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## Newly Passed Climate Bill Makes a Big Push for Home Electrification

President Biden recently signed the Inflation Reduction Act (IRA) into law. This tax, drug-pricing, and climate change bill was passed using the partisan reconciliation process. One of the components of the IRA is the newly created High-efficiency Electric Home Rebate Program which provides state energy offices with funds to give low and medium-income homeowners and landlords a rebate of up to $14,000 on qualifying changeovers to move homes from gas appliances to electric. To ensure homes are able to meet the energy demands of new electric appliances, the rebate program includes funds dedicated to upgrading electrical panels and home wiring. While $4.3 billion has been appropriated for the rebate program, it will be up to individual states to make the rebate available to residents and potentially write additional requirements and limitations.

Each of the following appliances and upgrades are eligible for rebates and the equipment must be certified by the Energy Star program:

- Electric wiring: $2,500
- Electric load service center upgrades: $4,000
- Electric stove, cooktop, range, or oven: $840
- Electric heat pump clothes dryer: $840
- Heat pump for space heating or cooling: $8,000
- Heat pump water heater: $1,750
- Insulation, air sealing, and ventilation: $1,600

In addition to individual rebate limitations for each upgrade/appliance, the rebate is also limited based on the income of the homeowner/tenant. The threshold for income is based on the median income for the area in which the person/family lives and the number of persons in the family. The income thresholds by state and metropolitan area can be found here:

- Homeowners/tenants earning more than 80% of the median area income threshold but less than 150% can get a rebate of up to 50% of the cost of the full electrification project, limited to the above rebates.
- Homeowners/tenants earning less than 80% of the median area income can get a rebate of 100% of the project cost, limited to the above rebates.

Owners of multi-family housing are eligible to fully retrofit the facility if more than 50% of residents meet the median area income test, however, clarification is needed on how the $14,000 maximum rebate is applied to the full building or per unit basis:

- If more than half of the residents earn more than 80% of the median area income but less than 150%, the building owner can get a rebate of up to 50% of the cost of the project, subject to the above rebates.
- If more than half of residents earn less than 80% of the median area income, the building owner can get a rebate of up to 100% of the cost of the project, subject to the above rebates.

Electrification projects are limited to:

- New construction,
- Replacement of a nonelectric appliance (currently would not be allowed as replacement of electric resistance heating system), or
- First time purchase of that appliance.

Unfortunately, because the bill was written quickly, there are some unknowns that will require the Department of Energy to write regulations to clarify including the maximum rebate amount available for retrofits to entire multi-family housing facilities, ensuring single replacement of a tenant's appliances under the commercial replacement on an entity's behalf qualifies for the rebate, and how income tests will apply to new construction of multi-family housing.

## Long-term Extension of Energy Efficiency Tax Credits Provides Opportunity; New Contractor Requirements Could Impact Utilization

As part of the Inflation Reduction Act, Senate Democrats included long-term extension of Section 25C, the renamed Energy Efficient Home Improvement Credit; Section 45L, New Energy Efficient Home Credit, and updates to Section 179D, Energy Efficient Commercial Buildings Deduction.

Tax credits included in the bill:

- Long-term extension of 25C, the Energy Efficient Home Improvement Credit: Section 25C, which allows homeowners to make energy efficiency upgrades and reduce their taxes by 30% of the total improvement costs, has been extended through December 31, 2032. The lifetime limit has been replaced with an annual limit of $1,200 per year for "qualified energy efficiency improvements" with $600 eligible for energy property improvements. The credit also includes another $600 eligible for windows, $500 for exterior doors (up to $250 per door), and $2,000 for an eligible heat pump, heat pump water heater (HPWH), biomass stove, or biomass boiler. Qualifying energy property must meet or exceed the highest efficiency tier set by the Consortium for Energy Efficiency for the year the equipment is placed in service. The expanded Section 25C goes into effect on January 1, 2023 and is not limited to primary residences.
- Long-term extension of 45L, the New Energy Efficient Home Credit: Section 45L, which allows eligible contractors to claim a tax credit for installing energy-efficient equipment in new or majorly remodeled homes. A dwelling qualifies for the credit if:
    - It is a "zero energy ready home," or
    - For single-family homes acquired before January 1, 2025, it meets the Energy Star Single-Family New Home National Program Requirements 3.1, or
    - For single-family homes acquired after December 31, 2024, it meets the Energy Star Single-Family New Home National Program Requirements 3.2, or
    - For multi-family homes the dwelling must meet the Energy Star Multifamily New Construction National Program requirements that are in effect on either January 1, 2023, if occupied before December 31, 2026, or January 1 of three calendar years prior to the date the dwelling was acquired if acquired after January 1, 2027.

In addition to the new energy efficiency requirements, the legislation also creates a tiered tax credit available to the contractor:

- For "zero energy ready homes" the credit is $5,000 for single-family homes and $1,000 per multi-family home
- For single-family homes, the credit is $2,500
- For multi-family homes, the credit is $500 per dwelling

If the contractor pays prevailing wages to all laborers and mechanics employed by the contractor or subcontractor working on the construction of the dwelling, the credit for multi-family homes is increased to $2,500 per dwelling ($5000 for zero energy ready multi-family homes). The prevailing wage will be the rates for construction, alteration, or repair of a similar building in that location as set by the Secretary of Labor. The new Section 45L will go into effect on January 1, 2023.

- Changes to Section 179D, the Energy Efficient Commercial Buildings Deduction: Section 179D allows commercial building owners to claim a deduction based on energy efficiency improvements made to the building and its envelope. The legislation changes the way the deduction is calculated. Under the new deduction, a building owner must have the total energy and power usage of the building certified before and after the improvements are made.

  Each percentage point improvement over 25% increases the value of the deduction by $.02 on top of the base $.50 per square foot deduction with a maximum deduction of $1 per square foot. For a building that sees a 40% reduction in energy costs, the building owner can claim an $.80 per square foot deduction (40% - 25% = 15%, 15% x $.02 = $.30 over the base deduction of $.50 for a total deduction of $80 per square foot).

  All equipment installed to meet the energy efficiency increase requirements must be listed in ASHRAE 90.1-2007 or the most recent 90.1 standard.

  Section 179D also has an increase in the deduction if prevailing wage requirements and a new apprenticeship requirement are met. If the prevailing wage and apprenticeship requirements are met the base deduction is increased to $2.50 per square foot increased by $.10 per percentage increase in efficiency with a maximum of $5 per square foot deduction. The deduction is reduced by any deductions taken in the previous three years. For buildings owned by tax-exempt organizations, the credit is available to the designer of the building upgrades.

The new contractor requirements in 45L and 179D will complicate the selling opportunity created by the long-term extension of these tax credits.

## Inflation Reduction Act Includes Indirect Tax Changes with the Potential to Impact Distributors

The Inflation Reduction Act included several direct tax changes aimed at large corporations, however indirect tax changes including new IRS funding have the potential to impact NAED members. While changes to pass-through business taxation were discussed in earlier versions of the IRA, no tax rate changes were included in the final bill for pass-through entities, however, a limitation on loss deductions was extended for two years later this decade.

IRA included $80 billion in new funding for the Internal Revenue Service intended to close the "tax gap", the difference between actual taxes collected and what the IRS expects to collect in a given year. Republicans rightly made the point that this new funding will very likely impact taxpayers making less than $400,000 per year, despite President Biden's promise to only target high earners. Pass-through businesses often possess less legal and accountancy resources used by larger companies to ensure tax credits and deductions are applied appropriately.

The creation of the Corporate Alternative Minimum Tax (Corp. AMT) will also impact some NAED members, but also will set a dangerous precedent for future tax changes that could impact smaller businesses. The current Corp. AMT is limited to businesses earning more than $1 billion per year over an average of three years. If the exemption is lowered in future tax bills more businesses could be affected and limit the use of tax deductions used by businesses to invest in the future.

While the overall impact of the IRA is more beneficial for NAED members than negative, the precedents set by the legislation and the uneven playing field created by the labor provisions are troublesome.

**For more information:**

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