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Tribal Gaming Revenue Allocations

Ethanol Producer Grant Program (Agriculture, Trade and Consumer Protection)

[LFB 2003-05 Budget Summary: Page 51, #3]

CURRENT LAW

1999 Act 55 created an ethanol producer grant program for annual payments of 20¢ per gallon to qualifying producers for up to 15 million gallons ($3 million per producer maximum) of ethanol produced in a 12-month period in Wisconsin. As specified by administrative rule ATCP 161, an ethanol plant must produce 10 million gallons of ethanol in the 12 months prior to the March 1 application deadline in order to be eligible for a grant under this program. Further, in order to be eligible for state grant payments, the producer must not have began producing ethanol in this state more than 60 months before the end of the production period identified in the producer's payment application. The program is scheduled to sunset on June 30, 2006. Fiscal year 2002-03, is the first year funds have been provided, with a total of $2,945,000 for ethanol producer grants appropriated ($1,045,000 GPR and $1,900,000 PR from tribal gaming revenues). ATCP 161 specifies that if the sum of all awards for a given year exceeds available funding, the grants be prorated based on eligible production.

For 2002-03, the Badger State Ethanol plant in Monroe (which produced 13,161,443 gallons of ethanol) and the Ace Ethanol plant in Stanley (which produced 10,508,286 gallons of ethanol) both qualified for, and received, grants.

GOVERNOR

Delete $1,045,000 GPR annually for grants to ethanol producers. This would leave $1,900,000 annually from tribal gaming program revenue for grants under the ethanol producer grant program in the 2003-05 biennium.

DISCUSSION POINTS

1. Although ethanol can be produced from various starch sources, over 90% of U.S. ethanol is made from corn. It is estimated that in 2002, 2.13 billion gallons of ethanol were produced using more than 800 million bushels of corn. Wisconsin ranks tenth among states in the production of corn for grain, harvesting 330 million bushels in 2001. Approximately 5.8 million bushels of corn are used to produce 15 million gallons of ethanol (one bushel of corn is equivalent to approximately 2.6 gallons of ethanol).

2. Some have estimated the price of corn increases by 5¢ to 10¢ per bushel for growers near ethanol plants. The Congressional Research Service indicates that when corn supplies are plentiful, the use of every 100 million bushels of corn for ethanol raises the national price of corn by 4¢ per bushel. When corn supplies are limited, the price impact is higher. In addition to its impact on commodity prices, an ethanol plant also may give local farmers a more stable market for their grain.

3. Two ethanol plants in Wisconsin, Ace Ethanol in Stanley (25 million gallon capacity) and Badger State Ethanol in Monroe (40 million gallon capacity), produced enough ethanol to qualify for an ethanol producer grant in 2002-03. In addition, the following table shows five other ethanol production plants that have been proposed or are currently under construction in Wisconsin.

TABLE 1

Proposed Ethanol Production Facilities

Municipality	County	Stage	Proposed Capacity (gallons per year)
Arlington	Columbia	Proposed	40,000,000
Augusta	Eau Claire	Proposed	20,000,000
Cambria	Columbia	Proposed	20,000,000
Colfax	Dunn	Proposed	40,000,000
Utica	Winnebago	Testing Equipment	25,000,000

4. State law requires state employees to use gasohol (an ethanol mix of up to 10%) or alternative fuel for the operation of all state-owned or state-leased motor vehicles whenever feasible. In addition, the federal Clean Air Act requires the use of reformulated gasoline or oxygenated fuels

in Kenosha, Milwaukee, Ozaukee, Racine, Washington and Waukesha Counties due to significant ozone levels in Southeastern Wisconsin. Most of the federal requirement is met through the use of a reformulated gasoline that is mixed with up to 10% ethanol.

5. The Department of Administration (DOA) estimates that in 2001, 85.9 million gallons of ethanol were used in Wisconsin (67.4 million gallons in reformulated gasoline and 18.5 million gallons blended as gasohol). In 2002, it is estimated that 88.2 million gallons were used (71.2 million in reformulated gasoline and 17 million gallons blended for gasohol).

Other Ethanol Production Incentives

6. A federal tax reduction of 5.2¢, which will be reduced to 5.1¢ in 2005, per gallon of gasoline mixed with up to 10% ethanol is in place through 2007. This incentive translates to a federal subsidy of approximately 52¢ per gallon of ethanol produced. While this subsidy serves to promote ethanol, it also reduces the amount of funding the state receives in federal highway aid, by reducing the total amount of federal fuel taxes collected, which are divided among the states.

7. Some states also provide tax reductions for gasohol. Iowa offers a 1¢ per gallon tax reduction for gasohol, South Dakota offers a tax reduction of 2¢ per gallon for gasohol, and Illinois offers a sales tax reduction of 1.875% (from 6.25% to 4.375%) for gasohol with 10% ethanol or higher.

8. Other states also offer ethanol production incentives. Nebraska offers an ethanol production incentive of 18¢ per gallon of ethanol produced, for all plants that produce a minimum of 100,000 gallons annually prior to June 30, 2004. The producer is eligible to receive credits for 96 consecutive months (eight years), with the program expiring on June 30, 2012. Producers may receive credit for a maximum of 15,625,000 gallons of ethanol produced per year (maximum payment of $2,812,500 annually), or 125,000,000 gallons over their 96 month period of eligibility. North Dakota also offers an ethanol production incentive program. It offers ethanol producers in operation before July 1, 1995, with production capacity of less than 15 million gallons, a 40¢ per gallon of ethanol produced incentive, up to $750,000 per fiscal year. Ethanol producers that were in operation before July 1, 1995, with production capacity of more than 15 million gallons of ethanol per fiscal year, or ethanol producers that began operation after June 30, 1995, are eligible to receive up to $500,000 in production incentives per fiscal year (at 40¢ per gallon). This program is set to expire at the end of 2009. Neither Illinois nor Indiana offer any ethanol production incentives.

9. Estimated 2003 full capacity (for all operating ethanol plants as well as those expected to be finished) of ethanol production for area states is listed in Table 2. Estimated 2003 total ethanol production capacity for the U.S. is 3.2 billion gallons of ethanol.

TABLE 2

Estimated Ethanol Production Capacity 2003

State	Capacity in Gallons
Illinois	766,000,000
Iowa	695,000,000
Nebraska	422,000,000
Minnesota	393,600,000
South Dakota	371,000,000
Indiana	95,000,000
Missouri	80,000,000
Kansas	79,500,000
Wisconsin	79,000,000
Michigan	45,000,000
North Dakota	33,500,000
Total	3,059,600,000

10. Some argue that if Wisconsin is to increase its ethanol production capacity, the state should offer ethanol production grants in order to stimulate the industry. Others argue that ethanol production subsidies have marginal effects on ethanol production, as Illinois offers no ethanol production subsidy, yet leads the nation in ethanol production.

11. Minnesota currently has the capacity to produce 393.6 million gallons of ethanol at 14 ethanol plants, and produced 230 million gallons of ethanol in 2002. State law also requires that all gasoline sold or offered for sale in Minnesota contain at least 2.7% oxygen by weight. As a result, it is estimate that 97% of the state's gasoline is blended with ethanol.

12. Faced with budget constraints for the current and upcoming biennium, the state of Minnesota has taken a number of steps to reduce its ethanol production incentive program. Prior to the 2002 Legislative session, Minnesota offered an ethanol production incentive program of 20¢ per gallon of ethanol produced to facilities that began production by June 30, 2000, with a maximum annual payment of $3 million for any one facility, and a maximum of $34 million per facility before the program's scheduled expiration on June 30, 2010. For the 2001-03 biennium, Minnesota originally appropriated $71 million for this program. In Minnesota's 2002 legislative session, the production credit was reduced by one cent per gallon of ethanol produced (to 19¢) for ethanol produced after July 1, 2004. Also, in 2002, $20 million was eliminated from this appropriation (a 28% reduction for the biennium), which led to a 30% reduction in payments due for the quarter ending on December 31, 2002, and the elimination of the remainder of the payments to be made in the biennium. In addition, a current proposal in the Minnesota Legislature would reduce the payment per gallon of ethanol produced to 10¢ per gallon.

13. Ethanol plants may be eligible to participate in Wisconsin economic development

programs through the Department of Commerce. The Wisconsin Development Fund offers grants and loans to businesses for items such as technology development and major economic development. Further, Commerce provides grants and loans through a Rural Economic Development (RED) program, which includes funding for business start-ups in rural areas. It could be argued that the state is already providing incentives for businesses to locate in the state. In addition, if the ethanol industry is offered additional incentives, other industries may seek production subsidies for their products.

Wisconsin Ethanol Grant Program

14. To date, in addition to the two plants that already qualify for state grants, and the Algoma Ethanol plant located in Utica (which is currently testing equipment) four other plants that would qualify for state production subsidies have expressed interest in locating in the state. As a result, some have questioned the necessity of ethanol producer grants. They argue that the two plants currently operating were financed before any funding was authorized for the ethanol producer grant program. Further, they argue that one additional plant has been built, and four more plants are currently proposed in the state despite limited funds available for ethanol producer grants.

15. For the ethanol production period lasting from March 1, 2002, to February 28, 2003, the Badger State Ethanol Plant in Monroe received grants for 13,066,562 gallons of ethanol produced, and the Ace Ethanol Plant in Stanley received grants for 10,508,286 gallons of ethanol produced. Due to total funding of $2,945,000 being available in 2002-03 for these grants, although, the payments to the two qualifying ethanol plants were prorated, with each plant getting around 62% of the amount of grants they were eligible for. Based on total ethanol produced, the two plants qualified for about $4.7 million in state grants. The Badger State plant was eligible for $2,613,300 in grants and received $1,632,300. The Ace plant was eligible for $2,101,700 in grants and received a payment of $1,312,700.

16. Some argue that with two producers who already qualify for the grants, and a third expected to qualify next year, a total subsidy of $1.9 million is insufficient. They argue that the program should aim to provide the statutory maximum of $3 million per producer, to all qualifying ethanol producers. They argue that $1.9 million divided among several producers provides each with an insufficient amount of revenue, and is less than was originally intended to be provided under the program. Further, with limited funding available for subsidies, producers argue that the required prorating of the grants will offset any appeal these subsidies would have to lending institutions that could potentially provide financing for future ethanol plants.

17. Others question the appropriateness of government subsidies for ethanol production at all. They argue that these payments may encourage other industries to seek government subsidies. Some have questioned what makes the ethanol industry more deserving of subsidies than other industries that may argue they could also be successful if given start-up help by the government.

18. Ethanol production grant supporters have argued that state grants for ethanol

production encourage the construction of new ethanol production facilities, which offers new jobs both for the construction of the facility and for the workers in the ethanol production plant. Others argue that under the program the three existing plants are likely to receive the bulk of funds under the program so the incentive for new plant construction is limited. Further, it could be argued that if the ethanol industry holds the potential for profit, the market will devote resources to it. They argue that government intervention in the form of subsidies will only divert resources from more efficient uses. Further, they argue that if the government desires to promote job creation, it could take other actions aside from giving direct subsidies to one particular industry.

19. Ethanol subsidies may help yield higher corn prices that benefit farmers, but businesses and consumers would also be faced with higher corn prices. While these increased corn prices economically help corn farmers, they subject consumers to higher prices, and force businesses to deal with higher costs of production.

20. The ethanol producer grant program is sunset on June 30, 2006. While this minimizes the state's potential future liability from providing an ethanol subsidy, some argue it decreases the investment confidence of ethanol producers and their lenders. Supporters of state ethanol subsidies have argued that ethanol producers have not been able to take full advantage of the subsidies due to the uncertainty that surrounds them. They argue that the state should enter into contracts with plants that are currently eligible for the grants so that these plants can use this guaranteed revenue to leverage loans and other debt. Others argue that guaranteeing state subsidies to a single industry would set a new precedent, and would unfairly shield the industry from budget reductions if tight fiscal circumstances arise. Further, it can be argued that if the purpose of ethanol producer grants is to help spur the start-up of ethanol plants across the state, then grants should not be offered to plants that are already built.

21. Due to groundwater contamination concerns relating to the use of methyl tertiary butyl ether (MTBE), a petroleum-based product, as an oxygenate in gasoline, the market for ethanol is expanding. Ethanol can be used as a substitute for MTBE, and federal Clean Air Act regulations require the use of oxygenated fuels in certain areas (including southeast Wisconsin). For instance, the state of California has banned the used of MTBE effective earlier this year, and ethanol-blended fuels are estimated to account for approximately 80 percent of the market in 2003. However, it is also possible that federal vehicular emission standards could be relaxed, which could reduce the demand for ethanol. Further, the profitability of ethanol production facilities would be adversely affected if federal subsidies were not reauthorized in 2007.

ALTERNATIVES

1. Approve the Governor's recommendation to eliminate annual base funding of $1,045,000 GPR for grants to ethanol producers. This would leave $1.9 million in tribal gaming program revenue available for ethanol producer grants annually.

2. Provide $1,045,000 GPR annually to continue the current level of funding for

ethanol producer grants ($2,945,000 annually).

Alternative 2	**GPR**
2003-05 FUNDING (Change to Bill)	$2,090,000

3. Adopt the Governor's recommendation to eliminate annual base funding of $1,045,000 GPR and, in addition, eliminate annual base funding of $1,900,000 PR (from tribal gaming revenues). This would eliminate all funding for the ethanol producer grant program.

Alternative 3	**PR**
2003-05 FUNDING (Change to Bill)	**-** $3,800,000

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