

**NEW AND IMPROVED:
FEDERAL ENERGY INVESTMENT TAX INCENTIVES
FOR COMMERCIAL BUILDINGS**

**BY: ANDREA MONTBRIAND, JD LEED
PAUL BOHN, JD**

For owners of commercial property, the federal energy tax incentives extended in the 2008 Energy Improvement and Extension Act and the 2009 American Recovery and Reinvestment Act (ARRA) could provide the stimulus for implementing that much needed lighting retrofit or an HVAC system upgrade. Aside from significant energy cost savings recognized by the owner or tenant, energy credits and deductions can also be a useful tool for new construction by offsetting the early operating costs of a business with tax refunds or deductions. Although much of the media focus has been on the incentives these Acts extended or created for individual consumers to make their homes more energy efficient, there are also significant provisions in the Acts for commercial building owners to do the same. Specifically, the Acts provide for two significant incentives for owners or tenants of commercial buildings: the Energy Efficient Commercial Buildings Deduction, and the Energy Investment Tax Credit.

Energy Efficient Commercial Building Deduction

Owners of new or existing commercial buildings may deduct the cost for installation of “energy efficient commercial building property” that is placed in service by January 1, 2014. Energy efficient commercial building property is defined as (1) interior lighting systems; (2) building envelope systems (e.g. insulation, natural ventilation, daylighting), or (3) heating, cooling, ventilation, or hot water systems that reduce the building’s total energy and power cost by 50% or more in comparison to a building meeting minimum requirements set by ASHRAE

Standard 90.1-2001. Any cost that can be capitalized can be deducted, however the deduction is capped at \$1.80 per square foot and must be claimed in the year the property is placed in service. If an owner does not want to pursue the complete tax deduction, improvements to one of the three qualifying building systems may also qualify for a partial deduction. For individual systems to qualify, each must reduce the total building energy and power costs by 16 2/3% or reduce costs by 20% for interior lighting, 20% for HVAC and 10% for building envelope. Interior lighting system improvements may also claim a deduction if the lighting power density is reduced by 50%. The deduction for individual system improvements is capped at \$0.60 per square foot and includes any cost that is normally depreciated and claimed over a period of years to be deducted in one lump sum in a single year. If the deduction does not cover the entire cost of the property, the basis of the property is reduced by the deduction amount and the remaining asset value is depreciated over its tax life for the class of property.

Energy Investment Tax Credits

The energy investment tax credit allows commercial building owners to claim a credit for the cost of certain “energy property” that is placed in service between October 4, 2008 and December 31, 2016. Specifically, a 10% investment tax credit is available for the installation of combined heat and power (CHP) systems, geothermal systems, and microturbines, and a 30% investment tax credit is available for the cost of fuel cells, solar panels, or wind turbines. There is no cap on the value of the credit for microturbines, solar energy property, small wind energy property, geothermal, and CHP systems, however, fuel cell credits are capped at \$1500 per kW. Prior to the ARRA, the energy investment credit was proportionately reduced by any amount of subsidized energy financing received from other state, federal, or local programs, however, this limitation has been repealed for property placed in service after December 31, 2008.

To elect the credit, the taxpayer must be the original user of the energy property, or the system must be constructed by the taxpayer. The energy property must also meet certain performance and quality standards in effect at the time the property is acquired and be operation in the year the credit is taken.

Who gets to claim the credit or deduction?

The person who owns the asset for tax purposes may take the deduction. If there are two or more owners, the statute allows allocation of the deduction to multiple taxpayers, but the aggregate amount can not exceed the cap (\$1.80 per square foot). When a tenant makes improvements to any of the three building components that would qualify the property for the tax deduction, a question may arise as to who can take the deduction, the owner or tenant. The answer is specific to the arrangement between the landlord and tenant. In the general case of tenant improvements, the lease should designate which party is the tax owner for purposes of claiming depreciation deductions. Ideally, the energy efficiency deduction should follow this designation, however, to ensure protection of a landlord or tenant's ownership interest in these improvements, applicable lease clauses should be carefully drafted and reviewed.

Conclusion

Before you replace that hot water heater or change out the lighting system in your building, make sure that you qualify to claim the energy credit or deduction. If you have a new construction project, consider integrating particular designs or technologies into your building plans. Many state and federal incentives compliment each other and can be obtained without a reduction in the incentives.

Andrea or Paul may be reached at (248) 380-0000 or amontbriand@fb-firm.com or pbohn@fb-firm.com.