Congress's Tax Incentives Send Mixed Signals for Automobile Buyers: Should Americans Buy Gas Guzzlers or Hybrids?

Bradley A. Ridlehoover
CONGRESS'S TAX INCENTIVES SEND MIXED SIGNALS FOR AUTOMOBILE BUYERS: SHOULD AMERICANS BUY GAS GUZZLERS OR HYBRIDS?

BRADLEY A. RIDLEHOOVER*

INTRODUCTION

I want to introduce you to four individuals, Amy ("A"), Billy ("B"), Charlie ("C"), and Doris ("D"), who are all interested in purchasing a new car. Each individual is in the process of researching different makes and models, prices, and possible taxes involved with their purchases. A is an environmentally-conscious individual who owns her own business and is only looking for a car that is safe for the environment. B is a 22 year-old recent college graduate who has started his own real estate business, has a love for sport utility vehicles, and believes the bigger the better when it relates to vehicles. C is also a small business owner who does not have a strong preference as to the type of car he buys, but is very interested in making the right financial decision with the optimum tax consequences. D is also a recent college graduate who will be commuting alone to work daily and needs to purchase a vehicle for personal use. A, B, and C will be using their vehicles for over 50% business purposes. D will use her vehicle for 100% personal use. Each of the four individuals has different factors weighing on their decisions to purchase a vehicle, but the crucial question is whether Congress has a desire to affect their respective decisions through legislative incentives and disincentives.

Studies have shown that, in the United States, a high percentage of commuters drive to work alone.1 With high levels of commuters comes

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Bradley A. Ridlehoover is a 2008 J.D. candidate at the William & Mary School of Law. Mr. Ridlehoover received a B.S. in Accounting and a B.A. in Political Science from Presbyterian College in South Carolina. The author would like to thank Professor Erin Ryan of the William & Mary School of Law for her help in finding a topic and for reviewing drafts of this Note. In addition the author would like to thank Professors Sam L. Howell, Dr. Ronald R. Raber II, and Dr. Jonathan C. Smith of Presbyterian College and attorney W. Andrew Arnold for their time in reviewing drafts and making great suggestions. Finally, the author would like to thank the editorial staff for all their support, assistance and time in preparing this Note for publication.

1 Roberta F. Mann, On the Road Again: How Tax Policy Drives Transportation Choice, 24 VA. TAX REV. 587, 588 (2005) ("In the United States, almost 80% of commuters drive
an increased demand for vehicles, as well as increased fuel consumption.
When commuters decide which vehicle they want to drive, they must be
thinking not only of the vehicle’s purchase price, but also about current
and future fuel costs. It is not uncommon for news articles focusing on the
price of gasoline to include headlines like *Shocker at the Pump: Will Gas
Reach $3 a Gallon*? or *Gas Prices on the Rise*.\(^3\) Having such a high percen-
tage of commuters drives an increase in the amount of fuel needed and
consumed in the United States.

Commentators believe that the United States is more dependent
on foreign oil than ever.\(^4\) In 2005, President Bush remarked that “most
of the serious problems, such as high gasoline costs or the rising depend-
ence on foreign oil, have developed over decades.”\(^5\) This fact would prob-
ably not have much influence on A’s decision as she is environmentally
conscious, nor would it have much of an impact on B, who is more con-
cerned with image. But it would impact C and D, who are focused on
financial considerations.

Increasing the fuel efficiency of vehicles is one way to decrease
dependency on foreign oil.\(^6\) Environmental groups, including the Sierra
Club, have expressed opinions on the issue, including the belief “that hybrid
electric vehicles (“HEVs”) and fuel cell vehicles are the best solutions to
global warming and air pollution.”\(^7\) Unfortunately, the cost of these HEVs
can be significantly more than the cost of traditional gasoline-powered

\(^2\) Tom Hanson, *Shocker at the Pump: Will Gas Reach $3 a Gallon?*, NAPLES DAILY
_pump_will_gas_reach_3_gallon (describing how, in a matter of seven days, gas prices in
the United States rose twenty cents in March 2007 due to higher crude oil prices, pressure
on refineries, and uncertainty in the United States). “[T]he highest prices [of gasoline]
of the year are normally between Memorial Day and Labor Day, which are known as the
summer driving months.” Id.

http://www.aikenstandard.com/homepage/288315201395584.php (indicating that mul-
tiple factors are causing the increase in fuel prices, including unrest in the Middle East,
in particular with Iran, and that refineries cut back production for maintenance); see also
phoenix.bizjournals.com/phoenix/stories/2007/02/26/daily39.html (indicating that one rea-
son the price of gasoline increases is the yearly switch to warm-weather blends of gasoline).

\(^4\) Heather Munoz, Comment, *The Clean-Fuel Vehicle Tax Deduction: Will it Drive an
States’ dependence on foreign oil sources is currently the highest in history.”).

\(^5\) Statement by President George W. Bush Upon Signing H.R. 6, 2005 U.S.C.C.A.N. S17,
S23 (Aug. 8, 2005).

\(^6\) Munoz, *supra* note 4, at 116.

\(^7\) Id. at 116-17.
To combat this price discrepancy, Congress has enacted tax incentives to encourage the purchase of environmentally-friendly automobiles. A tax incentive would be beneficial to A even though she is going to purchase this vehicle anyway, and will influence C if this is the most financially beneficial option. D, however, is the taxpayer Congress most wants to influence. D will not receive any special deduction for her daily commute and the car will be purchased entirely out of her own pocket. A tax incentive could potentially change D's choice.

Contemporaneously with the enactment of green tax incentives, Congress has counter-intuitively failed to reduce opportunities for taxpayers to also receive significant tax benefits for purchasing certain sport utility vehicles ("SUVs"). If Congress does not act, not only will B receive the most beneficial results, but C might purchase an SUV because of the greater tax benefits, even though there is a greater harm to the environment. D cannot take advantage of the SUV tax loophole because D is not a business owner; however, he might not desire to spend money on a hybrid without some type of incentive.

This Note argues that the environmentally-conscious policies of providing tax incentives for individuals who purchase fuel efficient cars are being limited by Congress's failure to remove the SUV tax loophole for small businesses and self-employed individuals. The environmental policy of the United States should send the same message to all taxpayers: that the United States desires to encourage the purchase of fuel efficient vehicles. In order to send a unified message, Congress must reevaluate the two

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8 See Eric Powers, Which Hybrid Car is Right for You?, ABOUT.COM, http://newautos.about.com/od/cars/a/whichhybridsep04.htm (last visited Oct. 22, 2007) (listing the prices of different hybrid vehicles and stating that hybrids cost between three and five thousand dollars more than non-hybrids).
10 A, B, and C may be able to deduct expenses for the purchase of their vehicles because they are small business owners, see infra Part III, but D cannot take advantage of these special deductions.
12 See infra Part IV.
provisions which provide the tax benefits, sections 30B\textsuperscript{13} and 179\textsuperscript{14} of the Internal Revenue Code, and enact legislation that will eliminate the mixed message being sent to individual taxpayers.

Part I of this Note provides the background for these conflicting provisions and explains how a hybrid vehicle operates and the benefits it can provide. In addition, this part examines the policy of enacting legislation that attempts to influence consumer choice when purchasing a vehicle. Part II outlines the current law that provides tax credits for the purchase of HEVs. It also shows how certain provisions of the Internal Revenue Code, such as the alternative minimum tax, affect the green tax incentives and set up the potential for wasting unused credits. This part also provides a background on prior law that allowed for a deduction to be taken instead of a tax credit, and how the switch in policy resulted in an array of different consequences to certain taxpayers.

While the previous part focuses on the green tax incentives, the following part examines the SUV tax loophole. Part III addresses the background, intent, and benefit of this loophole.

Part IV will compare the two tax incentives and discuss why their existence is important. This part addresses how tax incentives are factors that influence the consumer choices of individuals, and also the environmental concerns that make green tax incentives important considerations in enacting policies.

Next, Part V will introduce other provisions the federal government and states have introduced to encourage the use and purchase of hybrids. Finally, Part VI will provide recommendations for changing the law to allow for a unified policy goal of encouraging individuals to pursue environmentally-friendly vehicles.

I. BACKGROUND

A. What Is a Hybrid?\textsuperscript{15}

Although many people own hybrids, questions still remain: what makes a hybrid different from a traditional gasoline-powered vehicle

\textsuperscript{13} I.R.C. § 30B (West. Supp. 2007).
\textsuperscript{14} I.R.C. § 179 (West, Westlaw through 2007 amendments).
\textsuperscript{15} See Instructions, I.R.S. Form 8910, at 2 (2006) ("[A qualified hybrid vehicle] is a vehicle that draws propulsion energy from onboard sources of stored energy that are both an internal combustion or heat engine using consumable fuel and a rechargeable energy storage system and that meets certain additional requirements.").
and how does it actually work? Hybrid vehicles merge small combustion engines with an electric battery and motor.\textsuperscript{16} Hybrid cars are different from pure electric cars. “Unlike pure electric cars, [hybrids] never have to be plugged in. During braking or coasting, energy that would have been wasted recharges the battery.”\textsuperscript{17} The benefit of combining these two technologies is to “reduce fuel consumption and tailpipe emissions.”\textsuperscript{18} In a traditional gasoline-powered car, energy is lost during braking, while in a hybrid this energy can be captured and returned to the battery, in a process called “regenerative braking.”\textsuperscript{19} Furthermore, “[a] hybrid engine also operates more efficiently and produces less pollution than does combustion alone.”\textsuperscript{20} The five steps to identify the different classifications among hybrids are: 1) idle-off capability, 2) regenerative braking capacity, 3) power assist and engine downsizing, 4) electric-only drive, and 5) extended battery-electric range.\textsuperscript{21}

Advantages to owning a hybrid vehicle include the reduction in air and global warming pollution.\textsuperscript{22} Other advantages include high performance and range. With respect to global warming, hybrids consume less fuel than a traditional gasoline-powered vehicle.\textsuperscript{23} In particular, “[t]he first hybrids on the market will cut emissions of global warming pollutants by a third to a half.”\textsuperscript{24} Regarding range, having an electric powered battery in addition to a combustion engine allows cars, like Honda’s Insight, to run about 700 miles on one tank of gas.\textsuperscript{25} This is a significant difference compared to the range of miles a traditional vehicle can travel.

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\textsuperscript{17} Kathleen Pender, Hybrid Cars Draw Attention, S.F. CHRON., Mar. 2, 2003, at 11.
\textsuperscript{18} Hybrid Electric Vehicles, supra note 16.
\textsuperscript{19} Id.
\textsuperscript{20} Id.
\textsuperscript{21} Id.
\textsuperscript{22} Union of Concerned Scientists, Hybrid Center, How Hybrid Cars Work: Under the Hood, http://www.ucsusa.org/hybrid-center-how-hybrid-cars-work-under-the-hood.html (last visited Oct. 22, 2007). Once a hybrid car reaches step number three it is considered a “mild” hybrid. After reaching step number four, it is a “full” hybrid. Finally, if the hybrid reaches step five it is classified as a “plug-in” hybrid. Id.
\textsuperscript{23} Id.
\textsuperscript{24} Id.
\textsuperscript{25} Id.
Conversely, the disadvantages to owning a hybrid include higher costs and limited market availability. With the new technology, hybrids generally cost more than a traditional vehicle of a similar type, and there are not as many choices among the different hybrids. However, more models and different types of vehicles are being offered each year by different manufacturers. Some experts estimate that by the year 2010, manufacturers will have at least fifty different types of hybrids available in North America with a possible production of one million vehicles.

B. National Policy, Hybrid Vehicles and the Tax Combination

The benefits of hybrid vehicles seem to be music to the ears of environmentalists, but there remains a need to combat the disadvantages listed above. President George W. Bush stated,

For more than a decade, America has gone without a national energy policy . . . . We haven't had a strategy in place. We've had some ideas, but we have not had a national energy policy. And as a result, our consumers are paying more for the price of their gasoline . . . . And because we didn't have a national energy strategy over time, with each passing year, we are more dependent on foreign sources of oil.

\[\text{See id. ("Hybrids should be competitively priced when all the costs over the life of the vehicle are included. This is because any cost premium is likely to be offset by fuel savings.").}\]

\[\text{See Internal Revenue Service, Summary of the Credit for Qualified Hybrid Vehicles,}\]


\[\text{Corporate Average Fuel Economy: Hearing Before the Subcomm. on Commerce, Surface Transportation and Merchant Marine Infrastructure, Safety, and Security, 109th Cong. (2006) (statement of Frederick L. Webber, President and CEO, Alliance of Automobile Manufacturers) ("Automakers are committed to being first to market with breakthrough technologies that can produce new generations of autos with advanced powertrains and fuels . . . . Each year many new advanced technology models are offered on dealer lots.").}\]

\[\text{Id.}\]

In order to combat this problem, on August 8, 2005, President Bush signed the Energy Policy Act of 2005 into law. President Bush stated that this bill is “a first step toward a more affordable and reliable energy future for the American citizens. This bill is not going to solve our energy challenges overnight.” The bill focuses on allowing the United States to use other domestic energy sources like coal, nuclear power, oil, and natural gas. The bill also includes tax credits for installing energy efficient windows in American homes and for purchasing hybrid vehicles.

Automakers, including Ford, General Motors, Honda, and Toyota, all produce vehicles that qualify for the tax credits, but each vehicle has a different credit amount. Offering a tax credit for the purchase of hybrid vehicles furthers the national energy policy because hybrids produce fewer emissions and use less fuel than their gasoline-powered counterparts. This is because hybrids have both electric motors and gasoline-powered engines, which results in greater fuel efficiency.

Although the hybrids significantly reduce the costs of purchasing gasoline, looking long-term it is uncertain whether one can actually save money by purchasing a hybrid, as the price of a hybrid is about one-third more than a similar gasoline-powered vehicle. Without some incentive, such as a tax credit, pushing a buyer in a certain direction, the question for A, B, C, and D as to what type of vehicle would be their best choice continues to linger.

When evaluating the overall benefits of owning a hybrid, taxpayer A is not going to be ultimately concerned with whether the potential reduction in other costs, like fuel and maintenance, outweigh the higher costs of the vehicle; but taxpayers C and D are going to look to the potential reductions in costs over the long-term in addition to the higher initial capital.

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32 See id. at S17.
33 Id. at S23.
34 Id. at S21.
35 Id.
37 See Mann, supra note 1, at 631.
38 Id.
39 Pender, supra note 17, at 11 (discussing how hybrids get seventy percent better gas mileage in the city compared to gasoline only models and fifteen to twenty percent better mileage on the freeway).
It is possible that an individual might not be able to overcome the idea of later savings from buying a hybrid (i.e. lower fuel costs) because of the greater outlay of cash up-front, even though in the end overall savings may be greater.\(^4\)

Business concerns may also affect whether a business owner will purchase a hybrid vehicle for business purposes. Businesses are accountable to their shareholders. As a result, they may not be affected by or concerned about the damage caused by the use of traditional gasoline-powered vehicles, but may only be concerned about their responsibilities to bring returns to shareholders. On the other hand, environmentally-conscious shareholders may influence businesses in the opposite direction. Also, for a larger corporation, different environmental groups, like the Sierra Club, might attempt to lobby the company to pursue actions that benefit the environment.

In the cases of A, B, and C, each are business owners, but they are all sole owners. The only shareholder each will have to answer to is himself or herself. As indicated above, A will be concerned with the environmental ramifications, and her choice is already made as to which vehicle suits her and the environment’s needs the best. As for B and C, without other environmentally-conscious shareholders influencing them, they might not attempt to pursue green alternatives. On the other hand, an individual like D only has to answer to herself or her family and might not have many outside influences on her decision making.

Thus, incentives may be necessary to promote the use of hybrid vehicles. Although the primary purpose of the tax code is to generate revenue for the United States, at times the code is used to accomplish Congress’s social or economic goals.\(^4\) The action of Congress in passing legislation like the Energy Policy Act of 2005 points toward Congress being

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\(^4\) See Powers, *supra* note 8 (listing the prices of different models: 2006 Honda Insight—$21,530; 2006 Toyota Prius—$21,275; 2006 Honda Civic Hybrid—$21,850; 2006 Ford Escape—$28,595 (4WD); 2006 Mariner Hybrid—$29,840 (4WD); and 2006 Toyota Highlander Hybrid—$34,430 (4WD)).

\(^4\) See Posting of Jennifer to Go Hybrid Blog, http://go-hybrid.info/blog/2007/01/15/hybrid-cars-mean-overall-saving-on-cashhow/ (Jan. 15, 2007, 17:07 EST) (discussing how hybrids are more cost-effective than gasoline-powered vehicles when compared over a five year and 70,000 mile period, which results from savings in fuel costs, federal tax credits, license fees, and moderate maintenance costs).

\(^4\) Mann, *supra* note 1, at 620 (“Most would agree that the federal income tax system primarily exists to provide revenue for the federal government, but it also generally is accepted that the federal income tax system has been frequently used to accomplish both economic and social goals.”).
in the business of using tax incentives to shape national policy. In addition to the passage of this Act, individual Senators and Representatives in Congress are proposing bills that will increase the possibility of further tax cuts or credits, as well as extending those already enacted with more flexibility.43

II. THE "GREEN" TAX INCENTIVES

A. Tax Credit Options

1. Electric Vehicles

The Internal Revenue Code provides tax credits for electric vehicles in section 30,44 and it also provides for credits for four different types of vehicles in section 30B: advanced lean-burn technology vehicles, qualified hybrid vehicles, qualified alternative fuel vehicles, and the qualified fuel cell vehicles.45 Although the tax credit for electric vehicles has been phased out completely for vehicles put into service after December 31, 2006,46 it arguably helped establish electric cars as a potential alternative to gasoline-powered vehicles.

Section 30 provided a tax credit for purchasers of electric cars equal to ten percent of the cost of the vehicle.47 This credit was limited to a maximum of $4,000,48 and was subject to a phase-out as outlined in the Internal Revenue Code.49 The Code defines a qualifying vehicle as "any motor vehicle which is powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electrical current, the original use of which commences with the taxpayer, and which is acquired for use by the taxpayer and not for resale."50 Not many vehicles included in this category are readily available for the current public market. There are at least two car makers who view this as a high-end niche

43 See infra Part V.
44 I.R.C. § 30 (West Supp. 2007).
45 Id. § 30B.
48 Id. § 30(b)(1).
50 Id. § 30(c)(1).
market and are trying to bring these electric cars to production, but other attempts by manufacturers, like General Motors, have failed.

2. Section 30B Credits Including Hybrid Vehicles

Congress provided the tax credits for the four types of vehicles classified in section 30B of the Internal Revenue Code with the enactment of the Energy Policy Act of 2005. The Senate articulated the reason for the passage of the Energy Policy Act by stating:

It is the policy of the United States to reduce dependence on imported oil through increased efficiency and diversification of fuel sources through dramatically expanded use of clean alternative fuels. Such a reduction will increase the foreign policy flexibility of the United States, make the United States less vulnerable to oil supply disruption, and promote economic growth. The United States will continue to promote research and development of a range of alternatives fuels, and it will implement policies to accelerate the deployment and commercialization of existing efficiency and alternative fuels technologies.

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52 Both Tesla and Wrightspeed indicate that the technology will eventually trickle down to lower priced vehicles. As one blogger succinctly states, "Clearly, neither Wrightspeed nor Tesla are looking to sell to the hoi polloi, though each company claims to be making technological advances in electric vehicles that will eventually filter down to more mass-market models—probably manufactured by others." Posting of Joel Makower to Huffington Post Blog, Who's Reviving the Electric Car?, http://www.huffingtonpost.com/joel-makower/whos-reviving-the-electr_b_24549.html (July 7, 2006, 2:32 EST).


The position of many of the automakers is that the credit was enacted to jump-start the market and provide initial incentives to create a buzz for the purchases of these alternative fuel vehicles. Automakers are also concerned that the provisions that are enacted must remain "technologically neutral," not favoring one type of alternative fuel technology over the other. In order to receive a credit under any of the provisions referenced above, taxpayers have to input this information on their federal tax returns.

3. The Process for Filing for the Credit

In order to receive the tax credit, when filing an individual tax return the taxpayer would have to file Form 8910, "Alternative Motor Vehicle Credit," and include it with Internal Revenue Service ("IRS") Form 1040. For the taxpayer to be eligible to receive a credit, the vehicle must have been put into service after 2005. If it was used for business or investment purposes it will be treated as a business credit; but if not, it will be treated as a personal credit. For the vehicle to be classified as a qualified hybrid vehicle and to be able to count as a credit on a tax return, the vehicle must comply with the IRS definition of a hybrid.

55 See Kate Ackley, Proposal Sparks Battle Over Hybrids, ROLL CALL, May 9, 2006 (discussing Ford's spokesman Mike Moran's comments that "[w]e believe the advanced vehicle tax credits should provide a jump-start to attracting consumers to new technologies and assisting the market introduction . . . That was our position when legislation was proposed and enacted, and we're still consistent with that.").
56 See id. Dennis Fitzgibbons, director of public policy for DaimlerChrysler's Washington, D.C. office, has stated that his company has not entered the fray because they are not affected, as they do not have a qualifying vehicle. Id. The Alliance of Automobile Manufacturers, a trade group that represents domestic and foreign manufacturers, is: generally supportive in principle of consumer tax credits for all alternative fuel vehicles, with the caveat that they be technology neutral . . . The alliance does not have an official position on removing the cap. It creates competitive issues among our members. The cap, as it now stands, was very carefully crafted.

58 Id. at 2.
59 Id. The individual can take part of the credit as a general business credit by filing IRS Form 3800 based on the percentage of business use. For A, B, and C this is at least 50%. For D, all would be personal and she could not use this form.
60 See id. (stating that a hybrid "draws propulsion energy from onboard sources of stored energy that are both an internal combustion or heat engine using consumable fuel and a rechargeable energy storage system and that meets certain additional requirements.").
Congress, when enacting the provision enabling this credit, stated that "the term 'qualified vehicle' means any new qualified hybrid motor vehicle (described in subsection (d)(2)(A)) and any new advanced lean-burn technology motor vehicle." With Congress inserting the word "new" into the language of the statute, it means that no credit will be allowed for someone who purchases a vehicle from anyone except the manufacturer.

Before the IRS will allow a taxpayer to consider what amount of the credit will be allowed, the Service requires that the taxpayer place the amount of tax calculated under the traditional method on Form 1040 and then deduct the foreign tax credit, other credits on Form 1040, and the credit for qualified electric vehicles. After this calculation, any amount of the tax that remains is reduced by the minimum tax required under the alternative minimum tax from IRS Form 6251. Then, the smaller of the applicable credit or the remaining tax available will be applied to the overall amount of taxes owed. The tax credit is non-refundable, which means that, while it can reduce an individual's income tax liability to zero, it will never result in any of the disallowed credit being returned to the taxpayer.

For example, assume taxpayer A owed a tax of $5,000 before any credits were applied. Also, assume that taxpayer A had $3,500 of foreign tax credits applicable to other investments she held and was not subject to the alternative minimum tax. If A decided to purchase a 2006 Ford Escape, which has a $2,600 tax credit available, she would only recognize $1,500 of the credit. Any portion of the credit that is disallowed because of the limitation mentioned above cannot be carried to previous or future tax years. Due to the nature of the credit, even though A thought she would receive a $2,600 credit, she lost $1,100 due to other circumstances. This makes the calculation up-front difficult to determine for taxpayers who are unsure of their income. Taxpayer C or D might not be willing to purchase the hybrid because he or she could not be certain of the benefits.

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63 See id. lines 16-18.
64 I.R.S. Form 8910 lines 17-18; see infra Part II.C (regarding the effects of the alternative minimum tax on credits and how individuals who expect to receive a benefit from the tax might lose the possibility based on the adjusted gross income).
67 See Instructions, I.R.S. Form 8910, at 4.
In preparation for these tax credits, Congress estimated that "$874 million in 'alternative-technology vehicle' tax credits have been set aside for consumers." The amount of the credit allowed is based on the make and model of the vehicle. The one time credit ranges from about $250 to $3,000 per vehicle.

4. The Phase-Out for the Tax Credit

The allowable credits for hybrid and advanced lean-burn technology vehicles have a limitation which will eventually lead to a complete phase-out of the credit based on the number of vehicles produced by the manufacturer. The Energy Policy Act of 2005 went through multiple revisions and amendments before enactment. The House of Representatives version contained a credit for advanced lean-burn technology, but not for hybrid vehicles. However, the Senate version of the bill provided tax credits for qualified fuel cell, qualified hybrid, and qualified alternative fuel motor vehicles. After both the House and the Senate passed the Energy Policy Act of 2005, the bill proceeded to conference. At this point a phase-out of the credit was installed, based on the number of vehicles manufactured by each car company. The car manufacturer must certify that it has reached the 60,000 limit of vehicles sold in the United States after December 31, 2005 in order for the phase-out to begin.

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69 See Instructions, I.R.S. Form 8910, at 3.
73 Id. § 1531 (engrossed Senate amendment).
74 See id. § 1316.
75 STAFF OF JOINT COMM. ON TAXATION, 109TH CONG., REPORT ON ENERGY TAX INCENTIVES ACT OF 2005, at 67 ("The conference agreement imposes a limitation on the number [of vehicles] . . . sold by each manufacturer . . . eligible for the credit."). This provision was the result of great compromise. See Ackley, supra note 55 ("The hybrid tax credit was a carefully negotiated compromise," said a lobbyist for one of the domestic auto manufacturers. We don't want a handout. Those of us who do hybrid or clean diesel, we just want some incentives to see if this technology will catch on in the marketplace.").
stated in a press release that the bill would benefit Michigan communities, claiming that the 60,000 per manufacturer cap “ensures that the domestic manufacturers can benefit from the tax credit to the same extent that foreign manufacturers can.” Senator Levin also discussed the importance of decreasing the dependence on foreign oil, but he was ultimately concerned with his own constituents when he stated, “These auto tax credits will help reduce our dependence on foreign oil and help the Big Three create jobs with these new emerging technologies.”

Toyota, a foreign manufacturer, has reached the limit of 60,000 vehicles, and its Prius, Highlander, Lexus GS 450, and Camry Hybrid are all affected by this reduction. In 2005, Toyota sold 107,897 Priuses while Honda only sold 43,356 of its hybrid vehicle. The credit will be reduced by 50% for the second and third calendar quarters after the quarter in which the production mark is reached, then by 25% for the following two calendar quarters, and will be reduced to no credit for all quarters thereafter. In addition to the cap, there is also a timed phase-out provision that ultimately wipes away the credit, as it provides that the credit cannot be claimed for any hybrid motor vehicle purchased after December 31, 2009.

5. Arguments For and Against the Phase-Out

The Bush administration entered the fray over the production phase-out when in April 2006 it asked Congress to remove the cap on the number of hybrid and clean-burning fuel vehicles eligible for the tax credit. This request met resistance and set “off a new round of infighting among automakers, pitting the ‘hybrid haves’ against the ‘hybrid haves’.”

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78 Id.
79 Mike Spector, Tax Credits to Fall on Some Hybrids, WALL ST. J., Sept. 26, 2006, at D2.
80 Schaefer, supra note 65; see also US Automakers Want End to Hybrid Credits (Marketplace Public Radio broadcast May 9, 2006) (transcript available at http://marketplace.publicradio.org/shows/2006/05/09/PM200605096.html) (discussing statements by Don McKenzie, representative from the Union of Concerned Scientists, indicating that the cap will give “GM and Ford an unfair advantage, allowing them to catch up with their rivals. While Ford is turning out maybe 20,000 hybrids a year, for example, Toyota is selling close to 60,000-vehicle cap.”).
82 Id. § 30B(j)(3).
83 Ackley, supra note 55.
have nots." The different manufacturers have voiced their opinions for Congress and President Bush to hear. The President of Toyota Motor North America, Jim Press, stated, "The cap should be raised for us to allow us to expand . . . . Demand for Prius declined when there was a step down in hybrid tax credits. We need to have a certain volume to get the mainstream in for economies of scale." Honda has taken a different stance on the credit than Toyota and weighed in with their uneasiness, which can be found in statements made by Honda's Senior Vice President of the United States division, John Mendel. Mendel stated, "I'm not sure it's a good deal . . . [because hybrids] are a bridge technology to something else." Another Honda executive, Vice President of Government and Industry Relations Edward Cohen, commented that the whole system is flawed due to the fact that the current credits are based on a car's city driving fuel economy instead of its highway rating. Cohen also mentioned that instead of capping the credit based on vehicles sold, it should be timed out.

The opposition to the raising of the cap can also be found in statements from many of the different domestic manufacturers. In a 2006 article in Roll Call, staff writer Kate Ackley stated that "because Toyota's competitors fear that increasing the cap will give only the industry's sales leader an additional leg up, the proposal has been met with widespread opposition. In fact, the internal split has forced the industry's trade association to stay out of the issue altogether." One domestic auto manufacturer lobbyist

84 Id.
86 Woodyard, supra note 85 (quoting John Mendel, Honda's Senior Vice President of the United States Division). Ford Motor Company and General Motors have also made statements supporting a credit extension if it is modified in some ways. Id.
87 Ackley, supra note 55.
88 Id.
89 Id.

Cohen also said that, if the cap remains in place, once Toyota and Honda have exhausted their tax credits, it will put them at a disadvantage to automakers that have not yet maxed out their caps because they were further behind in developing the technology . . . . 'We'll be going head-to-head against [companies] with a very large government subsidy.'

Id.

One lobbyist for a domestic automaker said that turning around and asking Congress to lift the cap—which was included in last year's Energy
said, "[W]ith a Congress focused on deficits, lifting the cap on tax credits may not be 'the best fiscal policy.' The reduction based on the production levels of manufacturers has been criticized by the Sierra Club. As of August 12, 2007, the largest credit available to a car buyer would be for the purchase of a 2008 Ford Escape Hybrid 2WD or a Mercury Mariner Hybrid 2WD, each carrying a credit of $3,000.

Looking back to the four hypothetical taxpayers, if A decided to purchase one of these vehicles, she possibly would receive a $3,000 credit against her tax liability. This would depend on other considerations discussed above, such as the foreign tax credit and alternative minimum tax. C and D would have to evaluate whether a credit of $3,000 is beneficial and worth the cost of the hybrid.

Other steps are being encouraged to increase the popularity of hybrids, including requiring the government to purchase these vehicles for its fleets. Some of the manufacturers would prefer the credit to be based on other considerations, such as gallons of gas saved. As the law stands, however, taxpayers who purchase other brands of hybrid vehicles will also see a reduction in available credit once the automaker reaches the 60,000 production mark.

B. Deduction for Clean-Fuel Vehicles

For all clean-fuel vehicles purchased before December 31, 2005, the tax credits mentioned in Part II.A are not effective. Instead, the taxpayer could have taken a deduction under section 179A. This deduction for the year the vehicle was placed into service was equal to the cost of the vehicle. However, the deduction was limited to $2,000 for vehicles

Policy Act after House-Senate negotiations—will upset fiscal conservatives and undermine the claims made last year by automakers that they simply needed a helping hand to attract customers to the new vehicle.

Id.  
90 Id.  
91 Funk & Jensen, supra note 68, at 31 ("It penalizes the automotive leaders and awards the laggards.").  
93 Woodyard, supra note 85.  
94 See Ackley, supra note 55.  
under 10,000 pounds. Unlike the current credit, the deduction would not have been affected by the foreign tax credit or the alternative minimum tax. This is because the deduction was what is called an "above-the-line write-off, which means it can be claimed regardless of whether you itemize deductions, reducing by $2,000 the amount of income that's subject to taxation." Looking back to Taxpayer A purchasing the 2006 Ford Escape with the $2,600 available credit, if the deduction method would still have been in place, she would have received the full benefit of the $2,000 above the line deduction. Of course, which one provides the greater benefit depends on the applicable taxpayer's tax rates.

Also, the deduction under section 179A was allowed for all taxpayers regardless of whether the vehicle was for business or personal use. This is significant because generally an asset that is purchased for personal use is ineligible for tax benefits, and as a result D would have been able to take advantage of the deduction. When enacted, this provision was not to extend past vehicles placed into service after December 31, 2004.

C. The Alternative Minimum Tax Effect and Unused Credits

As discussed in Part II.A.3, the alternative minimum tax has an effect on the availability of the hybrid tax credit. It was originally enacted to target a select group of high income individuals who were paying zero income tax, but more middle-income taxpayers are now subject to it because the alternative minimum tax is not indexed. The alternative minimum tax adds back into the income consideration certain expenses that are considered a deduction under the traditional method, like medical and dental expenses, home mortgage interest, and certain taxes paid. Once these amounts are added back into the calculation, a new tentative tax liability is determined. The taxpayer will pay at least this amount in taxes.

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97 Id. § 179A(b)(1)(A)(i).
99 When the credit was applied instead of the deduction in Part II.A.3, A was only able to use $1,500 of her anticipated $2,600 credit because of other limitations imposed by the tax code.
for the year, regardless of applicable credits like the hybrid tax credit.\(^{104}\) Only those credits which are refundable, like the earned income credit discussed in Part IV, offset the alternative minimum tax.\(^ {105}\)

While generally a tax credit is more valuable than a deduction because it is a dollar for dollar benefit, for some taxpayers this tax credit is not as beneficial. Bradley Berman, editor of HybridCars.com, noted that “‘[s]urprisingly, for taxpayers who take a lot of deductions or use the alternative minimum tax, the previous tax deduction, which bit the dust in 2005, was more valuable.’”\(^ {106}\) Also, any leftover credit when calculating the credit for the current year that is not used disappears.\(^ {107}\) Even though a taxpayer may have thought at the time that the higher priced hybrid would result in a positive tax treatment, it is possible that no benefit will result. Taxpayers need to determine their potential taxable liability before deciding if purchasing a hybrid will assist them when it comes time to file their annual tax returns. This potentially can be challenging when trying to make a purchase if a taxpayer is uncertain as to the likely tax considerations that may be present.

For a taxpayer that has a cyclical flow of income or potential deductions, being able to predict with some degree of certainty whether the credit will be potentially useful could be a challenge, making the individual less likely to bother with the hassle. On paper, the tax credit looks ideal, but for many taxpayers, this selling point or factor in making the decision whether to purchase a hybrid might not even be a consideration.

### III. SUV Tax Loophole

The tax incentives discussed above have all aimed to encourage individuals to purchase vehicles that will benefit the environment and push forward the environmental goals stressed by the President and members of Congress. However, other provisions of the code take a different stance and allow a tax incentive for vehicles that do not benefit the environment.

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\(^{104}\) See I.R.S. Form 6251.


\(^{107}\) Instructions, IRS Form 8910, at 4.
A. The Beginning of the Benefit

The tax code currently provides a tax write-off of up to $25,000 for a vehicle used at least fifty percent for work purposes and weighing over 6,000 pounds. This results from the interplay of two sections of the tax code, sections 179 and 280F.

Section 179 allows a taxpayer to take as a deduction the entire cost of certain assets in the current year, instead of requiring the taxpayer to capitalize the asset and depreciate the cost over a period of time.\(^{108}\) In 2007, the amount of this deduction for the business in any one year has increased to $125,000 as long as the amount of assets purchased in the current year does not exceed $500,000.\(^{109}\) When first enacted, taxpayers were able to take this opportunity to write off in the year of purchase the entire cost of certain vehicles that fell into a specific weight category.\(^{110}\)

B. The Intent Behind the Provision

The original intent behind section 179 was to encourage small businesses to invest in pickup trucks, minivans, and other needed service vehicles and spawn a growth in the economy.\(^{111}\) In 2005, around forty different passenger SUVs, including one “which nets a combined 15 miles per gallon,” qualified under this section of the code.\(^{112}\) These larger SUVs escaped the limitations in section 280F, which limits deductions for passenger vehicles under 6,000 pounds,\(^{113}\) and businesses were taking advantage even though these vehicles were “not necessary for purposes of conducting the taxpayer’s business.”\(^{114}\)

Section 280F is entitled “Limitation on Depreciation of Luxury Automobiles; Limitation Where Certain Property Used for Personal Purposes,”\(^{115}\) and it was an attempt by Congress to crackdown on the

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\(^{109}\) I.R.C. § 179(b)(1)-(2) (West, Westlaw through 2007 amendments).
\(^{112}\) Id.
\(^{114}\) Dupic, supra note 11, at 696 (quoting S. REP. No. 108-192, at IV.F.13 (2003)).
purchase of luxury automobiles by businesses taking large deductions for them. The problem is that Congress failed to change the weight-based classification of the vehicles to which this limitation applies, creating a huge benefit for the largest, least efficient vehicles. The loophole exists based on the definition of a passenger automobile section 280F. In section 280F(d)(5), a passenger automobile is defined as "any 4-wheeled vehicle (i) which is manufactured primarily for use on public streets, roads, and highways, and (ii) which is rated at 6,000 pounds unloaded gross vehicle weight or less." Because many SUVs on the market weigh more than 6,000 pounds, the extra limits on deductions do not apply. Congress likely did not realize that the effect of section 179 on businesses was to create incentives to purchase gas guzzling SUVs.

C. The Benefits

These businesses and self-employed individuals received a great benefit and even were able to use these vehicles for some personal purposes. Upon realizing the effect of this loophole, Congress limited the ability to use section 179 for the purchase of SUVs to $25,000 by enacting section 179B(6)(A). Prior to this change in the law, this deduction was not the only deduction allowed in the first year. The taxpayer was also able to take bonus depreciation as provided in other sections of the code, but Congress removed the ability to take both types of deductions in one year.

Generally, a taxpayer benefits by expensing purchases of certain assets rather than capitalizing the purchase and taking depreciation deductions over a period of years. With the time value of money and the possibility of lower income in future years, it is usually more beneficial to take a deduction in the current year. If the taxpayer is forced to

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116 Dupic, supra note 11, at 677-78.
119 See id. § 280F(b) (stating that the taxpayer will have to recapture the depreciation deducted if the business use of the vehicle does not exceed fifty percent).
capitalized the asset and take deductions in future years, the cost of the asset is spread out over its useful life as outlined in section 167.\textsuperscript{123} The benefits of immediate reduction in taxable income for the business and the time value of money generally make it beneficial for the taxpayer to use any deductions in the current year instead of deferring to later years. This provision benefits small businesses and individuals who are self-employed as they can take this deduction, but they are able to do so only if it does “not exceed the aggregate amount of taxable income” in the year derived from engaging in a trade or business.\textsuperscript{124}

IV. COMPARISON AND CONSEQUENCES OF THE SUV TAX LOOPHOLE AND THE GREEN TAX CREDIT

A. Comparing the SUV Tax Loophole and the Green Tax Credit

As discussed above, Congress has two provisions in the tax code that encourage individuals to purchase vehicles. Unfortunately, the provisions are not pushing the individuals in the same direction. The SUV tax loophole encourages the purchase of SUVs, while the green tax incentives found in section 30B encourage the purchase of hybrids. These provisions are in conflict and do not send a unified message to taxpayers.

When enacted, the provisions in sections 179 and 280F were not intended to reach this result.\textsuperscript{125} This conflict has been noticed by other scholars, including Carrie M. Dupic in a comment published in the Lewis & Clark Law Review. She stated, “[W]ith the environmental concerns inherent to the SUV, this tax incentive to choose a heavy SUV over other types of vehicles contradicts other provisions of the Code designed to reward businesses for buying more environmentally-friendly vehicles such as electric cars.”\textsuperscript{126} Congress did have a reason for placing a weight limit in the provision. “The weight classification included in Section 280F(d)(5)(A)(ii) was intended to separate passenger automobiles from heavier vehicles typically used for farming, construction, and other hauling

\textsuperscript{123} See I.R.C. § 167 (West Supp. 2007).
\textsuperscript{125} Dupic, supra note 11, at 672 (“The existence of the SUV tax loophole in section 280F runs contrary to the original purpose of that section: to crack down on abusive deduction practices by businesses buying expensive luxury vehicles just to enjoy bigger tax write-offs.”).
\textsuperscript{126} Id.
work... so that businesses needing vehicles in the latter category would be entitled to uncapped expensing and depreciation deductions.\textsuperscript{127} Congressional intent has been circumscribed by the actual application of the provision.

In comparison, the green tax credits were enacted specifically to drive consumer choice and encourage individuals and businesses to pursue alternative technology.\textsuperscript{128} With this alternative technology that will benefit the environment also comes the reduction in the need for foreign oil sources.\textsuperscript{129} Over the past year, the rising and falling price of oil has been a key factor in the pressure for more efforts in Congress to reduce foreign oil dependence.\textsuperscript{130} Also, the extraordinary profits of oil companies while prices at the pumps remain high have stirred much debate.\textsuperscript{131}

There will be more efforts put forth in the coming sessions of Congress to push innovators to look to other potential energy sources, such as ethanol.\textsuperscript{132} In a speech to the Hispanic Chamber of Commerce,
President Bush stated, "All measures that I've discussed with you today are designed with one overriding goal: to address the root causes of higher energy prices and to address our dependency upon foreign sources of energy."\textsuperscript{133}

\textbf{B. Tax Incentives Drive Consumer Choice}

As discussed in prior sections, Congress intends for these incentives to make the possibility of purchasing a hybrid more likely. The hybrid tax credit could potentially make the purchase of a hybrid vehicle a more economical choice for individuals outside of the upper economic class and the small business person.\textsuperscript{134} These incentives are different for small businesses, which have incentives such as section 179 deductions.

One commentator noted that "[w]hen you combine the latest tax incentives with the rising cost of gas, you could easily save $5,000 to $10,000 on credits and fuel over the lifetime of your hybrid."\textsuperscript{135} These savings can be significant and actually make a difference to a new car buyer's decision-making model. The federal tax incentives are considered one of the main factors in deciding whether to purchase a hybrid.\textsuperscript{136}

There are, however, many factors that can influence a car buyer, and it is hard to say that one factor weighs extremely more than another. Take for example the hypothetical taxpayer A, who is environmentally conscious. She might place the environmental benefits above all else. This would be in stark contrast to taxpayers C and D, who are more concerned with money. When J.D. Power and Associates took a survey to determine what influences individuals when making a purchase, it found that "[c]oncern over fuel prices, the high level of U.S. dependency on foreign fuel supplies, a federal tax incentive and concern for the environment are the primary motivators behind consumer consideration to purchase a hybrid vehicle."\textsuperscript{137} Given that federal tax incentives do influence car

\textsuperscript{133} Id.
\textsuperscript{134} See Schaefer, supra note 65.
\textsuperscript{135} Id. A consumer visiting www.hybridcenter.org can complete a personal profile based on vehicle habits and needs and a computer program will determine if purchasing a hybrid vehicle is a good fit for the individual. See Union of Concerned Scientists, HybridCenter.org, http://www.hybridcenter.org (last visited Oct. 22, 2007).
\textsuperscript{136} Munoz, supra note 4, at 117 (citing Press Release, J.D. Power and Associates, infra note 137).
\textsuperscript{137} Press Release, J.D. Power and Associates, J.D. Power and Associates Reports: Interest in Hybrid Technology is High, Especially Among Women (Mar. 6, 2002), available at
buyers, other scholars have stated how Congress has decided to use this to drive individuals to pursue the path Congress desires. "The current tax code uses policy-driven tax incentive provisions to induce taxpayers to alter their individual behavior to conform with Congress's preferences, based on political or social reasons." Congress must make a decision as to whether the green tax incentives or the tax benefits for small businesses like the SUV tax loophole are more important.

A major concern initially voiced by car manufacturers was the need to jump-start buyers' entrance into the hybrid market. Gil Anderson, a salesman with Capitol Toyota, stated that "[i]t's a combination of the environment and fuel efficiency, and now the tax credit makes it more doable, offsets the cost of the hybrid system." Also, in 2006, J.D. Power and Associates reported that "hybrid-electric vehicle sales volumes are anticipated to grow by 268[%] between 2005 and 2012 . . . " Even with this large increase in sales, the percentage of the entire United States auto market share for HEVs will only increase from 1.3% in 2005 to 4.2% in 2012. The hybrid-electric vehicle market has grown from two models and fewer than 10,000 vehicles sold in 2000 to 11 models and an estimated 212,000 vehicles sold in 2005.

Consumers who purchase hybrids also contribute greatly to decreasing our country's dependence on foreign fossil fuels, and help to make us less vulnerable to energy price volatility. Increasing hybrid sales may indeed continue to be a valuable contribution to a greater self-sufficiency and energy efficiency amidst the global challenges we as a nation may face in the uncertain days ahead.

138 Munoz, supra note 4, at 129.
139 See US Automakers Want End to Hybrid Credits, supra note 80.
140 Gail Perry, IRS Hybrid Tax Credit Draws Mixed Response From Public, WEBCPA, July 2, 2006, at 10 (quoting Gil Anderson, a salesman with Capital Toyota).
142 Id.
143 Id.
144 Schaefer, supra note 65.
145 Id.
C. Environmental Concerns

Hybrids and SUVs have different effects on the environment, and many factors play into the purpose behind enacting provisions to encourage the purchase of each. When the Energy Policy Act of 2005 was first enacted, Congress was motivated to develop a national energy policy. Senator Pete Domenici of New Mexico issued the Statement of Administration Policy on the House resolution, which later became the Energy Policy Act of 2005. He stated, "It... would improve the Nation's energy security and reduce our dependence on foreign sources of oil by increasing the use and diversity of renewable energy sources and by reducing energy consumption through greater conservation and energy efficiency." The concern for reducing America's dependence on foreign oil is coupled with the concern for reducing the amount of oil used by Americans. One way to solve this problem is by developing new sources of energy.

Hybrids "can drive for 40-70 miles on one gallon of gasoline, much farther than a conventional vehicle." With this reduction in the amount of gasoline needed to power the vehicle, there is also less need for foreign oil. In addition, the energy used to power a hybrid is more secure because hybrids have the potential to run on renewable fuels.

Hybrids also assist in the effort to combat air pollution. The emissions from hybrids vary depending on the type of vehicle manufactured and its configuration, "[b]ut in general, HEVs have lower emissions than conventional vehicles because an electric motor is used with an internal combustion engine, which offsets how often the engine is used and, therefore, reduces fuel use and emissions." When the hybrid operates in electric only mode, emissions are reduced to zero, "which is optimal in congested areas and in areas where emissions are not tolerated."

147 Id.
149 Id. ("HEVs have the potential of running on alternative fuels, which can be renewable and/or produced in the United States. Therefore, HEVs can reduce U.S. dependence on fossil fuels and help decrease foreign oil imports, thereby increasing energy security.").
150 Id.
151 Id.
V. OTHER FEDERAL AND STATE TAX PROVISIONS ENACTED TO ENCOURAGE PURCHASE OF HYBRID VEHICLES

On the federal level other provisions are being introduced or enacted to push forward more environmentally-friendly vehicles. Bills are also being introduced in Congress to encourage taxpayers to purchase hybrids in order to get the tax credits. For example, Senator Jim Talent successfully added an amendment to the 2006 highway bill that allows states to provide for hybrids that have at least 45 miles per gallon to use High Occupancy Vehicle (HOV) lanes that are traditionally restricted to vehicles with multiple occupants.\(^{152}\) Two different private insurance companies are also offering discounts to individuals on their car insurance for purchasing a hybrid.\(^{153}\) As discussed in Recommendation A below, some members of Congress are introducing legislation that will either remove the phase-out on the credit or add another credit of up to $3,000 on top of the current credit for vehicles that are manufactured domestically.\(^{154}\)

Many states have also enacted provisions to encourage the use of alternative vehicles like hybrids.\(^{155}\) In Arkansas, a bill has been introduced that permits an exemption for the gross receipts tax on the purchase of a new HEV.\(^{156}\) Another bill in Arizona would allow for the reduction in the cost of a vehicle license equal to one percent of the manufacturer’s suggested retail price (MSRP) for the first twelve months.\(^{157}\) A Massachusetts proposal would allow hybrid owners to be exempt from the emissions and maintenance inspection requirement.\(^{158}\) A North Carolina legislator

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\(^{153}\) See id. (discussing Travelers and Farmers Insurance Group’s different insurance discounts available including a ten percent discount on certain vehicles, in certain states).

\(^{154}\) See id.

\(^{155}\) For a fifty state summary of hybrid incentives see id.


\(^{158}\) S. 1409, 185th Leg., Reg. Sess. (Mass. 2007).
has proposed a tax credit on the research side of the operation and desires to promote an increase in research and development in the industry. An interesting incentive was enacted in Los Angeles, which allows hybrids free parking at meters in the city. Many other states have their own hybrid tax credit, deduction, or proposal for incentives, including California, Illinois, Indiana, Iowa, Kansas, Louisiana, Maryland, Missouri, New Jersey, New York, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, and Wisconsin. In

160 The free metered parking program was extended through the end of 2007 by a vote of the Los Angeles City Council on June 21, 2006. Los Angeles Department of Transportation, Free Parking Info, www.lacity.org/LADOT/FreePark.htm (last visited Oct. 22, 2007); see also State and Federal Hybrid Incentives, supra note 152. The article also addresses many other cities around the country that have enacted similar provisions to provide free or reduced parking.
163 H.B. 1370, 115th Gen. Assem., 1st Sess. (Ind. 2007) (providing for a $1,500 tax deduction for the purchase of a "clean-[fuel vehicle").
164 H.S.B. 279, 82nd Leg., 1st Sess. (Iowa 2007) (providing for an income tax credit for the purchase of an alternative fuel vehicle).
165 H.B. 2222, 2007-2008 Leg., 1st Sess. (Kan. 2007) (providing for an income tax credit of up to $2,500 for the purchase of a hybrid motor vehicle); S.B. 140, 2007-2008 Leg., 1st Sess. (Kan. 2007) (providing for an income tax credit of up to $750 for the purchase of a hybrid motor vehicle).
171 S.B. 107, 127th Gen. Assem., Reg. Sess. (Ohio 2007) (establishing a $3,000 tax credit for the purchase of a hybrid vehicle with an EPA fuel economy rating of 40 or more mpg and a $2,000 credit for those with a rating of less than 40 mpg).
172 S.B. 1021, 74th Leg., Reg. Sess. (Or. 2007) (reducing the annual registration fee for hybrid vehicles).
173 73 PA. STAT. ANN. § 1647.3 (West 2007) (providing a tax rebate for the purchase of a
addition to the federal benefits, states are taking different approaches for encouraging the purchase of green vehicles.

VI. RECOMMENDATIONS

A. Lift the Limitation on Clean-Fuel Vehicle Tax Credit Based on Number of Vehicles Produced.

In order to continue with a policy of encouraging individuals to purchase HEVs, the tax incentives should not be limited based on the production levels of the manufacturer. If the hybrids produced by Toyota are more popular and in higher demand, why should an individual be forced to buy a Ford or Honda to get the same or any benefit? If Congress's true desire was to increase the purchase of these environmentally-friendly vehicles and to decrease the dependence on foreign oil, then this limitation must be lifted. Instead, Congress should be encouraging individuals to continue purchasing any HEV and assisting with the effort to stop the dependence on foreign oil.

In order to lift this limitation it will be necessary to remove section 30B(f) from the Internal Revenue Code. This provision provides for the phase-out of tax credits for each vehicle once the manufacturer has reached a production level of 60,000 vehicles. The tax credit is quickly phased-out and eliminated with a 50% and a 25% cutback. The more popular Toyota Prius will reach a credit of $787.50 for vehicles purchased between April 1 and September 30, 2007. This small credit is significantly less than the value of the credit on January 1, 2006 of $3,150.

One United States Senator agrees with this proposal and has attempted to make headway into this battle. On September 29, 2006, Senator Richard Lugar introduced Senate Bill S.4000 that would accomplish this

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hybrid vehicle).

176 A.B. 174, 2007-2008 Leg., 2nd Sess. (Wis. 2007) (providing tax credit for the purchase of a hybrid vehicle).
178 Id. § 30B(f)(3).
180 See id.
solution by striking the limitation paragraph. This bill has been referred to the Committee on Finance and has not been enacted. A similar bill was introduced by Senators Evan Bayh, Sam Brownback, and Joe Lieberman in 2005 that also would have lifted the cap on the hybrid manufacture limit as part of a package to reduce domestic oil usage, but the bill failed to make it out of the same committee. Don Becker of the Sierra Club, when lobbying Congress for the passage of this kind of legislation, said, “We were urging tax credits commensurate with the fuel economy of the vehicle, with no limit on the number sold . . . .”

The United States House of Representatives is also considering a similar bill introduced by Congresswoman Judy Biggert on September 29, 2006, which has been referred to the House Ways and Means Committee but has not left the committee. Also, as a part of a broad ranging energy bill, Congressman Chris Shays introduced legislation that would remove the cap on the number of hybrid tax credits. If Congress passes these bills, and the President signs the bills into law, the credit for HEVs will not be phased out at any point based on production numbers. This change will continue to encourage individuals to purchase these vehicles and increase the competition among manufacturers to win over customers.

B. Allow a Credit Regardless of the Alternative Minimum Tax.

The credit, in addition to being nonrestrictive in relation to production, must be available and beneficial for all taxpayers, not just certain favored taxpayers. Currently, if a taxpayer cannot use the tax credit in the current period it is lost forever. The credit can only be used in the year of purchase. This affects lower income individuals who do not pay much in federal income taxes because they have a low tax liability to be offset in the first place. What incentive would be provided to these individuals to make the purchase of a more expensive HEV, knowing that the tax incentive does not reach to their level of income?

Instead, Congress should enact legislation that provides a credit that can either be carried over into future years or is refundable. Congress

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184 Funk & Jensen, supra note 68, at 31 (quoting Dan Becker of the Sierra Club).
has in place other credits that are refundable like the earned-income credit.\footnote{See U.S. DEP'T OF THE TREASURY, INTERNAL REVENUE SERVICE PUBLICATION 596—EARNED INCOME CREDIT (2006), available at http://www.irs.gov/pub/irs-pdf/p596.pdf. The earned income credit is applied similarly to a withholding on a paycheck. Even if an individual pays zero taxes for the year or has a zero additional tax liability because of withholdings, it is possible to receive cash back for the year because of this credit. See \textit{id.} at 1. There are requirements, including that the individual be employed and earn less than $36,348. \textit{Id.} There are other tax provisions that enable taxpayers to carry forward the credit into future years and potentially gain the benefits then, or even to carry back the credit to prior years and receive a refund for prior taxes paid.} This would mean that taxpayers would receive cash back for the amount of the credit on the tax return in excess of what taxes they did pay.

C. \textit{Allow Either a Credit or a Deduction.}

A third proposal is in the alternative of Recommendation 2. Congress should give the taxpayer an option to choose between the credit allowed in section 30B, or to opt to use the former deduction allowed for a personal use automobile under section 179A. Taxpayers would have the option to choose which provision is more beneficial to their individual situations. This would eliminate the loss of the possible credit that cannot be carried forward. It would also provide taxpayers the option of taking an above the line deduction to lower their adjusted gross income.

D. \textit{Remove the SUV Tax Loophole.}

Congress will likely be concerned with the significant costs involved in the passage of the two prior proposals. Congress might also be wary of other legislation that could be just as costly. In order to make these proposals financially feasible, I would also propose the elimination of the SUV tax loophole. There are multiple ways to rectify this problem, and instead of simply limiting the deduction as Congress has previously done, it should now be eliminated. On April 27, 2006, Congresswoman Heather Wilson of New Mexico introduced the Fuel Efficient Vehicle Tax Incentive Act of 2006 with the goal of eliminating the SUV tax loophole.\footnote{H.R. 5251, 109th Cong. §§ 1, 3 (2006).} Congresswoman Wilson proposed that the definition of a passenger automobile in section 280F(d)(5) of the Internal Revenue Code of 1986 be amended to include an SUV with a weight between 6,000 pounds and...
14,000 pounds.\textsuperscript{190} This is one solution that goes right to the heart of the problem: the definition of a passenger automobile.

Another possible solution would be to adopt a functionality test instead of a weight test. The functionality test would allow for the type of vehicles used for farming and agriculture to be exempt from the new rules and maintain their deduction. The functionality test would exclude these type of operations from this limitation and allow them to continue taking deductions regardless of the gross vehicle weight.

CONCLUSION

This Note began with an introduction of four individual taxpayers who wanted to purchase a vehicle. The goal of the recommendations in this Note are to make it beneficial for taxpayer A to purchase an HEV and to influence taxpayers C and D to choose the more environmentally-friendly vehicle. There is less of a chance to influence taxpayer B, but it is always possible that, if the cost of gasoline increases significantly enough, even his desire to own an SUV will pass with the knowledge that he can have more options for his money when he purchases an HEV, especially with more hybrid SUVs being introduced.

American energy policy is affected by the different paths the United States Congress takes when it shapes tax incentives. Consumers are affected by these decisions and make many decisions based on which avenue is most beneficial to them financially. If the United States Congress does not act, then the mixed message that is currently being sent to Americans will not provide the incentives to have individuals switch to more environmentally-friendly automobiles.

It is important that America stops its dependence on foreign oil, but even more important that America take action to combat the damage certain automobiles are doing to the environment. President Bush stated, "[A]s we work to solve our energy . . . dependency, we[']ve got to remember that the market for energy is global, and America is not the only large consumer of hydrocarbons."\textsuperscript{191} Congress has the opportunity to make these changes by enacting new legislation that will eliminate the SUV tax loophole completely. In addition, Congress can ensure that

\textsuperscript{190} Id. § 3(a).
\textsuperscript{191} Statement by President George W. Bush Upon Signing H.R. 6 \textit{supra} note 5, at S23.
taxpayers who purchase HEVs will continue to receive the tax
deductions they deserve, no matter the production levels of each
manufacturer. Finally, Congress hopefully will act to ensure that the tax
benefits provided in the new legislation will be available to all taxpayers
and not eliminated by other tax provisions in the code. Now is the time
for Congress to send one message loud and clear.