

LIMITED-SCOPE AUDIT PROPOSAL

Determining What Issues the Kansas Department of Revenue Has Identified in Its Reviews of the Kansas Historic Rehabilitation Tax Credit

SOURCE

This audit proposal was requested by Senator Caryn Tyson, Senator Larry Alley, Representative Adam Smith, and Representative Sean Tarwater.

BACKGROUND

The legislature created the Kansas Historic Rehabilitation Tax Credit program in 2001 to encourage people to restore and preserve historic buildings. It allows taxpayers to claim an income, premium, or privilege tax credit for certain spending to renovate historic buildings. The owner of the historic building (which can be an individual or a business such as a bank) can claim a credit worth 25% to 40% of their qualified expenses depending on the size of the city where the building is located. Buildings in smaller cities are eligible for a 40% credit, whereas buildings in larger cities are eligible for a 25% credit. Taxpayers can carry forward the credit for up to 10 years. Taxpayers also can sell (or transfer) the credit to other Kansas taxpayers. Those taxpayers can carry forward the credit for up to 5 years so long as the full credit is used within the original 10-year timeframe.

The Kansas Historical Society and the Kansas Department of Revenue (KDOR) jointly implement the tax credit program. The Historical Society is responsible for determining which projects are eligible to participate in the program and approving all participants' rehabilitation plans to ensure compliance with federal and state requirements. KDOR is responsible for processing taxpayers' income tax returns. This includes the rehabilitation credits taxpayers claim against their tax liabilities.

The Historical Society and KDOR split responsibilities for reviewing taxpayers' claims under the Historic Rehabilitation Tax Credit program based on the projects' total costs. The Historical Society currently reviews all projects that cost less than \$1 million and KDOR reviews all projects that cost \$1 million or more. Those reviews are intended to ensure that taxpayers have documentation such as receipts to support their reported expenses.

Legislators have expressed interest in understanding the frequency and types of issues KDOR finds during its reviews.

AUDIT OBJECTIVES AND TENTATIVE METHODOLOGY

The audit objective listed below is the question we would answer through our audit work. The steps listed for the objective convey the type of work we would do. These may change as we learn more about the audit issues.

Objective 1: What issues has the Kansas Department of Revenue identified in its recent reviews of the Kansas Historic Rehabilitation Tax Credit program? Our tentative methodology would include the following:

- Read state law and regulations, work with KDOR and Historical Society staff, and review relevant program guidance to develop an understanding of the Historic Rehabilitation Tax Credit program. This work would include developing an understanding of both agencies' review processes such as which claims they review and what they review them for.
- For a few recent years, work with KDOR staff to review the findings from their reviews of the tax credit program to determine the frequency and types of issues they've identified and the causes of those issues. Review supporting documentation for a selection of KDOR's reviews as needed to verify their determinations.
- Talk to KDOR staff and Historical Society staff as needed about any recurring patterns or themes in the issues KDOR identified in its reviews and what they're doing to try to mitigate or prevent those systemic issues.

ESTIMATED RESOURCES

We estimate this audit would require **100 staff hours** to complete.