Could the New Markets Tax Credit benefit your business?

Businesses in economically distressed communities often have difficulty obtaining capital for expansion, equipment, facilities and other investments. The New Markets Tax Credit (NMTC) encourages private investment in these underserved areas by offering federal income tax credits to qualifying investors.

This credit was previously scheduled to expire on December 31, 2025. However, the One Big Beautiful Bill Act made it permanent. Let's take a closer look at how this tax break could benefit your small business.

Potential tax and financing benefits

The NMTC is generally available to individuals and businesses that make qualified equity investments in community development entities (CDEs). A CDE is generally a domestic corporation or partnership whose primary mission is to serve low-income communities or provide investment capital to them. To participate in the program, a CDE must be certified by the U.S. Department of the Treasury's Community Development Financial Institutions Fund.

The CDE then raises funds from investors to use for qualifying loans, equity investments or other approved activities in low-income communities. Your benefits depend on your role in the transaction. If your business *invests* in a CDE, you may be able to claim the tax credit. If your business *receives financing* from a CDE, you may benefit indirectly by gaining access to capital or financing terms that might not otherwise be available. For many small business owners, these financing opportunities may be the more relevant aspect of the NMTC program.

Credit amount and filing requirements for investors

The NMTC equals 39% of the investor's qualified equity investment in the CDE. The credit is claimed over seven years as follows:

- 5% of the investment in each of the first three years, and
- 6% in each of the next four years.

So, a qualifying $1 million investment could generate $390,000 in federal tax credits over seven years, subject to applicable limitations.

To claim the credit, you must make a cash investment that the CDE designates as a qualified equity investment. The CDE must use "substantially all" of the funds for qualified low-income community investments (QLICIs). In general, a CDE satisfies this threshold if it invests at least 85% of its aggregate gross assets in QLICIs (reduced to 75% in the seventh year).

The credit is calculated using Form 8874, "New Markets Credit," and reported as part of the general business credit on Form 3800.

Claiming the NMTC reduces your tax basis in the investment, which may affect the tax consequences of a later sale. In addition, previously claimed credits may be recaptured (with interest) if the CDE fails to meet program requirements or redeems your investment during the seven-year credit period.

Financing benefits for qualifying businesses

By encouraging investment in CDEs, the NMTC may expand access to financing for qualifying businesses and nonprofit organizations in low-income communities. Examples of businesses and projects that may receive NMTC-supported financing are:

- Real estate developments,
- Manufacturers,
- Retailers,
- Health care providers,
- Child care centers and schools,
- Hotels, and

- Community centers.

For example, suppose you own a grocery store in a qualifying community and need funds to renovate the building. A CDE could use capital raised from investors to provide your business with a loan or equity financing for this project. In this scenario, qualified investors would receive the federal tax credit, and your business would benefit from access to financing that might otherwise be difficult to obtain through conventional sources.

Simply operating in a low-income area doesn’t automatically qualify a business or project for NMTC-supported financing. The CDE must determine whether the business, location and planned use of the financing satisfy the program’s requirements.

Exploring NMTC opportunities

The now-permanent NMTC may offer a valuable tax break for qualified investors and provide an important source of financing for qualifying businesses and community development projects. However, the rules are complex. Contact us to learn more. We can help you estimate the potential tax or financing benefits and address the applicable compliance requirements.