



## Tax Credits for Replacing Heating and Cooling Systems

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Upgrading to an energy-efficient heating and cooling system can save hundreds on your utility bills and earn you a tax credit worth as much as \$1,500.

Replacing an aging heating and cooling system can save you money over time. According to Energy Star, a federal program that promotes energy efficiency, about half of what the average household spends on energy bills goes toward heating and cooling.

Upgrading your heating, ventilation, and air conditioning (HVAC) to energy-efficient units can cut utility costs by about 20%, or \$200 annually, on average. A tax credit for heating and cooling systems can make the project more affordable.

This type of home improvement doesn't come cheap. Prices vary widely based on where you live, unit specifications, and the condition of your home, but figure a high-efficiency furnace will start at around \$3,500, including installation, estimates Corbett Lunsford, executive director of Chicago-based Green Dream Group. A standard furnace may cost \$2,400. To help offset the price difference, the IRS allows a tax credit worth up to \$1,500 on eligible HVAC systems put into service during 2009 or 2010. Consult a tax adviser.

## **Pay attention to efficiency ratings**

To earn an Energy Star rating, furnaces must be more efficient than standard units, with annual fuel utilization efficiency ratings, or AFUE, of 85% for oil furnaces and 90% for gas furnaces. The Energy Star seal of approval alone isn't enough to garner the federal tax credit. Credit-eligible ([http://www.energystar.gov/index.cfm?c=tax\\_credits.tx\\_index#c3](http://www.energystar.gov/index.cfm?c=tax_credits.tx_index#c3)) gas furnaces (either natural gas or propane) must have AFUE ratings of 95% or greater; oil furnaces, 90%. A boiler must have an AFUE of 90%.

Heating by burning a fuel is inherently inefficient. Simply put, high-efficiency furnaces have components that are better designed to get more heat out of the combustion process, Lunsford says. You'll need to hire an HVAC contractor to calculate the size of the equipment needed for your home. Beware bidders who take a one-size-furnace-fits-all approach. Air source heat pumps ([http://energystar.custhelp.com/cgi-bin/energystar.cfg/php/enduser/std\\_adp.php?p\\_faqid=5799](http://energystar.custhelp.com/cgi-bin/energystar.cfg/php/enduser/std_adp.php?p_faqid=5799)) and advanced main circulating fans can also qualify for the \$1,500 tax credit.

Technically, a homeowner could replace either a furnace or a central air-conditioning unit and be eligible for the tax credit. Practically speaking, you probably will have to replace both for the A/C to qualify, says Enesta Jones, a spokeswoman for the U.S. Environmental Protection Agency. Most homes have split systems made up of an outdoor condenser and compressor that are connected to an indoor air handler that's part of the furnace. Split systems must have a SEER rating of at least 16 and an EER rating of at least 13. The higher the rating, the more energy efficient the unit. A package A/C system, which houses all of its components outdoors, requires lower ratings.

## **HVAC's value goes beyond savings**

It typically takes about a decade's worth of energy savings to recoup the investment in a new HVAC system, Lunsford says, though that time frame can vary greatly depending on how much fuel prices fluctuate. Less apparent in dollar terms are increasing the comfort level in your home and lowering your household's drain on non-renewable fossil fuels. Then there's the effect on your home's value when it comes time to sell.

You're going to enhance a home's salability by moving to a more energy-efficient heating and cooling system, says Frank Lesh, president of Home Sweet Home Inspection Co. in Indian Head Park, Ill. That doesn't mean adding a \$5,000 furnace will add \$5,000 to the sale price. Rather, potential buyers are less likely to push for repairs or negotiate a credit if the HVAC is in good shape. Evaluate systems older than 10 years for possible replacement.

But before you do, conduct a wider energy audit (<http://www.houselogic.com/articles/conduct-your-own-energy-audit/>) of your home. Lunsford, also manager of consumer education for the U.S. Green Building Council's Chicago Chapter, says he rarely recommends replacing a furnace as the first step in making a home more energy efficient. Instead, start by sealing it against air leaks. Do-it-yourself caulking and weather-stripping help, as does adding insulation in the attic. Professional air sealing, which is more effective, can cost as much as \$5,000 for a large house, he says. The payoff: Energy costs should go down, and you might be able to get by with a smaller HVAC system.

### **Getting tax credit for your upgrades**

The federal energy tax credit is based on 30% of the cost of an eligible HVAC system. Installation charges count too. A \$5,000 bill would max out the credit. You'll need to owe more in taxes than you're trying to claim in credits to qualify. Use IRS Form 5695. Save receipts for your records, as well as manufacturers' certification statements. If part of a new HVAC system qualifies for the credit but another part doesn't, ask the contractor to itemize the receipt.

The tax credit is aggregated for all qualifying energy upgrades-insulation, roofs, windows, and so on-so you can't claim separate \$1,500 credits for each project. Only improvements to your existing primary residence count. New homes and second homes are excluded.

*This article provides general information about tax laws and consequences, but is not intended to be relied upon by readers as tax or legal advice applicable to particular transactions or circumstances. Readers should*

*consult a tax professional for such advice, and are reminded that tax laws may vary by jurisdiction.*

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