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EPA Docket Center  
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WJC West Building, Room 3334  
1301 Constitution Avenue, NW  
Washington, DC 20004

The Tesoro Companies, Inc. (“**Tesoro**”) appreciate the opportunity to provide comment on the U.S. Environmental Protection Agency’s ***Proposed Denial of Petitions for Rulemaking to Change the RFS Point of Obligation*** issued on November 10, 2016 (the “**Proposed Denial**”). Tesoro strongly supports EPA’s Proposed Denial.

Tesoro structures its comments utilizing the outline of the primary points advanced by the EPA in its Proposed Denial.

#### Background

The Renewable Fuel Standards (“**RFS**”) “point of obligation” was established by the US Environmental Protection Agency (“**EPA**”) in 2010 through its notice-and-comment rulemaking authority. As currently in effect, these regulations impose the renewable fuel annual compliance obligations on refiners and importers of gasoline and diesel fuel (“**Obligated Parties**”).<sup>1</sup> Each year, EPA calculates and establishes a renewable fuel percentage standard based on volume targets in the statute and forecasts of US gasoline and diesel consumption from the Energy Information Agency (“**EIA**”). Based on EPA’s annual renewable fuel percentage standard, Obligated Parties must meet their unique renewable fuel volume obligations (“**RVOs**”). Obligated Parties satisfy their yearly RVOs<sup>2</sup> by retiring a sufficient number of Renewable Identification Numbers (“**RINs**”). RINs are acquired by: (i) purchasing renewable fuel with assigned RINs (to blend into the Obligated Party’s petroleum-derived transportation fuels) or (ii) buying RINs that have been separated from the renewable fuel on the open market.

#### I. The Current Program Structure Is Not Working to Achieve the Goals of the RFS Program; Shifting Point of Obligation Will Not Help

The RFS program<sup>3</sup> is an outgrowth of Congressional intent as expressed by two statutes, the *Energy Policy Act of 2005* (“**EPACT**”) and the *Energy Independence and Security Act of 2007* (“**EISA**”). The stated intent was twofold: (i) “*moving the United States toward greater energy independence and security*” and (ii) increasing the “*production of clean renewable fuels*” for the nation’s transportation fuels.

While Tesoro believes that the first objective has been largely achieved, its attainment has had little to do with the RFS and is more the result of a domestic energy production renaissance. The second objective is, at best, a work in progress. Witness the historic under-performance of the advanced

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<sup>1</sup> The EPA’s final rule establishing the regulatory RFS program was published on May 1, 2007 (generally referred to as “RFS1”) finalized the definition for “obligated parties” as “refiners and importers of gasoline.” “RFS2” is the EPA’s final rule published on March 26, 2010 and reflects the EISA amendments to include diesel producers and importers as obligated parties.

<sup>2</sup> An Obligated Party’s RVOs are calculated by multiplying the Obligated Party’s total annual production and import of gasoline and diesel by the four annual renewable fuels standards (cellulosic biofuel, biomass-based diesel, advanced biofuel and renewable fuel).

<sup>3</sup> 40 CFR 80.1406

biofuel industry to date which, while Tesoro hopes will improve and is making significant investments in pursuit of that goal, owes to varied dynamics beyond the scope of these comments.

Tesoro further believes that the RFS program is in dire need of significant and comprehensive reform for myriad reasons again beyond the scope of these comments.<sup>4</sup> Would that it were true that the problems with the RFS program could simply be cured or even mitigated by such a cosmetic fix as shifting the point of obligation.

Tesoro agrees that the RINs system, either as a compliance tool for the RFS program or as a trading market facilitating the program, has serious flaws in both architecture and function. Indeed, price volatility and instances of actual fraud continue to impact all Obligated Parties and generally limits the RFS program's overall effectiveness. Those parties seeking to shift the point of obligation would have us believe that pushing responsibility for compliance via RINs away from them would alleviate their respective financial hardships while simultaneously (and somewhat miraculously) functionally easing their compliance burden. While Tesoro seriously doubts the latter would occur from this one change, the broader economics currently impacting the domestic refining sector strongly suggest the former would fail to happen as well.

Consider that many refiners long ago recognized that the costs of RIN compliance had to be incorporated into their respective economic decision-making models and processes. This resulted in the market process for fuels which carry RINs obligations (such as gasoline "BOBs"<sup>5</sup> and diesel fuel) to price at a premium to fuels that do not carry this obligation (such as jet fuels or blended gasolines like E10). Analysis of publicly available pricing data, including that done by EPA and referenced in commentary supporting the Proposed Denial, suggest that RIN costs are passed through at the bulk finished product sales points and provide refiners with coverage of their exposure to them. The real reason for the financial discomfort of some refiners is less about RINs and more likely about a convergence of variables that impact the industry's financial health, including current global crude inventory levels being at all-time highs and the resulting downward pressure on finished product prices. It would seem that shifting the point of obligation, while perhaps a convenient distraction from these factors, will not materially impact the finances of petitioners as they believe or somehow rescue the refining industry as a whole. It could easily be expected that moving the point of obligation downstream would result in a decrease in the market price for these obligated fuels resulting in no net improvement to the financial position of those Petitioners who are blaming RFS for their poor profitability.

## II. Changing the Point of Obligation in the RFS Program Will Not Result in Increased Production, Distribution and Use of Renewable Fuels.

Advocates for moving the point of obligation have provided no convincing evidence to prove that such a change would increase production, distribution or use of renewable fuels. In fact, the reasons for the sluggish pace of sales nationwide for ethanol blends above 10% have far more to do with engine compatibility with these types of fuels, consumer acceptance generally and a range of market dynamics (including unique pricing variables relative to E85) which combine to inhibit traditional distribution channels.

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<sup>4</sup> In this comment letter Tesoro purposely does not address other aspects of the RFS program that we believe should be modified and/or improved. Changing the point of obligation is merely a distraction from the real issues and would add complexity to an already complex program.

<sup>5</sup> "BOBs" are Blendstocks for Oxygenate Blending; i.e. CBOB (Conventional) or RBOB (Reformulated).

While a shift in the point of obligation would not appreciably alter market dynamics to cause dramatic growth in the production, distribution or use of renewable fuels, granting the relief sought by Petitioners could negatively impact ongoing efforts to spur advanced biofuel production initiatives being pursued by the refining industry. Petitioners blithely ignore that many in the sector have (including Tesoro), in reliance on the existing regulations, made significant, strategic and long-term decisions, financial commitments and investments in renewable fuel development and research for infrastructure and technology in order to satisfy future obligations from the RFS program. Petitioners, who could also have made such choices and chose not to, now seek, substantially after-the-fact, to move the obligation further downstream away from them.

Tesoro's response to the current regulatory structure is both informative and likely reflective of others in the refining industry. Tesoro's stated renewable fuels strategy is to foster the development of high-quality, lower-carbon renewable feedstocks and blendstocks that can either be co-processed in existing refineries or blended seamlessly with traditional fuels. Tesoro believes it is important to commercialize new technologies that meet stakeholders' expectations and regulatory requirements by producing renewable fuels that do not compromise product quality. Changing the point of obligation could materially disrupt Tesoro's stated renewable fuels strategy and jeopardize these efforts.

Endeavors such as these in the advanced biofuel world take many years to commercialize. Tesoro announced in January 2016 its plan to develop biocrude from renewable biomass by collaborating with, among others, Fulcrum BioEnergy, Inc. (for biocrude produced from municipal waste) and Ensyn Corporation (for biocrude produced from tree residue). Each of these initiatives have been in the works for many years and are not expected to be operational for several more years due to technological and logistical challenges that must be overcome to bring these new, innovative technologies to commercial scale. Additionally, Tesoro announced in September 2016 its agreement to acquire Virent, Inc., an innovative renewable fuels company. Virent developed a proprietary technology that can convert sugars and other biomass derived feedstocks into renewable gasoline blendstock which is fully compatible with existing transportation fuel infrastructure and current vehicle warranties. Tesoro intends to foster more rapid commercialization of Virent's renewables technology, but even with this focus, commercial production is not expected to occur for some time.

A key component in all of Tesoro's actions in this space to date is premised on the investment in, and a partnership with, fledgling advanced biofuel entities so as to move production to commercial volumes. A shift now in the point of obligation could chill investments such as Tesoro's from occurring elsewhere in the refining industry as it would introduce yet another degree of uncertainty into what is already a challenging economic environment.

For the reasons stated above, Tesoro does not believe that shifting the point of obligation will result in the increased production, distribution and use of renewable fuels. Such a change would instead erect a barrier to the promising new co-processing technologies; a barrier that these new-obligated parties could not likely overcome or solve due to their lack of technical wherewithal and insufficient resources to implement.

### III. Changing the Point of Obligation Would Significantly Increase the Number of Obligated Parties and the Complexity of the RFS Program.

Moving the point of obligation downstream would exponentially increase the number of Obligated Parties, making compliance and enforcement a much more onerous task for all participants including EPA. The current number of Obligated Parties is approximately two hundred (200). EPA stated the obvious by observing that *“as a matter of regulatory design and implementation, it is desirable both to limit the number of obligated parties, and to limit burdening small businesses.”* If the point of obligation were moved from refiners and importers to downstream blenders, EPA would vitiate both of its stated desires since it is foreseeable that a change in the point of obligation would result in thousands (1000s) of Obligated Parties – many of whom are likely to be smaller in size. These smaller Obligated Parties likely have limited resources to facilitate compliance and lack familiarity with a complex system they would now be responsible in which to demonstrate compliance.

Basically stated, moving the point of obligation would merely shift the RFS compliance responsibility from the current group that is limited in number, familiar with the system intricacies and can draw upon significant resources to a new group that is much greater in number, less familiar with the system and with limited resources to draw upon. If the intent were to make an already dysfunctional RFS program even more so that it will collapse under its own weight, further impede policy objectives and invite additional fraud in the marketplace, then shifting the point of obligation certainly checks those boxes.

Point in fact, EPA previously contemplated moving the point of obligation downstream and chose not to do so for several reasons aforementioned. Those reasons included opposition from downstream parties that cited additional burdens for small businesses, a requirement for new systems to determine and report compliance, insufficient lead-time to satisfactorily implement and fewer resources available to manage such programs.

It is also important to keep in mind that since 2010, Obligated Parties have spent substantial resources on systems, personnel and training (as well as acquiring RINs) in order to satisfy their respective RVOs compliance. These Obligated Parties also enlisted extra resources in response to instances of RINs fraud. The current Obligated Parties have had more than six (6) years to train personnel, build systems and develop processes all with the goal to meet their respective RVOs. Passing the burdensome requirements from one entity to another merely injects further complexity into one already sufficiently challenging. Simply stated, changing the point of obligation would effectively put these new “obligated parties” and the RFS program (at best) back at square-one.

### IV. Changing the Point of Obligation Could Cause Significant Market Disruption.

In the RFS2 rule, EPA previously contemplated moving the point of obligation downstream. Of particular concern was the behavior of Obligated Parties to retain rather than sell excess RINs to ensure that they have a sufficient number for next year’s compliance. This behavior caused concern that RIN prices would escalate in response to demand for compliance demonstration and reduce liquidity in the RINs market. In addition, the impacts to the existing gasoline and diesel markets from RINs compliance requirements is understood; changing the point of obligation would change those impacts and trigger market uncertainty.

If the point of obligation is moved, this change would also impact Obligated Parties’ RVOs in future years relative to what they anticipated under the existing regulations. Such a change could lead to significant

disruption to the RINs markets. Those Obligated Parties with lower RVOs may have surplus, including carry-over RINs available while Obligated Parties with higher RVOs may have a greater deficit than planned. This change to a consistent regulatory structure upon which Obligated Parties have relied, planned and made investment as well as strategic decisions is likely to result in significant market volatility.

V. Conclusion.

Petitioners have failed to prove that moving the point of obligation would increase energy security or increase renewable fuel as a percentage of the nation's transportation fuel and their request should therefore be denied. For the reasons stated herein as well as those discussed in EPA's Proposed Denial, Tesoro objects to the point of obligation being moved.



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