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VIA ELECTRONIC AND U.S. MAIL

The Honorable Scott Pruitt
Administrator
U.S. Environmental Protection Agency
1200 Pennsylvania Avenue, N.W., 1101A
Washington, DC 20460

The Honorable William Wehrum
Assistant Administrator
Office of Air and Radiation
U.S. Environmental Protection Agency
1200 Pennsylvania Avenue, N.W., 1101A
Washington, DC 20460

Re: Small Refinery Hardship Under the Renewable Fuel Standard (“RFS”)

Dear Administrator Pruitt and Assistant Administrator Wehrum:

I am writing on behalf of the Small Refiners Coalition (“Coalition”) regarding the Renewable Fuels Association’s (“RFA”) January 24, 2018¹ and API’s February 12, 2018² letters concerning small refinery hardship under the RFS.

The Department of Energy, in a 2011 report for Congress, performed a detailed analysis of how the RFS program would evolve over time and cause harm to small refineries.³ As explained in the DOE study, small refinery hardship is caused by the increasing renewable fuel volume mandates (blendwall), the resulting increase in the price of RINs, and the inability of small refineries to position themselves to avoid the harm due to their lack of vertical integration, lack of market power, and capital constraints. Therefore, small refinery harm was expected to

¹ Letter from Renewable Fuels Association to Scott Pruitt, Administrator, U.S. EPA (Jan. 24, 2018) (<http://www.ethanolrfa.org/wp-content/uploads/2018/01/EPAsmallrefinerletterjanuary24-1.pdf>).

² Letter from American Petroleum Institute to William Wehrum, Assistant Administrator, U.S. EPA (Feb. 12, 2018) (<http://www.api.org/~media/Files/News/Letters-Comments/2017/API-Letter-2-12-18.pdf>).

³ U.S. Department of Energy, Small Refinery Exemption Study: An Investigation Into Disproportionate Economic Hardship (2011)(“DOE study”)(<https://www.epa.gov/sites/production/files/2016-12/documents/small-refinery-exempt-study.pdf>).

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grow worse over time, not diminish, as the volume mandates increased. As explained in the study:

The response to the RFS2 requirements depends in large measure on the size and scope of the operations of individual companies. Large integrated refiners can more easily obtain financing for blending facilities, generate options, accommodate their needs efficiently and shift emphasis from one sector to another as opportunities indicate. For example, over the past couple of years, compliance strategies for larger companies included engaging in joint ventures with ethanol producers, investing in companies in the renewable sector, or conducting research on renewable fuels. As a result, RFS2 compliance costs for the larger refiner may be a small part of overall operating costs.

Small companies are more limited in their options. They face a number of challenges and access to capital is generally limited or not available. Even when capital is available, they may have to choose between making substantial investments in blending and investing in other needed facilities to improve operating efficiencies to remain competitive.⁴

As predicted in the DOE Study, large integrated refiners have positioned themselves to respond to the increasing volume mandates by entering into joint ventures with biofuels producers and through their control of blending and retail. Fifty percent of retail outlets sell fuel under the brand of one of the 15 largest refiner-suppliers through supply agreements.⁵ These entities secure RINs because of the large amount of blending and retail they control. While RFA and API contend that small refineries “have had ample time to adjust their businesses to operate under the burden of the RFS,” small refineries would have to enter new business areas in other geographic areas to displace established, well-funded, long time market players from the wholesale and retail markets they control. This is not easily, cheaply or quickly accomplished and requires changing how these businesses operate.

More fundamentally, small refiners were never expected to make capital investments to avoid the harm caused by high-priced RINs. As EPA explained in the 2007 rulemaking, “obligated parties [would] be able to fulfill their renewable fuel obligation without having to make capital investments” and “sufficient RINs [would] be available and at reasonable prices.”⁶ These were the assumptions that were the foundation for EPA’s SBREFA analysis and EPA’s conclusion that small refineries would not be harmed.⁷ But the RIN market has not operated as

⁴ DOE Study at 23.

⁵ http://www.convenience.org/YourBusiness/FuelsReports/GasPrices_2013/Pages/WhoSellsGas.aspx

⁶ Regulation of Fuels and Fuel Additives: Renewable Fuel Standard Program, 72 Fed. Reg. 23900, 23926 (May 1, 2007).

⁷ “We have concluded that the final RFS rule will not have a significant impact on a substantial number of small entities. We based this conclusion on several criteria. First, the industry is expected to be overcomplying by a wide

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EPA intended. RIN prices have increased by 4-5000%, exempt distributor/retailer chains have retained windfall RIN revenues rather than investing in renewable fuel blending, retailers are “fuel agnostic” and unmotivated to sell higher ethanol blends,⁸ the RIN market has experienced unprecedented fraud, and distributor/retailers are lining their pockets instead of passing along RIN value to encourage E15/E85 use.⁹ Therefore, the market conditions are much worse than DOE expected when it concluded that small refineries could be significantly harmed.

Although they were not expected to do so, most small refineries have made investments to blend renewable fuel, but their investments have been displaced by exempt distributor/retailers. With the increase in the price of RINs since 2013, large distributor/retailers have made investments in blending in close proximity to small refinery racks, and then refused to buy blended fuel. The small refineries lost both their investments in rack blending and the RINs they had been generating for compliance. These examples are described in small refinery hardship petitions submitted to EPA. In addition, a now common practice in the industry is the capture of RIN value by large distributor/retailer chains by requiring discounts on the wholesale price of transportation fuel tied to the value of the RIN on the date of the sale. In requests for proposal and contracts with distributor/retailers provided to EPA through the hardship petition process, small refineries have demonstrated that even when they are able to make investments in renewable fuel blending, they cannot retain the RIN or the value of the RIN to reduce their RFS burden because of their lack of vertical integration (retail) and lack of market power.

API, citing an EPA study,¹⁰ contends that small refineries are not harmed by high RIN prices because large and small refineries are largely able to pass through their RIN costs. But the EPA study cited by API did not look at small refineries; it looked only at “merchant refineries.” As the DOE study explained, “the degree to which the costs burdening small refineries will be passed through to the market depends on many factors, including the market power and relative cost level of a small refinery relative to other market participants.”¹¹ Therefore, the ability of a small refinery to pass through its RIN costs will depend on the unique facts of the small refinery, its cost level and its market power. These factors are properly assessed through the small refinery hardship petition process.

margin independent of the standard, thus causing compliance costs to be minimal.” Regulatory Impact Analysis: Renewable Fuel Standard Program, page 336-337, April 2007.

⁸ Letter from David Masuret, Senior Vice President of Petroleum Supply and Operations, and Matthew Durand, Manager of Government Affairs and Public Policy, Office of the General Counsel, Cumberland Farms, to Gina McCarthy, Administrator, U.S. Environmental Protection Agency 9 (Nov. 2, 2016) (available at EPA-HQ-OAR-2016-0544-0055).

⁹ Renewable Fuel Standard Program: Standards for 2014, 2015, and 2016 and Biomass-Based Diesel Volume for 2017, 80 Fed. Reg. 77420, 77482-83 (Dec. 14, 2015).

¹⁰ “A Preliminary Assessment of RIN Market Dynamics, RIN Prices, and Their Effect,” Dallas Burkholder, Office of Transportation and Air Quality, US EPA. May 14, 2015.

¹¹ DOE Study at 22-23.

But EPA's study on RIN cost pass-through suffers from other infirmities. The study failed to explain how a merchant refiner can recover its RIN cost when competing at the rack with "a blender that does not have an RVO, i.e., a gasoline marketer, or . . . a refiner who blends in excess of its RVO."¹² In contrast to EPA's conclusion, DOE concluded that, after consideration of the ethanol margin and tax credits, the refiner that blends in excess of its RVO and the gasoline marketer would have a significant cost advantage over the merchant refiner at the rack.¹³ Unlike DOE's study, EPA's study failed to explain how, in the intensely competitive transportation fuel market, a merchant refiner could pass through its higher RIN cost when its rack competition has little or no RIN cost to pass through, any more than a refiner would have the ability to pass through higher labor or utility costs. Either the merchant refiner does not recover all of its RIN costs or the gasoline marketer and RIN-long refiner are recovering a cost they did not incur, either of which hurts the competitive position of the merchant refinery.

RFA and API express concerns that increasing the number and magnitude of small refinery hardship exemptions could destabilize the program or cause RIN market disruptions, but their worries are misplaced. First, as API acknowledges, its members have, through capital investments, taken steps to reduce their RFS burden. Therefore, small refineries owned by large integrated refiners are unlikely to apply for relief or receive it based on the findings in the DOE study. Small refineries not owned by large integrated companies produce less than 7.4% of the national transportation fuel volume and, to address RFA's particular concern, small refineries disproportionately produce diesel fuel, not gasoline. In fairness, EPA could address RFA's and API's concern, in part, by timely deciding hardship petitions. If hardship petitions were decided 90 days after submission, the exemptions would occur throughout the year and not all at once on the eve of the compliance deadline.

RFA also expresses concerns about a lack of transparency in the hardship petition process. However, the standard applied to small refinery hardship petitioners is already public. It is described in detail in the DOE study. The 10th Circuit Court of Appeals reminded EPA that hardship relief does not require a demonstration that compliance with the RFS will cause an existential threat to the small refinery, and that the hardship standard is intended to measure the disproportionate regulatory burden and not whether the refinery can absorb the disproportionate regulatory burden and remain profitable.¹⁴ The Coalition does not oppose EPA releasing the aggregated volume of exempted fuel, but does not support releasing the identity of refineries applying for or receiving hardship relief.

¹² DOE Study at B-5.

¹³ *Id.*

¹⁴ *Sinclair Refining Co. v. U.S. Environmental Protection Agency*, No. 16-9532 (10th Cir. Aug. 15, 2017) (available at <https://www.ca10.uscourts.gov/opinions/16/16-9532.pdf>).

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RFA is an aggressive advocate for the ethanol industry. It opposes lowering the nationwide volume mandates, opposes state waiver petitions, opposes granting relief to Philadelphia Energy Solutions in the pending bankruptcy proceeding, opposes moving the point of obligation downstream to those that control the blending, and now opposes small refinery hardship relief. EPA should be circumspect when weighing RFA's interests against the interests of all other stakeholders. The program is not working as Congress or EPA intended, and causing additional harm to small refineries in an effort to force more ethanol into the market is not the solution.

The Coalition supports RFS reform that would put small refineries back on a level playing field with the API members. EPA, RFA, API, the small refineries, and other interested parties should be working together to reform the RFS to achieve the goals of the program without causing harm to critical energy infrastructure and important American jobs. Until then, EPA should grant hardship relief to small refineries as Congress intended for all of the reasons described in the DOE Study.

Very truly yours,



LeAnn Johnson Koch

cc (via electronic mail only): Mandy Gunasekara, EPA
Members of the Coalition¹⁵

¹⁵ Alon Refining Krotz Springs, Inc.; American Refining Group, Inc.; Calumet Specialty Products Partners, L.P.; Lion Oil Company; Ergon Refining, Inc.; Ergon-West Virginia, Inc.; Hunt Refining Company; Placid Refining Company LLC; U.S. Oil & Refining Co.; Par Hawaii Refining, LLC and Wyoming Refining Company.