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Financial Institutions May Benefit From Extension of New Markets Tax Credit Program Through 2011

The New Markets Tax Credit (NMTC) program, which offers incentives to make investments or loans in low-income communities, has received a two-year extension under the recently enacted Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010. The program extension offers significant potential opportunities for banks and other financial institutions.

The NMTC program was created in 2000 to encourage investors to provide capital to low-income communities. Through 2009, the US Department of the Treasury (Treasury) awarded $26 billion in allocations to community development entities (CDEs) to support investments, loans, or other assistance to local businesses. Approximately 65 percent of NMTC investment has been used primarily for commercial real estate projects throughout the United States.

Through leveraged financing structures, the NMTC program offers potential subsidies in the range of 10-20 percent of project costs, depending on the size of the project and other variables.

The program expired at the end of 2009 but has now been extended retroactively for 2010 and for an additional year in 2011. For each year, Treasury has an additional $3.5 billion in credit authority to allocate. The allocations are made to CDEs on a competitive basis, with no predetermined allocations by state or locality, population, poverty rates, or other economic indicators.

Key features of the NMTC program are as follows:

- A federal income tax credit is available to an investor who makes a qualified equity investment (QEI) in a CDE that, in turn, makes a qualified low-income community investment (QLICI) in a qualified active low-income business (QALICB).
- The total amount of credits is 39 percent of the QEI and is spread over seven years (five percent in each of the first three years and six percent in each of the next four). The QEI must remain invested for the full seven years.

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- QALICBs include businesses that operate in low-income communities or that serve primarily low-income populations. The development and sale of housing is a qualified business, although the rental of dwelling units is not. There is no requirement that employees of the business be residents of a low-income community.
- Low-income communities include any census tract where the poverty rate is at least 20 percent *or* the median family income is not more than 80 percent of the median for the state or metropolitan area (whichever is greater).

Financial institutions may participate in, and benefit from, the NMTC program in a number of ways, including (1) making equity investments that qualify for the income tax credits, (2) providing the debt capital in a leveraged structure, and (3) sponsoring a CDE that makes QLICIs. Moreover, since such investment or lending activities are targeted to low-income communities, they may also qualify for Community Reinvestment Act credit.

We hope that you have found this advisory useful. If you have additional questions, please contact your Arnold & Porter attorney or:

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