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STATE OF HAWAII
DEPARTMENT OF TAXATION

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To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: Wednesday, April 3, 2019
Time: 2:00 P.M.
Place: Conference Room 308, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 1394, S.D. 2, H.D. 1, Relating to Historic Preservation

The Department of Taxation (Department) offers the following comments regarding S.B. 1394, S.D. 2, H.D. 1, for the Committee's consideration.

S.B. 1394, S.D. 2, H.D. 1, establishes a new nonrefundable tax credit for taxpayers who rehabilitate historic structures pursuant to a rehabilitation plan certified by the Department of Land and Natural Resources' State Historic Preservation Division (SHPD). A summary of key provisions are as follows:

- Adds a new section to Hawaii Revised Statutes (HRS) chapter 235, creating a nonrefundable tax credit for qualified expenses incurred as part of rehabilitation of a historic structure certified by the SHPD;
- Sets the amount of the credit at 30% of the qualified expenses;
- Allows unused credit to be carried forward until exhausted, or for ten years, whichever is earlier.
- Requires the SHPD to develop rules for the approval of rehabilitation plans;
- Requires owners of certified historic structures to notify the SHPD when the rehabilitation has been completed and requires the SHPD to review the rehabilitation and verify that it has been completed in accordance with the approved rehabilitation plan;
- Creates an unspecified aggregate cap on the total amount of credits that may be claimed for qualified rehabilitation projects;
- Requires SHPD, in consultation with the Department, to determine the information necessary to enable a quantitative and qualitative assessment of the outcomes of the tax credit to be determined.
- Requires taxpayers to submit a written, certified statement to the SHPD containing their

qualified rehabilitation expenses and any other information the SHPD or the Department may require;

- Specifies that all information submitted in the statement to SHPD by taxpayers claiming the credit is public information.
- Provides for recapture of the tax credit if the projected expenditures do not materialize, the rehabilitation plans do not proceed in a timely manner or in accordance with the approved plan, or the amount of affordable units differs from the projected amount;
- Requires the SHPD, in consultation with the Department, submit an annual report to the Legislature;
- Authorizes the Director of Taxation to require proof of the claim for the tax credit; and
- Has a defective effective date of January 1, 2050.

The Department notes that the Senate made numerous changes to this measure at the Department's recommendation. The Department appreciates the consideration of its testimony and notes that it can administer this measure as drafted, provided a functional effective date is inserted. If a functional effective date is inserted, the Department respectfully requests that it be made no earlier than taxable years beginning after December 31, 2019. This effective date will provide the Department sufficient time to make the necessary form, instructions, and computer system changes.

Thank you for the opportunity to provide comments.

DAVID Y. IGE
GOVERNOR OF
HAWAII

SUZANNE D. CASE
CHAIRPERSON
BOARD OF LAND AND NATURAL RESOURCES
COMMISSION ON WATER RESOURCE MANAGEMENT

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STATE PARKS

STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES

POST OFFICE BOX 621
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Testimony of
SUZANNE D. CASE
Chairperson

Before the House Committee on
FINANCE

Wednesday, April 3, 2019
2:00 PM
State Capitol, Conference Room 308

In consideration of
SENATE BILL 1394, SENATE DRAFT 2, HOUSE DRAFT 1
RELATING TO HISTORIC PRESERVATION

Senate Bill 1394, Senate Draft 2, House Draft 1 proposes to amend Chapter 235, Hawaii Revised Statutes (HRS), creating a tax credit for certified rehabilitation of certified historic buildings. **The Department of Land and Natural Resources (Department) supports this measure and offer comments.**

Tax incentives for rehabilitation of historic buildings have been proven to be enormously effective in preserving important buildings, ensuring their continuing economic viability, revitalizing communities, especially historic downtowns, preserving community character, and promoting heritage tourism. The Department believes that tax credit programs such as this can make an important contribution to the comprehensive State Historic Preservation Program established by Chapter 6E, HRS.

In its 2018 report on the federal historic tax credit program, the National Park Service (NPS) prepared in collaboration with Rutgers University (copy attached for your reference), notes that NPS certified 1,035 completed historic rehabilitation projects. The report documents $6.5 billion in rehabilitation investment during federal fiscal year 2017 (the last year for which figures are available), helped create 106,900 jobs, and $6.2 billion of gross domestic product.

If this measure is enacted, Hawaii will join the 38 states that already provide tax credits for the rehabilitation of historic structures. The nature of each state program is different, so it is difficult to extract information from them that could be directly useful in evaluating the effect of the program proposed in this measure. All states report that their programs are successful both in giving new life and continuing utility to significant historic structures, leveraging private investment at between $4 and $5 per tax credit dollar, contributing significant positive economic impact to affected communities…. At between 4 and 9 years, depending on the state and the level of the credit, generating revenue to the state exceeding the decrease in revenue due to the tax credit. Since the credit is paid out after the project is completed, the revenue payback begins from taxes on wages, goods, and services, before the credit is claimed.

Thank you for the opportunity to comment on this matter.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Historic Preservation Tax Credit

BILL NUMBER: SB 1394, HD-1

INTRODUCED BY: Senate Committee on Ways & Means

EXECUTIVE SUMMARY: Establishes a nonrefundable tax credit based on the qualified rehabilitation expenses of a historic structure. The adoption of this credit would provide tax relief to taxpayers regardless of their need for tax relief. It also would shift the burden of paying for government to the rest of us.

SYNOPSIS: Adds a new section to HRS chapter 235 to allow a credit for rehabilitation of a certified historic property that is certified by the historic preservation division of DLNR.

The credit is to be 30% of the qualified rehabilitation expenditures.

The credit is available in the taxable year in which the substantially rehabilitated structure is placed into service. If completed in phases, the tax credit shall be prorated to the identifiable portion of the building placed into service during that taxable year.

Tax credits that exceed the taxpayer's income tax liability may be carried forward up to 10 years.

The basis of eligible property for depreciation or accelerated cost recovery system purposes for state income taxes shall be reduced by the amount of credit allowable and claimed. In the alternative, the taxpayer shall treat the amount of the credit allowable and claimed as a taxable income item for the taxable year in which it is properly recognized under the method of accounting used to compute taxable income.

For a partnership, S corporation, estate, or trust, the cost upon which the credit is computed shall be determined at the entity level and the distribution and share of the tax credit shall be determined pursuant to section 704(b) of the Internal Revenue Code.

Requires the director of taxation to prepare any forms necessary to claim a credit, may require a taxpayer to furnish reasonable information to validate a claim for the credit, and adopt rules pursuant to HRS chapter 91. Requires claims for the credit, including any amended claims, to be filed on or before the end of the twelfth month following the taxable year for which the credit is claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the tax credit.

The aggregate amount of tax credits claimed shall not exceed $_____ for the 2020 tax year, $_____ for the 2021 tax year, $_____ for the 2022 tax year, $_____ for the 2023 tax year, and $_____ for the 2024 tax year and every year thereafter.

Provides that following the completion of rehabilitation of a certified historic structure, the owner shall notify the state historic preservation division that the rehabilitation has been completed. The owner shall provide the state historic preservation division with documentation of the costs incurred in rehabilitating the historic structure and shall submit certification of the costs incurred in rehabilitating the historic structure. The state historic preservation division shall review the rehabilitation and verify that the rehabilitation project complied with the rehabilitation plan. The administrator of the state historic preservation division shall certify in writing that the rehabilitation has been completed in accordance with the approved rehabilitation plan, and provide that certification to both the project proponent and the director of taxation.

Provides that each taxpayer claiming this credit shall, no later than the last day of the taxable year following the close of the tax year in which qualified costs were expended, submit a written, certified statement to the state historic preservation division containing the qualified rehabilitation expenditures incurred by the taxpayer and any other information the state historic preservation division or department of taxation may require. If this information is not submitted, the taxpayer shall not be eligible to receive the tax credit for those expenses, and any credit already claimed for that taxable year shall be recaptured in total. A recaptured tax credit shall be added to the taxpayer's tax liability for the taxable year in which the recapture occurs.

Provides for recapture of a previously claimed tax credit if any of the following occur: (1) the projected qualified expenditures do not materialize; (2) the qualified rehabilitation plans do not proceed in a timely manner and in accordance with the approved plans. Also provides that recapture shall occur if the department of land and natural resources notifies the department of taxation that the taxpayer has failed to comply with the law or its related rules promulgated by the state historic preservation division.

Defines “qualified rehabilitation expenditures” as any costs incurred for the physical construction involved in the certified rehabilitation of a certified historic structure; provided that for projects involving mixed residential and non-residential uses, at least thirty per cent of the total square footage of the rehabilitation is placed into service for residential use. “Qualified rehabilitation expenditures” shall not include the owner's personal labor.

Defines “rehabilitation plan” as any construction plans and specification for the proposed rehabilitation of a historic structure in sufficient detail for evaluation of compliance with the rules adopted by the state historic preservation division.

Defines “substantial rehabilitation” as the qualified rehabilitation expenditures of a historic structure that exceed twenty-five per cent of the assessed value of the structure.

EFFECTIVE DATE: July 1, 2050.

STAFF COMMENTS: Lawmakers need to keep in mind two things. First, the tax system is the device that raises the money that they, lawmakers, like to spend. Using the tax system to shape social policy merely throws the revenue raising system out of whack, making the system less than reliable as there is no way to determine how many taxpayers will avail themselves of the credit and in what amount. The second point to remember about tax credits is that they are nothing more than the expenditure of public dollars, but out the back door. If, in fact, these dollars were subject to the appropriation process, would taxpayers be as generous about the expenditure of these funds when our kids are roasting in the public school classrooms, there isn’t enough money for social service programs, or our state hospitals are on the verge of collapse?

If lawmakers want to subsidize the rehabilitation of certified historic buildings, then a direct appropriation would be more accountable and transparent.

Furthermore, the additional credit would require changes to tax forms and instructions, reprogramming, staff training, and other costs that could be massive in amount. A direct appropriation may be a far less costly method to accomplish the same thing.

Finally, the credit is directed to persons who might have no need for financial assistance.

Technical changes that are needed in the bill as it is now drafted include the following:

- There is no longer a need for (k)(1) because projected qualified expenditures are no longer creditable (they were in some prior drafts of this bill). Recapture condition (k)(2) is difficult to verify. Consider changing subsection (k) to the following:

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(k)  Any credit under this section shall be recaptured
following the close of the taxable year for which the credit
is claimed if the department of land and natural resources
notifies the department that the taxpayer has failed to comply
with the requirements of this section or its related rules
promulgated by the state historic preservation division.
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Digested 4/1/2019

HISTORIC HAWAI'I FOUNDATION

TO: Rep. Sylvia Luke, Chair
Rep. Ty J.K. Cullen, Vice Chair
Committee on Finance

FROM: Kiersten Faulkner, Executive Director
Historic Hawaii Foundation

Committee: Wednesday, April 3, 2019
2:00 p.m..
Conference Room 308

RE: **SB 1394 SD2 HD1, Relating to Historic Preservation**

On behalf of Historic Hawaii Foundation, I am writing in **support for SB 1394 SD2 HD1.** The bill would establish a historic preservation tax credit for qualified construction expenses incurred in rehabilitation of historic structures.

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

The bill would provide this important incentive to developers, property owners and financial institutions involved in preserving historic buildings and providing affordable housing.

Tax credit programs for rehabilitation of historic properties have been used at the federal level and by 38 other States that have adopted laws creating credits against state taxes to provide incentives for the appropriate rehabilitation of historic buildings. 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 federal historic tax credit available to income-producing historic properties.

National studies have found that historic rehabilitation 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.

Most programs include the following basic elements: criteria establishing which 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, generally involving the state historic preservation office and the state department of taxation. This bill includes all of these elements.

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.

Since 1974, Historic Hawaiʻi Foundation has been a statewide leader for historic preservation. Its members and 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.

Therefore, Historic Hawaiʻi Foundation supports SB 1394 SD2 HD1.

LATE

To:
Rep. Sylvia Luke, Chair
Rep. Ty J.K. Cullen, Vice Chair
Committee on Finance

From: Edmont P. D'Ascoli
Email: edas@hawaii.rr.com
Tel: 808-799-9135

Committee: Wednesday, April 3, 2019, 2:00 p.m.
Conference Room 308

Re: SB 1394, Relating to Historic Preservation

I am writing in support of SB 1394. In 2016 our family completed a restoration of a building in Chinatown, 75 N. King St., under the National Parks Service Tax Incentive Program. The tax credit enabled us to do a complete restoration including utility upgrades and emergency easement that were not available on the street front that allowed the fullest potential of the commercial property. With the Federal Tax Credit the project was not financially beneficial as an investment. Our passion for historic buildings is what was the deciding factor. Other property owners may not have the same passion however with the State also providing a tax credit the project would have been worth it as a financial investment.

Below are the numbers from our project. In addition which is not stated are the resulting employment from businesses being able to operate from a restored property that would not have been able to accommodate before restoration.

$ 4,000. GET approximately $4,700 generated from before property purchased

After purchase of property

$273,343.	Restoration materials/equipment
$618,584.	Restoration professional services/labor
$891,907.	Restoration total cost
$ 38,330.*	Restoration GET
$375,000.	Tenant Build-out materials/equipment
$225,000.	Tenant Build-out professional services/labor
$600,000.	Tenant Build-out total cost
$ 25,785.*	Tenant Build-out GET
$ 5,035.	2017 GET from tenant's rent
$ 13,393.	2018 GET from tenant's rent
$128,185.	Tenant 2017 GET from operation sales

$133,694.	Tenant 2018 GET from operation sales
$ 3,548.*	Tenant 2017 GET from operation vendor purchases
$ 3,713.*	Tenant 2018 GET from operation vendor purchases
$351,683.	Total GET generated in 3 years.

* Close Estimates.

With the states 25% tax credit for commercial property the return on investment is quick and substantial with longevity. It is important that the tax credit to be taken in one fiscal year as an incentive to do a proper build-out. Historic areas are most challenging due to the conditions of the building, access, surrounding area and in many historic areas lack of utilities.

We am currently restoring another property in the Capitol District with similar use and numbers. In my experience the GET and employment generated is not unique to one property but attainable with commercial properties within Historic Districts.

LAND USE RESEARCH
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LATE

April 3, 2019

Representative Sylvia Luke, Chair
Representative Ty J.K Cullen, Vice Chair
House Committee on Finance

Comments in Strong Support of SB 1394, SD2. HD1 Relating to Historic Preservation (Establishes a historic preservation tax credit. Appropriates funds for one temporary position to assist with the establishment and administration of the Hawaii historic preservation income tax credit program.)

FIN Hrg: Wednesday, April 3, 2019 at 2:00 p.m. in Conf. Rm. 308

The Land Use Research Foundation of Hawaii (LURF) is a private, non-profit research and trade association whose members include major Hawaii landowners, developers, resort operators and utility companies. LURF's mission is to advocate for reasonable, rational and equitable land use planning, legislation and regulations that encourage well-planned economic growth and development, while safeguarding Hawaii's significant natural and cultural resources, and public health and safety.

LURF appreciates the opportunity to provide comments in **strong support of SB 1394, SD2, HD1.**

SB 1394, SD2, HD1. This bill establishes a historic preservation tax credit for qualified construction expenses incurred in rehabilitation of historic structures; and appropriates funds for one temporary position to assist with the establishment and administration of the Hawaii historic preservation income tax credit program.

LURF's Position. LURF members maintain and are stewards of historic properties and structures. LURF and its members believe that preserving and appropriately using historic structures are ways to maintain and enhance a living display of Hawaii's history and community character, and also, in some cases, encourage heritage tourism.

Tax credit programs to encourage historic preservation have proven to be successful incentives for rehabilitating historic structures and returning them to useful life.

Logical changes to existing laws such as the historic preservation tax credit proposed by this bill are therefore significant, necessary and should be welcomed as a method to assist with the preservation of historic structures. This seemingly small tax credit measure has the potential to result in substantial and positive impacts on the preservation of historic structures, as well as supporting the local construction industry and advancing the State's economy and general welfare.

For these reasons, LURF is in **strong support of SB 1394, SD2, HD1**, and respectfully urges your favorable consideration.

Thank you for the opportunity to provide comments relating to this measure.