The Energy Tax Aspects of Auto Dealer Re-Imaging Programs

By Charles Goulding, Jacob Goldman and Joseph Most

Charles Goulding, Jacob Goldman and Joseph Most discuss how automobile dealerships can incorporate energy saving technology in their re-imaging programs and take advantage of the tax savings provisions of Code Sec. 179D.

In the aftermath of a severe economic downturn in the auto sector, the total number of auto dealer facilities in the United States shrank from some 22,000 to 18,000. The remaining dealers, along with the three major domestic automobile companies (GM, Ford and Chrysler), have focused on what the industry calls re-imaging, which includes substantial dealer facility renovations. Moreover, manufacturers have been able to require and support comprehensive facility renovations on dealer facilities due to a major reduction in the number of domestic brands and the manufacturer-mandated closure of a particularly high number of domestic dealerships. Dealers can realize substantial tax savings when these renovations meet Energy Policy Act (EPAct) energy efficiency standards.[1]

The EPAct Tax Opportunity

Pursuant to Code Sec. 179D, as enacted by the EPAct, car dealership owners or tenants making qualifying energy-reducing investments can obtain immediate tax deductions of up to $1.80 per square foot.

If the building project doesn't qualify for the maximum $1.80 per square foot immediate tax deduction, there are tax deductions of up to 60 cents per square foot for each of the three major building subsystems: lighting, HVAC and the building envelope. The building envelope is every item on the building's exterior perimeter that touches the outside world including roof, walls, insulation, doors, windows and foundation.

Chart 1 illustrates the potential EPAct tax deductions for an average size car dealership and for all car dealerships in the United States.

Domestic Brand Reduction

Domestic automobile dealers have undergone a substantial reduction in facilities as a result of manufacturer-directed closures and major brand terminations. The largest dealership facility reduction has been at General Motors, which has slimmed itself down to four brands—Cadillac, Chevrolet, Buick and GM. The company jettisoned Oldsmobile, Pontiac, Saab, Saturn and Hummer. Ford eliminated Mercury and sold Volvo. Chrysler merged with Fiat, giving Fiat a major U.S. distribution network for its more fuel-efficient product line.

Re-Imaging Energy Tax Planning

The key with dealership facility re-imaging tax planning is to balance the manufacturer's brand-focused strategy with the individual dealer's need to minimize operating costs. Recently reported dealer data indicated that the average Chrysler dealer's pre-tax earning fell to $150,000 during the economic down-

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turn. This means that a $15,000 reduction in facility energy operating costs equals a 10-percent increase in pre-tax earnings.

Manufacturers like striking, but generally cost-ineffective, showrooms to drive customer traffic. In contrast, dealers need to manage overall facility operating cost, which includes service bays, collision shops and parts storage. Manufacturers want multi-brand dealers to focus on their own brands but multi-brand dealers need to optimize the back of the house (spaces besides the showroom) shared-facility costs savings to remain competitive.

> Energy costs comprise a meaningful portion of dealer earnings, and today's building products can combine with utility rebates and EPAct tax savings to reduce costs.

GM has launched the largest and most wide-spreading re-imaging plan out of the domestic car companies They sent inspectors to analyze all of their dealerships in terms of appearance, location and overall quality. Many dealerships that were fortunate enough to not be shut down are now being forced to relocate, part with their foreign car brands and make major facility upgrades.[2] GM dealers should strive to upgrade to energy-efficient technologies as part of their required facility upgrades.

"How to" Energy Tax Plan

Some of the major manufacturers are funding showroom upgrades. Dealers should take this opportunity to have the assigned design teams, lighting suppliers and electricians upgrade the non-show room space to high energy efficiency levels at the same time. Once the project teams are going to be on site anyway there are major cost synergies from having the non-showroom spaces concurrently retrofitted.

Dealerships that have not upgraded lighting in the past five or more years often have inefficient T-12 or metal halide lighting whose production or importation is now banned by the federal government. Therefore, sooner or later these dealers will be forced to upgrade to more efficient lighting like T-5 and T-8 fluorescents, or the new highly efficient LED lighting.

Another way to improve building lighting efficiency, while keeping up with the manufacturer re-imaging design requirements, is the use of natural lighting during daytime hours.[3] Natural lighting can be used in several ways by integrating sensors with large showroom windows and/or skylights.[4]

When upgrading, a car dealer should always look to local utilities and the state government for energy efficient equipment installation rebates. Rebates vary in size, but at times can be substantial. For example, one dealership in Vermont recently upgraded to T-8 lighting among other energy efficient retrofits, and the owner expects to get all but $4,000 of the project cost back through rebates.[5]

Outside Lot Lighting

Many dealers have large outside lots that use energy intensive prior generation lighting. Although there are no tax incentives for upgrading outside lighting, there are typically meaningful utility rebates for performing this upgrade. Besides substantial energy cost savings, there are tremendous maintenance cost savings related to retrofitting outside lighting, particularly with very long-life LED lighting and induction lighting products that are increasingly popular with these applications.

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Chart 1.

Car Dealership Potential EPAct Tax Deductions

Car Dealership	Square Footage	Lighting Minimum Deduction	Lighting Maximum Deduction	HVAC Maximum Deduction	Building Envelope Maximum Deduction	Total Deduction
Average Size Dealership	20,000	$ 6,000	$ 12,000	$ 12,000	$ 12,000	$ 36,000
18,000 U.S. Dealerships	360,000,000	$ 108,000,000	$ 216,000,000	$ 216,000,000	$ 216,000,000	$ 648,000,000

collected to determine whether Amazon's in-state representatives were soliciting business or merely advertising on Amazon's behalf. In addition, there was also not enough evidence to determine whether the in-state representative's activities are "significantly associated" with Amazon's ability to do business in New York. Thus, the court remanded the as-applied Commerce and Due Process Clause claims to the lower court for further discovery.

Lastly, the court addressed the facial and as applied Equal Protection Clause challenges. At issue was whether the Statute exclusively targeted Amazon, and whether Amazon was being treated differently than other out-of-state retailers who advertise in New York but do not use a mechanism similar to its Associates Program. The court quickly concluded that Amazon was not the Statute's exclusive target because it was being treated the same as Overstock.com, another internet retailer with an associates program. In addition, the court explained that out-of-state retailers without similar associate programs are not similarly situated. Therefore, the court concluded that both the facial and as-applied Equal Protection Claims lacked merit.

North Carolina

In *Amazon.com LLC v. Lay*, the U.S. District Court for the Western District of Washington held that information requests made by the North Carolina Department of Revenue ("the Department") during a sales tax audit were overly broad and violated the First Amendment and the Video Privacy Protection Act, 18 U.S.C. § 2710. In so holding, the court explained that the Department could request either detailed product information or detailed customer information but it could not request both.[7]

The court also held that neither the Tax Injunction Act nor comity principles prevent Amazon from bringing the case in federal court because the declaratory relief requested did not prevent the Department from levying, assessing, or collecting tax and a plain, speedy or efficient remedy was not available in the North Carolina's courts or administrative process.

Oklahoma

The Oklahoma Tax Commission adopted Rule 710:65-21-8. The new rule provides guidance on the notice requirements for out-of-state remote retailers that are not required to collect the state's sales or use tax. Effective October 1, 2010, every noncollecting retailer must include on its Website/catalog and purchase invoice a notice informing Oklahoma purchasers that the state's use tax is due on nonexempt purchases of tangible personal property and that they need to pay the use tax. The rule explains what should be included in the notice, the duplicate notice requirements and the *de minimis* exceptions.

Endnotes

1 *In re Appeal of Imperial, Inc.*, Dkt. Nos. 472648 and 477927 (Cal. State Bd. Equal. July 13, 2010).
2 *Jim Beam Brands Co. v. Franchise Tax Bd.*, 133 Cal. App. 4th 514, [Cal.] St. Tax Rep. (CCH) ¶403-904 (2005).
3 Mass. Dept. of Rev., Letter Ruling 10-6 (Oct. 4, 2010).
4 *In re Xerox Corporation*, Dkt. No. 822620, [N.Y.] St. Tax Rep. (CCH) ¶407-008 (N.Y. Div. Tax App. Oct. 7, 2010).
5 *Amazon.com LLC v. New York State Dep't of Taxation & Fin.*, 2010 NY Slip Op 7823, [N.Y.] St. Tax Rep. (CCH) ¶407-041 (N.Y. App. Div. Nov. 4, 2010).
6 N.Y. Tax Law § 1101(b)(8)(vi).
7 *Amazon.com LLC v. Lay*, Dkt. No. 2:10-cv-664, [N.C.] St. Tax Rep. (CCH) ¶202-480. (W.D. Wash, No. Oct. 25, 2010).

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Service Bay and Collision Shop Heaters

Once the service bay and collision shop areas upgrade their lighting, they have an opportunity for $1.20 to $1.80 EPAct tax deductions for upgrading to high energy efficiency natural gas heaters. The lighting must be upgraded first since lighting is the biggest energy user in non-air conditioned spaces and the required IRS-approved EPAct tax software model will only support tax deductions when energy-efficient lighting is combined with an energy efficient heater.[6]

Conclusion

Dealer tax advisers need to stay current on showroom re-imaging programs and advise their clients to consider the synergies from concurrently retrofitting the non-showroom spaces. Energy costs comprise a meaningful portion of dealer earnings, and today's building products can combine with utility rebates and EPAct tax savings to reduce costs.

The re-imaging of domestic car dealerships is one of the early steps of the major overhaul that the U.S. car industry needs and EPAct tax incentives can be an important part of these initiatives.

Endnotes

1 Energy Policy Act of 2005 (P.L. 109-58). *See* Charles Goulding, Jacob Goldman and Raymond Kumar, *Energy Tax Aspects of Car Dealerships*, Corp. Bus. Tax'n Monthly, July 2009, at 11.

[2] See David Welch, *GM Will Push Dealers to Upgrade*, Bloomberg Bus. Week, Sept. 15, 2009, *available at www.businessweek.com/bwdaily/dnflash/content/sep2009/db20090915_870120.htm?chan=rss_topDiscussed_ssi_5.*

[3] *See* Charles Goulding, Jacob Goldman and Taylor Goulding, *The Tax Aspects of "Daylight Harvesting"*, Corp. Bus. Tax'n Monthly, Aug 2008, at 35.

[4] *See* NADA Greener Dealership Case Studies, *www.nada.org/green/greenstores/casestudies/greener_ studies.htm.*

[5] *See id.*

[6] *See* Charles Goulding, Jacob Goldman and Raymond Kumar, *Large EPAct Energy Tax Deduction Opportunities for Commercial Heaters*, Corp. Bus. Tax'n Monthly, Jan. 2010, at 11.

Figure 2. Direct Fired Natural Gas Heater EPAct Deductions

Warehouse, Industrial Facilities, Storage Centers and Truck Distribution Centers Potential EPAct Tax Deductions

Sample Square Footage	Typical Fluorescent Upgrade ($1.20/Sq ft)	Low Wattage Lighting Including Induction and LED Lighting ($1.80/Sq ft)
50,000	$60,000	$90,000
100,000	$120,000	$180,000
250,000	$300,000	$450,000
500,000	$600,000	$900,000
750,000	$900,000	$1,350,000
1,000,000	$1,200,000	$1,800,000

Energy Equipment

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lighting upgrade to highly energy efficient fluorescent, induction or LED lighting in order to maximize the EPAct tax deduction. Figure 2 illustrates the potential EPAct tax deductions for warehouses and industrial buildings where a high efficiency natural gas heater is installed with an energy efficient lighting upgrade.

Hybrid Gas/Electric Chillers

A hybrid chiller conditions a building using natural gas or electricity as alternative fuel sources. It is programmed to use gas in the summer months when electricity is more expensive and electricity during the winter months when natural gas is more expensive. Because a hybrid chiller takes advantage of time-of-day energy pricing and seasonal gas and electricity pricing to drastically lower building energy cost, and EPAct tax deductions are driven solely by total building energy cost reduction, the installation of a hybrid chiller will typically qualify for large immediate EPAct HVAC tax deductions.

Combined Heat and Power Systems

Combined Heat and Power systems, sometimes known as cogeneration facilities, are able to generate electricity while also producing thermal energy, essentially providing usable heat from the waste heat given off during the electrical generation process. Because CHP systems capture that waste heat, facilities relying on CHP can eliminate redundancy in their systems, reducing overall energy use and lowering overall building emissions. CHP systems are preferred by the U.S. Department of Energy and the EPA because of their energy efficiency and greenhouse gas reductions[9]. Also, installation of a CHP system will help a company comply with the EPA's July 2010 pollution emissions reduction proposal, which will affect 31 states and Washington D.C. Typically, natural gas is the fuel used in these highly energy efficient CHP systems.[10] In addition, CHP facilities are eligible for the 10-percent federal tax credit or cash grant mentioned above.

Conclusion

Huge new natural gas finds and improved natural gas distribution is going to enable building owners in cold winter jurisdictions, particularly in the Northeast, to have assured supplies of natural gas. Informed property owners can use Code Sec. 179D and 10-percent tax credits or cash grants to help reduce the cost of the required heating equipment.

Endnotes

[1] Energy Policy Act (EPAct) of 2005 (P.L. 109-58).

[2] American Recovery and Reinvestment Act of 2009 (P.L. 111-5).

[3] Payments for Specified Property in Lieu of Tax Credits Guidance, Mar. 2010, *www.ustreas.gov/recovery/docs/guidance.pdf.*

[4] Ben Casselman, *US Gas Goes From Bust to Boom*, Wall St. J., Apr. 30, 2009; *http://online.wsj.com/article/SB124104549891270585.html*, posted to Web Jan. 4, 2010.

[5] *Marcellus Shale Gas: New Research Results Surprise Geologists!* Geology.com—Earth Science News, Maps, Dictionary, Articles, Jobs, Jan. 4, 2010, *http://geology.com/articles/marcellus-shale.shtml.*

[6] *See, Exxon-Xto Energy Merger Completed*, iStockAnalyst.com, June 29, 2010, *http://istockanalyst.com/article/viewarticle/articleid/4259788.*

[7] *See* Tom Taulli, *Royal Dutch Shell Scoops Up East for $4.7 Billion*, dailyfinance.com, May 28, 2010, *www.dailyfinance.com/story/company-news/royal-dutch-shell-buys-east-resources/19495355/.*

[8] See Charles Goulding, Jacob Goldman and Raymond Kumar, *Large EPAct Energy Tax Deduction Opportunities for Commercial Heaters*, Corp. Bus. Tax'n Monthly, Jan. 2010, at 11.