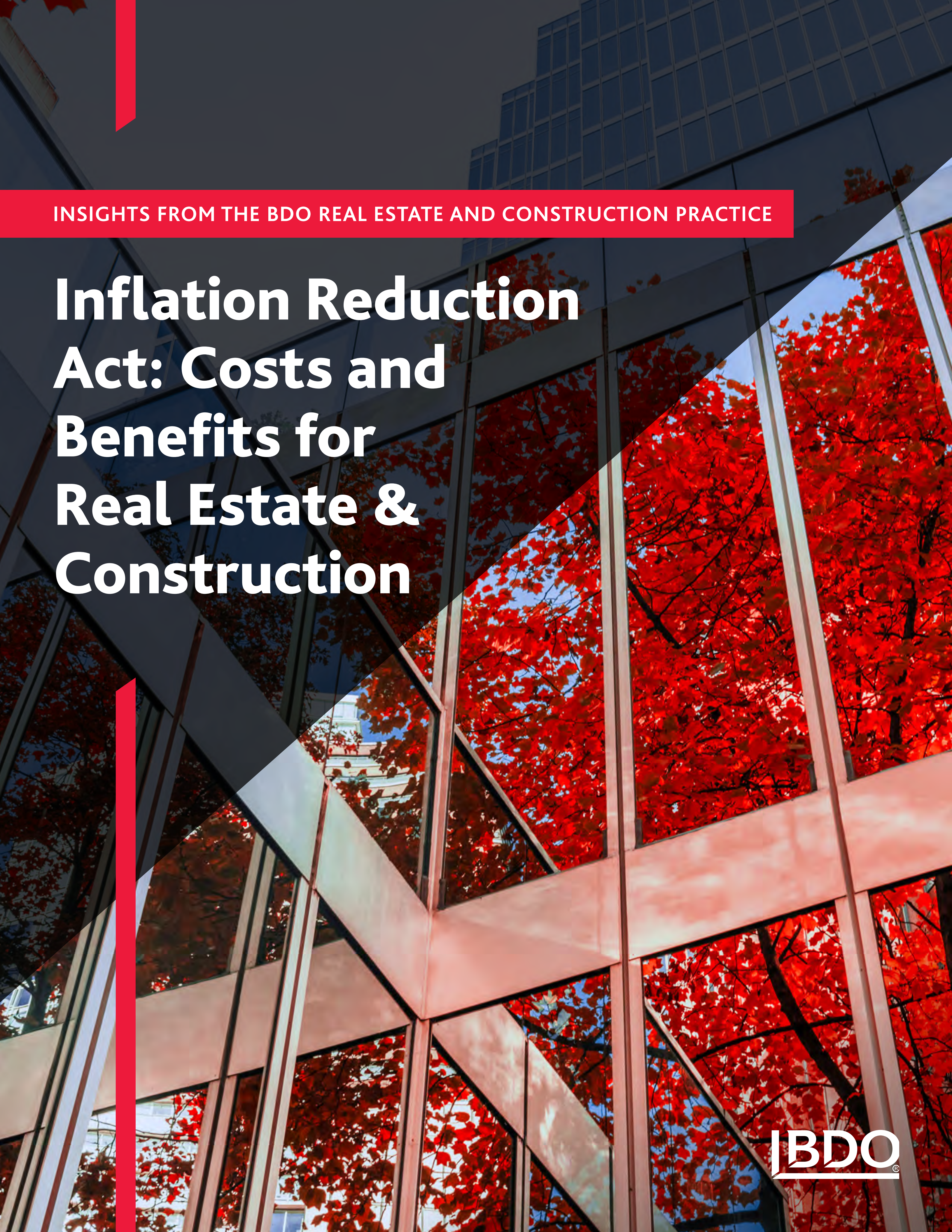


INSIGHTS FROM THE BDO REAL ESTATE AND CONSTRUCTION PRACTICE

Inflation Reduction Act: Costs and Benefits for Real Estate & Construction

The IRA injected roughly **$369 billion of clean energy** and climate change investment in the U.S.

The industry has **not confirmed** how portions of the IRA will be implemented and awaits further guidance

Companies can get prepared for **implementation with a feasibility analysis**

The [Inflation Reduction Act's](#) (IRA's) expansion of key energy efficiency [tax incentives](#) – such as the 179D energy efficient commercial buildings deduction and the 45L new energy efficient home credit – is anticipated to have a significant impact on the real estate and construction industry. The legislation could provide a significant financial boost for firms looking to utilize environmentally conscious building materials and practices, potentially ushering in a new wave of progress in clean energy construction.

Signed into law in August 2022, the IRA's stated intent is to reduce carbon emissions by 40% by 2030 and boost domestic energy production and manufacturing, as well as reduce the deficit and fight inflation. The new law both introduces and expands tax credits available for those investing in clean energy and extends their applicability, in many cases by up to 10 years.

TAX INCENTIVES TO WATCH

The **179D Energy Efficient Commercial Buildings Deduction** gives building owners a deduction of up to $5.00 per square foot for building or renovating energy-efficient buildings.

The **45L New Energy Efficient Home Credit** is a $2,500 tax credit for single family and multifamily developments that comply with Energy Star standards as well as a $5,000 credit for homes that comply with the Zero Energy Ready Homes Program.

CAN THE IRA'S INTENTIONS BECOME REALITY?

The IRA's tax incentives are designed to support a permanent shift toward clean energy in current and future construction projects. However, the dollars that those incentives free up for real estate and construction companies may not offset the significant investment that would need to be made to qualify for the incentives. For example, larger multifamily construction projects may incur more costs than the $500 per unit increase in the Sec. 45L credit to meet the new standards.

The IRA has established longer terms for tax credits and deductions, however. While clean energy tax incentives exist today, many of them have required renewal every one to two years. Uncertainty regarding tax credit renewal has historically made it more challenging for companies to plan for the total cost of construction. With the extension of these tax incentives, some by as many at 10 years, real estate and construction companies are able to plan future investments around these incentives with less risk.

Additionally, the IRA has intentionally focused on domestic supply chains through expanded incentives outside of historical investment in clean energy. Therefore, the domestic supply chain-focused provisions should indirectly benefit the real estate and construction industries should there be a rise in clean energy production in the U.S.

Many of the provisions within the law will require further guidance from the Department of the Treasury and IRS before they are able to be implemented. For example, guidance is required for a **15% corporate alternative minimum tax (CAMT)** based on book income, as well as credit transferability for investment tax credits (ITCs), which are tax credit incentives for investing in clean energy.

The IRA modified and extended the ITC program to provide a 30% tax credit for qualifying investments in clean energy that meet prevailing wage and apprenticeship requirements. However, the ITC is worth only 6% to those that don't meet these requirements, though bonus adders may be stacked on top of the ITC (see table below), and safe harbors do exist based on project size and start of construction deadlines.

Real estate investment trusts (REITs) in particular may be able to take advantage of ITCs in various ways, whether to monetize the credits or to use them to purchase solar facilities. Depending on the implementation of the investment tax credit transfer, REITs may also stand to gain a discount on a limitation on ITCs for REITs if they choose to transfer the credit. Ultimately, REITs could own a solar facility outside of traditionally utilized taxable REIT subsidiaries and take advantage of the ITC by monetizing it, should the anticipated guidance facilitate transferability.

New Energy Efficient Home Credit (IRC Sec. 45L)

Allows a $2,000 credit per single family residential housing unit and multifamily developers, investors, and construction that build energy efficient properties sold or leased through Dec. 31, 2022. The credit increases to $2,500 per unit under Energy Star and $5,000 per unit under the Zero Energy Ready Homes program from Jan. 1, 2023, through Dec. 31, 2032.

Energy Efficient Commercial Buildings Deduction (IRC Sec. 179D)

Enables building owners to claim a tax deduction for installing qualifying energy systems in buildings. The deduction can be up to $1.88 per sq. ft. through Dec. 31, 2022 and increases up to $5.00 per sq. ft. beginning in 2023 as long as the project meets **prevailing wage, and apprenticeship requirements**.

Investment Tax Credit (IRC Sec. 48)

Provides an energy tax credit for investments in various renewable energy properties including solar and geothermal. The credit rate for solar projects is 30% through the end of 2022. Beginning in 2023, there is a base and bonus structure that could increase the credit to 50% for some applicants. The project would still need to meet prevailing wage/apprentice requirements, domestic content requirements, and is located in an energy community. The credit was also expanded to include solar and wind energy investments in low-income communities, tribal land and other projects benefiting the underprivileged.

Alternative Fuel Refueling Property Tax Credit (IRC 30C)

Businesses that install EV chargers and equipment at their property can qualify for a tax credit of up to 30% of the cost. A location requirement was also introduced prescribing applicants should be "non-urban" or low-income sources. The maximum amount allowed was increased to $100,000 for projects completed after Dec. 31, 2022.

HIT THE GROUND RUNNING WITH A FEASIBILITY ANALYSIS

Though [prevailing wage and apprenticeship guidance] has recently been released addressing the IRA's two labor requirements for clean energy developments to provide basic hourly rate of wages and benefits standard for the region of work and to employ a certain amount of registered apprentices to qualify for the bonus tax credit rate, other implementation guidance is yet to be announced by the U.S. Treasury Department and the IRS. As a result, many companies are unsure of how to best incorporate the law's provisions into their development plans. Additionally, though the legislation has been touted as a step in the right direction by U.S. lawmakers, some international players have claimed that it violates international trade agreements and prioritizes domestic sourcing of building materials where cross-border trade practices are in place.

As we wait for further guidance, real estate and construction companies should work closely with their tax advisors to plan for a smooth transition by preparing the necessary documentation and certifications and performing a feasibility analysis. A feasibility analysis evaluates a company's projects and investments, as well as the incentives that will likely be applicable. From there, it maps out the potential business decisions that a company will need to make, depending on future guidance regarding the IRA.

A feasibility analysis can follow five simple steps:

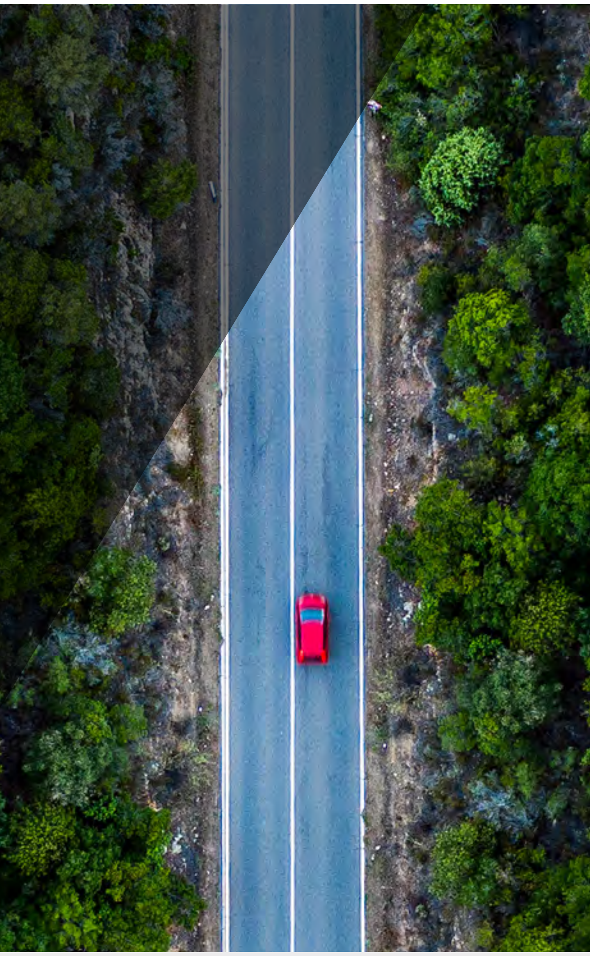
1. **Map out the project's goals.** Look into intended investments your company plans to make for its building project.
2. **Split investments up into distinct groups.** Section relevant investments into qualifying categories like clean energy storage, solar energy or wind energy.
3. **Match investments to potential IRA incentives.** Compare the list of intended investments with the list of available tax incentives and determine overlap.
4. **Conduct a cost-benefit analysis of implementing a tax incentive.** Calculate the degree of investment required to achieve eligibility and the return on investment the tax incentives would offer.
5. **Identify paths to substantiate claims to incentives.** Pull together the documentation required to prove existing or intended adherence to tax incentive requirements.

Another step companies can take to prepare for the implementation of the IRA's tax incentives is to ensure the company and its partners are registered with Energy Star and are following the proper steps for Sec. 45L eligibility. These steps can be taken regardless of whether it is ultimately advantageous to pursue the various incentives, as it can help companies:

- Remain aligned on project priorities
- Identify financial goals
- Stay abreast of current tax incentive offerings

By conducting feasibility analyses, preparing to substantiate claims for tax incentives, and ensuring compliance with industry accepted energy efficiency standards, real estate and construction firms can make the most of the benefits the IRA has to offer.

Careful planning must be balanced with flexibility, however, in order to be able to respond to any eventual changes to the law. Relying on a professional services provider to navigate the IRA can help prevent missed tax credits that result in cost savings or spending too much on qualifying for incentives that may not deliver a return on investment.



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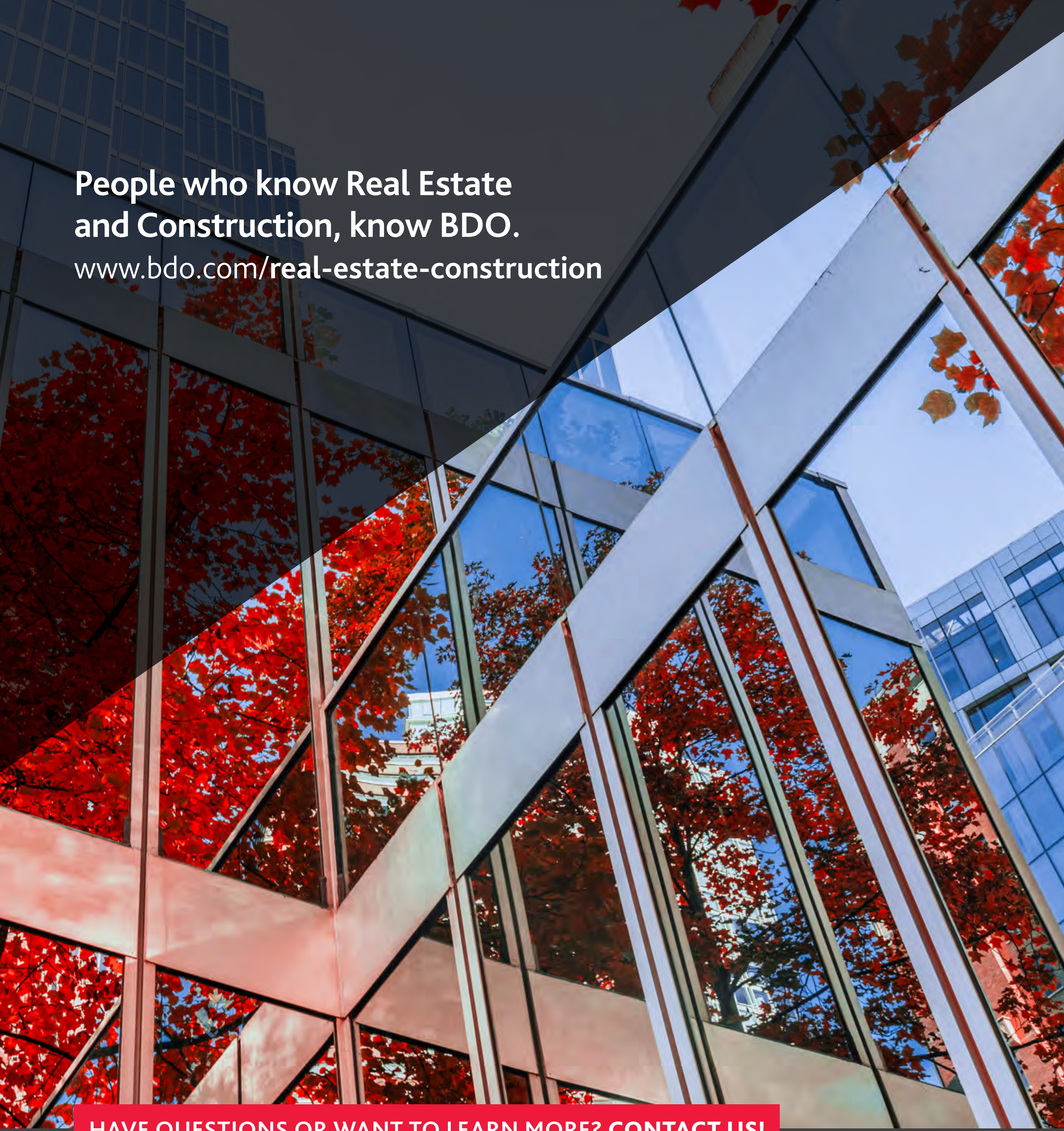

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