NACS®

May 17, 2006

The Honorable Stephen L. Johnson
Administrator
U.S. Environmental Protection Agency
Ariel Rios Building
1200 Pennsylvania Avenue, NW
Washington, DC 20460

Dear Administrator Johnson:

On behalf of the retail members of the National Association of Convenience Stores (NACS), thank you for the opportunity to provide input into the Governors' Task Force on Boutique Fuels. NACS believes the issue of boutique fuels to be of considerable importance and applauds the Agency for pursuing a cautious and deliberate approach as it assesses the potential effects of any possible changes to the fuel regulatory structure on fungibility, supply, price and environmental quality.

NACS is an international trade association comprised of more than 2,200 retail member companies operating more than 100,000 stores. The convenience store industry as a whole sold 143.5 billion gallons of motor fuel in 2005 and employs 1.5 million workers across the nation.

For many years, NACS has expressed its concern to Congress and the Administration that the proliferation of boutique fuels has contributed to increased complexity in, and fragmentation of, the motor fuels supply and distribution system, leading to more frequent supply interruptions and regional shortages and price spikes. We have advocated a measured approach to restoring fungibility to the system, with a strong caution against any regulatory changes that might result in a loss of supply.

In the Energy Policy Act of 2005, NACS endorsed Section 1541 which stopped the further fragmentation of the supply and distribution system by capping the number of fuels at 2004 levels. Further, the section directed EPA and the Department of Energy to conduct a comprehensive study of market conditions and report back to Congress with recommendations for a regulatory system that would improve fungibility without sacrificing supplies or environmental protection and without dramatically increasing fuel costs. In our opinion, this section represents a responsible approach to the issue of boutique fuels.

In preparation for Thursday's Task Force meeting, you asked NACS to provide responses to four specific questions relevant to EPA's 2001 Staff White Paper on Boutique Fuels and the pending work before the Governor's Task Force. We hope the following prove useful to your efforts:

Question 1: EPA's 2001 study analyzes four different scenarios for reducing the number of boutique fuels. Do you agree with these options? Are there other options that should be addressed?

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Answer: The fuel options assessed in the 2001 Staff White Paper represent a very good start, but there are other scenarios that should be modeled. In 2003, NACS commissioned a study into boutique fuels through which six potential regulatory structures were analyzed through refinery modeling for their affect on a 2007 Baseline. Similar to EPA's 2001 study, NACS found that as we reduced the number of fuels available in the market, while maintaining air quality performance, domestic gasoline production capacity was compromised. I have attached the executive summary of the NACS study, which includes details on the scenarios that were modeled and their results. Perhaps this will provide some valuable information to the Task Force as it conducts its review of the issue.

In recent years, legislation has been introduced that would establish a federal fuel slate comprised of five or six fuels. The House of Representatives in 2005 approved HR 3893, the Gasoline for America's Security Act, which would establish a fuel slate comprised of one Federal diesel fuel (considering the phase-in of ULSD as one fuel), Federal Reformulated Gasoline, Conventional Gasoline and two RVP controlled fuels to be determined. California, and the states its refineries supply, are exempt from the provisions of this legislation. This concept has been replicated to a large extent in additional legislation introduced in both the House and the Senate. Notably, included in each piece of legislation is a provision that would abandon the proposed fuel slate if DOE found that implementation of the program would result in a loss of domestic refining capacity. These proposals, which have gained significant attention in Congress, serve as an additional scenario that the Agency should analyze.

NACS would also suggest that the Agency take the requisite time to effectively assess the feasibility of a regional fuels program. As noted in the 2001 White Paper, this is a very complex scenario that will require time to complete an analysis. The NACS 2003 study assessed a type of regional fuel program based upon the existing PADD designations. Perhaps a good place for EPA to begin would be to assess the applicability of the current PADD designations for today's supply and distribution system. A careful analysis of the refining, distribution and petroleum storage infrastructure could provide greater insight into the affect on fungibility certain proposed fuel scenarios might have on the market, as well as facilitate an analysis of a regional fuels program.

Question 2: Given the current state of fuel requirements, are the 2001 study findings regarding the cost, fungibility, air quality and supply of the four options still accurate?

Answer: Since the Agency completed its Staff White Paper, several things have changed that would necessitate a recalibration of the initial findings. Among these are the following:

- Since May 5, 2006, the use of MTBE in the fuel supply has been effectively phased out. This is a significant difference from the original assumptions that state bans on the additive would be the primary factor in determining its presence in the marketplace.
- Implementation of the Renewable Fuels Standard, which was assumed in the original modeling, has yet to be finalized. This program will have an affect on marketplace fungibility and should be more carefully modeled in the analysis, especially in light of the fact that ethanol supplies are currently being diverted from conventional gasoline markets to RFG markets in the absence of MTBE.
- The affect of state renewable fuel mandates on the market's ability to utilize the flexibility envisioned by Congress when developing the Renewable Fuels Standard must be more

fully understood. NACS suggests that such state-level provisions inhibit the efficient distribution of renewable fuels throughout the nation by restricting their movements, thereby potentially contributing to increased costs associated with the RFS. This directly contradicts Congressional intent regarding the flexibility of the RFS.

- County designations for implementing the 8-hour ozone standard are now available and should be incorporated into the models to more accurately assess the affect of proposed fuels programs on production capacity. For example, the Staff White paper estimates the volume of gasoline that would be affected in each of the proposed fuel programs; under the 8-hour standard, these volumes may change due to the increased number of counties that could be anticipated to use an emissions controlling fuel.
- The Staff White paper assumes that as MTBE is phased-out of the system, it will be replaced by an increase in the production and use of alternative products, like iso-octanes and alkylates. Now that MTBE has to a great extent been phased-out, EPA and DOE should reassess the replacement potential of these alternative products.

Question 3: What data would be needed to complete additional analysis on these four factors for boutique fuel options?

Answer: In order to conduct a thorough analysis of various fuel programs on the four primary criteria (supply, price, fungibility and air quality), NACS recommends the Agency:

- Assess and model the emissions control options that would be utilized by counties designated in non-attainment under the 8-hour ozone rule. This would provide a reasonable estimate of which counties would seek emissions reductions based upon fuel selection, providing more accurate analysis regarding supply implications of various scenarios.
- Work with DOE to complete refinery modeling analyses for each proposed fuel program to accurately assess the production/supply implications. This will require assessment of the effects on refinery throughput as well as the reasonable expectation of individual refineries' ability to continue operations under the proposed new structure.
- Assess the effect of the proposed fuel programs on the availability of imports. Given the fact that imports of finished products have increase in recent years, and considering the effect sulfur reductions have had on availability of imported product, this is a component that must not be ignored.
- Plot the locations of wholesale terminals and assess the affect of each program on storage capacity at those locations. NACS recommends that such an analysis also include an assessment of storage requirements associated with accommodating two distinct on-road diesel fuels as well as the storage and blending equipment required to accommodate ethanol.
- Update the emissions model to more accurately assess the effects of gasoline in the modern vehicle fleet. In the Government Accountability Office's report on boutique fuels issued in 2005, GAO noted, with EPA concurrence, that the Agency's ability to validate the emissions characteristics of new fuels is inaccurate due to outdated data. Section 1506 of the Energy Policy Act of 2005 directs EPA to update this emissions modeling. NACS believes that updating this model is essential to accurately assessing the affect of a fuels scenario on environmental quality.

Question 4: How long would it take you to schedule an additional shipment if a refinery you service just produced a batch of low-RVP gasoline or RFG to supply an area experiencing a supply shortfall? Would it make a difference if this additional batch of fuel is or is not a fuel type you normally ship? If the fuel type is not standard for you, would you also need to provide breakout tankage for this additional fuel type and how would that delay its shipment?

Answer: NACS members are retailers of motor fuel and are therefore not qualified to provide a response to this question.

Again, thank you for the invitation to participate at tomorrow's briefing. I look forward to the opportunity to provide additional information from the perspective of the nation's convenience and petroleum retailers. In addition, I hope the information provided above proves to be useful to the Agency and the Governor's Task Force as it considers options for addressing the issue of boutique fuels.

If you have any additional questions, please do not hesitate to let us know.

Sincerely,

John Eichberger
Vice President, Government Relations

Attachment.