BOUSQUET HOLSTEIN PLLC

Alert

Brownfields Practice Group

# Lawmakers Reach Deal to Reform NYS Brownfield Cleanup Program

**Syracuse, New York** **April 2015**

New York State Governor Andrew Cuomo and the New York State Legislature have agreed to extend and modify the financial incentives under New York's Brownfield Cleanup Program (BCP) as part of the 2015-2016 State budget, which was signed into law on April 13, 2015. Important program changes to the BCP are also included in the legislation, along with the creation of a streamlined "BCP-EZ" program without tax incentives. This BCP extension and modification act (referred to below as "BEMA") resolves lingering uncertainty over the future of the statewide program for cleaning up and redeveloping properties blighted by contamination, often referred to as "brownfields."

In January, the Governor proposed changes to the BCP, along with significant curtailment of the tax incentives that have been part of the BCP since its adoption in 2003. Those proposals followed his unsuccessful attempt to modify and extend the program in the 2014-15 budget. Our prior alerts regarding the January proposal and the 2014 proposal can be found on our website at www.bhlawpllc.com/brownfields.

The BCP's tax incentives were to sunset for brownfield sites that do not receive a certificate of completion (*CoC*) from the NYS Department of Environmental Conservation (*DEC*) by December 31, 2015. During the 2014 legislative session, the Legislature passed a 15-month extension of that sunset date, but that extension was ultimately vetoed by the Governor.

Under current law, taxpayers may earn refundable New York State income/franchise tax credits for remediation and redevelopment activities, property taxes and on-site employment, and environmental insurance premiums for their BCP sites. The credit for remediation and redevelopment activities, known as the Brownfield Redevelopment Tax Credit (*BRTC*), is the focus of the proposed changes. BEMA will phase out the other two credits (the credit for real property taxes based on employment and the credit for environmental insurance premiums) for sites which have not been accepted into the BCP by the Effective Date noted below.

The BRTC has three components that are currently calculated based on whether the site was accepted into the BCP before, or after, the BCP credits were overhauled in June 2008. The 2008 law change limited the BRTC component for redevelopment costs (including buildings) to a multiple of eligible cleanup costs and an overall limit of $35 million, or $45 million for sites primarily used in manufacturing. In addition to the 2008 changes, BEMA introduces new eligibility criteria and incentives for sites accepted into the BCP after the effective date noted below.

## Effective Dates, Sunsets, and Grandfathering

BEMA makes significant changes to the tax credits for sites accepted into the BCP after the later of July 1, 2015 or the date NYSDEC publishes proposed regulations detailed below (referred to below as the "*Effective Date*"). Most provisions of BEMA take effect on that Effective Date. BEMA exempts, or "grandfathers," sites accepted before the Effective Date from the new tax credit structure.

Sites accepted into the BCP after the Effective Date and on or before **December 31, 2022** will be eligible for the new BEMA tax credit structure described below, provided a CoC is issued on or before **March 31, 2026**. No tax incentives will be available for sites accepted into the BCP after December 31, 2022.

Sites currently in the BCP must receive a CoC before specific deadlines in order to preserve the tax credit structure that they were accepted into (pre-2008 or post-2008):

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- Sites with a Brownfield Cleanup Agreement (BCA) dated before June 23, 2008 will have until **December 31, 2017** to obtain a CoC; otherwise they will only be eligible for the tax credits as if they entered the BCP after the Effective Date.
- Sites with a BCA dated on or after June 23, 2008 but before BEMA's Effective Date will have until **December 31, 2019** to obtain a CoC; otherwise they will only be eligible for the tax credits as if they entered the BCP after the Effective Date.

*Commentary: Overall, BEMA provides a dose of security after the last several years of legislative wrangling. The relatively long windows for the BCP included in BEMA will provide much needed stability for projects considering the program and the grandfathering provisions provide the same to projects already accepted into the program. Additionally, each of the timelines created by BEMA are more reasonable than some of the proposals introduced in 2014 and 2015.*

*Under BEMA, existing projects will have to complete remediation and obtain a CoC by either 2017 or 2019. Although this introduces new deadlines, they should actually come as relief to developers that were working up against the previous sunset date of December 31, 2015. Moreover, missing the applicable deadline has much less catastrophic consequences than the Governor had proposed in his 2014 Executive Budget. In that proposal, failure to obtain a CoC by the sunset date would mean the project would have been barred from claiming any of the BCP tax credits. Under BEMA, however, the failure to obtain a CoC by the applicable sunset date will only shift the project into the post-2015 paradigm.*

*As with other sections of BEMA, the measure of whether a project will be considered part of the post-2008/pre-2015 program or part of the post-2015 program is whether the project is accepted into the BCP as of the later of July 1, 2015 or the date the DEC issues required regulations. We have been told informally that DEC is targeting to have those regulations published by the July 1, 2015 date. As a result, projects that have applied or intend to apply to be eligible for the post-2008/pre-2015 program should do everything in their power to have an acceptance letter issued by July 1, 2015.*

## BRTC Credit changes affecting sites accepted on and after the Effective Date

BEMA includes several changes that would take effect for sites that receive notice of acceptance from NYSDEC on or after the Effective Date.

1. **NEW: Separate eligibility "gates" for the Tangible Property Credit Component for sites in NYC ONLY.** The Governor's 2014 and 2015 proposals put forth two "gates" of BCP eligibility - one set of criteria for acceptance into the BCP, and a second set of criteria for the site owner(s) to be eligible for the BRTC's tangible property credit component (*TPCC*). BEMA adopts the two-gate approach, but **only for sites located in a city with a population of one million or more persons**. New York City is the only city in New York State that currently exceeds that threshold. All other BCP sites do not have to meet any additional eligibility criteria for the TPCC. For sites located in such a city, applicants must demonstrate to the satisfaction of NYSDEC that the site meets one of three tests (the so-called "*second gates*"):

- *Option 1: ≥ 50% of site area in EnZone.* The applicant must demonstrate that at least half of the site is located in an Environmental Zone ("*EnZone*"), which the bill would also re-define (a brief description of the changes to EnZones is included below).

- *Option 2: Site is "upside down" or "underutilized."* The applicant would need to demonstrate that the site is either:
    - economically "upside down," meaning that, as of the date of the BCP application, the projected cost of the investigation and remediation exceeds the 75% of the appraised value of the site without contamination; or

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- is "underutilized," which is not defined; however, DEC is instructed to define "underutilized" in regulations after consultation with the business community and the City of New York (again, these gates apply only in NYC). Final regulations are to be adopted no later than October 1, 2015. It is the publication of these regulations on which the Effective Date depends.
- *Option 3: Affordable Housing.* The applicant would need to demonstrate that the site will be developed as an "affordable housing project." The definition of affordable housing was the subject of much debate in the eleventh hour and ultimately was left to be defined in regulations. However, sites that are eligible for the TPCC as "affordable housing projects" will only be eligible for the TPCC based on the affordable housing units, not the costs of the entire project (i.e., the eligible costs will be limited by the ratio of square feet of affordable units to the square feet of the entire building).

*Commentary: The Governor championed a "two-gate" approach in his Executive Budgets for two years in a row. This approach was touted as a response to development on contaminated property that might have otherwise been developed, particularly for sites in the NYC metropolitan area because of the high cost and high demand for land there. Unlike the Governor's proposals, which would have applied state-wide, application of the second gate only to NYC (and, potentially, other large cities) is a much more measured approach and more targeted at the criticisms lodged by the Governor and other critics of the BCP. While NYC sites will have to pass a second gate to be eligible for the TPCC, we expect that many sites will be eligible under the more expansive gates.*

**2. NEW: Limitations on Eligible Tangible Property.** For sites accepted into the BCP after the Effective Date, new limits on costs allowed for the TPCC will apply.

- The following property will be eligible:
  - Depreciable property with a useful life of 15 years or more;
  - "Costs associated with non-portable equipment, machinery, and associated fixtures and appurtenances used exclusively on the site," regardless of whether those items have a useful life of 15 years or more"; and
  - Costs associated with demolition, excavation, and foundation in excess of the amount properly included in the calculation of the site preparation credit component (see below).

*Commentary: Previously, taxpayers were permitted to calculate the TPCC based on the capitalized costs of tangible property with a useful life of four or more years. Items that were previously eligible but will now be ineligible include computers and other office machines, furniture, and decorative items such as artwork. Commercial and residential buildings and depreciable land improvements remain eligible, and most built-in, wired-in, or other items that cannot be regularly moved around should remain eligible. This change appears intended to eliminate credits for easily moved personal property that does not have a long-term life linked to the BCP site.*

*The ability to pick up demolition, excavation, and foundation costs should provide some consolation for taxpayers where the amount of such costs exceed the new limits on such costs in the site preparation component. However, a site's 3x/6x cap based on site preparation costs may be affected by the shift in such costs to the tangible property category.*

Costs for "related party service fees" may also be included. Previous changes proposed by the Governor sought to totally exclude any payments to related parties from the BRTC calculations.

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The concern appeared to be focused on accrued, but deferred, service fees payable to related businesses, such as development fees. BEMA therefore now requires "related party service fees" to be actually paid in order to be eligible for inclusion in the TPCC calculation, and allows the TPCC for those fees to be claimed only in the year actually paid. This approach is consistent with the recommendations of the Brownfield Task Force of the Environmental Law Section of the NYS Bar Association (the memorandum outlining the recommendation, to which Phil Bousquet and Julia Martin contributed, is available on our website at **http://bhlawpllc.com/publications/nysbarBCP**).

*Commentary: This change came out of a perceived abuse by the Tax Department relating to developer fees paid between related parties over a period of time. The Tax Department argued that taxpayers could increase the amount of these developer fees required to be paid to a related party under a contract, and thus boost their credit claims, but ultimately never pay the fee. Early proposals by the Governor would have barred the TPCC on any payments made to a related party. The method taken in BEMA is a significantly more measured approach. Under BEMA, taxpayers may claim the TPCC based on related party service fees only to the extent the fees are actually paid in the taxable year.*

*It is also important to note that related party service fees can be included in the TPCC, but not in the site preparation credit component or the on-site groundwater remediation credit component.*

3. **NEW: Clarification of the timing rule for the Tangible Property Credit Component.** BEMA clarifies that eligible taxpayers may claim the TPCC for up to 120 months after the CoC is issued. BEMA also clarifies that the TPCC will be allowed in the year the CoC is issued for property placed in service prior to the issuance of the CoC - a practice currently approved by the NYS Tax Department in informal advice and in a recent advisory opinion.

*Commentary: The previous provisions of the BCP allowed for the TPCC to be claimed for up to ten taxable years after the CoC was issued. The change from ten taxable years to 120 months can be significant. In the course of many projects, changes in ownership as a result of financing or other conditions may result in taxpayers being required to take a short taxable year. In that case, ten taxable years is actually less than ten calendar years or 120 months. Additionally, the 120 month window affords projects more certainty when determining which costs will be eligible; in order to be eligible for the TPCC, costs must be paid or incurred before the tenth anniversary of the CoC date.*

4. **Applicable Percentage for Tangible Property Credit Component.** BEMA modifies the "applicable percentage" used to calculate the TPCC. For eligible sites (i.e., sites either outside of NYC or in NYC and meeting one of the second gates described above), the TPCC would have an across-the-board base of **10%** of eligible costs (curtailed as noted below), and new "bump-ups" to the applicable percentage - **not to exceed 24%**, in the aggregate- calculated as follows:

- An additional **5%** for qualified tangible property placed in service on brownfield sites located within and developed in conformance with the goals of a Brownfield Opportunity Area (BOA);
- An additional **5%** for the affordable housing units in an affordable housing project as defined above (based on the proportion of square footage of the units in the overall building);
- An additional **5%** for sites used primarily for manufacturing activities;
- An additional **5%** for qualified tangible property placed in service on a brownfield site having at least fifty percent of its area located in an EnZone. ; and
- **NEW:** An additional **5%** for sites remediated to Track 1 standards (formerly 2%).

*Commentary: Compared with the previous TPCC applicable percentage schemes, the applicable percentage calculation under BEMA may be either positive or negative, depending on the characteristics of the site and the redevelopment. In either event, a single base percentage regardless of the type of taxpayer lends welcome predictability to the calculation of the TPCC.*

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The bill would not change the applicable percentage for the site preparation (SPCC) and on-site groundwater remediation (OSGRCC) credit components, but the calculation of those components (as well as the TPCC) would change due to the exclusions and adjustments to the credit bases noted below.

5. **NEW: Changes to the Site Preparation and On-Site Groundwater Remediation Credit Components.** BEMA makes several changes to the definitions of "site preparation costs" and "onsite groundwater remediation costs," which form the basis for calculating the respective credit components.

- "Site Preparation Costs" has been redefined to be all capitalized costs that are necessary to implement the site's investigation, remediation, or qualification for a CoC, including: excavation; demolition; activities undertaken under the oversight of the NYS Department of Labor (DOL) or in accordance with standards established by the Department of Health to remediate and dispose of regulated materials including asbestos, lead, or PCBs; environmental consulting; engineering; legal costs; transportation, disposal, treatment, or containment of contaminated soil; remediation measures taken to address contaminated soil vapor; cover systems consistent with applicable regulations; physical support of excavation; dewatering and other work to facilitate or enable remediation activities; sheeting, shoring, and other engineering controls required to prevent off-site migration of contamination from the qualified site or migrating onto the qualified site; and the costs of fencing, temporary electric wiring, scaffolding, and security facilities until the CoC is issued.
- BEMA also indicates that "site preparation costs" includes costs paid or incurred within 60 months after the last day of the tax year in which the CoC is issued "that are necessary for compliance with the [CoC] or subsequent modifications thereof, or the remedial program defined in such [CoC]," including: institutional controls, engineering controls, an approved site management plan, and the site's environmental easement.

  *Commentary: The list of enumerated types of costs included in the new definition of site preparation costs provides some clarity to taxpayers about what costs will be eligible. Some commenters have raised a concern that by providing such a list, BEMA will serve to exclude costs that would otherwise have been considered site preparation costs but were not included in the enumerated list (either unintentionally or because of unanticipated changes in technology). However, based on the language making the enumerated list inclusive, not exclusive, we believe the enumerated list is a positive change in the BCP legislation.*

  *BEMA does not revise the section of the law that deals with the timing of claims for the SPCC. Currently, SPCC claims based on post-CoC costs are allowed "for the taxable year in which the improvement to which the applicable costs apply is placed in service for up to five taxable years after the issuance [of the CoC]." This existing timing rule may be unworkable or unclear because BEMA indicates that appropriate post-CoC costs are compliance-type costs that may not relate to a particular improvement to be placed in service. In contrast, OSGWCC claims based on post-CoC costs are allowed in the taxable year such costs are paid or incurred. It is our expectation that the incongruous provisions of the existing SPCC timing rule will be addressed in technical corrections and the result will be similar to the timing rule for post-CoC OSGWCC claims. We will provide a future alert when and if this correction is made.*

- BEMA makes clear that "site preparation costs" includes foundation costs, but only to the extent of the costs of the cover system required for the site

  *Commentary: We recommend that developers obtain a quote for a site cover that meets the requirements of the applicable regulations. The quote will serve as the basis for determining the amount of foundation costs that are eligible to be included in the SPCC. As indicated above, any costs in excess of the comparable site cover is eligible to be included in the TPCC calculation.*

- BEMA includes a list of potential enumerated costs that would be eligible for the on-site groundwater remediation credit component.

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## Other changes to the BCP

The proposed budget includes many other non-tax BCP changes not discussed above, including:

1. **Elimination of Section 22 and 23 credits**. Consistent with the Governor's proposal, BEMA eliminates the BCP credits based on property taxes and environmental insurance premiums for all sites accepted into the BCP after the Effective Date.
2. **New definition of EnZone.** BEMA transfers the authority for designating EnZones to the Commissioner of the DOL and would base the determination of EnZone status on the characteristics of each census tract determined in the most recent five year American Community Survey (ACS). Currently, EnZones are based upon data from the 2000 Census. DOL must redraw EnZones based on the 2009-13 ACS within 90 days of enactment of BAM. At the request of DEC, EnZone designations may be updated based on the most recent five-year ACS. The determination of whether a site is located in an EnZone will be made based upon EnZone designations in effect as of the date DEC notifies an applicant that its application to participate in the BCP is complete.
3. **BCP-EZ Program**. BEMA creates a BCP-EZ Program that will allow volunteer applicants to waive their right to all BCP tax credits and enter into a modified remedial program exempt from procedural requirements (as specified by DEC) relating to investigation and remediation. The BCP-EZ Program has been proposed consistently in both the 2014 legislative session as well as the proposals set forth earlier this year.
4. **CoC transfers**. BEMA clarifies that a CoC can be transferred to a successor to a real property interest in all or a portion of a brownfield site, including legal title, equitable title, or leaseholds. BEMA also provides that the CoC could not be transferred to a responsible party.
5. **DEC oversight costs**. BEMA permits negotiation of flat-fee arrangements with participants.

## Next Steps

BEMA was passed into law on April 13, 2015. The final Effective Date will be determined once DEC issues proposed regulations on the definition of "underutilized." Bousquet Holstein's Brownfield Practice Group is closely monitoring developments in this area and we intend to issue an additional alert once the regulations are released. Please do not hesitate to **contact us** with any questions you may have regarding these BCP developments and how they may impact your brownfield projects.

**Philip S. Bousquet**

**phil@bhlawpllc.com**
**315.701.6309**

**Julia J. Martin**

**jmartin@bhlawpllc.com**
**315.701.6474**

**Bousquet Holstein PLLC**
**110 West Fayette Street, Suite 900 ◆ Syracuse, NY 13202 ◆ 315.422.1391**
**www.bhlawpllc.com**