PARAMOUNT PETROLEUM

a subsidiary of ALON USA

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

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VIA ELECTRONIC POSTING
Comment List: CAP-TRADE-DRAFT-WS

Elizabeth Scheehle
Manager, Climate Change Program Development
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Subject: Alon USA and Paramount Petroleum Comments on August 13, 2013 Refinery Benchmarking Workshop

Ms. Scheehle:

Paramount Petroleum Corporation and its parent, Alon USA Energy Inc. (collectively, Alon), appreciated the presentation and discussion opportunity provided by the California Air Resources Board (CARB or Board) to walk through the very important issue of refinery benchmarking at the August 13, 2013 workshop in Sacramento. Alon owns and operates three smaller refineries in California-one in Kern County (Bakersfield) and two in Los Angeles County (Paramount and Edgington). We listened hopefully to the presentations by CARB and Solomon Associates, and participated in the question and answer session that included your technical consultant Ecofys. By the end of the workshop, it was clear that Board staff did not have any proposals to address the specific and unique technical and economic issues associated with small refining operations in California, especially those set up to produce asphalt. We remain hopeful that CARB will take into account workshop comments and those in this letter and rethink your approach.

The Cap and Trade Regulation and Discussion Draft amendments contain many provisions that directly impact Alon's ability to operate in California, but none affect the competitive balance more so than the treatment of small refiners under the Industrial Assistance Allocation Methodology, i.e. refinery benchmarking.

It is critical that the Cap-and-Trade program continue to recognize that not all refineries were created equal. This fact has been recognized historically in the development of California's clean fuel regulations, as well as in the currently adopted version of the Cap-and-Trade Regulation. Ensuring that new competitive imbalances are not introduced into California's transportation fuel market is an important outcome of these amendments. Any regulatory changes that affect these remaining market participants will have dramatic effects on

California consumers and possibly impact CARB's entire Green House Gas (GHG) program. It is with this focus that we respectfully submit these comments and recommendations.

Summary of Comments

1) Alon supports the continued use of multiple refinery benchmarks as the program transitions to a Complexity-Weighted Barrel (CWB) methodology. We recommend that CARB recognize that refinery size and complexity have a direct relationship to GHG emission profiles and that benchmarking dissimilar facilities against each other places a competitive disadvantage into the marketplace. This is also true under the CWB and therefore, the yet-to-be-established refinery benchmark(s) should reflect that there is more than one class or grouping of refineries in California.
2) Alon seeks recognition that Asphalt refineries are unique and therefore should be addressed accordingly within the regulation. The unique nature of Asphalt refiners can also be seen in technical issues associated with CWB factors such as the need to retain the offsite energy factor.
3) Alon opposes the amending of section 95891(d)(1)(B) as a retroactive change to the regulation.

Comment Details

1) Refinery benchmarking is a complicated and contentious undertaking. Alon respects the fact that there may not be a perfect solution to this issue, but seeks to ensure that whatever the final regulations, they reflect as best as they can the realities of the industry and that the program doesn't permanently disadvantage California's remaining smaller refineries.

   The current Cap-and-Trade Regulation contains a bifurcated methodology for the allocation of allowances to the refining sector. This recognition that not all refineries can be compared against each other is currently scheduled to disappear in 2015. The original allocation methodology sought a way to highlight the differences in refinery size and complexity and therefore had two separate benchmark methodologies (EII and Simple Barrel). Alon recognizes the need to move beyond the methodology used previously, but does not want to see a single benchmark established for the entire sector—a codification of an apples-to-oranges comparison.

   Neither the Discussion Draft, nor the staff proposal recognizes the differences between refineries. Alon will continue to highlight that smaller, less complex refineries are able to produce transportation fuels on a lower energy input per gallon basis, even though they are limited in both physical and economic ability to achieve the efficiency of larger refiners. This inability, which is inherent and was confirmed at the workshop by Solomon Associates, will become a permanent competitive disadvantage to California's smaller refiners. Such a disadvantage is not within the

direction to reduce leakage under the AB 32 program. Even your own consultant, Ecofys, states in their report that "it is known that the CWT approach is not suitable for smaller refineries". **Therefore, Alon does not support the use of a single performance benchmark.**

2) It is an unfortunate fact that California now imports the vast majority of its asphalt product from out of state via railcars, whereas in-state asphalt production has diminished significantly, almost to the zero level. This is an example of economic and emissions leakage that *has already* occurred since AB 32 was passed and the start of the Cap-and-Trade program.

   The issue of asphalt refiners and their potential emission leakage has been on the table and discussed for several years. When Alon reviewed the Discussion Draft, it first appeared that CARB had taken a step to address this problem with the addition of a new activity category in Table 8-1 which addressed Asphalt. But after receiving clarification that this new activity is intended only for asphalt batch plants, Alon was disappointed that CARB missed an opportunity to finally address this issue. Batch plants need to be located in the areas they serve, whereas refined asphalt product can be shipped in from faraway locations—with an increase in GHG transportation emissions. The true leakage risk is at the refinery level.

   At the August 13, 2013 workshop, CARB was asked a direct question about how asphalt refiners would be treated under the regulation. And again the answer was that they would be treated the same as a larger fuels-focused refinery. This is not an acceptable answer, from either a GHG perspective or an economic perspective. It completely disregards an entire in-state industry, and ignores the GHG emissions associated with transportation of asphalt binder into the state.

   We understand that CARB currently is studying leakage risks for various sectors and activities with the goal of further amending the Regulation at a later date. Alon recommends adding a new specific activity categorization for Asphalt Refineries in Table 8-1, as well as, the addition of a new asphalt benchmark. This result would be consistent with other industries that have product specific benchmarks, such as cement manufacturing. Without individual recognition, Asphalt refiners will otherwise be unfairly competing against BOTH larger refiners and cement manufacturers. **Alon recommends that CARB complete the ongoing leakage analysis and commit to the establishment of Asphalt-specific allocations factors and benchmark.**

   <u>Offsite Factor</u>

   An option was proposed to eliminate the Offsite energy and non-crude sensible heat components of Solomon's refinery CWB calculation. Although It is not known exactly how this elimination will impact the predictive ability (R^2) of this methodology, it will have a larger negative impact (lower CWB and lower predicted CO_2e) on smaller,

less complex and asphalt refineries. This is because smaller, less complex refineries have fewer process units than larger refiners, which means the non-process factors will make up a proportionately larger portion of the final CWB calculated.

Physically, this is because smaller, less complex refineries must produce either a #6 fuel oil or asphalt product that must be delivered to trucks at high temperatures in order to flow through pipes. This also means that product tanks require additional heating, with asphalt binder tanks being required to maintain temperatures of approximately 350F. Asphalt rail car unloading, blending and milling also requires considerably more heat and power than unloading and blending lighter refined products. This is a key requirement of the facility, event if it is not producing product.

Additionally, smaller, less complex refineries are more likely to have internally and externally generated non-crude streams that require additional sensible heat, since they have fewer opportunities to have a fully heat integrated refinery process and are more likely to have intermittent or sporadic processing.

The issues described above become very important when a refinery is not processing crude oil (e.g. extended turnaround or economically driven outage). At these times there are still energy consuming offsite activities (e.g., nitrogen blanketing, instrument air, boilers, flare, vapor recovery, environmental recovery wells, hydrocarbon movements, equipment monitoring and others) that must continue for personnel and public safety as well as equipment protection. These CO_2 emissions will not be predicted without an Offsite factor, which will result in an under allocation and further competitive disadvantages. If you have questions on this very specific issue, Alon is willing to sit down at anytime and walk through with you.

3) The First Compliance Period refinery benchmark was negotiated and finalized in 2011. For CARB to seek to amend a portion of the regulation that is currently being implemented is problematic on several levels[1]. Alon is opposed to such a change as it would have significant implications on our business and market plans through a retroactive change in regulatory policy. This is bad public policy, and has serious implications as to whether the industry can trust CARB to not retroactively alter other aspects of the regulatory scheme and or market place.

   Resolution 11-32 contained language directing CARB staff to look forward and potentially adjust the benchmark and allocation methodology for the next two compliance periods. This was specifically called out, and nowhere were staff directed to go back and change how the first compliance period was addressed under the regulation.

[1] Changes to the regulatory structure on which the regulated entities have relied upon to make business decisions may be a prohibited taking.

> "BE IT FURTHER RESOLVED that the Board directs the Executive Officer to continue to work with stakeholders to further develop the allowance allocation approach for the petroleum refining sector and associated activities in the *second and third compliance periods*. This evaluation should include additional analysis of the Carbon Weighted Tonne approach and treatment of hydrogen production, coke calcining, and other activities that may operate under a variety of ownership structures." (emphasis added)
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> Regulatory changes need to be forward-effective and not retroactive. This is especially true with market-based regulations. Decisions have been made will be rendered moot by these changes. **Alon opposes the changes to Section 95891(d).**

California has actively worked to keep the smaller refiners operational based on its accurate belief that the consumer is best served by active competition between refiners and that even small refiners can impact prices and can be a counter to aggressive pricing by major oil companies. The belief that small refineries are important to maintain competition has been historically accepted by CARB as evidenced by new fuel regulations adopted over the last twenty years, it would be a shame if AB 32 did not have a similar recognition.

All of Alon's facilities are currently operating in a severely reduced mode. But when they reemerge from this minimal operational state, they will face immediate and substantial issues associated with their cap and trade compliance obligation. The current allocation proposal, including the new changes to 95981(d) add an additional competitive burden to startup and continued operation. For the policy, technical and economic reasons stated above, Alon requests that CARB recognize and address the issues with grouping all refiners in one basket. Finally, Alon requests that any changes to the regulation only be forward effective so that business decisions made to comply with the existing rules can be honored.

If you have any questions on these comments, please contact Jon Costantino at 916-552-2365 (jcostantino@manatt.com) or Gary Grimes at 562-531-2060 (ggrimes@ppcla.com).

Respectfully submitted,

Glenn Clausen

Glenn Clausen
VP West Coast Refining

cc: Steve Cliff
Eileen Hlavka
Steve Piatek
Gary Grimes
Jon Costantino