

Internal Revenue Code Section 198, The Tax Incentive for Brownfield Redevelopment: A Sheep in Wolf's Clothing

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I. INTRODUCTION

As the world advances, both industrially and technologically, society must endure the negative side effects of such advancements.¹ Most notably, urban sprawl and decay produce deplorable living conditions in urban areas.² A major component of urban sprawl and

* J.D., Washington University School of Law, 2001. I would like to dedicate this Note to my family, Tanveer and Nelofer Kirmani, Nay Haque, and most of all Syed and Najima Amin.

1. See Peter K. Johnson, Note, *Mr. Smith Goes to Washington: 1997 Superfund Amendments: Will it Solve the Liability Problem and How Will This Affect Massachusetts?*, 31 NEW ENG. L. REV. 1269, 1272 (1997) (discussing how industrialization produced not only jobs and technology, but also chemical wastes and manufacturing by-products that, when not disposed of properly, cause serious environmental harm).

2. William W. Buzbee, *Urban Sprawl, Federalism, and the Problem of Institutional Complexity*, 68 FORDHAM L. REV. 57, 69 (1999). Buzbee argues that the lack of inner-city investment causes a loss of refurbished residential housing which leads to decreasing property values, and in turn harms vulnerable residents such as children. *Id.* The declining property values lead to a decreased tax base, and illustrates the need for higher tax rates to compensate for lost revenue and to fund social services. *Id.* at 69-70. All the lost revenues and lack of investment leads to deteriorating housing, and is often accompanied by the departure of local employers and industry. *Id.* at 70 (citing KENNETH T. JACKSON, *CRABGRASS FRONTIER: THE SUBURBANIZATION OF THE UNITED STATES* 266-71 (1985)); see generally Georgette C. Poindexter, *Towards a Legal Framework for Regional Redistribution of Poverty-Related Expenses*, 47 WASH. U.J. URB. & CONTEMP. L. 3, 6-7 (1995) (describing the dilemma of municipal officials arising from the region's concentration of economically challenged residents in the inner-city). Consequently, the tax base of the city is disproportionately less than that of the area's suburbs. *Id.* at 7.

decay is a phenomenon known as “brownfields.”³ According to the Environmental Protection Agency (EPA), brownfields are sites in urban areas that are either abandoned, idled, or under-utilized because environmental contamination complicates redevelopment of those sites.⁴ The recent trend of investors developing outside of urban areas compounds the problem by building on unpolluted land instead of rehabilitating brownfields.⁵ Investors leave urban areas because they fear the potential liability of operating on or owning a contaminated site.⁶ Instead, they opt for non-polluted, suburban sites known as “greenfields.”⁷ While choosing a greenfield can be a sound business decision, the lack of investment in the inner-city results in reduced opportunities for local residents.⁸ Residents of the inner-city, where brownfields are found, are often members of economically vulnerable minority groups.⁹ Therefore, the lack of investment in the urban center erodes the job market and tax base of the inner-city, broadening the gap between the rich and the poor.¹⁰ Furthermore, the

3. *Multiple Factors Should Shape Choice of Technology for Brownfields*, 27 Env't Rep. (BNA) No. 48, at 2489 (Apr. 11, 1997) (explaining that there are as many as 650,000 brownfield sites throughout the United States and the average remediation effort for a brownfield site is \$250,000); *Brownfields: Agenda on Brownfields Shows Government at its Best, Browner Tells Conference*, Daily Env't Rep.; (BNA) No. 172, at A-3 (Sept. 5, 1997).

4. *Solid Waste and Emergency Response, U.S. EPA, The Brownfields Economic Redevelopment Initiative: Proposal Guidelines for Brownfields Assessment Demonstration Pilots*, EPA No. 500-F-97-156, 3 (Oct. 1997); see also Andrea Lee Rimer, *Environmental Liability and the Brownfields Phenomenon: An Analysis of Federal Options for Redevelopment*, 10 TUL. ENVTL. L.J. 63, 65 (1996).

5. *Tax Incentive Will Help Eliminate Urban Eyesores, Gore Says*, Daily Tax Rep. (BNA) (Feb. 5, 1996), available at LEXIS 1996 DTR 23 d9. Vice President Gore explained in a speech to the National Association of State Development Agencies that contaminated urban sites have not been redeveloped due to “‘the fear’ associated with the liability of owning contaminated sites.” *Id.*; see also Buzbee, *supra* note 2, at 69.

6. See William W. Buzbee, *Brownfields, Environmental Federalism, and Institutional Determinism*, 21 WM. & MARY ENVTL. L. & POL'Y REV. 1, 14 (1997).

7. Douglas A. McWilliams, Comment, *Environmental Justice and Industrial Redevelopment: Economics and Equality in Urban Revitalization*, 21 ECOLOGY L.Q. 705, 714 (1994). Unlike a brownfield a greenfield site is located upon land that is untainted by contamination because it has never been used for manufacturing or commercial activities. *Id.*

8. *Id.*

9. See, e.g., Mark R. Rank, *The Racial Injustice of Poverty*, 1 WASH. U. J.L. & POL'Y 95 (1999); JUST TRANSPORTATION: DISMANTLING RACE AND CLASS BARRIERS TO MOBILITY 25-26 (Robert D. Bullard & Glenn S. Johnson eds., 1997). See generally Edward A. Zelinsky, *Metropolitanism, Progressivism, and Race*, 98 COLUM. L. REV. 665 (1998) (book review).

10. See Zelinsky, *supra* note 9.

increasing demand for greenfields results in the bulldozing of forests and increased urban sprawl. As a result, cities must build new traffic infrastructures away from public transportation routes and the resulting longer commutes to work translates into increased pollution.¹¹

The federal government is attempting to redevelop troubled urban areas to promote commercial activity and thereby rejuvenate the inner-city.¹² The Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) was designed to remedy environmental problems, such as brownfield sites.¹³ However, CERCLA's results have fallen well short of Congress' anticipated goals.¹⁴ As a consequence, the federal government enacted section 198 of the Internal Revenue Code, to help curb the brownfield phenomenon.¹⁵ Section 198 of the Internal Revenue Code allows a tax deduction for brownfield remediation expenses.¹⁶ This incentive is designed to encourage private parties to pay for the

11. See R. Michael Sweeney, *Brownfields Restoration and Voluntary Cleanup Legislation*, 2 ENVTL. LAW. 101, 103 (1995).

12. Mildred Wigfall Robinson, *Empowerment Zones and Enterprise Communities Under the Omnibus Budget and Reconciliation Act of 1993: A Promising Concept With Some Modifications*, 11 J.L. & POL. 345, 346 (1995). Specifically, the Omnibus Budget and Reconciliation Act of 1993 implemented federal participation in the establishment of enterprise communities and empowerment zones. See Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, § 13301-13303, 107 Stat. 312, 548-56 (1993) (codified at I.R.C. §§ 1391).

13. See, e.g., Jerome M. Organ, *Superfund and the Settlement Decision: Reflections on the Relationship Between Equity and Efficiency*, 62 GEO. WASH. L. REV. 1043, 1046-48 (1994) (explaining that Congress passed CERCLA to force polluters to pay the cost of the clean-up of contamination, rather than placing the burden on the taxpayers).

14. See, e.g., Robert W. McGee, *Superfund: It's Time for Repeal After a Decade of Failure*, 12 UCLA J. ENVTL. L. & POL'Y 165 (1993); *Superfund Needs Reform to Speed Toxic Cleanup*, U.S.A. TODAY, Feb. 2, 1994, at 10A.

15. Adam Gropper, Note, *Getting the Green Back: Remediating Brownfields Under Internal Revenue Code § 198*, 5 ENVTL. LAW. 281, 282 (1998).

16. I.R.C. § 198 (West Supp. 1998).

remediation costs, because the government lacks funds to finance the cleanup itself.¹⁷

While brownfields remediation is of the utmost importance, the tax deduction strategy does not provide enough incentive to effectively accomplish urban redevelopment.¹⁸ The government should take affirmative action to provide real benefits to the remediator and ensure that the brownfield phenomenon is addressed.¹⁹ The current strategy of using a tax deferral as an incentive provides only a mediocre benefit to taxpayers who decide to remediate a brownfield site.²⁰

This Note discusses the potential consequences and drawbacks of the current tax treatment of environmental brownfields remediation. Part II provides a discussion of the applicable environmental clean-up mechanisms. Part III analyzes the tax treatment of environmental remediation projects. Part IV discusses problems with the current expensing of environmental remediation costs. Part V emphasizes the need for a thorough federalized approach. Finally, Part VI proposes a model federal tax credit program.

17. S. REP. NO. 105-33, at 110 (1997) (explaining expressing that the Senate Finance Committee enacted Code Section 198 “[t]o encourage the cleanup of contaminated sites” by private parties). See generally Steven G. Black, Note, *The Continuing Saga of Environmental Clean up Costs: Current Deduction Allowed Under the Restoration Principle of Plainfield-Union*, 4 BYU L. Rev. 1321, 1345-46 (1995).

18. In general, the more favorable the tax treatment, the more likely that the clean-up will be prompt and thorough. J. Andrew Hoerner, *Tax Treatment of Environmental Cleanup Costs: An Environmental View*, 94 TAX NOTES TODAY 166-445 (1994).

19. See generally LLOYD S. DIXON ET AL., RAND INSTITUTE FOR CIVIL JUSTICE, SUPERFUND: PRIVATE-SECTOR EXPENDITURES AND TRANSACTION COSTS 45 (1993) (citing problems with CERCLA enforcement due to its high transaction cost which prevent the intended benefit of CERCLA was not being realized).

20. See H.R. 4094, 105th Cong. (1998) (reporting on the Committee on Commerce is and the Committees on Ways and Means’ and Small Business’ consideration of an environmental remediation tax credit for the incurred costs of qualified contaminated sites).

II. CURRENT ENVIRONMENTAL CLEAN-UP MECHANISMS

*A. The Comprehensive Environmental Response, Compensation and Liability Act of 1980*²¹

In the wake of the Love Canal Disaster,²² Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA).²³ Congress designed CERCLA to clean up hazardous waste sites and to “find parties who could be held accountable to pay for such clean-ups.”²⁴ In addition, CERCLA gives the EPA the authority to enforce a clean up effort in the event of “release or threat of release”²⁵ of a “hazardous substance”²⁶ from a

21. See Comprehensive Environmental Response, Compensation, and Liability Act of 1980, Pub. L. No. 96-510, 94 Stat. 2767 (1986). For a discussion on the congressional intent behind CERCLA, see Organ, *supra* note 13, at 1046-54. In general, Superfund was enacted to address the environmental contamination resulting from past waste disposal practices, that had previously gone unregulated. *Id.* at 1046-47.

22. From 1942 through 1953, the Hooker Chemical Company placed 21,000 tons of chemical waste in an abandoned hydroelectric channel in Love Canal, New York. See PETER S. MENELL & RICHARD B. STEWART, ENVIRONMENTAL LAW AND POLICY 612-14 (1994). In 1953, Hooker Chemical covered the site and sold the property to the Niagara Falls Board of Education for one dollar. *Id.* at 612. In turn, the Board of Education built a school and playground on the site, and used the surrounding land for residential purposes. *Id.* at 612-13. Subsequently, toxic chemicals were discovered to have seeped into the soil and groundwater, thus endangering the health and safety of the community. The incident received national media attention, causing New York's health commissioner to declare a public emergency. *Id.* at 613. In March of 1998, twenty years after the fact, Occidental Petroleum, the successor to Hooker Chemical, paid compensation to 900 families for medical claims as well as an estimated \$300 million to the federal government and \$78 million to New York state for cleaning up the site and relocating the families. See *Coda for Love Canal: Last Suits are Resolved*, NAT'L L.J., May 11, 1998, at B2.

23. 42 U.S.C. §§ 9601-9675 (1994).

24. Andrea Lee Rimer, *Environmental Liability and the Brownfields Phenomenon: An Analysis of Federal Options for Redevelopment*, 10 TUL. ENVTL. L.J. 63, 66 (1996).

25. 42 U.S.C. § 9601(22) (1994) (“[A]ny spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, or disposing into the environment (including the abandonment or discarding of barrels, containers, and other closed receptacles containing any hazardous substance or pollutant or contaminant). . .”).

26. See ROBERT V. PERCIVAL, ENVIRONMENTAL REGULATION: LAW, SCIENCE, AND POLICY, 286 (2d ed. 1996) (“EPA has listed more than 700 substances as ‘hazardous substances’ for purposes of CERCLA. 40 C.F.R. § 302.”); STEVEN FERREY, ENVIRONMENTAL LAW: EXAMPLES AND EXPLANATIONS, 305 (1997) (“The definition of ‘hazardous substance’ is very broad.”). CERCLA incorporates by reference the lists of hazardous chemicals in other federal statutes regulating toxic substances including the Clean Water Act, Solid Waste Disposal Act (RCRA), the Clean Air Act, and the Toxic Substances Control Act. *Eagle-Picher Indus. v. EPA*, 759 F.2d 922, 926 (D.C. Cir. 1985).

“facility.”²⁷

CERCLA establishes a framework for dealing with potentially contaminated sites. First, the EPA must determine whether the site qualifies as a potentially contaminated site.²⁸ Next the EPA must then decide if that site warrants placement on the National Priorities List (NPL) of the most dangerous hazardous waste sites, otherwise known as Superfund sites.²⁹ After listing the site, the EPA may clean up the site or order any “potentially responsible party” (PRP) to remediate the site.³⁰

Six years after passing CERCLA, Congress enacted the Superfund Amendments and Reauthorization Act of 1986 (SARA), establishing

27. 42 U.S.C. § 9601(9) (1994):

(A) any building, structure, installation, equipment, pipe or pipeline (including any pipe into a sewer or publicly owned treatment works), well, pit, pond, lagoon, impoundment, ditch, landfill, storage container, motor vehicle, rolling stock, or aircraft, or (B) any site or area where a hazardous substance has been deposited, stored, disposed of, or placed, or otherwise come to be located; but does not include any consumer product in consumer use or any vessel.

28. A potentially *contaminated site* is defined as “an imminent and substantial danger to the public health or welfare or the environment.” 42 U.S.C. § 9604(a)(1) (1994).

29. See Charles de Saillan, *Superfund Reauthorization: A More Modest Proposal*, 27 ENVTL. L. REP. 10,201 (1997); Frona M. Powell, *Amending CERCLA to Encourage the Redevelopment of Brownfields: Issues, Concerns and Recommendations*, 53 WASH. U. J. URB. & CONTEMP. L. 113, 115 (1998) (citing Comprehensive Environmental Response, Compensation, and Liability Act of 1980, Pub. L. No. 96-510, § 221, 94 Stat. 2801. “In enacting CERCLA, Congress established a multibillion dollar fund (the ‘Superfund’) to help finance the clean up costs of such sites.”) *Id.*

30. 42 U.S.C. § 9607(a) (1994). There are four classes of liable parties who may be obligated to either remediate the site or to reimburse others for the cost of remediation. The first class involves the current owner and operator of the site. 42 U.S.C. § 9607(a)(1) (1994). However, owners have a defense: the “innocent landowner” provisions establish protection from liability if the owner purchased without knowledge of the existence of contamination and conducted an inquiry at the time of purchase to determine whether contamination existed. 42 U.S.C. § 9601(35) (1994); see, e.g., *Westwood Pharm., Inc. v. Nat’l Fuel Gas Distrib. Corp.*, 964 F.2d 85 (2d Cir. 1992); *United States v. Serafini*, 791 F. Supp. 107 (M.D. Pa. 1993); *New York v. Shore Realty Corp.*, 759 F.2d 1032 (2d Cir. 1985); *United States v. Price*, 523 F. Supp. 1055 (D. N.J. 1981). The past owner or operator of a site falls under the second class of potentially responsible parties. 42 U.S.C. § 9607(a)(2) (1994); see, e.g., *Nurad, Inc. v. William E. Hooper & Sons Co.*, 966 F.2d 837 (4th Cir. 1992). Persons who arranged for disposal of the hazardous substance that was disposed of at the site comprise the third class. 42 U.S.C. § 9607(a)(3) (1994); see, e.g., *Employers Ins. of Wausau v. Browner*, 52 F.3d 656 (7th Cir. 1995). Finally, the fourth class is comprised of any persons who transported the substances to the site if they were involved in the selection of that site. 42 U.S.C. § 9607(a)(4) (1994); see, e.g., *United States v. Aceto Agric. Chems. Corp.*, 872 F.2d 1373 (8th Cir. 1989).

statutory clean-up standards for Superfund sites.³¹ The most significant change brought about by SARA was contained in § 121 of CERCLA, the imposition of remedial standards on CERCLA.³² Under SARA § 113(h), the remediation must protect human health and the environment while being cost effective.³³

While Congress had high hopes for this legislation, the remediation projects have proceeded at a slow pace.³⁴ The primary reason for this failure is the enormous cost of an environmental clean-up, averaging \$30 million per Superfund site.³⁵ Compounding the problem is the fact that transactional costs have depleted the amount of money available for remediation.³⁶ In addition, squabbling amongst the PRPs as to what share of the clean-up cost is attributable to each and the difficulty in locating possible PRPs has led to further delays.³⁷

B. The Resource Conservation and Recovery Act

The Resource Conservation and Recovery Act (RCRA) establishes regulatory requirements for the disposal of solid and hazardous waste.³⁸ Congress enacted RCRA to complement CERCLA. While CERCLA is triggered when a toxic site exists, RCRA focusing on the handling of hazardous materials in order to prevent a toxic site from occurring.³⁹ RCRA can also serve as a basis for compelling clean-up of contaminated property.⁴⁰

31. Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499, 100 Stat. 1613 (1986) (codified at 42 U.S.C. §§ 9601-9675 (1994)).

32. 42 U.S.C. § 9621(b) (1994).

33. *Id.* § 9613(h).

34. U.S. ENVIRONMENTAL PROTECTION AGENCY, ENVIRONMENTAL PROGRESS AND CHALLENGE: EPA UPDATE (1989); *see* 140 CONG. REC. S12, 604-605 (daily ed. Aug. 25, 1994) (statement of Sen. Lautenberg).

35. U.S. ENVIRONMENTAL PROTECTION AGENCY, ENVIRONMENTAL STEWARDSHIP: EPA'S FIRST TWO YEARS IN THE BUSH ADMINISTRATION (1991).

36. MARK REISCH, CRS ISSUE BRIEF, SUPERFUND REAUTHORIZATION ISSUES IN THE 103D CONGRESS (Congressional Research Service updated Oct. 5, 1994), at 2.

37. *See, e.g.,* Sandy Shore, *Environmental Detectives Track Down Polluters Superfund*, L.A. TIMES, Jan. 15 1995, at B5.

38. 42 U.S.C. §§ 6901-6992 (1994).

39. *Id.* § 6902(a)(1). Subtitle C of RCRA defines the requirements for the disposal of hazardous wastes.

40. 42 U.S.C. § 6973(a) (1994) (authorizing the government to seek injunctive relief in

Although RCRA has no explicit cost recovery provisions, in *United States v. Valentine*,⁴¹ the District Court of Wyoming held that under RCRA § 6973(a), parties may recover past response costs for clean-up at solid waste management units.⁴² In addition, RCRA § 6972(a)(1)(B) gives citizens standing to bring an action to abate an “imminent and substantial endangerment” due to the release of solid or hazardous waste.⁴³ In fact, the Ninth Circuit in *KFC Western, Inc. v. Meghriq*⁴⁴ went so far as to grant recovery of past response costs under § 7002(a)(1)(B).⁴⁵

III. TAX TREATMENT OF ENVIRONMENTAL CLEANUP

In addition to environmental laws, the IRS attempts to assist remediation efforts by offering generous tax incentives for environmental clean-up.⁴⁶ When determining the tax treatment of a transaction, the first question is whether the transaction at issue qualifies as a deduction or as a capital expenditure.⁴⁷

A. Deductions

Generally, a taxpayer may deduct from his taxable income any and all expenses that he incurs in the day to day operation of his business.⁴⁸ There are several requirements that must be met under section 162(a) for an expense to be deductible. The expense must be: (1) ordinary and necessary,⁴⁹ (2) part of an ongoing trade or

certain cases when there is an “imminent and substantial endangerment”).

41. 856 F. Supp. 627 (D. Wyo. 1994).

42. *Id.* at 632.

43. 42 U.S.C. § 6972(a)(1)(B) (1994).

44. 49 F.3d 518 (9th Cir. 1995).

45. *Id.*; *see, e.g.*, *Key Tronic Corp. v. United States*, 114 S. Ct. 1960, 1967 (1994) (holding that litigation-related attorney’s fees are not recoverable in private party cost recovery actions under CERCLA).

46. S. REP. NO. 105-33, at 110 (1997).

47. *See* April I. Halle, *Clean-Up Costs: Deduction v. Capitalization Under Revenue Ruling 94-38*, 1 ENVTL. LAW. 591, 592 (1995) (noting that the IRS seeks to “match expenses with the revenues of the taxable period to which the expenses are properly attributable to avoid distortion of net income”).

48. I.R.C. § 162(a) (1994), provides for the deduction of all “ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.”

49. *See* *Welch v. Helvering*, 290 U.S. 111, 114-15 (1933) (defining “ordinary and

business,⁵⁰ (3) paid or incurred in the tax year,⁵¹ and (4) an expense (as opposed to capital expenditure).⁵² Although section 162(a) allows the deduction of “expenses,” I.R.C. section 263 mandates a different treatment for “capital expenditures.”⁵³

B. Capitalization

The objective of the capitalization requirement is to portray the taxpayer's income most accurately by matching expenses to related income.⁵⁴ Courts have enumerated that capital expenditures are those that (1) “add to the value” of the property,⁵⁵ (2) “substantially

necessary” as that which is customary or typical); *Comm'r v. Tellier*, 383 U.S. 687 (1966) (holding that unusual or infrequent expenses can be ordinary and necessary if they are incurred by average taxpayers in a particular type of business). *See generally* BORIS I. BITTKER & LAWRENCE LOKKEN, 1 FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS § 20.1.1 (1988); *see, e.g.*, Treas. Reg. § 1.162-3 (1994) (providing that a taxpayer may generally deduct the costs of incidental materials and supplies). Treas. Reg. § 1.162-4 provides that a taxpayer does not have to capitalize the cost of incidental repairs that do not materially increase the value or the useful life of the repaired property. *See generally* *Gilliam v. Comm'r*, 51 T.C.M. 515 (1986).

50. *See* BITTKER & LOKKEN, *supra* note 49, at § 20.4.4 (explaining that expenses in preparation for a new trade or business may not be deductible); *Doggett v. Burnet*, 65 F.2d 191, 194 (D.C. Cir. 1933) (stating that there can be no trade or business unless the taxpayer enters into and carries on the activity with a good faith purpose of turning a profit or in the belief that a profit can be made from the activity).

51. Determination of the time at which an expense was incurred is determined by the accounting method of the taxpayer. Expenses by taxpayers using a “cash” method of accounting are generally incurred in the year in which the money is actually spent. *See* Treas. Reg. § 1.461-1(a)(1) (1954). Expenses by taxpayers using the “accrual” method are not incurred until the “economic performance” has occurred. *See* Treas. Reg. § 1.461-1(a)(2) (1954). The “economic performance” test means that an accrual basis taxpayer cannot deduct expenditures until the money is paid or services are actually performed. *See* I.R.C. § 468(a)(1) (1994).

52. I.R.C. § 162 (1994).

53. Ordinary expenses that produce a benefit in the year incurred are deductible in that year. *See* *Comm'r v. Idaho Power Co.*, 418 U.S. 1 (1974); *United States v. Miss. Chem. Corp.*, 405 U.S. 298 (1972). Capital expenditures are for items with a fixed life that produce a long term benefit over many years. *See* *Encyclopedia Britannica v. Comm'r*, 685 F.2d 212 (7th Cir. 1982); Halle, Note, *supra* note 47, at 594.

54. *See* Rev. Rul. 94-38; Juliann Avakian-Martin & Marlis Carson, *Environmental Cleanup Issue: A Repeating Theme at ABA Meeting*, 60 TAX NOTES 925, 925 (1993) (“if the benefits point more to the future than to the past, then capitalization will be required”) (quoting Glenn R. Carrington); *see, e.g.*, *Encyclopedia Britannica v. Comm'r*, 685 F.2d 212 (7th Cir. 1982). *See generally* Donal E. Flannery et al., *KPMG Peat Marwick Advocates Current Deductibility of Environmental Cleanup Costs*, 7 NAT. RESOURCES TAX REV. 1272, 1273 (1994).

55. *See* Treas. Reg. § 1.162-4 (1994) (stating that “incidental repairs” are deductible as ordinary and necessary if the purpose of the expenditure is to keep the property in an ordinarily

prolong the useful life” of the property;⁵⁶ or (3) “adapt property to a new or different use”⁵⁷ from its previous use.⁵⁸ Section 263 prohibits the deduction of costs incurred for new buildings or for permanent improvements that increase the value of any property.⁵⁹ Such expenses are regarded as capital expenditures.

If an expense qualifies as a capital expenditure, the expenditure must be depreciated as a cost allocated over the period that corresponds to the benefit of the expenditure.⁶⁰ If the capital expenditure is for property that does not have a determinable life, such as land,⁶¹ the taxpayer adds the capital expenditure to the basis and recovers the cost either when the property is sold or exchanged, or upon the dissolution of the enterprise.⁶²

1. Repair vs. Improvement

A common method of distinguishing between a deductible expense and one requiring capitalization, is the determination of whether that expense was an improvement or repair.⁶³ Improvements include expenses that substantially increase the useful life and alter the property’s capacity or the function of an asset; these expenses are

efficient operating condition).

56. *Compare* I.M. Cowell v. Comm’r, 18 B.T.A. 997 (1930) (holding that expenditures made for modifying a hotel building that was incurred as a part of a plan to rehabilitate and improve the building had to be capitalized), *with* Buckland v. United States, 66 F. Supp. 681 (D. Conn. 1946) (holding that the expenses incurred in repairing a building to prevent leaks was deductible).

57. Tech. Adv. Mem. 94-110-02 (Nov. 19, 1993).

58. Treas. Reg. § 1.263(a)-1(b) (1994).

59. I.R.C. § 263(a)(1) (1994); *see* *Indopco, Inc. v. Comm’r*, 503 U.S. 79, 84 (1992) (stating that “deductions are exceptions from the norm of capitalization”); *see also* Treas. Reg. § 1.263(a)-1(b) (1994).

60. I.R.C. § 263(a) (1994); *Comm’r v. Boylston Market Ass’n*, 131 F.2d 966 (1st Cir. 1942) (holding that if a taxpayer prepays an expense that is attributable to subsequent years, that expense must be capitalized).

61. *Edinboro Co. v. United States*, 224 F. Supp. 301, 302 (W.D. Pa. 1963) (noting that land has an unlimited useful life).

62. The basis in realty may include the original purchase price, transfer taxes, legal expenses and title search. In addition, capital improvements such as the grading of the land may also be added to the basis. *See* I.R.C. §§ 164(a), 263(a)(1), 1016(a)(1) (1994); Treas. Reg. §§ 1.212-1(k), 1.263(a)-1(a)(1), 1.263(a)-2(a), and 1.1016-2(a) (1994).

63. BITTKER & LOKKEN, § 20.4.8.

generally capitalized.⁶⁴ Alternatively, expenses made to restore property damage and incidental repairs are generally deductible.⁶⁵ Since all repairs add some long-term value to the property, discerning the threshold at which a repair becomes an improvement is difficult.⁶⁶ The Internal Revenue Service makes this determination on a fact and circumstance basis.⁶⁷

2. "Future Benefits"

In *INDOPCO, Inc. v. Commissioner*,⁶⁸ the Supreme Court adopted the "future benefits" rationale for determining whether an expenditure should be deducted or capitalized.⁶⁹ In *INDOPCO*, the taxpayer incurred investment banker's fees and related costs in connection with a friendly merger offer by another firm.⁷⁰ The taxpayer, pointing out that no separate and identifiable asset had been created to which such outlays could be allocated, sought to deduct rather than capitalize.⁷¹ The Court held that the merger produced

64. See *Plainfield-Union Water Co. v. Comm'r*, 39 T.C. 333, 337 (1962); see also *Treas. Reg. § 1.263(a)-1(a)* (2000); see, e.g., *Mt. Morris Drive-In Theater Co. v. Comm'r*, 238 F.2d 85 (6th Cir. 1956). In *Mt. Morris*, the court denied the taxpayer was denied a current deduction for the cost of a drainage system it installed to stop run-off to nearby land. The taxpayer argued that the installation of the drainage system was a repair; the court ruled, however, that the need for a drainage system was foreseeable at the time the taxpayer constructed the drive-in theater. Consequently, the cost of the drainage system had to be capitalized. *Id.*

65. *Plainfield*, 39 T.C. at 338. See *Treas. Reg. § 1.162-4* (2000) (explaining that repairs can be deducted currently if they do not add to the life of the asset); see also *Midland Empire Packing Co. v. Comm'r*, 14 T.C. 635 (1950) (question of whether the cost of lining basement walls with concrete to prevent oil seepage created by a neighboring refinery should be treated as a deductible repair or as a capital expenditure). The walls of the basement which had been used for twenty-five years had proved entirely effective in keeping out moisture until the refinery went up, at which point the seepage began. *Id.* The court held that the expenditure was a repair and was deductible. *Id.*

66. Steven G. Black, *The Continuing Saga of Environmental Cleanup Costs: Current Deduction Allowed Under the Restoration Principle of Plainfield-Union*, 4 BYU L. REV. 1321, 1324 (1995).

67. See, e.g., *Encyclopedia Britannica, Inc. v. Comm'r*, 685 F.2d 212 (7th Cir. 1982).

68. 503 U.S. 79 (1992).

69. For an early proposal of the test, see George Mundstock, *Taxation of Business Intangible Capital*, 135 U. PA. L. REV. 1179, 1237 (1987); Noël B. Cunningham & Deborah H. Schenk, *How To Tax the House that Jack Built*, 43 TAX L. REV. 447 (1988).

70. 503 U.S. at 82.

71. *Id.* at 86 (advocating a "test in which 'creation or enhancement of an asset' is a prerequisite to capitalization, and deductibility under § 162(a) is the rule rather than the exception").

“significant benefits,” which would be realized by the taxpayer in future years.⁷² Consequently, the fees had to be capitalized.⁷³ In reaching its decision, the Court focused on the long term benefits the company received by being acquired.⁷⁴ The Court stated, however, that, while the expenditure need not have a determinable life, the mere presence of an incidental benefit may not warrant capitalization.⁷⁵ Rather, the crucial factor in determining the appropriate tax treatment of the expenditure is the taxpayer’s realization of benefits beyond the year in which the expenditures were made.⁷⁶

C. Refundable Tax Credits

A tax credit provides a dollar for dollar reduction in one’s tax liability. In other words, a tax credit reduces the amount of taxes due because the credit amount is subtracted after the applicable tax rate has been multiplied by the income.⁷⁷ By contrast, deductions reduce taxable income and thereby reduce the tax payable by the amount of the deduction multiplied by the relevant rate of tax.⁷⁸ Unlike a tax credit, which remains constant regardless of the rate of tax, a deduction benefits the taxpayer to the extent of that taxpayer’s tax bracket.⁷⁹

In a refundable tax credit, the amount of credit gathered by the taxpayer can be redeemed through the Internal Revenue Service for a refund.⁸⁰ In contrast, a nonrefundable tax credit does not entitle a

72. *Id.*

73. *Id.* at 90.

74. *Id.* at 86-87 (contrasting the instant case to *Lincoln Savings* which held that an “expenditure that ignores to create or enhance . . . a separate and distinct “asset should be capitalized,” but did not create an exclusive set).

75. *Id.* at 87.

76. *Id.*

77. John F. Dooling et al., *Deductions, Exemptions, and Credits*, in *FUNDAMENTALS OF FEDERAL TAXATION* 106 (Erwin N. Griswold & William C. Warren eds., 1948). See generally PHILIP F. POSTLEWAITE, *POLICY READINGS IN INDIVIDUAL TAXATION* 326 (1980) (discussing of investment tax credits); WILLIAM O. GREEN & ANN H. GREEN, *FEDERAL INCOME TAX* 49 (1976); JAMES EDWARD MAULE, *TAX CREDITS: CONCEPTS & CALCULATIONS* A-8 (1994).

78. See Dooling, *supra* note 77, at 103.

79. *Id.* at 106.

80. *Id.*

taxpayer to a refund if the credit exceeds the tax that would otherwise be owed by the taxpayer.⁸¹

D. Section 198

Section 198 permits taxpayers to deduct expenditures on brownfield environmental remediation in the year paid or incurred, instead of capitalizing the expenditure. Capitalizing the expenditure would be traditional tax policy treatment.⁸² The reason for this difference is that environmental remediation produces benefits that last longer than one year.⁸³ However, in order to receive the deduction under section 198, the remediation must be of "hazardous substances"⁸⁴ at a "qualified contaminated site."⁸⁵

Prior to the enactment of section 198, environmental remediation expenditures left taxpayers confused as to whether they should deduct or capitalize the expenditure.⁸⁶ Section 198 paints a clearer picture regarding the tax treatment of brownfield remediation, but does not address various other clean-up situations.⁸⁷

81. Janette M. Lohman & Paul N. Tice, *Beyond the Beltway: Using Tax Credits to Implement Public Policy: The Missouri Experiment*, AFFORDABLE HOUSING & COMMUNITY DEV. L., 284, 287 (1999).

82. I.R.C. § 198(a) (1999).

83. See *supra* note 64 and accompanying text.

84. I.R.C. § 198(d)(1)(A-B) (1999) (defining hazardous substance as "any substance . . . defined in § 101(14) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, and any substance which is designated as a hazardous substance under Section 102 of such Act").

85. I.R.C. § 198(c)(1)(A) (1999). A qualified contaminated site is defined as any area that:

- (i) is held by the taxpayer for use in 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;
- (ii) which is within a targeted area; and (iii) at or on which there has been a release (or threat of release) or disposal of any hazardous substance.

Id.

86. See Rev. Rul. 94-38, 1994-I C.B.35 (allowing current deduction for asbestos removal). *But see* Tech. Adv. Mem. 94-11-002 (Nov. 19, 1993) (requiring capitalization for remediation of contaminated soil).

87. H.R. REP. CONF. REP. NO. 105-220, at 488 (1997) (stating that "providing current deductions for certain environmental remediation expenditures under the conference agreement creates no inference as to the proper treatment of other remediation expenditures not prescribed in the agreement").

IV. PROBLEMS WITH CURRENT EXPENSING OF BROWNFIELD REMEDATION COSTS

By allowing an immediate deduction of the costs associated with remediation of brownfields, the Senate Finance Committee created incentives to clean-up contaminated sites.⁸⁸ The general drawback to the tax deduction strategy was that it provided more dollar benefits to high-bracket taxpayers than to low-bracket taxpayers, defeating the “vertical equity”⁸⁹ goal of the tax system.⁹⁰ The fact that deductions had to be itemized also indicated that such a method would be primarily used by high-bracket taxpayers.⁹¹

Congress has apparently not learned its lesson from the controversy surrounding CERCLA.⁹² CERCLA, although comprehensive and strict, never realized its projected potential and the results have been dismissed.⁹³ A deduction for the remediation of brownfields is really just a tax deferral system, which ultimately does not provide the incentive needed for a taxpayer to take on the table of brownfields remediation.⁹⁴

The reason why the section 198 tax “deduction” functions as a tax deferral relates to section 198’s reference to section 1245.⁹⁵ Section 1245 states that a gain on the sale of certain property is taxed as ordinary income for the amount of all depreciation or amortization deductions previously taken on the property.⁹⁶ Section 198 states that

88. S. REP. NO. 105-33, at 110 (1997); *see, e.g.*, Lawrence J. Arem, *Tax Benefits of Research and Development Expenses Increased by New Credit*, TAXATION FOR LAWYERS, Jan.-Feb. 1982, at 208.

89. Harold S. Peckron, *Reparation Payments—An Exclusion Revisited*, 34 U.S.F. L. REV. 705, 714 n.58 (2000) (citing J.S. NEWMAN, FEDERAL INCOME TAXATION: CASES, PROBLEMS AND MATERIALS 24-25 (1998)). Vertical equity is a distribution of the tax burden so that those with the greatest ability to pay will pay the most tax, and those with the least ability to pay will pay the least tax. *Id.*

90. *See* 129 CONG. REC. S2387 (daily ed. Mar. 9, 1983) (statement by Prof. Rabushka) (stating that the wealthy taxpayers are the one who benefit from deductions).

91. *Cf. Tax Subsidies: They Just Keep Climbing*, U.S. NEWS & WORLD REP., Mar. 21, 1983, at 75.

92. *See* McGee, *supra* note 14.

93. *See, e.g.*, 140 CONG. REC. S14, 736 (daily ed. Oct. 7, 1994) (statement of Sen. Dole).

94. *See, e.g.*, Nancy E. Schurtz, *Promoting Alcohol Fuels Production: Tax Expenditures? Direct Expenditures? No Expenditures?*, 36 SW. L.J. 597, 633-34 (1982).

95. I.R.C. § 198(e) (Supp. IV 1998).

96. I.R.C. § 1245(a) (1994).

any cost expensed under section 198 will be treated as a depreciation deduction attributable to section 1245 property.⁹⁷ Thus, the deduction taken in the year of the expenditure is recaptured and taxed as ordinary income in the year of the sale, making section 198 function only as a tax deferral, instead of a deduction. The investor will be better off investing in the greenfield because he will not have to incur any remediation expenses.⁹⁸ In sum, a brownfield investment will actually be more expensive for the investor than an investment in a greenfield,⁹⁹ and there is no real incentive for the investor to act in the manner prescribed by Congress through section 198.¹⁰⁰

Although Congress had high expectations when it added section 198 to the tax code in the Taxpayer Relief Act of 1997,¹⁰¹ section 198 was not nearly as strong an incentive as it could have been. CERCLA imposed a comprehensive strict liability standard; thus, Congress was enacting enforcement of the strongest caliber.¹⁰² By investing in a brownfield, the investor will always be liable for any cleanup costs arising in the future, by virtue of CERCLA's strict liability.¹⁰³ This is merely a tax deferral, which is definitely not the strongest tax incentive available to Congress.¹⁰⁴ Thus, Congress needs to take more affirmative steps by sharing the costs of such remediation and by

97. I.R.C. § 1245(a)(3)(A)-(B)(i) (1994). Properties affected include: (1) tangible and intangible property and (2) other tangible property (not including a building or its structural components) used as a central part of (a) manufacturing, (b) production, (c) extraction, or (d) the furnishing of transportation, communications, electrical energy, gas, water, or sewage disposal services. *Id.*

98. See Robert S. Berger et al., *Recycling Industrial Sites in Erie County: Meeting the Challenge of Brownfield Redevelopment*, 3 BUFF. ENVTL. L.J. 69, 73 (1995).

99. See Clement Dinsmore, *Recycling Brownfields: The Legislative Climate*, J. URB. TECH., Spring 1995, at 9 (defining greenfields as land which has never been used for a non-agricultural purpose).

100. See S. REP. NO. 105-33, at 110 (1997); H. R. CONF. REP. NO. 105-220, at 487 (1997).

101. One estimate suggested that \$100 billion in taxes could be generated by the use of brownfield sites. Administration of Brownfields Program Questioned at Hill Appropriations Hearing, 27 Env't Rep. (BNA) No. 49, at 2511 (Apr. 18, 1997).

102. See TODD S. DAVIS & KEVIN D. MARGOLIS, *BROWNFIELDS: A COMPREHENSIVE GUIDE TO REDEVELOPING CONTAMINATED PROPERTY* 7 (1997).

103. See *supra* note 30 and text accompanying notes 22-37.

104. See Daniel S. Goldberg, *Tax Subsidies: One-Time vs. Periodic An Economic Analysis of the Tax Policy Alternatives*, 49 TAX L. REV. 305, 308 n.18 (1994) (explaining that a tax credit is considered a valuable tax subsidy because it offers a dollar for dollar reductions in the amount of taxes a company will pay).

lessening the fear the investor has of CERCLA's strict and retroactive liability.¹⁰⁵

A. *What Level of Remediation is Adequate?*

One of potential investors' greatest fears of is CERCLA's liability subsequent to the remediation efforts.¹⁰⁶ The level of remediation needed to viably restore a brownfield site is based on contamination levels, which are sometimes calculated imperfectly.¹⁰⁷ Such potential miscalculations pose the problem of assigning future liability if additional contamination is later discovered.¹⁰⁸ Current law allocates any future liability to the owner/taxpayer¹⁰⁹ and requires that the owner demonstrate due diligence in looking for additional contamination.¹¹⁰ Though this arrangement does function to ensure that the initial remediation will be done thoroughly, it also discourages brownfield investment.¹¹¹

However, if a full remediation waiver were given to the owners of brownfields, they would not need to show due diligence in finding any further contamination. Thus, if further contamination were subsequently found, the government would assume liability for further remediation.¹¹² This method would require the government to potentially incur costs in the future, but it would also encourage wider investment in troubled brownfield sites.¹¹³

105. Al Stamborski, *More Incentives from the Government Would Help the Development of Brownfield Sites in the Metro East, Developers Say*, ST. LOUIS POST-DISPATCH, Feb. 21, 2000, at BP10. One EPA official commented, "In dealing with brownfields, it's not so much that people are adverse to taking on the environmental issues . . . Its not knowing about them that scares them." *Id.*

106. See DAVIS & MARGOLIS, *supra* note 102, at 9.

107. See Philip H. Gitlen, *Voluntary Cleanup Programs*, 1 ALBANY L. ENVTL. OUTLOOK 28 (1995).

108. See Krista J. Ayers, Comment, *The Potential For Future Use Analysis in Superfund Remediation Programs*, 44 EMORY L.J. 1503, 1509 (1995).

109. See 42 U.S.C. § 9607(a) (1994).

110. See 42 U.S.C. § 9607(b) (1994).

111. The taxpayer/owner will want to avoid expensive future liability, and thus ensure that the remediation efforts were done thoroughly.

112. The government would not have to assume the remediation cost of the later found contamination if it can locate PRPs and prosecute them under CERCLA § 121.

113. See Michael Allan Wolf, *Dangerous Crossing: State Brownfields Recycling and Federal Enterprise Zoning*, 9 FORDHAM ENVTL. L.J. 495, 498 (1998) ("brownfields . . .

The current system will discourage investment in brownfield sites.¹¹⁴ Investors fear the possibility of future liability; therefore, this system will negate whatever effects Congress intended to have with section 198 of the tax code.¹¹⁵ By allowing a deduction for the remediation of a brownfield site, we should also exclude the taxpayer from any future liability.¹¹⁶

Many states have adopted a “no action” letter policy, which waives CERCLA liability if the cleanup meets state certification standards.¹¹⁷ The state with the broadest waiver of liability is Michigan.¹¹⁸ Michigan has restructured its CERCLA law “to provide blanket protection from liability to an owner of a property that is not responsible for causing the contamination at the brownfield site.”¹¹⁹

ultimate goal [is] a dramatic improvement in the social climate and financial status of central-city residents”).

114. See *supra* note 102 and accompanying text.

115. Cf. Mark D. Anderson, *The State Voluntary Cleanup Program Alternative*, 10 NAT. RESOURCES & ENV'T 22 (1996) (stating that the high cost of conducting site investigation and remediation is a major discouragement to investment in brownfields).

116. The tax deduction provides recognition that the remediation was sufficient, and thus, the remediator has complied with the guidelines set forth by the EPA.

117. A release of liability or no action letter is available in: Arizona, California, Colorado, Connecticut, Delaware, Illinois, Maine, Michigan, Minnesota, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New York, North Carolina, Ohio, Oregon, Rhode Island, Tennessee, and Washington. Joel B. Eisen, ‘*Brownfields of Dreams*’: *Challenges and Limits of Voluntary Cleanup Programs and Incentives*, 1996 U. ILL. L. REV. 883, 951 (1995).

118. *Id.* at 950.

119. *Id.* (citing Mich. Comp. Laws Ann. § 324.20126(1) (West Supp. 1996)). The Michigan statute states in pertinent part:

Notwithstanding any other provision or rule of law and except as provided in subsections (2), (3), (4), and (5) and section 20128, the following persons are liable under this part:

(a) The owner or operator of a facility if the owner or operator is responsible for an activity causing a release or threat of release.

(b) The owner or operator of a facility at the time of disposal of a hazardous substance if the owner or operator is responsible for an activity causing a release or threat of release.

(c) An owner or operator of a facility who becomes an owner or operator on or after June 5, 1995, unless the owner or operator complies with both of the following:

(i) A baseline environmental assessment is conducted prior to or within 45 days after the earlier of the date of purchase, occupancy, or foreclosure. For purposes of this section, accessing property to conduct a baseline environmental assessment does not constitute occupancy.

(ii) The owner or operator discloses the results of a baseline environmental assessment to the department and subsequent purchaser or transferee if the baseline environmental assessment confirms that the property is a facility.

The EPA should encourage federal application of the Michigan liability waiver.¹²⁰ As investors and developers abstain from brownfields development due to liability fears, the no action letter is a step in the right direction. Indeed, inner-city revitalization will likely gain new life if the Michigan program is implemented uniformly in every state because potential investors will be free from the specter subsequent CERCLA liability.¹²¹

However, the no action letter is a release of liability only from the issuing state.¹²² In addition, if further contamination is subsequently discovered, the no action letter does not prevent CERCLA liability from being imposed.¹²³ In sum, the no action letter is of uncertain value to the investor.¹²⁴ If read in the most favorable light for a taxpayer, section 198 is merely a tax deferral system.¹²⁵ The primary benefit of the deferral to the taxpayer who outlays the funds for remediation is the time value of money.¹²⁶

The legislature's goal is for private money to fund brownfield remediation so that the government does not have to exhaust its limited resources.¹²⁷ The tax system is designed to be a revenue

Id.

120. See generally *supra* note 115 (describing the Michigan liability waiver).

121. See Eisen, *supra* note 117, at 952-56 (stating that the no action letter gives the developer assurance that the state will not pursue any enforcement actions at the site).

122. See *id.* at 954 n.303 (citing OFFICE OF TECHNOLOGY ASSESSMENT, STATE OF THE STATES ON BROWNFIELDS: PROGRAMS FOR CLEANUP AND REUSE OF CONTAMINATED SITES 20 (1995)); Mark D. Anderson, *The State Voluntary Cleanup Program Alternative*, 10 NAT. RESOURCES & ENV'T 22, 25 (1996); R. Michael Sweeney, *Brownfields Restoration and Voluntary Cleanup Legislation*, 2 ENVTL. LAW, 105, 134 (1995).

123. See Eisen, *supra* note 117, at 955 n.304 (stating that a no action letter should have a "reopener" provision to empower the issuing state to take action if contamination that was not discovered during the site investigation is subsequently found); see also *id.* at 1033.

124. See generally *id.* at 955 n.308, citing *Hearing Before Subcommittee On Conference, Trade, and Hazardous Materials of the House Committee on Commerce*, 104th Cong. (1995) (testimony of Jan Linsenmeyer and Robert Atkinson, Energy, Transportation and Infrastructure Program, Office of Technology, stating that the no action letter is nothing more than a marginal incentive to invest in brownfields).

125. See *Taxation Subsidiaries*, *supra* note 91.

126. See, e.g., Stephen J. Wolma, *Ambushed in a Safe Harbor: Taxation of Intrafamilial Installment Sales Contracts*, 33 VAL. U. L. REV. 309, 316-18 (1998) (describing methods for calculating the value of money over time).

127. Peter J. Wiedenbeck, *Charitable Contributions: A Policy Perspective*, 50 MO. L. REV. 85, 94 (1985) (stating that a reduction in private funding would cause the government to subsidize charitable and public service organizations).

source for the federal government.¹²⁸ Under the section 198 deduction method enacted by Congress, the only loss the government will realize is delay of tax receipts which will be lower due to the time value of money.¹²⁹

There is no true benefit for an investor to incur the cost to rehabilitate a brownfield and be able to deduct the costs involved, when the taxpayer can invest in a greenfield and not have to incur any remediation cost.¹³⁰ Furthermore, the problem is compounded by the fact that section 198 expenses are recaptured and taxed as ordinary income at the time of sale.¹³¹ Therefore, any benefit the investor did acquire by the remediation effort is taken away at the sale or exchange of the property.¹³²

V. THE NEED FOR A THOROUGH FEDERALIZED BROWNFIELD REMEDIATION APPROACH

The federal government should view the redevelopment of inner-cities as a business investment.¹³³ Remediating brownfields and returning them to productive use will attract more businesses to newly decontaminated sites.¹³⁴ New businesses will lead to increased job opportunities for local residents.¹³⁵ As a result, the federal, state,

128. See William A. Klein & Joseph Bankman, *FEDERAL INCOME TAXATION* 1 (11th ed. 1997) (stating that 86.1% of the total revenues taken in by the federal government were composed of income taxes).

129. See Wolma, *supra* note 126.

130. For a discussion of costs associated with investment in brownfields as opposed to greenfields, see McWilliams, *supra* note 7; Terry J. Tondro, *Reclaiming Brownfields to Save Greenfields: Shifting the Environmental Risks of Acquiring and Reusing Contaminated Land*, 27 CONN. L. REV. 789, 792 (1995).

131. See I.R.C. § 198(e) (West Supp. 1998).

132. See *id.*

133. Vincent M. Di Lorenzo, *Equal Economic Opportunity: Corporate Social Responsibility In The New Millennium*, 71 U. COLO. L. REV. 51, 73 (2000) (citing U.S. DEP'T OF HOUSING AND URBAN DEV., *THE STATE OF THE CITIES* (1998) (the availability of jobs and other public initiatives is needed to revitalize the inner city); U.S. DEP'T OF HOUSING AND URBAN DEV., *THE STATE OF THE CITIES* (1997); CITIZENS HOUSING AND PLANNING COUNCIL, *A PRELIMINARY ASSESSMENT OF COMMUNITY REDEVELOPMENT IN THE SOUTH BRONX* (1998)).

134. See, e.g., Al Stamborski, *Brownfield Incentives Program Saved 140 Jobs in Jennings*, ST. LOUIS POST-DISPATCH, Feb. 21, 2000, at BP10 (stating that the redevelopment of a brownfield site will double the employment of Stout Marketing in the coming decade).

135. See, e.g., *id.*

and local governments will profit by an increased tax base.¹³⁶ Thus, the revitalized inner-city will be a boon for jobs, reducing the need for social services within depressed areas.¹³⁷

Brownfield sites will have a better chance of being redeveloped if the government can offer more tax incentives to private parties who are willing to clean-up the sites.¹³⁸ Thus far, federal, state, and local governments have made substantial efforts to encourage redevelopment of brownfields.¹³⁹ Investors want the government to share a greater burden of the costs associated with remediation, as well as to provide them with security from the far-reaching grasps of CERCLA liability.¹⁴⁰

VI. THE MODEL FEDERAL TAX CREDIT PROGRAM

Some states are currently utilizing the tax credit incentive for remediation of brownfields.¹⁴¹ However, these credits are only applicable to one's state tax liability.¹⁴² A substantial federal tax credit program would provide a more attractive incentive because federal tax liabilities are normally much higher than state tax liabilities.¹⁴³ Although this proposed federal tax credit program would result in a considerable decrease in tax revenues for the treasury, it would stimulate future growth. In time, the initial loss of revenue

136. See generally John Machaleh & Jon Frondsant, *Republican Proposes Federal Aid for Contaminated Land*, GANNETT NEWS SERVICE, Jan. 26, 1996 (claiming that the failure to redevelop abandoned industrial sites is costing states and cities hundreds of millions and possibly billions of dollars in lost tax revenues).

137. See Dorothy A. Brown, *Racial Equality in the Twenty-First Century: What's Tax Policy Got To Do With It?*, 21 U. ARK. LITTLE ROCK L. REV. 759 (1999).

138. Al Stamborski, *More Incentives from the Government Would Help the Development of Brownfield Sites in the Metro East, Developers Say*, ST. LOUIS POST-DISPATCH, Feb. 21, 2000, at BP10. "[D]evelopers . . . want a crack at the grant money that's now available only to local governments." *Id.*

139. See Eisen, *supra* note 117, at 1033 n.20 (citing NATIONAL ENVIRONMENTAL POLICY INSTITUTE, HOW CLEAN IS CLEAN?: WHITE PAPER ON BROWNFIELDS 38 (1998)).

140. See DAVIS & MARGOLIS, *supra* note 102.

141. See Lohman, *supra* note 81, at 294 n.6 (stating that Missouri is not the only state that has experimented with transferable tax credit programs).

142. *Id.* at 287 (stating that state tax "credits may offset the gross premiums tax, the financial institutions tax, the corporate franchise tax, the state income tax, and the express company gross receipts tax").

143. Federal income tax paid is deducted from the state tax liability.

would be offset by the benefits of brownfield revitalization.¹⁴⁴

Congress should implement a federal tax credit to subsidize half of the costs associated with the remediation effort.¹⁴⁵ A percentage would be more useful to determine the credit amount than a concrete number because the remediation costs vary from site to site.¹⁴⁶ Furthermore, a uniform percentage will better achieve the goal of providing the same benefit to all investors.¹⁴⁷ The remaining half of the remediation costs should then be deductible under section 198.¹⁴⁸ Under this method, the investor would not incur any out-of-pocket expenses in conducting the remediation. However, by virtue of the recapture provision of section 198, the treasury will recover half of the remediation cost that was deducted in the year of sale of the property.¹⁴⁹ This proposed method would effectively correct the impotent deduction offered under section 198.¹⁵⁰ Furthermore, this method would utilize section 198 to its fullest potential.¹⁵¹ Although section 198 was passed with the best of intentions, its end-around incentive method of treating the deduction as analogous to that of depreciation expenses is not compelling enough to convince investors to remediate a brownfield site.¹⁵²

The EPA and federal government should urge states to offer a loan to investors for the redevelopment of the outdated facilities on

144. With the addition of new businesses generating new revenue, the tax base would increase which would result in increased tax revenue for the treasury.

145. See Stanley S. Surrey, *Tax Incentives As A Device For Implementing Government Policy: A Comparison With Direct Government Expenditures*, 83 HARV. L. REV. 705, 713-17 (1970) (stating that tax incentives are used in achieving a desired result, a public good). "Frequently a tax incentive is urged on the ground that the particular problem to be met is great and that the Government must assist in its solution by enlisting the participation of the private sector—generally business." *Id.* at 715-16. The advantages of a tax credit are enormous because once the program is put into effect, the results are near automatic and immediate. *Id.* at 716.

146. Robert H. Abrams, *Using Experience to Improve Superfund Remedy Selection*, 29 U. RICH. L. REV. 581, 584-87 (1995) (stating that each site should be evaluated separately due to the distinct characteristics of each site).

147. S. REP. NO. 105-33, at 110 (1997) (stating the need for a clear and consistent standard for the appropriate tax treatment of environmental remediation expenditures).

148. See *supra* Part III.D.

149. See I.R.C. § 198(e) (West 1999).

150. See *supra* Part IV.

151. See *id.*

152. See *id.*

brownfields.¹⁵³ Most brownfields have been abandoned for years and the buildings residing upon them are outdated.¹⁵⁴ The state would be receiving a substantial tax benefit through the remediation of brownfields.¹⁵⁵ Having the state offer the loan for the redevelopment project allows the costs of brownfield remediation projects to be shared by state and federal governments.

Critics could argue that this federal tax incentive model is offering more than the government can afford to give. However, investors will not invest in brownfields when they can invest in greenfields and incur no extra expenses by way of remediation costs or for fear of future liability.¹⁵⁶ Therefore, the government must shoulder the remediation costs by way of incentives to make investments in brownfields a profitable alternative.

153. See Rimer, *supra* note 24, at 117-18 (stating that loans are less burdensome to the government than grants). A drawback listed for loans is that the fear of subsequent environmental liability will deter potential investors from incurring such a heavy debt. *Id.* at 118. However, a loan in the context of the proposal in this Note does not require a loan be the sole incentive for brownfield remediation. In fact, the loan in this context would be used for the rehabilitation of old and outdated facilities located on the brownfield site. Thus, the loan would be a complementary incentive to the one provided by the federal government. *Id.*

154. See *id.* at 68 n.18.

[D]ecades of heavy industry in an era with limited environmental awareness have left a legacy of contaminated, often abandoned, industrial structures located on millions of acres of polluted land throughout the United States. The huge, empty shells of heavy industry in urban industrial centers are viewed as casualties of a shift in America's industrial base toward light manufacturing, and a related shift away from rail and waterway transport to interstate highways. In the shadow of these aging behemoths stand the remains of many secondary facilities that once fed off the work generated by them. Closed paint shops, plating shops, and other assorted "job shops" litter the inner-city with their own histories of contamination. Also gone are the businesses that relied on worker-generated consumer demand, such as gas stations and dry cleaners; these now sit idle due to releases or suspected releases of the hazardous materials endemic to their operations. The result is an urban environment where soil contamination is presumed, where groundwater and surface water pollution are likely, and where the "polluter pays" principle is failing to generate sufficient funds to clean up the mess.

Id. citing Douglas A. McWilliams, *Environmental Justice and Industrial Redevelopment: Economics and Equality in Urban Revitalization*, 21 *ECOLOGY L.Q.* 705, 714-15 (1994) (citation omitted).

155. See *supra* notes 137-41 and accompanying text.

156. See *supra* Part I.

VII. CONCLUSION

Tax incentives generally benefit the rich tremendously more than they do the poor, violating the vertical equity goal of the tax system. However, the tax incentive proposed by this note is pointed towards the redevelopment of inner-city brownfield sites, and will translate to an increase in the number of jobs available to the residents of the area. Nonetheless, a strong and uniform program must be implemented before we can reach our goal of a pollutant-free society.

