

IRS Fact Sheet

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Highlights of the Energy Policy Act of 2005 for Individuals

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During 2006, individuals can make energy-conscious purchases that will provide tax benefits when filling out their tax returns next year. The new law provides tax credits for making your principal residence, which must be in the United States, more energy efficient and for buying certain energy efficient items. At the same time the law provides credits for various types of alternative motor vehicles, including hybrids.

Credits for Individuals Who Make Their Homes More Energy Efficient

A recent tax law change provides a tax credit to improve the energy efficiency of existing homes. The law provides a 10 percent credit for buying qualified energy efficiency improvements. To qualify, a component must meet or exceed the criteria established by the 2000 International Energy Conservation Code (including supplements) and must be installed in the taxpayer's main home in the United States.

The following items are eligible:

- Insulation systems that reduce heat loss/gain
- Exterior windows (including skylights)
- Exterior doors
- Metal roofs (meeting applicable Energy Star requirements).

In addition, the law provides a credit for costs relating to residential energy property expenses. To qualify as residential energy property, the property must meet certification requirements prescribed by the Secretary of the Treasury and must be installed in the taxpayer's main home in the United States.

The following items are eligible:

- \$50 for each advanced main air circulating fan
- \$150 for each qualified natural gas, propane, or oil furnace or hot water heater
- \$300 for each item of qualified energy efficient property.

The maximum credit for all taxable years is \$500 – no more than \$200 of the credit can be attributable to expenses for windows.

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Additionally, the new law makes a credit available to those who add qualified solar panels, solar water heating equipment, or a fuel cell power plant to their homes in the United States. In general, a qualified fuel cell power plant converts a fuel into electricity using electrochemical means, has an electricity –only generation efficiency of more than 30 percent and generates at least 0.5 kilowatts of electricity. Taxpayers are allowed one credit equal to 30 percent of the qualified investment in a solar panel up to a maximum credit of \$2,000, and another equivalent credit for investing in a solar water heating system. No part of either system can be used to heat a pool or hot tub.

Additionally, taxpayers are also allowed a 30 percent tax credit for the purchase of qualified fuel cell power plants. The credit may not exceed \$500 for each .5 kilowatt of capacity.

These items must be placed in service after Dec. 31, 2005 and before Jan. 1, 2008.

Credit for Taxpayers Who Purchase or Lease Hybrid Vehicles or Other Alternative Motor Vehicles

The tax credit for hybrid vehicles, which was enacted by the Energy Policy Act of 2005, may be as much as \$3,400 for those who purchase the most fuel-efficient passenger vehicles and light trucks.

Hybrid vehicles have drive trains powered by both an internal combustion engine and a rechargeable battery. Many currently available hybrid vehicles may qualify for the tax credit.

Since taxpayers may claim the full amount of the allowable credit only up to the end of the first calendar quarter after the quarter in which the manufacturer records its sale of the 60,000th hybrid and/or advanced lean-burn technology motor vehicle, consumers seeking the credit may want to buy early in the year.

The phaseout period for a manufacturer begins with the second calendar quarter after the calendar quarter in which the manufacturer records its 60,000th sale. For the second and third calendar quarters after the quarter in which the 60,000th vehicle is sold, taxpayers may claim 50 percent of the credit. For the fourth and fifth calendar quarters, taxpayers may claim 25 percent of the credit. For quarters after that fifth calendar quarter, taxpayers may not claim the credit.

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For example, F Company is a manufacturer of hybrid motor vehicles, but not advanced lean burn technology motor vehicles. F Company sells its 60,000th hybrid car on March 31, 2006.

- Ms. Smith buys an F Company hybrid car on June 30, 2006, and claims the full credit.
- Ms. Maple buys an F Company hybrid car on Dec. 31, 2006, and claims 50 percent of the credit.
- Mr. Grey buys an F Company hybrid car on June 30, 2007, and claims 25 percent of the credit.
- Mr. Green buys an F Company hybrid car on July 1, 2007, and is unable to claim the credit, because the credit has phased out for F Company vehicles.

Tax credits are available for purchasing certain other vehicles.

Fuel cell vehicles are propelled by power derived from one or more cells which convert chemical energy directly into electricity by combining oxygen with hydrogen fuel. For passenger automobiles or light trucks, the maximum allowable credit is \$12,000 but greater credits are available for heavier vehicles.

Alternative fuel vehicles include those fueled by compressed natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, and any liquid that is at least 85 percent methanol. The maximum allowable credit for vehicles weighing 8,500 pounds or less is \$4,000.

Hybrid heavy trucks: For qualifying hybrid motor vehicles weighing more than 8,500 pounds but not more than 14,000 pounds, the maximum allowable credit is \$3,000. For qualifying hybrid motor vehicles weighing more than 14,000 pounds but not more than 26,000 pounds, the maximum allowable credit is \$6,000. For qualifying hybrid motor vehicles weighing more than 26,000, the maximum allowable credit is \$12,000.