



# HISTORIC REDEVELOPMENT AND TAX CREDITS

With the increasing popularity of “green building” and a growing focus on new technologies, materials, and building techniques, the redevelopment and reuse of existing historic buildings may seem counter-intuitive. However, Vermont’s historic downtowns, combined with generous tax credits, make urban redevelopment an attractive opportunity in Vermont. Vermont’s development community has become a national leader in rehabilitating traditional historic centers by redeveloping buildings that are newly environmentally efficient, while still ensuring preservation of their historic and cultural values.

Statewide redevelopment projects and opportunities were showcased last November at the annual Vermont Downtown Conference. This conference was hosted in the newly restored Town Hall Theater which won recognition as the Best Downtown Renovation Project of 2009. This article offers a summary of the historic tax credit programs that are available to help fund these renovations and revitalize our commercial centers.

**Stability and Orientation.** The attributes of historic preservation have been long recognized. Congress identified that “the preservation of historic properties is in the public interest” when it passed the National Historic Preservation Act of 1966. Congress expressly recognized that historic buildings offered “cultural, educational, aesthetic, inspirational, economic, and energy benefits.”

Vermont is home to many buildings that are not utilized to their fullest potential de-

spite their historic character. The rehabilitation of historic and older buildings is encouraged to give communities a sense of stability and orientation. Buildings that are strong candidates for successful rehabilitation include those built for an outdated purpose or that lag behind more contemporary building performance standards.

Efforts by the Department of Economic, Housing and Community Development (formerly the Department of Housing and Community Affairs) and the Division for Historic Preservation’s Downtown Program to promote public-private partnerships and the implementation of tax credits have played a critical and still growing role in Vermont’s downtown rehabilitation. This redevelopment offers significant public benefits as well as benefiting the opportunistic developer. Governor Douglas has said, “Rehabilitation through public-private partnerships has proven effective at returning abandoned and underused properties to the tax rolls, generating employment and much needed office space and housing in downtowns and villages.”

**What is a Tax Credit?** A tax credit, whether pursuant to a federal or state program, is an earned amount that lowers the amount of tax owed. Tax credits differ from grants in that no funds are conveyed directly. They also differ from income tax deductions, which lower the amount of income subject to taxation. Simply, one dollar of tax credit lowers the income tax owed by one dollar, regardless of the income level of the recipi-

ent. This tax credit incentive is taken in the year in which the renovated building is put into service and is useful to reducing project costs.

**Federal Historic Preservation Tax Incentive Credits.** The use of tax credits through the Federal Historic Preservation Tax Incentives promotes responsible rehabilitation and cost-effective community revitalization. Under the Federal Historic Preservation Tax Incentive Program, a 20 percent tax credit is available for the rehabilitation of certified historic structures. This credit is not capped and extends to labor and material costs as well as soft costs such as architectural and consulting fees. Nationally, approximately 1,200 tax credit rehabilitation projects are proposed and a similar number completed each year. According to the National Park Service, “The capital investment in the completed projects is around \$2.8 billion of private sector investment every year.”

A 10 percent federal tax credit is also available for the rehabilitation of non-historic buildings built before 1936, but this program has been less widely used. Pending legislative changes, discussed below, may expand the application of this program.

**Historic Tax Credit Program Qualifications.** To qualify for the 20 percent historic renovation tax credit, a building must first be recognized as an historic structure. This requires that the building either be listed in

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## UNBRIDLED DISCRETION

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a cantilevered porch on the easterly side of a residence adjacent to a stream. The appeal was brought on several questions, but ultimately turned on the zoning administrator's application of a fifty-foot setback requirement from "significant public waters." The appellant argued that the undefined term "significant public waters" bestowed unbridled discretion on the decision-making authority. The town argued that although "significant public waters" is not defined in the bylaws, the applicable section of the bylaw was not vague because the term is "universally understood" and therefore could be applied equally to all.

While the court agreed with the ZBA that there is an "established legal meaning" and "historical usage" of the term *public waters*, the term "significant" was meant to further distinguish certain waterways, and the town failed to identify which ones were important enough to qualify for this classification. The court's decision to grant the appellant's motion for Summary Judgment and approve his request to construct the easterly portion of his porch suggests that a definition or a map showing the location of "significant public waters," combined with the setback requirement, would be a reasonable standard that both an applicant could understand and an appropriate municipal panel (AMP) could apply. Without that additional direction in the bylaw, the court said "decision-makers and landowners are left without notice or guidance as to what waterways

are or are not to be protected" by the setback requirement.

This decision accentuates the need for consummate review of municipal bylaws and stresses how simply defining terms or mapping important features worthy of protection may clarify a standard necessary to withstand constitutional challenge.

The Municipal Assistance Center's advice to AMPs does not change in light of this decision. We continue to encourage AMPs to apply zoning and subdivision ordinances as written to the best of their ability. An AMP should not of its own volition invalidate a bylaw when it believes it is ambiguous or standardless. However, if the AMP or a zoning administrator believes some of the bylaws are vague, be sure to alert the planning commission and ask for clarification. This dialogue with the legislative body is important especially in towns where the quasi-judicial and legislative responsibilities are separate.

Please join us for a Vermont Interactive Television Workshop at 7:30 on February 4, 2010. We will discuss the importance of clear, unambiguous language as it pertains to planned unit development bylaws specifically.

To review this decision, go to [www.vermontjudiciary.org/GTC/Environmental/ENVCRT%20Opinions/Irish%20Construction%20Application%20%20Docket%2044-3-08%20Vtec.pdf](http://www.vermontjudiciary.org/GTC/Environmental/ENVCRT%20Opinions/Irish%20Construction%20Application%20%20Docket%2044-3-08%20Vtec.pdf).

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## DOWNTOWN TAX CREDIT

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the National Register of Historic Places or be located in a registered historic district and be certified as being of historic significance to the district.

The rehabilitation work to be performed must also be consistent with the historic character of the property and, where applicable, to the district in which it is located. Qualifying property owners agree to rehabilitate their historic buildings consistent with Standards promulgated by the secretary of the U.S. Department of the Interior through the National Park Service. These Standards define rehabilitation as "the process of returning a property to a state of utility, through repair or alteration, which makes possible an efficient contemporary use while preserving those portions and features of the property which are significant to its historic, architectural and cultural values." The Standards are not rigid absolutes but are to be flexibly applied in a reasonable manner, taking into consideration economic and technical feasibility. The Secretary's Standards expressly include regard for promoting energy efficiency, which is further discussed below.

The Internal Revenue Service also regulates the use of historic renovation tax credits. The IRS requires that buildings be income-producing, whether used for rental housing, retail or other commercial use. Owner-occupied residences will not qualify. The IRS also requires that the construction renovation cost exceed the adjusted cost basis of the building (exclusive of land costs) or \$5,000, whichever is greater. Despite this modest threshold, the costs associated with applying for tax credits are seen to preclude the program's appeal for less expensive renovations. However, recent legislative changes, further discussed below, propose to encourage tax credit advantages for smaller and less expensive rehabilitation projects.

**Vermont Historic Tax Credits.** In addition to the federal program, Vermont offers a 10 percent tax credit for owners or long-term lessees who qualify for the 20 percent federal reinvestment tax credit. This program piggybacks on federally qualified projects so that owners may receive a cumulative 30 percent tax credit. Unlike the fed-

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## DOWNTOWN TAX CREDIT

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eral program, tax credit funding under Vermont's program is competitive. Applications are submitted annually and tax credits are awarded in July. Not every qualified application for state tax credits is funded. Nevertheless, the use of tax credits has resulted in historic investment exceeding \$100 million in Vermont in over the past 10 years, and the use of tax credit rehabilitation in Vermont is increasing.

The use of rehabilitation tax credits has enabled the completion of successful projects that might otherwise have suffered from inadequate funding, especially during the present slowdown. Recent projects in Vermont that exemplify not only the success of these rehabilitation tax credits but the diversity of the qualifying projects include the Fellows Gear Shaper Plant project in Springfield which is again a manufacturing facility, the Shelburne Inn in Shelburne which offers commercial and restaurant space, and the Seymour Block mixed residential and commercial renovation in St. Albans.

**Energy Efficiency: Green Building and Historic Preservation.** Concerns about the energy efficiencies of older buildings are common. Architects, builders, developers, and preservationists have discovered that green building initiatives can be usefully applied to historic preservation and redevelopment. Consequently, historic building standards are being challenged with new and novel approaches to building reuse and restoration. Carefully applied and thoughtfully designed, historic rehabilitation can satisfy the Secretary's Standards and promote energy efficiency.

Energy efficiency is an important aspect of almost every rehabilitation project. The Secretary's Standards and related guidelines published by the National Park Service direct that "particular care must be taken not to obscure, radically change, damage or destroy character defining features in the process of rehabilitation work to make the building more energy efficient." The Energy Efficiency Standard specifies that the first step to making any building more energy efficient "should always be to identify and evaluate existing historic features to assess their inherent energy-conserving potential."

Debevoise Hall at the Vermont Law School exemplifies how historic structures

may be made energy efficient in adhering with the Secretary's Standards. Originally built in 1893 as the Town of South Royalton's first central "graded school," Debevoise Hall is part of a registered historic district.

Recently, Vermont Law School completed a \$6.5million rehabilitation of the town landmark. By restoring the original double hung wooden windows and newly installing interior glazed fiberglass storm windows and new insulation, air leakage from the building was reduced by four-fifths. Despite a significant expansion to the area of the building, the school's energy use for heating Debevoise Hall after the renovation dropped by two-thirds. As this project demonstrates, character defining historic features may be preserved while producing operating energy efficiencies that are the equivalent of contemporary new construction.

“ Vermont is home to many buildings that are not utilized to their fullest potential despite their historic character. ”

### Pending Legislative Program Changes.

Pending federal legislation may make historic tax credit projects in Vermont an even greater opportunity. Legislative changes introduced last October expand the federal rehabilitation tax credit and provide greater incentive for the reuse of historic and older buildings. This newly introduced bill not only encourages building owners to achieve substantial energy savings by boosting the received credit through the use of energy efficient materials, systems and appliances, but it expands to 30 percent the federal tax credit for "small" historic rehabilitation projects costing \$7.5 million or less. This increase will help offset the application costs that presently frustrate the use of tax credits on smaller projects.

The proposal will also reduce the qualifying cost for historic rehabilitation tax credits to only 50 percent of the adjusted basis, increasing the eligible pool of buildings in need of rehabilitation that may qualify for tax credit participation. Finally, the proposal will ensure that piggybacked state credits are not federally taxed or considered federal income unless so reported by the taxpayer. Each of these changes is intended to further promote smaller rehabilitation projects

in rural downtowns, such as are predominant in Vermont.

The pending legislative changes also propose to amend the non-historic tax credit program for older buildings. Two proposed changes are especially notable. First, while the 20 percent tax credit for historic renovation is allowed for income producing property including residential rental property, housing is not presently allowed under the 10 percent program for older, non-historic buildings. It is newly proposed that housing be included. The second change will bring forward the date of eligibility for older but non-historic buildings. Preservation policy has long relied upon 50 years or older as the age of "older" structures. In 1986, when Congress last amended the applicable Section 47 of the Tax Code, it implemented this 50 year or older threshold by requiring qualified structures to have been placed in service prior to 1936. It has not been changed since, preventing noteworthy "older" buildings from participating. The new proposal suggests that public policy is better served by declaring any qualified building to be "fifty-years old or older" rather than by the set year of 1936.

Each of these changes would make the downtown rehabilitation program in Vermont even stronger by further promoting smart growth, good-paying jobs, housing and office space, and sustainable development as an economic stimulus statewide. As the governor has recognized, "These projects leverage significant private investment, and rehabilitation of historic buildings in downtown areas results in increased economic activity. And of course it preserves a key part of what makes Vermont special: Our iconic downtowns and village centers."

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