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Tax Break, or Kickback? Energy Benefit Becomes a Lightning Rod

By Patricia Cohen

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Over the past decade, hundreds of public projects have benefited from a federal incentive meant to encourage investments in energy-efficient technology. The Port Authority of New York and New Jersey used it to save $1 million on building One World Trade Center and upgrading bus terminals and airports. In Florida, Miami-Dade County sliced $1.13 million off the price tag of an improved cooling system in its county hall, courthouses and downtown sports arena.

But a growing chorus of public agencies complain that they were prevented from benefiting from this same incentive in their own building projects. Conflicting interpretations of the law and how it should be applied, they say, have caused taxpayer- funded schools, prisons, military bases and libraries throughout the nation to lose out on millions of dollars in savings.

The issue has heated up as state and local governments, and other public entities, move more aggressively to claim a piece of this federal subsidy. Lobbyists and lawyers have joined the scramble as Congress revisits this incentive and decides whether to extend it along with a raft of other tax breaks left out of last year's tax overhaul.

The Joint Committee on Taxation has estimated that this one energy deduction, over the past five years, was worth $1.1 billion. Yet even as public entities miss out on the savings, a juicy chunk of the money is going to consulting firms that handle the complex certification and filing requirements.

To Steven M. Rosenthal, a senior fellow at the nonpartisan Tax Policy Center in Washington and a former member of the joint tax committee's staff, these types of tax breaks are inefficient, and fall short of the target.

"It rarely gives the benefits to the parties you intended to give it to," he said, "and more often rewards parties that you never intended to reward."

When Congress first approved this incentive — known as 179D — as part of the Energy Policy Act in 2005, the aim was to encourage energy efficiency in commercial property. One carrot was a tax deduction that enabled property owners to reduce the cost of green buildings.

A tax deduction, however, is of no use if you don't pay any income taxes — and government entities don't. So to include public projects, Congress added a provision allowing buildings on government-owned property to transfer the deduction — worth

$1.80 a square foot — to a private company that created the building's energy-saving system.

The law did not specify whether a public project or agency should get anything in exchange for the transfer. But taxpayer advocates argue that enabling a public entity to negotiate with a private contractor for a reduced fee or a rebate in return for signing away the 179D deduction was clearly the point.

"The whole purpose of the tax deduction was to incentivize owners, and our situation as a governmental entity is no different from Apple or any other corporate entity," Philip Aldridge, vice chancellor for business development at the University of Texas, said. The University of Texas System and the University of Houston System have filed a lawsuit arguing that they were misled into transferring incentives worth millions of dollars without compensation.

"We own the building, we financed 100 percent of the building, and we, as the owner, determined whether the building was going to be energy efficient or not," Mr. Aldridge said.

Jonathan Duchac, an associate professor of accounting at Wake Forest University, goes a step further. In a paper on the subject in The ATA Journal of Legal Tax Research, he and his co-authors argue that simply giving away the deductions violates most state constitutions, which have anti-gift provisions.

"Government can't give away things of value without being compensated," Mr. Duchac said.

There are fierce dissenters, especially among construction industry trade groups and the consulting firms that advise them. The American Council of Engineering Companies petitioned the Senate Finance Committee last summer arguing that the practice of public officials asking for compensation in exchange for a 179D transfer "raises a number of serious legal and ethical questions."

A few lawmakers have also warned federal officials that asking for fees in return for allocating the deduction might amount to a "kickback."

But more and more state agencies, public entities and others are pushing back against that interpretation.

In June, the California State University System changed its policy, requiring officials to negotiate reimbursement in exchange for allocating the energy deduction. In October, a Des Moines Register investigation into the tax break lamented that Iowa governments frequently "gained little or nothing for authorizing the deduction on taxpayer-funded construction." And in December, North Carolina overturned a rule that had prohibited state officials from similarly asking for compensation.

The question of who deserves to benefit from the 179D tax deduction is particularly complicated because both contractors and governments are often unaware of it until after the project's completion.

That's where the consultants come in.

"Not many know about this," said Barry Fischman, a partner at the accounting firm Marcum. Most of the time, he said, the deduction is sought when "the job is already done, finished and closed."

No matter that the tax break did not work as intended — since it did not act as an incentive to invest in energy efficiencies that wouldn't have been done anyway. It can still be claimed.

Tax consultants, pointing out that recent tax returns can be amended, urge private contractors to take advantage of a windfall and request 179D transfers related to previous public projects.

Public agencies, however, complain of simultaneously being told that they have no right to engage in a parallel look back and ask for a share of that money in return for the transfer.

That argument is what spurred the University of Texas and University of Houston Systems to file a lawsuit asserting that Alliantgroup, a politically connected tax-credit consulting firm, engaged in a "nationwide scheme" to obtain 179D tax deductions from "thousands of governmental entities without any compensation."

In the lawsuit, they accuse the firm of presenting false information that the university was required to allocate $12.25 million worth of deductions to its contractors without receiving any compensation. The firm, the suit said, also pressured unauthorized employees to sign the transfers.

In a statement, Alliantgroup said: "We are disappointed that the University of Texas System and University of Houston System have been led into a frivolous lawsuit against Alliantgroup and our client."

The firm also noted that members of Congress and other government agencies had said 179D "was not intended to provide kickbacks to government entities who do not pay taxes in exchange for a tax-deduction allocation letter."

Alliantgroup boasts an impressive roster of advisory experts to back up its interpretation, like Mark W. Everson, a former commissioner of the Internal Revenue Service, and Dean Zerbe, who worked on the Senate Finance Committee. Former I.R.S. managers, state governors, representatives and administration officials also sit on its strategic advisory board, including Tom Ridge, a former governor of Pennsylvania and secretary of homeland security, and Rick A. Lazio, a former New York congressman. In March, Mr. Lazio testified at a congressional hearing that the 179D deduction should be expanded to nonprofits and Indian tribes and made permanent.

Senator Benjamin L. Cardin, Democrat of Maryland, raised the issue of kickbacks, too, in 2016 when the federal Department of Housing and Urban Development asked for compensation in exchange for transferring its energy deductions from a completed project.

A spokeswoman for Mr. Cardin said the senator's objection referred solely to public agencies demanding a fee for administering the confirmation letter, and not to "using 179D writ large as a way to negotiate a project's cost."

Other schools have also taken issue with applications overseen by Alliantgroup. The University of Connecticut discovered that the firm had solicited a 179D transfer from unauthorized employees on behalf of different clients for the same project.

"I was dismayed," said Scott A. Jordan, the University of Connecticut's chief financial officer. "There seemed to be a bounty sort of system where companies like Alliant were coming in and pressing owners

to sign off on behalf of clients." The incident, he said, prompted the university to devise a formal policy on how to handle the incentive.

At the same time, concerns that private businesses may be improperly filing claims on work done in public buildings helped prompt the large-business division of the I.R.S. to add the 179D deduction to its watch list.

As for the broader issue of who should benefit, Mr. Jordan pointed out that the university's board already required buildings to be energy efficient. "If we have already established policy, we don't need an incentive to do that," he said.

But if the federal government is going to subsidize energy efficiency, he added, then "the owners should be the recipients of the subsidy and not the builder."