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Taxes and Historic Preservation

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TAXES AND HISTORIC PRESERVATION



The Law Library on East Side Square is an excellent example of rehabilitating an older structure for an "efficient contemporary use." It was built in 1913 for a department store; the 1974 renovation retained the significant architectural features but created a contemporary entrance since the original was unrecorded.

I. The Tax Reform Act of 1976

The Tax Reform Act of 1976, signed into law October 4, 1976, contains provisions (Section 2124) designed to stimulate the rehabilitation of historic buildings and discourage their destruction. To facilitate this, certain tax incentives are provided to owners who rehabilitate depreciable historic structures within the guidelines established by the Secretary of the Interior. Conversely, there are tax disincentives when such a structure is demolished. The following description of the tax consequences is for general informational purposes only.

ELIGIBLE PROPERTIES: To qualify, a structure must be a depreciable property; this generally means one that is subject to allowance for depreciation under Section 167 of the Internal Revenue Code of 1954 and excludes owner-occupi-

ed homes. In other words, it must be income-producing property which includes rental housing. IN ADDITION the building must be a "certified historic structure" which means that it satisfies any one of the following conditions:

1. Listed individually on the National Register of Historic Places.
2. Located in a district listed on the National Register and certified as being of historical significance to the district.
3. Located in a district designated under a state or local statute which has been certified by the Secretary of the Interior and individually certified as being of historical significance to the district.

Structures qualifying under condition 1 are automatically certified historic structures. Those structures located within a district (conditions 2 and 3) must be certified by filing Part I of the Historic Preservation Certification Application with the State Historic Preservation Officer (SHPO). He will forward the application to the National Register Division staff who then rules on whether or not the structure is of historical significance to the district and provides written notification of the decision to the owner.

REHABILITATION: The Tax Reform Act of 1976 provides major tax incentives for rehabilitation by owners of commercial historic structures. Rehabilitation means 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. This does not require restoration although a restoration would also be eligible for the same tax benefits if it met all the requirements. For an owner to

take advantage of the rehabilitation provisions of the tax law, he must have the rehabilitation certified by the Secretary of the Interior. This is



BEFORE: This two-story brick store house at 106 South Side Square was built in 1883 but through the years has suffered thoughtless modernizations and wanton neglect.

accomplished by filing Part II of the Historic Preservation Certification Application with the SHPO at any time during the rehabilitation work although to ensure acceptance it is advisable to submit the proposed rehabilitation plans prior to the start of construction so that any items which do not meet the standards may be corrected. The SHPO will forward the application to the Technical Preservation Services Divi-

sion for review and evaluation, and they will then notify the owner whether the project is consistent with the Secretary of the Interior's Standards for Rehabilitation. Upon completion of the rehabilitation work, the owner must notify the Technical Preservation Services Division, through the SHPO, that the project has been completed and submit appropriate materials documenting it.



AFTER: A sensitive renovation has highlighted the surviving original elements, the cleaned brick and repainted cornice, while remodeling the ground floor to both harmonize with the existing design and provide a contemporary entrance.

If the completed work meets the Standards for Rehabilitation, it will be certified and the owner will be eligible to

take advantage of the tax incentives.

THE TAX ADVANTAGES: The Tax Reform Act of 1976 provides two separate tax advantages for rehabilitation.

1. **THE 60-MONTH AMORTIZATION DEDUCTION** may be used by an owner for depreciating any capital expenditure incurred in connection with a certified rehabilitation of a certified historic structure in lieu of depreciation deductions otherwise allowed. A **CERTIFIED REHABILITATION** means any rehabilitation of a certified historic structure which the Secretary of the Interior has certified to the Secretary of the Treasury as being consistent with the historic character of such property or the district in which it is located. It does not require any minimum amount to be spent on rehabilitation work. The 60-month amortization deduction applies only to rehabilitation expenses incurred after June 14, 1976 and before June 15, 1981. This provision allows an owner to deduct capital expenditures incurred in rehabilitation over a sixty month period rather than being added to the adjusted basis of the structure and depreciated over its useful life.

2. **ACCELERATED DEPRECIATION DEDUCTIONS** may be taken at the owner's election on certified historic properties which are substantially rehabilitated. A **SUBSTANTIAL REHABILITATION** is one in which the expenditure for a 24-month period ending on the last day of any taxable year (reduced by any amounts allowed as depreciation or amortization with respect thereto) exceed the greater of 1. \$5,000 or 2. the adjusted basis of such property. The adjusted basis (initial cost of the property plus the costs

of improvements less the amounts allowed as depreciation) is determined as of the first day of the 24-month period. Accelerated depreciation applies to the total property, rather than just the rehabilitation expenses, and allows the owner to depreciate the property as though he were the original user of the property. The accelerated depreciation deduction applies to expenses incurred after June 30, 1976 and before July 1, 1981. It has not yet been determined, but it seems probable that a taxpayer will not be allowed to take both the 60-month amortization deduction and accelerated depreciation deduction. However on a substantial rehabilitation, the owner may elect to take either the accelerated depreciation deduction on the entire property or amortize over five years the rehabilitation expenditures. A lessee does not qualify for the rehabilitation tax incentives of the 1976 tax act but a life tenant can.

For either method of tax deduction outlined above, the Secretary of the Interior must certify that the structure is in fact a certified historic structure before the tax consequences accrue. However, rehabilitation plans will be reviewed for structures not yet designated as certified historic structures if it appears likely that they will receive such status.

DEMOLITION: The Tax Reform Act of 1976 is written to encourage the preservation of historic structures and to discourage their demolition. Therefore, for demolition purposes, any structure located within a registered historic district will automatically be

considered a certified historic structure unless the Secretary of the Interior certifies PRIOR to demolition that the structure is not of historic significance to the district. To obtain this decertification, the owner must submit Part I of the Historic Preservation Certification Application to the SHPO who will then forward it to the National Register Division for review. The owner will receive written notification of their decision. If an owner demolishes a certified historic structure, he cannot deduct expenditures or losses resulting from the demolition.

The law also prohibits accelerated depreciation for any property in whole or in part constructed, reconstructed, erected, or used on a site that was occupied by a certified historic structure that has been demolished or substantially altered other than by a certified rehabilitation. The provisions of the tax act apply only to demolitions after June 30, 1976 and before January 1, 1981.

FURTHER INFORMATION: The Internal Revenue Service is responsible for all procedures, legal determinations and rules and regulations concerning the tax consequences of the Tax Reform Act of 1976. For further clarification regarding these tax provisions, contact the District Director, Internal Revenue Service, 2121 8th Avenue, N., Birmingham, Alabama.

For additional information on the certification of historic structures and rehabilitation and for forms and assistance to apply for certification, contact the Huntsville Planning Commission. ✻

II. Standards for Rehabilitation

The following Standards shall be used by the Secretary of the Interior when determining if a rehabilitation project qualifies as certified rehabilitation pursuant to the Tax Reform Act of 1976.

1. Every reasonable effort shall be made to provide a compatible use for a property that requires minimal alteration of the building, structure, or site and its environment, or to use a property for its originally intended purpose.
2. The distinguishing original qualities or character of a building, structure, or site and its environment shall not be destroyed. The removal or alteration of any historic material or distinctive architectural features should be avoided when possible.
3. All buildings, structures, and sites shall be recognized as products of their own time. Alterations that have no historical basis and that seek to create an earlier appearance shall be discouraged.
4. Changes, which may have taken place in the course of time, are evidence of the history and development of a building, structure, or site and its environment. These changes may have acquired significance in their own right, and this significance shall be recognized and respected.
5. Distinctive stylistic features or examples of skilled craftsmanship which characterize a building, structure, or site shall be treated with sensitivity.
6. Deteriorated architectural features shall be repaired rather than replaced, wherever possible. In the event replacement is necessary, the new material should match the material being replaced in composition, design, color, texture, and other visual qualities. Repair or replacement of missing architectural features should be based on accurate duplication of features, substantiated by historic, physical, or pictorial evidence rather than on conjectural designs or the availability of different architectural elements from other buildings or structures.
7. The surface cleaning of structures shall be undertaken with the gentlest means possible. Sandblasting and other cleaning methods that will damage the historic building materials shall not be used.
8. Every reasonable effort shall be made to protect and preserve archeological resources affected by, or adjacent to, any project.
9. Contemporary design for alterations and additions to existing properties shall not be discouraged when such alterations and additions do not destroy significant historical, architectural or cultural material, and such design is compatible with the size, scale,

color, material, and character of the property, neighborhood or environment.

10. Wherever possible, new additions or alterations to

structures shall be done in such a manner that if such additions or alterations were to be removed in the future, the essential form and integrity of the structure would be unimpaired. ✱

III. Alabama Ad Valorem Taxation

As a result of the state wide property reappraisal and the proposed constitutional amendment on ad valorem taxation, the amount of property taxes paid next year could change dramatically. The Wallace Property Relief Package contains enabling legislation of which Act 728 is of particular interest to owners of historic property. The ad valorem taxation rates now in effect have no incentives for historic preservation; historic property is assessed at the current rate of either 25% for commercial property or 15% for single family dwellings. Act 728, which defines classes of taxable property and fixes the ratios of assessed value, would change this. Commercial assessment ratios would decrease from 25% to 20% of the appraisal value and residential assessment ratios, from 15% to 10%. In addition, provision is made for the first time for historic buildings and sites; these would be assessed at 10% regardless of the use to which such property is put. Historic buildings and sites are defined by the Act as all buildings or

structures (i) listed in the National Register of Historic Places, or (ii) located in a Registered Historic District and certified by the United States Secretary of the Interior as being of historic significance to the district. This means that historic properties would be assessed at the lowest rate even if they are used commercially; in other words, the assessment basis for historically significant commercial property would decrease from the current rate of 25% to the new rate of 10%.

All properties individually listed on the National Register would be assessed at 10%. All properties located in Old Town or Twickenham and used exclusively as a single family dwelling by the owner would be assessed at 10%. Those properties located in Old Town and Twickenham that are not owner occupied as a single family dwelling would be assessed at 20% UNLESS they are certified by the Secretary of the Interior as being of historic significance to the district, then

they would qualify for the 10% ratio of assessment regardless of their use.

The Wallace Property Relief Constitutional Amendment will be voted on in the November 7th general election. If passed, the amendment will become effective immediately, and the revised assessment bases described above will be applicable during the next tax year.

The lower assessment rates, however, do not necessarily mean that the amount of taxes paid by the property owner will decrease. They may, in fact, increase because of the property reappraisal which is now underway. The decrease in assessment rate may not be enough to offset the increase in appraisal value. Particularly hard hit will be those properties that have not been reappraised recently and, as a consequence, have a decidedly out-

of-date appraisal value on the tax books.

However, owners of historic commercial property will be able to cut their taxes in half merely by agreeing to have their historic properties listed on the National Register. This provision should be particularly attractive to people who own older structures in the central business district. Listing on the Register would not only decrease property taxes by half but would also make these properties eligible for certain tax incentives if they were rehabilitated.

If this constitutional amendment is passed in the November election, the QUARTERLY will carry a further article advising owners of National Register properties of their obligations to ensure that they receive the 10% ratio of assessment due them. *

IV. NATIONAL REGISTER PROPERTIES IN MADISON COUNTY

Clemons House
219 Clinton Avenue
Domestic Science Building
Alabama A & M Campus
Steele-Fowler House
808 Maysville Road
Hundley House
401 Madison Street
First Alabama Bank
216 West Side Square

Episcopal Church of the Nativity
208 Eustis Street
Redstone Test Stand
Redstone Arsenal
Memphis & Charleston Depot
Church Street
Humphreys-Rodgers House
502 Clinton Avenue
Old Town Historic District
Twickenham Historic District