Historic Tax Credits

Emily Cauzillo
FVP, Director of Mercantile Community Partners
MHPN Board Treasurer

Mercantile Bank®

Mercantile
Community Partners

- Subsidiary of Mercantile Bank formed in 2023
- Provides equity investment to community development projects using **tax credit incentive financing**
- One-Stop-Shop for non-profit and for-profit real estate developers providing construction debt and equity

Emily Cauzillo
FVP, Director
ecauzillo@mercbank.com

- 15 years commercial banking and 10 years tax credit financing
- Originated >$550 million in tax credit investment
  - 2,300 affordable housing units
  - 50+ adaptive reuse of historic buildings

Mercantile
Community Partners

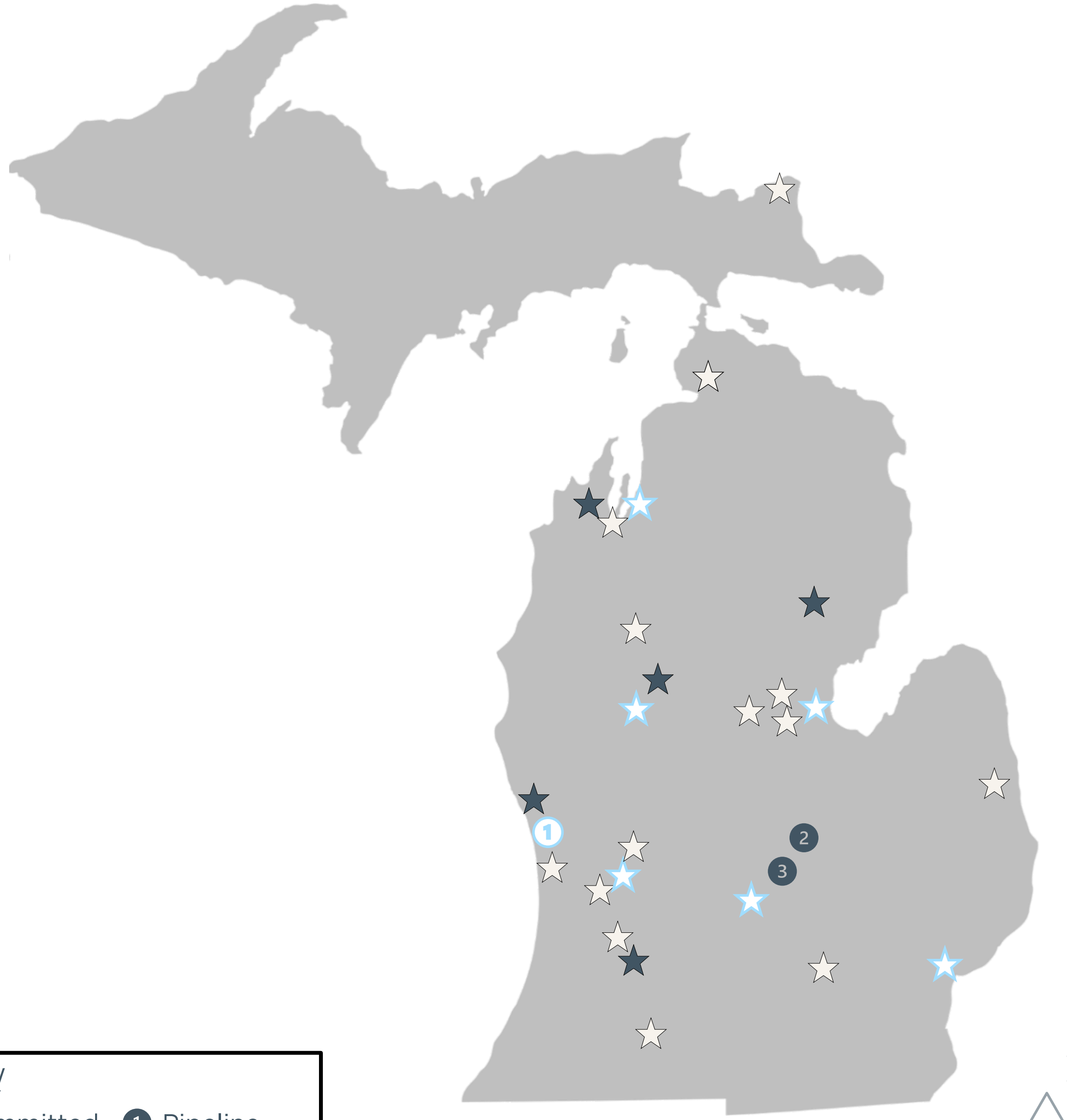
26 Projects - $157 Million Tax Credits

750+ Affordable Housing Units

Support of 150k+ SF. in Historic Rehabilitations

Exposure to 24 Counties Across the State

- ☆ *Landing at Spring Lake – Spring Lake, MI*
- ☆ ***Lexington School – Grand Rapids, MI***
- ☆ *Parkview – Traverse City, MI*
- ☆ ***Walter French Commercial – Lansing, MI***
- ☆ ***Annex Building – Sault Ste. Marie, MI***
- ☆ *Elmdale – Grand Rapids, MI*
- ☆ *Whisper Pines I – Pinconning, MI*
- ☆ *Mill Pond – Brooklyn, MI*
- ☆ *Westbury – Wayland, MI*
- ☆ *Village North II – Gladwin, MI*
- ☆ *Villa Esperanza – Wyoming, MI*
- ☆ ***Bonstelle Theatre – Detroit, MI***
- ☆ *Woodbrook – Three Rivers, MI*
- ☆ *Clarendon Glen – Clare, MI*
- ☆ *Rivercrest – Croswell, MI*
- ☆ ***Odd Fellows – Midland, MI***
- ☆ ***Leo's Building – Petoskey, MI***
- ☆ ***Cooley School – Cadillac, MI***
- ★ *Orchardview – Traverse City, MI*
- ★ *Flats on Bridge – Elk Rapids, MI*
- ★ *Kalrecovery – Kalamazoo, MI*
- ★ *West Shore – Whitehall, MI*
- ★ *Ryan Creek III – Big Rapids, MI*
- ★ *Southside I – West Branch, MI*
- ★ *South Main Flats – Evart, MI*
- 1 ***Froebel School - Muskegon, MI***
- 2 *Walnut Acres I & II - Corunna, MI*
- 3 ***Riverview - Owosso, MI***



Legend

☆ Closed Transactions ★ Committed 1 Pipeline

Tax Credits

- Dollar-for-dollar reduction in tax liability

  Taxable Income x Tax Rate = *Tax Liability*

  Income Tax Liability – Tax Credits = Tax Due

- Tax incentive designed to encourage certain types of investment to stimulate economic growth & promote policy goals (housing)

- Federal and State tax credits

- Monetized to generate capital for project financing

- Eligibility, application process, compliance period, structuring, economics, and many other factors vary depending on type of tax credit

Historic Tax Credits

National Stats	FY 2025	FY 1977- FY 2025
Private Investment	$8.64 billion	$135.76 billion
Rehab Housing Units	10,390	329,548
New Housing Units	11,544	377,293
Low- and Mod-Income Housing Units	11,582	216,892

Michigan Stats	FY 2025	FY 2021- 2025
Part 2 Approved Projects	21	73
Est. Qualified Rehab Expenditures (QREs)	$221 million	$1.3 billion
Est. Federal Tax Credits* **No reporting available for MI State HTC*	$40 million	$235 million

Data taken from the National Park Service's "Federal Tax Incentives for Rehabilitating Historic Buildings – Annual Report for Fiscal Year 2025"

Historic Tax Credits

HTC rehabs raised more in federal tax revenue ($52.9 billion) than it cost ($47 billion) in 2023 dollars

	FY2023 Historic Rehab Expenditures Resulted in:	Cumulative FY 1978-2023 Historic Rehab Expenditures Resulted in:
Jobs	162,000	3,326,000
Income	$7.0B	$195.7B
Output	$18.5B	$532.1B
GDP	$9.4B	$265.9B
Total Taxes	$2.6B	$75.3B
Federal Taxes	$1.7B	$52.9B
State	$0.4B	$11.0B
Local	$0.5B	$11.4B

Data taken from the National Park Service's "Federal Tax Incentives for Rehabilitating Historic Buildings – Annual Report for Fiscal Year 2023"

Historic Tax Credits

Federal Historic Tax Credits (FHTC)

- Created in 1976 to promote urban & rural revitalization
- Program administered by National Park Service (NPS) and the State Historic Preservation Office (SHPO)

State Historic Tax Credit (State HTC)

- 38 states - Michigan's HTC reinstated in 2020

Eligibility Requirements:

1. NPS Part 1 - Building must be listed on the National Register of Historic Places or be certified as contributing to the significance of a "registered historic district"
2. NPS Part 2 - Rehab must be done in accordance with the Secretary of the Interior's Standards for Rehabilitation
3. Rehab must meet the "substantial rehabilitation test"
4. Building must be "income-producing" for at least 5 years (FHTC only)

Eligibility Requirements

3. Rehab must meet the “substantial rehabilitation test”

    Basic: Qualified costs must exceed pre-rehab value

    Technical: Qualified costs must exceed the building’s adjusted basis

    Acquisition price
    − Price of land
    + Previous building improvements
    − Depreciation taken
    = Adjusted Basis

4. Building must be “income-producing” for at least 5 years (FHTC only)

    Commercial, industrial, agricultural, rental residential or apartment use

    Federal credit cannot be used for private residence

    Non-profits ARE eligible

Qualified Rehabilitation Expenditures (QRE)

YES!

- Building envelope - Façade, roof, windows, doors, elevators, stairs, chimneys, fire escapes
- Building utilities - Air conditioning and heating systems, electrical, plumbing, gas, sprinkling systems
- Permanent interior improvements – demolition, walls, partitions, floors, ceilings, paneling, tiling, paint
- Construction period interest, taxes and carrying costs
- Architectural, engineering, and construction management costs
- Developer fee (must be deemed reasonable)

NO!

- Land and acquisition costs
- Site work – permanent fencing, parking lots, decks, landscaping, sidewalks
- Enlargement that expands total volume beyond original footprint - rooftop additions, new basement
- Personal property – Appliances, furniture window coverings, moveable cabinets, tacked carpeting
- Leasing expenses
- Permanent financing fees
- New building construction

Tax Credit Calculation

	Cost	QRE %	QRE
Acquisition	$ 150,000	0	$ -
Construction Costs	$ 3,000,000	90%	$2,700,000
Soft Costs	$ 1,000,000	90%	$ 900,000
Developer Fee	$ 250,000	90%	$ 225,000
Total Development Costs	**$ 4,400,000**	**87%**	**$3,825,000**

	FHTC	State HTC - MI
Tax Credit %	QRE x 20%	QRE x 25%
Tax Credit $	$765,000	$956,250
Maximum	None, but all related party costs MUST be deemed **reasonable**	Capped at $2 million (commercial) and $1 million (residential)
Claiming Credits	5-year delivery period, ratably, beginning in the year the building is placed into service	1-year delivery in the year SHPO issues a certificate of completed rehab, after NPS Part III Approval

Claiming Tax Credits

	FHTC	State HTC - MI
How	Allocated to Property Owners based on % share of profits	Allocated to Property Owners OR Assigned/Transferred/Sold
Who	Individuals* Corporations Partners of passthrough entity Estates and Trusts * *must be a real estate professional or have passive income*	Individuals Corporations Partners of passthrough entity Estates and Trusts
When	5 years, ratably after placed-in service 1 year carryback 20 years carryforward	1 year, after Tax Certificate issued 10 years carryforward Non-refundable

Recapture Risk

	FHTC	State HTC - MI
Amount Subject	5 - year credit reduced annually by 20%	1 year credit vests over a 5-year compliance period
Triggers	• Historic character is altered • Property is disposed or ceases to be "income-producing" • Change in partnership interest by more than 1/3 (sale, admission, foreclosure) • Casualty loss (flood, tornado, fire)	• Part 3 approval revocation, including destruction of building • Transfer of ownership of all or part of the building UNLESS the seller and SHPO enter into a written agreement providing assurance and title restriction requiring the property will remain historic for the 5-year compliance period

Syndication

	FHTC	State HTC - MI
Structure	Equity Partnership	Certificated / Transferrable
Proceeds	Capital contributed upon completion of milestones (Pay-in Schedule)	Sale of credits with issuance of Tax Certificate *Taxable income to seller
User	Investor	Purchaser
Pricing	$0.60 - $0.85	$0.85 - $0.93
Recapture Risk	Allocated along with the credits	Remains with seller

Qualified Rehab Exp. (QRE)	$	3,825,000
FHTC %		20%
Total FHTC	**$**	**765,000**
FHTC Investor %		99%
FHTC to Investor	**$**	**757,350**
Investment Rate	$	0.70
FHTC Equity Investment	**$**	**530,145**

QRE	$	3,825,000
State HTC %		25%
State HTC	**$**	**956,250**
Investment Rate	$	0.85
State HTC Proceeds	**$**	**812,813**

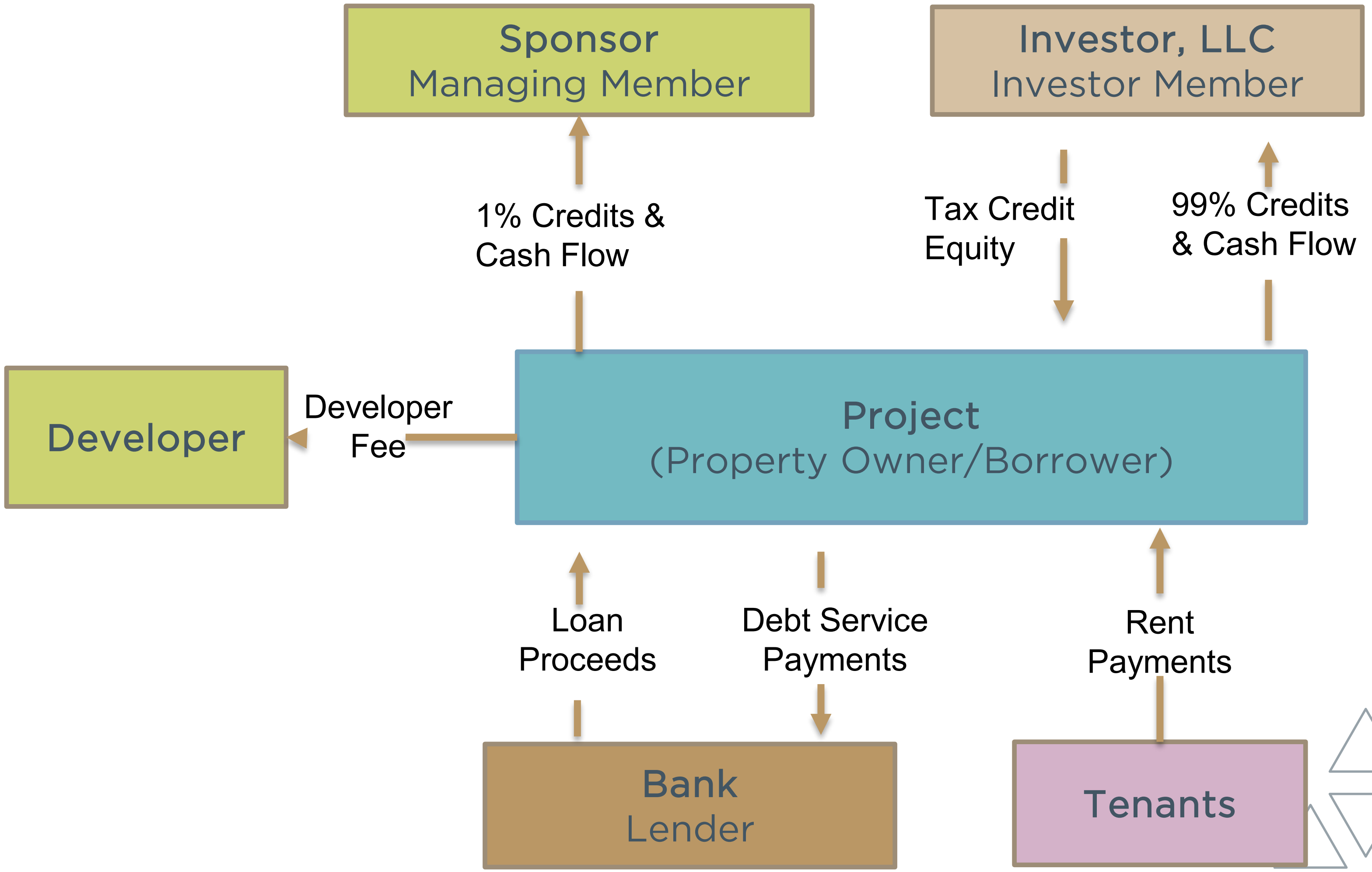
Syndication

Equity Pay-In Schedule				
Closing		132,536	25%	*Completion of real estate due diligence & operating agreement*
100% Completion		159,044	30%	
NPS Part 3 / Cost Certification		212,058	40%	*Certification of Completed Work*
Tax Return/K1		26,507	5%	
FHTC Equity Investment	**$**	**530,145**	**100%**	

	Construction		Permanent	
Owner's Equity	$ 657,042	15%	$ 657,042	15%
FHTC Equity	$ 132,536	3%	$ 530,145	12%
State HTC Proceeds	$ -	0%	$ 812,813	18%
HTC Bridge Loan	$ 1,210,422	28%	$ -	0%
Construction/Perm	$ 2,250,000	51%	$ 2,250,000	51%
Deferred Developer Fee	$ 150,000	3%	$ 150,000	3%
Total Sources	**$ 4,400,000**	**100%**	**$ 4,400,000**	**100%**

Syndication - Federal

- Structure: single entity or master tenant
- Investment Rate
- Equity Pay-in Schedule %
- Priority Return
- Asset Management Fees
- Tax Credit Adjusters
- Developer Fees
- Cash Flow and Tax Distributions
- Reserves & Contingencies
- Other real estate due diligence requirements



Syndication - Federal

Development Costs	**$ 15,000,000**	**$ 4,400,000**	**$ 1,000,000**
Qualified Rehab Exp. (QRE)	$ 13,500,000	$ 3,825,000	$ 900,000
FHTC %	20%	20%	20%
Total FHTC	**$ 2,700,000**	**$ 765,000**	**$ 180,000**
FHTC Investor %	99%	99%	99%
FHTC to Investor	**$ 2,673,000**	**$ 757,350**	**$ 178,200**
Investment Rate	$ 0.80	$ 0.70	$ 0.60
FHTC Equity Investment	**$ 2,138,400**	**$ 530,145**	**$ 106,920**
Investor Legal	$ (60,000)	$ (60,000)	$ (60,000)
Accounting	$ (10,000)	$ (10,000)	$ (10,000)
Investor Priority Return 2%	$ (213,840)	$ (53,015)	$ (10,692)
Put Option 5%	$ (106,920)	$ (26,507)	$ (5,346)
Net Benefit to Project	**$ 1,747,640**	**$ 380,623**	**$ 20,882**
Effective Investment Rate	*$ 0.65*	*$ 0.50*	*$ 0.12*

When to get MCP involved?

- Never too early!
- Can be too late (after C of O)
- Closing lead time ranges from 90 – 120+ days
- Most importantly…. a strong TEAM assembled
  - ❑ Sponsor / Developer / Guarantor
  - ❑ Historic Consultant
  - ❑ Environmental Consultant
  - ❑ General Contractor
  - ❑ Architect
  - ❑ Attorney
  - ❑ Accountant
  - ❑ Investor
  - ❑ Lender
  - ❑ Title Company
  - ❑ Insurance

Underwriting Info Needed

- ❑Proforma
  - Source/use, unit mix, cash flow
- ❑Construction
  - Budget, schedule, plans & specs
  - GC resume/experience and financial statements
  - Architect resume/experience
- ❑Property Management
  - Resume/experience, # units under management
- ❑Developer/Guarantor
  - Personal/corporate financial statements and tax returns
  - Global real estate schedule & contingent liabilities
- ❑Project Organizational Chart
- ❑Development team members
- ❑Market study and/or appraisal
- ❑Term sheets from financing sources
- ❑FHTC: Part 1 and Part 2 approvals
- ❑Environmental reports
- ❑Incentives Documentation
  - Tax abatement, PILOT, grants, OPRA, etc.

Lessons Learned

- Set realistic (conservative) timing expectations
- Understand that "issues" will arise during the closing due diligence process, and take the issues with stride
- Historic rehabs involving tax credits and incentives will be more involved than a new build
- Get to know your potential tax credit investor – we are a partner.
- If your lender and investor are not a related entity, introduce the parties as soon as possible

Types of Financing Incentives

- Tax Credits
- Grants – no repayment, taxable income
- Long-term and/or forgivable loans
- Tax Increment Financing (TIF)
  - Captures portion of increased property taxes and reimbursed over time
- Property Tax Abatement
  - Payment in Lieu of Taxes (PILOT)
  - Obsolete Property Rehabilitation Act (OPRA)
  - Neighborhood Enterprise Zones (NEZ)
- Michigan Economic Development Corporation (MEDC)
- Michigan State Housing Development Authority (MSHDA)

Annex Building

Sault Ste. Marie, MI

Project Overview

Rehab of the Sault Polyclinic Building into 11 affordable apartment units.

Total Development Cost	$4,200,000
Permanent Loan	$800,000
Owner's Equity	$643,000
MSHDA Missing Middle Grant	$869,000
MEDC CRP Grant	$1,363,000
DDA Funds	$10,000
FHTC Equity	$515,000

FHTC Calc	
QRE	$3,430,000
Tax Credit %	20%
Total FHTC	$686,000
Investment Rate	$0.75

Bonstelle Theater

Detroit, MI

Project Overview

Redevelopment of Temple Beth El into an event and performance space.

Total Development Cost	$9,000,000
State of Michigan Grant	$5,000,000
Owner's Equity	$2,784,000
FHTC Equity	$1,216,600

FHTC Calc	
QRE	$7,700,000
Tax Credit %	20%
Total FHTC	$1,540,000
Investment Rate	$0.79

Walter French Building

Lansing, MI

Project Overview

Phase 2 of the historic rehabilitation of former school building into a mixed-use office and childcare center.

Total Development Cost	$10,000,000
Permanent Loan	$700,000
Owner’s Equity	$612,000
State LEO Grant	$2,500,000
MEDC RAP Funds	$5,000,000
FHTC Equity	$1,188,000

FHTC Calc	
QRE	$8,250,000
Tax Credit %	20%
Total FHTC	$1,650,000
Investment Rate	$0.72

Oddfellows Building

Midland, MI

Project Overview

Redevelopment of historic building formerly used as a hotel, retail and office space, and lodging for members of the Oddfellows Professional fraternity into a mixed-use development with three retail spaces and five market-rate apartment units.

Total Development Cost	$4,200,000
Permanent Loan	$1,000,000
Owner's Equity	$1,285,000
MEDC RAP Grant	$1,400,000
FHTC Equity	$515,000

FHTC Calc	
QRE	$3,575,000
Tax Credit %	20%
Total FHTC	$715,000
Investment Rate	$0.72

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