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## THE NEW MARKETS TAX CREDIT ISSUE



# Additional Access to Capital: State NMTC Incentives Create Boost in Investment

**BRAD STANHOPE, SENIOR EDITOR, NOVOGRADAC**

When Mississippi Gov. Tate Reeves signed legislation in March to extend the state's new markets tax credit (NMTC) by three years, it was the sixth extension of the incentive since it was enacted in 2007 and showed the continuing value of state-level incentives for community development investment.

"It's very important," said Tony Toups, principal at Advantage Capital, a community development entity (CDE) that has received 12 federal NMTC allocations worth nearly \$800 million, as well as \$1 billion in state allocations. "If you look at states that were early adopters, such as Louisiana, Mississippi and Missouri, part of the [early] discussion was that there's this wonderful program rolling out of Washington, D.C., and some states are participating robustly.

"Early versions of state new markets programs have evolved over time to best ensure that private investment capital achieves the state's intended priorities," said Toups. "These programs are widely accepted as effective economic development tools, designed to incentivize investment in small business to grow local economies, put people to work and create good-paying local jobs."

Twenty years after the federal NMTC became part of the tax code, Mississippi is one of more than a dozen states with an NMTC incentive, ranging from Alaska to Maine and Nevada to Florida. More could be coming: legislation was introduced this year in Tennessee to create a state NMTC, while similar bills were introduced in recent legislative sessions in California and Minnesota.

## **A Boost for Investment**

Like state-level historic tax credit and low-income housing tax credit incentives, state NMTC incentives can help close financing gaps. But since the federal NMTC is capped at \$5 billion in allocations per year, state-level NMTCs can also increase the attractiveness of those states to receive investments from CDEs.

A study by Advantage Capital—based on data from the CDFI Fund—showed that, on average, states nearly tripled the federal NMTC investment after launching a state tax credit, going from roughly \$37 million to more than \$103 million annually. However, some states' federal NMTC investment skyrocketed following the adoption of a state program: Nebraska's soared by 971%, Louisiana's by 569%.

"At one point, Louisiana led the nation in NMTC investment on a per-capita basis and we attribute that directly to the state credit making investment more attractive to federal CDEs," Toups said. "[A state credit] benefits the qualified active low-income community businesses because otherwise, the new markets tax credit allocation would be going elsewhere."

Toups said a state credit also encourages the growth of CDEs in those states, which furthers the opportunity to provide access to capital and financing expertise.

Brad Elphick, CPA, a partner in Novogradac's Atlanta office and head of the Novogradac NMTC Working Group, echoed Toups' statements about the value of state credits.

"I think they are very significant," said Elphick. "They do a couple of things. They attract federal allocation because [NMTC properties] sometimes require other investment. They allow projects that need more subsidy to pencil out because of the state tax credit portion of the capital stack."

### **Even More Important Now**

The reduction of federal NMTC equity pricing in the wake of the COVID-19 pandemic and economic recession has added to the importance of state credits.

"With federal tax credit pricing down, state equity can help bridge the gap that an otherwise higher federal price could have provided," Elphick said.

Toups said in both the Great Recession and the COVID recession, state NMTC programs have been important.

"When there's a downturn like in 2008 or COVID, it becomes more vital to have these programs," Toups said. "Allocations are agnostic and when an allocation comes out, you have X number of months to raise capital and X number of months to deploy it. State credits can help businesses recover and expand, create good jobs for local residents and encourage further investment and opportunities for growth at a time when communities and people most need it."

### **'Laboratories of Democracy'**

All state NMTCs are not created equal, which is a benefit. Toups pointed out the advantage of states passing focused versions of the NMTC, citing a 2020 bill in Louisiana that accelerated the investment time

and required that at least half of the QALICBs be minority-, woman-, veteran-owned or in rural counties.

"This really shows states as laboratories of democracy," Toups said. "Different states have done different things, varying the value of the tax credits and also varying the ability to use the credit. Some states delay the ability of the investors to redeem until after the capital is invested, so the state gets the benefit without making a contribution until the money is going where the state wants to go."

Some states have programs that borrow elements of the NMTC, even if they don't fully reach the level of a state NMTC.

Toups cited the Georgia Agribusiness and Rural Jobs Act program that became law in 2017. While not a direct correlation to the federal NMTC, the program provides 60% credits (15% in years 3, 4, 5, 6) for business investment, either in debt or equity, in small counties. The legislation limits investments to counties with fewer than 50,000 residents and focused on manufacturing.

### **Bipartisan Support**

The support of state-level NMTC programs is similar to that of the federal credit: widespread and bipartisan.

"This has been fairly steady," Toups said. "I think there's a constant refrain in this country about the need for capital in low-income communities. You hear the same discussion around rural communities, minority communities and others. It's been said that in order to have capitalism, you have to have capital."

"It's all about access to capital," Toups added. "The support for this has been bipartisan. There are new markets tax credit programs signed by Democratic governors in Kentucky and Louisiana and Republican governors in Mississippi and Florida. When you see vote tallies at the state legislatures, it's typically overwhelming."

He said that there is a geographic element to states that push for their version of NMTC programs.

“I would say Southern states and Midwestern states have been very interested,” Toups said. “Higher-population states probably don’t see the need for it as much.”

Toups has some advice for states considering adding an NMTC: Borrow best practices from the federal NMTC as much as possible.

“If you are going to have a true state new markets tax credit, you want to piggyback as much as you can on the administrative work being done by Treasury,” Toups said. “By that, I mean your participants have to be qualified as CDEs by the Treasury and things like that. Let the federal government vet for participants and keep the investments within the parameters of the federal new markets tax credit. Using their definition of low-income communities, qualified low-income community investments, exclusions and other things are best practices.” ❖

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