The Mission Is Most Important

A Spotlight on National Equity Fund's Mission-Driven Innovations

By Abram Mamet

In the nearly four decades since its creation, the Low Income Housing Tax Credit (LIHTC) has become a critical engine for creating affordable multifamily housing in the United States. However, in its early years, many within the industry were uncertain as to how impactful the LIHTC program would be for the construction and preservation of affordable housing.

The Internal Revenue Service first introduced the concept of LIHTC as part of the Tax Reform Act that became effective on Oct. 22, 1986. Two and a half months later, National Equity Fund (NEF), founded by its affiliate The Local Initiatives Support Corporation (LISC), opened its doors on Jan. 9, 1987 as a nonprofit syndicator committed to establishing itself both as an advocate and a major industry player.

"The notion was that it was unproven and unknown what LIHTC would become," says Matt Reilein, president and CEO of NEF. "It was clearly a vehicle by which the federal government was going to support the creation of affordable housing. And the idea was to ensure that there was a nonprofit, mission-driven syndicator platform that was going to be involved not only in the genesis but also the early evolution of the program."


Matt Reilein

NEF leveraged its mission-driven spirit as a pioneer in this new industry, ultimately becoming a sophisticated player to help shape the future of the LIHTC program. "I do think that the early days of NEF's involvement in implementing the regulations did positively change the trajectory of the program and helped define the ecosystem that persists today," says Reilein.

Over the next 37 years, NEF would become one of the biggest players in the field, and today, stands as one of the largest syndicators of LIHTC-supported deals in the country, with business activity in 48 states, plus Puerto Rico and the U.S. Virgin Islands. Along the way, NEF has retained its core mission to "create and deliver innovative, collaborative financial solutions to expand the creation and preservation of affordable housing."

Primarily operating as a LIHTC syndicator for the bulk of its 37-year existence, NEF has in recent years branched out to other products and services and has even broadened its horizons beyond the LIHTC program itself. "The affordable housing crisis is not going to be solved by LIHTC alone," notes Reilein. "If we're going to try to be a leader and identify ways for capital markets to be part of the solution, we've got to broaden what it is we're doing."

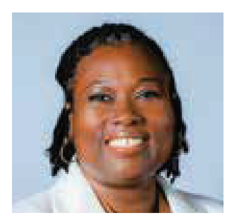
For example, NEF recently entered the mortgage lending space, joining investment firm Cinnaire and the Community Preservation Corporation to form the CPC Mortgage Company in an effort to serve as an impact-driven multifamily mortgage lender. This structure is novel and finds peer organizations in partnership over a shared mission. "While in some respects we're competitors," says Reilein, "we all have this nonprofit mission of making sure that there's a focus and commitment—and the sophistication—to bringing capital to multifamily affordable housing."

Though branching out and innovation can at times be risky, NEF's deep experience and substantial market engagement allow it to take chances on certain projects that other organizations—particularly ones motivated by profit—may not have the capacity to take on.

"We can leverage our track record and our expertise to accelerate the proof of concept for different solutions to today's wide-ranging affordability crisis," says Reilein. "And, whereas many firms must focus solely on their bottom line, we can be a bit of an incubator since we have a different underlying mission."

Bridging the Racial Development Gap: The Emerging Minority Developer Fund

One of the more recent products to come out of that innovative mindset is the Emerging Minority Developer Fund (EMDF). This fund is a result of NEF's efforts to "provide experienced LIHTC developers of color that are undercapitalized with unprecedented access to capital for the development of affordable housing," says Lydia Smith, vice president at NEF responsible for EMDF.


Lydia Smith

Indeed, developers of color are incredibly scarce in the industry. According to a report issued in March 2023 by Grove Impact, of the roughly 112,000 real estate development companies in the U.S., about 111,000 are white-owned. This underrepresentation becomes particularly acute as companies get larger, as only one out of an estimated 383 developers with more than $50 million in annual revenue is owned by a person of color.

In response, NEF launched the EMDF in the fall of 2020 to proactively narrow this gap and provide "experienced developers of color with access to capital they hadn't had before." The fund contains three components: LIHTC equity syndication, limited guarantee backstops and technical support funds. The fund is open to both for-profit and nonprofit entities that are predominantly either owned and managed or governed and managed by people of color.

EMDF intends to accelerate the growth in both the development capacity and financials of experienced LIHTC developers already operating in this space that are typically unable to access traditional LIHTC capital for development. More specifically, it is primarily for experienced yet undercapitalized LIHTC developer organizations that have developed or co-developed at least one LIHTC project from concept to placing it in service. Smith says, "We are seeking to advance those who have had a really hard time trying to build a business." Inexperienced LIHTC developers may be eligible with an experienced LIHTC development partner and a co-development agreement between them that is equitable for the new developer of color.

Critically, this is not meant to be a fund for developers to revisit year after year with each new potential LIHTC deal. Rather, Smith notes, the EMDF is for helping developers of color break "this constant cycle of having to partner, because they did not have deep enough pockets to provide guarantees."

Though a relatively young fund, Smith describes definite excitement about its possibility to impact the field. After strong interest during initial funding rounds in 2020, the EMDF eventually raised $147 million, which, according to Smith, will fund approximately 12 deals nationwide. Seven of those deals have already been closed and are now under development.

Though the EMDF is limited to this current round of $147 million in investment, Smith says that NEF is already looking forward to the next iteration of the EMDF, which will be called the Affordable Housing Equitable Access for Developers Fund (AHEAD). Despite the name change—which Smith notes is meant to elevate the equity goals of the fund—AHEAD will operate in largely the same way as the EMDF, with the same three components of LIHTC equity syndication, limited backstop guarantees and technical support funding.

Due to EMDF's success in providing proof of concept, Smith expressed optimism about AHEAD. "When we go out to our investors this time, it's not just a concept, but we have real deals to show them where and how we will put their investment dollars to work."

One of the major challenges to bridging the gap for developers of color is the fact that many of these smaller organizations may not even have the capital to assemble and execute a LIHTC application in the first place. Since the EMDF and AHEAD don't explicitly provide working capital or predevelopment funds, this can leave worthy and interested organizations unable to participate.

In response, NEF has put together the Pay it Forward Program (PIF). PIF, a program administered by NEF's charitable arm (NEF Housing Charities, Inc.), provides experienced LIHTC developers who are approaching submission of a LIHTC application with "a flexible and patient capital bridge to tax credit applications and awards in the form of recoverable grants and application assistance loans," according to the NEF website. Smith says that these funds can be critical in bridging the gap between potential tax credit applications and reality by providing funding for "expenses required in order to submit a viable tax credit application," such as "acquisition, architects, environmental and consultants." According to Smith, the eligibility requirements for PIF are generally the same as those for EMDF/AHEAD, however, PIF is strictly for developers of color who have already developed or co-developed a LIHTC deal.

Smith acknowledges that the EMDF/AHEAD funds are not the complete solution for racial equity in development and that it takes a system-wide approach to narrow those gaps. However, the type of targeted and proactive funds, like EMDF and AHEAD are, for now, vital, and Smith says, "NEF expects to have some form of these funds in its portfolio indefinitely at this point as we continue to try to figure out how to streamline this profile of developer into our regular operations."

This fund, it seems, is possible due to NEF's explicitly mission-oriented approach to syndication and capital deployment. According to Smith, the guarantees and technical support components of EMDF are funded primarily by NEF's fee that it normally takes for originating and syndicating these deals. "So, NEF doesn't stand to make money with these funds, at least in the short term. And that's okay. Because the mission is more important." TCA