

biodiesel production on soybean oil prices instead of on a raw soybean basis. A large majority, 1,635 respondents, wanted the program to increase rather than decrease payments; 296 opposed lowering the payment; 60 supported the proposed change; one stated payments should not be changed until after FY 2003; one supported higher overall payments for all biodiesel payments; and one suggested equal payment for all commodities based on soy oil. Related to the soybean payment issue, 197 respondents wanted increased program payments on animal fats and oils. The majority of respondents opposed proposed changes that revised biodiesel payment calculations, resulting in lower subsidy payments. Many respondents argued that the reduced biodiesel payments would not provide sufficient support to ensure biodiesel's affordability and maintain industry

growth. Some also argued that CCC's Bioenergy Program was the primary federal program providing support to the biodiesel industry and was largely responsible for biodiesel becoming one of the fastest growing alternative energy sources. A number of respondents argued that changes in the proposed rule contradicted the intent of Congress and the stated goal of increasing bioenergy production.

CCC agrees with many of the respondents' comments on several factors: Program biodiesel payments should be increased not reduced; payments on production from animal fats and oils should be increased; and all biodiesel payments should be based on the FY 2002 soybean payment formula. Therefore, in the final rule, 7 CFR 1424.3 has been adjusted. Also, the proposed language in 7 CFR 1424.8(e) related to gross payable units has been

moved to 7 CFR 1424.7. CCC will base all biodiesel payments on a soybean conversion and price, adjusted further by comparing the applicable oil or grease (animal fats and oils) price to the soy oil price. These changes will provide additional support to the biodiesel industry, maintain former payment levels for production from soybeans, and raise payments on production from animal fats and oils. This will reduce disparities between commodities in program payments for biodiesel production. The following table demonstrates how biodiesel payments will be determined taking into account the size-adjustment factor for large and small plants (which is statutory) and accounting for differences in feedstock to produce the eligible biodiesel.

Example:

Item	Soybeans	Animal fats and oils	Mustard seed
Gross Payable Units (Bushels) .....	714.30	.....	.....
Size Factor (2.5 if under 65 million gallons per year total capacity or 3.5) .....	2.50	.....	.....
Adjusted Bushels (Gross Bushels/Size Factor) .....	285.7	.....	.....
Soybean PCP, Macon County, Illinois <sup>1</sup> .....	\$5.59	.....	.....
Soybean Gross Payment (Soybean PCP × Adjusted Bushels) .....	\$1,597	\$1,597	\$1,597
Soy Oil Price, Cents per pound <sup>1</sup> .....	.....	22.59	22.59
Feedstock Price, Cents per pound <sup>1</sup> .....	.....	10.00	12.30
Feedstock Factor (Feedstock Price/Soy Oil Price) .....	.....	0.44	0.54
Gross Program Payment (Soybean Gross Payment × Feedstock Factor) .....	\$1,597	\$707	\$869

<sup>1</sup> Price on November 1, 2002.

No change is being made to the proposed rule's ethanol provisions in this area because there does not appear to be a similar need for adjustment.

#### Volume Basis for Payments

Forty-six respondents suggested program payments be made on all biodiesel production—base production (the previous FY volume) plus increased production this FY. One respondent suggested a two-tier payment with different payment rates used for base and increased biodiesel production, and another suggested a higher payment specifically for biodiesel. Respondents indicated that the biodiesel industry needs higher levels of support to maintain or increase industry growth.

CCC agrees with respondents that the biodiesel industry needs additional program support through higher payments. Consistent with the previous program, the 2002 Act requires the Secretary to make payments on the quantity of bioenergy produced during an FY that exceeds the quantity of bioenergy produced in the prior FY to date. Payment on increased production within a given FY may not provide sufficient incentives for long-term

investments in the biodiesel industry. Currently, biodiesel is not cost-competitive with conventional diesel. The payment on FY to FY increases therefore implicitly subsidizes base production of biodiesel, making it cost-competitive. As a result, each successive FY that a producer participates in the program, the level of implicit support for biodiesel production declines as the base production grows larger relative to the yearly increase in production. Furthermore, this may create a potential inequity in the market as newer producers may receive implicitly higher subsidies and, as a result, be more cost-competitive than established producers. This suggests that previous provisions carried forward by reference, arguably, in the new legislation may, if continued without amendment, promote instability, which would impede the goal of fostering growth in the industry. This situation does not apply to the ethanol industry with its more mature market and other Federal and State support programs. In addition, basing a payment only on increased year-to-year biodiesel production may encourage participants to frustrate the goals of the

program by increasing production one year, dropping it the next, then increasing it the following year in order to qualify for higher program payments. To avoid that result, CCC will use its original and continuing authority under section 5 of the CCC Charter Act, 15 U.S.C. 714c, as needed, and the program funding provided by the 2002 Act to make biodiesel production eligible for the program that would not be eligible solely under the bioenergy provisions of the 2002 Act by allowing payments on all of a producer's production and not just the increase in one year as compared with the preceding year. This support will be reduced each FY of the program to encourage industry independence from program payments. In no event will program funding exceed the \$150 million per FY funding provided by the 2002 Act. Accordingly, among other changes, 7 CFR 1424.7 as added in the final rule provides that biodiesel may receive payments in the normal manner on production eligible under the 2002 Act (year-to-year increases) plus a payment on the remaining production at 50 percent of that rate in FY 2003, 30 percent in FY