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Nonprofits Can Benefit from Energy-Efficient Tax Deduction

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Nonprofits can now benefit from tax deductions if they install energy-efficient equipment in new or renovated buildings that they own. Tax credits or deductions don't usually provide any benefit to nonprofits, since such tax-exempt organizations generally do not have any income tax liability. But changes in the [Inflation Reduction Act](#) (IRA) passed in 2022 extend a tax incentive that has been in the Internal Revenue Code since 2005 to nonprofits, giving organizations more negotiating power when building or renovating their structure.

What is the Section 179D Deduction?

Internal Revenue Code Section 179D (Code Section 179D) provides a tax incentive to those who build or renovate energy-efficient buildings. The tax deduction is triggered if building design improvements in heating, lighting, HVAC, hot water, or the building envelope (roof, walls, windows) result in efficiency of at least 25 percent. Starting in 2023, nonprofits can also benefit from Code Section 179D.

How Do Nonprofits Benefit?

Under Code Section 179D, commercial building owners claim a tax deduction for installing qualifying systems in their buildings. For nonprofits, the Code Section 179D deduction is passed through an “Allocation Letter” to a taxpaying entity (typically the architect or engineer) who then claims the tax deduction in exchange for adjusting the overall price or economics of the construction project.

Note that, under previous IRS rule regulations, government entities could benefit from the Code Section 179D program by passing that tax deduction to the architect and/or engineering firms designing their building. The Inflation Reduction Act extends this deduction to nonprofits and should work similarly to government entities, who cannot directly “keep the dollars” represented by the deduction, but can transfer the deduction to the designers of the property including architects, engineers, building contractors, energy service providers, or environmental consultants.

Nonprofits planning facility construction or structural improvements should consider whether incorporating sustainable elements can translate into economic savings. Energy-efficient facilities may also align with an organization's mission and values as well as provide ongoing savings in costs such as water, heat and electricity.

The qualified deduction for projects meeting prevailing wage and apprenticeship standards will range between \$2.50 and \$5 per square foot, depending on the building’s energy-efficiency level. For projects that do not meet prevailing wage and apprenticeship standards, the deduction level range will be between \$0.50 and \$1 per square foot.

The Code Section 179D incentive can now be taken on a specific commercial building every 3 years. Previously, the deduction was permitted once over the life of the building.