

August 30, 2007

Sent Via Mail and E-Mail

Mr. Matt Josephs
NMTC Program Manager
Community Development Financial Institutions Fund
U.S. Department of Treasury
601 13th Street, N.W., Suite 200 South
Washington, DC 20005

Dear Matt:

As members of the NMTC Working Group, we, the undersigned, have again joined together to provide the Community Development Financial Institutions Fund (the "CDFI Fund") our comments on the New Markets Tax Credit Program Allocation Agreement ("Allocation Agreement") so that you may review and consider them before releasing a new draft. For your convenience, we have provided specific comments in order of specific sections within the Allocation Agreement. We also believe it would be very beneficial if the CDFI Fund would provide a black-line copy of all of the changes made to the allocation agreement when it releases the next version.

Section 2.20 Reinvestment

We believe that the term "reinvestment" should be interpreted consistent with the rules set forth in the Internal Revenue Code ("IRC") and Regulations. As such, we recommend adding the following language to the end of the current definition: "...as set forth in IRC § 45D(b)(1)(B) and 26 C.F.R. 1.45D-1(d)(2)."

Section 2.21 Repayment

We believe that the term "repayment" should be interpreted consistent with the rules set forth in the IRC and Regulations. As such, we recommend adding the following language to the end of the current definition: "...as set forth in IRC § 45D(b)(1)(B) and 26 C.F.R. 1.45D-1(d)(2)."

Section 3.2(f) Authorized Uses of NMTC Allocation

In the last paragraph of Section 3.2(f), it states that an Allocatee "shall require that a Recipient CDE" make loans or investments with the same requirements regarding flexible, non-conventional or non-conforming terms and conditions as the Allocatee. We believe that the term "shall require" is unclear as to the requirement placed upon the Allocatee. As part of the Compliance and Monitoring Frequently Asked Questions document (November 2006), we request clarification that if the Allocatee requires a Recipient CDE to make loans or investments in accordance with Section 3.2(f) and provides penalties if the Recipient CDE fails to do so, then

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the Allocatee will not be in default of its Allocation Agreement if the Recipient CDE fails to make loans or investments in accordance with Section 3.2(f).

Question 17 of the 2007 NMTC Allocation Application was revised from allowing applicants to commit to offering products that had interest rates that were at least 25 percent lower than prevailing market rates to allowing the applicant to select from 5 options. In a comment letter submitted simultaneously with this one, we suggested that the wording of question 17 be changed from using a specific percentage below market to a specific amount of basis points below market due to the finite amount of subsidy that the NMTC provides. For this reason, we recommend that the sample language below be used for Schedule 1 and the first paragraph of Section 3.2 (f):

Schedule 1

Section 3.2(f): FLEXIBLE PRODUCTS

Flexible Products Clause: Applicable Not Applicable

The Applicant will commit that 100% of its QLICs will:

- (a) be provided in the form of equity; equity-equivalent financing; debt with interest rates at least 300 basis points below market; or debt that otherwise satisfies at least 5 indicia of flexible or non-traditional rates and terms, as listed in Section 3.2 (f).
- (b) be provided in the form of equity; equity-equivalent financing; debt with interest rates at least 250 basis points below market; or debt that otherwise satisfies at least 4 indicia of flexible or non-traditional rates and terms, as listed in Section 3.2 (f).
- (c) be provided in the form of equity; equity-equivalent financing; debt with interest rates at least 200 basis points below market; or debt that otherwise satisfies at least 3 indicia of flexible or non-traditional rates and terms, as listed in Section 3.2 (f).
- (d) be provided in the form of equity; equity-equivalent financing; debt with interest rates at least 150 basis points below market; or debt that otherwise satisfies at least 2 indicia of flexible or non-traditional rates and terms, as listed in Section 3.2 (f).

ARTICLE III THE NMTC ALLOCATION

3.2 (f) If applicable, at such time that the Allocatee has made 100 percent of its QLICs or September 30, 2010, whichever date is earlier, and until the Allocatee redeems its first Qualified Equity Investment related to its NMTC Allocation, the Allocatee shall demonstrate **as directed in Schedule 1** that QLICs made in the form of loans to or investments in CDEs or QALICBs (as opposed to loan purchases or the provision of Financial Counseling and Other Services) incorporated terms and conditions that, at the time the QLICs were made, were flexible, non-conventional, or non-conforming with reference to either the Allocatee's underwriting guidelines or standard practice in the marketplace as

~~documented by the Allocatee. Specifically, the Allocatee must have made QLICIs that (a) are equity or equity equivalent financing, (b) have interest rates that are at least 25 percent lower than the prevailing market rates for the particular product or at least 25 percent lower than the Applicant's current offerings for the particular product, or (c) meet at least three of the **The Allocatee may meet the requirement listed in Schedule 1 using the** following criteria, provided nothing in this Allocation Agreement shall be construed to require the Allocatee to engage in unsafe or unsound underwriting practices:~~

Section 3.2(h) Authorized Uses of NMTC Allocation

In our comment letter regarding the 2007 NMTC Allocation Application, we recommended that non-metropolitan counties be identified as a fourth geographic area of high distress in question 29(a) of the Application. Also, we recommended revising question 29(b) so that it includes non-metropolitan counties in the top tier of qualifying areas of higher distress. In addition to the non-metropolitan county changes, we recommend making what was previously the fourth item into three individual items. In order to incorporate these comments into the allocation agreement, we recommend the following sample language:

- 3.2 (h) If applicable, at such time that the Allocatee has made 100 percent of its QLICIs or September 30, 2010, whichever date is earlier, and until the Allocatee redeems its first Qualified Equity Investment related to its NMTC Allocation, the Allocatee shall have made at least 75 percent of the total dollar amount of its QLICIs in areas that are (1) characterized by at least one of items (i) – (iv) on the list below for each QLICI, (2) characterized by at least two of items (v) – (xviii) on the list below for each QLICI, or (3) characterized by item (xix) on the list below as of the date the Allocatee closed the QLICI transaction:
- (i) [30% POVERTY] Census tracts with poverty rates greater than 30%.
 - (ii) [60% MEDIAN FAMILY INCOME] Census tracts with, if located within a non-Metropolitan Area, median family income that does not exceed 60% of statewide median family income, or, if located within a Metropolitan Area, median family income that does not exceed 60% of the greater of the statewide median family income or the Metropolitan Area median family income.
 - (iii) [1.5 UNEMPLOYMENT RATE] Census tracts with unemployment rates at least 1.5 times the national average.
 - (iv) [NON-METROPOLITAN AREAS] Non-Metropolitan Census Tracts.
 - (v) [25% POVERTY] Census tracts with poverty rates greater than 25%.
 - (vi) [70% MEDIAN FAMILY INCOME] Census tracts with, if located within a non-Metropolitan Area, median family income that does not exceed 70% of statewide median family income, or if located within a Metropolitan Area, median family income that does not exceed 70% of the

- greater of the statewide median family income or the Metropolitan Area median family income.
- (vii) [1.25 UNEMPLOYMENT RATE] Census tracts with, unemployment rates at least 1.25 times the national average.
 - (viii) [FEDERAL ECONOMIC DEVELOPMENT ZONES] Federally designated Empowerment Zones, Enterprise Communities, or Renewal Communities.
 - (ix) [SBA HUB ZONES] SBA designated HUB Zones to the extent QLICIs will support businesses that obtain HUB Zone certification by the SBA.
 - (x) [BROWNFIELDS] Brownfield sites as defined under 42 U.S.C. 9601(39).
 - (xi) [HOPE VI REDEVELOPMENT] Areas encompassed by a HOPE VI redevelopment plan.
 - (xii) [FEDERAL NATIVE AREAS] Federally designated Native American or Alaskan Native areas, Hawaiian Homelands, or redevelopment areas by the appropriate Tribal or other authority.
 - (xiii) [ARC/DRA AREAS] Areas designated as distressed by the Appalachian Regional Commission or Delta Regional Authority.
 - (xiv) [COLONIAS AREAS] Colonias areas as designated by the U.S. Department of Housing and Urban Development.
 - (xv) [FEDERAL MEDICALLY UNDERSERVED AREAS] Federally designated medically underserved areas, to the extent QLICI activities will result in the support of health related services.
 - (xvi) [TARGETED POPULATIONS] As permitted by IRS and related CDFI Fund guidance materials, projects serving Targeted Populations to the extent that: (a) such projects are located in non-metropolitan areas; or (b) such projects are 60% owned by low-income persons (LIPs); or (c) at least 60% of employees are LIPs; or (d) at least 60% of customers are LIPs.
 - (xvii) [HIGH MIGRATION] High Migration Rural County.
 - (xviii) [STATE/LOCAL ECONOMIC ZONES] Enterprise zone programs, or other similar state/local programs targeted towards particularly economically distressed communities.
 - (xix) [FEMA DISASTER AREAS] Counties for which the Federal Emergency Management Agency (FEMA) has: issued a “major disaster declaration” and made a determination that such County is eligible for both “individual and public assistance”; provided that, with the exception of the GO Zone, the initial investment will be made within 24 months of the disaster declaration.

Furthermore, to the extent that the Allocatee makes QLICIs in the form of loans to or investments in CDEs (“Recipient CDEs”), the Allocatee shall require that the Recipient CDE makes loans to or investments in QALICBs in areas that are

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(1) characterized by at least one of items (i) – (iv) on the list above for each loan or investment, (2) characterized by at least two of items (v) – (xviii) on the list above for each loan or investment, or (3) characterized by item (xix) on the list above for each loan or investment.”

Section 3.3(h) Restrictions on the Use of NMTC Allocation

We believe, in general, this provision suffers from many of the same kinds of problems that caused the IRS to withdraw its regulation regarding “substantial improvements” because it is vague, ambiguous, and creates serious impediments to the use of New Markets Tax Credits for real estate projects. Some of the questions it presents are:

- How much “new construction” or “substantial rehabilitation” must occur and how is it measured?
- Is there any time frame within which such “new construction” or “substantial rehabilitation” must occur?
- What is a “substantial rehabilitation”?

We recommend that guidance to the questions above be added in the Compliance and Monitoring Frequently Asked Questions document (November 2006).

Section 3.3(i) Authorized Uses of NMTC Allocation

We believe that the last sentence of this section will precipitate many questions to the CDFI Fund as to what falls within the generally consistent parameters as deals change from the original proposals in the allocation application. It is unclear if generally consistent refers to the type of transactions, including percentage of allocation used in various types of transactions (real estate loans versus equity investments in start-up businesses), community impact, or something else.

Moreover, the term “strategies” could refer to any or all of a wide range of things covered in the application, *e.g.*, methods and sources of raising capital, types of products (debt vs. equity), terms of products (rates, maturities), targeted uses (real estate vs. non-real estate, types of target businesses), targeted geographic areas, community impacts, etc. Much of the information that applicants are asked to provide (such as the projections in Tables B1 through B7) are merely goals or best estimates, yet this provision raises a concern that applicants are now somehow bound to adhere to them.

Our preference would be that the CDFI Fund deletes this sentence entirely. To the extent that there are specific elements of the Allocatee’s business plan as set forth in the application that the CDFI Fund wants the Allocatee to comply with, such elements should be listed in Schedule 1. This language will generate significant concerns for investors as to compliance with the Allocation Agreement due to (i) the lack of clarity and guidance on what “generally consistent” means and what the “strategies” are that the Allocatee must conform to, and (ii) the fact that, because this provision applies globally to all of the Allocatee’s investments taken as a whole, investors for each particular QLICI would be subject to the immediate and ongoing risk of whether all of the Allocatee's investments comply with this provision.

As an alternative, we ask that the CDFI Fund at least consider revising the language in a manner that removes some of these uncertainties. We offer the following suggested revision:

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“In its use of the NMTC Allocation as authorized in Section 3.2 of this Allocation Agreement, at such time as the Allocatee has made 100 percent of its QLICIs or September 30, 2010, whichever is earlier, Allocatee shall demonstrate that it has made, or used commercially reasonable efforts to make, substantially all of its QLICIs in a manner generally consistent with the types of products, targeted uses, and targeted markets identified in its responses to Question 15 and Question 16(b) of the Allocation Application.”

Section 6.2(b) Fraud, Waste and Abuse

We believe the language in this section is too broad in scope and will cause much uncertainty. We believe that the language should more closely approximate the language in Treasury Regulation 1.45D-1(g)(1).¹ Specifically, we believe that the language should be as follows:

“If a principal purpose of a transaction or a series of transactions is to achieve a result that is inconsistent with the purposes of ~~the Act~~, **Section 45D**, the NMTC Program Income Tax Regulations, the Notice of Allocation Availability (70 FR 41075 and as amended 71 FR 12423), or this Allocation Agreement, the Fund, ~~in its sole discretion~~, may treat the transaction or series of transactions as causing an event of default subject to the remedies available under Section 8.3 of this Agreement.”

The above language replaces “the Act”, with “Section 45D”. The Act, as defined in Section 2.1, includes more than Section 45D. For purposes of this provision, we believe that Section 45D is the relevant provision of the Act.

The above language removes the parenthetical “in its sole discretion”. This omission makes the language consistent with Treasury Regulations 1.45D-1 (g)(1). We believe that if the phrase is left in that it will generate significant concerns with investors who will feel uncertain about how the CDFI Fund will interpret the requirements of each section. “In its sole discretion” appears in numerous other places in the Allocation Agreement and we similarly believe it should be removed.

Section 6.9(g) Advise the Fund of Certain Material Events

We believe that this specific section should be removed from the Allocation Agreement as it causes an Allocatee to be in default for an event that an Allocatee rarely has foreseeable control over. At some time during the compliance period, it is reasonable to assume key management officials may leave a company for various reasons. We believe that the Allocation Agreement should not give power to the CDFI Fund to determine that the Allocatee is in default due to these changes or, in effect, to assert control over the employment decisions and circumstances of Allocatees.

¹ Treas. Reg. Sec. 1.45D-1(g)(1) “Anti-abuse. If a principal purpose of a transaction or a series of transactions is to achieve a result that is inconsistent with the purposes of section 45D and this section, the Commissioner may treat the transaction or series of transactions as causing a recapture event under paragraph (e)(2) of this section.”

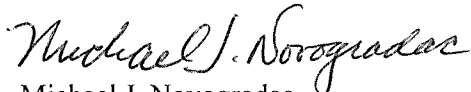
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Conclusion:

We are excited about the New Markets Tax Credit Program being able to reach and benefit more businesses and individuals who lack adequate access to loans or equity investments. Thank you in advance for your time and consideration. Please do not hesitate to contact us if you have any questions regarding our comments or if we can be of further assistance.

Yours very truly,
Novogradac and Company LLP

Novogradac and Company LLP



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along with the undersigned

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