Findings on Hawaii Gasoline Prices and Policies

Presented to the

Hawaii Department of Business, Economic Development and Tourism

By the
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NATIONAL CONFERENCE *of* STATE LEGISLATURES

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The National Conference of State Legislatures is the bipartisan organization that serves the legislators and staffs of the states, commonwealths and territories.

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Executive Summary and Recommendations

The National Conference of State Legislatures presents this report at the request of the Hawaii Department of Business, Economic Development and Tourism (DBEDT) pursuant to requirements laid out in Act 77, Session Laws of Hawaii 2002. This report analyzes policies that Hawaii could pursue to reduce gasoline prices and the resources that the state would need to expend to carry out those policies. The list of policies available to the state is broad; this report focuses on a small number of policies.

In preparing this report, NCSL coordinated with Stillwater Associates, which is another consulting firm hired under separate contract by DBEDT. The two reports and their conclusions rest as separate documents.

This report concludes the following;

- Gasoline and petroleum products are critical to Hawaii—and probably more so than in many other states.

- Because gasoline and petroleum products are so important to Hawaii, the state is well-justified in expending effort on policies and regulations that will keep prices at reasonable levels and alert policymakers to situations when they exceed reasonable levels.

- Based on experience in other jurisdictions, if the State elects to pursue a strategy of monitoring and evaluating the market, it is likely that DBEDT will require three new staff with expertise in oil markets. The annual budget for such an effort amounts to approximately $250,000. Without the financial resources to devote to this effort, it is unlikely that DBEDT will be able to carry out the market monitoring and evaluation tasks.

- If the state pursues a strategy that requires periodic audits in addition to monitoring and evaluation, the costs increase substantially. Depending on the type of audits required, the budget will likely be either $475,000 or $639,000.

- The addition of an independent audit function is incompatible with the duties of DBEDT, which acts primarily as an economic development organization. Independence is key to the audit function; however, economic development agencies such as DBEDT typically work closely and in collaboration with businesses in the state.

- As detailed in the accompanying report by Stillwater Associates, the current price cap formula may lead to higher prices in some situations. The state may consider a range of other possibilities detailed in this report.

- Other states and jurisdictions have adopted policies to monitor or analyze gasoline prices, but no other state regulates gasoline prices. Two Canadian provinces and a number of Pacific island nations do regulate gasoline prices.

Based on the analysis prepared for this report, NCSL recommends that the state consider the following actions:

1a. If the state chooses to leave the gasoline price cap in place, Hawaii should revise the structure of the cap.

1b. If the state chooses to remove the gasoline price cap, consider the following measure.

- Remove permanent price caps but give the governor authority to apply price caps in certain situations.

1c. Whether the state chooses to remove the price cap or to leave the price cap in place, consider the following seven measures.

- Make market transparency a goal, giving industry and government the authority and duty to collect and disseminate data to identify specific trends and potential abuses of market power.
- Remove or revise the requirement that the DBEDT perform periodic audits.
- Provide a specific mechanism for funding state market monitoring, analysis, reporting and auditing.
- Remove lease rent cap.
- Remove divorcement requirements.
- Conduct a concentrated outreach program, in coordination with industry, to reduce unnecessary use of high-octane gasoline.
- Develop a single, integrated state energy plan.

2. The state should fund the appropriate agencies to perform analysis and audit functions.

Given the
1) Costs of implementing and enforcing a price cap;
2) Administrative challenges to implementing and enforcing a price cap;
3) Challenges associated with substituting a government-administered price regime for a market-based regime, and;
4) The conclusion of Stillwater Associates that the Hawaii gasoline market is competitive, with certain bottlenecks,

NCSL suggests that the state place greatest weight on consideration of 1b and 1c.

1. Background and Introduction

Hawaii's energy situation is unique among the 50 states for several reasons, not the least of which is the state's almost complete dependence on petroleum not only for its transportation energy sector but also for its electricity sector. Hawaii depends on imports to meet almost all its energy needs. This dependency, combined with other factors—such as inter-island transportation, high land prices and a number of regulations specific to Hawaii—has meant that gasoline prices in the state have tended to be among the most expensive in the nation. Although accusations of collusion and market control have remained unproven in the courts, many in the state remain suspicious that the market is, at the very least, not as price-efficient as it could be.

Hawaii's almost total dependence on imported oil for so much of its energy sector is unique within the United States. This dependence demonstrates, more than in any other state, the interdependence among energy markets. Circumstances that raise or reduce world oil prices affect gasoline pump prices in Hawaii just as they affect pump prices in the other 49 states. In Hawaii, however, they also affect electricity prices, since the electric company relies on oil to power its generators[1]. Other linkages between gasoline markets and the broader economy exist as well; refineries that produce gasoline for cars and fuel oil for power plants also produce jet fuel and asphalt for roads.

Hawaii's energy markets illustrate one integrated system. Policies that affect gasoline, or one variety of gasoline, affect other products as well; it is quite possible that, because the products are so closely linked, a gasoline price cap could have an inadvertent effect on fuel oil prices and the economics of the refineries that process crude oil into its many refined products.

It is for this reason that the policies surrounding oil markets—and gasoline prices in particular—are so important; policies that govern one energy product affect most other energy products in the state. This study, with that of Stillwater Associates, relies on this assumption of integration.

The report is divided in three sections: 1) a review of policy options that other jurisdictions employ, 2) policy options available to Hawaii, and 3) resources required to carry out the market oversight, monitoring, analysis and audit functions described in Act 77.

1. The other 49 states, by contrast, have gradually phased out almost all reliance on fuel oil for their power plants, and instead have diversified into a mix of coal, nuclear power, hydro electric power and, to an increasing extent, renewable energy and natural gas.

2. Policy Options

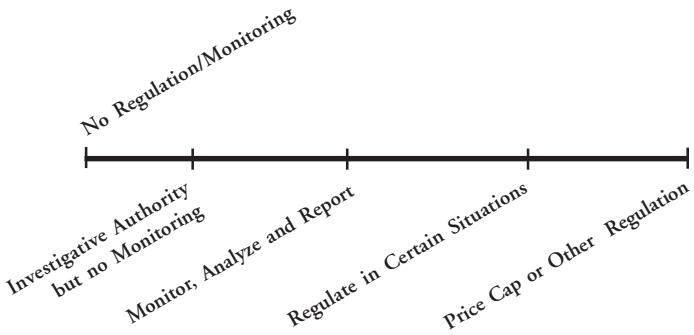
Hawaii has many policy options at its disposal that could influence gasoline prices. For the most part, these policies are not new; other states have tried them or currently have them in place.

It is possible to view the policies on a continuum that ranges from little or no government intervention in gasoline markets to one that exhibits a great deal of market intervention. Different policies are appropriate for each jurisdiction. What works best depends on the policymakers' assessment of the characteristics of the energy markets in that jurisdiction.

Petroleum and gasoline markets that demonstrate unexpected prices or prices that significantly differ from those in similar markets, given world oil market conditions, may require government intervention. Such government action would be justified by a demonstrated and proven assertion that the markets were not competitive and were unlikely to become competitive. Two provinces in Canada and a number of small Pacific island nations have decided that competition will not work in their markets and that price regulation is necessary. None of the other 49 states have made such a decision, although some have adopted other less intrusive policies to oversee gasoline and oil markets.

Figure 1 shows the continuum of policies described above.

Figure 1. Continuum of Policies



Source: NCSL, 2002.

Policies in Other States and Jurisdictions

This section reviews the policies that other jurisdictions employ. It uses the continuum as an organizational tool, showing first the policies that involve relatively limited government

intervention and then those that involve much greater government intervention in gasoline and energy markets.

No Regulation or Monitoring

The majority of states do not regulate gasoline prices in any way, nor do they have any formal monitoring system. As described earlier in this report, each state develops policies that are appropriate to its own situation. Hawaii cannot ignore the fact that it depends on oil more than any other state. As a result, it is legitimate that Hawaii take a more active role in oil markets.

Investigatory Authority but no Monitoring

Several states have policies that specifically empower the state attorney general to investigate anti-competitive gasoline pricing practices. These states do not offer quantitative standards that dictate when the attorney general may initiate such an investigation, or do they have ongoing studies or analysis of the oil industry in their states.

For example, Indiana enacted legislation in 2002 (IC 4-6-9.1) to prevent fuel price gouging during a state of emergency. If a retailer sells gasoline at a price that "grossly" exceeds the average price from the seven days prior to the state of emergency, the attorney general can investigate complaints and seek to levy or collect a civil penalty of up to $1,000 for each violation.

Monitor, Analyze and Report

One state—California—has an extensive program of monitoring, analysis and reporting on the petroleum industry. Another organization—the Pacific Island Forum—performs market analysis on behalf of a consortium of Pacific island nations. Michigan has recently begun price monitoring.

California

California maintains an active price and supply monitoring capability. This capability involves a greater level of effort than Hawaii would likely require. Still, it offers a model for Hawaii to consider on a smaller scale. No other state maintains an active market monitoring activity. Another organization—the Pacific Island Forum—also monitors oil markets and performs some analysis.

California's market monitoring function encompasses a broad array of activities, ranging from direct monitoring of prices to detailed analytical reports. The stated purpose of this activity is to ensure the state has a " … thorough understanding of the operations of the petroleum industry … to enable it to respond to shortages, oversupplies and to assess whether all consumers, including emergency service agencies, [government] and agricultural and business consumers … have adequate and economic supplies of fuel" (CA SB 1962, 2000). The audience for the California Energy Commission's work is threefold, consisting of the CEC itself, the governor and Legislature, and the general public.

The CEC has the power to allocate fuel to areas of the state that experience scarcity in times of emergency. (The state of Hawaii has similar authority, but without an equivalent monitoring and analysis capability [Chapter 125C. HRS]). One purpose of the analysis func-

tion is to be able to determine when such an emergency might occur. The CEC also uses its analysis capability to assist the governor and Legislature on major policy issues; it developed recommendations on the implications of and methods to phase out MTBE as a fuel additive, for instance. The CEC also attempts to reach the public through posting of fuel prices in order to promote transparency of markets.

The Transportation Fuel Supply and Demand Office monitors a variety of regional retail, wholesale, and spot prices of finished and unfinished petroleum products. Volume production and intrastate shipments also are tracked, with varying degrees of reporting timeline requirements. Generally speaking, gasoline and diesel retail prices and wholesale prices are tracked daily throughout various regions within the state. Spot gasoline and diesel prices are tracked in the two major trading markets of San Francisco and Los Angeles.

Crude oil, MTBE, ethanol and natural gas prices are followed on a weekly or daily basis from available subscription-based sources. Imports and exports of petroleum products also are tracked, along with refining capacities.

Refinery production and inventories are tracked on a weekly and monthly basis by refinery location. Pipeline shipments within the state are tracked weekly for each product type delivered.

Information Sources. The CEC gathers its data through a combination of three sources, involving data that are available from information that the CEC collects by law from industry, from subscriptions and from public sources.

1. By Law—Mandatory reporting of operations enables the California Energy Commission to collect a variety of proprietary information. Information submitted to federal agencies also is copied in care of the Energy Commission to satisfy reporting requirements.

2. By Subscription—Legislation requiring the Energy Commission to monitor retail and wholesale price changes is satisfied through mandatory reporting as indicated above and by purchasing subscription—based data services. The Energy Commission follows the Oil Price Information Service very closely.

3. From Public Sources—Other data collection falls under this category. Data is continually downloaded from Web sites that offer timely and accurate information. For example, the New York Mercantile Exchange offers daily historical close-of-business-day trading information, the *Wall Street Journal* covers Alaska North Slope crude oil prices, and the International Petroleum Exchange offers daily closing prices for its North Sea Brent crude oil forward contracts. Other Internet resources such as the federal Energy Information Administration offer historical and current data that is used by the Energy Commission.

Information Dissemination. To disseminate its information, the Energy Commission regularly updates a variety of Web site pages to display the latest data received from industry. For example, weekly refinery and production data is published on the Internet in such a way as to protect the individual refinery's data but to still present data for the state as a whole. Price data is disseminated in a similar way, sometimes through the use of graphs to protect the source.

Much of the information the CEC collects also is disseminated through other state agencies under confidential data-sharing agreements. All information shared in this way is first approved by the original respondent to ensure confidentiality.

Confidential information also is published in public reports, where aggregated summary data is presented. Such data also is made available on the Energy Commission's Web site or through the Energy Commission's publication.

Lessons from California. The California Energy Commission staff offered several lessons from their experience in monitoring, analyzing and reporting on the oil industry.

1. It is important to obtain a stable, long-term funding source to support staffing and program continuity. Fluctuations in state budgets can make it difficult to carry out roles and responsibilities when budget shortfalls occur. California's lack of stable funding has hindered the agency's efforts.

2. In addition to the contractors, any state agency that performs this analysis requires several staff with oil industry experience to provide a solid understanding of how the industry works. Such expertise may be very helpful in designing public policy strategies that are effective in responding to issues and for developing legislative proposals.

3. Securing contract dollars to obtain expert petroleum industry analysis also is critical for providing industry perspective and insight that may not be available in-house. California currently has a number of former oil industry personnel under contract who provide invaluable assistance on refinery operations, trading, marketing and product pricing. This expertise has been crucial in addressing the logistical issues facing California during the replacement of MTBE with ethanol.

Pacific Island Forum

The Pacific Island Forum was established to coordinate the work of 16 Pacific Island nations[1] and to carry out tasks that they could not do individually. One task that the forum performs is to monitor fuel prices for its members. The goals of the Pacific Island Forum's monitoring activity are to understand how regional fuel prices are changing, to increase awareness of prices in neighboring islands, and to highlight potential price discrepancies due to oil company abuse or other actions that may affect industries such as tourism or fishing. The forum monitors anomalies between gasoline prices among its members. If it notes anomalies, it notifies the member nation and may help it to craft a regulatory response. Fourteen of the forum's members regulate gasoline prices.

Michigan

In February 2003, Michigan Governor Jennifer Granholm ordered state officials to schedule statewide surveys of gasoline prices in an effort to prevent price gouging. Under the executive order, the state will give consumers pricing information, and any possibly unfair prices will be reported to the attorney general. The executive order discussed political situations in Venezuela and Iraq as factors, but focused on concerns about national security after Sept. 11, 2001.

1. The Pacific Island Forum consists of the following nations: Australia, the Cook Islands, the Federated States of Micronesia, Fiji, Kiribati, Nauru, New Zealand, Niue, Palau, Papua New Guinea, the Republic of the Marshall Islands, Samoa, the Solomon Islands, Tonga, Tuvalu and Vanuatu.

Senate Bill No. 560 (2001), which died in committee, would have required the state to establish a real-time database for gasoline terminal operators and retailers to report changes in the price of gasoline and diesel. The database would include a monthly report of prices charged by oil companies in Michigan. It also would compare fluctuations in wholesale and retail prices for the current month and the two months preceding. The database also would help the state surmise which oil companies might be setting 'the price to beat' in certain geographic areas. The responsible agency would submit an annual analysis of the data, along with recommendations about possible future trends in the pricing of gasoline and diesel.

Regulate in Certain Situations

Many states regulate their gasoline and petroleum markets: 1) in certain situations, or 2) to prevent limited types of abuse. States also regulate certain components of the business. Some of these policies are designed to support small business gasoline retailers, rather than to regulate prices. In some cases, these policies actually may have the effect of raising prices somewhat.

Refiner-retailer agreements

Some states have sought to regulate the relationship between refiner and retailer by setting standards for the agreements that govern this relationship.

- In Oregon, the franchiser cannot require a service station to operate more than 16 hours per day. Similar time-related statutes have been enacted in Georgia, Maryland, and the District of Columbia.

- Statutes in Georgia and Maryland prohibit refiners from requiring gas station operators to charge a certain price or to participate in promotional offers.

- In Connecticut and Georgia, refiners must sell gasoline at wholesale prices in reasonable quantities to retail distributors, whether they are independent companies or are wholly owned and operated by the refiner.

- Puerto Rico requires oil companies to treat all gas stations they supply equally. Each petroleum producer or refiner that supplies gasoline to service stations must provide any discounts, deductions or other price reductions uniformly and evenly to every service station. Similarly, suppliers must apply uniform rental fees for equipment and signs to every retailer they supply. During periods of supply shortage, producers and refiners must distribute proportionally, uniformly and equitably, and not discriminate among the service stations.

Advantages	Disadvantages
May help limit oil companies' control over retail prices. Prevents vertical integration of the industry.	It may be more efficient and economical for oil companies to also operate gas stations.

Selling gasoline below cost (predatory pricing)

Predatory pricing refers to the practice of selling gasoline below wholesale cost with the intent of forcing small, thinly capitalized businesses out of the market. Small-volume

dealers fear that they will be forced out of business while the large-volume stations and oil company-owned stations survive a period of lower prices because of their larger reserves of cash and capital.

- Several states have laws to prevent oil companies from selling at below cost to drive out competition. These states include Colorado, Florida, Georgia, Maine, Maryland, Massachusetts, Minnesota, Missouri, New Jersey, Pennsylvania, Tennessee, Utah and Wisconsin.

Sample Legislative Language from Massachusetts and Maryland

Massachusetts

Chapter 94: Section 295P.

Section 295P. No retail dealer shall, with intent to injure competitors or destroy substantially or lessen competition, advertise, offer to sell, or sell at retail motor fuel at less than cost to such retail dealer.

Maryland

Business Regulation § 10-304.1.

a) Except as provided in subsection b) of this section, a retail service station dealer may not sell motor fuel below cost.
b) A retail service station dealer may sell motor fuel below cost if the sale is:
    1) made in good faith to meet competition;
    2) made as part of a final liquidation or closing of the business of the retail service station dealer;
    3) made as part of a bona fide charitable promotion lasting no longer than two days; or
    4) made under the direction or order of a court or government entity.
c) If the Comptroller receives a complaint in writing that a retail service station dealer is selling motor fuel below cost, the Comptroller shall investigate and determine within three business days of the receipt of the complaint whether the allegations contained in the complaint are true.
d) The Comptroller shall issue a stop sale notice and may suspend or revoke the certificate of registration of a retail service station dealer if the Comptroller determines that the retail service station dealer is in violation of this section.

Advantages	Disadvantages
Encourages competition, especially by smaller retailers.	Sets a price barrier that does not allow consumers to benefit from very low prices.

Price gouging

A number of states have enacted laws to prohibit the opportunistic raising of prices during an emergency or supply shortage. These laws may apply only to gasoline or may apply to other products as well.

- Arkansas, California, Connecticut, Florida, Indiana, Louisiana and the District of Columbia have prohibited the raising of commodity prices during declared emergencies. Hawaii has similar authority.

Sample Legislative Language

Louisiana

§732. Price gouging; prohibited

A. During a state of emergency as declared by the governor or as declared by the parish president, the value received for goods and services sold within the designated emergency area may not exceed the prices ordinarily charged for comparable goods and services in the same market area at, or immediately before, the time of the state of emergency. However, the value received may include reasonable expenses and a charge for any attendant business risk, in addition to the cost of the goods and services which necessarily are incurred in procuring the goods and services during the state of emergency.

B. Each sale or offer for sale in violation of this Section constitutes a separate offense.

C. The penalties provided in R.S. 29:734 are in addition to civil remedies provided by law, including attorney's fees.

D. Local governing authorities may adopt appropriate ordinances to implement the provisions of this Section.

Acts 1993, No. 800, §1, eff. June 22, 1993.

Advantages	Disadvantages
Prevents oil companies from taking advantage of panic and fear that may accompany emergencies.	Some emergencies could lead to wholesale supply shortages, and retailers might not be able to recover their own higher costs.

Zone pricing

Oil companies often engage in a practice known as zone pricing, a practice that sets prices according to the geographic area and the nature of competitive forces in that area. These zones explain the varied gasoline prices throughout different neighborhoods in the same city. Some policymakers believe this practice is anticompetitive and discriminatory.

Several state legislatures have considered zone pricing restrictions, but it is important to note that none has passed. Most investigations into zone pricing have failed to prove illegal practice.

- Connecticut and New York have recently attempted to regulate or outlaw the practice of zone pricing for gasoline. In 1998, 1999, 2001 and 2002, Connecticut legislators proposed bills to monitor and/or regulate zone pricing. Each of the bills failed.

- Bills to prohibit zone pricing were filed in 1999, 2001 and 2003 in New York. The latest, SB 55, would fine gasoline retailers $5,000 for zone pricing violations.

- New York Senate Bill 963, which failed in the 2001 session, would have regulated marketing practices of motor fuel, refiners and distributors. The bill would have prohibited the imposition of inequitable prices to consumers by prohibiting refiners or distributors from selling motor fuel to any dealer at a price that exceeded 94 percent of the consumer retail price for the same fuel sold from a company-owned service station in the same area.

- In Maryland, an executive order mandated that a task force study the issue and provide a report with recommendations. The report found no illegal practices occurring in connection with zone pricing, but did recommend closer market monitoring.

Advantages	Disadvantages
May stop oil companies from targeting potential competitors by reducing gasoline prices in specific areas without lowering price throughout a broader marketing area. Also restricts refiners' ability to exercise market power.	The major oil companies have claimed that this differential pricing mechanism simply helps them meet the competitive situation in each zone.

In California, the Utility Consumers' Action Network (UCAN) requested that the federal trade commission conduct a study of zone pricing. Although UCAN found the uncompetitive practice of "price undercutting" in California, the three-year FTC report—which addressed the states of Arizona, California, Nevada, Oregon and Washington—found no evidence of conduct that violated antitrust laws.

Divorcement

In order to prevent oil companies from exercising too much control over retail gasoline prices, some states have enacted legislation to prevent the companies from owning or directly operating gas stations. In some cases, refiners may own stations but must maintain a minimum distance from other stations they own or from stations franchised by the company.

- Hawaii prohibited gasoline manufacturers from converting franchise-owned stations into refiner-owned stations after 1997. Hawaii also established lease-rent restrictions and established a minimum distance of one-eighth of a mile between new company operated retail service stations and dealer-operated retail service stations in an urban area. The prescribed distance is one-quarter mile in other areas.

- Connecticut, Maryland, the District of Columbia and Puerto Rico have laws prohibiting gasoline companies or refiners from owning or directly operating gasoline stations.

- Puerto Rico established a fine of between $5,000 and $25,000 for violation of the divorcement law.

- Nevada places a restriction on the number of service stations that can be directly operated by a refiner.

- Virginia establishes a minimum distance of 1.5 miles between a refiner-operated service station and one operated by a franchised dealer.

- Maryland statute specifies that, along the John F. Kennedy Memorial Highway, a sufficient number of stations operated by at least two different companies may be established in each service area along the highway. According to the statute, one person may not be awarded a lease for or have the use of more than one-half of the total number of stations on the entire highway. In addition, one supplier may not have the right to market fuel identified by its brand at more than one-half of the stations on the highway. The Maryland Transportation Authority is required to regulate the prices of fuel

products sold on the highway to the extent necessary to ensure reasonable costs to patrons.

Price Cap or Other Regulation

No state regulates gasoline prices to the extent Hawaii does, except in the limited ways described above. Only two provinces in North America regulate gasoline prices.

Newfoundland and Labrador, Canada

In 2001, the legislature established the Petroleum Products Pricing Commission (PPPC) to ensure fairness in the marketing and supply of petroleum products within the province. The commission establishes monthly maximum prices for all types of gasoline, home heating fuel, diesel and propane. Companies are allowed to sell below, but not above, the established prices. The monthly price is based on the average daily world prices for refined petroleum products during the previous month. A marketing margin is added that includes transportation and distribution costs, capital investment and infrastructure, sales volumes throughout the province, seasonal adjustments, and special circumstances such as isolated communities. The PPPC disseminates monthly price information to the public, the media, oil companies and townships via its Web site and fax. The commission provides some unofficial forecasting by monitoring industry data, watching petroleum inventories and staying abreast of current events. The commission also is responsible for monitoring compliance, and staff have the authority to issue tickets for violations.

Prince Edward Island, Canada

The Petroleum Products Act regulates the distribution and sale of petroleum products and ensures a "just and reasonable price" for heating and motor fuel within the province. The Island Regulatory and Appeals Commission (IRAC) uses a formula based on the New York harbor price of gasoline to set monthly prices for heating and motor fuels on the island. In addition, the commission also considers regional prices in nearby Nova Scotia and New Brunswick and uses its judgment, based on a detailed understanding of the industry and its costs, to determine the monthly price. IRAC is responsible for monitoring compliance and levying fines on any company that sells above the set price. The commission does not engage in any type or forecasting activity.

Maryland

Maryland regulates gasoline prices on one highway, through contract specifications. The Maryland Transportation Authority (MTA) has four service stations on the John F. Kennedy Memorial Highway. They are operated under contracts that include requirements for pricing of fuels. MTA contract language states that " … maximum retail prices for fuels shall be determined by the Baltimore Wholesale Price Average as determined by the publication Lundberg Letter plus State and federal taxes plus twenty-five (25) cents per gallon markup for full service. Self-service fuel shall be priced at a maximum as follows: Regular gasoline—five and one-half (5 ½) cents, Mid-grade gasoline—ten and one-half (10 ½) cents, Super gasoline—fifteen and one-half (15 ½) cents."

3. Policy Options for Hawaii

Hawaii has many policies at its disposal that could influence gasoline prices. Some of those policies derive from those in place in other states or countries. Others are variations on existing Hawaii law. The difficult task facing Hawaii state policymakers is to identify policies that will balance the oversight role of government with the implementation role of industry. Hawaii policymakers have the additional institutional challenge of assigning oversight roles to the appropriate state government agency or agencies based on the statutory charter policymakers have assigned. When industry appears to be operating in an economically inefficient manner, such policies may attempt to balance the need to encourage industry to make new and efficient investments with the government role. Inefficiency in this case may be measured by anomalous or unexplained market prices. Such prices could indicate that there is a lack of competition or that one company is exercising undue control over prices. Hawaii Act 77 sets out a policy of highly activist government control over prices, indicating a conclusion that the Hawaii gasoline market is not operating efficiently.

This report does not present an analysis of the Hawaii gasoline market. Instead, it seeks to set out a series of policies that are available to Hawaii that could influence gasoline prices. It builds on the conclusions of an accompanying report from Stillwater Associates, which presents an analysis of the Hawaii gasoline market. Stillwater Associates' report concludes that competition exists in Hawaii for the most part, with Maui and the Kona side of Big Island having infrastructure "bottlenecks." These bottlenecks interfere with competition. Stillwater's analysis has led to the conclusion that price caps are not needed. In addition, the Federal Trade Commission concluded in testimony to the legislature that "…(i)f the price controls in Act 77 become effective and succeed in reducing retail gasoline prices, they likely will impose significant non-price costs on customers." (Testimony of Jerry Ellig, Deputy Director, Office of Policy Planning, FTC, Before the State of Hawaii Joint Hearing, January 28, 2003.) Although a wide array of policies are available to Hawaii (listed in an appendix to this report) the following section focuses on those policies that, given Hawaii's unique situation, warrant particular attention.

This section is divided into two parts.

- Policy that is appropriate should the Legislature determine that the gasoline market is not competitive.

- Policies that assume the market works at least some of the time, or has potential to work efficiently.

Policy Appropriate to Non-Competitive Markets

This section highlights a policy that may be appropriate, should the Legislature deem the gasoline market to be non-competitive. This is one among a number of policies available, and is the policy that builds on existing Hawaii law.

1. Leave price cap in place but revise the formula to reflect market realities.

This option assumes, based on the accompanying report from Stillwater Associates, that a price cap based on using U.S. West Coast prices as a benchmark will produce prices in Hawaii that have little to do with current Hawaii supplies. For example, a refinery outage in California would raise prices in Hawaii, even though it had no physical effect on the Hawaii market, which secures its petroleum from Pacific Rim nations.

Adoption of this option assumes that Hawaii policymakers have concluded that competition is not feasible in the Hawaii context and that small numbers of those in the market that currently—and will in the future—exert undue influence over gasoline prices and supplies. This option would revise the price cap to reflect a benchmark that is not the U.S. West Coast, since Hawaii's gasoline market exhibits vastly different characteristics from the U.S. West Coast market. In essence, use of a West Coast benchmark forces Hawaii to import all of California's gasoline price characteristics and problems. It also would reexamine the pricing structure for neighbor islands. It might consider alternative pricing and price regulation models as well, such as those adopted in Prince Edward Island or in other Pacific islands. The following table summarizes the advantages and disadvantages of a price cap approach.

Advantages	Disadvantages
	Price caps rely heavily on a formula. That formula will inevitably affect the market and prices not only for gasoline, but also for other crude oil-based products in the state. A price cap may have unintended consequences.
A price cap is appropriate for a situation in which the market is consistently subject to manipulation.	Price caps rely on a benchmark that is not reflective of the Hawaii market, even if that benchmark is more appropriate than the West Coast price benchmark.
Addresses concerns about market power by placing pricing authority with government instead of with the market.	Price caps place the government, instead of industry, in charge of prices, partially removing market forces from the picture. Government may or may not do a better job of setting prices in a way that both encourages continuing investment in the industry while holding prices to a fair level.
	Price caps will discourage new suppliers from entering the Hawaii market or may push refiners out of the Hawaii market.
	Price caps may, in some situations, lead to shortages.

Policies Appropriate to Competitive or Non-Competitive Markets

This section reviews eight policies that Hawaii may consider whether or not the Legislature deems the gasoline market competitive. These policies may either enable or encourage competition, while building the state government capacity to monitor and evaluate gasoline markets.

1. Remove permanent price caps but give the governor authority to apply price caps in certain situations.

Price caps may be valuable as a threat or as a backup measure that the governor may impose under certain conditions. Legislation could give the governor authority to impose price caps under certain circumstances, including:

- Proven price manipulation;
- Proven supply manipulation; or
- Specific emergency situations that could result in either price or supply manipulation.

The price cap would be put in place upon specific recommendation from the attorney general. The attorney general would have responsibility for monitoring the gasoline market for abuse.

Such legislation would further clarify that any concerns about price manipulation or other illegal activity could be forwarded, with appropriate background material, to the Hawaii Attorney General's office.

2. Make market transparency a goal, giving industry and government the authority and duty to collect and disseminate data in order to identify specific trends and potential abuses of market power.

Act 77 set out a number of requirements to guide DBEDT in collecting industry data. DBEDT would use this data to monitor and analyze oil price and supply trends. Given the specific data requirements and needs for a gasoline market monitoring effort, it is likely that the specific requirements within Hawaii statute may need to be altered. The accompanying report by Stillwater Associates details specific data requirements that the Legislature may wish to consider adding to the statute.

3. Remove or revise the requirement that DBEDT perform periodic audits.

Act 77 required DBEDT to perform periodic audits of oil companies. This role is inconsistent with DBEDT's role as Hawaii's economic development agency, although it may be consistent with the role of a regulator operating in a price cap regime. An audit function may also be inconsistent with the needs of the State, should the state choose to eliminate the price cap. The audit requirement could be removed or revised in one of the following ways.

a. Remove the audit requirement entirely from statute.

   Removing the audit requirement from statute would mean that the state would be left with only with the subpoena authority granted through the courts, or the

power of police searches in cases of criminal misconduct. Such authority is useful only if the state suspects criminal activity.

b. Remove existing Act 77 audit requirement. Instead require the state to hire inspectors to enforce the price cap.

Hawaii law lays out two objectives for state audits of oil companies: whether the oil companies are 1) violating applicable policies, laws or rules; or 2) withholding supplies from the market.

The first objective represents a compliance function that asks DBEDT to ensure that companies are complying with the letter of the price cap law. If the price cap stays in place, this element of the audit function is also important, based on experience in other jurisdictions. This compliance function may best be situated in a regulatory agency such as the public utilities commission.

The second objective requires detailed investigation involving an understanding of world oil markets and oil refining and technology. Proof of withholding supply is difficult to ascertain and requires far greater analytical ability than currently exists in Hawaii—or any other—state government. As detailed later in this report, it will be expensive for the state to hire the staff to perform this function well. Hawaii should reconsider the need for this element of the audit function.

c. Place the audit requirement with a regulatory agency such as the utility commission or attorney general's office.

DBEDT was established to perform several functions, including policy analysis, planning and advising government and the private sector on energy policy issues. Hawaii has placed its energy function in the Economic Development Office—the office that works closely with industry to find ways to improve the business climate for industry in the state.

The law states that DBEDT now will be responsible for auditing oil businesses to determine if they are violating applicable laws (including the price cap law) as well as whether they are withholding fuel supplies from the market in order to drive up the price of fuel. This role was previously filled by the utility commission. Although the commission was not required to perform the audit function, it was given the option to audit oil companies.

In general, audit functions rely to a large degree on more distant relationships and independence. Auditors function best if they have minimal relationships with the firm under audit. Yet, as an economic development agency, DBEDT's role is to collaborate with business.

It will be difficult—and a contradictory role—for DBEDT to serve both as an independent auditor of business and as the business-friendly, collaborative agency. Because of this conflict, the Legislature should place the audit function with a different agency such as the utility commission because it operates more independently and at a greater distance from business.

To the extent that the state also hires inspectors to check for compliance with the cap, it also may be appropriate for those inspectors to be located within the regulatory agency.

d. Give authority to the state to perform audits, but make such authority optional and at the discretion of the state agency.

Rather than simply abandon the authority for a state agency to perform audits of oil companies, Hawaii could grant the authority to perform audits to an agency, but give the agency discretion as to whether to perform an audit. This leaves open the option for an audit in cases where state government deems it useful and appropriate.

4. Provide a specific mechanism for funding state market monitoring, analysis, reporting and auditing.

Provide specific funding commensurate with work required for a state agency to perform study, analysis, and investigatory or audit duties (as specified by law).

The state should establish a mechanism to fund the various agencies that perform audit, investigative and analysis functions. Similar to the fees assessed on utilities to fund state regulatory commissions and also modeled on a funding mechanism for a similar role used in Newfoundland and Labrador, industry could be charged a small throughput-based fee that would raise the funds necessary to perform the analysis and market oversight. This fee would support the efforts of DBEDT or another state entity charged with gasoline market oversight, analysis and/or regulation. The level of fee in Newfoundland is $0.0007 per liter.

5. Remove lease rent cap

Some states protect individual gas station operators by placing caps on the amount that station owners can charge tenants for rent. The amount often is based on a certain percentage of a station's total sales. Opponents of this policy argue that the property in Hawaii is much more valuable than the rent cap allows them to collect. Opponents also claim that lease rent caps decrease competition and create a disincentive for new suppliers to enter the market.

6. Remove divorcement requirements

Divorcement laws separate the wholesale and retail sectors of the gasoline industry by preventing refiners from operating the retail gasoline stations they own. Although this policy protects small, independent business owners who run the stations, some argue that it also inflates the price of gasoline and limits competition. A Federal Trade Commission Report from July 1999 concluded that divorcement laws raised the average price of regular, self-service gasoline by 2.7 cents per gallon in the states where such laws were in effect. This study included Hawaii, Connecticut, Delaware, Maryland, Nevada, Virginia and the District of Columbia.

7. Conduct a concentrated outreach program, in coordination with industry, to reduce unnecessary use of high-octane gasoline.

The octane rating of gasoline is the measure of a fuel's ability to burn under pressure. Many consumers wrongly assume that using a high-octane gasoline increases an engine's

power or gas mileage. In fact, most passenger vehicles require only low—octane gasoline and only a small percentage of high—performance engines benefit from the more expensive high-octane fuel. The price of premium gasoline typically is 25 cents to 35 cents higher than the price of regular grade gasoline. Education about the differences between regular and premium gasoline is important to helping customers save at the pump. A joint effort between the state and industry could help people determine whether they are unnecessarily paying for more expensive fuels that their vehicles do not require. State government could promote this information via public service announcements and websites, while the gasoline retailers could post signs at pumps.

8. Develop a single, integrated state energy plan

Hawaii, in particular, exhibits an integrated energy system in which the electricity sector is closely intertwined with gasoline and other petroleum products. A price cap that affects only gasoline will have unexpected effects on the remainder of the Hawaii energy market. Yet, the relatively high price of gasoline in Hawaii may be symptomatic of a broader need to reexamine a coordinated energy strategy in the state. Such a coordinated, integrated, long-term energy strategy is a long-term policy that should be viewed as distinct and supplemental to the other policies laid out in this document.

Stillwater Associates, in the accompanying report, describes several issues related to such a plan.

A long-term energy strategy would take into account the following.

- Feasibility of using liquefied natural gas to power electric generation facilities in parts of the state.
- Price volatility of natural gas and contractual mechanisms to hedge against higher prices.
- Policy issues surrounding reliance on imported natural gas compared to imported petroleum products.
- Energy security issues surrounding liquefied natural gas (LNG) terminals compared to security of existing energy infrastructure.
- Feasibility and cost of upgrading refineries in the state to be able to supply the supply-constrained California market.
- Air emissions benefits of converting power plants to natural gas.
- Role of energy efficiency in meeting energy needs of the state.
- Role of small-scale, distributed resources in meeting the energy needs of the state.
- Role of renewable energy resources in meeting the energy needs of the state.
- Role of government in making such a large-scale transition in the energy system.

4. Resources Needed to Carry Out Act 77 Requirements

Act 77[1] set up a mechanism to oversee, monitor, analyze and audit the Hawaii petroleum industry. The requirements delegated several of functions to the Hawaii Department of Business, Economic Development and Tourism, as described below, and some to the utilities commission. Many of these functions are similar to those that other jurisdictions employ. This section evaluates the personnel and financial resources that would be required if DBEDT were to carry out the requirements of Act 77.

This section makes the assumption that, as in the other jurisdictions that perform these duties, the state will earmark some limited but critical financial resources to carry out the policies that it adopts for overseeing gasoline markets. Funding for such financial resources could come either from the state general fund or from a fee-based revenue source based on a small cent-per-gallon charge for gasoline. Such a fee would likely be between $0.0007 and $0.0016 per gallon.

Requirements Currently in Hawaii Law

Act 77 places a number of specific requirements on the Hawaii Department of Business, Economic Development and Tourism. Broadly, these requirements fall into two categories: 1) data collection and analysis, and 2) periodic audits of oil companies. Hawaii law clearly specifies the types of information that it requires DBEDT to collect and analyze, and also clearly specifies to the kinds of activities that DBEDT should pursue in its audit function. Hawaii law now requires that DBEDT examine and analyze the following information.

Data Collection and Analysis Functions

- Nature, cause and extent of petroleum product shortages.
- Economic and environmental impacts of shortages.
- Industry forecasting methodology of petroleum product demand and supply.
- Prices and changes in prices at wholesale and retail.
- Income, expenses and profits before and after taxes of oil industry and firms within Hawaii. Compare data with other major industry groups.
- Emerging trends in supply, demand and conservation of petroleum.
- Nature and extent of efforts to expand refinery capacity and acquire more supply.

1. Session Laws of Hawaii (2002).

The law also requires DBEDT to disseminate the results of its analysis through a petroleum and petroleum products information system that it would develop.

In addition to the data collection and analysis function, the law requires that DBEDT assume a regulatory and enforcement role through the following tasks.

Regulatory and Enforcement Functions
- Conduct random audits and inspections to determine if companies are:
  - Withholding supplies from market.
  - Violating applicable policies, laws or rules.

Finally, the law requires that DBEDT submit an annual report detailing:

- Study conclusions,
- Civil penalties imposed, and
- Referral of violations to the attorney general.

This section is divided into two parts: 1) a brief review of resources in other jurisdictions, and 2) an analysis of resource requirements for Hawaii.

Resources in Other Jurisdictions

Two other organizations perform a market monitoring function: the California Energy Commission and the Pacific Island Forum. Their activities are not perfect analogies for what is proposed in Hawaii, but California, especially, is close. Newfoundland and Labrador, Canada, and Prince Edward Island, Canada, maintain a regulatory staff with some monitoring and enforcement functions. This section describes the resources that California, the Pacific Island Forum, Newfoundland and Labrador, Canada, and Prince Edward Island, Canada, devote to their respective activities.

California

The California Energy Commission's Transportation Fuel Supply and Demand Office has 19 people whose backgrounds range from three to 25 or more years with the commission. The staff are highly educated; several hold Ph.D. degrees in engineering, economics, geography or computer science.

The annual budget for the office is:

- Personnel: approximately $1,000,000 + benefits
- Contractual: $100,415
- Discretionary Operating: $31,665
- Student Assistant: $25,000

Pacific Island Forum

The Pacific Island Forum employs two full-time people to perform its monitoring function. A total budget of approximately $200,000 includes travel, staff, and other expenses such as data subscriptions. This monitoring function is somewhat more limited than the combination of monitoring and analysis functions laid out in Hawaii law.

Newfoundland and Prince Edward Island

Each of these two Canadian provinces supports commissions that monitor the prices of various petroleum products. The Petroleum Products Planning Commission monitors the price of motor fuels, heating oil and propane for the Newfoundland and Labrador province. Six full—time employees and one part-time consultant perform a variety of analytical duties. The positions in this office are as follows: Commissioner, Research Director, Research Officer, Financial Officer, Communications Officer, Information Officer and an Executive Assistant. These employees have a diverse range of analytical skills, including degrees in economics, business, computer science, public administration, journalism and education. The commission also is considering hiring another employee to perform audits and investigate allegations of abuse. The annual budget for this office, approximately $500,000 Canadian (approximately U.S. $340,000), is funded through a fuel tax of $0.0007 per liter.

The Island Regulatory and Appeals Commission (IRAC) regulates the price of petroleum products and distillates in the Canadian province of Prince Edward Island. This group has three full-time and six part-time commissioners who also work with public utility and land use issues. IRAC has a total of 18 staff members, three of whom specifically monitor petroleum prices. These three employees include an Assistant Director, a Research Analyst and a Field Inspector whose skills include research and technical analysis and experience working in the petroleum industry. Their salaries range from just above $30,000 to nearly $60,000, and the annual operating budget for IRAC is $450,000 (approximately U.S. $307,000).

	Prince Edward Island	Newfoundland
Population	135,294	512,930
Area (square miles)	2,038	133,380
Funding	General budget	.07 cent per liter fuel tax
Staffing	3 FTEs for fuel pricing	6 FTEs, half-time consultant
Budget	Approx. U.S. $307,000	Approx. U.S. $ 340,000

Source: Stillwater Associates, 2003.

Hawaii Resources Required

DBEDT will require dedicated staff and resources to fulfill the functions set out in the law. Several states and jurisdictions now maintain similar functions, and each is supported by dedicated funding. The activities currently contemplated by the law could not be achieved with existing staff and would require additional staff, with some budget for consultants and some for data and informational services (such as Platt's online oil price information).

DBEDT will require three types of resources to fulfill the functions of the law:

- Full-time technical, administrative and supervisory staff;
- Consultant resources; and
- Funding for expenses such as oil price data services.

Full-time staff will perform most functions and identify major issues or concerns. They will call in consultants as needed.

The following section describes in more detail the resources that the state would require to accomplish two tasks: a monitoring and analysis function or a combination of monitoring, analysis and auditing. These two options are highlighted in order to present a small selection of options for the state to pursue and also to better reflect the examples of activities taking place in other states (that focus primarily on either market monitoring or analysis and regulation, but not on an audit function).

Option 1. Monitors and report prices and market activity (like California or the Pacific Island Forum). This staffing level falls short of the Act 77 requirements.

Option 2. Monitor, report and also audit. This staffing level will meet requirements of Act 77.

Budget Implications for Hawaii

This section lays out scenarios through which Hawaii could accomplish the goals laid out in Act 77, or the goals of alternative policy measures. It is divided into three sections, as follows:

Option 1 reflects resources and staffing that Hawaii would require to accomplish a goal of market monitoring and analysis only. This task is based on an assessment of specific needs in Hawaii and on an adaptation of resources that California and the Pacific Island Forum have devoted to this task.

Option 2a reflects the resources described in *Option 1,* plus one additional staff (located within PUC) to set a price cap and inspectors (located within the PUC) to enforce the price cap.

Option 2b reflects the resources for both *Option 1* and *Option 2a,* plus resources to perform detailed audits of oil companies, as described in Act 77.

Option 1: Monitoring, Analysis and Reporting Only

If Hawaii pursues *Option 1*, to monitor and report on market activity only, it would require the following distinct activities:

Information gathering from:	Information analysis by:	Information dissemination through:
Paid subscription sources	Hawaii DBEDT staff with oil industry expertise	Electronic means
Information submitted per Hawaii law	Consultant resources as needed	Reports to the governor and Legislature
Public sources		

These tasks require expertise and understanding of the oil industry. It requires that DBEDT have on staff individuals with a background in data analysis, petroleum industry economics and research. These staff would rely to some extent on outside sources of information, such as Platt's, the Energy Information Administration and so on. They also would have the background and ability to analyze and process the large volumes of information submitted

to them under Hawaii law. Without this expertise on staff, DBEDT will be unlikely to take advantage of the information that it collects.

NCSL estimates that three full-time staff will be required to perform these functions: two substantive staff plus administrative support:

- Economist,
- Research analyst, and
- Administrative assistant.

Based on NCSL's review of experience in California and the Pacific Island Forum and with the Federal Energy Regulatory Commission, and based on an analysis of current pay scales in Hawaii state government, the resources required in Hawaii for *Option 1* would be approximately $250,000 for three dedicated full-time staff, plus a consulting budget for occasional expert analysis of $75,000, and other expenses.

Option 1					
Expenses	**Item**	**# of FTE**	**Salary & Benefits**	**Category Total**	
Salary & Fringe Benefits					
	Economist	1	$ 67,845	$ 67,845	
	Research Analyst	1	$ 49,535	$ 49,535	
	Secretary	1	$ 35,245	$ 35,245	
Salary & Fringe Benefits Total				$152,625	
Consultant				75,000	
Other Expenses*				26,769	
Grand Total					**$ 254,394**

*Other expenses include estimates for office furniture, computer and related equipment, and subscription-based data services.

Option 2a and Option 2b: A function that monitors, reports and also audits and enforces price caps.

Act 77 requires that, in addition to monitoring the market and performing market analysis, DBEDT will:

- Conduct random audits and inspections to determine if [the oil companies] are:
  - Withholding supplies from market, and
  - Violating applicable policies, laws or rules.

No other state or jurisdiction maintains such a combination of data analysis, market monitoring and extensive audit functions. Newfoundland has an inspection and enforcement function, but has no extensive audit function. The Federal Energy Regulatory Commission (FERC) is the only other agency of government that appears to have established a comparable audit function. However, the differences between electricity and gasoline markets and the differences between national and single-state markets are such that the analogies are limited. The skill sets required for the FERC activity offer some guidance. However, few comparable situations exist from which to judge resources that would be required for the fairly extensive audit function described in Act 77.

The two audit functions described in Act 77 require two very different levels of expertise and personnel. Option 2a describes an audit function focused on compliance with the price cap. It relies on inspectors to enforce the cap.

Option 2a. Collect data, monitor, analyze, report and enforce compliance with the price cap.

An audit function that simply monitors for compliance with a price cap can rely on three inspectors to ensure that the retail gasoline stations, in particular, are complying with the price cap. Given the regulatory function of the PUC, it makes sense for these inspectors to be employed by the PUC. Experience from Newfoundland demonstrates that gasoline retailers tend to self-enforce the cap, often informing the province when competitors violate the cap. The province has hired or is in the process of hiring two inspectors to enforce the price regulation.

In addition, *Option 2a* requires an economist to set the price caps and to respond to industry questions about the price caps or, in some cases, to address technical issues that arise in setting the caps; this individual would likely be housed at the utilities commission.

This option also requires an economist to lead the market monitoring and analysis function at DBEDT. This function was described in Option 1 above.

The budget for *Option 2a* would be approximately $475,000, based on Hawaii state government pay scales, office equipment needs and a consulting budget of $75,000. As with *Option 1* above, this budget would be required for consulting expertise to assist in analysis of oil markets.

Option 2a					
Expenses	**Item**	**# of FTE**	**Salary & Benefits**	**Category total**	
Salary & Fringe Benefits					
	Economist	2	$ 67,845	$135,690	
	Research Analyst	1	$ 49,535	$ 49,535	
	Audit/Inspector Staff	3	$ 45,790	$137,371	
	Secretary	1	$ 35,245	$ 35,245	
Salary & Fringe Benefits Total				$357,841	
Consultant				$ 75,000	
Other Expenses*				$ 42,000	
Grand Total					**$ 474,841**

*Other expenses include estimates for office furniture, computer and related equipment, and subscription-based data services.

Option 2b: Collect data, monitor, analyze, report and audit not only for compliance but also for supply manipulation.

An audit function that both inspects retail locations to ensure that they comply with the cap and also performs detailed analysis and audits to determine if companies are withholding supplies from the market involves much more expertise, background and understanding of the economics of the international petroleum market, including the following.

- Petroleum economics and finance for an understanding of the economics of oil markets, including such issues as the interactions among different products (gasoline, fuel oil, diesel, jet fuel and so on), the interaction between in-state refineries and imported refined products, and so on.

- Chemical engineering, for an understanding of the products that certain types of refineries can produce, and investments and physical plant changes necessary to produce certain products, and the feasibility of selling certain products.

- Law, especially antitrust law.

- Auditing and data analysis to be able to systematically analyze the operations and economics of the companies under audit.

- Support staff and Web support.

The skill sets required to perform both audit functions and the price cap function will entail the following full—time and dedicated staff:

- Two economists, with background in petroleum economics and finance to perform analysis function (within DBEDT) and to set price caps (within the utility commission);

- Three inspectors at the PUC;

- Chemical engineer;

- Attorney; and

- Administrative support.

The budget for *Option 2b* would be approximately $639,000, based on Hawaii state government pay scales, office equipment needs and a consulting budget of $100,000. The consulting budget of $100,000 would be required for consulting expertise in case the full-time staff discover significant anomalies that require further expertise.

Option 2b					
Expenses	**Item**	**# of FTE**	**Salary & Benefits**	**Category total**	
Salary & Fringe Benefits					
	Economist	2	$ 67,845	$135,690	
	Research Analyst	1	$ 49,535	$ 49,535	
	Chemical Engineer	1	$ 67,845	$ 67,845	
	Attorney	1	$ 67,845	$ 67,845	
	Audit/Inspector Staff	3	$ 45,790	$137,371	
	Secretary	1	$ 35,245	$ 35,245	
Salary & Fringe Benefits Total				$ 493,531	
Consultant				$ 100,000	
Other Expenses*				$ 45,460	
Grand Total					**$ 638,991**

*Other expenses include estimates of office furniture, computer and related equipment, and subscription-based data services.

Paying for Options 1, 2a and 2b

Although the state may use general funds for the above activities, it may also adopt a variant on the Newfoundland model, which assesses a fee on oil companies based on fuel throughput. For each of the above options, the per-gallon fee would amount to the following, based on Hawaii's annual consumption of slightly less than 400 million gallons of gasoline:

Option 1: $0.0007 per gallon
Option 2a: $0.0012 per gallon
Option 2b: $0.0016 per gallon

5. List of Policy Options and Conclusions

1. **Leave price cap in place but revise benchmark to reflect market realities.**
   This option would revise the price cap to reflect a benchmark that is not a U.S. West Coast benchmark, since Hawaii does not import significant amounts of crude or refined products from California.

2. **Remove permanent price caps, but give the governor authority to apply price caps in certain situations.**

3. **Revise the requirements of 486J as follows:**

   - Revise the data gathering requirements for DBEDT

   - Remove the requirement that DBEDT perform periodic audits in one of the following ways:

     - Remove the audit requirement entirely from statute.

     - Place the audit requirement with a regulatory agency such as the utility commission or attorney general's office.

     - Revise the audit requirement to include compliance only with the requirements of the price cap statute; remove requirement that DBEDT or other state agency investigate for unnecessary creation of supply shortages.

     - Give authority to the state to perform audits, but make such authority optional and at the discretion of the state agency.

     - Provide specific funding commensurate with work required for a state agency to perform study, analysis, investigatory or audit duties (as specified through law).

     - Provide a specific mechanism for funding agency work.

   A mechanism could be developed that would charge industry a small throughput-based fee. This fee would support the efforts of DBEDT or another state entity charged with gasoline market oversight, analysis and/or regulation.

4. **Make market transparency a goal, giving industry and government the authority and duty of collecting and disseminating data in order to identify specific trends and potential abuses of market power.**

5. **Remove lease rent cap.**

6. **Remove divorcement requirements.**

7. **Conduct a concentrated outreach program, in coordination with industry, to reduce unnecessary use of high-octane gasoline.**

8. **Develop a single, integrated state energy plan.**

NCSL suggests that Hawaii place the greatest weight on policies 2 through 8.

Notes

1. Background and Introduction

1. The other 49 states, by contrast, have gradually phased out almost all reliance on fuel oil for their power plants, and instead have diversified into a mix of coal, nuclear power, hydro electric power and, to an increasing extent, renewable energy and natural gas.

2. Policy Options

1. The Pacific Island forum consists of the following nations: Australia, the Cook Islands, the Federated States of Micronesia, Fiji, Kiribati, Nauru, New Zealand, Niue, Palau, Papua New Guinea, the Republic of the Marshall Islands, Samoa, the Solomon Islands, Tonga, Tuvalu and Vanuatu.

5. List of Policy Options and Conclusions

1. NCSL focused on the policy options listed here as most feasible in the near- to medium-term. It is understood that other long-term approaches exist. These approaches include:

- Leave price cap in place but revise to better reflect neighbor island markets
- Expand price cap regulation of gasoline beyond regular grade gasoline to all grades.
- Continue to regulate gasoline prices but do so under a different mechanism.
- Place the state government in the gasoline wholesale business as a refined product importer.
- Place the state government in the gasoline wholesale business as an owner and operator of a refinery.