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Reforming the Biodiesel Tax Incentive to a Production Credit

Converting the current \$1 per gallon tax credit for Biodiesel, Renewable Diesel and Renewable Aviation Fuels from a blender's credit to a producer's credit for domestic production is a common-sense reform that would deliver significant public policy benefits:

Stop Subsidizing Foreign Manufacturing: U.S. tax dollars and energy policy should be – and typically are – aimed at incentivizing domestic production, not foreign production. The current structure of the biodiesel tax incentive as a blender's credit increasingly allows foreign producers to access the credit if their fuel is blended in the U.S. Subsidizing foreign manufacturing is obviously not the intent of Congress, and we should close this loophole by reforming the credit as a domestic production credit. Importantly, this reform would not block imported biodiesel from entering the U.S. market, and in fact significant imports would likely continue coming to the U.S. and receiving incentives under the RFS and California's Low Carbon Fuel Standard.

Save Taxpayers Dollars: Biodiesel imports to the U.S. have grown sharply in recent years, largely as a result of the tax credit. In 2015 alone, the U.S. Treasury spent more than \$600 million on tax credits for imported biodiesel and renewable diesel. Importantly, this fuel often had already received subsidies in its country of origin (Argentina, Indonesia and the European Union, for example). According to the Joint Committee on Taxation, reforming the tax incentive would save U.S. taxpayers \$90 million as imports are reduced and domestic production grows.

Mobilize U.S. Capacity and Create American Manufacturing Jobs: There is more than enough U.S. production capacity to meet U.S. demand. With significant underutilized capacity in the domestic industry, biodiesel producers across the country are waiting for the right policy signals to expand production. With more than 3.1 billion gallons of installed capacity last year and about 1.4 billion gallons of actual domestic production, the U.S. industry is more than capable of meeting robust requirements under the Renewable Fuel Standard (RFS). We estimate U.S. production would immediately rise by approximately 400 million gallons, creating thousands of jobs while strengthening U.S. energy security and improving refining capacity to prevent bottlenecks that result in price spikes.

Level the Playing Field: U.S. biodiesel producers need a level playing field to compete with foreign production. For example, since 2009, the European Union has levied duties on U.S. biodiesel that effectively block U.S. biodiesel from entering the European market. At the same time, U.S. policy is incentivizing European biodiesel shipments to the U.S. by rewarding it with the \$1-per-gallon credit. Additionally, Argentinian biodiesel that receives significant incentives under that country's Differential Export Tax regime is increasingly being shipped to the U.S. market where it also can qualify for the U.S. tax incentive. Without this reform, U.S. tax policy is increasingly creating competitive disparities in which U.S. companies are losing U.S. market share to subsidized foreign production in Europe, Argentina and other nations.

Continue to Lower the Cost of Diesel Fuel for Consumers: The \$1-per-gallon production tax credit is passed down through the biodiesel value chain throughout the distribution system, ultimately decreasing costs for retail consumers. Biodiesel producers and blenders already structure transactions with the value of the credit “baked into” the sale. The credit as reformed would have the same value as the historical “blender’s” credit, and blenders would continue to benefit.

Streamline IRS Administration and Reduce Potential for Tax Fraud: Today, thousands of “blenders” are registered to blend biodiesel and renewable diesel to produce transportation diesel fuel and home heating oil (Bioheat). It is difficult for the IRS to administer the credit and monitor compliance under this decentralized blending system. However, fewer than 200 companies are producing biodiesel and renewable diesel today. This reform would significantly streamline administration of the credit and avoid fraud or abuse by sharply narrowing the number of potential claimants for the credit.

Address International Trade Laws: The proposed reform is well within the parameters of established international trade accords. The limitation of tax benefits to activity within the U.S. has been a feature of numerous tax provisions, as well as recent proposals for new benefits, such as the Boustany-Neal Innovation Box and the recently introduced American Energy Innovation Act of 2015, where both the electricity and fuel sections contain a domestic production requirement. Other provisions that target tax benefits to domestic US activity include bonus depreciation (Section 168(k)), the R&D tax credit (Section 41), the domestic manufacturers deduction (Section 199), as examples.

Strengthen the Bioheat Market: The U.S. biodiesel industry has invested millions of dollars and spent years to help build the Bioheat market, particularly in the Northeast, where biodiesel is increasingly blended into home heating oil to create a cleaner product. There is more than enough domestic production to meet the demand from the U.S. Bioheat market, and this reform will strengthen that market by continuing to grow a strong domestic biodiesel industry with regional production nationwide. The value of the tax credit will be the same for Bioheat under a producer’s credit. The credit would be negotiated and shared throughout the distribution chain just as it is under a blender’s structure, and the reform will ensure that Bioheat blenders incur no new tax liability.

Increase Quality Control of Finished Diesel Fuel: Misfueling is a hazardous condition for truck drivers and other consumers. A production tax credit would decrease the number of inefficient blenders seeking to take advantage of the credit, which would increase fuel quality.