Alaska Adopts Legislation to Promote the Use of NMTCs

By Vincent Ravaschiere, New Markets Capital Company

The state of Alaska has adopted legislation designed to promote the use of federal new markets tax credits (NMTCs) in Alaska. Under this new program, the Alaska Industrial Development and Export Authority (AIDEA) can facilitate NMTC transactions by acting either as the guarantor of an NMTC leverage loan or as the lender of last resort, providing the loan itself in situations where the existence of the AIDEA guarantee proves insufficient to induce a private financial institution to do so. AIDEA’s loan guarantee covers 100 percent of the leverage loan and would be available only to third party leverage lenders.

Leverage loans have a number of specific features necessitated by NMTC programmatic and transactional requirements. First, leverage loans are not made directly to the project entity, but are made through one or more conduit entities before the funds flow to the project entity. The funds typically flow from the leverage lender to a special purpose investment entity, which then combines the loan proceeds with the tax credit equity and invests the funds in another special purpose entity (the sub-community development entity (CDE)) in exchange for the tax credits. It is the sub-CDE which then lends directly to the project entity.

Second, leverage loans are not secured by mortgages or other direct liens on the project itself; the interests of the leverage lender are typically protected by other mechanisms, including the pledge of membership interests in the various conduit entities. Third, leverage loans cannot be called during the seven-year NMTC compliance period even in the event of a default; the leverage lender must forbear from any foreclosure actions during that time. Finally, the leverage loan must be structured as interest only for the seven-year NMTC compliance period.

Under the proposed program, AIDEA will undertake two basic functions: provide a 100 percent guarantee on a third party leverage loan made by a private financial institution, including instances in which the source of the leverage loan is a bond financing; and provide a direct leverage loan in those instances in which it can be demonstrated that at least two private financial institutions have declined to make a leverage loan to the project, notwithstanding the availability of the AIDEA leverage loan guarantee.

AIDEA will guarantee or provide leverage loans on such terms as AIDEA deems prudent and in accordance with regulations to be adopted by AIDEA pursuant to this new program. The terms of the guarantees and the direct loans will be determined by AIDEA on a case-by-case basis in accordance with its regulations. The cost of the guarantee has yet to be determined, but it is anticipated that the fee will be rolled into the principal amount of the leverage loan.

The legislation specifically allows AIDEA’s loans to be made in a manner consistent with the requirements of the typical NMTC leverage structure. For example, the legislation incorporates the understanding that these loans will be made to an intermediary investment fund rather than directly to the project itself. The legislation also allows for such loans to be made by AIDEA without being directly secured by a mortgage.
In addition, AIDEA will guarantee or provide leverage loans with the understanding that the leverage lender must forebear from triggering any foreclosure actions regarding the loans from the sub-CDE to the project entity during the seven-year NMTC compliance period. AIDEA also will guarantee or provide leverage loans structured as interest only for the seven year compliance period.

Finally, AIDEA will guarantee or provide leverage loans in transactions where there may be more than one leverage loan or more than one source for the leverage loan. In transactions in which there is more than one leverage loan, AIDEA may guarantee or provide direct leverage loans in whatever combination or permutation it deems appropriate.

The legislation anticipates that the specific terms of the privately made leverage loans eligible for the AIDEA guarantee will be a matter of negotiation between the third party lender and the other parties to the NMTC transaction. The AIDEA guarantee will stay in place for the term of the loan, even in the event that the term extends beyond the seven year NMTC compliance period. Provided that the payments on the leverage loan are current at the expiration of the NMTC compliance period, all or a portion of the leverage loan will be eligible for takeout by a loan issued under AIDEA’s existing Loan Participation Program.

Vincent Ravaschiere is president of New Markets Capital Company LLC and advised the state of Alaska with respect to the development of this legislation.

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