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BILL ANALYSIS

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Senate Bill 427 (as passed by the Senate)

Sponsor: Senator Harmon Cropsey

Committee: Finance

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RATIONALE

Prior to December 31, 1985, the State had for several years taxed the sale of gasohol (a mixture of at least 10% alcohol and not more than 90% gasoline combined to produce an alcohol-gasoline fuel) at a rate less than it had taxed gasoline. Public Act 333 of 1980 provided an exemption through 1982 which taxed gasohol at a rate equal to five cents less per gallon than the rate for gasoline, and subsequent legislation provided for a gradual reduction in the exemption in ensuing years. The Federal government has had a similar tax differential between gasohol and gasoline: the Federal tax on gasohol is six cents less per gallon than it is on gasoline, and will remain so through 1992 when the program is scheduled to expire. Proponents of the 1980 State exemption suggested that reducing the State tax on gasohol would encourage its use, thus cutting the amount of petroleum used and reducing our dependence on petroleum-based fuels. It was argued that if gasohol usage were increased, it could encourage the development of Michigan-based ethanol alcohol manufacturing plants, which in turn could create jobs and provide a market for Michigan farmers' surplus corn.

Some of the predictions have come true, as Michigan became and has remained one of the top gasohol consuming states. While gasohol sales have been encouraging, however, State production thus far has been considered a disappointment. There has been little significant production of ethanol to use for gasohol in Michigan. Currently, there is one plant in operation in Springport, which last year used 1.2 million bushels of corn to produce 3 million gallons of ethanol, according to the Department of Agriculture. According to Senate Finance Committee testimony, there were 382 million gallons of gasohol sold in Michigan in 1986, meaning that there were around 38 million gallons of ethanol used, of which all but 3 million gallons had to have been produced outside the State. It has been pointed out that to date the State's tax incentives regarding gasohol have focused on the consumption of the product by reducing the pump price. Some people feel that if the tax laws could be adjusted to direct tax benefits toward production, the State could persuade the industry to operate plants in Michigan.

CONTENT

The bill would amend the Single Business Tax Act to allow taxpayers to claim credits against their single business tax (SBT) liability for bushels of corn they purchased and used in the production of alcohol. The credit could be claimed only if the alcohol were produced in Michigan and used in gasohol (an "alcohol-gasoline fuel" of at least 10% alcohol and not more than 90% gasoline).

The credit would be in the following amount for each bushel, up to the number of bushels shown below, according to the tax year:

Credit (in cents)	Bushels (in millions)	Tax Year
50	1.5	1988 & 1989
40	1.875	1990 & 1991
30	2.5	1992
20	3.75	1993
10	7.5	1994

In addition, in each year, taxpayers who exceeded these limits could claim a five-cent per-bushel credit for the next 11 million bushels. If the allowable credit exceeded a taxpayer's SBT liability, the Department of Treasury would have to refund the excess to the taxpayer, without interest. The maximum credit could not exceed \$1,300,000 per year.

When making a claim for the credit, a taxpayer would have to include in the claim the number of gallons of alcohol produced for use in gasohol, and state that the number produced and the amount of the credit were public record.

Proposed MCL 208.38c

FISCAL IMPACT

The bill would result in an indeterminate loss of Single Business Tax revenue. The cost would depend on how many firms claimed the credit for ethanol production. Currently, only one plant operating in Michigan would be eligible for the credit in Senate Bill 427. At full capacity that plant uses 1.2 million bushels of corn per year, translating into a 1988 tax credit of \$600,000.

ARGUMENTS**Supporting Argument**

The bill offers a chance for the State to encourage the development of new industry in Michigan. Sales data have shown that the State has been and remains one of the nation's leaders in the consumption of gasohol. Few of the State's farmers, workers, or communities have benefitted directly from this market, however, because very little ethanol has been produced here for use in gasohol. It appears that the State's use of tax incentives regarding gasohol, by reducing the tax per gallon of fuel sold, have encouraged consumption but not production. Most of the ethanol that has been used here was purchased from facilities in Illinois and Indiana, meaning, in effect, that the tax dollars that would have gone to the State's transportation fund (had the gasohol tax exemption not

S.B. 427 (10-29-87)

existed) have been used to subsidize other State's ethanol industries. Rather than lowering taxes at the point of distribution, the bill would offer an incentive for increased ethanol production by providing single business tax credits, thus encouraging the building and operation of production facilities and creating jobs. This approach would keep gasohol prices competitive without cutting transportation tax revenues, and would guarantee that "subsidy" tax expenditures would benefit the economy of Michigan without disturbing scarce funds used for road improvements.

Supporting Argument

Since a bushel of corn produces about 2.5 gallons of ethanol, the 38 million gallons of ethanol consumed in Michigan last year would demand over 15 million bushels of corn. The creation and development of an alcohol-fuel-producing industry would strengthen Michigan agriculture by providing farmers with a welcome alternative when they need to sell their corn. A healthy gasohol industry not only would open a market for farmers, but could considerably reduce a farmer's transportation and storage costs if an ethanol plant were within a reasonable distance of the farmer.

Supporting Argument

Though at this time the nation is not faced with a petroleum shortage, it can be assumed that at some time in the future this problem will resurface. Encouraging the development of a renewable energy source, such as alcohol distilled from corn, is simply good sense because it reduces our dependence on petroleum-based fuels and ultimately makes the existing crude oil last longer.

Opposing Argument

Some people who are supportive of encouraging the production of gasohol in Michigan nonetheless are uncomfortable with the bill, because it is seen as an attempt by the State to subsidize an industry that has thus far not shown an ability to survive here. In attempting to promote industrial development the State must compare the potential benefits against the costs of luring such development. World oil prices have plunged this year and driven the price of gasoline down, which in turn lowered the demand for gasohol. The State should examine whether there is a more efficient use of tax dollars than to promote an industry that produces a product which has questionable marketability.

Response: Michigan ranks as one of the top states in ethanol use. Because the demand is there now, now is the time to promote the industry in Michigan.

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.