

Brownfields Tax Incentive - Frequently Asked Questions

This document provides answers to some of the most frequently asked questions (FAQ) about the federal Brownfields Tax Incentive. The questions are divided into the following sections:

- I. Background on the Brownfields Tax Incentive**
- II. Meeting the Contamination Criteria**
- III. Determining Eligible Expenses**
- IV. Meeting the Ownership Criteria**
- V. Securing State Eligibility Statements**

I. Background on the Brownfields Tax Incentive

Q1: What is the Brownfields Tax Incentive?

A1: The Brownfields Tax Incentive was passed as part of the Taxpayer Relief Act of 1997 (Public Law 105-34), and codified through Section 198(a) of the Internal Revenue Code. The incentive allows a taxpayer to fully deduct the costs of environmental cleanups in the year the costs were incurred rather than spreading them over a period of years. Its purpose is to spur the cleanup and redevelopment of brownfields.

In December 2006, the Brownfields Tax Incentive was extended to cover eligible expenses through December 31, 2007 and expanded to allow the deduction of expenses for the cleanup of petroleum products (e.g., crude oil, crude oil condensates, and natural gasoline), which had previously been ineligible.

Q2: Why is the Brownfields Tax Incentive beneficial?

A2: Federal tax law generally requires that the cost of property improvements must be deducted over a period of years. Other expenses, such as repairs, may be deducted in the same year they are incurred. For some taxpayers, the accelerated deduction of the Brownfields Tax Incentive may provide a financial benefit that will stimulate brownfields cleanup and revitalization.

Q3: What properties are eligible for the Brownfields Tax Incentive?

A3: The Brownfields Tax Incentive is applicable to properties that meet specific land use and contamination requirements. To satisfy the land use requirement, the property must be held by the taxpayer incurring the eligible expenses for use in a

trade or business or for the production of income; or the property must be included in the taxpayer's inventory. To satisfy the contamination requirement, the taxpayer must demonstrate that there has been a release, threat of release, or disposal of a hazardous substance at the property.

Sites listed, or proposed for listing, on EPA's Superfund National Priorities List (NPL) are not eligible for the incentive. Only expenses that are paid for or incurred in connection with the abatement or control of a hazardous substance qualify for the incentive. Taxpayers should consult with their tax counsel to determine which expenses are eligible. Taxpayers must also consult with their appropriate state Brownfields Tax Incentive contact to verify a property's eligibility and obtain the required state property eligibility statement. A list of state Brownfields Tax Incentive contacts can be found at: <http://www.epa.gov/swerosps/bf/stxcntct.htm>.

Q4: Are taxpayers who cause contamination eligible for the Brownfields Tax Incentive?

A4: Responsible parties who contaminate and remediate a property without changing its use have always been able to deduct environmental cleanup costs as an operating expense. The Brownfields Tax Incentive allows these same property owners to also expense these costs if they are changing the use of the property.

Q5: Are there still geographic/socioeconomic area eligibility requirements for the Brownfields Tax Incentive?

A5: The Brownfield Tax Incentive's geographic and socioeconomic requirements no longer apply. These former requirements, which were part of the original incentive when it took effect on August 5, 1997, were eliminated on December 21, 2000.

Q6: Have there been lapses in the Brownfields Tax Incentive?

A6: The Brownfields Tax Incentive became temporarily inactive after its earlier expiration date of December 31, 2005. On December 20, 2006, the incentive was reactivated retroactively to January 1, 2006 and extended through December 31, 2007. Eligible expenses incurred in 2006 prior to the incentive's reactivation can still be deducted under the incentive. So while the incentive was temporarily inactive, its coverage of eligible expenses has not lapsed.

II. Meeting the Contamination Criteria

Q7: What is the definition of "hazardous substance" in the tax provision?

A7: The definition of "hazardous substance" in the tax provision is in large part based on Section 101(14) of the Comprehensive Environmental Response,

Compensation, and Liability Act (CERCLA)¹.

Q8: Does the Brownfields Tax Incentive distinguish between hazardous wastes and hazardous substances?

A8: The definition of “hazardous substance” in CERCLA Section 101(14) includes certain “hazardous wastes.” For example, the CERCLA definition of hazardous substances includes wastes that EPA lists under RCRA or hazardous wastes that are ignitable, corrosive, reactive, or toxic.

Q9: Are petroleum and oil eligible contaminants under the Brownfields Tax Incentive?

A9: In December 2006, the tax incentive was amended to allow the deduction of expenses for the cleanup of petroleum products (e.g., crude oil, crude oil condensates, and natural gasoline). This new eligibility for petroleum products applies to cleanup expenses incurred from January 1, 2006 through the incentive’s current expiration date of December 31, 2007.

Q10: Can EPA clarify “a release or threat of a release”?

A10: CERCLA 101(22) defines the term “release” to include, “any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, or disposing into the environment.” Much case law exists on what constitutes a release or threat of a release that should help the states in making this determination. Taxpayers should consult with tax counsel and their appropriate state agency contact to clarify whether the circumstances at their property qualify as a release or threat of release under the tax incentive. A list of state contacts can be found at: <http://www.epa.gov/swerosps/bf/stxcntct.htm>.

Q11: What documentation must taxpayers provide to their state to show that there has been a release or a threat of release?

A11: Taxpayers and/or their tax counsel should contact their designated state agency to determine what documentation the state will require in order to provide the state property eligibility statement. A list of state contacts can be found at: <http://www.epa.gov/swerosps/bf/stxcntct.htm>.

Q12: How does the Gulf Opportunity Zone Act complement the Brownfields Tax Incentive?

A12: On December 21, 2005, President Bush signed the Gulf Opportunity Zone (GO Zone) Act of 2005 to provide tax benefits for areas affected by Hurricane Katrina, and certain additional areas affected by Hurricanes Rita and Wilma.

¹ U.S. Code Title 26, Subtitle D, Chapter 38, Subchapter A, §§4612

Intended to speed rebuilding efforts in hurricane-impacted gulf areas, the GO Zone Act allows businesses to deduct 50 percent of their cleanup and demolition costs. Because the Brownfields Tax Incentive allows the deduction of 100 percent of cleanup costs, and because deductions under the incentive and the GO Zone cannot be claimed simultaneously, it may be more beneficial to use one or the other depending on expense eligibility. Taxpayers should consult with tax counsel and their appropriate state agency contact to determine the circumstances in which a taxpayer's activities may qualify for deduction. A list of state contacts can be found at: <http://www.epa.gov/swerosps/bf/stxcntct.htm>.

Q13: Are there any petroleum-cleanup deductions under the GO Zone Act not allowed under the Brownfields Tax Incentive?

A13: While the Brownfields Tax Incentive allows the deduction of petroleum-related cleanup expenses incurred from January 1, 2006 to the incentive's current sunset date of December 31, 2007, those expenses are allowable under the GO Zone Act from August 28, 2005 through December 31, 2007. The GO Zone Act only allows deductions for 50 percent of these costs; but if your petroleum-related cleanup expenses were incurred from August 28, 2005 through December 31, 2005, this provides an opportunity not allowable under the Brownfields Tax Incentive to deduct half of those costs.

III. Determining Eligible Expenses

Q14: What is the difference between incurring and paying for an expenditure? If the taxpayer incurs an allowable expenditure in one tax year, but pays for it in another tax year, does the taxpayer get to elect in which tax year to take the deduction?

A14: Generally, the year in which the taxpayer may take a deduction will depend on the taxpayer's accounting method. Taxpayers should consult with tax counsel to determine when specific expenditures must be taken into account for tax purposes.

Q15: Referring to Section 198(b)(1)(A) of the Brownfields Tax Incentive, what does it mean to be "otherwise chargeable to capital account?" What are allowable expenses?

A15: The Brownfields Tax Incentive was created to permit a taxpayer to obtain a current deduction for certain environmental remediation costs, rather than delay the deduction to a future year. Certain environmental remediation costs must be capitalized, i.e., included in the cost of the taxpayer's property and recovered as the property is used, sold, or otherwise disposed of. Other environmental remediation costs may be expensed during the year in which they were paid for or incurred. The Brownfields Tax Incentive only seeks to impact the former category. If an expense is already deductible within the year it was incurred, there

is no need to invoke the provisions of the incentive.

The category of allowable expenses under the Brownfields Tax Incentive is broad. Taxpayers should consult with tax counsel to determine whether specific cost items are allowable expenses.

Q16: Can the expenditures from the removal of asbestos or lead from a building be deducted under the Brownfields Tax Incentive?

A16: Section 198(d) of the Brownfields Tax Incentive excludes expenditures associated with substances for which a removal or remedial action would not be permitted under CERCLA §104(a)(3). CERCLA §104(a)(3) generally provides that a removal or remedial action cannot be taken to address products that are part of the building structure and result in exposure within residential buildings or business or community structures (e.g., interior lead-based paint contamination or asbestos which results in indoor exposure). Taxpayers should consult with tax counsel and their appropriate state agency contact to determine the circumstances in which a taxpayer's activities may qualify for deduction. A list of state contacts can be found at: <http://www.epa.gov/swerosps/bf/stxentet.htm>.

Q17: Do costs for site assessment and investigation activities qualify as remediation expenditures under the Brownfields Tax Incentive?

A17: Yes. Site assessment and investigation activities are qualified environmental remediation expenditures if incurred "in connection with the abatement or control of hazardous substances at a qualified contaminated site." Site assessment efforts must, therefore, be part of a larger abatement or control effort to qualify under the tax incentive.

Q18: Can expenditures for assessment or monitoring inside a building qualify for the Brownfields Tax Incentive?

A18: These expenditures may qualify for the Brownfields Tax Incentive if the costs can be characterized as environmental remediation costs and were used in connection with the abatement or control of a release or a threat of release of a hazardous substance. However, see Question/Answer #16 regarding limitations on expenditures associated with indoor contamination.

Q19: Do the costs related to construction of access roads and operations and maintenance (O&M) qualify as remediation expenditures?

A19: Yes, if the access road or O&M activity is paid for or incurred in connection with the abatement or control of a release, threat of release, or disposal of a hazardous substance at the property.

Q20: Do state voluntary cleanup program (VCP) oversight fees qualify as

remediation expenditures?

A20: Yes, if these costs are used in connection with the abatement or control of a release, threat of release, or disposal of a hazardous substance at the property.

Q21: Can taxpayers deduct and/or depreciate the remediation expenditures under the Brownfields Tax Incentive if they are going to reuse the property for a park or open space?

A21: No, the taxpayer must hold the property for use in trade or business or for the production of income to qualify for the Brownfields Tax Incentive.

Q22: How would the Brownfields Tax Incentive apply in a situation where a taxpayer capped soil contamination with a parking lot?

A22: The service costs related to the soil remediation and cap construction would be deductible. The portion of the parking lot truly functioning as the cap (underneath the asphalt) may qualify as a deductible expense under the incentive.

Q23: Assume a responsible party settled with a state, and the state uses these settlement funds to conduct remediation activities over the next few years. Can the taxpayer claim these expenditures under the Brownfields Tax Incentive?

A23: Qualified settlement funds were not addressed in the legislation. It is unlikely that the taxpayer would be able to claim these expenses since the funds have already been turned over to the state.

Q24: Does the IRS plan to issue regulations listing those costs that qualify as eligible expenses under the Brownfields Tax Incentive and those that do not?

A24: No. At this point, the IRS does not plan to issue regulations about the Brownfields Tax Incentive.

Q25: How far back can cleanup costs be deducted under the Brownfields Tax Incentive?

A25: The Brownfields Tax Incentive became law on August 5, 1997. While amended tax returns may be filed to deduct expenditures from prior tax years, IRS guidance indicates that such returns must be filed within three years after the date a corporation filed its original return, or within two years after the date a corporation paid the tax (if filing for a refund), whichever is later. The IRS or a qualified tax professional should be consulted if there is any uncertainty as to whether prior tax year deductions are allowable.

IV. Meeting the Ownership Criteria

Q26: With regard to the definition of “qualified contaminated site” in Section 198(c)(1)(A) of the Brownfields Tax Incentive, what types of uses constitute “a trade or business or for the production of income, or which is property described in section 1221(1) in the hands of the taxpayer?”

A26: Each of these terms is a term of art in the tax world. Generally, any property used for non-personal purposes will be considered qualified under this portion of the law. Section 1221(1) properties are generally inventory properties or properties held by the taxpayer for sale in the course of his or her trade or business.

Q27: Does an environmental assessment paid for by a prospective purchaser of a qualified contaminated site qualify as an environmental remediation cost?

A27: Generally, these costs are not eligible for the tax incentive since the law requires that the property must be “held by the taxpayer.” Taxpayers should consult with tax counsel to determine circumstances in which property is considered “held by the taxpayer” for purposes of determining whether it is a “qualified contaminated site.”

Q28: Can investment properties and properties held by a developer for future sale qualify for the tax incentive?

A28: Yes. Properties held by the taxpayer for use in trade or business or for the production of income, including investment properties and properties held by a developer for future sale, can qualify for the Brownfields Tax Incentive.

Q29: Are properties owned by a municipality, and leased to a taxpayer, eligible for the Brownfields Tax Incentive?

A29: The answer depends upon whether the property is considered “held by the taxpayer.” There are conceivable circumstances where a municipally-owned property might be considered a qualified contaminated property and where environmental remediation costs might qualify for the incentive. A taxpayer who pays for remediation at a property for which he or she has a long-term lease (e.g., 99 years) on municipally-owned property might qualify for the incentive. Taxpayers should consult with tax counsel to determine circumstances in which a taxpayer’s property may qualify for the incentive.

Q30: Are there any circumstances where leased or rented properties would meet the criteria “held by the taxpayer?” For example, if an historic land trust specifically prevents ownership and the tenant operates on repeating 3-

year leases, would the tenancy qualify as being held by the taxpayer-tenant?

A30: Again, the answer depends upon whether the property is considered “held by the taxpayer.” There are conceivable circumstances where a leased property might qualify for the incentive. A taxpayer who pays for remediation at a property for which he or she has a long-term lease (e.g., 99 years) might qualify for the incentive. Short-term leases, including 3-year leases, would probably not qualify unless there was a continuing commitment to renew the lease year after year. Taxpayers should consult with tax counsel to determine circumstances in which the taxpayer’s property may qualify.

V. Securing State Property Eligibility Statements

Q31: What are the states’ roles under the Brownfields Tax Incentive?

A31: States address two basic requirements under the tax incentive. First, the law required that each state designate, within sixty (60) days after the law’s enactment (August 5, 1997), a lead agency as the “appropriate state environmental agency” to handle inquiries and requests for property certifications from its taxpayers. The law authorized EPA to make this designation if states did not make it within 60 days.

Second, the law required that states provide each of their taxpayers, upon request, a written statement that a specific property meets the following two elements of the “qualified contaminated site” requirement: (a) the property is within a defined targeted area (this geographic requirement is no longer applicable; see Question/Answer #5 for further details); and (b) there has been a release, threat of release, or disposal of any hazardous substance at or on the property. It is expected that taxpayers will rely upon tax counsel, not their designated state agency, for clarification of other issues related to the Brownfields Tax Incentive.

If contact information at the designated state agency changes, the state should notify EPA of the information change. States can send updated contact information to EPA’s Office of Brownfields Cleanup and Redevelopment at (202) 566-2777. A listing of state contacts can be found here:

<http://www.epa.gov/swerosps/bf/stxcntct.htm>.

Q32: How can a taxpayer verify that a property is eligible for the Brownfields Tax Incentive?

A32: Taxpayers need to receive a statement from their designated state agency (usually the department responsible for environmental protection) that there has been a release, threat of release, or disposal of any hazardous substance at or on the property. Taxpayers and/or their tax counsel should contact their designated state agency to learn what documentation the state requires the taxpayer to submit in order to obtain this statement. Once the statement is issued, the IRS will

consider it valid for the life of the tax incentive. To claim the deduction, you need simply write “Section 198 Election” on your income tax return next to the line where you claim the deduction. Any written verification received from the state should be maintained in the taxpayer’s records.

Taxpayers can find contact information for their designated state agencies by accessing EPA’s Office of Brownfields Cleanup and Redevelopment Web site at <http://www.epa.gov/swerosps/bf/stxcntct.htm>. The taxpayer is responsible for certifying that he or she holds the property for business purposes and that he or she incurred qualified environmental remediation expenses.

Q33: How does a state verify eligibility?

A33: Methods of verifying a property’s eligibility vary from state to state. Wisconsin, for example, will require that the applicant attach a letter from the appropriate municipality indicating that the area meets the industrial zoning criteria. Several states provide property eligibility statements for taxpayers. Michigan, for example, relies on taxpayers to verify that there has been a release or threat of a release, or disposal, of a hazardous substance at or on the property. Michigan has developed a checklist that walks taxpayers through eligibility requirements and provides guidance on the type of information they must submit to prove that a property meets the established criteria. In addition, Michigan developed an affidavit template for taxpayers to complete and submit to the state. Once the taxpayer has submitted the affidavit and supporting documents, Michigan conducts a desktop review of the materials and either declares the property eligible or tells the taxpayer what sort of additional information is needed. Taxpayers should check with their designated state agency for more information.

Q34: How long are state property eligibility statements valid? Will the states have to issue statements for sites incurring ongoing O&M costs each year?

A34: Property eligibility statements are valid for the applicable life of the incentive (currently scheduled to sunset on December 31, 2007). The IRS, not the states, has the authority to determine whether the ongoing O&M costs are eligible remediation expenditures.

Q35: Can a state declare a property eligible before any work has been done on abatement and control?

A35: Yes. States are responsible for providing a statement that there has been a release or threat of a release, or disposal, of a hazardous substance at or on the property. States are not responsible for determining whether or not any abatement or control activities have taken or will take place.

Q36: What if a request for a state property eligibility statement identifies a

contaminated property of which the state was not previously aware? Do properties identified pursuant to the tax incentive go on a federal cleanup “list?”

A36: If a state learns about a property through its property eligibility process, it may determine that the property warrants state involvement. EPA does not believe this will create a disincentive to requesting a state property eligibility statement. This does, however, raise the point that the taxpayers may want to gather some preliminary information on their property before talking to the state about it. Taxpayers can use tools available over the Internet, such as census data, to do this. There is no federally maintained list of properties identified under the Brownfields Tax Incentive. States, however, may maintain such a list and may choose to refer sites of potential federal interest to EPA.

Q37: Can a state that requires taxpayers by law to inform the state of a release or threat of a release use the Brownfields Tax Incentive state property eligibility statement requests as a form of such notification and require the owner to undergo cleanup?

A37: A state may determine, based on information provided in order to obtain a state property eligibility statement, that a release or threat of release warrants state involvement, including a state enforcement action. EPA recommends that states that plan on using submitted information in this manner inform taxpayers of this possibility on the property eligibility statement application.

Q38: How are the Tribal reservations being handled with regard to the Brownfields Tax Incentive?

A38: The statute does not specifically address this issue. The Department of the Treasury has indicated that this will be handled on a case-by-case basis.

Other Resources

These Frequently Asked Questions were prepared in partnership with the Department of Treasury, Department of Commerce's Economic Development Administration, Department of Housing and Urban Development, and the Small Business Administration. Taxpayers should also consider the following resources for information on the Brownfields Tax Incentive.

- Internal Revenue Service Publications. To confirm whether property or expenses are eligible for deduction under the Tax Incentive, taxpayers should consult with tax counsel. It may also be useful to consult with an environmental attorney. In addition, the state contacts available at <http://www.epa.gov/brownfields/stxcntct.htm> may provide needed technical assistance on using the tax incentive.
- U.S. Environmental Protection Agency. For more information, please contact EPA's Office of Brownfields Cleanup and Redevelopment at (202) 566-2777 or your [Regional Brownfields Coordinator](#).
- U.S. EPA's Enviromapper. This Web-based database enables a user to map various types of environmental information, including air releases, drinking water, toxic releases, hazardous wastes, water discharge permits, and Superfund sites. Enviromapper can be accessed at: <http://www.epa.gov/enviro/html/em/index.html>.
- Guidelines on the Brownfields Tax Incentive, as well as a general fact sheet, can be found at: <http://www.epa.gov/brownfields/bftaxinc.htm>.
- Five case studies on the Brownfields Tax Incentive can also be found at: <http://www.epa.gov/brownfields/bftaxinc.htm>.