

NEWSLETTER

Nonbusiness Energy Property Credit

This letter explains the requirements and computation of the new credit for nonbusiness energy property added by the Energy Tax Incentives Act of 2005.

The nonbusiness energy property credit is a credit for improvements that increase the energy efficiency of existing homes. The maximum amount of credit that you may be able to claim is the amount you paid for energy-efficient home heating, water heating, and air conditioning systems, plus 10% of the amount you paid for energy-efficient windows, doors, roofs, and insulation. Expenditures that you made from subsidized energy financing are not eligible for the credit.

The credit is available for 10% of "qualified energy efficiency improvements." These include insulation materials, exterior windows (including skylights) and doors, and certain metal roofs, which meet the following requirements: (1) they meet or exceed the 2000 International Energy Conservation Code criteria (or, in the case of metal roofs, the Energy Star program requirements); (2) they are installed, in 2006 or 2007, in or on a dwelling in the United States that you own and use as your principal residence; (3) their original use begins with you; and (4) they reasonably can be expected to remain in use for at least five years.

Subject to dollar-amount limits, 100% of "residential energy property expenditures" also qualify for the credit. These include expenditures for energy-efficient building property, qualified natural gas, propane, or oil furnaces or hot water boilers, and advanced main air circulating fans, which are installed in 2006 or 2007 on or in connection with a dwelling unit in the United States that you own and use as your principal residence, which meet any regulatory standards and/or certification requirements in effect at the time of the completion of the construction/reconstruction/erection of the property, and of which you are the original user. Expenditures for onsite preparation, assembly, and original installation of qualified energy property are considered residential energy property expenditures and, therefore, are eligible for the credit.

"Energy-efficient building property" includes: (1) an electric heat pump water heater that yields an energy factor of at least 2.0 in the standard Department of Energy test procedure, (2) an electric heat pump that has a heating seasonal performance factor (HSPF) of at least 9, a seasonal energy efficiency ratio (SEER) of at least 15, and an energy efficiency ratio (EER) of at least 13, (3) a geothermal heat pump that (i) in the case of a closed loop product, has an energy efficiency ratio (EER) of at least 14.1 and



a heating coefficient of performance (COP) of at least 3.3, (ii) in the case of an open loop product, has an energy efficiency ratio (EER) of at least 16.2 and a heating coefficient of performance (COP) of at least 3.6, and (iii) in the case of a direct expansion (DX) product, has an energy efficiency ratio (EER) of at least 15 and a heating coefficient of performance (COP) of at least 3.5, (4) a central air conditioner that achieves the highest efficiency tier established by the Consortium for Energy Efficiency, as in effect on January 1, 2006, and (5) a natural gas, propane, or oil water heater that has an energy factor of at least 0.80. The amount of credit allowed for each item of energy-efficient building property is \$300.

A qualified natural gas, propane, or oil furnace or hot water boiler achieves an annual fuel utilization efficiency rate of at least 95. The amount of credit allowed for each qualified natural gas, propane, or oil furnace or hot water boiler is \$150.

An advanced main air circulating fan is a fan used in a natural gas, propane, or oil furnace, the annual electricity use of which is 2% or less of the furnace's total annual energy use. The amount of credit allowed for each main air circulating fan is \$50.

There is a lifetime limit on the amount of nonbusiness energy property credit that you can claim. The maximum amount of credit that you may claim with respect to the same dwelling *for all taxable years* is \$500 (no more than \$200 of which can be for windows).

There are two additional limits on the amount of the credit. First, if more than 20% of a credit-eligible property is used for business purposes, then you may claim the credit only for expenditures for the portion of the property that is used for *nonbusiness* purposes. Second, the credit is nonrefundable, which means that the amount of the credit cannot exceed your tax liability for that year.

An expenditure that otherwise qualifies for the nonbusiness energy credit is not disqualified because it was made for more than one dwelling unit. In that case, the credit is computed separately with respect to the amount of the expenditure made for each dwelling unit.

If two or more persons used a dwelling unit as their residence during the year and made expenditures that qualify for the credit, then each resident is entitled to a proportionate share of the credit amount for each energy item based on his/her share of the expenditures for that energy item. If you live in a condominium or cooperative, you are eligible for a credit for your proportionate share of the cooperative corporation's or condominium association's qualifying expenditures.

The increase in your basis that would otherwise result from qualifying expenditures is reduced by the amount of credits allowed for such expenditures.

The nonbusiness energy property credit will not be available after 2007.

I hope this information is beneficial to you. Please call our offices if you have any further questions.