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**Overview of “Cash for Clunkers”**

On June 24, the President signed into law the Supplemental Appropriations Act of 2009. Title XIII of the Act (the “Consumer Assistance to Recycle and Save Act,” colloquially known as the “cash for clunkers”), gives a cash incentive for individuals and businesses to trade in older vehicles for new, more fuel-efficient ones. The incentive takes the form of a voucher of \$3,500 or \$4,500 depending on the type of vehicle traded in and the fuel efficiency of the vehicle purchased. The new vehicle would have to be purchased between July 1 and November 1 of 2009. The \$3,500 or \$4,500 vouchers are not to be treated as gross income for purposes of the Code, or for federal or state assistance programs.

**Cash for clunkers program in brief.** For passenger autos, the voucher amount is \$3,500 if the new fuel efficient automobile is a passenger automobile and its combined fuel economy (CFE) is at least 4 mpg higher than the CFE of the eligible trade-in vehicle. The voucher is \$4,500 if the new fuel efficient vehicle's CFE is at least 10 mpg higher than the CFE of the eligible trade-in vehicle.

For trucks, the voucher amount is \$3,500 if:

- The new fuel efficient vehicle is a category 1 truck and its CFE is at least 2 mpg higher than the CFE of the eligible trade-in vehicle;
- The new fuel efficient vehicle is a category 2 truck that has a CFE of at least 15 mpg and: (a) the eligible trade-in vehicle is a category 2 truck and the CFE of the new truck is at least 1 mpg higher than the CFE of the eligible trade-in vehicle; or (b) the eligible trade-in vehicle is a category 3 truck of model year 2001 or earlier; or

- The new fuel efficient vehicle is a category 3 truck and the eligible trade-in vehicle is a category 3 truck of model year 2001 or earlier and is of similar size or larger than the new fuel efficient vehicle automobile as determined in a manner prescribed by the Treasury Secretary.

For trucks, the voucher amount is \$4,500 if:

- The new fuel efficient vehicle is a category 1 truck and its CFE is at least 5 mpg higher than the CFE of the eligible trade-in vehicle;
- The new fuel efficient vehicle is a category 2 truck that has a CFE of at least 15 mpg and its CFE is at least 2 mpg higher than the CFE of the eligible trade-in vehicle and the eligible trade-in vehicle is a category 2 truck.

**Key definitions.** A passenger auto is one meeting the definition at United States Code (USC) title 49, sec. 32901(a)(18) that has a CFE of at least 22 mpg. A category 1 truck is a non-passenger auto as defined at USC title 49, sec. 32901(a)(17), that has a CFE of at least 18 mpg, a category 2 truck is a large van or large pickup as categorized by the Treasury Secretary; and a category 3 truck is one defined as such at USC title 49, sec. 32901(a)(19). The term CFE depends on the model year. Could there be a more difficult way to define vehicles?

A “new fuel efficient auto” is a passenger auto, or category 1, 2, or 3 truck as defined above:

- The equitable or legal title of which has not been transferred to any person other than the ultimate purchaser;
- That carries a manufacturer's suggested retail price of \$45,000 or less;
- That meets certain certification standards, and

- That has the CFE of at least (1) 22 mpg for a passenger auto; (2) 18 mpg for a category 1 truck; or (3) 15 mpg for a category 2 truck;

The qualifying replacement vehicle must be new, but a “demonstrator” vehicle never titled may qualify even if it had substantial mileage.

Trade-in vehicles eligible for the voucher program are those that at trade-in time: are in drivable condition; have been continuously insured and registered to the same owner for at least one year; were manufactured less than 25 years before the trade-in date; and in the case of an auto, achieve a CFE of 18 mpg or less. A single person may get only one trade-in voucher and only one voucher is available for joint registered owners of a single eligible trade-in vehicle.

The one-year rule prevents someone from buying an old clunker now and making money on a trade-in.

For autos, the mpg limits mean that the old one can't have a CFE of more than 18 mpg, and the new one must have at least a CFE of 22 mpg and exceed the old one's CFE by at least (a) 4 mpg (for a \$3,500 voucher) or (2) 10 mpg (for a \$4,500 voucher).

**Treatment of voucher.** The voucher, which will be sent by the Treasury to the dealer, will offset the new vehicle's purchase price or lease price for a qualifying lease. A qualifying lease is a lease of an auto for at least five years. The selling dealer must use the voucher in addition to any other rebate or discount that it advertises or the manufacturer offers, and the voucher can't be used to offset a rebate or discount. There are other restrictions on the dealer, such as having to scrap the traded-in vehicle, except for certain salvaged parts.

Within 30 days of the enactment date, Treasury is to provide details and requirements relating to the program, including a comprehensive list, by make and model, of new fuel efficient autos meeting the requirements of the voucher program.

**Income tax aspects.** The vouchers are not treated as gross income of the vehicle purchaser for Federal tax purposes.

For a business, trading in a qualifying vehicle with a low or zero basis definitely beats selling it for an amount equal to or less than the voucher's value. In fact, it may even pay to forego a higher sale price and instead trade in the old vehicle and get a tax-free voucher. For example, if a business paying tax at an effective tax rate of 30% sells a zero-basis truck for \$6,000, it would have \$4,200 left after paying a \$1,800 tax. If the business trades in the old truck and qualifies for a tax-free \$4,500 voucher under the new program, it would be \$300 ahead.

Buyers also may be able to claim an income tax deduction for qualified motor vehicle taxes paid on the vehicle, whether they itemize or claim standard deduction. Additionally, buyers may be able to claim a credit for vehicles that qualify for the hybrid credit for vehicles, or the advanced lean burn technology motor vehicle credit. The credit varies with the type of vehicle. For example, the advanced lean burn technology motor vehicle credit is \$1,300 for a Volkswagen 2009 Jetta.

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