State Historic Tax Credits

A Policy Brief on Return on State Investment

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April 11, 2015

Executive Summary

Independent studies have shown that states that invest in the redevelopment of historic buildings experience a positive return on their investment in the post-construction phase. Two studies from Maryland and Ohio show that one-third of a state's investment is paid back during the construction period -- before the building is placed into service and the credit issued. The remaining two-thirds of the state's investment are returned after the formerly abandoned or under-utilized building is placed into service.

Depending on the final use of a renovated building, the payback time period to the state varies. For example, when buildings are reused for hotels, like the former Pabst Brewery in Milwaukee, Wisconsin, several employees are hired and different state taxes are generated so the payback occurs quickly. These rehabilitations also increase local property tax revenues like the new Brewhouse Inn and Suites which increased Milwaukee's assessed values by a factor of ten – from $1,419,700 to $14,300,000.

The Gorman Company renovated an 1882 former brewery in Milwaukee, Wisconsin and turned it into the Brewhouse Inn and Suites. Approximately 111 jobs were created during the rehabilitation. Today, the 90 room extended-stay hotel employees 28 people (18 FT/10PT), while the restaurant/bar has 51 employees (26 FT/ 25 PT) . Before the renovation, the building was assessed at $1,419,700 and after the rehabilitation, the assessed value rose to $14,300,000.

While the timing may vary on the return on investment, studies that have examined the post-construction phase have seen a positive return on the state's investment. A taskforce appointed by Maryland Governor Bob Ehrlich, for example, found that for **every dollar of tax credit invested by the state, the state receives "an average return of approximately $1.02 during the first year after a project's completion, and $3.31 within five years after project completion**."[1]

[1] *Final Report of the Governor's Taskforce on Maryland's Heritage Structures Rehabilitation Tax Credit*, 2004

Introduction

There are currently 34 states that offer credits against state taxes to incentivize the certified rehabilitation of qualifying historic buildings. Most of the programs adopted the structure of the successful federal historic tax credit which was established in 1986.[2]

Federal Historic Tax Credit

Since its inception, the 20 percent federal historic tax credit has leveraged private investment in the rehabilitation of over 40,000 historic buildings across the country. Rutgers University Center for Urban Policy Research developed the Preservation Economic Impact Model (PEIM) to evaluate the economics of the federal HTC for the National Park Service. The PEIM modeling revealed that over the life of the program, $24 billion in federal tax credits had leveraged more than $28.6 billion in federal tax revenue directly attributable from the taxes collected from rehabilitated historic properties.

Maryland's Historic Tax Credit Program

Maryland Governor Robert L. Ehrlich, Jr. established a taskforce in 2003 to examine the Maryland Heritage Structure Rehabilitation Tax Credit Program to determine the efficacy of their state's investment in historic tax credits.[3] The Governor's Task Force concluded:

- The state historic tax credit program is "self-financing and does not require an outside revenue source. The total fiscal benefits of the Program, taken as a whole, far exceed the costs to the Treasury."
- The program **generates "approximately 34 cents in tax revenues for every dollar of tax credit during construction before any claim can be made for the tax credit**." This revenue generated during the construction phase is "derived from the sales tax on materials, income tax derived from employees on the

[2] Schwartz, Harry K., *State Tax Credits for Historic Preservation*, National Trust for Historic Preservation, February 2014

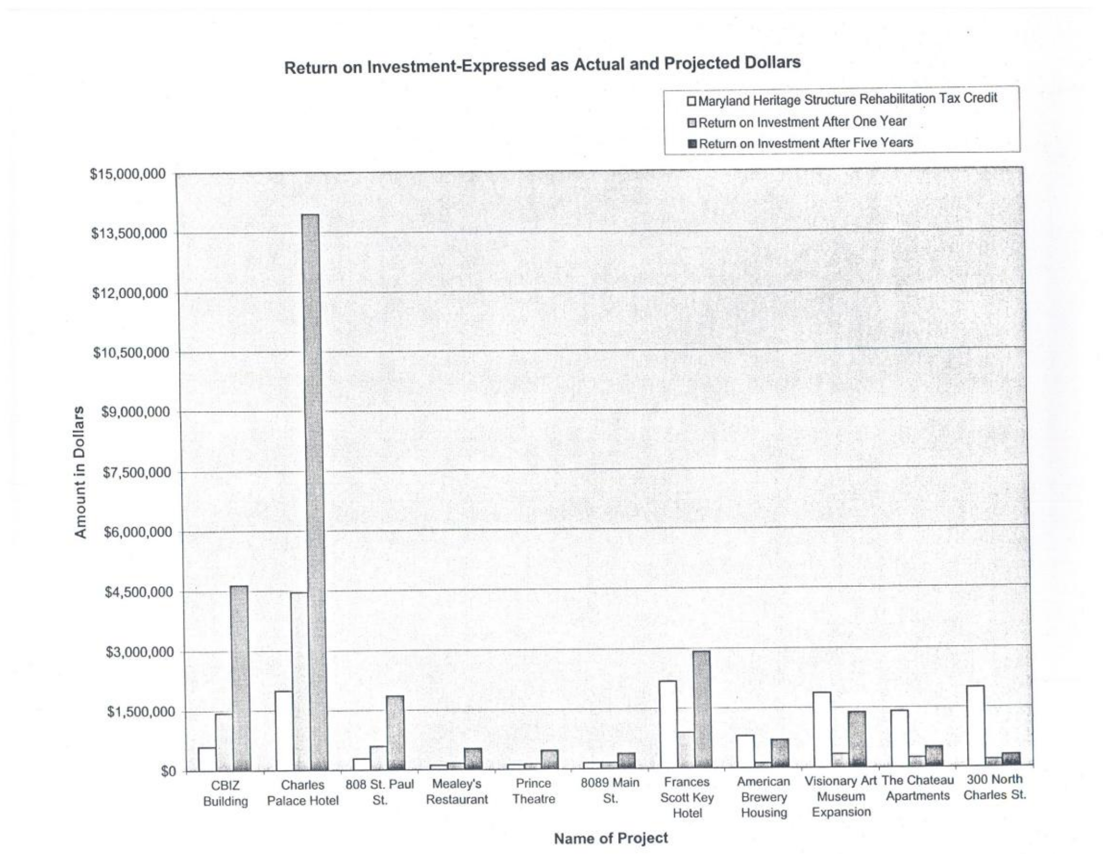
[3] Governor Ehrlich appointed William Donald Schaefer, Comptroller of the Treasury, to chair the Task Force which included among its membership, Victor L. Hoskins, Secretary, Department of Housing and Community Development; Aris Melissaratos, Secretary, Department of Business and Economic Development; James "Chip" DiPaula, Secretary, Department of Budget and Management; Audrey E. Scott, Secretary, Department of Planning; William J. Pencek, Jr., City of Baltimore; Larry Giammo, Mayor of Rockville; Mr. Harry Schwartz; Mr. G. Bernard Callan; Mr. Ronald Kreitner, Westside Renaissance, Inc.; Ms. Betty Jean Murphy, Savannah Development Corporation; Mr. David F. Tufaro, Summit Development Corporation; Mr. David Hillman, Southern Management, Inc.; Delegate Sheila Hixon, Chair, House Ways and Means Committee; Delegate Adelaide C. Eckardt, Senator David R. Brinkley; and Senator Ulysses Currie, Chair, Senate Budget and Taxation Committee. The Task Force was staffed by Ms. Louise Hayman, Office of the Comptroller and Mr. J. Rodney Little, Director, Division of Historical and Cultural Programs.

development team including architects, engineers, construction crew, etc.)" as well as fees from applicable permits and licenses.

- For every dollar of tax credit invested by the state, the state receives "an average return of approximately $1.02 during the first year after a project's completion, and $3.31 within five years after project completion."[4]

The Maryland Department of Housing and Community Development also examined 11 historic tax credit projects[5] and found that **large commercial, mixed- use projects with multiple office and commercial tenants produce the fastest rate of return on the state's investment**. The break-even period for these projects was often less than one year. These were followed by single use commercial rehabilitations, such as restaurant and retail establishment upgrades. The break-even period for these projects was typically less than 5 years.

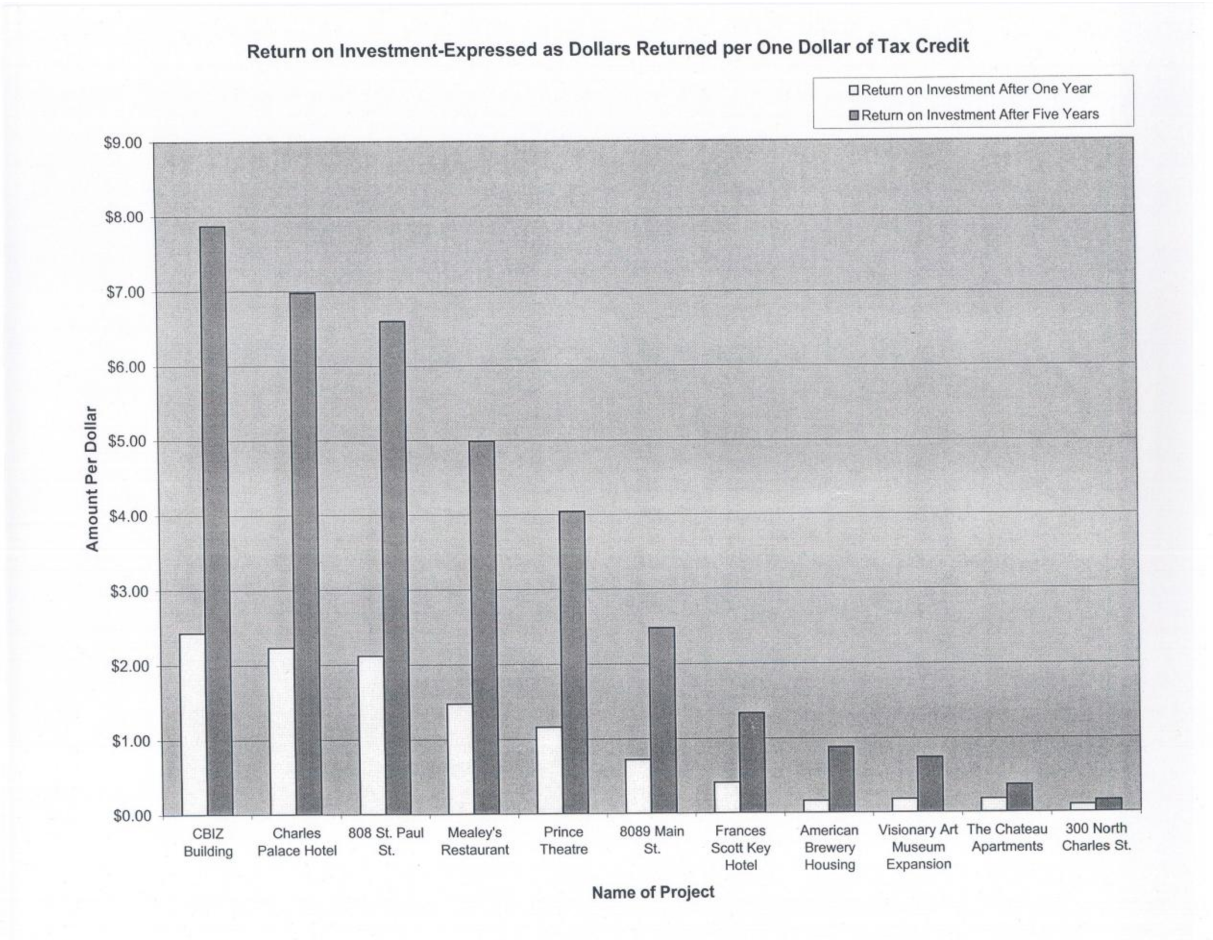
Table 1 – Return on Investment of 11 Maryland Historic Tax Credit Projects



[4] *Final Report of the Governor's Taskforce on Maryland's Heritage Structures Rehabilitation Tax Credit*, 2004

[5] The analysis outputs were for "wages and salaries, jobs (full time employment), State retail sales tax, State personal income tax, State real property tax, local personal income tax, local real property tax and other local taxes."

Table 2 – Return on Investment of 11 Maryland HTC Projects (per $1 spent)



Ohio

The Ohio historic tax credit program was enacted in 2006. The program currently has an annual cap of $60 million and is jointly administered by the Ohio Development Services Agency, the Ohio Historic Preservation Office and the Ohio Department of Taxation. The 25% historic tax credit is awarded during two application periods per year.

The Ohio legislature requires a cost-benefit analysis for each historic rehabilitation project during the application process. The state must determine whether rehabilitation of the building and awarding the credit will result in a net revenue gain in state and local taxes once the building is placed in service.

The Market Block Building in Warren, Ohio, provides a clear example for how the state's cost-benefit analysis is conducted. The Ohio Development Services Agency estimated that 31% of the state's investment of $630,800 in historic tax credits was recovered during the construction phase and before the tax credit was awarded. The analysis also estimated that 100% of the state's investment will be recovered in new revenues by the fourth year of operation. Tax revenue projections for additional out years are as follows: by year 10 the building will have generated additional state and local tax revenues of $494,000 in excess of the amount of the credit, or a return on investment of 80%; and by year 15, the building will have generated approximately $839,000 in new tax revenue, representing a return on investment of 130%.[6]

The Chesler Group renovated four 1868 buildings along the Courthouse Square in Warren, Ohio. Estimates by the Ohio Development Services Agency show a 100% return on the state's investment by its fourth year of operation as the offices of the non-profit Raymond John Wean Foundation. They estimate by the office's 15th year of operation, the redevelopment will have generated approximately $839,000 in new tax revenues, representing a return of 130% on the state's investment.

In 2011, an economic impact study of the state HTC program was conducted by the Great Lakes Environmental Finance Center at Cleveland State University (CSU).[7] Using the Regional Economic Models, Inc. (REMI) model[8], CSU estimated the economic impact created by 111 redevelopment projects that were completed between 2007 and 2011. CSU researchers concluded that the construction and operation of the 111 historic tax credit projects will create an estimated annual average of 6,976 jobs. Taxes collected by the state include: State Income Tax (2.88%), Business to Business Sales Tax, Consumer Sales Tax, and the Commercial Activity Tax.

[6] Data provided by Ohio Development Services Agency, September 2014.
[7] Great Lakes Environmental Finance Center, Goodman Levin College of Urban Affairs, Cleveland State University, *Estimates of the Economic Impact of the Ohio Historic Preservation Tax Credit Program on the State of Ohio*, May 2011.
[8] The REMI Model uses the following measures of outputs: Employment, Gross State Product, Wages by Places of Work, Local Wage Tax (@2%), State Income Tax (2.88% ATR), CAT: Self-Supply, CAT: Imports, Sales (Business to Business), Sales: Consumer, Total State Revenue Estimates, Total Public Revenue Estimates, Total Economic Impact)

CSU estimates that the 2,942 construction jobs created between the 2007-2013 time period will generate $799.6 million in wages and pay $64.4 million to the state treasury and $15.99 million to local governments. (See Table 3)

Table 3: Estimated Construction Impacts of the Ohio HTC (Based on 2,942 jobs Created Annually between 2007-2013)

Wages by Place of Work	$799,697,875
Local Wage Tax (@2%)	$15,993,958
State Income Tax (2.88%)	$24,015,301
State Commercial Activity Tax: Self Supply	$1,965,180
State Commercial Activity Tax: Imports	$502,222
State Sales: Business to Business	$24,524,649
State Sales: Consumer	$13,747,489
Total State Revenue Estimates	$64,484,842
Total State and Local Revenue Estimates	$80,478,800

Using square footage, retail operating data on space utilization from the Urban Land Institute, and the new uses of the formerly vacant or underutilized buildings, CSU estimates an annual creation of jobs of 4,502 jobs during the operational phase.[9] Jobs created are projected to earn $4.6 billion in wages between 2009-2025 generating $254.25 million for state treasury and $92.33 million for local governments. (Table 4)

Table 4: Estimated Operational Impacts of Ohio HTC (Based on 4,502 Jobs Created Annually between 2009-2025)

Wages by Place of Work	$4,616,659,348
Local Wage Tax (@2%)	$92,333,187
State Income Tax (2.88%)	$138,604,440
State Commercial Activity Tax: Self Supply	$8,037,067
State Commercial Activity Tax: Imports	$2,524,264
State Sales: Business to Business	$20,327,658
State Sales: Consumer	$84,719,598
Total State Revenue Estimates	$254,249,027
Total State and Local Revenue Estimates	$346,582,214

[9] The operational estimates used by Cleveland State University for the analysis include: 90% occupancy for residential with 50% substitution; 80% occupancy for commercial buildings with 20% substitution; 66% occupancy for hotels with 75% substitution; and 75% occupancy for retail with 85% substitution.

CSU estimates that the total jobs created by Ohio's historic tax credit will generate over $5.41 billion in wages and those wages will generate $318.7 million in state revenues. Moreover, CSU estimates that the redeveloped buildings will generate $108.3 million in local revenues through a local wage tax (@2%). (see Table 5)

Table 5: Total Economic Activity Generated by Ohio's HTC Program (Based on Estimated Average of 6,976 Jobs Created Annually)

Wages by Place of Work	$5,416,357,223
Local Wage Tax (@2%)	$108,327,145
State Income Tax (2.88%)	$162,655,741
State Commercial Activity Tax: Self Supply	$9,732,247
State Commercial Activity Tax: Imports	$3,026,486
State Sales: Business to Business	$44,852,307
State Sales: Consumer	$98,467,087
Total State Revenue Estimates	**$318,733,869**
Total State and Local Revenue Estimates	$427,061,014

CSU estimates that these revenues will effectively pay back the state's total investment of $246,393,097 in nine years.

In addition to studying how much the tax credit returns on the state's investment, CSU also examined when the credits were paid back. Based on their research, the economists estimate that the State of **Ohio recovers $0.31 of every dollar invested prior to the disbursement of the tax credit** when the developer completes the rehabilitation project.

Researchers also found that 82% of the buildings were vacant to being redeveloped with the state's historic tax credit.[10] This means that buildings were put back on the property rolls and began generating local revenues,

Maine

In 2011, the research firm Planning Decisions, Inc. examined the revenue gains to both the state and local governments.[11] In 2007, Maine adopted a historic tax credit to

[10] Similar vacancy rates are found in other states. For example, the Wisconsin Historic Preservation Office found that 60% of the historic tax credit projects they approved in 2014 were vacant before their rehabilitation – including some that had been vacant 10, 20 and even 30 years.

enable the rehabilitation of the Hathaway Creative Complex in Waterville. After seeing the leveraging effect of the incentive, the legislature extended the tax credits to all historic properties in the state.

The first ten projects to be certified under the program "increased the assessed values in their community by $36 million (or ten times)."

Table 6: Local Property Tax Revenue Growth from Historic Tax Credit Projects

Project Name	Town	Assessed value Prior to Rehabilitation	Assessed value After Rehabilitation
Hathaway/Lockwood Mill	Waterville	$0	$12,000,000
Mill at Saco Falls	Biddeford	$389,000	$6,034,000
Squire Perley Building	Hallowell	$210,000	$6,811,000
North Berwick Woolen Mill	North Berwick	$606,600	$4,180,000
Baxter Library	Portland	$0	$2,500,000
Chestnut Street Church	Portland	$675,000	$1,162,400
Samuel T. Pickard House	Portland	$374,400	$374,400
Shepherd Block	Rockport	$843,700	$1,325,400
Union Hall	Rockport	$505,300	$505,300
Bessey School	Scarborough	$0	$1,534,400
Total		**$3,604,000**	**$36,426,900**

Researchers, calculated the revenues to the Maine treasury and local governments, created as a result of the rehabilitation undertaken with the historic tax credits.

Table 7: Revenue to State & Local Governments from Historic Tax Credit Projects

Year	Cumulative Increase in Property Value	Revenue Gain to Local Govt's from Property Taxes	Income/Sales Tax Revenue to Maine	Combined Revenue to State and Local Govt'	Cost of Historic Tax Credits	Net Effect on State Tax Revenue
2007	$6.9M	$0.10M	$0.18M	$0.28M	$0	$0.18
2008	$38.4M	$0.54M	$2.44M	$2.98M	$0	$2.44
2009	$57.5M	$0.80M	$1.35M	$2.15M	$0	$1.35
2010	$94.4M	$1.32M	$2.62M	$3.94M	-$2.44M	$1.50M
2011 (projected)	$134.7M	$1.89M	$2.63M	$1.89M	-$3.57M	-$.94M

[11] Planning Decisions, Inc., *The Economic and Fiscal Impact on Maine of Historic Preservation and The State Historic Preservation Tax Credit*, Maine Preservation, 2011.

In terms of timing, researchers also found that the state income and sales tax paid during the construction phase "front-loaded" -- or started paying back -- the state's investment. The construction phase "usually starts two years before occupancy." Then costs of the income tax credit are "not incurred until the next year's tax return is filed."

The researchers were also surprised by the amount of new construction these historic tax credit projects had spurred. They found that $25 million in new construction was generated by the $135 million spent in rehabilitation.[12]

The increase in property values is not just for the rehabilitated building alone. Historic tax credit projects also increase neighborhood property values according to a report done by real-estate researcher Donovan Rypkema. In a 2014 report, Rypkema found that since the complete of two key rehabilitation projects in Salt Lake City's Depot District, the market value of properties in the area had increased 22.5% -- at a time when the city-wide property values declined more than 17%.[13]

Conclusion

Historic tax credits generate a positive economic return on the state's investment through a combination of sales, income, and business taxes as well as applicable fees charged by the state. One-third of a state's investment is paid back during the construction phase. The payback period for the remainder of the investment varies depending on the end use of the historic property. The rehabilitated buildings – previously abandoned or underutilized – also generate additional revenues to local governments through increased property taxes. Historic tax credits also have been found to spur new construction and increase the property values in the surrounding neighborhoods. Historic tax credits are a smart state investment.

[12] Planning Decisions, Inc., *The Economic and Fiscal Impact on Maine of Historic Preservation and The State Historic Preservation Tax Credit*, Maine Preservation, 2011.
[13] Place Economics, "*Catalyst for Change, The Federal Historic Tax Credit: Transforming Communities.*" Prepared for the National Trust for Historic Preservation, June 2014.