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Question of the Month: New tax laws deliver the gold for 2017 and beyond: What are the deductions and credits included? - by Jeff Hiatt and Phil Mann

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The Tax Cuts and Jobs Act (TCJA) has created enormous tax savings opportunities for real estate owners. In addition, the low-key Bipartisan Budget Act of 2018 passed this month has restored many of the energy-efficient tax credits and deductions that had expired. Let’s start with the TCJA.

100% Bonus Deduction

While a vast majority of the provisions of the TCJA are effective beginning in 2018, the provision to allow taxpayers to take 100% bonus on assets depreciated over 20 years or less is effective for assets acquired after September 27, 2017. Under the prior tax law bonus depreciation was only allowed at a 50% rate. For the first time ever bonus depreciation is now allowed on used assets at 100%. Under the prior law if a taxpayer constructed or renovated a building, any assets classified as personal property such as carpeting or cabinetry or land improvements such as paving were eligible to be written off 50% in the first year the asset was placed in-service. A taxpayer who acquired an already existing building did not receive this benefit. They do now.

An example will illustrate this benefit. In December 2017, a taxpayer purchases an office building for $5 million, net of land. In a typical office building approximately 10% (in this example $500,000) of the total cost of the building can be allocated to personal property items such as removable flooring, cabinetry, electrical and many other items that have an IRS depreciable life of 7 years. In a suburban office building approximately 15% (in this example $750,000) of the total cost can be allocated to land improvements such as paving, curbs, sewers and many more which have an IRS depreciable life of 15 years. The taxpayer in this example can choose to write-off 100% of the personal property and land improvements for a total deduction of $1.25 million or 25% of the acquisition cost. If the choice was not made the taxpayer would only be allowed to expense $40,000 under the IRS depreciation rules.

Two things to keep in mind for 2017. A taxpayer can elect to take zero, 50% or 100% bonus depreciation on assets acquired between September 28, 2017 and December 31, 2017. In addition, for a building acquisition, if a written binding contract is in place prior to September 28, 2017, the personal property and land improvements are not eligible for the 50% or 100% bonus depreciation unless there are contract contingencies.

20% Pass Through Deduction

Most real estate projects will now be eligible for a 20% pass through deduction. The basic rule is that a real estate entity with $500,000 of taxable income will be allowed to deduct 20% or $100,000 off of the taxable income of the taxpayers owning the real estate entity. There are complicated calculations involved to take the deduction and the deduction will be limited by many factors including the amount of payroll of the entity and the gross asset value of assets times a 2.5% factor and the ultimate taxable income of the taxpayer. While extremely complicated the tax savings opportunity is well worth the cost of hiring a professional to determine the benefit.

The Bipartisan Budget Act of 2018 extended many of the energy efficiency deductions and credits that were not included in the TCJA.

Section 179D Energy-Efficient Commercial Building Tax Deduction

For taxpayers that install energy-efficient buildings or renovations, IRC Code Section 179D provides up to $1.80 per s/f tax deduction for increasing the energy efficiency of HVAC, lighting, and building envelope that meet prescribed energy use reduction standards established by the IRS. Taxpayers can claim the deduction for buildings placed in-service as far back as 1/1/2006 and no amended return is required.

In addition, architects, designers and engineering firms can receive the tax deduction for providing services to a government owned building and they may take the deduction in the year the property is placed in-service or may amend tax returns for 3 prior years to obtain the deduction.

Section 45L Energy-Efficient Home Credit (for apartment owners)

Taxpayers are eligible to receive up to a $2,000 tax credit per dwelling unit for any new construction or renovations that meets prescribed energy use reduction standards established by the IRS. The properties eligible include apartment buildings, adult care facilities, and single and multifamily residences. Taxpayers may take the credit in the year the property is placed in-service or may amend tax returns for 3 prior years to obtain the credit.

This article is intended for general educational and/or informational purposes only and does not replace specific, independent professional advice. This article is based on our current interpretations of the law. These interpretations may ultimately, after further IRS or other guidance be changed.

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