

# Legislative Analysis

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## **HISTORIC REHABILITATION TAX CREDITS; HIGH COMMUNITY IMPACT CREDITS**

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**House Bill 6496 as enrolled**  
**Public Act 447 of 2008**  
**Sponsor: Rep. Steve Tobocman**  
**House Committee: New Economy and Quality of Life**  
**Senate Committee: Commerce and Tourism**

**Senate Bill 973 as enrolled**  
**Public Act 448 of 2008**  
**Sponsor: Sen. Cameron S. Brown**  
**Senate Committee: Commerce and Tourism**  
**House Committee: Commerce**

### **Second Analysis (7-23-09)**

**BRIEF SUMMARY:** The bills would revise the tax credits for historic rehabilitation that may currently be applied against the State Income Tax, and the Michigan Business Tax, effective January 1, 2009.

**FISCAL IMPACT:** Senate Bill 973 is estimated to increase the cost of the Michigan Business Tax's historic preservation credit by at least \$9.0 million by tax year 2012, increasing to about \$14.0 million by the 2016 tax year, according to the Senate Fiscal Agency. The loss in revenue could be higher than estimated. For details, see [Fiscal Information](#). House Bill 6496 is expected to have a minimal impact on state revenue because the cost of the income tax credit is relatively small.

### **THE APPARENT PROBLEM:**

Historic resources are tangible links with our past. They impart a sense of identity, stability, and orientation to a community. To promote and preserve historic resources, Michigan offers historic preservation tax incentives--tax credits that lower the amount of tax owed. The tax credits, administered jointly by the Department of Treasury and the State Historic Preservation Office in the Michigan Department of History, Arts, and Libraries, reward Michigan taxpayers who are willing to invest in the enduring beauty of the built environment; and to preserve continuity in more lively and livable communities.

For example, the Michigan historic preservation tax credit--a state income tax credit of 25 percent on qualified rehabilitation expenditures--is available to taxpayers who will preserve historic buildings, structures, and sites. Applications for rehabilitation are certified by the state following an evaluation to determine whether the applicant's project meets the U. S. Secretary of the Interior's "Standards for Rehabilitation."

In addition, Michigan commercial property owners, business owners and long-term lessees who rehabilitate historic resources can apply for a credit against their state income tax or the Michigan Business Tax of up to 25 percent of qualified expenditures.

The U. S. Tax Reform Act of 1986 also makes available federal rehabilitation tax credits in the amount of 20 percent for residential purposes and 10 percent for non-residential purposes. In some instances, historic preservationists may combine the federal and state tax incentive programs--if, for example, a site is listed on the National or State Register, or located in a locally designated historic district--although in Michigan the two credits cannot be "stacked" on top of each other. (See Background Information.)

Legislation has been introduced to add greater flexibility to Michigan's historic preservation tax credits; add a new tax credit for "high community impact" historic rehabilitation projects; and also make the state and federal programs more compatible.

### ***THE CONTENT OF THE BILLS:***

The bills would revise the tax credits for historic rehabilitation that may currently be applied against the Michigan Business Tax and the State Income Tax. Their effective date is January 1, 2009. A detailed description of each bill follows.

#### **Senate Bill 973**

The bill would amend the Michigan Business Tax Act (MCL 208.1435) to revise the historic rehabilitation tax credit in the following ways.

#### ***Qualified Expenditures/IRS Regulations***

Currently under the law, a qualified taxpayer with a rehabilitation plan can credit against the Michigan Business Tax the amount of qualified expenditures for the rehabilitation of an historic resource, provided that the certification of completion is issued not more than five years after the rehab plan is certified by the Michigan Historical Center. The bill would eliminate this provision, and specify instead that the only qualified expenditures would be those that are paid or incurred during the time period prescribed for the credit under Section 47(a)(2) of the federal Internal Revenue Code and any related Treasury regulations.

#### ***Eligibility Criteria***

The current law specifies the location criteria under which an historic resource can be claimed as a qualified expenditure, including among other things its location in a designated historic district. Senate Bill 973 would retain these provisions, and add *the historic resource is subject to a historic preservation easement*.

#### ***Reassignment of Credit***

The bill specifies that for projects for which a certificate of completed rehabilitation is issued (for a tax year beginning) after December 31, 2008, a taxpayer may assign all or any portion of the credit allowed. The credit assignment would be irrevocable and be

made in the tax year in which the certificate was issued. The taxpayer could claim a portion of a credit and assign the remaining amount. If the qualified taxpayer both claimed and assigned portions of the credit, the taxpayer would claim the portion it claimed in the tax year in which the certificate was issued. Further, the credit could also be assigned *or reassigned* (as long as it was done on an approved form) and claimed against the assignees' Michigan Business Tax or the State Income Tax (by attaching a copy of the assignment certificate to the annual tax return). Currently the credit cannot be reassigned.

### ***Refunds Instead of Carryovers***

The bill also specifies that for a tax year beginning after December 31, 2008, for projects less than \$250,000, a taxpayer may elect to forgo the carryover period and instead receive a refund of the amount of the credit that exceeded the qualified taxpayer's tax liability. The amount of the refund would be equal to 90 percent of the amount of the credit that exceeded the liability. This could only be done in the year that a certificate of completion was issued, and it would be irrevocable. Currently under the law, a refund is not allowed.

### ***Revocation/Tax Liability Add-Backs***

The bill revises the revocation provisions of the law, for tax years beginning after January 1, 2009. Currently, if a certificate is revoked, the remaining portion of the credit is added back to the tax liability of the taxpayer. For example if the revocation was less than one year after the year in which the credit was claimed, then 100 percent; if between one and two years, then 80 percent; if between two and three years, then 60 percent; if between three and four years, then 40 percent; if between four and five years, then 20 percent; and if the revocation occurred five or more years after the credit was claimed, then no liability is added back.

Senate Bill 973 would retain this schedule of added tax liability in the event of revocation or sale within five years, but do so subject to Section 47(b)(1) of the Internal Revenue Code and related Treasury regulations. The bill also specifies that this schedule of added tax liability would not apply if the qualified taxpayer entered into a written agreement with the State Historic Preservation Office that would allow for the transfer or sale of the historic resource, and if the taxpayer provided the following:

- Reasonable assurance that after the transfer the property would remain an historic resource.
- A method that the department could recover an amount from the taxpayer equal to the appropriate percentage of the credit added back (as described above).
- An encumbrance on the title to the historic resource being sold or transferred, stating that the property must remain an historic resource throughout the five-year period after being placed in service.
- A provision for the payment by the taxpayer of all legal and professional fees associated with the drafting, review, and recording of the written agreement.

### ***Additional Credits***

Senate Bill 973 creates a new section of the law to allow additional tax credits, after January 1, 2009, for taxpayers who have a "pre-approval letter." The bill defines the term "pre-approval letter" to mean a letter issued by the director of the Department of History, Arts, and Libraries or a designee that indicates the date that the completed Part 2 application was received and the amount of the credit allocated to the project based on the estimated rehabilitation cost included in the application.

Under this section, a taxpayer can claim an additional credit equal to a percentage established in the pre-approval letter for the rehabilitation of an historic resource or the actual amount of the taxpayer's (qualified) expenditures incurred during the rehabilitation of the resource, whichever was less. However, the bill specifies that the total amount of all additional credits under this program cannot exceed \$8 million in the tax year ending on December 31, 2009; \$9 million in 2010; \$10 million in 2011; \$11 million in 2012; and \$12 million in 2013.

The bill also specifies that at least 25 percent of the allotted amount for additional credits must be allocated to rehabilitation plans that have \$1 million or less in qualified expenditures.

On October 1 of each calendar year, if the total of all credits approved is less than the minimum allotted amount, then the Department of History, Arts, and Libraries may use the remainder to approve applications for additional credits already submitted in that calendar year. To be eligible for the additional credits, the taxpayer would have to apply to and receive a pre-approval letter and comply with the following:

- For rehabilitation plans that have \$1 million or less in qualified expenditures, the department director is authorized to determine an amount between 10-15 percent of expenditures for which a credit may be claimed.
- For rehabilitation plans that have more than \$1 million in qualified expenditures, the department director, subject to the approval of the president of the Michigan Strategic Fund (or a designee) is authorized to approve up to 15 percent of expenditures for which a credit may be claimed.

The bill requires that an application be approved or denied within 15 business days after the HAL director has determined the percentage amount of the credit and submitted it to the Strategic Fund.

### ***High Community Impact Historic Rehabilitation***

Senate Bill 973 would allow the director of HAL, subject to the approval of the president of the Strategic Fund and the state treasurer, to approve three additional credits during 2009, of up to 15 percent, and two additional credits of up to 15 percent during 2010, 2011, 2012, and 2013. These rehabilitation plans would need to be "high community impact" plans having a significantly greater historic, social, and economic impact than others. To be eligible for these credits, a taxpayer would have to apply and receive a pre-approval letter from the director of HAL. The bill requires that an application be approved or denied within 15 business days after the director of the department has

determined the percentage amount of the credit and submitted it to the Strategic Fund and the state treasurer. The bill also requires the director to consider all of the following criteria:

- The importance of the historic resource to the community.
- If the rehabilitation for the historic resource will act as a catalyst for additional rehabilitation or revitalization of the community.
- The potential that the rehabilitation of the historic resource will have for creating or preserving jobs and employment.
- Other social benefits the rehabilitation will bring.
- The amount of local community and financial support for the rehabilitation.
- The taxpayer's financial need for the additional credit.
- Whether the taxpayer is eligible for the credit allowed under Section 47(a)(2) of the federal Internal Revenue Code.
- Any other criteria that the department director, and Strategic Fund president, and the state treasurer consider appropriate.

The maximum amount of credit that a taxpayer could claim under the High Community Impact Historic Rehabilitation program during a tax year would be \$3 million. If the amount approved was greater, then that portion that exceeded the cap would be carried forward to offset tax liability in subsequent tax years.

In addition to meeting the criteria listed above, two of the three credits available during the 2009 calendar year for a high community impact rehabilitation plan would have to be for an application that met one of the following set of criteria:

(1) The historic resource must meet all of the following: be at least 80 years old; comprise at least 75,000 total square feet; be located in a county with a population of more than 1,500,000; be located in a city with an unemployment rate that is at least two percent higher than the current state average unemployment rate at the time of the application; and, receive a federal earmark appropriation and be the former home of a former professional sports team.

(2) The historic resource must meet all of the following: be at least 85 years old; comprise at least 120,000 total square feet; be located in a county with a population of more than 400,000 and less than 500,000; be located in a city with a population of more than 100,000 and less than 125,000; and, be located in a city with an unemployment rate that is at least two percent higher than the current state average unemployment rate at the time of the application.

#### ***Pre-approval Letter Amendments***

Under the bill, the department director could (a) make amendments to the pre-approval letter, which could include revising the amount of qualified expenditures for which the taxpayer could claim additional credit; and (b) with 45-days written notice, revoke the pre-approval letter if not enough progress were made toward completion of the rehabilitation plan. If any credits were revoked, they would be added to the annual cap.

Likewise, any difference in the credits awarded and the credits claimed would be added to the annual cap.

### **House Bill 6496**

The bill would amend the Income Tax Act of 1967 (MCL 206.266) to make similar revisions as in the MBT Act to the historic rehabilitation tax credit, allowing credits to be issued in compliance with Section 47(a)(2) of the Internal Revenue Act and related Treasury regulations. (The description below repeats many provisions found in the description of the MBT bill, Senate Bill 973.)

#### ***Eligibility Criteria***

The current law specifies the location criteria under which an historic resource can be claimed as a qualified expenditure, including among other things its location in a designated historic district. House Bill 6496 would retain these provisions, and add *the historic resource is subject to a historic preservation easement.*

#### ***Refunds Instead of Carryovers***

The bill specifies that for projects less than \$250,000, a taxpayer may elect to forgo the carryover period and receive a refund of the amount of the credit that exceeded the qualified taxpayer's tax liability. The amount of the refund would be equal to 90 percent of the amount of the credit that exceeded the liability. This could only be done in the year that a certificate of completion was issued, and it would be irrevocable. Currently under the law, a refund is not allowed. (This applies for a tax year beginning after December 31, 2008.)

#### ***Revocation/Tax Liability Add-Backs***

The bill revises the revocation provisions of the law, for tax years beginning after January 1, 2009. Currently, if a certificate is revoked, the remaining portion of the credit is added back to the tax liability of the taxpayer. For example if the revocation was less than one year after the year in which the credit was claimed, then 100 percent; if between one and two years, then 80 percent; if between two and three years, then 60 percent; if between three and four years, then 40 percent; if between four and five years, then 20 percent; and if the revocation occurred five or more years after the credit was claimed, then no liability is added back. House Bill 6496 would retain this schedule of added tax liability in the event of revocation, but do so subject to Section 47(b)(1) of the federal Internal Revenue Code and related Treasury regulations. The bill also specifies that this schedule of added tax liability would not apply if the qualified taxpayer entered into a written agreement with the State Historic Preservation Office that would allow for the transfer or sale of the historic resource, and if the taxpayer provided the following:

- Reasonable assurance that after the transfer the property would remain an historic resource.
- A method that the department could recover an amount from the taxpayer equal to the appropriate percentage of credit added back (as described above).

- An encumbrance on the title to the historic resource being sold or transferred, stating that the property must remain an historic resource throughout the five-year period after being placed in service.
- A provision for the payment by the taxpayer of all legal and professional fees associated with the drafting, review, and recording of the written agreement.

House Bill 6496 further specifies that if, after December 31, 2008, a taxpayer who received a certificate of completed rehabilitation sold the historic resource for which the credit was claimed in less than five years, and that certificate was then revoked less than five years after the historic resource was placed in service (as defined in Section 47(b)(1) of the Internal Revenue Code and related Treasury regulations) because of unapproved alterations made by the purchaser, then the appropriate percentage of the credit previously claimed would be added to the tax liability of the purchaser in the year of the revocation.

***BACKGROUND INFORMATION:***

For further information about Michigan's Historic Preservation Tax Incentives, visit the website of the Department of History, Arts, and Libraries at <http://www.michigan.gov/hal>

***FISCAL INFORMATION:***

Senate Bill 973, according to estimates by the Senate Fiscal Agency, will increase the cost of the Michigan Business Tax's historic preservation credit by at least \$9 million by tax year 2012, and then this cost will increase gradually to an estimated \$14 million by the 2016 tax year. The loss in revenue could be higher than estimated due to the uncertainty of how much one of the new credits will cost, given that the dollar limit on the amount that may be claimed in any one year is \$3 million. In addition, it is very likely that the cost of this bill will vary significantly from year to year due to annual fluctuations in both the number and the size of credits that will be claimed. Under the original state credit, which equals 25% of qualified expenditures less the federal credit of 20% of expenditures, the number of credits that were claimed each year from 2003 to 2006 ranged from 12 to 25, and the total cost of the state portion of these credits ranged from \$1.7 million to \$2.7 million, a fluctuation of over 50 percent.

The SFA says that Senate Bill 973 will increase the cost of the state historic preservation tax credit for five major reasons: 1) The bill creates a new credit beginning in tax year 2009 for projects approved by December 31, 2013, with the total amount of these credits capped at \$8.0 million in 2009, \$9.0 million in 2010, \$10.0 million in 2011, \$11.0 million in 2012, and \$12.0 million in 2013; 2) this new credit, in combination with the existing 25% state/federal credit, provides a total credit of up to 40% of qualified expenditures and this increase in the total credit percentage will make some currently marginal historic preservation projects more viable and therefore it will increase the number of taxpayers that will claim this credit; 3) the bill expands the ability of taxpayers to assign these credits to other taxpayers, which also will help improve the financial viability of current marginal projects and thus increase the number of credits granted; 4) for credits less than

\$250,000, a taxpayer may receive a refund equal to 90% of the amount by which the credit exceeds tax liability; and 5) the bill creates new special credits (three credits in 2009 and two each year from 2010 to 2013), which may not exceed 15% of the project's qualified expenditures, and not more than \$3.0 million may be claimed as a credit in any given year. The loss of revenue under this bill will reduce the General Fund/General Purpose budget.

***ARGUMENTS:***

***For:***

This legislation enhances Michigan's Historic Preservation Tax Incentives program. The tax credits--available to encourage investment in Michigan historic resources--enable business owners and citizens to preserve tangible links to the past. Those often elegant links located within the built environment afford citizens a greater sense of identity and stability within their communities, making them better able to meet the uncertainty and challenges of the future.

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.