P.O. Box 684823
Austin, Texas 78768
P (512) 236-2245
F (512) 236-2002
www.biodieselcoalitionoftexas.org

October 27, 2008

CC:PA:LPD:PR (REG–155087–05),
Room 5203
Internal Revenue Service
PO Box 7604
Ben Franklin Station
Washington, DC 20044

Submitted Electronically *via the Federal eRulemaking Portal at http://www.regulations.gov (IRS REG–155087–05).*

Delivered By Hand *to CC:PA:LPD:PR (REG–155087–05), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC.*

The Biodiesel Coalition of Texas (BCOT) appreciates the opportunity to provide comments on the Internal Revenue Service's (IRS) notice of proposed rulemaking pertaining to ***Alcohol Fuel and Biodiesel; Renewable Diesel; Alternative Fuel; Diesel-Water Fuel Emulsion; Taxable Fuel Definitions; Excise Tax Returns (REG-155087-05).***

Comments in Brief:

- BCOT is concerned with the Proposed Regulations that would make B99.9 a taxable fuel without regard to existing IRS regulations pertaining to excluded liquids. This would have a significant, negative impact on the industry. Further, IRS implementation of an ExStars-based reporting requirement to track below the rack biodiesel sales would have an even more onerous impact on industry.
- BCOT requests that the IRS implement the provision in P.L. 110-343 that allows all biodiesel, regardless of feedstock used to produce the fuel, to claim the $1 per gallon biodiesel blenders excise tax in a timely manner consistent with the January 1, 2009 effective date in P.L. 110-343.
- BCOT urges the IRS to use authority provided in P.L. 110-343 to close the so-called "splash and dash" loophole.
- BCOT asks the IRS to revise Notice 2007-37 to reflect the change in P.L. 110-343 that clarifies that co-processed renewable diesel does not qualify for the $1 per gallon renewable diesel tax incentive.

•To avoid putting the American Society of Testing and Materials (ASTM) in the position of a regulatory body and to give non-ASTM members adequate time to review changes in biodiesel fuel specifications, IRS should proceed with a rulemaking process before changing the version of the ASTM D6751 fuel specification applicable to the biodiesel tax incentive.

About BCOT: BCOT is a trade association established to promote the development of biodiesel in the State of Texas. BCOT's long-term mission is to work with the public and private sector to foster the production, distribution and use of biodiesel in Texas. BCOT has over 25 members, ranging from producers to distributors to consultants in related industries.

Background and Industry Overview: Biodiesel is a diesel fuel replacement that is made from agricultural oils, fats and waste greases that meets a specific commercial fuel definition and specification. The fuel is produced by reacting feedstock with an alcohol to remove the glycerin and meet the D6751 fuel specifications set forth by the American Society for Testing and Materials (ASTM International).

Biodiesel is primarily marketed as a blended product with conventional diesel fuel, typically in concentrations up to 20%. It is distributed utilizing the existing fuel distribution infrastructure with blending most commonly occurring "below the rack" by fuel jobbers.

Texas and Biodiesel

Texas has quickly become the nations leading producer of biodiesel, with over 500 million gallons of installed capacity. The economic impact from biodiesel development in Texas is substantial. According to a study by the Texas A&M University, in 2006 biodiesel accounted for approximately $800 million of direct, indirect and induced economic impact to the state. The biodiesel industry also created roughly 1,100 jobs. If operating at capacity in 2008, the economic impact of the biodiesel industry would be $3.6 billion and represent almost 10,000 jobs. Further, should the state develop a jatropha industry to supply feedstock for the 2008 Texas biodiesel industry capacity, it would represent an estimated $22.5 billion industry and create over 141,000 jobs. A majority of these jobs and economic benefits go to small businesses such as farmers and biodiesel producers.

Biodiesel Tax Incentive Success Story: The biodiesel tax incentive has helped achieve the worthwhile policy goal of increasing the production and use of biodiesel in the U.S. Since the inception of the biodiesel excise tax credit in 2004, the industry has grown from 25 million gallons per year to 500 million gallons of production in the US in 2007. This production displaced 20 million barrels of petroleum.

Public Policy Benefits: There are numerous compelling energy, environmental, and national security policy arguments favoring increased biodiesel production and use in the U.S., and the

Larry
Jul 20, '07, 10:18 AM
Added Text

Larry
Jul 20, '07, 10:18 AM
Added Text

Larry
Jul 20, '07, 10:20 AM
Added: Space

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:21 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:21 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:25 AM
Added: Space

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:19 AM
Added Text

Larry
Jul 20, '07, 10:14 AM
Added: Paragraph Break

biodiesel tax incentive is an integral part of a sound public policy framework that will allow biodiesel to play a constructive role as part of the nation's overall energy strategy.

Biodiesel Reduces our Dependence on Foreign Oil: Biodiesel can play a major role in expanding domestic refining capacity and reducing our reliance on foreign oil. Increased use of renewables in the transportation sector can play a significant role in helping achieve the objective of displacing foreign petroleum with domestically produced renewable fuel. Merrill Lynch commodity strategist Francisco Blanch says that oil and gasoline prices would be about 15% higher if biofuel producers were not increasing their output.

The 500 million gallons of biodiesel produced in the U.S. in 2007 displaced 20 million barrels of petroleum, and increased production and use of biodiesel will further displace foreign oil. In addition, biodiesel is an extremely efficient fuel that creates 3.5 units of energy for every unit of energy that is required to produce the fuel.

Biodiesel is Good for the Environment: Biodiesel is an environmentally safe fuel, and is the most viable transportation fuel when measuring its carbon footprint, life cycle and energy balance. The USDA/DoE lifecycle study shows a 78% reduction in lifecycle CO2 emissions for B100. One billion gallons of biodiesel will reduce current life cycle greenhouse gas emissions by 16.12 billion pounds, the equivalent of removing 1.4 million passenger vehicles from U.S. roads. In 2007 alone, biodiesel's contribution to reducing greenhouse gas emissions was equal to removing 700,000 passenger vehicles from America's roadways.

Biodiesel's emissions significantly outperform petroleum-based diesel. Research conducted in the U.S. shows biodiesel emissions have decreased levels of all target polycyclic aromatic hydrocarbons (PAH) and nitrited PAH compounds, as compared to petroleum diesel exhaust. These compounds have been identified as potential cancer causing compounds.

Biodiesel is the only alternative fuel to voluntarily perform EPA Tier I and Tier II testing to quantify emission characteristics and health effects. That study found that B20 (20% biodiesel blended with 80% conventional diesel fuel) provided significant reductions in the total hydrocarbons, carbon monoxide, and total particulate matter. Typically, emissions of nitrogen oxides are either slightly reduced or slightly increased depending on the duty cycle of the engine and testing methods used. Research also documents the fact that the ozone forming potential of the hydrocarbon emissions of pure biodiesel is nearly 50% less than that of petroleum fuel. Pure biodiesel typically does not contain sulfur and therefore reduces sulfur dioxide exhaust from diesel engines to virtually zero.

Biodiesel helps preserve and protect natural resources. For every one unit of energy needed to produce biodiesel, 3.5 units of energy are gained. This is the highest energy balance of any fuel. Because of this high energy balance and the fact it is domestically produced, biodiesel use can greatly contribute to domestic energy security.

The Biodiesel Industry is Creating Green Jobs and Making a Positive Contribution to the Economy: In 2007 alone, the U.S. biodiesel industry contributed over $4.1 billion to the nation's Gross Domestic Product (GDP) and supported 21,803 jobs. In addition, economic modeling suggests that a vibrant biodiesel industry will positively impact the U.S. economy in multiple ways. America's biodiesel industry will add $26 billion to the U.S. economy between 2007 and 2012, assuming biodiesel growth reaches 1 billion gallons of annual production by 2012. Biodiesel production will create a projected 38,856 new jobs in all sectors of the economy and additional tax revenues from biodiesel production will more than pay for the federal tax incentives provided to the industry. Equally important, it will keep billions of dollars in America that would otherwise be spent on foreign oil.

H.R. 1424, the Emergency Economic Stabilization Act of 2008 (P.L. 110-343): In addition to extending the expiration date on the income tax credits and excise tax credits that comprise the biodiesel tax incentive through December 31, 2009, P.L. 110-343 also contained several important changes that enjoy the strong support of industry.

Feedstock Equalization: Under prior law, agri-biodiesel produced from virgin vegetable oils and animal fats qualified for a $1 per gallon tax incentive. Biodiesel produced from waste greases and second use oils qualified for a 50 cents per gallon incentive. P.L. 110-343 provides that all biodiesel, regardless of feedstock used to produce the fuel, is eligible for a $1 per gallon incentive. P.L. 110-343 contains the following language that is effective January 1, 2009:

> *(b) Increase in Rate of Credit-*
>
> *(1) INCOME TAX CREDIT- Paragraphs (1)(A) and (2)(A) of section 40A(b) are each amended by striking `50 cents' and inserting `$1.00'.*
>
> *(2) EXCISE TAX CREDIT- Paragraph (2) of section 6426(c) is amended to read as follows:*
>
> *`(2) APPLICABLE AMOUNT- For purposes of this subsection, the applicable amount is $1.00.'.*
>
> *(3) CONFORMING AMENDMENTS-*
>
> *(A) Subsection (b) of section 40A is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.*
>
> *(B) Paragraph (2) of section 40A(f) is amended to read as follows:*
>
> *`(2) EXCEPTION- Subsection (b)(4) shall not apply with respect to renewable diesel.'.*
>
> *(C) Paragraphs (2) and (3) of section 40A(e) are each amended by striking `subsection (b)(5)(C)' and inserting `subsection (b)(4)(C)'.*

(D) Clause (ii) of section 40A(d)(3)(C) is amended by striking `subsection (b)(5)(B)' and inserting `subsection (b)(4)(B)'.

BCOT asks that IRS implement the changes necessary to reflect the will of Congress in a timely manner. Specifically, all biodiesel, regardless of feedstock used to produce the fuel, should qualify for the $1 per gallon incentive on January 1, 2009.

Splash and Dash Prohibition: A "splash and dash" transaction occurs when biodiesel produced in a foreign country is sent to the U.S.; splash blended with diesel fuel to claim the U.S. biodiesel blenders excise tax credit; and then sent to a third country for final use as biodiesel or diesel fuel at any blend level. There is clearly no energy or tax policy justification for this sort of transaction and the NBB is fully supportive of efforts to close this unjustified and unforeseen tax loophole. _

P.L. 110-343 contains the following language that is designed to give IRS the statutory authority to stop so-called "splash and dash" transactions:

SEC. 203. CLARIFICATION THAT CREDITS FOR FUEL ARE DESIGNED TO PROVIDE AN INCENTIVE FOR UNITED STATES PRODUCTION.

(a) Alcohol Fuels Credit- Subsection (d) of section 40 is amended by adding at the end the following new paragraph:

`(7) LIMITATION TO ALCOHOL WITH CONNECTION TO THE UNITED STATES- No credit shall be determined under this section with respect to any alcohol which is produced outside the United States for use as a fuel outside the United States. For purposes of this paragraph, the term `United States' includes any possession of the United States.'.

(b) Biodiesel Fuels Credit- Subsection (d) of section 40A is amended by adding at the end the following new paragraph:

`(5) LIMITATION TO BIODIESEL WITH CONNECTION TO THE UNITED STATES- No credit shall be determined under this section with respect to any biodiesel which is produced outside the United States for use as a fuel outside the United States. For purposes of this paragraph, the term `United States' includes any possession of the United States.'.

(c) Excise Tax Credit-

(1) IN GENERAL- Section 6426 is amended by adding at the end the following new subsection:

`(i) Limitation to Fuels With Connection to the United States-

`(1) ALCOHOL- No credit shall be determined under this section with respect to any alcohol which is produced outside the United States for use as a fuel outside the United States.

`(2) BIODIESEL AND ALTERNATIVE FUELS- No credit shall be determined under this section with respect to any biodiesel or alternative fuel which is produced outside the United States for use as a fuel outside the United States.

For purposes of this subsection, the term `United States' includes any possession of the United States.'.

(2) CONFORMING AMENDMENT- Subsection (e) of section 6427 is amended by redesignating paragraph (5) as paragraph (6) and by inserting after paragraph (4) the following new paragraph:

`(5) LIMITATION TO FUELS WITH CONNECTION TO THE UNITED STATES- No amount shall be payable under paragraph (1) or (2) with respect to any mixture or alternative fuel if credit is not allowed with respect to such mixture or alternative fuel by reason of section 6426(i).'.

(d) Effective Date- The amendments made by this section shall apply to claims for credit or payment made on or after May 15, 2008.

Splash and dash transactions lack economic substance and run counter to the underlying purpose of the biodiesel tax incentive, thereby undermining public confidence in the incentive. Accordingly, industry asks IRS to use the authority it has been granted by Congress to aggressively deny the biodiesel blenders excise tax credit to fuel produced outside the U.S. for use as a fuel outside the U.S. In addition, industry asks IRS to enforce this provision consistent with the statutory effective date, which is May 15, 2008.

Co-Processed Renewable Diesel: P.L. 110-343 contains the following language to clarify the definition of renewable diesel as it applies to the $1 per gallon renewable diesel excise tax credit:

(d) Coproduction of Renewable Diesel With Petroleum Feedstock-

(1) IN GENERAL- Paragraph (3) of section 40A(f) is amended by adding at the end the following new sentences: `Such term does not include any fuel derived from coprocessing biomass with a feedstock which is not biomass. For purposes of this paragraph, the term `biomass' has the meaning given such term by section 45K(c)(3).'.

(2) CONFORMING AMENDMENT- Paragraph (3) of section 40A(f) is amended by striking `(as defined in section 45K(c)(3))'.

The statutory language of P.L. 110-343 establishes the following effective date for this provision:

(2) COPRODUCTION OF RENEWABLE DIESEL WITH PETROLEUM FEEDSTOCK- The amendment made by subsection (d) shall apply to fuel produced, and sold or used, after the date of the enactment of this Act.

The IRS has previously issued guidance (IRS Notice 2007-37) that had the effect of permitting co-processed renewable diesel to claim the renewable diesel tax incentive. As the effective date of the provision described above is October 3, 2008, the date of enactment for P.L 110-343, the U.S. biodiesel industry asks IRS to in a timely manner revise this guidance so that it is consistent with current statute.

Definition of Agri-Biodiesel: P.L. 110-343 added camelina to the illustrative list of biodiesel feedstocks that qualify as agri-biodiesel. In addition to this statutory change, industry requests IRS to clarify that algae qualifies as an agri-biodiesel feedstock.

Modifications to the ASTM D6751 Fuel Specification: Section 40A(d)(1) of the Internal Revenue Code establishes the requirements for fuel to qualify for the income tax credits and excise tax credits that comprise the biodiesel tax incentive. Specifically, biodiesel must meet the registration requirements for fuels and fuel additives established by the Environmental Protection Agency (EPA) under section 211 of the Clean Air Act (42 U.S.C. 7545) and the requirements of the American Society of Testing and Materials ASTM D6751.

The EPA's final rule implementing the Renewable Fuels Standard, (40 CFR Part 80, Regulation of Fuels and Fuel Additives: Renewable Fuel Standard Program), published on May 1, 2007, defines biodiesel as:

> *Under today's rule, the term "biodiesel (mono-alkyl esters)" means a motor vehicle fuel which: (1)Meets the registration requirements for fuels and fuel additives established by the Environmental Protection Agency under section 7545 of this title (Clean Air Act Section 211); (2)is a mono-alkyl ester; (3)meets ASTM specification D-6751-07; (4) is intended for use in engines that are designed to run on conventional, petroleum derived diesel fuel, and (5) is derived from nonpetroleum renewable resources.*

Further, a footnote in 40 CFR Part 80 also notes:

> *In the event that the ASTM specification D6751 is succeeded with an updated specification in the future, EPA may revise the regulations accordingly at such time. Regulations cannot be promulgated that only reference "the most recent version" of an ASTM standard, since doing so would place the American Society for Testing and Materials in the position of a regulatory body.*

Currently, neither IRS regulations nor the Internal Revenue Code specify which version of ASTM D6751 is applicable to biodiesel for purposes of claiming the biodiesel tax incentive. However, 40 CFR Part 80, the EPA's RFS final rule does clarify that ASTM D6751-07 is the specification applicable to biodiesel. In addition, these same rules note that to avoid putting ASTM in the position of a regulatory body, that subsequent EPA rulemaking would be required to update the ASTM D6751 specification that defines biodiesel.

On October 13, 2008, ASTM published an update to the ASTM D6751 (ASTM D6751-08) fuel specification for biodiesel. For biodiesel producers and marketers who are not ASTM members, the official publication of this new specification was the first time the public had access to the changes in the ASTM D6751 specification.

For purposes of consistency with EPA, the IRS should proceed with a rulemaking process before changing the version of the ASTM D6751 fuel specification applicable to the biodiesel tax incentive. This avoids putting ASTM in the position of a regulatory body. It also provides the public and other industry participants who are not ASTM members adequate time to adopt and comply with a change in the D6751 fuel specification. This approach is consistent with the existing statute and falls within the IRS' regulatory discretion.

Biodiesel Mixtures and Liability for Tax: Under existing regulations, for purposes of the 24.3 cents per gallon diesel fuel excise tax, diesel fuel does not include "excluded liquids." Among other things, liquids with less than 4% paraffin content are considered an excluded liquid. Existing IRS regulations allow B99.9 biodiesel blends and other blends to qualify for the biodiesel blenders excise tax credit, even if the blend is an excluded liquid not subject to the federal diesel fuel excise tax. B99.9 blends do not have a 4% paraffin content, and thus, are not currently subject to the diesel fuel excise tax. However, Section 4041 of the IRC provides a backup tax that subjects fuel used in a diesel powered highway vehicle to the diesel fuel excise tax regardless of the fuel's paraffin content.

The Proposed Regulations would revise the definition of "excluded liquid" so that all biodiesel mixtures containing at least 0.1% diesel fuel will be classified as diesel fuel for tax purposes. Thus, under the Proposed Regulations, in a situation where B99.9 is produced by a biodiesel producer outside the bulk transfer/terminal system, the tax would be imposed on the sale or removal of the mixture by the mixture producer, and the mixture producer (for example, the biodiesel producer) would be liable for the tax, and that tax would be offset against any excise tax credits generated upon the sale or removal of the blended fuel. It is the industry's understanding that if the sale of a mixture is for tax-exempt purposes, the biodiesel producer could comply with the dyeing requirements for non-taxable diesel fuel and sell the dyed biodiesel free of tax.

Impact on Biodiesel Producers: BCOT respectfully suggests that the proposed changes would create an unnecessary hardship on the biodiesel industry. The current system seems to include the necessary authority, mechanisms, and provisions to ensure that biodiesel is taxed appropriately. As an industry, we are committed to seeing tax applied in an appropriate fashion. From BCOT's perpective, the proposed rule changes seem to entail significant capital outlays and reporting requirements which would severely hamper the growth of the industry.

At present biodiesel is often sold as a 99.9 biodiesel blend to marketers/customers of the product at a point below the rack. At the time of the sale, the ultimate use of the product has not been

determined. Therefore, it is the marketer's/customer's responsibility to determine the end-use and apply the appropriate tax. If a producer, legitimately selling product below the rack, is forced to pay the excise tax on product that is ultimately determined to be an "excluded liquid" and then claim a rebate- or worse- force a customer to file the rebate, the producer and the ultimate taxpayer will have significant working capital increases for what amounts to an involuntary loan to the U.S. Government until such time as the refund can be processed. Given the thin margins and already large working capital requirements of the industry, this would have a devastating affect. It seems inappropriate to force producers/customers to pay a tax and then request a refund for taxes they are, ultimately, not required to pay. It seems far more appropriate to have the party selling the product for its ultimate end-use, determine and apply the appropriate taxes. IRS already has the authority to enforce this transaction flow and it seems a much more appropriate course of action.

BCOT does not feel it is appropriate for biodiesel producers to be forced to install mechanical dyeing systems. First, it would involve a significant, unnecessary cash outlay for producers to comply with in a system in which dye injection systems are already in place to meet IRS's needs. The industry is not in a position to absorb these costs. Second, producers often do not know the final use of the product they sell as the final use gets determined at a later date. Dyeing in advance of the time product reaches its final commercial designation will retard appropriate and legitimate sales. If a producer of biodiesel decides to dye their product it arbitrarily limits the end-use of the product as there is no way to un-dye the product. Customers will, therefore be less likely to buy the product. Also, as there is also no infrastructure in place to handle dyed biodiesel, it creates yet another market impediment.

Impact in the Marketplace: Disqualifying biodiesel B99.9 blends from the definition of excluded liquid will also have an impact in the marketplace. A significant amount of biodiesel sales currently occur "below the rack," or outside of the existing bulk transfer/terminal system. Allowing a biodiesel producer to register as a biodiesel blender and claim the blenders excise tax credit on a B99.9 blend achieves the policy goal of making biodiesel price competitive with petroleum diesel. From a marketing perspective, this regime allows the customer – in most cases a fuel marketer – to benefit indirectly from the tax incentive in the form of reduced fuel cost without having to deal with the regulatory obligations associated with being an IRS registered blender.

The treatment of B99.9 as an excluded liquid provides both biodiesel producers and marketers with needed flexibility in below the rack transactions. In the vast majority of instances, B99.9 biodiesel blends are further blended to B5 through B20 levels for final use in the marketplace. When a fuel marketer purchases a B99.9 blend from biodiesel producer, it is often unknown at the time of sale whether the biodiesel will ultimately be used in a taxable or a tax-exempt application. Thus, under current law, fuel is ultimately taxed or dyed downstream from a biodiesel plant when the fuel's ultimate end use is determined. It is currently the IRS'

responsibility to ensure that diesel fuel excise taxes are being collected on biodiesel blends that no longer meet the definition of an excluded liquid under IRS regulations.

In a situation where taxed B99.9 is subject to the 24.3 cents per gallon diesel fuel excise tax and the B99.9 is used for a tax-exempt use, a refund of the excise tax could only be claimed by the end user of the fuel. This could have the unintended tax consequence of artificially inflating the market price charged to consumers for cleaner-burning, renewable biodiesel compared to petroleum based products. Further, end users would be compelled to claim an excise tax refund to claim a refund on the 24.3 cents per gallon excise tax assessed on the fuel, again placing an additional regulatory burden on a consumer that opted for a renewable fuel as opposed to petroleum based product. For example, in a situation where taxed biodiesel was ultimately used for a home heating oil application, the homeowner who ultimately used the fuel would be the only entity eligible to claim the diesel fuel excise tax refund – a scenario that is likely to deter consumers from using biodiesel.

Impact on Fuel Distribution and Terminals: Subjecting B99.9 blends to the diesel fuel excise tax could also further complicate the taxation and distribution of biodiesel in fuel terminals. For example, under the Proposed Regulation, a B99.9 blend sold by a biodiesel producer to a position holder in an IRS registered terminal would be subject to the 24.3 cents per gallon diesel fuel excise tax. When the B99.9 fuel is further blended to a B5 through B20 level and breaks bulks at the terminal in a taxable sale, the biodiesel component of the blend would again be subject to the diesel fuel excise tax. Though there is an existing regime that would allow for the refunds, this system is not timely and is difficult for taxpayers to navigate. As a result, this change would again have the unintended consequence of artificially inflating the price of biodiesel in the marketplace on account of the fuel being subject to double taxation and could cause cash flow issues for fuel marketers and terminal operators who sell and promote biodiesel in the marketplace. As with biodiesel producers, terminal operators who handle both B100 and B99.9 biodiesel blends also would be forced to expend capital to purchase additional storage tanks and other infrastructure to handle biodiesel, again serving as a deterrent to the expanded use and sale of biodiesel through the nation's fuels terminals.

Collection of Excise Tax on Taxable Biodiesel Blends: Under current law and existing IRS regulations, biodiesel blends are subject to the diesel fuel excise tax at the point they no longer qualify as an excluded liquid. IRS already has the authority to enforce current law and collect excise tax on blends that do not meet the definition of an excluded liquid absent the change in the Proposed Regulations pertaining to B99.9 blends.

In October, 2007, a joint biodiesel industry-IRS work group (work group) held the first of several meetings to discuss administration of the biodiesel tax incentive. The work group's discussions have thus far focused on the formulation and administration of ExStars reporting requirements for biodiesel producers.

However, during the course of the task force's discussions, IRS signaled their intention to formulate and implement a system to track below the rack sales of biodiesel to the point where excise tax was paid or the fuel was dyed and entered into the tax exempt market. This tracking system would be separate and distinct from the existing regime employed by the EPA to track fuel under the RFS, and would be an additional reporting requirement implemented under the existing ExStars program. This tracking system would also be a separate reporting regime from those being considered to track biodiesel production. The concept entailed the assignment of a tracking number similar to a Renewable Identification Number (RIN) under the RFS program to every batch of biodiesel, with the imposition of ExStars reporting requirements on each party that handled the fuel in the distribution stream. This broad concept was discussed publicly in February, 2008 by IRS officials at the National Biodiesel Conference and Expo in Orlando, Florida.

The incorporation of this additional type of below the rack biodiesel tracking system in the ExStars program would impose new regulatory and potentially significant financial burdens on biodiesel producers and fuel marketers. This would discourage fuel marketers and distributors from handling biodiesel and curtail vital below the rack biodiesel sales.

Again, it is important to note that IRS has ample authority under current law to enforce existing excise tax rules as they apply to biodiesel blends that do not qualify as an excluded liquid. Both subjecting B99.9 biodiesel blends and a below the rack fuel tracking and reporting regime under ExStars will have a significant impact on the biodiesel industry. However, the change in the Proposed Regulation that would subject B99.9 blends to the diesel fuel excise tax without regard to the fuel's paraffin content would be less onerous than a below the rack fuel tracking and reporting regime under the ExStars system. In addition, from an equity standpoint, the IRS should apply similar rules to other fuels and fuel blends that qualify for the renewable diesel tax incentive and the alternative fuels tax incentive. Lastly, as with petroleum diesel fuel, biodiesel producers who export B99.9 blends with appropriate documentation should not be forced to remit the federal diesel fuel excise tax.

Again, BCOT appreciates the opportunity to comment on the IRS' Proposed Regulation pertaining to *Alcohol Fuel and Biodiesel; Renewable Diesel; Alternative Fuel; Diesel-Water Fuel Emulsion; Taxable Fuel Definitions; Excise Tax Returns (REG-155087-05)*. If you have additional questions or would like to further discuss this or any other matter, please do not hesitate to contact me.

Thank you in advance for your consideration of BCOTs views on these important issues.

Sincerely,

Jeff Trucksess
Vice President of Regulatory Affairs
Biodiesel Coalition of Texas