Taxes

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Going, Going, Gone: The Hybrid Vehicle Tax Credit

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The Energy Policy Act of 1992 (P.L. 102-486) created IRC §179A, Deduction for Clean-Fuel Vehicles and Certain Refueling Property. This Code section allowed a deduction for alternative fuel vehicles but didn't apply to electric vehicles, which had their own tax credit under IRC §30, Credit for Qualified Electric Vehicles. The Energy Tax Incentives Act of 2005 (P.L. 109-58) replaced IRC §179A with IRC §30B. Under the new IRC §30B, Alternative Motor Vehicle Credit, all credits are consolidated into one code section. Plus, there is a specific hybrid motor vehicle credit. If you want to buy a qualifying car and take the credit, however, you need to move quickly.

Old Law

The credit was calculated under IRC §30 as 10% of the cost of the vehicle, with a maximum allowable credit of $4,000. In IRC §30(c), a "qualified electric vehicle" is "powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electrical current." The vehicle also had to have four wheels and be intended for use on public streets and roads. If the vehicle wasn't "primarily powered by an electric motor," it didn't qualify for the credit.

New Law

IRC §30B(d) contains the specifics of the hybrid motor vehicle credit, which comprises two parts. This credit applies to vehicles that draw their propulsion energy from onboard sources of stored energy, which can include either an internal combustion engine (or a heat engine using consumable fuel) and a rechargeable energy storage system. For passenger automobiles and light trucks with a gross vehicle weight rating of 8,500 pounds or less, 4% of maximum available power must be from the rechargeable energy storage system. The new vehicle must be placed in service by the taxpayer before January 1, 2011, and not held for resale.

The vehicle must have received a certificate of conformity under the Clean Air Act, and it must meet or exceed the equivalent qualifying California low emis-

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sion vehicle standard of the Clean Air Act for that make and model year. There are additional Bin 5 or Bin 8 Tier II emission standards depending on whether the vehicle is less than 6,000 pounds or between 6,000 and 8,500 pounds. These are specified in the Clear Air Act, but most vehicle manufacturers publish the vehicle classification information.

The Credit

The hybrid motor vehicle credit contains two elements: the fuel economy credit and the conservation credit. The fuel economy credit is based on a comparison of achieved fuel economy for the hybrid vehicle expressed as a percentage of the 2002 model year city fuel economy. The dollar amount of the fuel economy credit depends on the percentage increase in city fuel economy in bracket amounts. For example, an increase in fuel economy of at least 175% but less than 200% yields a credit of $1,200. An increase in economy over 250% yields the maximum credit of $2,400.

The conservation credit is based on the estimated lifetime fuel savings expressed in gallons of gasoline. For example, if a hybrid vehicle will save between 1,800 to 2,400 gallons of gasoline over its lifetime, the credit is $500. According to IRC §30B(c)(4), the lifetime fuel savings is any excess from the following calculation:

"120,000 divided by the 2002 model year city fuel economy for the vehicle inertia weight class, over 120,000 divided by the city fuel economy for such vehicle."

Fortunately, it isn't necessary to understand this obtuse formula and its requirement to be intimately familiar with Title II of the Clear Air Act and its definitions in order to benefit from the credit.

How Much Can I Take?

The IRS has simplified the whole process. No, really. The list of cars and light trucks and the respective tax credits is available on the IRS website. Go to www.irs.gov/newsroom/index.html and select the article "Hybrid Cars and Alternative Motor Vehicles." Here are some examples for model year 2007:

- Chevrolet Silverado 2WD Hybrid Pickup Truck—$250
- Chevrolet Silverado 4WD Hybrid Pickup Truck—$650
- Ford Escape Hybrid 2WD—$2,600
- Ford Escape Hybrid 4WD—$1,950
- GMC Sierra 2WD Hybrid Pickup Truck—$250

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- GMC Sierra 4WD Hybrid Pickup Truck—$650
- Honda Accord Hybrid AT—$1,300
- Honda Accord Hybrid Navi AT—$1,300
- Honda Civic GX—$4,000††
- Honda Civic Hybrid CVT—$2,100
- Lexus GS 450h—$775†
- Lexus RX 400h 2WD and 4WD—$1,100†

These figures are correct as of July 6, 2007, but they may change for some vehicles on the complete list in a later quarter. The dagger symbol (†) after the Lexus GS 450h and RX 400h signifies a decrease in the amount of the credit originally available. The double dagger (††) after the Honda Civic GX indicates that this credit will never be reduced until December 31, 2010.

Why does the Honda Civic GX credit remain the same while the Lexus credits are reduced? The simple answer first. The credit for the Honda Civic GX doesn't decrease because the Civic GX burns natural gas and is an "alternative fuel" vehicle, not a hybrid vehicle. So the $4,000 credit remains the same until the termination date of IRC §30B.

As for the Lexus vehicles, the credit for hybrid vehicles phases out depending on the production of the manufacturer. The more popular the vehicle, the faster the credit disappears. The credit for the Lexus vehicles was reduced because the manufacturer (Toyota) indicated that its cumulative sales of qualified vehicles reached the limit for the credit phaseout.

The Phaseout

IRC §30B(f) contains the details of the phaseout. As described in FS-2007-09, "Taxpayers may claim the full amount of the allowable credit only up to the end of the first calendar quarter *after* the quarter in which the manufacturer records its sale of the 60,000th hybrid vehicle" [emphasis added]. For the next two calendar quarters, only half of the credit is available. In the third and fourth quarters after the quarter in which full credit ends, only one quarter of the credit is allowed. No credit is allowed after the fourth quarter.

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For example, as explained on the IRS website, Toyota surpassed the 60,000 vehicle limit in the quarter ending June 30, 2006. That means that the full credit is still available for a qualified Toyota vehicle purchased in the quarter following that one (i.e., July 1, 2006-September 30, 2006). In the next two quarters (October 1, 2006-March 31, 2007), 50% of the credit is available. Finally, it is then reduced to 25% in the two quarters after that (April 1, 2007-September 30, 2007). After September 30, 2007, the credit is no longer available for any Toyota hybrid vehicle.

Manufacturers report their sales to the IRS, which publishes updates at the website identified above. Notice that the phase-out applies to a manufacturer, not to a vehicle. Because Toyota manufactures the popular Prius and Camry hybrids as well as the Lexus GS 450h and RX400h, sales for all these models are included when calculating the 60,000 vehicle limit.

Why would Congress choose to limit the credit on the most popular (by sales) hybrid vehicles? The limitation wasn't in the original draft—it was added in the Conference Agreement. We can pose two possible reasons. First, Congress isn't serious about fossil fuel conservation, and IRC §30B was just to appease "green" constituents. Second, the "Detroit Three" (since they are no longer the "Big Three") car manufacturers are behind Toyota and Honda in hybrid technology and production. Allowing the full credit to run until the expiration of IRC §30B in 2010 might cause consumers to consistently choose Toyota and Honda automobiles instead of Detroit Three cars. By limiting the credit, taxpayers who want the credit will be forced into Detroit Three cars or trucks. ■

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