COMMUNITY DEVELOPMENT
FINANCIAL INSTITUTIONS FUND

www.cdfifund.gov

Introduction to the New Markets Tax Credit Program

PREPARED ON
June 13, 2013

Presentation Roadmap

- Overview of CDFI Fund Programs & Initiatives
- NMTC Program History and Overview
- NMTC Program Key Terms
- CDE Certification
- How can NMTCs work for your organization?

CDFI Fund Overview

- Created in 1994
- **Mission:** To increase economic opportunity and promote community development investments for underserved populations and in distressed communities in the United States.
- **Vision:** To economically empower America's underserved and distressed communities.

CDFI Fund Overview

- The CDFI Fund achieves its mission by directly investing in and supporting Community Development Financial Institutions (CDFIs), Community Development Entities (CDEs), and other financial institutions through the following programs and initiatives:
  - New Markets Tax Credit (NMTC) Program
  - Bank Enterprise Award (BEA) Program
  - CDFI Program (FA & TA)
  - Native Initiatives (NACA)
  - CDFI Bond Guarantee Program

NMTC Program History

- The NMTC Program was authorized under the Community Renewal and Tax Relief Act of 2000, and has been subject to reauthorization since 2006. Most recently, the American Taxpayer Relief Act of 2012 extended the program through 2013.
- In the 10 application rounds to date, the CDFI Fund has made 749 allocation awards totaling $36.5 million in tax credit authority.
  - Includes $3 billion in Recovery Act awards and $1 billion for recovery and redevelopment from Hurricane Katrina.

NMTC Program Overview

- The NMTC Program is jointly administered by the CDFI Fund and the Internal Revenue Service (IRS).
- Investments made through the NMTC Program must comply with regulations outlined in Section 45D of the Internal Revenue Code.

NMTC Program Overview

- 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)."
  - **NMTCs are awarded to CDEs, not to individuals or businesses.**
- CDEs, in turn, use the proceeds of these QEIs to make Qualified Low-Income Community Investments (QLICIs), such as business loans, in Low-Income Communities.

Non-Metropolitan Counties

- The CDFI Fund awards the proportional allocation of QEIs to Non-Metropolitan Counties.
  - The proportion of awardees that are Rural CDEs is equal to the proportion of applicants in the Phase 2 review pool that are rural CDEs.
  - A goal of 20 percent of QLICIs made using QEI proceeds to be invested in Non-Metropolitan Counties.
- To be a Rural CDE, an organization must:
  - Have a track record of at least 3 years of direct financing experience;
  - Have dedicated at least 50 percent of its direct financing activities in the last 5 years to Non-Metropolitan Counties; and
  - Commit that at least 50 percent of QLICIs will be directed to Non-Metropolitan Counties.

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%

Tax Credit Amount - 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

Tax Credit 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.
  - The CDE ceases to qualify as a CDE.

**It is not an event of recapture if a CDE files for bankruptcy. An investor may continue to claim NMTCs.*

NMTC Program Key Terms

- Community Development Entity (CDE)
- Qualified Equity Investment (QEI)
- Qualified Low-Income Community Investment (QLICI)
- Qualified Active Low-Income Community Business (QALICB)
- Low-Income Community (LIC)
- Financial Counseling and Other Services (FCOS)

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.

Only CDEs Can Apply for an NMTC Allocation

- CDEs or organizations with a pending CDE certification Application are eligible to apply for an NMTC allocation.
- To be awarded an allocation of NMTCs, CDEs must apply through a competitive application process administered by the CDFI Fund.
- Only a certified CDE that has been awarded an allocation of NMTCs can offer NMTCs for sale to investors.
- If awarded an NMTC allocation, CDEs must offer NMTCs to investors within **5 years** of receiving an allocation.

Qualified Equity Investment (QEI)

- In order to claim the NMTCs, an investor must make an equity investment into a CDE – either stock in a corporation or a capital interest in a partnership – in exchange for the credits.
- The equity investment must be acquired by the investor at its original issue, solely in exchange for cash.
- The equity investment must be designated by the CDE as a Qualified Equity Investment (QEI).
- 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.

Qualified Low-Income Community Investments (QLCIs)

QLICIs include:

- Any capital or equity investment in, or loan to, a "Qualified Activity 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).

Examples of QALICBs

- An operating business located in a Low-Income Community (LIC).
- A business that develops or rehabilitates commercial industrial, retail, and mixed-use real estate projects in an LIC.
- A business that develops or rehabilitates community facilities, such as charter schools or health care centers, in an LIC.
- A business that develops or rehabilitates for-sale housing units located in LICs.

What is a Low-Income Community?

- "Low-Income Communities" (LICs) are census tracts:
  - Where the poverty rate is at least 20%; **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, **or**
  - Where the census tract has a population of less than 2,000 and is contained within a Federally designated Empowerment Zone and is contiguous to at least one other LIC.

Low-Income Communities – Targeted Populations

- Businesses not located in LICs but that otherwise serve Targeted Populations may also qualify as QALICBs.
- 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.

Finding a Low-Income Community

- The CDFI Fund offers tools and guidance on determining whether a business is located in an LIC.
- For more information, visit our website – www.cdfifund.gov/nmtc and look in the section titled "Census Low-Income Community Eligibility Data."

Purchasing Loans from Other CDEs

CDEs may purchase loans, but **not** investments, from other CDEs if:

- The purchased loans were originated by an entity that was a CDE at the time the loan was sold; and
- The loans qualified as QLICIs at either the time the loan was:
  - Originated, or
  - Purchased by the Allocatee CDE.

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 business or residents of LICs.
- All time limits must be met as if the CDE with the allocations directly made the QLICI.

Allocatee CDE → **CDE A** → **CDE B** → **QALICB**

Allocatee CDE	CDE A	CDE B	QALICB
• Receives QEI from investor	• Receives QLICI from Allocatee CDE	• Receives QLICI from CDE A	• Receives QLICI from CDE B

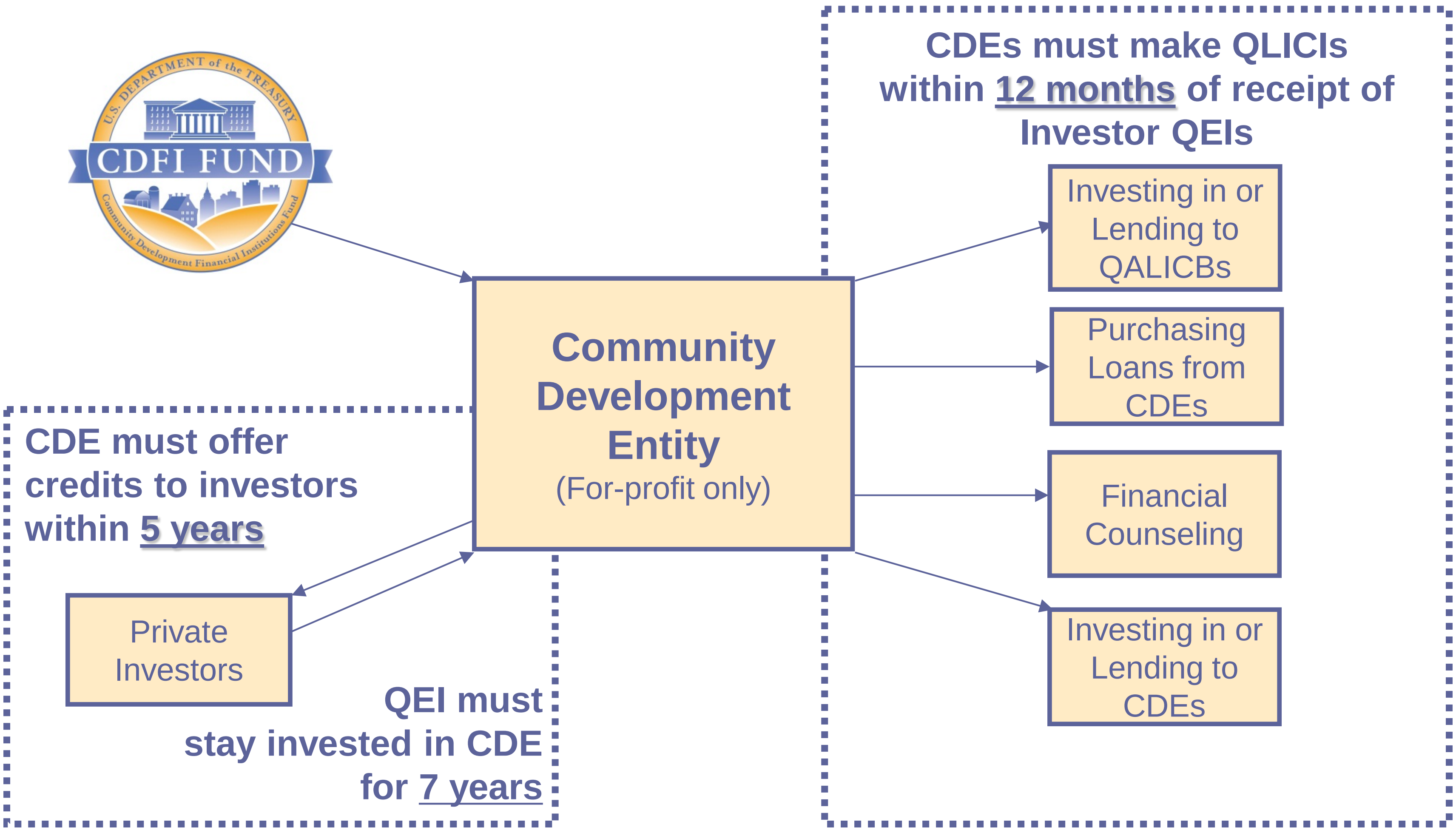
Financial Counseling and Other Services (FCOS)

- FCOS is “advice provided by the CDE relating to the organization or operation of a trade or business.”
- Possible FCOS activities include:
  - Business plan development
  - Assistance with business financials
  - Operating assistance to non-for-profit organizations

Activities Ineligible for NMTC Investment

- 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.

Summary Graphic



CDE Certification

- To receive CDE certification, a domestic corporation or partnership must:
  - Demonstrate a primary mission of serving or providing investment capital for low-income communities or people; **and**
  - Maintain accountability to Low-Income Communities through representation on the organization's Governing Board or Advisory Board.
- Organizations certified as a CDFI by the CDFI Fund or be designated as a Specialized Small Business Investment Company (SSBIC) by the Small Business Administration automatically qualify as CDEs.

CDE Certification

- Generally, CDE certification applications are accepted on a rolling basis.
- However, there are strictly enforced deadlines for an organization to apply for CDE certification if it would like to apply concurrently for an NMTC allocation.
- Refer to the applicable Notice of Allocation Availability for more information on these deadlines.
- More information on CDE certification can be found on the CDFI Fund's website (www.cdfifund.gov/cde).

How can NMTCs work for your organization?

- **If you are a financing entity** (e.g. loan fund, bank), you may want to consider applying for CDE certification.
  - For more information, visit www.cdfifund.gov/cde.
- **If you are a certified CDE**, you can:
  - Apply for an allocation of NMTCs;
  - Receive a loan or investment from another CDE with NMTC allocation authority;
  - Sell loan(s) to another CDE with NMTC allocation authority if those loan(s) are QLICI(s).
  - For more information, visit www.cdfifund.gov/nmtc

How can NMTCs work for your organization?

- **If you are a business** looking for financing, you can contact a CDE directly to inquire about NMTC enhanced financing.
  - For more information, see the "Find CDEs with an NMTC Allocation" section on www.cdfifund.gov/nmtc.

Contact Information

If you have additional questions on the New Markets Tax Credit Program, you can reach the CDFI Fund via one of the following methods:

CDFI Fund's New Market Tax Credit Website	www.cdfifund.gov/nmtc
NMTC Program Help Desk Phone	(202) 653-0421 *Option 3
CDE Certification Help Desk Phone	(202) 653-0423
CDFI Fund's Help Desk Email	cdfihelp@cdfi.treas.gov
IRS Help Desk Email	new.markets.tax.credit@irs.gov