

Hundreds of structures across North Carolina (NC) tell the ever-evolving history of the state, and nowhere is this reflected better than in the hundreds of mill structures still standing throughout the state. Until the mid-1990s, NC's economy was dominated by agriculture and textiles. Since then, hundreds of mills and warehouses across the state have closed and/or fallen into disrepair. Recently, many of these structures, and consequently their surroundings, have been rehabilitated for re-use. This paper will examine the factors that led to the closing of these structures, as well as the economic impact resulting from the rehabilitation and redevelopment of one famous project: the American Tobacco facilities in downtown Durham, NC. Much of the information provided within this paper – especially as it relates to American Tobacco – came from an interview with Michael Goodman and several conversations with Jonathan Cowan, both of whom work for American Tobacco-developer Capitol Broadcasting Corporation – Real Estate.

NC Economic Environment (1997-2005)

Between 1997 and 2005, both the rising value of the US dollar as well as the industrial development in the third-world left many American manufacturers uncompetitive in the global marketplace, forcing hundreds to close or move overseas. During this period, between 215 and 250 textile plants closed, resulting in the loss of 175,000 -200,000 manufacturing jobs.¹² The impact of this shift in economic realities was especially strong in NC with its rich agricultural history. Today, NC has hundreds of mills and agricultural facilities which remain vacant.³ According to information provided by Capitol Broadcasting Corporation, NC alone experienced 170 mill closings during this same period, accounting for a loss of almost 40,000 jobs.

The mill closings have had a significant detrimental impact to the economies of smaller towns across the state for several reasons. From the first NC mill construction in 1815⁴ and beyond, many of these mills shaped the development of small towns. Mills were typically constructed in areas with railroad access, and became some of the first examples of urban migration in the state. As such, many towns and cities around the state developed around these mills, which upon closing, left an aesthetic eyesore and an economic void in the middle of central business districts. In many NC towns, textile mills or tobacco warehouses were the most prominent employers, and after closing, left many towns facing significant emigration – as a direct result of manufacturing employment loss as well as peripheral losses from outside services. A Robeson County, NC case study showed that for every manufacturing job loss there were an additional 1.1x in ripple effect job losses, many of which were often higher paying (and thus higher revenue generating) jobs.⁵

For instance, if we assume that the average employee was compensated at the NC median household income level of \$40,863⁶ the loss of 39,505 NC manufacturing jobs represents a loss of over \$1.6 billion in direct compensation to employees. By factoring in the ripple effects of these job losses, total economic contraction of approximately \$3.4 billion, significantly affecting local municipalities and businesses.

¹ *Kannapolis, NC – How One Community Accepts Globalization*. **Market Wire**. July, 2004.

(http://findarticles.com/p/articles/mi_pwwi/is_200407/ai_n8555542)

² *Letter to President Bush Regarding Strong Dollar*. National Cotton Council of America. May 26, 2005.

(<http://www.cotton.org/issues/2002/strong-dollar.cfm>)

³ *Conversation with Jonathan Cowan, Capitol Broadcasting Corporation – Real Estate*

⁴ North Carolina Business History – Textiles. <http://www.historync.org/textiles.htm>

⁵ *The Economic and Social Impact of Job Loss in Robeson County, NC 1993-2003*. **Sociation Today**. Fall 2004.

(<http://www.ncsociology.org/hossfeld.htm>)

⁶ 2000 US Census Data. (<http://census.gov>)

Legislative Change

To help lessen the sting of manufacturing job losses, in 2006, the NC General Assembly passed House Bill 474 which provided up to a 40% tax credit for qualified expenses related to the revitalization of historic mill facilities.⁷ Although the law would help to preserve the structures which capture NC's industrial history, the primary reason for its passing was to spur economic development in blighted areas.

The legislation allowed for developers to receive up to a 40% tax credit towards qualified rehabilitation expenses for the rehabilitation of manufacturing facilities and ancillary buildings. The most attractive element of this law stipulated that the mill rehabilitation tax credit was additive to the 20% federal tax credit, with minimal additional paperwork and bureaucracy. In addition, the owner of the tax credit could apply the entire amount towards income in one year as opposed to spread equally across five years with the federal credit. This stipulation expanded the potential pool of investors for these tax credits to corporations that would have enough taxable income for the one year shield and enabled the developers of the projects to receive better terms during the syndication process. The total impact of this change was groundbreaking for the preservation and rehabilitation of historic structures. With more money available to them and better economic terms, developers were incentivized to undertake projects which would were unthinkable before the legislation.

To qualify for this credit, the site has to exhibit several characteristics. In addition to the manufacturing and ancillary building stipulation, the structure has to be certified historic and 80% vacant for at least 2 years. Qualified rehabilitation expenses must exceed \$3 million and the structure must have continuous ownership for five years after completion. Each of these poses some limitations on the ability to use tax credits. Of the estimated 750 – 900 vacant manufacturing structures in NC, approximately 300 would currently be eligible for the mill rehabilitation tax credit.⁸

Economic Impact

Obviously, legislation alone will not create value and spur economic development and activity in towns blighted by closed manufacturing facilities. To be viable, a rehabilitation project must have tenants, residents, and /or customers for a sustained period of time after the rehabilitation is complete. In essence, no project can be considered successful unless the positive economic impacts have a lasting effect.

Across the state, these former one-company towns have had to reinvent themselves to stem rising unemployment. Former mills and manufacturing facilities have found new lives with a variety of new and entrepreneurial uses – from civic facilities, such as schools, museums, and municipal buildings, to private businesses such as high-tech business incubators, sawmills, and agricultural facilities.⁹

The economic impact from all this investment takes several forms. First, during the rehabilitation phase, construction jobs are created. Due to an often comparable skill set, former workers in these manufacturing facilities often fill these jobs. Second, and more importantly, the long term impact from the rehabilitation creates local businesses, which creates local jobs, and circulates capital through the local economy – both of which are desperately needed in towns devastated by the loss of manufacturing jobs. Much research has been done on this topic by members of the preservation community, and although the economic impact varies by geography, one prominent study found that for each \$1 million investment, almost twenty local

⁷ General Assembly of North Carolina, Session 2005. House Bill 474. Approved June 29, 2006.

⁸ Conversations with Myrick Howard and representatives of Capitol Broadcasting Corp. Real Estate.

⁹ *Old Mills Hum with New Uses*. **The Christian Science Monitor**. July 30, 2002
(<http://www.csmonitor.com/2002/0730/p02s01-usgn.html>)

jobs were created with many more out-of-state jobs created.¹⁰ Furthermore, because the US economy continues to shift from a manufacturing based to service based economy, many of these new jobs are better paying professional jobs.

In addition, the homegrown small businesses created to fill the void in these former one-company manufacturing towns have, nationally, experience the fastest growth of any business type. Because the cost of rehabilitation is cheaper than that of new construction, these businesses (all else equal) are able to pay less rent and are thus better able to survive and thrive.¹¹ The rent roll at the American Tobacco project is a testament to this, with dozens of start-up bioscience and technology firms sprinkled among professional firms and larger Fortune 500 firms.¹²

In addition to the direct economic impact are the positive psychological impacts to towns that have been devastated by manufacturing job losses. For instance, when American Tobacco closed its downtown Durham operations in 1987, much of the downtown economy left with it. Vacant store fronts littered a downtown with a stigma as a barren wasteland. With the American Tobacco campus rehabilitation, not only have high paying professional jobs relocated and sprung up in downtown Durham, but the facility draws thousands of visitors each year to the former blighted area for minor league baseball and outdoor concerts. This has not only increased tax revenues for the city, but the project has drawn enough mass to downtown to make other new development projects more viable.

Although I was unable to locate direct data on the job growth impact from historical mill and manufacturing facility rehabilitation, the following chart shows that in spite of labor force growth in NC and the large number of manufacturing closings during the past ten years, unemployment growth has trailed this significantly. This information points to job creation – a portion of which would come directly from mill rehabilitation. Without the mill tax credit spurring investment, much of this job creation would not have occurred.

Table 1: NC Labor & Unemployment Growth 1998-2007

| <u>Year</u> | <u>Labor Force Growth</u> | <u>Unemployment Growth</u> |
|-------------|---------------------------|----------------------------|
| 1998 | 49,853 | (17,256) |
| 1999 | 81,060 | 7,906 |
| 2000 | 56,237 | 41,124 |
| 2001 | 25,087 | 103,981 |
| 2002 | 45,007 | (6,983) |
| 2003 | 43,010 | (15,795) |
| 2004 | 37,579 | (30,386) |
| 2005 | 86,385 | (10,861) |
| 2006 | 132,377 | (6,406) |
| 2007 | <u>13,326</u> | <u>(1,368)</u> |
| | 569,921 | 63,956 |

¹⁰ Listokin, David, and Michael L. Lahr. "Economic Impacts of Preservation in New Jersey and Texas," Forum Journal (2000).

¹¹ "Historic Preservation as Economic Development." **The Economics of Historic Preservation.** Donovan Rypkema, 1994.

¹² (www.americantobaccohistoricdistrict.com)

American Tobacco Campus

Old Bull, constructed in 1874 at the corner of Blackwell and Vivian Streets, is the oldest of the remaining buildings comprising the present day American Tobacco Campus. This structure was imposing for its time – the first brick tobacco factory in the country – and much larger than any other structures in Durham. For the next 30 years, the American Tobacco Company expanded the factory and facilities, with increased manufacturing capacity, a power plant, large coal building, and hundreds of thousands of square feet in warehouse space. Most of the present day structures on the campus were constructed by 1910, as the American Tobacco Company grew into one of the largest companies in American. The history of the buildings and construction on site grew in direct correlation to the success of the company. The company expanded its facilities southward from the Old Bull factory as demand for tobacco products increased, constructing the Fowler, Strickland, and Crowe buildings in the 1930s, 1940s, and 1950s, respectively. When the company began moving operations out of Durham, many of the unutilized warehouses (on the site of the present day Durham Bulls Athletic Park) were demolished. The structures remaining on the campus today appear to be very similar to the build-out in 1965.

In 1987, American Tobacco relocated all remaining operations out of downtown Durham, effectively ending their 100 year presence there. After several failed attempts at redevelopment/rehabilitation of the site, Capitol Broadcasting Corporation (CBC) bought the site in 2002. From 2002 to 2004, CBC completed new office developments opposite the new baseball stadium. In addition, CBC began rehabilitation of the southern end of the campus, bringing office and restaurant users into the facility. For the initial phase of the project, CBC secured 20% federal historic rehabilitation tax credits for income-producing properties, as well as federal new markets tax credits, and incentives from the City of Durham. CBC worked with a renowned historical rehabilitation firm, Streuver Brothers, Eccles, and Rouse (SBER), on the northern-most second phase of the project. SBER secured federal historic rehabilitation tax credits to this project and utilized the newly-approved NC mill rehabilitation tax credit. The total project is comprised of 1.3 million square feet of office, retail, and residential uses – from both rehabilitation and new development of surrounding land parcels.¹³¹⁴

In total, downtown Durham has seen \$1.5 billion in the rehabilitation and investment of over 3 million square feet of historic real estate. All this investment, as a direct result of the historical tax credits, has pushed office rents in downtown Durham from an average of \$16 per square foot to almost \$25 per square foot. In addition, land values surround the project have almost doubled – from about \$550,000 to \$1.1 million per acre – since the American Tobacco rehabilitation occurred.¹⁵

According to CBC, none of this rehabilitation would be feasible without the combination of state and federal historic tax credits, as well as local incentives. In addition, although Durham was well-positioned in the heart of the Triangle, development challenges and demographics posed significant challenges to redevelopment and new construction of the site.

As a result of these tax credits spurring rehabilitation, Durham has seen, and will continue to see, tremendous economic growth. In the early 1990s, three in ten downtown office building floors were completely vacant. Today, the downtown district has experienced 90% occupancy at rental rates higher than ever imagined. The number of office employees in downtown Durham has grown threefold during this time to about 16,000 per day. In fact, Phase I alone added approximately 1,800 employees to the site, which is equivalent to the maximum employment of the American Tobacco Company during its operations there.¹⁶

¹³ “Blackwell’s Durham Tobacco / American Tobacco Co.” **Endangered Durham**. (www.endangereddurham.org)

¹⁴ Conversations with Jonathan Cowan, CBC

¹⁵ Kalette, Denise. “Durham Restores Old Warehouses.” **National Real Estate Investor**. January 1, 2008.

¹⁶ Jacobson, Louis. “Durham Converts Tobacco Sites, Revives Downtown.” **Planning**. November 2003.

Not only has this increased office investment, business development and growth in the city, but also new restaurants and retail shops have opened as well, further contributing to the vibrancy of the local economy. In addition, residential growth has grown rapidly, from approximately 800 individuals to over 3,000 by 2009. All this investment has increased City of Durham tax revenues significantly during this period, from locations that were formerly vacant blighted manufacturing facilities. In addition, even with the increased number of residents and workers in Durham, crime rates have decreased significantly, approximately 40% since many of the first rehabilitation projects came online.^{17,18}

According to the NC State Historic Preservation Office, two projects within the American Tobacco Campus utilized NC mill rehabilitation tax credits: the Hill Warehouse and the Lucky Strike Building. Durham County is considered an Enterprise III tier location, allowing qualified rehabilitation expenses to gain a 30% tax credit, which is 10% higher than the NC historic preservation tax credit for income-producing properties. Since the law only became active in the 2006 tax year, most of the rehabilitation to date at American Tobacco did not qualify. However, the developers plan to pursue these tax credits for future phases of the project.

The Lucky Strike and Hill Buildings were rehabilitated into over 100,000 square feet of office space. The following table shows the qualified rehabilitation expenses and tax credits available at statutory rates.¹⁹

Table 2: Summary of Tax Credit Potential For Selected ATC Buildings

| | <u>Hill</u> | <u>Lucky Strike</u> |
|---------------------------|-----------------------|----------------------|
| <u>Qual. Rehab Exp.</u> | \$20,199,711 | \$13,043,191 |
| <u>Federal Tax Credit</u> | | |
| Rate | 20.0% | 20.0% |
| Amount | \$4,039,942 | \$2,608,638 |
| <u>NC Mill Tax Credit</u> | | |
| Rate | 30.0% | 30.0% |
| Amount | \$6,059,913 | \$3,912,957 |
| Qual. Rehab Exp. | \$20,199,711 | \$13,043,191 |
| Tax Credits | <u>(\$10,099,856)</u> | <u>(\$6,521,596)</u> |
| Net Rehab Expense | \$10,099,856 | \$6,521,596 |

At full completion, experts have estimated that the complete American Tobacco project will bring 3,600 permanent jobs to downtown Durham. At the current NC median household income amount, that represents almost \$150 million annually in direct returns – before accounting for the indirect economic effects (which are more difficult to assess). Several studies have estimated the present value benefit to municipal revenues of state tax credits at \$1.30 - \$5.02 per \$1.00 tax credit.²⁰ For the projects above, that would represent increased tax revenues of \$13 - \$50 million solely from these two projects. This doesn't even consider the positive economic impact provided to the private sector, which would presumably far outweigh the public sector benefit.

¹⁷ Kalette, Denise. "Durham Restores Old Warehouses." **National Real Estate Investor**. January 1, 2008.

¹⁸ "Durham Crime Numbers Down – Again." **Bull City Rising**. August 24, 2007. (www.bullcityrising.com)

¹⁹ Unfortunately, for proprietary reasons, I was unable to obtain the amount of tax credit / equity received through the syndication process.

²⁰ Lipman Frizzell, and Mitchell LLC. 2002. *State of Maryland Heritage Structure Rehabilitation Tax Credits: Economic and Fiscal Impacts*. Baltimore: Preservation Maryland.

Conclusion

As discussed above, the NC mill rehabilitation tax credit program has several attractive features. However, the best feature of the program is that it effectively allows for those areas with greater relative wealth to subsidize and renew those areas with less relative wealth. For example, a blighted downtown area like Durham has witnessed tremendous revival and renewed civic pride as a result of the NC mill rehabilitation tax credit program. The City of Durham receives most of the benefits, in terms of increased investment, tax revenues, and jobs; however, the state of NC subsidizes the cost through the tax credit. Given the locales of most vacant manufacturing facilities in the state, this program is a tremendous example of wealth redistribution through opportunity and entrepreneurial business development, rather than more traditional, and arguably unsuccessful, wealth redistribution programs.

This program not only enables us to preserve and renew the architectural features which are woven into the state's history, but it better enables economic development in blighted areas, and also provides incentives to clean up environmental hazards from these former manufacturing sites.