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## HISTORIC TAX CREDIT TOOL BOX

# Historic Tax Credits: The Basics



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Anyone redeveloping an existing building should consider the possibility of using historic tax credits (HTCs) as part of their funding toolbox.

### What is the federal historic tax credit?

The federal government offers a 20 percent investment tax credit for certified rehabilitation of certified historic buildings. As the name implies, it is not a tax deduction, but a dollar-for-dollar credit applied to federal taxes. Only certain expenditures count toward the tax credit. Acquisition costs, site development, new construction outside the envelope of the building and furnishings and fixtures are the most common exclusions.

What is included are the soft and hard costs associated with the building itself. This includes systems (structural; mechanical, electrical and plumbing; HVAC; elevators; fire and life safety), exterior envelope repairs (e.g., brick, mortar, windows), and generally most interior work (e.g., new floors, walls, ceilings) that is not related to fixtures and furniture. Soft costs include developer fees, architectural fees, permitting and application fees. For purposes of HTC application, these costs may be estimated; for

purposes of claiming the credits, typically a formal cost certification by a certified public accountant is required.

One critical positive aspect of the federal HTC program is that it is a credit by right. An owner with an approved project has assurances of the credit award. This is distinguished from other tax credit programs such as the new markets tax credit (NMTC), which is a competitive process where finite credits are allocated.

A second positive aspect is that the HTC program may be combined with various other funding sources. Examples of other programs commonly combined with the HTC include state HTC incentives, NMTC, low-income housing tax credits and brownfield tax credits.

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### What is a certified historic structure?

For a building to secure HTCs, the building must be determined to be a certified historic structure. A certified historic structure is a building individually listed on the National Register of Historic Places or a contributing building to a National Register or certified local historic district.

**Individual buildings:** For buildings not located in a historic district, it is not necessary that the building already be listed on the National Register in order to pursue HTCs. The HTC program accommodates consideration of nondesignated properties by offering a “preliminary determination of eligibility.” To secure this preliminary determination, an applicant must submit a formal application to the state historic preservation office (SHPO), which will then forward the application to the National Park Service (NPS). This application device is the “Part 1: Evaluation of Significance.” The submission consists of the application cover sheet, a draft National Register nomination, and sufficient color exterior and interior photographs to allow an understanding of the property.

Generally, buildings need to be at least 50 years old to be considered historic. It may come as a surprise that as of 2019, this cutoff is 1969 and today includes a wide spectrum of post-World War II construction. However, the process also has flexibility to consider buildings less than 50 years old. In the simplest terms, if construction began more than 50 years ago, even if the building was not completed for two or three years, then it considered potentially eligible. Alternatively, a property that represents a continuation of a historic trend that began before 1969, such as a public housing complex, might be considered eligible. Even more modern structures might be considered eligible, provided thoughtful justification can be provided, though obviously the more recent the construction, the greater the challenge.

The important point is that the National Register program, and as such, the HTC program, has broad flexibility in recognizing buildings as historic. The onus to make the case lies with the applicant, which means that the developer will want to engage a qualified historic preservation consultant that understands the program nuances but can also construct a compelling explanation of a property’s significance.

To become a certified historic structure a property must ultimately be listed in the National Register. The preliminary determination (e.g., a Part 1 approval) is the first step in the HTC process but does not eliminate the need for listing. It is also important to consider the project schedule as different states take different approaches to the listing process. Some states allow the National Register process to run parallel to the redevelopment, while others require that the National Register process proceed only after construction on the property is complete.

**Contributing Buildings in a District:** When the project involves a contributing building in a historic district, the process is considerably simpler. Similar to the preliminary determination of individual significance, this process also requires the submission of a Part 1 application to SHPO, which then forwards the application to NPS with their recommendation. This submission confirms that a property still contributes to the historic district. Typically, this justification is that the property has not substantially changed since the district was listed. This Part 1 application consists of the cover sheet supported by a narrative that discusses the district, the building and recent changes to the building. Again, the application is also supported by sufficient color exterior and interior photographs that allow an understanding of the property. Once NPS approves the Part 1 application for a contributing building in a district it is considered a certified historic structure.

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### What is a Certified Rehabilitation?

A project is certified by the NPS when the completed work meets the Secretary of the Interior's Standards for Rehabilitation, a set of 10 broadly framed standards that address use, retention and treatment of historic character and materials (including those elements that may have achieved significance over time), and the compatibility of new construction, including additions. These standards apply to all work within the scope of the project. Either a project as a whole meets the Standards or it does not. It is an all-or-nothing program and there are no partial credits.

The credits do not actually exist until all construction work is complete and the NPS issues a final certification. The program, however, recognizes that to be effective, work must be proposed and reviewed before execution. The final certification process should simply be confirmation that work was completed as proposed, reviewed and approved by the NPS.

This review of proposed work occurs through the Part 2: Description of Rehabilitation application. This application consists of a cover sheet, project narrative, supporting architectural and related plans, and photo-documentation of existing conditions. The plans are supplemental to the narrative and work in the plans that is not described in the narrative may not be considered approved even if the application is approved. Clarity is the responsibility of the applicant.

Like the Part 1 application, the Part 2 application is submitted to SHPO, which then forwards it to the NPS with a recommendation. The NPS makes the ultimate decision and the potential outcomes of a review are approval, approval with conditions or denial. Depending upon the application, conditions associated with an approval may run the gamut. Some may be formalities, such as a requirement to submit tenant improvement

designs for as yet unleased space to SHPO and the NPS for review and approval. Others may relate to some general work items, such as requiring a sightline study on a proposed rooftop addition. Others may deny a specific work item but approve the larger project, such as not approving proposed window replacement but otherwise approving the project.

As mentioned, developments are reviewed against the Secretary of the Interior's Standards alone. Standards, codified in 36 CFR 67, have been used for more than 40 years and while the *Standards* themselves have not significantly changed, their interpretation has evolved as historic preservation has.

The Standards pertain to all materials, construction types, sizes and occupancy, and encompass the exterior and interior, related landscape features and the building's site and environment as well as attached, adjacent or related new construction. The Standards are applied to projects on a case-by-case basis. Because the standards have evolved, work that may have been approved on projects even five years prior may not be currently approvable. Work driven by aspects of economic viability, sustainability, code requirements and market requirements falls outside the evaluation process.

Most historic preservation consultants stay current with SHPO/NPS interpretations. Published guidance can be found in "Illustrated Guidelines for Rehabilitating Historic Buildings," which is also available at the NPS website. The process is intended to be iterative. It is rare to submit a project with construction level drawings encompassing all work. For large-scale projects, there are inevitably design changes required in the course of SHPO/NPS review. More often, projects are submitted at the stage where the scope of work is sufficiently developed to understand how the property is to be

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redeveloped. The initial Part 2 application is then followed up with amendments that typically address any design changes, value engineering or responses to project conditions.

The Part 2 and any amendments should present sufficient documentation so that the SHPO and NPS reviewers have a full and accurate understanding of the development as it evolves so that the completed project conforms to what was expected. While informal communication can be quicker (e.g., a phone call), it is prudent to have written documentation to address changes during construction.

The process is also intended to be flexible enough to accommodate varying scales, types and complexities of projects. Applications may be phased and most are. A single-phase project must be completed within 24 months and there are no exceptions. More typically, projects are multiphase, the developer being the one to determine the phasing, though the proposed use usually drives the definition.

It is also important to recognize that the reviewers assess proposed work using only the documentation provided and site visits are rare, so the thoroughness of the submissions benefits both the applicant and the reviewer. The preservation of historic character and fabric is the reviewer's first and primary lens, so providing more information on work that affects such features is preferred. By way of example, on the West Coast, more and more communities are requiring seismic upgrades to specific magnitude levels. These upgrades are nearly always enormously destructive. Hence, rather than simply submitting the proposed seismic strategy, it is helpful to provide an alternatives analysis, which show what options were considered in the seismic upgrade and why the submitted option is the one that makes the most sense.

Once the project is entirely complete and the construction crews have left the site, the developer files a "Part 3—Request for Certification of Completed Work." This application consists of a cover sheet and photo documentation of the completed project sufficient to illustrate the entirety of the scope. This is submitted to SHPO, which then forwards the application to the NPS with its recommendation. Frequently, as part of its assessment, SHPO will request a property tour. It is possible to obtain Part 3 approval before securing a lease for properties with leased commercial space, but to achieve this, work typically must be completed to a "white box" level which requires that walls and ceilings are finished, if only temporarily until leasing plans can be submitted post certification.

### How are projects reviewed?

The application process calls for everything to be submitted in duplicate to SHPO. SHPO then reviews the application and makes a written recommendation. During this time, SHPO may ask for design modifications, additional documentation or additional information. Typically, the SHPO takes 30 days, though sometimes there is a project backlog. Any request for additional information restarts the review calendar. The entire packet is then forwarded to NPS for decision.

Sometimes the NPS will ask for additional information that may be submitted directly to the NPS. Typically, the NPS will also take 30 days, though occasionally longer depending on workload. Again, request for additional information restarts the review calendar. There are fees associated with the tax credit application. Typically, half of the required fee must be paid before NPS review of the Part 2 and the other half before NPS review of the Part 3.

### Conclusion

The HTC offers substantial financial benefits. It may be considered a complicated program with a number of

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nuances and inherent complexities, many of which have not been discussed. The financial upside and flexibility of the program, however, is significant and well worth contemplating in any redevelopment concept. To capitalize on the HTC program, it is always best to start the process as early as possible and to develop a strong HTC team that includes a historic preservation consultant, architect, accountant and attorney. ❖

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