



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

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The Honorable Aaron Shock
Member, U.S. House of Representatives
100 NE Monroe, Room 100
Peoria, IL 61602

Attention:

Dear Congressman Schock:

I am responding to your inquiry dated August 25, 2010, on behalf of your constituent, [redacted] wrote to you on behalf of her husband and herself ("the [redacted]") to ask about the Residential Energy Efficient Property credit that is available for qualified geothermal heat pump property. (See enclosed section 25D of the Internal Revenue Code (the Code)). [redacted] wrote that they installed geothermal heat pump property on a home they own, but the home is not their permanent residence. The [redacted] son lives in the home. The letter does not indicate who purchased the geothermal heat pump property or whether the [redacted] rent the home to the son.

Tax Credit for Geothermal Heat Pump Property under Section 25D of the Code

The law provides a tax credit for 30 percent of the qualified geothermal heat pump property (the equipment) expenditures that a taxpayer makes during a taxable year.

The equipment must:

- Use the ground or ground water as a thermal energy source to heat a dwelling unit or a thermal energy sink to cool a dwelling unit, and
- Meet the requirements of the Energy Star program in effect at the time that the taxpayer makes the expenditure for the equipment.

A taxpayer does not have to own the home on which he or she installs the equipment to claim the credit. The taxpayer must install the equipment on or in a dwelling unit located in the United States that he or she uses as a residence. It does not have to be the taxpayer's principal residence but may include a taxpayer's second home, such as a vacation home. The law sometimes deems a taxpayer to use a home as a residence if a family member of the taxpayer, including the taxpayer's lineal descendants, uses the

home for personal purposes for a certain amount of days during the taxable year (see section 280A(d) of the Code).

If the _____ purchased the qualified geothermal heat pump property and they use the home as a residence, they are eligible for the section 25D credit. Alternatively, if the _____ son purchased the qualified geothermal heat pump property and he uses the home as a residence, he is eligible for the section 25D credit.

Energy Credit under Section 48 of the Code

If the _____ purchased the qualified geothermal heat pump property for a home that they rent to their son, neither the _____ nor their son qualify for the section 25D credit during the rental period. The _____, however, may qualify for the 10-percent energy credit under section 48 of the Code. The energy credit provides a 10-percent credit for the cost of equipment that uses the ground or ground water as a thermal energy source to heat a structure or as a thermal energy sink to cool a structure.

The section 48 energy credit is only available for property that a taxpayer can depreciate (sections 48(a)(3)(A)(vii) and 48(a)(3)(D) of the Code). Generally, a taxpayer can take a depreciation deduction for the exhaustion and wear and tear of property used in a trade or business, or of property held for the production of income, such as a rental property. The law provides that a taxpayer using a dwelling unit as a residence may only depreciate the portion of the dwelling unit that the taxpayer also uses in a trade or business or for the production of income (section 167 of the Code). Thus, for the _____ to qualify for the section 48 energy credit, they must use the home in a trade or business or for the production of income, and not for personal purposes.

As mentioned earlier, the law generally treats a taxpayer as using a home as a residence and thus for personal purposes, rather than in a trade or business or for the production of income, if a family member of the taxpayer uses the home as a residence. A taxpayer, however, does not use a home for personal purposes if he or she rents the home to a family member for use as a principal residence by that family member. Therefore, if the _____ purchased the geothermal heat pump property for installation on the home, and the son pays fair rental to them for use of the home as his principal residence, the _____ may be eligible for the 10-percent energy credit under section 48.

These questions are complex, but I hope this information is helpful in explaining the requirements a taxpayer must meet to qualify for these credits. If the _____ or you have further questions on this matter, please contact _____ at _____ or me at _____.

Sincerely,

Curt G. Wilson
Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure