

The Energy Tax Aspects of Revitalizing Detroit's Building Engine

By Charles R. Goulding, Shane Holmes and Charles G. Goulding

Charles R. Goulding, Shane Holmes and Charles G. Goulding discuss how Detroit building owners and investors can qualify for large EPAct tax incentives as they renovate buildings that are being valued at bargain prices.

Detroit has some of the nation's most impressive commercial building inventory. As a result of the economic downturn, the market values of those properties have declined to bargain prices that are getting leading property investors' attention. Many of these buildings require renovations eligible for large EPAct tax incentives.

Tax Opportunities

Pursuant to Code Sec. 179D, as enacted by the Energy Policy Act of 2005 (EPAct),¹ buildings 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 doesn't qualify for the maximum \$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, heating, ventilating and air conditioning (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.

Recent Transaction

The economic downturn has hurt the property value of iconic Detroit buildings. For example, the Penobscot Building was sold to the Canadian real estate company Triple Group for \$5 million.² The \$5-per-square-foot price was a bargain compared to \$28 per square foot at which buildings in downtown Detroit were valued in 2011, and vastly cheaper than the \$200 per-square-foot average price tag for buildings nationwide, according to Real Capital Analytics.

Detroit's Population Trend

One of the factors contributing to Detroit's falling real estate values is the city's declining population. According

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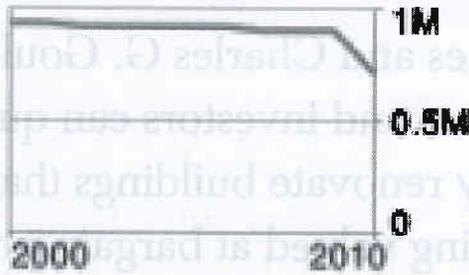
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to data from the U.S. Census, Detroit's population has declined from 945,297 in July 2000 to 713,777 in July 2010. The most pronounced drop occurred between July 2009 and July 2010, when 85 percent of the aforementioned population decline occurred.

Chart 1.



Discerning Tenants

As energy costs rise and lease prices fall, the relative cost of energy becomes increasingly discernible. The Department of Energy (DOE) estimates that the average energy cost for an office building is \$1.51 per square foot.³ In New York City, where rent per square foot is \$48,⁴ energy is approximately three percent of lease costs. By contrast, Triple Properties plans to rent space in the Penobscot Building at a price of \$10;⁵ at that price, energy costs amount to 15 percent of a lease. With energy constituting a much greater portion of the costs to rent a Detroit office space, and with energy benchmarking becoming increasingly standardized (if not required), Detroit office managers have a need to assist owners in making their properties more attractive to tenants through energy-efficient improvements.

Chart 2.

Location	Approximate Cost of Energy	Average Cost to Lease Office Space per S.F.	Cost of Energy as a Percentage of Rental Costs
New York City	\$1.51	\$48	3.1%
Detroit	\$1.51	\$16	9.4%
Penobscot Building	\$1.51	\$10	15.1%

Sample Detroit EAct Tax Opportunities

Chart 3 presents the EAct potential benefits for the Penobscot Building.⁶ Additionally, the EAct opportunity for some of Detroit's other larger buildings are presented, including the downtown Westin hotel, a marquee property already restored, and the new Whole Foods currently under construction.

Conclusion

Population decline has been a major factor in the decline of Detroit real estate values. By making improvements to lighting, HVAC and the building envelope, building owners can improve the energy efficiency of their buildings as well as save taxes. Reduced energy costs, in turn, should help lure more tenants back to Detroit properties as the city continues its efforts at overhaul and revitalization.

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Chart 3.

Property	Total Square Footage	Lighting		HVAC	Building Envelope	Total
		Minimum Deduction	Maximum Deduction	Maximum Deduction	Maximum Deduction	
DTE Energy Headquarters (25 floors)-One Energy Plaza	2,050,525	\$ 615,158	\$ 1,230,315	\$ 1,230,315	\$ 1,230,315	\$ 3,690,945
GM Headquarters-Detroit Marriott at the Renaissance Center (73 floors)- 400 Renaissance Center Drive	1,812,000	\$ 543,600	\$ 1,087,200	\$ 1,087,200	\$ 1,087,200	\$ 3,261,600
One Detroit Center (45 floors)-500 Woodward Avenue	1,674,000	\$ 502,200	\$ 1,004,400	\$ 1,004,400	\$ 1,004,400	\$ 3,013,200
Book Tower (40 floors)-1265 Washington Boulevard	1,276,290	\$ 382,887	\$ 765,774	\$ 765,774	\$ 765,774	\$ 2,297,322
Patrick V. McNamara Federal Building (28 floors)- 477 Michigan Avenue	1,000,000	\$ 300,000	\$ 600,000	\$ 600,000	\$ 600,000	\$ 1,800,000
Penobscot Building (49 floors)-645 Griswold Street	776,486	\$ 232,946	\$ 465,892	\$ 465,892	\$ 465,892	\$ 1,397,675
Guardian Building (40 floors)-500 Griswold Street	750,000	\$ 225,000	\$ 450,000	\$ 450,000	\$ 450,000	\$ 1,350,000
Ford Headquarters (11 floors)- P.O. Box 6248, Dearborn, MI	596,673	\$ 179,002	\$ 358,004	\$ 358,004	\$ 358,004	\$ 1,074,011
211 West Fort Building (29 floors)-211 West Fort Street	565,000	\$ 169,500	\$ 339,000	\$ 339,000	\$ 339,000	\$ 1,017,000
Renaissance Center 100 Tower (39 floors)	550,000	\$ 165,000	\$ 330,000	\$ 330,000	\$ 330,000	\$ 990,000
Renaissance Center 200 Tower (39 floors)	550,000	\$ 165,000	\$ 330,000	\$ 330,000	\$ 330,000	\$ 990,000
Renaissance Center 300 Tower (39 floors)	550,000	\$ 165,000	\$ 330,000	\$ 330,000	\$ 330,000	\$ 990,000
Renaissance Center 400 Tower (39 floors)	550,000	\$ 165,000	\$ 330,000	\$ 330,000	\$ 330,000	\$ 990,000
John Madden Building (28 floors)- 150 West Jefferson Avenue	493,000	\$ 147,900	\$ 295,800	\$ 295,800	\$ 295,800	\$ 877,400
Fisher Building (30 floors)- 3011 West Grand Boulevard	486,991	\$ 146,097	\$ 292,195	\$ 292,195	\$ 292,195	\$ 876,584
Westin Book Cadillac Hotel (32 floors)- 1114 Washington Boulevard	438,114	\$ 131,434	\$ 262,868	\$ 262,868	\$ 262,868	\$ 788,605
Cadillac Tower (40 floors)-65 Cadillac Square	348,000	\$ 104,400	\$ 208,800	\$ 208,800	\$ 208,800	\$ 626,400
One Woodward Avenue (29 floors)	332,735	\$ 99,821	\$ 199,641	\$ 199,641	\$ 199,641	\$ 598,923
David Broderick Tower (37 floors)-10 Witherell Street (being renovated)	193,315	\$ 57,995	\$ 115,989	\$ 115,989	\$ 115,989	\$ 347,967
David Stott Building (41 floors)-1150 Griswold Street	163,000	\$ 48,900	\$ 97,800	\$ 97,800	\$ 97,800	\$ 293,400
Buhl Building (29 floors)-535 Griswold Street	117,382	\$ 35,215	\$ 70,429	\$ 70,429	\$ 70,429	\$ 211,288
Whole Foods Market-corner of Mack Ave. and John R. St. (under construction)	21,000	\$ 6,300	\$ 12,600	\$ 12,600	\$ 12,600	\$ 37,800
Totals:	15,294,511	\$ 4,588,353	\$ 9,176,707	\$ 9,176,707	\$ 9,176,707	\$ 27,530,120

- ² Available online at www.idc.com/getdoc.jsp?containerId=prUS23299912.
- ³ Available online at <http://bits.blogs.nytimes.com/2012/05/30/rim-shares-drop-and-analysts-warn-of-further-trouble/>.
- ⁴ Charles R. Goulding, Spencer Marr and Charles G. Goulding, *New Car Fuel Rules Drive Product Innovation and R & D Tax Credits*, CORP. BUS. TAX'N MONTHLY, May 2012.
- ⁵ Available online at www.tuaw.com/2012/05/29/how-anodizing-aluminum-finishes-apples-products/.
- ⁶ Available online at www.youtube.com/watch?v=ZPZ7y1EDKvk&feature=player_embedded#1.
- ⁷ Available online at www.motorola.com/Consumers/US-EN/Consumer-Product-and-Services/Mobile-Phones/DROID-RAZR-MAXX-by-MOTOROLA-US-EN.
- ⁸ Available online at www.tmonews.com/2012/05/editorial-why-a-snapdragon-s4-galaxy-s-iii-is-awesome/.
- ⁹ Available online at www.otterbox.com/armor-series/armor-series,default,pg.html.
- ¹⁰ Available online at www.zagg.com/invisibleshield/index.php.
- ¹¹ Available online at <http://content.usatoday.com/communities/sciencefair/post/2011/06/obama-unveils-manufacturing-initiative/1#.T9YHNdVYuUI>.
- ¹² Available online at www.whitehouse.gov/the-press-office/2011/02/10/president-obama-details-plan-win-future-through-expanded-wireless-access.

Monetizing

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Assessment (BEPA) standard. The new BEPA standard is designed to help buyers and lenders understand and compare a building's energy consumption and related operating costs and has been critical to the emerging fields of energy savings performance contracts and energy savings warranty insurance.

Conclusion

The large property managers are sophisticated companies serving sophisticated clients. Billion-dollar tax incentives for an industrial sector do not arise often. Hopefully the industry will soon realize the magnitude of the EAct tax incentive opportunity and act on it.

ENDNOTES

- ¹ Energy Policy Act of 2005 (P.L. 109-58) ("EAct").
- ² Theresa Agovino, *Brokers battle for share*, CRAIN'S NEW YORK BUSINESS, May 2012.
- 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 Available online at <http://www.bizjournals.com/dayton/datacenter/leed-certified-building-database.html?appSession=615188892608404>.
- ⁵ Charles R. Goulding, Taylor Goulding and Amelia Aboff, *How LEED 2009 Expands EAct Tax Savings Opportunities*, CORP. BUS. TAX'N MONTHLY, Sep. 2009.
- ⁶ See <http://www.irs.gov/pub/irs-pdf/i3115.pdf> for IRS Form 3115.
- ⁷ Charles R. Goulding and Spencer Marr, *Washington D.C. Energy Benchmarking Impacts Local Hotels*, June 2011, available online at www.energytaxsavers.com/articles/Article%20-%20Washington%20D.C.%20Energy%20Benchmarking%20Impacts%20Local%20Hotels%20-%20Google%20Knol.pdf.

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ENDNOTES

- ¹ Energy Policy Act of 2005 (P.L. 109-58) ("EAct").
- ² *Doubling Down in Detroit*, WALL ST. J., June 6, 2012, at C8.
- ³ Available online at www.eia.gov/emeu/consumptionbriefs/cbecs/pbawebsite/office/howuseenergy.htm.
- ⁴ Available online at www.inc.com/news/articles/2010/10/washington-dc-rents-top-those-in-nyc.html.
- ⁵ Available online at www.crainsdetroit.com/article/20120506/SUB01/305069976/silverdome-owner-buys-penobscot.
- ⁶ Square footage is estimated using Google Earth and taken from the following websites: Wikipedia, www.mobileair.com/guardian-building, www.transwestern.net/city/Detroit/Property-Listings/Pages/Lease-Properties.aspx, www.crainsdetroit.com/article/20091020/FREE/910209995/northern-group-loses-control-of-cadillac-tower-judge-appoints-farbman-group-to-monitor-building, ezinearticles.com/?Detroit-Commercial-Property--Now-Is-The-Time-to-Buy!&id=6815809, www.redico.com/leasing-opportunities/land/property/71-one-woodward, www.loopnet.com/Listing/16168358/10-Witherell-Street-Detroit-MI/, www.loopnet.com/Listing/16923760/211-W-Fort-Street-Detroit-MI/, and www.freep.com/article/20120514/BUSINESS06/120514018/Whole-Foods-Midtown-Detroit.

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Conclusion

While touting the pilot program as a more rational and practical interpretation of the statute, some practitioners remain concerned that the PBGC has not yet taken the opportunity to clarify what types of business transactions constitute ERISA Sec. 4062(e) events. Accordingly, it seems that defined benefit pension plan sponsors, their legal counsel and actuarial advisors must continue to carefully scrutinize business transactions in order to ascertain whether they believe that the requirements of ERISA Sec. 4062(e), with its accelerated funding and reporting obligations, are applicable. Without such careful analysis, defined benefit pension plan sponsors may be surprised by heavy unanticipated funding obligations and PBGC penalties imposed for reporting and disclosure failures. It remains to be seen what modifications will ultimately be made by the PBGC with respect to the 2010 Proposed Regulation.

ENDNOTES

- ¹ Matthew I. Whitehorn, *ERISA Sec. 4062(e): A Potential Liability Trap for the Unwary Downsizing Pension Plan Sponsor*, CORP. BUS. TAX'N MONTHLY, May 2012, at 31.
- ² 75 FR 48283 (Aug. 10, 2010). 29 CFR §4062.1-10.
- ³ Matthew I. Whitehorn, *Update On ERISA Sec. 4062(e): A Potential Liability Trap for the Unwary Downsizing Pension Plan Sponsor*, CORP. BUS. TAX'N MONTHLY, Nov. 2012, at 9.
- ⁴ Available online at <http://pbgc.gov/about/faq/pg/frequently-asked-questions.4062.html>.
- ⁵ See ERISA Sec. 4063(e).