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How a Tax Incentive Within the Inflation Reduction Act Could Reshape the Construction Industry



By Marty McCarthy of Marcum LLP

According to the Department of Energy, the tax incentives within section 179D primarily benefit property owners and tenants that make construction expenditures. If you haven't revisited them lately, it's important to note that they were greatly enhanced by the Inflation Reduction Act. Let's take a closer look at the details of the new legislation, and you'll see just how advantageous these recently updated tax incentives can be for contractors and construction firms.

In fact, the incentives introduced by the legislation are so monumental that some construction firms should evaluate applicability to maximize the benefits available.

SECTION 179D TAX INCENTIVES

Officially, section 179D has been a part of the Energy Policy Act since 2005 and was made a permanent fixture in 2020. But, following the Inflation Reduction Act, it's only now becoming much more significant.

Prior to the Inflation Reduction Act, section 179D offered a tax deduction that was capped up to \$1.88 per square foot as long as the project resulted in a 50% improvement in energy efficiency across all of a property's lighting, HVAC, and "building envelope," which covers the energy efficiency of a building's windows, walls, roofing, and foundation, among other areas. For projects that didn't quite reach that bar, partial deductions were available as well. From an accounting perspective, all deductions are good deductions; but \$1.88 per square foot didn't cause contractors to rush out and specialize in energy efficiency. It also didn't lead to a huge explosion in demand for projects focused on improved energy efficiency.

The Inflation Reduction Act, though, changed the benefits in a material way. Under the new legislation, section 179D offers up to \$5.36 in deductions for each square foot of space associated with a project that satisfies the energy efficiency criteria. The tax benefit of 179D can be triggered by new construction, as well as projects that retrofit property and result in a 25% reduction in that property's energy use.

If you're not pulling out a calculator to reassess the value of your projects, you may not yet fully appreciate the significance of this legislative change. This may prove to fundamentally change not only how contractors approach their work, but also, because of a new criteria, even how their business is organized and staffed.

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Alongside that eye-catching increase in the maximum value of the deduction, the legislation introduced a new qualification criteria—a wage determination requirement centering on apprenticeship. This aspect of the legislation requires that 12.5% of total trade hours involved in a project be associated with the work of an apprentice. That percentage will rise to 15% by 2024.

FURTHER ACCOUNTING CONSIDERATIONS

The fine print further stipulates that, to qualify for the maximum benefit, a qualified engineering firm must certify the energy efficiency improvements associated with a project applying for the deduction.

WIN/WIN

With labor pressures continuing to act as a major stressor industry-wide, the apprenticeship criteria is a powerful incentive to do something you may have already considered—an apprenticeship program. It's not only good for the future of the workforce, with that \$5.36 per square foot deduction in mind; but also, it's hard to see how a business could lose on the arrangement. It's difficult to imagine a scenario where the costs of apprentice labor are not far eclipsed by the value of the deductions on offer.

ENSURING YOU QUALIFY

If it still hasn't sunk in, consider this: by meeting wage determination and energy improvement criteria, you could qualify for a quarter of a million dollars in deductions for a 40,000 square foot project. And there's no cap, so multiply that by the total number of projects you have with the potential for resulting in energy efficiency improvements.

Of course, as mentioned above, your firm does need to possess the expertise necessary to carry out energy efficiency projects that will pass muster with a third-party engineering firm. Hopefully that serves to encourage the workforce to broadly expand its skillset and quickly develop energy-related expertise. The Better Buildings Initiative is a great place to start if you're not familiar with energy-efficiency practices and want to get up to speed quickly. Lighting, renewable materials, and site conditioning are three key areas of focus and can lead to major efficiency improvements with relatively minor adjustments.

Once those skills are onboard, every project your firm undertakes can be assessed for its potential to improve energy efficiency. That knowledge can be put to use—saving your clients cash on their utility bills, helping your firm qualify for a valuable deduction, preparing the future of the labor workforce, and maybe even helping us get one step closer to solving the climate crisis.

Find Out More

Read a NASBP Blog from Marcum LLP on the Section 179D tax incentive: <https://bit.ly/3u50rkE>. Access a NASBP Virtual Seminar by McCarthy on a similar topic: <https://learn.nasbp.org/p/InflationReductionActConstructionContractors>. Access all NASBP Virtual Seminars here: <https://learn.nasbp.org/>.



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