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Is Your Project a Candidate for NMTC Funding?

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Originally published in *Development Incentives Quarterly*.

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The federal New Markets Tax Credit (NMTC) program was created in 2000 for the purpose of encouraging investment in businesses and commercial projects, including real estate development, that benefit low-income communities. The NMTC program is not permanent, but rather is subject to Congressional renewal. Historically renewal has often been for one to two years at a time. However, in 2015 the NMTC program was extended through 2019, with \$3.5 billion in allocation authority for each year in this period. This unprecedented extension has created greater certainty that funding will be available to the NMTC program over the next several years (though the increased possibility of comprehensive tax reform as a result of the recent election results in additional uncertainty for federal income tax benefits generally). The following provides a brief description of the NMTC program, and projects that may benefit from credits.

The NMTC program is administered by the federal government through the Community Development Financial Institutions (CDFI) Fund. Generally, Congress specifies the amount of New Market Tax Credits that the CDFI Fund may award for each taxable year. Community Development Entities (CDEs) then submit applications to the CDFI Fund each year to be awarded an allocation of NMTCs for such year. The process of allocating NMTCs among applicant CDEs by the CDFI Fund is highly competitive, and typically occurs on an annual basis.

NMTCs themselves are actually claimed by investors who invest in qualifying projects through CDEs with available NMTC awards. Investors make investments (typically with leveraged funds) in projects located in qualifying low-income census tracts (Qualified Active Low-Income Community Businesses, or QALICBs) which projects are selected by the CDE. These investments are made with below market terms that typically result in the bulk of the value of the NMTCs being retained by the QALICB.

Whether a particular census tract qualifies as a “low income community” for purposes of the NMTC program is determined under rules specific to the NMTC program. The CDFI Fund website includes a mapping tool that indicates which census tracts qualify for this purpose. (Other NMTC consultants have mapping tools as well that may be helpful.)

A QALICB can be an operating business or a real estate project. Generally speaking, a real estate project must be physically located in a qualifying census tract. The determination of whether an operating business is “located” within a qualifying census tract is more complicated, and is generally based upon the location in which revenue is derived from the QALICB’s activity, the location of tangible property and the location of service performance by employees. In some instances, a QALICB not otherwise considered to be located in a qualifying census tract may still qualify for NMTC financing if the QALICB provides services for “targeted populations” (generally, individuals who are low-income persons or otherwise lack access to financing).

In order to obtain NMTC financing, a project must locate a CDE (or multiple CDEs) with a NMTC award that is willing to commit to allowing an investor in the project to claim a portion of those NMTCs. Given the high demand for NMTC financing, to say that convincing a CDE to make such a commitment for a particular project is competitive is an understatement.

During a CDE’s application for an allocation of NMTCs, CDEs typically commit to investing in projects that involve specified activities (e.g., health-related facilities, mixed-use facilities, community centers, etc.), projects that achieve specified goals (e.g., job creation, improving access to healthy foods, increasing environmental sustainability) or projects that are located in specified communities (e.g., within a particular region, state or community). Identifying a CDE with missions and goals in line with a particular project may improve the likelihood of receiving NMTC funding.

In April, the CDFI Fund announced that it would make \$7 billion of NMTC allocations available to CDEs for the combined two-year period of 2015/2016, creating the largest single allocation round award of credits under the NMTC program since its inception. It is generally anticipated that, by the end of the year, the CDFI Fund will announce the CDEs that will receive allocations of these NMTCs.

Despite its size, this pending NMTC award will likely only make a small dent in the overall market demand by deserving projects seeking NMTC program funding. We expect that many CDEs have already identified the projects that they intend to fund if they receive an allocation of NMTCs in connection with the upcoming awards. Given the multi-year horizon of the NMTC program, however, it is not too soon for qualifying projects to begin strategizing to be successful in future NMTC program funding rounds.