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Historic Structure Rehabilitation Credit

To encourage preservation of historic buildings, Minnesota allows tax credits (or grants in lieu of the credit) to individuals and entities that spend substantial amounts rehabilitating qualifying buildings. This credit and grant program ("Historic Structure Rehabilitation Credit" or "Historic Credit") mirrors the similar federal income tax credit and is administered in much the same way. The program was enacted in 2010 and is scheduled to expire after fiscal year 2021.

What projects qualify for credits or grants?

To qualify for a credit or grant, the project must also qualify for the federal tax credit. That requires projects to:

- rehabilitate a building that is certified as a historic structure by the National Park Service (NPS)—i.e., the building either must be on the national register or be certified as contributing to a registered historic district;
- be an income-producing property (e.g., rental housing qualifies but owner-occupied residences do not); and
- spend "substantial" amounts on rehabilitation that meets NPS standards.

What is the credit rate?

The credit rate is 20 percent. (The federal credit rate is also 20 percent, so the combined state and federal credit can equal up to 40 percent of qualifying expenses.) The grant in lieu of the credit equals 90 percent of the credit, so its effective rate is 18 percent (20% * 90% = 18%). No maximum or "cap" applies.

What expenses qualify for the credit?

The credit applies to expenditures to rehabilitate a qualifying building. The amount spent must be substantial, which federal law defines as the greater of (1) $5,000 or (2) the tax basis of the property. The credit cannot be used to pay for:

- acquiring the property;
- personal property (e.g., equipment that doesn't become part of the building);
- enlargement or expansion of the building; or
- site work.

Who administers the credit and what actions must taxpayers take to qualify?

The federal and state credits are jointly administered by the tax administrators (the federal Internal Revenue Service and Minnesota Department of Revenue) and the agencies responsible for historic preservation (NPS and Minnesota State Historic Preservation Office or SHPO). To receive the tax credits or grants, projects must go through a multi-part certification process administered by SHPO and NPS. This process generally must begin before work starts on the project. Credits are paid only after completion of work and when the project is "placed in service." Detail on these processes (for both the federal and Minnesota credits) is available on the websites of the NPS and Minnesota Historical Society.

Which taxes are the credits allowed against?

The Minnesota credit is allowed against any of the following taxes: the individual income, corporate franchise, or insurance premiums taxes. The credit is refundable and the taxpayer may assign or sell the credit (once) to another individual or entity.

How do the federal and state credits affect calculation of federal and state taxes?

The federal and state credits are direct subtractions from tax liability, so they provide a dollar-for-dollar reduction in tax liability under the respective federal and state taxes. (Because the Minnesota credit is refundable, the full amount is paid regardless of the amount of the tax liability.) Allowance of the credit also has other effects on calculation of tax. Federal law provides that the federal credit reduces tax basis and that straight-line (rather than accelerated) depreciation must be used for the project. These rules flow through to calculation of Minnesota individual or corporate tax and result in some of the apparent benefit of the credit being offset by a reduction in tax benefits available to similar real estate investments that are not allowed the credit.

In addition, because state income taxes are deductible (e.g., as business expenses) by real estate investors, federal income tax will rise as a result of allowance of the state credit—in effect, the state credit increases federal tax.

What is the purpose of the grant option?

The Minnesota program allows projects to claim a grant (equal to 90 percent of the credit amount) instead of a credit. The grant is paid by the Minnesota Historical Society and no differences in qualifying rules apply to a grant versus a tax credit. The grant may be paid to an entity other than a taxpayer. The grant option allows projects involving tax-exempt entities an option for avoiding the indirect federal income tax on state tax credits, as described above. How successful the grant is in minimizing federal tax on projects is unclear, since the federal tax treatment of the grants is somewhat uncertain.

What is the fiscal impact of the program?

The table shows Minnesota Management Budget's forecast of the tax credit and the grant-in-lieu-of-credit amounts for fiscal year 2014 through fiscal year 2019 for the November 2016 revenue forecast. Fiscal years 2014 to 2016 are actual amounts. The forecast is based on SHPO application and certification data.

Fiscal year	Tax Credit (in thousands)	Grant (in thousands)
2014	$12,244	$344
2015	56,704	-
2016	13,781	-
2017	97,406	3,737
2018	41,657	1,294
2019	29,223	3,332

Where are most projects located?

To date, most projects have been located in Minneapolis and St. Paul, where many historic buildings are located and where recent robust real estate development has occurred. Through fiscal year 2016 (the most recent year with actual data), 77 percent of the projects and 98 percent of the credit/grant amounts were in Minneapolis and St. Paul.

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