

Memorandum

TO: Iowa Legislator's Clean Fuels Panel
FR: Douglas A. Durante, Executive Director, Clean Fuels Development Coalition
DA: June 30, 1999
RE: CFDC Iowa Clean Fuels Panel Briefing Follow-up
Cedar Rapids, Iowa
June 22, 1999

Thank you for taking the time to meet with Todd Sneller, Burl Haigwood and myself regarding the fuel ethanol industry and potential clean fuel public policy options for Iowa. On behalf of my colleagues, I believe we covered a lot of information and had a great information exchange.

As you know from the briefing, CFDC supports the development of all oxygenated fuels in an open market approach that will create a sustainable market place, increase the production and use of oxygenated fuels, reduce oil imports and enhance air quality. To reach this goal, we must take into consideration the position of automakers, ethanol producers and the ag community, receive bipartisan political support and withstand the scrutiny of the media and any possible detractors.

With all that in mind we have summarized a few points and outlined several possible options Iowa legislators could begin addressing.

Iowa Ethanol Market Overview

- ◆ Gasoline sales in Iowa are 1.5 billion gpy.
- ◆ An estimated 40% of the state's gasoline contains 10 vol% ethanol blends, or the equivalent of 60 million gpy of ethanol.
- ◆ Ethanol production capacity in Iowa is 418.5 million gpy, we will call it 400 million gpy for this exercise. Therefore, an estimated 340 million gpy of ethanol is exported to other states.
- ◆ If 10-vol% ethanol were blended into 100% of the gasoline sold in Iowa, ethanol demand in the state would increase from 60 million gpy to 150 million gpy, or an increase of 90 million gpy.
- ◆ This increase in ethanol sales would put pressure on state tax revenues to account for the additional 90 million gpy of increased ethanol sales, but would likely result in the construction of new facilities if the tax incentive were structured in a manner to attract investment.
- ◆ Obviously, the majority of fuel ethanol production in the state is exported and receives the tax benefits from surrounding states.

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- ◆ The critical path for the Iowa Legislator's Clean Fuels Panel at this time:
 - ✓ Can/should Iowa invest in protecting the integrity of Midwest ethanol blending programs by modifying current legislation to increase in-state ethanol sales and justify the need for increased ethanol production in the United States?
 - ✓ Do legislators want/need to set an example for other Midwestern states by creating a model ethanol tax incentive program to 1) protect the longer-term out-of-state ethanol sales interests of Iowa ethanol producers and; 2) by creating opportunities in other states to follow suite, increase ethanol demand in other Midwest states and stimulate national ethanol production levels?

Based on the assumption that most Iowa legislators believe increased ethanol production is good for the state and would like to see a logical, sustainable, politically palatable approach that would lead to increased ethanol production in the state, CFDC offers the following insights, legislative options (see Table 1) and recommendations.

About Banning MTBE

- ◆ Banning MTBE is not necessary in Iowa and could actually jeopardize ethanol state tax incentives in Iowa (and other states) with likely court challenges under NAFTA. It also creates a “backdoor ethanol mandate” which could loose appeal by more conservative constituents.
- ◆ Creating an “MTBE cap” of 2.0 vol% will reduce MTBE blending in premium gasoline sales because traditionally those levels are about 5-6 vol%. However, this tactic could also create an opportunity for detractor companies to preempt ethanol blending in the state with lower “trace” volumes of ethanol (i.e., 10 vol% ethanol blends can not be blended if gasoline already contains trace amounts of MTBE due to the 3.5 wt% oxygen limit for gasoline).

Recommendations

- ◆ Repeal the ban on MTBE to protect the longer-term integrity of the program, reduce legal challenges. Under this scenario, like Minnesota, Milwaukee and California, local political and consumers pressures would likely discourage any MTBE entering into the state's gasoline pool.
- ◆ Create a “Iowa Legislators Clean Fuels Panel” to address these ethanol issues in depth and create a solid base of environmental and economic science to support opportunities in other states to increase ethanol sales. This would create an “In My Backyard” attitude for other states and set an example at the federal level to pursue longer-term programs.

⇒ Commission a “Gasoline Quality Survey” to determine the exact amounts of ethanol, MTBE, aromatics and air toxics in the state gasoline pool.

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- ⇒ Commission a “State Ethanol Tax Incentive Cost Benefit Analysis” to determine the impact of various legislative initiatives and the legal viability and the states and create a model for other states.
- ⇒ Commission a statewide “Underground Gasoline Tank Survey” to determine the viability and impact of a statewide fuel ethanol program.
- ⇒ Hold hearings in Iowa to create a record for the national political interests, federal agencies, and detractors of the program.
- ⇒ At this time, CFDC would suggest legislative options #4 or #6 to encourage the development of ethanol in Iowa for local economic stimulation.

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