

UNITED STATES  
DEPARTMENT OF  
THE TREASURY



# Community Development Financial Institutions (CDFI) Fund

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New Markets Tax Credit Program  
2008 Application Workshop

January 2008

# Presentation Roadmap



- **Brief Overview of the CDFI Fund**
- Overview of NMTC Program
- Applying for CDE Certification
- Applying for NMTC Allocations
- Prior NMTC Award Information

# CDFI Fund Mission and Background



- Created in 1994
- Mission:
  - To expand the capacity of financial institutions to provide credit, capital, and financial services to underserved populations and economically distressed communities in the United States.

- **CDFI Program:**  
Provides assistance to CDFIs and emerging CDFIs.
- **NACA Program:**  
Supports development and growth of Native American CDFIs.
- **Bank Enterprise Award (BEA) Program:**  
Provides awards to insured depository institutions for increasing investments in CDFIs and/or activities in distressed communities.
- **New Markets Tax Credit (NMTC) Program**

# Presentation Roadmap



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# NMTC Program Background



- Enacted on December 21, 2000.
- Part of the Community Renewal Tax Relief Act of 2000.
- June 10, 2002 - First issue of Notice of Allocation Availability.
- March 14, 2003 - The Fund announces that 66 organizations were selected to receive \$2.5 billion of tax credit allocations under the 1<sup>st</sup> round.

# Overview of NMTC Program



- Provides a credit against Federal income taxes for investors that make Qualified Equity Investments (QEIs) into Community Development Entities (CDEs).
- CDEs in turn use the proceeds of these investments to make make Qualified Low-Income Community Investments (QLICIs).
- QLICIs include, among other things, investments in businesses and real estate projects in low-income communities.

- The credit is taken over a 7-year period.
- The credit rate is:
  - In each of the first three years, 5% of the original investment amount.
  - In each of the final four year, 6% of the original investment amount.
- Equals 39% of amount of original investment.



# Example



The Fund awards an allocation of \$1 million to a CDE. The CDE offers the tax credit to a single investor in exchange for a \$1 million equity investment. How much can the investor claim as a credit on its Federal taxes?

Years 1-3      Tax Credit at 5%      Value \$50,000 per year

Years 4-7      Tax Credit at 6%      Value \$60,000 per year

**TOTAL VALUE OVER 7 YEARS.....\$390,000**

# What is a CDE?



- A domestic corporation or partnership that is an intermediary vehicle for the provision of loans, investments or financial counseling in “Low-Income Communities” (LICs).
- CDEs are required to demonstrate that they:
  - Have a **primary mission** of serving, or providing investment capital for, LICs or Low-Income Persons.
  - Are **accountable** to residents of the LICs that they serve.

# What is a “Low-Income Community?”



“Low-Income Communities” (LICs) are census tracts:

1. With at least 20% poverty rate; ***or***
2. Where the median family income does not exceed 80% of the area median family income; ***or***
3. That have a population of less than 2,000, are contained within a Federally designated Empowerment Zone, and are contiguous to at least one other LIC; ***or***
4. Where the median family income does not exceed 85% of the area median family income, provided the census tract is located in a high migration rural county.

# Low Income Communities (cont'd)



- Projects not located within LICs, but that otherwise serve ***Targeted Populations***, may also qualify for NMTC investments.
- Targeted Populations include:
  1. Low-Income Persons, to the extent the project is located in a census tract with a median family income at or below 120% of the applicable area median family income; or
  2. For Gulf Opportunity (GO) Zone allocations, individuals that have been displaced from their homes and/or have lost their principal source of employment in the wake of Hurricane Katrina.
- Refer to IRS and CDFI Fund guidance for additional details.

# Qualified Equity Investment (QEI)



- NMTCs are offered to investors for “Qualified Equity Investments” (QEIs) in the CDE.
- QEI is:
  - An equity investment in a CDE - an equity investment is stock in a corporation or any capital interest in a partnership.
  - The equity investment must be acquired by the investor at its original issue solely in exchange for cash.
  - The equity investment must meet the substantially-all requirement, and
  - The equity investment must be designated by the CDE.
- QEIs must remain invested in the CDE during a **7-year** credit period - Investors claim credits as of the date a QEI is initially made.

# Timing of Investments



- CDEs must offer NMTCs to investors within **5 years** of receiving an allocation.
- CDEs have **12 months** to invest their QEI proceeds into Qualified Low-Income Community Investments (QLICs).
- Generally, CDEs that receive returns of capital will have **12 months to reinvest** those funds in QLICs.
  - Reinvestment is not required in the final year of the 7-year credit period.

**“Substantially all”** of the QEI proceeds must be invested in QLICs within 12 months

**Years 1-6: Substantially All = 85% of amount paid by investor at original issue**

**Year 7: Substantially All = 75%**

At all times, 5% of the original QEI issue amount may be used for certain reserves by the CDE and count towards meeting the substantially-all requirement.

- A CDE may demonstrate that it has satisfied the substantially-all requirement in 2 ways:
  - Direct tracing:
    - Under **direct tracing**, CDE is required to trace at least 85% of the QEI proceeds to specified QLICs.
  - Safe harbor:
    - Under a **safe harbor**, a CDE must demonstrate that 85% of its aggregate gross assets are invested in QLICs.



## Eligible Investments (QLICs):

- 1) Any capital or equity investment in, or loan to, any “Qualified Active Low-Income Community Business” (QALICB).
- 2) Purchase of a loan from another CDE if the loan is a QLIC.
- 3) “Financial Counseling and Other Services” (FCOS) to businesses located in, or residents of, LICs.
- 4) Any equity investment in, or loan to, any CDE.

## Requirements

- QEI proceeds must be invested in QLICs throughout the 7-year credit period.
- CDE reinvestment requirement
  - Years 1-6:
    - Generally, returns of equity, capital or principal must be reinvested within 12 months.
    - Periodic loan repayments may be aggregated for up to 24 months before reinvestment is required.
  - No reinvestment required in year 7.

## What is a typical QALICB?

- An operating business located in a LIC.
- A business that develops or rehabilitates commercial, industrial, retail and mixed-use real estate projects in a LIC.
- A business that develops or rehabilitates community facilities, such as charter schools or health care centers, in a LIC.
- A business that develops or rehabilitates for-sale housing units located in LICs.

# Qualified Active Low Income Community Business (QALICB)



## To be a QALICB

- At least 50% of the total gross income is from the active conduct of a qualified business in Low-Income Communities (LICs); and
- At least 40% of the use of tangible property of the business is within LICs; and
- At least 40% of the services performed by the business' employees are performed in LICs; and

## To be a QALICB (cont'd)

- Less than 5% of the average of the aggregate unadjusted bases of the property is attributable to collectibles (e.g., art and antiques), other than those held for sale in the ordinary course of business (e.g., inventory); and
- Less than 5% of the average of the aggregate unadjusted bases of the property is attributable to nonqualified financial property (e.g., debt instruments with a term in excess of 18 months).

## To be a QALICB (cont'd)

- The gross income test is deemed to be met if either the use of tangible property or the use of services performed test is met at 50% or higher.
- If a business has no employees, it can meet both the services performed and gross income tests if it meets the use of tangible property test at 85% or higher.

# Ineligible Activities



- Residential rental property:
  - Buildings or structures which derive 80% or more of its gross rental income from renting dwelling units
- Certain types of businesses:

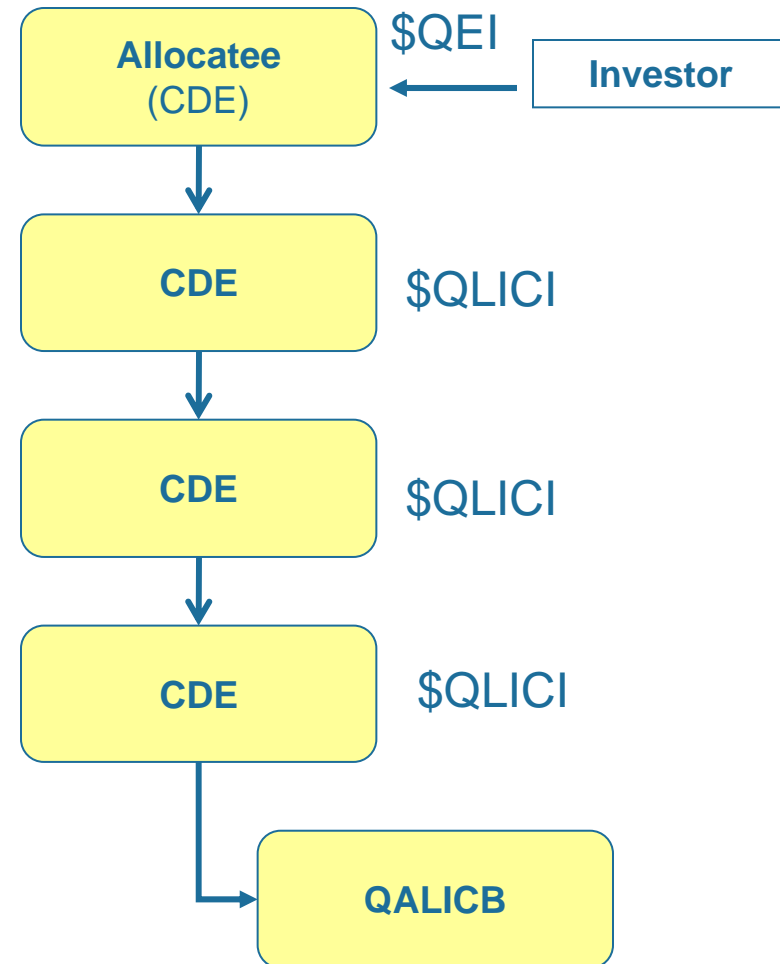
- |                                     |  |
|-------------------------------------|--|
| – <b>Golf courses</b>               | – <b>Massage Parlors</b>   |
| – <b>Race tracks</b>                | – <b>Hot tub facilities</b>  |
| – <b>Gambling facilities</b>        | – <b>Suntan facilities</b>   |
| – <b>Certain farming businesses</b> | – <b>Stores where the principal business is the sale of alcoholic beverages for consumption off premises</b> |
| – <b>Country clubs</b>              |  |

- Refer to IRS regulations for additional details

## 2: Investing in Other CDEs



- Investments may be made through multiple layers of CDEs (i.e., up to 4 CDEs)
- The last CDE recipient needs to demonstrate that it used those dollars to:
  - Make loans to or investments in QALICBs; and/or
  - Provide FCOS to businesses or residents of LICs.



All time limits must be met as if the CDE with the allocation directly made the QLICI.



# Purchasing Loans from Other CDEs



CDEs may purchase loans – but not investments – from other CDEs if:

- The purchased loans were originated by an entity that was a CDE at the time the loan was sold; and
- The loans qualified as QLICs at either the time the loan was:
  - Originated; or
  - Purchased by the allocated CDE.



FCOS is “advice provided by the CDE relating to the organization or operation of a trade or business.”

- Possible FCOS activities:
  - Business plan development
  - Assistance with business financials
  - Operating assistance to non-profit organizations

NMTCs may be recaptured from investors during the 7-year credit period if:

- The QEI fails the **“Substantially-all”** requirement
  - Failure to invest 85% as allowed; or
  - Failure to meet QALICB requirements; or
  - Failure to meet one-year investment requirement.
- The CDE ceases to qualify as a CDE.
- The CDE redeems the investment.

It is not an event of recapture – and an investor may continue to claim NMTCs – if a CDE files for bankruptcy.

**Step 1:** Entities apply to the Fund for CDE certification.

**Step 2:** Entities apply competitively to the Fund for a NMTC allocation.

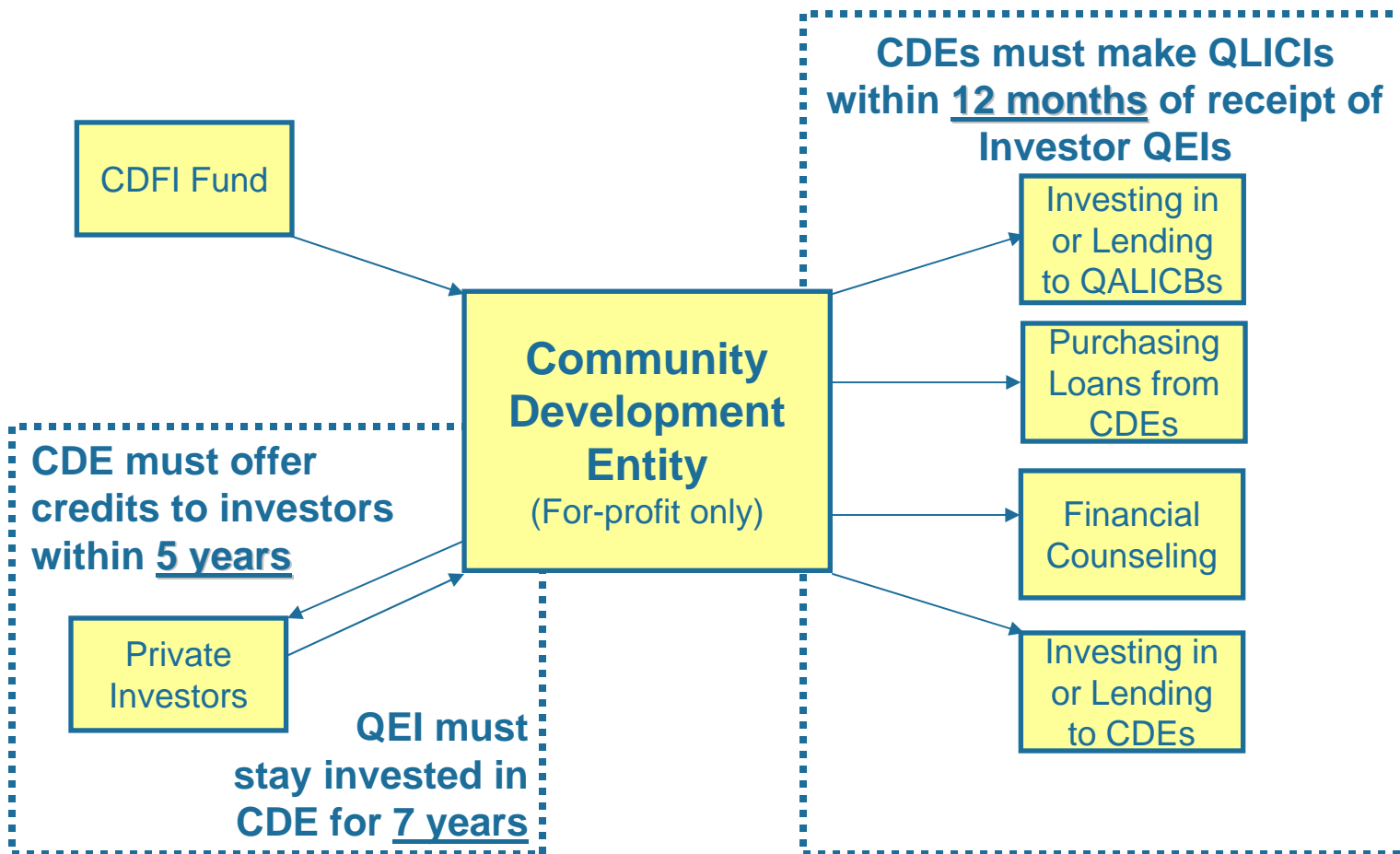
**Step 3:** The Fund selects CDEs to receive NMTC allocations.

**Step 4:** CDEs enter into an Allocation Agreement with the CDFI Fund.

**Step 5:** CDEs offer NMTCs to investors for cash.

**Step 6:** CDEs use proceeds to make “Qualifying Low-Income Community Investments” (QLICs).

# Summary Graphic



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# Why Become a CDE?



- For-profit CDEs may raise capital by offering tax credits to investors.
- All CDEs (including non-profits) are eligible to receive loans and investments from or sell loans to CDEs that have been issued tax credit allocations by the Fund.

# Timeframe to Apply for CDE Designation



- Generally, CDE applications are accepted on a rolling basis.
- Any entity not yet certified as a CDE that intends to apply for an allocation of NMTCs in the 2008 round must submit a CDE certification application that is:
  - **Postmarked on or before February 6, 2008**



- Automatically qualify for CDE certification.
- May register as CDEs electronically at [www.cdfifund.gov](http://www.cdfifund.gov)
- To apply for an allocation of NMTCs under the 2008 round, CDFIs/SSBICs must register as CDEs **by February 6, 2008.**
- Affiliates and subsidiaries of CDFIs and SSBICs
  - Do not automatically qualify as CDEs.
  - Must complete a CDE Certification Application.

- **Legal Entity**--*Be incorporated or formed as a domestic corporation or partnership for federal tax purposes;*
  - The entity must have a valid and distinct EIN (Employer Identification Number)
- **Primary Mission**– *Serving a LIC or Low-Income People*
- **Accountability**– *CDE is accountable to LICs in the service area*

## Step 1:

Provide organizational documents evidencing an appropriate primary mission.

Such organizational documents may include:

- Bylaws,
- Articles of incorporation or organization,
- Partnership agreements, or
- Board resolutions.

## Step 2:

Submit “Certification of Authorized Representative” demonstrating that at least 60% of products and services are and will continue to be directed to

- Low-Income Persons (LIPs):
- Low-Income Communities (LICs); or
- Organizations serving LIPs or LICs.

## Step 1:

Identify a service area

- Local  
*(e.g., city; county; metropolitan area; Indian Reservation)*
- Statewide or territory-wide
- Multi-state
- National

## Step 2:

- Complete the “Accountability Tables” to
  - Demonstrate that 20% of the members of either the governing board or advisory board(s) represent LICs in the service area.
- Applicants using multiple advisory boards must complete information for each advisory board.

## Step 2 (cont'd):

Applicant CDEs fulfilling accountability through an advisory board will need to provide narrative indicating:

- ✓ How advisory board members are selected;
- ✓ How often the advisory board convenes;
- ✓ How it solicits feedback from the community; and
- ✓ How it informs the actions of the governing body.

# Who is Representative of LICs?



- A board member must either:
  - Reside in a LIC in the service area; or
  - Represent the interests of residents of LICs in the service area.
- Examples of representation include:
  - A small business owner whose business is located in a LIC in the service area.
  - An employee or board officer of a community-based or charitable organization primarily serving LICs in the service area.
  - An employee of a governmental agency that principally provides services benefiting LICs.



# Who is not Representative?



- Board members that are principals or staff members of the Applicant CDE, its affiliated entities or its investors cannot be deemed representative of LICs.
- With the exception of board members that are also on the board of an affiliate as representative of LICs, if:
  - The board members are not principals or staff members of the Applicant CDE, its affiliated entities or its investors; and
  - The board members can be deemed representative of LICs through means other than their association with the affiliated entity.

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# NMTC Investment Authority Available



2002	\$2.5 billion	→	Includes 2001 Round
2003	\$1.5 billion	→	Combined for 2004 Round
2004	\$2 billion		
2005	\$2 billion		
2006	\$3.5 billion		+ \$600 million GO Zone
2007	\$3.5 billion		+ \$400 million GO Zone
2008	<u>\$3.5 billion</u>		
<b>TOTAL</b>	<b>\$19 billion</b>		

Unallocated investment authority may be carried over from year to year through 2014.

# 2008 Round Deadlines (Anticipated)



Deadline	Date
Release of NOAA and application materials	<u>December 18, 2007</u>
CDE Certification Applications must be postmarked on or before	<u>February 6, 2008</u>
Last day to contact the CDFI Fund	<u>March 3, 2008</u>
<u>Online Submission of Allocation Application</u>	<u>March 5, 2008</u>
Attachments and signature page must be postmarked on or before	<u>March 7, 2008</u>
Date by which prior-year allocatees must issue the requisite percentage of QEIs	<u>June 13, 2008</u>

Additional details to be addressed in NOAA

# Who Can Apply?



- Both for-profit and non-profit entities may apply.
- In its Allocation Application, a non-profit applicant must discuss its strategy to:
  - Form at least one for-profit subsidiary.
  - Transfer its entire allocation to for-profit subsidiaries.

# Preparing for the Online Application



- Register as a user through myCDFI-Fund.
- Ensure you have sufficient internet access.
- Familiarize yourself with the paper application.
- Start constructing your responses in MS Word or other word processing software.
- **Give yourself plenty of time for submitting.**

**Application deadline: March 5, 2008 @ 5:00 P.M. EST**

# Review Criteria



- Maximum of 110 points
- Four sections of 25 points each:
  - Business Strategy
  - Community Impact
  - Capitalization Strategy
  - Management Capacity

**Applicants may earn an additional 10 “priority” points**

## “Priority” points given under Business Strategy section to CDEs:

- 1) With a track record of having successfully provided capital or technical assistance to disadvantaged businesses or communities; or
- 2) Intending to invest in businesses in which unrelated parties hold the majority equity interest.



## To score favorably, an Applicant must demonstrate:

- ✓ That its products and services are significantly more flexible or non-traditional than industry standards.
- ✓ An excellent track record of providing products and services similar to those it intends to deploy with QEI proceeds.
- ✓ A strong pipeline of proposed projects.
- ✓ That the NMTCs will add significant value to the proposed products and services.

- Deploy debt or equity capital, or offer products and services which:
  - Are designed to meet the needs of underserved markets.
  - Focus on customers or partners that typically lack access to conventional sources of capital.
- Applicants without a track record can reference the track record of an identified Controlling Entity.
- Projected activities are best discussed with appropriate details, including examples.
- Projected deployment levels should be consistent with the applicant's track record and proposed pipeline of transactions.

## To score favorably, an Applicant must demonstrate:

- ✓ A high percentage of its QLICs will be made in areas of higher economic distress.
- ✓ It has historically achieved significant community impacts per dollar invested.
- ✓ That its projected impact are credible, relevant, and quantifiable.
- ✓ That it has the ability to track projected impacts.
- ✓ That it has the ability to achieve both economic development impacts (*e.g. jobs*) and community development impacts (*e.g. jobs to Low Income Persons*).
- ✓ That it coordinates with local development plans.
- ✓ That its activities will catalyze other non-NMTC investments in the low-income communities.

- Provide at least 75% of QLICs to severely economically distressed areas (Q. 29a & b);
- Clearly identify and quantify impacts; particularly impacts to Low-Income Persons or residents of LICs;
- Provide supporting discussion of the methodologies used to derive those projections; and
- Discuss how data will be collected going forward.

**To score favorably, an Applicant must articulate its management team's past experiences, as well as its anticipated duties and responsibilities, in the following areas:**

- ✓ Deploying capital in LICs.
- ✓ Raising capital— particularly from profit-motivated investors.
- ✓ Managing the addition of NMTC activities into its current portfolio of activities, including asset management and program compliance.
- ✓ Obtaining meaningful feedback from community representatives.

## To score favorably, an Applicant must demonstrate

- ✓ That it has raised capital close to the requested allocation amount – particularly at market or near market terms.
- ✓ That it has secured QEI commitments from investors or has a strong fundraising strategy for doing so.
- ✓ That it can issue QEIs in the near term.
- ✓ That the economic benefits of the NMTC will be passed through to borrowers and investees.
- ✓ That it is offering products and services that are substantially different from those of its investors or affiliates.
- ✓ That it intends to deploy more than 85% of its QEI proceeds into QLICs.

# Selection Process



## Peer Review

Fund staff & external reviewers evaluate/score applications and recommend allocation amounts.

## Panel Review

Applications that meet minimum scoring thresholds in each of the four major application sections are sent to a Fund panel for consideration.

## Selection of Applicants

Selecting Official makes final determinations based upon panel recommendations.

During Panel the CDFI Fund will review past transactions from Prior Allocatees.

Adjustments may be made to the final pool to ensure proportional representation from CDEs serving Non-Metropolitan Counties.

# Non-Metropolitan Counties



- The Fund will ensure proportional allocation of QLICs in Non-Metropolitan Counties:
  - Proportion of awardees that are Rural CDEs equal to proportion of applicants in Phase 2 review pool that are Rural CDEs.
  - At least 20 percent of QLICs made using QEI proceeds are invested in Non-Metropolitan Counties.
- Rural CDEs:
  - Historically dedicated at least 50 percent of activities to Non-Metropolitan Counties;
  - Committed at least 50 percent of NMTC activities will be conducted in Non-Metropolitan Counties.

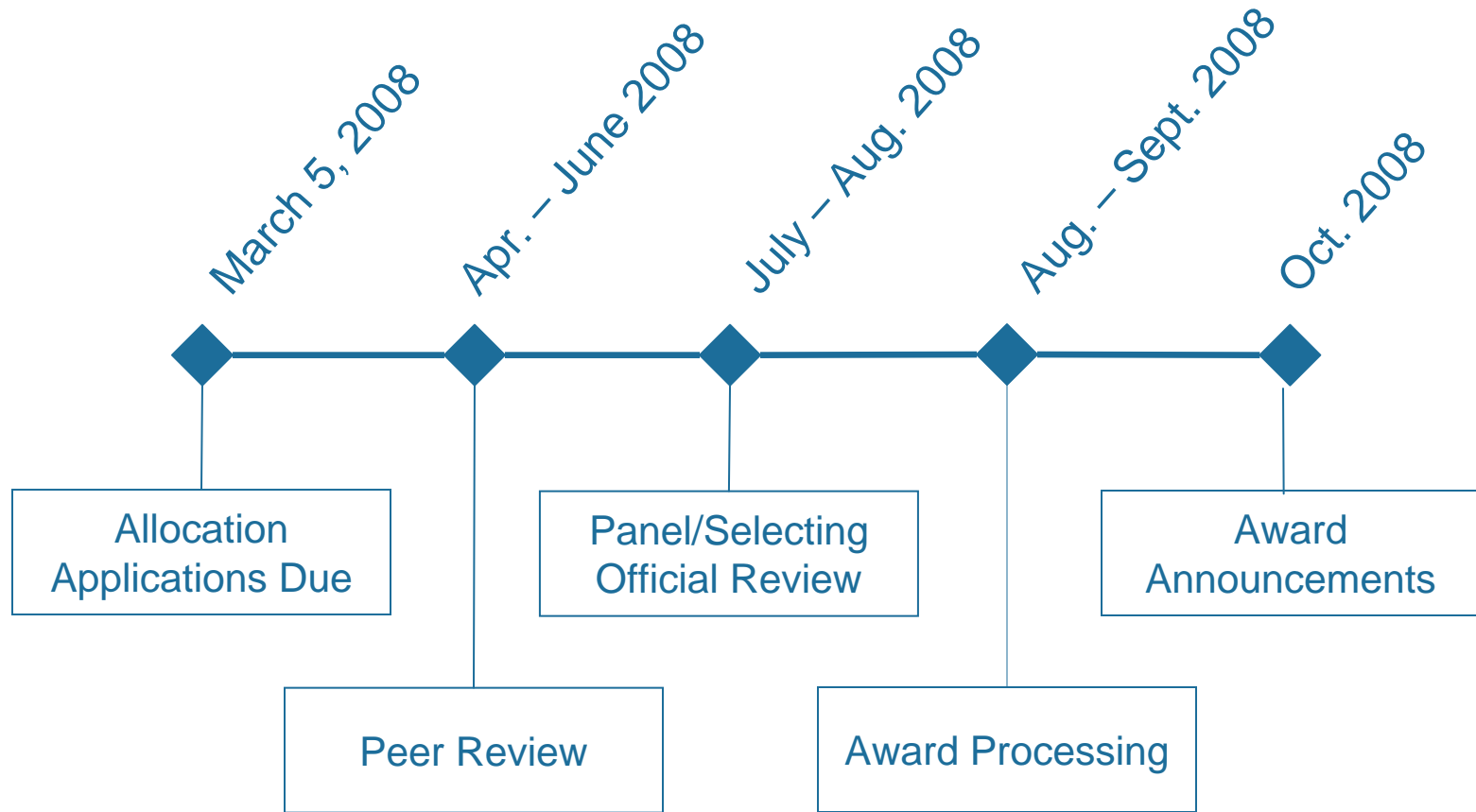


# Non-Metropolitan Counties



- Applicants will establish minimum and maximum percentage of total NMTC activity in Non-Metropolitan Counties.
- There will be no adjustments or alterations made during the Peer Review and Panel Review process.
- Adjustments may be made after the applicants are initially selected for awards. Specifically, the Fund will review the distribution of awards and awardees to determine whether:
  - (i) Additional “Rural CDEs” need to be added to the awardee pool, to ensure a proportional representation from Rural CDEs; and/or
  - (ii) Awardees will be required to meet an amount higher than their minimum projected level of investments in Non-Metropolitan Counties, to ensure that at least 20 percent of QLICs are invested in such counties.

# Review Process Timeline



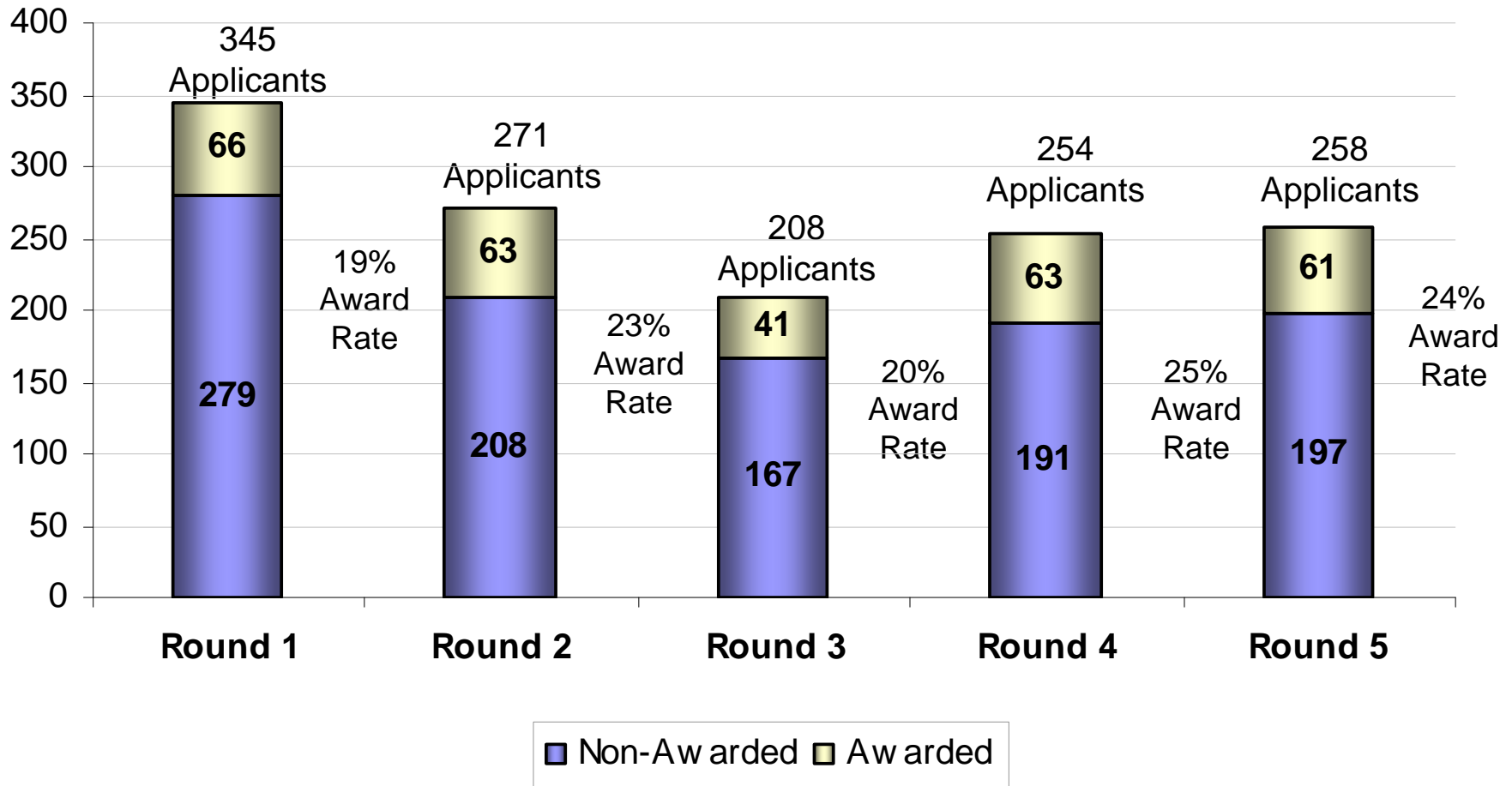
# Presentation Roadmap



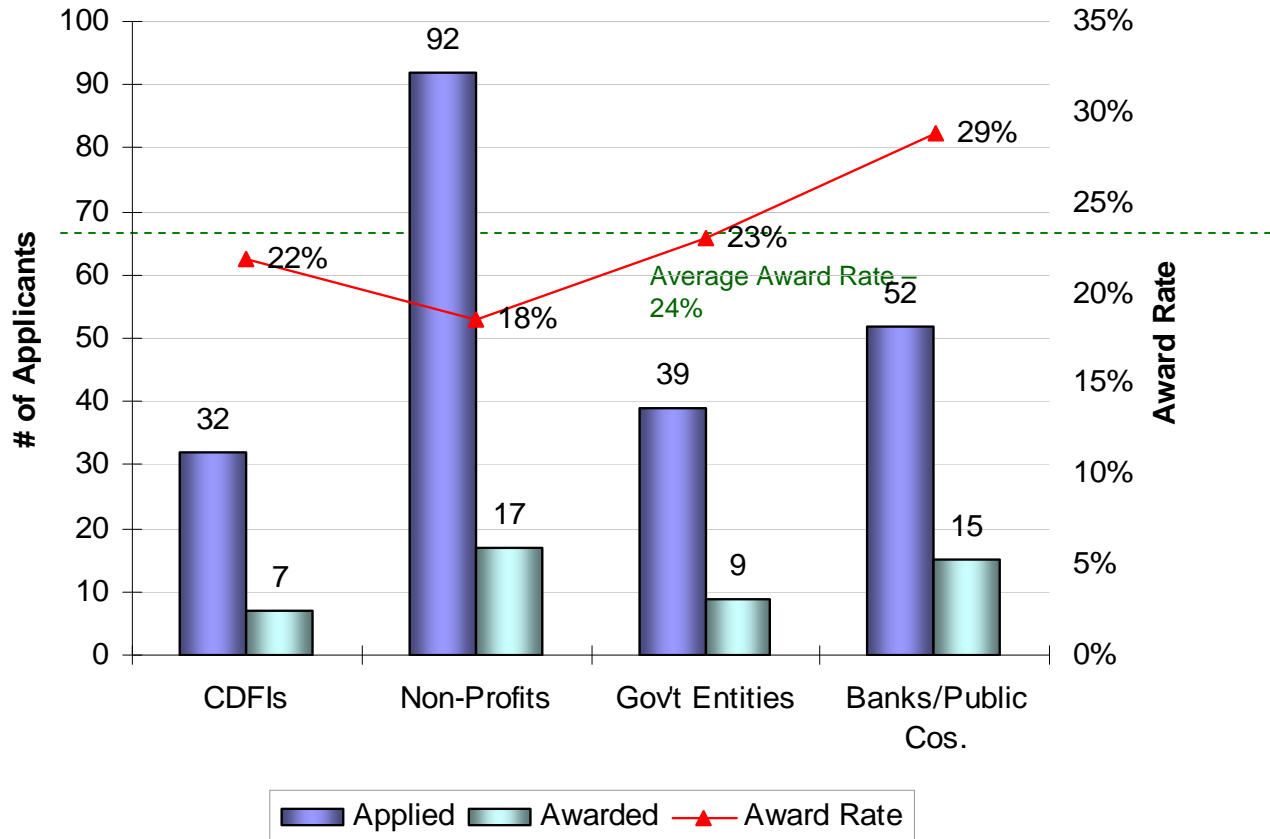
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- The Fund has certified over 2,400 entities as CDEs.
- In the first five allocation rounds, the Fund received over 1,328 applications for allocations of NMTCs.
- These entities collectively requested \$135 billion in allocation authority.
- The Fund has made 294 awards totaling \$16 billion in allocation authority.

# Applicants/#Allocatees

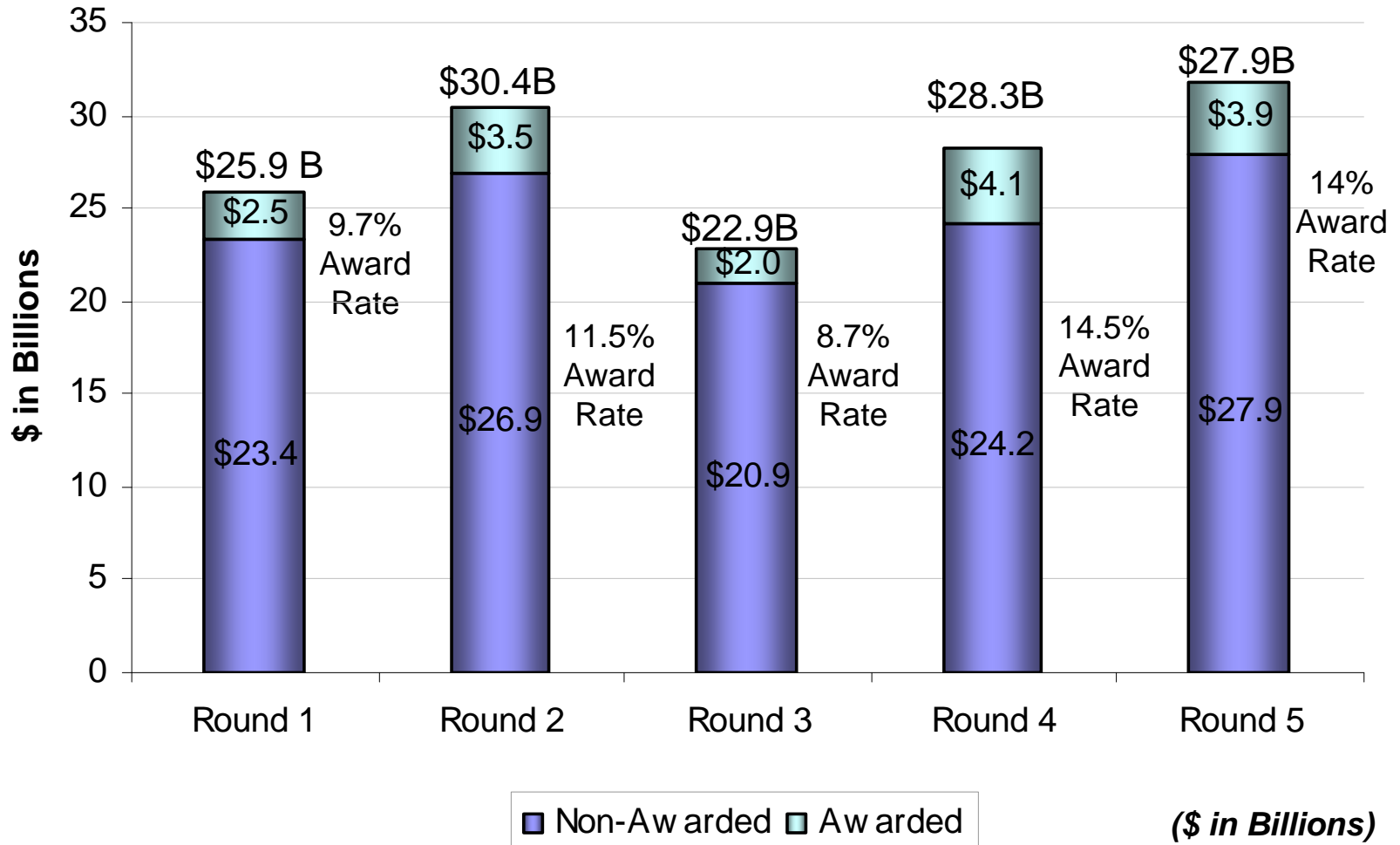


## Award Profile by Entity Type



**\*Please note that the number of allocatees represented in this chart does not total 61, since some allocatees are classified in more than one entity type category (e.g. some CDFIs are also counted as non-profits; some banks are also counted as publicly traded entities) and some allocatees do not fall under any of the categories identified.**

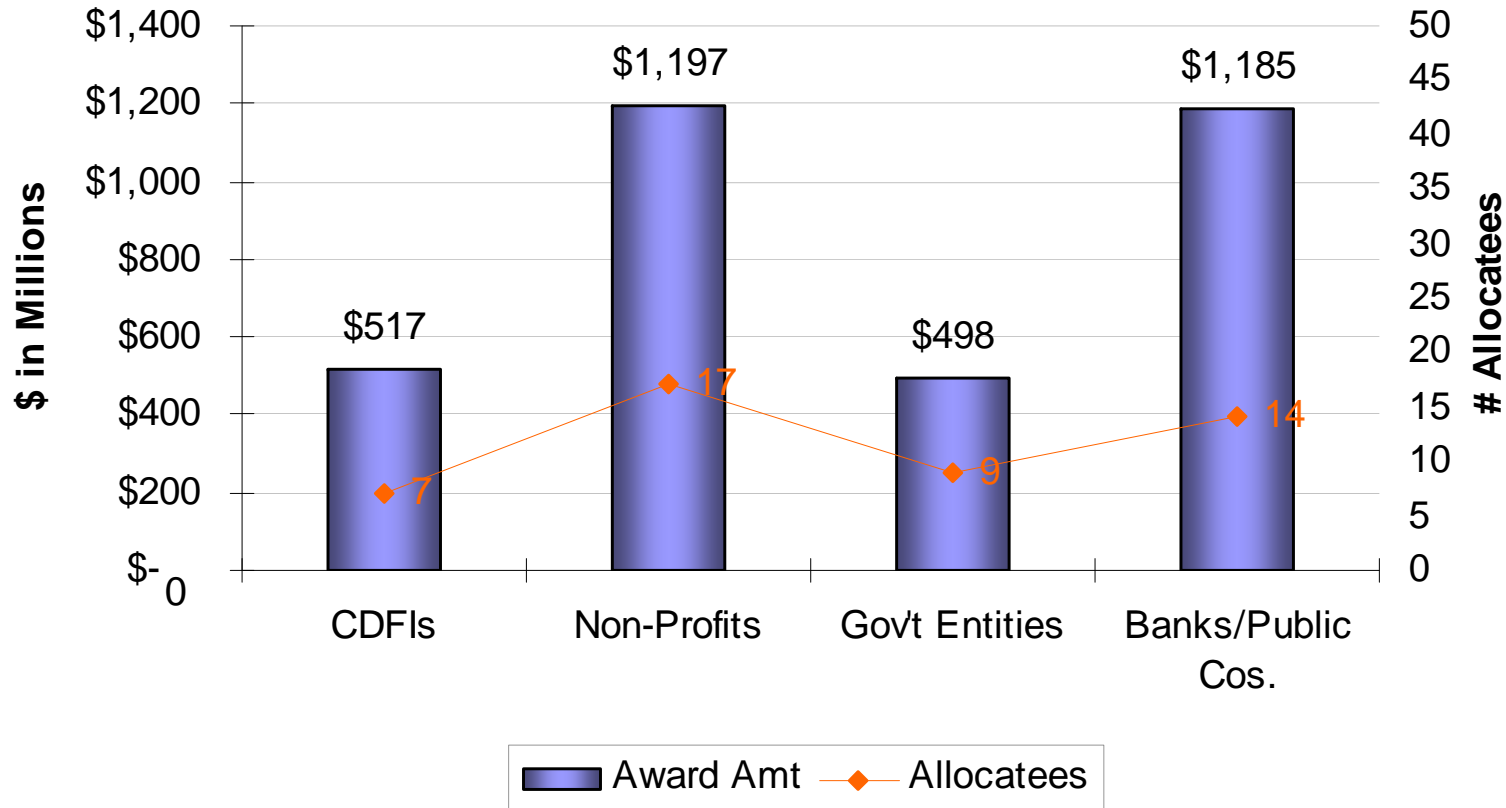
# \$ Requested/\$ Awarded



# Fifth Round Allocatees\*



## Award Amount by Entity Type



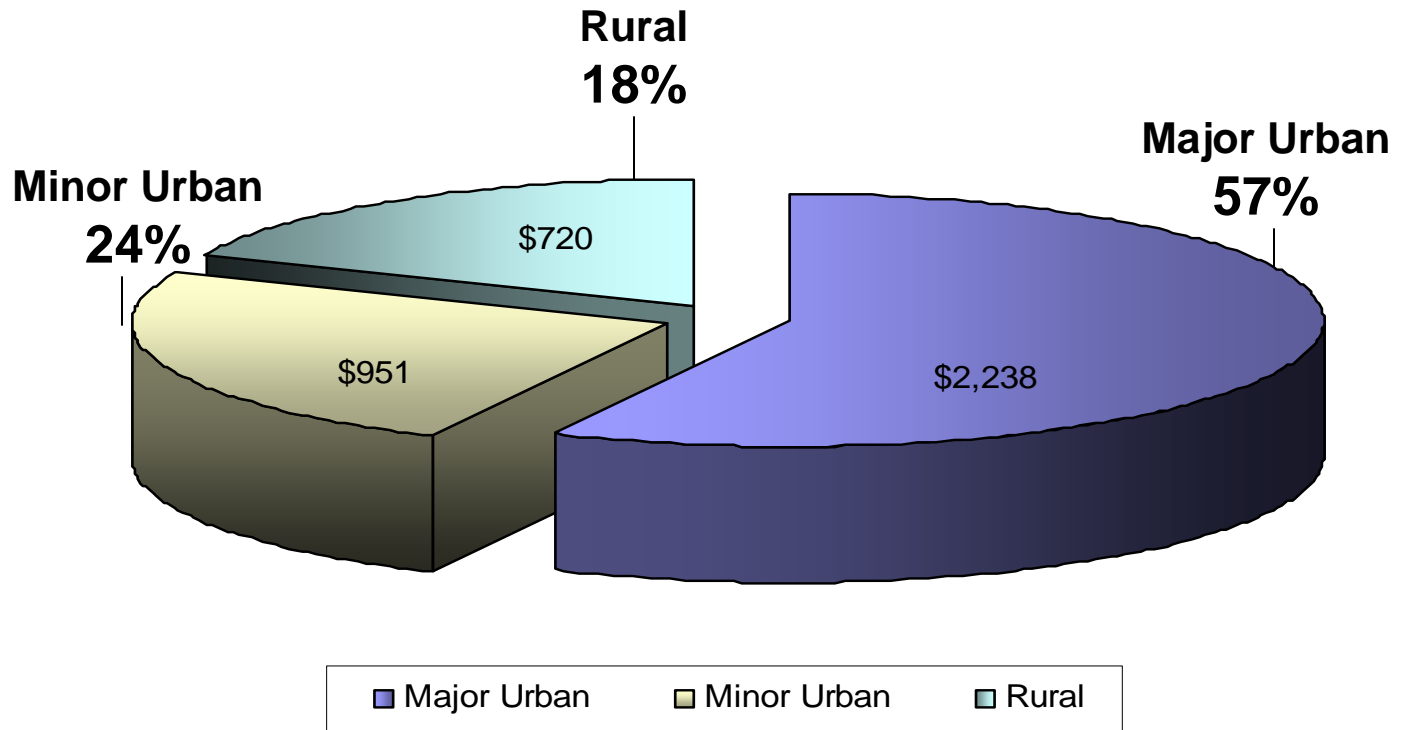
*\*Please note that the allocation amount represented in this chart does not total \$4.1 billion awarded, since some allocatees are classified in more than one entity type category (e.g. some CDFIs are also counted as non-profits; some banks are also counted as publicly traded entities) and some allocatees do not fall under any of the categories identified.*



# Market Served (5<sup>th</sup> Round Allocatees)

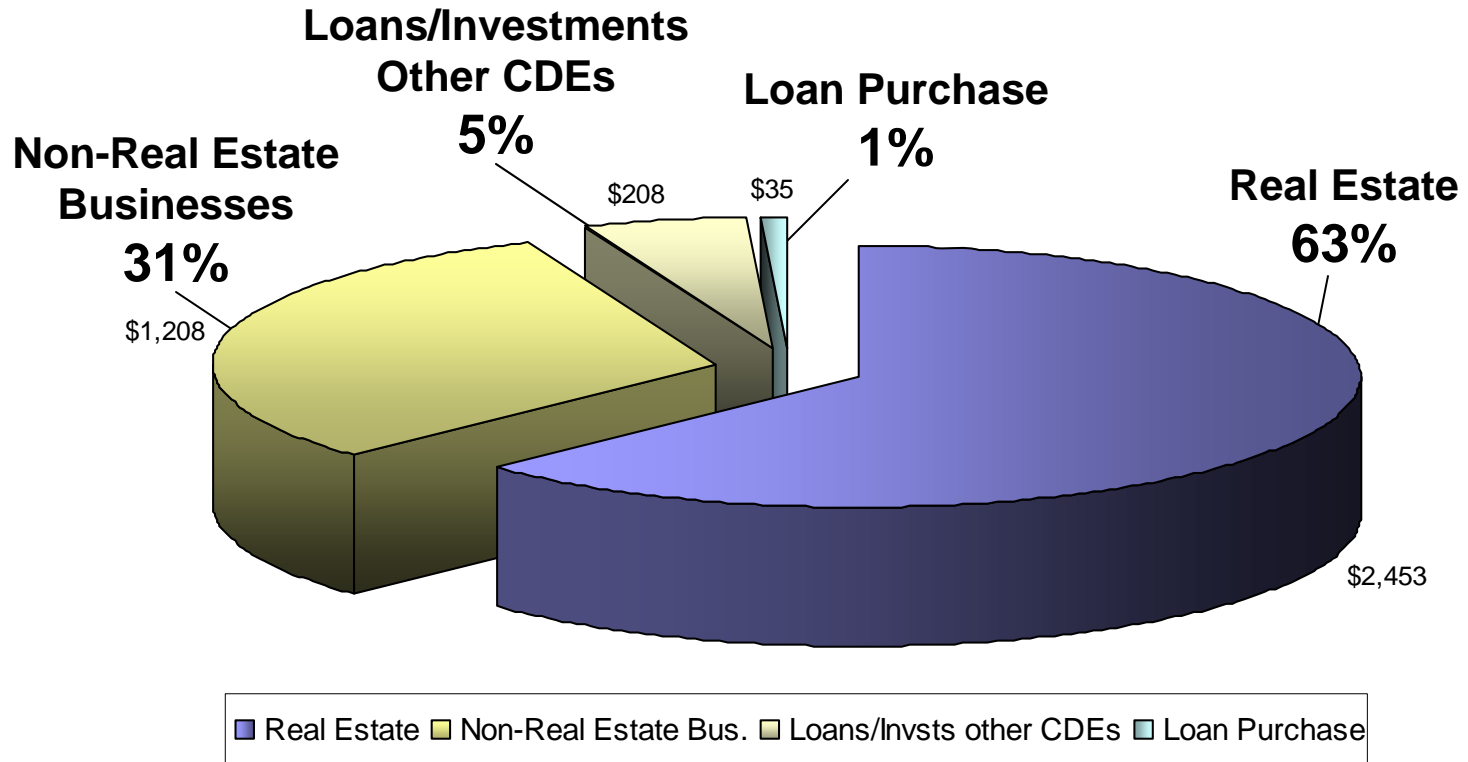


## Estimated Use of NMTC Fifth Round



(\$ in Millions)

# Estimated Activities (5<sup>th</sup> Round Allocatees)



*(\$ in Millions)*

- All 61 allocatees have committed to achieve certain programmatic goals above and beyond what is minimally required by statute and regulation.
- Fifty-two of the 61 allocatees indicated that 100% of their investment dollars would be made either in the form of equity, or in the form of debt that is at least 50% below market and/or is characterized by multiple concessionary features.
- All 61 of the allocatees indicated that they would invest more than the minimally required 85% of QEI dollars into qualified low-income community investments.
  - 49 of the 61 allocatees indicated that at least 97% of their Quality Equity Investment (QEI) dollars would be provided as qualified low-income community investments.
  - At least \$501 million above and beyond what is minimally required by the NMTC Program will be invested in low-income communities.

- Over \$9 billion in QEIs have been made into CDEs that received awards under the first four allocation rounds.
  - This represents over 75% of the \$12.1 billion allocated under those first three allocation rounds.
- Through FY 2006, awardees have reported making over \$5.4 billion of NMTC loans and investments into QLICs
  - Preliminary data indicates that:
    - \$3.7 billion has been invested in real estate, helping to develop or rehabilitate over 46 million square feet of real estate in LICs and create 146,000 construction jobs.
    - \$1.74 billion has been invested in support of operating businesses in LICs, helping to create or maintain over 20,000 full time equivalent jobs.

# Sample Activities



- The development of a high-tech business incubator in inner city ***Detroit*** that will provide opportunities for minority and women business owners.
- Investment in a sustainable forest project in ***rural Maine*** that will restore operations to a formerly closed mill, creating 650 new jobs.
- Investment in a minority-owned car dealership in ***Lake Charles, LA*** that suffered damages resulting from Hurricane Rita.
- Purchase of a loan that enabled a female, Native American pharmacist in ***Montana*** to purchase her facility.
- Investment in a commercial airplane parts manufacturer to expand operations and open a new plant, creating 500 new jobs in ***rural Oklahoma***.

# Contact Information



Contact IRS at [new.market.tax.credit@irs.gov](mailto:new.market.tax.credit@irs.gov)

For questions about:

IRS Regulations, Eligibility of possible QLICI activities and

Other tax implications of the program

Visit the Fund's website at [www.cdfifund.gov](http://www.cdfifund.gov)

**Contact the Fund directly:**

Program Support

Ph: (202) 622-6355 (option 3)

Fax: (202) 622-7754

Email: [cdfihelp@cdfi.treas.gov](mailto:cdfihelp@cdfi.treas.gov)

IT Support

Ph: (202) 622-2455

Email: [ithelpdesk@cdfi.treas.gov](mailto:ithelpdesk@cdfi.treas.gov)