DEPARTMENT OF TAXATION
2018 Fiscal Impact Statement

1. Patron Jason S. Miyares

2. Bill Number HB 1363
House of Origin:
X **Introduced**
____ **Substitute**
____ **Engrossed**

Second House:
____ **In Committee**
____ **Substitute**
____ **Enrolled**

3. Committee House Finance

4. Title Historic Rehabilitation Tax Credit; Expands Availability of Credit for Projects for Schools

5. Summary/Purpose:

This bill would expand the Historic Rehabilitation Tax Credit by allowing taxpayers to claim credits for eligible expenses incurred in the rehabilitation of certain public schools.

This bill would be effective for historic rehabilitation projects certified by the Department of Historic Resources on and after January 1, 2018.

6. Budget amendment necessary: Yes.
Item(s): Item 374, Department of Historic Resources

6. Fiscal Impact Estimates are: Preliminary. (See Line 8.)
7a. Expenditure Impact:

Fiscal Year	***Dollars***	***Positions***	***Fund***
2017-18	$0	0	GF
2018-19	$70,110	1	GF
2019-20	$70,110	1	GF
2020-21	$70,110	1	GF
2021-22	$70,110	1	GF
2022-23	$70,110	1	GF
2023-24	$70,110	1	GF

8. Fiscal implications:

Administrative Costs

The Department of Taxation ("the Department") has not assigned any administrative costs to this bill because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, the Department considers implementation of this bill as "routine," and does not require additional funding.

The Department will provide specific administrative costs on any legislation that is not "routine." Additionally, the Department will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either house is unusually large, it is possible that additional resources will be required. If so, the Department will identify the costs at that time.

This bill would result in annual administrative costs to the Department of Historic Resources ("DHR") of $70,110 beginning in Fiscal Year 2019. DHR anticipates that this bill may result in a large influx of credit applications. Because current DHR staff would not be able to accommodate the increase in workload, the agency would need to hire an additional full-time employee to review credit applications. In addition, DHR may incur other administrative costs as a result of this bill.

Revenue Impact

This bill would result in an unknown negative General Fund revenue impact beginning in Fiscal Year 2019. School divisions are not generally subject to state income tax or other taxes against which Historic Rehabilitation Tax Credits could be claimed. The Department anticipates that there would be public-private partnerships formed between school divisions and private parties, where such parties would incur rehabilitation expenses eligible for the credit. It is unknown how many of these partnerships would be formed to rehabilitate public schools. There is currently no cap on the amount of Historic Rehabilitation Tax Credits that may be issued annually. The amount of credits claimed during the prior three fiscal years is shown in the table below.

Fiscal Year	Number of Returns	Amount	Average Per Return
2015	1,038	$97,998,279	$94,411
2016	1,095	$98,069,652	$89,561
2017	899	$87,762,096	$97,622

According to DHR, this bill could also result in an unknown non-General Fund revenue impact beginning in Fiscal Year 2019. Under current law, DHR charges fees for reviewing rehabilitation certification requests. These fees are based on the amount of rehabilitation costs incurred. For Fiscal Year 2017, fees from the Historic Rehabilitation Tax Credit program brought in revenue of $842,140. This bill would likely increase the number of projects but would also provide a lower cost threshold for purposes of qualifying for the credit for public school rehabilitation projects than what is otherwise permitted under current law. The non-General Fund revenue impact is uncertain because it is unknown how many applications would be submitted for public school projects and what the assessed value of such projects would be.

9. Specific agency or political subdivisions affected:

Department of Taxation
Department of Historic Resources

10. Technical amendment necessary: No.

11. Other comments:

Federal Historic Preservation Tax Credit

Under federal law, an investment tax credit is allowed to taxpayers for the rehabilitation of historic income-producing properties. The federal credit is equal to 20 percent of the cost of rehabilitating or preserving commercial, agricultural, industrial, or rental residential buildings that are certified as historic. The Historic Preservation Tax Credit is intended to reward private investors for investing in rehabilitating historic properties, such as abandoned or under-used schools, warehouses, factories, churches, retail stores, apartments, hotels, houses, and offices. Public Law 115-97, known as the “Tax Cuts and Jobs Act” ("the TCJA"), changes the Historic Preservation Tax Credit by providing that the federal credit is allowable ratably over a five-year period starting with the year the qualified rehabilitated building is placed in service.

Virginia’s Historic Rehabilitation Tax Credit

An individual, estate, trust, or corporation with eligible expenses in the rehabilitation of a certified historic structure is entitled to claim Virginia’s Historic Rehabilitation Tax Credit. The credit is equal to 25 percent of eligible rehabilitation expenses for projects completed in 2000. The credit may be claimed against individual, fiduciary, and corporate income taxes as well as the bank franchise tax, the insurance premium license tax, and the tax on public service corporations.

A "certified historic structure" is defined as a property listed individually on the Virginia Landmarks Register, or certified by the Director of DHR as contributing to the historic significance of a historic district that is listed on the Virginia Landmarks Register or certified by the Director of the Virginia Department of Historic Resources as meeting the criteria for listing on the Virginia Landmarks Register.

"Eligible rehabilitation expenses" is defined as expenses incurred in the material rehabilitation of a certified historic structure and added to the property's capital account.

"Material rehabilitation" is defined as improvements or reconstruction consistent with the Secretary of the Interior's Standards for Rehabilitation, the cost of which amounts to:

- At least 50 percent of the assessed value of such building for local real estate tax purposes for the year prior to the initial expenditure of any rehabilitation expenses; or

- For an owner-occupied building, at least 25 percent of the assessed value of such building for local real estate tax purposes for the year prior to the initial expenditure of any rehabilitation expenses.

To claim the credit, the taxpayer is required to apply to DHR, which is required to determine the amount of eligible rehabilitation expenses and issue a certificate to the taxpayer. The taxpayer is required to attach the certificate to the Virginia tax return on which the credit is claimed.

There is currently no cap on the amount of credits that may be issued annually. However, the credit claimed by any taxpayer for any taxable year may not exceed the lesser of:

- A taxpayer’s tax liability for the taxable year; or

- For taxable years beginning on and after January 1, 2017, but before January 1, 2019, $5 million.

If the amount of such credit exceeds either one of these limitations, the amount that exceeds such limitation may be carried over for credit against the taxes of such taxpayer in the next ten taxable years or until the full credit is used, whichever occurs first.

Proposed Legislation

This bill would expand the Historic Rehabilitation Tax Credit by allowing taxpayers to claim credits for eligible expenses incurred in the rehabilitation of certain public schools. This would be accomplished by modifying the definition of the terms "certified historic structure," "eligible rehabilitation expenses," and "material rehabilitation."

The term "certified historic structure" would be amended to include any public school in a school division in which at least half of the schools receive funding pursuant to federal law.

For the rehabilitation of a school or structure to be used as a school, the term, "eligible rehabilitation expenses," would be amended to include expenses incurred in the material rehabilitation of a certified historic structure regardless of whether the person who incurs such expenses owns such structure. For all projects other than rehabilitation of a school or structure to be used as a school, the term "eligible rehabilitation expenses" would retain its meaning under current law.

For buildings being rehabilitated that are schools, the term "material rehabilitation" would be amended to include improvements or reconstruction:

- Consistent with "The Secretary of the Interior's Standards for Rehabilitation" under federal law ("the federal standards"); and

- Which amounts to at least 10 percent of the assessed value of the building, as determined by the locality in which the school is located, for the year prior to the initial expenditure of any rehabilitation expenses.

Notwithstanding the federal standards, DHR would be required to consider a material rehabilitation to have met the requirement that a project be placed in a new use that requires minimal change to the defining characteristics of the building and its site and environment if the project is placed in use as a school.

This bill would be effective for historic rehabilitation projects certified by the Department of Historic Resources on and after January 1, 2018.

cc : Secretary of Finance