

CRS Report for Congress

Selected Issues Related to an Expansion of the Renewable Fuel Standard (RFS)

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Summary

High petroleum and gasoline prices, concerns over global climate change, and the desire to promote domestic rural economies have greatly increased interest in biofuels as an alternative to petroleum in the U.S. transportation sector. Biofuels, most notably corn ethanol, have grown significantly in the past few years as a component of U.S. motor fuel supply. Ethanol, the most commonly used biofuel, is blended in nearly half of all U.S. gasoline (at the 10% level or lower in most cases). However, current biofuel supply only represents about 4% of total gasoline demand.

While recent proposals have set the goal of significantly expanding biofuel supply in the coming decades, questions remain about the ability of the U.S. biofuel industry to meet rapidly increasing demand. Current U.S. biofuel supply relies almost exclusively on ethanol produced from Midwest corn. In 2006, 20% of the U.S. corn crop was used for ethanol production. To meet some of the higher ethanol production goals would require more corn than the United States currently produces, if all of the envisioned ethanol was made from corn.

Due to the concerns with significant expansion in corn-based ethanol supply, interest has grown in expanding the market for biodiesel produced from soybeans and other oil crops. However, a significant increase in U.S. biofuels would likely require a movement away from food and grain crops as feedstocks. Other biofuel feedstock sources, including cellulosic biomass, are promising, but technological barriers make their future uncertain. Therefore, some proposals would require ever-larger amounts of biofuels produced from feedstocks other than corn starch, including sugarcane, oil crops, and cellulose, to promote the development of these fuels.

The Senate-passed energy bill (H.R. 6) would require the use of 36 billion gallons of renewable fuels annually in 2022, of which only 15 billion gallons could be ethanol from corn starch. The remaining 21 billion gallons would be so-called “advanced biofuels.” The current RFS would only require the use of 7.5 billion gallons in 2012, increasing to an expected 8.6 billion gallons in 2022, of which only 250 million gallons of cellulosic biofuels would be required.

Issues facing the U.S. biofuels industry include potential agricultural “feedstock” supplies, and the associated market and environmental effects of a major shift in U.S. agricultural production; the energy supply needed to grow feedstocks and process them into fuel; and barriers to expanded infrastructure needed to deliver more and more biofuels to the market. A key question is whether a renewable fuel mandate is the most effective policy to promote the above goals. This report outlines some of the current supply issues facing biofuels industries, including implications for agricultural feedstocks, infrastructure concerns, energy supply for biofuel production, and fuel price uncertainties.

This report supersedes CRS Report RL33928, *Ethanol and Biofuels: Agriculture, Infrastructure, and Market Constraints Related to Expanded Production*.

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Selected Issues Related to an Expansion of the Renewable Fuel Standard (RFS)

Introduction

High petroleum and gasoline prices, concerns over global climate change, and the desire to promote domestic rural economies have raised interest in biofuels as an alternative to petroleum in the U.S. transportation sector. Biofuels, most notably corn-based ethanol, have grown significantly in the past few years as a component of U.S. motor fuels. For example, nearly half of all U.S. gasoline contains some ethanol (mostly blended at the 10% level or lower). However, current supply represents only about 4% of annual gasoline demand on a volume basis, and only about 3% on an energy basis. In 2006, the United States consumed roughly 5 billion gallons of biofuels (mostly ethanol); this 5 billion gallons was blended into roughly 65 billion gallons of gasoline. Total annual gasoline consumption is roughly 140 billion gallons.

Recent proposals, including President Bush's goal in his 2007 State of the Union Address, aim to expand biofuel supply significantly in the coming decades. The President's goal would be to expand consumption from 5 billion gallons in 2007 to 35 billion gallons in 2017. While this proposal included not just biofuels but alternative fuels in general (including fuels from coal or natural gas), it would likely mean a significant growth in biofuels production over the next 10 years. Other legislative proposals would require significant expansion of biofuels production in the coming decades; some proposals would require 30 billion gallons of biofuels alone by 2030 or 60 billion gallons by 2050. The Senate-passed energy bill (H.R. 6) would require the use of 36 billion gallons in 2022, including 21 billion gallons of "advanced biofuels."¹

Current U.S. biofuel supply relies almost exclusively on ethanol produced from Midwest corn (**Table 1**). Other fuels that play a smaller role include ethanol from Brazilian sugar, biodiesel from U.S. soybeans, and ethanol from U.S. sorghum. A significant increase in U.S. biofuels would likely require a movement away from food and grain crops. For example, U.S. ethanol production in 2006 consumed

¹ The term "advanced biofuel" comes from current legislation in the 110th Congress, including the Senate energy bill (H.R. 6). In many cases, the definition of "advanced biofuel" includes mature technologies and fuels that are currently produced in large amounts. For example, the H.R. 6 definition of "advanced biofuel" includes ethanol from sugarcane, despite the fact that Brazilian sugar growers have been producing fuel ethanol for decades. H.R. 6 defines "advanced biofuels" as biofuels other than ethanol derived from corn starch. Possible fuels include biodiesel from oil seeds, ethanol from sugarcane, and ethanol from cellulosic materials (including non-starch parts of the corn plant, such as the stalk).

roughly 20% of the U.S. corn crop. If only corn is used, expanding ethanol production to 35 billion gallons would require more corn than the United States currently produces, which would be infeasible. Corn (and other grains) have myriad other uses, and such a shift would have drastic consequences for most agricultural markets, including grains (since corn would compete with other grains for land), livestock (since the cost of animal feed would likely increase), and land (since total harvested acreage would likely increase). In addition to agricultural effects, such an increase in corn-based ethanol would likely affect fuel costs (since biofuels tend to be more expensive than petroleum fuels), energy supply (natural gas is a key input into corn production), and the environment (since the expansion of corn-based ethanol production raises many environmental questions). These concerns are discussed below.

Table 1. U.S. Production of Biofuels from Various Feedstocks

Fuel	Feedstock	U.S. Production in 2006
Ethanol	Corn	4.9 billion gallons
	Sorghum	less than 100 million gallons
	Cane sugar	No production (656 million gallons imported from Brazil and Caribbean countries)
	Cellulose	No production (one demonstration plant in Canada)
Biodiesel	Soybean oil	approximately 200 million gallons
	Other vegetable oils	less than 10 million gallons
	Recycled grease	less than 10 million gallons
	Cellulose	No production
Methanol	Cellulose	No production
Butanol	Cellulose, other biomass	No production

Sources: Renewable Fuels Association; National Biodiesel Board; CRS analysis.

Due to the concerns with significant expansion in corn-based ethanol supply, interest has grown in expanding the market for biodiesel (a diesel substitute produced from vegetable and animal oils) and spurring the development of motor fuels produced from cellulosic materials (including grasses, trees, and agricultural and municipal wastes). However, all of these so-called “advanced biofuel” technologies are currently even more expensive than corn-based ethanol (with the exception of ethanol produced from Brazilian sugarcane).

In addition to expanding domestic production of biofuels, there is some interest in expanding imports of sugar-based ethanol from Brazil and other countries. However, ethanol from Brazil is currently subject to a \$0.54 per gallon tariff that in

most years is a significant barrier to direct Brazilian imports. Some Brazilian ethanol can be brought into the United States duty free if it is dehydrated (reprocessed) in Caribbean Basin Initiative (CBI) countries.² Up to 7% of the U.S. ethanol market could be supplied duty-free in this fashion, although historically ethanol dehydrated in CBI countries has only represented about 2% of the total U.S. market.³

Any fuel produced from biological materials (e.g., food crops, agricultural residues, municipal waste) is generally referred to as a “biofuel.” More specifically, the term generally refers to liquid transportation fuels. The most significant biofuel in the United States is ethanol produced from U.S. corn.⁴ Approximately 4.9 billion gallons of ethanol were produced in the United States in 2006, mostly from corn. Other domestic feedstocks for ethanol include grain sorghum and sweet sorghum; imported ethanol (656 million gallons in 2006) is usually produced from sugar cane in Brazil. Ethanol is generally blended into gasoline at the 10% level (E10) or lower. Ethanol can be used in purer forms such as E85 (85% ethanol and 15% gasoline) in vehicles specially designed for its use, although E85 represents less than 1% of U.S. ethanol consumption.

After ethanol, biodiesel is the next most significant biofuel in the United States, although 2006 U.S. production is estimated at only about 225 million gallons. Biodiesel is a diesel fuel substitute produced from vegetable and animal oils (mainly soybean oil in the United States), as well as recycled cooking grease. Other biofuels with the potential to play a role in the U.S. market include ethanol and diesel fuel substitutes produced from various biomass feedstocks containing cellulose. However, these “cellulosic” biofuels are currently prohibitively expensive relative to conventional ethanol and biodiesel. Other potential biofuels include other alcohols (e.g., methanol and butanol) produced from biomass.

This report outlines some of the current issues related to a significant expansion of the renewable fuel standard (RFS) established in the Energy Policy Act of 2005 (P.L. 109-58), including implications for agricultural feedstocks, infrastructure constraints, environmental concerns, energy supply issues, and fuel prices.

The Renewable Fuel Standard (RFS)

The Current RFS

Section 1501 of the Energy Policy Act of 2005 (P.L. 109-58) established a renewable fuel standard (RFS) requiring the use of renewable fuels in gasoline. Starting in 2006, the law requires the use of 4.0 billion gallons of renewable fuel in

² For more information on CBI imports, see CRS Report RS21930, *Ethanol Imports and the Caribbean Basin Initiative*, by Brent D. Yacobucci.

³ In 2006 ethanol prices rose sharply, and direct imports from Brazil rose sharply, despite the tariff.

⁴ For more information on ethanol, see CRS Report RL33290, *Fuel Ethanol: Background and Public Policy Issues*, by Brent D. Yacobucci.

gasoline, increasing to 7.5 billion gallons in 2012. After 2012, the minimum renewable content for a given year must be no lower than the percentage of renewable fuel in gasoline in 2012. Also, starting in 2013, at least 250 million gallons of the mandate must be met using cellulosic biofuel. Although the RFS has been called an “ethanol mandate,” there is no explicit requirement to use ethanol. For example, there are specific provisions for generating credits through the use of biodiesel and other renewable fuels. That said, it is expected that the vast majority of the RFS will be met using ethanol produced from corn starch.

RFS as Public Policy. An expansion in the RFS could have significant policy implications. Issues include questions of energy/petroleum security, pollutant and greenhouse gas emissions, agricultural commodity and food market effects, and infrastructure costs. Proponents and opponents of mandated biofuel use both claim that an RFS would promote or run counter to the general public interest on several different policy fronts. For example, supporters of an RFS claim it would serve several public policy interests including:

- reduced investment risk by guaranteeing demand for a projected period (such risk would otherwise keep significant investment capital on the sidelines);
- enhanced energy security via the production of liquid fuel from a renewable domestic source resulting in decreased reliance on imported fossil fuels (the U.S. currently imports over half of its petroleum, two-thirds of which is consumed by the transportation sector); and
- enhanced environmental benefits (non-toxic, biodegradable, reduced GHG emissions compared with fossil fuels, etc.).

Critics of an RFS have taken issue with many specific aspects of biofuel production and use, but a general public policy criticism of the RFS is that, by picking the “winner,” policymakers may exclude or retard the development of other, potentially more preferable alternative energy sources.⁵ They contend that biofuels are given a huge advantage via billions of dollars of annual subsidies which distort investment markets by redirecting venture capital and other investment dollars away from competing alternative energy sources. Instead, these critics have argued for a more “technology neutral” policy such as a carbon tax, a cap-and-trade system of carbon credits, or a floor price on imported petroleum.

The Proposed RFS Defined

This report examines the specific issues regarding the implementation of an extended RFS as contained in the Senate-passed energy bill (H.R. 6), but does not address the broader public policy issue surrounding how best to support U.S. energy

⁵ For example, see Bruce A. Babcock, “High Crop Prices, Ethanol Mandates, and the Public Good: Do They Coexist?” *Iowa Ag Review*, Vol. 13, No. 2, Spring 2007; and Robert Hahn and Caroline Cecot, “The Benefits and Costs of Ethanol,” Working Paper 07-17, AEI-Brookings Joint Center for Regulatory Studies, November 2007.

policy.⁶ The proposed RFS expansion would include all motor fuel, as well as heating oil (**Table 2**). It would expand the current RFS mandate to 13.2 billion gallons (bgal.) in 2012 (compared with the current RFS of 7.5 bgal.); 15 bgal. by 2015; and 36 bgal. in 2022. However, the corn-based ethanol share of the proposed RFS would be capped at 15 bgal. Starting in 2016, the proposed RFS would increase the RFS by an additional 3 bgal. annually, to be derived entirely from “advanced biofuels” — defined as biofuels derived from feedstocks other than corn starch. The advanced biofuel share increases to 21 bgal. by 2022. An additional requirement associated with the proposed RFS is that renewable fuels produced in facilities that commence operation after enactment must achieve at least a 20% reduction in life-cycle greenhouse gas emissions relative to gasoline.

Table 2. Proposed H.R. 6 Expansion of the Renewable Fuel Standard

Year	Current RFS (billion gallons)	Biofuel mandate for motor fuel, home heating oil, and boiler fuel (billion gallons)	Portion to be from advanced biofuel (i.e., not corn starch) (billion gallons)	Cap on corn starch-derived ethanol (billion gallons)
2006	4.0			
2007	4.7	—		—
2008	5.4	8.5		8.5
2009	6.1	10.5		10.5
2010	6.8	12.0		12.0
2011	7.4	12.6		12.6
2012	7.5	13.2		13.2
2013	7.6 (est.) ^a	13.8		13.8
2014	7.7 (est.) ^a	14.4		14.4
2015	7.8 (est.) ^a	15.0		15.0
2016	7.9 (est.) ^a	18.0	3.0	15.0
2017	8.1 (est.) ^a	21.0	6.0	15.0
2018	8.2 (est.) ^a	24.0	9.0	15.0
2019	8.3 (est.) ^a	27.0	12.0	15.0
2020	8.4 (est.) ^a	30.0	15.0	15.0
2021	8.5 (est.) ^a	33.0	18.0	15.0
2022	8.6 (est.) ^a	36.0	21.0	15.0

^aStarting in 2013, a minimum of 250 million gallons must be derived from cellulosic biomass. After 2012, the ratio of renewable fuel to gasoline must at least equal the ratio in 2012.

The proposed RFS involves two distinct components — a corn-starch-ethanol RFS and a non-corn-starch-ethanol RFS — that are best analyzed separately because the various supply and demand factors affecting their development also are fairly distinct.

⁶ The same RFS extension is also proposed in the Domenici Amendment (S.Amdt. 3614) to the Senate Agriculture Committee’s approved farm bill (S. 2302).

Potential Issues with an Expanded RFS

Overview of Long-Run Corn Ethanol Supply Issues

The U.S. ethanol industry has shown rapid growth in recent years, with national production increasing from 1.8 billion gallons in 2001 to 4.9 billion in 2006. This rapid growth — which is projected to continue for the foreseeable future — has important consequences for U.S. and international fuel, feed, and food markets.

Corn accounts for about 98% of the feedstocks used in ethanol production in the United States. USDA estimates that 3.2 billion bushels of corn (or 24% of the 2007 corn crop) will be used to produce ethanol during the September 2007 to August 2008 corn marketing year.⁷ As of November 27, 2007, existing U.S. ethanol plant capacity was a reported 7.2 billion gallons per year, with an additional capacity of 6.2 billion gallons under construction.⁸ Thus, total annual U.S. ethanol production capacity in existence or under construction as of November 27, 2007, was 13.4 billion gallons. This production capacity is well in excess of the 7.5 billion gallon supply required in 2012 by the Renewable Fuel Standard (Energy Policy Act of 2005 (P.L. 109-58)). The current pace of plant construction suggests that annual corn-for-ethanol use will likely require more than 4 billion bushels in 2008 and approach, or possibly exceed, 5 billion bushels by 2010.⁹ In 2007, U.S. corn production was a record 13.2 billion bushels.

The ethanol-driven surge in corn demand has been associated with a sharp rise in corn prices. For example, the futures contract for March 2007 corn on the Chicago Board of Trade rose from \$2.50 per bushel in September 2006 to a contract high of over \$4.16 per bushel in January 2007 (a rise of 66%). Although a record U.S. corn harvest eased upward pressure on corn prices slightly during 2007, by November 2007 prices for 2008 futures contracts were again trading at over \$4.00 per bushel. Both USDA and the Food and Agricultural Policy Research Institute (FAPRI) (**Table 3**), in their annual agricultural baseline reports, project corn prices to remain well above \$3.00 per bushel through 2016 compared with an average farm price of \$2.15 during the previous 10-year period (1997-2006).

This sharp rise in corn prices owes its origins largely to increasing corn demand spurred by the rapid expansion of corn-based ethanol production capacity in the United States since mid-2006. The rapid growth in ethanol capacity has been fueled by both strong energy prices and a variety of government incentives, regulations, and programs. Major federal incentives include a tax credit of \$0.51 to fuel blenders for every gallon of ethanol blended with gasoline; the Renewable Fuel Standard; and the

⁷ USDA, WAOB, *World Agricultural Supply and Demand Estimates (WASDE) Report*, Nov. 9, 2007, Washington; available at [<http://www.usda.gov/oce/>].

⁸ See Renewable Fuels Association, *Industry Statistics*, at [<http://www.ethanolrfa.org/industry/statistics/>].

⁹ FAPRI, *Baseline Update for U.S. Agricultural Markets*, FAPRI-MU report #28-07, August 2007.

54¢ per gallon most-favored-nation duty on most imported ethanol.¹⁰ A recent survey of federal and state government subsidies in support of ethanol production reported that the total annual federal support fell somewhere in the range of \$5.1 to \$6.8 billion per year.¹¹

Market participants, economists, and biofuels skeptics have begun to question the need for continued large federal incentives in support of ethanol production, particularly when the sector would have been profitable during much of 2006 and 2007 without such subsidies.¹² Their concerns focus on the potential for widespread unintended consequences that might result from excessive federal incentives adding to the rapid expansion of ethanol production capacity and the demand for corn to feed future ethanol production. These questions extend to issues concerning the ability of the gasoline-marketing infrastructure to accommodate more ethanol in fuel, the likelihood of modifications in engine design, the environmental impacts, and other considerations.

Overview of Non-Corn-Starch-Ethanol RFS Issues

Although most references to “advanced biofuels” involve cellulosic ethanol, the “advanced biofuels” component of the proposed RFS extension may be met by essentially any non-corn-starch-derived biofuel. News reports often refer to cellulosic ethanol as “nearing a break-through” or “just around the corner” but the reality is that there is considerable uncertainty about the speed with which this technology will become commercially viable (even with substantial government support). Many scientists still suggest that commercial realization of cellulosic ethanol is 5 to 15 years down the road.¹³ Although research is ongoing, presently there are no commercial-scale cellulosic biofuel plants in the United States, and there is only one demonstration-scale plant in Canada.¹⁴ A major barrier to cellulosic fuel production is that production costs remain significantly higher than for corn ethanol or other alternative fuels. Currently, various production processes are prohibitively expensive, including physical, chemical, enzymatic, and microbial treatment and conversion of these feedstocks into motor fuel.

¹⁰ For more information on incentives (both tax and non-tax) for ethanol, see CRS Report RL33572, *Biofuels Incentives: A Summary of Federal Programs*, by Brent D. Yacobucci.

¹¹ Koplou, Doug. *Biofuels — At What Cost? Government Support for Ethanol and Biodiesel in the United States*, Global Subsidies Initiative of the International Institute for Sustainable Development, Geneva, Switzerland, October 2006; available at [<http://www.globalsubsidies.org>].

¹² Chris Hurt, Wally Tyner, and Otto Doering, Department of Agricultural Economics, Purdue University, *Economics of Ethanol*, December 2006, West Lafayette, IN.

¹³ For example, the Department of Energy’s goal is to make cellulosic biofuels cost-competitive with corn ethanol by 2012. Other groups are less optimistic.

¹⁴ However, on February 28, 2007, DOE announced availability of \$385 million in grant funding for six commercial-scale cellulosic ethanol plants in six states. If operational, combined capacity of these six plants would be 130 million gallons per year. DOE, *DOE Selects Six Cellulosic Ethanol Plants for Up to \$385 Million in Federal Funding*, February 28, 2007, Washington, D.C.

Unintended Policy Incentives of the “Advanced Biofuels” Mandate.

The uncertainty concerning cellulosic ethanol production raises the stakes for a government mandate on its use. If cellulosic ethanol production is unable to advance rapidly enough to meet the RFS mandate for non-corn-starch ethanol, then other unexpected biofuel sources may step in and fill the void, such as:

- domestic sorghum-starch ethanol whose production may expand across the prairie states and in other regions less suitable for corn production;
- costly domestic sugar-beet ethanol or even costlier domestic biodiesel production may be undertaken to fill the mandate; or
- imports of Brazilian sugar-cane ethanol could expand.

Potential Benefits Are Vast. Ethanol and biodiesel produced from cellulosic feedstocks, such as prairie grasses and fast-growing trees or agricultural waste, have the potential to improve the energy and environmental effects of U.S. biofuels while offering significant cost savings on the production side (e.g., high-yielding, grown on marginal land, perennial rather than annual). Further, moving away from feed and food crops to dedicated energy crops could avoid some of the agricultural supply and price concerns associated with corn ethanol (as discussed later in this report).

A key potential benefit of many of cellulosic feedstocks is that many can be grown without the need for chemicals. Reducing or eliminating the need for chemical fertilizers would address one of the largest energy inputs for corn-based ethanol production. Using biomass to power a biofuel production plant could further reduce fossil fuel inputs. Improving the net energy balance of ethanol would also reduce net fuel-cycle greenhouse gas emissions.

Cellulosic Biofuel Production Uncertainties. There are substantial uncertainties regarding both the costs of production for such feedstock as well as the costs of producing biofuel from them. Perennial crops are often slow to establish and can take several years before a marketable crop is produced. Crops heavy in cellulose tend to be bulky and represent significant problems in terms of harvesting, transporting, and storing. Seasonality issues involving the operation of a biofuel plant year-round based on a 4- or 5-month harvest period of biomass suggest that bulkiness is likely to matter a great deal. In addition, most marginal lands (i.e., the low-cost biomass production zones) are located far from major urban markets, bringing the plant location choice versus ethanol transportation issue into play.

Furthermore, increases in per-acre yields would be required to make most cellulosic energy crops for fuel production economically competitive. Questions remain whether high yields can be achieved without the use of fertilizers and pesticides. Another question is whether there is sufficient feedstock supply available. USDA estimates that, by 2030, 1.3 billion tons of biomass could be available for bioenergy production (including electricity from biomass, and fuels from corn and cellulose).¹⁵ From that, enough biofuels could be produced to replace roughly 70

¹⁵ Oak Ridge National Laboratory for DOE and USDA, *Biomass as a Feedstock for a* (continued...)

billion gallons of gasoline per year (about 4.5 million barrels per day). However, this projection assumes significant increases in per-acre yields and, according to USDA, should be seen as an upper bound on what is possible. Further, new harvesting machinery would need to be developed to guarantee an economic supply of cellulosic feedstocks.¹⁶

In addition to the above concerns, other potential environmental drawbacks associated with cellulosic fuels must be addressed, such as the potential for soil erosion, runoff, and the spread of invasive species (many potential biofuel crops are invasive species when introduced into non-native localities). In the near term, the obvious choice of using corn stover to fuel existing corn ethanol plants has its own set of environmental trade-offs, paramount of which is the dilemma of sacrificing soil fertility gains from no- or minimum-tillage corn production.

Energy Supply Issues

Biofuels are not primary energy sources. Energy stored in biological material (through photosynthesis) must be converted into a more useful, portable fuel. This conversion requires energy. The amount and types of energy used to produce biofuels, and the feedstocks for biofuel production, are of key concern. Because of the input energy requirements, the energy and environmental benefits of corn ethanol, particularly, may be limited.

Energy Balance. A frequent argument for the use of ethanol as a motor fuel is that it reduces U.S. reliance on oil imports, making the U.S. less vulnerable to a fuel embargo of the sort that occurred in the 1970s. However, while corn ethanol use displaces petroleum, its overall effect on total energy consumption is less clear. To analyze the net energy consumption of ethanol, the entire fuel cycle must be considered. The fuel cycle consists of all inputs and processes involved in the development, delivery and final use of the fuel. For corn-based ethanol, these inputs include the energy needed to produce fertilizers, operate farm equipment, transport corn, convert corn to ethanol, and distribute the final product. Some studies find a significant positive energy balance of 1.5 or greater — in other words, the energy contained in a gallon of corn ethanol is 50% higher than the amount of energy needed to produce and distribute it. However, other studies suggest that the amount of energy needed to produce ethanol is roughly equal to the amount of energy obtained from its combustion. A review of research studies on ethanol's energy balance and greenhouse gas emissions found that most studies give corn-based ethanol a slight positive energy balance of about 1.2.¹⁷

¹⁵ (...continued)

Bioenergy and Bioproducts Industry: The Technical Feasibility of a Billion-Ton Annual Supply, April 2005, Oak Ridge, TN.

¹⁶ For example, the study assumes roughly 400 million tons of biomass from agricultural residues. To economically supply those residues to biofuel producers, farm equipment manufacturers likely would need to develop one-pass harvesters that could collect and separate crops and crop residues at the same time.

¹⁷ Alexander E. Farrell, Richard J. Plevin, Brian T. Turner, Andrew D. Jones, Michael (continued...)

If, instead, biomass was used to produce biofuels, the energy balance could be improved. It is expected that most biofuel feedstocks other than corn will require far less nitrogen fertilizer (produced from natural gas). Further, if biomass were used to provide process energy at the biofuel refinery, then the energy balance could be even greater. Some estimates are that cellulosic ethanol could have an energy balance of 8.0 or more.¹⁸ Similarly high energy balances have been calculated for sugarcane ethanol and biodiesel.

An expanded RFS would certainly displace petroleum consumption, but the overall effect on fossil fuel consumption is questionable, especially if there is a large reliance on corn-based ethanol. The mandate in the Senate bill to require an increasing amount of “advanced biofuels” would likely result in reduced fossil fuel consumption relative to gasoline. As the share of advanced biofuels grows, this effect would increase. However, by 2022, advanced biofuels will likely represent less than 10% of gasoline energy demand, so the total amount of fossil energy displaced would be less than the expected growth in fossil energy consumption from passenger transportation over the same time period.¹⁹

Natural Gas Demand. As ethanol production increases, the energy needed to process the corn into ethanol, which is derived primarily from natural gas in the United States, can be expected to increase. For example, if the entire 4.9 billion gallons of ethanol produced in 2006 used natural gas as a processing fuel, it would have required an estimated 240 to 290 billion cubic feet (cu. ft.) of natural gas.²⁰ If the entire 2006 corn crop of 10.5 billion bushels were converted into ethanol, the energy requirements would be equivalent to approximately 1.4 to 1.7 trillion cu. ft. of natural gas. This would have represented about 6% to 8% of total U.S. natural gas consumption, which was an estimated 22.2 trillion cu. ft. in 2005.²¹ The United States has been a net importer of natural gas since the early 1980s. A significant increase in its use as a processing fuel in the production of ethanol — and a feedstock for fertilizer production — would likely increase prices and imports of natural gas.

The Senate RFS proposal would likely promote an increase in corn ethanol to 15 billion gallons by 2015, requiring an increase in natural gas and/or fertilizer consumption. After 2015, the bill would promote a growing demand for fuels less dependent on natural gas.

¹⁷ (...continued)

O’Hare, and Daniel M. Kammen, “Ethanol Can Contribute to Energy and Environmental Goals,” *Science*, Jan. 27, 2006, pp. 506-508.

¹⁸ David Andress, *Ethanol Energy Balances*. November 2002.

¹⁹ For example, EIA projects that motor gasoline consumption will increase 22% between 2007 and 2011. EIA, *Annual Energy Outlook*. Table 11.

²⁰ CRS calculations based on energy usage rates of 49,733 Btu/gal of ethanol from Shapouri (2004), roughly 60,000 Btu/gal from Farrell (2006). Hosein Shapouri and Andrew McAloon, USDA, Office of the Chief Economist, *The 2001 Net Energy Balance of Corn-Ethanol*, 2004, Washington; Farrell, op. cit.

²¹ U.S. Department of Energy (DOE), Energy Information Administration (EIA), *Annual Energy Outlook 2006 with Projections to 2030*, Table 1-Total Energy Supply and Disposition Summary, Washington; at [<http://www.eia.doe.gov/oiaf/aeo/index.html>].

Energy Security.²² Despite the fact that ethanol displaces gasoline, the benefits to energy security from ethanol are not certain. As stated above, while roughly 20% of the U.S. corn crop is used for ethanol, ethanol only accounts for approximately 2% of gasoline consumption on an energy equivalent basis.²³ The import share of U.S. petroleum consumption was estimated at 54% in 2004, and is expected to grow to 70% by 2025.²⁴ Further, as long as ethanol remains dependent on the U.S. agricultural supplies, any threats to these supplies (such as drought), or increases in crop prices, would negatively affect the supply and/or cost of biofuels. In fact, that happened when high corn prices caused by strong export demand in 1995 contributed to an 18% decline in ethanol production between 1995 and 1996.

Further, expanding corn-based ethanol production to levels needed to significantly promote U.S. energy security is likely to be infeasible. If the entire 2007 U.S. corn crop of 13.2 billion bushels were used as ethanol feedstock, the resultant 35 billion gallons of ethanol (23.6 billion gasoline-equivalent gallons (GEG)) would represent about 16.7% of estimated national gasoline use of approximately 141 billion gallons.²⁵ In 2007, an estimated 86 million acres of corn were harvested (largest since 1944). Nearly 137 million acres would be needed to produce enough corn (20.5 billion bushels) and resulting ethanol (56.4 billion gallons or 37.8 billion GEG) to substitute for roughly 20% of petroleum imports.²⁶ Thus, barring a drastic realignment of U.S. field crop production patterns, corn-based ethanol's potential as a petroleum import substitute appears to be limited by crop area constraints, among other factors.²⁷

If an expanded RFS requires a significant amount of advanced biofuels, then the specific definition of "advanced biofuel" could affect the overall energy security picture for biofuels. For example, if ethanol from sugarcane is allowed under an expanded RFS (as under the Senate bill), this could provide an incentive to increase imports of sugarcane ethanol, especially from Brazil. If not, then the expanded RFS

²² A key question in evaluating the energy security benefits or costs of an expanded RFS is "what is the definition of energy security." For many policymakers, "energy security" and "energy independence" (i.e., producing all energy within our borders) are synonymous. For others, "energy security" means guaranteeing that we have reliable supplies of energy regardless of their origin. For this section, the former definition is used.

²³ By volume, ethanol accounted for approximately 3.6% of gasoline consumption in the United States in 2006, but a gallon of ethanol yields only 67% of the energy of a gallon of gasoline.

²⁴ DOE, EIA, *Annual Energy Outlook 2004 with Projections to 2025*, Washington.

²⁵ Based on USDA's Jan. 12, 2007, *World Agricultural Supply and Demand Estimates (WASDE) Report*, and using comparable conversion rates.

²⁶ This represents roughly half of gasoline's share of imported petroleum. However, petroleum imports are primarily unrefined crude oil, which is then refined into a variety of products. CRS calculations assume corn yields of 150 bushels per acre and an ethanol yield of 2.75 gal/bu.

²⁷ Two recent articles by economists at Iowa State University examine the potential for obtaining a 10 million acre expansion in corn planting: Bruce Babcock and D. A. Hennessy, "Getting More Corn Acres From the Corn Belt"; and Chad E. Hart, "Feeding the Ethanol Boom: Where Will the Corn Come From?" *Iowa Ag Review*, Vol. 12, No. 4, Fall 2006.

might provide an incentive for imports of biodiesel and other renewable diesel substitutes from tropical countries.

Energy Prices. The effects of an expanded RFS on energy prices are uncertain. If wholesale biofuels prices remain higher than gasoline prices (when all economic incentives are taken into account), then mandating higher and higher levels of biofuels would likely lead to higher gasoline pump prices. However, if petroleum prices — and thus, gasoline prices — remain high, the use of some biofuels might help to mitigate high gasoline prices.

Current costs are so high for some biofuels, especially cellulosic biofuels and biodiesel from algae, that significant technological advances (or even greater increases in petroleum prices) are necessary to lower their production costs to make them competitive with gasoline. Without such cost reductions, mandating large amounts of these fuels would likely raise fuel prices. If a price were placed on greenhouse gas emissions — a policy not proposed in the Senate energy bill — then the economics could shift in favor of these fuels despite their high production costs, as they have lower fuel-cycle and life-cycle greenhouse gas emissions (see below).

Greenhouse Gas Emissions

Biofuels proponents argue that a key benefit of biofuel use is a decrease in greenhouse gas (GHG) emissions. However, some question the overall GHG benefit of biofuels, especially corn-based ethanol. There is a wide range of fuel-cycle estimates for greenhouse gas reductions from corn-based ethanol. However, most studies have found that corn-based ethanol reduces fuel-cycle GHG emissions by 10%-20% per mile relative to gasoline.²⁸ These estimates vary depending on several factors including the cultivation practice (e.g., minimum-tillage versus normal tillage) used to grow the corn and the fuel used to process the corn into ethanol (e.g., natural gas versus coal). These same studies find that biofuels produced from sugar cane or cellulosic biomass could reduce fuel-cycle GHG emissions by as much as 90% per mile relative to gasoline.

However, fuel-cycle analyses generally do not take changes in land use into account. For example, if a previously uncultivated piece of land is tilled to plant biofuel crops, some of the carbon stored in the field could be released. In that case, the overall GHG benefit of biofuels could be compromised. One study estimates that taking land use into account (a life-cycle analysis, as opposed to a fuel-cycle analysis), the GHG reduction from corn ethanol is less than 3% per mile relative to gasoline,²⁹ while cellulosic biofuels have a life-cycle reduction of 50%.³⁰

The Senate bill requires that to qualify under the expanded RFS, biofuels produced at facilities commencing operations after the date of enactment must have

²⁸ EPA, *Greenhouse Gas Impacts of Expanded Renewable and Alternative Fuels Use*. April 2007; Farrell, et al.

²⁹ Mark A. Delucchi, *Draft Report: Life cycle Analyses of Biofuels*. 2006.

³⁰ While a 50% life-cycle reduction is still significant, it is far less than the 90% reduction suggested by fuel-cycle analyses.

a 20% life-cycle emissions reduction. However, it is expected that this provision may not be relevant to a large share of conventional ethanol since much of the capacity to meet the 15 billion gallon cap is currently existing or will come from expansions of existing plants. If enactment of the Senate bill is delayed (or if plants currently under construction are grandfathered under the bill) the GHG reductions from conventional ethanol may be insignificant. However, the more “advanced biofuel” required under the bill, the greater the likely benefit in terms of GHG reductions.

Agricultural Issues

A continued expansion of corn-based ethanol production could have significant consequences for traditional U.S. agricultural crop production and rural economies. Supporters of an expanded RFS claim that increased biofuels production and use would have enormous agricultural and rural economic benefits by increasing farm and rural incomes and generating substantial rural employment opportunities.³¹ However, large-scale shifts in agricultural production activities will likely also have important regional economic consequences that have yet to be fully explored or understood. As corn prices rise, so too does the incentive to expand corn production either by expanding onto more marginal soil environments or by altering the traditional corn-soybean rotation that dominates Corn Belt agriculture. This shift could displace other field crops, primarily soybeans, and other agricultural activities. Further, corn production is among the most energy-intensive of the major field crops. An expansion of corn area would likely have important and unwanted environmental consequences due to the increases in fertilizer and chemical use and soil erosion. The National Corn Growers Association estimates that U.S. corn-based ethanol production could expand to between 12.8 and 17.8 billion gallons by 2015 without significantly affecting agricultural markets.³² However, as noted below, other evidence suggests effects are already being felt in the current expansion in corn production.

Food versus Fuel. Many critics of federal biofuels subsidies and the RFS argue that a sustained rise in grain prices driven by ethanol feedstock demand likely will lead to higher U.S. and world food prices with potentially harmful effects on consumer budgets and nutrition.³³ As evidence they cite USDA’s estimate that the U.S. Consumer Price Index (CPI) for all food is forecast to increase 3.5% to 4.5% in 2007 compared with an increase of 2.4% in 2006 and, an average annual rate of 2.5% over the past ten years (1997-2006).³⁴ However, in analyzing this critique it is

³¹ For example, see John M. Urbanchuk (Director, LECG LLC), *Contribution of the Ethanol Industry to the Economy of the United States*, white paper prepared for National Corn Growers Assoc., February 21, 2006.

³² National Corn Growers Association, *How Much Ethanol Can Come From Corn?*, November 9, 2006, Washington D.C.

³³ For a discussion, see the National Corn Growers Association’s online “Food versus Fuel Debate,” at [<http://www.ncga.com/news/OurView/pdf/2006/FoodANDFuel.pdf>].

³⁴ ERS, USDA, Briefing Room “Food CPI, Prices, and Expenditures,” at [<http://www.>

important to distinguish between prices of farm-level crops and retail-level food products because most “food” prices are largely determined by costs and profits after the commodities leave the farm.³⁵ Basic economics suggests that the price of a particular retail food item varies with a change in the price of an underlying ingredient in direct relation to the relative importance (in value terms) of that ingredient. For example, if the value of wheat in a \$1.00 loaf of bread is about 10¢, then a 20% rise in the price of wheat translates into a 2¢ rise in a loaf of bread.

As a result of corn’s relatively small value-share in most retail food product prices, it is unlikely that the ethanol-driven corn price surge is a major factor in current food price inflation estimates.³⁶ Furthermore, economists generally agree that most retail food price increases are not due to ethanol-driven demand increases, but rather are the result of two major factors — a sharp increase in energy prices which ripples through all phases of marketing and processing channels, and the strong increase in demand for agricultural products in the international marketplace from China and India (a product of their large populations and rapid economic growth).³⁷

Feed Markets. Most corn grown in the United States is used for animal feed. From 1995 through 2005, domestic feed use accounted for 58% of U.S. corn use. As corn-based ethanol production increases, so do total corn demand and corn prices. As a result, prolonged higher corn prices likely will have significant consequences for traditional feed markets and the livestock industries — hog, cattle, dairy, and poultry — that depend on those feed markets. Corn traditionally has represented about 57% of feed concentrates and processed feedstuffs fed to animals in the United States.³⁸ Persistently high feed costs will tighten profit margins and likely squeeze out marginal livestock producers. Because economies of scale tend to favor larger producers, persistently tighter profit margins suggest a potential for increased concentration in the livestock sector. The National Cattlemen’s Beef Association (NCBA) has been one of the foremost critics of an expanded RFS. Instead, the NCBA argues for a phase out of current ethanol subsidies and a more market-based approach to renewable fuels policy.³⁹

³⁴ (...continued)

ers.usda.gov/Briefing/CPIFoodAndExpenditures/consumerpriceindex.htm].

³⁵ Helen H. Jensen and Bruce A. Babcock, “Do Biofuels Mean Inexpensive Food is a Thing of the Past?” *Iowa Ag Review*, Spring 2007, Vol. 13, No. 2, pp. 1-3.

³⁶ For examples, see Food & Water Watch, “Retail Realities: Corn Prices Do Not Drive Grocery Inflation,” Sept. 2007; and John M. Urbanchuk (Director, LECG LLC), “The Relative Impact of Corn and Energy Prices in the Grocery Aisle,” white paper prepared for National Corn Growers Assoc., June, 14, 2007.

³⁷ For examples, see Jacque Diouf, Director General of the U.N. Food and Agriculture Organization, “Why Are Food Prices Rising?” in *Financial Times Online*, Nov. 26, 2007; [<http://media.ft.com/cms/s/2/f5bd920c-975b-11dc-9e08-0000779fd2ac.html?from=textlink>]. See also, Keith Collins, Chief Economist, USDA, Testimony before the House Committee on Agriculture, October 18, 2007.

³⁸ USDA, ERS, *Feed Situation and Outlook Yearbook*, FDS-2003, Apr. 2003, Washington.

³⁹ “NCBA on Renewable Fuel Policy,” NCBA Issue Backgrounder-2007; available at [<http://www.beefusa.org/uDocs/NCBAonRenewableFuelPolicy-2007.pdf>].

Table 3. U.S. Farm Prices for Major Agricultural Commodities

Commodity	Unit	Farm Market Prices				USDA Program Prices ^g	
		Average 1997-2006	Actual 2006/07	Projections		Loan rate	Target Price
				2007/08 ^d	2012/13 ^e		
Wheat ^a	\$/bu	3.24	4.26	6.20	4.29	2.75	3.92
Corn ^a	\$/bu	2.15	3.04	3.50	3.25	1.95	2.63
Sorghum ^a	\$/bu	2.04	3.29	3.30	3.02 ^f	1.95	2.57
Barley ^a	\$/bu	2.38	2.85	3.85	3.11 ^f	1.85	2.44
Oats ^a	\$/bu	1.54	1.87	2.40	1.90 ^f	1.33	1.44
Rice ^a	\$/cwt	7.17	9.74	11.00	9.64	6.50	10.50
Soybeans ^a	\$/bu	5.72	6.43	9.00	7.72	5.00	5.80
Soybean oil ^b	¢/lb	21.4	31.0	39.5	36.8	—	—
Soybean meal ^b	\$/st	187.7	205.4	250.0	202.0	—	—
Cotton, Upland	¢/lb	50.3	46.5	53.9 ^e	59.9	52.0	72.4
Choice Steers ^c	\$/cwt	73.5	85.4	91.6	86.4	—	—
Barrows/Gilts ^c	\$/cwt	42.2	47.3	47.0	54.3	—	—
Broilers ^c	¢/lb	37.9	64.4	76.1	77.2	—	—
Eggs ^c	¢/doz	63.7	71.8	109.1	85.4 ^f	—	—
Milk ^c	\$/cwt	13.91	12.90	19.00	15.7	—	—

- a. Season average farm price from USDA, National Agricultural Statistical Service, *Agricultural Prices*. — = no loan rate.
- b. USDA, Agr. Marketing Service (AMS), Decatur, IL, cash price, simple average crude for soybean oil, and simple average 48% protein for soybean meal.
- c. Calendar year data for the first year, e.g., 2000/2001 = 2000; USDA, AMS: choice steers — Nebraska, direct 1100-1300 lbs.; barrows/gilts — national base, live equivalent 51%-52% lean; broilers — wholesale, 12-city average; eggs — Grade A, New York, volume buyers; and milk — simple average of prices received by farmers for all milk.
- d. Unless otherwise indicated: mid-point of price projection range from USDA, *World Agricultural Supply and Demand Estimates (WASDE)* Nov. 9, 2007;.
- e. Unless otherwise indicated: FAPRI, *Baseline Update for U.S. Agricultural Markets*, August 2007.
- f. FAPRI, *U.S. Baseline Briefing Book, February 2007*, FAPRI-UMC Report #02-07.
- g. For more information on U.S. commodity programs see CRS Report RL33271, *Farm Commodity Programs: Direct Payments, Counter-Cyclical Payments, and Marketing Loans*.

The price of corn also is linked to the price of other grains, including those destined for food markets, through competition in the feed marketplace and in the producer's planting choices for limited acreage. The price runup in the U.S. corn market has already spilled over into price increases in the markets for soybeans and soybean oil. Supply distortions also are likely to develop in protein-meal markets related to expanded production of the ethanol processing by-product distiller's dried grains with solubles (DDGS), which averages about 30% protein content and can substitute in certain feed and meal markets.⁴⁰

⁴⁰ For a discussion of potential feed market effects due to growing ethanol production, see (continued...)

While DDGS use would substitute for some of the lost feed value of corn used in ethanol processing, about 66% of the original weight of corn is consumed in producing ethanol and is no longer available for feed. Furthermore, not all livestock species are well adapted to dramatically increased consumption of DDGS in their rations — dairy cattle appear to be best suited to expanding DDGS's share in feed rations; poultry and pork are much less able to adapt. Also, DDGS must be dried before it can be transported long distances, adding to feed costs. There may be some potential for large-scale livestock producers to relocate near new feed sources, but such relocation likely would have important regional economic effects.

Domestic Food Prices. Although corn primarily is used as a livestock feed or for ethanol production, corn also is used widely as an ingredient (albeit minor) in many processed foods, e.g., soft drinks, snack foods, and baked goods. Since corn prices are a relatively small share of the price of most retail food products, their price impact is concomitantly small. Higher corn prices have their largest impact on meat prices. The feed-price effect will first translate into higher prices for poultry and hogs, which are less able to use alternate feedstuffs. Dairy and beef cattle are more versatile in their ability to shift to alternate feed sources, but eventually a sustained rise in corn prices will push their feed costs upward as well. A recent economic study estimated that a 30% increase in the price of corn, and associated increases in the prices of wheat and soybeans, would increase egg prices by 8.1%, poultry prices by 5.1%, pork prices by 4.5%, beef prices by 4.1%, and milk prices by 2.7%.⁴¹ The effect on all food consumed was a 1.1% increase (0.9% on at-home food and 1.3% on away-from-home food consumption). Thus, the price impact of higher corn prices is small but important for most livestock products, and probably much smaller for most other retail food products.

The overall impact to consumers from higher food prices depends on the proportion of income that is spent on food. Since food costs represent a relatively small share of consumer spending for most U.S. households (about 10%), food price increases (from whatever source) are absorbed relatively easily in the short run. However, low-income consumers spend a much greater proportion of their income on food than do high-income consumers. Their larger share combined with less flexibility to adjust expenditures in other budget areas means that any increase in food prices potentially could cause hardship.⁴² In addition, higher commodity prices combined with shrinking inventories mean that local school districts and the U.S. government will be forced to pay higher market prices for food for school lunch

⁴⁰ (...continued)

Bob Kohlmeyer, "The Other Side of Ethanol's Bonanza," *Ag Perspectives* (World Perspectives, Inc.), Dec. 14, 2004; and R. Wisner and P. Baumel, "Ethanol, Exports, and Livestock: Will There be Enough Corn to Supply Future Needs?," *Feedstuffs*, no. 30, vol. 76, July 26, 2004.

⁴¹ Simla Tokgoz and others, "Emerging Biofuels: Outlook of Effects on U.S. Grain, Oilseed, and Livestock Markets," Staff Report 07-SR 101, Center for Agricultural Research and Development (CARD), Iowa State University, May 2007.

⁴² Helen H. Jensen and Bruce A. Babcock, "Do Biofuels Mean Inexpensive Food is a Thing of the Past?" *Iowa Ag Review*, Spring 2007, Vol. 13, No. 2, pp. 1-3.

programs. And the automatic food price escalators built into the food stamp program mean rising expenditures as well.⁴³

International Food Prices. Due to trade linkages, the increase in U.S. corn prices has become a concern for international markets, as well. High commodity prices ripple through international markets where impacts vary widely based on grain import dependence and the ability to respond to higher commodity prices. Import-dependent developing country markets are put at greater food security risk due to the higher cost of imported commodities. In particular, lower-income households in many foreign markets where food imports are an important share of national consumption and where food expenses represent a larger portion of the household budget may be affected by higher food prices.⁴⁴ In China, where corn is an important food source, the government recently has put a halt to its planned ethanol plant expansion due to the threat it poses to the country's food security. Similarly, humanitarian groups have expressed concern for the potential difficulties that higher grain prices imply for developing countries that are net food importers.⁴⁵

Exports. The United States is the world's leading exporter of corn. In the past decade (1997 to 2006), the United States has exported about 20% of its corn production, accounting for nearly 66% of world corn trade.⁴⁶ Increased use of corn for ethanol production could diminish U.S. capacity for exports. In 2006, the volume of corn used for ethanol equaled exports, with a 20% share of total use. By the 2009/10 marketing year (September-August), ethanol's share of U.S. corn production is expected to reach nearly 36%, while the export share falls to 13%.⁴⁷ FAPRI projections clearly suggest that higher corn prices will result in lost export sales. It is unclear what type of market adjustments will occur in global feed markets, since several different grains and feedstuffs are relatively close substitutes. Price-sensitive corn importers may quickly switch to alternative, cheaper sources of feed, depending on the availability of supplies and the adaptability of animal rations. In contrast, less price-sensitive corn importers, such as Japan and Taiwan, may choose to pay a higher price in an attempt to bid the corn away from ethanol plants. There could be significant economic effects to U.S. grain companies and to the U.S. agricultural sector if ethanol-induced higher corn prices led to a sustained reshaping of international grain trade.

Economic Impact. Several studies claim that increased biofuels production and use would have enormous agricultural and rural economic benefits by increasing

⁴³ Ibid.

⁴⁴ Shahla Shapouri and Stacey Rosen, "Energy Price Implications for Food Security in Developing Countries," *Food Security Assessment, 2006*, GFA-18, Economic Research Service, USDA.

⁴⁵ International Monetary Fund, *World Economic Outlook: Globalization and Inequality*. October 2007. Washington.

⁴⁶ USDA, Production, Supply and Distribution Online (PSD database) available at [<http://www.fas.usda.gov/psdonline/psdHome.aspx>].

⁴⁷ FAPRI, *Baseline Update for U.S. Agricultural Markets*, August 2007.

farm and rural incomes and generating substantial rural employment opportunities.⁴⁸ One estimate suggested that the economic benefit from the ethanol industry to the U.S. economy for 2005 was \$17.7 billion of GDP; the creation of over 150,000 jobs; \$5.7 billion in spinoff economic activity, and more than \$3.5 billion in government tax revenues.⁴⁹ However, a recent critical review of the standard input-output methodology used to generate such economic impact estimates suggests that the income and job growth attributable to biofuels production has been grossly overstated (perhaps by as much as a factor of 4 or 5).⁵⁰ Yet, while the magnitude may be called into question, there appears to be no doubt about the potential positive value of biofuels production to rural economies. First, in addition to temporary construction work to build a new plant, several dozen permanent jobs also accompany a biofuel plant (the eventual job number depends on the size of the plant's operating capacity). Second, the new demand boosts the local prices received by farmers for corn and sorghum. Third, important secondary economic activity is associated with the operation of an ethanol plant. Fourth, given the high level of federal and state subsidies for the biofuels industry, any locality that is home to a biofuels plant can expect substantial net transfers of government funds into the area's economy.

The policy question of interest is not whether there are positive gains from growth in the ethanol industry, but whether the growth and its economic implications are sufficient to merit large government subsidies. A growing number of critics argue that the answer is no.⁵¹ Other suggest that, at the very least, the issue deserves more study before expanding current government support levels.⁵²

⁴⁸ For example, see John M. Urbanchuk (Director, LECG LLC), *Contribution of the Ethanol Industry to the Economy of the United States*, white paper prepared for National Corn Growers Assoc., February 21, 2006; see also Urbanchuk, *Contribution of the Biofuels Industry To the Economy of Iowa*, white paper prepared for the Iowa Renewable Fuels Association, February 2007.

⁴⁹ Urbanchuk (2006).

⁵⁰ David Swenson, "Input-Outrageous: The Economic Impacts of Modern Biofuels Production," Dept. of Econ, Iowa State University (ISU), June 2006. Similar results are found in: David Swenson, "Understanding Biofuels Economic Impact Claims," Dept. of Econ, ISU, April 2007; Lisa Eathington and Dave Swenson, "Dude, Where's My Corn? Constraints on the Location of Ethanol Production in the Corn Belt," Dept. of Econ, ISU, paper presented at 46th Annual Meeting of the Southern Regional Science Assoc., Charleston, SC, March 29-31, 2007; Swenson and Eathington, "Determining the Regional Economic Values of Ethanol Production in Iowa Considering Different Levels of Local Investment," Dept. of Econ, ISU, July 2006.

⁵¹ Examples include Robert Hahn and Caroline Cecot, "The Benefits and Costs of Ethanol," Working Paper 07-17, AEI-Brookings Joint Center for Regulatory Studies, November 2007; Richard Doornbosch and Ronald Steenblik, "Biofuels: is the Cure Worse Than the Disease?," paper presented at an OECD Round Table on Sustainable Development, Paris, September 11-12, 2007; and Doug Koplow, *Biofuels at What Cost? Government Support for Ethanol and Biodiesel in the United States: 2007 Update*, report prepared for the Global Studies Initiative of the International Institute for Sustainable Development, Geneva, Switzerland, October 2007.

⁵² For example, see Bruce A. Babcock, "High Crop Prices, Ethanol Mandates, and the Public (continued...)"

Infrastructure and Distribution Issues

In addition to the above concerns about raw material supply for biofuel production (both feedstock and energy), there are issues involving biofuel distribution and infrastructure. Expanding ethanol production likely will strain the existing supply infrastructure. Further, expansion of ethanol use beyond certain levels will require investment in entirely new infrastructure that would be necessary to handle a higher and higher percentage of ethanol in gasoline. If biomass-based diesel substitutes are produced in much larger quantities, some of these infrastructure issues may be mitigated.

Distribution Issues. Ethanol-blended gasoline tends to separate in pipelines. Further, ethanol is corrosive and may damage existing pipelines. Therefore, unlike petroleum products, ethanol and ethanol blended gasoline cannot be shipped by pipeline in the United States. Another issue with pipeline transportation is that corn ethanol must be moved from rural areas in the Midwest to more populated areas, which are often located along the coasts. This shipment is in the opposite direction of existing pipeline transportation, which moves gasoline from refiners along the coast to other coastal cities and into the interior of the country. While some studies have concluded that shipping ethanol or ethanol-blended gasoline via pipeline could be feasible, no major U.S. pipeline has made the investments to allow such shipments.⁵³

Thus, the current distribution system for ethanol is dependent on rail cars, tanker trucks, and barges. These deliver ethanol to fuel terminals where it is blended with gasoline before shipment via tanker truck to gasoline retailers. However, these transport modes lead to higher prices than pipeline transport, and the supply of current shipping options (especially rail cars) is limited. For example, according to industry estimates, the number of ethanol carloads has tripled between 2001 and 2006, and the number is expected to increase by another 30% in 2007.⁵⁴ A significant increase in corn-based ethanol production would further strain this tight transport situation.

Because of these distribution issues, some pipeline operators are seeking ways to make their systems compatible with ethanol or ethanol-blended gasoline. These modifications could include coating the interior of pipelines with epoxy or some other, corrosion-resistant material. Another potential strategy could be to replace all susceptible pipeline components with newer, hardier components. However, even if such modifications are technically possible, they likely will be expensive, and could further increase ethanol transportation costs.

⁵² (...continued)

Good: Do They Coexist?" *Iowa Ag Review*, Vol. 13, No. 2, Spring 2007.

⁵³ Some small, proprietary ethanol pipelines do exist. American Petroleum Institute, *Shipping Ethanol Through Pipelines*. Available at [<http://www.api.org/aboutoilgas/sectors/pipeline/upload/pipelineethanolshipment-2.doc>]

⁵⁴ Ilan Brat and Daniel Machalaba, "Can Ethanol Get a Ticket to Ride?," *The Wall Street Journal*, Feb. 1, 2007, p. B1.

If non-corn biofuels play a larger role, as required in the Senate bill, some of the supply infrastructure concerns may be alleviated. Cellulosic biofuels potentially can be produced from a variety of feedstocks, and may not be as dependent on a single crop from one region of the country. For example, municipal solid waste is ubiquitous across the United States, and could serve as a ready feedstock for biofuel production if the technology were developed to convert it to fuel economically. Further, increased imports of biofuels from other countries could allow for greater use of biofuels, especially along the coasts.

Higher-Level Ethanol Blends. One key benefit of gasoline-ethanol blends up to 10% ethanol is that they are compatible with existing vehicles and infrastructure (e.g., fuel tanks, retail pumps, etc.). All automakers that produce cars and light trucks for the U.S. market warranty their vehicles to run on gasoline with up to 10% ethanol (E10). This 10% currently is an upper bound to the amount of ethanol that can be introduced into the gasoline pool. If most or all gasoline in the country contained 10% ethanol, this would allow only for roughly 15 billion gallons, far less than the amount of biofuel mandated in the Senate bill.

As a major producer of ethanol for its domestic market, Brazil has a mandate that all of its gasoline contain 20-25% ethanol. For the United States to move to E20 (20% ethanol, 80% gasoline), it may be that few (if any) modifications would need to be made to existing vehicles and infrastructure. Vehicle testing, however, would be necessary to determine whether new vehicle parts would be required, or if existing vehicles are compatible with E20. Similar testing would be necessary for terminal tanks, tanker trucks, retail tanks, pumps, etc. In addition, EPA would need to certify that the fuel will not lead to increased air quality problems.

There is also interest in expanding the use of E85 (85% ethanol, 15% gasoline). Current E85 consumption represents only about 1% of ethanol consumption in the United States. A key reason for the relatively low consumption of E85 is that relatively few vehicles operate on E85. The National Ethanol Vehicle Coalition estimates that there are approximately six million E85-capable vehicles on U.S. roads,⁵⁵ as compared to approximately 230 million gasoline- and diesel-fueled vehicles.⁵⁶ Most E85-capable vehicles are “flexible fuel vehicles” or FFVs. An FFV can operate on any mixture of gasoline and between 0% and 85% ethanol. However, owners of a large majority of the FFVs on U.S. roads choose to fuel them exclusively with gasoline, largely due to higher per-mile fuel cost⁵⁷ and lower availability of E85.

E85 capacity is expanding rapidly, with the number of E85 stations roughly doubling between February 2006 and February 2007. But those stations still

⁵⁵ National Ethanol Vehicle Coalition, *Frequently Asked Questions*, accessed February 3, 2006, at [<http://www.e85fuel.com/e85101/faq.php>].

⁵⁶ Federal Highway Administration, *Highway Statistics 2003*, November 2004, Washington.

⁵⁷ Ethanol has a lower energy content than gasoline per gallon. Therefore, FFVs tend to have lower fuel economy when operating on E85. For the use of E85 to be economical, the pump price for E85 must be low enough to make up for the decreased fuel economy relative to gasoline. Generally, to have equivalent per-mile costs, E85 must cost 20% to 30% less per gallon at the pump than gasoline.

represent less than 1% of U.S. gasoline retailers. Further expansion will require significant investments, especially at the retail level. If a new E85 pump and underground tank are necessary, they can cost as much as \$100,000 to \$200,000 to install.⁵⁸ However, if existing equipment can be used with little modification, the cost could be less than \$10,000.

Vehicle Infrastructure Issues. As was stated above, if a large portion of any increased RFS is met using ethanol, then the United States likely does not have the vehicles to consume the fuel. The 10% limit on ethanol in gasoline for conventional vehicles poses a significant barrier to expanding ethanol consumption beyond 15 billion gallons per year.⁵⁹ To allow more ethanol use, vehicles will need to be certified and warranted for higher-level ethanol blends, or the number of ethanol FFVs will need to increase.

Conclusion

There is continuing interest in expanding the U.S. biofuel industry as a strategy for promoting energy security and environmental goals. However, there are limits to the amount of biofuels that can be produced from current feedstocks and questions about the net energy and environmental benefits they would provide. Further, rapid expansion of biofuel production may have many unintended and undesirable consequences for agricultural commodity costs, fossil energy use, and environmental degradation. As policies are implemented to promote ever-increasing use of biofuels, the goal of replacing petroleum use with agricultural products competes with these other potential consequences. Further, alternative strategies for energy conservation and alternative energy production are widely seen as warranting consideration.

⁵⁸ David Sedgwick, *Automotive News*, January 29, 2007. p. 112.

⁵⁹ Note that 15 billion gallons is the corn starch ethanol limit for the expanded RFS in the Senate-passed energy bill.