Introduction to the New Markets Tax Credit Program

... a project level overview
Agenda/Goals

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, 16th round announced last week for $3.5 billion.
- CDFI Fund makes 70-85 awards averaging between $40 - $50 million per eligible organization.
## Allocation Rounds

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

<table>
<thead>
<tr>
<th>Party</th>
<th>CDFI FUND</th>
<th>CDE</th>
<th>NMTC Investor</th>
<th>Project Borrower</th>
<th>Leverage Lender</th>
</tr>
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<tbody>
<tr>
<td><strong>Who are they?</strong></td>
<td></td>
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<td></td>
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<tr>
<td>Department of the Treasury</td>
<td></td>
<td>CDFIs</td>
<td>Banks</td>
<td>Developers</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Banks</td>
<td>Some C Corps</td>
<td>Non-profits</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Developers</td>
<td></td>
<td>Businesses</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Govt. agencies</td>
<td></td>
<td>Gov’t agencies</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Other nonpros</td>
<td></td>
<td>Others</td>
<td></td>
</tr>
</tbody>
</table>

| **What do they do?**         |           |            |               |                  |                 |
| Program Administrator        |           | Provide NMTC allocation | Make equity investment in CDE in return for tax credits | Develop and operate Project | Make loans through NMTC structure |
| Provide allocation to CDEs   |           | Make loans using capital from investor and lender |                | Operate business or non-profit |                   |
| Ensure Program Compliance    |           |                |               |                  |                 |

| **What are their requirements and expectations** |           |            |               |                  |                 |
| Reporting of community benefits and outcomes of CDE investments |           | Select projects that meet their application strategy | Financial return through tax credits | Received low cost flexible loans or equity financing from CDEs | Can be market rate or below market/philanthropic source of funds. |
| Reporting of community benefits and outcomes of CDE investments |           | Monitor projects that have been financed |                | Meet financial and program regulations | Receive debt service |
| Reporting to CDFI Fund       |           | Reporting to CDFI Fund |                | Report community outcomes to CDEs | 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

CDFI Fund

Submits NMTC Application

CDE

Receives NMTC Allocation

Uses portions of allocation

Partnerships w/Investor

Investor

Lender

Receives flexible financing

Project/Borrower

Community Capital Link
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

- 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
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

<table>
<thead>
<tr>
<th></th>
<th>Example 1</th>
<th>Example 2</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>QEI</strong></td>
<td>$10,000,000</td>
<td>$10,000,000</td>
</tr>
<tr>
<td><strong>NMTC Rate (over 7 years)</strong></td>
<td>39%</td>
<td>39%</td>
</tr>
<tr>
<td><strong>Total NMTCs Generated</strong></td>
<td>$3,900,000</td>
<td>3,900,000</td>
</tr>
<tr>
<td><strong>Equity Price per NMTC</strong></td>
<td>$0.80</td>
<td>$0.83</td>
</tr>
<tr>
<td><strong>Gross NMTC Equity Generated</strong></td>
<td>$3,120,000</td>
<td>$3,237,000</td>
</tr>
</tbody>
</table>
# NMTC Gross Equity Calculations

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</tr>
</thead>
<tbody>
<tr>
<td>Gross NMTC Equity Generated</td>
<td>$3,120,000</td>
<td>$3,237,000</td>
</tr>
<tr>
<td>Less: CDE upfront fee (% of QEI)</td>
<td>$400,000</td>
<td>$400,000</td>
</tr>
<tr>
<td>Less: NMTC transaction costs</td>
<td>$450,000</td>
<td>$450,000</td>
</tr>
<tr>
<td>Less: CDE Asset Management Fee (% of QEI)</td>
<td>$350,000</td>
<td>$350,000</td>
</tr>
<tr>
<td>Less: CDE Audit / Tax Return Expense</td>
<td>$96,000</td>
<td>$96,000</td>
</tr>
<tr>
<td>Less: Success Fee (% of QEI)</td>
<td>$20,000</td>
<td>$20,000</td>
</tr>
<tr>
<td>Total transaction cost</td>
<td>$1,316,000</td>
<td>$1,316,000</td>
</tr>
<tr>
<td>Net Equity</td>
<td>$1,804,000</td>
<td>$1,921,000</td>
</tr>
<tr>
<td>Net Equity (% of QEI)</td>
<td>18%</td>
<td>19%</td>
</tr>
</tbody>
</table>
So how do I start?

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?

**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 different in ("LIPs") Low Income Persons’ lives?
- # jobs to 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 impact 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

- 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 negotiate 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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