



Regulatory Advisory

December 2011



Low Carbon Fuel Standard (LCFS) Supplemental Regulatory Advisory 10-04B

UPDATE ON LCFS LITIGATION

On December 29, 2011, the U.S. District Court for the Eastern District of California issued several rulings in the federal lawsuits challenging the LCFS. One of the court's rulings preliminarily enjoins the Air Resources Board (ARB or Board) from enforcing the regulation during the pendency of the litigation. While ARB intends to appeal these rulings and to seek an order staying the preliminary injunction, as long as the injunction remains in effect, ARB will respect the Court's ruling and withhold enforcement of the LCFS requirements, including enforcement of the requirements described in this supplemental regulatory advisory. In seeking a stay of the preliminary injunction, ARB will request an order that all requirements of the LCFS in 2011 and 2012 are enforceable for the entire period. Thus, to the extent that existing guidance issued by ARB is expiring or stakeholders or the Board has requested modifications to the regulation, ARB will continue its stakeholder and rulemaking processes. This includes the issuance of this advisory to provide guidance in response to stakeholder requests.

SCOPE

Subject to the limitation on enforcement noted above, the ARB is issuing a Supplemental Regulatory Advisory today, 10-04B ("Advisory 10-04B"), which goes into effect January 1, 2012. This Advisory 10-04B applies in conjunction with Supplemental Regulatory Advisory 10-04A ("Advisory 10-04A"), as described below, which was issued in July 2011 and is incorporated herein by reference. This Advisory 10-04B will remain in effect through December 31, 2012, unless otherwise superseded by a subsequent ARB regulatory action, advisory or notice.

BACKGROUND & OVERVIEW

In 2009, the California Air Resources Board (ARB or Board) approved for adoption the Low Carbon Fuel Standard (LCFS) regulation, which became fully effective in April 2010 and is codified at title 17, California Code of Regulations, sections 95480-95490. The regulatory text is available at <http://www.arb.ca.gov/regact/2009/lcfs09/lcfscombofinal.pdf>. The LCFS will reduce greenhouse gas emissions by reducing the carbon intensity of transportation fuels used in California by at least 10 percent by 2020. Carbon intensity (CI) is a measure of the GHG emissions associated with the various production, distribution, and use steps in the "lifecycle" of a transportation fuel.

In July 2011, the Board issued Advisory 10-04A to facilitate implementation of specific provisions in the LCFS. Among its provisions, Advisory 10-04A provided guidance to regulated parties pertaining to their use of transportation fuels in 2011 that are derived from high-carbon-intensity crude oil (HCICO). This Advisory 10-04B modifies and extends specific provisions in Advisory 10-04A.

On December 16, 2011, the Board considered staff's proposed amendments to the LCFS regulation, which were released for public review in October 2011. Among other things, the proposed amendments included refinements that, when fully adopted as final regulations, will significantly modify the LCFS provisions that address HCICOs. At the December 16th hearing, the Board considered the staff proposal and directed the Executive Officer to develop and adopt final regulations consistent with the proposed revisions. Accordingly, this Advisory 10-04B is intended to bridge the gap between the current regulatory provisions and, if finalized by the Executive Officer and approved by the Office of Administrative Law, the anticipated January 1, 2013, entry into force of the proposed amendments. A description of the effects of Advisory 10-04B delineated by calendar year is provided below:

For Calendar Year 2011

The provisions of Advisory 10-04A remain in full effect, and volumes of fuels and blendstocks derived from all crudes, including HCICOs and potential-HCICOs, which were delivered to California refiners between January 1, 2011, and December 31, 2011, must be accounted for in the 2011 annual credit balance calculation of each regulated party that produced fuels derived from crudes classified as HCICOs or potential HCICOs.

For Calendar Year 2012

Consistent with the anticipated modifications of the LCFS regulation, the use of HCICOs and potential-HCICOs (as defined under the existing regulation) delivered in 2012 will not be subjected to specific mitigation in 2012. It is anticipated that the current HCICO provisions will be replaced by a method that uses an annual California Average Crude CI approach to determine if there has been an increase in the average CI of crudes delivered or supplied to California refineries in 2012 over the CI of the crude mix delivered or supplied in the LCFS baseline year (2010). Under this approach, mitigation of any such increase will be required in 2014, if such an increase is determined to have occurred. Therefore, this Advisory 10-04B rescinds the provisions of Advisory 10-04A, pertaining to mitigation of the impact of HCICOs and potential-HCICOs delivered between January 1, 2012, and December 31, 2012, inclusive, on the annual credit balance calculation for 2012.

For Calendar Year 2013 and Subsequent Years

The provisions in the amended regulation shall apply, if the proposed amendments considered by the Board at the December 16, 2011, hearing are adopted pursuant to the Board's delegation to the Executive Officer and approved by the Office of Administrative Law.

DEFINITIONS

For purposes of this Advisory 10-04B, "we" means ARB, the Board, or ARB staff, and "Executive Officer" refers to the ARB Executive Officer or his or her designee. Also, "this advisory period" and "term of this Advisory" mean the period during which this Advisory 10-04B will remain in effect, which is January 1, 2012, through December 31, 2012, except as otherwise specified below or superseded by a subsequent ARB regulatory action, advisory, or notice. Unless otherwise stated, all references to "section" are to the LCFS regulation, and references to the "Lookup Table" are to one or both of the carbon intensity lookup tables in section 95486(b)(1) of the LCFS regulation.

ELECTRONIC REPORTING REQUIREMENTS

A. Current Action: Use of Generic CI Value for Ethanol and Biomass-Based Diesel

This Advisory 10-04B extends the guidance issued by ARB, as specified in Part A of the prior Advisory 10-04A, through the end of the term of this Advisory 10-04B.

B. Current Action: Use of Interim CI Value for HCICO-Related Reporting and Annual Credit Balances

For calendar years 2011 and 2012, no fuel or blendstock sold, supplied, or offered for sale in California during this advisory period (between January 1, 2011, and December 31, 2012) will be deemed in violation of the LCFS regulation solely because it was derived wholly or in part from non-HCICO, HCICO, or potential-HCICO.

This Advisory 10-04B extends a portion of the guidance issued by ARB, as specified in Part B of the prior Advisory 10-04A, through December 31, 2012. Accordingly, for purposes of reporting through the LCFS Reporting Tool (LRT) and in annual credit balance calculations, a regulated party may use through December 31, 2012, the baseline CI value of 95.86 g CO₂e/MJ for CARBOB or 94.71 g CO₂e/MJ for diesel fuel, whichever applies, irrespective of whether the fuel or blendstock was derived from a non-HCICO, a HCICO, or a potential-HCICO. This provision now applies to crude that is delivered or supplied to a California refinery by December 31, 2012, for producing CARBOB or diesel fuel. A regulated party operating under this guidance must maintain, and submit to the Executive Officer within 20 days after a written request, records of the volumes and crude marketing names (also known as "marketable crude oil name" or MCON) for all crudes delivered or supplied to that regulated party.

C. Current Action: Calculation and Treatment of Credits & Deficits for Fuels/Blendstocks Derived from Potentially High Carbon-Intensity Crude Oils in Calendar year 2011

While Part B above addresses the use of the baseline CI values for reporting and annual credit balance calculations for CARBOB and diesel fuels and blendstocks, this section clarifies the treatment of credits/deficits generated for a fuel pool in calendar years 2011 and 2012 that is comprised in some part of fuel/blendstock derived from potential-HCICO. Advisory 10-04A provided guidance on the actions ARB will take to address the calculation of credits and the treatment of incremental deficits due to HCICO and potential-HCICO in 2011. This Advisory 10-04B reaffirms that guidance for crudes delivered through December 31, 2011, but modifies the portion of Advisory 10-04A that would have affected crudes

delivered on or after January 1, 2012. The provisions in Advisory 10-04A applicable to HCICO and non-HCICO crudes remain unchanged for 2011. For potential-HCICOs in 2011, the three options provided in Advisory 10-04A will remain in effect during the term of this Advisory 10-04B, as follows:

A regulated party's annual credit balance for both 2011 and 2012 is to be calculated pursuant to section 95484(b)(2) and using the approach specified in Part B above. However, any credits generated during 2011 must be adjusted by the incremental deficits due to HCICO and potential-HCICO, as summarized in the table below. It should be noted that the process for adjusting 2011 net credits will be more fully specified in a subsequent advisory.

Incremental Deficits and Credit Adjustments for Products Derived from HCICO or Potential-HCICO in 2011

If a crude:	Then:	Therefore, the regulated party:
<ul style="list-style-type: none"> Determined to be a HCICO under Table 2, Advisory 10-04A 		<ul style="list-style-type: none"> must calculate its HCICO incremental deficits pursuant to section 95486(b)(2)(A)2.a. using either the CI value approved by the Executive Officer under Method 2B or the CI value determined by ARB staff analysis for the HCICO-derived product, and may use without restriction any credits remaining after the regulated party's 2011 annual credit balance has been adjusted with the incremental deficits.
<ul style="list-style-type: none"> Is neither a HCICO or a non-HCICO under Table 2, Advisory 10-04A 	<p>the crude is deemed to be a potential-HCICO</p>	<p>can choose one of the following options that apply only when its 2011 annual credit balance is positive (i.e. there is a net credit); if the balance is negative (i.e. there is a net deficit), that deficit must be carried over into 2012, for reconciliation in all cases.</p> <p><u>Option 1</u></p> <ul style="list-style-type: none"> Incremental HCICO deficits are set at zero; and No net credits for 2011 can be traded or transferred to 2012. <p><u>Option 2</u></p> <ul style="list-style-type: none"> A portion of any net credit for 2011, proportional to the regulated party's use of potential HCICO in its crude slate as specified below, must be set aside and kept in the regulated party's bank. That set aside portion cannot be accessed until the crude has been determined to be either non-HCICO or HCICO with a designated CI value, and adjusted as follows; <ul style="list-style-type: none"> If the crude is determined to be non-HCICO, there are no incremental deficits and no further adjustments are needed; If the crude is determined to be a HCICO, the crude's CI value is to be determined using a calculation or method posted by ARB for this purpose on its website; the CI for each such crude must be used to calculate incremental deficits pursuant to section 95486(b)(2)(A)2.a.; and the 2011 net credits must be adjusted accordingly; and Any net credit remaining after the above incremental deficit adjustment can be carried over to 2012 and beyond. <p><u>Option 3</u></p> <ul style="list-style-type: none"> The CI values of 107.79 gCO₂e/MJ for CARBOB and 106.64 gCO₂e/MJ for diesel fuel must be used to calculate incremental deficits pursuant to section 95486(b)(2)(A)2.a. and the 2011 and 2012 annual credit balances; and Any remaining 2011 net credits can be carried over into 2012 and beyond without restriction.

For Option 2 above, ARB staff expects to have the CIs determined for HCICOs and potential HCICOs by mid-2012; regulated parties will be allowed to reconcile, by the due date for 2012 annual compliance report, any deficits from 2011 calculated based on the CIs determined for HCICOs and potential HCICOs. The set-aside credits under Option 2 shall be the smaller of either the full amount of 2011 net credits or the amount of credits sufficient to fully offset an incremental deficit calculated assuming a CI of 20.0 g CO₂e/MJ for the crude production and transport step and the volume of potential HCICO delivered or supplied to the regulated party in 2011. Under no circumstances shall ARB be held liable for any change in value for any credits held in such accounts or for any other consequences related to or resulting from the holding of credits in such accounts.

As already provided in the LCFS regulation, a regulated party applying the above guidance to its credit/deficit calculation will need to keep and maintain adequate documentation to support its claimed volumes and CI of fuels/blendstocks. A regulated party operating under this guidance must maintain, and submit to the Executive Officer within 20 days after a written request, records of the volume (in gallons) and the MCON for each crude delivered or supplied to that regulated party.

FOR MORE INFORMATION

Currently, the LRT can be accessed at <https://ssl.arb.ca.gov/LCFSRT>, as specified in a listserv announcement on September 2, 2010. Other LRT-related materials can be accessed at: <http://www.arb.ca.gov/fuels/lcfs/workgroups/workgroups.htm>. The final regulation order and other rulemaking documents can be found in the LCFS rulemaking website at: <http://www.arb.ca.gov/regact/2009/lcfs09/lcfscombfinal.pdf>. For any questions regarding this supplemental advisory, please contact Mr. Floyd Vergara, Chief, Alternative Fuels Branch, at (916) 327-5986 or via email at fvergara@arb.ca.gov, or Mr. Mike Waugh, Chief, Transportation Fuels Branch, at (916) 322-6020 or via email at mwaugh@arb.ca.gov. If you need this document in an alternate format or language, please contact Mr. Stephen d'Esterhazy at (916) 323-7227 or sdesterh@arb.ca.gov. TTY/TDD/Speech to Speech users may dial 711 for the California Relay Service.