

# **Introduction to New Markets Tax Credit Program**

# HISTORY AND OBJECTIVES OF NMTC PROGRAM

- Enacted on December 21, 2000 as part of the Community Renewal Tax Relief Act of 2000 to revitalize low-income communities.
- New Markets Tax Credits (NMTC) are federal, dollar-for-dollar tax credits to assist in the funding of neighborhood changing/job creating commercial real estate projects and businesses located in low-income census tracts.
- Low-income communities have trouble attracting investment, leading to dormant or vacant buildings and businesses, inadequate access to healthcare and education, lower property values, leading to low-income communities becoming distressed communities.

## OVERALL BENEFITS

- Between 2002 and 2018, the federal government has provided NMTC allocations to more than 350 Community Development Entities (CDEs), totaling \$54 billion in tax credit authority.
- Since 2003, the NMTC Program has created or retained an estimated 275,000 jobs. It has also supported the construction of 37 million square feet of manufacturing space, 80 million square feet of office space, and 61 million square feet of retail space.
- For every \$1 invested by the federal government, it is estimated that \$8 of private investment is generated, making it one of the most efficient uses of tax dollars of any government program.
- According to a GAO study (2007), 88% of NMTC investors would not have considered investing in a project without the NMTC

## CURRENT DEVELOPMENTS

- Round 14 applications were awarded February 13, 2018.
- There were 230 applications requesting \$16.2 billion. Applicants were headquartered in 29 states, the District of Columbia and Guam.
- Allocation awards ranged from \$15 million to \$75 million with the average being \$47.95 million for 73 awardees.

## EXAMPLE PROJECTS

Charter schools, health care facilities, community centers, child care providers, supermarkets, restaurants, museums, hotels, performing arts centers, pharmacies, convenience stores, manufacturers, processors, distributors, trucking companies, printing companies, waste management, renewable energy projects, sporting goods, office buildings, shopping centers, substance abuse treatment facilities, recording studios, movie studios, parking garages, etc.

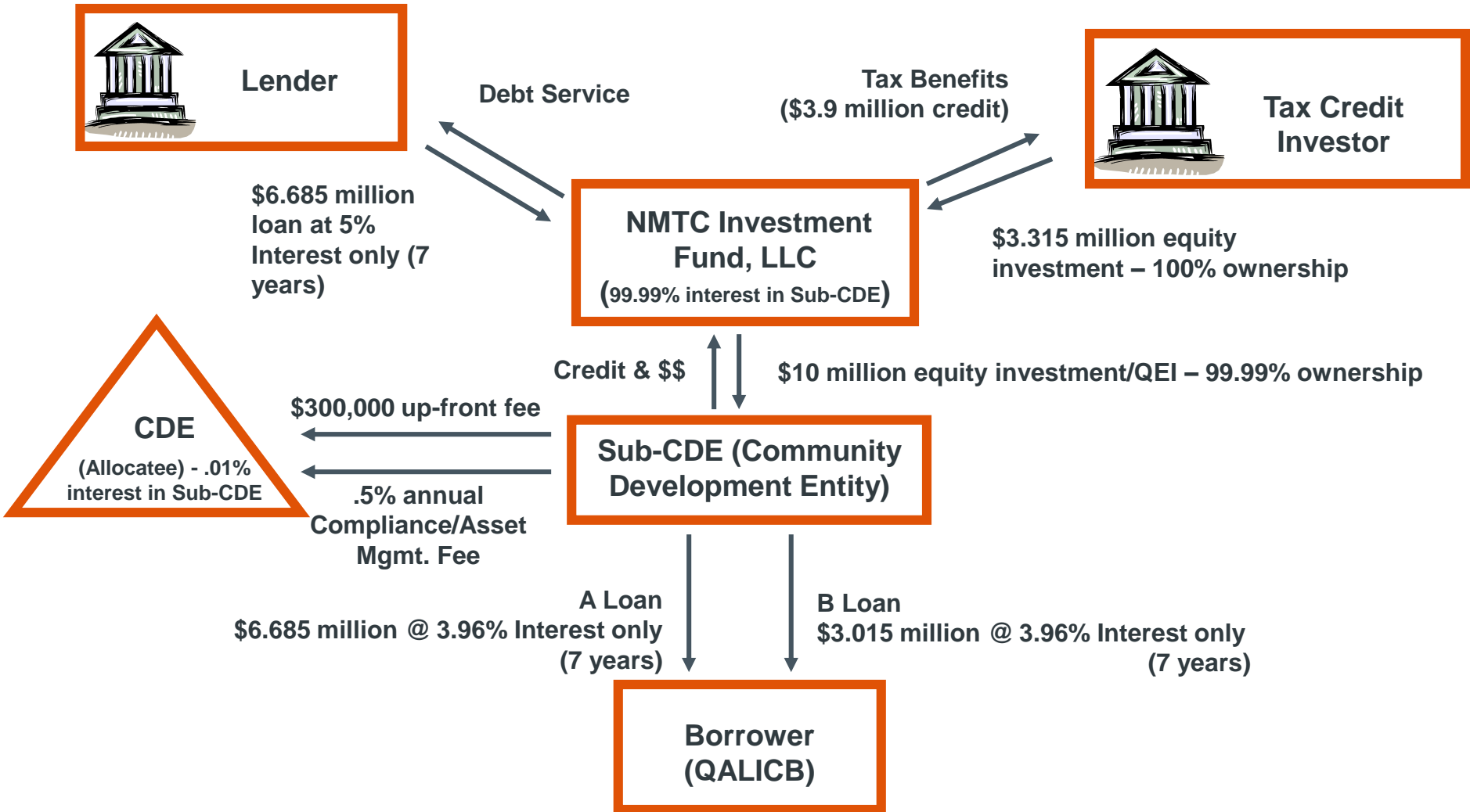
# PROCESS OVERVIEW

- Step 1: Entities apply to the CDFI Fund for CDE certification (*rolling basis*).
- Step 2: CDEs apply competitively to the CDFI Fund for a NMTC allocation.
- Step 3: The CDFI Fund allocates NMTCs to CDEs that are selected.
- Step 4: CDEs use allocations to offer NMTCs to investors for cash investments called a Qualified Equity Investment (“QEI”).
- Step 5: CDEs use proceeds to make Qualified Low-Income Community Investments (“QLICs”) in QALICB.

# PLAYERS IN A NMTC DEAL

- Community Development Financial Institution Fund (CDFI Fund)
- Internal Revenue Service (IRS)
- Community Development Entity (CDE)
- Investor
- Leveraged Lender
- Qualified Active Low-Income Community Business (QALICB)

# Leveraged NMTC Structure





# TIMING AND CALCULATION OF THE CREDIT

- NMTCs are offered to investors for Qualified Equity Investments (QEIs) in the CDE.
- Credit equals 39% of amount of QEIs.
- Credit claimed over 7 Years:
  - *5% in each of the first three years, and*
  - *6% for each of the final four years.*
- Full year of credit claimed regardless of when (during the year) the QEI is made.

## EXAMPLE

- CDE receives a \$10 million allocation of NMTCs. This is only allocation authority!
- \$10 million of allocation x 39% credit = \$3.9 million of federal tax credits to be received by the investor.

If a single investor made the \$10 million investment into the CDE today then the investor will receive tax credits over time equal to...

Year 1	@ 5%	= \$0.5 million
Year 2	@ 5%	= \$0.5 million
Year 3	@ 5%	= \$0.5 million
Year 4	@ 6%	= \$0.6 million
Year 5	@ 6%	= \$0.6 million
Year 6	@ 6%	= \$0.6 million
Year 7	@ 6%	= \$0.6 million
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7 Years	@ 39%	= \$3.9 million

# Qualified Active Low-Income Community Business (QALICB) benefits

- Access to non-conventional, non-conforming financing
  - Lower than market interest rates
  - Subordinated debt
  - Lower or no origination fees
  - Higher LTV
  - Lower DSCR
  - Fixed rate debt
  - Typically, the 7 years with little to no amortization (interest only)
- Gap financing – But For

# THE QLIC MUST BE MADE IN A QUALIFIED AREA

- There are generally two hurdles
- Hurdle #1—QALICB located in a LIC or serve Targeted Population
- LICs are census tracts with...
  - *Poverty of at least 20%, or*
  - *Median family income at or below 80% of the area median family income,*

# THE QLIC IS ALMOST ALWAYS MADE IN A HIGHLY DISTRESSED COMMUNITY

- Hurdle #2—QALICB in a “highly distressed” community
- Highly distressed LICs are:
  - *Poverty of at least 30% of the national average, or*
  - *Median family income at or below 60% of the area median family income, or*
  - *Unemployment at least 1½ times the national average, or*
  - *Non-Metro, or*
  - *Targeted Populations at 60% threshold*
  - *Other options as defined in section 3.2(h) of the Allocation Agreement*
    - Brownfield site
    - Hope VI Redevelopment Plan
    - Native American or Alaskan American area
    - Federally designated medically underserved area (if investment supports health services)
    - Food Desert
    - State enterprise zone programs, or other similar state/local programs targeted towards particularly economically distressed communities

# WHAT IS A QUALIFIED ACTIVE LOW-INCOME COMMUNITY BUSINESS?

- 50% or more of the total gross income is from active conduct of a qualified business in a Low-Income Community; and
- 40% or more of the use of the tangible property is located in a Low-Income Community; and
- 40% or more of the services provided by the business' employees are performed in a Low-Income Community; and

## Exceptions:

1. **The gross income test is met if either the tangible property or the services test is met at 50% or higher.**
2. **A business venture with no employees (e.g., real estate partnership) meets the services and gross income tests if it meets the tangible property test at 85% or higher.**
3. **“Active conduct” includes start-ups (for profit and not-for-profits) if the entity is reasonably expected to generate revenue (receive donations) within three years of the date of the QLICI.**

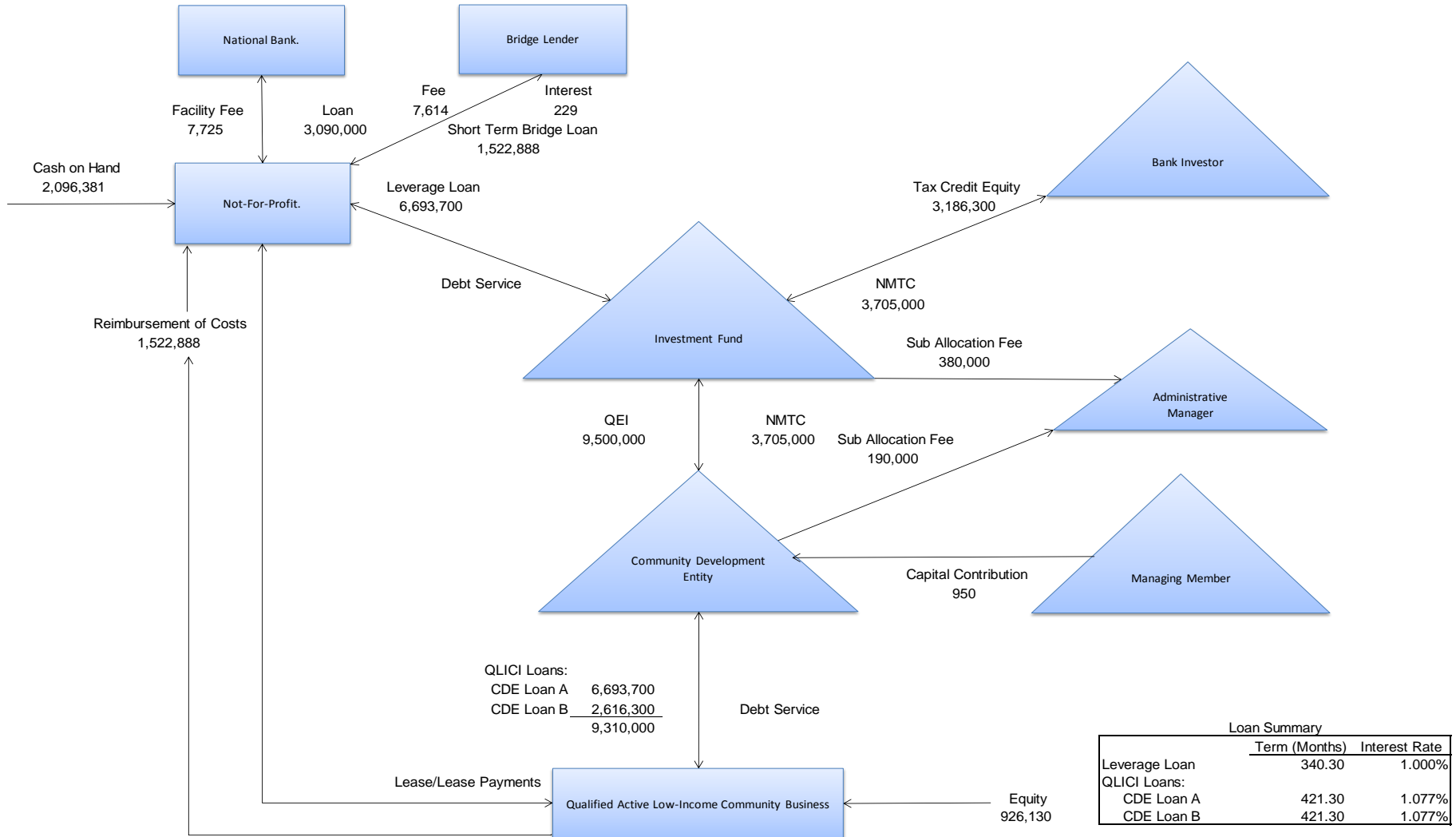
# WHAT IS A QUALIFIED ACTIVE LOW-INCOME COMMUNITY BUSINESS (CONTINUED)

- Less than 5% of the average aggregate unadjusted bases of the property is attributed to;
  - *Collectibles (e.g., art and antiques, other than for sale in the ordinary course of business), and*
  - *Non-qualified financial property (e.g., debt instruments with a term in excess of 18 months OR unreasonable levels of working capital in cash and cash equivalents [QLICI made to support construction activity within twelve months of investment is considered reasonable working capital]).*
- Ineligible business activity;
  - *Operation of residential rental property which derive 80% or more gross rental income from dwelling units*
  - *Rental of real property where no substantial improvements are made*
  - *Rental of real property where any tenant is not a qualified business*
  - *Trade or business consisting predominantly of development or holding of intangibles for sale or license*
  - *Farming*
  - *Operation of golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack, gambling facility, or liquor store (referred to as “sin businesses”).*

# Sample NMTC Deal

Sample

## NEW MARKETS DIAGRAM - SUMMARY





# Sample NMTC/HTC Twin Deal

Sample

## NEW MARKETS DIAGRAM - SUMMARY

