

Energy Efficiency Deduction Available to Owners and Designers

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The Energy Tax Incentives Act of 2005 (Pub. L. 109 – 58) added Internal Revenue Code (IRC) Section 179D, which allows a deduction for energy efficient commercial building property that is placed in service before December 31, 2013. If a taxpayer owns, leases, designs or builds energy efficient property, it may be entitled to a federal income tax deduction in addition to depreciation for the cost of such property.

The maximum deduction for a building is equal to the amount spent on energy efficient property installed in a building, with a maximum deduction equal to \$1.80 per square foot. Energy efficient property is property that satisfies four conditions. First, it must be property that is subject to the allowance for depreciation (generally, capitalizable expenditures). Second, it must be installed on or in any building located in the United States, and within the scope of Standard 90.1-2001 of the American Society of Heating, Refrigerating, and Air Conditioning Engineers (ASHRAE) and the Illuminating Engineering Society of North America (Standard 90.1-2001), as in effect on April 2, 2003. Third, it must be installed as part of the interior lighting systems; the heating, cooling, ventilation and hot water systems; or the building envelope (collectively, the systems). Fourth, it is certified that the systems installed in the building will reduce the total annual energy and power costs with respect to the combined usage of the building's systems by 50 percent or more as compared to a building that meets the minimum requirements of Standard 90.1-2001.

The amount of the Section 179D deduction reduces the taxpayer's basis in the property for purposes of depreciation.

If the property meets all of the above criteria except the 50 percent reduction threshold set out above, a partial deduction may be available. Basically, the full cost of any of the three systems is immediately deductible if any of the individual systems is certified to meet certain energy efficiency standards set by the Internal Revenue Service (IRS), up to 60 cents per square foot. For example, if the three systems do not meet the 50 percent threshold set forth in the previous paragraph, but the interior lighting system alone meets the IRS-set efficiency standards for interior lighting systems, the taxpayer may deduct the cost of the interior lighting system, with a maximum deduction equal to 60 cents per square foot. This partial deduction may be taken for any or all of the systems meeting the IRS's criteria, with a maximum deduction equal to \$1.80 per square foot.

If the property does not meet the 50 percent threshold set out above and does not meet the requirements for energy efficiency set for the interior lighting system, there is a deduction equal to the amount spent on the interior lighting system, up to 60 cents per square foot, if the property achieves a reduction in lighting power density of at least 25 percent. This alternative method for obtaining the deduction is known as the "interim lighting rule."

IRS Notice 2006-52 requires that before a taxpayer may claim the Section 179D deduction with respect to property installed on or in a commercial building, the taxpayer must obtain a certification with respect to the property. The certification must be provided by a qualified individual and satisfy the requirements of Section 179D(c)(1). A taxpayer is not required to attach the certification to the return on

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which the deduction is taken. However, Section 1.6001-1(a) of the income tax regulations requires that taxpayers maintain such books and records as are sufficient to establish the entitlement to, and amount of, any deduction claimed by the taxpayer. Accordingly, a taxpayer claiming a deduction under Section 179D should retain the certification as part of the taxpayer's records for purposes of Section 1.6001-1(a) of the income tax regulations.

One thing that is unusual to Section 179D is that in the case of energy efficient property installed on or in property owned by a federal, state or local government, the deduction may be allocated to the person primarily responsible for designing the property or among several designers in lieu of the owner of such property. IRC Section 179D(d)(4) and Notice 2008-40. A designer is a person who creates the technical specifications for installation of energy efficient building property (or partially qualifying commercial building property for which a deduction is allowed under Section 179D). A designer may include, for example, an architect, engineer, contractor, environmental consultant or energy services provider who creates the technical specifications for a new building or an addition to an existing building that incorporates energy efficient commercial building property (or partially qualifying commercial building property for which a deduction is allowed under Section 179D).

By way of example, Boca Village Corporate Center South Tower in Boca Raton, Fla. has achieved LEED Core and Shell 2.0 Silver certification. The building has 106,957 square feet of office space and a parking garage that qualified for the lighting tax benefit. The building itself exceeded 50 percent greater energy efficiency over 2001 ASHRAE guidelines, which allowed this property owner to take the maximum tax benefit available under Section 179D.

The property contains T8 and LED lighting throughout the building and the HVAC system was designed with a SEER rating of 13.5 and has maximum efficiencies.

The structure contains an R-30 roof and R-19 envelope that is very efficient.

Corporate Centre – Office Towers at Boca Village

Envelope	106,957 square feet	= \$64,174.20 tax benefit
Lighting	220,220 square feet	= \$132,132.00 tax benefit
HVAC	106,957 square feet	= \$64,174.20 tax benefit
Total tax benefit		= \$260,480.40

The building owners felt the investment in these efficiencies had a dramatic impact on lowering their operating costs due to utilities and that the Section 179D deduction had a very positive impact on the return on investment. ❖

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