MEMORANDUM

TO: Members of the Authority

FROM: Tim Sullivan
Chief Executive Officer

DATE: February 9, 2022

SUBJECT: Proposed New Rules for the
Historic Property Reinvestment Program (N.J.A.C. 19:31-26)

Request

The Members are asked to approve:

1. The attached proposed new rules for the new Historic Property Reinvestment Program and to authorize staff to (a) submit the proposed program rules for promulgation in the New Jersey Register and (b) submit the proposed program rules as final adopted rules for promulgation in the New Jersey Register if no formal comments are received; subject to final review and approval by the Office of the Attorney General and the Office of Administrative Law;

2. Delegation to Authority staff (Chief Community Development Officer, Managing Director – Community Development, or Director of Historic Preservation) to establish a date/s for the availability of the application and the date/s by when applications must be submitted on an annual basis; and

3. The creation of the Historic Property Reinvestment Program, as initially authorized by the New Jersey Economic Recovery Act of 2020 (Sections 2 through 8 of P.L. 2020, c. 156 and later amended by Sections 1 through 4 of P.L. 2021 c.160), to incentivize rehabilitation of identified historic properties in New Jersey by providing tax credits in an amount based on a percentage of the project's eligible costs, subject to final adopted rules.

New Jersey Economic Recovery Act

On January 7, 2021, Governor Phil Murphy signed the New Jersey Economic Recovery Act of 2020, P.L. 2020, c.156 (ERA) into law. The ERA presents a strong recovery and reform package that will address the ongoing economic impacts of the COVID-19 pandemic and position New Jersey to build a stronger and fairer economy that invests in innovation, in our communities, and in our small businesses the right way, with the protections and oversight taxpayers deserve. Tax incentives and other investment tools are critical to economic development, and when used correctly they can drive transformative change that uplifts communities and creates new opportunities for everyone.

The ERA includes 15+ economic development programs, including:

- Tax credits to incentivize job creation and capital investment;
- Investment tools to support and strengthen New Jersey's innovation economy;
- Tax credits to strengthen New Jersey's communities including revitalization of brownfields and preservation of historic properties;
- Financial resources for small businesses, including those impacted by the COVID-19 pandemic;
- Support for new supermarkets and healthy food retailers in food desert communities;
- Additional tax credits for film and digital media.

On July 7, 2021, Governor Murphy signed P.L. 2021 c.160 amending P.L. 2020, c.156 and further improving the programs established under the ERA.

The program being presented for the Members' approval in this memorandum is the Historic Property Reinvestment Program – one of the 15+ programs under the ERA. The Historic Property Reinvestment Program (HPRP) is a tax credit program designed to work in conjunction with the Federal Historic Tax Credit Program to encourage and bolster smart growth investments focused on the rehabilitation of existing identified historic structures throughout New Jersey.

This memorandum provides a summary about the HPRP including program limits, eligibility criteria, specific program requirements, application process, and general details about the program. The specific details – and what will be promulgated and will govern the program – are included in the attached rules proposed for Board approval.

Program Purpose and General Description

The HPRP focuses on historic preservation as a component of community development, encouraging long-term private investment into the State while preserving properties that are of historic significance. The program can be used to leverage the federal Historic Tax Credit program to incentivize rehabilitation of identified historic properties. The amount of tax credits a rehabilitation project receives is a percentage of the project's eligible costs, subject to a statutory cap determined by whether the project includes a qualified property or a transformative property and on project location. The overview provided here highlights key aspects of the program. Additional program details are included in the sections below, and full program details are contained in the draft rules (attached) and the statute.

To be eligible for the HPRP, a project must meet various eligibility criteria at the time of application. For example, a project must:

- Demonstrate at time of application that without the tax credit, the rehabilitation project is not economically feasible.
- Prove that a project financing gap exists, and the tax credit award being considered for the project is equal to or less than the project financing gap.
- Have not commenced any construction or rehabilitation activity at the site of the rehabilitation project prior to submitting an application and will not commence any construction or rehabilitation activity until the execution of the Rehabilitation Agreement (with certain limited exceptions).
- Include business entity contributed equity of at least 20 percent of the Total Cost of Rehabilitation, or if located in a government-restricted municipality, the equity shall be at least 10 percent of the Total Cost of Rehabilitation.
- Meet minimum cost requirements where the cost of rehabilitation for the selected rehabilitation period shall not be less than the greater of the adjusted basis of the structure or $5,000.
- For a residential project, the structure must serve a residential rental purpose and also contain at least four dwelling units.
- For a residential project or a redevelopment project consisting of newly-constructed residential units, at least 20 percent of the residential units constructed shall be reserved for occupancy by low- and moderate-income households with affordability controls as required under the "Fair Housing Act."
- Include the rehabilitation of a qualified property, or transformative property.

Projects under the HPRP are subject to an annual program cap of $50 million for a total of $300 million for a period of six years. Annual unused amounts may be included in the amounts available for approval in the subsequent year.

The HPRP is a competitive program, under which projects must apply within a defined application window, with all applications to be considered following the closure of the application period. The Authority, on an annual basis, will establish a date for the availability of the application and a date by when applications must be submitted. The Authority may establish separate dates for transformative projects and for all other rehabilitation projects.

Applicants can utilize the program to receive tax credits to rehabilitate only "qualified" or "transformative" properties. "Qualified property" means a property located in the State of New Jersey that is an income producing property, and that is:

- Individually listed, or located in a district listed on the National Register of Historic Places, the New Jersey Register of Historic Places, or designated by the Pinelands Commission; or

- Individually identified or registered, or located in a district composed of properties or structures and such district is identified or registered, for protection as significant historic resources in accordance with criteria established by a municipality in which the property, structure or district is located if the criteria for identification or registration has been approved by the officer as suitable for substantially achieving the purpose of preserving and rehabilitating buildings of historic significance within the jurisdiction of the municipality. If located within a district, the property must be certified by the Officer as contributing to the historic significance of the district.

A “transformative property” means a property that is:

- An income producing property, not including residential, whose rehabilitation the Authority determines will generate substantial increase in State revenues through the creation of increased business activity within the surrounding areas.
- Individually listed on the New Jersey Register of Historic Places.
- Received a Determination of Eligibility from the Keeper of the National Register of Historic Places.
- Located within a one-half mile radius of the center point of a transit village, as designated by the NJDOT and within a city of the first class, OR located within a government restricted municipality.

The Historic Property Rehabilitation program awards are calculated based on a percentage of the cost of rehabilitation (eligible costs), with actual percentages dependent on the type of property (e.g., whether it is a qualified property or a transformative property) and on location of the project. Most eligible projects can receive tax credits worth up to 40% of eligible costs up to a project cap of $4 million for qualified properties. Eligible projects located within a qualified incentive tract or in government-restricted municipalities can receive tax credits worth up to 45% of eligible project costs up to a project cap of $8 million for qualified properties. Transformative projects can receive tax credits worth up to 45% of eligible project costs up to a project cap of $50 million. Awards are scored on a competitive basis.

In addition to meeting the program eligibility, the business entity and any co-applicant must be in substantial good standing with the NJ Department of Labor and Workforce Development, the NJ Department of Environmental Protection, and the Department of Treasury (as determined by each Department). If a compliance issue exists, the eligible developer or co-applicant may have an agreement with the respective Department that includes a practical corrective action plan, as applicable. The eligible business entity and any co-applicant must have no unpaid liability in excess of any threshold dollar amount(s) that may be established by each respective Department. Furthermore, the business entity will be required to provide, prior to execution of a grant agreement, a valid tax clearance certificate from the NJ Division of Taxation within the NJ Department of Treasury.

The HPRP rules also require that the rehabilitation project pay prevailing wages for construction work during the duration of the project and to building service workers for a period of 10 years following project completion for single phase project, or 10 years following the completion of the first phase for multiphase rehabilitation projects.

Some of the areas described above are outlined in greater detail further in this memorandum and in the attached rule proposal.

Eligibility Criteria

The following highlights key eligibility requirements for the Historic Property Reinvestment Program. Full eligibility details are contained in the draft proposed rules in section N.J.A.C. 19:31-26.3, based on Section 4 of the ERA (P.L. 2020, c.156, amended by Section 2 of P.L. 2021 c.160). To be eligible, a project must meet the definition of a rehabilitation project and meet various eligibility criteria at application, which the Board ascertains when the project is presented to the Board, and at project completion, when the developer must submit certifications evidencing satisfaction of Program requirements and conditions.

Rehabilitation Project

A specific construction project or improvement or phase of a project or improvement undertaken by a business entity that includes the rehabilitation of a qualified property, or transformative property.

Economic Feasibility

The business entity must demonstrate at time of application that without the tax credit, the rehabilitation project is not economically feasible. Financial information of the rehabilitation project must include all phases, including, but not limited to, any State or local financial assistance for the project, proposed terms of financing, projected reasonable and appropriate return on investment based on the business entity's equity, net margin, and cash on cash yield, and a certification from the chief executive officer or equivalent officer of the business entity that additional capital cannot be raised from other sources on a non-recourse basis after making all good faith efforts to raise additional capital, and any other documentation demonstrating economic and commercial viability.

Project Financing Gap

Given that the HPRP is intended to incentivize rehabilitation projects that would not be possible without the HPRP tax credits, the statute requires that a project must demonstrate the existence of a project financing gap in order to be eligible for tax credits under this Historic Property Reinvestment Program.

This means that the project must demonstrate that there is part of the total cost of rehabilitation, including reasonable and appropriate return on investment, that remains to be financed after all other sources of capital have been accounted for. Total cost of rehabilitation is used to evaluate the return and is based upon all costs incurred by the business entity prior to completing the project, versus eligible costs as defined in the rules, which includes softs costs associated with the rehabilitation project, but excludes costs not directly connected with the rehabilitation of the qualified or transformative property such as any costs associated with an increase in total building volume.

The project financing gap analysis shall include, but not be limited to, an evaluation of the total cost of rehabilitation, amount of capital sufficient to complete the rehabilitation project, proposed rental rates, vacancy rates, reasonable and appropriate return on investment, and, in the Authority's sole discretion, a comparison to alternative financing structures for a comparable project available to the developer or its tenants. Additionally, the business entity shall demonstrate that the rehabilitation project has equity of at least 20 percent of the total cost of rehabilitation, except that if a rehabilitation project is located in a government-restricted municipality, the equity shall be at least 10 percent of the total cost of rehabilitation.

Further information regarding the gap analysis can be found in N.J.A.C. 19:31-26.3(c).

Commencement of Construction

Pursuant to the statute, and excepting situations described in this section, projects applying for assistance under the HPRP must not have commenced any construction or rehabilitation activity at the site of the rehabilitation project prior to submitting an application, and cannot commence any construction or rehabilitation activity until the execution of the rehabilitation agreement except as follows:

- If the business entity has been ordered by a building code or other official with jurisdiction over the site or the rehabilitation project to correct a health, safety, or other hazard if:
    - The business entity provides a copy of the order to the Authority;
    - The business entity documents to the Authority's satisfaction that the proposed construction or rehabilitation activity is limited to resolve the hazard; and
    - The proposed construction or rehabilitation activity complies with the Secretary of the Interior's Standards for Rehabilitation, 36 C.F.R. § 67.7, and as described by the National Park Service at: https://www.nps.gov/tps/standards/rehabilitation.htm.

- Any construction or rehabilitation activity at the site of the rehabilitation project was conducted by an entity that is not the current owner or business entity, or an affiliate of the current owner or business entity, and was not done at the direction of or under contract with the owner, business entity, or an affiliate of the owner or business entity.

Project Equity

Business entity contributed capital may consist of cash, deferred development fees, costs for project feasibility incurred within the 12 months prior to application, property or site value less any mortgages when the business entity owns the project site, and any other investment by the business entity in the project deemed acceptable by the Authority. Property or site value will be valued at the lesser of: the purchase price, provided the property or site was purchased pursuant to an arm's length transaction within 12 months of application; or the value as determined by a current appraisal acceptable to the Authority. Equity shall include Federal or local grants and proceeds from the sale of Federal or local tax credits, including, but not limited to, the Historic Rehabilitation Tax Credit, Low-Income Housing Credit, and New Market Tax Credit. Equity does not include State grants or tax credits or proceeds from redevelopment area bonds. For a residential project utilizing Low-Income Housing Tax Credits awarded by the New Jersey Housing and Mortgage Financing Agency, equity includes the portion of the developer's fee that is deferred for a minimum of five years.

Minimum Cost

Pursuant to the statute, the cost of rehabilitation during a business entity's selected rehabilitation period cannot be less than the greater of the adjusted basis of the structure of the qualified property or transformative property used for federal income tax purposes as of the beginning of the business entity's selected rehabilitation period, or $5,000.

Project Scoring

The Authority has established scoring criteria for the evaluation of proposed rehabilitation projects. These criteria can be used to set a minimum acceptable score for reviewed rehabilitation projects or to allocate tax credits in circumstances where the requests for tax credits exceeds the annual maximum cap established by the statute.

Based on the statute imposed annual cap for the HPRP, as well as data reviewed from other states with historic tax credits programs, and information on applicants to the federal historic tax credit program for New Jersey projects, staff anticipate that there is a possibility for the program to be oversubscribed. As a result, staff is recommending the utilization of preestablished scoring criteria as a means to competitively rank or compare projects. If the volume of HPRP tax credit award requests is less than currently anticipated, resulting in the program to be undersubscribed for any particular year, a minimum score approach to assess whether a proposed rehabilitation project is consistent with the objectives, goals and principles of the HPRP will be utilized.

Please refer to Appendix B for the "Historic Property Reinvestment Program Scoring Criteria" for the specific proposed criteria, and further clarification on each of the different aspects the Authority will consider in its scoring evaluation of proposed rehabilitation projects.

Post-Approval Process

After the Board has voted to approve their rehabilitation project, the business entity must sign an approval letter and subsequently a rehabilitation agreement with the terms and conditions to receive the tax credit. Upon completion of the rehabilitation project, the business entity must submit satisfactory evidence of the completion of the rehabilitation project and satisfaction of the program eligibility requirements. The rehabilitation project must demonstrate compliance with eligibility criteria including affirmative action, prevailing wage and substantial compliance with the Secretary of the Interior's Standards for Rehabilitation. The business entity must also provide certification by the architect or design consultant of record that all work was completed in accordance with the construction documents in the rehabilitation agreement.

There are several scenarios where a tax credit award may be reduced or recaptured. These include, but are not limited to, the following, where applicable:

- If during the compliance period, a business entity that has received a tax credit modifies the qualified property or transformative property so that it ceases to meet the requirements for the rehabilitation of a qualified property or transformative property as defined under the program or ceases to meet the requirements of the rehabilitation agreement. The requirements include, but are not limited to:

  - Substantial compliance with the Secretary of the Interior's Standards for Rehabilitation;
  - Remaining an income producing property;
  - Minimum number of residential units, if applicable;
  - Maintaining the rehabilitation project so that it meets the minimum score; and
  - For a transformative project, continuing to meet the definition of transformative property;

- If during the compliance period, the business entity ceases to maintain adequate climate control or fails to preserve the building envelope;

- Non-compliance with affirmative action or prevailing wage requirement; or

- A material misrepresentation on the applicant's application, project completion certification, annual report, or any related submissions. In this case, the rules also state that the Authority may recapture any and all tax credits.

Further information regarding reduction and recapture of tax credits under the HPRP can be found in N.J.A.C. 19:31-26.13.

Rulemaking Process

The ERA authorizes the Authority to promulgate rules for the Historic Property Reinvestment Program, which will include a 60-day public comment process pursuant to the Administrative Procedure Act's rulemaking procedures. Any approvals while rules are proposed will be subject to the rules as finally adopted.

Compliance with Executive Order 63

In accordance with the Executive Order 63 directive to ensure outreach efforts are made to the public and affected stakeholders for agency rulemaking, the Authority issued a news release advising the public that the draft Historic Property Reinvestment Program rules were available for review and of the opportunity to provide informal input.

The Authority staff convened two virtual public "Listening Sessions", which provided an overview of the Historic Property Reinvestment Program draft rules and the opportunity for the public feedback, on:

- Friday, December 17th, 2021 at 11:00 a.m.
- Monday, December 20th, 2021 at 11:30 a.m.

Additionally, the public were able to submit written feedback through the NJEDA's Economic Recovery Act transparency website (www.njeda.com/economicrecoveryact) or through the newly established email account (HistoricTaxCredit@njeda.com) from December 9th through December 23th 2021.

Chief Compliance Officer Certification of Draft Rule Proposal

Pursuant to Section 101(a) of the ERA, the Chief Executive Officer is required to appoint a Chief Compliance Officer (CCO) to, among other things, "review and certify that the provisions of program rules or regulations provide the authority with adequate procedures to pursue the recapture of the value of an economic development incentive in the case of substantial noncompliance, fraud, or abuse by the economic development incentive recipient, and that program rules and regulations are sufficient to ensure against economic development incentive fraud, waste, and abuse."

Bruce Ciallella has been designated the CCO. In that capacity, Mr. Ciallella has reviewed the proposed rules and regulations for the Historic Property Reinvestment Program and is prepared to sign the certification, subject to the Board taking action to approve the same for submission to the New Jersey Office of Administrative Law for publication in an upcoming issue of the New Jersey Register.

Fees

The fee structure as outlined below is also included in the proposed new rules. Prior to establishing the proposed fee structure for this program as outlined in the proposed new rules, Authority staff conducted an internal review to estimate the likely administrative costs to the Authority to administer the Historic Property Reinvestment Program. This review considered areas cross-organizationally where the Historic Property Reinvestment Program may require staff time, and the estimated percentage of staff time that would be required.

Fees are determined on a tiered basis based on a project's eligible costs, with a separate tier for transformative projects, as project cost and type is a reasonable proxy for the complexity of a project and, therefore, the administrative expense to the Authority in the form of staff time required to evaluate the application. The relevant tiers, in addition to the separate tier for transformative projects, include projects with eligible costs under $10 million and those with eligible costs over $10 million. In addition to the established tiers, there will also be a reduced agreement fee for projects that have applied for Federal Historic Preservation Tax Credits and who have received prior approval of Part 1 and 2 of the federal program's application from DEP's Historic Preservation Office (HPO). Prior approval of Parts 1 and 2 of the federal program will eliminate the need for a detailed review by the Authority for substantial compliance with the Secretary of the Interior's Standards for Rehabilitation, and will therefore significantly reduce Authority's staff time needed to complete the necessary review prior to execution of the rehabilitation agreement.

An applicant for the Historic Property Reinvestment Program will be responsible for a one-time, non-refundable application fee. This fee will be $2,000 for a project with eligible costs of $10 million or less, $7,000 for a project with eligible costs of more than $10 million, and $18,000 for a transformative project.

Additionally, prior to the approval of a tax credit award by the Board, the business entity will be responsible for a one-time approval fee, which may be refunded if the project is not approved for a tax credit award. This fee will be $5,000 for a project with eligible costs of $10 million or less, $14,000 for a project with eligible costs of rehabilitation of more than $10 million, and $125,000 for a transformative project.

Prior to the execution of a rehabilitation agreement, the business entity will be responsible for an agreement fee. For projects with eligible costs under $10 million, the fee shall be $10,000, however if the business entity is applying for a Federal Historic Preservation Tax Credit and has received prior approval of applications from the HPO under Parts 1 and 2 of the Historic Preservation Certification Application the fee shall then be $5,000; for projects with eligible costs of over $10 million, the feel shall be $28,000, however if the business entity is applying for a Federal Historic Preservation Tax Credit and has received prior approval of applications from the HPO under Parts 1 and 2 of the Historic Preservation Certification Application the fee shall then be $14,000. For a transformative project, the agreement fee shall be $250,000 unless the business entity is applying for a Federal Historic Preservation Tax Credit and has received prior approval of applications from the HPO under Parts 1 and 2 of the Historic Preservation Certification Application, in such a case the fee shall be $125,000.

Prior to the receipt of a tax credit certificate, the business entity will be responsible for a certification fee which will be $5,000 for a project with eligible costs of $10 million or less, $14,000 for a project with eligible costs of more than $10 million, and $125,000 for a transformative project. For a rehabilitation project with a selected rehabilitation period of 60 months, the business entity will be responsible to pay an additional non-refundable fee prior to the approval of the project cost certification for the second phase and each subsequent phase.

Additionally, the developer may be responsible for a modification fee should the project require modifications. For a modification subject to Board approval that fee shall be $5,000 for a project with eligible costs of $10 million or less, $10,000 for a project with eligible costs of more than $10 million, and $125,000 for a transformative project. For any administrative changes, additions, or modifications the fee shall be $2,500 for a project with eligible costs of $10 million or less, $5,000 for a project with eligible costs of more than $10 million, and $50,000 for a transformative project.

If the developer elects to sell the tax credit, a transfer fee will also apply. That fee for each transfer shall be $10,000 for a project with eligible costs of $10 million or less, $14,000 for a project with eligible costs of more than $10 million, and $125,000 for a transformative project.

If a business entity requests an extension to the date by which the business entity shall submit the certification with respect to the capital investment, employment, and other eligibility requirements of the program, a non-refundable extension fee will apply.

Finally, a business entity seeking to terminate an existing rehabilitation agreement will be responsible for a termination fee.

Further information regarding program fees under the HPRP can be found in N.J.A.C. 19:31-26.5

<u>Reports on Implementation of Program</u>

On or before December 31, 2025, staff, in consultation with the HPO and the Treasury Department's Office of Taxation, will prepare a report that will include program data regarding the effectiveness of the tax credits provided in promoting the rehabilitation of historic properties. The report will include data such as: the number and total monetary amount of tax credits granted for the rehabilitation of qualified properties or transformative properties, the geographical distribution of the credits granted, a summary of the tax credit transfer, as well as recommendations for any administrative or legislative changes to increase the effectiveness of the program. As required by the statute, the report will be submitted to the Governor and the Legislature.

Recommendation

The Members are asked to approve:

1. The attached proposed new rules for the new Historic Property Reinvestment Program and to authorize staff to (a) submit the proposed program rules for promulgation in the New Jersey Register and (b) submit the proposed program rules as final adopted rules for promulgation in the New Jersey Register if no formal comments are received; subject to final review and approval by the Office of the Attorney General and the Office of Administrative Law;

2. Delegation to Authority staff (Chief Community Development Officer, Managing Director – Community Development, or Director of Historic Preservation) to establish a date/s for the availability of the application and the date/s by when applications must be submitted on an annual basis; and

3. The creation of the Historic Property Reinvestment Program, a tax credit program as initially authorized by the New Jersey Economic Recovery Act of 2020 (Sections 2 through 8 of P.L. 2020, c. 156 and later amended by Sections 1 through 4 of P.L. 2021 c.160), to encourage and bolster smart growth investments focused in the rehabilitation of existing identified historic structures by providing tax credits in an amount based on a percentage of the cost of rehabilitation (eligible costs), subject to final adopted rules.

Tim Sullivan
Chief Executive Officer

Prepared by**:** C. Aidita Milsted

Attachments:
Appendix A – Proposed New Rules – Historic Property Reinvestment Program
Appendix B – Historic Property Reinvestment Program Scoring Criteria
Appendix C – Reasonable and Appropriate Return on Investment