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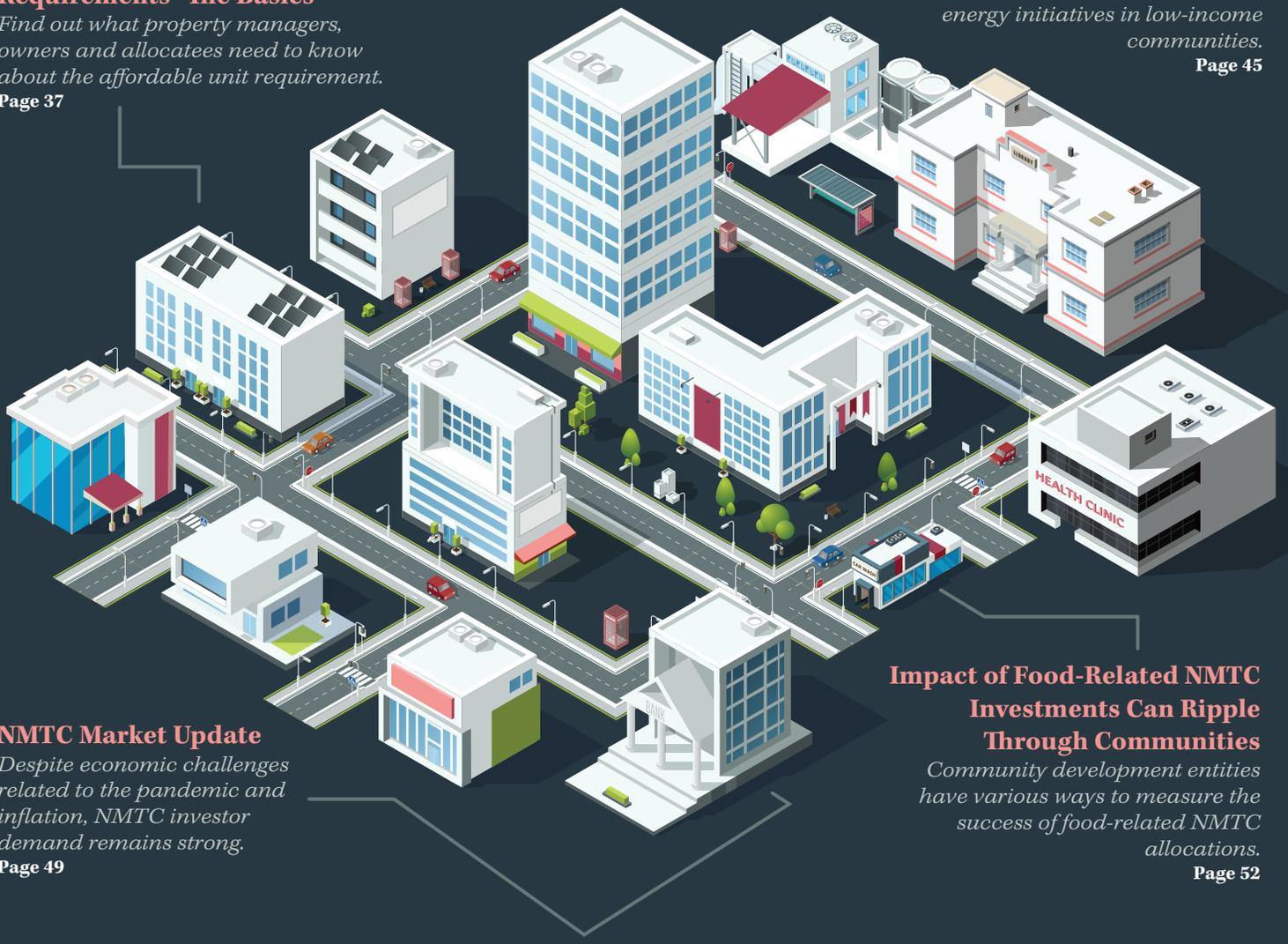
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## HISTORIC TAX CREDIT TOOL BOX 🌿

# Rehabbing Horlick Malted Milk: Stakeholder Perspectives



CINDY HAMILTON, HERITAGE CONSULTING GROUP

Earlier this year, the first historic tax credit (HTC) development at the historic Horlick Malted Milk complex in Racine, Wisconsin, was completed. With National Park Service (NPS) approvals secured, the two primary factory buildings at the complex, Factory 1 and Factory 2, were rehabilitated into multifamily housing, now identified as the William and the Arabella. The project milestone signifies an important step in the economic rebirth of Racine, but it only scratches the surface of what is to come.

*Image: Courtesy of J. Jeffers & Co.*

The William, the Horlick Malted Milk Company's Factory #1, was recently rehabilitated into multifamily apartment units. The factory's transformation will soon be followed by the remainder of the historic complex.

Horlick, like many other mill and factory complexes, consists of numerous buildings, all of which played an integral role in the company's manufacture of

malted milk-based products. Through the NPS' functionally related guidance, a second HTC project will be undertaken, which will result in the complete transformation of the complex into a mixed-use destination. The Horlick rehabilitation also serves to illustrate the complexities of project financing.

Although the NPS considers the overall rehabilitation as separate HTC projects, each with multiple phases, the number of "projects" and "phases" differs between the developer and investor as those entities consider project financing, which is not considered by the NPS. The capital stack for the Horlick rehabilitation, for example, differs between the first and second HTC project, with each using a different variation of incentives, including HTCs, low-income housing tax credits (LIHTCs) and new markets tax credits (NMTCs), among others. Horlick's rehabilitation, therefore, affords a behind-the-curtain view to demonstrate how complex these projects truly are. What seems on the surface to be two straightforward HTC projects are actually a complex interplay of construction, financing and investment schedules, which all need to coincide with the NPS framework for functionally related complexes.

The variations in financial structuring effectively display how each stakeholder views the project in terms of the timeline and project milestones.

### **Horlick Malted Milk Company Complex**

The Horlick Malted Milk Company was founded in 1874 in Chicago by brothers William and James Horlick. By 1877, the company moved to Racine and began construction on an expansive complex that encompassed nearly 16 acres. Between approximately 1885 and 1950, the Horlick Malted Milk Company developed its site and complex, all while manufacturing its world-renowned malted milk, which was purchased by a wide variety of people, including the United States military and mothers of newborn babies. While today best known as part of sweet treats including milkshakes and malted milk balls, malted milk was a revolutionary "health" food for much of the late-19<sup>th</sup> and early to mid-20<sup>th</sup> centuries.

Today, the Horlick complex consists of 11 buildings that share similar Gothic Revival-style architectural elements. The brick buildings are defined by their projecting towers and rooftop crenellations, which convey a uniquely cohesive group of buildings. While much of the site was converted for other uses upon Horlick's departure in 1951, unsympathetic changes left the site underused and deteriorated. The HTC projects will restore the complex to its former glory as one of Racine's most important grouping of buildings.

The completion of the first HTC project accomplished the first phase of this transformation. Due to the overall scale and financial structure of the project, however, definition on what stage of the project the team is currently at depends on who you ask.

### **The Developer's Perspective**

The rehabilitation of the former Horlick Malted Milk Company complex is being undertaken by J. Jeffers and Company, a Milwaukee-based developer that has long been involved in the rehabilitation of historic buildings. Most development projects, particularly those using tax credits, require a complex financial structure. Tyler Parbs, vice president, investments at J. Jeffers & Co., explained that, "tackling a project the size of Horlick has unique challenges with significantly more complex financial structuring required when multiple tax credit incentives are utilized."

The first HTC project, completed in phases, resulted in the rehabilitation of Factory #1, Factory #2 and associated site work. The second HTC project will include the rehabilitation of the remaining buildings, new construction and additional site work, undertaken in multiple phases.

For the development team, the complexity of the project financing and construction presents a unique challenge when layered with the requirements of the NPS functionally related guidance. To finance the rehabilitation, the first HTC project included three separate transactions. "Due to the nature of each transaction, it was necessary to structure the rehabilitation of the two factory buildings individually," said Parbs.

Factory #2, known today as the Arabella after William Horlick's wife, was the first transaction. The rehabilitation of Factory #2 resulted in the creation of 60 low-income housing units that were funded through twinned HTCs and LIHTCs. The second transaction was the rehabilitation of Factory #1, which was funded through HTCs only. Upon completion, the William featured 86 market-rate apartment units. The third transaction involved new construction. It was separately financed, as it did not include HTCs, and this construction, while funded, was pushed to occur as part of the second HTC project to adhere to the functionally related guidance. Each of the three transactions had its own milestones and timelines that had to be considered and planned for in tandem with the NPS process.

For the second HTC project, financial structuring will again expand the number of phases in the eyes of the developer. Parbs identified the focus of the development team, stating, "in looking ahead, the focus will be on the rehabilitation of the former garage and machine shop buildings." Parbs further explained that "the garage will feature over 20 apartment units, which will be its own transaction, while the machine shop will be converted into leasable commercial space and will be its own transaction." Unlike the earlier phases, the commercial components of the second HTC project enable the development team to seek NMTCs to twin with HTCs, requiring that this be its own transaction.

The proposed rehabilitation of the remaining buildings in the complex will follow a similar path, individually financed developments that use different funding sources. A key component of the rehabilitations of the buildings in the second HTC project, however, will be twinning the HTCs with NMTCs.

For the developer, the rehabilitation of Horlick is considered one large project with each transaction constituting an individual phase. Tracking the phasing and the timelines dictated by the investors, parallel with the construction schedule, is the challenge

the developer faces in these complex projects. These challenges are further layered with the NPS' functionally related guidance, which only permits the applicant to have a single HTC project at a time, thus only receiving final certification when the entire HTC project is complete.

### The Investor's Perspective

Throughout the rehabilitation of the Horlick complex, the investor's perspective of project phasing and financing differed from that of the remainder of the development team. Stephen Kramer, senior vice president for U.S. Bancorp Community Development Corporation (USBCDC), has been heavily involved with the Horlick project since the first NPS HTC project started. USBCDC invested in the completed NPS HTC project and will be the investor on the second HTC project as well.

Kramer explained his perspective on the project phasing and financing.

"I think of Horlick as three projects so far," he said. "The first two being the twinned LIHTC and HTC project (Factory #2) and the HTC only project (Factory #1). So, this was really two separate investments for us."

As for the third project, Kramer explained, "the next project from our perspective will be the twinned NMTC and HTC project (Garage and Machine Shops)."

For USBCDC, investing in the entirety of the project was an easy decision.

"We were in on the first phase, so carrying over into the second HTC project was a simple conversion," Kramer said. "We would not want another investor involved, as that could potentially impact our investment on the first project, which of course is still ongoing as part of the NPS's five-year recapture period." Additionally, U.S. Bancorp has a strong relationship with J. Jeffers & Company, with the Horlick project accounting for their sixth investment in a Jeffers rehabilitation.

As the second HTC project gets started and the project financing shifts to a twinned HTC and NMTC focus, USBCDC remains positive about the outlook for the final product. Kramer noted how at USBCDC, unlike other investors, twin transactions are handled by the same internal group and a developer will deal with that group throughout the closing and asset management portions of the project. For the second Horlick project, Kramer noted that, “the major challenges will be finding an allocation partner for the NMTCs and ensuring that the community benefit of the project is enticing enough to attract said partner.” Regardless of the project financing, the investors see the shift in project financing as a great opportunity.

## Conclusion

Looking ahead to Horlick’s second HTC project, the historic malted milk manufacturing complex

will continue to evolve into a modern, mixed-use hub. The complexities of project financing, and ultimately, how the project team sees each “phase,” will continue to evolve as uses and proposed plans for each of the remaining buildings are identified. With more and more HTC projects falling under the NPS’s functionally related guidance, understanding the varying requirements of the NPS and the project stakeholders is important for the successful orchestration of the complex financing. Horlick’s rehabilitation serves as an excellent representation of this. With the successful rehabilitation of Factory #1 and #2, the future of the complex will be exciting to follow. ❖

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*Cindy Hamilton is president of Heritage Consulting Group.*

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