

HELP FOR RESPONSIBLE HOMEOWNERS | JUNE 2009

Advance Rebates for Energy-Efficient Home Improvements

By Anne Kim and Ryan McConaghy

The economic recovery package passed by Congress included a generous boost in the tax credit for energy-efficient home improvements. But homeowners must wait until tax time next April to reap its benefits—diminishing the credit’s appeal to potential home improvers and blunting its impact. Congress can solve this problem by making the credit advanceable to provide a rapid rebate for energy-efficient home improvements. This simple adjustment can significantly help homeowners handle the initial costs of installation, help spur demand for efficiency improvements, and make it easier for middle class Americans to reduce the energy burden on their check-books by cutting their power bills.

THE PROBLEM

Consumers need swift relief from upfront costs of energy-efficient home improvements

Energy-efficient home improvement can save homeowners significant amounts of money in the long run. But it can also be an expensive upfront investment that many homeowners are too cautious to take on in the current economic climate.

In a weak economy, consumers are more hesitant to spend.

From May of 2008 to May of 2009, general consumer spending posted a 56% decline.¹ The home improvement market is not immune—according to the National Association of Homebuilders Remodeling Market Index, despite recent improvement market conditions and future expectations for home additions, alterations, and repairs in the first quarter of 2009 are still down from the previous year.² Even with the new tax benefit, the combination of consumer cautiousness, financial concerns, and premium costs for energy-efficient items may present an economic barrier for homeowners considering efficiency improvements.³

As the recession has progressed, consumers have indicated a continued interest in purchasing energy efficient products, but economic concerns have overtaken environmental considerations, and consumers are now looking for a return on their investments.⁴ These new priorities may make consumers slower to upgrade or replace inefficient home equipment for an additional upfront cost, despite an underlying desire to purchase efficient equipment and realize long-term savings.

Current tax breaks are generous but available only after the fact.

The American Recovery and Reinvestment Act enhanced the tax credit designed to help homeowners pay for energy efficiency improvements (such as the installation of qualifying windows and doors, insulation, roofing, HVAC equipment, water heaters, and other items).⁵ Instead of listing different levels of benefits for individual items, the new law provides a streamlined, aggregated credit for improvements made in 2009 and 2010, and increases benefits from 10% of the total cost (up to a maximum of \$500) to 30% of the cost (up to a maximum of \$1500).

These changes have substantially beefed up federal support for home efficiency improvements. However, taxpayers must still wait until after filing their year-end returns to receive the credit.⁶ As a result, the homeowner who spends extra money on a new, efficient air conditioner this summer would need to wait nearly one full year before receiving a rebate.

THE SOLUTION

Advance rebates for energy-efficient home improvements

Given the current state of the economy and consumer activity, making it possible for homeowners to swiftly pocket the tax credit for efficiency improvements may help to convince more homeowners to take the initial plunge, thereby furthering the goal of boosting efficiency to reduce power costs and lower energy demand.

Converting the recently-enacted tax credit for home energy efficiency into an advanceable credit will allow consumers to forego the delay of waiting for a standard tax payment. It would also help stimulate the energy-efficiency market and jump-start the nation's transition to a clean energy economy.

The proposal would provide rapid relief.

Under this proposal, the existing energy efficiency tax credit would be restructured to allow consumers to make an immediate claim by filing an amended tax return for 2008. (This is the same mechanism now available for

the First-Time Homebuyer Tax Credit included in the American Recovery and Reinvestment Act). Rather than being forced to wait months to file for the credit, consumers would be able to receive their benefits in short order, thereby accelerating the financial return for investing in an efficient home improvement, helping assuage consumer concerns about delays and spurring sales.

The proposal would improve home values while reducing energy costs.

By spurring efficiency improvement activity, the modified credit would help Americans shore up home values in a volatile housing market. It has been estimated that for every dollar of annual utility bill savings achieved through home energy efficiency measures, \$20 is added to a home's value.⁷ In a market that has seen home prices post record declines at the beginning of 2009, dropping 19.1% from the beginning of 2008 and over 32% from their peak in the middle of 2006,⁸ fostering efforts to raise home values will not only help to accelerate energy savings benefits, but will also help to address one of the key factors in the economic downturn.

The proposal would provide significant future savings for consumers.

According to some estimates, total energy bills for the average homeowner will equal approximately \$2300 this year.⁹ Much of this cost will be for electricity, which has been consuming a growing share of home energy expenses. The average residential retail cost of electricity jumped by 30% from 2003 to 2008,¹⁰ and the average residential electric bill in America increased from about \$879 in 2000 to just over \$1196 per year in 2007.¹¹

Efficiency upgrades to existing homes can help to counteract the rising price of power by allowing homeowners to use less energy. For example, substituting an Energy Star-certified central air conditioning unit for an older, inefficient model can cut home cooling costs by 30%.¹² Consumers who choose to replace their hot water heaters with Energy Star-certified heat pump water heaters hitting the market in 2009 will be able to trim their annual electric bills by almost \$300.¹³ But because these technologies have initial costs that are higher than the less efficient alternatives, it may take a few years to recoup that early investment before generating net savings.¹⁴ An advance rebate can make this initial investment more attractive to homeowners on the fence.

■ THE ROLLOUT

- **Hold a press conference/speech** with a local family interested in making energy-efficient home improvements or with vendors hoping to increase sales of energy-efficient products.

- **Issue a report** on rising utility costs and the savings benefits of improvements covered under this proposal

CRITIQUES & RESPONSES

Advance Rebates for Energy Efficient Home Improvements

It's too expensive.

This proposal does not create a new tax benefit. Rather, it just puts money in the pockets of individual taxpayers faster than the current system. The cost of expanding the old tax credits, which was estimated at about \$2 billion,¹⁵ has been addressed through the American Recovery and Reinvestment Act. Since this proposal changes the timing, but not the scope of existing tax benefits, its budgetary impact should be minimal. In addition, the increased cost of greater participation in the program would be a worthwhile investment in helping middle class families to cut their utility bills and reduce energy demand.

It's too complicated.

No, this proposal builds on an existing model already used by the Internal Revenue Service to allow consumers to expedite receipt of their tax benefits. Allowing individual consumers to amend their returns will allow the government to process their claims more quickly and provide them increased incentive to make energy-efficient home improvements.

* * *

THE AUTHORS

Anne Kim is the Director of the Third Way Economic Program and can be reached at akim@thirdway.org. Ryan McConaghy is Deputy Director of the Third Way Economic Program and can be reached at rmcconaghy@thirdway.org.

ABOUT THIRD WAY

Third Way is the leading think tank of the moderate wing of the progressive movement. We work with elected officials, candidates, and advocates to develop and advance the next generation of moderate policy ideas.

For more information about Third Way please visit www.thirdway.org.

■ ENDNOTES

1 Dennis Jacobe, "Weekly Economic Wrap: Post-Memorial Day Spending Falls," Gallup.com, June 2, 2009, available at <http://www.gallup.com/poll/118973/Weekly-Economic-Wrap-Post-Memorial-Day-Spending-Falls.aspx>.

2 On May 19, 2009 the Remodeling Market Index for current market conditions had dropped from 41.8 in the first quarter of 2008 to 34.5 in the first quarter of 2009. The index for future expectations had dropped from 37.9 to 30 in the same period. National Association of Homebuilders "Remodeling Market Index", May 19, 2009, available at <http://www.nahb.org/page.aspx/category/sectionID=136>.

3 Energy efficiency experts have acknowledged concern about the impact of the current economic climate in relation to the new tax credit included in the American Recovery and Reinvestment Act. Lowell Ungar, Policy Director of the Alliance to Save Energy, noted that while the credit can help to address incremental costs, "People are still going to have to come up with the other two-thirds". The American Council for an Energy Efficient Economy's Steve Nadel has remarked that, "It will get some people to buy...Other people just aren't going to be able to come up with the money." H. Josef Hebert, "Homeowners Could Reap Big Benefits for Energy Savings," Chicago Tribune, February 5, 2009, available at <http://www.chicagotribune.com/features/lifestyle/green/sns-ap-stimulus-energy-green,0,3714286.story>.

4 In the survey, 71% of consumers cited saving money as a reason to buy energy-efficient products, as opposed to 55% citing the environmental concerns and 49% citing conservation concerns. In 2006 and 2007 environmental concerns had trumped other considerations. The survey also found that consumers are moved by the potential for utility bill savings and disappointed if they do not come to fruition. "Shelton Group Survey: Recession-Wearry Consumers Willing to Spend on Green Products – If They Get Green in Return," Reuters, March 23, 2009, available at <http://www.reuters.com/article/pressRelease/idUS132663+23-Mar-2009+BW20090323>.

5 ENERGY STAR, "Federal Tax Credits for Energy Efficiency," May 26, 2009, available at http://www.energystar.gov/index.cfm?c=products.pr_tax_credits.

6 Ibid.

7 Rick Nevin, Christopher Bender, and Heather Gazan, "More Evidence of Rational Market Values for Home Energy Efficiency," The Appraisal Journal, October 1999, available at http://www.icfi.com/Markets/Community_Development/doc_files/apj1099.pdf.

8 Standard and Poors Press Release, "Nationally, Home Price Began 2009 with Record Declines According to the S&P/Case-Shiller Home Prices Indices," May 26, 2009, available at http://www2.standardandpoors.com/spf/pdf/index/CSHomePrice_Release_052619.pdf.

9 Testimony of Jennifer Amann, Director, Buildings Program, American Council for an Energy Efficient Economy, U.S. Senate Energy and Natural Resources Committee hearing, "To Provide Recommendations for Reducing Energy Consumption in Buildings," February 26, 2009, available at http://energy.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=672e1daf-bcc8-6e90-6e55-f95a8889b65e&Witness_ID=1de485cb-f55d-4bc2-872f-753318ccfc8.

10 Third Way calculation using data from the Energy Information Administration, "Electric Power Monthly," Table 5.3, May 15, 2009, available at http://www.eia.doe.gov/cneaf/electricity/epm/epm_sum.html.

11 Third Way calculation using data from the Energy Information Administration, "Electric Sales and Revenue 2000," Table 1, January, 2002, available at <http://tonto.eia.doe.gov/FTPROOT/electricity/054000.pdf> and Energy Information Administration, "Electric Sales, Revenue, and Average Price 2007," Table 5, January, 2009, available at http://www.eia.doe.gov/cneaf/electricity/esr/esr_sum.html.

12 ENERGY STAR, "Central Air Conditioners," available at http://www.energystar.gov/index.cfm?c=cac.pr_central_ac.

13 ENERGY STAR, "Save Money and More with ENERGY STAR Qualified Heat Pump Water Heaters," available at http://www.energystar.gov/index.cfm?c=heat_pump.pr_savings_benefits.

14 Payback rates for air conditioners vary based on local cost and cooling hours. The payback period for heat pump water heaters has been estimated to be approximately three years. ENERGY STAR, "Central Air Conditioners," available at http://www.energystar.gov/index.cfm?c=cac.pr_central_ac and ENERGY STAR, "Save Money and More with ENERGY STAR Qualified Heat Pump Water Heaters," available at http://www.energystar.gov/index.cfm?c=heat_pump.pr_savings_benefits.

15 Joint Committee on Taxation, "Estimated Budget Effects of the Revenue Provisions Contained in the Conference Agreement for H.R. 1, the American Recovery and Reinvestment Act of 2009," February 12, 2009, available at <http://www.jct.gov/x-19-09.pdf>.