

New Market Tax Credits (NMTC):

A Tool for Community Development, As Well As Sustainable Forestry, and Community Partnerships

EXECUTIVE SUMMARY

New Market Tax Credits (NMTC) were designed to promote investment in low-income communities. However, recent projects have shown that they have potential to also support Forest Service objectives in land management with used in conjunction with local and national partnerships. Specifically, NMTC can help fund stewardship contractors, promote sustainable forest practices on private land, develop low-income community businesses to utilize small diameter wood for products and bio-mass fuel, and promote partnerships and community involvement in monitoring forest practices on both private and federal lands.

BACKGROUND

The Community Renewal Tax Relief Act of 2000 authorized tax credits¹ to stimulate \$15 Billion in equity investments in low income and economically distressed communities. It is viewed as a modest subsidy, and functions more like an interest subsidy than a capital grant. This means that financed activities will have to generate a positive cash flow and a return on capital in order to attract investors. However, the tax credits can make a marginally profitable investment into an attractive investment.

Over 40% of all US census tracts qualify for investments, and over one-third of the US population lives in these tracts. Overlaying the qualifying census tracts with a map of National Forests, it is apparent that significant areas of National Forest System lands occur in these tracts.

By the end of 2003, sixty-six Community Development Entities, in at least twenty states, had been allocated credits. Although most of the eligible Community Development Entities invest primarily in urban areas, approximately 20% invest primarily in rural areas. Approximately 14% of the total credits allocated by the end of 2003 are to entities that focus on community development in rural and mixed areas.

Community development entities were selected in March 2003 but most New Market Tax Credits (NMTC) investments were just being initiated by December 2003. Therefore, selected projects have had little time to start showing results. Further allocation of tax credits will occur in 2005, 2006, and 2007 with \$9.0 billion remaining to be allocated.

NMTC provide an opportunity to bridge financing gaps, and create partnerships among investors, communities, businesses, NGOs, and government. An additional \$9.0 billion is available for allocation to qualified Community Development Entities. If 20% of these

¹ The tax credit can be used to offset up to 39% of an investment or loan, recouped over a seven year period. The PNV of the tax credit is approximately 30%.

funds are used in rural areas, it can be expected that, at least some of the funds could be used to provide low-cost loans or equity investments in communities in, or adjacent to National Forests.

PROCESS

1. The US Treasury, through its Community Development Financial Institutions Fund, certifies qualified Community Development Entities. These entities must have a primary mission of community development, and serve or provide capital to low-income persons, or in low-income communities.
2. The Community Development Entities then submit applications and compete for an allocation of the tax credits. Priority for allocation goes to entities with a successful track record in providing capital or technical assistance to disadvantaged businesses or low-income communities.
3. The Community Development Entities use the allocated tax credits to raise capital or financing from private investors for a term of at least seven years.
4. The Community Development Entities then use substantially all of the investment funds in low-income communities for a wide range of business activities such as equity investment, small business lending, financial counseling, and real estate investment.

EXAMPLES

MAINE: Of the sixty-six Community Development Entities that received allocations by 2003, only one had promoting "sustainable forestry" as part of its mission statement. In Maine, this Community Development Entity, in conjunction with the Nature Conservancy utilized NMTC to help preserve the area near Baxter State Park from development. The Community Development Entity, or CDE, helped provide capital (long term loan), supported by tax credits, for the Katahdin Forest Project. A 200,000 acre area will be managed for long term sustainable forestry, provide a woodshed for two paper mills, and permit traditional recreational uses and access. Future development of the area is restricted by conservation easements.

ARIZONA: The non-profit CDE involved in the Maine project is now expanding nationally and plans to finance investment in timber related projects in low income areas. They have applied for \$65 million in additional tax credits. In the Southwest United States, it plans to use \$20 million in tax credits to stimulate industries that use small diameter logs. In addition to spurring investment in areas of low income, their goals include promoting healthy forests, preventing catastrophic wildfires, and reducing insect and disease infestations.

The CDE has a partnership with the Nature Conservancy (TNC). By phone calls, mail, press releases, and meetings, TNC is informing, potential bidders for the Apache-Sitgreaves-White Mountain Stewardship Contract that they would be willing to finance investments in plant and machinery needed to undertake stewardship contracting work².

² In addition, the State of Arizona recently passed forest health tax credits to lower small log industry start-up costs.

The Nature Conservancy is interested in contributing to the success of forest stewardship contracts. In an evolution and continuance of their past successes of encouraging responsible management of private lands, they see a role for themselves in fostering good management on public lands. Therefore, they are proposing to help finance biomass generation plant(s) and perhaps an Orientated Strand Board mill in the area to utilize thinned material.

Their goal is to help forest restoration on a landscape scale. TNC is also involved in the multi-party monitoring board created to recommend landscape level monitoring tied to the stewardship contract. TNC requires that projects that they invest in provide a written plan showing that they will use science-based criteria in their forest restoration projects, and include monitoring ecological objectives in their proposal. This coincides well with Forest Service objectives.

SUMMARY

NMTC in the amount of \$9.0 billion are available for distribution to qualified Community Development Entities. Priority for distribution is to entities that have a proven track record in providing capital or technical assistance to disadvantaged businesses or communities.

NMTC are designed to help low income communities develop business that provide economic development and jobs, including tribal areas with high levels of unemployment and poverty, and in many areas close to, or adjacent to, National Forests.

NMTC have the potential to provide investment equity and/or low cost loans to companies that undertake HFI restoration projects, stewardship projects, or practice sustainable forestry.

NMTC have been allocated to at least one Community Development Entity (CDE) that have indicated a desire to work with the Forest Service to promote sustainable forestry.

NMTC are supported by tribal groups, regional development corporations, some NGO organizations (The Nature Conservancy, The Conservation Fund), and elected officials at the local, State, and national level.

RECOMMENDATIONS

1. Continue monitoring progress of using NMTC for development of forest industries in Arizona and other states. (S&PF, WO)
2. Have R-3 share information on how NMTC assisted in the success of their stewardship contract program, as well as the multi-party monitoring board, and Forest service-community partnership for forest restoration. (R-3, A-S)
3. Distribute information to rural development coordinators in Regions
4. Follow up with Coastal CDE on using tax credits to promote sustainable forestry projects in areas of National Forest System lands. (S&PF, WO)

5. Follow-up with TNC to explore possibilities of expanding program beyond the A-S. TNC wishes to expand their participation with beyond the 150,000 acre restoration project on the apache-Sitgreaves.
6. Renew contacts between USDA Forest Service and US Treasury CDFI Fund to encourage further investment and use of NMTC in projects that contribute to sound forest management projects in low-income areas. (S&PF, WO)
7. Share information on NMTC with other program areas in the Forest Service. Community Development Entities have used NMTC to protect historic buildings so there may be opportunities in either the Heritage or Facility program areas to form partnerships with local development entities.

FURTHER INFORMATION

General Accounting Office Report:
GAO-04-326 New Markets Tax Credit Program
www.gao.gov/index.html
(Type "New Market Tax Credit Program" in Search Box)

Community Development Financial Institutions Fund
www.cdfifund.gov

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