

# 179D Federal Energy Tax Deductions and Cost Segregation Studies

Presented by:





# *Cost Segregation*

**An Opportunity Worth Pursuing**

# Current Status

<b>Depreciable Life</b>	<b>Description</b>
39-Year	Nonresidential Real Property
27.5-Year	Residential Rental Property
15-Year	Land Improvements
15-Year	Qualified Leasehold Improvements (effective 12/31/09)
7-Year	Office Furniture, Fixtures, Equipment, Certain Personal Property
5-Year	Cars, Trucks, Computer Related Equipment, Certain Personal Property

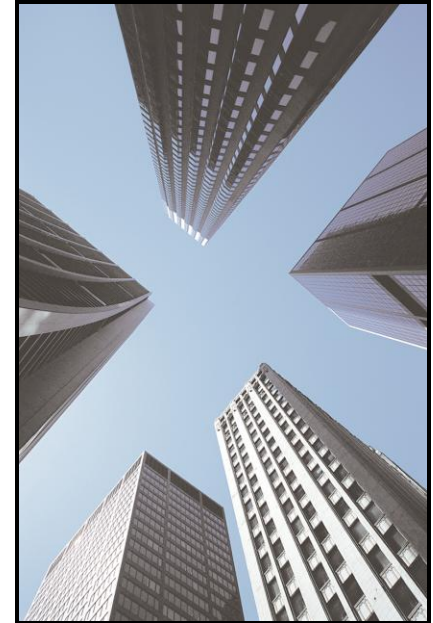
# IRS Standards

- Recommends 3<sup>rd</sup> Party Study
- Recommends Engineering Based Studies
- Enforces 2004 Audit Techniques Guide
- Regulates Circular 230 Compliance



# Cost Segregation Opportunities

- New Construction
- Purchase of Existing Property
- Renovations or Expansions
- Leasehold Improvements
- Existing Property Placed in Service After 1986 (“Look-Backs”)
- Real Property Stepped-Up Through Estate



# Typical Percentages of Accelerated Property

Property Types	Typical % Eligible
Manufacturing/Processing	30-60%
Research & Development	30-60%
Automobile Dealerships	25-50%
Medical Office Buildings	30-50%
Golf Courses	20-40%
Offices	25-45%
Restaurants (Single or Multiple)	20-40%
Apartments	20-35%
Retail (Dept/Specialty Stores)	35-50%
Grocery Stores	20-30%
Hotels/Motels	20-45%
Senior Living/Assisted Living	15-25%
Strip or Regional Malls	5-30%
Tenant Improvements	5-50%



# The Benefit

Each \$100,000 in assets reclassified from a 39-year recovery period to a five-year recovery period results in approximately \$22,000 in net-present-value savings, assuming an 8% discount rate and a 40% marginal tax rate.

*Journal of Accountancy, Copyright 2005 by the AICPA*

# The Look-Back Benefit

**\$10 million retail shopping center, placed into service 7 years ago:**

Original Depreciation Method: 39-year Straight Line

Reclassified Amount with Cost Segregation Study:

- 5-year Property- \$1 million
- 15-year Property- \$1.5 million

## **Adjustment Calculation and Resulting Tax Benefit:**

Depreciation Reported Previously	\$2,564,100
Cost Segregation Study Depreciation	\$3,923,070
Section 481(a) Adjustment	<u>\$1,358,970</u>
Tax Rate	40%
<b>Tax Benefit in Year of Study</b>	<b>\$543,588</b>

*The Bottom Line* – by performing an engineering-based cost seg study, the building owner was able to increase the amount of depreciation expense, thus reducing the current year taxable income, resulting in an increase in cash flow of \$544k.

# Data Requirements

## New Construction, Leasehold Improvements, & Renovation

1. Tax Depreciation Schedules (“look-back” only)
2. Site Survey (“look-back” only)
3. Capitalized Cost supported by:
  - AIA Payment Application (form G702/G703)
  - Change Orders (including description & cost)
4. Project Budget Summarizing all associated costs
  - Indirect Costs not included in Pay Application
  - Cost Paid Directly to Subcontractors Outside General Contract
5. Complete Set of As-Built Construction Drawings (after proposal approval)



# Data Requirements

## Acquisition

1. Closing Statement
2. Recent Appraisal
3. Property Rent Roll as of Acquisition Date
4. Historical Information

Tax Depreciation Schedules or Fixed Assets  
Schedules (look-back only)

Inventories of Furniture, Fixtures, & Equipment

5. Land Value Allocated
6. Site Survey
7. Any Available Construction Drawings





# §179D EPA Act Tax Deductions

# Who Benefits from 179D?

## Commercial Building Owners

- Retailers
- Industrial Buildings
- Warehouses
- Office Buildings

## Primary Designers of Government Buildings

- Architects
- Engineers
- Lighting Designers
- Design & Build Firms



# Energy Policy Act of 2005 (EPAct)

- Incentivized areas:
  - Lighting
  - HVAC
  - Building envelope
- Available for New Construction and Existing Buildings
- Also available for:
  - Tenant owned lease-hold improvements
  - Rental Apartment Buildings 4 stories or above
  - Primary Designers of Government Buildings

# What's it Worth?

Square Footage	Lighting Maximum Deduction \$.60/sq. ft.	HVAC Maximum Deduction \$.60/sq. ft.	Building Envelope Maximum Deduction \$.60/sq. ft.	Total Maximum \$1.80/sq. ft.
50,000	\$30,000	\$30,000	\$30,000	\$90,000
100,000	\$60,000	\$60,000	\$60,000	\$180,000
250,000	\$150,000	\$150,000	\$150,000	\$450,000
500,000	\$300,000	\$300,000	\$300,000	\$900,000
750,000	\$450,000	\$450,000	\$450,000	\$1,350,000
1,000,000	\$600,000	\$600,000	\$600,000	\$1,800,000

Note: For government buildings, these deductions go to the primary designer.



# Lighting Retrofit Economics

## (For Existing Buildings)

- Energy Savings is usually the main driver
- In some states, utilities offer rebates for energy efficient lighting Installations
- Tax Savings is the newest opportunity
- Demand Response is another potential income stream
- Capitalizing on all of the incentives can bring payback for projects to below 2 years and in some cases less than 1 year

# Retrofit Math

100,000 sq.ft. Warehouse

250 Metal Halides replaced with High Bay Fluorescents

- Cost of Project = \$75,000 (Assumes \$300/fixture installed)
  - Annual Energy Savings = \$24,461/yr
  - Rebate = \$24,600
  - Added PV of Tax Deduction = \$13,461
- Payback = 1.5 Years
- IRR = 58%

Without rebate, Payback = 2.5 yrs, IRR = 37%

# Credit/Grants

Specified Energy Property	Credit Termination Date	Applicable Percentage of Eligible Cost Basis
Geothermal Heat Pumps	Jan 1, 2017	10%
Fuel Cells	Jan 1, 2017	30%**
Microturbines	Jan 1, 2017	10%***
Combined Heat & Power	Jan 1, 2017	10%
Large Wind	Jan 1, 2013	30%
Closed-Loop Biomass Facility	Jan 1, 2014	30%
Open-loop Biomass Facility	Jan 1, 2014	30%
Geothermal under IRC sec. 45	Jan 1, 2014	30%
Landfill Gas Facility	Jan 1, 2014	30%
Trash Facility	Jan 1, 2014	30%
Qualified Hydropower Facility	Jan 1, 2014	30%
Marine & Hydrokinetic	Jan 1, 2014	30%
Solar	Jan 1, 2017	30%
Geothermal under IRC sec. 48	Jan 1, 2017	10%*
Small Wind	Jan 1, 2017	30%

\*Geothermal Property that meets the definitions of qualified property in both § 45 and § 48 is allowed either the 30% credit or the 10% credit but not both.

\*\* For fuel cell property the maximum amount of the payment may not exceed an amount equal to \$1,500 for each 0.5 kilowatt of capacity.

\*\*\* For microturbine property the maximum amount of the payment may not exceed an amount equal to \$200 for each kilowatt of capacity.