TESTIMONY OF SONJA HUBBARD

ON BEHALF OF THE

NATIONAL ASSOCIATION OF CONVENIENCE STORES

AND THE

SOCIETY OF INDEPENDENT GASOLINE MARKETERS OF AMERICA

BEFORE

THE SUBCOMMITTEE ON ENERGY AND AIR QUALITY
COMMITTEE ON ENERGY AND COMMERCE

U.S. HOUSE OF REPRESENTATIVES

"LEGISLATIVE HEARING ON
DISCUSSION DRAFT CONCERNING ALTERNATIVE FUELS,
INFRASTRUCTURE AND VEHICLES"

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Good morning. My name is Sonja Hubbard. I am the Chief Executive Officer of E-Z Mart Stores, Inc., headquartered in Texarkana, Texas. My company owns and operates over 300 motor fuel outlets in five states -- Texas, Oklahoma, Louisiana, Arkansas, and Missouri. Our company sells nearly 200 million gallons of gasoline and diesel fuel each year and we employ over 2,200 clerks, managers, and other personnel in these five states. We sell gasoline under our own brand and, at some locations, under the brand of our refiner suppliers.

I appear today on behalf of the National Association of Convenience Stores (NACS) for whom I currently serve as Vice Chairman of the Board. NACS is a non-profit trade association representing the convenience and petroleum retailing industry. Our industry operates more than 145,000 retail locations and, in 2006, sold $405.8 billion worth of motor fuels.

I also appear on behalf of the Society of Independent Gasoline Marketers of America (SIGMA), of which I am a member. SIGMA is an association of more than 250 independent motor fuel marketers operating in all 50 states. SIGMA members sell more than 30 percent of all motor fuels sold in the United States and supply more than 35,000 retail outlets across the nation.

Together, NACS and SIGMA members account for approximately 80 percent of all motor fuels sold at retail in the United States every year.

Thank you for providing me with the opportunity to share our industry's perspective on the Committee's discussion draft legislation regarding alternative and renewable fuels. Before I begin, let me make it perfectly clear that retailers are agnostic about which motor fuels we sell, with a single caveat: We want to sell motor fuels that are available and that our customers want to buy.

Today, I will focus my comments on those provisions of this discussion draft that most directly affect the motor fuels retail industry.

Alternative Fuels Program

Let me begin with a couple of comments regarding the proposed Alternative Fuels Program. Two years ago, the Energy Policy Act of 2005 established a renewable fuels standard (RFS), mandating that at least 7.5 billion gallons of renewable fuels be sold in the United States by the year 2012. As everybody should by now be well aware, the industry is implementing the program ahead of schedule and is on pace to exceed the 2008 requirement to blend 5.4 billion gallons.

Now, however, it seems there is widespread interest on the part of political leaders to accelerate and expand upon this accomplishment. The discussion draft before us proposes to increase the mandate to 35 billion gallons by the year 2025, beginning with 14 billion gallons in the year 2013. Another proposal calls for the program to expand to 36 billion gallons by 2022, beginning with 8.5 billion gallons in 2008. Still another requires 35 billion gallons by 2017, starting with 10 billion gallons in 2010.

In light of these competing proposals, one can say that the discussion draft before this Committee appears to be a more conservative approach because it provides additional time to implement the increase. Regardless, each of these proposals contains very ambitious goals, and we must ask if they are the best course of action.

The market is proceeding to offer renewable fuels ahead of the federally mandated schedule. There is no reason to believe that this will not continue in the absence of an increased mandate. However, as we have testified before, if Congress feels compelled to accelerate this transition through a revised federal mandate, NACS and SIGMA call upon Congress to construct the revised program with the interests of consumers in mind.

Any increase beyond the existing RFS should be predicated upon a finding by the Secretaries of Energy and Agriculture that there will be both sufficient supplies of renewable fuels and sufficient distribution infrastructure to deliver that product to retail without placing an undue financial burden on consumers. If these assurances cannot be made, then the proposed increase should be delayed until conditions are sufficient to support its implementation. Further, such a decision should be made with enough lead time to enable the petroleum industry to make necessary arrangements to accommodate the requirements.

If such consumer protections based upon market analysis are not provided, we will be concerned about potential market disruptions and the impact these could have on our customers. Last year, the disruptions we experienced in this area due to the transition from MTBE to ethanol were primarily the result of inadequate distribution infrastructure and insufficient supply in appropriate markets. It is critical that this program protects against a repeat of that experience.

Alternative Fuels Infrastructure

I would like to direct the rest of my testimony toward the provisions in the discussion draft focusing on alternative fuels infrastructure.

The proposal before the Committee implements a mandate for retailers to install E-85 compatible equipment. **Let me state clearly and unconditionally: NACS and SIGMA are strongly opposed to this provision.** It is anti-free market; it will put retailers in significant economic jeopardy; it is an extreme overreaching by the Federal government into private enterprise; and, it is unsupported by existing or anticipated market conditions.

Further there seems to be little support for the mandate within any segment of motor fuels industry. For example, the National Ethanol Vehicle Coalition, the primary advocate for the use of E-85 fuel, testified on April 18 that it "opposes the mandatory establishment of E-85 fueling locations." The Coalition's Executive Director, Phil Lampert, said, "Mandated establishment of E-85 fueling locations is counter productive and will lead to poor pricing, disinterested marketing, lackadaisical vendor performance, undesirable locations and general dissatisfaction by the consumer."

Given the apparent lack of support, we are at a loss as to why the Committee would propose implementing this retailer mandate.

Considerations for Mandate Implementation

To be fair, the discussion draft before us perhaps represents the best effort to date by Congress to reflect market factors when imposing an E-85 retailer mandate. NACS and SIGMA appreciate the Committee’s efforts to address some of our itemized concerns centered around such a program. Specifically, we appreciate that the draft directs the Secretary of Energy to determine an appropriate schedule and plan for implementation, contingent upon the promulgation of a rule. Further, we appreciate that Congress directs the Secretary to consider: 1) the availability of E-85 within a region and number of competing E-85 wholesale suppliers; 2) the level of financial assistance available to retailers within a region; 3) the potential inability of retailers to install E-85 due to property restrictions; 4) the economic burden the mandate will impose on a business; and, 5) the time it will take a retailer to comply with the mandate.

These are positive provisions that do help mitigate the negative consequences of the mandate. However, they do not explain how the Secretary will select, from a list eligible retailers in a market, which will be required to make the mandatory investment and which will not. The legislation does not give the Secretary any direction as to how to determine the winners and losers in this system.

I cannot think of any provision or combination of provisions that would be sufficient to secure the support of the retail community other than elimination of this mandate.

The fundamental problem is that if a retailer is forced to install E-85 against its will, the bill before the Committee fails to ensure that consumers will actually purchase E-85. In other words, the proposal imposes an expensive mandate on us without any promise that our forced investment will provide any return.

This is the critical question for retailers and explains why many have been slow to make the conversion investment on their own accord. It is not due to animosity towards an alternative fuel and it is not due to limitations imposed by our suppliers. Rather, it is because consumer demand for the product is insufficient to justify the cost of the investment. Trust me, my fellow NACS and SIGMA members and I will make E-85 pumps available when the market calls for it. But to illustrate the basis of our concerns, let me start by explaining the costs associated with E-85 systems.

Cost to Convert E-Z Mart Store to Sell E-85

The primary impediment to retailers converting a dispenser to E-85 is equipment compatibility. Because E-85 is more corrosive than regular gasoline or E-10, it requires equipment that is certified compatible with the fuel.

In preparation for this hearing, I inquired of my equipment supplier to determine what would be required to convert one of my newer stations to sell E-85. These stations have the newest equipment and, therefore, hold the best chance for existing equipment compatibility. I learned that my new steel tanks and my fiberglass tanks were certified compatible with E-85. Our automatic tank gauges were listed compatible as were our fiberglass piping systems. However, we would have to replace several of the ancillary fittings, including the submersible turbine pump, the overfill drop tube and others like flexible hoses, spill buckets, ball valves, etc. In addition, our hanging hardware, which includes conventional nozzles, swivels, breakaways and curb hoses would have to be replaced with nickel plated units at an increased cost. For all of these conversions, including tank cleaning, we estimated the cost to be between $6,000 and $7,000.

However, this does not include the dispenser itself. The two dispenser manufacturers each charge an additional fee for a new E-85 compatible dispenser -- $8,000 for Dresser-Wayne and $7,300 for Gilbarco. Thus, a typical E-85 dispenser can cost upwards of $17,000 per unit. And this cost is for equipment that has not yet been certified compatible with E-85 by Underwriters Laboratories.

While it is conceivable to convert an existing dispenser, this would require at a minimum replacing the meters, internal piping, filter inlets, compression fitting, control valves and seals, and any non-ethanol compatible sealants. Consequently, converting an existing dispenser would cost in excess of $5,000.

In short, to convert one of my newer stores to sell E-85, I would face an expense of at least $11,000, not including labor expenses. For older locations, the cost would be considerably higher than this. According to colleagues in the industry who have installed E-85 systems, such an investment would be considered a bargain. One reported spending upwards of $55,000 on a new system, while another in California reports the cost of installing a basic diesel system at more than $200,000—not including the up-charge associated with compatible equipment.

Consumers Are Not Buying the Fuel

As we have testified repeatedly, fuel retailers are not picky. We will sell whatever products our customers want to buy. As an industry, we have been watching the development of E-85 and flexible fuel vehicles quite closely, and many of my colleagues have taken the initiative to convert a dispenser to sell E-85. The results have not been overwhelmingly positive.

The fundamental fact is that most drivers of FFVs (Flex Fuel Vehicles) do not want to buy E-85 unless it is offered at a substantial discount compared to gasoline. Because these drivers can purchase either E-85 or gasoline, they make economic decisions when at the pump.

Clearly, consumers have made the economic calculation regarding the decreased fuel economy associated with E-85 (approximately 25 percent fewer miles per gallon than gasoline) and they are demanding a benefit in price. Absent that benefit, they will follow their economic interests and purchase gasoline.

NACS and SIGMA have spoken with retailers throughout the nation who sell E-85, and we have learned that sales of E-85 fall off dramatically when the price is not significantly lower (at least 20 cents per gallon) than gasoline. Some retailers report that the price differential to maintain volumes is actually closer to 40 cents per gallon.

Unfortunately, it is not always possible for retailers to obtain supplies of E-85 at a price that enables them to sell it at such a discount. The provision in the proposal requiring consideration of the number of E-85 wholesale suppliers is important, because without adequate competition in the E-85 supply market, retailers will have little to no chance to obtain competitively priced product. However, there are no guarantees that even a competitive market will produce E-85 supplies that can be priced well below gasoline.

The lack of consumer acceptance of E-85 is a major problem. Fuel sales, which generate incredibly low margins, drive traffic to the store, where margins are much stronger. We have spoken with several retailers who lament their decision to install E-85 equipment because they have been unable to generate sufficient sales from these fueling positions to support their overall business model.

Our opposition to the proposed mandate is not necessarily a “just say no” position. Rather, it is reflective of actual market conditions and the need for retailers, who, on average, generated less than $34,000 in pre-tax profit per outlet in 2006, to protect the financial stability of their business and to preserve for themselves the right to make any decisions which might affect that very stability.

The government has no responsibility to generate sales sufficient to pay my employees. By the same token, it should not make decisions affecting my ability to sell a marketable commodity.

Franchise Agreements

Let me address one final provision of the discussion draft. There is some confusion about whether retailers are not voluntarily installing E-85 because they are prohibited from doing so by their franchise agreements. Neither NACS nor SIGMA have heard from any of our members complaining that their suppliers were preventing them from installing E-85 dispensers. Rather, we believe this is a red herring being used to cover the fact that consumer demand for the product is not strong to make such investment a viable option for most retailers.

Regardless, neither NACS nor SIGMA are opposed to Congress enacting legislation that will clarify a retailer's right to convert their own equipment for the sale of E-85. The proposal in this discussion draft, however, does require some modification to ensure that only the entity which owns the fueling equipment, and assumes the liability for that equipment and the land on which it sits, shall be empowered to make the decision to convert and install an E-85 compatible system.

There are instances where the operator of a retail outlet does not own the land or equipment which it operates. Rather, that individual may lease the land and equipment from his franchisor, which could be a refiner but is more likely an independent wholesale distributor. In these circumstances, the individual operator who does not own the equipment should not be permitted to make conversion decisions about that equipment. Converting existing equipment, much less installing a new storage and piping system, has significant potential liability implications for the owner of the real estate. I submit that none of you would permit another the unilateral right to create this kind of long-term liability for you. It is simply not fair. It is simply not right. We encourage this Committee to amend the proposed language to reflect this reality.

Conclusion

NACS and SIGMA are not antagonistic to the expanded market availability of alternative and renewable fuels, provided our customers want to buy them. Expanding the mandate for these fuels as provided in this proposal can be dramatically improved by requiring the executive branch to find that sufficient supplies and distribution infrastructure exist to support the specific increase. Absent such a finding, a pending increase should be suspended. This will protect consumers from market disruptions associated with insufficient supplies.

The effort to eliminate any potential for a supplier to prevent an independent retailer from installing E-85 infrastructure must not endanger the legitimate interests of the owner of the land or the equipment, even if that be the supplier, to make decisions concerning the conversion or installation of such equipment.

While we appreciate the efforts made by the Committee to address itemized retailer concerns regarding an E-85 retail mandate, NACS and SIGMA consider such proposals completely unnecessary. NACS and SIGMA will oppose legislation like the discussion draft unless and until it offers the petroleum marketplace a chance to work in the best interest of consumers.

Finally, NACS and SIGMA members are extremely sensitive to our customers' concerns about motor fuel prices. Our businesses compete with each other on the basis of pennies per gallon as we seek to attract the increasingly price conscious consumer. Consequently, we become very concerned regarding any proposals that could potentially affect supplies or distributing efficiencies or otherwise put upward pressure on prices. Therefore, we urge this Committee to consider carefully the supply and price implications of policies under your jurisdiction. Our customers, your constituents, deserve no less.

Thank you again for the opportunity to share our thoughts regarding the discussion draft pending before the Committee.