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The Pricing of Ethanol Blended Gasoline

Beginning in 1978, federal law has provided for an excise tax exemption for gasoline with ethanol and there have been several minor changes made over the years. The original intent of the legislation was to provide ethanol with a federal tax exemption, leveling the playing field with the tax breaks provided gasoline and enabling ethanol to compete in the marketplace with highly subsidized petroleum products.

How the Federal Tax Exemption works

Today the Federal Excise Tax on unblended gasoline is 18.4¢ per gallon and a 10% ethanol blend is taxed at a rate of 13.3¢ per gallon; **a 5.1¢ difference**. Therefore, 10 gallons of gasoline pays \$1.84 in federal taxes and 9 gallons of gasoline blended with 1 gallon of ethanol pays \$1.33 in federal taxes; **a 51¢ difference**. This allows a gasoline distributor to pay 51¢ more for a gallon of ethanol than the wholesale (or rack) price of gasoline and retain the same profit margin. Remember the consumer pays \$1.84 in federal taxes on 10 gallons of gasoline whether it is an ethanol blend or not, however when the gasoline marketer sells an ethanol blend, **the marketer only passes on \$1.33 to the government, pocketing the rest!**

How the market works to establish price

We have all wondered why posted gasoline prices can move up as much as 10¢ per gallon overnight and no one can provide a satisfactory answer except to say it is "supply and demand." It gets even more difficult to understand when 10% of the product is ethanol, with a different supply source than gasoline and different pricing factors. Yes, the national supply and demand for ethanol certainly affects prices but history shows that ethanol, minus the 5.1 ¢ tax exemption is nearly always cheaper than gasoline, providing the gasoline marketer with a lower priced product.

The real world case in Minnesota

Minnesota instituted a mandate for ethanol blends in 1997 and it was implemented without difficulty and maintained without controversy ever since. Not only are ethanol blends used in all types of engines but an analysis by the state has demonstrated that replacing 10% of the gasoline demand with ethanol has lowered the pump price for the consumer.

The attached chart provides an indication of the increased gasoline margins for blending ethanol using actual prices in three separate scenarios. Each case reflects a gross operating margin of 15¢ per gallon for the retailer and a selling price for midrange gasoline at 7¢ per gallon over unleaded.

1. Historic, average pricing of gasoline and ethanol prior to the year 2000 when energy prices began the move to the current higher level.
2. The actual prices six months ago, during September of 2005
3. Today's prices. During the past six weeks gasoline prices have risen, while ethanol prices have actually decreased, reflecting a temporary change in market conditions and market psychology.

All three scenarios reflect a lower net cost of an ethanol blend to the gasoline marketing system. Why is that not passed on to the consumer?

	Octane Rating	Ave.Rack Price/Gal	Price of 10 Gals.	Federal Exise tax	State Gas tax	Cost per Gallon, Product + taxes	Price Advantage, Product + taxes	Est. Sales Price	Gross Margin for the Retailer
Gasoline 87 Octane Pre-2000	87	Gasoline \$0.90	\$9.00	\$0.184	\$0.27	\$1.354		\$1.504	\$0.15
Blend :9 Gals. Gas +1 Gal. Ethanol Pre-2000	89.5	Ethanol \$1.25	\$9.35	\$0.133	\$0.27	\$1.338	\$0.016¢ /Gallon	\$1.574 7 cents Midrange Premium	\$0.236
Gasoline 87 Octane Sep. 2004	87	Gasoline \$1.35	\$13.50	\$0.184	\$0.27	\$1.804		\$1.954	\$0.15
Blend :9 Gals. Gas +1 Gal. Ethanol Sep. 2004	89.5	Ethanol \$1.67	\$13.82	\$0.133	\$0.27	\$1.785	\$0.019¢ /Gallon	\$2.024 7 cents Midrange Premium	\$0.239
Gasoline 87 Octane March 2005	87	Gasoline \$1.62	\$16.20	\$0.184	\$0.27	\$2.074		\$2.224	\$0.15
Blend :9 Gals. Gas +1 Gal. Ethanol March 2005	89.5	Ethanol \$1.35	\$15.93	\$0.133	\$0.27	\$1.996	\$0.078¢ /Gallon	\$2.2947 cents Midrange Premium	\$0.298