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Driving Trucking's Success

Bill Graves
President and Chief Executive Officer

May 18, 2006

The Honorable Stephen L. Johnson
Administrator
U.S. Environmental Protection Agency
Washington, D.C. 20460

Re: Governors' Task Force on Boutique Fuels -- Statement of Governor Bill Graves, President and Chief Executive Officer, American Trucking Associations, Inc.

Dear Administrator Johnson,

The American Trucking Associations (ATA) appreciates the opportunity to address this task force concerning the adverse impact of boutique *diesel* fuels on the trucking industry. ATA is a federation of motor carriers, state trucking associations, and national trucking conferences created to promote and protect the interests of the trucking industry. ATA's membership includes trucking companies and industry suppliers of equipment and services. Directly and through its affiliated organizations, ATA encompasses over 37,000 companies and every type and class of motor carrier operation.

Concerns about fuel supply, rising fuel prices, and the proliferation of boutique fuels often focus upon gasoline, but the impact that boutique diesel fuels have on the trucking industry and the U.S. economy must not be underestimated. While gasoline moves people, diesel fuel moves the economy.

BACKGROUND

The trucking industry is the lynchpin of the transportation system, hauling nearly 70% of all the domestic freight transportation tonnage in the United States and accounting for more than 80% of the nation's freight bill. Over 80% of the communities in the U.S. receive their goods exclusively from trucks. Trucking also accounts for over 70% of the value of trade between the U.S. and Mexico and Canada. Simply put, without the trucking industry, the U.S. economy would come to a grinding halt.

Diesel fuel is the lifeblood of the trucking industry. For most trucking companies diesel fuel is their second largest expense, after labor, and accounts for up to 20 to 25 percent of their total operating expenses. Typically, the smaller the carrier, the larger percentage fuel represents of total operating expenses. The motor carrier industry is

comprised of thousands of small carriers. According to the Federal Motor Carrier Safety Administration (FMCSA), as of August 2005, 96% of the 564,000 interstate motor carriers operated fewer than 20 trucks.

The trucking industry consumes 36 billion gallons of diesel fuel each year. Based on the U.S. Department of Energy's May 2006 price forecast, ATA projects that the trucking industry will spend over $98 billion in 2006, $10.6 billion more than last year and more than double the amount spent just four years ago. As such, diesel supply and the price of diesel fuel is of paramount importance to the trucking industry and the U.S. economy.

The proliferation of boutique diesel fuels is problematic for the trucking industry and our nation's economy. Boutique fuels stress an already overburdened fuel distribution system, exacerbate temporary fuel shortages, and result in higher and more volatile fuel prices.

A. Boutique Fuels Defined.

Most of the discussions of boutique fuels have focused upon the myriad of boutique gasoline blends. This statement, however, focuses upon boutique diesel fuels.

The definition of what constitutes a boutique diesel fuel is critically important to the trucking industry and this task force. *A boutique fuel is any state-mandated fuel specification that prevents the sale of federally-compliant fuel within the state.*

Using this definition, there are presently three boutique diesel fuels in the United States:[1] (1) California's CARB diesel; (2) Texas' Low Emission Diesel; and (3) Minnesota's 2% biodiesel mandate. While only Texas' boutique fuel required EPA approval, each of these states have established unique diesel fuel specifications that effectively prevent fuel meeting the federal diesel fuel specifications (40 CFR Part 80) from being transported into and sold within the state. Thus, each of these states have prevented the fungibility of diesel fuel and isolated their diesel fuel markets from competition.

B. Boutique Fuels Harm the Trucking Industry.

Boutique diesel fuel mandates harm the trucking industry by artificially increasing fuel costs and preventing diesel fuel from simply being transported from one jurisdiction

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[1] Washington recently enacted a biodiesel mandate; however, this boutique fuel mandate does not take effect until 2008. We are aware of several other states that are considering boutique biodiesel mandates.

to another in times of shortage. While the trucking industry may pass along some of the added fuel costs to shippers (which ultimately impacts consumers), frequently not all such costs are recouped by motor carriers.

Due to their limited markets, boutique fuels typically are produced by only a handful of refineries, which results in less competition and higher fuel prices. California, which requires a boutique diesel fuel, provides a perfect example of this principle. The state's CARB-diesel is a specially formulated diesel fuel with a higher cetane index and lower aromatic content than the federal diesel fuel specifications. Using the Energy Information Administration's price data, since 1998, after accounting for tax differentials and deducting 5 cents to account for the higher production costs of CARB-diesel, the California diesel price has averaged more than 4 cents higher than the national average price. This difference is most likely explained by higher distribution costs and the oligopolistic pricing associated with boutique fuels. This price differential has been as high as 40 cents per gallon and as of May 15, 2006, the price differential was over 8 cents.

State biodiesel mandates also distort the free market and allow biodiesel producers to charge more for their mandated product. Appendix A to this statement sets forth a sensible approach to biodiesel.

The price disparity that results from state-mandated boutique fuel blends hurts the trucking industry by creating an uneven playing field and causing damaging fuel price spikes. Due to the competitive nature of the trucking industry, which has average operating margins of only two to four percent, a sudden increase in the price of diesel fuel turns a marginally profitable truck route into an unprofitable one. Moreover, the companies located within the boutique fuel jurisdiction have an economic incentive to refuel their trucks outside the jurisdiction, resulting in additional vehicle miles traveled, additional fuel consumed, and additional air emissions.

C. Responses to Questions Presented

In your invitation, you asked ATA to respond to five specific questions concerning EPA's 2001 *Study of Unique Gasoline Fuel Blends ("Boutique Fuels"), Effects on Fuel Supply and Distribution and Potential Improvements*. The EPA study focused exclusively upon boutique gasoline and did not address our concerns with the proliferation of boutique diesel fuels. Our answers to the questions below focus upon the problems created by boutique diesel fuels.

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

Each of the four scenarios discussed in EPA's 2001 study focus on the problem of boutique gasoline: (1) three-fuel option; (2) two-fuel option; (3) a 49-state Federal fuel; and (4) a California fuel available nationwide. The trucking industry depends upon a plentiful, fungible supply of *diesel* fuel, which these options do not address.

The trucking industry, and the supply of on-road diesel fuel, would benefit from a single national diesel fuel standard. Due to the interstate nature of the trucking industry and the need for an adequate supply of diesel fuel across jurisdictional lines, we believe that only one diesel fuel should be permitted, regardless of the solution selected to address the proliferation of boutique gasolines. Should improvements in the diesel fuel quality be deemed necessary, then those improvements should be required federally, rather than on a state-by-state basis. We encourage EPA and DOE to analyze the option of a national diesel fuel standard.

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?*

Again, the 2001 study does not address diesel fuel; however, the issues of fungibility, air quality and supply are critical to understanding the benefits and detriments of boutique diesel fuels.

The benefits of a fungible diesel supply and problems with boutique diesel fuels were discussed in section B, above. Fungibility ensures that localized diesel shortages can be addressed swiftly. Fungibility also maximizes competition in the refining of diesel fuel, ensuring that the price of diesel fuel is not artificially inflated by markets that have only a few refineries capable of producing diesel fuel.

In light of the transition to ultra low sulfur diesel fuel and EPA's stringent heavy-duty diesel engine emissions standards, which took effect in 2002, there is little reason to permit alternate diesel fuel formulations for on-road diesel fuel. The air quality benefits from alternate diesel fuel formulations are insignificant in new on-road engines and the improvements in the federal diesel formulation from the transition to ultra-low sulfur diesel fuel, render California's and Texas' boutique fuel environmental benefits *de minimis*.

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

The EPA study did not address the four factors as they relate to *diesel* fuel. Understanding the production costs, impact upon supply, effect of reduced fungibility, effects on air quality, and impact upon the end-users (cost, operability and safety) are critically important and will lead to the conclusion that there should be a single national diesel fuel standard.

On the issue of cost, boutique diesel fuels cost more to manufacture and distribute than the dominant federal diesel fuel. These additional costs stem from specific refining techniques or the use of required diesel additives, as well as the costs associated with the distribution and storage of an additional grade of diesel fuel (*e.g.*, shipment of smaller batches, additional storage tanks, and pipeline restrictions). Most significantly, analysis of the increased cost of boutique diesels must include the additional profits that flow to the limited number of refineries that participate in the boutique fuel market. In light of the increased refinery margins, it is not surprising that many refineries support the use of boutique fuels as a clean air strategy. The trucking industry is comprised of primarily small businesses with relatively slim profit margins. Rapid escalations in the price of diesel fuel from boutique fuel supply disruptions, are difficult to pass-on and will result in business failures, lower capital investment, and negative employment trends.

The impact upon overall supply also must be studied. While some boutique fuels reduce refinery throughput and limit the overall supply of diesel fuel (*e.g.*, CARB-diesel, Texas LED); others are manufactured with the use of additives (*e.g.,* biodiesel) that may actually help to extend the supply of diesel fuel, provided that there is an uninterrupted supply of the required additive.

In all cases, the effect of state-mandated boutique fuels is a reduction in fuel fungibility between jurisdictions. As a result, boutique fuels exacerbate temporary supply shortages by preventing the market from allocating additional fuel to the local jurisdiction experiencing the shortage. Diesel fuel, like other commodities, is subject to the laws of supply and demand. Reduced fungibility prevents an efficient market response to temporary supply shortages and often results in dramatic price spikes that are detrimental to the trucking industry.

An analysis of the impact on air quality also is critical to an evaluation of boutique fuels. Since 2002, heavy duty diesel trucks have been subject to stringent emissions standards. There is little or no environmental benefit from burning boutique diesel fuels in these low-emitting vehicles. Next month, the country will begin the transition to ultra low sulfur diesel (ULSD). This transition to a cleaner burning diesel fuel will further reduce the air quality benefits derived from boutique diesel fuels. In addition to analyzing the emissions benefits of a boutique diesel fuel compared to ULSD, EPA also must consider the fact that the primary consumer of diesel fuel is the interstate trucking industry. As part of a highly-competitive industry, truck owners logically seek to reduce their expenses from fuel purchases. Because every penny counts, many motor carriers utilize data mining software and wireless technologies to inform the drivers where to refuel based on the current price of diesel at numerous alternative locations. As a result, many truck owners will choose to refuel their vehicles outside of the boutique fuel jurisdiction to maximize profits. Indeed, some truck owners actually will travel additional vehicle miles to refuel their trucks outside the boutique fuel jurisdiction as a cost savings measure. These additional vehicle miles increase total emissions and may present additional safety and security issues.

Additional data on the impact of a boutique fuel upon the end-user is critical to an understanding of the boutique diesel issue. This subject is discussed in response to question 5, below.

4. *What impact do state boutique fuels have on your station operations?*

Many trucking companies are centrally refueled and operate their own refueling stations. The primary impact of boutique fuels upon these operations is increased costs and potential supply disruptions. Certain boutique diesel fuels, however, can have operational impacts upon central-refueling stations. For example, a biodiesel mandate may require special care for biodiesel blending, including the need to install heaters or other mechanical devices to ensure a proper mixing of the blended fuel. Biodiesel also acts a solvent, which may require central refueling stations to change their storage tank fuel filters several times as the sediment in their tanks becomes dislodged by the biodiesel.

5. *What impact do state boutique fuels have on vehicle and engine operation?*

The introduction of state-mandated boutique fuels has resulted in unexpected adverse consequences for the operation of heavy duty trucks. For example, when California introduced its boutique fuel (CARB-diesel), the trucking industry was assured that the fuel would not create operational problems. This proved to be untrue, as numerous trucks suffered mechanical problems associated with the failure of engine seals and leaking O-rings.

Similarly, Minnesota's biodiesel mandate also created problems for the trucking industry as fuel filters became clogged and required replacement ahead of their regularly scheduled maintenance program. Some of the malfunctions were the result of poor quality biodiesel, some were due to biodiesel's reduced cold weather performance, and some were caused by the fact that biodiesel acts as a solvent and dislodges the sediment that naturally accumulated in truck fuel systems over time.

The bottom line is that the real world impact of the introduction of new diesel fuels cannot always be predicted accurately. Over-the-road trucks are particularly vulnerable to these operational challenges, since they often travel far from their base of operations and routine maintenance (*i.e.*, changing fuel filters) may be difficult to perform in between regularly scheduled vehicle check-ups.

CONCLUSION

We greatly appreciate the opportunity to educate the members of the Governors' Task Force on Boutique Fuels. We believe that this task force must distinguish between

boutique gasoline and boutique diesel fuels. Gasoline moves people, but diesel moves the economy.

It is critically important to the health of the trucking industry and the U.S. economy to ensure that there is a single national on-road diesel standard. A single national diesel fuel standard will limit the duration and magnitude of fuel price spikes, which are devastating to the economic health of the trucking industry. To the extent that certain fuel parameters can be adjusted to provide emissions benefits without compromising supply, these adjustments should take place at the federal level.

ATA looks forward to working with the EPA and the Task Force to address the problems created by boutique fuels. In that regard, if there are questions concerning boutique diesel fuels, please contact Richard Moskowitz at (703) 838-1910.

Sincerely yours,

Bill Graves

Appendix A

A Sensible Approach to Biodiesel

The high cost of petroleum-based diesel fuel, coupled with the desire to eliminate the United States' dependence upon foreign sources of oil has resulted in renewed interest in the production and use of biodiesel. Subject to the following caveats, the ATA supports the *voluntary* use of biodiesel in blends up to five percent as a means to help extend the nation's supply of diesel fuel and reduce particulate emissions in older vehicles:

- Any biodiesel used must be tested and certified to be in compliance with the American Society of Testing Materials (ASTM D 6751) standard.
- Biodiesel should not be used in blends exceeding five percent for on-road uses, and all finished blends must comply with the ASTM D 975 standard.
- All pumps dispensing biodiesel for on-road use should be properly labeled to indicate the amount of biodiesel in the blend.
- No state should be permitted to create a boutique fuel by mandating the use of biodiesel in on-road diesel fuel.

1. Ensuring Biodiesel Quality is Critical.

The recent experience in Minnesota (the only state with a biodiesel mandate) highlights the need to enact federal requirements that ensure that biodiesel used in on-road engines complies with the ASTM specifications and does not cause operational difficulties for over the road trucks. Earlier this year, shortcuts taken by certain biodiesel producers resulted in a biodiesel that did not meet the ASTM specifications. This poor quality fuel found its way into the on-road diesel supply and caused numerous trucks to malfunction and become stranded. To prevent this situation from being repeated, government must require all biodiesel used in on-road engines to be tested and certified to be in compliance with the ASTM D 6751 standard.

2. Biodiesel Blends Should be Limited to 5% for On-Road Use.

Low percentage blends of biodiesel that meet the ASTM specifications should perform comparably to today's petroleum based diesel fuel. However, blends exceeding 5% present operational challenges for the trucking industry.

- High percentage blends of biodiesel could create difficulties with manufacturer warranty claims – most heavy-duty truck engine manufacturers do not recommend biodiesel in blends exceeding 5%.
- High percentage blends of biodiesel gel at a higher temperature than petroleum-based diesel and may cause trucks to become stranded in cold weather.

- High percentage blends of biodiesel have a lower energy value, requiring more fuel to be purchased to perform an equivalent amount of work.
- Biodiesel acts like a solvent and will dislodge sediment that accumulates in truck fuel systems, requiring a fuel filter change in advance of regularly scheduled maintenance.

It is important to distinguish between off-road diesel fuel, which is used in vehicles that do not travel far from their base of operations, and on-road diesel fuel, which is used by the commercial trucking industry for vehicles that travel hundreds of miles away from their base of operations. Cold weather performance and unscheduled fuel filter changes are manageable issues for most off-road engine applications; while over-the-road trucks using on-road diesel fuel may have difficulty overcoming the operational challenges presented by biodiesel blends that exceed 5%.

3. High Percentage Biodiesel Blends are Not Necessary to Support the Biodiesel Industry.

Last year the trucking industry consumed more than 36 *billion* gallons of diesel fuel. Other modes and off road engines also consumed billions of gallons of diesel fuel. In 2005, the biodiesel industry produced only 75 *million* gallons (0.2% of the total on-road diesel fuel used by the trucking industry). This year the biodiesel industry is expected to produce 150 million gallons (0.4% of the on-road diesel fuel used by the trucking industry). With the continuation of financial incentives, the biodiesel industry may reach a billion gallons by 2015, but even at a billion gallons biodiesel would account for only a few percentage points of the diesel fuel consumed by the trucking industry alone. As such, there is no reason to allow blends of biodiesel that exceed 5%.* A 5% cap on biodiesel blends will protect the trucking industry from operational problems and will ensure that the biodiesel industry can continue to grow for many years to come.

4. On-Road Diesel Pumps Should be Labeled to Indicate the Amount of Biodiesel Being Used.

Presently there is no law requiring fuel dispensers to be labeled to indicate the quantity of biodiesel being used. This presents a problem for the consumer, who has no way of knowing whether they are refueling with a high percentage biodiesel blend that could present operational challenges (*e.g.*, cold weather performance issues) or result in difficulty with a future engine component warranty claim.

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* Higher percentage blends of biodiesel may be permitted for off-road vehicles and state and municipally-owned vehicles, which seldom travel far from their base of operation.

5. State Biodiesel Mandates Are Not Necessary and Should be Prohibited.

ATA remains opposed to state biodiesel mandates, which harm the trucking industry. EPA should prohibit states from enacting boutique biodiesel mandates. Generous federal (and state) tax incentives already make the cost of producing biodiesel less expensive than the cost of petroleum based diesel. State boutique biodiesel mandates are not necessary to ensure that there is a market for biodiesel. However, state boutique fuel mandates will harm the trucking industry.

- State biodiesel mandates distort the free market and allow biodiesel producers to charge more for their mandated product.

- Boutique biodiesel mandates preclude fuel fungibility between jurisdictions, which exacerbate temporary fuel shortages and may result in dramatic price spikes.

- Boutique fuels create artificial price differentials and an uneven playing field for the trucking industry.

- Boutique fuels create incentives for locally-based trucking companies to refuel outside the local jurisdiction, which results in more vehicle miles traveled, undermining environmental benefits and increasing traffic and safety concerns.