WHAT THEY ARE SAYING

THE POINT OF OBLIGATION

Whitepaper
AMERICAN PETROLEUM INSTITUTE

EPA received formal petitions to change the Renewable Fuel Standard (RFS) program by moving the "point of obligation" downstream of the refinery gate and from port of entry.

The change would no longer require that refiners and importers be responsible for meeting the biofuel mandate and shift the compliance responsibility to companies that own gasoline and diesel at regional distribution terminals. Various stakeholders submitted comments, and, collectively, these have indicated that a broad and diverse group of interests oppose the change. EPA should expeditiously issue a final decision to deny the petitions and remove the ongoing uncertainty in the marketplace.

ON THE ISSUE

The American Petroleum Institute (API) is the only national trade association that represents all aspects of America's oil and natural gas industry. Our more than 625 corporate members - from the large major oil and gas companies to the small independents - come from all segments of the industry. They are producers, refiners, suppliers, marketers, pipeline operators and marine transporters as well as service and supply companies. API members that refine or import gasoline or diesel fuel are obligated to comply with the RFS, and they provide a unique perspective to the debate as many of these members would continue to be "obligated parties" if the point of obligation were moved.

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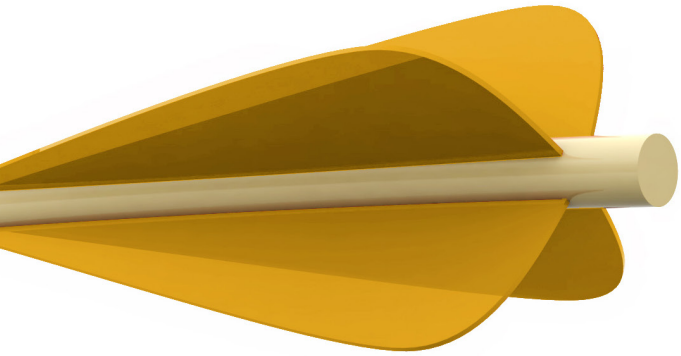
THE POINT OF OBLIGATION

Congress established the Renewable Fuel Standard (RFS) program in 2005 and revised the program in 2007, requiring that ethanol and other biofuels be blended into our domestic transportation fuel supply. Congress instructed the Environmental Protection Agency (EPA) to set RFS standards annually that are **"applicable to refineries, blenders, distributors, and importers, as appropriate, to ensure that the requirements [of the RFS] are met."**



EPA promulgated rules that defined refiners and importers of gasoline and diesel as the "obligated parties" responsible for demonstrating compliance with the standards. EPA set other requirements for renewable fuel producers and importers and other parties in the fuel distribution system to ensure the program would work. Renewable fuel producers generate credits corresponding to the biofuel produced and are required to pass these credits, known as "RINs," along with the biofuel, through the distribution system. Obligated parties acquire RINs from blending biofuels or by purchasing them from other parties that blend biofuels. Then, the obligated parties submit an appropriate amount of RINs to EPA that corresponds to the volume of gasoline and diesel that the company provided to the domestic market.

CHANGING THE POINT OF OBLIGATION WILL CREATE ADDITIONAL UNCERTAINTY IN THE RFS PROGRAM AND THE RIN MARKET THAT COULD INCREASE RETAIL FUEL COSTS:

Changing the point of RFS obligation would create additional uncertainty in the RFS program and in the RIN market and, as suggested in comments submitted to the EPA, could result in increased retail fuel costs. RFS compliance plans, investments and commercial agreements that were premised on the current structure would be disrupted. Others have highlighted that such a major structural change a decade into the program creates additional uncertainty about other critical components of the program.

"[Changing the point of obligation] would inject such massive disruption and uncertainty into fuels markets that retail fuel prices will inevitably skyrocket and the incentive for fuel marketers to integrate renewable fuels into their product lines will dissipate."

David H. Fialkov, NATSO Representing America's Travel Plazas and Truckstops

"Changing the point of obligation would inject massive disruption into fuel and renewable fuel markets, undercut investment-backed expectations, and raise prices for consumers all to help a narrow constituency of merchant refiners and a small portion of their branded retailers."

Dawn M. Carlson, President and CEO, Petroleum Marketers and Convenience Stores of Iowa (PMCI)

"Parties involved with fuel production, distribution, and sales have had over a decade to plan for compliance with increasing RFS requirements. Many entities, such as certain independent fuel retailers, have made significant business decisions based on the RFS as currently structured. Independent retailers have assembled complex supply chains involving commercial arrangements above the rack, at blending terminals, and downstream. A change in the point of obligation would threaten to undercut these complex relationships"

Emily Skor, CEO, Growth Energy

"Changing the point of obligation would eliminate supply options ahead of and at the rack, which will lead to an increase in rack (and below the rack) prices."

Kathryn D. Krimayer, Senior VP, Law and General Counsel, Association of American Railroads

Commenters have noted that changing the point of obligation is likely to result in the unintended consequence of reducing competition at the wholesale level, as companies currently engaged in the bulk market focus on their core business rather than creating the necessary mechanisms involved in RFS compliance.

"If the RFS obligation were shifted downstream, it would force UPS to re-examine its above-the rack purchases, which we began long before the RFS began"... "For us, the RFS program would move from an effective incentive to purchase renewable fuels voluntarily to a disincentive to our purchase of fuels above the rack."

Michael Kiely, Managing Director, SVP U.S. Government Affairs, UPS

"ABFA believes the increased cost to these companies would ultimately lead to less competition at the rack. We saw this very phenomenon occur in California when the state placed the responsibility for compliance with its Low Carbon Fuel Standard (LCFS) at the rack rather than with the obligated parties. The state saw a number of companies leave the rack, resulting in less competition and a significant rise in cost to all customers of these fuels."

Michael J. McAdams, President Advanced Biofuels Association

"Moving the point of obligation downstream to "position holders" at the terminal rack would inevitably result in a decrease in the number of position holders – these parties would be incentivized to refrain from acquiring fuel "above the rack" in order to avoid RFS obligations."

Glen P. Kedzie, Vice President, Energy & Environmental Counsel, American Trucking Associations

CHANGING THE RFS POINT OF OBLIGATION DOES NOT IMPACT THE OVERALL VOLUME OF RENEWABLE FUELS IN THE MARKET

The blend wall is a constraint based on fuel incompatibilities with vehicle and retail infrastructure and a lack of consumer demand for higher ethanol blends like E15 and E85. EPA has recognized the blendwall and used its waiver authorities to reduce annual RFS standards.

"These realities – which EPA has articulated in justifying its exercise of its waiver authority – would continue to exist if the point of obligation changed. The only difference is that their effect would be exacerbated."

David H. Fialkov, NATSO Representing America's Travel Plazas and Truckstops

Petitioners seeking to change the RFS point of obligation claim that, because they cannot blend renewable fuels at the refinery, they are in no position to ensure, or even contribute to, growth in the use of renewable fuels. If the point of obligation were to change, bulk fuel purchasers, that would in many cases become obligated parties, are in arguably less of a position to contribute to the growth in renewable fuels. The incentive for refiners to develop drop-in biofuels would diminish, and these fuels are not limited by the constraints of the ethanol blendwall.

"Obligating railroads would not promote renewable fuels and could create huge administrative compliance and Renewable Identification Number burdens on railroads for no public policy benefit".

Timothy J. Strafford, Counsel for Association of American Railroads

"Advanced drop-in fuels like Renewable Hydro-treated Diesel and Renewable Gasoline can be comingled with petroleum-based diesel and gasoline at the refinery gate and can share transportation and common storage downstream. Unfortunately, these feed stocks are not widely available"

Michael Kiely, Managing Director, SVP U.S. Government Affairs, UPS

CHANGING THE POINT OF OBLIGATION WOULD INCREASE THE COMPLEXITY OF THE RFS

Changing the point of obligation would increase the complexity for EPA to administer and enforce the program, as the number of obligated parties would increase. The increased complexity affects the fuel distribution industry as the identification of obligated fuels becomes more difficult.

"[Moving the point of obligation] would shift the compliance responsibility from the current readily identifiable obligated refiners and importers to various entities which includes, but it not limited to, small marketers, distributors, retail owners and trading companies" … "The proposed change could easily triple the number of obligated parties"

James Holland, VP Technical Services, Kinder Morgan

Those petitioners who support moving the point of obligation claim that this change would reduce the number of obligated parties. API disagrees and asserts that the number of obligated parties would increase significantly. More importantly, focusing only on the number of obligated parties fails to recognize the more significant impact of changing the point of obligation – specifically, the added complexity in the program that such a decision would create. Renewable volume obligations are based on the volume of gasoline and diesel produced and imported by 59 refiners at approximately 140 refineries and approximately 30 importers at various facilities. Changing the point of obligation would require the tracking and reporting of fuel volumes through roughly 1,300 terminals. The current obligated parties refine and import large volumes of transportation fuels; for example, a fuel batch size of 200,000 barrels can be common and could be listed as a single line item in a report. Moving the point of obligation to the rack reduces individual batch report volumes, increasing the number of individual reporting events. Consider that a single 200,000 barrel refinery batch could become 1,000 separate line items to report as the volume is divided into truckload by truckload sizes of roughly 200 barrels each. The result is an exponential growth in the number of reporting events irrespective of the number of obligated parties, with each event becoming a potential opportunity for error. The increased complexity also makes it more difficult for EPA to identify incidences of fraud.

"A shift in obligation would expand the players and their roles, likely bringing in many new and small companies that have not been required to participate in the RFS. These companies do not have the experience in dealing with the RFS and RIN accountability, nor do many of them have the resources to handle the implementation that would be required."

Lindsay C. Fitzgerald, Senior Manager, Government Affairs, Renewable Energy Group

"Any proposals to move the PoO that would increase the potential for fraud or manipulation in the RFS program should be rejected by EPA. The integrity of the RFS program must be maintained, and any structural changes that would magnify the risk of fraud or abuse must be avoided at all costs."

Bob Dinneen, Renewable Fuels Association

EPA recognized that some obligated parties, including merchant refiners, did not control the downstream blending of ethanol or other biofuels and would need to have access to RINs. EPA addressed this concern by structuring the RFS with provisions to facilitate compliance for all obligated parties, which include the ability for obligated parties to separate RINs and a 20% limit on RINs that can be carried over for compliance. EPA reconsidered the point of obligation issue following the enactment of the Energy Independence and Security Act in 2007 and decided that refiners and importers should remain the "obligated parties."

On March 2, 2017, sixteen associations representing a diverse and varied set of interests and industries wrote to EPA Administrator Scott Pruitt urging EPA not to move the point of obligation. Signatories of the letter represent fuel users and stakeholders throughout the fuel supply chain, which shows that companies that oppose moving the point of obligation are at every step in the fuel supply chain.