

Downtown Memphis



Historic Preservation Tax Incentive Program

Administered by:
Guilford Capital Corporation

Coordinated by:
Memphis Center City Commission

federal historic preservation tax incentive **OVERVIEW**

The federal government offers a 20% tax credit incentive for rehabilitating commercial historic properties. One dollar of tax credit reduces the amount of income tax owed by the property owner by one dollar.

The tax credit applies to projects designated as a certified rehabilitation of a certified structure by the Secretary of Interior. Certified structures are buildings listed in the National Register of Historic Places or a building located in a registered district and certified by the National Park Service as contributing to the historic significance of that district.

How Tax Credits Work

The tax credit goes to the owner of the building. This can be an individual or a pass-through entity like an LLC or LP, but limitations may exist for pass-through entities unless active real estate professional rules are met. Corporations do not have limitations on the amount of credit but there must be enough tax liability to take advantage of it. Unused credits can be carried forward but the present value of the credit goes down when it is not completely used in one year. Thus, selling the credits can be attractive for many developers.

Since the credit goes to the owner of the building, the credits are not literally "sold". The transaction is structured with an investor such that a pass-through entity (LP or LLC) is formed to own the building, of which the investor will own the agreed upon share of the entity, entitling it to the tax benefits.

Investors typically pay 90 cents or more per historic tax credit dollar for deals raising more than \$1.5 million in equity. Pricing is less for smaller projects and often there is no market for the sale of smaller project credits. Transaction costs, including legal and accounting fees, can be significant and often make projects under \$1 million uneconomical.

The Center City Commission and Guilford Capital Corporation teamed together to help these smaller projects benefit from the tax credits.

Eligibility Requirements

To be eligible, projects must meet the following basic tax requirements of the Internal Revenue Service:

The building must be depreciable. Rehabilitated property is depreciated using the straight-line method over 27.5 years for residential property and over 39 years for non-residential property. The depreciable basis of the building must be reduced by the full amount of the tax credit claimed.

The rehabilitation must be substantial.

The property must be returned to use following the rehabilitation. The tax credit is generally allowed in the taxable year the property is placed back in service. Tax credits on phased projects can be claimed before completion of the project provided that a "substantial rehabilitation test" has been met. Unused tax credits can be "carried back" one year and "carried forward" 20 years.

Qualified rehabilitation expenditures include work undertaken on the historic building, architectural and engineering fees, site surveyance, legal expenses, development fees and other construction-related costs. It does not include acquisition costs, furnishings, expansions to the existing building or new building construction, parking lots, sidewalks, landscaping, or other facilities related to the building.

The owner must hold the building for five full years after completing the rehabilitation, or pay back the credit. If the owner disposes of the building within the first year after being placed in service, 100% of the credit must be paid back. Between the first and fifth year, the tax credit recapture is reduced by 20% per year.

Guilford Capital Corporation is offering projects in Down- town Memphis favorable terms on tax credit projects.

Guilford will purchase 99.9% of interest in the "Partnership".

A Guilford Fund will pay _____** cents (see below) for each credit dollar the Limited Partner receives, to be paid with the following pay schedule:

Closing - up to 10% of the equity

Completion - up to 90% of the equity

Stabilization - remaining balance.

**** The range for credit prices is as follows:**

Below \$500,000	75-80 cents
\$500-\$750,000	80-85 cents
\$750,000-\$1 million	83-88 cents
\$1 million - \$1.5 million	85-92 cents
\$1.5 million plus	90 + cents

General Provisions:

A fixed rate permanent loan or forward commitment, which must be in the form approved by Guilford, must be in place at closing. The permanent loan term shall be a minimum of 60 months beginning with construction completion.

Guilford will require the project to establish a Repair and Replacement Reserve and an Operating Reserve. Both reserves will be under the joint control of the "General Partner" and Guilford. The Repair and Replacement Fund will be funded beginning in January of the first full year of operation at the annual rate of \$200-\$300 per residential unit and 55-65 cents per square foot of commercial space. The Operating Reserve will be funded out of capital sources of funds. The amount of the reserve shall be not less than six months debt service.

A Completion Guaranty is required, ensuring that the project will be completed on schedule and within budget. A Tax Credit Guaranty is required, ensuring that the project will not lose tax credits for any reason. An Operating Deficit Guaranty is required, ensuring funding of operating deficits for the 60-month compliance period.

The partnership shall pay Guilford a syndication fee of \$30,000-\$50,000 to reimburse legal, accounting, and tax fees, construction report and other due diligence costs. For deals \$500,000 and lower, the due diligence reimbursement expense will increase to \$60,000, and for deals over \$1.5 million, the reimbursement expense is negotiable.

Compliance and operations are the responsibility of the Property Manager and the General Partner. Guilford will provide oversight for its investor services and will be compensated \$7,500 each year for five years.

The Guilford Fund shall receive annually a 3% cash-on-cash return based on upon its equity investment plus its annual tax liability (if any).

At the end of the 60-month compliance period, the Limited Partner shall have the right to require the General Partner to purchase the Limited Partner's interest. The purchase shall equal 20-30% (negotiable for projects larger than \$1.5 million) of the Limited Partner's capital contribution. Terms and conditions of the Put Option will be further negotiated.

Guilford's approval of a tax credit project is subject to tax credit and underwriting approval.

For more information on Guilford Capital Corporation's Historic Tax Incentive Assistance Program, contact:

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For more information on financial incentives available for development projects in Downtown Memphis, contact:

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