

# Introduction to the New Markets Tax Credit Program

*... a project level overview*

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# Agenda/Goals

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## Goals:

- Understand the basics of how NMTCs can benefit projects in your community
- Understand the process for obtaining NMTC Allocation

## Agenda:

- Program overview
- Allocation rounds
- How the program works
  - Key roles of program participants
  - Eligible borrowers and projects
- Cost and benefits
- How do I start?
- Additional Q&A?

# Program Background

**The NMTC program is a financing tool created to incentivize private capital investments in low-income communities and fill gaps in projects capital budgets**

- Created by Congress as part of the Community Renewal Tax Relief Act of 2000
- Codified in Section 45D of the Internal Revenue Code
- Administered by the Community Development Financial Institutions (CDFI) Fund of the US Treasury Department
- Awards are determined based on a highly competitive application process
- \$3.5 billion annually authorized by Congress, \$57.5 billion authorized to date of which \$52.3 billion has been used to finance community businesses or projects
- 15 awards rounds have been made since inception, 16<sup>th</sup> round announced last week for \$3.5 billion.
- CDFI Fund makes 70-85 awards averaging between \$40 - \$50 million per eligible organization.

# Allocation Rounds

	Year	Award Amount	Amount Finalized	Amt. Remaining
Round 1	2001-02	\$2,485,699,042.00	\$2,485,699,041.8	\$0.13
Round 2	2003-04	\$3,493,786,205.00	\$3,493,786,204.29	\$0.71
Round 3	2005	\$1,964,688,856.00	\$1,964,688,855.60	\$0.00
Round 4	2006	\$4,099,765,000.00	\$4,099,765,000.00	\$0.00
Round 5	2007	\$3,892,249,021.00	\$3,892,249,020.48	\$0.36
Round 6	2008	\$4,964,500,010.00	\$4,964,500,009.34	\$0.36
Round 7	2009	\$4,987,650,000.00	\$4,987,649,999.17	\$0.00
Round 8	2010	\$3,475,000,000.00	\$3,475,000,000.00	\$.83
Round 9	2011	\$3,622,919,753.00	\$3,622,919,753.00	\$0.00
Round 10	2012	\$3,500,000,000.00	\$3,500,000,000.00	\$0.00
Round 11	2013	\$3,501,392,113.00	\$3,494,907,113.00	\$6,485,000.00
Round 12	2014	\$3,512,350,000.00	\$3,501,812,559.00	\$10,537,441.00
Round 13	2015-16	\$6,958,000,000.00	\$6,486,310,092.00	\$471,689,908.00
Round 14	2017	\$3,500,000,000.00	\$2,339,496,149.00	\$1,160,503,851.00
Round 15	2018	\$3,500,000,000.00	\$0.00	\$3,500,000,000.00
Total		\$57,458,000,000.00	\$52,308,783,796.75	\$5,149,216,202.03

# Financing For Projects

**Taxpayers receive a tax credit in their federal tax returns in exchange for investing in Community Development Entities (“CDEs” or a “CDE”) or Community Development Financial Institution (“CDFI”) which then use the capital to make soft loans to projects.**

- It is a national program and Puerto Rico has received NMTC allocation via several CDEs
- Can fill between 15 and 20% gaps on projects capital budgets
- Represents a 39% tax credit to investors
- For projects, it is low cost equity like, soft loan with flexible terms which is left in the project as permanent capital
- Program has a 7-year compliance period

# Other project-level considerations

- Investors do not make a direct investment into project; instead, the CDE typically makes loans to projects
- While it is a form of subsidy, the financing is not a grant, but it is left in the projects or business as permanent capital
- Unlike other tax credit programs, NMTCs are generated by enhancing other projects sources, rather than being based on project expenditures (“uses”).
- Compared to 9% Low Income Housing Tax Credit projects, where the tax credit equity can be as much as 50% of the total development cost, NMTCs are a relatively shallow subsidy
- There is no “standard” deal but highly flexible how you can use the program.
- It is not a direct investment into project by the tax credit Investor; instead, the CDE typically makes loans to projects.

# Participants Roles

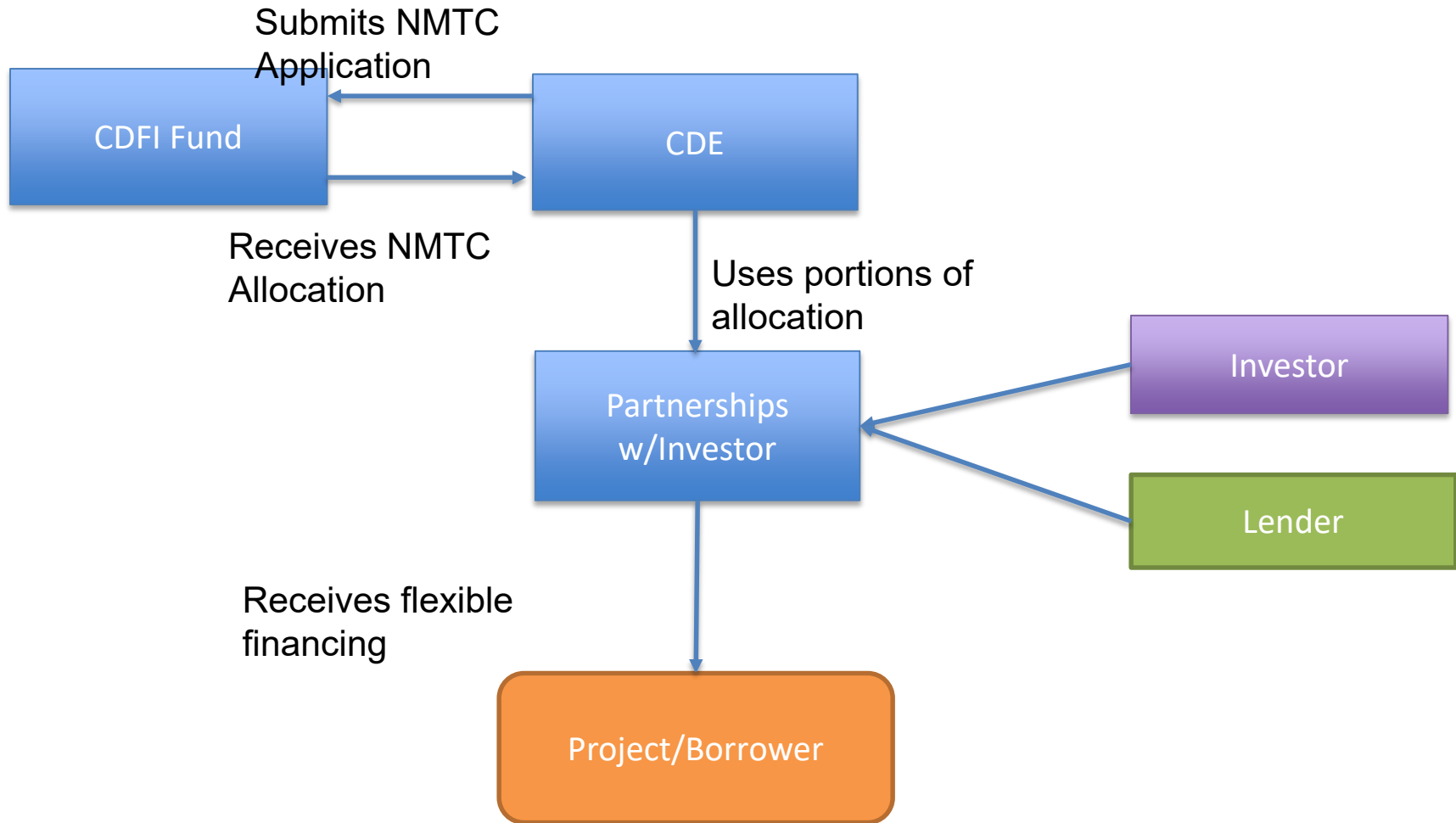
Party	CDFI FUND	CDE	NMTC Investor	Project Borrower	Leverage Lender
Who are they?	<input type="checkbox"/> Department of the Treasury	<input type="checkbox"/> CDFIs <input type="checkbox"/> Banks <input type="checkbox"/> Developers <input type="checkbox"/> Govt. agencies <input type="checkbox"/> Other nonprofits	<input type="checkbox"/> Banks <input type="checkbox"/> Some C Corps	<input type="checkbox"/> Developers <input type="checkbox"/> Non-profits <input type="checkbox"/> Businesses <input type="checkbox"/> Gov't agencies	<input type="checkbox"/> Banks <input type="checkbox"/> CDFIs <input type="checkbox"/> Gov't agencies <input type="checkbox"/> Others
What do they do?	<input type="checkbox"/> Program Administrator <input type="checkbox"/> Provide allocation to CDEs <input type="checkbox"/> Ensure Program Compliance	<input type="checkbox"/> Provide NMTC allocation <input type="checkbox"/> Make loans using capital from investor and lender	<input type="checkbox"/> Make equity investment in CDE in return for tax credits	<input type="checkbox"/> Develop and operate Project <input type="checkbox"/> Operate business or non-profit	<input type="checkbox"/> Make loans through NMTC structure
What are their requirements and expectations	<input type="checkbox"/> Reporting of community benefits and outcomes of CDE investments	<input type="checkbox"/> Select projects that meet their application strategy <input type="checkbox"/> Monitor projects that have been financed <input type="checkbox"/> Reporting to CDFI Fund	<input type="checkbox"/> Financial return through tax credits <input type="checkbox"/> Compliance with NMTC regulations and reporting by CDEs and QALICBs <input type="checkbox"/> Other benefits such as CRA credit or community relations	<input type="checkbox"/> Received low cost flexible loans or equity financing from CDEs. <input type="checkbox"/> Meet financial and program regulations <input type="checkbox"/> Report community outcomes to CDEs	<input type="checkbox"/> Can be market rate or below market/ philanthropic source of funds. <input type="checkbox"/> Receive debt service <input type="checkbox"/> Other benefits such as CRA credit or benefit of multiplier effect

# How the program works

- CDE applies for and receives NMTC “allocation authority” from CDFI Fund – average of between \$40 to \$50 million
- CDE uses portions of the allocation authority for each project it selects to finance, currently averages between \$6 to \$10 million per project
- CDE forms partnerships with investors (to sell the tax credits to investors)
- Lenders make loans to the “partnership” which is combined with the investor’s capital contributions to make investments (soft or equity like loans) in qualified projects
- Qualified projects result in new or rehabbed facilities, job creation and/or other benefits.
- Project borrowers report annually to CDEs on community benefits achieved by the project
- CDE report annually to the CDFI Fund on specific data points including flexible terms and impact



# How the program works



# Qualified Borrowers

- A corporation or partnership (including a nonprofit corporation) engaged in the “active” conduct of a qualified business that meets 5 separate requirements and is not engaged in an excluded business or activity
  - “Active” means the business can reasonably be expected to generate revenues within 3 years after the flexible financing is provided to the project (or for a nonprofit to generate funds to further support its mission)
- Located in a Low-Income Community (“LIC”) – defined by the CDFI Fund database
- Projects located in areas of high distress have a better chance of obtaining allocation from CDEs
- Services must be provided in the LIC
- Tangible assets must be in the LIC

# Excluded businesses and restrictions

## EXCLUDED BUSINESSES

- Liquor store
- Racetrack or other gambling facility
- Massage parlor
- Hot tub facility
- Suntan facility
- Country club
- Golf course

## RESTRICTIONS

- No business which develops or holds intangibles for sale or lease
- No certain farming businesses
- No residential rental property

# Types of Construction

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- New Construction or Substantial Rehab
- Avoid refinancing of existing buildings (can do take-out).
- Can be combined with Historic Tax Credits.
- Cannot be combined with LIHTC (unless a separate legal entity within the development).
- Development of rental housing is excluded but can finance mixed use projects (+ additional requirements).

# Costs and benefits to project

- Benefits are generally equal to NMTC equity minus incremental costs associated with NMTC such as:
  - Fees to CDE or CDEs
  - Fees to attorneys, accountants and/or consultants for the CDE, Investor and QALICB
  - Expenses related to CDE audit and asset management
- Focus on the net benefit to the transaction, typically about 15 – 20% of the “QEI”
- The greater the QEI, the greater per credit net benefit received from the NMTC
- Some “economies of scale” for projects with greater allocation, but it is harder to secure larger amounts of allocation

# Costs and benefits to project

- The extra time, expense and complexity with the NMTC is justified for the subsidy provided
- NMTC process require lengthy timeline from “start to finish”
- Timeframe includes having a deal “ready to go”
- Typically 3 to 6 months once a project is ready but can be longer
- Recommendation is to start early and iron out the details before engaging NMTC Investors and CDEs

# NMTC Gross Equity Calculations

	Example 1	Example 2
QEI	\$10,000,000	\$10,000,000
NMTC Rate (over 7 years)	39%	39%
Total NMTCs Generated	\$3,900,000	3,900,000
Equity Price per NMTC	\$0.80	\$0.83
Gross NMTC Equity Generated	\$3,120,000	\$3,237,000

# NMTC Gross Equity Calculations

	Example 1	Example 2
Gross NMTC Equity Generated	\$3,120,000	\$3,237,000
Less: CDE upfront fee (% of QEI)	\$400,000	\$400,000
Less: NMTC transaction costs	\$450,000	\$450,000
Less: CDE Asset Management Fee (% of QEI)	\$350,000	\$350,000
Less: CDE Audit / Tax Return Expense	\$96,000	\$96,000
Less: Success Fee (% of QEI)	\$20,000	\$20,000
Total transaction cost	\$1,316,000	\$1,316,000
Net Equity	\$1,804,000	\$1,921,000
Net Equity (% of QEI)	18%	19%



# So how do I start?

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CDEs typically evaluate a project from the following perspectives:

- Project readiness to close within a specific timeline
- The projected community impact/outcomes
- Additional committed sources of financing

# So how do I start?

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## PROJECT READINESS

- Is the project ready to close within 3-6 months?
- Is the development team in place (architect, GC, Legal, NMTC Consultant and Accountant)?
- Has site control been obtained?
- Are retail or office spaces leased or under Letters of Interest?
- Have all NMTC eligibility requirements been met?

# So how do I start?

## PROJECTED COMMUNITY OUTCOMES

- Is the story around community outcomes compelling?
- Is the development going to make a difference in (“LIPs”) Low Income Persons’ lives?
- # jobs to be created, accessible to LIPs, and that are good quality jobs
- Community and commercial goods and services being provided by the project to LIPs
- Quantify W/MBEs utilization and environmentally sustainable outcomes, flexible lease rates and terms to tenants
- What are the catalytic impacts in the community?
- Is the project going to attract additional investment in the community? Etc.

# So how do I start?

## PROJECTED SOURCES OF FINANCING

- Are there commitments for other “leverageable” source of financing?
- What is the gap the project needs to fill with NMTC financing?
- Can the project cash flow support additional debt?
- If capital campaign sources, what amount of capital has been raised? Are the pledges secured?
- Are other sources of financing willing to work within the requirements of the NMTC program?

# Help is available

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- ❑ There are significant resources available for Sponsors, Borrowers or developer without experience in the program
- ❑ NMTC consultants typically prepare packages of information for CDEs and fill out Intake Forms, help negotiates with CDEs and Investors
- ❑ Accountants, Attorneys and other professionals are engaged as the project matures within the development stage
- ❑ If you have a project in early stages, engage a consultant to help you determine if the Project is eligible for the program and to structure the transaction using NMTC

# NMTC 101

## Introduction to NMTCs

Any additional questions?

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