House Legislative Analysis Section
House Office Building, 9 South
Lansing, Michigan 48909
Phone: 517/373-6466

REVISE HISTORIC RESTORATION CREDIT

Senate Bills 888 and 889 (Substitutes H-2)
First Analysis (12-8-99)

Sponsor: Sen. John J.H. Schwarz, M.D.
House Committee: Tax Policy
Senate Committee: Finance

THE APPARENT PROBLEM:

Under federal law, tax credits are offered for the restoration of historic sites that are income producing. Public Acts 534 and 535 of 1998 amended the Single Business Tax Act and Income Tax Act, respectively, to allow qualified taxpayers to claim a credit against either or both taxes for qualified expenditures made for the rehabilitation of historic resources, regardless of whether the properties were income producing or for private use. Under the acts, a "historic resource" is defined as a publicly or privately owned historic building, structure, site, object, feature, or open space that is either located within a historic district that is designated by the national register of historic places, the state register of historic sites, or a local unit acting under the Local Historic Districts Act; or that is individually listed on the state register of historic sites or national register of historic places. A property can be an owner-occupied personal residence; an income-producing commercial, industrial, or residential property; property owned by a governmental body or nonprofit organization; and other resources that can benefit from rehabilitation, as long as expenditures meet strict federal and state criteria. Eligible taxpayers can receive a tax credit of 25 percent of qualified expenditures.

The 1999 tax year will be the first year in which taxpayers can apply for the tax credit created under Public Acts 534 and 535. However, over the course of this year, several problems with the acts became apparent as the Department of Treasury conducted training seminars on administering the credit and as consumers interested in applying for the credit began to ask questions. For instance, some of the time frames specified in Senate Bills 105 and 106, which became Public Acts 534 and 535, respectively, were not consistent with an amendment that added a sunset provision. Further, the tax credit was modeled on the federal tax credit for qualified restorations, which includes provisions for the reassignment of tax credits to other entities, referred to as "flow throughs". However, under state law, the Single Business Tax does not have a procedural mechanism to allow the flow through to work properly. Also, it was found that in some circumstances, particularly with regard to property owned by the state or houses owned privately but located on state property, no state equalized valuation (SEV) has been determined. As the tax credit is based on expenditures that equal or exceed a specified percentage of the SEV, it is necessary to amend the acts to provide for these situations. Further, other minor problems that are technical in nature have surfaced as the acts have been more closely scrutinized.

Adding urgency to the situation is that the printing of the tax forms used to claim the tax credit will begin in mid-December. If the problems identified with the current law are not corrected before the printing begins, it is expected that the Department of Treasury will either have to reprint the tax forms at a later date, or that taxpayers may have to file amended forms. Legislation has been proposed to correct the technical errors, clarify confusing language, and address the concerns discussed above.

THE CONTENT OF THE BILLS:

Senate Bill 888 would amend the Single Business Tax Act (MCL 208.39c) and Senate Bill 889 would amend the Income Tax Act (MCL 206.266) to revise provisions under both acts pertaining to the credits allowed for historic preservation.

Currently, a qualified taxpayer may claim a credit against either or both taxes for qualified expenditures made for the rehabilitation of a "historic resource". A historic resource includes a publicly or privately owned historic building, structure, site, object, feature, or open space located within a historic district as designated by the National Register of Historic Places, the State Register of Historic Sites, or a local unit that established a historic district under the Local Historic

Districts Act. A historic resource also includes a historic building, structure, etc., that is listed individually on the national or state register. The credit is equal to 25 percent of the qualified expenditures, and may be claimed for tax years beginning after 1998 and before 2003.

The bills specify that if a "qualified taxpayer" was a partnership, limited liability company, or subchapter S corporation, the qualified taxpayer could assign all or any portion of a credit allowed under either of the acts to its partners, members, or shareholders, based on each entity's proportionate share of ownership or based on an alternative method approved by the Department of Treasury. Such a credit assignment would be irrevocable and would be made in the tax year in which a certificate of completed rehabilitation was issued. A qualified taxpayer could claim a portion of the credit and assign the remaining credit amount, but an assignee could not subsequently reassign a credit or any portion of a credit assigned to him or her. A credit amount assigned under this provision could be claimed against a tax liability under either of the acts. Further, the credit assignment would be made on a form prescribed by the department. The qualified taxpayer and any assignees would have to send a copy of the completed assignment form to the department in the tax year in which the assignment was made and attach a copy of the completed assignment form to the annual return for that tax year that is required to be filed under both acts.

The credit may be claimed in the year in which a rehabilitated historic resource is placed in service; or the year in which a final payment of qualified expenditures is made if the project is a phased project and construction is planned for two to five years. Instead, the bills would specify that a qualified taxpayer with a rehabilitation plan certified after December 31, 1998 and before January 1, 2003 could claim a credit in the year in which the certification of completed rehabilitation of the historic resource was issued provided that the certification of completed rehabilitation was issued not more than five years after the rehabilitation plan had been certified by the Michigan Historical Center. In addition, expenditures made after December 31, 2002 and not more than five years after the certification of the rehabilitation plan would be qualified expenditures only if the rehabilitation plan had received certification by the Michigan Historical Center before January 1, 2003.

Currently, if the credit allowed for the tax year, and any unused carryforward of the credit, exceeds the taxpayer's tax liability for the tax year, the portion that exceeds the tax liability may not be refunded but may be carried forward to offset tax liability in subsequent tax years, for 10 years or until used up, whichever occurs first. Under the bills, a carryforward could be claimed in tax years that began after 2002, for a credit based on a project that began before 2003. The acts provide that the total of the credits claimed by a taxpayer under both acts may not exceed 25 percent of the total qualified expenditures eligible for the credit. Under the bills, the total credits claimed for a rehabilitation project could not exceed 25 percent of the total qualified expenditures <u>for that rehabilitation project</u>.

Currently, to claim a credit a qualified taxpayer must have qualified expenditures for the rehabilitation of the resource equal to or greater than ten percent of the state equalized valuation (SEV) of the property. If the historic resource is a portion of a historic or nonhistoric resource, the SEV of only that portion of the property must be used. If the assessor for the appropriate local tax assessing unit determines the SEV of that portion, that determination must be used; if the assessor does not determine the SEV, then qualified expenditures must be equal to or greater than five percent of the appraised value as determined by a certified appraiser. The bills further provide that if the historic resource to be rehabilitated did not have an SEV, qualified expenditures would have to be equal to or greater than five percent of the appraised value of the resource as determined by a certified appraiser.

Under the acts, the Michigan Historical Center may inspect a historic resource at any time during the rehabilitation process and revoke certification if the rehabilitation is not undertaken as represented in the rehabilitation plan, or if unapproved alterations to the completed rehabilitation are made during the five years after the tax year in which the credit was claimed. The bills provide that if a certificate were revoked less than five years after a credit was claimed, a percentage of the credit amount previously claimed would have to be added back to the tax liability of the taxpayer in the year of the sale. If the revocation were less than one year after the year in which the credit was claimed, the taxpayer would have to add back 100 percent of the credit. If the revocation were made at least one year but less than two years after the credit was claimed, the taxpayer would have to add back 80 percent; between two and three years, 60 percent; three and four years, 40 percent; four and five years, 20 percent. After five years, the taxpayer would not have an addback made to his or her tax liability.

HOUSE COMMITTEE ACTION:

House substitutes were adopted for each bill to correct technical errors.

BACKGROUND INFORMATION:

Senate Bills 888 and 889 would clarify provisions added to the Single Business Tax Act and Income Tax Act by Public Acts 534 and 535 of 1998, respectively. The intent of last year's legislation was to provide an incentive to the owners of historic resources to rehabilitate the properties. It was believed that offering a tax credit to offset the expense of such rehabilitative efforts would result in many benefits not just to the owners, but also to surrounding neighborhoods and the public in general. For more information, see the Senate Fiscal Agency's analysis on Enrolled Senate Bills 105 and 106 of the 1997-1998 legislative session, dated 2-4-99.

FISCAL IMPLICATIONS:

According to testimony offered by a representative from the Department of Treasury, the bills are not expected to result in a fiscal impact on state or local government as they are technical in nature and do not allow any additional parties to qualify for the tax credit. (12-8-99)

ARGUMENTS:

For:

The bills would correct technical problems with Public Acts 534 and 535 of 1998 that were not identified before the acts went into effect in January of this year. For instance, time frames in the bills are not consistent with a sunset that was added by a House amendment. Some of the provisions contain awkward language that is difficult to understand. In other instances, the bills would correct oversights, such as providing a mechanism for partnerships and limited liability companies to assign a tax credit to individual partners or shareholders, which would be in line with federal laws. Also, since qualified expenditures must be equal to or greater than a certain percent of the state equalized valuation (SEV) in order to claim the tax credit, the bills would provide for those situations in which the SEV of a property has not been determined, such as a qualified resource that is owned privately but located on state land.

According to a representative from the Department of Treasury, the bills are viewed as being technical in nature and not seen as making any substantive changes to the Single Business Tax Act and Income Tax Act. However, since the printing of the tax forms for 1999 is about to begin, it is important for these corrections to be made quickly so that the forms can reflect the clarifications. Otherwise, it is believed that either the department will have to reprint the forms whenever the bills are enacted, or that taxpayers will have to file amended returns. In either case, the department is likely to incur increased administrative costs and taxpayers will face confusing language and the time and expense of filing amended returns.

POSITIONS:

The Department of Treasury supports the bills. (12-7-99)

The State Historic Preservation Office supports the bills. (12-8-99)

Analyst: S. Stutzky

■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.