New Markets Tax Credit Program 101
The Basics

Making the New Markets Tax Credit Work in Native Communities

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COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND
www.cdfifund.gov

New Markets Tax Credit – 101

- Introduction to NMTC
- Program History & Overview
- NMTC Key terms
- CDE Certification
- How can NMTC work for your organization

NMTC Authority

- The New Markets Tax Credit was authorized under the Community Renewal and Tax Relief Act of 2000, and has been subject to reauthorization since 2006.
- Most recently, the Protecting Americans from Tax Hikes (PATCH) Act of 2015 extends the program through 2019, providing tax credit authority at $3.5 billion per year.
- Earlier this month, we opened the CY2018 Round.

What is the New Markets Tax Credit?

- NMTCs provide a **credit** against Federal income taxes for **investors** that make ***Qualified Equity Investments (QEIs)*** in certified financial intermediaries called **Community Development Entities (CDEs).**

- **CDEs,** in turn, use the proceeds of these QEIs to make **Qualified Low-Income Community Investments (QLICIs),** such as business loans or equity investments, in **Low-Income Communities** into **Qualified Active Low Income Businesses (QALICBs).**

Tax Credit Amount

- The New Markets Tax Credit is taken over a 7-year period.
- The credit rate is:
  - 5% of the original investment amount in each of the first three years; and
  - 6% of the original investment amount in each of the final four years.
- Total credit equals 39% of the original amount invested in the CDE.

Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Total
5%	5%	5%	6%	6%	6%	6%	39%

Example

- The CDFI Fund awards a tax credit allocation of $1 million to a CDE.
- The CDE offers the tax credit to a single investor in exchange for a $1 million equity investment.
  - Generates a $50,000 credit annually for the first three years;
  - Generates a $60,000 credit annually for the final four years.
- Total credit value over 7 years is $390,000.

Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Total
$50,000	$50,000	$50,000	$60,000	$60,000	$60,000	$60,000	$390,000

Key Terms

- Community Development Entity **(CDE)**
- Substantially All **(Sub-All)**
- Qualified Equity Investments **(QEI)**
- Qualified Low-Income Community Investments (QLICI)
  - Qualified Active Low-Income Community Businesses **(QALICB)**
  - Low-Income Community **(LIC)**
  - Financial Counseling and Other Services **(FCOS)**
  - Subsidiary Community Development Entity **(Sub-CDE)**

How does NMTC work?

- The NMTC Program encourages private-sector investment in Low Income Communities by providing a credit against Federal income taxes to investors that make Qualified Equity Investments (QEIs) into Community Development Entities (CDEs).
- CDEs must use substantially all of the QEI proceeds (cash) to make Qualified Low Income Community investments (QLICI).
  - Provides access to capital in Low-Income Communities
  - Federal Government foregoes tax revenue to channel investment capital to achieve program goals.

What is a CDE?

- A Community Development Entity (CDE) is a domestic corporation or partnership that is an intermediary vehicle for the provision of loans, investments, or financial counseling in Low-Income Communities.
- To qualify as a CDE, a domestic corporation or partnership must apply for and receive certification from the CDFI Fund.

CDE Certification

- Legal Entity at time of Application
- Primary Mission of serving LICs
- Must be accountable to the LIC it serves.
  - Governing Board
  - Advisory Board
- Service Area - determine the service area it will serve
  - National, Multi-State, Statewide, Local

Qualified Equity Investment

- A CDE that receives an Allocation raises capital from an Investor.
- In order to claim the NMTCs, an investor must make an equity investment into a CDE – provide *cash* for either stock in a corporation or a capital interest in a partnership – in exchange for the credits.
- The equity investment must be designated by the CDE as a Qualified Equity Investment (QEI), using the CDFI Fund's electronic tracking system.
- The QEI must remain invested in the CDE during the 7-year tax credit period from the date the investment was initially made.

Use of QEI Proceeds

- **"Substantially all"** of QEI proceeds must be invested in Qualified Low-Income Community Investments (QLICIs) within 12 months:
  - Years 1 – 6: Substantially All = 85% of amount paid by investor at original issue. Generally, returns of equity, capital or principal must be reinvested within 12 months.
  - Year 7: Substantially All = 75%. Reinvestment is not required in the final year of the 7-year credit period.

What is a Low Income Community?

- LICs are census tracts
  - with at least 20% poverty rate; or
  - where the median family income does not exceed 80% of the area median family income; or
  - where the median family income does not exceed 85% of the area median family income, provided the census tract is located in a high migration rural county.
- Targeted Population- Businesses not located in LICs but that otherwise serve Targeted Populations may also qualify for NMTC-enhanced loans/investment. Targeted Populations include:
  - Low-Income Persons (e.g. family income no greater than 80% of the applicable area median family income), to the extent the project is located in a census tract with a median family income at or below 120% of the median family income.
- Refer to IRS and CDFI Fund guidance for additional details.

Qualified Low Income Community Investment

QLICIs include:

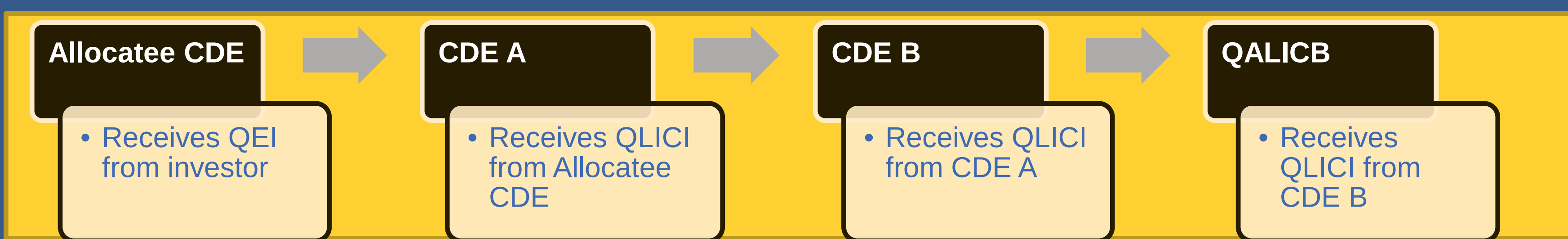
- Any capital or equity investment in, or loan to, a "Qualified Active Low-Income Community Business" (QALICB).
- Purchase of a loan from another CDE if the loan is a QLICI.
- Any equity investment in, or loan to, a CDE.
- "Financial Counseling and Other Services" (FCOS) to businesses located in, or residents of, Low-Income Communities (LICs).

Qualified Active Low-Income Community Business (QALICB)

- A QALICB must meet these requirements:
  - At least 50% of the total **gross income** is from the active conduct of a qualified business in Low-Income Communities (LICs); and
  - At least 40% of the **use of tangible property** of the business is within LICs; and
  - At least 40% of the **services preformed** by the business' employees are performed in LICs; and
  - **Less than 5%** of the average of the aggregate unadjusted basis of the property is attributable to **collectibles** (e.g. art and antiques), other than those held for sale in the ordinary course of business; and
  - **Less than 5%** of the average of the aggregate unadjusted basis of the property is attributable to **non-qualified financial property** (e.g. debt instruments with a term in excess of 18 months).

Investing in Other CDEs

- Investment may be made through multiple layers of CDEs (e.g. up to 4 CDEs).
- The last CDE recipient needs to demonstrate that it used those dollars to:
  - Make loans to, or investments in QALICBs; and/or
  - Provide FCOS to businesses or residents of LICs.
- All time limits must be met as if the CDE with the allocations directly made the QLICI



Ineligible Activities

- Residential rental property
  - Buildings or structures that derive 80% or more of their gross rental income from renting dwelling units.
- Certain types of businesses:

• Golf courses • Race tracks • Gambling facilities • Certain farming businesses • Country clubs	• Massage Parlors • Hot tub facilities • Suntan facilities • Stores where the principal business is the sale of alcoholic beverages for consumption off premises

Refer to IRS regulations for additional details.

Recapture

- NMTCs may be **recaptured** from investors during the 7 **year credit period** under certain conditions.
- Events triggering recapture include:
- The QEI fails the **“substantially-all”** requirement.
  - Failure to **invest 85% of original QEI**; or
  - Failure to meet **“Qualified Active Low-Income Business” (QALICB)** requirements; or
  - Failure to meet **one-year investment/ reinvestment requirement**
- The CDE **redeems the investment** before the 7 year credit period has ended.
- The CDE **ceases to qualify** as a CDE.

Summary Graphic

CDEs must make QLICIs within **12 months** of receipt of Investor QEIs

Community Development Entity
(For-profit* only)

- Investing in or Lending to QALICBs
- Purchasing Loans from CDEs
- Financial Counseling
- Investing in or Lending to CDEs

CDE must offer credits to investors within **5 years**

Private Investors

QEI must stay invested in CDE for **7 years**

CDFI Fund & IRS Roles

The CDFI Fund

- Co-administers the NMTC Program with the IRS
- CDFI Fund's mission is to expand economic opportunity for underserved people and communities by supporting the growth and capacity of a national network of community development lenders, investors, and financial service providers.
- Certifies Community Development Entities
- Manages the competitive Allocation Award process

Internal Revenue Service

- NMTC Investments must comply with regulations outlined in Section 45D of the Internal Revenue Code.

Information on Prior NMTC Allocations

- Since the first round CY2002, the CDFI Fund has awarded $54 billion in Allocation Authority, including:
  - $7 billion for the Combined CY2015-16 round
  - $3.5 billion for the CY2017 Round

- $41.9 billion in Loans and equity investments (2003-2015)

NMTC investments in Native Communities (2003-2015)

- $991 MM** invested in Native Communities
- 94 projects
- Examples:
  - Seafood Processing Plant, Platinum, AK
  - Administrative Building, Chinle, AZ
  - Water & Waste Water Treatment System , Laguna, NM
  - Health Center Kailua Kona, HI
  - Hotel, Choctaw, MS
  - Telecomm, Standing, ND
  - Aircraft Engine Parts Manufacturing, Bristown, OK
  - Tribal Headquarters, Nespelem, WA
  - Dental Clinic, Odanah, WI

NMTC – a community development tool

- It's a flexible took that can be used for a variety of different projects from day care centers to manufacturing/industrial facilities.
- Projects must be of a certain size in order to make NMTC feasible.
- NMTC is intended to serve as gap financing
  - Need other sources of financing as part of the capital stack
- IRS Regulations require that QLICIs be loans (true debt) or equity investments. QLICIs are not grants.

Little Big Horn College Health and Wellness Center – Crow Agency, MT

- NMTC Closing – 2011, Date Completed - 2012
- Higher education institution of the Crow Tribe of Indians.
- Provides education programs and exercise facilities.
- Total project cost: $10.3 million
- NMTC Equity: $2.4 million