WRITTEN ONLY

TESTIMONY BY KALBERT K. YOUNG
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON VETERANS, MILITARY &
INTERNATIONAL AFFAIRS & CULTURE AND THE ARTS
ON
HOUSE BILL NO. 1422

February 6, 2013

RELATING TO HISTORIC STRUCTURES

House Bill No. 1422 establishes: 1) a historic preservation revolving fund into which shall be deposited appropriations made by the Legislature and counties, provided that, for each fiscal year, all legislative appropriations to the historic preservation revolving fund shall equal one-half of all county appropriations to the fund; and 2) a historic preservation income tax credit under Chapter 235, HRS, allowing the owners of historic structures to claim a tax credit for the rehabilitation of their historic properties.

The department does not support the creation of any revolving fund which does not meet the requirements of Section 37-52.3 of the HRS. Special or revolving funds should: 1) reflect a clear nexus between the benefits sought and charges made upon the users or beneficiaries of the program; 2) provide an appropriate means of financing for the program or activity; and 3) demonstrate the capacity to be financially self-sustaining. In regards to House Bill No. 1422, it is difficult to determine whether the proposed source of revenues will be self-sustaining.

I encourage the Legislature to scrutinize the fiscal and operational plan for this program to ensure that it does conform to the requirements of Section 37-52.3, HRS.

NEIL ABERCROMBIE
GOVERNOR OF HAWAII

WILLIAM J. AILA, JR.
CHAIRPERSON
BOARD OF LAND AND NATURAL RESOURCES
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CONSERVATION AND RESOURCES ENFORCEMENT
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HISTORIC PRESERVATION
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STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES
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Testimony of
WILLIAM J. AILA, JR.
Chairperson

Before the House Committee on
VETERANS, MILITARY & INTERNATIONAL AFFAIRS &
CULTURE AND THE ARTS

Wednesday, February 6, 2013
8:30 a.m.
State Capitol, Conference Room 312

In consideration of
HOUSE BILL 1422
RELATING TO HISTORIC STRUCTURES

House Bill 1422 proposes to create a historic preservation revolving fund for the purpose the historic preservation income tax credit under Chapter 235, Hawaii Revised Statutes. The historic preservation income tax credit would allow the owners of historic structures to claim a tax credit for the rehabilitation of their historic properties. Properties would have to be duly listed on the State or National Registers of Historic Places. **The Department of Land and Natural Resources (Department) supports this bill and provides the following recommendations for consideration**.

The Department requests clarification on whether the Legislature intends to include the rehabilitation of archaeological or cultural sites in the tax credit program. The Department suggests that archaeological sites and cultural site be included.

Further, the Department believes a source of funds for this tax credit should be identified, otherwise it is likely that while having a tax credit on the books, there will be no money to fund a tax credit. Such a contradictory situation will lead to further frustration with historic preservation in Hawaii rather than meet the goal of the bill, which is to promote historic preservation.

NEIL ABERCROMBIE
GOVERNOR

SHAN TSUTSUI
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To: The Honorable K. Mark Takai, Chair
and Members of the House Committee on Veterans, Military, & International Affairs, & Culture and the Arts

Date: Wednesday, February 6, 2013
Time: 8:30 a.m.
Place: Conference Room 312, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. 1422 Relating to Historic Preservation

The Department appreciates the intent of H.B.1422 and provides the following information and comments for your consideration.

H.B. 1422 creates a refundable tax credit against net income tax for expenditures made to rehabilitate a historic structure. The bill creates a revolving fund to fund the credit. The credit applies to tax years beginning after December 31, 2012.

To be eligible, structures must be listed on the Hawaii or national register of historic places or be located in and significant to a registered historic district. Qualified expenditures are limited to those expended on rehabilitation of a structure that is at least thirty per cent residential by square footage. The rationale for limiting expenditures to those expended on a residential structure is not stated.

H.B 1422 also requires that the taxpayer's rehabilitation projects and expenditures be certified by qualified staff of the State Historic Preservation Division and sets an aggregate cap for the credit. The Department has serious concerns regarding aggregate caps and allowing other agencies to certify tax credits. Issues arise when the certifying agency provides erroneous advice or wrongfully certifies the credit. In these cases, the Department is placed in a situation that is difficult to resolve.

The bill will also impose additional administration costs on the Department. The bill imposes two reporting requirements on the Department and requires the Department to develop an assessment tool for the credit. The current state of our computer system prevents the Department from reporting on information such as this tax credit if it were adopted.

In addition, the Department is required to develop rules and forms for administration of the credit. Since this a new tax credit that will require a significant amount of development to implement, the Department suggests that the tax credit could not be administered earlier than tax years beginning after December 31, 2013.

Thank you for the opportunity to provide comments.

HISTORIC HAWAI'I FOUNDATION

To: Rep. K. Mark Takai, Chair
Rep. Ken Ito, Vice Chair
Committee on Veterans, Military, & International Affairs, & Culture and the Arts

From: Kiersten Faulkner
Executive Director, Historic Hawai'i Foundation

Committee Date: Wednesday, February 6, 2013
8:30 a.m.
Conference Room 312

Subject: **HB 1422, Relating to Historic Structures**

On behalf of Historic Hawai'i Foundation (HHF), I am writing in support of HB 1422, which establishes a tax credit for qualifying rehabilitation expenses of historic structures and establishes a revolving fund administered by the state historic preservation division to fund the tax credit.

Since 1974, Historic Hawai'i Foundation has been a statewide leader for historic preservation. HHF's 850 members and numerous additional supporters work to preserve Hawaii's unique architectural and cultural heritage and believe that historic preservation is an important element in the present and future quality of life, economic viability and environmental sustainability of the state.

Historic preservation tax credit programs have proved to be successful incentives for rehabilitating older structures and returning them to useful life. Preserving and using our historic buildings are ways to enhance community character, provide an alternative to sprawl, create jobs, provide affordable housing, encourage heritage tourism, and generally spur economic development in older neighborhoods and commercial districts.

Tax credit programs have been used at the federal level and by almost two-thirds of the States. While the details of the programs vary state by state, preservation tax credits have universally been shown to be effective, especially when coupled with the 20% federal historic tax credit available to income-producing historic properties, such as commercial, office, industrial and resort properties. At the request of the Legislature in 2007, Historic Hawai'i Foundation released a study into the economic benefits realized by states that use a rehabilitation tax credit. The study found that the tax credits spurred economic development and increased direct tax revenues that offset the tax credit expense. Through increased economic output, the state recovers its investment in rehabilitation tax credits through four sources: construction period taxes, real property taxes, post-construction sales and income taxes.

Some 31 states have adopted laws creating credits against state taxes to provide incentives for the appropriate rehabilitation of historic buildings. Most programs include the following basic elements:

- Criteria establishing what buildings qualify for the credit;

- Standards to ensure that the rehabilitation preserves the historic and architectural character of the building;
- A method for calculating the value of the credit awarded, reflected as a percentage of the amount expended on that portion of the rehabilitation work that is approved as certified rehabilitation;
- A minimum amount, or threshold, required to be invested in the rehabilitation; and
- A mechanism for administering the program, general involving the state historic preservation office, and in some cases, the state department of revenue or of economic development.

HB1422 addresses each of these provisions, and also mirrors the qualifications and programs of the federal rehabilitation tax credit program. These technical elements help to ensure that the program can be administered with minimal new training or procedures, and that it is consistent with experience and best practices learned from other jurisdictions.

Many of the states that provide a historic preservation tax credit have conducted economic impact studies to determine the fiscal effect. All of them determined that the fiscal return was greater than the state's forgone taxes, often returning three to five times more revenue to the state in new taxes and significant new investment. The rehabilitation tax credit also was successful in creating new jobs, increasing loan demand and deposits in local financial institutions, enhancing property values and generating sales. In addition to these direct fiscal impacts, the tax credit also has proven benefits related to environmental sustainability, affordable housing, tourism and visitation, and neighborhood revitalization.

These tax credit programs help to return historic properties to tax rolls and generate employment and housing where they are needed most. State investments in tax credits can pay heavy dividends. For example, the Rhode Island historic preservation tax credit, passed in 2002, generated a total of $795 million in economic activity from an investment by the state of $145 million. The study, which was commissioned by Grow Smart Rhode Island, estimates that the state rehabilitation tax credit will add $242 million to the tax base of local communities and to generate a present value basis of $179 million in additional property tax revenue and $42 million in sales and income tax revenue.

As an incentive for reinvestment in our neighborhoods and communities, the historic property tax credit program makes sense. As an economic development program, it also makes fiscal sense for the state.

Therefore, Historic Hawai'i Foundation urges the Legislature to support HB1422.

L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Historic preservation tax credit

BILL NUMBER: HB 1422

INTRODUCED BY: McKelvey, Carroll, Evans, Hanohano, Morikawa, Nakashima, Tsuji and 1 Democrat

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers to claim a tax credit for the qualified rehabilitation expenses incurred to rehabilitate a historic structure. For each rehabilitation plan accepted by qualified staff of the state historic preservation division of the department of land and natural resources (DLNR), the credit shall be: (1) 25% of the projected qualified rehabilitation expenditures; or (2) 30% of the projected qualified rehabilitation plans if: (a) at least 20% of the units are rental units and qualify as affordable housing; or (b) at least 10% of the units are individual home ownership units and qualify as affordable housing.

The tax credit shall be available in the tax year in which the substantially rehabilitated historic structure is placed in service provided the tax credit shall be prorated for projects completed in phases.

Requires the qualified staff of the state historic preservation division to develop standards and criteria for the approval of certified historic structures for which the credit is sought. Requires the taxpayer to notify the state historic preservation division upon completion of the structure and submit documentation and certification of the costs incurred in rehabilitating the historic structure. The qualified staff of the state historic preservation division shall review the rehabilitation and verify its compliance with the rehabilitation plan.

Delineates how the credit is to be computed in the case of a partnership, S corporation, estate or trust. Stipulates that if a deduction is taken under section 179 of the IRC, no tax credit shall be allowed for the qualifying costs for which the deduction is taken.

Tax credits in excess of a taxpayer's income tax liability shall be refunded provided such amounts are over $1. Requires all claims for the credit to be filed on or before the twelfth month following the close of the taxable year for which the credit is claimed. Directs the director of taxation to prepare the necessary forms, require the furnishing of information to validate a claim for the credit, and adopt rules pursuant to HRS chapter 91.

Limits the aggregate amount of tax credits that may be claimed for qualified rehabilitation projects to $___ per year. Establishes recapture provisions. Directs the state historic preservation division, in consultation with the department of taxation, to annually determine the types of information necessary to enable a quantitative and qualitative assessment of the outcomes of an application for the tax credit. Requires the submission of a statement to the review board by the last day of the taxable year following the close of a tax year in which the qualified expenditures were expended. Failure to file the required statement shall result in the recapture of such credits. The statement submitted shall be a public document.

Requires the state historic preservation division, in consultation with the department of taxation, to submit a report annually evaluating the effectiveness of the tax credit.

Defines “certified historic structure,” “qualified rehabilitation expenditures,” “qualified staff of the state historic preservation division,” “rehabilitation plan,” and “substantial rehabilitation” for purposes of the measure.

Adds a new section to HRS chapter 6E to establish the historic preservation revolving fund which shall be expended for the historic preservation income tax credit provided that: (1) moneys in the fund equal to the total amount of historic preservation income tax credits approved in the previous year shall be paid to the credit of the general fund on an annual basis; (2) the director of taxation shall report annually to the state historic preservation division on the total amount of the historic preservation income tax credits approved in the previous year; and (3) the director of taxation and the state historic preservation division each may adopt rules pursuant to HRS chapter 91 to effectuate this section

EFFECTIVE DATE: Tax years beginning after December 31, 2012

STAFF COMMENTS: This measure proposes an incentive in the form of an income tax credit to encourage taxpayers to rehabilitate historic properties for mixed residential and nonresidential use in the state. While it appears that the credits are proposed on a prospective basis - that is, it would provide tax credits to the taxpayer based on the projected qualified rehabilitation expenditures prior to the rehabilitation of the historic property, the tax credits would only be available in the tax year the historic structure is placed in service.

Utilizing the tax system to accomplish social goals, such as this measure addresses, sets poor tax policy and cannot be justified. Note well, that the legislature is surrendering its oversight as to what will qualify for the tax credit to the state historic preservation division of DLNR, leaving the door wide open to whatever the board decides as guidelines to qualify as a historic structure. Given the track record of this division in recent years, one must ask why would the legislature allow a non-tax agency to determine whether not the taxpayer qualifies for a tax benefit?

To the extent that this measure would grant a preferential tax treatment because of circumstances unrelated to the imposition of the tax, the burden of the tax would be shifted to other taxpayers on an inequitable basis. If this measure is enacted, it would result in a public subsidy of costs incurred for historic preservation by a private taxpayer.

Again, tax credits are designed to alleviate some unusual burden of taxes such as the food excise tax credit which is designed to alleviate the general excise tax burden on essentials purchased by those in lower income categories. In the case of the proposed tax credit for historic preservation, there is no indication of a need for financial help, in fact, in order to claim the tax credit the taxpayer has to make the expenditures first before the credit can be claimed. And if those expenditures are of any substance, the taxpayer probably already has the ability to make those expenditures. At the county level where there are complete exemptions of such sites from the real property tax, a wealthy resident living a multimillion dollar valued historic home pays absolutely no real property taxes but benefits from the multitude of city services. Inasmuch as a tax benefit is already extended at the county level, one must question why another tax incentive is necessary at the state level.

If it is the intent of the legislature is to encourage and assist such rehabilitation of historic sites, then an appropriation of public funds subject to legislative review would be more appropriate. Even a no-interest, low-interest loan revolving fund would be more appropriate as the needs of the taxpayer and the kinds of improvements to be financed would be subject to an informed review.

Finally, with all of the proposals this session to raise additional revenues, one must ask why lawmakers deem it so important to provide yet another hand out of those tax dollars. From that perspective, this proposal represents nothing more than a shift of the tax burden to other taxpayers who are not so blessed with a historic structure. Taxpayers should realize that such targeted tax credits that are not based on need for tax relief amount to nothing more than an expenditure of public dollars albeit out the back door where there is no oversight and no public awareness.

Digested 2/5/13