14700 Downey Avenue
P.O. Box 1418
Paramount, CA 90723
(562) 531-2060

December 15, 2010

Via Electronic Posting

Kevin Kennedy
California Air Resources Board
1001 I Street, P.O. Box 2815
Sacramento, CA 95812

Subject: CARB Proposed Regulation to Implement California Cap-and-Trade Program
Agenda Item 10-11-1
Comment List: capandtrade10

Dear Mr. Kennedy:

The Paramount Petroleum Corporation, and its parent, Alon USA Energy (Paramount) appreciate the opportunity to comment on the proposed Cap and Trade Regulation (Regulation). Paramount supports the use of cap and trade as a component of California's comprehensive plan to reduce greenhouse gas (GHG) emissions over direct command and control regulations that would otherwise be necessary. However, the Regulation, as proposed, does not make a distinction between large complex refineries and smaller simpler refining operations of the type owned and operated by Paramount. Small, non complex refineries are dramatically different from the larger complex refineries of major oil companies, and this difference needs to be acknowledged within the Regulation.

Throughout the staff report and backup documents, a unifying theme of the program is the promotion of the efficient production of a given product.. Paramount concurs that having lower carbon intensity associated with bringing a product to market should be rewarded within the cap and trade program. With some relatively minor changes, the Board can alter the proposed program to acknowledge the distinction between large and small refineries, and recognize that small refineries actually produce transportation fuels with the lowest greenhouse gas profile available.

Paramount Petroleum owns and operates three refineries in California. Its primary refinery is a 55,000 bpd facility located in Los Angeles County. The facility does not have sophisticated process units, so many of the products produced by the plant must be shipped to other non related refiners for further processing to turn the intermediate product into gasoline and other transportation fuel. In fact, due to its simplistic profile, the product stream produced by Paramount can be broken down into three categories. About a third of every barrel of crude run at the plant is converted to diesel fuel, jet fuel and gasoline for sale to all. A third of the product produced are intermediates, which is the product stream sold to major refiners for further processing. The final third of a

typical barrel is converted into asphalt, which is then used for road construction or roofing.

Major refiners do not produce asphalt because they have installed sophisticated equipment, such as cokers, that expend a lot of energy and produce large amounts of emissions in order to convert their asphalt type products into transportation fuel. Thus Paramount's product slate is produced with far less energy than the products manufactured by major refiners, and in addition, the majors convert, from a barrel of crude, a much higher percentage of their products into gas and other transportation fuels.

The recent purchase by Paramount and its parent of the former Big West refinery in Bakersfield was acquired in the hope of using that equipment to convert some of Paramount's intermediate products, currently sold to our competitors at distressed prices, into transportation fuel. The refinery will not be processing crude oil. Although not currently operating, when started, the Bakersfield facility will actually serve as an additional process unit for the product streams produced at Paramount, further complicating Paramount's compliance with the proposed cap and trade regulations. The third refinery owned by Paramount is the former Edgington Refinery located in Long Beach, CA. This facility has not been operating for about a year due to economic conditions.

Paramount is a member of WIRA, a trade association representing small and independent refiners on the West Coast and has been an active participant in CARB rulemakings for many years. WIRA is also submitting comments today. Paramount, on its own and through WIRA has met with CARB staff many times over the last few decades to remind CARB that small refiners are very different than the major oil refineries in the state. The Board's previous rulemakings have consistently acknowledged that small and independent refiners are an important pro competitive force in the market for petroleum products. Since Paramount and other WIRA members do not have the same access to capital or economies of scale or the integrated business of major oil companies, it is imperative that mechanisms within this new regulatory scheme not disadvantage the smaller players in the refining sector. It is also important for the Regulation to specifically acknowledge the inherent efficiencies of a simpler refining processes.

Paramount believes that in-state production of lower-carbon transportation fuels can be encouraged with the correct regulatory structure. It is with that general theme that we respectfully submit the following comments and recommendations:

More analysis of the refining sector is needed

Staff has acknowledged in the staff report and in recent meetings that many technical details still need to be analyzed with respect to the allocation distribution formula. It is currently unclear exactly how each of the benchmarking options proposed will affect Paramount. A fuller understanding of CARB proposals is needed before a conclusion can be reached.

WIRA is committed to working with CARB staff to resolve these technical issues and requests that the Board direct staff to continue these discussions with industry. Choosing

a specific benchmarking metric at this point, without further analysis, could put independent refiners at a disadvantage in the market. In addition, since these small refiners survive on very thin margins which are often non existent (unlike the majors, who make money on the production and marketing side of the business), so one mistake in CARB's regulatory program can lead to the quick demise of the few small refiners remaining in California.

Need to recognize the inherent efficiency of the smaller refiner

The larger and more complex the refinery, the greater the GHG emissions per gallon of transportation fuel produced.. Currently, small and large refiners are categorized the same throughout the Regulation. Staff should provide separate tiers within the Regulation or find other ways to distinguish between large and small refiners. This disaggregation would allow for a more tailored approach on the various aspects of the program, including benchmarking and leakage analysis.

Clarifications and modifications are needed to the free allocation methodology

Paramount agrees with WIRA and recommends clarifications and modifications to the free allocation methodology provided in Subsection 9 of the Regulation.

CARB needs to clarify how it would determine a facility "output" of a unit that is currently non-operational. The use of the term "unavailable data" is unclear. The Regulation should clarify that the calculation for annual average output not include time periods of non-operation. For example, Paramount purchased the Bakersfield Refinery out of bankruptcy. The facility was not operating at the time of its purchase, and will not start processing Paramount's feed streams until the second quarter 2011. With at least a full year of non operation, the staff needs to not burden this asset with allocations that result from its inactivity.

As mentioned above, the criteria for determining which benchmark to use for the refining sector, is not specified. Nor is it fully understood how each of the options would impact Paramount's refineries

Placing large and small refiners within the same category for leakage assistance may not be appropriate. Appendix K-Leakage Analysis specifically notes that the petroleum refining sector was aggregated for leakage analysis. WIRA requests that a separate leakage analysis be done for small refiners as they have unique circumstances.

Assumed cost pass through for allowance costs of transportation fuels is incorrect

The Regulation and staff report assert that the costs associated with allowance value of transportation fuels will be passed along to the consumer, thereby relieving the obligated party from bearing the burden of those costs. This assertion is incorrect for independent, non-vertically integrated refiners.

For consumers to see the additional carbon cost of the program and to adjust their behavior accordingly, a mechanism needs to be in place for those costs to be passed along directly. Relying on general market forces to adjust for the price of carbon is not sufficient when the marketplace includes such diverse players as importers, small refiners, large integrated exploration, refining and retail operations, speculators and others who have the ability to establish product price independent of actual production costs or market forces. Paramount recommends allowing for the cost of allowances to be specifically invoiced nearer the final point of sale.

Concern about third-party market participants and possible market manipulation

Paramount is also concerned about the ability of non-obligated party's to participate in California's carbon market. Speculators in the oil and gas markets have historically affected price and reduced the efficiency of the open market. Paramount recommends CARB limit the eligibility or participation, of non-obligated parties so that influence on the carbon market unassociated with manufacturing or production can be minimized.

Treatment of Biodiesel emissions

Paramount supports the staff position that GHG emissions associated with Biodiesel not be subject to an allowance obligation. This policy will continue to promote the development of non-fossil fuel based alternative fuels.

Penalty for untimely surrender of allowances

The severity of the penalty for untimely surrender of allowances should be re-evaluated. Subjecting an entity to both a monetary penalty and the requirement to surrender additional allowances is a double penalty for the same violation. In addition, the calculation methodology for monetary penalties should be limited. The current method, based on a per ton, per day violation, could generate disproportionate penalty amounts. As an example, a $10,000 fine for Paramount has a much greater impact than the same penalty assessed against a major oil company.

Built-in review of the program's effectiveness is needed

As with all new programs, especially one this complicated, it is necessary for regular reviews of it effectiveness. WIRA recommends the Regulation, or adopting resolution contain language requiring periodic public reviews by the Board on the various elements of the programs to ensure that it is working as intended and to evaluate any unintended consequences.

Definition of Greenhouse Gas needs to be amended

The reference to "hydrocarbons" within the definition of Greenhouse Gases in Section 95802(a)(84) needs to be removed.

In conclusion, Paramount wishes to recognize all the work staff has put into this very large and complex regulation and commends them on such a difficult task. But it is imperative for the Board to "get this right". Not only does this regulation affect the entire California economy, but it has the potential to be the model for other regions and states.

Paramount appreciates the opportunity to comment on the Cap and Trade Regulation.

Respectfully Submitted,

Steven Farkas
Vice President and General Counsel

cc: Craig Moyer, Esq.

Jon Constantino

Ed Juno, Vice President West Coast Refining