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Understanding New Markets Tax Credits

HOW THIS INNOVATIVE PROGRAM COULD HELP YOU
BUILD AND GROW TO SERVE COMMUNITIES IN NEED.

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What Are New Markets Tax Credits?

In late 2022, a food bank in the Southeast wanted to expand. In order to aid more families who were suffering from food insecurity, they needed additional room. Their 12,000-square-foot facility served 34 counties but was operating at 565% capacity for refrigerated food, 227% capacity for frozen food and 130% capacity for dry goods. The nonprofit envisioned a 30,000-square-foot

facility that could not only support more food but also provide extra services.

In addition to additional cooler and freezer space, the larger facility would have a commercial kitchen, a volunteer space and a market. They imagined that the facility would be a distribution center and a donation center for food drives. It would also host nutrition and education programs. But donations and grants were not enough to complete the project. They had purchased the property where their



new facility would be constructed, but project costs rapidly increased—leaving them with a gap between what they needed and what they brought in from a capital campaign.

The Regions team alerted the food bank to the federal New Markets Tax Credit (NMTC) Program as a possible source of low-cost gap funding. After walking the organization through the benefits and eligibility requirements, the Regions NMTC team introduced it to consultants specializing in NMTC projects, as well as a community development organization that was actively seeking projects of this nature to finance with its NMTC allocation.

Whether in big cities or rural areas, nonprofits serving low-income communities face unique challenges. While the need for their services only grows, securing financing for capital projects to improve residents’ lives can be arduous.

To help ease the process, the federal NMTC Program offers crucial gap financing for nonprofit organizations operating in low income, underserved communities which are seeking to expand. Activities may span a broad range, including but not limited to:

- ▶ Health care
- ▶ Access to healthy foods
- ▶ Community facilities
- ▶ Early childhood education/charter schools/universities
- ▶ Workforce development training

Since the program began in 2000, more than \$71 billion in NMTC financing has supported thousands of projects nationwide. For borrowers, the benefits can include lower interest rates and flexible and more favorable terms. A subsidy can complete roughly 15% to 20% of a project’s capital stack.

Yet, securing financing through NMTC isn’t automatic. Only certain organizations and projects qualify, and even those who qualify could feel daunted by the process or may even be unaware that the program

exists. How does the program work? Does your organization and project qualify? What support and guidance do you need to move forward? If what you read in this paper interests you, we hope you’ll reach out for a conversation.

NEW MARKETS TAX CREDITS AT A GLANCE

Since 2000, when the program was founded, through 2021*

\$71 billion

Tax credits awarded

938,000

Jobs created or retained

\$8

Private investment generated for every \$1 of federal commitment

76%

Investments that go toward “highly distressed” areas

SUPPORTED CONSTRUCTION

76.9 million

sq. ft. manufacturing

118.3 million

sq. ft. office space

77.1 million

sq. ft. retail space

*Most recent available statistics
Source: CDFI Fund, “New Markets Tax Credit Program Fact Sheet”

How the Program Works

For nonprofit organizations, financing for capital improvements often comes from multiple sources, such as:

- ▶ Bank loans
- ▶ Foundation grants and soft loans
- ▶ Public funding
- ▶ Private donations

The NMTC Program isn't intended to replace these sources, known collectively as a project's "capital stack." But when the capital stack comes up short, NMTC loans can fill the gap, providing that remaining 15% to 20% of funding that enables the project to move forward.

The program is administered by the Community Development Financial Institutions (CDFI) Fund, which is part of the U.S. Department of the Treasury. While the CDFI Fund is the program's ultimate authority, you as the borrower interact mainly with private organizations known as community development entities (CDEs) and investors, such as Regions, that turn tax credits into dollars.

Located around the country, CDEs act as intermediaries for the program. They apply to the CDFI Fund for tax credits, which they use to attract private investors. Then, they typically offer that investment capital in the form of loans to qualifying nonprofit organizations or businesses for their development projects.

CDEs usually serve specific geographic areas and/or support specific missions, such as rural jobs, manufacturing, education, health care or community services. For an organization seeking NMTC financing, it's important to find a CDE with a special interest in your area or in the type of service or benefit you provide.

Investors (usually financial institutions such as Regions) make equity investments in a CDE, for which they receive tax credits equal to 39% of the total qualified equity investment. The CDE can then use the proceeds of the equity investments to provide seven-year



low-cost loans to nonprofits or businesses for projects that align with the CDE’s mission. Investors, like CDEs, decide whether to invest in specific projects based on the extent to which the projects help low-income communities, along with other considerations.

In this win-win scenario, the investor realizes the benefit of the tax credits over a seven-year period; you as the borrower receive a flexible, low-interest-rate loan; and most important, your community benefits from new services, new jobs or both.

Organizations and Communities That Qualify

To qualify for NMTC loans, nonprofits or businesses must serve low-income communities and provide vital services the communities might otherwise be lacking. Among the requirements:

- ▶ At least half of the organization’s income comes from activities in low-income communities.
- ▶ At least 40% of tangible property and services performed are in those communities.
- ▶ The borrower cannot be a government entity.

How are low-income communities defined?

Communities eligible for NMTC projects are identified by census tract data, searchable using this mapping tool: cdfifund.gov/cims. Generally, though, the poverty rate must be at least 20%, or the median family income must be 80% or less of the area median income (AMI) for the community where the project is located.

Beyond those baseline qualifications, special preference is given to “highly distressed” areas. These may include communities with even higher poverty rates, lower incomes as compared to the local AMI, high unemployment rates and compounding factors such as:

- | | |
|--|---|
| <ul style="list-style-type: none"> ▶ Rural areas ▶ Food deserts ▶ FEMA disaster sites | <ul style="list-style-type: none"> ▶ Medically underserved areas ▶ Brownfields (contaminated areas) |
|--|---|

What projects aren’t allowed?

Even if they might provide jobs or benefits to low-income communities, organizations won’t qualify for NMTC loans if their activities comprise:

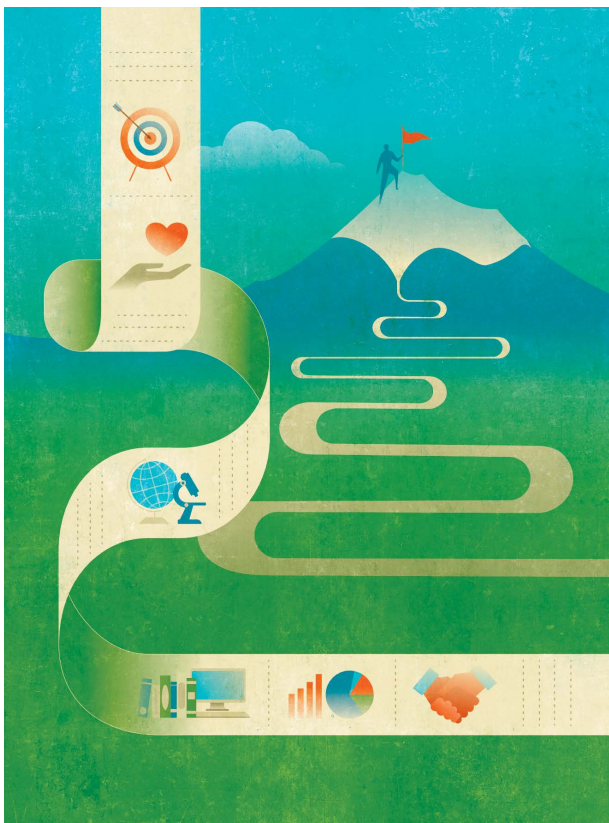
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| <ul style="list-style-type: none"> ▶ Residential rental properties* ▶ Racetracks or gambling facilities ▶ Golf courses or country clubs | <ul style="list-style-type: none"> ▶ Liquor stores ▶ Massage or tanning businesses ▶ Certain farming businesses |
|--|--|

*Mixed-use projects are allowed, but at least 20% of rent must come from commercial tenants.

Navigating a Competitive Process

The CDFI Fund issues about \$5 billion of NMTC allocation to CDEs nationally each year. To gain a share of those credits, CDEs must compete with one another, and the competition is stiff—only about half (or fewer) of registered CDEs are awarded credits in a given year.

As such, CDEs work hard to find and support projects that align closely with their own missions, and that can have direct, measurable impact on communities. That translates into a competitive process for organizations seeking NMTC financing, since CDEs tend to be highly selective. Finding the right fit for your project may require speaking with several CDEs.



Creating a Project Summary

Unlike traditional loan applications that mainly ask for hard financial data, the application process for CDEs is typically more subjective. While requirements vary from one CDE to the next, most will require a detailed project summary including your organization's history and goals and specifics of the project you're pursuing.

NMTC professionals can help you through the application process. That said, you can help your case by ensuring your project has the qualities necessary to improve its chances of acceptance. A project may be more likely to succeed if you can demonstrate:

- ▶ **Immediate and measurable impact**
If the project moves forward, will communities quickly receive tangible benefits? If the proposed project moves forward, how many low-income community members are likely to benefit?
- ▶ **Shovel readiness**
To help ensure that projects can maximize benefit for communities, CDEs look for projects for which the other sources within the capital stack are already lined up, and that have already satisfied zoning, construction and other permitting requirements.
- ▶ **A true need**
Organizations may increase their chances by demonstrating not only that they are doing good works, but that they are providing a service that the community might otherwise lack access to.
- ▶ **Your group's qualifications**
Why is your organization uniquely qualified to provide this service to this community?
- ▶ **A broad canvas**
If the proposed project moves forward, how many low-income community members are likely to benefit?

How Regions Can Help

While the NMTC program is intended to provide the last piece of financing for your project, don't wait until the last minute to start planning. A good place to start is by having a conversation with Regions' NMTC professionals. Even if your project is still in the conceptual phase and months or years from breaking ground, we can help you evaluate whether your project might qualify and walk you through the NMTC benefits and requirements.

If so, we can also introduce you to consultants and attorneys who specialize in the program. Together with these professionals, we can help direct you to CDEs and help to advocate for your project. As the investor, Regions would also actively coordinate on the structuring and closing of your NMTC transactions and, in some cases, Regions may also provide traditional loan financing, in addition to investing through the NMTC Program.

While the New Markets Tax Credit Program won't apply to every organization or project, in the right situations it can provide an essential boost to a development project, helping you fulfill your underlying mission of helping communities.

If you'd like more information, we welcome you to reach out to our team.

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