



**Federal Tax Credits
for Historic Theatres**

2008 LHAT Annual
Conference

Tax Credit Financing for Historic Theatres

- Revitalizing Historic Theatres – A growing movement
- Tax Credit Programs
- Requirements
- How this can work for Non-profits
- Costs
- Benefits

Revitalizing America's Historic Theatres – A Growing Movement

- WHY?
 - Space for performing arts and film
 - Reinvigorates downtowns and neighborhoods
 - Provide sense of continuity and heritage
 - Easily adaptable asset
 - Architecture reflects importance to community
 - Multiple additional uses
 - Weddings, Lectures, Corp meetings, etc.

Benefits Are Far Reaching

- Improved aesthetics
- Job creation – during and after construction
- Jobs for artists, managers, technicians
- Patronage for restaurants, hotels, parking lots
- Catalyst for investment in additional revitalization projects

Challenges

- Existing conditions
- Control of ownership
- Department of Interior requirements
- Current codes
- Technical feasibility
- Sufficient space
- Economic feasibility
- Cost

2 Federal Tax Credit Programs

- Rehabilitation Tax Credits (RTCs)
- New Markets Tax Credits (NMTCs)
- These programs can be "Twinned"
- Other programs may also apply
- State Tax Credits available in many states

Rehabilitation Tax Credits

- Began in 1976
- Encourages rehabilitation vs. Demolition
- Historic structures receive 20% credits on Qualifying Rehab Expenditures (QREs)
- **No "Cap"** on total amount of credits provided in any given year
- 3 Agencies in Control
 - National Park Service
 - State Historic Preservation Offices
 - Internal Revenue Service

Requirements for Rehab Tax Credits

- Comply with Secretary of Interior's Rehab Standards (20% Credits only)
- Listed on National Register of Historic Places
 - Individually, or
 - Contributing Building in National Register listed historic district (File "Part 1")

Requirements for Rehab Tax Credits-Continued

- Qualified Rehab Expenses (QRE's) must exceed the greater of the adjusted basis of the building or \$5,000
 - QRE's – most hard and soft costs except for
 - Acquisition
 - Unattached furnishings
 - Landscaping
 - New construction outside historic footprint
 - Fundraising expense

Requirements for Rehab Tax Credits-Continued

- Qualified Rehab Expenses (QRE's) must exceed the greater of the adjusted basis of building or \$5,000
 - Adjusted Basis
 - Original cost of building (not land)
 - Plus closing costs
 - Plus prior capital improvements
 - Minus depreciation

Requirements for Rehab Tax Credits-Continued

- Facility must produce income
 - Credible 7 – 10 year operating plan
 - Show a profit even if small
 - Business basis
 - Elements unique to the Nonprofit are excluded
 - Flexibility as to what costs are included in analysis

10% Rehabilitation Tax Credits

- Non historic buildings built before 1936
 - State Historic Preservation Office and National Park Service do not consider structure to have architectural, historic or cultural significance
 - Requirements for wall retainage and interior mass
 - Does not require compliance with Secretary of the Interior's Standards for Historic Rehabilitation

New Markets Tax Credits

- Program launched in 2001 for 7 years and recently extended to 2008
- Offers tax credits to investors who fund business development in "underserved" areas
- 39% credit on the investment over 7 years
- Requires an allocation earmarked by a CDE
- High \$\$ potential, low probability of achieving

New Markets Tax Credits- Continued

- 2 Administering agencies
 - US Department of the Treasury's Community Development Financial Institutions Fund (CDFI fund)
 - Internal Revenue Service

New Markets Tax Credits- Continued

Different than the Rehabilitation Tax Credit

- Amount of credits available and life of program are limited
- Credits earned over seven years after investment is made
- Requires allocation of investment dollars eligible for the credit

New Markets Tax Credits Requirements

- Community Development Entities (CDEs) must use substantially all of the proceeds from Qualified Equity Investments (QEIs) to make Qualified Low-Income Community Investments (QLICIs) to Qualified Active Low-Income Community Businesses (QALICBs) located in Low-Income Communities

Requirements for New Markets Tax Credits-Continued

- "Realistic Musts"
 - "Highly Distressed" Census Tract
 - Poverty rates >30%
 - Median family income <=60% of MSA or State median, whichever is greater
 - Unemployment rate at least 1.5 X National Average
 - Other factors-Enterprise Zones, HotZones, Brownfields, etc.
 - "Non MSA" tracts have specific targets
 - Certain FEMA disaster areas have specific targets
 - Definable economic Impact-especially Jobs
 - Relationship with a CDE – developed "early on"

"Recapture"

- Both Rehab and New Markets Tax Credits are subject to recapture during compliance period
 - Business must remain active
 - Remain qualified as "Qualified Active Low Income Community Business" for New Markets Tax Credits
 - Rehab Tax Credit recapture can occur upon additional changes to the historic structure (including fire)
 - Ownership must not change (Rehab Tax Credits)
 - Amount of recapture depends on nature of default

Can a Non-Profit Owned Theatre Benefit from Tax Credits?

- Non-profit continues to exist for purposes of donations and fundraising activities
- Forms a partnership
 - For profit entity that pays a large amount of taxes – contributes cash (equity) in exchange for tax credits
 - Non-Profit Theatre contributes Theatre, and funds from fundraising activities

No “Free Lunch”

- Rehab Tax Credit investor will require a priority return over the life of the 5 year compliance period
- Funds must be set aside to exit the partnership
- CDE typically requires an up front fee and loan administration or asset management fees over the 7 year term

No “Free Lunch” –Continued

- Owner’s, Investor’s, and CDE all require people knowledgeable in the process who must get paid
- Owner must consider use of the credits early in the process and make some initial cost:
 - Determine if project qualifies for credits
 - Determine how rehabilitation affects design, functionality, overall project cost estimate
 - Develop the business plan, the “pitch paper” and the relationship with possible CDEs and investors
- DO NOT COUNT on NMTCs in base funding

“No Free Lunch” - Owner Support

- Architects knowledgeable about Secretary of Interior Standards and Historic Rehabs
- General Contractor with experience in Historic Rehabs
- Investors and Lenders experienced in process
- Local Real Estate and National Tax Credit Attorneys
- Local Financial and National Tax Credit Accountants
- CDE Allocatee willing to allocate to the project
- Project Coordinator(s)-Financing, Design, Construction

Is It Worth It?-Rehab Tax Credits

■ Project Cost -	\$10,500,000
■ Qualified Rehab Expense	\$10,000,000
■ Rehab Tax Credit (20%)	\$ 2,000,000
■ Investor Purchase Price	\$ 1,900,000
■ Less Costs and Reserves*	<u>\$ 500,000</u>
■ Net Benefit-Rehab Tax Credits	<u>\$ 1,400,000</u>

*Includes Working Capital Reserve (may get back), "Put" Reserve for buy out, annual 3% return, Professional Fees, Compliance costs

Is It Worth It?-New Market Tax Credits

■ Project Cost -	\$10,500,000
■ New Market Tax Credit (39%)	\$ 4,095,000
■ Investor Purchase Price	\$ 3,071,250
■ Less Costs and Reserves*	<u>\$ 819,000</u>
■ Net Benefit-Rehab Tax Credits	<u>\$ 2,252,250</u>

*Includes Asset Management Fee upfront and annually; legal, accounting, other professional fees for CDE, Investor and yourself

Is It Worth It? -Continued

- Rehab Tax Credits Example
 - Over 13% of funding through Federal Credits-Net*
 - For Every \$ donated, \$.15 extra from Federal Credit
 - Could be much more if State Tax Credits Available

- New Markets Tax Credits Example
 - Over 21% of funding through Federal Credits-Net*
 - For Every \$ donated, \$.27 extra from Federal Credit
 - Could be much more if State Tax Credits Available
 - TOUGH TO GET

*Assumes that all annual costs must be reserved. If not, the initial return increases significantly

Is It Worth It? -Continued

- Funding from Tax Credits increases Owner's equity
- Priority return is much lower than interest cost for borrowed money
- Leverages fund raising activities significantly
- State Tax credits can further increase impact
- Rehabilitation and operation of a historic theatre can provide a significant economic engine for the community

Is It Worth It? -Continued

- This is a means to bring federal and, perhaps, state funding into the community
- This is an alternative to consider if you engage the trained professional team whom you can and will trust and the Owner has the time and tenacity to follow this through.

LHAT CAN HELP

- Historic Theatre Rescue, Rehabilitation and Adaptive Reuse Manual
- PAR (Peer Advisory Review) program
- Membership Directory and Historic Theatre Inventory
- Articles "In League"
- Reference to Members who have successfully rehabbed theatres using tax credits
- Conference, Forums, Workshops and Seminars
- Prior Conference Materials
- Additional information through LHAT Staff and Board Members
