State Historic Preservation Tax Credit

ACTION: INSTITUTE A STATE HISTORIC PRESERVATION TAX CREDIT

Thirty-five states have a historic preservation tax credit. New Jersey is not one of them. Without the historic preservation tax credit, New Jersey is missing out on a proven tool for economic growth and revitalization. Between 1978 and 2015, the National Park Service's federal Historic Tax Credit for income-producing buildings led to $28.1 billion in federal tax receipts, a significant net gain over the $23.1 billion in allocated credits.[1] States that have their own historic preservation tax credits see similarly strong returns on investment at the local level.

BACKGROUND

In 2011, the New Jersey Senate voted unanimously to approve the Historic Property Tax Credit Act (S-659). The Assembly also passed an identical version of the bill. The Historic Property Tax Credit Act had strong bipartisan support.[2] However, it was part of the Democratic package for economic development, and Governor Christie vetoed it. This continued a pattern that had been in place since the mid-1990s and early 2000s, when bills for a historic tax credit garnered support on both sides of the aisle but never quite passed.

HISTORIC PRESERVATION TAX CREDIT AS A POLICY TOOL FOR ECONOMIC REVITALIZATION

A historic preservation tax credit drives economic development in the following ways:

- It creates jobs, during both the rehabilitation phase and the building's operation.
- It increases revenue in the form of income taxes, sales taxes, and property taxes.
- It incentivizes developers and banks to invest locally, especially in economically distressed areas they might not otherwise consider.
- It revitalizes run-down areas while making use of existing infrastructure.[3]
- It results in "spillover" effects that extend beyond the rehabilitated building, improving the local economy and attracting businesses to the surrounding area.

HOW THE CREDIT WORKS

Although each state has its own variants, the following steps describe how most historic preservation tax credit programs generally work. Most states keep their credit requirements consistent with the federal preservation standards so developers can apply to state and federal programs simultaneously. This makes the credit program doubly attractive to developers while promoting effective historic preservation within the state.

1. The state determines what types of buildings qualify.
2. Owners of qualified buildings submit an application to the state office or agency that administers the program. Proposals are evaluated competitively with a cost-benefit analysis that looks at how much tax revenue they will generate.
3. Winning projects earn a credit equal to a set percentage (20-30% in most states) of qualified expenses. The owner must pay the remainder of expenses, often financed by a loan.
4. Once the building is operational and has fulfilled all requirements, including compliance with historic rehabilitation standards, the credit is applied against the property owner's taxes—usually income tax.

MODELS IN OTHER STATES

Pennsylvania – Eligibility extends to qualified taxpayers completing restoration of a qualified historic structure into an income-producing property. Taxpayers apply through the Department of Community and Economic Development's electronic application system, and applications are reviewed on a first-come, first-serve basis. Tax credits apply toward up to 25% of qualified expenditures and may go toward personal income tax, corporate net income tax, capital stock-franchise tax, bank and trust company shares tax, title insurance companies share tax, insurance premiums tax, or mutual thrift institutions tax. The state program has a total annual cap of 3 million in credits per fiscal year (with $500,000 per project).[4]

Delaware – Eligibility extends to a property that is listed within the National Register of Historic Places, located within a National Register historic district, designated a local historic landmark, or located within a local historic district. The four-part application certifies that it is a historic property, that the rehabilitation process is valid, that the project has been completed, and that the owner requests an award of credit. Credit is awarded after the project is completed and certified as having met historic preservation standards. The credit may be applied against Delaware income tax liability or transferred to another tax payer. Credits are equal to 20% of the cost of rehabilitation for income-producing historic buildings. The credit may equal up to 30% if the project qualifies for low income tax credits. Delaware also offers a 30% credit for other non-commercial historic buildings. [5]

New York – Historic commercial buildings are eligible if they are located in a Qualified Census Tract with median family income at or below the state family median income level. State Historic Preservation Office staff review projects for compliance with federal preservation standards. The credit is worth 20% of the owner's state and federal income taxes. Unused credits are refundable. New York also has a separate tax credit program for owners of historic homes.

Ohio – Building owners and certain long-term lessees apply for a tax credit to rehabilitate eligible historic buildings. Ohio's Development Services Agency evaluates each application by conducting a cost-benefit analysis to determine whether the project will generate a net gain in state and local tax revenue. The DSA distributes up to $60 million in credits to top-scoring projects, with a cap of $5 million per project. The credit equals 25% of qualified expenditures against income tax, foreign and domestic insurance company gross premiums taxes, and financial institutions tax, up to the $5 million cap. Developers submit progress reports during the building's rehabilitation period. Once the renovation is finished, "developers receive the credit only after construction is complete and all requirements are verified." [6]

ECONOMIC BENEFITS

A study on Maryland's Heritage Structures Rehabilitation Tax Credit found that for every dollar of tax credit invested, the state receives "an average return of approximately $1.02 during the first year after a project's completion, and $3.31 within five years after project completion." In Maine, a study found that the first ten projects completed through the historic tax preservation credit "increased the assessed values in their community" from $3.6 million to $36 million, resulting in increased revenue from property and income taxes. [7]

Revenue is generated in the following ways:

- Historic preservation requires labor-intensive work, employing carpenters, electricians, plumbers, and other tradespeople. [8]
- Completed operational buildings create permanent jobs for employees who staff the businesses and maintain the building.
- New jobs mean new income, creating income tax revenue.
- Rehabilitation increases property values, resulting in increased property tax revenue. Increased property tax comes from the enhanced nature of the completed building. Because New Jersey property tax is based on the value of the structure and not the land, gains are especially pronounced when a dilapidated structure is rehabilitated, effectively putting the property back on the tax rolls.[9]
- Other taxes collected are state income tax, business-to-business sales tax, consumer sales tax, and commercial activity tax. [10]
- Indirect jobs are created by workers spending income and generally increased economic activity, such as other businesses moving to the area.
- States with state-level historic tax credit programs attract far more funding from the federal program. For instance, Kansas, before creating its own state program, completed around 50 projects over 21 years with the federal credit, with a combined $114 million in investment. After instituting its state program, Kansas completed 542 projects in 8 years, representing a total investment of $271 million. [11]

Not only does a historic preservation tax credit generate revenue, it's also been shown to foster greater economic growth than new construction:

- The distribution of costs in new construction average 40% labor and 60% materials. In contrast, rehabilitation costs on average 60% labor and 40% material, meaning more jobs. [12]
- In Delaware, $1 million output from a manufacturing firm generated about 9.2 jobs. A $1 million new construction project generated 11.2 jobs. Rehabilitation of a historic building beat both figures, with 14.6 jobs created for every $1 million spent.
- Delaware also benefited from the income those jobs generated. A manufacturing firm that spent $1 million generated on average about $344,000 in household income. A $1 million new construction project generated more than $477,000 in household income. Both paled in comparison to $1 million invested in rehabilitation of a historic building, which generated nearly $540,000 in household income. [13]
- "A $1 million investment in historic rehabilitation in Kansas realizes a markedly better economic effect to Kansas with respect to employment, income, GSP,

and state-local taxes compared to a similar increment of investment (i.e. $1 million) in an array of residential and nonresidential new construction (including building highways) in Kansas or a #1 million investment in an array of business activities important in Kansas, such as manufacturing (e.g., electrical machinery and automobile), agriculture (wheat farming), and services (telecommunication)." [14]

Finally, not having an historic preservation tax credit is an opportunity cost. Because New Jersey's bordering states all have tax credit programs, developers favor rehabilitation projects in those states over New Jersey.

ADDITIONAL BENEFITS

Preservation protects the cultural and aesthetic qualities of historic neighborhoods, providing a sense of community cohesion.[15] Historic neighborhoods attract the most economic and racial diversity, and they retain a greater percentage of their residents over time, creating social stability.[16] Historic rehabilitation also makes use of existing development and infrastructure, slowing sprawl and preserving farmland and open space. [17]

COSTS ASSOCIATED WITH HISTORIC TAX CREDITS

As a tax expenditure, the historic tax credit does have public costs. Potential costs include the following:

- Loss of immediate tax revenue—although these tax credit programs have been shown to more than pay for the initial loss over time. Loss of tax revenue can be limited by setting an annual cap on credits distributed.
- Cost of administering the program (evaluating applications, checking compliance, etc.)
- Opportunity cost for property values: A rehabilitated historic building generally results in higher property values than before the building was restored. However, it is possible that replacing the historic building with a new building (such as a high-rise apartment building) would result in even higher property values.

WHY IS A STATE CREDIT NECESSARY IN ADDITION TO THE FEDERAL PROGRAM?

The federal tax credit, which equals 20% of qualified rehabilitation expenditures, is sometimes not enough incentive for banks and developers to invest in rehabilitating historic properties. Rehabilitation projects in states with a state historic tax credit are more likely to win additional funding from the federal program, which in turn makes them more attractive to private investors. In Maryland, it is estimated that "$172.2 million in Federal Historic Preservation Tax Incentives Program tax credits have been leveraged by the Maryland tax credits—almost a one-to-one match. Owning to their challenging nature, most commercial projects would not be attempted without the equity provided by the combination of state and federal incentive programs."[18] There are numerous examples of successful projects that combined federal and state tax credits, such as the Parkside neighborhood redevelopment in Philadelphia.[19] In short, a state historic preservation tax credit would make New Jersey projects more competitive in receiving matching federal funds.

OPTIONS FOR STRUCTURING THE HISTORIC TAX CREDIT PROGRAM

The historic preservation tax credit is a proven method of economic stimulus that has had bipartisan support in New Jersey. Negotiations over the bill will likely come down to selecting different methods for structuring the credit to fulfill specific development or budgetary goals.

Income-producing vs. homeowner– The federal tax credit is limited to buildings used in trade or business for the production of income. Some states have chosen to extend eligibility for the state credit to houses belonging to individual homeowners, especially since the federal program does not cover this type of structure. If the primary goal is to generate jobs and tax revenue, the state may choose to define only income-producing buildings as eligible. It may be possible for the state to start with commercial structures and pilot a separate program for homeowners, perhaps with a focus on economically distressed areas.

Regional focus – The state can choose to focus the tax credit on a specific region that is targeted for redevelopment. Some states include geographical distribution in the tax code to ensure that both rural and urban areas benefit. Others focus the credit on economically distressed areas. In this scenario, the goal is to revitalize the economically distressed area, reducing its long-term reliance on state aid. In Vermont, credits are limited to commercial buildings in designated downtowns or village centers so that the credit operates as a strategic tool for revitalization.[20] The credit thus incentizives banks and developers to "revitalize often abandoned and underperforming properties that have a financing gap between what banks will lend and the total development cost of the transaction." [21]

Transferability – Some states allow the tax credit to be transferred. This is useful in cases where a building owner does not have enough tax liability to make full use of the credit. In Kansas, Kentucky, Oklahoma and Missouri, the taxpayer can sell the credit to a third party. Other options are to allow a tax credit not fully useable in the current year to be carried back to offset previous taxes, or for the tax credit to be refundable, with unused amounts payable in cash to the credit holder. [22]

Incentives for smaller projects — Beyond transferability, there are other ways to make sure smaller-scale projects can make use of the credit. The bill could offer a higher percentage of credit to projects with smaller spending projections (for instance, $1-2 million). Smaller entities could also benefit from more flexibility in local ordinances relating to redevelopment.

Zoning exemptions for historic buildings — One challenge in rehabilitating historic buildings is that they may not meet current zoning requirements. For instance, if a historic factory in a downtown is rehabilitated into an office building, there might not be room for the hundreds of parking spaces required by local zoning laws. Exemptions for historic buildings can help attract developers to these projects.

Credit amount – Of the 34 states with a tax credit, 28 issue a credit equal to between 20 and 30% of qualified expenditures. At the low end, Montana provides 5% when the federal 20% credit is also used, and North Carolina provides 15%. At the high end, New Mexico offers a 50% credit with a per-project cap of $25,000. To control overall costs of the programs, states usually have caps for individual projects as well as overall aggregate caps. For instance, Ohio has a $5 million individual project cap and a $60 million annual aggregate cap. Nebraska has a $1 million project cap and a $15 million annual aggregate cap. [23]

Qualified expenditures – The state defines what counts as a qualified expenditure. For instance, Ohio defines these expenses as costs paid or incurred by the owner to rehabilitate the building, including architectural or engineering fees. Excluded costs are the price of acquiring or expanding a building and work done on facilities such as parking lots or sidewalks. The federal credit excludes expenses for expanding the building or costs associated with a portion of the building that will be used for tax-exempt purposes. [24] The federal credit also includes cleanup for brownfield sites, which is often a critical component of redevelopment projects. Because rehabilitation projects occur on land that is already developed, it is recommended that state programs keep brownfield cleanup as an eligible expense.

AREAS OF NEW JERSEY THAT WOULD BENEFIT FROM A HISTORIC TAX CREDIT

Because of New Jersey's industrial heritage, the state has a high percentage of buildings over 40 years old. Many of these buildings are sitting vacant. They are perfect for rehabilitation because industrial buildings can be converted into a wide variety of uses, and are often located in urban settings with existing infrastructure and transportation. Cities like Trenton, Perth Amboy, Rahway, and Elizabeth are strong candidates for historical rehabilitation. A study on markets in the City of Trenton found that given its "historic import," there is high potential to capitalize on its existing assets to invigorate commercial activity. The city's eight historic districts and 51 historical landmarks are eligible for the federal tax credit program. However, the city would see a larger number of projects completed if New Jersey had a state tax credit. This would encourage developers to invest in the city. [25]

Without the state tax credit, many historical buildings across New Jersey remain vacant or underutilized. One example is the Hahne and Co. Building in Newark. This commercial structure was built as a department store in 1901 and thrived through the 1950s. With the creation of suburban shopping malls, Hahne's went into decline, with its last store leaving in 1986.[26] The building stood empty for more than two decades. Eventually—through a public-private partnership between L + M Development Partners, Goldman Sachs, Prudential Financial, Citibank, New Jersey Housing and Mortgage Finance Company, and the state Economic Development Authority—the building was rehabilitated into a mixed-use facility with stores, apartments, and an art facility for Rutgers University at Newark. It officially reopened in 2017.[27]

While it is positive that Hahne's has reopened, the building remained vacant for more than 20 years—20 years that represent missed opportunities on property taxes, economic activity, and housing in Newark's downtown. If New Jersey had had a state historic preservation tax credit, it is likely that the building would have been rehabilitated sooner.

A similar example is the Keystone Watch Case Co. building in Riverside. The building was constructed in 1908. The factory closed in the 1950s after wristwatches replaced pocket watches. Another company, Root Metals, occupied the building until 1978. After that, the building stood mostly vacant. Various developers have proposed but never completed plans for the building. In 2016, a Brooklyn development firm purchased the building with plans to convert it to luxury apartments. However, it remains to be seen whether this redevelopment project will be finished. Without incentives for developers, the factory has remained underutilized for nearly four decades. [28]

STAKEHOLDERS

Businesses — Businesses favor historic tax credits for commercial buildings. Unique, historic buildings are particularly attractive to entrepreneurs and local businesses. In an era where online shopping has made experiential retail newly important, businesses desire buildings with character and history.

Developers — Developers support historic tax credit programs, as they provide needed incentives to redevelop eligible buildings. Developers favor state historic tax credits that mirror the requirements for the federal programs so that they can apply to both programs simultaneously. Developers also require credit programs with faster application and approval cycles. They cannot afford to pay taxes and mortgage on a building that long sits vacant. An ideal credit program for developers would allow for preliminary or fast-track approval of an application. If the project is completed according to the proper standards, the credit would then be earned.

Homeowners — Homeowner eligibility for the tax credit will depend on the scope and budgetary limits of the credit. Homeowners are likely to support the bill if their houses are eligible. Some early drafts of the New Jersey bill included homeowners in order to win their support. However, this must be balanced against the demands of the Treasury, which generally wants a credit with more limited scope. Making homeowners eligible would add approximately 35,000 historic homes to the potential pool of projects, though only a small percentage of these would apply for credits in any fiscal year.

Residents – Residents are generally supportive of maintaining unique historic structures that define their neighborhoods.

State Treasury – The New Jersey State Treasury has opposed state historic preservation tax credits. The Treasury views tax credits as lost revenue, partly due to the fact that increased property taxes on completed projects go to municipalities and not the state. Potential counterarguments are that revenue from rehabilitation is not coming to New Jersey in the first place—real estate developers prefer to work on historic buildings in bordering states that offer the credit. New Jersey is losing out on this potential economic development.

BIBLIOGRAPHY

Clisham, Elaine, "From Empty Store to Downtown Anchor," New Jersey Future, (Trenton: 2016), http://www.njfuture.org/smart-growth-101/smart-growth-awards/2016-smart-growth-award-winners/hahne-building.

Corbalis, Jay, "Historic Preservation Tax Credit Awaits Governor's Signature," New Jersey Future, (Trenton: 2011), http://www.njfuture.org/2011/01/14/historic-preservation-tax-credit-awaits-governors-signature.

Cronyn, Joseph and Evans Paull, "Heritage Tax Credits: Maryland's Own Stimulus to Renovate Buildings for Productive Use and Create Jobs, an $8.53 Return on Every State Dollar Invested," The Abell Report, vol. 22 no. 1, (Baltimore: The Abell Foundation, 2009).

Delaware Historic Preservation Tax Credit Program. (Delaware, 2017). http://history.delaware.gov/preservation/taxcredit.shtml.

Everett, Rebecca, "Iconic factory to become luxury apartments, perhaps even with indoor pool," NJ.com, (2016), http://www.nj.com/burlington/index.ssf/2016/12/iconic_south_jersey_watch_case_factory_to_become_l.html.

Historic Tax Credit Coalition, "Prosperity Through Preservation: Historic Tax Credit Improvement Act of 2017," (Washington, DC: Historic Tax Credit Coalition).

Kuhlman, Renee. "State Historic Tax Credits: A Policy Brief on Return on State Investment." (Washington D.C.: National Trust for Historic Preservation, 2015).

Larisa Ortiz Associates and Urbanomics. Trenton Citywide Economic Market Study. (Trenton: 2014), p. 27, 58-9.

Peterson, Bob, Tim Schaffer, et al. "Report on the Ohio Historic Preservation Tax Credit." (Columbus: Tax Policy Study Commission, 2016).

Rutgers University, Center for Urban Policy Research. Annual Report on the Economic Impact of the Federal Historic Tax Credit for 2015. (New Brunswick: Rutgers, 2016).

Rypkema, Donovan D. and Caroline Cheong, "The Delaware Historic Preservation Tax Credit Program," (Washington, DC: PlaceEconomics: 2010).

Rypkema, Donovan D. and Katherine M. Wiehagen. "The Economic Benefits of Preserving Philadelphia's Past." (Philadelphia: Preservation Alliance for Greater Philadelphia, 1999).

Schwartz, Harry K. and Renee Kuhlman, "State Tax Credits for Historic Preservation: A Policy Report," (Washington, DC: National Trust for Historic Preservation, 2015).

Strunsky, Steve, "Hahne's building opening celebrated as a sign of Newark's rebirth," NJ.com, (2017), http://www.nj.com/essex/index.ssf/2017/01/hahnes_ribbon_cutting_in_newark_1.html.

ENDNOTES

1 Rutgers University, Center for Urban Policy Research, Annual Report on the Economic Impact of the Federal Historic Tax Credit for 2015. (New Brunswick: Rutgers, 2016), 5.

2 Corbalis, Jay, "Historic Preservation Tax Credit Awaits Governor's Signature," New Jersey Future, (Trenton: 2011), http://www.njfuture.org/2011/01/14/historic-preservation-tax-credit-awaits-governors-signature.

3 Rypkema, Donovan D. and Katherine M. Wiehagen, "The Economic Benefits of Preserving Philadelphia's Past." (Philadelphia: Preservation Alliance for Greater Philadelphia, 1999), 2."Historic Preservation Tax Credit." (PA Department of Community and Economic Development, 2017). http://dced.pa.gov/programs/historic-preservation-tax-credit-hptc.

4 "Historic Preservation Tax Credit." (PA Department of Community and Economic Development, 2017). http://dced.pa.gov/programs/historic-preservation-tax-credit-hptc.

5 Delaware Historic Preservation Tax Credit Program. (Delaware, 2017). http://history.delaware.gov/preservation/taxcredit.shtml.

6 Peterson, Bob, Tim Schaffer, et al., "Report on the Ohio Historic Preservation Tax Credit." (Columbus: Tax Policy Study Commission, 2016), 1-11.

7 Kuhlman, Renee, "State Historic Tax Credits: A Policy Brief on Return on State Investment." (Washington, DC: National Trust for Historic Preservation, 2015), 4-11.

8 Rypkema and Wiehagen, 2.

9 Cronyn, Joseph and Evans Paull, "Heritage Tax Credits: Maryland's Own Stimulus to Renovate Buildings for Productive Use and Create Jobs," The Abell Report, vol. 22 no. 1, (Baltimore: The Abell Foundation, 2009), 4.

10 Kuhlman, 7.

11 Listokin, David, Michael L. Lahr, et al. "Economic Benefit and Impact of Historic Rehabilitation Tax Credits in Kansas." (New Brunswick: Rutgers University, 2010), ii.

12 Historic Tax Credit Coalition, "Prosperity Through Preservation: Historic Tax Credit Improvement Act of 2017," (Washington, DC: Historic Tax Credit Coalition), 3.

13 Rypkema, Donovan D. and Caroline Cheong, "The Delaware Historic Preservation Tax Credit Program," (Washington, DC: PlaceEconomics: 2010), 5.

14 Listokin and Lahr, ii.

15 Ibid., 12

16 Rypkema and Wiehagen, 5-6.

17 Rypkema and Cheong, 11.

18 Cronyn and Paull, 3.

19 Rypkema and Wiehagen, 6.

20 Schwartz, Harry K. and Renee Kuhlman, "State Tax Credits for Historic Preservation: A Policy Report," (Washington, DC: National Trust for Historic Preservation, 2015), 11.

21 Historic Tax Credit Coalition, 2.

22 Schwartz and Kuhlman, 3

23 Ibid., 5-11.

24 Peterson, Schaffer, et al., 13.

25 Larisa Ortiz Associates and Urbanomics. Trenton Citywide Economic Market Study. (Trenton: 2014), p. 27, 58-9.

26 Clisham, Elaine, "From Empty Store to Downtown Anchor," New Jersey Future (Trenton: 2016), http://www.njfuture.org/smart-growth-101/smart-growth-awards/2016-smart-growth-award-winners/hahne-building.

27 Strunsky, Steve, "Hahne's building opening celebrated as a sign of Newark's rebirth," NJ.com (2017), http://www.nj.com/essex/index.ssf/2017/01/hahnes_ribbon_cutting_in_newark_1.html.

28 Everett, Rebecca, "Iconic factory to become luxury apartments, perhaps even with indoor pool," NJ.com (2016), http://www.nj.com/burlington/index.ssf/2016/12/iconic_south_jersey_watch_case_factory_to_become_l.html.

CONTACT:

Courtnay D. Mercer, PP, AICP
Director
Preservation New Jersey
PO Box 7815
West Trenton, NJ 08628
609-83-0881
cmercer@preservationnj.org
www.preservationnj.org

Emily Eckart
Development and Communications Associate
New Jersey Future
16 W. Lafayette Street
Trenton, NJ 08608
609-393-0008 x 113
eeckart@njfuture.org
www.njfuture.org