



The Residential Energy Property Credit

- RESIDENTIAL ENERGY PROPERTY CREDIT is available for properties placed into service in 2006 and 2007.
- RESIDENTIAL ENERGY PROPERTY CREDIT HAS A LIFETIME CREDIT UP TO A MAXIMUM OF \$500.

Introduction

Residential energy use is a significant percentage of the nation's energy consumption. With the recent power grid failure, spike in usage, and countless other factors, this nation must learn and find the ability to use energy more wisely. Responding to such need, Congress and The President have passed a series of energy credits for which not only businesses can use, but also the individual can use. The credits are easy to use and are worth consideration by everyone.

The first of two credits given to taxpayers is the RESIDENTIAL ENERGY PROPERTY CREDIT. (The second credit is known as THE CREDIT FOR RESIDENTIAL

ALTERNATIVE ENERGY EXPENDITURES and will be discussed in the next advisory.) The Residential Energy Property's thrust is to encourage homeowners to make improvements on the dwelling envelope and heating and cooling equipment to improve energy efficiency and reducing energy consumption. The envelope is defined as everything that separates the interior of the building from the outside environment, including the windows, walls, foundation, basement, slab, ceiling, roof, and insulation.

This credit is available for property placed into service in 2006 and 2007. It is a lifetime credit up to a maximum of \$500 subject to the following: 1) the **residential energy property expenditures**, plus 2) 10%

A CASE STUDY

Gift v. Compensation

The Tax Court has ruled that a son's work and aid in a business owned by his parents did not result in taxable compensation, but were instead construed to be a gift. The taxpayer in question worked and aided his parents in the operation

of a business belonging to his parents. His parents gave him money. The IRS contended that the money was remuneration for work done in the family business and was therefore taxable wages. The taxpayer countered and won, contending the money

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of the cost of **qualified energy efficiency improvements** added to a qualified personal residence.

As you will notice, there are two parts to this credit. The first is the **Residential Energy Property Expenditures**. The expenses are fully deductible as part of the equation, subject to limitation. Residential Energy Property Expenditures are divided into three classes and are described as follows: a) Energy Efficient Building Property which includes qualified heat pumps, air conditioners, and hot water heaters, b) qualified natural gas, propane or oil furnace or hot water boiler, and c) advanced main air circulating fans. Generally, if the property a homeowner puts into place during 2006 and 2007 qualifies and meets the guidelines as established by the IRS, it qualifies for the credit. The equipment is subject to the following limits among others: \$300 for any energy efficient building property, \$150 for any qualified natural gas, propane, or oil furnace, or hot water boiler, and \$50 for an advanced main circulating fan.

The second part of the credit includes **Qualified Energy Efficiency Improvements**. These improvements go more to the actual envelope of the building as opposed to equipment. These improvements qualify if they meet the criteria set forth in the 2000 International Energy Conservation Code as in effect on August 8, 2005 or if the improvement is a metal roof that meets energy star requirements. The improvement must be installed on or in connection with the taxpayer's principal residence in the United States and must be expected to be in use for at least five years.

Building envelope materials are specifically defined as 1) insulation materials or a system designed to reduce heat loss or gain of a dwelling unit, 2) exterior windows and skylights (subject to a \$200 limitation), 3) exterior doors, and 4) any metal roof as previously stated. Keep in mind, these improvement expenses are subject to only 10% usage as a credit. Residential Energy Property Expenditures (air conditioners, circulating fans, and boilers)



are fully deductible subject to the dollar limitation.

Limits

For purposes of the credit discussed here, the property must be placed in use (installation completed) in 2006 or 2007. Property mixed with business use must be 80% used as personal residence, otherwise a percentage applies. Property purchased with subsidized funding is not eligible for the credit; and the credit is a \$500 lifetime credit.

Conclusion

Individuals will not only reap the tax benefits from this bill, but will also see lower heating and cooling bills. Not only is this bill good for the individual installing efficient equipment and improving the integrity of the home, it is beneficial to the nation and its power supply. The consumer should be sure to save the receipts and of course always be able to provide proof that the credit taken is legitimate. The Center routinely engages in tax, estate, and business succession planning and would like to aide you in all of you tax needs. If you have more questions on how the credit works, contact Marcus Renwick, attorney and Director of Research at The Center.

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was a gift as part of a larger estate plan.

Editor's Comment:

Generally, any money given for an effort expended is taxable compensation. The taxpayer was very fortunate to win the case. From the facts as presented, the son did work in the business because his parents were not well. However, the son did not have to work, was not told what to do, and was able to prove that he was just helping his parents. Thus the Tax Court said that the money given to the son was just the parents' way of saying "thank you", i.e. a gift to their son.



How to Prepare Your Business for a Sale

By John E. Calia

Selling a business can be the largest and most important deal of an entrepreneur's career. Yet, most business owners prepare very little if at all. In the best of all worlds, the owner begins to prepare his or her business for sale a year or two in advance. Records should clearly document all transactions so that potential buyers can easily evaluate the company and so that a new manager can take over with minimal training.

The most important single factor in preparing your business for sale is to eliminate yourself as the most necessary employee of the company. You should not be the only member of the team with relationships with customers or perform a critical function with no backup.

Recently, I encountered a business owner who would like to sell his business so he can retire. When I told him the value of his business he expressed disappointment and asked what he could do. I advised him to set up his business so that a new owner could step in and begin to manage the company without risk of losing revenue and having to rebuild.

I have stayed in touch with this potential client and found that he has taken my advice. He has added a designer to do most of the creative work historically done by the owner and a sales manager to help grow the business. For this business owner, the value of his business is an important component of his retirement plan. He will do what is necessary to ensure his financial future.

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Frequently asked questions:



Q Can an officer of a corporation be held personally responsible for taxes of the corporation?

A: Generally it depends on the type of tax debt. If the taxes stem from employee withholding, usually the IRS will hold the officers of the company directly responsible for the debt in the event it is not paid. Therefore, it is wise to keep withholding taxes current. All other taxes tend to be situation specific, but usually the officers will escape liability if corporate formalities are obeyed.

Q What can I do to ensure that my business is successfully passed from me to the next generation?

A: To make sure a business passes from one generation to the next, it is best to engage in business succession planning. The biggest hurdle businesses face is not the estate tax, but death of the owner. If the owner dies before business succession is complete, the business stands very little chance of passing from one generation to the next.

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