New Markets Tax Credits
The Market for New Markets

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Background

• The first investments through the program occurred during the first quarter of 2004.
• The intent of the program is to encourage capital to flow to businesses and real estate development in low-income communities.
• The majority of NMTC investments have been into real estate projects in urban areas.
• Recent emphasis has targeted rural investments and healthy food related businesses in low-income communities.
• $4 billion in allocation remains from older allocations with $3.5 billion to be awarded in late 2012 or early 2013.
Tax Credit Award Process

• Through a competitive application process, certified CDEs [non-profits, local government, corporations, banks, and smaller financial firms] apply on a roughly annual basis for an allocation of NMTCs to the CDFI Fund, an arm of the Treasury Department.

• Approximately 25% of the 250 to 300 applicants each round receive an allocation.

• CDEs that receive a NMTC allocation are responsible for identifying and funding qualifying investments in line with their application and maintaining compliance for seven years in order to earn the tax credits and to be able to apply again in the future.

• In the vast majority of cases, CDEs sell the seven-year stream of tax credits to large national banks at a discount at the time of the initial investment. The proceeds of the sale of the tax credits are used to pay transaction costs and provide a loan to the project.
Characteristics of Common NMTC Deals

• NMTC deal sizes range from $5 million to $80 million. Allocation totaling more than $20 million is more difficult to arrange.
• CDEs often only provide $10 million or less in allocation per project.
• NMTC financing typically results in a seven-year interest-only loan equal to 20% to 25% of the allocation amount. So, $10 million in allocation would result in $2 million to $2.5 million in subsidized financing.
• Interest rates range from 1% to 4%.
Qualifications for NMTCs

• Qualification is based on census tract data. Program is currently shifting from the 2000 census to 2010 American Community Survey data.

• Qualifying areas are census tracts with either a median income level of 80% or less of area AMI or a poverty rate of over 20%.

• Virtually all investments have been targeted to “highly distressed” areas which must have a median income level of 60% of less of are AMI, a poverty rate of 30% or greater, or an unemployment rate of 1.5x the national rate or higher. Additionally, there are a number of area designations (brownfields, TIF, etc.) that can help qualify an area as “highly distressed”.

Structuring

• Due to the subsidized financing only being a portion of the required investment amount, NMTC investments must be leveraged with other forms of capital. Bank debt, bonds, grants, government loans, and equity investments can be used as leverage.

• Leveraged funds will not receive direct security in the real estate.

• After the 7 year compliance period, the loan will mature but may not require full repayment if the terms of the loan are successfully met over the full seven-year period.

• The borrower will often also agree to a community benefit agreement addressing job creation expectations, planned community benefits or services, additional reporting, and compliance with the program rules.
Project Characteristics

The beneficiaries of NMTC financing vary widely and include:

- Retail centers, hotels, industrial property, and mixed use developments.
- Manufacturing businesses and renewable energy projects.
- Non-profit facilities, charter schools, community clinics, and job training facilities.

CDEs with allocation vary greatly in several ways:

- Geographic focuses (single county to the entire nation)
- Preferred business or non-profit types, and targeted outcomes for their investments. Focus may be on non-profits, minority owned businesses, Native American regions, charter schools or environmental benefits.
- Focus on quality job creation sometimes with specific jobs per allocation amount targets.
Additional Thoughts

• The NMTC industry is a relatively small but very diverse niche market with hundreds of projects and businesses seeking investments from perhaps a hundred CDEs with allocation at a given time.

• The tax credit investor market is the most limited at this time with only a few large national investors dominating the market.

• An existing relationship with a CDE is very helpful.

• Projects or businesses that have the leveraged funds in place and would be able to close within six months will often receive priority from CDEs and tax credit investors.

• Beyond qualification, a business or real estate development must have a good “story” behind it regarding job creation, services to low-income people, or community redevelopment. Previous investment impacts are the primary driver for CDEs gaining additional NMTC allocation.