



Incentives for Historic Preservation

Historic places help define the character of our communities by providing a tangible link with the past. Today, historic districts around the country are experiencing unprecedented revitalization as cities use their cultural monuments as anchors for redevelopment.

Sometimes, efforts to preserve and revitalize historic buildings run up against financial obstacles that create challenges in reusing these unique structures. Fortunately, there are several incentives available which can make preservation more economically feasible.

These incentives are available to all qualifying projects: unlike other tax credit programs, none of the historical incentives involve a risky competition or lottery process. This overview outlines the financial and construction incentives that can make a significant difference in preserving buildings and can provide significant benefits to both property owners and the public at large.

There are several types of incentives to help preserve historic buildings. Financial incentives can provide income and property tax reductions. Other construction-based incentives offer additional flexibility in meeting building code requirements, which can make potential projects significantly more affordable. Below is a brief summary of the major incentives currently available.

Financial Incentives

- **Rehabilitation Tax Credits** provide a 10% or 20% tax credit on rehabilitation spending for old and historic buildings.
- **Conservation/Facade Easements** offer an income tax deduction for the donation of a specified portion of a historic building.
- **The Mills Act** provides property tax relief in exchange for the continued preservation of historic properties.

Construction Incentives

The **City of Los Angeles Adaptive Reuse Provisions** streamline the permitting process and provide flexibility in meeting zoning and building code requirements for adaptive reuse projects, which convert underused commercial buildings to more productive uses such as live/work and residential units.

The **California State Historical Building Code** provides flexibility in meeting code requirements in historic buildings.

20% Rehabilitation Tax Credit

Description: The Federal Historic Preservation Tax Incentive is a program administered by the National Park Service (NPS) that rewards private investment in rehabilitating income-producing historic properties, such as offices, rental housing, and retail. The incentive provides a 20% tax credit for all qualifying hard and soft cost expenditures during rehabilitation.

Benefits: The incentive offers a 20% tax credit for the rehabilitation of certified historic structures. The credit equals 20% of the amount spent on qualifying rehabilitation expenditures and is claimed in the year in which the rehabilitated building is put into service.

Restrictions and Eligibility

Property Types Allowed: Commercial, industrial, agricultural and rental residential properties. Buildings must be depreciable and used in a trade or business to produce income. Owners or long term lessees of at least 27.5 years for residential property and 39 years for nonresidential property may apply.

Property Types Not Allowed: Properties used exclusively as an owner's private residence. However, Congress is currently considering legislation that would create a similar 20% tax credit for the rehabilitation of private homes.

Certified Historic Structure: To be eligible, a building must be listed in the National Register of Historic Places or be a contributing structure in a National Register Historic District. Many more structures are eligible for the Register, and property owners may apply for National Register designation as part of the tax credit process. The Los Angeles Conservancy can assist a property owner in determining the eligibility of potential properties. In Los Angeles, National Register districts include the Broadway Historic Theatre District, the Spring Street Financial District, and the Hollywood Boulevard Commercial District.

Hard Costs: Rehabilitation expenditures must be capital in nature and depreciable as real property. Routine maintenance costs such as painting and repairs are not eligible unless they are part of an overall rehabilitation. Acquisition and building enlargement costs do not qualify.

Soft Costs: Qualified expenditures may also include soft costs such as architectural and engineering fees, site survey fees, legal expenses, development fees and other construction-related costs, if such costs are added to the basis of the property and determined to be reasonable and related to the services performed.

Holding Period: Building owners must hold the structure for five years following the completion of the rehabilitation or pay back the credit. Any alterations during the five years must be reviewed by the National Park Service.

Maintenance and Alterations: Building owners must not damage, destroy, or cover materials or features, interior or exterior, that help define the building's historic character.

Tax-Exempt Restrictions: Expenditures allocable to that portion of a building that is, or is reasonably expected to be, "tax-exempt use property" do not qualify. Moreover, the property becomes ineligible if tax-exempt entities occupy more than 35% of the building.

Scope: During a 24-month period, the rehabilitation expenditures must exceed \$5,000 or the adjusted basis of the building, whichever is greater. For phased projects with complete sets of architectural drawings and specifications for each phase, the window of eligibility is 60 months. The adjusted basis of the building equals the purchase price plus capital improvements less total depreciation and does not include land value. Also, all new work is expected to meet the Secretary of the Interior's Standards for the Rehabilitation of Historic Properties.

Administration: Building owners must complete a three-part application in order to receive the 20% Rehabilitation Tax Credit. Part 1 verifies that the building is listed in or eligible for the National Register. In Part 2, applicants submit a description of the proposed work for approval by the National Park Service. In Part 3, the completed project is compared to Part 2 and evaluated for compliance with the Standards for Rehabilitation. The incentive is jointly administered by the National Park Service (NPS) in partnership with the State Historic Preservation Officer (SHPO), who acts on behalf of the U.S. Department of the Interior. The Internal Revenue Service (IRS) also participates on behalf of the Department of the Treasury. The application is first reviewed by the SHPO and is then forwarded to the NPS for review. The NPS encourages property owners to apply prior to the start of construction.

Fees: Processing fees to cover the review of the application range from \$500 to \$2,500 depending on the cost of rehabilitation.

Code References: Tax Reform Act of 1986 (PL 99-514; Internal Revenue Code Section 47)

A General Overview of Tax Credits: A tax credit lowers the amount of tax owed, while a deduction lowers the amount of income which is subject to taxation. In general, every dollar of tax credit reduces the amount of tax owed by one dollar. Every dollar of tax deduction reduces the amount of tax owed by a fraction of a dollar equal to the taxpayer's tax rate.

10% Rehabilitation Tax Credit

Description: A 10% tax credit rewards private investment in rehabilitating non-residential buildings built before 1936. In contrast to the 20% credit, the 10% Rehabilitation Tax Credit applies to properties that are not listed in or eligible for the National Register of Historic Places.

Benefits: The incentive provides a 10% tax credit on the amount spent on qualifying hard and soft cost rehabilitation expenditures of non-historic, non-residential buildings built before 1936.

Restrictions and Eligibility

Property Types Allowed: Non-residential buildings, including hotels

Property Types Not Allowed: Residential buildings, including rental housing and private homes

Hard Costs: Rehabilitation expenditures must be capital in nature and depreciable as real property. Routine maintenance costs such as painting and repairs are not eligible unless they are part of an overall rehabilitation. Acquisition and building enlargement costs do not qualify.

Soft Costs: Qualified expenditures may also include soft costs such as architectural and engineering fees, site survey fees, legal expenses, development fees and other construction-related costs, if such costs are added to the basis of the property and determined to be reasonable and related to the services performed.

Tax-Exempt Restrictions: Expenditures allocable to that portion of a building that is, or is reasonably expected to be, “tax-exempt use property” do not qualify. Moreover, the property becomes ineligible if tax-exempt entities occupy more than 35% of the building.

Scope: Projects must pass physical tests for retaining the exterior walls and interior structural framework. Fifty percent of the existing exterior walls must remain in place. Seventy-five percent of the existing interior walls must remain in place. During a 24-month period, the rehabilitation expenditures must exceed \$5,000 or the adjusted basis of the building, whichever is greater. For phased projects with complete sets of architectural drawings and specifications for each phase, the window of eligibility is 60 months. The adjusted basis of the building equals the purchase price plus capital improvements less total depreciation and does not include land value. Also, all new work is expected to meet the Secretary of the Interior’s Standards for the Rehabilitation of Historic Properties.

Additional Restrictions: The 10% and 20% tax credits are mutually exclusive. Owners can receive one of the credits, but not both. In addition, owners of historic buildings that are denied certification for the 20% credit may not claim the 10% credit. The 10% Rehabilitation Tax Credit only applies to non-historic, non-residential buildings built before 1936. The type of building, not the owner, determines which credit is applicable.

Application: There is no formal review process for the rehabilitation of non-historic buildings. The tax credit must be claimed on IRS form 3468 for the tax year in which the rehabilitated building is placed in service.

Code References: Tax Reform Act of 1986 (PL 99 - 514; Internal Revenue Code Section 47)

Mills Act Property Contracts Program

The Mills Act is a state law that allows cities to enter into contracts with owners of historic properties to provide property tax relief in exchange for the continued preservation of the historic property. For properties where land represents a large portion of the market value, such as in high-density commercial and residential districts, the Mills Act adjusts the property tax to reflect the actual use of the site, therefore offering significant tax reductions of approximately 50% for newly improved or recently purchased properties.

Eligibility and Restrictions for the City of Los Angeles

Property Types: Owner-occupied single family residences with a property tax assessment of \$500,000 or less are eligible. Income producing commercial properties (including apartment and industrial) valued at \$1,500,000 or less are also eligible. The Cultural Heritage Commission may grant exemptions to these limits, which has occurred more frequently in recent years as property values have soared. Properties located in the Downtown Historic Core or Hollywood Redevelopment District is exempt from the property value limits.

Certified Historic Structure: To be eligible, a building must be listed in the National Register of Historic Places or be a contributing structure in a National Register Historic District. In addition, owners of City Historic-Cultural Monuments and buildings contributing to a City Historic Preservation Overlay Zone are eligible. All new work is expected to meet the Secretary of the Interior's Standards for the Rehabilitation of Historic Properties.

Contract Period: The minimum contract period is ten years and is renewed annually. The contract is executed between the local government and the property owner and is binding for all successive owners during the ten - year period. The property owner must allow for the periodic inspection of the interior and exterior to verify compliance.

Origin: The enabling legislation was passed in 1976 and was subsequently adopted by local cities. Los Angeles, Pasadena and San Diego have all adopted the act.

Administration: The Los Angeles Department of City Planning, Office of Historic Resources handles Mills Act administration.

Fees: Nonrefundable application fee of \$268.

Valuation:

- Property is valued according to the income method in the Revenue and Tax Code Section 439.21. Income or projected rental income less certain expenses is divided by a capitalization rate to determine the assessed value of the property. The Mills Act assessed valuation is recalculated each year to reflect changes in income, expenses, interest rate and amortization.
- If the property is owner occupied, the income is based on comparable rents for similar property in the area, or if insufficient rental information is available, the income that it could reasonably be expected to produce under prudent management.

Code Reference: California Government Code Section 50280 and Revenue and Tax Code Section 439.1

City of Los Angeles Adaptive Reuse Ordinance

The Adaptive Reuse Ordinance, approved by the City Council in 1999 and revised in 2002, aims to revitalize Los Angeles' architectural and cultural resources and encourage the development of live/work communities. Adaptive reuse projects convert underused buildings to more productive uses such as live/work units, rental dwelling units, condominiums, and hotels. The provisions streamline the application process and provide significantly more flexibility in meeting building code and zoning requirements.

Benefits:

- Land Use Ordinance (City Planning)
- Discretionary review by the Planning Department is not required.
- Many non-compliant site conditions (including building height, parking, floor area, and setbacks) are permitted without requiring a variance. Residential density requirements are also waived. New mezzanines less than one-third the floor area of the room below are not counted as floor area.

Construction Guidelines (Building and Safety): The conversion of existing buildings to privately owned residential use will not trigger disabled access requirements in the residential use area. Disabled access is still required in areas used by employees and that are open to the general public. The construction guidelines provide some flexibility in meeting structural and fire and life safety compliance requirements. Please contact the Department of Building and Safety or Fire Department for specific potential benefits.

Eligibility and Restrictions

Location and Age: Buildings must be located in one of the following areas: Central City, Figueroa Corridor Economic Development Strategy Area, Chinatown, Lincoln Heights, Hollywood Community Redevelopment Project Area, Central Avenue south of the Santa Monica Freeway and north of Vernon Avenue, and portions of the Wilshire Center / Koreatown Community redevelopment area. Buildings located in commercial and multi-residential (R5) zones whose original building permits were issued before July 1, 1974 are eligible to receive the benefits listed under the Adaptive Reuse Ordinance by right.

Compliance: All newly constructed floor area, except for mezzanines, must comply with the city zoning code. Size: Dwelling units and live/work units must average 750 square feet in floor area with no unit less than 450 square feet.

Administration: Three departments of the City of Los Angeles will guide, assist, and facilitate the adaptive reuse implementation through a project facilitating team. The team will help projects through the design, permitting and construction processes.

- Office of the Mayor
- Department of Building and Safety
- Fire Department

California Historical Building Code

Preservation and rehabilitation are frequently made more difficult by unnecessarily rigid interpretation of the building code. The intent of the California Historical Building Code (CHBC), formerly the State Historical Building Code, is to protect California's architectural heritage by recognizing the unique construction problems inherent in historic environments and offering an alternative code to deal with these problems. The CHBC provides alternative building regulations and standards for the rehabilitation, preservation, restoration, relocation, or change of occupancy of designated historic buildings. The CHBC aims to preserve the original or restored architectural elements, encourage cost-effective conservation and provide safety for building occupants.

Benefits: The CHBC gives property owners flexibility to find economical methods to allow for the restoration of historic features while still retaining the structures' historic integrity. Many projects that would otherwise be financially impossible under today's building codes are made feasible by the CHBC, whose regulations are performance oriented rather than prescriptive.

Eligibility and Restrictions: To be eligible, a building must be listed in the National Register of Historic Places or contribute to a National Register Historic District. In addition, owners of City Historic-Cultural Monuments and buildings contributing to a City Historic Preservation Overlay Zone are eligible. All new work is expected to meet the Secretary of the Interior's Standards for the Rehabilitation of Historic Properties. New

construction must conform to the regular code, while elements within the historic portion are afforded the latitude of appropriate alternatives.

Substandard Buildings: The CHBC is not a license to maintain a substandard building. Under Section 8 - 109, all qualifying buildings must comply with minimum standards outlined by the code.

Origin: The CHBC was passed in 1976 and was the first of its kind in the nation. The CHBC supersedes all other California building codes.

Enforcement: The State Historic Building Safety Board (SHBSB) within the Office of the State Architect oversees the CHBC and its appeals. However, local enforcing agencies such as the Los Angeles Department of Building and Safety are also required to use the code. Alternative standards are handled on a case-by-case basis depending on the building and its use.

Code References

- California State Health and Safety Code Part 2.7 – California Historical Building Code, Sections 18950 - 18961
- California Administrative Code – State Building Standards, Title 24, Part 8

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