

**From:** Erik Hoffman [<mailto:EHoffman@kleinhornig.com>]  
**Sent:** Tuesday, November 20, 2018 8:20 PM  
**To:** Nicholson, Laura 6-9190  
**Subject:** SC QAP Revisions--Comments on Related Party Ground Leases

Hello Laura-

I have worked with a few South Carolina developers and work exclusively on tax credit financings and wanted to provide my feedback on the proposed QAP/Manual change that will prohibit related party ground leases.

Related party ground leases are common for housing authorities. Housing authorities often use ground leases in financings (mixed finance projects, RAD) and often the housing authority is part of the tenant that applies for the credits. This is a common practice when the project is being conveyed to a private developer or a related party developer to ensure that the critical public asset, the land, is protected no matter what happens to the project.

Similarly, we have seen more churches with excess land engage in affordable housing and put their property to use to help others. Often those churches will have development arms that will want to be part of that ownership to ensure it meets the needs of those in its community. Those churches often cannot dispose of the land, but can transfer an interest through a long term ground lease. Those leases would be prohibited by this change.

Also, ground leases with related parties are frequently used to better structure the financing for certain projects and nonprofit sponsors. Again, it protects the long term interest in the land in case the lender foreclosed (if the lease is senior to the financing) or the investor removed the related general partner. For the financing, the lease can often remove the land from certain tax credit requirements, like the 50% test which includes depreciable costs and the land in the denominator. Removing the land lowers the amount of tax exempt bonds needed to meet that test. This means less interim debt for the project, which saved funds (lender and legal fees, interest, and other transactional costs) and preserves more of the limited tax exempt volume cap that can be put to use in other projects.

Note, we do fully agree that the tax credit restrictive covenants should be imposed on both the landlord and the tenant, especially in a related party financing. Those tax covenants should span the full 30 years and only should terminate due to a foreclosure of debt from an unrelated lender.

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~~Only local government or public housing authority applicants may have~~The Applicant has an executed land lease or an executed option on a land lease either of which must not ~~The lease term may not~~ be for a term of less than fifty (50) years in term. ~~Such land lease or executed option on a land lease must be in the name of the government or PHA Applicant.~~ Long

term leases are not allowed for developments electing to convert to homeownership after fifteen (15) years. Related party land leases are not allowed. For projects proposing a land lease, the Authority will underwrite debt related to the lease at the lesser of the actual terms of the lease or the annual debt service produced by amortizing the appraised value of the land at the same rate and terms as the permanent loan. The Debt Coverage Ratio (DCR) rules identified in 8 a) through 8 d) located in the **IV. Financial Underwriting Standards** section will apply. **The Lessor will be required to execute the Agreement as to Restrictive Covenant.**

**Thank you for your consideration and enjoy the holidays.**

**Erik T.**

**Klein Hornig LLP**

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ERIK T. HOFFMAN | 1325 G Street NW | Suite 770 | Washington DC 20005  
D 202 842 0125 | F 202 842 3936 | [www.kleinhornig.com](http://www.kleinhornig.com)

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