

ENERGY EFFICIENCY PAYS

BY JERROLD J. STERN



If energy bills and the IRS are taking too big a bite out of your income, take note. Homeowners can receive tax credits for certain energy efficiency property and improvement expenditures.

Careful planning is necessary because one tax credit, the nonbusiness energy property credit, expires at the end of 2007, and the other, the residential energy-efficient property credit, expires at the end of 2008. In general, tax credits are a dollar-for-dollar reduction of tax liability.

Nonbusiness Energy Property Credit

The nonbusiness energy property credit falls into two categories: credit for certain residential energy property expenditures paid during the year, and credit for 10 percent of the cost of certain energy-efficient improvements installed during the year.

Total accumulated credit limits for 2006 and 2007 are as follows:

- An overall limit of \$500 for the total of 2006 and 2007 expenditures (that is, the after-tax cost of these expenditures can be reduced by up to \$500),
- An accumulated credit limit of \$200 for certain windows, and
- An accumulated credit limit of:
 - \$50 for any advanced main air circulating fan used in natural gas, propane or oil furnaces;
 - \$150 for any qualified natural gas, propane or oil furnace or hot water boiler; and
 - \$300 for certain energy-efficient building property, such as heat pumps, central air conditioners and water heaters.

To qualify for the credit, the improvements and property must meet specific IRS standards and requirements. Energy property must be new, not used.

To illustrate, say Lauren purchases a heat pump for \$2,000 in 2006 and spends \$1,500 for a hot water boiler in 2007. For 2006, her credit is \$300 (the limit for certain energy-efficient building property). For 2007, her credit is \$150 (the limit for boilers).

If she also spends \$1,000 for qualifying windows in 2007, only \$50 of that amount would apply toward a credit because she will have reached the overall \$500 credit limit (\$300 from 2006 plus \$150 plus \$50). Her total credit for 2007 would be \$200 (\$150 plus \$50).

If the \$500 overall limit is not exceeded, a tax credit for 10 percent of the cost of qualified energy-efficiency improvements may be available. These items must be new and reasonably expected to remain in use for at least five years. The following items may qualify if they meet IRS specifications:

- Insulation material or an insulation system primarily designed to reduce the heat loss or gain of a home,
- Exterior windows (including skylights),
- Exterior doors, and
- Any metal roof installed on a home, but only if this roof has appropriate pigmented coatings that are specifically designed to reduce the heat gain of the home.

For example, if a homeowner purchases an exterior door for \$1,200 and windows for \$3,000, the total credit would be \$320 (10 percent of 1,200 [\$120] plus the \$200 limit on windows).

Residential Energy-Efficient Property Credit

Homeowners may also be able to take advantage of the residential energy-efficient property credit pertaining to solar and fuel cell property. This credit expires in 2008 rather than 2007 and can lead to much higher tax savings. However, the overall cost and the likelihood of needing professionals to do the work rather than taking a "do-it-yourself" approach is also greater.

The credit is 30 percent of the homeowner's costs for qualified photovoltaic property, solar water heating property, and fuel cell property. Fuel cells use a chemical reaction to transform hydrogen and oxygen into electrical power, water and heat in an environmentally friendly manner.



TANKLESS water heaters, heat pumps and central air conditioners may be eligible for a \$300 tax credit.

The credit is limited as follows:

- \$2,000 for qualified photovoltaic property costs (for example, solar panels),
- \$2,000 for qualified solar water heating property costs, and
- \$500 for each half kilowatt of capacity of qualified fuel cell property for which qualified fuel cell property costs are paid.

Taxpayers contemplating energy-related purchases should consider accelerating those transactions to take advantage of these energy credits. Consultation with a tax accountant or tax attorney is recommended. ♣

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THE TAKEAWAY

Homeowners can receive tax credits for certain energy efficiency property and improvement expenditures. The nonbusiness energy property credit expires at the end of 2007; the residential energy-efficient property credit expires at the end of 2008.