

State biofuel subsidies costly but effective, MSU research shows

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States aiming to lead the emerging biofuel industry may need to ante up substantial subsidies and tax incentives to ethanol producers just to get in the game, Michigan State University researchers say.

"State subsidies have played an important role in ethanol plant location decisions," explained Mark Skidmore, MSU professor of agricultural, food and resource economics. "The size of the incentives is important, too -- the larger the subsidy or tax credit, the more likely it is that an ethanol plant will locate in that state."

Skidmore and Chad Cotti, assistant professor of economics at the University of Wisconsin-Oshkosh, examine the influence of federal and state incentives for corn-grain ethanol production in the April 2010 issue of the *Southern Economic Journal*.

Experts agree that federal subsidies -- currently 51 cents per gallon for ethanol/gasoline blends -- have helped expand national ethanol production capacity. Skidmore and Cotti's paper is one of the first to analyze the effect of state incentives on the corn-grain ethanol industry. No commercial [cellulosic ethanol plant](#), using wood and field waste instead of corn, has yet opened in the United States.

Such economic incentives don't come cheap. In Wisconsin, which offers a subsidy of 20 cents per gallon for ethanol up to 15 million gallons, the cost works out to be about \$71,000 per ethanol plant worker, according to the scientists' research. Many of the incentives are ongoing, Skidmore

added, so represent a long-term commitment from the state to subsidize biofuel production.

"Ultimately, state tax dollars are used to pay for these subsidies," he said. "It's up to a state's political leaders to decide if ethanol subsidies are the best use for those funds and if the benefits of ethanol production are worth the cost."

U.S. ethanol production was minimal in 1980, but increased to 6,500 million gallons by 2007. Michigan has had ethanol tax credits and subsidies in place since 2003 and the state's [ethanol production](#) capacity in 2007 was 262 million gallons.

"If a state wants to play a significant role in the emerging biofuel industry, then policymakers may need to consider ethanol incentives," Skidmore said. "States such as Iowa and Nebraska offered ethanol incentives relatively early and this has enabled them to lead the industry -- plus those two states also have ideal corn growing conditions. But even states such as Oklahoma and Montana, which can't grow corn very well, offer ethanol subsidies. Like Michigan, this could set them up to be leaders in the cellulosic ethanol industry when that becomes commercially viable."

More information: The paper "The Impact of State Government Subsidies and Tax Credits in an Emerging Industry: Ethanol Production 1980-2007" is available online on *Southern Economic Journal*.

Provided by Michigan State University

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