

Understanding Hotel LED Lighting/Chiller Combination Tax Opportunities

By Charles Goulding, Kenneth Wood and Christopher Zalesky

Charles Goulding, Kenneth Wood and Christopher Zalesky suggest ways that hotel building owners can update their lighting systems and use EPAct to generate operating and tax savings.

Throughout the country hotels are upgrading to very energy-efficient LED lighting. For the hotel industry, 2011 was the best year since 2008, giving hotel owners renewed confidence. Large hotels often have central chillers and can utilize the EPAct tax incentive opportunities to support the investment of LED and/or HVAC upgrades. Many hotels deferred maintenance and facilities upgrades during the economic downturn. The industry is now seeing a marked increase in energy-efficient retrofits.

The EPAct Tax Opportunity

Pursuant to Code Sec. 179D, as enacted by the Energy Policy Act of 2005 (EPAct),¹ warehouse 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.

EPAct Category of Hotels

Hotels are one of the most favored EPAct tax deduction categories.² Hotel lighting in guest rooms is exempt from the EPAct tax bi-level switching rule, which is an advantage since guest rooms are the largest space category in hotels.

The EPAct tax ASHRAE rule set uses the inefficient individual room units, commonly called PTAC units, as the reference building for tax savings. A hotel with a centralized chiller system is very energy efficient compared to hotels that utilize PTAC units. This is why hotels with a central HVAC system are a favored EPAct category (chillers are quite common in large hotels).

LED Lighting and Hotels

LED lighting is characterized by low wattage that greatly reduces energy-related operating costs and long life which greatly reduces replacement-related maintenance costs. LED lighting is particularly

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suitable for interior guest room packages (the largest category of spaces in a hotel), restaurants and retail spaces.³

Putting the LED Chiller Tax Combination Together

LED lighting is expensive so hotel owners with chillers should consider modeling the building in IRS-approved software, seeking either a \$1.20- or a \$1.80-per-square-foot EAct tax deduction.

Hotel LED/Chiller Tax Planning Example

Presume a 300,000 square foot chiller hotel is interested in installing LED lighting at an installed project cost of \$500,000. An EAct knowledgeable tax adviser can predetermine whether the project will qualify for a \$1.20- or a \$1.80-per-square-foot tax deduction.

At \$1.20 per square foot, the EAct tax deduction for the LED project will be \$360,000. At \$1.80 per square foot, the EAct tax deduction will be for the full LED project cost of \$500,000.

Hotel Energy Bench Marking

Large hotels, 50,000 square feet or greater, are subject to mandatory building energy bench marking in major hotel markets such as New York, Washington D.C., all of California, Austin and Seattle.⁴ Tax advisors for large hotels in these jurisdictions should discuss the bench marking results with facilities personnel and make sure they realize that EAct tax incentives are available to support the energy-reducing investments necessary to remedy low scores.

Kitchen and Laundry Space

Hotels often have large kitchen and laundry (so-called "back of the house") spaces that have historically used T-12 fluorescent lighting. This lighting is so energy inefficient compared to today's lighting

products that it was made illegal to manufacture this type of lighting in the United States as of July 1, 2010.

Once the manufacturing of these products ceases, the cost of replacing these inefficient lamps will increase. Simply stated, hotels should consider acting as soon as possible to replace these lighting fixtures to save on both energy and lamp replacement costs. The EAct lighting tax incentive can be used to address the opportunities related to these legally mandated product changes.

Parking Garages

Many hotels have large adjoining parking garages that can save substantial energy costs and generate large tax deductions by upgrading to energy-efficient fixtures. It is generally advisable to use vapor sealed lighting fixtures in these applications so that the auto exhaust fumes do not compromise the lighting fixture.

In Notice 2008-40,⁵ the IRS announced that parking garages are a property class specifically entitled to use the EAct tax deductions. Also, parking garages are excluded from the tax bi-level switching requirement.⁶

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ENDNOTES

- ¹ Energy Policy Act of 2005 (P.L. 109-58) ("EAct").
- ² Charles R. Goulding, Jacob Goldman and Taylor Goulding, *Hotels and Motels Most Favored Energy Policy Act Tax Properties*, CORP. BUS. TAX'N MONTHLY, Mar. 2009.
- ³ Charles R. Goulding, Raymond Kumar and Jennifer Pariente, *LED Lighting Can Play a Key Role in Securing EAct Tax Benefits*, IMARK NOW, Feb. 2012.
- ⁴ Charles R. Goulding and Spencer Marr, *Washington D.C. Energy Benchmarking Impacts Local Hotels*, WORDPRESS, Jun. 2011, available online at <http://energytaxsavers.wordpress.com/article/washington-d-c-energy-benchmarking-1xedf26uc9hpij-37>.
- ⁵ Notice 2008-40, IRB 2008-14, 725.
- ⁶ Charles R. Goulding, Jacob Goldman and D. Malcolm Thomas, *Multiple Lighting Technologies Drive Large EAct Tax Deductions for Parking Garages*, PARKING PROFESSIONALS, Aug. 2010.