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EXCERPT

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HISTORIC TAX CREDIT TOOL BOX 🌿

The Importance of State Historic Tax Credits



CINDY HAMILTON, HERITAGE CONSULTING GROUP

Minnesota's Legislature adjourned May 23 without extending the state's historic tax credit (HTC). Now that the program's sunset date passed, HTC developments in Minnesota can no longer twin federal HTCs with the state's expired 20% offering.

The loss of Minnesota's state HTC will have significant effects on the potential to rehabilitate historic buildings across the state. It is an excellent reminder of the importance of the state HTC programs and the impact that they have on economic development across the country. Fortunately, this expiration seems to be an outlier, as additional states enact

HTC programs and there is significant support for reestablishing the Minnesota credit.

Thirty-seven states currently feature a state HTC program. Like the federal program, most respective state HTC programs involve a review-and-approval process, though each state varies in the level of information required in their application process. Additionally, the amount of credits available, as well as the credits available per project, varies. Regardless of the differences between each program, state

Image: Courtesy of Heritage Consulting Group

Elyria, Ohio's historic Dixon Building will be rehabilitated through twinned federal and state HTCs. The adjacent Robinson Building (the blue aluminum panel building at right), will also seek an award through the Ohio state HTC program.

HTCs, which are most often twinned with the federal program, are an integral part of the capital stack and are frequently a deciding factor in whether or not a rehabilitation development makes financial sense.

Many states' HTC programs are competitive, with a limited amount of funds for the hundreds of projects annually applying. Project teams, therefore, actively work to compile information necessary to ensure that the project will receive an award. For example, in states such as Illinois and Ohio, this requires projects to meet a certain number of points that are weighed against other applicants. In other states, the program is by-right and largely mirrors that of the federal HTC program.

Regardless of the HTCs afforded to each project, state HTC programs remain one of the industry's best tools to facilitate adaptive reuse of historic buildings. Two specific projects, the Dixon Building in Elyria, Ohio, and the Dayton Department Store in Minneapolis, Minnesota, highlight the impact state HTCs can have on a project. These projects also illustrate the differences in state HTC programs and the requirements that they entail.

By-Right State HTCs: Dayton Department Store

HTC developments in the 37 states with state programs are afforded an opportunity to secure additional funding and further reduce gaps in the capital stack. For the most part, state HTCs require a similar level of documentation as federal HTCs. This allows properties to “piggyback” off the federal application and ensure additional funds, so long as the project meets the Secretary of the Interior's *Standards for Rehabilitation*. Even if a state's program is competitive, the additional funds can play a significant role in the project's overall financing.

Before the sunset of the Minnesota HTC, the program largely functioned in this way, affording projects the opportunity to piggyback off the federal program. While the Minnesota credit was essentially “by-right,” a project could not get a state credit allocation from

the Department of Revenue until it received Part 2 approval from the NPS, so submitting comprehensive HTC submissions was essential to obtaining approvals required for an allocation. Minnesota's HTC enabled Dayton's Department Store, a landmark commercial building in downtown Minneapolis and home to the famous opening scene in “The Mary Tyler Moore Show,” to undergo its current rehabilitation. Don Kohlenberger, president of Hightower Initiatives, spearheaded the Dayton's rehabilitation since the project's initial inception in 2017. Through the project, the former department store will continue to be used as a commercial building, transitioning to leasable office and retail space. Kohlenberger explained the importance of the state HTC.

“Without the Minnesota HTC, adaptive reuse of Dayton's would not have been financially viable due to the significant amount of work necessary to bring the building to market,” he said.

By rehabilitating the building as two separate HTC projects—as facilitated by the NPS's functionally related guidance—the Dayton's project received two state HTC allocations. The ongoing Dayton's rehabilitation was awarded its second state HTC before the sunset date of Minnesota's program. Timing on the project was critical, due to the requirement outlined in the functionally related guidance that required a year gap in construction between the two HTC projects. Meaningful coordination with the state historic preservation office (SHPO) and the NPS enabled the development to move forward in a timely manner while meeting this requirement. Had the second project began just a few months later, it would not have been able to use the sizable amount of credits that Kohlenberger noted were essential. The second project likely would have been placed on hold, leaving the Dayton's renovation incomplete.

Having just beaten the clock, Kohlenberger is acutely aware of the challenges to financing HTC projects under normal conditions, let alone factoring in the uncertainty of whether a funding program such as the state HTC will be available.

“I hope that Minnesota re-enacts the state HTC program in the near future,” he said. “This economic tool was so important to Dayton’s. Its loss will undoubtedly impact the ability of future historic rehabilitations to get off the ground. The state HTC program is a critical financing tool for reactivating historic buildings, especially as our towns and cities work to comeback from the pandemic.”

Competitive State HTCs: The Dixon Building

Unlike Minnesota, Ohio’s state HTC features a competitive process, which uses a scoring rubric to determine which projects receive awards and the amount of the award in any given round. Due to the level of competition applying for Ohio state HTCs, it is beneficial for a project team to include a financial incentives consultant to help guide the project through the application and place the project in favorable position to receive an award.

Stephanie Mercado, in her role as project director at BLS & Company LLC, actively works with developers and historic consultants to strategize how best to optimize project scoring and to prepare the significant amount of data required for the Ohio Department of Development (ODOD). Unlike other states that provide credits once a project has received its SHPO and NPS approvals, the Ohio HTC is awarded by ODOD based on metrics that ensure the winning projects provide an economic benefit to the state, once they have received their baseline historic approvals. Mercado recently worked alongside Elyria Block Development LLC to secure a state HTC award for the historic Dixon Building in Elyria, Ohio.

“The Dixon Building serves as a centerpiece of Elyria’s historic commercial corridor and will be part of a larger project that will include adaptive reuse of the adjacent Robinson Building as well as new construction,” Mercado said. “With assistance from the state HTC, the building will be transformed for a unique, 21st century use that will include an E-sport arena as part of the Forge 417 project.”

The Dixon Building has been an integral component of Elyria’s downtown since its construction in 1873. Its rehabilitation will retain the building’s commercial history and will be a unique reuse, both for the local community and the HTC program in general. Like Dayton’s Department Store, the Dixon Building’s rehab would not be possible without the state HTC.

“Project financing relied heavily on HTCs, both federal and state,” Mercado said. “Had the state award not been secured, the gap in the capital stack would have been very hard to fill, especially in today’s climate.”

Many states feature competitive state HTC programs. As Mercado attested, it is important to retain a qualified and experienced project team to ensure that the project receives an appropriate award allocation.

Conclusion

State HTC programs throughout the country are tied to specific legislation. As such, those programs often include sunset dates that can result in the loss of this impactful economic redevelopment tool. For many developers and investors, the loss of this potential funding source can be detrimental to the viability of the project. Equally important is the loss to potential projects in communities from small to large, as seen in the widespread support in Minnesota from public officials, newspapers and preservation advocates. It is hoped that this widespread support will prevent other state credits from sunset and will lead to the eventual reinstatement of the Minnesota credit.

State HTC programs serve as an excellent complement to the federal program and provides developers with the added financial benefit often necessary to rehabilitate historic buildings. The rehabilitations of Dayton’s Department Store and the Dixon Building serve as two examples of the thousands of projects that are undertaken each year that were made possible through the use of state HTCs. ❖

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Cindy Hamilton is president of Heritage Consulting Group.

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