Montana State Legislature

Exhibit Number: 10

Exhibit 10 has several different documents.

1. **Letter from Larry Johnson**
2. **RFA Public Policy**
3. **GAO – Resources, Community, and Economic Development Division.**
4. **RFA Report "Homegrown for the Homeland" - Ethanol Industry Outlook 2005 [Index Scanned]**

This exhibit has several different documents with numerous pages in each; it consequently exceeds the amount that can be scanned. Therefore we have scanned a small portion for your research. The original exhibit is on file at the Montana Historical Society and may be viewed there

EXHIBIT 10
DATE 2/10/05
HB 464

FROM THE DESK OF LARRY JOHNSON

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STATE PRODUCER PAYMENTS, THE RATIONALE AND EFFECTS

February 10, 2005

It is not a coincidence that much of the dry mill ethanol production that has come on line in the past 10 years has been in states with some form of state incentives. The original idea of producer payments began when marketplace incentives for in-state produced ethanol were ruled to be in violation of interstate commerce. Minnesota and Nebraska were the first states to offer producer payments because they realized the reluctance of investors and bankers to invest in a new and unproven industry. A direct producer payment provided a strong statement that the state encouraged the development of an ethanol industry and would provide a guaranteed cash flow contribution to facilitate debt service and lower risk.

Minnesota's Governor Perpich provided strong leadership in 1986 by establishing a $10 million fund to provide 20¢/gallon to any Minnesota ethanol producer able to finance and build a production facility. He had the vision to realize the state accepted no financial obligation; until the investments were made, the construction was completed, the jobs were in place, the ethanol was produced and the value was added to the agricultural raw materials. The initial $10 million cap has been raised many times to accommodate the expanding industry and has resulted in cumulative General Fund payments of more than $300 million. Despite this significant budget expenditure, nearly all Minnesota policy makers are proud and supportive, most of them wanting to take some credit for their part in creating a vibrant new industry in Minnesota. Many economic analysis have reported returns to the state of as much as $12 for every public $1 invested. Today, Minnesota's ethanol producers produce more than 400 million gallons of ethanol; adding $600 million to the tax base, both direct and spin-off jobs, investor profits and more than $100 million in annual value to the state corn crop, in addition to having revitalized many rural communities.

Many other states, including Montana, South Dakota, Missouri, Iowa, Illinois, Indiana, Texas, Mississippi, Kansas and Oklahoma now offer a variety of incentives to attract new ethanol production facilities, although Only Iowa and South Dakota have been able to match the success of Minnesota and Nebraska. South Dakota and Iowa production capacity was built later; following proven successes in Minnesota and Nebraska, availability of low priced and abundant corn and proximity to cattle feedlots to utilize the wet distillers grains. It appears that Corn belt states offering a simple and direct cash payment for ethanol production have been much more successful in attracting production than non-Corn belt states with more complicated state incentive schemes. It is a fact of life that money will flow to where there is a lower perceived risk; and ethanol from anything other than corn is still perceived as carrying a higher risk.

The Voice of the Ethanol Industry

RFA
Renewable Fuels Association

A "Volumetric Ethanol Excise Tax Credit" Eliminates the Impact of the Ethanol Tax Incentive on the Highway Trust Fund

Under current law, the excise tax on gasoline is 18.4 ¢ per gallon. The tax is collected on a quarterly basis using the Form 720. The tax is deposited into the General Fund (GF), where the LUST transfer of .1¢ is deducted, the remainder is transferred to the Highway Trust Fund (HTF). Once in the HTF, a transfer of 2.86¢ is deposited into the Mass Transit Fund. The same process takes place for ethanol, except that due to the partial excise tax exemption, ethanol blended gasoline only remits 13.2¢ to the GF (18.4 – 5.2); and an additional 2.5¢ is transferred from the HTF to the GF for deficit reduction purposes. Thus, under current law, the HTF realizes the following revenue from gasoline and ethanol blended fuels:

Current Law

	Gasoline	E-10
Gas Tax	18.4	18.4
Excise Tax Exemption		(5.2)
Deposited to GF	18.4	13.2 (paid by blender)
LUST Transfer	(0.1)	(0.1)
Transferred to HTF	18.3	13.1
Deficit Reduction Transfer		(2.5)
Mass Transit Fund Transfer	(2.86)	(2.86)
Benefit to HTF	15.44¢	7.74¢

By creating a new "Volumetric Ethanol Excise Tax Credit," the tax collection system would change slightly, allowing all "gasoline" and "ethanol-blended gasoline" to contribute 18.4¢ per gallon to the General Fund, which would then be transferred to the Highway Trust Fund. The effect on the blender or marketer would not change. Under the proposal, the HTF would realize the following benefit on gasoline and ethanol blended fuels:

Proposal

	Gasoline	E10	VEETC

gasoline tax.
- All blenders, big, small, and "At the Rack" will continue to receive the benefit of the tax incentive on a quarterly basis.
- "Below the Rack" blenders will receive the benefit of the tax incentive within 20 days.
- Given that the system will be based on gallons of ethanol rather than current blend rates (5.7%, 7.7% and 10%), E85 will qualify for the credit, and would no longer be limited to the income tax credit.
- Ethanol supporters will be able to work with the transportation industry on meeting the multiple goals of supporting the ethanol and petroleum industries, while at the same time supporting a robust highway trust fund.
  - It is estimated that the new "Volumetric Ethanol Excise Tax Credit" will contribute an average of an additional $2 billion per year into the Highway Trust Fund over the next 10 years ($1.4 billion through the change to the "ethanol excise tax exemption" and $600 million by eliminating the retention of the 2.5¢ used for deficit reduction).
- The alternative minimum tax (AMT) does not become an issue for any blender, related to the ethanol tax incentive.
- The §40, alcohol fuels tax credit, is still available to blenders.

Petroleum Industry

- Simplification.
- One system and one credit for "At the Rack" blenders
  - easy to use,
  - easy to measure,
  - easy to keep track of, and
  - easy to certify gallons
- A streamlined and more efficient system for "Below the Rack" Blenders
  - 20 day electronic refund process should insure no negative impacts on the time value of money. If a blender buys gasoline and ethanol below the rack on April 1 the blender will have a tax refund check by April 20.

Internal Revenue Service

- Simplification
- A system to track the volume of ethanol used will be more efficient than the current system.
- Certification of gallons through gallon receipts will simplify the process.

Ethanol and the Highway Trust Fund (in cents)

I. Current Law:

100% Gasoline (one gallon)

Tax collected to General Fund (GF)	18.40
Transferred from GF to LUST	(0.10)

[4]§9053(b)

[5]§9053(b)

[6]New Section of IRC§6426, and listed on Form 720 as "gallons of ethanol used x 5.2¢. For example: 100 gallons at 5.2¢ = $5.20 "voluetric ethanol tax credit.

[7]§9053(b)(4)(E)

If you have questions or comments, please contact Larry Schafer at the Renewable Fuels Association at (202)289-3835.

Return to RFA Home Page

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GAO
Accountability * Integrity * Reliability

United States General Accounting Office
Washington, DC 20548

Resources, Community, and
Economic Development Division

B-286311

September 25, 2000

The Honorable Tom Harkin
Ranking Minority Member
Committee on Agriculture,
Nutrition, and Forestry
United States Senate

Subject: Petroleum and Ethanol Fuels: Tax Incentives and Related GAO Work

Dear Senator Harkin:

Over the years, the federal government has granted tax incentives, direct subsidies, and other support to the petroleum industry, as well as some tax and other benefits to the ethanol industry, in an effort to enhance U.S. energy supplies. The tax incentives generally decrease revenues accruing to the U.S. Treasury. In earlier reports, we addressed various issues related to these incentives, including their impact on federal revenues and effectiveness in accomplishing their objectives.

You requested that we provide you with information on the tax incentives[1] that benefit the petroleum and ethanol[2] industries. Accordingly, we are providing revenue loss estimates for tax incentives designed to encourage the exploration and production of petroleum and the production of ethanol (see enc. I). In addition to this specific information, we are providing a summary of key findings from our earlier reports on these and related issues (see enc. II). We used the enclosed material to brief your staff on June 30, 2000. A summary of the tax incentive information follows.

[1]Tax incentives are federal tax provisions that grant special tax relief designed to encourage certain kinds of behavior by taxpayers or to aid taxpayers in special circumstances. The revenue losses that result from these provisions–called tax expenditures–may, in effect, be viewed as spending channeled through the tax system. The Congressional Budget and Impoundment Control Act of 1974 requires that a list of tax expenditures be included in the budget. The act defines "tax expenditures" as "revenue losses attributable to provisions of Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability." Each year, estimates of tax expenditure revenue losses are prepared by the Department of the Treasury and by the staff of the Joint Committee on Taxation. According to the Committee, these special income tax provisions are referred to as tax expenditures because they may be considered as analogous to direct outlay programs, and the provisions and programs can be considered as alternative means of accomplishing similar budget policy objectives.

[2]Under the Internal Revenue Code, a tax exemption and/or tax credits are available for any biomass-derived alcohol fuel, including ethanol and methanol. However, alcohol fuel derived from petroleum or natural gas does not qualify for the exemption or the credits.

The estimated revenue losses for these tax incentives should not be added together. The estimate for each tax incentive is made independently of any other tax incentive, and the effect of making more than one change might be greater than or less than the sum of the changes. Enclosure I contains more detailed information on these estimates of revenue losses from the petroleum and ethanol tax incentives (see tables 2-9), as well as descriptions of the incentives and summaries of their legislative histories.

Scope and Methodology

To prepare the information for this report, we compiled Treasury's and JCT's yearly revenue loss estimates for tax incentives received by the petroleum and ethanol industries. Treasury's estimates are from annual editions of the *Budget of the United States Government*, Analytical Perspectives volume, Tax Expenditures section. JCT's estimates are from annual editions of the *Estimates of Federal Tax Expenditures*. To put the dollar amounts for different years on a comparable basis, we adjusted these estimates for inflation, using a fiscal year gross domestic product (GDP) deflator.[3] Descriptions of the tax incentives and their legislative histories are from JCT's *Present-Law Tax Rules Relating to Domestic Oil and Gas Exploration and Production and Description of H.R. 53 and H.R. 423* (JCX-8-99, Feb. 23, 1999) and the Senate Committee on the Budget's *Tax Expenditures: Compendium of Background Material on Individual Provisions* (Dec. 1996). Additionally, we reviewed and summarized previous GAO studies related to petroleum and ethanol tax incentives and other subsidy programs. We conducted our work from July through September 2000 in accordance with generally accepted government auditing standards.

Unless you publicly announce its contents earlier, we plan no further distribution of this report until 14 days after the date of this letter. At that time, we will send copies to interested Members of Congress and make copies available to others on request.

If you have any questions about this report or need additional information, please call Daniel Haas or Godwin Agbara at (202) 512-3841.

Sincerely yours,

Jim Wells
Director, Energy, Resources,
and Science Issues

Enclosures - 2

[3]The deflator was obtained from the *Budget of the United States Government, Fiscal Year 2001*, Historical Tables volume, table 10.1.