



Statement of the Window and Door Manufacturers Association

for the

Tax Reform Working Group on Energy

Committee on Ways and Means
United States House of Representatives

on

Economic Impact of the Residential Energy Efficiency (25C) Tax Credit

April 15, 2013

Introduction

Founded in 1927, WDMA is the premier trade association representing the leading manufacturers of residential and commercial window, door and skylight products for the domestic and export markets. WDMA members are focused on Total Product Performance™ products that are designed and built to performance-based standards. WDMA members are leading America's efforts to develop and utilize energy efficient windows, doors and skylights for both new and replacement construction.

In 2005, Congress passed the *Energy Policy Act* (P.L. 109-58) and established a number of important tax incentives to promote greater energy efficiency in the built environment – single family, multifamily and commercial homes and buildings. These incentives acted as the only federal-level programs to address energy efficiency in new and existing homes and buildings, with the intent of moving the market towards greater efficiency and the delivery of innovation and technology transfer in building design and practice. Included as part of those incentives was the Section 25C Qualified Energy Efficiency Improvements Tax Credit, which provides a tax credit to home owners making energy efficient upgrades.

As the Committee considers options for tax reform, WDMA appreciates the opportunity to provide some insight on the goals of energy efficiency in buildings and specifically on the importance of the 25C tax credit in attaining the dual objectives of increased energy efficiency and creating jobs.

Meeting Our Nation's Energy Goals Through Window, Door and Skylight Replacement

Much has been said and written about reducing the nation's reliance on foreign oil and investing in renewable energy technologies—both important goals—but not as much attention has been paid to the impact that improving the energy efficiency of existing buildings could have on reducing energy consumption, and, as a result, reducing our dependence on foreign oil and other fossil fuels.

Residential and commercial buildings account for 41 percent of all energy use in the United States (U.S.), while U.S. buildings alone accounted for 7.4 percent of global energy consumption in 2008.¹ Significantly contributing to that energy consumption is the stock of nearly a billion single-pane windows still in use in residential buildings alone. As the California Energy Commission notes, the amount of energy lost each year through inefficient windows and doors is equivalent to the amount of oil the nation receives from the Alaska pipeline.²

Any national energy tax policy needs to make replacing inefficient windows and doors a high priority if we are to make improvements in the overall efficiency of our nation's residential and commercial building stock.

The Residential Energy Efficiency (25C) Tax Credit

Enacted as part of the Energy Policy Act of 2005, the original purpose of the Residential Energy Efficiency Tax Credit (Internal Revenue Code Section 25C) was to save energy. However, in recent years, the 25C incentives have achieved two compelling national goals:

¹ 2012 Building Energy Data Book, U.S. Department of Energy, Office of Energy Efficiency and Renewable Energy

² "Today's Windows," California Energy Commission, Consumer Energy Center, www.consumerenergycenter.org

- Saving energy by making energy efficient home improvements more affordable for a wide spectrum of the American public; and
- Saving thousands of U.S. manufacturing and construction jobs.

We believe that a properly focused residential tax credit can efficiently and effectively spur private investment in energy saving measures. While niche populations utilize other tax credits, the 25C tax credit is broad-based. By all accounts, it was hugely popular with the American homeowner, particularly the middle class, in 2009 and 2010. Internal Revenue Service (IRS) data for 2009 and 2010 shows taxpayers with adjusted gross income of under \$100,000 claimed two-thirds of the credit.

Also known as the Nonbusiness Energy Property Credit, 25C provides a credit to homeowners who make qualified energy efficiency improvements, including windows, doors and skylights, to an existing residence. In 2009 and 2010, the credit was increased to 30 percent of the cost of improvements up to \$1,500. For 2011, the 25C tax credit was reduced to 10 percent of the cost of improvements up to \$200 for windows and skylights and \$500 for exterior doors. The 25C tax credit expired at the end of 2011. On January 2, 2013, as part of the American Taxpayer Relief Act, the 25C tax credit was extended through 2013 and made retroactive for 2012.

Although unsuccessful last year, WDMA supported legislation introduced by Reps. Jim Gerlach (R-PA) and Richard Neal (D-MA) titled the Home Energy Savings Act (H.R. 6398), that would have increased the credit to \$1,000 up to 10 percent of product costs, included labor costs for installation of all qualifying products and made the credit permanent.

Many of the products that qualify for the 25C tax credit, including windows, doors and skylights, are manufactured—and later installed—in America, unlike alternative energy sources that have benefited from other federal incentives.

The nation's housing industry is finally recovering from a prolonged slump, which has had a profound impact on the window, door and skylight industry. Remodeling and replacement window demand remains sluggish after a decline of three percent in 2012. Moreover, private residential investment remains near record low levels at 2.8 percent of gross domestic product for the fourth quarter of 2012—in comparison to its historic average of approximately 5 percent.³

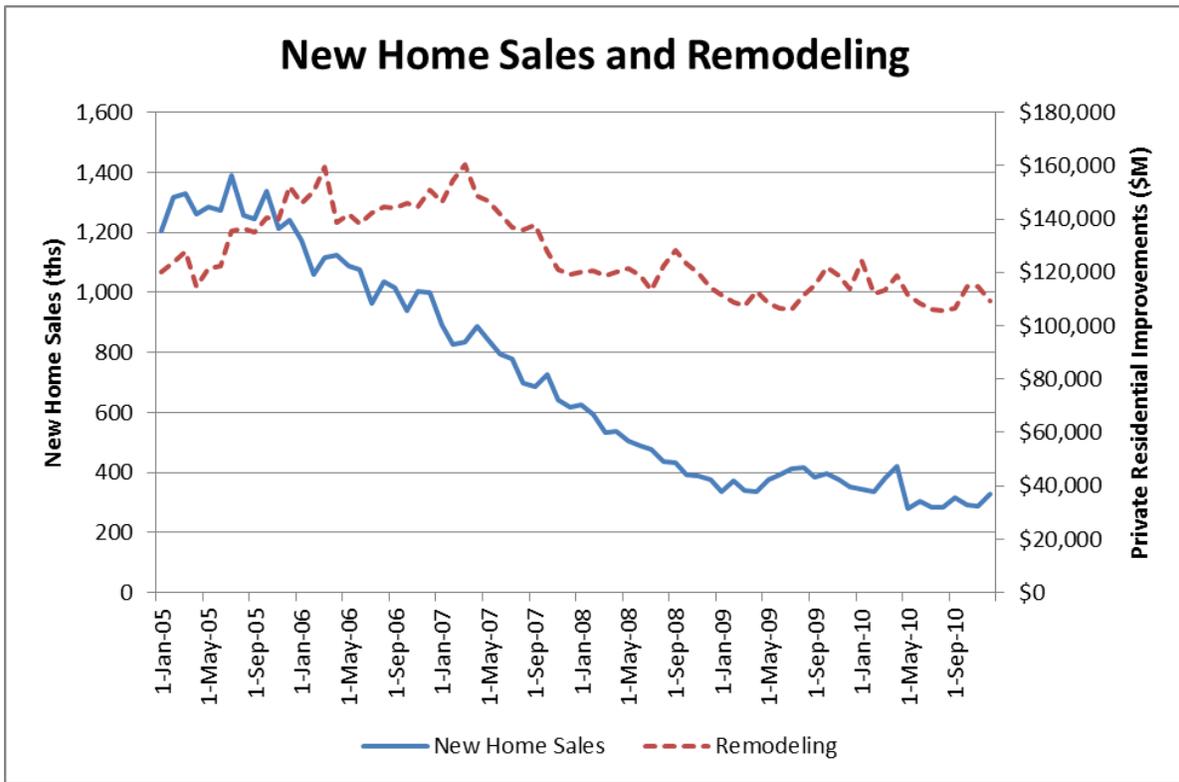
During the housing downturn, there was a demonstrable shift to the remodeling and retrofit market for the window, door and skylight industry, spurred in part by the 25C tax credit. The 25C tax credit in effect for 2009 and 2010 was tremendously successful in supporting the industry and its workers during the worst housing downturn since World War II. The tax credit can be directly tied in our industry to the preservation and creation of American jobs and keeping plants and production lines open.

This shift to the remodeling and retrofit market is evident in comparison to new home sales during the same period. While total remodeling activity declined somewhat, it certainly weathered the

³ U.S. Bureau of Economic Analysis data

economic downturn much better than new home construction, in large part due to the increased 25C energy tax incentives Congress enacted in 2009.

The following chart courtesy of the National Association of Home Builders (NAHB) plots new home sales (left axis) and total remodeling expenditures (right axis). The data indicates that remodeling expenditures fared better over the 2006 through 2010 period than new home sales. The tax credit program provided a floor on remodeling activity, which declined only 25 percent from its peak over the period compared to 72 percent for new home sales.



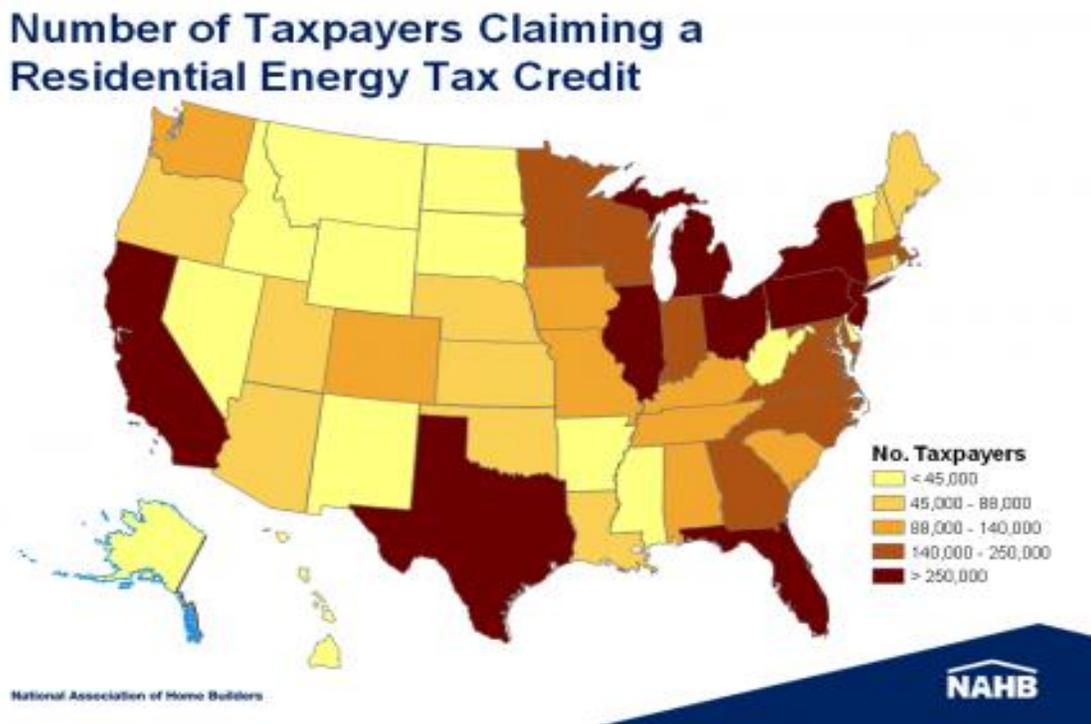
Economic Impact of the Residential Energy Efficient Tax Credit

Using the 2009 IRS tax data, the net economic impacts of the 25C tax credit programs from a remodeling perspective are significant (setting aside the long-run energy efficiency benefits for homeowners).

- For tax year 2009, IRS data indicates \$25.1 billion of remodeling expenses in connection with the section 25C tax credit
- NAHB estimates that this level of remodeling activity was associated with 278,610 full-time jobs
 - 135,540 of these jobs were in the construction and remodeling sectors
- Homeowners received a tax benefit of \$5.17 billion from the 25C credit
- 93 percent of taxpayers claiming the energy credit had adjusted gross income of \$200,000 or less

The 25C credit is claimed on the same tax form (5695) as a similar remodeling credit, the section 25D credit, which provides a nonrefundable 30 percent tax credit to consumers for the purchase and installation of certain power production property for a home. Typical uses include solar, geothermal, fuel cells, and small wind energy. The credit is uncapped, meaning that all qualified expenses may be claimed. Labor costs are eligible, and unlike section 25C, the section 25D credit can be claimed against the AMT.⁴

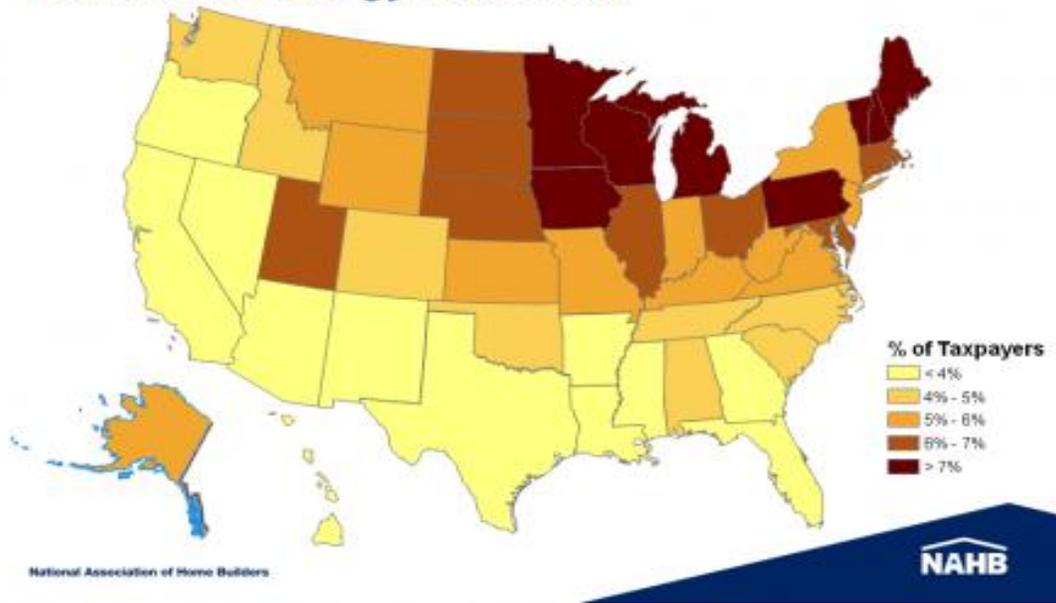
The map below tracks the number of taxpayers in each state that claimed either or both the 25C and 25D tax credit, although NAHB estimates that nearly 90 percent of claims were 25C related. Intuitively, larger states in terms of population had larger numbers of taxpayers claiming the credits.



A slightly different picture emerges in the next map, which presents the percentage of taxpayers in each state who claimed either or both the 25C and 25D tax credits in 2009. A clear concentration of tax credit use can be seen for states in the Northeast and upper Midwest. There are two leading explanations for this. First, homeowners in states in cold weather climates have more to gain from energy-efficient improvements in terms of reduced utility bills. However, there is no reason to believe that warm weather homes could not also benefit from energy-efficient improvements.

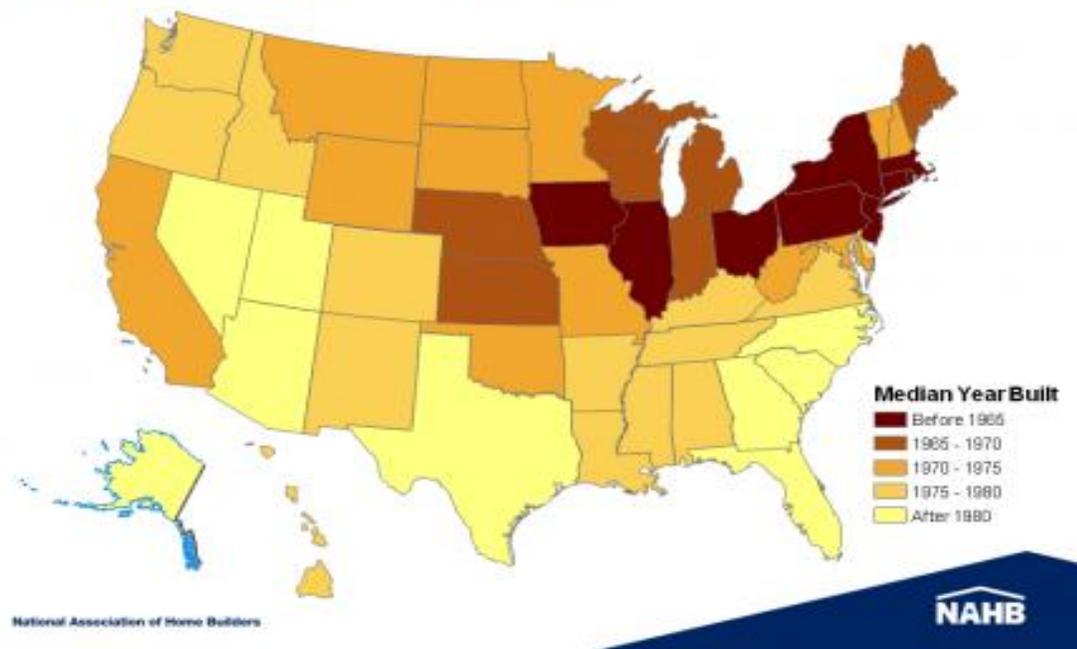
⁴ Although the tax code does not allow taxpayers to claim section the 25C credit against the AMT, the annual AMT “patch” typically allows taxpayers to claim section 25C and other personal, nonrefundable tax credits against AMT. The simple, straightforward approach used in section 25D offers a model for improving the section 25C tax credit. A 30% tax credit that includes labor costs and is automatically AMT-preferred is simple, straightforward and effective.

Percent of Taxpayers Claiming a Residential Energy Tax Credit



Thus, the second explanation, and the stronger one, is that the states with relatively more common use of the energy tax credits also contain older homes. The following map details the median year of construction for housing units in each state, and there is indeed a rough correlation between tax credit use and older housing with concentrations of both in many northern states.

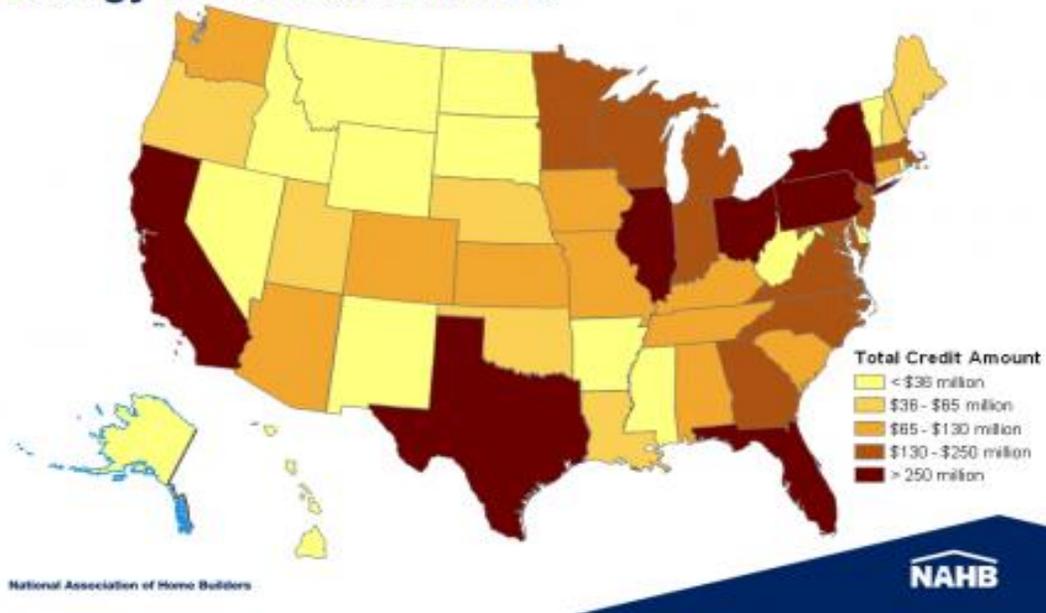
Median Year of Houses Built



A homeowner with a 50-year-old home is much more likely to improve their residence than a homeowner who has purchased a newly constructed home, with new construction more common in the southern part of the nation.

The last map tracks the total amount of the tax credits claimed. Overall, in 2009 taxpayers claimed nearly \$5.9 billion in 25C and 25D tax credits. For the two tax credits combined, **93 percent of tax credit claims were made by taxpayers who had an adjusted gross income of no more than \$200,000**, which is indicative of a middle class tax program.

Total Amount of Residential Energy Tax Credit Claimed



With respect to the 25C credit for energy-efficient remodeling of existing homes, the IRS data indicates a total of \$25.1 billion of qualified expenditures in 2009.

Because the tax credit in 2009 was limited to \$1,500 per taxpayer, not all of this activity generated tax credits. In fact, according to the IRS data, just a little more than 71 percent of these costs (\$5.404 billion versus potential \$7.539 billion) were allowed in the 25C calculation due to the \$1,500 limit. Moreover, due to other tax rules, only \$5.172 billion of the \$5.404 billion were allowed as realized 25C tax credits.

The first portion of the 25C credit usage is related to energy-efficient building envelope improvements, with 13 percent of the 25C claims associated with insulation, 34 percent with windows and skylights, 9 percent with doors and another 9 percent with qualified roofing materials. The second part of the credit dealt with energy-saving appliance installation, with 16 percent of the total claims connected to qualified heat pumps, air conditioners, water heaters and stoves; 17 percent with qualified natural gas, propane, oil furnaces or hot water boilers; 3 percent with advanced main air circulating fans used with a natural gas, propane or oil furnace.

An economic impact model has been developed by NAHB to estimate total employment and economic income impacts from home building and remodeling.⁵ The model uses Bureau of Economic Analysis (BEA) data and BEA input-output tables to generate economic impacts by sector. The following table presents the impacts resulting from \$100,000 of remodeling activity.

⁵ <http://www.nahb.org/generic.aspx?sectionID=734&genericContentID=103543&channelID=311>

Income and Employment Impacts of Remodeling on the U.S. Economy

	Number of Full-time Jobs	Wages and Salaries	Proprietors' Income	Corporate Profits	Total Income
<i>\$100,000 Spent on Remodeling</i>					
All industries	1.11	\$52,709	\$13,810	\$16,147	\$82,667
Construction	0.54	\$25,573	\$6,601	\$4,232	\$36,406
Manufacturing	0.18	\$8,136	\$824	\$4,529	\$13,489
Wholesale and retail, Transportation and warehousing	0.16	\$6,432	\$849	\$2,307	\$9,588
Finance and insurance	0.02	\$1,487	\$71	\$1,459	\$3,017
Real estate and rental and leasing	0.01	\$315	\$1,652	\$758	\$2,725
Professional, Management, administrative services	0.12	\$6,970	\$2,191	\$764	\$9,924
Other services	0.09	\$3,797	\$1,623	\$2,098	\$7,518

Source: NAHB estimates, based primarily on data from the U.S. Bureau of Economic Analysis.

The jobs are measured on a full-time equivalent (FTE) basis. Thus, NAHB estimates that every \$100,000 of remodeling activity creates 1.11 jobs on an FTE basis. 48.6 percent of those jobs are in the construction and remodeling sector.⁶

Putting all the data together, the IRS data and the NAHB economic impact model indicate that for 2009, a total of 278,610 full-time jobs were in connection with the 25C credit—135,540 of these jobs were in the construction and remodeling sectors. The program supported approximately \$13.2 billion in wages for these workers and \$7.5 billion in net business income.

Treasury Inspector General Report on Residential Energy Credits

On April 19, 2011, the U.S. Department of Treasury Inspector General for Tax Administration issued a report on the residential energy efficient tax credits (IRC 25C and 25D) and came to the conclusion that inadequate processes were in place to verify eligibility for the credits. Specifically, the report stated that:

*The IRS **cannot verify** [emphasis added] whether individuals claiming Residential Energy Credits are entitled to them at the time their tax returns are processed. The IRS does not require individuals to provide any third-party documentation supporting the purchase of qualifying home improvement products and/or costs associated with making energy efficiency improvements and whether these qualified purchases and/or improvements were made to their principal residences.*⁷

⁶ The Direct Impact of Home Building and Remodeling on the U.S. Economy. NAHB Economics.

⁷ "Processes Were Not Established to Verify Eligibility for Residential Energy Credits," Treasury Inspector General for Tax Administration, Reference Number 2011-41-038, April 19, 2011

While the report did note a number of deficiencies with the IRS process for establishing verification of eligibility for the credit, some of the credits claimed are legitimate despite the inability to establish eligibility for the credit. In addition, the IRS notes that it can improve its processes to add additional safeguards and improve its ability to verify eligibility. WDMA stands ready to assist the government in ensuring the credit goes only to those who truly deserve it.

To that end, WDMA has recommended consumer-friendly verification techniques to the IRS with the goal of improving the system for assuring that the tax credit claimed on returns are actually for qualifying energy efficient windows, doors and skylights. Currently, no documentation is provided on tax returns about the qualifying product. Taxpayers must maintain documentation in the event of an audit.

There are a variety of methods that should be explored to provide an identifying number or code that could be included on tax returns to help the IRS establish the eligibility of a product for the tax credit, which could be implemented for use with electronic filing. WDMA will continue to work with Congress and the IRS to improve the system of product verification.

Conclusion

Without question, the nation is facing the twin challenges of reducing energy consumption while spurring job creation. The 25C residential energy efficient tax credit encourages middle-income home owners to undertake important and beneficial energy saving upgrades, which in turn supports American jobs across the housing industry supply chain—from manufacturing to distribution to sales to installation. The 25C credit has been popular because it works.

The 25C tax credit has broad support among window, door and skylight manufacturers. WDMA supports a robust extension of the 25C tax credit, knowing the \$1,000 level would effectively leverage consumer activity and job preservation.

WDMA would like to thank the Committee and the energy working group for the opportunity to provide this statement and looks forward to working with it in extending the 25C tax credit at a level that will support the nation's energy goals while creating and preserving American jobs.

For More Information Contact

Ben Gann

Director of Legislative Affairs

