



# IRC §179D deduction for energy efficient commercial building property

## Accounting Methods and Credit Services

Since 2005, a deduction of up to \$1.80 per square foot has been available to commercial building owners or lessees that install energy efficient property resulting in at least 50% energy savings compared to a baseline building. **The deduction, which reduces the property’s depreciable basis, is properly claimed in the year that the improvements generating the energy savings are placed in service but generally may be claimed in a subsequent year through the filing of an automatic accounting method change.** While this deduction has historically been temporary, and thus subject to the uncertainty of the extension process, it was made permanent by the Appropriations Act, 2021 (CAA), enacted on December 20, 2020.

The deduction cannot exceed the cost of the energy efficient commercial building property generating the energy savings, and such property must be installed as part of the interior lighting system; the heating, cooling, ventilation, and hot water systems (HVAC and HW); or the building envelope. The full deduction of up to \$1.80/sf is allowed so long as the 50% energy savings is achieved, even if the installed energy efficient property is part of only one or two of the systems.

System-specific deductions up to \$0.60/sf are available for property installed as part of only one of the systems so long as the relevant system achieves an energy savings target resulting from the installation. The \$0.60/sf deduction is allowed for lighting systems, HVAC and HW systems, and building envelope systems that achieve a 25%, 15% or 10% energy cost reduction, respectively, compared to a standard reference building. For lighting systems, IRC §179D provides an “Interim Lighting Rule” allowing a deduction of \$0.30 to \$0.60/sf, on a linear sliding scale, for power use reductions of 25% to 40% beyond baseline building levels.

	Fully qualifying property	Partially qualifying property				Interim Lighting Rule
		IRS notice (Effective dates)	Envelope	HVAC and HW	Lighting	
<b>Saving requirements</b>	50%	2012-26 (3/12/12–12/31/20)	10%	15%	25%	25%–40% lower lighting power density (50% for warehouses)
<b>Tax deduction</b>	\$1.80/ft <sup>2</sup>		\$0.60/ft <sup>2</sup>	\$0.60/ft <sup>2</sup>	\$0.60/ft <sup>2</sup>	\$0.30–\$0.60/ft <sup>2</sup> on a sliding scale

Source: *Office of Energy Efficiency & Renewable Energy (2022)*

In addition to making the IRC §179D deduction permanent, the 2021 CAA also modified the statute to provide: (1) an annual increase in the deduction starting in 2021 to account for inflation, and (2) for property placed in service after 2020, periodic tightening of the energy efficiency criteria based on the most recent version of the designated building construction standards.

For buildings owned by government entities, the deduction may be allocated to the designer of the energy efficient commercial property. Allocated deductions must be claimed in the year the property is placed in service on either an original or amended return.

### **Verification of compliance**

To verify compliance, field inspections of each building must be performed by a qualified individual after the property has been placed in service to confirm that the building has met, or will meet, the energy-saving targets prescribed by the National Renewable Energy Laboratory (NREL). The building consultant must be either a professional engineer or a contractor licensed in the jurisdiction in which the building is located.

### **KPMG scope of services**

**Building retrofits** – KPMG will analyze whether the lighting, envelope, or HVAC systems replacement constitutes a repair to the building that is currently deductible under IRC §162.

**Lighting, HVAC, and/or envelope upgrades** – For new construction or retrofit projects not constituting a repair, we will coordinate with your design consultant and contractor to prepare the required building energy model according to the designated building standards. The energy model will be used to calculate the resulting deduction under IRC §179D.

**Lighting upgrades only under the “Interim Lighting Rule”** – For new construction or retrofit projects not constituting a repair, we will calculate the achieved lighting power density reduction as compared to the designated standard and the resulting deduction under IRC §179D.

### **Qualifying technologies**

KPMG has worked with clients to identify an IRC §179D deduction resulting from the installation of numerous different interior lighting, HVAC and HW, and building envelope systems, including:

- Dedicated outdoor air systems
- Low-temperature radiant heating and cooling and chilled beams
- Thermal energy storage systems
- Exhaust air or ground source heat pumps
- Variable frequency drives
- Right sizing of HVAC equipment due to efficient lighting and passive envelope design, including a well-insulated envelope, minimized thermal bridges, airtight construction, energy efficient windows, daylighting, passive solar and thermal mass.

### **Why KPMG?**

Our team members include LEED-accredited professionals, licensed architects, professional engineers, and certified public accountants. We will meet with contractors, vendors, and project managers to gain an in-depth understanding of the project. On most of these projects, we have coordinated our work with other KPMG practices to provide a unified and integrated team to the client.

# Contact us

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