



UNDERSTANDING THE
FEDERAL TAX INCENTIVES
FOR COMMERCIAL
GEOHERMAL HEAT PUMPS

JANUARY 2026



 **YORK**[®]

Available Federal Tax Incentives

Thirty Percent Investment Tax Credit (ITC)

The Inflation Reduction Act² (IRA) of 2022 introduced major updates to existing clean energy tax credit incentives. Section 48 of the Internal Revenue Code (Code) provides investment tax credits (ITCs) for qualified energy property, including geothermal heat pumps (GHPs). Tax-exempt entities, as well as state, local, and tribal governments remain eligible for direct payment of the ITC. For-profit entities that meet certain requirements under the Code can also transfer or sell their ITCs to other taxpayers with available tax capacity.

The One Big Beautiful Bill Act (OBBBA), signed into law on July 4, 2025, enacted certain changes in respect of the ITCs available with respect to GHPs.

Ten Percent Credit for Domestic Content Projects

The ITC provides a 6% base credit, which can increase to 30% if specific requirements are met. Geothermal projects under 1 MW (approximately 284 tons) automatically qualify for the full 30% credit. Projects exceeding 1 MW must satisfy prevailing wage and apprenticeship requirements to receive the 30% rate; otherwise, they are limited to the 6% base credit. To qualify for the GHP ITC, construction must begin before January 1, 2035. The base credit begins to phase out for property beginning construction in 2033 and 2034: a 5.2% base credit in the case of property beginning construction in 2033 (for a maximum full credit percentage of 26%) and a 4.4% base credit in the case of property beginning construction in 2034 (for a maximum full credit percentage of 22%). Please consult tax professionals for individualized guidance on this subject.

Ten Percent Credit for Energy Communities

The Energy Community bonus tax credit is for clean energy development in communities that have been sites of legacy energy production. The Energy Community bonus tax credit is 10% for projects less than 1MW. The bonus credit is 2% for larger projects unless the apprenticeship and prevailing wage requirements are met. The credit also applies to tax-exempt entities, state, local and tribal governments. The IRA defines energy communities as:

- A brownfield site (as defined in certain subparagraphs of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA))
- A “metropolitan statistical area” or “non-metropolitan statistical area” that has (or had at any time after 2009) 0.17% or greater of direct fossil fuel employment or 25% or greater local tax revenues related to the extraction, processing, transport, or storage of coal, oil, or natural gas; and has an unemployment rate at or above the national average unemployment rate for the previous year
- A census tract (or directly adjoining census tract) in which a coal mine has closed after 1999; or in which a coal-fired electric generating unit has been retired after 2009

The following QR codes are linked to useful mapping resources for Energy Communities. Please consult tax professionals for individualized guidance on this subject.

U.S. Department of Energy - Energy Community Tax Credit Bonus



Coal Power Plan Redevelopment Visualization Tool



American Clean Power - IRA Energy Communities



Available Federal Tax Incentives

Leasing of Geothermal Systems

Section 70513 of the OBBBA provides for a determination of the ownership of GHP property without regard to whether it is readily usable by a person other than the lessee or service recipient. Although the IRS has not yet published interpretative guidance with respect to this provision of the OBBBA, this change will likely expand GHP ownership and financing flexibility within the market. Please consult tax professionals for individualized guidance on this subject.

Accelerated Depreciation of Energy Property

Section 70509 of the OBBBA eliminates five-year cost recovery for geothermal heating and cooling systems. Previously, commercial geothermal systems qualified for five-year accelerated depreciation.

The OBBBA also makes 100% bonus expensing permanent for eligible property placed in service beginning in the first taxable year ending after January 19, 2025. Property with a class life under 20 years qualifies, but eligibility for bonus expensing and accelerated depreciation depends on ownership structure and system details. Please consult tax professionals for individualized guidance on this subject.

Tax Deduction for Energy-Efficient Commercial Building Property

This energy-efficient commercial building tax deduction applies to new and existing buildings that have been completed since Jan. 1, 2006. The buildings must meet certain American Society of Heating, Refrigerating, and Air Conditioning Engineers (ASHRAE) efficiency standards to qualify. It allows for a tax deduction in the year the property is placed in service. The deduction can be up to \$5.81 per square foot for projects meeting prevailing wage and apprenticeship labor requirements with the amount depending on reduction of total annual energy and power costs for the building. With for-profit businesses, the deduction can be taken by the building owner. The deduction includes buildings owned by not-for-profits, instrumentalities, and Indian Tribal Governments. For not-for-profit organizations, the deduction can be taken by the designers of these buildings.

Section 70507 of the OBBBA terminates the energy efficient commercial buildings tax deduction for projects that begin construction after June 30, 2026. Please consult tax professionals for individualized guidance on this subject.

Who's Eligible for the Federal Geothermal Incentives?

Equipment that uses the ground or ground water as an energy source for heating and cooling a building is eligible for the Code Section 48(a) tax credit. The system must be in the United States and the tax incentives can benefit for-profit or not-for-profit organizations. After equipment is installed, the taxpayer must take legal title of the equipment and have all necessary licenses and permits needed for its operation.

How to Claim These Tax Advantages

Use IRS Form 3468 to claim the ITC. The Section 48 tax credit can be used to offset both regular income taxes and alternative minimum taxes (AMT). If the tax credit exceeds the income tax liability, the loss can be carried back 3 taxable years and the remaining balance can be carried into future years.

Commercial building owners can take the energy efficient commercial buildings tax deduction for building projects completed since Jan 1, 2006 and which have begun construction by June 30, 2026. A standard form for this deduction will be available within IRS Form 7205 and to claim this deduction, use the "Other" deduction line on such form. IRS Form 3115 is used for catch-up on all prior year unclaimed energy-efficient commercial building tax deductions. Designers of government projects must amend prior year returns and can only adjust the prior 3 years.

Please consult tax professionals for individualized guidance on this subject.

Projects completed with a geothermal loop and heat pumps may qualify for:

- **to 30%** credit on system cost
- **Up to 10%** credit for domestic content
- **Up to 10%** credit for energy communities
- **Up to \$5.81 per square foot** tax deduction¹



New construction example

A corporation installs a geothermal HVAC system at a cost of \$1,500,000 in its new office building.

Geothermal HVAC Cost	Tax Rate	
\$1,500,000	21%	

	Year	
WITH TAX INCENTIVES	0	1
30% Tax Credit		\$450,000
10% Domestic Content		\$150,000
10% Energy Community		\$150,000
Total Tax Incentive		\$872,850
% paid for by Tax Incentives in 1st year	50%	

For this example, the project meets the requirements for prevailing wage, apprenticeship, domestic content and energy communities. A 2023 project example with the tax rules of 2025 applied.

Retrofit construction example

A corporation has an existing building that uses a water-loop heat pump system with a boiler and cooling tower. They remove the existing boilers and cooling tower and install a backup boiler for \$100,000. They install a geothermal heat exchange loop and upgrade their heat pumps to high-efficiency geothermal models with a total cost basis for the system of \$1,000,000.

Boiler	Geothermal HVAC Cost	Tax Rate
\$100,000	1,000,000	21%

	Year	
WITH TAX INCENTIVES	0	1
30% Tax Credit		\$300,000
10% Domestic Content		\$100,000
10% Energy Community		\$100,000
Value of 15 year QIP for Boiler		\$420
Total Tax Incentive		\$500,420
% paid for by Tax Incentives in 1st year	45.49%	

For this example, the project meets the requirements for prevailing wage, apprenticeship, domestic content and energy communities. A 2023 project example with the tax rules of 2025 applied.





ASK US HOW YOU CAN SAVE UP TO 50% ON YOUR NEXT COMMERCIAL PROJECT WITH THE FEDERAL GEOTHERMAL INCENTIVES.

1. Expires June 30, 2026
2. Additional benefits are available under the Inflation Reduction Act and are not covered in this brochure. The Federal tax credits may be combined with utility rebates and other tax incentives.

Statements in this document are being finalized by the federal government and are subject to change and interpretation. To understand what you qualify for, please consult your tax professional.

Sources: Energy Tax Savers, Inc., Geothermal Exchange Organization the Inflation Reduction Act of 2022, and the One Big Beautiful Bill Act of 2025.

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