

Tax Trends

The power of energy saving products

A number of new tax incentive programs provide powerful reasons to purchase energy saving products.

The Energy Policy Act of 2005 included new personal federal income tax credits designed to generate new investment in energy-efficient products for personal residences.

IRC Section 25C provides a maximum lifetime credit of \$500 for certain energy saving improvements to principal residences in 2006 and 2007. The credit for the improvements eligible under Section 25C credit is calculated as the sum of:

10% of the expenditures for qualified energy efficiency improvements

+

100% of expenditures for qualified residential energy property

Energy efficiency improvements eligible for the 10% calculation include purchases for the following building envelope components:

- Insulation materials designed to reduce heat loss or gain.
- Energy efficient exterior windows, including skylights and storm windows.
- Energy efficient exterior doors, including storm doors.
- Metal roofs designed to reduce heat gain and meet Energy Star program requirements.

The 10% Section 25C credit is limited to amounts paid for the components and not for contractor installation. Furthermore, the credit for windows is limited to no more than \$200 for 2006 and 2007 combined.

Three additional requirements must be met in order to claim the 10% Section 25C credit. First, the component must be installed in or on a dwelling unit located in the U.S. and the dwelling must be the taxpayer's principal residence at the time of installation. Secondly, the use of the component must begin with the taxpayer; the credit doesn't apply to used or reused materials. Finally, the component must be reasonably expected to remain in use for at least five years or come with a manufacturer's warranty, at no extra charge, of at least two years.



Residential energy property eligible for the 100% Section 25C credit includes the following:

- Qualified electric heat pumps, electric heat pump water heaters, geothermal heat pumps, and central air conditioners. The credit cannot exceed \$300 per qualifying piece of equipment.
- Qualified natural gas, propane, and oil furnaces, hot water heaters, and hot water boilers. The credit cannot exceed \$150 per qualifying piece of equipment.
- Advanced main air circulating fans used in a natural gas, propane or oil furnace. The credit cannot exceed \$50 per qualifying fan.

Unlike the 10% Section 25C credit for building envelope components, the 100% Section 25C credit for residential energy property does allow for both the cost to purchase the products and for labor costs related to onsite preparation, assembly and installation.

Two additional requirements must be met to claim the 100% Section 25C credit for qualified residential energy property. First, the component must be installed in or on a residence located in the U.S. and the dwelling must be the taxpayer's principal residence at the time of installation. Secondly, the product must be new and first placed in service by the taxpayer.

To determine if a product is eligible for either the 10% or the 100% Section 25C credit, consumers may rely on the manufacturer's

certification. However, the taxpayer should be sure to obtain a certification statement for tax recordkeeping purposes. Manufacturers may include the statement with the product's packaging, or it may be available in printable form on the manufacturer's website. Each certification statement must contain the following information:

- Manufacturer's name and address.
- Description of the product along with the make, model number, and any other appropriate identifiers.
- Statement that the product qualifies for the Section 25C credit.
- A declaration, signed by an authorized person for the manufacturer, stating: "Under penalties of perjury, I declare that I have examined this certification statement, and to the best of my knowledge and belief, the facts are true, correct, and complete."

Under the Tax Increase Prevention and Reconciliation Act, dated May 23, 2006, the Section 25C credit is available against the Alternative Minimum Tax (AMT) for 2006. However, unless Congress extends it, the credit won't be available for 2007. Taxpayers likely to be subject to AMT in 2007 should consider making purchases this year.

The State of Connecticut provides further incentives for home energy improvement by offering sales tax exemptions on qualified purchases. For more information, read on.

Connecticut Sales Tax Exemption Seals the Benefits of Home Weatherization

Connecticut added one more incentive designed to fuel enthusiasm for home weatherization improvements. In May of 2006, Governor M. Jodi Rell signed a bill establishing an exemption from Connecticut sales tax on the sale of home weatherization products between June 1, 2006 and June 30, 2007. Rising energy costs combined with the potential 6% savings on specific products is certain to generate additional interest.

Connecticut's sales and use tax exemption during the period covers a broad range of weatherization products, including:

- Programmable thermostats;
- Window film;
- Caulking;
- Window and door weather strips;
- Insulation;
- Water heater blankets;
- Water heaters;
- Boilers that meet the federal Energy Star standard. (Energy Star qualified boilers have an annual fuel utilization efficiency (AFUE) rating of 85% or greater.);

- Natural gas furnaces that meet the federal Energy Star standard;
- Propane furnaces that meet the federal Energy Star standard;
- Windows that meet the federal Energy Star standard;
- Doors that meet the federal Energy Star standard;
- Oil furnaces that are not less than 85% efficient based on the AFUE rating; and
- Ground-based heat pumps that meet the minimum federal energy efficiency rating.

The exemption is limited to products designed and marketed for residential use and not for commercial use. In addition, the exclusion covers only the weatherization products, but does not exempt any taxable contractor labor, so itemized receipts are important.

In order to qualify for the exemption, the sale must occur during the exclusion period. Products ordered and paid for in full prior to June 1, 2006 are not covered. However, deposits placed before June 1, 2006 on qualified products are tax free if delivered during the exclusion period.



Tax Credits: A driving force behind hybrid vehicles

The Energy Policy Act of 2005 also provides a credit for taxpayers who purchase certain energy efficient and alternative fuel vehicles. The credit, ranging from \$250 - \$4,000, is available for qualifying vehicles purchased by individuals and businesses. A majority of the vehicles currently are hybrid models; however, the Honda Civic GX, which operates on compressed natural gas, was just certified for a \$4,000 credit.

It is up to manufacturers to certify to the Internal Revenue Service (IRS) that vehicles qualify for the credit. As of July 11, 2006, the IRS recognizes qualified hybrid vehicles manufactured by Ford, Mercury, Toyota, Lexus, Honda, Saturn, General Motors and Chevrolet.

In addition to purchasing a certified vehicle, taxpayers must meet the following requirements to qualify for the credit:

- The vehicle must be in service after 12/31/05 and purchased on or before 12/31/10.
- The credit may only be claimed by the original owner of a new vehicle. It does not apply to a used vehicle.
- The taxpayer claiming the credit must be the one who acquired the vehicle.
- If a qualifying vehicle is leased to a consumer, the leasing company may claim the credit.
- Sale of a qualifying vehicle for use by a tax-exempt entity permits the seller to claim the credit provided the seller clearly discloses the credit to the tax-exempt entity.
- The vehicle must be used predominantly within the United States.

One important caveat under this program is the manufacturer phase out provision. The motor vehicle credit begins to phase out in the second calendar quarter after at least 60,000 of the manufacturer's qualifying passenger automobiles and light trucks have been sold. Currently, this provision affects only Toyota/Lexus vehicles. After September 30, 2006, the credit on Toyota/Lexus vehicles will be reduced by 50% every six months and will expire completely after September 30, 2007.

The State of Connecticut sales and use tax exemptions on qualified vehicles is one more reason to consider the new line of energy efficient vehicles. See the inset for more information.



New Connecticut Energy Efficiency Fund Offers Savings for Businesses and Homeowners

Both businesses and homeowners can benefit from a new initiative, the Connecticut Energy Efficiency Fund. For businesses, the Fund offers innovative programs to maximize energy efficiency, lower operating costs and improve productivity. For residents, it offers incentives to replace energy inefficient appliances, rebates on energy-saving lighting products and more. Call 1-877-WISEUSE or visit www.ctsavesenergy.org/programs for detailed information.

Connecticut's Tax Exemptions Highlight the Hybrids

The State of Connecticut offers a tax exemption for hybrid vehicles purchased or leased on and after October 1, 2004 and prior to October 1, 2008. The tax exemption applies to the purchase or lease of a new or used qualifying motor vehicle from a motor vehicle dealer as well as the purchase of a used qualifying motor vehicle directly from its owner.

Connecticut's exemption is based upon mileage rating. It is applicable to any passenger car utilizing hybrid technology that has a United States Environmental Protection Agency estimated highway gasoline mileage rating of at least 40 miles per gallon. Currently, the Honda Civic Hybrid, Honda Insight and Toyota Prius meet the eligibility requirements for the sales and use tax exemption.

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For information, contact David Putt, Director, Blum Shapiro Consulting, at (860) 561-6836.

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