

# PA Historic Preservation Incentive Act to Spur Renovation of Historic Structures

[On behalf of Dornish Law Offices, PC](#) | Sep 16, 2012 | [All, Real Estate Practice](#)

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When Governor Corbett signed House Bill 761 on July 2, 2012, the Historic Preservation Incentive Act, which was part of a larger Bill that provided amendments to the Tax Reform Code of 1971, became law. (Pa. Pub. Law. No. 751, Act No. 85, Art. No. XVII-H (July 2, 2012) (*available*

at <http://www.legis.state.pa.us/WU01/LI/LI/US/HTM/2012/o/0085.htm>

). This Act is important for real estate investors who plan to renovate historic buildings in Pennsylvania. It is hoped that the very substantial tax credit, up to 25% of the cost of a rehabilitation project, up to \$500,000 per taxpayer per year, will spur more development of historic structures.

Keep in mind that a tax credit saves a taxpayer one dollar in tax for each dollar in credit, so a tax credit is worth significantly more to a taxpayer than a tax deduction of the same amount. If you are a “qualified taxpayer” and spend \$100,000 on “qualified expenses” on a “qualified building,” you can save \$25,000 in “qualified” Pennsylvania taxes, and thereby reduce the real cost of your project without any lien or mortgage for the amount of the credit.

Now that I have your attention, what are all the qualifications mentioned above? First, a “Qualified Historic Structure” is a commercial building located in Pennsylvania which meets the criteria under Section 47(c)(3) of the Internal Revenue Code, 26 U.S.C. § 47(c)(3). Section 47(c)(3) provides as follows:

(3)(A) In general. The term ‘certified historic structure’ means any building (and its structural components) which—

(i) is listed in the National Register, or

(ii) is located in a registered historic district and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

(B) Registered historic district. The term ‘registered historic district’ means–

(i) any district listed in the National Register, and

(ii) any district–

(I) which is designated under a statute of the appropriate State or local government, if such statute is certified by the Secretary of the Interior to the Secretary as containing criteria which will substantially achieve the purpose of preserving and rehabilitating buildings of historic significance to the district, and

(II) which is certified by the Secretary of the Interior to the Secretary as meeting substantially all of the requirements for the listing of districts in the National Register.

As such, to be a “Qualified Historic Structure,” your building must be located on a National Register or located in a registered historic district and certified by the Secretary of the Interior as being of historic significance to the district. Registered historic districts are either districts listed in the National Register; or districts designated by State or local statute as a historic district if the statute is certified by the Secretary of the Interior; or any district certified by the Secretary of Interior as meeting the requirements to be listed on the National Register. The procedures and guidelines for a building to be certified as being of “historic significance” to the district are set forth by the Secretary of the Interior at Title 36, Part 67 of the Code of Federal Regulations, 36 C.F.R. § 67.4 – 67.5.

The second qualification, a “Qualified Rehabilitation Plan” is a plan to rehab such a structure which has been approved by the PA Historical and Museum Commission as complying with the standards for rehabilitation and guidelines for rehabilitation of historic buildings adopted by the U.S. Secretary of the Interior. These Standards are codified at Title 36, Part 67.7 of the Code of Federal Regulations.

Generally, the Standards for Rehabilitation pertain to “historic buildings of all materials, construction types, sizes, and occupancy and encompass the exterior and the interior of historic buildings. The Standards also encompass related landscape features and the building’s site and environment, as well as attached, adjacent, or related new construction.” 36 C.F.R. § 67.7. The following Standards “are to be applied to specific rehabilitation projects in a reasonable manner, taking into consideration economic and technical feasibility”:

- (1) A property shall be used for its historic purpose or be placed in a new use that requires minimal change to the defining characteristics of the building and its site and environment.
- (2) The historic character of a property shall be retained and preserved. The removal of historic materials or alteration of features and spaces that characterize a property shall be avoided.
- (3) Each property shall be recognized as a physical record of its time, place, and use. Changes that create a false sense of historical development, such as adding conjectural features or architectural elements from other buildings, shall not be undertaken.
- (4) Most properties change over time; those changes that have acquired historic significance in their own right shall be retained and preserved.
- (5) Distinctive features, finishes, and construction techniques or examples of craftsmanship that characterize a historic property shall be preserved.
- (6) Deteriorated historic features shall be repaired rather than replaced. Where the severity of deterioration requires replacement of a distinctive feature, the new feature shall match the old in design, color, texture, and other visual qualities and, where possible, materials. Replacement of missing features shall be substantiated by documentary, physical, or pictorial evidence.
- (7) Chemical or physical treatments, such as sandblasting, that cause damage to historic materials shall not be used. The surface cleaning of structures, if appropriate, shall be undertaken using the gentlest means possible.
- (8) Significant archeological resources affected by a project shall be protected and preserved. If such resources must be disturbed, mitigation measures shall be undertaken.
- (9) New additions, exterior alterations, or related new construction shall not destroy historic materials that characterize the property. The new work shall be differentiated from the old and shall be compatible with the massing, size, scale, and architectural features to protect the historic integrity of the property and its environment.
- (10) New additions and adjacent or related new construction shall be undertaken in such a manner that if removed in the future, the essential form and integrity of the historic property and its environment would be unimpaired.

36 C.F.R. § 67.7. Illustrated guidelines for rehabilitating a historical building are set forth more in depth by the U.S. Department of Interior at:

<http://www.nps.gov/tps/standards/rehabilitation/rehabilitation-guidelines.pdf>.

The third qualification, a “Qualified Taxpayer” can be a natural person, corporation, business trust, LLC, partnership, Limited Liability Partnership, association or any other form of legal business entity which:

- a) Is subject to PA Commonwealth taxes other than employer withholding taxes; and
- b) owns a qualified historic structure

Finally, the fourth qualification, “Qualified Expenditures” are simply the costs and expenses incurred by the taxpayer to restore the structure in accordance with the plan, and which meet the definition provided in Section 47 (c)(2) of the Internal Revenue Code, 26 U.S.C. §47 (c)(2). This Section provides in pertinent part:

(c)(2)(A) In general. The term ‘qualified rehabilitation expenditure’ means any amount properly chargeable to capital account—

(i) for property for which depreciation is allowable under section 168 [26 USCS § 168] and which is—

- (I) nonresidential real property,
- (II) residential rental property,
- (III) real property which has a class life of more than 12.5 years, or
- (IV) an addition or improvement to property described in subclause (I), (II), or (III), and

(ii) in connection with the rehabilitation of a qualified rehabilitated building.

(B) Certain expenditures not included. The term ‘qualified rehabilitation expenditure’ does not include—

(i) Straight line depreciation must be used. Any expenditure with respect to which the taxpayer does not use the straight line method over a recovery period determined under subsection (c) or (g) of section 168 [26 USCS § 168]. The preceding sentence shall not apply to any expenditure to the extent the alternative depreciation system of section 168(g) [26 USCS § 168(g)] applies to such expenditure by reason of subparagraph (B) or (C) of section 168(g)(1) [26 USCS § 168(g)(1)].

(ii) Cost of acquisition. The cost of acquiring any building or interest therein.

(iii) Enlargements. Any expenditure attributable to the enlargement of an existing building.

(iv) Certified historic structure, etc. Any expenditure attributable to the rehabilitation of a certified historic structure or a building in a registered historic district, unless the rehabilitation is a certified rehabilitation (within the meaning of subparagraph (C)). The preceding sentence shall not apply to a building in a registered historic district if–

(I) such building was not a certified historic structure,

(II) the Secretary of the Interior certified to the Secretary that such building is not of historic significance to the district, and

(III) if the certification referred to in subclause (II) occurs after the beginning of the rehabilitation of such building, the taxpayer certifies to the Secretary that, at the beginning of such rehabilitation, he in good faith was not aware of the requirements of subclause (II).

....

(vi) Expenditures of lessee. Any expenditure of a lessee of a building if, on the date the rehabilitation is completed, the remaining term of the lease (determined without regard to any renewal periods) is less than the recovery period determined under section 168(c) [26 USCS § 168(c)].

(C) Certified rehabilitation. For purposes of subparagraph (B), the term ‘certified rehabilitation’ means any rehabilitation of a certified historic structure which the Secretary of the Interior has certified to the Secretary as being consistent with the historic character of such property or the district in which such property is located.

(D) Nonresidential real property; residential rental property; class life. For purposes of subparagraph (A), the terms ‘nonresidential real property,’ ‘residential rental property,’ and ‘class life’ have the respective meanings given such terms by section 168 [26 USCS § 168].

If you meet all four qualifications, you may apply to the PA Department of Community and Economic Development (DCED) with an application form provided by the Department ([www.esa.dced.state.pa.us](http://www.esa.dced.state.pa.us)). The application must include a qualified rehabilitation plan, which means the plan must be sent by the DCED for review and approval by the PA Historical and Museum Commission (HMC). The application must be submitted by February 1, after which it will be sent for review by the HMC. The HMC has 30 days to review the plan, and must notify the taxpayer of its determination within 15 days of making such determination.

Assuming the plan is approved by the HMC, the HMC will notify the DCED of both verification of a completed project and the amount of qualified expenditures incurred in the project. The DCED then issues a tax credit

certificate by April 1, which the taxpayer can use as credit against a qualified tax liability on or after July 1, 2013. If the taxpayer doesn't owe enough PA tax in the year in which the tax credit is first approved, it can be carried forward for up to seven years, sold with approval of the DCED, or passed through to shareholders, members or partners of a pass through entity. However, a shareholder, member or partner cannot carry back, carry forward, sell or assign the credit.

The credits under this Act will be available for seven years, and are in addition to Federal Historic Tax credits of up to 20% of the costs of historic renovations. This means the developer who meets both the Federal and State Historic Credit requirements could save up to 45% of the cost of a project in state and federal tax. If that isn't enough of an incentive to plan your next project as a historic renovation, you may be able to combine façade grants on certain commercial buildings with the above tax credits on the rest of the project not covered by the grants.

I'm working on such a project right now, and have received a \$5,000 grant for architectural services. I hope to be able to obtain a façade grant of about \$40,000, and to be able to get Federal and State tax credits of 45% of the remaining \$100,000 project cost. That means grants and credits should cover \$90,000 of a \$145,000 project cost, and my net costs of \$55,000 will (in theory anyway) only be just under 40% of the total costs, while I retain 100% of ownership, subject only to a five year disappearing lien for the façade grant.

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