

# MARKS PANETH

ACCOUNTANTS & ADVISORS

## MARKS PANETH REAL ESTATE ADVISOR OCTOBER 2014: STRATEGIES AND SOLUTIONS FOR CONTINUING TO GROW YOUR REAL ESTATE BUSINESS

### GREEN LEASE IS FINALLY DEFINED AND THE GREEN LEASE LEADER CERTIFICATION PROGRAM IS LAUNCHED

Today, many tenants are “thinking green.” Compliance with sustainability standards can affect occupancy rates and, in turn, a property’s financial leverage capacity. The U.S. Department of Energy’s Better Buildings Alliance and the Institute for Market Transformation have just launched the “Green Lease Leader” certification program to recognize commercial landlords and brokerage teams that have successfully implemented environmentally friendly leases.

The Green Lease Leader designation can help the commercial real estate industry respond to market pressures to improve sustainability by providing a reliable method for landlords to signal their willingness to participate in such initiatives.

#### **The Green Lease Standards**

Green Leasing has been a topic of discussion, and even execution, for some years now. Yet, a “Green Lease” remained to be clearly defined until now. As a result, landlords have struggled with the language to include in their leases to attract sustainability-minded tenants.

The Green Lease Leader program fills the gaps by setting a new standard with a uniform definition for “Green Lease.” To satisfy the qualifications of a Green Lease, a lease must include provisions intended to save energy. A Green Lease must have at least three of the following:

- A provision requiring tenant disclosure of utility data to facilitate whole-building energy benchmarking,
- Minimum standards and/or tenant improvement specifications for energy efficiency (for example, “Tenant will install only ENERGY STAR appliances”),
- Sustainable operations and maintenance rules and regulations covering restricted HVAC weekend operating hours, the provision of janitorial services during daytime hours, and the prohibition of tenant space heaters,

- Submetering of tenant spaces or separate metering of tenant plug load and equipment, including data centers (ideally, tenants will be billed according to actual use, not on a pro rata basis), and
- A landlord agreement to incorporate energy management best practices in building operations, such as regular benchmarking, energy audits or commissioning of building systems.

A commercial landlord must have a Green-Leased portfolio that exceeds 50,000 gross square feet to qualify for the designation.

### **The application process**

The 2015 application cycle is scheduled to open this fall. Applicants must pay a \$250 fee and submit at least two signed and executed Green Leases. (Submitted leases may be redacted to protect sensitive or proprietary information.)

The application also requires a narrative description of the landlord's internal Green Leasing initiative. The narrative portion will be scored based on the Green Leasing-related accomplishments. For example, developing a model Green Lease as an internal resource will earn 4 points, while holding meetings with decision-making executives to discuss incorporating green clauses into leases will earn 2 points. Developing and distributing a "Green Tenant Guide" scores 3 points.

A property must earn 15 points to be certified as a Green Lease Leader. 10 will come from the leases, with each approved lease worth 5 points. A minimum of 5 points is required from the narrative portion.

### **Going green to get green**

Now that the benchmark has been established, property owners should consider steps they can take to achieve Green Lease Leader status. Adopting the changes required to get the Green Lease Leader designation could reduce costs, lure environmentally-conscious tenants and improve tenant satisfaction.

### **BUYER BEWARE: ACQUIRING THE STOCK OF C CORPORATIONS CAN BE HAZARDOUS**

There are many ways to buy real estate. Some buyers acquire properties outright, while others choose a less-advantageous acquisition method by acquiring stock in a C corporation that holds property as its primary asset. If you select the latter route, understand that you could encounter some tax pitfalls and legal complications.

## **Look beyond price**

To minimize their tax burden, owners of a C corporation that holds real estate would prefer to sell the corporation's stock rather than incur the double taxation that would be imposed if the real estate were sold and the proceeds were distributed to the stockholders. To facilitate a quick transaction, the owners might, therefore, offer a reduced price if a buyer is willing to assume their corporate structure.

Potential purchasers, however, need to look beyond the price and should consider certain tax issues that could arise.

For example, one of the primary disadvantages of a C corporation is the double taxation associated with corporate structures. That is, the corporation's profits are first taxed at the corporate level. Then, if the corporation pays out some of its profits as dividends, the dividend recipients are also taxed. On the flip side, ongoing tax losses — common with real estate activities — can't be used to offset a shareholder's other income because the losses are inside the corporation.

Moreover, it usually isn't advantageous to convert a C corporation to S corporation status because of the taxes owners would face on built-in gains. Converting to a limited liability company could also have substantial negative tax consequences because it would likely be treated as a liquidation of the corporate entity — which would result in multiple levels of tax.

## **No Step-ups in Tax Basis**

When you buy a C corporation, the tax basis in its real estate holdings isn't stepped up to reflect the purchase price, as it would be in a direct purchase. While the purchaser would hold a tax basis in the stock equal to the purchase price, the depreciable assets inside the corporation would continue to be depreciated using the corporation's tax basis which is likely lower than the purchase price paid for the assets.

## **Legal exposure**

Beyond tax issues, when acquiring C corporation stock, potential legal issues should be carefully vetted as they can survive the acquisition of the company by a new owner. Such exposure can include other things, slip-and-fall claims, tax delinquencies, including tax withholding payment arrears, environmental issues, employment claims, etc. These liabilities stay with the corporation — they don't go away with the sellers. It's imperative that due diligence- legal, financial, environmental and tax be performed very thoroughly and thoughtfully when considering acquisition of a property by purchasing the stock of a C corporation.

The experienced professionals in our firm's [Real Estate Group](#) can assist in the due diligence process and guide you in making an informed decision about whether or not to acquire stock in a C corporation.

## **ASK THE ADVISOR: CAN I CLAIM THE HOME OFFICE DEDUCTION?**

Many individual taxpayers involved in real estate investment or development maintain a home office. But, even though the IRS recently made it easier to claim the home office deduction, you may still not qualify for it.

### **New safe harbor**

The IRS now offers a safe harbor for claiming a tax deduction if you use a portion of your home for business. Previously, the only way to claim the deduction was to track all actual costs related to your use of the home space and complete Form 8829. This new, simplified option should reduce your paperwork and record-keeping burden.

The safe harbor allows you to claim a standard deduction of \$5 per square foot for up to 300 square feet — a cap of \$1,500 per year. Although you can't depreciate the portion of your home that's used as an office — as you can under the regular Form 8829 method — you *can* claim allowable mortgage interest, real estate taxes and casualty losses in full as itemized deductions on Schedule A, without needing to apportion them.

### **Two eligibility requirements**

Regardless of which method you elect for a given tax year, you need to satisfy two requirements to qualify for the deduction:

- 1. Regular and exclusive use.** You must use part of your home exclusively for conducting business. If you use an extra room both for your work as a developer and to lodge guests overnight, you can't take the deduction.
- 2. Principal place of your business.** You must show that you use your home as your principal business or, if you also conduct business at a location outside of the home, that you use the home space as a place to meet in person with clients or customers in the normal course of your business. This can be the stumbling block for those in the real estate industry who often have an office outside of the home.

You can also claim the deduction for a separate freestanding structure, such as a garage, if you

use it exclusively and regularly for your business — even if it's not your principal place of business or the only place you meet clients.

### **Choosing the best course**

Both the new safe harbor and regular method are subject to additional restrictions and rules, and they come with the potential for unexpected tax effects down the road. Consult with your tax advisor to chart the best course for you.

## **SPOTLIGHT ON MARKS PANETH**

### **NYC Real Estate Expo**

Marks Paneth will be a sponsor of the 6th Annual NYC Real Estate Expo, which will be held at the Hilton Hotel on November 6. We will also be launching the next *Gotham Commercial Real Estate Monitor* survey at the expo. Please be sure to stop by our booth and take the survey.

James Robbins, Tax Principal, will be participating in a panel on “EB-5 Lending to Foreign Buyers: It Can Be Done” at 3:45 p.m. to 5:30 p.m. at Gramercy East /West Room. Please [click here](#) for more information.

### **Is NY's Tech Sector Expected to Spark a Commercial Real Estate Boom?**

The results of our latest *Gotham Commercial Real Estate Monitor* survey, which tracks the concerns, opinions, outlook and forecasts of New York's commercial real estate executives and decisions makers are in. Please [click here](#) to read more.

### **Marks Paneth Named a Top 3 Forensic Accounting Firm for the 5th Straight Year**

Readers of the New York Law Journal (NYLJ) have again ranked Marks Paneth as one of the [top three forensic accounting providers](#) serving the New York legal community in the publication's annual Reader Rankings Survey. This is the fifth year in a row that we have received this honor and the second year that we have been ranked #2.

More than 8,000 votes were cast. Marks Paneth is the only major regional firm to be selected as one of the top three firms in the category of forensic accounting for all five years of the survey – 2010, 2011, 2012, 2013 and 2014. For more information about our firm's forensic accounting

services, please contact [Steven Henning](#), Partner-In-Charge, Litigation and Corporate Financial Advisory Services, a 212.201.3179 or [shenning@markspaneth.com](mailto:shenning@markspaneth.com).



## **New York State and City Residency Rules Create Tax Traps for the Unwary**

Is your client a resident of New York State for tax purposes? Under NYS Tax Law Section 605(b), a resident is defined as someone who maintains a “permanent place of abode” and spends more than 183 days of the tax year in New York. But a recent case has redefined “permanent place of abode” for the purposes of determining statutory residency – and taxpayers and their counsel need to be careful: City and state residency rules remain complex and continue to lay many tax traps for the unwary. [Click here](#) to read a recent article by [Steven P. Bryde](#), Tax Principal that was originally published in *The Metropolitan Corporate Counsel*, September 2014.

## **FOR FURTHER INFORMATION**

If you have any questions, please contact [William Jennings](#), Partner-in-Charge of the [Real Estate Group](#), at 212.503.8958 or [wjennings@markspaneth.com](mailto:wjennings@markspaneth.com) or any of the other partners in the [Marks Paneth Real Estate Group](#):

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Additional information about the Marks Paneth Real Estate Group can be found at [www.markspaneth.com](http://www.markspaneth.com).

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