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ETIA of 2005 and New Energy-Efficient Appliances

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In the previous two columns, we looked at the tax credits created by the Energy Tax Incentives Act of 2005 (ETIA) made available for energy conservation improvements to alternative energy sources in an existing residence, the business tax deductions and credits for the construction of new energy-efficient homes,

production of energy-efficient products, and the incorporation of energy-efficient business property. This month we discuss the new credit for the eligible production of certain energy-efficient appliances, such as dishwashers, clothes washers, and refrigerators.

Energy-Efficient Appliances

A new general business credit added by ETIA is found in IRC §45M. This credit is for the eligible production of certain energy-efficient appliances, such as dishwashers, clothes washers, and refrigerators.

In general, the appliance credit is calculated separately for each type of qualified energy-efficient appliance that's produced by the taxpayer after December 31, 2005, and prior to January 1, 2008. The appliance credit amount, more specifically, is the

product of the eligible production amount for that type of appliance and the credit for that type (new IRC §45M(a)(2)).

The total credit for the taxpayer is the sum across the types of appliances.

There are three types of qualified energy-efficient appliances according to new IRC §45M(d): dishwashers, clothes washers, and refrigerators. The category of qualified refrigerators is further subdivided into three efficiency levels.

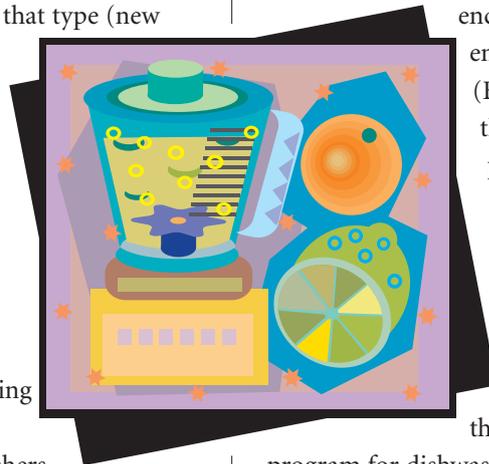
Dishwashers. New IRC §45M(b)(1) states that the applicable amount for a dishwasher is the energy savings amount (as defined in new IRC

§45M(b)(2)) that applies to dishwashers produced in 2006 and 2007 and that meet the Energy Star program requirements in effect in 2007. The energy savings amount per dishwasher is the lesser of (1) \$100 or (2) \$3 multiplied by 100 times the energy savings percentage. Thus the maximum credit available is \$100 per unit.

The energy savings percentage is defined as the ratio of (1) the difference between the energy factor (EF) required by the Energy Star program for dishwashers in 2007 and the EF required in 2005 and (2) the EF required by the Energy Star

program for dishwashers in 2007. By the way, the 2007 standards aren't known yet!

Clothes Washers. In the case of clothes washers, the credit is simply \$100 per eligible clothes washer manufactured in calendar year 2006 or 2007 that satisfies the requirements of the Energy Star program in



effect for clothes washers in 2007.

Refrigerators. The third type of appliance is refrigerators, which are subdivided into three energy savings categories: 15%, 20%, and 25%. The credit for refrigerators is based on the standard of the energy savings categories and the year of manufacture. The energy savings categories are determined relative to the 2001 energy conservation standards promulgated by the Department of Energy.

Refrigerators that qualify in the 15% savings category are those that are manufactured in calendar year 2006 and consume at least 15% but no more than 20% fewer kilowatt hours per year than the 2001 energy standards. The credit for this category of refrigerators is \$75 per unit.

Refrigerators that qualify in the 20% savings category are those that are manufactured in calendar year 2006 or 2007 and consume at least 20% but no more than 25% fewer kilowatt hours per year than the 2001 energy standards. The credit for this category of refrigerators is \$125 per unit.

Refrigerators that qualify in the 25% savings category are those that are manufactured in calendar year 2006 or 2007 and consume at least 25% fewer kilowatt hours per year than the 2001 energy standards. The credit for this category of refrigerators is \$175 per unit.

One should recognize that there appears to be a glitch in the legislative language categorizing the refrigerators. A refrigerator that uses exactly 20% less energy falls into both the 15% and 20% definition; likewise, a refrigerator that uses exactly 25% less energy falls into both the 20% and 25% definition. Presumably, this error will be corrected.

Not all appliances qualify for the credit. For dishwashers and clothes washers, the only units eligible are those produced by the taxpayer in the United States that are in excess of the average number of same-category appliances that were produced by the taxpayer (or any predecessor) in the U.S. in the three prior calendar years. In other words, if a taxpayer's average production for the previous three years was 100,000 units, then the credit is earned on production exceeding 100,000 units. Refrigerators have similar rules except that those eligible are the units produced in excess of 110% of the average production from the three prior calendar years. In the prior example, production would need to exceed 110,000 units (100,000 x 110%).

Limitations and Special Rules

The total credit amount that's available to each taxpayer is limited. A taxpayer may not claim credits in excess of \$75 million for all taxable years. Also, a taxpayer may not claim more than \$20 million credit on refrigerators qualifying under the 15% category in 2006.

Furthermore, the credit may not exceed 2% of the average annual gross receipts of the taxpayer for the three taxable years preceding the taxable year in which the credit is determined for all appliances (new IRC §45M(e)(3)).

As one might suspect, there are a few special rules in this new provision. First, the Secretary has the opportunity to promulgate rules for requesting the credit. That is, no credit is permitted to any taxpayer that hasn't submitted the information or certification deemed necessary by the Secretary, in consultation with the Secretary of Energy

(new IRC §45M(g)(3)). Second, for purposes of this general business credit, all employees of all corporations that are members of the same controlled group of corporations shall be treated as employed by a single employer, and, likewise, all employees of partnerships and proprietorships that are under common control are treated as a single employer. Finally, this credit doesn't apply to organizations listed in IRC §52(c), (d), and (e) (e.g., tax-exempt organizations, estates and trusts, real estate investment trusts (REITs)).

This and the prior two Taxes columns have only provided an overview of some of the energy credits available to taxpayers in 2006 and 2007. There is a lot more information in the law itself.

Will these credits be extended beyond 2007? Only time will tell! Then again, the same can be said about numerous other tax provisions enacted since the Economic Growth and Tax Relief Reconciliation Act of 2001, which includes the infamous 2010 sunset provision. ■

Note: Part of the material for this article came from the MicroMash CPE course "Energy Incentive Tax Act of 2005" by Tony Curatola and Catina Scafidi.

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