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2008 NATIONAL INTERAGENCY COMMUNITY REINVESTMENT CONFERENCE

INTRODUCTION TO BASIC INVESTMENTS

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CHASE

Agenda

New Markets Tax Credits Background: Program Basics

- The New Markets Tax Credit (NMTC) was created by Congress as part of the Community Renewal and New Markets Act of 2000
- It is a program of the U.S. Treasury and the CDFI Fund (Community Development Financial Institutions) to generate $19.5 billion in new private-sector investments in low-income communities, which includes a special set-aside for the GO Zone
- The NMTC provides a 39% tax credit over 7 years (5% each of the first 3 years, 6% each of the remaining 4 years)
- All NMTC funds must be invested for 7 years; if funds are returned early they must be reinvested within 12 months or risk full recapture of all tax credits claimed

How NMTCs are Obtained:

- The CDFI Fund allocates NMTCs to qualified Community Development Entities (CDEs) with a primary mission of providing investment capital to low-income communities
- Allocations are through a competitive process, with applicants being judged on their underlying business strategy, track record and community impact
- Tax credits are generated by equity investments in a CDE, which invests (or makes loans) in qualifying businesses and commercial real estate projects

NMTC Background: Qualified Uses

- The NMTC can be used for a broad range of eligible projects in specified target areas – **but it is focused on commercial development**
- Qualifying census tracts have 80% or less of AMI and/or 20% or greater poverty rate
- Based on the 2000 Census, about 39% of all census tracts are eligible and about 36% of the nation's population live in eligible census tracts
- QALICBs are generally one of the following three asset types:
  - Commercial Real Estate Projects
    - Projects located in a qualified census tract that derive at least 20% of its gross income from commercial activities
    - Office, retail, light industrial, mixed-use
  - Community Development Financial Institutions
    - Loan pools or community banks that serve low-income persons or communities
  - Businesses and Non-Profits
    - Businesses and non-profits that are located in and serve low-income communities

JPMC and the NMTC Program

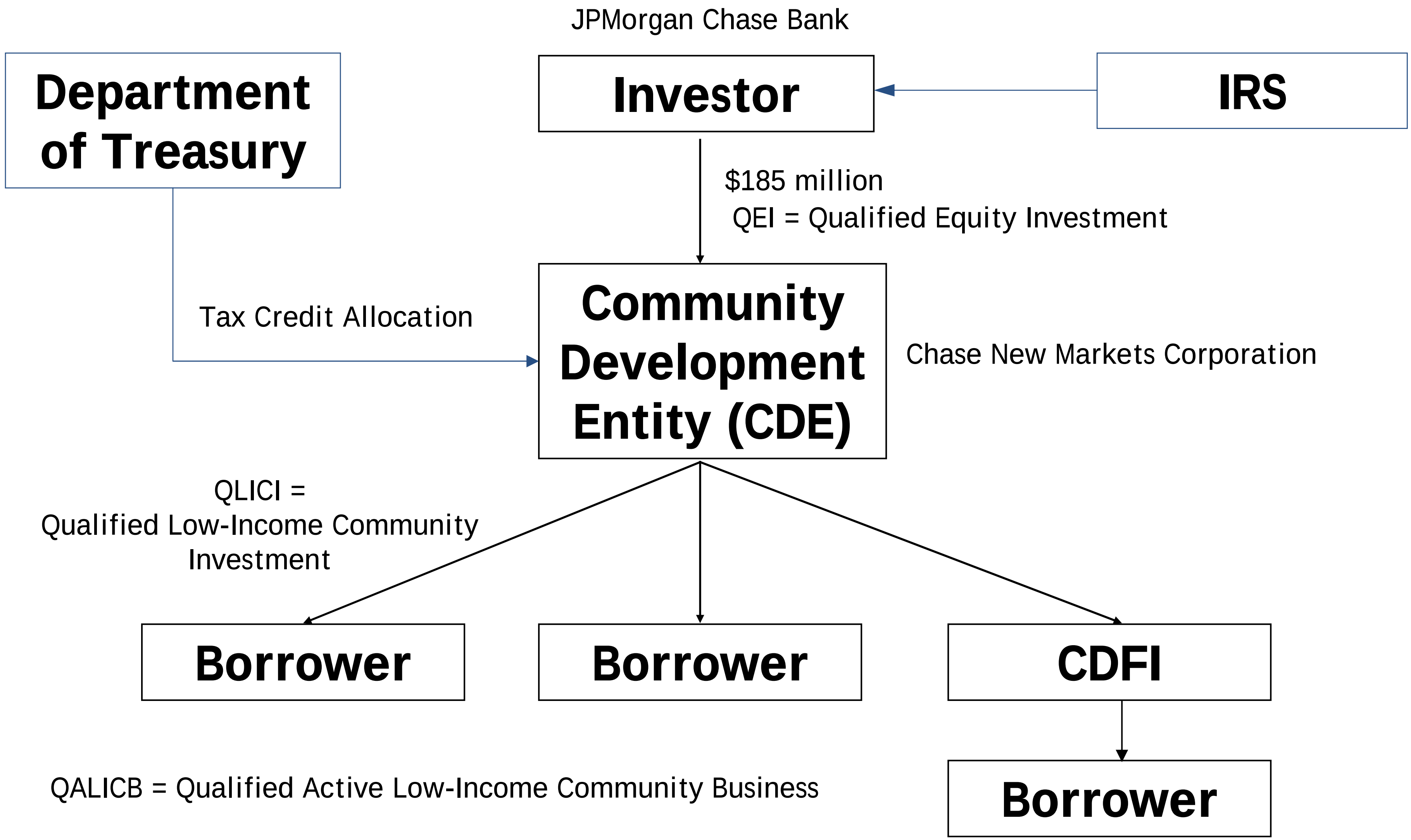
JPMC works with the NMTC in two distinct ways:

- A subsidiary of JPMC has received allocations and originates loans using the subsidy to reduce the interest rate charged to clients
- JPMC makes strategic investments in other organization's NMTC allocations, which allow JPMC to provide equity into a client's project

JPMorgan Chase is one of only a few organizations to have received three consecutive allocations of NMTCs:

- In 2005, JPMC received a $75 million NMTC allocation with a national footprint,
- In June 2006, JPMC received a $50 million NMTC allocation for use in the Gulf Opportunity Zone (GO Zone),
- In October 2007, JPMC received a $60 million NMTC allocation with a national footprint
- JPMC uses these funds to provide below-market interest loans to our customers

JPMC’s Proprietary NMTC Allocations - Structure Overview



JPMC Invests in 3rd Party NMTC Allocations

- JPMC is also interested in strategically partnering with other NMTC allocatees and investing in their tax credits to support lending opportunities
- Most organizations that receive NMTC allocations are not financial institutions – many are non-profits and quasi-governmental agencies that “sell” their tax credits to investors
- Because the New Markets Tax Credit is a shallow credit (i.e. only 5-6% per year of the amount of the investment), an investor must rely on both the tax credit and the financial viability / economic return of the project
- Therefore, JPMC prefers to split the transaction into two portions

  1. A loan that is based upon the credit worthiness of the borrower / project

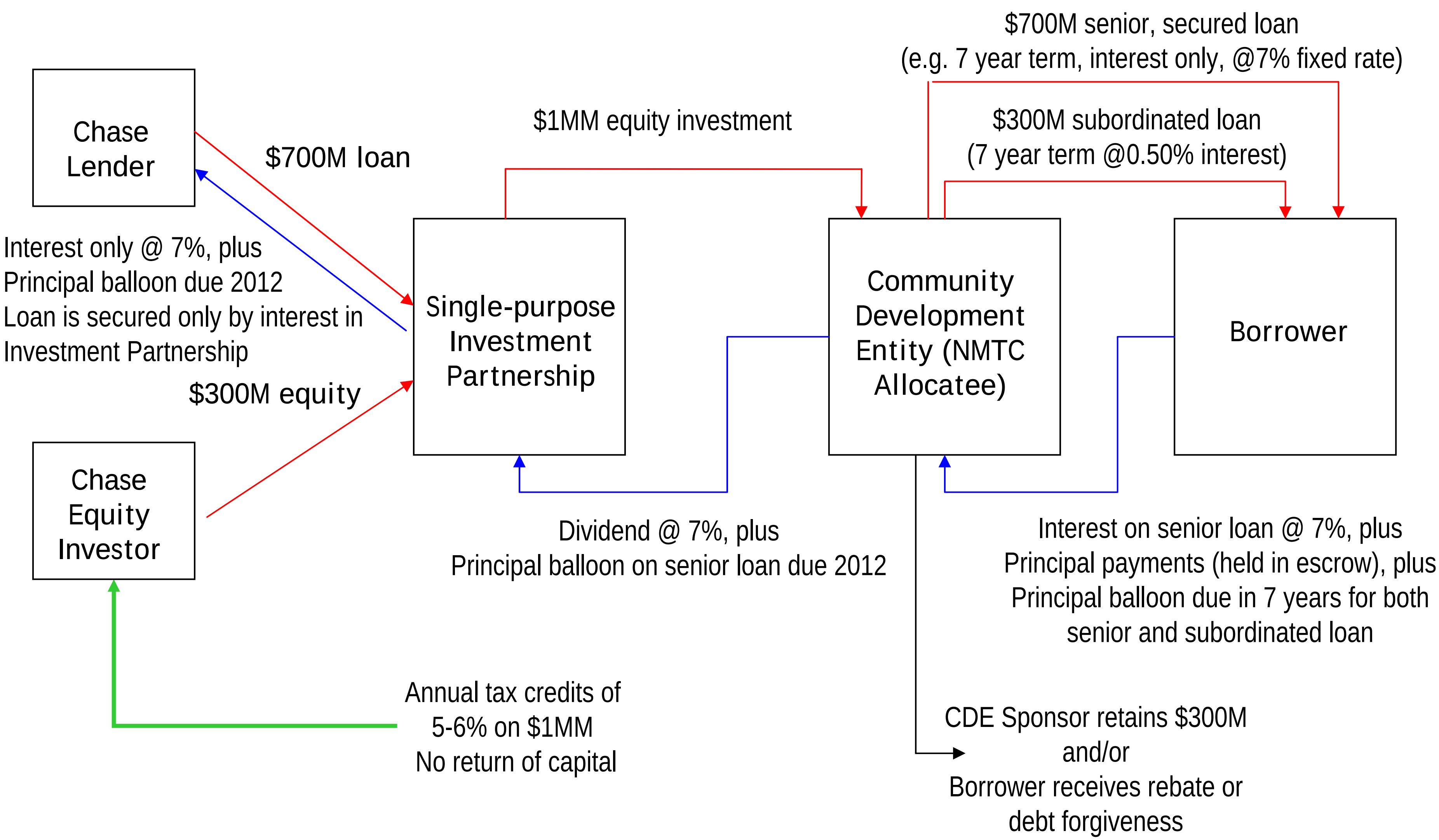
  AND

  2. An equity investment that is based entirely upon the expected receipt of tax credits

- This bifurcated structure also assigns responsibility in the transaction based upon expertise (creditor focuses on financial viability of project, equity investor focuses on tax credit compliance)

NMTC Investment with 3rd Party Allocatee - Transaction Diagram

- Creditor underwrites and approves loans to borrower
- Creditor accounts for 70% of funding to CDE which is passed thru to borrower
- Equity Investor accounts for 30% of funding to CDE which is passed thru to borrower



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Overview of JPMC's Community Development Private Equity Investing

- An active investor in community development investment funds since the mid to late 1990's
- Portfolio includes 50+ relationships using a fund-of-funds approach with total commitments exceeding $135 million
- Current investment activities aimed at balancing the need for attractive risk-adjusted returns with the firm's long term mission of being a leader in community development
- Market presence includes three regions (Northeast, Midwest, and Southwest)
- Product mix includes funds that invest in venture capital (later stage), private equity, and real estate funds

Private Equity Funds

There are three classes of private equity investment vehicles:

Community Development Venture Capital Funds ("CDVCs") - Strategy is to invest in businesses with strong growth potential that promise to provide outstanding financial returns for investors. These funds use a "Double bottom line" investment strategy.

Small Business Investment Companies ("SBICs") - SBICs are private investment companies co-funded or credit enhanced by the Small Business Administration ("SBA"). SBICs provide businesses with debt or equity financing options. SBICs receive up to $2 of leverage for every $1 of private capital raised.

Community Development Private Equity Real Estate Funds - Strategy includes rehabilitating, developing and leasing properties in LMI areas. Typical size of fund is either $15 mm (housing) or $100 mm + (commercial)

Factors to Consider When Investing in Private Equity Funds

- Mission: Funds with a primary mission of community development (investing in LMI communities or benefiting LMI individuals). Many funds are more active in "underserved markets" but not necessarily in community development funds that generate CRA eligible activity
- Management - Private equity/venture capital <u>teams</u> with strong track records:
  - 10+ years of investment experience
  - Realized exits with cash returns to investors
  - Consistency in strategy and execution
- Structure - The typical structure dictates:
  - Funds providing a return OF capital beginning within 5 years (final return of capital within 10 years)
  - Financial and legal terms that are consistent with the mainstream market
- Double Bottom Line: Balancing <u>your firm's need</u> for attractive returns with community development/CRA needs
  — Risk vs. return vs. impact