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Biodiesel Tax Credits & Alternative Fuel Vehicle (AFV) Credits for End-Users

Overview: Biodiesel is a non-toxic, renewable, and biodegradable fuel composed of mono-alkyl esters of long chain fatty acids derived from vegetable oils or animal fats. Biodiesel is commonly sold in blended form (e.g. 20% biodiesel and 80% diesel fuel is known as "B20"; 100% biodiesel is "B100"). Biodiesel can be used in existing diesel engines by public and electric utility fleets to meet federal mandates for the utilization of alternative fuel vehicles (AFVs). Diesel end-users may also enjoy economic incentives associated with the use of biodiesel blends due to federal biodiesel tax credits and the exemption enjoyed by biodiesel from State diesel fuel tax.

Alternative Fuel Vehicle (AFV) Credits: The Energy Policy Act (EPAAct) requires certain public fleets and electric utility-owned fleets, to purchase a certain percentage of alternative fuel vehicles (AFVs). Fleets covered by these mandatory purchasing requirements may operate existing diesel vehicles on blends of biodiesel and thereby generate "biodiesel fuel use credits" in lieu of purchasing new AFVs or EPAAct credits.

Federal Tax Credits: The IRS allows two federal income tax credits for using biodiesel. The biodiesel fuel credit, which is more germane for traditional end-users because it does not require the end-user to register, is claimed as a general business credit when an end-user purchases and uses biodiesel directly from a biodiesel producer (i.e., the credit may not be claimed if the biodiesel was purchased from a retail sale). The biodiesel mixture credit may be claimed by a registered blender when biodiesel (e.g., B100) is blended with un-dyed (on-road) diesel fuel outside the bulk transfer terminal system. Due to the registration requirements, this tax credit is most commonly used by producers, blenders, and marketers. The biodiesel tax credits are \$1.00 per gallon for agri-biodiesel (i.e., produced from virgin seed oil crops (e.g., soy and cotton) and 50 cents per gallon for other types of biodiesel.

Texas' Biodiesel Incentives: Biodiesel (B100) and the volume of biodiesel that is blended with regular diesel fuel is exempt from paying the Texas 20 cent per gallon "diesel fuel tax." A person producing a B20 blend (20% biodiesel and 80% diesel) would not be taxed on the volume of biodiesel used to make the fuel mixture. Biodiesel is defined to include any motor fuel or mixture of motor fuels that is: 1) derived wholly or partly from agricultural products, vegetable oils, recycled greases, or animal fats, or the wastes of those products or fats; and 2) advertised, offered for sale, suitable for use, or used as a motor fuel in an internal combustion engine. Texas also offers a biodiesel production incentive, which entitles biodiesel producers to receive a 20 cent per gallon payment (which is a net 16.8 cent payment given the 3.2 cent pay-in requirement). This program is not applicable to end-users.

Practical Use of AFV Credits & Tax Credits by Diesel End-users: The credits discussed above create significant economic incentives for diesel end-users to use biodiesel blends. For fleets subject to EPAAct, AFV requirements make the use of biodiesel attractive given the ability to create marketable "biodiesel fuel use credits" (currently valued at \$600-700 per credit) & avoid the cost of purchasing new AFVs (\$25,000+/AFV) or EPAAct credits (current value of \$750-1,200). The tax benefits of biodiesel can be leveraged in a number of ways by end-users. Beyond the exemption for the biodiesel component of biodiesel blends at the State level, traditional end-users have a choice of how best to maximize the \$1.00/50 cent federal biodiesel tax credit. End-users are most likely to enjoy the tax credit in the form of a discounted biodiesel price offered by fuel jobbers/registered blenders who can reduce the price by blending the fuel and then claiming the blender's credit. For end-users interested in maximizing the direct benefit of the biodiesel tax credit, they can purchase B100 directly from a producer and blend and use the biodiesel without registration requirements and themselves claim the \$1.00/50cent tax credit for each gallon of B100 used in their business, so long as they obtain and keep biodiesel certification records from the producer or biodiesel importer.

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