

**API Statement to EPA's Governor's Boutique Fuels Task Force  
May 18, 2006**

API, on behalf of its U.S. oil and natural gas industry members, welcomes the opportunity to provide input to the Task Force. Our industry looks forward to a more extensive, longer-term interaction with EPA and DOE to keep this effort moving forward with a more comprehensive, up-to-date review.

The national fuels landscape has changed significantly since 2001, thus the Agency's 2001 options and paper should be reviewed and updated as appropriate. Likewise, the agency's conclusions regarding cost, fungibility, air quality and supply should be reviewed. EPA and DOE need to look at the boutique fuels landscape today. This should be a fresh analysis of costs, supply, fungibility and air quality. It will be important to take into account the impact of the major fuels changes this year, including the removal of the RFG oxygen mandate, the implementation of the renewable fuels standard and the ULSD program.

A "boutique fuel" is a specialized fuel formulation that is unique to a particular market, usually by virtue of federal, state or local laws, and that cannot be obtained from other markets in the same regional distribution system. Boutique fuels can contribute to tight supplies and price volatility, particularly when there is a supply disruption or stress. Nothing is more important in our business than the reliability of supply and a rigid system of state-specific boutique fuels reduces that reliability.

While the patchwork of localized boutique fuels is not principally responsible for the recent higher gasoline prices, the proliferation of these fuels in recent years has presented significant challenges to U.S. refiners and resulted in an inflexible fuel system.

Boutique fuels contribute to the tight supplies and price volatility so decried by consumers. A classic example of the disadvantage of boutique fuels is in the Atlanta area, which has a one-of-a-kind gasoline blend in the summer. Most gasoline on the major pipelines that service Atlanta cannot be used to address any supply shortage in that market. Refiners and suppliers have made the refinery and distribution system investments to handle the Atlanta gasoline. However, if a serious infrastructure problem occurs in the refineries, the pipelines, or the terminals that supply this area with gasoline, the boutique fuel involved could lead to serious supply disruptions.

Of utmost importance in our business is the reliability of supply. Fuel providers need the flexibility to get fuel to where it is most needed and to quickly adjust to changes in demand. Additionally, marketers need some assurance that, if they do not have access to a particular supplier or terminal, they will be able to go elsewhere for product. However, a rigid system of state-specific boutique fuels

reduces the reliability of supply and increases the risk of spot shortages and price volatility.

Our industry has worked long and hard to discourage the spread of boutique fuels. Some success was realized when the Energy Policy Act of 2005 (EPACT05) included a provision setting some restrictions on EPA for approval of states fuels intended for reducing air pollution. In addition, Congress required that EPA and the DOE complete two studies regarding boutique fuels (one this year and one in 2008). These provisions clearly indicated that policy-makers were finally recognizing the harmful effects of widespread adoption of boutique fuels.

EPACT05 attempted to balance supply issues with state authority to adopt fuel programs. EPACT05 reduced the number of options available to states by adopting a PADD fuel-type cap but still allows a state to implement a specialized fuel if it can demonstrate that additional emission reductions are needed to meet its National Ambient Air Quality Standards requirements and there are no other non-fuel controls available that are reasonable or practicable. These prerequisites should not be abandoned. EPA should also consider the supply impact of a state fuels provision before approval.

API supports the boutique fuels provisions in EPACT05 as an initial step to help address the boutique fuels issue. The results of the two studies should provide guidance to Congress as to whether further steps should be taken regarding boutique fuels.

However, there is more to be done. The boutique fuels provisions in EPACT05 only cover state programs that are considered by EPA under section 211(c)(4)(C) of the Clean Air Act. Many boutique fuels are not covered by this EPACT05 provision:

- State mandates for renewables such as ethanol and biodiesel and other fuel additives
- Winter oxygenated fuels programs and other fuels requirements that are approved under the general SIP provisions of section 110 of the Clean Air Act
- State distillate requirements (such as the recently enacted Connecticut home heating oil legislation)

Just as the patchwork approach of boutique fuels covered by the EPACT05 cap has made it much more difficult for our industry to deal with tight supplies and to get fuel to where it is most needed, state renewables mandates and other state fuel requirements further aggravate this.

If the issue is fuel fungibility and distribution, boutique fuels include all gasolines and diesel fuels mandated at any government level. Whether the fuel requirement is imposed at the federal, state, or local level, for environmental or

other reasons, if the result is a different fuel, it should be included in the limitations imposed by EFACT05.

API supports the flexibility contained in the Renewable Fuels Standard in EFACT05. A credit banking and trading component was a key element in making the national RFS program possible – it will provide flexibility, allowing refiners to use renewables where it is most efficient. Flexibility is critical for the reliable supply of fuels. State mandates undermine that flexibility and create obstacles to the achievement of Congress' goals.

Individual states should not force the use of ethanol by devising their own blend of gasoline/ethanol mandates. The last thing our nation needs now is an expansion of the boutique fuels patchwork of state-by-state laws by mandating ethanol use at different concentrations and/or under different terms. At the time of the EPA boutique fuels study in 2001, only Minnesota had a renewable mandate in place. It was anticipated that the passage of a federal RFS program mandating 7.5 billion gallons of renewables by 2012 would eliminate the need for additional state mandates. However, just the opposite has occurred. Today four additional states have implemented (Hawaii) or enacted (Missouri, Montana and Washington) varying forms of mandates. Moreover, three other state legislatures have passed a mandate in at least one house and many others have actively considered such legislation.

Integrating ethanol into the gasoline marketplace is too important – and presents too many challenges – to be approached in an individual, state-by-state manner. In order to meet consumer fuel needs, we want to produce more, refine more, and distribute more – but state ethanol mandates would make this difficult. Ethanol cannot be moved by common carrier pipeline, as is more than 70 percent of U.S. oil products, and requires a long supply chain to serve consumers. That means a longer reaction time when problems occur. State ethanol mandates would significantly add to that reaction time. We oppose this patchwork approach, whose adverse impacts are felt most by individual gasoline consumers.

API opposes additional state renewable mandates for E-85, E-10 and biodiesel and other state fuel requirements that undercut the flexibility that Congress provided in the national RFS program. As with any other boutique, they may also interfere with the reliable supply of fuels and contribute to price volatility when supplies of either gasoline or ethanol are tight.

As an example, state mandates for E10 are likely to cause the following refinery and distribution system problems:

- A per gallon mandate requires that E10 be available at all times. Thus, a shortage of ethanol for any reason means that gasoline could not be sold.

- Refiners may need to produce a low RVP blendstock (BOB) for conventional gasoline if the governor has chosen to eliminate the 1 pound waiver or if the state has a low rvp fuel requirement.
- A BOB may also be warranted to ensure that finished gasoline meets applicable ASTM volatility requirements and to provide adequate vehicle drivability.
- For areas requiring RFG, refiners would be required to produce a lower RVP blend of RFG, i.e. RBOB, for blending with ethanol. While most are choosing to do this now, it is possible that in the future some will choose to produce RFG with no oxygenates. This would not be possible in a mandate state.

The EPACT05 boutique fuels provision should be extended to include state renewable mandates. Given the existence of a federal Renewable Fuels Standard mandating the use of a minimum volume of biofuels each year, and a trading program intended to provide flexibility in where the biofuels are used, all state biofuel mandates should be federally preempted. Existing state biofuel mandates should become subject to review by EPA and DOE to determine whether they are likely to (or have) adversely impact the supply of fuel to the mandated area, or surrounding areas.

To avoid the fungibility issues that now plague gasoline, API also recommends that diesel fuel types should be limited to California diesel and federal diesel. The diesel distribution system will be under stress for several years as the federal diesel sulfur reduction program proceeds. Fungibility is critical for the successful distribution of diesel fuel and boutique diesel fuels must be avoided.

In 2002, in response to EPA's Boutique Fuels White Paper, API recommended adoption of five gasoline fuels as follows:

- California CBG for use in California;
- Federal RFG or Cleaner Burning Gasoline (CBG) with no mandated oxygen content, meeting either a 6.8 psi RVP cap or the current southern grade RFG VOC performance standard;
- 9.0 psi conventional gasoline (CG);
- 7.8 psi CG; and
- 7.0 psi CG.