

HB

263

Revision Date: May 7, 1997 5:00 pm Dept. Affected: Revenue
 Title: Motor Fuel Tax: Lignocellulose/10% Alcohol BRU: Revenue Operations
 Component: Income and Excise Audit
 Sponsor: Representative Williams
 Requestor: H (TRA) COMPONENT SERIAL NO. 113

Expenditures/Revenues: (Thousands of Dollars)

OPERATING EXPENDITURES	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES (GF)	8,000.0	8,000.0	**	**	**	**
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY97) cost \$ 0.0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary)

** Because the production of wood ethanol is still in the experimental stage it is not possible to derive an estimate of the loss in revenue due to the exemption of wood ethanol based gasohol from the motor fuel tax. However, we estimate that (starting in FY 98) removal of the exemption for non-wood based gasohol will increase revenues by 8 million a year.

Prepared by: Brett Fried Phone: (907) 465-3682
 Division: Income and Excise Audit Date: May 7, 1997
 Approved by Commissioner: Wilson L. Condon Date: May 7, 1997
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*The Case for Wood-Based Ethanol
Motor Fuel Tax Incentives
Legislation*

Presented by Sealaska Corporation
To the House Transportation Committee
May 8, 1997

Alaska law currently exempts fuel containing at least 10 percent ethanol from the state's motor fuel tax. AS 43.40.100(2)(F). The use of ethanol helps several communities maintain their air quality during winter inversion periods when conventional motor fuel use was causing the communities to become non-attainment areas.

With Alaska's public revenues declining, the state is even more insistent on ensuring that incentive programs produce tangible economic, as well as social benefits. In that respect, there is currently only one source of ethanol for which the current exemption serves economic, as well as environmental goals. That source is wood and wood waste. For this class of ethanol, the exemption serves the general environmental purpose of the broader exemption. But the exemption also serves a significant economic function, by providing another potential use of low-quality wood, and by helping the wood products industry cope with the costly burden of disposing or recycling of wood waste.

The proposed legislation would accordingly retain the exemption for wood-generated ethanol. The legislation would greatly narrow the universe of eligible ethanol, because nearly 99% of the ethanol produced in the United States is derived from corn.

The wood products industry is situated differently. Logging operations and wood product plants, such as sawmills and sort yards, produce considerable low quality wood

and waste material from their operations--such as cull logs, sawdust and shavings. As one example, Sealaska Timber Corporation estimates that either disposing or recycling of wood wastes from a new Southeast Alaska sawmill would require a \$5 million capital investment. Currently, most sawmill woodwaste is either burned or disposed of in landfills; however, solid waste disposal and air pollution restrictions continue to limit those options.

For low value products such as cull wood, ethanol conversion offers the opportunity to covert these sub-marginal products to a higher, more valuable use. Conversion also offers the possibility of opening a market for diseased or insect-infested timber, such as the Southcentral and Interior Alaska forests plagued by bark beetle. Developing an economic market for this timber would at once serve Alaska's environmental concerns while, at the same time, provide new and enhanced business opportunities for the timber industry and the distressed communities that are dependent upon that industry.

Today, less than 1/5th of 1% of America's ethanol is produced from wood-derived products--principally from paper sludge by Georgia Pacific Corporation in Bellingham, Washington. And, the commercial use of wood waste as an ethanol source presents a challenge that is being addressed through new technology development. For example, the U.S. Department of Energy's National Renewable Energy Laboratory is currently engaged in a wood waste biomass testing program to gauge the susceptibility of Southeast Alaska softwoods and bark to efficient ethanol conversion.

As with any developing technology, the investments necessary to achieve commerciality hinge on a favorable tax climate. To that end, the proposed legislation

would retain the current broad exemption for ethanol-based fuels only for ethanol produced from wood or wood waste. The economic benefits of the proposal are two-fold:

- Direct employment, and capital investment, in the conversion of wood products to ethanol; the construction and operation of companion power plants and wastewater treatment facilities; and the transportation and distribution of wood-based ethanol. A linchpin of Alaska's future economy is its ability to add value-added industry to its raw resource base, and the productive use of forest by-products and wastes into ethanol fits neatly within that goal; and
- Enhancing ultimate recovery of timber from Alaska's existing forest industry, and increasing the attractiveness of other value-added industries--most specifically, sawmill and export sort-yard operations. Remember, in this respect, that one goal of encouraging wood-based ethanol manufacturing is not, necessarily, to make the process profitable on a stand-alone basis, but rather to provide an alternative, less-costly means of treating the considerable quantities of wood waste generated by other forest products industries.

Under the proposal, the incentive for wood-based ethanol would take effect once at least one source of wood-based ethanol was reasonably available to Alaska users.

*Testimony of Mr. Robert W. Loescher
Executive Vice President, Natural Resources
Sealaska Corporation*

Before the Alaska House Transportation Committee
Regarding HB 263 (Motor Fuel Tax Exemption for Wood-Based Ethanol)
May 8, 1997

My name is Robert W. Loescher. I am Sealaska Corporation's Executive Vice President for Natural Resources, and I'm pleased to appear today to lend Sealaska's enthusiastic support for HB 263. As the state's general motor fuel tax exemption for ethanol-based fuel appears destined for repeal, HB 263 recognizes that there remain compelling public policy reasons for retaining a more targeted exemption for wood-based ethanol. With this bill, the Alaska Legislature may help unlock one door to the revitalization of Alaska's timber industry. As Alaska's largest private timber owner, Sealaska supports that initiative.

With the loss of Southeast Alaska's two pulp mills, the market for the lower end of Alaska's forest products has declined considerably. At the same time, timber owners in Southcentral

and Interior Alaska face the challenge of marketing marginal timber infested by bark beetle. On a statewide basis, then, Alaskans are challenged by the need to find, and encourage, a reliable long-term market for a considerable portion of the state's timber inventory.

The use of lower-end wood products to manufacture ethanol is a potential answer to that challenge. And ethanol manufacturing would aid our forest industry in a different way as well. The already-marginal economics of in-state wood processing are driven even lower by the costly burden of disposing of sawdust and other wood wastes from sawmill operations. Indeed, Sealaska has estimated that opening a new sawmill in Southeast Alaska would carry with it the need to invest \$5 million in wood waste disposal facilities. And with the two current options for wood waste disposal--that is, either incineration or landfilling--being disfavored by regulators, the problem of solid waste disposal becomes a legal, as well as an economic, disincentive.

Legislation that offers a targeted tax incentive to: (1) create a market for lower-end forest products; and (2) turn costly solid waste into profitable feedstock, would represent a concrete, creative and pro-active response to the ills that have befallen Alaska's forest products industry.

I cannot tell you, sitting here, that an exemption from an 8-cent-per-gallon tax will transform wood-based ethanol production from a concept into reality. The truth of the matter is that less than 1/5th of 1 percent of America's total ethanol production is currently attributable to wood. We are dealing here with a concept--an exciting possibility, and not a reality. But as Ms. Megan Smith of the National Biofuels Institute told the House Resources Committee on February 20, some of our nation's most respected biofuels experts, including those at the U.S. Department of Energy's National Renewable Energy Lab, are sufficiently encouraged by the prospect to have at least begun exploring this technology's feasibility.

Like any exciting new technology, the promise of this one depends on the willingness of good people to devote the time and money necessary to try, test and develop. And that, in turn, depends on the existence of a favorable economic climate, which is what HB 263 would help create.

And it would do so, I would add, at little cost. If the legislation fails its purpose, it would cost nothing, for no wood-based ethanol plant would exist to claim its exemption. And if it succeeds too well, spawning a healthy new industry that needs no further help, this legislature can take due credit for its birth, while future legislatures can amend the law to prevent excesses.

But succeed or fail, HB 263 would signal to all Alaskans that the Alaska Legislature has done what it could to aid a beleaguered industry. And that, I think, may ultimately prove both the finest virtue of this legislation.

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Representative William K. Williams

SPONSOR STATEMENT

HB 263 Motor Fuel Tax: Lignocellulose/10% Alcohol

House Bill 263 was introduced to encourage a renewable energy industry in Alaska. Technology is now under development which would allow ethanol to be produced from wood and wood wastes. Alaska could be at the forefront of a new high value-added, environmentally friendly wood ethanol industry.

Southeast Alaska's timber industry has suffered terrible job loss over the last six years. Absent any pulp mills, there are no current manufacturing techniques which use the low end, former pulp quality wood. We may soon be 'chipping and shipping' low quality logs, and jobs, from Southeast.

If we are able to entice investors and start wood ethanol plants in Alaska, we could employ many of the now unemployed timber workers of the region. Wood ethanol plants could convert milling waste, low quality wood chips, and even paper into ethanol.

Current Alaska law taxes motor fuel at 8 cents a gallon. Gasohol, or gasoline blended with 10% ethanol, is exempt from this tax. HB 263 proposes to end the 8 cent a gallon tax credit for all gasohol except for gasohol that uses ethanol derived from wood. Corn, barley, and other grain based ethanol would not qualify for the gasohol tax credit.

Under the bill, gasohol using wood ethanol would be taxed at 8 cents lower than the prevailing motor fuel tax rate. So, if the motor fuel tax were raised in the future, the wood/ethanol gasohol tax rate would rise at the same rate and remain 8 cents below whatever the new motor fuel rate was.

Also, the wood ethanol gasohol tax incentive would only be in effect for five years after the first wood derived ethanol is sold in the gasohol market.

According to the National Renewable Energy Lab, there are no plants which currently produce ethanol from wood. This legislation will send the message to investors that the state of Alaska wants to encourage a new renewable energy industry in our state, and create an environmentally friendly high value-added wood product.

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CAPITAL EXPENDITURES						
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Alaska Department of Revenue
Income and Excise Audit Division

Motor Fuel Tax: Lignocellulose/10%Alcohol
HB 263 (TRA)
May 7, 1997
Page 2 of 3

DRAFT BILL ANALYSIS

Section 1 amends AS 43.40.010(a) to exempt motor fuel that is 10 percent wood ethanol from motor fuel taxes. To qualify for the exemption the wood ethanol must have been produced within five years of initial production of wood ethanol by a facility that processes lignocellulose from wood.

Section 2 insures that the motor fuel exemption, as described in section 1 of this act, still takes effect even if the tax rate on aviation fuel is changed to reflect changes in state landing fees at rural airports (see section 7).

Section 3 amends AS 43.40.010(b) to exempt motor fuel that is 10 percent wood ethanol from motor fuel taxes. To qualify for the exemption the wood ethanol must have been produced within five years of initial production of wood ethanol by a facility that processes lignocellulose from wood. repeals section 2 of this Act.

Section 4 insures that the motor fuel exemption, as described in section 1 of this act, still takes effect even if the tax rate on aviation fuel is changed to reflect changes in state landing fees at rural airports (see section 7).

Section 5 provides for editorial changes necessitated by the removal of gasohol from the list of what "motor fuel" does not include.

Section 6 removes the exclusion of gasohol from what "motor fuel" does not include. Consequently, gasohol is only exempt from the motor fuel tax if it meets the conditions described in section 1 of this act.

Section 7 makes section 2 and 4 conditional on increases in state landing fees at rural airports.

Section 8 establishes an effective date of July 1, 1997 for sections 1,3 and 5-7 of this Act.

Section 9 establishes an effective date for section 2 and 4 of this act of the later of 30 days after the effective date of a state landing fee increase at rural airports or day after the day section 7 of this act becomes law.

Alaska Department of Revenue
Income and Excise Audit Division

Motor Fuel Tax: Lignocellulose/10%Alcohol

HB 263 (TRA)

May 7, 1997

Page 3 of 3

Operating Expenditures

The Department of Revenue is not requesting any additional funds for meeting its obligations under this Act.

Revenue Collected

Because the production of wood ethanol is still experimental it is not yet possible to estimate the loss in revenues due to the exemption of wood ethanol based gasohol from the motor fuel tax. However, we do estimate that (starting in FY 98) the removal of the exemption for non-wood based gasohol will result in an \$8 million increase in revenue.