

Frequently Asked Questions about the Small Commercial Tax Credit Program

Eligibility for the Credit

How do I find out if my property is historic?

Answer: Your property is historic if it is individually listed in the National Register of Historic Places, if it is a contributing structure within a National Register historic district, if it is an individually designated local landmark, or if it is located in and contributes to a locally designated historic district. Local designations **must** also meet National Register standards of eligibility **as determined by the MHT**. MHT's website lists all National Register properties and districts in Maryland. Maps are available for most, which you can use to complete Part 1 of the application. You may contact MHT at 410-514-7628 if the National Register map of your district is not available online. County governments and municipalities maintain lists of locally designated historic properties. Contact your local planning office for information. Additionally certain non-listed or non-historic structures may be eligible if certified by the Maryland Heritage Areas Authority as contributing to the significance of a Certified Heritage Area. Please contact the Heritage Areas Program Administrator for more information at 410-514-7685.

How do I find out if my property contributes to the significance of a National Register or local historic district?

Answer: This is the purpose of Part 1, "Certification of Significance." MHT will determine whether a structure contributes to the significance of a district based on the documentation available in the Part 1 application, National Register nomination forms or in the case of local districts, Determination of Eligibility forms.

I am working on getting my property designated, but want to get started on the rehabilitation project now. Can I submit Parts 1 and 2 before my property is officially designated?

Answer: The tax credit program statute requires that the structure be officially designated, either by the local government or the National Register, by the end of the calendar year in which the rehabilitation project was completed. Failure to receive this designation by the required deadline will result in the rehabilitation being ineligible for the tax credit. You may apply for the tax credit once a draft nomination has been submitted to MHT for Part 1 certification and sufficient documentation is provided for a complete application for the property's designation.

Can lessees of a property apply for and claim the small commercial tax credit?

Answer: Possibly. Qualified ownership leases may be eligible for the credit. Contact MHT staff for more information.

Can non-profits apply for and claim the small commercial credit?

Answer: Possibly. The non-profit must be the fee-simple owner of the property or a lessee with a qualifying ownership lease.

The property is my personal residence; however I run a small business out of the basement. Can I apply for the small commercial tax credit?

Answer: No. The property must be *primarily* income producing and be assessed as a commercial property by the Maryland Department of Assessment and Taxation. In this case you may apply for the homeowner tax credit and receive a pro-rated credit based on the portion of your home that is exclusively your residence.

Does the residential rental requirement apply to the pre-rehabilitation use of the property or the post-rehabilitation use of the property?

Answer: No more than 75% of the building can be used for residential rental purposes AFTER the building is rehabilitated. Spaces that will be used for residential rental use should be clearly marked on floor plans and submitted with the Part 2 Application.

How should the residential rental square footage be calculated? What about shared spaces like lobbies?

Answer: 1) calculate a percentage of the total square footage that is exclusively residential rental, 2) use that percentage amount to pro-rate the square footage of shared spaces, 3) add the square footage of exclusively residential rental to the pro-rated square footage to determine the TOTAL residential rental Square footage, 4) divide that by the TOTAL building square footage to calculate the final percentage of residential rental space.

- 1) $\frac{\text{exclusively residential rental sf}}{\text{total building sf}} = \% \text{ exclusively residential}$
- 2) $\text{shared sf} \times \% \text{ exclusively residential rental} = \text{pro-rated sf}$
- 3) $\text{exclusively residential rental sf} + \text{pro-rated sf} = \text{total residential rental sf}$
- 4) $\frac{\text{total residential rental sf}}{\text{total building sf}} = \% \text{ residential rental}$

A justification of the rental residential square footage calculation must be submitted with the Part 3 Request for Certification.

I own a 2 story residential building that is used for rental apartments. The carriage house is rented storage space. Does the carriage house satisfy the 25% non-residential commercial requirement?

Answer: No, each historic building on a property must contain no-more than 75% residential rental use.

I own a mixed-use property that contains 50% restaurant use and 50% residential-rental use. Are the expenses for the residential-rental portion eligible?

Answer: Yes, as long as the costs are determined by MHT to be qualified rehabilitation expenditures.

I own a bed and breakfast, a portion of which is my residence. Am I eligible to apply?

Answer: If the primary use of the property is an income-producing bed and breakfast and is assessed as a commercial property by the Maryland Department of Assessments and Taxation, then you are eligible to apply.

The Review Process

How long will it take MHT to process my application?

Answer: Applications are handled on a first-come, first-served basis. MHT's review of a complete application is generally 30-45 days but may be longer or shorter, depending on the volume of tax credit applications. Additionally, application review times may vary based upon the complexity of the project and the completeness and clarity of the application. From time to time, MHT will post special announcements on the Tax Credit webpage advising applicants of the current review period. MHT will contact you if there are questions about your application or if you will be required to provide additional information. If you wish to confirm that MHT has received your application, MHT recommends that you use a courier that tracks its packages to submit your application or submit your application by USPS Certified Mail/Return Receipt Requested.

Is there a fee for reviewing my application?

Answer: There is no fee for the review of Part 1 Applications. There is a \$10 fee for the certification of Part 2 Applications. There is also a Part 3 certification fee which is based on the reserved credit amount in the Part 2 Application. The Part 3 fee is 3% of the amount of the tax credit estimated in the Part 2 application (up to \$50,000) less the initial \$10 processing fee submitted with the Part 2 Application. Therefore \$1,490 is the maximum Part 3 fee for a project estimated to cost \$250,000+. Note: The Part 3 fee is based on qualified rehabilitation expenditures only. Insurance proceeds and other ineligible costs, such as new construction and/or additional State or local grants, loans, or State tax incentives from a State agency, are *not* considered qualified rehabilitation expenditures.

Last year, I completed a rehabilitation project but only recently heard about the State tax credit program. Can I still apply for the credit?

Answer: Unfortunately, no. Completed projects cannot be accepted. This is because qualified rehabilitation expenditures are only those incurred AFTER the Part 2 Application is certified by MHT.

I have a million dollar rehabilitation planned. Can I complete half of it, and then apply for the small commercial tax credit to cover the remaining \$500,000?

Answer: No. If MHT has reason to suspect that the overall project was more than the program limit of \$500,000, the project may be disqualified.

I am undertaking a \$250,000 rehabilitation with a \$500,000 planned addition? Does this project exceed the \$500,000 limit?

Answer: No. The \$500,000 limit refers to Qualified Eligible Expenditures. New construction is not a qualified expenditure, so the cost of the proposed addition is not counted towards the \$500,000 limit.

My local historic preservation commission has already approved my rehabilitation project and I'm anxious to get started. Do I also need MHT's approval to begin the work?

Answer: Absolutely. MHT must review all applications for tax credits. Neither local nor federal agencies oversee the state tax credit program. MHT is the only government agency charged with administration of the state tax credit program and is solely responsible for certifying that structures are certified historic structures and that rehabilitation plans and completed projects meet the Secretary of the Interior's *Standards for Rehabilitation*.

Can I apply for the federal credit as well? If so, do I have to submit 3 applications and three sets of photos?

Answer: If you meet eligibility requirements for the federal tax credit, you can apply for both the federal and state programs. You must submit two federal applications with 2 sets of supplementary documentation as well as one copy of the state application form. The only additional documentation needed for the state application is a map of the designated Sustainable Community.

I just received a letter from the MHT which states that my application was denied because aspects of my proposed project did not meet the Secretary of the Interior's *Standards for Rehabilitation*. I have contacted historic preservation professionals from both my local government and the federal government to better understand how the *Standards* are interpreted in practice. It would appear that there are some differences in how each government representative interprets the *Standards* and MHT's interpretation. Why aren't the *Standards* interpreted uniformly regardless of which agency applies them?

Answer: The MHT cannot speak to the way in which preservation professionals from other governments interpret the Standards; however, for the last 30 plus years, the MHT has consistently applied the Standards in a conservative manner. In the event that there is a difference in the way the MHT and any other government agency interprets the Standards, the MHT's interpretation will be final for the purposes of the state tax credit program.

I submitted a Part 2 application to the tax credit program; however, the Part 2 was denied for the proposed work not meeting the *Standards*. Can I re-apply with a new Part 2 for additional proposed work to my property?

Answer: Yes, but you must provide MHT proof that you have not done any of the work that was denied in the previous Part 2 in the interim. If you have undertaken any of the work that was denied in the Part 2 application, then you must wait 24 months from the project start date to reapply.

I just completed my project and have a certified Part 3 for \$250,000 of qualified rehabilitation expenditures. Even though that phase of the project is finished, I still have more work to do. Can I submit another Part 2 application for the additional work to be completed this year?

Answer: No. The statute for the tax credit program limits the amount of eligible rehabilitation costs for small commercial projects to \$250,000 in any one 24-month period. In other words, a project cannot be awarded more than \$50,000 in tax credits within a contiguous two-year period. Additionally, applicants cannot submit more than one completed Part 3 application for certification within a single, taxable year.

If the rehabilitation work described in my Part 2 Tax Credit Application is for the exterior only, why do I need to submit photographs of the interior of my property?

Answer: These photographs establish a baseline record of the entire property at the time of the tax credit application submittal. They will be used for the purpose of reviewing the proposed project and to assist the MHT in tracking changes that may not have been identified in the Part 2 Application. Alterations that do not meet the Secretary of the Interior's *Standards for Rehabilitation* and were not included in the Part 2 Application, may result in a denial of the entire application. Alterations that do not meet the *Standards* and are completed within the first 5 years after the tax credits are awarded may result in the recapture of all or a portion of previously awarded credits. If thorough photographic documentation of the property prior to rehabilitation is not available, review and evaluation of the Part 2 Application cannot be completed and may result in a denial.

How is the review of my application impacted by other relevant or applicable laws?

Answer: The property owner(s) is/are responsible for complying with all Federal, state, and local laws applicable to the project. This responsibility may include, but is not limited to, compliance with local zoning, building, and life safety codes, review by local historic preservation commissions, and federal and state licensing, permitting, and environmental requirements. Note: Certification from MHT of a final project in no way constitutes compliance with any of the above laws or regulations.

I have to undertake additional work that was not included in my Part 2 Application. What should I do?

Answer: You must submit an Amendment form describing the additional work for MHT to review and approve; however, the Part 2 estimated qualified rehabilitation expenditures may not be amended. The final tax credit award will be capped at the Part 2 estimate, so additional expenditures that exceed the Part 2 estimate will not be eligible for tax credits.

Questions about Qualifying Rehabilitation Work

I understand that work must be undertaken within a 24 month period. When does that start?

Answer: The 24-month period may start when eligible pre-construction costs related to the rehabilitation project are incurred. This could include certain fees as described below. If there are no pre-construction costs, the 24 month period starts when actual construction work begins after MHT certifies the Part 2 Application.

Are architectural fees eligible?

Answer: Yes. Architectural, engineering, and similar consultant fees, including tax credit consultant fees, are eligible. Expenses incurred in order to prepare the application (such as architect's or engineer's fees) are the only costs incurred prior to Part 2 certification that are eligible; however, in order for these fees to be included in the total rehabilitation costs, they must have been incurred within the 24-month period as described above.

What about acquisition costs, financing charges, and building permit fees?

Answer: No. These costs are not eligible.

Are landscaping and site work costs eligible?

Answer: The costs associated with the restoration of significant historic landscape features may be eligible when there is adequate documentation of the feature's historic significance. Costs for all other landscaping features, such as driveways, sidewalks, and retaining walls, are not eligible.

Are solar panels considered an eligible expense?

Answer: Possibly. The scale, location, visibility, and installation of the solar panels must meet all requirements of the Secretary of the Interior's *Standards for Rehabilitation*. The system must be purchased, not rented or leased from a supplier.

The restrooms in my office building were last remodeled in the 1980s. I want to renovate them, but I'm not sure if it will be considered "remodeling only." Can you provide guidance?

Answer:

"'Rehabilitation' means the process of returning a structure to a state of utility, through repair or alteration, which makes possible an efficient use while preserving those portions and features of the structure and its site and environment which make the structure and its site and environment historically, architecturally, or culturally significant. 'Rehabilitation' does not include an alteration which is primarily remodeling."

The rehabilitation of spaces with no or few defects is likely to be determined to be remodeling and the costs are thus not eligible for the credit. As noted above, the overall purpose of the Sustainable Communities Tax Credit Program is to "return a structure to

a state of utility.” Many bathroom projects include no work that would be considered rehabilitation.

Projects described in a proposed plan of rehabilitation submitted with the Part 2 Application and determined by MHT to be primarily remodeling will not qualify for the tax credit program. Projects that include appropriate rehabilitation of deteriorated spaces and spaces that function but have reached the end of their useful life, including kitchens and bathrooms, will continue to be considered rehabilitation work and eligible for the program. Eligibility will be determined as part of the Part 2 Application review.

Are additions, new patios, new back decks, new roof decks, or similar new construction eligible?

Answer: No. The costs for new construction do not qualify.

Are rehabilitation costs for barns, garages, and other outbuildings eligible?

Answer: If these structures are historically associated with the commercial structure, contribute to the significance of the property, and contain no more than 75% residential rental use, then the rehabilitation costs may qualify. Non-historic separate structures are not eligible.

The building has a rear addition that was built in the 1980’s and needs to be rehabilitated. Do these costs qualify?

Answer: Yes. Additions to historic structures are considered part of the overall structure, even though they do not have historic significance. Changes to these additions must still conform to the Standards.

Are interior finishes eligible?

Answer: Interior capital expenditures are eligible for the credit. For the interior, this usually means finishes that become part of the structure. Eligible costs may include repair or restoration of wainscoting, mantels, interior shutters, molding, floors, plaster, and paint. Items that are not eligible include, but are not limited to: appliances, carpets, drapery, window treatments, pictures, furniture, and closet shelving installation. Consult MHT staff for a final determination of eligibility.

I plan on building an addition as part of the rehabilitation project. Do I have to include that work in my application even though it is not eligible for the tax credit?

Answer: Yes. MHT reviews a rehabilitation project in context with all work proposed for the property, including any attached or related new construction. Certification is based upon whether the overall project is consistent with the Secretary of the Interior’s *Standards*. Therefore, if you are building a new addition, constructing a new garage or outbuilding, or undertaking landscaping or site work, those work items should be included in your Part 2 and clearly shown as ineligible costs in your Part 3. All work to be undertaken during the project period must be included in your Part 2 and reviewed by MHT for compliance with the *Standards*. All aspects of the completed project, even those which are not eligible for the

tax credit, must conform to the *Standards* in order for the Part 3 to be certified by MHT and for the owner to claim any tax credit.

My property had vinyl windows installed by a previous owner. If I am not planning to remove them as part of my rehabilitation project, will my project still be eligible for tax credits?

Answer: Yes. MHT will not require owners to replace non-historic materials installed by a previous owner if there is no work planned for this feature. However, if replacement of the windows is proposed, they must be replaced with a historically appropriate window.

If the property is damaged and I am reimbursed by my insurance company to pay for the repairs/restoration, can I include those expenses in my Total Qualified Rehabilitation Expenditures on Part 3 and claim a credit for them?

Answer: No. Expenses reimbursed by an insurance company cannot be claimed. These costs must be subtracted from the total qualified rehabilitation expenditures on the Part 3 Application and must be documented as such in the Itemized Expense Spreadsheet submitted with the Part 3. Note: For this reason, insurance proceeds should not be factored into the Part 2 estimated qualified rehabilitation expenditure total (QRE) amount.

If I will be receiving additional funding to help with the rehabilitation of my property from any State or local government agencies, such as grants, loans, or State energy tax credits, can I claim these expenses as well toward the credit?

Answer: No. Additional funding including state and local grants and loans or other state tax credits are not eligible and must be subtracted from the total qualified rehabilitation expenditures on the Part 3 Application. This must be documented on the Itemized Expense spreadsheet that is required to be submitted with the Part 3 Application. Note that any anticipated funds from a local tax incentive program do not need to be subtracted from the final qualified rehabilitation expenditure amount.

What if I am receiving additional funding from a Federal agency, such as a Federal energy tax credit, do I need to back these costs out of the final rehabilitation expenditure total on the Part 3 as well?

Answer: No. Additional funding from a Federal agency that pertains to the rehab of your property does not have to be subtracted from the Part 3 Application.

Questions about Part 3

I decided not to undertake some of the work described in the Part 2 Application. What should I do before submitting the Part 3 Application?

Answer: You should include an Amendment form with the Part 3 Application stating what work you did not undertake. If you wish to undertake that work in the future, you must file a new Part 2 Application describing the work and include additional photographs.

How should I document expenses in the Part 3 Application?

Answer: The Part 3 Itemized Expense Sheet, filled out according to the Part 3 Itemized Expense Sheet Instructions, must be submitted with your Part 3 Application, with eligible and ineligible expenses clearly delineated. For each item on the spreadsheet you must include (1) a copy of the invoice or receipt, showing which goods or services were purchased, and (2) certifiable proof of payment, which may consist of one of the following:

1. A dated credit card receipt
2. A cancelled check
3. A bank statement showing the check number, date, payee name, and amount
4. A signed statement from the contractor or vendor stating the amount paid (an invoice simply marked "PAID" is not sufficient).

Please submit copies of the proof of payment with sensitive information and account numbers redacted or blacked out for security purposes.

The Part 3 Itemized Expense Sheet Instructions contain an example spreadsheet that shows how your expenses must be broken down and itemized for the purposes of calculating your qualified rehabilitation expenditures for the tax credit program. The instructions and a blank spreadsheet for you to fill out can be downloaded from MHT's website.

My final project was over \$250,000. Do I need to submit paid invoices for the remaining costs that I will not get a credit for?

Answer: Yes, all expenses must be included so we can verify that the project does not exceed the 500,000 eligibility limit.

My estimated project costs in the Part 2 were \$500,000, which exceeds my final QRE of \$250,000? Do I have to pay the 3% fee based on the \$500,000 estimate?

Answer: No. The Part 3 fee is based on the estimated credit amount on the Part 2 application which is \$50,000 for projects with estimated qualified expenditures (QRE) of \$250,000 and up. Therefore the fee would be \$1,500 minus the \$10 Part 2 fee (\$1,490).

Claiming the Credit

Is the credit fully refundable? Do I just get a check back?

Answer: To the extent the credit exceeds the taxpayer's tax liability, the credit is refundable. You must file for the credit with the Comptroller of Maryland for the tax year in which the project was *completed*. Use Maryland Form 502S specific to the year in which you are filing. The certified Part 3 Application must be attached to Form 502S.

Can a non-resident of Maryland claim the credit/refund?

Answer: Yes. The program has no restrictions on residency.

Do I have to pay federal income taxes on the refund the following year?

Answer: Possibly. The IRS considers the State income tax refund to be taxable income.

Recapture Rule

I received tax credits for a rehabilitation project certified by MHT one year ago. If I plan to do additional work on the same structure this year that will not conform to the Secretary's *Standards*, do I risk losing my previous credit?

Answer: Yes. If disqualifying work is undertaken on a property that has received tax credits, the credits will be recaptured. If the disqualifying work is performed during the year in which the rehabilitation was completed, 100% of the credit will be recaptured; if during the first full year after the rehabilitation was completed, 80% will be recaptured; if during the second full year, 60% will be recaptured; if during the third full year, 40% will be recaptured; and after the fourth full year, 20% will be recaptured. After five years the credit is not subject to recapture.

If I sell the property, will my tax credit be recaptured?

Answer: Yes. If the property is disposed of during the year in which the rehabilitation was completed, 100% of the credit will be recaptured; if during the first full year after the rehabilitation was completed, 80% will be recaptured; if during the second full year, 60% will be recaptured; if during the third full year, 40% will be recaptured; and after the fourth full year, 20% will be recaptured. After five years the credit is not subject to recapture.