Navigating the Historic Rehabilitation Tax Credits: A Flow Chart & Guide from the North Carolina Main Street & Rural Planning Center





The N.C. Main Street & Rural Planning Center (MS&RP) is part of the Rural Economic Development Division within the N.C. Department of Commerce. MS&RP works in regions, counties, cities, towns, downtown districts, and in designated North Carolina Main Street communities, to inspire placemaking through building asset-based economic development strategies that achieve measurable results such as investment, business growth, and jobs.

MS&RP is committed to strengthening communities through preservation-based economic development. Within this capacity, we are pleased to provide this document as a resource to community leaders, property owners, and developers who may be interested in pursuing historic rehabilitation tax credits to reactivate North Carolina's historic buildings.

Document Outline:

- ⇒ An Overview of the Historic Tax Credit Program (Federal & State): Page 2
- ⇒ A Guide for the Community Leader: Page 3
- ⇒ A Guide for the Developer/Property Owner: Page 4—5

We would like to extend a special thanks to those who helped produce this resource alongside MS&RP staff: Gene Rees of REF Properties, The North Carolina State Historic Preservation Office, and Preservation North Carolina.

Neither the State of North Carolina, the North Carolina Judicial Branch or any of its employees, shall be held liable for any improper or incorrect use of the information described and/or contained herein and assumes no responsibility for anyone's use of the information. Please consult a qualified tax advisor to determine eligibility and use of the Historic Tax Credit program.

Navigating Historic Rehabilitation Tax Credits: An Overview of the Historic Tax Credit Program



NC

State

Varied

Credit



What are the Historic Rehabilitation Tax Credits?

The Historic Rehabilitation Tax Credit affords the owner of certified historic structures the ability to capitalize upon a 20% federal tax credit and varied state tax credit when they rehabilitate a building (1) that is depreciated; (2) where the rehabilitation meets the <u>Secretary of the Interior's Standards for Rehabilitation</u>, and (3) where the investment exceeds the adjusted basis of the building(s). The <u>National Park Service</u>, through its <u>Technical Preservation Services</u> division, and the <u>Internal Revenue Service</u> administer the program in partnership with the <u>State Historic Preservation Office (SHPO)</u>.

Are You Eligible to use Tax Credits?

Federal 20% Credit

CONSULT A QUALIFIED TAX ADVISOR TO DETERMINE ELIGIBILITY:

For a list of experienced accountants, visit the Preservation NC (presnc.org). The rehabilitation credit is an investment credit and part of the general business credit that a taxpayer can claim against the income tax. Taxpayers that own an interest in the building are eligible to claim the rehabilitation credit and generally include: individuals, corporations, partners, shareholders, and beneficiaries of a passthrough entity, estates, and trusts.

If a developer/property owner is not in a position to use the tax credits, banks or other third parties may invest in the credits to raise equity funding for the HTC project, reducing the amount of debt financing developers need for the property's rehab.

<u>Visit : National Parks Service: Historic Tax Credit Eligibility</u> <u>Information</u>

FEDERAL TAX CREDIT INCOME PRODUCING PROPERTIES:

A 20% federal income tax credit is available for qualified rehabilitation expenditures (QRE's) of historic buildings that are determined to be "certified historic structures" by the National Park Service. The buildings must be considered depreciable under the Internal Revenue Code, such as in a business, commercial, or other income-producing use. Learn more from the National Parks Service.

Visit: National Parks Service: Historic
Tax Credit Frequently Asked
Questions

NC INCOME-PRODUCING PROPERTIES:

A 15% state tax credit for rehabilitation of income-producing certified historic structures is awarded to rehabilitations that qualify for the federal tax credit and spend up to \$10 million. A 10% state tax credit for rehabilitation of income-producing certified historic structures is awarded to rehabilitations that qualify for the federal tax credit and are for expenses from \$10 million to \$20 million.

There is also a 5% bonus if the development is within a Tier 1 or Tier 2 county or is located in an eligible targeted investment site. This bonus may be applied for expenses up to \$20 million. To find your county's tier designation, visit the County Development Tier Designations page from EDPNC. Read more from the State Historic Preservation Office (SHPO).

READ MORE: INCOME-PRODUCING REHABILITATED MILLS

NC NON-INCOME PRODUCING/HOMEOWNER PROPERTIES:

Homeowners may receive a 15% state tax credit for qualified rehabilitation of owner-occupied residential properties that contribute to a National Register Historic District or are listed individually on the National Register of Historic Places. The rehabilitation of the historic structure must exceed \$10,000 within a 24-month period. Eligible rehabilitation expenses are limited to \$150,000, with a maximum state credit of \$22,500. There is no federal credit for non-income producing projects. All rehabilitation work must meet The Secretary of the Interior's Standards for Rehabilitation.

Contact the SHPO's Homeowner Tax Credit Coordinator, Meghan Sullivan, for more information at meghan_sullivan@dncr.nc.gov.

Navigating Historic Rehabilitation Tax Credits: A Guide for the Community Leader

project. Now what?



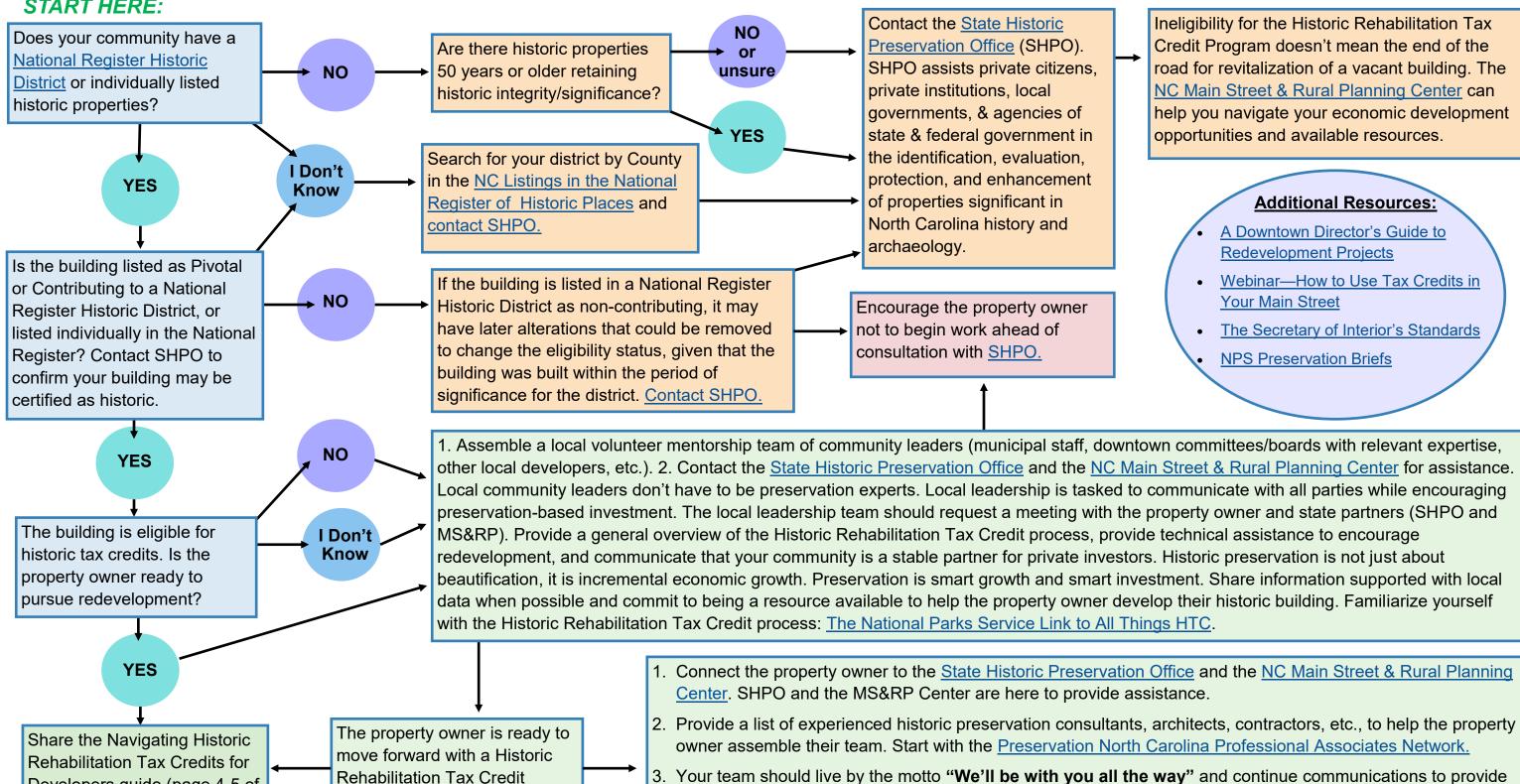
technical assistance to the property owner from groundbreaking to ribbon cutting. You are the connector.



START HERE:

Developers guide (page 4-5 of

this document).



Navigating Historic Rehabilitation Tax Credits: A Guide for the Developer/Property Owner





START HERE (The starting point on page four assumes the property is a confirmed certified historic structure. (See page two for establishing eligibility):

You own a certified historic structure (must confirm with SHPO) and are interested in Historic Rehabilitation Tax Credits. Where do you begin?

Confirm

Project Eligibility Connect to Resources Before doing any work to the building, contact the <u>State Historic Preservation Office</u> (<u>SHPO</u>). SHPO provides a variety of technical preservation services to the public and governmental agencies, including rehabilitation guidance and coordination of Federal and State tax credit programs.

After contacting SHPO, contact the <u>NC Main Street & Rural Planning Center</u> for resource identification and technical assistance. Contact your local community leaders: town administrators and downtown organizations for local assistance & incentives.

The rehabilitation work must be done according to the <u>Secretary of the Interior's Standards for Rehabilitation</u>. These are ten principles that, when followed, ensure the historic character of the building has been preserved in the rehabilitation. The Standards are applied to projects in a reasonable manner, taking into consideration economic and technical feasibility.

After rehabilitation, the historic building must be depreciable, such as in a business, commercial or other income-producing use, for at least five years or the tax credits will be subject to recapture.

Complete Part 1 HTC Application to certify that your property is a certified historic property and submit to <u>SHPO</u>. Detailed photographic documentation of existing conditions will be required. You should consider working with a <u>historic preservation consultant</u> to prepare Part 1. During review, continue assembling your project team.

Understanding Historic Tax Credits:

- Webinar—How to Use Tax Credits in Your Main Street
- The Secretary of Interior Standards
- The National Parks Service Link to All Things HTC
- IRS Rehabilitation (Historic Preservation) Credit FAQs

Understanding HTC Application Process:

A three-part application is required to qualify for the state and federal tax credits:

- Part 1 certifies the building as historic.
- Part 2 certifies the proposed rehabilitation work. The proposed work will be evaluated based upon the <u>Secretary of the Interior's</u> Standards for Rehabilitation.
- Part 3 of the application is submitted after the project is complete and documents that the work was completed as proposed in Part 2 and that all conditions were met. NPS approval of the Part 3 certifies that the project meets the Standards and is a "certified rehabilitation."

Preservation) FAQs | Internal Revenue Service (irs.gov) 2. Once you know your building is a certified historic structure, the project must meet the "substantial rehabilitation test." This means that the expenditures must exceed the adjusted basis. More information here: Substantial Rehabilitation Test Information.

1. Confirm your ability to use Historic Tax

Credits. Rehabilitation Credit (Historic

Assemble
Your
Team
Begin
Planning

You will need an experienced team including historic preservation accountants, consultants, architects, engineers, contractors, etc.

<u>Contact SHPO</u> for a list of resources or use the <u>Preservation North Carolina Professional</u> Associates Network. Begin Part 2 (description of the rehabilitation work) application. It is recommended to hire an <u>architect with historic preservation experience</u>. Part 2 requires a description of all work that will be undertaken to the building and property, including items that are not qualified rehabilitation expenditures. Break the overall project down into existing and proposed building parts, features, and materials including but not limited to: the overall site, the roof, masonry, siding, trim, windows, doors, porches, ceilings, walls, floors, PME, trim, fireplaces, stairs, bath, kitchen, and proposed additions and alterations. Begin with sitework, followed by the exterior, and then the interior, of the building. Do this for each building on the property, if there are multiple buildings. Part 2 submittal includes the project description, project summary, architectural plans, and photographs. Part 2 should be submitted to the <u>State Historic Preservation Office (SHPO)</u>. After review, SHPO forwards the application to the <u>National Park Services (NPS)</u> with a recommendation. Review of the Part 2 application will generally take 30 to 60 days. With HTC projects, factor in approval times in your project timeline.



Navigating Historic Rehabilitation Tax Credits: A Guide for the Developer/Property Owner





CONTINUE HERE:

You've just submitted your Part 2 Historic Rehabilitation Tax Credit application to <u>The State Historic Preservation Office (SHPO)</u>. Do you have all parties of your development team (historic preservation consultant, architect, landscape architect, general contractor, engineers, accountant, etc.) in place?



It is not recommended to begin construction prior to review being completed. Those who elect to begin prior to the review being completed may jeopardize their tax credits.

The applicant (owner, partner, long-term lessee) may claim the historic tax credit after rehabilitation is complete and certified with a Part 3 approval. Claiming the credit is straightforward. The taxpayer submits IRS Form 3648 along with the NPS project number with your annual tax documents.

The owner of the building must be a for-profit taxpaying entity, but that can take several forms:

While the Part 2 HTC application is under review, use this time to complete your development team. Consider contacting SHPO for resources or the Preservation North Carolina Professional Associates Network.

- Hire a <u>qualified tax advisor</u> to calculate Historic Tax Credit eligible basis and qualified rehabilitation expenditures. A qualified tax advisor may provide in-depth transaction analysis, develop transaction structures, and evaluate deal terms from prospective tax equity partners.
- 2. Determine that <u>Qualified Rehab Expenditures (QRE)</u> meet the <u>Substantial Rehabilitation Test (SRT)</u>: the qualified rehabilitation expenditures must exceed the adjusted basis within a 24-month window or a 60-month window for phased projects. Phased projects must be phased from the outset and cannot change from non-phased to phased.
- 3. Be sure you have confirmed eligibility.

Let's Talk About The Timeline:

Property owners may begin claiming the tax credits in the taxable year the "qualified rehabilitated building" is placed in service provided that all requirements are met. The rehabilitation credit is an investment credit that is part of the general business credit that a taxpayer can claim against the income tax. A taxpayer is generally allowed to carryback one year and carryforward 20 years unused portions of the general business credit. More information from the IRS here. The state historic tax credits may be claimed entirely the year the structure is placed into service, or carried forward up to nine years. The property owner must retain ownership for five years.

If <u>SHPO</u> or <u>NPS</u> feels that any element of the scope of work does not meet the <u>Standards</u>, either SHPO or NPS may place a condition(s) on the project. As long as the completed rehabilitation addresses this condition, the Part 3 application will be approved at the end of the project. Applicants can file an amendment to officially revise the scope of work to address any conditions.

Upon completion of construction, have your preservation consultant and experienced accountant review the Part 3 HTC application (request for certification of completed work) before submittal to SHPO. Part 3 certifies that the completed rehabilitation meets the Standards for Rehabilitation. The submittal includes "after" photos documenting the exterior and interior of the completed rehabilitation, estimated QRE and non-QRE costs, and ownership information (for assignment of credits). The date of Part 3 approval must be attached your annual tax return (corporate or individual) in order to claim the tax credits. Equity partners in the project must be on the deed on the placed in service date.



- A fee simple property owner of the property may be an individual, partnership or corporation.
- A limited partnership can distribute the benefit to its members. In this scenario, an equity
 partner can invest in the project in exchange for rights to the credit. The investment helps
 finance rehabilitation.
- Under certain circumstances, the lessee of a newly rehabilitated building can claim the credit.
 Read more about it on the IRS Rehabilitation Credit FAQs website.

Remember: lean into the State

Historic Preservation Office and
the NC Main Street & Rural

Planning Center for technical
assistance with your Historic
Rehabilitation Tax Credit project.