

## **Changes to the New Markets Tax Credit to Facilitate Investment in Small Businesses**

### **Background on the New Markets Tax Credit**

The New Markets Tax Credit (NMTC) spurs investment of private sector capital in distressed communities by providing a tax credit for taxpayers who make qualified equity investments (QEIs) in designated Community Development Entities (CDEs).

The credit provided to the investor totals 39 percent of the investment in a CDE and is claimed over a seven-year credit allowance period. In each of the first three years, the investor receives a credit equal to five percent of the total amount paid for the stock or capital interest at the time of purchase. For the final four years, the value of the credit is six percent annually. Investors may not redeem their investments in CDEs prior to the conclusion of the seven-year period.

The FY13 Budget proposal would authorize two more rounds of NMTC allocations (for 2012 and 2013), with an allocation amount of \$5.0 billion for each round.

### **Changes to the New Markets Tax Credit to encourage investment in small business**

Generally, a CDE must invest substantially all its assets in low-income community investments for the 7-year credit period. In addition, a CDE that receives returns on investments must reinvest those proceeds within 12 months into qualified low-income community investments during the 7-year credit period or risk losing the entire credit. These requirements make real estate projects a safer investment, because real estate does not move out of a low-income community, and loans for real estate can extend through the end of the 7-year credit period. With non-real estate investments, the risk is higher that the business might move, and working capital and equipment loans to non-real estate businesses are ordinarily amortizing loans with a term of five years or less. Therefore, the majority of new markets tax credit investments to date relate to real estate projects.

To facilitate investment in non-real estate businesses, such as manufacturing businesses, landscaping businesses, restaurants, and alternative energy companies, Treasury and the IRS issued regulations in September, 2012 modifying the reinvestment requirement for non-real estate projects to allow a CDE that makes a qualified low-income community investment in a non-real estate business to reinvest the proceeds in a certified community development financial institution instead of requiring reinvestment in another qualified low-income community project.