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Take the Money and Run: A Case for Benchmarking in the New Markets Tax Credit Program

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TAKE THE MONEY AND RUN:
A CASE FOR BENCHMARKING IN THE NEW MARKETS
TAX CREDIT PROGRAM

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INTRODUCTION

In the Langley Park District of Baltimore, Maryland, the state's largest immigrant service organization opens the doors of its new \$13.8 million dollar facility for the first time.¹ The center provides

1. Press Release, CASA de Md., Maryland's Largest Immigrant Organization to Open New Headquarters as It Celebrates Its 25th Anniversary (June 15, 2010),

essential services to the many immigrants who live in the area—especially catering to women and low-income workers. The new center is brimming with activity. An English as a Second Language class has commenced for the evening in one of the center’s brand new classrooms. In another area of the building, a single mother receives legal aid to help recover unpaid wages she is owed. Elsewhere, a middle-aged man receives help in opening his first bank account, one of over 1,700 people the organization will assist in doing so in this year alone.² A man with a family to feed gets help finding a job. A first generation immigrant collects information on registering to vote. Another speaks with a counselor about how to become a U.S. citizen.

The organization, CASA of Maryland, financed the opening of their new Multicultural Center through a \$7.9 million tax credit from the United States government.³ This special type of tax credit, a New Markets Tax Credit (NMTC), was specifically intended for developments that help low-income people in economically depressed areas.

Across town, a business and office park opens. It employs many scientists and other highly educated, skilled professionals. BioPark’s sleek new development contains twelve buildings catering mostly to science, biotech and drug development companies. The laboratories are state of the art. A gourmet café serves lunch on site. Deals are negotiated. Investors make money.

Curiously, this sparkling office park, filled with advanced degrees, fancy lunches and tailored suits, also received the same tax credits intended for low-income people in economically depressed areas. What is even more incredulous, BioPark received a greater amount of tax credits than the CASA Multicultural Center—a whopping \$15 million.⁴ Something, it seems, is amiss.

available at http://casademaryland.org/index.php?option=com_content&view=article&id=1288:casa-celebrates-25th-anniversary-with-new-offices&catid=45:press-release&Itemid=128.

2. CASA DE MD., ANNUAL REPORT 2010, at 2 (2010), *available at* http://casademaryland.org/index.php?option=com_content&task=view&id=17&Itemid=36.

3. *New Markets Tax Credits Portfolio: CASA Multicultural Center, ENTERPRISE COMMUNITY INVESTMENT*, http://www.enterprisecommunity.com/products_and_services/nmtc-portfolio-CASA.asp (last visited Jan. 15, 2011).

4. Robbie Whelan, *As U of Md., Baltimore Opens Doors to BioPark Building*

In 2000, the federal government unveiled this novel program of tax credits to reward businesses that invested in and/or operated businesses in “new markets.”⁵ These “new markets” were in economically distressed areas in the United States—areas in which American businesses certainly were not clamoring to operate. The goal of this new tax program was to stimulate private investment in rural and urban communities.⁶ NMTCs were to provide a market-based approach for prompting community revitalization⁷ and act as an incentive for the private sector to invest in economically depressed areas.⁸

A current national study revealed that over \$120 million in retail spending comes from low-income community members, which accounts for about eight percent of all U.S. retail spending.⁹ However, much of this demand is not being met by neighborhood retailers, and thus must be met by outside retailers.¹⁰ A 1999 research study performed in the year before the NMTC program was enacted showed that compared to the rest of Los Angeles, Southern Los Angeles had “65 percent fewer grocery stores, 40 percent fewer banks and other financial institutions, and 20 percent fewer clothing stores.”¹¹ Instead

Two, Work Already Begun on Building Three, DAILY REC. (Balt.), Apr. 1, 2008.

5. Mark L. Silow, *Tax Credits Allow for Investments in Low-Income Communities Act Hoped to Increase Interest by \$15 Billion*, LEGAL INTELLIGENCER (Phila.), May 29, 2001, at 8.

6. *Id.* Under the NMTC code provisions, an economically depressed or “low-income community” is one where (1) the poverty rate in that community is at least twenty percent; (2) the median family income in that area does not exceed eighty percent of the statewide median family income; or (3) in a metropolitan area, the median family income in that community does not exceed eighty percent of the greater of the statewide median family income or the metropolitan area median family income. I.R.C. § 45D(e)(1) (2006).

7. Michael S. Barr, *Access to Financial Services in the 21st Century: Five Opportunities for the Bush Administration and the 107th Congress*, 16 NOTRE DAME J.L. ETHICS & PUB. POL’Y 447, 453 (2002).

8. James A. Fellows, *Tax Incentives for Investment in Low-Income Communities*, 33 REAL. EST. L.J. 317, 317 (2004).

9. ICIC’s *State of the Inner City Economies Database*, INITIATIVE FOR A COMPETITIVE INNER CITY, http://www.icic.org/site/c.fnJNKPNhFiG/b.5345879/k.6AA2/Inner_City_Economies/apps/lk/content2.aspx (last visited Jan. 16, 2011).

10. Ted M. Handel, *The New Market Tax Credit Program*, 25 L.A. LAW. 13, 13 (2003).

11. *Id.*

of using their income to reinvest in their own communities, low-income consumers are forced to flush this cash outside of the community, simply because they do not have retail options within the community. Among other economic and social benefits, NMTCs help pave the way for an initial influx of capital to satisfy this demand for goods and services and, in the process, promote community revitalization by keeping spending within the local community.

Once the NMTCs are allocated to individual investors, there are no performance objectives that the businesses must meet,¹² despite the fact that the credits are highly competitive.¹³ In a few situations, the federal government may “recapture” or take back the credits if the entities involved cease performing the basic function of operating in a low-income community.¹⁴ This is not a performance objective as much as it is a criterion the entity must meet to receive the credits in the first place.

The purpose of this Comment is to advocate that performance objectives need to be added to the NMTC code through the form of recapture provisions, as well as to provide some proposed performance objectives that companies should have to meet to avoid recapture of the credits. In order to determine which performance objectives should be added to the code, this comment looks at actual NMTC developments in Maryland to identify characteristics of “successful” NMTC developments. Maryland was chosen as a case study because of its high concentration of NMTC activity. “Successful” developments are those that meet the program’s goals of fighting poverty and blight in low-income communities, and do not simply benefit private investors. Successful developments not only

12. Kristen M. Tluchowski, *Update: The New Market Tax Credit and New Market Venture Capital Companies*, 11 J. AFFORDABLE HOUSING & COMMUNITY DEV. L. 105, 106 (2001).

13. Roughly twenty-three percent of the entities that apply for NMTCs receive them. CMTY. DEV. FIN. INSTS. FUND, PROMOTING INVESTMENT IN DISTRESSED COMMUNITIES: THE NEW MARKETS TAX CREDIT PROGRAM iv (2008), available at http://www.cdfifund.gov/docs/2008/nmtc/CDFI_PromotingInvest.pdf [hereinafter PROMOTING INVESTMENT].

14. I.R.C. § 45D(g) (2006). The CDFI will force a recapture of the NMTCs if (1) the community development entity (CDE) ceases to be qualified as a CDE; (2) substantially all proceeds of the investment cease to be used for low income community members; or (3) the CDE redeems the investment. § 45D(g)(3).

operate in low-income communities; they actually *help* low-income community members as well.

Essentially, NMTCs put money back into the pockets of investors. Without some set of performance objectives, investors are free to use the credits in ways that only benefit themselves, instead of focusing on community economic revitalization. They are, in essence, free to “take the money and run.”¹⁵ In these cases the NMTC program may be awarding tax credits to ineffective developments, when directing that otherwise-collected tax revenue into other anti-poverty programs would be a more effective use of the funds.¹⁶ Having benchmarks in place ensures these tax credits will go to the entities that put them to the highest and best use in promoting the social goals of the NMTC program. In order to meet these proposed benchmarks, the Community Development Financial Institutions Fund (CDFI)¹⁷ should mandate that entities submit periodic reports regarding their activities to show whether they are meeting these benchmarks.

Part I provides background on the credits—including an explanation of how they work, the legislative intent behind them, and the economic theories they are based upon. It also includes a brief background on why Maryland was chosen as a case study, and describes arguments for and against the use of NMTCs. Part II offers an argument for why benchmarks are needed for the NMTC program. Part III outlines proposed benchmarks that should be added through recapture provisions. These proposed benchmarks are related to: job production; mandatory reinvestment in the community; social services offerings to low-income people; affordable housing; increased occupancy of commercial developments and; the sale of consumer goods.

15. STEVE MILLER BAND, TAKE THE MONEY AND RUN (DCC Compact Classics 1976).

16. By awarding these tax credits, less tax revenue is generated by the government. This otherwise collected tax revenue could have been used to fund other government programs that benefit low-income communities, and thus may make low-income communities *worse* off.

17. The CDFI is an arm of the Department of the Treasury and is the administrator of the NMTC program. Handel, *supra* note 10, at 14.

I. BACKGROUND OF THE NMTC PROGRAM

The NMTC program was enacted “to provide an incentive to stimulate investment in low-income communities.”¹⁸ The premise behind the credits was relatively simple: The government offered NMTCs to get businesses operating in areas that investors previously had little incentive to even care about, let alone invest in. The tax credits are a way for companies to reduce their tax liability.¹⁹ This, in theory, would make investing in these underserved markets financially less risky.²⁰ To receive the credits, companies must apply for them through the CDFI.²¹ Typical NMTC developments include “small technology firms, inner-city shopping centers, manufacturers, retail stores and microentrepreneurs.”²² The NMTC developments in Maryland considered in this Comment include a halfway house, the headquarters for a Latino/immigrant advocacy group, a life sciences/industrial park, a large commercial/retail/residence mixed use development, a performing arts theater, a science lab/office facility, and a retail center.

President Clinton enacted the NMTC program at a time when the United States economy was strong. Unemployment was at a three-decade low in American inner cities, and joblessness in Black and Hispanic communities was the lowest that had ever been recorded.²³ The Dow Jones Industrial Average had steadily been climbing for over a decade,²⁴ and in 2000, poverty rates in the U.S. were the lowest they had been since 1974.²⁵ Despite the fact that the economy was

18. Peter M. Fass, *The New Market Tax Credit*, N.Y. L.J., Oct. 1, 2008, at 3.

19. *Id.*

20. As a direct result, the investment becomes less risky to investors because they have to pay fewer taxes. The goal of the NMTC program is to bring more economic development to low-income areas, as a result of the lowered risk.

21. Handel, *supra* note 10, at 13.

22. Tluchowski, *supra* note 12, at 105.

23. Richard S. Dunham, *Clinton's New Markets Initiative: Will Corporate America Invest at Home?*, BUS. WK., July 2, 1999, <http://www.businessweek.com/bwdaily/dnflash/july1999/nf90702a.htm>.

24. *DJA Basic Chart*, YAHOO! FIN., <http://finance.yahoo.com/q/bc?s=DJA&my&l=on&z=l&q=l&c=> (last visited Jan. 15, 2011).

25. *Historical Poverty Tables*, U.S. CENSUS BUREAU, <http://www.census.gov/hhes/www/poverty/data/historical/people.html> (click on Table 2: Poverty Status, by Family Relationship, Race, and Hispanic Origin) (last visited Jan. 15, 2011).

strong as a whole, the Clinton Administration voiced concern about the pockets of poverty that still existed in many American cities.²⁶ American corporations had been “leaping at the chance to gamble on developing overseas markets,” but were still very hesitant about investing in underdeveloped markets on the home front.²⁷ The NMTC program was modeled in part on the Overseas Private Investment Corporation,²⁸ which provides incentives for American businesses to invest in emerging markets abroad.²⁹ “I woke up one day and realized that American businesses could get lower risk to invest in the developing economies overseas than they could in the developing economy here in America. And I think that’s wrong,” President Clinton said in an interview with *Business Week* magazine.³⁰ “What we tried to do is to create at least the same—if not greater—incentives for American businesses to invest in America than we give them in developing countries overseas.”³¹ President Clinton also stressed the moral value of investing in poor communities. “There is a moral logic here,” he said, “which is that we don’t want to go into the 21st century at an all-time high in prosperity and leaving so many people behind.”³² When Congress eventually passed the NMTC legislation in December of 2000³³ (administered under I.R.C. § 45D), it claimed to do so as an attempt to help equalize the “unequal access to economic opportunities”³⁴ in distressed communities in America and to fight “joblessness, poverty and low incomes.”³⁵ Congress also was

26. Dunham, *supra* note 23.

27. *Id.*

28. The Overseas Private Investment Corporation (OPIC) “enables U.S. business to create revenues, jobs and growth opportunities at home and abroad. OPIC helps secure America’s competitive foothold in pivotal developing economics, brings stability to unstable regions, and paves the way for U.S. private capital to help solve our world’s most urgent challenges.” *Overview, OVERSEAS PRIVATE INVESTMENT CORP.*, <http://www.opic.gov/about-us> (last visited Feb. 2, 2011).

29. Dunham, *supra* note 23.

30. *Id.*

31. *Id.*

32. *Id.*

33. Silow, *supra* note 5, at 8.

34. H.R. REP. NO. 106-706, at 2 (2000).

35. *Id.*

motivated to take advantage of, and pump capital into, these “untapped markets.”³⁶

A. *Economic Theory Behind NMTCs*

Access to capital and financial services is key to economic growth in both advanced and developing economies.³⁷ These tools help drive business formation, fuel economic growth, and allow consumers to purchase goods conveniently.³⁸ A lack of access to credit hinders growth in economically depressed communities.³⁹ NMTCs help provide this much-needed financial capital to businesses that operate in low-income communities. The theory is the growth of one new business might start a domino effect of growth and revitalization in a depressed community, and could be a catalyst for other capital expenditures in that community.⁴⁰ In the article, *Can Free Enterprise Cure Urban Ills?: Lost Opportunities for Business Development in Urban Low-Income Communities Through the New Market Tax Credit Program*, Professor Janet Thompson Jackson argues the initial capital that NMTCs provide can potentially spawn a large amount of growth in a community:

The increased employment opportunities would attract more residents to the community, which would stimulate housing rehabilitation and development. A stronger economic and residential base can then exert more pressure for improved schools, effective transportation, enhanced public safety, health and other services. As these pieces come together, a once struggling community is transformed into a healthy urban neighborhood.⁴¹

Additionally, Jackson notes, the integration of new businesses into a community can provide disadvantaged youth an opportunity for “initial employment experiences” and can help promote the idea that

36. *Id.*

37. Barr, *supra* note 7, at 447.

38. *Id.*

39. *Id.*

40. Janet Thompson Jackson, *Can Free Enterprise Cure Urban Ills?: Lost Opportunities for Business Development in Urban Low-Income Communities Through the New Market Tax Credit Program*, 37 U. MEM. L. REV. 659, 701 (2007).

41. *Id.* at 701-02.

community life is organized around work.⁴² This influx of capital and jobs helps “integrate residents into the mainstream economy as workers and consumers.”⁴³ The growth of these new businesses brings products and services to traditionally underserved communities, and also brings jobs⁴⁴ and tax revenue.⁴⁵ Local businesses also keep revenue and spending within the community, instead of funneling it outside of the community.⁴⁶ All these factors combine as a result of a single NMTC allocation and add substantially to the economic vitality of the local community.

B. *The NMTC Application Process*

Once a business has been selected to receive an NMTC, the credits are distributed over the course of seven years.⁴⁷ In each of the first three years of the investment, the investor receives an annual credit of five percent of the initial equity investment.⁴⁸ For the final four years of the credit, the credit is six percent annually of the initial equity investment.⁴⁹ Thus, over the course of seven years, the tax credits combine to create a total tax credit of thirty-nine percent of the initial equity investment.⁵⁰ The credits are applied on the date of the initial equity investment and on the six subsequent investment-anniversary dates.⁵¹

Only Community Development Entities (CDEs) can apply to receive NMTCs,⁵² and the CDFI determines which entities do and do

42. *Id.* at 703.

43. *Id.* at 701.

44. Jeffrey Robinson, *Urban Entrepreneurship: Patterns and Policy*, 30 W. NEW ENG. L. REV. 103, 104 (2007).

45. Roger M. Groves, *More Private Equity, Less Government Subsidy, and More Tax Efficiency in Urban Revitalization: Modeling Profitable Philanthropy and Investment Incentives*, 8 FLA. ST. U. BUS. REV. 93, 99 (2009).

46. *See* Handel, *supra* note 10, at 13.

47. I.R.C. § 45D(a)(3) (2006).

48. § 45D(a)(2)(A).

49. § 45D(a)(2)(B).

50. § 45D(a)(1).

51. § 45D(a)(3).

52. Handel, *supra* note 10, at 14.

not qualify as CDEs.⁵³ There are a number of requirements listed in the Internal Revenue Code, but essentially a CDE has to meet the primary mission of serving or providing investment capital for low-income communities or low-income people.⁵⁴ Once the CDE is authorized and has received the credit, the CDE can offer the credit to private investors on the basis of their investment in the CDE or keep the credit to offset its own tax liability.⁵⁵ To qualify as a CDE, the business's investment must be in a Qualified Low-Income Community (QLIC).⁵⁶ A QLIC is a community that, according to the U.S. Census Tract, meets one of the following criteria: 1) a poverty rate of at least twenty percent; 2) a location outside a metropolitan area where the median family income is below eighty percent of the median statewide family income; or 3) a location in a metropolitan area where the median family income is below eighty percent of the greater of either the statewide or metropolitan area median family income.⁵⁷ Additionally, residents of the low-income community served by the CDE must be on its governing or advisory board.⁵⁸

An investor must file two applications to receive a NMTC⁵⁹: an application to be certified as a CDE,⁶⁰ and an application to receive the actual NMTC allocation.⁶¹ In determining which CDEs will be awarded the credits, the Department of the Treasury considers seven categories: "1) institutional investment and community development track record; 2) financial and operational capacity; 3) capacity, skills

53. Kenneth Weissenberg & Aninda Dhar, *Real Estate Investments Made Sweeter by Tax Credits*, METROPOLITAN CORP. COUNS., Apr. 1, 2010, at 31.

54. § 45D(c)(1)(A).

55. Jackson, *supra* note 40, at 696.

56. Handel, *supra* note 10, at 17.

57. § 45D(e).

58. Under the NMTC code sections, the CDE must maintain "accountability to residents of low-income communities through their representation on any governing board of the entity or on any advisory board to the entity." § 45D(c)(1)(B).

59. Silow, *supra* note 5, at 8.

60. *Id.*; see also CMTY. DEV. FIN. INSTS. FUND, CDE CERTIFICATION APPLICATION (2009), available at <http://www.cdfifund.gov/docs/certification/CDE/CDEcertificationApplication.pdf>.

61. Silow, *supra* note 5, at 8; see also CMTY. DEV. FIN. INSTS. FUND, NEW MARKETS TAX CREDIT ALLOCATION APPLICATION (2010), available at <http://www.cdfifund.gov/docs/nmtc/2010/2010%20NMTC%20Application%20Final%205%207%2010.pdf>.

and experience of the management team; 4) market analysis; 5) capitalization strategy; 6) investment strategy; and 7) projected community development activity and projected impact.”⁶² On average, less than twenty-three percent of all applicants receive NMTCs.⁶³

Once a CDE has been slotted to receive the NMTC, no specific performance objectives need to be met.⁶⁴ However, the credits may be subject to recapture. Currently, the credits can be recaptured by the government if any of the following occur: the recipient fails to qualify as a CDE during the seven year period; the proceeds of the qualified equity investment are not used in a way that satisfies the “substantially all” requirement under I.R.C. § 45D(b)(1)(B);⁶⁵ or the investor cashes out during the seven year period.⁶⁶ In these situations the credits will be recaptured with interest.⁶⁷

C. Maryland Developments as a Case Study

Maryland was chosen for this study because of its prolific use of NMTCs, especially in relation to its small size. Maryland is the nineteenth most populous state⁶⁸ and the eighth smallest by geographic area,⁶⁹ yet it has received the fifth most NMTC allocations, both dollar for dollar and in number of allocations, since the program’s inception.⁷⁰ Also included in the top five were

62. Tluchowski, *supra* note 12, at 109 n.9.

63. PROMOTING INVESTMENT, *supra* note 13.

64. Tluchowski, *supra* note 12, at 106.

65. The NMTC code provisions also require that “substantially all” of the cash raised as a result of the sale of qualified equity investments be used to make qualified low-income community investments. I.R.C. § 45D(b)(1)(B) (2006). This “substantially all” test is met if at least eighty-five percent of the aggregate gross assets of the CDE are invested in qualified low-income community investments. § 45D(b)(3).

66. § 45D(g)(3).

67. § 45D(g)(2).

68. *Resident Population Data*, U.S. CENSUS 2010, <http://2010.census.gov/2010census/data/apportionment-dens-text.php> (last visited Jan. 15, 2011).

69. U.S. CENSUS BUREAU, UNITED STATES SUMMARY: 2000, at 29 (2000), available at <http://www.census.gov/prod/cen2000/phc3-us-pt1.pdf>.

70. *Searchable Awards Database*, U.S. TREASURY: CDFI FUND, <http://www.cdfifund.gov/awardees/db/index.asp> (under the “Program” tab, select NMTC; then click “Submit”) (last visited Jan. 15, 2011).

California, New York and Ohio (three of the most populous states) and Louisiana (a state that received a large number of allocations as part of Hurricane Katrina disaster relief efforts).⁷¹ Thus, Maryland is somewhat of an outlier because it has produced a very large amount of NMTC activity in such a concentrated area. This seems to be an indicator that entities in Maryland are doing *something* right.

D. *Arguments For and Against NMTCs*

While only a handful of law review articles have discussed the topic of NMTCs, many of them criticize the program. Critics of the program contend that the credits are too small relative to the need for them.⁷² These critics argue that while the credits are well intentioned, they do not have a major transformative impact.⁷³ These critics also claim that the relatively small tax deductions probably will not spawn massive community revitalization; instead, rewarding return on investment would be a better tool in prompting large-scale revitalization.⁷⁴ Other scholars question whether the tax credits are adequately helping the low-income individuals the program is designed to serve.⁷⁵ Critics argue that programs like the NMTCs “primarily benefit private investors,”⁷⁶ and not the local communities. Finally, some critics maintain that targeting a geographical area—as opposed to targeting the specific needs of residents in that area—does not guarantee economic mobility to low-income residents through job placements, and also fails to address other issues such as schools, job training and housing.⁷⁷ These critics argue that the latter factors are

71. *Id.*

72. Matt Fellowes, *Making Markets an Asset for the Poor*, 1 HARV. L. & POL’Y REV. 433, 448 (2007).

73. Groves, *supra* note 45, at 96.

74. *Id.* at 97.

75. Sarah Vallim, *The New Markets Tax Credit and the Community Economic Development Movement: A Los Angeles Case Study*, 16 J. AFFORDABLE HOUSING & COMMUNITY DEV. L. 117, 136 (2007).

76. Jennifer Forbes, *Using Economic Development Programs as Tools for Urban Revitalization: A Comparison of Empowerment Zones and New Markets Tax Credits*, 2006 U. ILL. L. REV. 177, 177.

77. *Id.* at 194-95.

key components in attaining long-term economic success.⁷⁸ The performance objectives advocated in this Comment provide ways of addressing these criticisms.⁷⁹

On the other hand, there are many proponents of the NMTC program. Perhaps the most obvious reason for endorsing the program is that it takes some of the onus off the public sector in improving communities and gets the private sector involved in revitalization efforts. Proponents also argue that the private sector can operate, in many cases, more efficiently than the public sector and is not as constrained by jurisdictional boundaries.⁸⁰ Private companies are able to conduct business across state, city or county lines in a less constrained fashion than the public sector.

The NMTC program has also been lauded because it uses “local knowledge to leverage nonlocal resources in targeted areas.”⁸¹ A partnership with local community members is required because, under the NMTC code sections, the CDE must have representation of low-income residents from the community it is serving on its governing board.⁸² This means that investors must work with local actors and entrepreneurs. These actors and entrepreneurs usually have established networks in the local community and “understand the community norms and values and have learned the intricacies of the existing policies, crime patterns and practices” of their own communities.⁸³ However, the local actors and entrepreneurs might not understand or be able to overcome significant social and institutional factors that hinder community improvement. The NMTC program addresses this divide by partnering local actors with investors who have such understanding and ability.⁸⁴ Many scholars believe one of the biggest barriers to asset accumulation for asset-poor individuals is lack of access to tools like information, technology, and mainstream financial

78. *Id.* at 195.

79. *See infra* Part III.

80. Dimitri Pappas, *A New Approach to a Familiar Problem: The New Market Tax Credit*, 10 J. AFFORDABLE HOUSING & COMMUNITY DEV. L. 323, 329 (2001).

81. Robinson, *supra* note 44, at 113.

82. I.R.C. § 45D(c)(1)(B) (2006).

83. Robinson, *supra* note 44, at 113.

84. *Id.* at 115.

services.⁸⁵ This lack of access to resources that could improve their quality of life ensures individuals who are asset-poor remain asset poor and perpetuates the cycle of poverty.⁸⁶ The partnership of CDEs with local businesses and actors through the NMTC program gives asset-poor individuals access to the resources they need to break the cycle of poverty.

Finally, proponents of the program argue flexibility is one of its greatest advantages.⁸⁷ Once the credits are allocated, there are no performance objectives that must be met.⁸⁸ Thus, the NMTC program allows local entrepreneurs to create businesses that uniquely address the specific needs of their community. However, the absence of performance objectives means investors who participate in the NMTC program can make business decisions for their own benefit, rather than for the benefit of the community.

II. THE NEED FOR BENCHMARKS

In general, there is a paucity of data quantifying the impact of community economic development programs like NMTCs.⁸⁹ This is not surprising considering the difficulty of measuring the impact of these types of programs.⁹⁰ Economies, on any scale, are complex, and determining the causal chain of economic changes in any community is extremely difficult. For example, a positive change in a community—such as an increase in homeownership rates—could be the result of many factors at work: an influx of affordable housing, a reduction of crime, or improved schools, among others. Because economic changes in a given community over time can be the result of

85. Sarah Molseed, *An Ownership Society For All: Community Development Financial Institutions as the Bridge Between Wealth Inequality and Asset-Building Policies*, 13 GEO. J. ON POVERTY L. & POL'Y 489, 500 (2006).

86. *Id.*

87. Pappas, *supra* note 80, at 342.

88. Tluchowski, *supra* note 12, at 106.

89. Alan Greenspan, Chairman, Fed. Reserve Bd., Remarks at the 2005 National Community Reinvestment Coalition Conference: Empowering Communities, Attracting Development Capital, and Creating Opportunities (Mar. 18, 2005) (transcript available at <http://www.federalreserve.gov/boarddocs/speeches/2005/20050318/default.htm>).

90. *Id.*

hundreds of forces at work, determining where and how an NMTC development fits into the causal chain of economic change can be incredibly difficult, time-consuming, and expensive. An additional difficulty in determining the effectiveness of NMTCs lies in the fact that their effectiveness may not become apparent for a long period of time.⁹¹ The scarcity of available data underscores the fact that entities receiving NMTCs should be required to submit periodic records to the CDFI.

Despite the difficulty in quantifying the benefits of programs like the NMTC program, research related to community economic development programs is essential for two main reasons. First, programs like the NMTC program depend on research to be renewed by Congress.⁹² A lack of research threatens the viability of the program because it is reauthorized on a rolling basis. It is only with hard data that truly informed arguments for the extension of the NMTC program can be made.

Second, data—and a critical analysis of this data—are needed to establish some sort of benchmarking for the program.⁹³ As Alan Greenspan, former Chairman of the Federal Reserve stated, “Success of these programs can be understood only through measurement and critical analysis.”⁹⁴ Greenspan advocated for the need to establish *some* sort of benchmarking in community economic development programs, despite the complexity in doing so.⁹⁵ Greenspan stated, “In the quest to do good for our society's most-vulnerable populations and communities . . . analysts must embrace the challenge to develop objective and quantifiable standards for assessing community development programs.”⁹⁶ The challenge is to come up with simple benchmarking tools that do not take years to produce and do not essentially mine for data, which is costly and time-consuming. Local investors have undoubtedly learned lessons over the years regarding which strategies work for improving communities through the NMTC

91. *Id.*

92. *Id.*

93. *Id.*

94. *Id.*

95. *Id.*

96. *Id.*

program and which ones do not.⁹⁷ Their experiences can be learned from, and should be used to guide the creation of performance objectives. Adding benchmarks that address the policy concerns regarding NMTCs keeps focus on those low-income members of our community that President Clinton was concerned with “leaving . . . behind.”⁹⁸

As mentioned above, there are currently no performance objectives built into the NMTC code provisions.⁹⁹ Once a CDE has received the tax credits, it does not need to meet any further specifications and does not need to meet any economic, social, or public benefit criteria. The CDE only needs to meet certain basic requirements to avoid recapture of the credits, but these are minimal.¹⁰⁰ Such a laissez-faire approach to these credits may have been appropriate in the formative years of the program, but now, eleven years after the program’s enactment, more substantial benchmarking is needed. Some set of mechanisms is needed to determine which developments are successfully using these federal funds to achieve the community economic development goals of the NMTC program. Investors have had ample time to try out methods, work out kinks, and go through the expected growing pains associated with a new program. Investors should no longer be given *carte blanche*, especially when tax revenue is at issue. Otherwise, the program may be awarding tax credits to ineffective developments, when directing that otherwise-collected tax revenue into other anti-poverty programs would be a more effective use of the funds.

Examples of “inefficient” uses of the funds in Maryland include the France-Merrick Performing Arts Center (formerly the Hippodrome Performing Arts Theatre) and the University of Maryland’s BioPark, both located in Baltimore. The France-Merrick Performing Arts Center is a pre-World War I era, 2,250-seat theater that received a \$2 million NMTC allocation.¹⁰¹ The theater is making *some* economic

97. *Id.*

98. Dunham, *supra* note 23.

99. Tluchowski, *supra* note 12, at 106.

100. See I.R.C. § 45D(g) (2006) (enumerating circumstances under which the CDFI will force a recapture of the credits).

101. *Hippodrome Theatre, Baltimore, MD*, NAT. TR. COMMUNITY INVESTMENT CORP., <http://ntcicfunds.com/projects/hippodrome-theatre-baltimore-md> (last visited Jan. 15, 2011).

impact.¹⁰² However, the theater provides neither retail options, social services, nor affordable housing. The theater currently employs only about thirty full-time employees.¹⁰³ In addition to the relatively small number of jobs created by the theater, jobs in a creative field like this may not be the best for building employable skill sets that translate well into other fields. While the theater may be having small positive effects on the community, due to the competitive nature of the credits, there are many other developments that could serve a low-income community better than a performing arts theater.

The University of Maryland's BioPark is another example of an inefficient use of NMTCs. BioPark is a ten acre, 1.8 million square-foot science lab and office facility located in twelve different buildings on the University of Maryland's campus.¹⁰⁴ The development received \$15 million in NMTCs.¹⁰⁵ BioPark employs over five hundred people, including Ph.D-level scientists, lab technicians, clinical healthcare workers, administrative support, and various professionals in the fields of business development, marketing, and law.¹⁰⁶ The University of Maryland, as a public institution, already receives substantial government funding, so awarding these highly-in-demand tax credits intended for private investors to a public institution is not in sync with the rest of the NMTC program. Additionally, allocating NMTCs to an office and science park, which provides little meaningful support and few services or jobs to low-income community members, does not promote the policy goals of the NMTC program. BioPark also does not provide any retail options to local community members or provide affordable housing.

To avoid such inefficient uses of NMTCs, simple and easily identifiable performance objectives are needed. Congress cannot

102. The theater attracted 410,000 patrons in its first year of operations, and over the course of five years generated \$18 million in personal income for its employees and spent \$26 million on expenditures. *Id.*

103. E-mail from Stella Benkler, Gen. Manager, France-Merrick Performing Arts Center, to author (Jan. 11, 2011, 15:22 PST) (on file with author).

104. *BioPark Overview*, BIOPARK, U. OF MD., <http://www.umbiopark.com/biopark/> (last visited Jan. 15, 2011).

105. Whelan, *supra* note 4.

106. *BioPark Jobs*, BIOPARK, U. OF MD., <http://www.umbiopark.com/biopark/jobs.aspx> (last visited Jan 15, 2011).

mandate that investors undertake the complex process of amassing data, untangling causal chains of economic change in a community, and providing a complex analysis of the development's effects.¹⁰⁷ Such a mandate would increase the transaction costs of using NMTCs dramatically, and may render them inefficient. Instead, simple benchmarks should be included in the Internal Revenue Code, which investors would have to meet to avoid recapture of the credits. Simple benchmarks would make the program more accessible and less costly.

As mentioned above, there are already three recapture provisions in the current Internal Revenue Code for NMTCs. The recapture provisions of the Code should be expanded to allow for recapture of the tax credits if certain benchmarks, aimed at promoting community development and revitalization goals, are not met over a five-year time span. These various benchmarks ensure that community economic development is at the forefront, and that wealthy investors are not the only ones benefitting from the use of the credits. If NMTC developments do not meet the criteria laid out in at least two of these benchmarking categories for a period of five years, the CDFI should (1) take this into consideration when awarding subsequent NMTCs to that specific CDE, and (2) force a recapture of the allocated tax credits. The five-year time period should begin following a two-year "grace period," after the development opens its doors for business, during which these performance objectives need not be met. The purpose of this grace period is to allow the business to get on its feet. Recapture is a stiff penalty, so businesses should be given time to meet these performance objectives.

III. PROPOSED RECAPTURE PERFORMANCE OBJECTIVES

To retain their NMTCs, investors should be required to meet at least two of the recapture performance objectives listed below. Overall these benchmarks are simple, yet provide a much needed system of what Greenspan calls "objective and quantifiable standards for assessing community economic development programs" in order to do the most good for "society's most-vulnerable populations and communities."¹⁰⁸ In doing so, these benchmarks address the

107. It would be difficult to causally relate to the NMTC program effects such as a decrease in unemployment, increased wages or a decrease in crime in the area.

108. Greenspan, *supra* note 89.

overarching criticism of the NMTC program that the tax credits are primarily serving investors, instead of the low-income community members the credits are designed to help.

It is also important to take into consideration the extent to which the original NMTC development played a role in attracting subsequent developments to the local community. While this effect is important, it is by and large extremely difficult to gauge with any objectivity. Adding this factor as a formal benchmark would call for investors to engage in a much more sophisticated and complex analysis than should be required. However, to the extent that investors can prove this effect, it should be taken into account as an optional factor to offset poor performance in relation to the other proposed performance objectives. As mentioned previously, the potential “domino effect” articulated by Janet Thompson Jackson is perhaps one of the most important policy objectives behind the NMTC program itself,¹⁰⁹ so this factor needs to be taken into consideration in assessing NMTC developments, despite the difficulty in doing so.

Proposed Benchmark #1: Job Production

The first benchmark relates to job production. To avoid recapture under this benchmark: (1) new or existing businesses must create a minimum of seventy-five full-time, low-moderate income jobs;¹¹⁰ (2) existing businesses that use NMTCs to expand or renovate their current facilities or to move into new ones must create thirty percent more full-time, low-moderate income jobs; or (3) new or existing businesses must create a minimum of 2,000 jobs at any income level. Low-moderate income jobs will provide local community members with jobs they can actually vie for, because it is likely that many local community members in these distressed areas will not be highly educated.

This benchmark is important because it addresses the criticism that NMTCs only target specific geographic spaces, instead of targeting specific residents and providing them with job placement

109. See Jackson, *supra* note 40, at 701.

110. Low-moderate income levels vary by city. For a table of income limits, see *Income Limits*, U.S. DEPT. OF HOUSING AND URB. DEV., http://www.huduser.org/portal/datasets/mtsp/mtsp10/HERA_Income_Limits_Report.pdf (last visited Jan. 15, 2011).

and job training.¹¹¹ It also furthers the policy goals of community economic development by providing increased employment opportunities, which in turn attracts residents, stimulates housing rehabilitation and development, and reinforces the idea that community life is organized around work.¹¹²

An example of this benchmark being met and far surpassed is East Baltimore Development Inc., which consists of an 88-acre site in East Baltimore, Maryland.¹¹³ The development consists of new and rehabilitated housing, retail space, and a life sciences and technology park.¹¹⁴ The project contains over 1.7 million square feet of biotech, retail and office space, and provides a K-8 public school and 2,100 units of mixed-income housing units.¹¹⁵ In addition to the social benefits of the development, it will create between 4,000 and 6,000 new jobs.¹¹⁶ This development would thus meet the proposed benchmark of providing at least 2,000 new jobs at any income level.

Proposed Benchmark #2: Mandatory Reinvestment in the Community

The second benchmark relates to reinvestment in the local community. To avoid recapture, NMTC developments must invest in local community businesses through their contractual relations. Every business needs to purchase goods and services to facilitate its day-to-day operations. To meet the performance objectives of this benchmark, NMTC developments must prove they are purchasing at least \$200,000 or twenty percent of these goods, services and equipment from local businesses. The majority of a business's large capital start-up expenditures will accrue during the early years of the company. Thus, the two year grace period will allow businesses to purchase these expensive and potentially very specialized items wherever they please.

111. Forbes, *supra* note 76, at 194-95.

112. See Jackson, *supra* note 40, at 701-02.

113. *New Markets Tax Credits Portfolio: East Baltimore Development Inc.*, ENTERPRISE COMMUNITY INVESTMENT, http://www.enterprisecommunity.com/products_and_services/nmtc-portfolio-eastbaltodev.asp (last visited Jan. 15, 2011).

114. *Id.*

115. *Id.*

116. *Id.*

This benchmark is important because it addresses the criticism that the NMTCs themselves are too small to make a significant impact on local communities. This benchmark provides that community investors must indirectly use NMTCs to keep the local economy active by purchasing local goods and services. This addresses the criticism that the tax credits are too small to have a major transformative impact because the NMTC developments, combined with their spending power if kept in the community, can potentially have a huge transformative impact. This benchmark furthers the policy objectives of the NMTC by mandating that a “domino effect” occur as the result of this influx of capital into the community. This creates a stronger economic base in the community that can exert more pressure to improve schools, enhance transportation and public safety, as well as attract more businesses to the area.¹¹⁷

An example of this benchmark being applied and met can be seen in Volunteers of America’s Residential Re-Entry Center and Headquarters Renovation in Baltimore and Lanham, Maryland, respectively. This company received an \$11.3 million NMTC allocation to renovate its headquarters facility and relocate its prisoner re-entry program to a new facility.¹¹⁸ The company’s prisoner re-entry program offers residents case management services such as housing assistance, substance abuse counseling, educational programming, and employment assistance.¹¹⁹ The demand for these types of programs outweighs the supply in Maryland, so Volunteers of America’s expansion into a new building, which could accommodate more participants, was greatly needed by the community and state.¹²⁰ In addition to the social benefits, the Center has great economic effects on its surrounding community as well. Both Volunteers of America’s headquarters building and its Prisoner Re-Entry Center are located in census tracts labeled as “Severely Distressed.”¹²¹ A large part of its positive impact on its community is through its contractual relations with local businesses. Annually, the Prisoner Re-Entry Center and

117. See Jackson, *supra* note 40, at 701-02.

118. New Markets Tax Credit Finance Request Package for VOAC Residential Re-Entry Center, front cover (May 11, 2010) (on file with author).

119. *Id.* at 1.

120. See *id.* at 2.

121. *Id.* at 16-17.

Headquarters facility purchases more than \$298,000 worth of goods and services from local businesses, and has proven this through an itemized list of expenditures to local businesses.¹²²

Proposed Benchmark #3: Social Services to Low-Income People

The third benchmark relates to the social impact of these NMTC developments. Many of the NMTC developments in Maryland provide some sort of social service to their respective communities, including educational, medical, religious, and other social programs. Thus, it is important not only to look at the economic impacts of a NMTC development, as the other benchmarks do, but also to take into consideration the social benefits a given development provides. To meet this benchmark, the NMTC development must prove that at least fifty percent of its educational, medical, religious, or other non-profit services are provided to low-income community members.

This benchmark is important because it addresses the criticism that NMTCs do not combat other social ills in communities—factors that might contribute to a lower quality of life. Additionally, this benchmark addresses the criticism that NMTCs do not adequately help the low-income individuals the program is intended to serve. These social programs focus specifically on helping low-income members of these communities.

An example of this benchmark being applied and met can be seen in the CASA Multicultural Center in Langley Park, Maryland. CASA is the largest advocacy group for Latinos and immigrants in Maryland, and received \$7.9 million to redevelop the historic McCormick-Goodhart Mansion in Langley Park.¹²³ CASA works with community members to “improve the quality of life and promote equal treatment and full access to resources and opportunities for low-income Latinos and their families.”¹²⁴ The Center provides educational, vocational, employment and English as a Second Language (ESL) services.¹²⁵ With the new facility, the Center was able to double the amount of

122. *Id.* at 25.

123. *New Markets Tax Credits Portfolio: CASA Multicultural Center, ENTERPRISE COMMUNITY INVESTMENT*, http://www.enterprisecommunity.com/products_and_services/nmtc-portfolio-CASA.asp (last visited Jan. 15, 2011).

124. *Id.*

125. *Id.*

beneficiaries it serves each year from 3,000 to 6,000, seventy-five percent of whom earn less than \$25,000 a year.¹²⁶

*Proposed Benchmark #4: Development Includes
Affordable Housing Units*

The fourth benchmark relates to affordable housing. This benchmark is rather straightforward in that it is met as long as the development provides some sort of affordable housing.

This benchmark is important because it addresses the criticism that NMTCs are used mostly for wealthy investors and not the low-income people the credits are designed to help. Ordinarily, investors would seek to make more money by offering apartments at market-rate. However, in pursuit of this performance objective, they would decrease their profits by offering affordable housing units. This puts more emphasis back on the needs of the low-income community itself, instead of the investor. Additionally, this benchmark creates a stronger residential base in the community, the benefits of which Janet Thompson Jackson articulates above.¹²⁷

An example of this benchmark is Miller's Court in Baltimore. The complex is a 77,000 square-foot mixed-use development designed for teachers' housing.¹²⁸ Investors used \$9.4 million in NMTCs to rehabilitate the H.F. Miller and Sons Building, a former tin box manufacturing plant built in the early 1900s that sat vacant since the early 1990s.¹²⁹ The development contains forty apartments, 34,000 square feet of office space, and 1,000 square feet of retail space.¹³⁰ Ten of the forty apartments would qualify as affordable housing.¹³¹

126. *Id.*

127. *See* Jackson, *supra* note 40, at 701-02.

128. *New Markets Tax Credits Portfolio: Miller's Court*, ENTERPRISE COMMUNITY INVESTMENT, http://www.enterprisecommunity.com/products_and_services/nmtc-portfolio-Miller%27s-Court.asp (last visited Jan. 15, 2011).

129. *Id.*

130. *Id.*

131. *Id.*

*Proposed Benchmark #5: Commercial Development Lessor Proves
Increased Occupancy*

The fifth proposed benchmark relates to existing commercial developments. Under this benchmark, a commercial lessor must prove that, due to the use of NMTCs, it was able to increase the occupancy of a multi-business development over the course of five years. The business must prove that the occupancy rate over each year of the five-year period is at least thirty percent higher than the year before the NMTC was allotted, or has reached a total occupancy of seventy-five percent of the available space as a result of the NMTC allocation.

This benchmark is important because as the occupancy of existing commercial developments increases, so does the potential for more jobs and greater retail options within the low-income community. By keeping spending within the community, low-income community members are able to promote the economy of their own communities, instead of flushing their cash to outside communities.

An example of this benchmark being applied and met is Belvedere Square, an existing retail center located in Baltimore, Maryland. The site was originally constructed in 1984, and in 1992 began to see a decline in occupancy due to a combination of economic recession, an increase in security costs, and poor landlord-tenant relations.¹³² The current developer applied for an NMTC allocation in an attempt to rehabilitate the shopping center.¹³³ The rehabilitation included improvements to the tenant spaces, new heating systems, curbs, gutters, landscaping, and a brick crosswalk.¹³⁴ Over 28,000 residents live within a one-mile radius of the development, and the surrounding community includes a mix of commercial and residential.¹³⁵ Prior to the rehabilitation of the center, the development “was significantly under-leased and contribut[ed] little to the economic activity in the community.”¹³⁶ However, after the rehabilitation the NMTCs were able to provide, the center went from thirty percent to eighty percent

132. *New Markets Tax Credits Portfolio: Belvedere Square*, ENTERPRISE COMMUNITY INVESTMENT, http://www.enterprisecommunity.com/products_and_services/nmtc-portfolio-belvedere.asp (last visited Jan. 15, 2011).

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

occupancy.¹³⁷ Belvedere Square now contains retail and dining options and continues to generate employment opportunities for area residents.¹³⁸

Proposed Benchmark #6: Development Provides Consumer Goods to Low-Income Community Members

The sixth benchmark relates to the sale of consumer goods.¹³⁹ This benchmark is also rather straightforward in that it is met as long as the development is predominantly used for the sale of consumer goods.

This benchmark is important because it addresses the current dearth of retail options in low-income communities. Providing retail options to low-income community members, especially through community-owned retailers, will help keep spending within the community. When spending is kept locally, it can add to the economic vitality of that community.¹⁴⁰

An example of this benchmark being met and applied in Maryland is Belvedere Square, outlined in Proposed Benchmark #5.

CONCLUSION

In summary, performance objectives related to community economic development goals must be added to the NMTC code provisions. Quite simply, the NMTC program needs measurement and critical analysis incorporated into its framework. These benchmarks do not limit the flexibility of the program; they simply provide mechanisms for ensuring the credits are allocated to investors who will use them in ways that will provide the most impact for society's most vulnerable populations and communities. Without these mechanisms in place, there is no way to gauge whether the policy goals of the NMTC are being met, or whether the credits are being used mostly to benefit wealthy investors. The NMTCs are highly competitive, which only bolsters the need to have some set of

137. *Id.*

138. *Id.*

139. Consumer goods are "goods that are used or bought for use primarily for personal, family or household purposes." U.C.C. § 9-102(a)(23) (2000).

140. *See Jackson, supra* note 40, at 701-02.

mechanisms in place to determine which entities are putting the credits to the highest and best use, and which ones are not. Maryland has provided several good examples of successful NMTC developments. Eleven years after the initial enactment of the NMTC program, there is no excuse not to learn from these successful developments, and put those lessons into action through these performance objectives.

These proposed benchmarks—related to job production, mandatory reinvestment in the community, social service offerings to low-income people, affordable housing, the increased occupancy of commercial developments, and the sale of consumer goods—are simple enough that they do not create unreasonable hurdles that investors must overcome. Instead, they simply require a small amount of recordkeeping. All proposed benchmarks address the original legislative intent of the NMTC program, which placed a focus on joblessness, poverty, and low-incomes in these communities. These benchmarks ensure that these poor and vulnerable populations are not, once again, left behind.

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