NEW MARKETS TAX CREDIT COALITION

February 6, 2012

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

Dear Bob:

The New Markets Tax Credit Coalition (The Coalition) is a national membership organization made up of community development organizations, investors, public officials and experts in community development and community development finance. The Coalition has a long history with the New Markets Tax Credit (NMTC) that dates back to the original Clinton administration proposal in 1999.

The Coalition is pleased to respond to the Community Development Financial Institutions (CDFI) Fund's solicitation for comments on the New Markets Tax Credit. It is important to note that the New Markets Tax Credit has achieved its intended purpose: attracting private sector capital to low income communities to stimulate economic activity, spur revitalization, create jobs and improve communities.

As you know, enactment of NMTC in December 2000 marked a shift in federal community development policy. Instead of creating a new grant-in-aid program to revitalize distressed urban and rural communities, the NMTC, and the other elements of the bi-partisan Community Renewal Tax Relief Act, relied on tax incentives to the private sector to stimulate economic activity.

There is ample evidence that the NMTC has done just that. According to a recent CDFI Fund report, over the history of the program (2003-2010) about $21 billion has been invested in low income communities through NMTC. The total project cost of businesses financed by NMTC comes to more than $32 billion. The Credit has financed some 1500 businesses that have created over 300,000 jobs, including over 200,000 jobs in the construction industry.

Recently, NMTC activity has accelerated. In 2010 alone, $4.7 billion was invested in low income communities through NMTC with total project cost of businesses financed by the NMTC coming to $9.5 billion. Between 2009 and 2011, annual NMTC investments increased from $3.4 billion to $5.7 billion. That's a 67% increase in investments that spur job growth and economic development in our most economically distressed communities.

In 2010, NMTC investments created 70,000 private sector jobs including almost 38,000 jobs in the beleaguered construction industry. The NMTC provides a bigger "bang for the buck" than many other government programs. Based on revenue estimates generated by the Joint Committee on Taxation (JCT) the NMTC create one job for every $17,000 in revenue lost from the NMTC.

In 2009, Harvard's Kennedy School recognized NMTC as one of its "Top Government Innovations" for its efficient and effective delivery of private investment into distressed communities. As you will read, the NMTC has financed a broad range of businesses and projects in America's low income communities. These range from the Near Eastside Legacy Center in Indianapolis, which will provide house education, recreational and cultural services to thousands of young people in one of the poorest neighborhoods in the country, to Farwest Steel's future fabrication and processing center near the Port of Vancouver which will employ 228 people.

It is also important to note that while the NMTC targets communities in distress, approximately 75% of NMTC activity goes well above and beyond the level of poverty mandated by the statute, delivering private capital to communities that suffer from *extreme* levels of economic distress – including poverty rates of at least 30% or median incomes below 60% of the area median. Over 60% of credit investment impacts communities with an unemployment rate at least 1.5 times the national average.

The legislation that established NMTC provided for $15 billion in credit authority between 2001 and 2007. This long term authorization allowed the government the time necessary to launch and refine the program and gave the community development industry and investors the time to prepare to undertake the NMTC.

Following the expiration of the original authorization legislation, Congress extended NMTC for 2008, 2009, 2010 and 2011. The last extension was enacted in December 2010 as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010. This provided an extension of NMTC for both 2010 and 2011 at $3.5 billion in annual credit authority.

While the Coalition enjoyed the support of both the Bush and Obama Administrations for extension of the NMTC, the lack of a long-term authorization continues to create market inefficiencies and uncertainty that inhibit the NMTC's full potential. <u>The best thing that Congress and the Administration can do to improve the New Markets Tax Credit is to enact a long term or permanent extension of the program.</u>

NMTC expired on December 31, 2011. Absent a near term extension, there is great potential that private capital will go elsewhere. Indeed, we believe that one of the reasons for the dramatic increase in NMTC investments in 2011 was the two year extension of the NMTC enacted in December, 2010.

Investors take cues from Congress and the run up in NMTC investment activity was aided by clear signals from Capitol Hill of the intention to extend the NMTC. While the final extension legislation was not enacted until December 2010, the House passed its version of tax extender legislation (The Tax Extender Act of 2009) nearly a year earlier in December 2009. The message to the investor market was clear: an NMTC extension was on the way. Without this level of certainty, the stage would not have been set for the substantial increase in NMTC investments in 2011.

A long-term or permanent authorization should also include a provision on the Alternative Minimum Tax (AMT) that exempts NMTC investments thus putting the NMTC on par with other similar tax credits including Low Income Housing and Historic Tax Credits. Without this incentive, NMTC is at a disadvantage in the investor marketplace. Without both AMT and a long-term extension, it will be difficult to broaden the credit's investor base beyond the core investors comprising large CRA motivated banks. More investors will increase competition for Credits, resulting in better pricing and more subsidies going to qualified businesses.

1. Identifying and Targeting NMTC Eligible Low-Income Communities and Areas of Higher Distress

1a) Should the CDFI Fund consider using different standards or methodologies for determining whether census tracts meet the statutory definition of low-income communities?

■ The Coalition recommends that the CDFI Fund clarify the acceptable sources of poverty and income data by providing additional tools beyond the CDFI Fund's mapping system to verify the eligibility of a census tract. The CDFI Fund's Geocoded mapping system provides a common source of income and poverty data for CDEs, investors and other program participants to determine the eligibility of a census tract based on the decennial census. However, when the CDFI Fund's mapping system cannot locate a census tract based on an address, or a lack of address in some cases (a low population rural area or downtown), some CDEs have turned to other mapping systems to identify the eligibility of an area but without verification from the CDFI Fund's system, there is always the risk that the tract could be deemed ineligible and investors are less likely to invest.

■ The Coalition recommends that the CDFI Fund clarify that the individual poverty rate is the standard it employs to determine the eligibility of census tracks. It is important to note that the individual poverty rate is the standard for most federal community development programs because economists consider it a more definitive and accurate count of the number of people in a community actually living in poverty. The family poverty rate excludes unrelated adult persons living together and by doing so severely underestimates the number of persons living in poverty. Using the family poverty measure would exclude 25% of the nearly 34 million people living in poverty in the United States, mainly by undercounting unrelated people who live together, most of whom are low income and elderly.

■ The Coalition encourages the CDFI Fund to utilize American Community Survey (ACS) data with the decennial census data as a way of maintaining timely and current poverty and income data. Over the past decade, the country has experienced a significant socio-economic reshuffling, particularly in urban areas, and these changes argue for a more regular update of geocoded census tract data. The Coalition recommends that the CDFI Fund update the data in its geocoded mapping system every 5 years so CDEs and investors may identify census tracts that are NMTC eligible based on current poverty and income indicators. This will enable CDEs to effectively respond to the needs of businesses and communities impacted by a recession or a sudden and severe economic downturn. To ensure a smooth transition and predictability for CDEs, investors and other program participants, the Coalition recommends that the CDFI Fund institute a standard transition period that would guide and instruct CDEs when census data is updated.

1b) In the allocation award process, should the CDFI Fund increase the commitment percentage from 75% of investments made in Areas of Higher Distress in order to receive the highest Community Impact score?

■ The Coalition recommends that the CDFI Fund continue to provide additional points to CDE applicants that commit to invest at least 75% of their QLICI dollars in Areas of Higher Distress but not to increase the required percentage. Because of the highly competitive nature of the program, most CDE applicants commit to target at least 75% of their investments to Areas of Higher Distress. Successful CDE applicants signed allocation agreements holding them to this minimum targeting commitment. To our knowledge, few if any other federal program delivers such a high percentage of investment to highly distressed communities.

It is important to note that 100% of all NMTC investments are made in low income communities – communities where at least 20% of the population lives in poverty or where incomes do not exceed 80% of the area median income. The NMTC statute intentionally targets NMTC investments to low-income communities that have historically been overlooked by conventional investors and lenders. The Coalition is concerned that qualified businesses with the potential to create jobs in a NMTC qualified census tract but not an Area of High Distress will be overlooked if CDEs are encouraged to place an even higher percentage of their investment dollars in Areas of High Distress as defined by the CDFI Fund.

1c) Should the CDFI Fund include additional distress indicators, alter or eliminate any existing indicators?

■ The Coalition recommends adding the following indicators of economic distress to the list posted annually in the NMTC allocation application:

- Educationally Underserved or Disadvantages Areas – The Department of Education's maintains a No Child Left Behind database with information on failing schools across the country. This indicator could be used by a CDE to the extent that the CDE's investments will result in the support of education related services.
- Base Realignment and Closure (BRAC) Property – Since 1988, the Office for Economic Adjustment (OEA) within the Department of Defense has identified more than 300 BRAC properties – military installations to be closed or realigned. In 2005, 39 sites were added to the BRAC list, 16 of which are located in NMTC qualified census tracts. The OEA estimates that over 108,000 direct jobs have/or will be lost in these 39 BRAC communities with 64,478 of the job losses in NMTC qualified census tracts.

2. Treatment of Certain Businesses

2a) Are there certain types of businesses, other than those currently banned, that should be discouraged or barred from receiving NMTC investments?

2b) Should the CDFI Fund provide additional opportunities in the allocation award process for applicants to score more highly by committing to invest in certain business types over others (e.g., small business or rural investment, operating businesses vs. real estate projects, etc.)?

■ The Coalition opposes any additional limitation on the types of businesses financed under the NMTC and the Coalition does not support providing allocation preferences for specific business activities or sectors. The purpose of the NMTC is to direct private sector capital to low-income communities to stimulate economic activity, spur revitalization, and create jobs. The NMTC was designed as a flexible financing tool to accommodate local community and business needs. According to CDFI Fund data more than 1,500 businesses, varying in size, scope and location, have received NMTC financing since the program was launched. What these businesses have in common is that they are located in the low-income communities and that the vast majority are located in the most economically distressed communities in the country. NMTC financed businesses have a profound impact in communities. They provide an important community service by creating jobs and business opportunities. The purpose of NMTC is to move capital to communities left out the economic mainstream and in our view any measure that tilts

NMTC investing toward a certain type of business or business sector will dampen the ability of the NMTC to respond to individual communities and business financing needs.

> ***2c) Are there specific administrative or regulatory changes that would facilitate the financing of specific types of businesses while preserving public policy objectives and safeguards?***

■ The Coalition continues to recommend that the CDFI Fund and Treasury adopt rules to facilitate more NMTC investing in operating businesses. The Coalition has recommended that the Internal Revenue Service (IRS), provide safe harbor protection for any CDE specifically organized to make QLICIs in operating businesses. The Coalition uses the term 'operating business' to refer to a non-real estate business that makes a good or provides a service.

The Coalition's safe harbor proposal is designed to address investor concerns about the recapture risk associated with investing in CDEs that provide flexible debt and equity financing to operating businesses. The 7-year term of the NMTC coupled with reinvestment and 'substantially all' requirement are the principal barriers that prevent more NMTC investment in operating businesses. Investors are well aware of the severe recapture penalties that are triggered if a CDE falls short of its 'substantially all' requirements at any point during the 7-year compliance period. As a result, investors seek NMTC investment opportunities with CDEs that can guarantee that a Qualified Equity Investment (QEI) will remain fully invested in a QLICI for the full 7-year term of the NMTC, thus limiting a CDE's ability to offer the flexible financing products that many operating businesses need and are difficult to secure in the current lending environment.

The Coalition proposes a 'safe harbor' for investments made in CDEs investing in operating businesses because it would directly address this concern by providing a safety net that investors can rely on if and when a CDE receives a return on investment that for some reason it cannot re-invest in another operating business. In order to take advantage of the safe harbor protection, a CDE would have to:

1) Satisfy the 'substantially all' test as defined in paragraph 1.45D-1(c)(5), with the initial deployment of the Qualified Equity Investment (QEI) into one or more (Qualified Low Income Community Investments (QLICIs) made in one or more Qualified Active Low Income Community Businesses (QALICBs) as long as the business was established for a purpose other than the development, management, or leasing of a real estate project or projects; and

2) Any amounts received by the CDE as a return of capital, equity or principal with respect to such a QLICI must either be reinvested in another qualified non-real estate business or retained by the CDE for the remaining term of the 7-year credit period.

To implement this safe harbor, the Coalition recommends that the CDFI Fund amend its allocation agreement to ensure that any CDE using the safe harbor be required to make a reasonable effort to re-deploy any principal returned to the CDE within the regulatory period and present evidence of such effort. Existing IRS anti-abuse provisions would also be applied to any CDE transactions. If a CDE failed to satisfy either of proposed safe harbor tests, the CDE would be subject to the remedies set forth in its allocation agreement, including disbarment from receiving further NMTC allocations, but the investor **would not** be subject to recapture. We believe this safe harbor protection would ease current investor fears and encourage investors to make QEIs in experienced CDEs with a business plan in place and a track record of lending and/or investing in operating businesses in low income communities.

The Coalition provided additional details on the safe harbor proposal in the letter submitted to the IRS on September 8, 2011, in response the proposed modification of the NMTC regulations designed to encourage investment in non-real estate businesses.

3. Community Accountability

3a) Should the CDFI Fund increase the community accountability standards for an entity to qualify as a CDE?

■ Yes. The Coalition recommends that the CDFI Fund increase the percentage of Low-Income Community Representatives required on a CDE's board (governing or advisory) from 20% to 40% in order to encourage additional community engagement. The Coalition suggests that any changes made to the community accountability requirements of a CDE be made in the CDE certification application rather than through the NMTC allocation application. The Coalition recommends that any changes to this requirement be applied prospectively, or applied along with reasonable transition period in place to provide existing CDEs with time to adjust their boards as needed.

3b) Should some minimum number of Low Income Community representatives on a CDE's board be locally base?

■ The Coalition opposes requiring a CDE to have locally based board members serve on a governing or advisory board. Such a requirement would not guarantee community accountability and could have unintended negative consequences, especially for multi-state and national CDEs that finance a significant percentage of the NMTC transactions each year.

3c) Should CDE community accountability standards differ for CDEs depending on whether they use governing or advisory boards to demonstrate accountability?

■ The Coalition believes the community accountability thresholds should be the same for all CDEs regardless of whether the CDE uses a governing or advisory board to meet the accountability requirements.

3d) Should the CDE be required to have Low-Income Community Representatives approve of investments made by the CDE?

■ It is important to note that the NMTC allocation agreement is a contract between the Federal Government and the CDE allocatee which clearly assigns the CDE with the responsibility to approve QLICIs. Therefore, a CDE's governing board or other officers should maintain final approval of all NMTC investment decisions and be held accountable by the CDFI Fund and investors. The Coalition believes that Low-Income Community Representatives on a CDE's board, whether governing or advisory, should have input on all investment under consideration and the potential community impacts of such investments to ensure that investments meet the goals set forth in the CDE's allocation application and is in accordance with the allocation agreement. However, while a CDE can elect to have Low Income Representatives serve on its governing board a CDEs should ***not*** be required to do so.

3e) Should a CDE's activities be required to be coordinated with community stakeholders? If so, how should this coordination be conducted and demonstrated?

■ The Coalition does not support placing any additional coordination requirements on a CDE and urges the CDFI Fund to consider the cost associated with placing additional requirements on a CDE. There are ample safeguards already in place that ensure that a CDE's activities are coordinated with and reflect the interest of community stakeholders. In fact, the allocation application currently grants points to a CDE that commits to investing in state or local economic zones, state Enterprise Zones or other state/local programs targeted towards "particularly economically distressed communities" all of which involve a community plan as well as community participation.

3f) Should the CDFI Fund implement measures to increase the transparency of CDE activities?

■ The Coalition believes the CDFI Fund has the systems in place to ensure CDE compliance and there is no need to require additional reporting to increase transparency. The CDFI Fund holds CDEs to a high level of transparency by requiring timely reports on investments as well as transactions. The CDFI Fund's definition of "*control*" ensures that a CDE's governing board and/or controlling entity maintains overall *control* of investment decisions, allocation agreement compliance, and day-to-day management of the CDE. CDEs report annually on all NMTC transactions (CIIS) and also certify CDE compliance, including compliance with community accountability requirements. CDEs are subject to site visit reviews by the CDFI Fund and most investors require third-party verification reports to document a CDE's ongoing compliance with program requirements to guard against recapture.

The competitive nature of the NMTC allocation process provides sufficient incentives to encourage CDEs to work with local communities to ensure that NMTC investments address the needs of the low-income community being served. A CDE is required to describe how it intends to work with the low income communities where it invests. In addition, allocation agreements are drafted to ensure that CDE allocatees adhere to commitments made in the allocation application. CDEs are private entities and as such should not be required to open meetings or publish minutes from such proceedings. Such requirements could severely discourage investors from participating or investing in CDEs since they are already subject to recapture and loss of tax credits.

3g) Should CDE community accountability requirements differ for allocatee CDEs and non-allocatee CDEs?

■ The Coalition believes the community accountability thresholds should be the same for all CDEs regardless of whether the CDE is an allocatee, a sub-allocatee, or a non-allocatee.

4. Transaction Costs

4a) Should there be greater disclosure of (and perhaps limitations on) the fees and other sources of compensation and profits that NMTC applicants propose and NMTC allocatees and their affiliates charge to or receive from the borrowers, investors or other parties involved in NMTC transactions?

4b) Should such information be made available by applicants and allocatees directly or through the CDFI Fund to the public or remain excluded from disclosure as proprietary business information?

4c) Should the CDFI Fund provide an opportunity for CDEs that commit to limit fee and other forms of compensation to earn a higher score in the allocation award process? If so, please provide specific standards that could be used.

4d) Are there specific administrative or regulatory changes that would reduce transaction costs while preserving public policy objectives and safeguards?

■ The Coalition recommends that the CDFI Fund, in conjunction with the IRS and the Office of Tax Policy, convene a NMTC advisory group to include a representative cross-section of CDEs, investors, and other NMTC professionals to discuss the costs associated with executing a NMTC business strategy. An advisory group of NMTC professionals could be a valuable resource to the Treasury Department's NMTC team in helping to address the questions on fees and compensation and where possible develop industry accepted practices and standards for NMTC transactions.

■ The Coalition does not support, and sees no need to require CDEs or investors to disclose additional information regarding fees or compensation. The CDFI Fund already collects a significant amount of information from CDEs on fees, fee structures, compensation, and how the benefits of the NMTC subsidy are shared.

■ The Coalition encourages the CDFI Fund to work with the IRS to reduce the costs associated with NMTC transactions by clarifying a number of outstanding tax questions that decrease the efficiency of NMTC transactions. The fundamental purpose of the NMTC is to attract private sector capital to economically distressed communities using a federal tax credit as the incentive. Unlike a federal loan guarantee program where the federal government assumes some risk in a transaction, under the NMTC the CDE accepts the responsibility for preparing an allocation application, formulating a business plan, marketing the NMTC to investors, and then deploying qualified investments in low income community businesses. The taxpayer, or qualified equity investor, puts its capital at risk in return for the NMTC. The CDE covers the costs associated with implementing and administering the program and maintaining compliance with the statutory and regulatory requirements governing the NMTC for the entire seven year compliance period. Almost 75% of all NMTC investments are in communities with high levels of economic distress and therefore more difficult to sustain.

We have already mentioned how a long term or permanent extension of the NMTC would provide investors and other industry professionals with more certainty. This change would lead to more efficient and cost effective transactions but it would require Congressional action. However, there are steps that Treasury can take to increase the efficiency of NMTC transactions. For example, Treasury could clarify how several tax provisions – the Economic Substance Doctrine, IRC Section 183, and true debt analysis – apply to a NMTC transaction. Under current practice most investors are advised by counsel to solicit tax opinions on how these provisions apply to **every** transaction – resulting in significant fees that a CDE must cover. Offering clear guidance on how these provisions apply to NMTC will have a salutary effect on the program and result in substantially lower transaction costs.

→ ***Economic Substance Doctrine***: The current misinterpretation of how the Economic Substance Doctrine is applied to a NMTC transaction adds a significant cost to many NMTC transactions. In recent years Congress has become concerned that many taxpayers engage in a transaction simply to secure favorable tax treatment and that while these transactions might meet the technical requirements of the law, the results of such activities were not intended by Congress. The essence of Economic Substance

Doctrine is that taxpayers should only engage in activities for profit and any tax beneficial consequence should be of a secondary nature.

However, Congress has been clear that in cases in which the realization of tax benefits is consistent with Congressional intent, then the tax benefit should not be disallowed under economic substance. Most recently in the Joint Tax Committee's Revenue provisions related to the Affordable Care Act (March 21, 2010, JCX-18-10), the Committee noted in footnote no. 344:

> *"it is not intended that a tax credit (e.g., section 42 (low-income housing credit), section 45 (production tax credit), section 45D (new markets tax credit), section 47 (rehabilitation credit), section 48 (energy credit), etc.) be disallowed in a transaction pursuant to which, in form and substance, a taxpayer makes the type of investment or undertakes the type of activity that the credit was intended to encourage.* "

In short, the doctrine of economic substance does not apply to New Markets Tax Credits.

→ ***IRC Section 183*** **-** Section 183 of the Code is intended to curtail abusive tax shelters by requiring that equity investors enter into business transactions with the expectation that they will secure a profit. Section 183 presents a problem for investors involved in a leveraged transaction that may be largely driven by the NMTC rather than the economics of the deal. Though Section 183 applies only to the activities of individuals and S corporations, the Coalition is requesting that the IRS clarify that section 183 not be applied to NMTC transactions. In light of the recent legislative history we request that IRS issue a notice clarifying that Section 183 not be applied to the NMTC. A similar ruling has already been issued for Low Income Housing Tax Credits.

→ ***True Debt Analysis*** – The cost of NMTC transactions would also be reduced if Treasury could provide clarification regarding the application of true debt analysis to NMTC investments. CDEs have expressed concern, particularly during this time of fast-declining real estate values, that the current true debt analysis is misleading and creates an impediment to closing deals in low-income communities where the appraised value of a property is frequently far below the true development costs. Many CDEs are finding that the appraised value of properties has been impacted by the market drop and that real estate is appraising for less now than what it was just months ago. This is especially the case in low-income communities where NMTC transactions occur because values in these areas are markedly depressed. CDEs are therefore increasingly finding that the sum of the QLICI loans to a real estate QALICB will exceed the appraised value of the assets being financed. Tax counsel for the investors are taking the position that some or all of the QLICI cannot be considered true debt and crafting documents that conform to the true debt analysis often leads to a protracted negotiation adding significant time and considerable cost in legal and accounting fees to a project.

■ The Coalition encourages the CDFI Fund to consider ways to increase the efficiency – and thus reduce the transaction costs – associated with investments involving multiple CDEs and investors. One of the results of the tight private credit market is that NMTC investments are financing a greater share of total project costs. In the Coalition's *2011 NMTC Progress Report,* CDEs indicated an increasing pressure to finance larger share of overall project costs. There is substantial anecdotal evidence that multiple CDEs are joining forces to finance larger investments. In these instances, each CDE makes a separate Qualified

Low Income Community Investment (QLICI), thereby requiring a separate closing and legal and accounting fees.

The Coalition recommends that in instances in which more than one CDE is investing in a project, the participating CDEs be authorized to designate a 'lead CDE', which would accept QLICIs from other participating CDEs for the purpose of making a qualified investment in the NMTC qualified business. The result of this consolidation should be lower transactions cost as the participating CDEs could share legal counsel and share the costs associated with compliance and asset management fees.

5. Evaluation of Financial Products

> ***5a) Should the CDFI Fund use a defined Effective Annual Percentage Rate (EAPR) for purposes of the application and compliance measurement? Should the CDFI Fund alter the flexible rates and terms question to base the scoring preference on a basis point reduction from a market benchmark determined by the CDE (or a standard metric such as LIBOR) instead of a percentage? Should the benchmarks be raised?***

■ The Coalition opposes placing hard and fast benchmarks or metrics against which all CDEs would compare their financial products to market products. In many low income areas, especially in areas of higher distress, the issue is not the cost of capital, but the availability of capital. If there essentially is no market for financing, it is difficult to evaluate a CDE's financial product against a benchmark that does not exist in the community.

■ The Coalition recommends that the CDFI Fund provide more space in the allocation application for CDE applicants to describe how they craft a financing package – using debt and equity if applicable – to provide the level of subsidy needed to make the business or economic development project a success. At present the application is focused almost entirely on how the CDE plans to structure below market debt and a there is focus on how a CDE blends its products to provide patient, below market rate financing structured to meet the needs of a specific business.

> **(b) Are there specific administrative or regulatory changes that would facilitate the provision of specific financial products while preserving public policy objectives and safeguards?**

■ The Coalition recommends that the IRS amend the current definition of control as it applies to the reasonable expectations test in order to facilitate additional equity investing under the NMTC. Under current regulations (§1.45D-1(d)(6)) a CDE that "…reasonably expects, at the time the CDE makes the capital or equity investment in, or loan to, the entity, that the entity will satisfy the requirements to be a qualified active low-income community business [for the term of the investment…]" then the business will continue to be treated as a QALICB even if it falls out of compliance at a later time. This provision permits a CDE, and its investors, to avoid a recapture event if and when a business entity ceases to qualify as a QALICB during the 7-years credit period for reasons that are outside the control of the CDE.

In cases where the CDE has control of the QALICB, the regulations require that the CDE ensure that the business remains a QALICB for the entire 7-year compliance period. If a CDE obtains control of a QALICB at any point during the 7-years compliance period the CDE is required to ensure that the business remain a QALICB for the remainder of the term and the CDE can no longer rely on the reasonable expectation protection it assumed when the initial QALICI was made. Investors are reluctant to allow a CDE to acquire a majority equity interest in a QALICB unless they can be guaranteed that the CDE will be able to exercise meaningful control of the business. This ensures that the CDE will remain in compliance with all requirements of a QALICB and thus, protects the investor from the risk of recapture. Therefore, we recommend that the definition of "control" in (§1.45D-1(d)(6)(ii)(B) be amended to clarify voting and management rights and to read:

> *"Control means, with respect to an entity, control of voting or management rights that enable the CDE to either (i) cause the QALICB to take actions that result in the QALICB failing to remain a QALICB, or (ii) to override or block actions by the QALICB that are necessary to enable the entity to remain a QALICB.*
>
> *(a) The existence of rights in the CDE to remove for cause a managing member of a limited liability company, a general partner of a limited partnership, or majority of directors of a corporation by substituting a new managing member, general partner, or majority of directors with control would not, by itself, be deemed to give the CDE 'control' for purposes of this provision."*

If this change is made to the definition of control, we believe investors would be more inclined to make equity investments in qualified NMTC businesses.

6. Use of Other Federally Subsidized Financing in Conjunction with NMTCs

6a) Should there be any additional restrictions in the allocation award process regarding the use of NMTCs with other sources of federally subsidized financing? If so, are there certain types of federal financing that should be disallowed? Should it matter whether the financing is made as part of the QEI investment (e.g., through the leveraged debt structure) or at the project level?

6b) Assuming that it is appropriate for any other source of federally-subsidized financing to be used in conjunction with NMTC investments, would it be prudent for the CDFI Fund to limit, as part of the allocation process, the overall amount of QEI dollars or project level investments that may be supported with other sources of federal financing?

■ The Coalition does not support limiting or restricting the use of NMTC financing with other sources of federally subsidized financing. The goal of the NMTC is to spur investment in low income communities and the Coalition believes that the statute was intentional in NOT restricting the ability of CDEs to leverage other federal financing tools – as long as the core purpose of the NMTC is not compromised.

■ The NMTC program provides a relatively shallow credit of 39% of QEI. The highly successful LIHTC program provides a much deeper credit of 90% of qualified basis. As long as the NMTC credit remains shallow, there often is a need for additional support or financing to make the business or economic development project viable. Often, the only other financing sources available are publicly subsidized – including federal, state and local. Federal programs including HUD 108 and CDBG, SBA 504 and 7(a), and USDA guarantee programs have been used successfully by CDEs to enhance the impact of a NMTC investment. Like the NMTCs, these federal programs are intended to support businesses and investments in low income and underserved distressed communities. If the CDFI Fund were to limit the ability of

CDEs to leverage other public sector incentives, fewer NMTC projects would be done in Areas of High Distress where private sector lenders are not yet willing to lead.

The many benefits of combining NMTC with other public sector tools include:

- Better underwriting: Private sector underwriting skills are brought to every NMTC project and result in stronger and bettered structured public sector financing. Because the tax credit investor is subordinate to the public sector financing, the investor will apply its underwriting skills to the public sector loan.

- Better rates: Because public sector financing often carries attractive rates, the CDE can offer lower rates to a QALICB. The decreased rate enhances the prospect for the project's success.

- Better community impacts: Because the other federal tools have requirements that beneficially impact a low income community (e.g., providing a living wage), using the NMTC to leverage other public sector tools is a win-win outcome for the community.

- Pump priming: In areas of severe distress, where conventional lenders are not active, the use of public sector financing is essential to begin the investment process.

- More competition: eliminating the ability to use public sector financing with NMTC in distressed areas will substantially reduce the very limited pool of capital in these communities and lead to higher priced private sector debt that no longer needs to worry about the public sector option.

- Increased signs of community support: Using NMTC financing in conjunction with other public sector financing tools ensures additional vetting of the investments by community residents as well as public and private financing partners.

Please consider the following examples of how CDEs have used the NMTC with other *federally-subsidized financing tools.*

NMTC and HUD 108 financing working together:

→ The Taylor County Health Center, in Abilene, Texas, is a public health facility that consolidates and expands services that were distributed among several locations throughout the city, with no single location providing a full range of programs. This single location allows the Health Department to concentrate client services and provide them on a daily basis, rather than a staggered schedule. The $4 million project encloses 20,760 s.f. of formerly vacant land, providing services to low-to moderate-income persons, and is located near other government services on a public transportation line. The center was the first new construction in Abilene's downtown in many years and has had a positive impact on surrounding property values, enhanced the potential for further development and contributed to a richer mix of private and public sector land uses within the central business district that will eventually result in new business development, an expanding tax base and the creation of private sector jobs. The facility brings 50,300 clients annually and 50 staff persons daily to the Central Business District, further promoting the redevelopment of the area.

→Yonkers Recreational Pier, on the Hudson River in Yonkers, New York, is the only turn-of-the 20th century pier still in use on the Hudson and its restoration was an important step in the renewal of the Yonkers waterfront. The restored first-floor pavilion of the pier provides public recreation space and access to the waterfront. The second level holds a 260-seat "five star" restaurant. The total project cost of the renovation was $12 million of which $950,000 came as a HUD Section 108 loan from the City of Yonkers. The renovated pier created 96 jobs that were filled largely by residents from the surrounding low income communities.

NMTC and the Historic Tax Credit working together:

→ NMTC financing twinned with Historic Tax Credit (HTC) financing allowed for the rehabilitation and conversion of a vacant, landmark building in downtown New Orleans into a non-profit community center, police substation, and retail center. The total project cost was $11.7 million and because of the weak commercial market, and the project sponsor's commitment to keeping rents affordable for local nonprofit tenants, the project faced a financing gap of $6.3million. Because the project is a landmark historic property located in the GO Zone it was eligible for the 26% federal HTC resulting in $2.3 million in equity. In addition the project was eligible for state HTC which generated an additional $1.1 million, for total historic tax credit equity of $3.4million. The remaining $2.8 million in project financing was generated by leveraging the federal and state HTC equity into a NMTC structure which covered the remaining financing gap and allowed the project to move forward.

Example of NMTC and SBA financing working together:

→ CDEs can utilize SBA loan guarantee authority to generate new capital sources for small businesses located in our economically distressed communities. This combination helped spark the growth of Xiolink, a provider of managed infrastructure and hosting, collocation and private cloud computing solutions. Xiolink serves both mid-market and enterprise clients around the world and does so out of its headquarters in a low income community in St. Louis. Missouri with median incomes below 70% of area median income and unemployment more than 150% of the national rate. NMTC financing combined with financing made available through an SBA 7A loan Xiolink was able to expand its data center which allowed the company to add jobs and generate additional economic activity in its home base community. The initial expansion attracting nearly $10 million in follow-on capital for its continued expansion and in 2010 Xiolink was honored as a "St. Louis Business of the Year" by Mayor Francis Slay and the St. Louis Development Corporation.

NMTC and USDA financing working together:

→ GAME Equipment is a manufacturer of harvesting equipment located in Napoleonville, Louisiana a rural community with just over 700 resident, a poverty rate of 36% and a 10% unemployment rate. The company needed expansion capital to increase its production in order to meet increased international demand. A CDE stepped in a $2.3 million financing package that included a NMTC investment as well as a USDA guaranteed loan. Being able to attract lower-cost, flexible financing provided through the NMTC and USDA programs allowed the company to increase both its production/exporting capacity and employment by 50%. GAME was recently named Business of the Year for 2011 by the US Department of Agriculture for its impact on the economy of rural Louisiana.

The NMTC Coalition appreciates the opportunity to submit comments and contribute to the CDFI Fund's ongoing efforts to support the work of CDEs and investors using the NMTC to grow businesses and support revitalization efforts in low-income communities across the country.

Sincerely,

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