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

Dr. Steve Cliff
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Subject: Alon USA and Paramount Petroleum Comments on July Discussion Draft Amendments to California's Cap-and-Trade Regulation

Dr. Cliff:

Paramount Petroleum Corporation and its parent, Alon USA Energy (collectively, Alon), appreciate the opportunity to comment on the potential amendments contained within the July Discussion Draft of California's Cap-and-Trade Regulation. Alon owns and operates three refineries in California-one in Kern County (Bakersfield) and two smaller ones in Los Angeles County (Paramount and Edgington). Through the years, Alon and CARB staff have been able to work through various issues surrounding this very complex program. Alon believes that in-state production of transportation fuels by smaller refinery operations is a necessary market element that can continue to exist so long as the correct regulatory mechanisms are in place. The Cap and Trade Regulation and draft amendments contain many provisions that directly impact Alon's ability to operate in California.

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. It is with this focus that we respectfully submit these comments and recommendations.

Summary of Comments

1) Alon supports the change in the Second Compliance Period's Industrial Assistance Factor (Table 8-1, Section 95870).
2) Alon supports the continued use of multiple refinery benchmarks. We recommend that CARB recognize in the upcoming refinery benchmarking efforts 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. The refinery benchmarks should reflect that there is more than one class or grouping of refineries in California (Table 9-1, Section 95891).
3) Alon recommends additional regulatory language to address the unique issues associated with operations that experience a prolonged or significant production slowdown (Sections 95802 and 95853).
4) Alon seeks recognition that severe leakage has already occurred with respect to asphalt production at California refineries. We recommend the addition of a specific activity categorization for Asphalt Refineries, and that it be placed in the High Leakage Risk Classification (Table 8-1, Section 95870).

Comment Details

1) Extending the First Compliance Period's Industrial Assistance Factor values through 2018 is an important amendment to insulate California's in-state refining industry from some of the effects of increased transportation fuel imports. The production and sale of transportation fuel in California is a competitive national and international business. Additional incremental costs associated with producing transportation fuels in California, such as refinery GHG emission costs, shrink the cost differential for imports. When those differences reach zero, significant emissions and economic leakage of the industry will occur. **Therefore, Alon supports the revised Industrial Assistance Factors in Table 8-1 for Petroleum Refineries.**

2) 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, reflect as best as they can the realities of the industry regulated to ensure the program doesn't permanently disadvantage California's remaining smaller refineries.

   The current Cap-and-Trade Regulation contains a bifurcated methodology for the free 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 EII 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.

The Discussion Draft has placeholder language until CARB can work through this issue. Alon will continue to actively participate in this process, including the August 13, 2013, workshop, and will continue to highlight that smaller, less complex refineries are able to produce transportation fuels on a lower energy input per gallon basis. This reality can be recognized through the continued use of the existing Simple Barrel benchmark for similarly classified refineries. **Alon does not support the use of a single performance benchmark.**

3) The Cap-and-Trade program operates on the fundamental assumption that compliance entities operate in a relatively steady state of operation. This is not always true. Due to economic or other circumstances beyond the control of a covered entity, production levels and, therefore, GHG emission levels can vary significantly and over a prolonged period of time.

   The revised allocation True Up provisions are intended to smooth out the routine and relatively minor production variances across the California economy. Alon supports the changes to the True Up provisions that allow for the use of limited allowance borrowing, but those provisions do not help when a facility has undergone a lengthy and significant slowdown and then seeks to again operate in California.

   Alon purchased its Bakersfield refinery out of Bankruptcy from the previous owner, Big West. Big West purchased this refinery to avoid its permanent shut down as proposed by the previous owner, Shell Oil. At the time of Shell's announcement regarding the refinery closure, the State of California, through Attorney General Jerry Brown's office, actively worked to keep the refinery open by convincing Shell to find a new owner that would continue the refinery's operation. The State's involvement was 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 is accepted by CARB as evidenced by the new fuel regulations adopted over the last twenty years.

   The Bakersfield facility is currently undergoing modifications that will enable it to again produce fuel for California, but in the meantime its operations have been minimized. When it reemerges from this reduced operational state, it will face an immediate and substantial issue associated with its cap and trade compliance obligation because the allocation methodology does not anticipate such a prolonged reduction in production. The allocation formula, including the new True Up provisions, simply do not have a mechanism to address such a situation. Regulatory language is attached to this letter to address this unusual and very limited situation. **Alon recommends inclusion of the attached additional language as a necessary fix to the regulation (Sections 95802 and**

95853).

4) 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 to almost zero. 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. 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.

   We understand that CARB currently is studying leakage risks for various sectors and activities with the goal of further amending Table 8-1 at a later date. Alon recommends adding a new specific activity categorization for Asphalt Refineries in Table 8-1, and that this new activity should be placed in the High Leakage Risk Classification. This result would be consistent with Cement Manufacturing's classification. Cement and asphalt are not only competing products, but they have very similar leakage risk profiles as bulk products.

   Because the assistance factors for the first compliance period have been extended, the timing of this issue is not as critical as it was, but we will continue to work to ensure CARB has full understanding of the asphalt refining industry and the pressure it faces from out-of-state producers.

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,

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310019471.1

Cap-and-Trade Regulation Amendment Request

General Information

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Submitted by: Jon Costantino

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Section

Primary section(s): Section 95802

Related section(s): 95853(d)

Amendment Request

Type of amendment: ☒ Policy ☐ Error ☐ Clarity

Reason for amendment: The Cap-and-Trade program operates on the fundamental assumption that compliance entities operate in a relatively steady state of operation. This is not always true. Due to economic or other circumstances beyond the control of a covered entity, production levels and, therefore, GHG emission levels can vary significantly and over a prolonged period of time. Alon recommends additional regulatory language to address the unique issues associated with operations that experience a prolonged or significant production slowdowns (Sections 95802 and 95853).

Additional information:

310017882.1

Suggested amendment:

§ 95802. Definitions.

(XX) "Significant and Prolonged Production Limitation" means a covered entity's GHG emissions during three consecutive calendar years, as reported and verified pursuant to MRR, are less than 20% of its emission inclusion level as specified in section 95812(b).

§ 95853. Calculation of Covered Entity's Triennial Compliance Obligation.

(d) A covered entity that initially exceeds the threshold in section 95812 in the second year of the first compliance period, ~~or~~ the third year of a later compliance period, *or resumed operations after a significant and prolonged production limitation* has a compliance obligation for its emissions that received a positive or qualified positive emissions data verification statement, or were assigned emissions pursuant to section 95131 of MRR for that year, but the entity's triennial compliance obligation for the current compliance period is not due the following year. Instead the entity's reported and verified or assigned emissions for this year will be added to the entity's triennial obligation for the subsequent compliance period.