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## Missouri Historic Preservation Tax Credit

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### Introduction

The federal government offers an incentive to rehabilitate designated buildings that are older than 50 years. Missouri authorized a tax credit with the same purpose, the Missouri Historic Preservation Tax Credit, in Senate Bill 1 of the second 1997 extraordinary session. Shortly after the state program was approved by the legislature, Carolyn Toft, the Executive Director of the Landmarks Association of St. Louis, compared the program to publicly financed sports stadiums and said, "this is precisely the kind of incentive that brings the things we hear about when people are discussing sports palaces... bit by bit you can put a community or a main street or a neighborhood back together" (Young, 1997). The federal and state programs have been used to redevelop old buildings in small and large cities throughout Missouri. Since the state program was created, the use of the program and the cost to the state has grown significantly.

### Problem Statement

Currently, the Missouri Historic Preservation Tax Credit is an entitlement program without a cap or a sunset. Since the inception of the credit, its use has steadily increased. In fiscal year 1999, the Missouri Department of Economic Development authorized \$20 million in tax credits (Joint Committee on Tax Policy, 2009); the department authorized \$170,058,700 in credits under the program in fiscal year 2008 (MO DED Form 14, 2008). Some policy-makers have concerns that this dramatic growth in the credit's use could have a negative impact on

the state budget in the near future. The aim of this policy note is to provide information to policy-makers and the general public in regards to the state budget impact, use, and prevalence of the credit.

### Federal Historic Preservation Tax Credit

The administration of Missouri's historic preservation tax credit relies heavily on the regulations of the federal historic preservation tax credit. The federal credit allows taxpayers to receive 20% of qualified expenditures for the rehabilitation of historic properties. Qualified expenditures include fees associated with the architectural, legal, engineering, development, and construction costs in addition to the costs of rehabilitating the existing historic structure. Not included in eligible expenditures are acquisition or furnishing costs, any new construction on the property, or improvements related to the area surrounding the building (National Park Service, 2009).

### A property is eligible to receive a credit if it meets one of two criteria:

1. It is listed individually on the National Register of Historic Places; or
2. It is a building within a historic district and is certified by the National Park Service as contributing to the historic significance of the district.

A state or local district may qualify a building as historic if the U.S. Secretary of the Interior approves such a designation (National Park Service, 2009).

To receive the 20% credit, the rehabilitation of the certified historic structure must be consistent with the historic character of the property. In addition, the property must meet the following requirements as stipulated by the Internal Revenue Service:

- The property must be depreciable serving as an income producing property;
- The rehabilitation must occur within 2 years and must cost the greater of either \$5,000 or the adjusted basis of the property (acquisition cost or total basis of the property after subtracting the value of the land, adding the value of improvements, and subtracting any depreciation already taken); and
- The property must be placed into service.

A taxpayer who owns the rehabilitated historic building must maintain ownership of the property for at least five years following the completion of the rehabilitation or, if not, the federal government could recapture all or a portion of the credits (National Park Service, 2009).

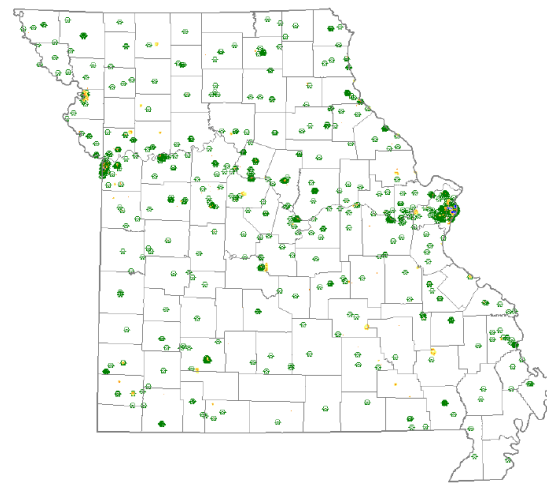
**Missouri Historic Preservation Tax Credit**

Missouri’s historic preservation tax credit shares many features with the federal credit. Missouri taxpayers who own designated buildings are entitled to receive a credit equal to 25% of eligible expenditures; if the building is an income-producing building used for commercial purposes, the taxpayer may be eligible to receive both the federal and the state credit. The expenditures that qualify for the state credit are identical to those that qualify for the federal credit. The federal historical designation is a requirement of Missouri’s eligible buildings as well.

Missouri’s historic preservation credit differs from the federal credit in some aspects. One of the main differences between the federal and the state credit is that owner-occupied (residential) properties are eligible to receive the credit. The rehabilitation of the property must cost at least 50% of the total basis of the property rather than the federal credit’s requirement that the rehabilitation cost 100% of the adjusted basis of the property. Also, there is not a requirement that the taxpayer who rehabilitates the property must hold onto the property for five years following the rehabilitation, meaning that the tax credit is not subject to a recapture or clawback provision (Sections 253.545-253.559, RSMo 2008).

According to the Missouri State Historic Preservation Office, there are more than 1,900 historic entities in Missouri on the National Historic Register; these entities include either individual historic properties or entire historic districts. The office projected that approximately 30,000 to 33,000 properties in the state could qualify for the tax credit (Missouri State Historic Preservation Office, 2009). The following map shows where these eligible properties are located.

Figure 1. Sites Receiving a Historic Tax Credit



Source: MO Department of Natural Resources, GIS, (2009)

The credit can be applied to a taxpayer’s past three tax years (similar to a reimbursement of taxes already paid) and can be applied to taxes for up to ten years subsequent to receiving the credit. Credits are issued in the form of a certificate and may be transferred or sold to other taxpayers; a marketplace exists for the buying and selling of these tax credits. According to the Department of Economic Development, historic preservation credits that are sold had the following transfer prices for each \$1 of state tax credits during fiscal year 2006:

Min Price	25th Percentile	Median Price	75th Percentile	Max Price
\$.00	\$.90	\$.91	\$.92	\$1.00

Source: (Missouri Department of Economic Development, 2008 “Transfer Price Request”)

A majority of the credits are sold for anywhere between 90-92 cents. The Internal Revenue Service has advised taxpayers in the past that certain state tax credits that are evidenced by certificates are treated as payments of tax liability because the certificate is a piece of property; it would be the same if a taxpayer paid income taxes with a parcel of land. The alternative is if the tax credit is not evidenced by a certificate and, instead of paying a taxpayer’s tax liability, the credit works by reducing the taxpayer’s tax liability; in this scenario, taxpayers is not able to receive the full federal deduction of their state tax liability, only the portion, if any, that is not reduced by the tax credit. The IRS also provided a disclaimer that the advice provided to the taxpayers “may not be used or cited as precedent” (IRS Memorandum 200445046, 2004) (IRS Memorandum 2007002, 2007).

## The Past, Present, and Future Impact of the Credit on the State Budget

A tax credit is a dollar-for-dollar reduction or payment (depending on the structure of the credit) of taxes owed to Missouri. Specifically, the Missouri Historic Preservation Tax Credit can offset corporate or personal income taxes, insurance premium taxes, or other financial institutions' taxes. The prevalence and use of the credit has increased substantially in the past ten years. The General Assembly does not appropriate for the credit; rather, when the credit is redeemed, it is subtracted from the amount of revenue that the state would otherwise collect.

Missouri has a tax revenue limitation popularly referred to as the Hancock Amendment. This constitutional provision, instituted in 1980, limits the amount of revenue that the state can collect; if the state collects too much revenue from taxes, Missouri must provide a refund to all taxpayers in an amount equal to the revenue amount which exceeds the total state revenues limitation. The Missouri Supreme Court has interpreted, in *Missouri Merchants and Manufacturers Association, et al., v. State of Missouri* (2001), that the amount of tax credits that are redeemed in any fiscal year are not part of total state revenues as referred to in the Hancock Amendment unless the use of the tax credit is not tied to a person's tax liability as in the case of a refundable tax credit. Refundable tax credits work as if the taxpayer has overpaid taxes and provides a refund to the taxpayer for the difference. The Missouri Historic Preservation Tax Credit is not a refundable credit and therefore the amount of historic tax credit redemptions are not part of the total state revenues calculation as delineated in the Hancock Amendment of the Missouri Constitution. As a result, the annual amount of Historic Preservation tax credit redemptions is not a factor in determining whether the state must issue refund checks to its taxpayers when revenues exceed the "Hancock Amendment" threshold.

The Missouri Historic Preservation Tax Credit has three stages: authorization, issuance, and redemption. Authorization occurs when the taxpayer who owns the property submits an application to the Department of Economic Development. At this stage, the taxpayer is verifying that the property is an eligible historic property. Issuance occurs when the taxpayer has completed the rehabilitation of the property and submits qualified expenditures to the department in order to obtain the credit. Credits are issued in the form of a certificate. Finally, redemption occurs when the taxpayer submits the certificate to the Department of Revenue to offset any eligible state taxes owed by the taxpayer.

After fiscal year 2008, the Department estimated that there are \$65 million in tax credits that have been issued but not yet redeemed (Department of Economic Development, 2008). However, after tallying the difference between issuance and redemption amounts from fiscal years 1999–2008 (credits can be carried forward for up to ten years), the estimate of outstanding credits could be as high as \$179.7 million (Joint Committee on Tax Policy, 2009). The following chart outlines the credit's past ten years of authorization, issuance, and redemption amounts (See Figure 2).

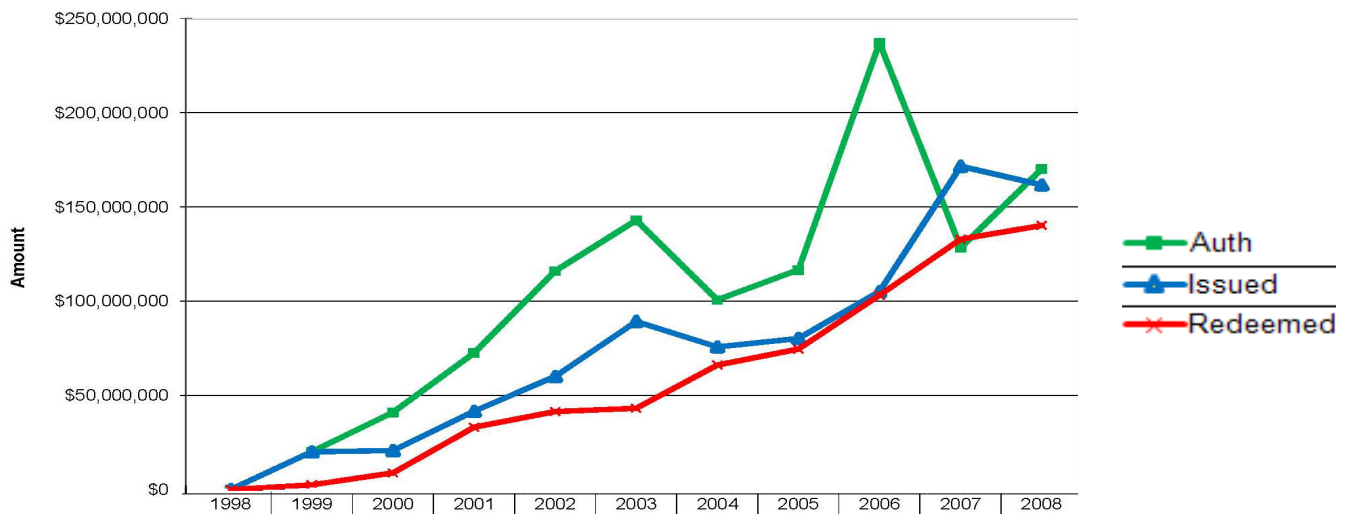
While the chart shows the growth of the credit, it is important to put it in terms relative to the amount of money collected in the state's general revenue (GR) fund, the fund which receives money from most of Missouri's taxes and is used to pay for general services provided by the state. In fiscal year 1999, Missouri collected \$6.1 billion in its GR fund while \$2.55 million in historic preservation tax credits were redeemed against tax collections; Missouri historic tax credits represented .042% of GR collections. In fiscal year 2008, GR collections totaled \$8.3 billion while the amount of historic tax credits that were redeemed in the same year was \$140 million; Missouri historic tax credit represented 1.688% of GR collections. As of March 31, 2009 the total amount of tax credits that were redeemed through the first three-quarters of fiscal year 2009 was \$147 million (Missouri Department of Revenue, 2009).

Missouri appropriates money each year for the purposes of administering state government functions. Missouri has 12 appropriation items that are larger than \$100 million. See table 1 on the next page for the list.

During the 2009 legislative session, the Missouri General Assembly passed House Bill 191, an omnibus economic development bill; HB 191 was recently signed into law by Governor Jay Nixon. One of the provisions of the legislation altered the Missouri Historic Preservation Tax Credit Program by placing a cap on authorizations of \$70 million for the period between January 1, 2010 and June 30, 2010; each fiscal year thereafter, the program will have a cap on authorizations of \$140 million. The bill creates an exemption from the cap for small projects that would receive \$275,000 or less in tax credits (House Bill 191, 2009).

The result of this change is that Missouri will have a finite amount of money that can be dedicated to restoring historic buildings with rehabilitation costs of \$1,100,000 or greater in any future fiscal year. While this cap on tax credit authorizations will provide a degree of certainty to budget writers in future years, this change will not impact the timing or amount of tax credit redemptions, which ultimately affects general revenue collections.

Figure 2. Historic Tax Credits in Missouri, 1998-2008



Source: (Joint Committee on Tax Policy, 2009)

Table 1. General Revenue Collections & Historic Tax Credit Redemptions

	Net GR	Redeemed	% of GR
FY99	\$6,128,300,000	\$2,559,713	0.042%
FY00	\$6,133,600,000	\$8,874,766	0.145%
FY01	\$6,388,900,000	\$33,169,951	0.519%
FY02	\$6,210,900,000	\$41,401,415	0.667%
FY03	\$5,926,307,000	\$43,153,986	0.728%
FY04	\$6,345,800,000	\$66,089,980	1.041%
FY05	\$6,711,400,000	\$74,532,355	1.111%
FY06	\$7,332,200,000	\$103,134,226	1.407%
FY07	\$7,716,400,000	\$132,841,728	1.722%
FY08	\$8,003,875,000	\$140,111,002	1.751%

Source: Missouri Senate Appropriations and Joint Committee on Tax Policy (2009)

Table 2. Major Expense Categories, Missouri General Revenue Fund, FY2009

	GR Expenditure	Amount
1	Education Foundation Formula	\$2,606,776,481
2	University of Missouri	\$414,606,569
3	Managed Care	\$243,623,969
4	State Employee Healthcare	\$235,279,555
5	Medicare Part D	\$175,000,000
6	State Employee Retirement	\$173,004,456
7	MO HealthNet Services	\$169,168,874
8	Nursing Facilities	\$163,427,935
9	DHSS Services	\$159,590,239
10	Mental Health	\$152,911,330
11	MO HealthNet Drug Prescription Funding	\$150,526,710
12	Community Colleges	\$135,884,434

If the Missouri Historic Preservation Tax Credit Program were an appropriation item in the state's annual budget, as of March 31, 2009, the program would be the 12th largest GR expenditure in state government. The program's fiscal year 2009 cost is likely to increase through June of this year.

**Who's Using the Credit?**

The Tax Credit Accountability Act of 2004 required tax credit recipients to report a variety of information to the Department of Economic Development in regards to the nature of tax credit projects (Senate Bill 1099, 2004). These data indicate that there are 555 unique projects totaling \$334.5 million in historic tax credits that have been issued (Department of Economic Development, 2009).

Of the 555 projects, 339 were described by tax credit recipients as purely residential projects, 99 were described by tax credit recipients as purely commercial projects, and 57 were described by the tax credit recipients as both commercial and residential in nature. Sixteen projects were described as neither commercial nor residential; however, this must have been a misunderstanding on the part of the tax credit recipient because the building must be used for one of those purposes in order to receive the Missouri credit.

City of St. Louis (below) and City of Kansas City (right) eligible historic properties and districts. Eligible historic properties and districts for St. Louis are show below in Figure 3; Those for Kansas City are shown in Figure 4, right. Source: MO Department of Natural Resources, GIS, (2009)

Figure 3. Locations of historic tax credits properties - St. Louis.

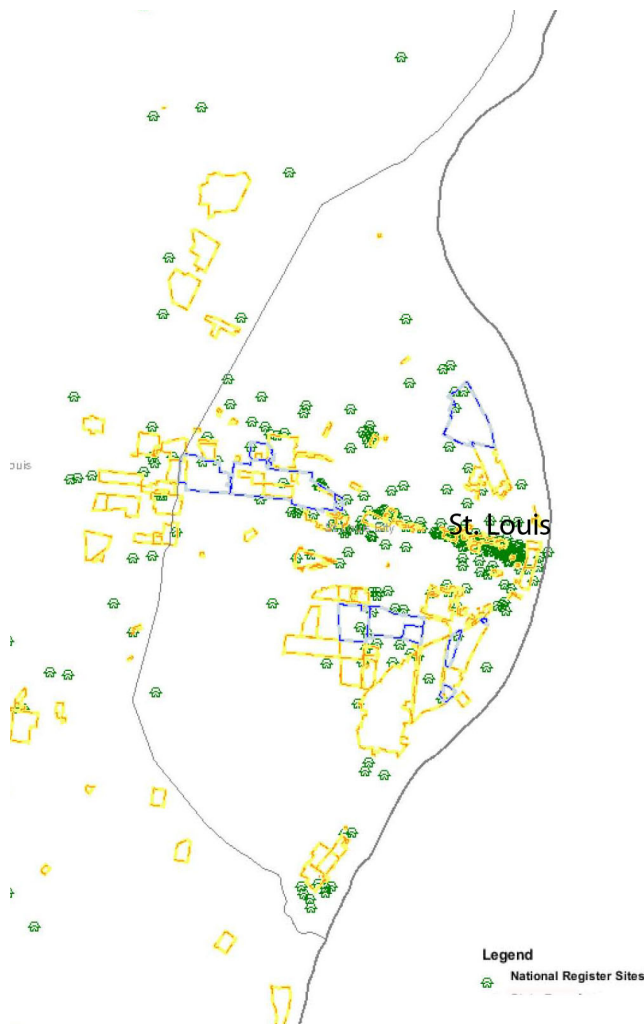
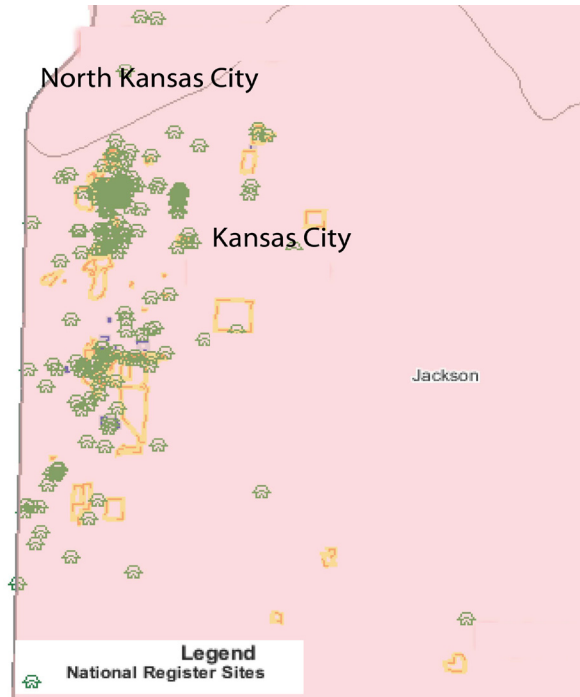


Figure 4. Locations of historic tax credits properties- Kansas City



Of the 555 projects, 389 or 70.1% were located in the City of St. Louis, 67 or 12.1% of the projects were located in Kansas City, and 99 or 17.8% were located throughout the rest of the state. In actual dollars of tax credits, out of the \$334.5 million issued, \$201.4 million or 60.2% of the dollar amount of the tax credits issued were to taxpayers with projects in the City of St. Louis, \$105.8 million or 31.6% of the dollar amount of the tax credits issued were to taxpayers with projects in Kansas City, and \$27.25 million or 8.1% of the dollar amount of tax credits issued to taxpayers with projects in cities throughout the rest of the state (See Figures 5 and 6).

Figure 5. Regional distribution of Missouri historical tax credit

Number of Historic Tax Credit Projects per Region

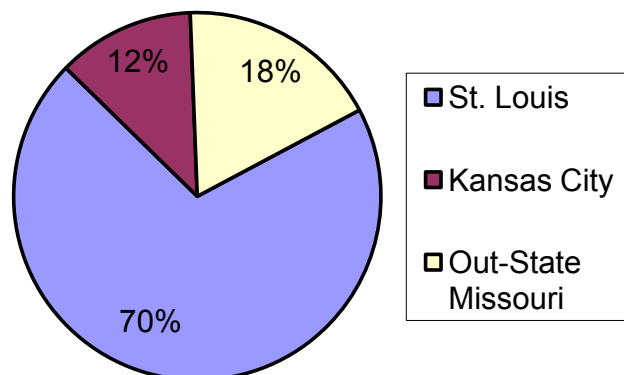
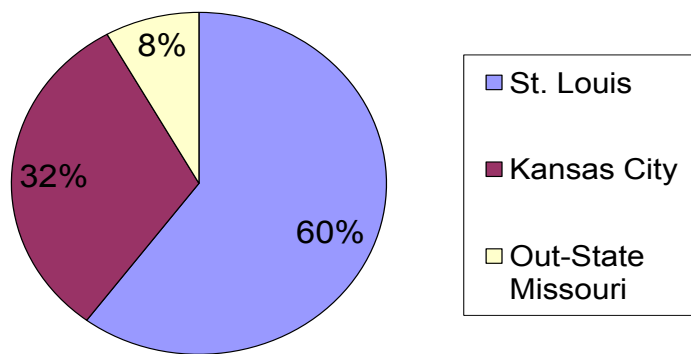


Figure 6. Dollar Amount of Historic Tax Credits per Region



### Conclusion

It is clear from the data that the use of the Missouri Historic Preservation Tax Credit has grown significantly since its inception. This has led to a dramatic increase in the redemption of the credits when compared to the growth of Missouri's general revenue collections. This increase concerned lawmakers due to the impact that the redemption of the credits have on the state budget. Legislation passed during the 2009 session places a cap on program authorizations which will limit the amount of credits that can be redeemed in the future. However, the changes do not alter the redemption of tax credits, which will still leave a degree of uncertainty in future years' general revenue collections. From a regional perspective, it is also apparent that the City of St. Louis had both the greatest number of projects that used the credit as well as the greatest amount of dollars of credits going to projects compared to the rest of the state.

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