OPPORTUNITIES AND OBSTACLES
IN YEAR 15

There are many factors that must be considered when deciding what to do with a low-income housing tax credit ("LIHTC") project after the expiration of the 15-year compliance period. The options differ significantly if a non-profit corporation is involved with the project. The considerations are based largely on how the transaction is structured at the initial closing. Consequently, it is important to evaluate the options that are available at the initial closing and how they impact the choices available at the end of the 15-year compliance period. Recent actions taken by some aggressive investors and related litigation may impact how transactions are structured going forward.

Considerations at Initial Closing

When structuring a LIHTC transaction, an important consideration is whether there is an entity classified as a non-profit corporation ("NPC"), as defined under Section 42(h)(5) of the Internal Revenue Code, a government agency, or a tenants' organization that is or could be involved in acquisition of the project after the end of the compliance period. The involvement of an NPC, governmental entity, or tenant's organization expands the options available at the end of the compliance period.

As background, to claim LIHTC, the investor must be characterized as an owner of an interest in the project. An investor needs to have an opportunity to have some upside in a project to be classified as having an ownership interest. Where a partner was only entitled to reimbursement of its expenses and a fixed profit, the court found against the existence of a partnership.[1] Consequently, the partner was found not to have an ownership interest and was not entitled to pass through tax benefits.

The rules are less stringent for LIHTC projects than for historic and other credits. Section 183 of the Code disallows losses, deductions, or credits to activities that are not engaged in for-profit. However, Treas. Reg. § 1.42-1 states Section 183 does not apply to LIHTC projects. As a result, financial projections do not have to show a significant profit to the investor. However, the inapplicability of Section 183 does not completely eliminate the requirement that the investor have some possibility of receiving some upside in addition to the tax credits. This concept has a significant impact on how year 15 exits can be structured.[2] It makes it impossible for the general partner to have the right to purchase the project or the investor's interest for a fixed price determined at initial closing.

Options

In general, subject to the exception described below for non-profits, an investor can agree to transfer its interest in the project at the end of the compliance period but the purchase price has

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[1] https://www.wbur.org/investigations/2021/04/29/investors-low-tncome-housing-boston-south-end

[2] *ASA Investering Partnership v. Commissioner*, 201 F.3d. 505 (U.S. App. D.C. 2000).

to be based on fair market value. The agreement can provide that a specified party, typically the general partner/managing member can have an option to acquire the project or the investor's interest for fair market value. For business, and not tax reasons, the agreement frequently also requires a payment equal to any amounts owed to the investor.

The agreement may contain certain provisions regarding how fair market value is calculated including taking any continuing low-income restrictions into consideration. However, investors will be reluctant to include provisions that are clearly designed to discount traditional fair market value.

The strategies for exit on year 15 include a right of first refusal under 42(i)(7) ("ROFR") when a non-profit or governmental entity is involved in the project, an option to acquire the project or the limited partnership interest at fair market value, a put by the limited partner, or disposition of the project pursuant to a qualified contract pursuant to Treas. Reg. 1.42-18. See Exhibit ___.

Section 42(i)(7) Right of First Refusal

Section 42(i)(7) of the Code contains a special provision pursuant to which a qualified non-profit organization, governmental entity or tenant organization (a "Qualified Purchaser") can acquire the project after the compliance period. A Qualified Purchaser can have a right of first refusal to acquire the project for the outstanding debt on the project (excluding any debt incurred within a five-year period prior to the sale) plus any federal, state, and local taxes resulting from the sale. Typically, the agreement will also require the purchaser to pay any unpaid fees or other benefits due to the investor.

It is interesting to note that the Code references a right of first refusal ("ROFR") rather than an option. Unlike an option which can be exercised unilaterally by the grantee, a ROFR needs to be triggered by another offer to purchase the project. In addition, a ROFR usually requires the grantee to match the third-party offer. The ROFR under Section 42(i)(7) is for a fixed price equal to outstanding debt plus to the partner's tax liability. This is confusing because the Section 42(i)(7) ROFR seems to combine the need for a third party offer with the fixed price typical for an option. It is hard to imagine what third party would make an offer knowing that the general partner could then buy the project for a lower price.

Questions have been raised about what constitutes a bona fide third-party offer. This is dependent on the language in the ROFR. While some courts have found that a traditional third-party bona fide offer is not required,[3] some investors have contended that a bona fide third party is required and have been challenging the right of Qualified Purchasers to exercise the ROFR. As noted above, the requirements of 42(i)(7) may make it difficult to get a bonafide third party offer. The offer may have to come from a friendly unrelated third party that has the financial ability to purchase the project.

Investors are challenging both the ability of general partners and others to exercise ROFRs and the purchase prices that must be paid under options. Many of those investors were not the

[3] *Homeowner's Rehab Inc,* v. *Related Corporate V SLP, L.P.*, (SJC/2441) (Mass. 2018).

initial investors but instead acquired their interest from the initial investor.[4] These investors are referred to as "aggregators" and they acquire interests in LIHTC projects with a goal to maximize profits, including using aggressive litigation tactics.[5] As a result, consideration should be given to adding a provision restricting transfer of the investor's interest to certain entities. Some aggregator's currently may include Alden Torch Financial, The Wentwood Companies, and Boston Financial.

Some agreements are now including a prohibited transferee list. While it is difficult to predict the identity of aggregators in fifteen years, the agreement can at least identify current entities engaged in aggressive litigation about the exercise of ROFRs or the value of properties under options.

Another issue is what is purchased under the ROFR. The language in the Code is that "'No federal income tax benefit shall fail to be allowable to the taxpayer with respect to any low-income building merely by reason of a right of first refusal...to purchase the property." Clearly, the land and building can be purchased pursuant to the ROFR. It is unclear as to whether personal property is included. Reserves are probably not included in acquisition under the ROFR. This can make structuring an offer more complicated.

Drafting Right of First Refusal

It is important to carefully draft the ROFR. Disputes about the enforceability of ROFRs have made it increasingly important to make sure that the grantees of ROFRs can exercise the rights granted in the ROFR. Litigation by Alden Torch and other "aggregators" challenging the right to exercise ROFRs have highlighted the need to carefully draft the terms of a ROFR. It is important to consider:

Grantee should receive the following:

a. Options

(i) To purchase project

(ii) To purchase limited partnership interest

b. Right of first refusal (ROFR)

Grantee needs to have adequate time to exercise right of first refusal. It should extend beyond the compliance period.

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4 See, A Report from the Washington State Housing Finance Commission, September 2019, www.wshfc.org/admin/Reporton 15 YearTransferDisputes.PDF

5 *Tenants' Development Corporation v. AMTAX Holdings 227, LLC and Alden Torch Financial LLC*, Civil No. 20-10902-LTS (D. Mass. Dec. 23,2020).

(i) Grantee should be given adequate time to close after exercising the ROFR.

(ii) Interests should be valued as a going concern rather than liquidation value.

(iii) The purchase price for the partnership interest should not have the outstanding debt as the minimum price.

(iv) The purchase price for the project should take into account restrictions on rent and occupancy of the project.

(v) Grantee should have the right to assign the ROFR/Option to another eligible entity.

(vi) ROFR/Option should not terminate on any default by general partner and any cured defaults should not be a basis for termination.

(vii) Make sure that process for determining fair market value is clearly defined.

(viii) To trigger ROFR, offer should come from third party but should not have to be a bona fide offer.

(ix) Consider limiting transferees of the investors limited partnership interest to prohibit transfers to identified aggregators.

(x) If the ROFR takes into consideration restrictions on the property in determining the fair market value. See Exhibit A for an example of a ROFR that includes suggested changes to a ROFR. Note that not all of the suggested changes may be accepted by a limited partner investor.

Puts

Another provision that can be included in the documents at initial closing is a right for the investor to put its interest to the general partner. This means that the investor can require the general partner for a pre-established price. A put can be at less than fair market value. Because this decision is under the control of the investor, it does not create an issue as to whether the investor has an upside and will be treated as a partner. Frequently, the put price is nominal but may also include any amount that the general partner owes the investor for investor loans, credit adjusters, exit taxes, and other amounts owed to the investor.

Qualified Contracts

Another consideration at the initial closing is whether the project may be transferred pursuant to a Qualified Contract under Section 42. A Qualified Contract enables an owner of a

project to terminate the 15-year extended use period.[6] Frequently, to get additional points in its application, an applicant for LIHTC may waive the ability to terminate the extended use agreement. It is important to make a decision when applying for LIHTC to decide whether to waive the ability to offer the project pursuant to a Qualified Contract. Note that many states now require applicants to waive the Qualified Contract as a condition to receiving LIHTC.

Pursuant to the Qualified Contract provision, an owner of an affordable housing project can request the state housing agency find a buyer pursuant to a qualified contract. This may be done any time after the 14th year of the 15-year compliance period. If no purchaser is found, the land use restrictions can be terminated, subject to a three-year transition period. The Qualified Contract price includes the fair market value of any non-low-income portion of the building, plus the formula contract price for the low-income portion of the building. The value of the low-income building is an amount not less than the sum of (1) the outstanding debt, (2) adjusted investor equity, and (3) other capital contributions, less cash distributions. Only capital contributions for capital costs may be included in the calculation. The fair market value of the non-low-income portion of the building is added to the price and includes the fair market value of the land underlying the entire building. The state credit agency cannot establish a maximum fair market value that is less than the Qualified Contract price.

The adjusted investor equity is the amount of cash invested (the unadjusted investor equity) increased by an annual cost-of-living adjustment. Unadjusted investor equity means the aggregate amount of cash invested for qualifying building costs. Amounts paid for land and other items excluded from eligible basis are not included. The adjusted investor equity is determined based on the investor's commitment as of the beginning of the credit period.

The Qualified Cost-of-Living Adjustment is the quotient of (i) The sum of the 12 monthly Consumer Price Index (CPI) values whose average is the CPI for the calendar year that precedes the calendar year in which the Agency offers the building for sale divided by, or (ii) the sum of the 12 monthly CPI values whose average is the CPI for the base calendar year.

An example illustrates that the Qualified Contract Price is very high so that it is difficult for the state allocator to find a purchaser.

An investor contributed $20,000,000 in equity to a building in 1997, which was the first year of the credit period for the building. In 2011, the owner of the project requested the tax credit agency to find a buyer to purchase the building, and the tax credit agency offered the building for sale to the general public during 2011. The CPI for 1997 (within the meaning of section 1(f)(4)) is the average of the Consumer Price Index as of the close of the 12-month period ending on August 31, 1997. The sum of the CPI values for the twelve months from September 1996 through August 1997 was repay the investor its capital 1913.9. The CPI for 2010 (within the meaning of section 1(f)(4)) is the average of the Consumer Price Index as of the close of the 12-month period ending August 31, 2010. The sum of the CPI values for the twelve months from September 2009 through August 2010 is 2605.959. At no time during this period (after the base calendar year) did the CPI for any calendar year exceed the CPI for the preceding calendar year by more than 5 percent. The

[6] IRC § 42(h)(6)(F); Treas. Reg. § 1.42-18.

qualified-contract cost-of-living adjustment is 1.3615962171 (the quotient of 2605.959, divided by 1913.9). Owner's adjusted investor equity, therefore, is $27,231,924, which is $20,000,000, multiplied by 1.3615962171, rounded to the nearest dollar. While the increase from $20,000,000 to $27,231,924 is not shocking, the need to include a return of equity makes purchase of the property infeasible in virtually all situations.

Outstanding indebtedness means the remaining stated principal balance (which is initially determined at the time of the credit agency's offer of sale of the building to the general public) of any indebtedness secured by, or with respect to, the building that does not exceed the amount of qualifying building costs. Any refinancing indebtedness or additional mortgages in excess of the qualifying building costs are not outstanding indebtedness. Examples of outstanding indebtedness include certain mortgages and developer fee notes (excluding costs not included in eligible basis). Outstanding indebtedness does not include debt used to finance non-depreciable land costs, syndication costs, legal and accounting costs, and operating deficit payments. Outstanding indebtedness includes only obligations that are indebtedness under general principles of federal income tax law and that are actually paid to the lender upon the sale of the building or are assumed by the buyer as part of the sale of the building.

In calculating the Qualified Contract Price distributions to investor are subtracted, distributions include:

a. All distributions from the building to the owners or to persons whose relationship to the owner is described in section 267(b) or section 707(b)(1)) of the Code, including distributions under section 301 (relating to distributions by a corporation), section 731 (relating to distributions by a partnership), or section 1368 (relating to distributions by an S corporation); and

b. All cash and cash equivalents available for distribution at, or before, the time of sale, including, for example, reserve funds whether operating or replacement reserves, unless the reserve funds are legally required by mortgage restrictions, regulatory agreements, or third-party contractual agreements to remain with the building following the sale.

There are typically limited distributions to investors in LIHTC transactions.

An appraisal must be done to calculate the Qualified Contract Price for any non-low-income portion of a building. The regulation does not adopt any specific methodology or standards for appraising the property. Appraisers currently on any list for active suspension or revocation for performing appraisals in any state or listed on the Excluded Parties Lists System (EPLS) maintained by the General Services Administration for the United States Government are barred. Agencies have discretion to select the appraisers involved in the qualified contract process and to require all appraisers to be state-certified general appraisers.

With respect to a Qualified Contract, a credit allocator may charge an administrative fee (appraisal costs, etc.). The agency may require additional information before offering the property for sale pursuant to a Qualified Contract, require verification of information, and require appraisers

to be acceptable to the agency. The credit allocator may also specify other conditions applicable to the Qualified Contract consistent with the Code and Regulation 1.42-18.

The inclusion of debt and equity, plus an escalator on equity, generally makes the Qualified Contract Price higher than fair market value. State agencies cannot limit the Qualified Contract Price to fair market value. As a result, many state agencies are using the LIHTC application process to effectively prohibit the use of Qualified Contracts. There have also been recent federal legislation proposals to change the Qualified Contract provision.

Prior to the close of the three-year period following the termination of the low-income restrictions, no owner shall be permitted to evict or terminate the tenancy (other than for good cause) of an existing tenant of any low-income unit or increase the gross rent for the unit in a manner or amount not otherwise permitted by Section 42 of the Code.

Structure of Limited Partnership

Another factor to consider at the initial closing are the losses allocated to the investor. While the investor typically wants to maximize losses to improve return, higher losses can impact the amount to be paid to get the investor to exit the transaction. Higher losses may require the general partner to pay the limited partner to exit the transaction. This is particularly the case when the general partner is relying on a ROFR for the year 15 exit. Since the 42(i)(7) ROFR includes exit tax liability, allocations of losses to the investor can have a direct impact on the exit price. Losses allocated to the investor may be increased with higher interest rates on loans, shorter depreciation periods, and the structure of expenses paid by the owner or other parties such as a service provider.

Another consideration at the initial closing is the term of the extended use agreement ("LURA"). A longer extended use period under the LURA will usually reduce the fair market value of the project in year 15. Similarly, additional restrictions on rents and tenants' incomes will reduce the fair market value of the project.

LURA

Since 1990 a project must be subject to an extended low-income housing commitment (LURA) Under Code Section 42(h) the LURA must:

1. Require that the applicable fraction for each year in the extended use period be not less than the applicable fraction specified in the agreement;

2. Allow qualifying tenants (whether prospective, present or former tenants) the right to enforce in any state court the requirements of the agreement;

3. Prohibit the disposition to any person of any portion of the building to which the agreement applies unless all of the building to which the agreement applies is disposed of to such person;

4. Prohibit the refusal to lease to a Section 8 voucher or certificate holder because of the status of the prospective tenant as such a holder;

5. Be binding on all successors of the taxpayer;

6. Be recorded pursuant to state law as a restrictive covenant applicable to the property.

The LIHTC compliance period is 15 years during which period LIHTC may be recaptured. The extended use period must be at least an additional 15 years beyond the compliance period during which period the state allocator and tenants can bring an action to enforce the restrictions contained in the LURA. Frequently, the extended use period is longer than 15 years based on points awarded during the LIHTC application process. Some states mandate a longer extended use period for all projects.

The LURA can be terminated by a conveyance as a result of foreclosure or deed-in-lieu other than a foreclosure structured to avoid termination of the LURA, subject to a three-year phase out. If not waived, the failure of the allocator to find a purchaser at the Qualified Contract Price may also terminate a LURA.

The IRS does not enforce LURA after the compliance period. The credit allocator, tenants and prospective tenants may enforce the LURA. In Nordbye v. BRCP GM Ellington,[7] the Court found that tenants who were evicted because of termination of LURA had a cause of action. The Court also found that the Oregon credit allocator could not terminate the LURA upon a finding of owner's material noncompliance with the LURA. This case has made credit allocators nervous about modifying or terminating a LURA.

Choices in Year 15

There are a number of potential opportunities for a general partner/managing member in year 15. As noted above, the available choices will depend in large part on the type of acquiring entity and how the transaction was initially structured.

Potential choices include an acquisition of the project or investor's interest at fair market value, sale pursuant to a ROFR, transfer pursuant to a Qualified Contract, resyndication, transfer pursuant to a put, a bargain sale, or conversion to homeownership. However, despite all of the choices available under Section 42, the most common occurrence in year 15 is a transfer pursuant to negotiations between the parties. The terms of the transfer are not and cannot be described in the initial documents. Frequently, the investor is willing to transfer its interest for nominal consideration, an agreement that could not be included in the initial syndication documents. Note that this is not always the case and an increasing number of investors are trying to maximize return in year 15. "This new breed of investors is challenging housing groups in cities where real estate values have soared. The firms are looking to invest cash and control away from local non-profits and developers, lawsuits show, or attempting to oust managers from partnerships.''[8]

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[7] *246 Ore. App. 209, 266 P.3d 92 (Ct. App. Ore. 2011).*

[8] *After The Low Income Housing Tax Credits Are Done, Investors Want More*, Forbes January 13, 2021 https://*www*.forbes.com/sites/peterjreilly/2021/01/13/after-the-low-income-housing-tax-credits-are-done-investors-want-more/?sh=74c20d364765. *Investors Mine for*

To commence the process, it is important to collect the applicable documents. First, the organizational documents contain important terms, so it is essential to review the Limited Partnership Agreement or Operating Agreement and all amendments. Of particular interest are any transfer restrictions, consent requirements, sale provisions, including any options, puts, or rights of first refusal. Note that options and rights of first refusal may be in separate agreements. It is also important to review the original projections, updated projections, and tax returns to determine the status of the partners' capital accounts and information about projected exit taxes. Restrictions contained in any declarations or regulatory agreements, including the LURA, are also important. These can be used to determine when use restrictions, including the compliance period and extended use period expire. Note that compliance periods expire on December 31, even if a project is placed in service during the calendar year.

Refinancing may be an option for a property that has few capital repair needs.

There are also some practical considerations. The physical condition of the property has an impact on the choices. A property with significant capital needs may be a candidate for resyndication. The interests of third parties need to be considered as well. The willingness of public and private lenders to permit assumption and any necessary loan modifications need to be considered. Resident, local government, and community attitudes about the project can also have an impact on available choices. Strong resident and community support can be beneficial.

A first possibility is the acquisition of the project or the investor's interest in the project if there is an option to do so in the organizational documents or a separate agreement. If there are options to acquire either the project or the investor's interest, it will be important to evaluate which is better. If the project is subject to significant debt and needs capital improvements, the value of the project may be limited. Because the investor usually receives limited cash distributions and is no longer receiving tax credits, the value of that interest may be low, particularly if the investor has a smaller interest in the sales proceeds and cannot force a sale. If the parties cannot agree on value, it will be necessary to obtain an appraisal to determine the value of the interest on the project. Acquisition of the limited partnership interest may avoid some transactional costs.

If available, a second possibility is acquiring the project pursuant to a right of first refusal. While the ROFR technically requires a third party offer to trigger the ROFR, some investors may waive this requirement. However, others will require strict compliance with the ROFR requirements. Consequently, it is necessary to carefully review the time frames, procedures and third party offer requirements. It may be necessary to find a friendly third party to make an offer.

The investor may require the general partner to offer the project to the credit allocator pursuant to the Qualified Contract provisions, particularly if the initial organizational documents contained this requirement. This may not be required if the taxpayer waived its right to offer the project to the allocator pursuant to a Qualified Contract.

Profits In Affordable Housing Leaving Thousands of Tenants at Risk, www.wbur.org/investigations/2021/04/29/investors-low-income-housing-boston-south-end (April 29, 2021).

Another possibility is to resyndicate the project. This means selling and rehabilitating the project and claiming a new acquisition credit and rehabilitation credit. The project can be sold to a new partnership provided that partners in seller retain less than a 50% interest in buyer. The resyndication needs a new allocation of tax credits or tax-exempt bonds. The sale is eligible for the 4% credit and the rehabilitation is eligible for the 9% credit (unless financed with tax-exempt bonds, in which case the 4% credit applies). This choice is most appropriate for projects with deferred maintenance needs. A project cannot claim a new acquisition credit until the end of the compliance period. Resyndication frequently requires debt restructuring with resulting complex tax issues. If the appraised value of the property exceeds the debt, Seller take back notes can help to address cash flow distribution issues caused by the 50% ownership limitation.

The investor may also decide to put its interest back to the general partner if the general partner does not exercise its option or ROFR. As noted, this put will be pursuant to provisions in the original organizational documents and it does not have to be at the fair market value of the interest.

In some instances, a bargain sale or charitable contribution may be a possibility. If the fair market value of the property exceeds the amount of the debt, a transfer to the non-profit may be treated as part sale and part donation. This can reduce/offset exit taxes payable by the limited partner. However, A partner's charitable deduction cannot exceed its share of the excess fab-market value over liabilities, reduced by its share of the gain that would have been treated as other than long-term capital gain if the donated portion of the property was sold for its fair market value

In some instances, a project may be converted to home ownership at the end of the compliance period. A purchase by a tenant pursuant to Section 42(i)(7) of the Code may terminate an extended use agreement (Rev. Rul. 95-49). Frequently, the transaction will be structured as an acquisition by the general partner with subsequent sales to the tenants since it is difficult to get all tenants to buy simultaneously and the investor will not want to deal with the tax consequences of sales to tenants. Some states, including Minnesota have guidelines for sales to tenants.

Recently it has been more common for investors to exit the partnership before the end of the compliance period. An investor can exit between year 10 and year 15 without recapture if compliance with the tax credit is maintained. There is no longer a need to post a bond. Usually, the investor will want an indemnity against tax credit recapture from an entity with sufficient net worth.

There are several considerations when negotiating investment terms with the investor. First, the general partner should try to get the right to acquire the investor's interest in the partnership in addition to an option to acquire the project. The option to acquire the interest should give the general partner at least one year to exercise the option to purchase the partnership interest and it should include sufficient time to close on the acquisition, including time to obtain any necessary approvals. To the extent possible, loan documents should permit transfer of limited partnership interests without lender consent. The language should make it clear that the investor's taxes attributable to the sale are not part of the purchase price. The language should also clearly state that the transfer of partnership interest does not trigger the liquidation provisions of the partnership agreement.

Although some investors may resist it, if possible, record the right of first refusal/option in the real estate records. This will avoid a sale to a third party to circumvent the option.

Any ROFR should be assignable to another party eligible to exercise the ROFR.

The Future

There are two areas where proposed legislation could improve year 15 opportunities. First, proposed legislation, if passed by Congress, would eliminate some of the issues with ROFRs.

Second, revision or elimination of the Qualified Contract provisions could help to address long term affordability of LIHTC projects.

The proposed legislation to revise § 42(i)(7) of the Code:

1. Would expressly permit options.

2. Would permit an option to acquire the investor's partnership interest.

3. Provides that the option or right of first refusal may be exercised without the approval of the investor.

RECORD AND RETURN TO:

_____

Ballard Spahr LLP

_____

_____

OPTION AND
RIGHT OF FIRST REFUSAL AGREEMENT

THIS OPTION AND RIGHT OF FIRST REFUSAL AGREEMENT (this "**Agreement**") is entered into as of _____, 2023, by and among OWNER LLC, a State X limited liability company (the "**Owner**"), AFFORDABLE HOUSING DEVELOPMENT, a State X non-profit corporation (the "**Grantee**"), with MANAGING MEMBER LLC, a State X limited liability company (the "**Managing Member**"), as a consenting party.

RECITALS:

A. The Owner owns these certain improvements to be constructed, consisting of 104 dwelling units and commercial space, and a leasehold interest in the land on which the improvements are to be situated located in City, State X, which is more particularly described on Exhibit A, attached hereto and made a part hereof by this reference (together, the "**Project**").

B. The Owner is governed by that certain Amended and Restated Limited Liability Company Agreement dated as of June 1, 2019, by and between the Investor Member and the Managing Member, as may be amended (the "**Operating Agreement**").

C. The Owner desires to give, grant, bargain, sell and convey to the Grantee certain rights to purchase the Project on the terms and conditions set forth herein.

D. As acknowledged in the Operating Agreement, Investor Member desires to give, grant, bargain, sell and convey to the Grantee certain rights to purchase the Investor Member's Interest on the terms and conditions set forth herein.

E. All capitalized terms used but not otherwise defined in this Agreement shall have the meanings ascribed to them in the Operating Agreement.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:

ARTICLE I
GRANT OF OPTION AND RIGHT OF FIRST REFUSAL

1.1 The Owner hereby grants to the Grantee a purchase option (the "**Option**") and right of first refusal (the "**Right of First Refusal**") to purchase the Project and the Investor Member's Interest on the terms and conditions set forth in this Agreement.

1.2 If at any time during the term of this Agreement the Managing Member is no longer a managing member or a member of the Managing Member of the Company pursuant to the terms of the Operating Agreement, the grant of the Option and the Right of First Refusal shall continue unless the removal of Managing Member was caused by the action or inaction of Grantee or its Affiliates.

ARTICLE II
TERM OF OPTION AND RIGHT OF FIRST REFUSAL

2.1 Term of Option. The term of the Option to purchase the Project shall commence one day after the Owner shall have completed the Compliance Period and continue for a period of thirty-six (36) months. The term of the Option to purchase the Investor Member's Interest shall begin one day after the conclusion of the Credit Period and continue for a period of thirty-six (36) months after the Compliance Period; provided, however, that the exercise of the Option prior to the conclusion of the Compliance Period is dependent upon the Investor Member's receipt of a recapture guaranty that.is satisfactory to it in its sole discretion.

2.2 Term of Right of First Refusal. The term of the Right of First Refusal shall commence one day after the Owner shall have completed the Compliance Period and shall continue for a period of thirty-six (36) months (the "**RoFR Term**").

ARTICLE III
MANNER OF EXERCISING OPTION AND RIGHT OF FIRST REFUSAL

3.1 Exercise of Option. The. Grantee shall exercise the Option to purchase the Project by delivering to the Owner, with a copy to the Investor Member, written notice of the exercise of the Option. The note of exercise of the Option shall state that the Option is exercised without condition or qualification.

3.2 Exercise of Right of First Refusal.

3.2.1 With respect to the Right of First Refusal, if, during the RoFR Term, 1) the Owner receives an unrelated third party written offer (an "**Offer**") to purchase the Project, at a price not less than the minimum purchase price under Section 42(i)(7) of the Code (the "**Statutory Purchase Price**"); 2) the Managing Member determines that it is in the best interest of the Owner to sell the Project upon the terms set forth in the Offer, subject to the terms of the loan documents applicable to the Project; and 3) the Owner provides to the Grantee a notification in writing of the Offer (an "**Offer Notification**") and the Owner's determination to sell, the Grantee then may notify the members of the Owner (the "**Members**") of its intent to exercise its right of first refusal to purchase the Project, provided that the Grantee or its designee is then a qualified nonprofit organization or governmental agency as required for the purposes of Section 42(i)(7)(A) of the Code (an "**Eligible Purchaser**"). For purposes of this Agreement, the calculation of the Statutory Purchase Price shall be based on the assumption that each Member (or, if any such Member is a pass-through entity for tax purposes, each of the partners, members or participants of or in such entity) is subject to tax with respect to such disposition at the highest federal, state and local tax rates applicable to it and the deductibility of state taxes paid for federal income tax purposes.

3.2.2 The Grantee shall receive at least ninety (90) days' prior notice of Owner's intent to sell and shall be given no less than one hundred eighty (180) days to review and consider the Offer Notification. If, within such 180-day period, the Grantee notifies Owner of its plans to exercise its right of first refusal, then the Grantee shall have no less than one hundred twenty (120) days from the notification date of its intent to exercise the right of first refusal to reach a financial closing on such purchase. In the event the Grantee has issued such a notification of intent to exercise the right of first refusal and is unable to reach a financial closing within such 120-day period, but is making commercially reasonable progress to secure financing for such purpose, the Grantee shall be given an extension of no less than another one hundred and twenty days (120) to complete the financial closing.

3.2.3 Notwithstanding anything to the contrary set forth in this Article III, the parties agree that if (i) the Code allows or the Internal Revenue Service issues authority to permit the owner of a low-income housing tax credit project to grant an "option to purchase" pursuant to Section 42(i)(7) of the Code as opposed to a "right of first refusal" without adversely affecting the status of such owner as owner of its project for federal income tax purposes, and (ii) Owner provides a tax opinion reasonably satisfactory to the Investor Member which concludes that a third party offer is not required to trigger a "right of first refusal" under Section 42(i)(7) of the Code, then the parties shall agree that the Owner shall grant Grantee an option to purchase the Project at the Statutory Purchase Price.

3.2.4 Notwithstanding anything to the contrary set forth in this Article III, the parties agree that if the Code allows or the Internal Revenue Service hereafter issues authority to permit the owner of a low-income housing tax credit project to grant a "right of first refusal to purchase membership interests" pursuant to Section 42(i)(7) of the Code as opposed to a "right of first refusal to purchase the property" without adversely affecting the status of such owner as owner of its project for federal income tax purposes, the Grantee may, at its election, in lieu of a direct acquisition of the Project pursuant to the Right of First Refusal, acquire the membership interests (but not less than all of such interests) of the Members in the Owner for a purchase price to each of them equal to the amount which would be distributable to each such Member of the Owner pursuant to the capital proceeds waterfall following any sale of the Project under the Right of First Refusal at the RoFR Purchase Price.

ARTICLE IV
PURCHASE PRICE

4.1 Option Purchase Price. Subject to Section 4.1.3 below, with respect to the Option, the aggregate price to be paid by the Grantee or its designee for the Project or the Investor Member's Interest, as applicable (the "**Option Purchase Price**"), shall be equal to the Fair Market Value (as such term is defined below) of the Project or the Investor Member's Interest, as applicable, taking into account all applicable restrictions on rents and income of the residents as set forth in any Project Documents and will assume the Company continues as a going concern. Notwithstanding the foregoing: (a) the Option Purchase Price, with respect to the purchase of the Project, shall instead be the Statutory Purchase Price if it is less and the Code so allows and the Investor Member receives a tax opinion reasonably satisfactory to the Investor Member that concludes that the exercise of the Option at the Statutory Purchase Price will not have any adverse tax impacts on the Investor Member, the Project (as defined in the Operating Agreement), the

Credits (as defined in the Operating Agreement), or the Owner; (b) any unpaid fees owed to Grantee or its affiliates shall be paid before the transfer; and (c) any unreimbursed Credit Reduction Payment shall be paid by the Managing Member before the transfer. Subject to any required lender or governmental consent, the Grantee may use the Project reserves to fund the Option Purchase Price in the event the Option is exercised in connection with the purchase of the Investor Member's Interest only.

4.1.1 "Fair Market Value" shall be determined in the following manner. Within fifteen (15) business days of the Grantee's notice of its intent to exercise the Option, the Grantee and the Investor Member shall select a mutually acceptable independent appraiser. Such appraiser shall be an MAI appraiser with at least five (5) years of relevant experience.

4.1.2 In the event that the parties are unable to agree upon such appraiser during such time period, the Grantee and the Investor Member each shall select an independent appraiser within the next succeeding five (5) business days. If either party fails to select an independent appraiser within such time period, the determination of the other independent appraiser shall control. If the difference between the fair market value set forth in the two appraisals is not more than ten percent (10%) of the fair market value set forth in the lower of the two appraisals, the Fair Market Value shall be the average of the two appraisals. If the difference between the fair market value set forth in the two appraisals is greater than ten percent (10%) of the fair market value set forth in the lower of the two appraisals, then the two appraisers shall jointly select a third independent appraiser whose determination of Fair Market Value shall be deemed to be binding on all parties as long as the third determination is between the other two determinations. If the third determination is either lower or higher than both of the other two appraisers, then the average of all three appraisals shall be the Fair Market Value. If such appraisers cannot agree on the selection of a third appraiser, the appraiser shall be selected by the President of the State X Chapter of the American Arbitration Association upon application by either the Investor Member or the Grantee. The Owner and the Grantee shall each pay one-half of the fees and expenses of any mutually acceptable appraiser and any third appraiser selected pursuant to this Section, but otherwise will bear the expenses of its own appraiser.

4.1.3 Notwithstanding anything to the contrary contained in this Article IV, the Option Purchase Price with respect to the Investor Member's Interest shall be equal to such amount that would be distributable to 'the Investor Member pursuant to the capital proceeds waterfall following the hypothetical sale of the Project at Fair Market Value under Section 4.1 above.

4.2 Purchase Price Under Right of First Refusal.

4.2.1 To the extent the Grantee's exercise of the Right of First Refusal qualifies as a sale under Section 42(i)(7) of the Internal Revenue Code, the aggregate price to be paid by the Grantee for the Project, the Investor Member's Interest, or, if permitted by Section 42(i)(7), the entire interest of any one or more members of Owner, shall be equal to the Statutory Purchase Price, plus repayment of the Includible Loan (as such term is defined below), and payment of customary transaction costs, but less any unpaid fees owed to the Grantee or its affiliates by Owner (the "**RoFR Purchase Price**"). Any unreimbursed Credit Reduction Payment shall be paid to the Investor Member by the Managing Member before the transfer. Subject to any required lender or

governmental consent, the Grantee may use the Project reserves to fund the RoFR Purchase Price in in connection with the purchase of the Investor Member's Interest only.

4.2.2 The Includible Loan is the aggregate amount of any loans owed to the Managing Member, Investor Member or any affiliate of either at the time of the exercise of the Right of First Refusal; provided that, with respect to a Voluntary Loan owed to the Managing Member or an affiliate, either (a) the Grantee or its affiliate has consented in writing to such loan(s) being treated as an Includible Loan, or (b) at the time the Voluntary Loan was made, (i) the Managing Member is not in default of any obligation under the Project Documents (beyond any applicable notice and cure period); (ii) the Owner provided the Grantee with written notice of such Voluntary Loan (which notice shall be given thirty (30) days' in advance of the making of the Voluntary Loan unless a shorter time is required for emergency circumstances), such notice to include appropriate justification for the Voluntary Loan; (iii) the event(s) causing the need for the Voluntary Loan was not due to the negligence, omission or willful misconduct of the Managing Member; (iv) such Voluntary Loan is necessary because Project reserves that are permitted to be used for such purpose are inadequate to pay (A) for the Project to initially qualify, and to continue to qualify, for Tax Credits, including maintaining compliance with all applicable requirements set forth in the Regulatory Agreement, (B) to correct any material deficiencies noted in the REAC inspection report of the Project or otherwise to maintain the Project in a satisfactory manner, or (C) to prevent any material violation or default by the Project or the Owner under the Project Documents; and (v) the Grantee or its affiliate, within thirty (30) days of the receipt of the notice by the Owner, fails to object in writing, with specificity, to the treatment of such Voluntary Loan as an Includible Loan pursuant to the foregoing criteria. Should the Grantee or its designee object as aforesaid, the parties will seek in good faith to resolve their differences or otherwise proceed in accordance with Article IX, but the Voluntary Loan will not be treated as an Includible Loan absent agreement or judicial resolution. To the extent such Voluntary Loan is made, the member making the Voluntary Loan shall notify the Grantee in writing, and shall provide the Grantee with copies of all loan documentation setting forth the loan amount and applicable interest rate, if any, and other material reasonably requested by the Grantee within ten (10) days of the execution and delivery of such loan.

ARTICLE V
COMPLETION OF SALE UNDER OPTION

5.1 The sale of the Project shall close no later than one hundred eighty (180) days after the Owner's receipt of the Grantee's written notice of exercise of the Option, at which time the purchase price shall be payable as set forth in Section 4.1. At or before the closing, the Owner shall obtain the consent to the sale from HUD, the State Agency, and from the holders of any mortgages or deeds of trust on the Project, and any other consents required under the Project Documents, if required.

5.2 The Owner shall convey the Project to the Grantee in an "as is" condition without representation or warranty.

ARTICLE VI
NOTICES

Any notice or other communication required or permitted to be given under this Agreement shall be in writing and shall be personally delivered, including but not limited to overnight delivery, or deposited in the U.S. mail, certified, return receipt requested, first class and postage prepaid, addressed to each party at the following addresses or such other address as may be designated by a notice pursuant to this Article VI:

If to the Company or the Managing Member:

with copies to:

If to the Investor Member:

and

If to the Grantee:

With a copy to:

And to:

Any notice provided in accordance with this Article VII shall be deemed to have been given on the delivery date or the date that delivery is refused by the addressee, as shown on the return receipt.

ARTICLE VII
ATTORNEY FEES

In the event of any action, arbitration, or proceeding at law or in equity to enforce any provision of this Agreement or to protect or establish any right or remedy of any party hereunder, the unsuccessful party to the litigation shall pay to the prevailing party all costs and expenses,

including reasonable attorneys' fees incurred therein by the prevailing party, and if the prevailing party recovers judgment in any action, proceeding, or arbitration, the costs, expenses, and attorney fees shall be included in and as a part of the judgment.

ARTICLE VIII
ARBITRATION

Any party hereto that becomes involved in any controversy relating to this Agreement may require that all disputes, claims, counterclaims, and defenses ("**Claims**") relating in any way to this Agreement or any transaction of which this Agreement is a part (the "**Transaction**") be settled by binding arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association and Title 9 of the U.S. Code; provided that such arbitration need not be conducted under the jurisdiction of the American Arbitration Association. All Claims will be subject to the statutes of limitations applicable if they were litigated.

If arbitration occurs, one neutral arbitrator will decide all issues unless any party's claim is $100,000 or more, in which case three neutral arbitrators will decide all issues. In the event the parties cannot mutually agree upon an arbitrator or arbitrators, then the rules for selecting an arbitrator or arbitration service under the Commercial Arbitration Rules of the American Arbitration Association and Title 9 of the U.S. Code shall apply. All arbitrators will be active State X State Bar members in good standing. All arbitration hearings will be held in State X. In addition to all other powers, the arbitrator(s) shall have the exclusive right to determine all issues of arbitrability. Judgment on any arbitration award may be entered in any court with jurisdiction.

If any party institutes any judicial proceeding relating to the Transaction, such action shall not be a waiver of the right to submit any Claim to arbitration. In addition, all parties have the right before, during, and after any arbitration to exercise any number of the following remedies, in any order or concurrently: (i) setoff, (ii) self-help repossession, (iii) judicial or nonjudicial foreclosure against real or personal property collateral, or (iv) provisional remedies, including injunction, appointment of receiver, attachment, claim and delivery, and replevin.

ARTICLE IX
MISCELLANEOUS

(a) The rights and obligations of the Owner and the Grantee under this Agreement shall inure to the benefit of, and bind, their respective successors and assigns.

(b) The captions used herein are for convenience of reference only and are not part of this Agreement and do not in any way limit or amplify the terms and provisions hereof.

(c) Time is of the essence of each and all of the agreements, covenants, and conditions of this Agreement.

(d) This Agreement shall be interpreted in accordance with and governed by the laws of the State of State X.

(e) This Agreement constitutes the entire agreement between the Owner and the Grantee with respect to the subject matter hereof and supersedes all prior offers and negotiations,

oral and written. This Agreement may not be amended or modified in any respect whatsoever except by an instrument in writing signed by the parties.

(f) This Agreement shall be binding upon and inure to the benefit of the parties hereto, and their heirs, executors, personal representatives, successors, and assigns. No party to this Agreement may assign the rights under this Agreement without the consent of each other party hereto; provided, however, that Grantee may assign its rights under this Agreement to an Affiliate that qualifies as an Eligible Purchaser without the consent of the other parties.

(g) Each provision of this Agreement shall be considered severable, and if for any reason any provision that is not essential to the effectuation of the basic purposes of the Agreement is determined to be invalid and contrary to any existing or future law, such invalidity shall not impair the operation of or affect those provisions of this Agreement that are valid.

(h) No party hereto shall be deemed to have waived any rights hereunder unless such waiver shall be in writing and signed by such party. The waiver by any party of any breach of this Agreement shall not operate or be construed to be a waiver of any subsequent breach.

(i) This Agreement and any amendments hereto may be executed in several counterparts, each of which shall be deemed to be an original copy, and all of which together shall constitute one agreement bind on all parties, hereto, notwithstanding that all the parties shall not have signed the same counterpart.

(j) The parties hereto acknowledge that Investor Member shall be deemed a third party beneficiary to this Agreement.

[Remainder of page intentionally left blank]

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

EXHIBIT A
LEGAL DESCRIPTION OF THE PROJECT