A cost-benefit analysis of the SUV tax loophole

In an attempt to boost business investment, the 2003 Jobs and Growth Tax Relief Reconciliation Act gave business owners an income tax deduction of up to $100,000 of the purchase price of any vehicle greater than 6,000 pounds used for business purposes. This is a 200% increase from the previous maximum deduction allowed. This paper estimates the effects of this tax break on the demand for heavy vehicles and attempts to address the efficiency of the policy in terms of both increased business investment and costs imposed by heavier vehicles. The extent to which the policy is successful in increasing business investment depends heavily on whether or not the tax break generated new purchases of heavy vehicles. Policy effectiveness is undermined when business owners already planning to buy a vehicle substitute heavier vehicles covered under the tax break for lighter vehicles not covered under the tax break. Moderate evidence is found of an increase in demand for heavier vehicles. Weak evidence for substitution effects of heavier vehicles covered under the tax break for lighter vehicles not covered by the tax break is found. The overall evidence suggests a slight increase in the demand for larger vehicles, implying minimal both environmental costs and business investment. This counters most arguments of both the automakers who supported the tax break and environmental activists who criticized it.