<u>New GAO Report on New Markets Tax Credit</u>

Background

Congress created the New Market Tax Credit program in 2000 to encourage investments in low-income communities. The NMTC program is run by the Community Development Financial Institutions Fund (CDFI Fund) at the Department of the Treasury. The CDFI Fund allocates tax credit authority to Community Development Entities, which use the tax credits to raise capital for projects in low-income areas. The investor may claim a 39 percent tax credit over seven years on the NMTC investment.

The Government Accountability Office (GAO) previously issued three reports on the NMTC program, and this week released a new report highlighting some concerns with the program's complexity and effectiveness.

Report Findings

- 62 percent of NMTC projects received other public funding from 2010 to 2012 (federal, state & local)
- 33 percent of NMTC projects received other federal funding
- 21 percent of NMTC projects received funding from multiple other government programs

A majority of NMTC-financed projects utilize more than one source of *public* funding, despite the purpose of the tax credit being to leverage *private* investment.

Investors are able to claim the tax credit on the equity provided by the other public sources—such as historic tax credits, Recovery Zone bonds and qualified school construction bonds—meaning private investors can claim the NMTC on more money than they actually invested in the project.

> *In a case study reported by the Urban Institute, an investor appeared to put in about $500,000 of NMTC equity to claim $1.2 million of NMTCs representing a return of about 26 percent compounded annually. The NMTC was leveraged entirely with $2.5 million of federal and state HTCs without use of a conventional leveraged loan in the NMTC structure.* ***As a result, 83% of the qualified equity investment [on this project] on which investors are claiming NMTCs is provided by other federal and state tax credit programs" (emphasis added)***

GAO found the complex financial arrangements and fees charged by the CDEs reduced the amount of assistance provided to low-income community projects by $619 million (7.1 percent) from 2011 to 2012.

GAO also pointed to evidence that in transactions with lower fees, they may be offset by higher interest rates.

This figure does not include other fees charged by third parties, such as law firms or financial entities involved in structuring the deal. Every dollar paid to a CDE or a third party reduces the investment intended to benefit a low-income community.

GAO Recommendations (only two of several)

- GAO recommended that Treasury "ensure that controls are in place to limit the risk of unnecessary duplication at the project level in funding or assistance from government programs and to limit above market rates of return, i.e. returns that are not commensurate with the NMTC investor's risk."
- GAO recommended a clarification be issued on how NMTC can be combined with other sources of government funding, including whether an investor can claim the tax credits on equity provided by other government programs.