The EPAct Tax Aspects of the New Multifamily High-Rises Energy Star Designation

By Charles Goulding, Spencer Marr and Daniel Penza

In light of the EPA's announcement that the Energy Star designation now extends to multifamily high-rises, Charles Goulding, Spencer Marr and Daniel Penza discuss tax incentives available to building owners across the United States and then focus on recent New York City law changes to illustrate how local laws can be used in concert with federal laws to achieve Energy Star designation.

The Environmental Protection Agency (EPA) announced on August 30, 2011, that it will now be extending the Energy Star designation to multifamily high-rises.[1] The EPA announcement is going to have important cost-saving and tax consequences for owners of such properties. The Energy Star Program is the nation's most highly regarded and universally accepted means of benchmarking the energy efficiency of specific buildings against the energy performance of similar facilities.

In 2010 alone, buildings participating in the Energy Star Program saved $18 billion on their utilities, and that was a year in which multifamily high-rises were excluded from the program. Now that the EPA has expanded the purview of the Energy Star Program, it is able to serve the entire residential building sector.

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This is an extremely important development because the huge cadre of existing multifamily apartment buildings is particularly energy-inefficient.

Since the primary motivator to join the program is utility savings, multifamily high-rise owners must incorporate a wide range of energy-efficient improvements into the building's design and construction in order to garner the Energy Star designation. Typically, these improvements include measures to increase the energy efficiency of lighting, heating and cooling systems, insulation and windows. Fortunately, the federal Energy Policy Act (EPAct)[2] program exists as a tax-saving supplement to the Energy Star Program, so that building owners can reap the combined benefits of utility cost savings and tax savings when they upgrade their building's energy efficiency.

While the EPA's multifamily policy change is going to have a national impact, New York City serves as an illustrious example of how a city's local codes interact with the Energy Star Program to have a comprehensive impact on multifamily high-rise owners. The first portion of this article describes the tax incentives available to all multifamily apartment owners and the second portion focuses on the New York City-specific impact.

Nationwide Tax Incentives: Code Sec. 179D

Pursuant to Code Sec. 179D, as enacted by EPAct, multifamily high-rise owners making qualifying energy-reducing investments in their new or existing locations can obtain immediate tax deductions of up to $1.80 per square foot.

If the building project does not qualify for the maximum Code Sec. 179D $1.80-per-square-foot immediate tax deduction, there are tax deductions of up to $0.60 per square foot for each of the three major building subsystems: lighting, HVAC (heating, ventilating and air conditioning) 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.

Alternative Energy Tax Credits and Grants

There are also multiple 30-percent and 10-percent tax credits available through the American Recovery and Reinvestment Act (ARRA)[3] to multifamily high-rise owners for a variety of alternative energy measures, with varying credit termination dates. For example, the 30-percent solar tax and fuel tax credits, as well as the 10-percent combined power tax credit, expire January 1, 2017. The 30-percent closed-loop and open-loop biomass credit expires January 1, 2014.

All alternative energy measures that are eligible for the 30-percent and 10-percent tax credits are also eligible for equivalent cash grants for the three years starting January 1, 2009, and ending December 31, 2011.

Unique 2011 Opportunity: Enhanced Bonus Tax Depreciation

The credits described above are ordinarily eligible for five-year modified accelerated cost recovery system (MACRS) depreciation, but building owners who installed these renewable energy systems after September 8, 2010, and before December 31, 2011, can take a 100-percent depreciation tax bonus immediately. Even if building owners missed this 2011 window, they can enjoy a 50-percent tax depreciation bonus on alternative energy equipment placed in service from January 1, 2011, through December 31, 2012.

Federal Lighting Bans

Multifamily apartment buildings are impacted by three federal lighting bans related to:

1. metal halides
2. T-12 fluorescent
3. incandescent lighting

As of January 1, 2009, there is a national manufacturing ban on most probe-start metal halides. As of July 1, 2010, T-12 fluorescent lights were similarly banned and limited to 10 per pack for distribution.

Starting in 2012, manufacturers are banned from manufacturing and importing the traditional 100-watt light bulbs. Bulbs will have to be more energy-efficient using no more than 72 watts, even including halogen, incandescent, compact fluorescent (CFL) and light-emitting diode (LED) light bulbs. This bulb change is part of the federal Energy Independence and Security Act signed in 2007.[4] Beginning in 2012 new bulbs must use 25-to-30-percent less energy nationwide starting with the 100-watt light bulb. Other incandescent bulbs such as 75-, 60- and 40-watt bulbs will be phased out by 2014. Many apartment buildings have incandescent lighting inside the resident apartments that needs to be upgraded and often have T-12 lighting in the support spaces that needs to be retrofitted.

Apartment Building HVAC EPAct Incentives

All apartments with central HVAC systems get special privileges under the EPAct tax provisions in accordance with the 2001 American Society of Heating Refrigeration and Air Conditioning Engineers (ASHRAE) reference building standards. An apartment building with individual room units is by definition less efficient than a building with central HVAC systems. Simply stated, apartment buildings that install central cooling systems typically qualify for EPAct tax savings.

The New York City Multifamily High-Rise Energy Star Opportunity

It is the authors' opinion that the New York City (NYC) multifamily apartment building market typifies the interaction between local laws and the Energy Star Program. The rest of this article describes how to integrate multiple recent NYC law changes and the federal EPAct tax incentives into Energy Star accomplishment levels.

NYC's Benchmarking Requirements

With the new local benchmarking law in effect, all buildings in NYC with an area over 50,000 square feet are obligated to submit an annual energy benchmark rating. Energy benchmarking requires data submissions reporting total energy and water use for a building for the previous year using the U.S. Environmental Protection Agency's web-based Portfolio Manager. The NYC law includes all buildings over 50,000 gross square feet and includes two or more buildings on the same lot that total 100,000 square feet or more.

This new benchmarking law requires NYC building owners or operators to submit their energy data and have it compared to similar buildings within the city. This is going to have a major effect on the multifamily high-rise market, as a significant portion of the city's apartment buildings occupy at least 50,000 square feet. We believe that buildings performing below the 50-percentile level for building energy and water use (performing lower than half of the comparable buildings) will be avoided by tenants who are increasingly conscious of their utility expenses.[5]

> In 2010 alone, buildings participating in the Energy Star Program saved $18 billion on their utilities, and that was a year in which multifamily high-rises were excluded from the program.

It would behoove any NYC apartment building owner who gets favorable results from the mandatory benchmarking to give strong consideration to applying for Energy Star designation so that their tenants know that the building is performing at higher energy efficiency levels as compared to similar multifamily buildings.

NYC Energy Conservation Code

New York City's Energy Conservation Code (ECC) is effective as of December 2009, requiring the use of modern technical methods, devices and improvements that tend to minimize consumption of energy for newly constructed commercial and specified existing buildings. NYC's EEC is intended to comply with the requirements of the ARRA.

The ARRA specifies that states and localities should implement the ASHRAE 90.1-2007 standard. NYC's EEC is required for new construction or additions, alterations, renovations or repairs to an existing building as if they relate to new construction.

For lighting, the NYC's EEC requires that if 50 percent or more of the lighting in a space is being replaced than all the lighting has to be retrofitted. By requiring a complete lighting upgrade for 50 percent or more restoration the law facilitates a higher benchmarking rating and larger EPAct tax incentives as discussed above.

NYC's Heating Law Requirements

Building owners in NYC will have to phase out their most polluting grades of heating regulation and replace their buildings' heating systems with a cleaner fuel source by 2015.[6] Further, any newly installed boilers will have to burn an even less polluting grade of oil, known as No. 2 oil, or use natural gas. The law is part of Mayor Bloomberg's aggressive environmental policy known as PlaNYC.[7]

Boilers that are not replaced by 2030 will need to be modified to meet the new regulations. Since building owners across the city will already be required to make a minimum level of investment in their heating systems, they should consider making further energy-reducing investments that will enable them to qualify for federal EPAct tax deductions, particularly energy-efficient lighting.

Combining Financial Incentives

In addition to energy savings and tax savings, the two other economic incentives available for these heating and lighting upgrades are financing and utility rebates. All of the incentives often produce additive benefits when used with a combined measure, meaning upgrading more than one energy savings measure item at once. A large amount of financing is available for these projects from a variety of sources, including financial institutions, vendor financing from equipment sellers and on-bill financing from energy sellers.

NYC Laws and Incentives

Utility rebates are available from Con Edison, New York State Energy Research and Development Authority (NYSERDA) and National Grid for both lighting and HVAC, depending on the nature of the energy savings equipment and the location of the project.

Con Edison Incentives for NYC Residential/ Multifamily Buildings

Con Edison customers who own or manage between five- and 75-unit buildings are eligible to participate in Con Edison's multifamily energy survey. Under that program, an energy professional will assess customers' lighting, heating and cooling equipment and appliances, after which they will give these customers energy saving recommendations.

An enrolled building can receive free CFLs, water saving devices and smart strips for the residence, and building owners are offered incentives and rebates for upgrades to lighting fixtures, LED exit signs, chillers and HVAC systems.

Learn About Eligible Equipment and Incentives

To learn more about the eligible equipment and incentives from Con go to Con Edison's energy efficiency website: *http://www.coned.com/energyefficiency/*.

NYSERDA Incentives for NYC Buildings

NYSERDA has commenced a benchmarking pilot, an initiative that provides benchmarking and operational assessments. Energy and Resource Solutions (ERS) will compare participating facilities with the EPA's Portfolio Manager and develop site-specific reports recommending operational or system modifications that can result in immediate energy savings.

This program from NYSERDA offers up to $7,000 per commercial, industrial or institutional building with no cost sharing required. This will eliminate out-of-pocket expenses for participants under the $7,000 threshold as funds are paid directly from NYSERDA to ERS. Participants will receive benchmarking services to guarantee their fulfillment with Local Law 84 and a walk-through of the building with the facilities staff to identify low- and no-cost operational and maintenance energy-efficient procedures.[8]

Conclusion

By extending the Energy Star Program to multifamily high-rises, the EPA has completed the circle of residential energy performance standards around the country. Owners of multifamily apartment buildings, especially those in major metropolitan areas like New York City, are advised to use the multitude of local, state and federal incentives in retrofitting their buildings' energy systems in order to qualify for the Energy Star Program.

Endnotes

1 Energy Star Program information may be found at *http://yosemite.epa.gov/opa/admpress.nsf/0/69eba6bb753e8499852578fc005571b0?OpenDocument*.

2 Energy Policy Act of 2005 (P.L. 109-58).

3 American Recovery and Reinvestment Act of 2009 (P.L. 111-5)

4 Energy Independence and Security Act of 2007 (P.L. 110-140).

5 Charles Goulding and Daniel Penza, New York City Hotels Energy Benchmarking Related Legal and Tax Compliance, Google Knol, June 18, 2011, available online at http://knol.google. com/k/charles-goulding/new-york-city-hotels-energy/1xedf26uc9hpj/33#.

6 Charles Goulding and Spencer Marr, *The Energy Tax Aspects of New York City's 10,000 Building Heating Oil Conversion*, Google Knol, June 23, 2011, available online at *http://knol .google.com/k/charles-goulding/the-energy-tax-aspects-of-new-york-city/1xedf26uc9hpj/39#*.

7 Information about PlaNYC is available online at *www.nyc.gov/html/planyc2030/html/about/about.shtml*.

8 Find out more about the programs in reference to the Greener, Greater Building Plan offered by NYSERDA, along with how multifamily buildings can participate in the benchmarking pilot on NYSERDA's website: *www.nyserda.org/programs/flextech-benchmarking/*.