**New Markets Tax Credit (NMTC) Program**

**A Comprehensive Guide for CDFIs and Community Developers**

**Executive Summary**

This guide provides an in-depth overview of the New Markets Tax Credit (NMTC) program, including recent legislative updates, program mechanics, and best practices for Community Development Financial Institutions (CDFIs) and project sponsors. The NMTC program remains one of the federal government's most effective tools for driving private capital into low-income communities, financing community facilities, businesses, and mixed-use developments that might otherwise lack access to conventional financing.

**Part I: NMTC Program Overview**

**Program Background and Purpose**

The New Markets Tax Credit program was established by Congress in 2000 as part of the Community Renewal Tax Relief Act. The program is designed to incentivize community development and economic growth through the use of federal tax credits that attract private investment to distressed communities.

Key facts:

* Administered by the CDFI Fund at the U.S. Department of the Treasury
* Has allocated over $71 billion in tax credit authority through 2024
* Responsible for creating or retaining an estimated 830,000+ jobs since inception
* Financed over 7,000 businesses and community facilities in low-income areas

**Program Extension and Recent Updates**

**2024 Program Extension** The NMTC program received a two-year extension through December 31, 2025, as part of the Consolidated Appropriations Act passed in December 2023. Key updates include:

* Annual allocation authority of $5 billion for both 2024 and 2025 calendar years
* Maintained the same Qualified Census Tract eligibility criteria (poverty rate of at least 20% or median family income not exceeding 80% of area median)
* Continued priority for investments in rural areas (20% minimum allocation)

**Recent Administrative Updates**

* Enhanced reporting requirements for Community Development Entities (CDEs) regarding job creation metrics
* Updated compliance monitoring systems with new AMIS portal functionality
* Clarified guidance on qualifying business types and refinancing transactions
* Increased emphasis on community impact and outcomes measurement

**Basic NMTC Mechanics**

The NMTC program operates through a competitive application process with the following key components:

1. **Application and Allocation**
   * CDFIs and other eligible entities apply to become certified as Community Development Entities (CDEs)
   * CDEs apply for NMTC allocation authority from the CDFI Fund
   * Treasury awards tax credit allocation authority to selected CDEs
2. **Investment Structure**
   * CDEs use their allocation authority to raise capital from investors (typically banks, insurance companies, or corporate investors)
   * Investors receive tax credits worth 39% of their investment, claimed over a seven-year period (5% for years 1-3, 6% for years 4-7)
   * CDEs use investor capital to make Qualified Low-Income Community Investments (QLICIs) in eligible projects and businesses
3. **Compliance Period**
   * Seven-year compliance period during which the project/business must maintain eligibility
   * CDE must maintain compliance with program requirements or risk recapture of tax credits
   * After seven years, investors have received their full tax credit benefit, and exit strategies are implemented

**Part II: NMTC Eligibility and Qualification**

**Qualified Low-Income Community (QLIC) Requirements**

For a project to qualify for NMTC financing, it must be located in a QLIC, defined as:

* Census tracts with poverty rates of at least 20%, OR
* Census tracts with median family income not exceeding 80% of area median income, OR
* Designated "Targeted Populations" with demonstrable lack of access to capital

**Higher Distress Criteria** Projects in areas with "higher distress" receive priority consideration:

* Poverty rates ≥ 30%
* Median income ≤ 60% of area median
* Unemployment rates ≥ 1.5x national average
* Non-metropolitan counties
* Brownfield sites, HOPE VI redevelopment areas, or Federal Native Areas

**Qualified Active Low-Income Community Business (QALICB) Requirements**

The entity receiving NMTC investment must qualify as a QALICB by meeting these requirements:

1. **Location Test**:
   * At least 50% of gross income derived from business in QLIC
   * At least 40% of tangible property located in QLIC
   * At least 40% of services performed in QLIC
2. **Business Type Limitations**:
   * Cannot be a "sin business" (golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack, gambling facility, or liquor store)
   * Cannot primarily hold intangibles or be a residential rental business
   * Limited non-qualified financial property (less than 5% of assets can be held as financial instruments)
3. **Operational Requirements**:
   * Must be actively conducting operations
   * Cannot be in lease-back arrangement with investor or related parties

**Typical NMTC Project Types**

The NMTC program has successfully financed various project types, including:

1. **Community Facilities**:
   * Federally Qualified Health Centers (FQHCs)
   * Charter schools and educational facilities
   * Social service facilities
   * Community centers and recreational facilities
   * Arts and cultural centers
2. **Commercial Real Estate**:
   * Grocery stores and food access projects in food deserts
   * Mixed-use developments with commercial components
   * Office space for non-profit organizations
   * Industrial and manufacturing facilities
3. **Operating Businesses**:
   * Manufacturing companies
   * Healthcare providers
   * Technology businesses in distressed areas
   * Small business incubators

**Part III: NMTC Transaction Structure**

**Standard NMTC Structure Components**

A typical NMTC transaction involves multiple entities and a complex structure:

1. **Investment Fund**:
   * Created by the tax credit investor (usually a bank or institutional investor)
   * Capitalized with investor equity and often a leverage loan
2. **CDE (Community Development Entity)**:
   * Recipient of NMTC allocation from Treasury
   * Issues qualified equity investments (QEIs) to Investment Fund
   * Makes qualified low-income community investments (QLICIs) to QALICB
3. **QALICB (Qualified Active Low-Income Community Business)**:
   * Project sponsor/borrower
   * Receives loan proceeds from CDE to fund project
   * Responsible for ongoing compliance with NMTC requirements
4. **Leverage Lender**:
   * Provides loan to Investment Fund as part of capital stack
   * Often an affiliate of the project sponsor, bank, or CDFI

**Leveraged vs. Direct Investment Structures**

**Leveraged Structure** (most common):

* Investor creates Investment Fund that receives both equity from investor and debt from Leverage Lender
* Investment Fund invests 100% as equity into CDE
* CDE makes loans to QALICB (typically A/B loan structure)
* Advantages: Larger tax credit benefit, potential for debt forgiveness at exit

**Direct Investment Structure**:

* Investor invests directly into CDE without leverage component
* Less common but simpler structure
* Used for smaller transactions or when leveraged debt is unavailable
* Advantages: Lower transaction costs, simpler exit

**Typical NMTC Transaction Economics**

**Benefit Calculation**:

* Investor receives 39% tax credit on QEI amount over 7 years
* "Net benefit" to project typically ranges from 18-22% of QEI amount
* Example: $10M NMTC allocation generates approximately $1.8-$2.2M in net benefit to project

**Fee Structure**:

* CDE upfront fees: 2-5% of QEI
* CDE asset management fees: 0.5-1% of QEI annually
* Legal and accounting fees: $300,000-$500,000 for standard transaction
* Minimum transaction size usually $5M+ to justify costs

**Exit Strategy**:

* Most common: Put/call option at end of 7-year compliance period
* Investor "puts" its interest for nominal amount
* Results in forgiveness of B Note (when using leveraged structure)
* Alternative: Refinancing of A Note and repayment of B Note

**Part IV: NMTC Application Process and Timeline**

**CDE Certification Process**

Before applying for NMTC allocation, organizations must be certified as CDEs:

1. **Eligibility Requirements**:
   * Primary mission of serving low-income communities
   * Accountability to residents of low-income communities
   * Legal entity status (corporation or partnership)
2. **Application Process**:
   * Submit CDE certification application through CDFI Fund's AMIS portal
   * Provide organizational documents, mission statement, and board/advisory board information
   * Demonstrate accountability to low-income communities through board representation
3. **Timeline**:
   * Processing typically takes 60-90 days
   * Certification remains valid indefinitely if requirements are maintained

**NMTC Allocation Application**

The annual competitive application process for NMTC allocation:

1. **Application Components**:
   * Business strategy (pipeline, projects, products, markets)
   * Community impact (outcomes, targeting, accountability)
   * Management capacity (experience, asset management)
   * Capitalization strategy (investor commitments, track record)
2. **Competitive Factors**:
   * Prior performance and deployment rate
   * Community impact metrics and tracking systems
   * Innovative uses of allocation
   * Focus on severely distressed communities
   * Rural strategy
3. **Timeline**:
   * NOAA (Notice of Allocation Availability) released annually (typically Q2/Q3)
   * Application deadline approximately 60 days later
   * Awards announced 6-8 months after application deadline

**Closing an NMTC Transaction**

Once allocation is secured, the transaction closing process includes:

1. **Pre-Closing Activities** (3-6 months):
   * Project structuring and financial modeling
   * Securing leverage loan commitments
   * Investor due diligence
   * Site control and entitlements
2. **Closing Process** (60-90 days):
   * Legal documentation preparation
   * CDE and investor approvals
   * Allocation agreement compliance verification
   * Simultaneous closing of all transaction components
3. **Post-Closing Requirements**:
   * Disbursement of funds per construction schedule
   * Initial compliance reporting
   * Asset management systems implementation

**Part V: Compliance and Asset Management**

**NMTC Compliance Requirements**

Maintaining compliance during the 7-year period is critical to avoid tax credit recapture:

1. **Ongoing QALICB Compliance**:
   * Maintain qualified business activity
   * Adhere to location requirements
   * Avoid "substantial modifications" without CDE approval
2. **CDE Reporting Obligations**:
   * Annual CDFI Fund reporting via CIIS/AMIS
   * Transaction-level data reporting
   * Community impact metrics
   * Financial data
3. **Recapture Events**:
   * CDE ceases to be qualified
   * Failure to use substantially all QEI proceeds for QLICIs
   * QEI redeemed or cashed out
   * QALICB ceases to qualify

**Asset Management Best Practices**

Effective asset management is critical for successful NMTC programs:

1. **Portfolio Monitoring Systems**:
   * Regular QALICB financial review (quarterly recommended)
   * Annual compliance certifications
   * Site visits (annual recommended)
   * Community impact data collection
2. **Documentation Management**:
   * Comprehensive compliance manual for each transaction
   * Secure document storage system
   * Clear audit trail for all decisions and modifications
3. **Early Warning Systems**:
   * Financial covenant testing and tracking
   * Regular communication with borrowers
   * Proactive approach to potential issues

**Part VI: Recent Industry Trends and Best Practices**

**Impact Measurement Evolution**

The NMTC industry has significantly advanced its approach to impact measurement:

1. **Standardized Metrics**:
   * Jobs created (direct, indirect, construction)
   * Community services provided (patients served, students educated)
   * Environmental benefits (brownfield remediation, energy efficiency)
   * Food access (USDA-designated food deserts served)
2. **Community Engagement Practices**:
   * Formal community benefits agreements
   * Local hiring requirements (typically 30%+ local hiring targets)
   * Living wage commitments
   * MWBE contracting goals (typically 25%+ of contract value)
3. **Reporting Innovations**:
   * Real-time impact dashboards
   * GIS mapping of investments and outcomes
   * Longitudinal studies of community change
   * Third-party impact verification

**Innovative Transaction Structures**

Recent structural innovations in the NMTC market include:

1. **Twinned Credits**:
   * Combining NMTC with Historic Tax Credits
   * Combining NMTC with Low-Income Housing Tax Credits (commercial portion only)
   * Combining NMTC with Opportunity Zone investments
   * Combining NMTC with Renewable Energy Tax Credits
2. **Small Business Focused Models**:
   * Revolving loan funds within NMTC structure
   * Loan funds with standardized products for businesses under $4M
   * Technical assistance components integrated into NMTC structure
   * "Mini-NMTC" programs for deals under $5M
3. **Capital Stacking**:
   * Strategic use of CDFI Fund's Capital Magnet Fund with NMTC
   * Integration with USDA rural development programs
   * Pairing with HHS community facilities programs
   * Leveraging philanthropy for enhanced community benefits

**Program Permanence Efforts**

Efforts to make the NMTC program permanent continue:

1. **Legislative Proposals**:
   * Multiple bipartisan bills introduced to make NMTC permanent
   * Proposed increases in annual allocation authority to $5-7B
   * Inflation adjustment proposals for allocation amounts
   * AMT relief provisions for NMTC investors
2. **Industry Advocacy**:
   * New Markets Tax Credit Coalition coordinating advocacy efforts
   * Impact data collection to demonstrate program effectiveness
   * Success stories highlighting transformative community projects
   * Bipartisan congressional champions engaged

**Part VII: Case Studies**

**Case Study 1: Rural Healthcare Facility**

**Project Overview**:

* $18M Critical Access Hospital in rural Kentucky
* 30,000 sq. ft. facility with emergency care, primary care, and diagnostic services
* Located in census tract with 32% poverty rate and 125% of national unemployment rate

**NMTC Structure**:

* $15M NMTC allocation from two CDEs
* $4.8M leverage loan from USDA Community Facilities program
* $6.2M leverage loan from project sponsor (capital campaign)
* $4M tax credit equity from national bank

**Community Impact**:

* Created 75 permanent healthcare jobs
* Serving 15,000 patients annually
* Reduced emergency care travel time by 45 minutes
* First new healthcare facility in county in 40 years

**Case Study 2: Manufacturing Expansion**

**Project Overview**:

* $25M expansion of food manufacturing facility in urban area
* 90,000 sq. ft. production facility and warehouse
* Located in census tract with 27% poverty rate in former industrial area

**NMTC Structure**:

* $20M NMTC allocation
* $13M leverage loan from regional bank
* $7M tax credit equity from insurance company investor
* $5M project sponsor equity outside NMTC structure

**Community Impact**:

* Created 110 new production jobs with average wage of $18/hour
* 85% of new hires from low-income communities
* Implemented local hiring program with community