

# THE HISTORIC TAX CREDIT COALITION

## **Summary of the Revised Community Restoration and Revitalization Act 111<sup>th</sup> Congress**

**Section 1. Enabling Smaller Rehabilitation Projects (Modified from section 4 of the previous bill)** *Amend Section 47 of the Tax Code to increase the historic tax credit from 20 to 30 percent for “small projects” with \$5 million or less in Qualified Rehabilitation Expenditures (QREs).*

In 2008 only 37% of all historic tax credit transactions had total development costs over \$1 million. Small businesses have great difficulty attracting private capital to these investments because they do not meet the minimum threshold for institutional investors. Allowing a deeper credit of 30 percent for historic rehabilitation projects of \$5 million or less in qualified rehab expenditures would boost the net equity for smaller projects and make them more attractive for private investment. Many of these projects house businesses that provide essential small town and rural Main Street retail services in communities that need the reinvestment most.

**Section 2. Providing Downtown Housing in Older Buildings (In Section 5 of the previous bill.)** *Amend Section 50 of the Code to permit the 10 percent non-historic credit for older buildings to be used for rehabilitating residential rental property.*

Under current law, the 20 percent portion of the Section 47 credit is available for the rehabilitation of any income producing property. Housing is not allowed, however, under the 10 percent portion of the Section 47 credit for non-historic older buildings. Allowing the 10% credit for rental housing would enable an existing inventory of smaller Main Street, neighborhood-oriented retail buildings to also provide places to live. Many were originally constructed with “above-the-store” dwelling units that once housed tenants and are now largely vacant. These upper floor units are often located in areas already served by transit and existing public infrastructure.

**Section 3. Using a Practical Definition for “Older Buildings” (In Section 6 of the previous bill.)** *Amend Section 47 to use the common definition of an older building as one that is at least fifty years old in determining eligibility for the 10 percent credit.*

Other federal and state law routinely use 50 years old or older as common definition of a historic or older building. In 1986 when Section 47 was amended, Congress recognized this standard by establishing 1936 as the age requirement for projects qualifying for the 10 percent credit. It has not been changed since then, preventing whole categories of strategic older buildings from rehabilitation through the credit. Buildings must now be 73-years old to qualify, and fewer will be eligible as time passes. Rather than use a fixed date to determine eligibility, it would be better public policy to define an older building as one that is fifty years old or older.

**Section 4. Rehabilitating Historic and Older Buildings that are leased to government and nonprofit tenants (In Section 7 of the previous bill.)** *Amend Section 47 of the Code to allow certain leasing arrangements with nonprofits and government entities that are now precluded.*

The tax-exempt use property rules of Section 168(h) penalize many non-abusive, preservation-based community development projects. With some slight changes, many of these projects could use the rehabilitation tax credit without weakening the anti-abuse function the rules were originally designed to perform.

Section 168(h) defines as “tax-exempt use property” any property leased to a tax-exempt entity in a “disqualified lease.” Further, the Code does not allow historic tax credits to be claimed on QREs in tax-exempt use property. However, based on amendments from last year’s bill approved by Congress in 2008, properties are exempt if 50 percent or less of the building is leased under disqualified leases.

Similar to last year, this bill would modify Section 47(c) to limit the definition of a disqualified lease to those leases that are part of a sale leaseback. The other three types of disqualified leases: those with purchase options, leases in excess of 20 years and leases in buildings that use tax-exempt financing would be eliminated.

•  
**Section 5. Facilitating Smaller Projects through Transferability (Not in the previous bill.)** Amend Section 47 to allow for the transfer of rehabilitation tax credits to taxpayers outside the LLC or limited partnership for projects under \$5 million in qualified rehabilitation costs.

By making the historic tax credit transferable outside the partnership for small deals, partnership transaction costs would be eliminated, resulting in a larger net percentage of the credit value available to defray rehab rather than third-party costs. Transferability for small deals would also boost critically need private market demand for small credit amounts by attracting investors who would prefer to stay out of a property ownership role.

**Section 7. Encouraging Moderate Rehabilitation through Reducing the Substantial Rehabilitation Test (Not in the previous bill.)** Amend Section 47 to allow for moderate rehabilitation by reducing by half the substantial rehabilitation requirements.

Under current law rehabilitation tax credits can only be used if the property meets the requirement for substantial rehabilitation. During a 24-month period selected by the taxpayer, rehabilitation expenditures must exceed the greater of \$5,000 or 100% of the adjusted basis of the building. This proposal would allow for credits to be earned on moderate rehabilitation projects, if the cost of rehab is just fifty-percent of the adjusted basis.

**Sections 8 and 9. Making Historic Buildings Energy-Efficient (Not in previous bill.)** Amend Sections 47 and 45 of the Code to encourage building owners who are in the process of rehabilitating historic and older buildings to strive for substantial energy savings and allow graduated increases in the historic credit based on the level of energy efficiency achieved.

Forty-three percent of all carbon dioxide emissions in the United States come from the operation of buildings. They are also the source of 72 percent of all electricity consumption in America. The adaptive reuse of existing old buildings is an inherently green, transit-oriented, smart growth strategy. The rehabilitation tax credit should enhance the green existing benefits of rehab by encouraging the retrofit of historic and older buildings for energy efficiency.

The proposed amendment would provide a boost in the value of the credit from \$2.00 to \$5.00 per square foot depending on a range of energy savings starting at 30 percent and graduating up to 50 percent. This additional “energy supplement” would be awarded on a performance basis, recognizing actual energy reductions over a baseline measured after a rehabilitation is complete.

Another provision would specify that equipment and materials (such as solar panels or geothermal systems) used to achieve certified energy efficiency improvements, affixed to the top of or adjacent to a property, would be deemed Qualified Rehab Expenditures.

The bill’s “green” amendments also allow for twinning of the Section 45 Renewable Energy Tax Credits with the historic tax credit. Similar to the twinning of Low-Income Housing and rehabilitation tax credits, combining Section 47 and 45 credits would require a reduction of the Energy Credit basis by the amount of the HTC.

Finally, the bill would alter the definition of a “substantial rehab” again for the purpose of doing an energy retrofit only. Any energy improvement costs that qualify for the “energy supplement” outlined above, would by themselves meet the substantial rehab test, thereby encouraging property owners with buildings otherwise in good shape to do energy upgrades.

**Section 10. Allowing State Historic Tax Credits to Work More Effectively with the Federal Credit** Amend Part III of subchapter B of Chapter 1 of the Code to specify that the proceeds from the sale of state historic tax credits should not be taxed at the federal level.

Over 30 states have their own historic tax credit program. When combined with federal RTC, state credits can provide critical additional subsidy for building rehabilitations. However, state credits price lower in private equity markets than federal RTCs because a reduction in an investor’s state taxes results in higher taxable income at the federal level due to the loss of the federal deduction. This provision would allow the price paid for state tax credits and the equity support generated for property rehabs to float higher to approximate the higher relative pricing of the federal credits.