



PROGRAM OVERVIEW and FREQUENTLY ASKED QUESTIONS

Historic Theatre Financing Fund

League of Historic American Theatres
and
National Trust Community Investment Corporation

Introduction

The Historic Theatre Financing Fund helps groups rehabilitating historic theatres access federal and state tax credits and convert these credits into equity (cash) to help finance the rehabilitation project. The equity can actually be used for a number of purposes, from defraying construction costs to creating an operating reserve. In most instances, though, the equity from tax credits is invested in the theatre's rehabilitation, reducing the amount of money that needs to be raised through debt financing and/or traditional fund raising.

The result of a partnership launched in 2004 between the [League of Historic American Theatres](#) and the [National Trust Community Investment Corporation](#), the Historic Theatre Financing Fund makes millions of dollars in equity investments available to [League members](#) for theatre rehabilitation. There are a number of technical requirements imposed by the Internal Revenue Service, National Park Service, and the Fund's equity investor in order to obtain the tax credits and convert them to equity. The League of Historic American Theatres helps streamline this process by providing basic information and guidance on the overall process to its members and helping them gather the basic information that will be needed by the tax credit equity investor.

In addition to providing information and guidance on the tax credit investment process, HTFF also brings theatre groups together with representatives of the National Trust Community Investment Corporation to pursue equity investments by the Fund's tax credit equity investors.

There are other institutional investors interested in tax credit projects, also. The League chose NTCIC to be its primary partner for several important reasons. First, unlike other tax credit investment entities, NTCIC's mission is the preservation of historic buildings (other investors invest in non-historic buildings and may have no institutional concern for the preservation of historic buildings). Second, NTCIC has access to one of the largest tax credit investment pools available for historic buildings and is willing to devote a large percentage of that equity to historic theatre rehab projects. Third, using tax credit investments to finance theatre rehabilitations is complicated, and the League and NTCIC are making a mutual investment of time and knowledge in the partnership to become as expert as possible in theatres and thus make the overall process easier for our members. Finally, NTCIC is the nation's most

experienced community development entity at “twinned” tax credit projects, and was the first in the nation to complete “twinned” projects with historic rehabilitation and New Markets credits.

Regardless of whether a League member chooses to use NTCIC or another tax credit investor, HTFF offers basic guidance to all members interested in learning more about tax credit investments, and NTCIC refers members to other tax credit investors in instances for which other investors might be more appropriate.

Why use tax credits?

Tax credit equity investments can be an extremely valuable part of a historic theatre’s rehabilitation financing plan, typically providing 20 percent or more of the project’s funding. In addition, the presence of tax credit equity investments in a theatre rehabilitation project can help a theatre organization raise additional revenue for the project, providing valuable leverage. In some instances, tax credits have made the difference between a theatre being rehabilitated or being demolished.

The federal and state governments offer three income tax credits that offer significant benefits for groups interested in rehabilitating historic theatres, and the Historic Theatre Financing Fund uses all of these tax credits:

- The federal historic rehabilitation tax credit encourages people to rehabilitate historic and non-historic older buildings.
- The federal New Markets Tax Credit encourages investors to make capital available to support business development in low-income neighborhoods. Most downtown districts – where historic theatres are usually located – qualify and are therefore usually eligible for the federal New Markets Tax Credit program.
- Many states offer state historic tax credits that can be combined with the two federal credits. North Carolina, Rhode Island, Virginia, Maryland, Missouri, Massachusetts, West Virginia, Michigan and Louisiana are among the states with the best programs.

Most groups rehabilitating historic theatres are not able to use the tax credits themselves – nonprofit organizations and public agencies do not pay federal or state income taxes and therefore have no tax liability against which to apply the credit. And for-profit operators of historic theatres rarely earn enough income (and therefore rarely have enough income tax liability) to use the full value of the credit.

Fortunately, it is possible for a group rehabilitating a historic theatre to transfer the tax credit to a for-profit investor who then uses the tax credit to offset some of its own tax liability. To do this, the theatre’s owner forms a limited partnership or limited liability corporation with the investor so that the investor becomes one of the theatre’s owners for a 5-7 year period of time. The investor can then claim the federal and state tax credits and, in exchange, invests equity into the theatre rehabilitation project. The amount of equity the investor invests in exchange for the tax credit varies, depending on the investor, but it is usually equal to about 90-95 percent of the total value of the historic rehabilitation tax credit, 45-85 percent of the state credits, and 50-55 percent of the New Markets Tax Credit.

This guide:

- provides an overview of the two federal tax credit programs to which the Historic Theatre Financing Fund provides access; (For information on your state tax credits, go to www.nationaltrust.org and click on State and Local Policy).
- outlines some of the requirements involved with the two tax credit programs that may affect planning

for the physical design of the theatre's rehabilitation, the organizational structure of the entities involved in the rehabilitation project, and the type and structure of financing involved;

- discusses the general process of claiming the credits and converting them to equity for the theatre rehabilitation project and provides an outline of the information needed to do so; and
- provides answers to some commonly asked questions about using the two tax credit programs for theatre rehabilitation projects.

Basic qualifications for the Fund's assistance

In order to qualify for the Fund's assistance:

- a theatre must be considered "historic" – meaning that it is listed on the [National Register of Historic Places](#), or is eligible to be listed, or that it is a "contributing" building in a National Register historic district; OR
- the theatre must be a non-historic building *built before 1936* (its non-historic status must be verified by your State Historic Preservation Officer); AND
- the organization in charge of the theatre's rehabilitation must be a theatre-level [member](#) of the League of Historic American Theatres.

While it is not required, we strongly recommend that one or more representatives of the organization in charge of the theatre's rehabilitation take part in one of the "Financing Historic Theatre Rehabilitation" training workshops offered each year by the League and NTCIC. Please [contact us](#) for a schedule of upcoming workshops or check the League's [website](#).

About tax credits

Historic rehabilitation tax credits

The federal government began offering historic rehabilitation tax incentives in 1976 to encourage owners of historic commercial buildings to rehabilitate them, rather than to build new ones. Property owners who rehabilitate a historic building can claim an income tax credit equal to 20 percent of the qualified rehabilitation expenses. (There is also a rehabilitation tax credit equal to 10 percent of qualified rehabilitation expenses for non-historic buildings built before 1936.) This is a credit against bottom-line income tax liability – not a deduction, but an actual credit that reduces taxes on a dollar-for-dollar basis – and is therefore a very valuable financial tool. Unlike other federal tax credit programs (like the low-income housing tax credit), there is no 'cap' or limit on the total amount of historic rehabilitation tax credits that taxpayers can claim in any given year.

The historic rehabilitation tax credit program is administered jointly by the Internal Revenue Service (IRS), the National Park Service (NPS), and the [State Historic Preservation Offices](#) (SHPOs). The program is codified in [Section 47](#) of the Internal Revenue Code.

A few basic requirements of the federal historic rehabilitation tax credit program, as they apply to historic theatres:

- The theatre must be listed in the National Register of Historic Places, either individually or as a

“contributing” building in a National Register-listed historic district. The National Register is maintained by the National Park Service, in the US Department of the Interior. The Park Service works in conjunction with the SHPOs to review applications for listing on the National Register.

- The theatre’s rehabilitation must be consistent with the guidelines contained in the [Secretary of the Interior’s Standards for Rehabilitation](#).
- In order to be eligible for federal historic rehabilitation tax credits, the qualified rehabilitation expenses must exceed the adjusted basis of the building or \$5,000, whichever is greater. “Qualified rehabilitation expenses” (QREs) include most soft and hard costs related to the theatre’s rehabilitation, other than property acquisition and (in most cases) enlargement. The “adjusted basis” is the original cost of the building (not including land), closing costs, and the value of capital improvements, minus depreciation (if any has been taken).
- In order to use federal rehabilitation tax credits (and, if they are available, state historic rehabilitation tax credits), the theatre must be owned by a for-profit entity, since nonprofit entities have no federal income tax liability against which to apply the credits. Many historic theatres, of course, are organized as nonprofit entities – so the nonprofit must be willing to either create a for-profit subsidiary or to partner with a new, freestanding for-profit entity in order to make it possible to claim the tax credits (we will discuss this in greater detail later in this bulletin).

[A number of states offer rehabilitation tax credits](#), as well, providing a tax credit against state income taxes. Like the federal rehabilitation tax credit, these state-level credits can be transferred to an investor, increasing the total amount of the equity investment in the theatre’s rehabilitation.

New Markets Tax Credits

The federal New Markets Tax Credit program was created to bring new capital to underserved areas that typically have difficulty attracting investors. Launched in 2001, the program provides a 39 percent tax credit, spread over seven years, to investors who make money available for loans and equity investments in qualified business development activities in eligible areas. Unlike federal and state historic rehabilitation tax credits, which directly benefit the owner of a historic building, the New Markets Tax Credit directly benefits the investors who make loans or invest equity in a project. The investors, in turn, usually make more equity available than they might otherwise do, or make a loan at better rates. The program is expected to attract \$15 billion in new investment to underserved areas by the time it expires in 2007.

Groups involved in rehabilitating a historic theatre don’t really need to be concerned with most of the details of how to create a New Markets Tax Credit investment group or obtain an allocation of credits – but, in brief, the program works like this:

- The New Markets Tax Credit program is administered by the [Community Development Finance Institutions \(CDFI\) Fund](#) (part of the US Department of the Treasury), and the Internal Revenue Service.
- A nonprofit or for-profit entity interested in making more capital available for business development in a specific geographic area, or for a specific project, applies to the CDFI Fund for certification as a “community development entity,” or CDE.
- The CDE partners with an investor, or a group of investors, interested in making tax-advantaged financing available to eligible projects.
- The CDE then applies to the CDFI Fund for an allocation of New Markets Tax Credits. This is a highly competitive process, and the application is quite complicated.

- Once a CDE receives an allocation of New Markets Tax Credits, it passes those credits along to its investors, who, in turn, make loans and equity investments in eligible projects through the CDE.

The Historic Theatre Financing Fund helps League members find investors (including, but not limited to, NTCIC) with allocations of New Markets Tax Credits and who are interested in making equity investments in historic theatre rehabilitation projects. The New Markets Tax Credits can be combined with federal and state historic rehabilitation tax credits. If a theatre is in an eligible census tract, this can increase the total amount of equity available for qualified projects by roughly 25 percent of the amount of the federal and state historic rehabilitation tax credit equity investment.

The New Markets Tax Credit program has a number of requirements for CDEs and investors, but there are only a few that a group rehabilitating a historic theatre needs to know about:

- In order to be eligible for the New Markets Tax Credit program, the [census tract](#) in which the theatre is located must have a poverty rate over 20 percent or a median family income of 80 percent or less than that of the metropolitan area or of the state (whichever is less).
- If the theatre is part of a larger, mixed-use rehabilitation project, no more than 80 percent of the overall project's gross revenue can come from housing uses.

The League strongly encourages groups rehabilitating historic theatres to take advantage of the federal New Markets Tax Credits program, if the theatre is located in an eligible census tract. Unless reauthorized by Congress, the New Markets Tax Credits program will only be available through 2007, which means that it represents a short-term opportunity to increase the amount of tax credit equity available for historic theatre rehabilitation projects. We will therefore automatically investigate the possibility of using the New Markets Tax Credit in all theatre rehabilitation projects with which the Fund works.

Additional qualifications for the Historic Theatre Financing Fund

In addition to the Internal Revenue Service's and National Park Service's requirements, the Historic Theatre Financing Fund has a few additional guidelines and requirements:

- The financing for the theatre rehabilitation cannot include any foreclosable debt (e.g., a loan for which the theatre itself serves as collateral). Loans may, however, be collateralized by grants, pledges, or real estate unrelated to the project.
- Ideally, the transfer of ownership from the theatre's owner to the limited partnership or LLC should take place before the rehabilitation project begins.
- There are some Internal Revenue Service rules regarding the use of federal tax credit when a building is occupied by a tax-exempt entity (like a nonprofit theatre management organization). If tax-exempt tenants use more than 35% of the building's leasable space, the financing package cannot include using tax-exempt financing (like tax-exempt bonds) to pay for rehabilitation expenses (although tax-exempt financing may be used to pay for non-rehabilitation expenses, such as construction of a new building in conjunction with the theatre rehabilitation project). Leases to nonprofits occupying more than 35% of the building should be less than 20 years. Use of the building by a tax-exempt entity prior to placement in service as a tax credit project may preclude use of the federal historic tax credit. You should discuss the situation with us if any of these facts fit your project.
- The theatre must be substantially rehabilitated before it is placed in service.

- You should be prepared to put together a development team with experience in historic rehabilitation tax credit projects. It is particularly important that your project architect, outside counsel, preservation consultant, and tax accountant have experience with federal and state historic rehabilitation tax credits and with New Markets tax credits.
- Your project should have the support of local government.
- You'll need an operating plan, development budget (outlining the sources and uses of funds for the theatre's rehabilitation) and seven-year operating proforma (projecting the theatre's sources of income, once in operation), all approved by your board.
- Your key financing should be identified and committed.

Don't worry if your project already involves some elements that contradict these guidelines, or if some of these things are not yet in place; some problems can be resolved, particularly if HTFF is able to review the overall project relatively early in the rehabilitation planning process.

Using the tax credits

The basic process of obtaining historic rehabilitation tax credits

Every theatre rehabilitation project is different – and the sequence of activities involved in the tax credit equity investment process will therefore be different for every project. In general, though, the basic sequence of events goes like this:

- The group involved in rehabilitating the historic theatre assembles a project team that includes an architect, historic preservation consultant, contractor, restoration specialist, accountant, tax attorney, fund raising consultant, and a project coordinator. Ideally, all key team members should have experience working with historic buildings and with the federal historic rehabilitation tax credit. The team will essentially have two functions:
 - Ensuring that the physical rehabilitation of the theatre meets the Secretary of the Interior's Standards for Rehabilitation and that the rehabilitation expenses will therefore be eligible for the tax credits, and
 - Ensuring that the financing for the theatre rehabilitation and the organizational structure of the entities involved in the rehabilitation meet the Internal Revenue Service's requirements.
- The theatre's rehabilitation project team certifies that the theatre is historic by filing Part I of the [Historic Preservation Certification Application](#) with the appropriate State Historic Preservation Office (SHPO). This application is reviewed by the SHPO, which then forwards it to the National Park Service with a recommendation for approval or rejection.
- Assuming the Part I application is approved by the SHPO and National Park Service, the rehabilitation project team then files Part II of the Historic Preservation Certification Application with the SHPO in order to certify that its plans for rehabilitating the theatre are consistent with the Secretary of the Interior's Standards for Rehabilitation. In Part II, the project team documents the theatre's condition and appearance before rehabilitation and outlines its rehabilitation plans in detail. The SHPO reviews the Part II application carefully and will want to discuss the project with the architect and other key team members to ask questions and make suggestions. The SHPO then forwards the Part II application to the National Park Service with a recommendation for approval or rejection.

[NOTE: Sometimes, the Part I and Part II applications are submitted together.]

- When the project is completed, the rehabilitation project team files Part III of the Historic Preservation Certification Application with the SHPO, certifying that the rehabilitation was carried out according to the plans outlined in Part II. When the Part III is approved and the theatre is placed in service, the theatre's owner can then claim the tax credit by filing IRS Form 3468 with its federal income tax return. If the entity that owns the theatre does not have enough tax liability to use the entire credit, it can spread the credit over as many as 20 years into the future or can 'carry back' the credit one year, amending the prior-year tax return.

Turning the tax credits into equity investments

It is very rare for for-profit historic theatres to generate enough profits to be able to use the full value of the historic rehabilitation tax credit to offset its own income tax liability – and nonprofit theatres have no income tax liability against which to apply tax credits. But, the owner of a historic theatre can transfer the tax credit to someone who needs tax credits to offset tax liability, then use the proceeds of the transfer to help finance the theatre's rehabilitation or operation. In essence, the theatre organization forms a partnership with an equity investor (a tax-paying entity that would like to reduce its tax liability by obtaining tax credits). The equity investor becomes the 99.99% owner of the theatre for a period of time, usually five years⁽¹⁾, with a for-profit subsidiary of the nonprofit theatre organization becoming the .01% owner and retaining control of and management responsibility for the theatre. During that period, the investor claims the tax credits and uses them to reduce its income tax liability. In exchange, the investor invests an amount of equity in the theatre rehabilitation project equal to 90-95% of the tax credit, less the closing costs. After the compliance period, the investor will typically allow the nonprofit to buy it out for about 15% of the original capital invested.

By launching the Historic Theatre Financing Fund, the League and its Fund partner, NTCIC, have simplified the process of finding a tax credit equity investor for historic theatres. In addition, by focusing on historic theatres, the Fund's equity investor has developed specialized expertise in using historic rehabilitation tax credits and New Markets Tax Credits for theatre rehabilitation projects.

Using the Historic Theatre Financing Fund

The Historic Theatre Financing fund provides two major benefits for groups rehabilitating historic theatres:

- It helps groups rehabilitating historic theatres understand the tax credit equity investment process and organize the information they will need in order to partner with a tax credit equity investor, and
- It offers access to NTCIC, an equity investor with extensive experience in both the historic rehabilitation and New Markets tax credit programs, in combining the two tax credit programs, and in investing in historic theatre rehabilitation projects.

If you think your theatre might be a candidate for tax credit equity investments, or if you would like to discuss the program in greater detail, please contact Kennedy Smith (kennedy@lhat.org). We can help you explore the possibility and, if it seems like your theatre might be a good candidate for HTFF's assistance, we will arrange a meeting or conference call with a representative of our equity investor, the

¹ Five years is the "recapture" period (meaning the period of time in which the tax credits could be taken back by the federal government), if there is a transfer of ownership or the character of the building is altered during this compliance period.

National Trust Community Investment Corporation (NTCIC). If, after meeting with NTCIC, it appears that the project can move forward, NTCIC will develop a term sheet – basically, an expression of the terms on which the equity investment will be made – for your theatre group to approve. From that point forward, we will stay in close contact with you throughout the process of finalizing the project's equity investment.

We can also help you find professionals – architects, engineers, fund raising consultants, and others – experienced in historic theatre rehabilitation projects using tax credits.

HTFF's services are free to the League's theatre-level members⁽²⁾.

Information needed

There is quite a bit of information that needs to be assembled in order to obtain almost any type of financing for a major rehabilitation project – and tax credit equity investments are no exception. Among the information you will ultimately need to assemble:

- Project overview: A written summary of the project, including a description of the theatre at the current time (location, square feet, number of seats, physical condition, etc.), an overview of the proposed rehabilitation project, and a proposed timeline (including target dates for property acquisition, construction period, and theatre opening).
- Overview of the current ownership structure: A written description of the entity that currently owns the theatre, including information on how long the entity has owned the theatre and whether it, or a related entity, operated the property after acquiring it.
- Overview of the development team: A written summary of the development team's key members, including:
 - project coordinator (the “clerk of the works”)
 - project architect
 - historic preservation consultant
 - general contractor
 - restoration consultant (decorative specialist)
 - tax attorney
 - accountant
 - booking and leasing agent (if applicable)
 - fund raising consultant

Highlight each member's previous experience with projects involving historic buildings and the historic rehabilitation tax credits.

- Overview of the proposed theatre management entity: A written description of the management entity that will manage the theatre, once the rehabilitation is completed. If you have a written agreement in place with a management company, include a copy of the agreement. If you are planning to hire a management company but have not yet done so, include a list of the operators under consideration.

² If the project closes on an NTCIC-based equity investment package, NTCIC will earn compensation from its investors for a variety of tasks including investment underwriting and real estate investment closings. The League will then receive a referral fee from NTCIC, which the League uses to support its educational programs. This does not affect the amount of equity a theatre receives.

- “Phase 1” environmental assessment report: This assessment identifies any potential environmental hazards that might exist in the theatre and that will probably need to be properly removed before the project can proceed. It is not uncommon for older theatres to contain asbestos or lead-based paint, for example, or for oil from oil tanks to have leaked into the basement and subsoil beneath the theatre.
- Status of National Park Service approvals: A written summary of the status of the theatre’s National Register listing and Parts I and II of the National Park Service’s Historic Preservation Certification Application, with hard copies of the Parts I and II (if they have already been filed).
- A “sources and uses” spreadsheet: A spreadsheet that lists the sources of funding/financing for the theatre rehabilitation project and a development budget that lists how those funding sources will be used (see attached example).
- A 7-year operating pro forma: A spreadsheet that details projected revenues and expenses for seven years after reopening (see attached example).
- Fund raising summary: A written summary and/or spreadsheet detailing amounts raised to date, paid and outstanding pledges, and the total amount remaining to be raised.
- Photos: 10-15 photos (digital, if possible) of the theatre’s exterior, interior, and surrounding environment.
- Maps: Map showing the theatre’s location in the community and showing its immediate environment.
- Copies of financing commitments (construction and permanent), if available
- Most recent year-end audited financial statements for the key sponsoring entity (theatre foundation, theatre company, developer) and guarantor (if different from the key sponsoring entity).
- Appraisal report: Almost every lender will require a full appraisal of the theatre before providing financing for the rehabilitation project. NTCIC will accept the lender’s appraisal if there is one, or under some circumstances, waive the appraisal requirement.

Questions + Answers

What expenses are considered “qualified rehabilitation expenses”?

Most structural components – walls, ceilings, floors, stairs, elevators, plumbing, electrical wiring, heating/air conditioning systems – are eligible. Many “soft” costs are eligible, also, such as architects’ fees, construction management fees, and interest and taxes paid during the construction phase. Most non-permanent components (like sound systems or appliances) and components located outside the building (like paving, landscaping, and retaining walls) are not eligible. Acquisition costs, feasibility studies, and demolition expenses are not eligible, either. Only expenses that pertain to the building’s rehabilitation (versus any new construction, such as an addition) are eligible.

Are seats considered a “structural component,” and do they therefore qualify for the historic rehabilitation tax credit?

Yes, if they’re bolted in place (and are therefore a permanent building component).

How can I find out if my theatre is eligible for historic rehabilitation tax credits?

If it is listed individually in the National Register of Historic Places, or if it is a “contributing” building³ in a historic district that is listed in the National Register, it is eligible for historic rehabilitation tax credits (assuming that your rehabilitation plans conform to the Secretary of the Interior’s Standards for Rehabilitation). Check with your local historic preservation organization, your city planning office, or your state historic preservation office to ask if your theatre is listed in the National Register or is in a National Register-listed historic district.

I checked with my city planning office, and it says that my theatre is not listed in the National Register of Historic Places. How can I get it listed?

Contact your state historic preservation office (see “Resources”, below). Its staff can help you with this.

How can I find out if my theatre is in a census tract that’s eligible for New Markets Tax Credits?

The federal Community Development Financial Institutions Fund (CDFI Fund, for short) – a program of the US Department of the Treasury – has an online service through which you can check to see if your theatre is in a New Markets Tax Credit-eligible census tract. However, the process is very complicated, and it requires you to create an account with the CDFI Fund in order to access it. HTFF is therefore happy to check your theatre’s eligibility for you. Just email your theatre’s name, its *street address* (not mailing address or PO box), and its zipcode to kennedy@lhat.org. We will check your theatre’s eligibility and will email you a copy of the CDFI Fund’s website’s report for your records.

The historic rehabilitation tax credit is available for income-producing commercial property, and you say that the theatre should therefore have an operating profit. But our theatre has been closed for ten years. How can we show it having an operating profit?

You can use a solid business plan providing realistic projections of the revenue you anticipate. Include all likely sources of income, including ticket sales from productions your organization sponsors, rentals to other organizations, concession sales, and annual fund raising. Lenders and the equity investor will probably want to know how you developed these projections, so you should plan to document your projections thoroughly, providing information on any market studies that might have been conducted, on revenues generated by comparable theatres in similar market areas, and on other resources you have used to develop your income projections.

We don’t feel comfortable with the idea of sharing ownership of the theatre with a tax credit investor. How can we be sure the investor will transfer ownership back to us at the end of the five-year recapture period?

There is really no danger that the investor will not exercise its option to transfer ownership back to you. There are “put” and “call” provisions built into the deal so that the development organization can obtain control of the project after the compliance period is over. Once the investor is out of the deal, it only takes a vote of the sole remaining member – usually a for-profit subsidiary of the theatre – to sell the asset back to the nonprofit theatre organization. To further ensure that the investor will transfer ownership back to the theatre organization, you should ask the tax credit investor to agree to an additional capital call in the operating agreement that penalizes the investor if it does not promptly transfer ownership.

We are planning to rehabilitate our theatre in phases, over the course of several years. Can

³ “Contributing” means that it contributes positively to the district’s significant architectural or historic characteristics.

we still use the rehabilitation tax credits?

Yes – but the project must be completed within five years. The 60-month rule is permitted if architectural plans and written specifications for all phases are in place and approved before rehabilitation begins and if it is reasonably feasible that the entire rehabilitation project can be completed within five years. However, it is difficult to use the New Markets Tax Credit in a five-year phased project. Also, the compliance or recapture period on a phased project will not begin until the last qualified rehab expenditure is made.

Our city government is issuing tax-exempt bonds to help finance the theatre rehabilitation. Can I still use the tax credits?

It will be very difficult to use the federal historic credit. But it may be possible for the city to issue taxable bonds or to convert the tax-exempt bonds to taxable bonds, which would make your project eligible for the federal historic rehabilitation tax credit. Tax-exempt bonds can be use with the New Markets Tax Credit and most state historic rehabilitation tax credits.

We estimate that the total cost of rehabilitating our theatre will be around \$1 million, so the 20 percent federal rehabilitation tax credit will be about \$200,000. I know we will need to pay an accountant, a tax attorney, and other professionals to complete the tax credit equity investment transaction. Will these costs approach or exceed the value of the tax credit?

Your question raises an excellent point: Larger projects are more financially “efficient” than smaller ones. Due diligence and transaction expenses can be costly, and it takes almost as much time and energy to do the paperwork for a small project as it does for a large one. It is therefore much easier to recoup those expenses on a larger project (over \$3 million or so) than on a smaller one.

For smaller theatre rehabilitation projects, HTFF often works with a tax credit equity investor who specializes in smaller historic rehabilitation tax credit projects (under \$2 million in total development costs, more or less), which might make it easier for smaller projects to obtain tax credit equity investments.

The family that owns our downtown theatre doesn’t want to sell or rehabilitate it – but they are willing to lease it to our nonprofit theatre organization. If we rehabilitated the theatre, could we use the historic rehabilitation tax credit?

Yes, with a long-term lease of at least 45 years. In certain situations, it might be possible to renegotiate the lease after the historic rehabilitation tax credit recapture period has expired.

We have already begun our rehabilitation project and are not sure that some of the work we have done would qualify for the historic rehabilitation tax credit. Is it too late for us to use the tax credits?

It may not be too late. Although the National Park Service generally frowns on projects that seek the tax credit after construction has already begun, it is often possible to file the necessary paperwork retroactively and claim the credit. In order to do so, you will need to have very good records documenting all the work that has been done so far (including good photographs of the theatre before rehabilitation work began and of all the work that has been completed to date). You should talk with a historic preservation consultant experienced in working with historic theatres as soon as possible. Given how valuable the credits can be, it is certainly worth exploring the possibility.

We are interested in converting three contiguous historic downtown storefront buildings

into a theatre. Would this project be eligible for tax credits?

Possibly. You should talk with your State Historic Preservation Office to see if your project might qualify for the historic rehabilitation tax credits.

We need to enlarge the stage house of our theatre in order to attract major productions – otherwise, we just can't compete with larger theatres in our region, and our theatre might be at risk of being demolished. Are the expenses associated with this new construction eligible for the historic rehabilitation tax credit?

Good question! In general, the costs of expanding a historic building (specifically, for increasing its volume) are not eligible for the historic rehabilitation tax credit.⁴ However, there are a few instances in which a SHPO has considered a stage house enlargement to be essential for the theatre to continue functioning economically. In general, it is best to avoid increasing the volume of the theatre, if at all possible⁵. If expansion is really the only option for the theatre's survival, though, talk with your project architect and historic preservation consultant about how you might best do this without putting the rehabilitation tax credits at risk.

My theatre isn't historic, so it wouldn't qualify for the federal historic rehabilitation tax credit. But, can I still use the New Markets Tax Credit program?

Yes, if it is located in a census tract eligible for New Markets Tax Credits. The historic rehabilitation tax credit and the New Market Tax Credit are separate programs. There are significant advantages in combining the two credits, if a theatre is eligible for both – but there is certainly no requirement in either of these two federal tax credit programs that they be combined.

Also, keep in mind that there is a 10 percent rehabilitation tax credit available for *non*-historic buildings constructed prior to 1936. Like the 20 percent historic rehabilitation tax credit, the 10 percent credit can be combined with the New Markets Tax Credit.

Do we need any special kind of insurance coverage for our theatre in order to use the Historic Theatre Financing Fund's services?

Your lenders and investors (including NTCIC) will want documentation that your theatre has adequate insurance, both during rehabilitation and after the rehabilitation is complete and the theatre is operating. Historic theatres have special insurance needs, so the League has partnered with Maury Donnelly & Parr, a Baltimore-based insurance brokerage, to put together an insurance program designed to provide comprehensive coverage for historic theatres at very competitive rates. Please contact Colleen Poehlman (cpoehlman@lhat.org) for more information.

Which investors participate in the National Trust Community Investment Corporation?

There are a number of investors, including Chevron, Texaco, US Bank, National City Bank, and Bank of America. Bank of America is NTCIC's largest single investor.

Can individual donors who make sizable contributions to my theatre's rehabilitation project

⁴ There are also some very specific requirements about how much of the original exterior surface area of a historic building must be retained in order for the building's rehabilitation expenses to be eligible for the historic rehabilitation tax credits. See the Secretary of the Interior's Standards for Rehabilitation for more information.

⁵ Sometimes, it might be possible to expand the theatre's space by using adjacent buildings. Dressing rooms or rooms for equipment or scenery storage, for example, might fit well into adjacent storefront buildings, freeing up space within the theatre itself for expansion without having to enlarge the building's shell.

serve as the project's tax credit investors, rather than using an investor like NTCIC?

Theoretically, yes – but, in practice, no. Your project would need to be an enormous one in order for the amount of the tax credit investment to cover their due diligence costs. The dozen or so major tax credit investors in the US have full-time staffs of attorneys and accountants who specialize in tax credit investments, and most of them make hundreds of millions of dollars in equity investments annually, thus making the process financially feasible for them.

This all seems so overwhelming. Is it worth going through the process?

Tax credit investments can provide a significant percentage of the amount of money needed to rehabilitate a historic theatre. This is particularly true for theatre rehabilitation projects that are eligible for both historic tax credits and New Markets Tax Credits. Several of the theatres HTFF is currently working with may be able to obtain as much as 40 percent of the financing needed for their rehabilitation projects from tax credit investments. It does involve a lot of work, though – that's why the League created HTFF, to help make the process easier for groups rehabilitating historic theatres.

This all seems so overwhelming. Where should I get started?

Send us an email (kennedy@lhat.org), and we'll arrange a telephone call to explain the overall process, discuss your plans, and answer any initial questions you might have. It would be helpful to include a little bit of information in your email message about your theatre. We'll need to know:

- When it was built
- If it's listed in the National Register of Historic Places (or, if not, if you think it is eligible for listing)
- Its street address (not mailing address) and zipcode
- How much you estimate the theatre's rehabilitation will cost
- How you plan to operate the theatre
- Who currently owns the theatre
- Whether the theatre is currently in operation
- What you envision your main sources of funding or financing being for the rehabilitation, how much you have raised or secured so far, and whether any of your funding includes tax-exempt sources (like tax-exempt bonds)

For many projects, we think it is a good idea for you to hire someone early on who can serve as an overall project coordinator – a “clerk of the works”, so to speak, to work with the rest of your project team (architects, attorneys, accountants, and historic preservation consultants, in particular) to be sure the physical rehabilitation plan and the project's financing meet all the requirements for the tax credits and that the process unfolds as smoothly as possible. It is essential that this person be familiar with both tax credit equity investments and with historic theatre rehabilitation projects.

Resources

Program partners:

League of Historic American Theatres:

<http://www.lhat.org>

National Trust Community Investment Corporation:

http://www.nationaltrust.org/community_partners/hist_tax_credit.html

Historic rehabilitation tax credits:

Information from the National Park Service on the federal rehabilitation tax credit program:

<http://www.cr.nps.gov/hps/tps/tax/brochure1.htm>

Directory of State Historic Preservation Offices:

http://grants.cr.nps.gov/Shpos/SHPO_Search.cfm

The Secretary of the Interior's Standards for Rehabilitation:

<http://www.cr.nps.gov/hps/tps/tax/rehabstandards.htm>

National Register of Historic Places:

<http://www.cr.nps.gov/nr/>

Information from the Internal Revenue Service on the federal rehabilitation tax credit program:

<http://www.irs.gov/businesses/small/industries/article/0,,id=97599,00.html>

Rehabilitation Tax Credit Guide:

http://www.nationaltrust.org/community_partners/taxcreditguide/index.html

Section 47 of the Internal Revenue Code:

http://assembler.law.cornell.edu/uscode/html/uscode26/usc_sec_26_00000047----000-.html

New Markets Tax Credits:

Community Development Financial Institutions:

<http://www.cdfifund.gov/>

Census tracts:

http://www.census.gov/geo/www/cen_tract.html

New Markets Tax Credit Coalition:

<http://www.newmarketstaxcreditcoalition.org>

Sample "Sources and Uses" Budget

Sources of Funds	Construction	Permanent
Permanent Financing: 1st Mortgage		-
Bridge Loan	4,110,890	-
Capital Contribution	22,405,579	22,405,579
Master Tenant Equity (Federal HRTC & NMTC)		82,500
Other	-	0
Deferred Developer Fee		1,000,000
Total Sources	\$26,516,469	\$23,488,079
GAP		\$5,895,164

Uses of Funds (Development Budget)	Total	Depreciable QRE	Depreciable non - QRE	Amortized	Funded Expense	Excluded Items
Acquisition	-					-
Land	670,000	-	-	-	-	670,000
Building	770,000	-	770,000	-	-	-
Closing & Carrying Costs	-	-	-	-	-	-
Sub-Total: Acquisition	\$1,440,000	\$0	\$770,000	\$0	\$0	\$670,000
Construction Hard Costs						
Site Improvements	-	-	-	-	-	-
Environmental Remediation	380,000	380,000	-	-	-	-
Construction Cost	15,798,859	15,039,859	759,000	-	-	-
Payment and Performance Bond	103,000	98,052	4,948	-	-	-
Construction Inspection & Monitoring	30,000	28,559	1,441	-	-	-
Construction Cost: Owner Purchased Materials	-	-	-	-	-	-
Demo: Owner Related	30,000	28,559	1,441	-	-	-
Hard Cost Contingency @ xx	1,780,142	1,694,621	85,521	-	-	-
Furniture, Fixtures, & Equipment	210,000	-	210,000	-	-	-
Preconstruction Consulting & Exploration	40,000	40,000	-	-	-	-
Telecommunications Network	100,000	50,000	50,000	-	-	-
Construction Period Security	45,000	42,838	2,162	-	-	-
Proscenium Prefinish Test	12,000	12,000	-	-	-	-
Wurlitzer Protection During Renovation	9,000	9,000	-	-	-	-
Sub-Total: Construction	\$18,538,001	\$17,423,488	\$1,114,513	\$0	\$0	\$0

Soft Costs						
Architecture & Engineering: Programming & Pre-design	238,000	226,566	11,434	-	-	-
Architecture & Engineering: A&E services	2,316,779	2,205,478	111,301	-	-	-
Architecture & Engineering; Reimbursable expenses	250,000	237,990	12,010	-	-	-
Architecture & Engineering: Historic Certification	30,000	30,000	-	-	-	-
Third Party Printing/Reproduction	25,000	23,799	1,201	-	-	-
Geotechnical	38,300	36,460	1,840	-	-	-
Interior Surveys	10,000	9,520	480	-	-	-
Surveys	10,000	9,520	480	-	-	-
Environmental Review	20,000	19,039	961	-	-	-
Permits & Fees	-	-	-	-	-	-
Insurance	323,000	307,483	15,517	-	-	-
Real Estate Taxes	35,000	33,319	1,681	-	-	-
Other Taxes	35,000	33,319	1,681	-	-	-
Construction Period Utilities	100,000	95,196	4,804	-	-	-
Appraisal & Market Study	5,000	4,760	240	-	-	-
Historic Tax Credit Consultant (NTHP)	35,000	33,319	1,681	-	-	-
Legal: Local Counsel	82,500	78,537	3,963	-	-	-
Legal: Tax Opinion	25,000	23,799	1,201	-	-	-
Title Insurance	50,000	47,598	2,402	-	-	-
Asset Management Fee	15,000	-	-	-	15,000	-
Accounting & Cost Certification	35,000	33,319	1,681	-	-	-
Local Accounting, Compliance, Related Services	75,000	-	-	-	75,000	-
Marketing & Project Start-up	35,000	-	-	-	35,000	-
Insurance Deductible Contingency	40,000	-	-	-	-	40,000
Soft Costs Contingency @ xx%	30,000	22,500	7,500	-	-	-
Sub-Total: Soft Costs	\$3,858,579	\$3,511,517	\$182,062	\$0	\$125,000	\$40,000
Financing Costs						
Construction Financing (Consortium): Fees	12,500	11,899	601	-	-	-
Construction Financing (Consortium): Legal	15,000	14,279	721	-	-	-
Construction Financing (Consortium): Interest Expense	100,000	95,196	4,804	-	-	-
Equity Bridge Financing: Fees	10,277	9,783	494	-	-	-
Syndication	20,000	-	-	-	-	20,000
Equity Bridge Financing: Legal	10,000	9,520	480	-	-	-
Equity Bridge Financing: Interest Expense	125,000	93,750	31,250	-	-	-
Equity Bridge Financing: Closing Costs	5,000	-	-	5,000	-	-
Sub-Total: Financing Costs	\$297,777	\$234,428	\$38,349	\$5,000	\$0	\$20,000

Reserves						
Operating Reserve	300,000	-	-	-	-	300,000
Investor Buyout Reserve	700,000					700,000
Replacement Reserve	15,000	-	-	-	-	15,000
Sub-Total: Reserves	\$1,015,000	\$0	\$0	\$0	\$0	\$1,015,000
Development Fees	\$4,233,886	\$4,233,886	\$0	\$0	\$0	\$0
Total Development Cost	\$29,383,243	\$25,403,318	\$2,104,925	\$5,000	\$125,000	\$1,745,000

Sample Pro Forma

ANNUAL OPERATIONS BUDGET PROJECTIONS FOR 5 YEARS

(Assumes general inflation rate of 3%)

Forecast by Year				
FY	FY	FY	FY	FY
2005	2006	2007	2008	2009

No of Fine Arts Performances	24	27	30	33	35
No of Pop/Rock Performances	24	27	30	30	32
No of Revenue Days	150	156	162	165	172
Percent of Capacity Sold	72%	73%	75%	75%	75%
Advertising/Event Sponsorships, net	\$88,000	\$94,000	\$106,000	\$118,000	\$138,000
Theatre Usage Fee Increase Over Prior Year	100%	0%	0%	10%	0%

REVENUES

Ticket Sales for Performances Booked by Primary Tenant:

General	\$2,357,492	\$2,484,767	\$2,627,560	\$2,599,171	\$2,685,744
Dedicated to Capital and Maintenance Reserve Fees	\$69,068	\$76,628	\$85,280	\$88,769	\$95,746
Dedicated To Theatre User Fees	\$130,000	\$145,000	\$161,000	\$185,900	\$194,700
	<u>\$2,556,5</u>	<u>\$2,706,3</u>	<u>\$2,873,8</u>	<u>\$2,873,8</u>	<u>\$2,976,1</u>
Total Ticket Sales	60	95	40	40	90
Capital and Maintenance Reserve Fees - Private and Nonprofit Events	\$42,160	\$42,160	\$42,160	\$42,160	\$42,160
Theatre User Fees - Private and Nonprofit Events	\$275,250	\$275,250	\$275,250	\$302,775	\$302,775
Concessions and Mixed Drinks Income	\$68,000	\$68,000	\$68,000	\$68,000	\$68,000
Parking, Merchandise, Other Miscellaneous Income	\$54,854	\$59,059	\$63,865	\$65,807	\$68,698
Advertising/Event Sponsorships, net	\$88,000	\$94,000	\$106,000	\$118,000	\$138,000
	<u>\$3,084,8</u>	<u>\$3,244,8</u>	<u>\$3,429,1</u>	<u>\$3,470,5</u>	<u>\$3,595,8</u>
	24	64	15	82	23

NET REVENUES

EXPENSES

Operating Expenses

Management Fee	\$168,000	\$176,400	\$181,692	\$181,692	\$187,143
Advertising and Promotion	\$33,000	\$33,525	\$34,066	\$36,023	\$36,754
Audit and Accounting	\$40,000	\$41,000	\$42,050	\$45,153	\$46,310
Insurance	\$55,000	\$66,000	\$75,900	\$83,490	\$90,169
Legal Expense	\$10,000	\$10,000	\$10,000	\$10,400	\$10,400

Maintenance: Building, Equipment and Janitorial	\$48,000	\$45,189	\$46,112	\$47,789	\$48,766
Office and Administration Expenses	\$35,000	\$35,474	\$35,992	\$36,533	\$37,051
Taxes	\$54,000	\$54,000	\$54,000	\$54,000	\$54,000
Telephone	\$14,000	\$14,390	\$14,792	\$15,305	\$15,732
Utilities	\$120,000	\$123,600	\$127,308	\$131,127	\$135,061
Total Operating Expenses	\$577,000	\$599,578	\$621,911	\$641,512	\$661,386
<u>Program Expenses</u>	\$1,189,000	\$1,235,000	\$1,282,500	\$1,282,500	\$1,320,000
Talent Expense					
Expenses Paid to Primary Tenant					
Booking and Marketing Fee	\$141,912	\$166,831	\$192,197	\$176,911	\$181,548
Production Expenses	\$138,300	\$156,300	\$169,800	\$175,800	\$185,400
Booking, Marketing, Production Expenses paid to Primary Tenant	\$280,212	\$323,131	\$361,997	\$352,711	\$366,948
Advertising Expense for Events	\$272,000	\$285,000	\$298,500	\$298,500	\$309,800
Credit Card Charges	\$50,811	\$53,902	\$57,355	\$57,355	\$59,178
House Labor	\$124,155	\$130,890	\$137,625	\$138,525	\$143,535
Miscellaneous Expense	\$152,696	\$162,609	\$173,076	\$175,379	\$182,407
Projectionist	\$2,400	\$2,400	\$2,400	\$2,400	\$2,760
Film Rentals & Shipping	\$28,555	\$28,555	\$28,555	\$28,555	\$32,884
Movie Booking Fees	\$1,320	\$1,320	\$1,320	\$1,320	\$1,560
Movie Presentation Costs	\$32,275	\$32,275	\$32,275	\$32,275	\$37,204
Security	\$22,240	\$23,240	\$24,440	\$24,440	\$25,240
Sound/Lights	\$184,500	\$194,500	\$205,000	\$205,000	\$212,000
Total Program Expenses	\$2,307,889	\$2,440,547	\$2,572,768	\$2,566,685	\$2,656,312
Annual change	5.75%	5.42%	-0.24%	3.49%	2.04%
TOTAL OPERATIONS AND PROGRAM EXPENSES	\$2,884,889	\$3,040,125	\$3,194,679	\$3,208,197	\$3,317,698
NET OPERATIONS AND PROGRAM INCOME	\$199,935	\$204,739	\$234,436	\$262,385	\$278,125