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## Internal Revenue Code Section 40

Alcohol, etc., used as fuel

(a) General rule.

For purposes of section 38, the alcohol fuels credit determined under this section for the taxable year is an amount equal to the sum of-

- (1) the alcohol mixture credit,
- (2) the alcohol credit,
- (3) in the case of an eligible small ethanol producer, the small ethanol producer credit, plus
- (4) the second generation biofuel producer credit.

(b) Definition of alcohol mixture credit, alcohol credit, and small ethanol producer credit.

For purposes of this section, and except as provided in subsection (h) -

(1) Alcohol mixture credit.

(A) In general. The alcohol mixture credit of any taxpayer for any taxable year is 60 cents for each gallon of alcohol used by the taxpayer in the production of a qualified mixture.

(B) Qualified mixture. The term "qualified mixture" means a mixture of alcohol and gasoline or of alcohol and a special fuel which-

(i) is sold by the taxpayer producing such mixture to any person for use as a fuel, or

(ii) is used as a fuel by the taxpayer producing such mixture.

(C) Sale or use must be in trade or business, etc. Alcohol used in the production of a qualified mixture shall be taken into account-

(i) only if the sale or use described in subparagraph (B) is in a trade or business of the taxpayer, and

(ii) for the taxable year in which such sale or use occurs.

(D) Casual off-farm production not eligible. No credit shall be allowed under this section with respect to any casual off-farm production of a qualified mixture.

(2) Alcohol credit.

(A) In general. The alcohol credit of any taxpayer for any taxable year is 60 cents for each gallon of alcohol which is not in a mixture with gasoline or a special fuel (other than any denaturant) and which during the taxable year-

(i) is used by the taxpayer as a fuel in a trade or business, or

(ii) is sold by the taxpayer at retail to a person and placed in the fuel tank of such person's vehicle.

(B) User credit not to apply to alcohol sold at retail. No credit shall be allowed under subparagraph (A)(i) with respect to any alcohol which was sold in a retail sale described in subparagraph (A)(ii).

(3) Smaller credit for lower proof alcohol.

In the case of any alcohol with a proof which is at least 150 but less than 190, paragraphs (1)(A) and (2)(A) shall be applied by substituting "45 cents" for "60 cents".

(4) Small ethanol producer credit.

(A) In general. The small ethanol producer credit of any eligible small ethanol producer for any taxable year is 10 cents for each gallon of qualified ethanol fuel production of such producer.

(B) Qualified ethanol fuel production. For purposes of this paragraph, the term "qualified ethanol fuel production" means any alcohol which is ethanol which is produced by an eligible small ethanol producer, and which during the taxable year-

(i) is sold by such producer to another person-

(I) for use by such other person in the production of a qualified mixture in such other person's trade or business (other than casual off-farm production),

(II) for use by such other person as a fuel in a trade or business, or

(III) who sells such ethanol at retail to another person and places such ethanol in the fuel tank of such other person, or

(ii) is used or sold by such producer for any purpose described in clause (i).

(C) Limitation. The qualified ethanol fuel production of any producer for any taxable year shall not exceed 15,000,000 gallons (determined without regard to any qualified second generation biofuel production).

(D) Additional distillation excluded. The qualified ethanol fuel production of any producer for any taxable year shall not include any alcohol which is purchased by the producer and with respect to which such producer increases the proof of the alcohol by additional distillation.

(5) Adding of denaturants not treated as mixture.

The adding of any denaturant to alcohol shall not be treated as the production of a mixture.

(6) Second generation biofuel producer credit.

(A) In general. The second generation biofuel producer credit of any taxpayer is an amount equal to the applicable amount for each gallon of qualified second generation biofuel production.

(B) Applicable amount. For purposes of subparagraph (A), the applicable amount means \$1.01, except that such amount shall, in the case of second generation biofuel which is alcohol, be reduced by the sum of-

(i) the amount of the credit in effect for such alcohol under subsection (b)(1) (without regard to subsection (b)(3)) at the time of the qualified second generation biofuel production, plus

(ii) in the case of ethanol, the amount of the credit in effect under subsection (b)(4) at the time of such production.

(C) Qualified second generation biofuel production. For purposes of this section, the term "qualified second generation biofuel production" means any second generation biofuel which is produced by the taxpayer, and which during the taxable year-

(i) is sold by the taxpayer to another person-

(I) for use by such other person in the production of a qualified second generation biofuel mixture in such other person's trade or business (other than casual off-farm production),

(II) for use by such other person as a fuel in a trade or business, or

(III) who sells such second generation biofuel at retail to another person and places such second generation biofuel in the fuel tank of such other person, or

(ii) is used or sold by the taxpayer for any purpose described in clause (i) .

The qualified second generation biofuel production of any taxpayer for any taxable year shall not include any alcohol which is purchased by the taxpayer and with respect to which such producer increases the proof of the alcohol by additional distillation.

(D) Qualified second generation biofuel mixture. For purposes of this paragraph, the term "qualified second generation biofuel mixture" means a mixture of second generation biofuel and gasoline or of second generation biofuel and a special fuel which-

(i) is sold by the person producing such mixture to any person for use as a fuel, or

(ii) is used as a fuel by the person producing such mixture.

- (E) Second generation biofuel. For purposes of this paragraph-
- (i) In general. The term "second generation biofuel" means any liquid fuel which-
    - (I) is derived by, or from, qualified feedstocks, and
    - (II) meets the registration requirements for fuels and fuel additives established by the Environmental Protection Agency under section 211 of the Clean Air Act (42 U.S.C. 7545).
  - (ii) Exclusion of low-proof alcohol. The term "second generation biofuel" shall not include any alcohol with a proof of less than 150. The determination of the proof of any alcohol shall be made without regard to any added denaturants.
  - (iii) Exclusion of certain fuels. The term "second generation biofuel" shall not include any fuel if-
    - (I) more than 4 percent of such fuel (determined by weight) is any combination of water and sediment
    - (II) the ash content of such fuel is more than 1 percent (determined by weight), or
    - (III) such fuel has an acid number greater than 25.
- (F) Qualified feedstock. For purposes of this paragraph, the term "qualified feedstock" means-
- (i) any lignocellulosic or hemicellulosic matter that is available on a renewable or recurring basis, and
  - (ii) any cultivated algae, cyanobacteria, or lemna.
- (G) Special rules for algae. In the case of fuel which is derived by, or from, feedstock described in subparagraph (F)(ii) and which is sold by the taxpayer to another person for refining by such other person into a fuel which meets the requirements of subparagraph (E)(i)(II) and the refined fuel is not excluded under subparagraph (E)(iii)-
- (i) such sale shall be treated as described in subparagraph (C)(i),
  - (ii) such fuel shall be treated as meeting the requirements of subparagraph (E)(i)(II) and as not being excluded under subparagraph (E)(iii) in the hands of such taxpayer, and
  - (iii) except as provided in this subparagraph, such fuel (and any fuel derived from such fuel) shall not be taken into account under subparagraph (C) with respect to the taxpayer or any other person.

(H) Allocation of second generation biofuel producer credit to patrons of cooperative. Rules similar to the rules under subsection (g)(6) shall apply for purposes of this paragraph.

(I) Registration requirement. No credit shall be determined under this paragraph with respect to any taxpayer unless such taxpayer is registered with the Secretary as a producer of second generation biofuel under section 4101.

(J) Application of paragraph.

(i) In general. This paragraph shall apply with respect to qualified second generation biofuel production after December 31, 2008, and before January 1, 2022.

(ii) No carryover to certain years after expiration. If this paragraph ceases to apply for any period by reason of clause (i), rules similar to the rules of subsection (e)(2) shall apply.

(c) Coordination with exemption from excise tax.

The amount of the credit determined under this section with respect to any alcohol shall, under regulations prescribed by the Secretary, be properly reduced to take into account any benefit provided with respect to such alcohol solely by reason of the application of section 4041(b)(2) , section 6426 , or section 6427(e) .

(d) Definitions and special rules.

For purposes of this section-

(1) Alcohol defined.

(A) In general. The term "alcohol" includes methanol and ethanol but does not include-

(i) alcohol produced from petroleum, natural gas, or coal (including peat),  
or

(ii) alcohol with a proof of less than 150.

(B) Determination of proof. The determination of the proof of any alcohol shall be made without regard to any added denaturants.

(2) Special fuel defined.

The term "special fuel" includes any liquid fuel (other than gasoline) which is suitable for use in an internal combustion engine.

(3) Mixture or alcohol not used as a fuel, etc.

(A) Mixtures. If-

(i) any credit was determined under this section with respect to alcohol used in the production of any qualified mixture, and

(ii) any person-

(I) separates the alcohol from the mixture, or

(II) without separation, uses the mixture other than as a fuel,

then there is hereby imposed on such person a tax equal to 60 cents a gallon (45 cents in the case of alcohol with a proof less than 190) for each gallon of alcohol in such mixture.

(B) Alcohol. If-

(i) any credit was determined under this section with respect to the retail sale of any alcohol, and

(ii) any person mixes such alcohol or uses such alcohol other than as a fuel,

then there is hereby imposed on such person a tax equal to 60 cents a gallon (45 cents in the case of alcohol with a proof less than 190) for each gallon of such alcohol.

(C) Small ethanol producer credit. If-

(i) any credit was determined under subsection (a)(3), and

(ii) any person does not use such fuel for a purpose described in subsection (b)(4)(B),

then there is hereby imposed on such person a tax equal to 10 cents a gallon for each gallon of such alcohol.

(D) Second generation biofuel producer credit. If-

(i) any credit is allowed under subsection (a)(4), and

(ii) any person does not use such fuel for a purpose described in subsection (b)(6)(C),

then there is hereby imposed on such person a tax equal to the applicable amount (as defined in subsection (b)(6)(B)) for each gallon of such second generation biofuel.

(E) Applicable laws. All provisions of law, including penalties, shall, insofar as applicable and not inconsistent with this section, apply in respect of any tax imposed under subparagraph (A) , (B) , (C), or (D) as if such tax were imposed by section 4081 and not by this chapter.

(4) Volume of alcohol.

For purposes of determining under subsection (a) the number of gallons of alcohol with respect to which a credit is allowable under subsection (a) , the volume of alcohol shall include the volume of any denaturant (including gasoline) which is added under any formulas approved by the Secretary to the extent that such denaturants do not exceed 2 percent of the volume of such alcohol (including denaturants).

(5) Pass-thru in the case of estates and trusts.

Under regulations prescribed by the Secretary, rules similar to the rules of subsection (d) of section 52 shall apply.

(6) Special rule for second generation biofuel producer credit.

No second generation biofuel producer credit shall be determined under subsection (a) with respect to any second generation biofuel unless such second generation biofuel is produced in the United States and used as a fuel in the United States. For purposes of this subsection, the term "United States" includes any possession of the United States.

(7) Limitation to alcohol with connection to the United States.

No credit shall be determined under this section with respect to any alcohol which is produced outside the United States for use as a fuel outside the United States. For purposes of this paragraph, the term "United States" includes any possession of the United States.

(e) Termination.

(1) In general.

This section shall not apply to any sale or use-

(A) for any period after December 31, 2011, or

(B) for any period before January 1, 2012, during which the rates of tax under section 4081(a)(2)(A) are 4.3 cents per gallon.

(2) No carryovers to certain years after expiration.

If this section ceases to apply for any period by reason of paragraph (1), no amount attributable to any sale or use before the first day of such period may be carried under section 39 by reason of this section (treating the amount allowed by reason of this section as the first amount allowed by this subpart) to any taxable year beginning after the 3-taxable-year period beginning with the taxable year in which such first day occurs.

(3) Exception for second generation biofuel producer credit.

Paragraph (1) shall not apply to the portion of the credit allowed under this section by reason of subsection (a)(4).

(f) Election to have alcohol fuels credit not apply.

(1) In general.

A taxpayer may elect to have this section not apply for any taxable year.

(2) Time for making election.

An election under paragraph (1) for any taxable year may be made (or revoked) at any time before the expiration of the 3-year period beginning on the last date prescribed by law for filing the return for such taxable year (determined without regard to extensions).

(3) Manner of making election.

An election under paragraph (1) (or revocation thereof) shall be made in such manner as the Secretary may by regulations prescribe.

(g) Definitions and special rules for eligible small ethanol producer credit.

For purposes of this section-

(1) Eligible small ethanol producer.

The term "eligible small ethanol producer" means a person who, at all times during the taxable year, has a productive capacity for alcohol (as defined in subsection (d)(1)(A) without regard to clauses (i) and (ii)) not in excess of 60,000,000 gallons.

(2) Aggregation rule.

For purposes of the 15,000,000 gallon limitation under subsection (b)(4)(C) and the 60,000,000 gallon limitation under paragraph (1), all members of the same controlled group of corporations (within the meaning of section 267(f)) and all persons under common control (within the meaning of section 52(b) but determined by treating an interest of more than 50 percent as a controlling interest) shall be treated as 1 person.

(3) Partnership, S corporations, and other pass-thru entities.

In the case of a partnership, trust, S corporation, or other pass-thru entity, the limitations contained in subsection (b)(4)(C) and paragraph (1) shall be applied at the entity level and at the partner or similar level.

(4) Allocation.

For purposes of this subsection, in the case of a facility in which more than 1 person has an interest, productive capacity shall be allocated among such persons in such manner as the Secretary may prescribe.

(5) Regulations.

The Secretary may prescribe such regulations as may be necessary-

(A) to prevent the credit provided for in subsection (a)(3) from directly or indirectly benefiting any person with a direct or indirect productive capacity of more than 60,000,000 gallons of alcohol during the taxable year, or

(B) to prevent any person from directly or indirectly benefiting with respect to more than 15,000,000 gallons during the taxable year.

(6) Allocation of small ethanol producer credit to patrons of cooperative.

(A) Election to allocate.

(i) In general. In the case of a cooperative organization described in section 1381(a), any portion of the credit determined under subsection (a)(3) for the taxable year may, at the election of the organization, be apportioned pro rata among patrons of the organization on the basis of the quantity or value of business done with or for such patrons for the taxable year.

(ii) Form and effect of election. An election under clause (i) for any taxable year shall be made on a timely filed return for such year. Such election, once made, shall be irrevocable for such taxable year. Such election shall not take effect unless the organization designates the apportionment as such in a written notice mailed to its patrons during the payment period described in section 1382(d).

(B) Treatment of organizations and patrons.



(i) Organizations. The amount of the credit not apportioned to patrons pursuant to subparagraph (A) shall be included in the amount determined under subsection (a)(3) for the taxable year of the organization.

(ii) Patrons. The amount of the credit apportioned to patrons pursuant to subparagraph (A) shall be included in the amount determined under such subsection for the first taxable year of each patron ending on or after the last day of the payment period (as defined in section 1382(d) ) for the taxable year of the organization or, if earlier, for the taxable year of each patron ending on or after the date on which the patron receives notice from the cooperative of the apportionment.

(iii) Special rules for decrease in credits for taxable year. If the amount of the credit of the organization determined under such subsection for a taxable year is less than the amount of such credit shown on the return of the organization for such year, an amount equal to the excess of-

(I) such reduction, over

(II) the amount not apportioned to such patrons under subparagraph (A) for the taxable year,

shall be treated as an increase in tax imposed by this chapter on the organization. Such increase shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit under this chapter or for purposes of section 55.

(h) Reduced credit for ethanol blenders.

(1) In general.

In the case of any alcohol mixture credit or alcohol credit with respect to any sale or use of alcohol which is ethanol during calendar years 2001 through 2011-

(A) subsections (b)(1)(A) and (b)(2)(A) shall be applied by substituting "the blender amount" for "60 cents",

(B) subsection (b)(3) shall be applied by substituting "the low-proof blender amount" for "45 cents" and "the blender amount" for "60 cents", and

(C) subparagraphs (A) and (B) of subsection (d)(3) shall be applied by substituting "the blender amount" for "60 cents" and "the low-proof blender amount" for "45 cents".

(2) Amounts.

For purposes of paragraph (1), the blender amount and the low-proof blender amount shall be determined in accordance with the following table:

In the case of any sale or use during calendar year:	The blender amount is:	The low-proof blender amount is:
2001 or 2002	53 cents	39.26 cents
2003 or 2004	52 cents	38.52 cents
2005, 2006, 2007, or 2008	51 cents	37.78 cents
2009 through 2011	45 cents	33.33 cents.

- (3) Reduction delayed until annual production or importation of 7,500,000,000 gallons.
- (A) In general. In the case of any calendar year beginning after 2008, if the Secretary makes a determination described in subparagraph (B) with respect to all preceding calendar years beginning after 2007, the last row in the table in paragraph (2) shall be applied by substituting "51 cents" for "45 cents".
- (B) Determination. A determination described in this subparagraph with respect to any calendar year is a determination, in consultation with the Administrator of the Environmental Protection Agency, that an amount less than 7,500,000,000 gallons of ethanol (including cellulosic ethanol) has been produced in or imported into the United States in such year.