



**Virginia  
Regulatory  
Town Hall**

**Proposed Regulation  
Agency Background Document**

<b>Agency Name:</b>	Department of Historic Resources
<b>VAC Chapter Number:</b>	17 VAC 10-30
<b>Regulation Title:</b>	Historic Rehabilitation Tax Credit
<b>Action Title:</b>	Proposed Regulations
<b>Date:</b>	October 2001

This information is required pursuant to the Administrative Process Act (§ 9-6.14:9.1 *et seq.* of the *Code of Virginia*), Executive Order Twenty-Five (98), Executive Order Fifty-Eight (99), and the *Virginia Register Form, Style and Procedure Manual*. Please refer to these sources for more information and other materials required to be submitted in the regulatory review package.

**Summary**

*Please provide a brief summary of the proposed new regulation, proposed amendments to an existing regulation, or the regulation proposed to be repealed. There is no need to state each provision or amendment or restate the purpose and intent of the regulation; instead give a summary of the regulatory action and alert the reader to all substantive matters or changes. If applicable, generally describe the existing regulation.*

Since the passage of the enabling legislation for the Virginia Historic Rehabilitation Tax Credit program in 1996, the Department of Historic Resources has been operating the program under draft regulations. The purpose of the current action (submission of the proposed regulations) is to formally implement these regulations. They will provide clear guidance to Virginia taxpayers about eligibility for the program, application requirements and procedures, review standards, appeal procedures, and coordination with the federal Certified Historic Rehabilitation program.

## Basis

*Please identify the state and/or federal source of legal authority to promulgate the regulation. The discussion of this statutory authority should: 1) describe its scope and the extent to which it is mandatory or discretionary; and 2) include a brief statement relating the content of the statutory authority to the specific regulation. In addition, where applicable, please describe the extent to which proposed changes exceed federal minimum requirements. Full citations of legal authority and, if available, web site addresses for locating the text of the cited authority must be provided. Please state that the Office of the Attorney General has certified that the agency has the statutory authority to promulgate the proposed regulation and that it comports with applicable state and/or federal law.*

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The Department of Historic Resources has specific statutory authority, and is mandated, under Va. Code §58.1-339.2 to promulgate regulations necessary to implement its review and certification of historic rehabilitation projects in order for those projects to receive state tax credits. The statute provides that the Director of the Department of Historic Resources shall establish by regulation the requirements needed for the program, including the fees to defray the necessary expenses and the extent to which the availability of the credit is coextensive with the availability of the federal rehabilitation tax credit. The Office of the Attorney General has certified that the agency has the statutory authority to promulgate the proposed regulations, and that they comport with applicable state law.

The statute is located at <http://leg1.state.va.us/cgi-bin/legp504.exe?000+cod+58.1-339.2>

## Purpose

*Please provide a statement explaining the need for the new or amended regulation. This statement must include the rationale or justification of the proposed regulatory action and detail the specific reasons it is essential to protect the health, safety or welfare of citizens. A statement of a general nature is not acceptable, particular rationales must be explicitly discussed. Please include a discussion of the goals of the proposal and the problems the proposal is intended to solve.*

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These regulations are mandated by state law, and will protect the health, safety, and welfare of the citizens of Virginia by providing a clear and understandable process for qualifying for and claiming historic rehabilitation tax credits, while also assuring that those credits are issued for projects that meet high criteria for historic significance, quality rehabilitation and public benefit. The rehabilitation of historic buildings benefits not only individual property owners, developers, and investors, but entire communities. Through the tax credit program, private dollars are invested in preservation, resulting in enormous public advantage. This money represents costs paid into the construction industry to architects, contractors, craftsmen, and suppliers, as well as to professionals in related fields such as banking, legal services, private consulting, and real estate. The capital improvement to the buildings can result in dramatic increases in local property taxes, enhanced commercial activity, and community revitalization. The rehabilitated buildings

provide needed housing (in many cases, low- and moderate-income housing), and office, retail, and other commercial space. Communities benefit from property improvement, blight removal, and increased occupancy of buildings in historic core neighborhoods.

## Substance

*Please identify and explain the new substantive provisions, the substantive changes to existing sections, or both where appropriate. Please note that a more detailed discussion is required under the statement providing detail of the regulatory action's changes.*

The proposed regulations set forth the requirements and procedures for obtaining the tax credit authorized by section 58.1-339.2 of the Virginia Code. The regulations address the following areas:

- Definitions
- Introduction to certifications of significance and rehabilitation
- Certifications of historic significance
- Standards for evaluating significance within registered historic districts
- Certifications of rehabilitation
- Standards for rehabilitation
- Appeals
- Fees for processing certification of rehabilitation requests
- Forms
- Definition of rehabilitation project
- Eligible rehabilitation expenses
- Qualification for credit
- Amount and timing of credit
- Entitlement to credit
- Transition rules for projects begun before 1977
- Coordination with the federal Certified Historic Rehabilitation program

## Issues

*Please provide a statement identifying the issues associated with the proposed regulatory action. The term "issues" means: 1) the primary advantages and disadvantages to the public, such as individual private citizens or businesses, of implementing the new or amended provisions; 2) the primary advantages and disadvantages to the agency or the Commonwealth; and 3) other pertinent matters of interest to the regulated community, government officials, and the public. If there are no disadvantages to the public or the Commonwealth, please include a sentence to that effect.*

1) The proposed state regulations parallel the well-established corresponding federal rehabilitation tax credit regulations to a large extent. Where they differ, it is primarily in ways that are advantageous to Virginia taxpayers. Advantages to the public include the following:

- The state credit, unlike the federal credit, is available to homeowners.
- The state credit is triggered by a different spending threshold than the federal credit. In order to qualify for the federal credit, rehabilitation expenditures must exceed the owner's adjusted basis in the building. In order to qualify for the state credit, rehabilitation expenditures for an income-producing building must be at least 50% of the locally assessed value of the building. This is usually a lower threshold, thus allowing property owners undertaking smaller rehabilitation projects to participate in the state program even if they are ineligible for the federal program.
- The federal credit is available only for properties that are individually listed on the historic register or are contributing structures in listed historic districts. The state program expands eligibility by allowing the credit for properties that are certified by the Director of the Department of Historic Resources as eligible for individual listing, even if they are not actually listed.
- The proposed state regulations, unlike the federal regulations, allow for disproportionate allocation of the credit among partners. This flexibility in the use of the credit will attract out-of-state investors and allow for more creative and innovative financing of projects. It will also result in nonprofit organizations being able to make use of the state credit by forming partnerships with investors.
- The submission requirements for state applications are somewhat less stringent than the submission requirements for federal applications. Most notably, the federal program requires that Part 1 of the application, the Request for Certification of Significance, be submitted prior to completion of the rehabilitation. This sometimes precludes owners whose rehabilitation work would otherwise qualify them for the credit from applying at all. The proposed state regulations require that all parts of the application be submitted within one year of completion of the rehabilitation work, thereby preventing denial of the credit for a technicality in the paperwork.

2) The primary advantage of this program to the agency is the opportunity to provide an incentive for the use of private investment to further the agency's mission to protect historic resources. Through this program property owners and developers are encouraged to do appropriate work on historic buildings so that they can remain in, or be returned to, useful service. Since 1977, over 900 historic Virginia buildings have been rehabilitated using the federal credit, representing private investment of nearly \$524 million. The state program has already resulted in over \$11 million in economic activity independent of the federal credit.

Another advantage to the agency is the opportunity to create an income stream through the use of fees for review and processing of projects. Details of the fee structure are listed below in the agency's statement on the fiscal impact of the program.

Because the implementation of the state tax credit has resulted in a considerable increase in the number of new projects submitted each year, the primary disadvantage to the agency is the rapidly growing workload in a time of budgetary stagnation and associated personnel shortages. Federal regulations require state reviewers to review and forward federal applications within 30 days of receipt. The proposed regulations also establish a 30-day target for review of projects. In addition, the program is growing in complexity and sophistication, and applicants expect Department staff to be able to provide increasingly complex guidance and technical assistance. Currently the Department has the equivalent of one full-time position and one part-time 1500-hour wage position dedicated to this program and charged against the program receipts. The

Department is seeking authorization of one additional nongeneral fund position, to assist with the workload created by the growing popularity and sophistication of the program.

Because the state tax credit could not be granted without clear and precise regulations governing eligibility of projects, and because participation in the program is limited to property owners who voluntarily choose to seek the credit, these regulations will not result in any disadvantage to the public or the Commonwealth.

### Fiscal Impact

*Please identify the anticipated fiscal impacts and at a minimum include: (a) the projected cost to the state to implement and enforce the proposed regulation, including (i) fund source / fund detail, (ii) budget activity with a cross-reference to program and subprogram, and (iii) a delineation of one-time versus on-going expenditures; (b) the projected cost of the regulation on localities; (c) a description of the individuals, businesses or other entities that are likely to be affected by the regulation; (d) the agency's best estimate of the number of such entities that will be affected; and e) the projected cost of the regulation for affected individuals, businesses, or other entities.*

(a) The Department of Historic Resources accounts for Virginia's Rehabilitation Tax Credit Program in under program 502 (Historic & Commemorative Attraction Management), subprogram 02 (Historic Structures Conservation & Assistance Services) and fund 0200 (special).

Currently DHR has the equivalent of one full-time position and one part-time 1500-hour wage position dedicated to the Tax Act Program work and charged against the program receipts (fund 0200). Soon, the Department expects approval of an additional full-time position to meet critical needs associated with the program. Salary costs for the new position are estimated to be \$58,250 annually and are considered "on-going. No one-time costs have been identified; however, any equipment, supply or travel needs that arise can and will be funded from program receipts (fund 0200).

Revenue impact and economic implications: The credit claimed by applicants for certified rehabilitations is 25% of eligible rehabilitation expenses. The impact on state revenue is therefore a direct function of how many projects are submitted and approved in a given year. Direct impacts on revenue, however, are more than offset by economic benefits attributable to rehabilitation projects. Because rehabilitation projects tend to be labor-intensive, they generally create more jobs than new construction projects of comparable size. In addition to construction industry jobs, rehabilitation projects create jobs for architects and consultants, and in the financial, legal, and real estate industries. Studies have shown that \$1 million spent in rehabilitating old buildings creates 15.6 construction jobs and 14.21 ancillary jobs -- 3.4 more jobs than \$1 million spent in new construction. Moreover, \$1 million spent in rehabilitation adds \$779,800 to household incomes -- \$53,000 more than \$1 million spent on new construction. For projects completed in 2000, \$108.3 million in rehabilitation costs were certified. This translates to over 3,200 jobs for Virginians, and \$84.5 million in household income. Studies have also shown that rehabilitation projects often result in increased retail and new business activity, that the economic benefits of rehabilitation projects tend to be locally concentrated, and that historic

preservation projects can stabilize local economies during economically volatile times. The revitalization of blighted areas can reduce crime and vandalism, and increase the local property tax base. Because rehabilitation tax credits are often combined with low income housing tax credits, they contribute to the preservation and enhancement of the Commonwealth’s housing stock – particularly for low- and middle- income citizens. In addition, because the state tax credit can be combined with the federal tax credit, and because the disproportionate allocation provisions of the state credit make it a flexible and useful financing device, out-of-state investors are increasingly seeking opportunities to become involved in Virginia projects. Although these economic benefits are difficult to quantify, they clearly result in considerable financial advantage to Virginia.

It is also important to note that the Commonwealth provides economic support for historic preservation in two ways: through direct grants to non-profit organizations and local governments, and through these rehabilitation tax credits to private taxpayers. The General Assembly grant program makes possible many worthy projects, but also results in long-term obligations for public resources. Properties which are rehabilitated using tax credits remain on the local tax rolls, require no public commitment for long-term maintenance, and remain in the private sector as examples of history and heritage in everyday places. Use of the tax credits leverages private investment, resulting in significant public benefit at minimal public cost.

(b) These regulations will result in no cost to localities, and indeed, will likely result in long-term revenue enhancement through improvements to local tax bases.

(c) The only individuals, businesses, or other entities that will be affected by these regulations are applicants voluntarily seeking certification of their projects.

(d) Since 1997, as the state credit has been phased in and as property owners, developers, and investors have learned of the program, the number of projects submitted has increased every year. The following chart summarizes the growth of the program:

Year	Number of new projects seeking state credit only	Number of new projects seeking both state and federal credits
1997	6	80
1998	11	67
1999	26	99
2000	16	122

Although the number of new projects can be expected to vary with such factors as the strength of the economy, interest rates, and investor confidence, it is anticipated that the program will continue to grow.

(e) As authorized by state law, the Department charges fees for review of state tax credit applications in order to cover processing costs. No fee is charged for review of Part 1. Fees for Parts 2 and 3 are charged in accordance with the following schedules:

Rehabilitation Costs	Part 2 Review Fee	Part 3 Review Fee
Less than \$50,000	Fee waived	\$100
\$50,000 - \$99,999	\$250	\$250
\$100,000 - \$499,999	\$400	\$400
\$500,000 - \$999,999	\$750	\$750
\$1 million or more	\$1,500	\$1,500

## Detail of Changes

*Please detail any changes, other than strictly editorial changes, that are being proposed. Please detail new substantive provisions, all substantive changes to existing sections, or both where appropriate. This statement should provide a section-by-section description - or cross-walk - of changes implemented by the proposed regulatory action. Where applicable, include citations to the specific sections of an existing regulation being amended and explain the consequences of the proposed changes.*

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The Department of Historic Resources has been administering the Rehabilitation Tax Credit program under draft regulations since passage of the enabling legislation. The draft regulations have been available upon request from the Department, and were published with the NOIRA. Aside from editorial clarifications, the proposed regulations make few changes to the draft regulations. The substantive changes are as follows:

§1 Definitions. Includes the following new definitions:

“Completion year” means the calendar year in which the last eligible rehabilitation expense is incurred or the final certificate of occupancy (if appropriate) is issued.

“Eligible Rehabilitation Expenses” means expenses incurred in the material rehabilitation of a certified historic structure and added to the property's capital account.

“Material rehabilitation” means improvements or reconstruction consistent with “The Secretary of the Interior's Standards for Rehabilitation,” the cost of which amounts to at least fifty percent of the assessed value of the building for local real estate tax purposes for the year prior to the initial expenditure of any rehabilitation expenses, unless the building is an owner-occupied building, in which case the cost shall amount to at least twenty-five 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. Material rehabilitation does not include enlargement or new construction.

“Owner-occupied building” means any building, at least 75% of which is used as a personal residence by the owner, or which is available for occupancy by the owner for at least 75% of the year.

“Plan of Rehabilitation” means a plan pursuant to which a certified historic structure will be materially rehabilitated.

“Start of Rehabilitation” means the date upon which the taxpayer applies for the building permit for the work contemplated by the plan of rehabilitation, or the date upon which actual work contemplated by the plan of rehabilitation begins.

§3 Certifications of Historic Significance. Includes a new section allowing for submission of Part 1 by an applicant who is not the owner of the building, provided a signed acknowledgement from the owner is included. This will allow for certifications of significance by a potential purchaser of a building.

§5 Certifications of Rehabilitation. A. Adds a requirement that information submitted with Part 3 of the application include the assessed value of the building in the year preceding the start of the rehabilitation.

B. Adds a requirement that each rehabilitation be completed in accordance with a plan of rehabilitation which provides the Department with sufficient information to determine whether the rehabilitation qualifies for certification, and affirmatively placing the burden on the applicant to provide sufficient information for the Department to make a determination.

F. (Formerly subsection E) Deletes provision allowing for revocation of certification if an applicant makes unauthorized changes in property following issuance of certification.

§10 Definition of Rehabilitation Project. For phased projects, allows submission of a phasing plan contemporaneously with submission of Part 2 of the application rather than before physical work on the rehabilitation begins. For the federal credit, the IRS requires that the election to phase a project be made before work actually begins. This requirement contemplates large-scale rehabilitations where the threshold spending requirements are too great to be met in a 2-year period. This requirement, however, is proving to be too strict for many homeowners seeking the state credit, who don't hear about the credit or fail to submit their applications until work has already begun.

§11 Eligible Rehabilitation Expenses. B. Allows for inclusion of all rehabilitation expenses from the start of rehabilitation to completion of rehabilitation. Deletes provisions effectively limiting the credit to expenses incurred during a three-year period.

F. Requires a lease term of at least five years where a landlord elects to pass the credit through to a tenant or tenants.

§13 Amount and Timing of Credit. Deletes the phase-in provisions that specified the percentage of eligible rehabilitation expenses that could be taken as a credit between 1997 and 2000. All applications which will be submitted to the Department after these regulations become final will be eligible for the 25% credit.

§15 Transition Rules for Projects Begun Before 1997. Deletes the one-time transfer provision which was added to the draft regulations as an equity and reliance measure for multi-year projects which were initiated before 1998 legislative changes.

## Alternatives

*Please describe the specific alternatives to the proposal considered and the rationale used by the agency to select the least burdensome or intrusive alternative that meets the essential purpose of the action.*

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There is no feasible alternative to promulgating these regulations. The regulations are mandated by state law, and they are necessary to provide clear guidance and an efficient procedure for qualifying for and claiming the tax credit. Therefore, the Department has not considered any alternatives.



**Public Comment**

*Please summarize all public comment received during the NOIRA comment period and provide the agency response.*

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No public comments were received during the NOIRA period.

**Clarity of the Regulation**

*Please provide a statement indicating that the agency, through examination of the regulation and relevant public comments, has determined that the regulation is clearly written and easily understandable by the individuals and entities affected.*

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A multi-disciplinary committee composed of representatives from both the public and private sectors established the draft regulations under which this program has been administered. The draft regulations were based on the corresponding federal regulations, but were reorganized and worded for maximum clarity and accessibility. Although no formal public comment was received during the NOIRA period, informal comments and citizen participation in the program have indicated that the draft regulations were clear and easily understandable. To the extent that questions or ambiguities were identified in the draft regulations, they have been addressed in the proposed regulations.

**Periodic Review**

*Please supply a schedule setting forth when the agency will initiate a review and re-evaluation to determine if the regulation should be continued, amended, or terminated. The specific and measurable regulatory goals should be outlined with this schedule. The review shall take place no later than three years after the proposed regulation is expected to be effective.*

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These regulations will be reviewed and re-evaluated no later than three years after they become effective to ensure that they are as clear and understandable as possible, and that there are no less burdensome alternatives to their continued effectiveness.

**Family Impact Statement**

*Please provide an analysis of the proposed regulatory action that assesses the potential impact on the institution of the family and family stability including the extent to which the regulatory action will: 1) strengthen or erode the authority and rights of parents in the education, nurturing, and supervision of their children; 2) encourage or discourage economic self-sufficiency, self-pride, and the assumption of responsibility for oneself, one's spouse, and one's children and/or elderly parents; 3) strengthen or erode the marital commitment; and 4) increase or decrease disposable family income.*

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Rehabilitation of historic buildings results in, among other benefits, improved housing stock, preservation of neighborhoods, and enhanced property values. In many cases, the historic rehabilitation tax credits are combined with low-income housing tax credits, resulting in increased housing for low and moderate income families. The Virginia credit, unlike the corresponding federal rehabilitation tax credit, is available for owner-occupied buildings. This creates a financial incentive for homeowners to improve their property, resulting in a positive influence for families.

1. This program will not directly affect the authority and rights of parents with regard to the education, nurturing, or supervision of their children.
2. This program will encourage economic self-sufficiency, self-pride, and the assumption of responsibility for oneself and one's family by providing a financial incentive to homeowners to rehabilitate and improve their property and the community in which they live.
3. This program will not directly affect marital commitments.
4. This program will have a positive effect on disposable family income, not only by allowing homeowners to take advantage of the credits, but also by enhancing economic activity in general through money paid into the construction industry and related fields such as real estate, law, and banking, and by enhancing retail and business activity.