new light rail project; largely privately financed
4. History of limited state funding and support for city
5. Limited bank lending and no large Detroit-based banks
6. Growing CDFI sector and role, larger than in Boston

Detroit: Development Capacity

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- Most development projects conceived & driven by civic, nonprofit, or quasi-public groups
 - Weak local private development sector
- Effective community-based developers in small set of neighborhoods
- Several private entrepreneurs investing in downtown
- “Anchor institutions” driving much investment
- Deals need deep subsidy: very complex layered financing
 - 22 layers for “model” Cadillac Hotel project
- Weak human capital and expertise throughout system

Detroit: Emerging System Changes

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- **Strategic investment framework (Detroit Future City)**
 - Target centers and corridors
 - Economic growth + neighborhoods + infrastructure
- **Growing CDFI capacity**
 - Second national CDFI (IFF) entered market in 2014
 - Local Invest Detroit expanded capital and capacity
- **Post-bankruptcy: better city government + new resources**
 - Professional planning, housing, economic development leaders
 - New city funding to reduce blight (\$115 million/year)
- **More private sector activity & developer interest**
 - Chase (\$100 million); Goldman Sachs 100K small businesses
 - Multiple new bank and insurance company investments
 - New project by national housing developer

Questions for Class Project

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- Which financing tools are appropriate for your project?
 - How to combine them into a viable financing plan?
 - Critical project financing gaps and how to address them?
- Which state and local intermediaries are critical to financing the project?
 - Capacity to lead coordination and structuring of financing?
 - Services and resources to address demand side and development services?
- What does your project reveal about the Charlottesville and Virginia finance system?
 - Functional, product and capacity gaps?
 - Alignment with local vision and priorities?
 - Coordination among intermediaries and programs?