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NDC Highlights ‘American’ P3 Model, Funded with Tax-Exempt Debt

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LOS ANGELES – The National Development Council is highlighting what it describes as its proven “American model” for social infrastructure public-private partnerships, which uses tax-exempt bonds.

“It’s unique in the world of public sector developers, because it possesses a group exemption letter from the IRS,” said Dan Marsh, executive vice president of the National Development Council. “We can incorporate any number of single-asset stand-alone corporations.”

The National Development Council traces its roots to 1969, when the not-for-profit’s original thrust was for community revitalization projects in New York City. It evolved to work with clients nationally and in Puerto Rico advising small businesses and providing technical assistance and support on community economic development projects.

It began developing financial products in the 1980s when it found many low-income communities struggling to obtain equity and debt.

That led in 1989 to the formation of NDC Housing and Economic Development Corp., the entity that holds the IRS letter. Marsh is its president.

Marsh said the NDC model uses tax-exempt bond financing and employs a private sector development team to maximize the benefits of private sector development expertise.

Under the IRS group exemption, it creates bankruptcy-remote special purpose vehicles.

The process begins when the NDC Housing and Economic Development Corp. sets up a not-for-profit owner/issuer of tax-exempt bonds, then hires a private developer, architect and general contractor who are charged with developing the facility. The development team is under contract to take construction and delivery risk.

After construction is completed, the facility is leased to the governmental client and then transferred to the client at no risk when the debt is retired. Lease payments are set at debt service plus operating costs.

The NDC said it has financed over \$2.5 billion in social infrastructure projects through its

public-private partnerships, working on 37 projects developing more than 3.7 million square feet into municipal office space, city halls, justice centers, student housing, libraries and hospitals.

One of the largest is a multi-phased biomedical campus developed for the University of Washington in Seattle's South Lake Union neighborhood.

Vulcan Real Estate, a company owned by Microsoft co-founder Paul Allen, began assembling properties in the neighborhood with the goal of creating a Seattle Commons area with an urban park. When a ballot measure to support the project failed, Allen began working instead to develop the area into a vibrant neighborhood with restaurants, homes and major employers.

The neighborhood is well-known today for hosting offices of Internet behemoth Amazon, but the University of Washington played a major role in energizing the area, with NDC financing.

As Vulcan first began formulating its redevelopment plan in 2002, UW was discovering it did not have enough space on its existing campus to expand its biomedical program.

A year later, UW entered into a partnership with Vulcan, Architects Perkins + Will and NDC to develop the new biomedical campus in South Lake Union, three miles south of its main Seattle campus.

Since then, seven series of bonds with a total par amount of \$494.71 million have been issued for the UW buildings, including a \$13.2 million taxable series in 2010, said Bill Starkey, the university's associate treasurer.

Most recently, Washington Biomedical Research Properties, the special purpose vehicle created for the UW bonds, issued \$131 million in tax-exempt bonds on Oct. 7, 2015. The deal was issued at ratings of AA-plus from Standard & Poor's and Aa1 from Moody's Investors Service.

The debt service is paid with lease payments from UW, said Chris Malins, the university's vice president for treasury.

It is hard to say what the savings are, because the university would have to have built the same building using public works procurement laws in order have a comparison, Malins said.

"The idea is that having private development, management, and the ability to reconfigure the space through tenant improvements in a faster way, are the advantages," he said.

Work began on the UW School of Medicine Campus in 2003. The first project involved renovating an existing 105,000-square-foot building into a biomedical research facility. Since then, it has built two more laboratory buildings and one office building. When it completes what it calls phase 3.1, it will have laboratory and office space totaling more than 638,000 square feet.

NDC uses its group exemption to create individual 63-20 nonprofit corporations to issue tax-exempt bonds directly, without a conduit issuer.

The method of issuing bonds was historically used to avoid statutory debt limitations, but private developers working with public agencies have used the structure to develop transportation projects since the early 2000s.

With its group tax exemption letter, and because it is a recognized 501(c)3 nonprofit, NDC can form the single-use corporations more quickly, Marsh said.

“We don’t have to spend a year seeking a determination that our organization qualifies in issuing debt,” he said.

NDC received the group tax exemption letter, he said, because it was able to make a compelling case that it could further the mission of lessening the burden of government.

“Our mission is to find and build assets for municipalities that helps them in revitalization and to provide space for government programs,” he said.

NDC maintains the asset, which it allows the municipality or nonprofit to use for a proscribed period of time through a lease arrangement. At the end of the lease period, the asset is handed over to the municipality at no cost, he said.

Unlike in a traditional design-build-finance-operate and maintain model, NDC does not own the biomedical buildings; the special service vehicle (in the case of the UW projects, Washington Biomedical Research Properties) is the owner, said Matt Calcavecchia, NDC’s communications director.

NDC provides many of the same services as a private developer in the DBFOM model with one main difference – 100% of the financing comes through the tax-exempt debt market, which is the lowest cost of capital in the U.S. for financing not-for-profit and municipal bond projects, Calcavecchia said.

Its “American Model” allows NDC to work on projects of \$20 million and up, whereas typical equity-fueled P3 DBFOM projects are feasible at \$200 million or up, Calcavecchia said.

When NDC started on the project in Seattle, the South of Union neighborhood was blighted, but Marsh said NDC’s structure is equally effective in areas that are not blighted. The project has to fulfill the mission of lessening the burden of government.

When it worked on the Riverside County Law Building in Indio, Calif. that was completed in 2012, it came in \$4.2 million under budget. The cost savings was split between the developer and the county, he said.

“We aren’t criticizing other models; there is more than one way to achieve a solution,” Marsh said. “It is just when you are working with municipalities you need to explore all of the options and find the best solution for the project.”

Many times NDC has told clients they are better off issuing general obligation bonds than doing a P3, Marsh said.

“There is no one size fits all, or that we are the universal solution,” he said. “We think there are public policy benefits to what we do and that we have an obligation to find the most cost effective way to do it.”



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