

**DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
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The Honorable Jeanne Shaheen  
United States Senator  
1589 Elm Street, Suite 3  
Manchester, NH 03101

Attention:

Dear Senator Shaheen:

I am responding to your inquiry of February 22, 2010, on behalf of your constituent, . asked about the federal tax treatment of state incentives for individuals who install alternative energy systems at their residences.

A customer who purchases or installs any energy conservation measure does not include in his or her gross income the value of any subsidy that a public utility provides (directly or indirectly) (section 136 of the Internal Revenue Code (the Code)). To the extent the taxpayer excludes the subsidy amount from gross income, he or she may not take a tax credit for a qualified expenditure.

In addition to a public utility, a state may provide energy-efficiency incentives for qualified expenditures. Section 136 does not address these payments, and a recipient may have to include them in gross income. Generally, gross income means all income from whatever source derived. However, certain state payments made primarily to low and moderate-income individuals to assist in energy expense management may qualify for exclusion from gross income under general welfare principles. If a state provides these payments to residents without regard to income levels, the recipient must generally include the amounts in gross income.

'Rebates' generally represent a return of capital or a purchase-price adjustment to the property acquired with the incentive payment. Therefore, the individual does not include them in gross income. However, the amount of the rebate would reduce the taxpayer's cost basis (and, hence, available tax credit) in the acquired property. Many

state-provided energy related incentives are erroneously referred to as rebates, but do not in fact constitute rebates or purchase-price adjustments for federal income tax purposes. These incentives do not require a cost-basis (or credit) reduction for property acquired with the payments, if the recipient includes the incentives in gross income (or excludes them under general welfare principles).

I thank you for your interest in this matter and hope this information is helpful. If we can assist you further, please contact me or \_\_\_\_\_ at \_\_\_\_\_.

Sincerely,

/s/ William A. Jackson

William A. Jackson  
Chief, Branch 5  
Associate Chief Counsel  
(Income Tax & Accounting)