July 2, 2001

Jeffrey Berg
Acting Director
Community Development Financial Institutions Fund
U.S. Department of the Treasury
601 13th Street, N.W.
Suite 200 South
Washington, DC 20005

Re: Response to request for guidance on the New Markets Tax Credit program

Dear Mr. Berg:

Self-Help Ventures Fund appreciates the opportunity to provide comments to you on CDFI Fund's request for guidance related to the New Markets Tax Credit.

Over the past 20 years, Self-Help Ventures Fund and its affiliates have provided over $1 billion in financing to over 16,000 small businesses, non-profit organizations and individuals. We target our financing activities to assist low-income communities and businesses to help create economic opportunities. Our lengthy and successful record of providing financing to businesses in low-income communities gives us unique insight into ways to make the new markets tax credit program successful in achieving its goal of creating new private investment in low-income communities.

Before addressing the specific questions raised in the request for guidance, we wish to raise a few other issues in the request.

Section II. The New Markets Tax Credit Program: How the Credit Works
Timing of Allocation Agreements: The guidance states that a Community Development Entity (CDE) may not issue any qualified equity investments to its investors until the CDE and the Fund have executed an Allocation Agreement. According to the draft guidance, an Allocation Agreement would specify the terms and conditions of the NMTC allocation to the CDE. While we understand why such a document needs to be finalized before a CDE can enter into transactions with investors, we want some assurance that the Fund will move in a timely manner in issuing Allocation Agreements once a CDE has been notified of their allocation. Regulations will require a CDE to get 'substantially all' of its cash invested in qualified low-income community investments soon after it has secured cash from investors and thus CDEs will need to develop a pipeline of qualified low-income community investments once they are notified of

their allocation. Therefore, we recommend that the final regulations specify that the Fund will finalize Allocation Agreements within two months of a CDE being notified of an allocation award.

Section IV. Eligibility

Community Accountability: While the statute states that community accountability can be met by having residents serve on "any" governing or advisory board of the CDE, the guidance states that the "accountability requirement may be met if residents of low-income communities are represented on the governing or advisory board of the entity's managing general partner or other controlling entity." In addition, the guidance cites an example of accountability as having low-income people or residents of low-income communities on such a board.

Thus, the guidance suggests a much more restrictive definition of "accountability" than the Fund uses for its other programs. For example, under the CDFI core program, an entity can be certified as a CDFI if it has representatives of the "target market" on its governing board or uses other approaches, such as an advisory board, focus group or community meetings. A CDFI applicant must provide a brief narrative of how it is meeting the accountability requirement in its application. We recommend that the Fund apply a similarly flexible accountability test for the Credit.

In addition, we recommend that the guidance definition of "representative of low-income community" be expanded to include people whose primary job or activity is serving or working in low-income communities, such as a pastor, business owner or CDC director, who may live elsewhere, but is representative of the community and aware its needs. The current guidance definition is limited to people who either are low-income or are residents of the low-income community.

Finally, we recommend that a CDE be treated as meeting the accountability test if a majority of its governing or advisory board (if it employs such an approach) meets the "representative test."

Section V. Evaluation

We are concerned that the draft guidelines propose an evaluation process that could be unnecessarily time consuming. While we understand the Fund has a fiduciary responsibility to underwrite NMTC allocations and insure that CDE applicants are eligible and have the capacity to carry out a proposed Comprehensive Investment Plan, we encourage the Fund to recognize the market driven nature of the NMTC program. Once a CDE is certified and secures a NMTC allocation from the Fund, it will need to market the Credit to private investors that will do their own due diligence before investing in the CDE. A CDE will need to pass the scrutiny of both the Fund and their private investors before it can actually utilize the NMTC.

The draft guidelines require a CDE to supply a Comprehensive Investment Plan that provides historical information and a minimum five-year investment strategy. Upon receiving notice of an award of an allocation, a CDE must then negotiate and finalize its NMTC Allocation Agreement with the Fund. We are concerned the application, evaluation and final allocation processes will be onerous and could substantially delay the availability of the tax credits to spur new investment. Therefore, we suggest a streamlined application process for CDEs that have previously submitted their Comprehensive Investment Plan to the Fund for one of the other CDFI Fund programs. In such cases, we also suggest that the Fund not conduct a site visit if it has constructed such visits in the past.

Our responses to your specific questions follow below.

1. IRC §45D(f)(2) requires that in making allocations of NMTCs, priority be given to: (a) any applicant that has a record of having successfully provided capital or technical assistance to disadvantaged businesses or communities or (b) any applicant which intends to satisfy the Substantially All Test by making Qualified Low-Income Community Investments in one or more businesses in which persons unrelated to the CDE hold a majority equity interest.

(a) How should the Fund implement this policy? For instance, should the Fund incorporate preference points into the scoring? Should the Fund make awards to organizations that are deemed competitive and meet one or both of these criteria before providing an allocation to any other applicant?

The Fund should implement this policy by carefully examining the applications submitted and evaluating them based on the totality of the circumstances. We believe the intent of the statute was to give equal treatment to these preferences and we recommend that the regulations clarify that a CDE can get preference for either a successful record of providing capital to disadvantaged businesses or communities or for planning to invest in unrelated businesses, but not both.

We also note that IRC §45D(i)(5) instructs the Secretary to prescribe regulations which apply the provisions of §45D to newly-formed entities. Due to the accounting, tracking and reporting requirements we expect to be required as part of the new markets tax credit program, we believe many, if not most, CDEs will be newly-formed entities. When evaluating newly-formed entities for allocations of NMTCs, we believe the Fund should examine the record of the entity that controls the newly-formed entity. The controlling entity (such as the managing member of an LLC or a controlling shareholder of a corporation) should then be evaluated as though it was the entity seeking an allocation of NMTCs.

(b) What specific factors should the Fund consider when evaluating whether an applicant meets the requirements for priority treatment?

There are several specific factors the Fund should consider. First, in determining whether an applicant (or its controlling entity in the event of a newly-formed entity) has a successful record of providing capital or technical assistance to disadvantaged businesses, the Fund should consider:

- The total amount of capital provided by the applicant to disadvantaged businesses, including non-profit organizations
- The number of disadvantaged businesses that have received capital from the applicant

- The overall success rate of the applicant in providing capital, measured in terms of loan loss rates, net income, and other financial metrics, including financial metrics used to evaluate non-profit organizations, as applicable.
- The ratio of activities that provide capital or technical assistance to disadvantaged businesses to the overall activities of the organization. For instance, an organization that has provided \$10 million in capital, all of it to disadvantaged businesses, should receive higher priority than an organization that has provided \$50 million in capital to disadvantaged businesses, but for which that figure pales in comparison to overall capital provided of \$4 billion.

Second, the Fund should evaluate applicants' intention to satisfy the "substantially all" test by making qualified low-income community investments in one or more businesses in which persons unrelated to the CDE hold a majority equity interest by requiring applicants to submit a detailed investment plan. The Fund should evaluate that plan based on its overall credibility, including the reasonableness of the plan objectives and strategy, and the historical record of the applicant in executing its strategy.

(c) Should more weight be given to one priority category over the other and should an applicant be allowed to receive preference points under both priority categories?

Although we believe that both of the priority categories are important, we believe that applicants that have demonstrated success in providing capital to low-income community businesses should be given more weight than those applicants that intend to meet the "substantially all" test by making investments in which persons unrelated to the applicant hold majority equity interest. We believe this approach would further the purposes of the NMTC, which is to create new investment in low-income community businesses, while preventing abuse of the availability of NMTCs for such activities.

2. Should there be limits as to the amount of a NMTC allocation that may be awarded to an applicant in a calendar year?

We believe it is important to ensure that the expected benefits of the NMTC program are extended throughout the country to a variety of low-income communities. To accomplish this, we believe a broad range of CDEs, both in terms of size and geographic location, should receive an allocation of credits.

The main purpose of the NMTC is to spur private economic development in low-income communities. There is a broad range of low-income communities in the United States, and the opportunities offered by the NMTC should be extended to as many of them as possible. If all NMTCs were allocated to one organization, it is likely that organization would focus its low-income community investment efforts in a limited geographic region and to a limited number of types of businesses. The result is that the benefits of the NMTC would not extend as widely as possible.

Rather than establish specific limitations on the amount of an allocation that may be awarded to an applicant in a calendar year, we believe you should make allocations with these considerations in mind. Imposing strict limits on the amount of credit allocations available may result in the available allocation being undersubscribed, which would be a unnecessary waste or delay in implementing the benefits of the program. Therefore, the principles we outline here should be guidelines for making allocations, rather than shackles that limit your flexibility and judgment.

3. During the evaluation process of NMTC applications, the Fund will request that applicants provide information on their track records for providing capital or technical assistance to Low-Income Communities and disadvantaged businesses and the effect that such investment/technical assistance has had on such Low-Income Communities or businesses. Applicants may also be required to describe the social underwriting criteria that they will use when deciding which companies to invest in. If an applicant receives an NMTC allocation, it will be required to report to the Fund on the ways in which the Qualified Equity Investments are used to benefit Low-Income Communities.

(a) What indicators should the Fund assess when evaluating the community development impact of an applicant's prior activities or the social underwriting criteria of its loan policies?

There are several indicators the Fund should consider when evaluating the community development impact of an applicant's prior activities and social underwriting criteria, including:

- The total dollar amount of investments made by the applicant
- The number of organizations that have received capital from the applicant, and how many of them are located in low-income communities
- The number of jobs maintained or created as a result of capital from the applicant

Although these criteria are helpful considerations when evaluating an applicant for an allocation of credits, they should not be tracked on an ongoing basis after allocations are made, since such considerations are not contemplated by statute. Any ongoing reporting should focus on compliance with the statute, rather than social outcomes. The low income housing tax credit is a program that recognizes this and has implemented its ongoing reporting requirements accordingly.

(b) On what basis should the Fund judge how "successfully" capital or technical assistance has been provided?

The Fund should judge how successfully an applicant has provided capital or technical assistance by considering:

- The overall historical financial performance of the applicant, as measured in accordance with generally accepted accounting principles. This may include overall operating income, loan loss ratios for applicants that provide debt capital, and return on investment for applicants that provide equity capital.

- The number of low-income community businesses that received capital from the applicant, and the financial performance of those businesses.

(c) What information should the Fund request from allocation recipients as indicators for evaluating the effectiveness of the NMTC Program (e.g., number of jobs created or retained, increases in revenues of businesses receiving Qualified Low-Income Community Investments, rates of return to investors from Qualified Equity Investments, or number of clients served at facilities that are developed)?

We believe the Fund should focus its evaluation efforts on whether the CDEs that receive allocations of credits remain in compliance with the program. The new markets tax credit statute is designed to spur additional private financial investment in low-income communities, and evaluation programs should focus on that goal. Measuring the success of CDEs to accomplish that goal can be done through tax reporting that addresses amounts of capital raised by CDEs and the amount that CDEs invest in qualified low-income community businesses. Examining the number of jobs created or clients served are not helpful indicators of that, and the statute does not state those factors to be goals of the statute.

You may contact me at 919-956-4434 or bob@self-help.org if you have any questions. Thank you for your consideration, and we look forward to working with you to implement the new markets tax credit.

Sincerely,

Robert N. Schall
President