April 15, 2015

The Honorable Orrin Hatch, Chairman
The Honorable Ron Wyden, Ranking Member
Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

Re: Energy-Efficiency Tax Incentives

Dear Chairman Hatch and Ranking Member Wyden:

On behalf of the A. O. Smith Corporation, I thank you for your continued bipartisan effort to revise the U.S. tax code to promote simplification, fairness, and efficiency. A. O. Smith shares these policy goals and provides the following comments in an effort to improve Section 25C of the tax code, which as currently structured, insufficiently promotes Congress's goal of stimulating investment in energy-efficient residential equipment.

A. O. Smith is one of the world's leading manufacturers of residential and commercial water heating equipment. The Corporation is a global leader in applying innovative technology and energy-efficient solutions to products marketed in more than 60 countries around the world, including solar, heat pump, and gas hybrid water heaters, along with the highest efficiency residential gas storage water heaters on the market. Consequently, A. O. Smith is uniquely qualified to comment on the impact that Section 25C plays in the marketplace, and we look forward to discussing our perspective as the Committee's tax reform process evolves.

Congress originally intended Section 25C to provide a tax credit "for certain energy-efficiency improvements … [that] will reduce national energy consumption."[1] Congress recognized that "residential energy use for heating and cooling represents a large share of national energy consumption," and accordingly believed that these measures "have the potential to substantially reduce national energy consumption." The final version of the law included specified credits for air circulating fans, furnaces and water boilers, and water heaters.[2]

A. O. Smith believes that Section 25C as currently structured no longer promotes the goals that motivated Congress to adopt the provision in the Energy Policy Act of 2005. This is because: (1) the credit's criteria creates an un-level playing field (advantaging foreign-manufactured products over domestically-manufactured products) by allowing the same credit for mid-efficiency imported heaters that is only available to much higher efficiency domestically produced heaters; (2) the amount of the credit is too low to influence purchasing behavior, particularly considering the credit's

[1] U.S. House, Committee on Ways and Means, Enhanced Energy Infrastructure and Technology Tax Policy Act of 2005, (to accompany H.R. 1541), (109 H. Rpt. 45), page 39.

[2] Joint Committee on Taxation. General Explanation of Tax Legislation in the 109th Congress, JCS-1-00 (January 17, 2007), page 56.

"lifetime cap" on homeowners who make qualifying purchases of eligible products; and (3) the tax credit has typically been extended at the end of each year, if at all, providing no certainty to consumers. Retroactive extension, such as occurred at the end of 2014, cannot influence a consumer to make an energy-efficient purchasing decision, but merely provides "free ridership" for purchases already made.

Congress can address at least some of these inadequacies in the current structure of Section 25C for water heater manufacturers by placing all such manufacturers on a level playing field. To do so, A. O. Smith recommends, at a minimum, amending the eligibility criteria for Section 25C for residential energy property expenditures, including water heaters and boilers. Legislation introduced near the end of the 113th Congress by Representatives Mike Kelly (R-PA) and Ron Kind (D-WI) (H.R. 5775, the "Powering American Jobs Act of 2014"), would accomplish that objective in a budget-neutral manner. A. O. Smith supports this bipartisan effort to address existing shortfalls in the eligibility criteria for Section 25C which would make the energy factor (EF) requirement equitable for all types of water heaters and boilers.

The criteria amendments in H.R. 5775 will provide limited, narrow improvements to Section 25C in its present form. Notwithstanding these modest amendments, which should be implemented as a matter of policy in any extension of Section 25C, Section 25C will continue to fail to meaningfully incentivize consumers to purchase high-efficiency water heaters if the allowable percentage and dollar amount of the credit are not addressed.

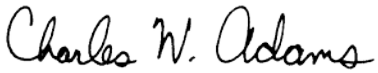
For these reasons, and as an alternative to the Section 25C, A. O. Smith believes that the best path forward for energy-efficiency tax credits is the "whole home" approach to incentivizing homeowners to make energy-efficiency improvements embodied in the Section 25E proposal that was introduced by Senators Cardin, Feinstein, and Schatz respectively in the 113th Congress (see S. 2189, The Energy Efficiency Tax Incentives Act.) That proposal represents a performance-based tax credit that incentivizes a "whole home" approach that would promote innovation, provide consumers with more choice, create American jobs, and increase the competitiveness of American manufacturers.

As proposed, , Section 25E would provide verifiable energy-efficiency gains, only rewarding consumers once they have reached a minimum of 20% energy savings, and provide incentives on a sliding scale based on the amount of energy savings actually realized. This performance-based credit will encourage significant energy savings and ensure the greatest savings per tax credit dollar, as opposed to Section 25C which prescribes specific measures and provides credits not on the basis of energy savings, but on the cost of the prescribed measures.

Importantly, Section 25E will ensure that more domestically-manufactured water heaters can qualify for tax credits and level the playing field for American manufacturers, while also providing the greatest incentive for the most energy-efficient products on the market. This is a far superior alternative than an extension of current law or even a narrow amendment to Section 25C's eligibility criteria.

A. O. Smith urges the Committee to consider amending the current tax code to include Section 25E and looks forward to working with the Committee to ensure that the tax code continues to promote Congress's original vision for stimulating consumer investment of energy efficient products in 2015 and beyond.

Sincerely,



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