



# Two Tax Incentives Every Contractor Should Know by Heart

BY **BRIAN AUMUELLER**, alliantgroup Managing Director

APRIL 1, 2015

For contractors looking for ways to add to their bottom line or hire additional employees, the answer may lie in two vastly overlooked tax incentives.

The Research and Development (R&D) tax credit and the Energy Efficient Commercial Building Deduction (better known as Section 179D) are two of the most valuable tax incentives available for the benefit of the wider construction industry. For electrical, mechanical and general contractors of all shapes and sizes, both the R&D credit and 179D deduction are a proven means to generate additional value through even the simplest everyday projects.

How valuable can these tax incentives be for your business? Depending on the number of qualifying projects and the nature of your work, the potential savings can be a real game changer for your company. Case in point, for improving the overall energy efficiency of several buildings, one **mechanical contractor received over \$4.7 million in 179D tax deductions**. While this is a high-end result for sure, it does show how powerful these tax incentives can be in adding the funds necessary to expand your workforce.

## The R&D Tax Credit: Don't Let the Name Fool You

A fixture of the tax code since 1981, the R&D tax credit certainly isn't new. Numerous guideline and regulatory changes however have greatly expanded the application of the credit. Currently, the credit and other related tax breaks save American businesses an estimated \$12 billion annually.

Taking into account those impressive stats, it probably comes as a shock to know that most businesses actually under-sell themselves when claiming R&D credits. Currently, only one out of every 20 eligible businesses is

taking advantage of the credit – and in my experience, contractors are among the groups most likely to overlook their qualifying projects.

So why are so many contractors failing to take advantage of the credit? Well, for starters, the term “research and development” often causes contractors to relate the credit only to scientific or medical research, when the reality behind the credit is much simpler.

### **How Contractors Qualify for R&D**

A company can become eligible for the R&D tax credit by improving a product, process or technique, a broad standard that can include a host of eligible contractor activities. Simply put, applied science counts toward eligibility, and the trial-and-error experimentation that occurs at a construction site or during the modeling process is as valid as any R&D taking place in a lab.

In the past, contractors have seen substantial returns for any number of activities, including those relating to means and methods, LEED initiatives, building information modeling, mechanical equipment sizing, HVAC, electrical system coordination, constructability and value engineering. Remember, as long as you are making improvements during your projects (think better, greener and more efficient), there is a good chance that activity qualifies for the R&D credit.

For example, **a general contractor received \$463,000 in federal and state credits** for projects relating to the installation of new mechanical systems, including the HVAC and the plumbing, of an old air force base. Eligible projects included finding the optimal process to remove the existing equipment in a small mechanical room and installing the same equipment in a limited space.

Finding practical solutions to everyday problems – those are the exact sort of projects the R&D credit is designed to reward.

### **Section 179D: Why Energy Savings Equal Tax Savings**

Originally passed by Congress as part of the 2005 Energy Policy Act, Section 179D of the tax code benefits architects, engineers – and yes, contractors (be they general, mechanical, electrical, etc.) – whenever they make energy efficient enhancements or renovations to buildings owned by the government. As government entities typically do not pay tax, Section 179D allows a government entity to allocate the tax savings to the designer or contractor making the enhancements to the building through a signed allocation letter. For any business performing eligible energy efficient improvements to buildings owned by government entities at the federal, state or local levels, that business can receive a tax deduction of up to \$1.80 per square foot, providing an obvious value depending on the size and scope of the project.

### **Which Buildings Qualify?**

The definition of a building under 179D is extremely broad and can include structures ranging from office buildings, factories, warehouses, parking garages, barracks, schools, universities, airports – basically any structure that is built for any level of government. With the deduction available for such a broad spectrum, it is important for contractors to keep an open mind when evaluating their projects for the deduction.

## What Systems Qualify and How “Green” Do the Buildings Need to Be?

So what building systems do you need to make energy efficient? And furthermore, what exactly is the bar for “energy efficiency” under 179D? It’s a good question with an answer that may surprise you.

Whenever people hear the term “energy efficiency,” they have the habit of thinking of wind farms and solar panels, but the requirements for 179D are much simpler. For energy efficient improvements made to the interior lighting, HVAC systems, hot water systems or for enhancements to the buildings envelope, a contractor can qualify or partially qualify for the deduction. Generally, the more systems you make energy efficient and the higher the square footage of the building, the higher your deduction will be. As far as green standards go, you only need to exceed 2001 ASHRAE standards – standards that most state codes already surpass.

Remember that mechanical contractor from earlier that received almost \$5 million in 179D deductions? This contractor qualified by making both mechanical and interior lighting improvements to a host of government-owned buildings, including elementary schools, college buildings, parking garages and even an exposition center.

If you feel any of the above activities or projects relate back to your business, then I would highly recommend you explore your options with respect to the R&D tax credit and 179D. Both tax incentives may very well be what you need to jump start your construction business.

*This article was originally published by Site-K Construction Zone, an online publication that carries all of the monthly feature stories and case studies from each of the Associated Construction Publications (ACP) magazines.*



**Brian Aumueller** is a Managing Director at alliantgroup with more than 20 years of experience providing consulting services to CPAs and their clients. Brian specializes in federal and state tax credits and incentives, managing CPA firm relationships and helping CPA firms identify qualified clients. Brian is a national practice leader with alliantgroup's software, architecture, engineering and contractor practices and has worked with hundreds of small to mid-sized businesses in the area of Research & Development tax credits. He was the former COO at a regional consulting firm and was responsible for the strategic direction of the firm and setting business strategy for its clients.