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June 14, 2013

Michelle Buffington
California Air Resources Board
Email: mbuffing@arb.ca.gov

Re: Potential Concepts to Further Incent Investment in Low-CI Fuels and Provide Additional Compliance Strategy Options

Dear Ms. Buffington:

On May 23, 2013 ARB released a White Paper containing five potential concepts to further incent investments in low-CI fuels and provide additional compliance strategy options. These five potential concepts are:

1. Credit Window Option;
2. Reinvestment Plan Option;
3. Credit Multiplier Option;
4. Credit Clearance Option; and,
5. Noncompliance Penalty.

Below, we provide our initial thoughts on these concepts. We encourage ARB to establish a work group to further develop the first two concepts. I look forward to participating on that work group.

I. Shell Generally Supports the Concept of Alternative Compliance Mechanisms But Believes They Are Not a Substitute For Feasible Standards

We generally support the concept of including additional compliance strategy provisions in the LCFS program. We do not believe, however, that such provisions are a substitute for establishing feasible standards in the first place. Thus, we urge ARB to reevaluate the standards and adjust them to ensure that they are in fact feasible.

Additional compliance strategy provisons are an important compliment to feasible standards. The LCFS by design attempts to predict the future in terms of the availability and consumer acceptance of low carbon fuels and vehicles. Such predictions will invariably need to be adjusted, as it is simply impossible to predict the future with the accuracy ARB attempts. The first two concepts can serve that purpose, while protecting consumers and the State's economy from the impact of infeasible standards.

II. The Alternative Compliance Mechanism Must Address the Fundamental Problem – Insufficient Credits – To Avoid Severe Adverse Impacts on Consumers and the State's Economy

Of the five potential concepts, we believe that only the first two – the Credit Window Option, and the Reinvestment Plan Option – are worthy of further consideration. The other three options do not address the fundamental problem created by the low carbon fuel standard – i.e., insufficient credits limiting the availability of gasoline and diesel in the State.

As explained in the attached May 6, 2011 letter, it is critical that ARB ensure that the standards are feasible at all times:

> One key aspect of the LCFS construct is that it links and ultimately limits the supply of petroleum-derived gasoline and diesel fuel to the availability of volumes of low carbon alternative fuels. Thus, if the actual volumes of low-carbon alternative fuels produced or imported to California are too low, the likely result will be reduced supply of gasoline and diesel fuel in the State. This could have significant adverse impacts on consumers and the State's economy.

In other words, the credits under the LCFS program are effectively permits to supply gasoline and diesel fuel for consumption in California. If there are insufficient credits, the result will be to limit supplies of both gasoline and diesel fuel. There is currently no other option for regulated parties to remain in compliance with the law. Therefore, as ARB considers the concepts in the White Paper, it is critical that ARB ensure that the solutions address the fundamental problem and ensure that there will be adequate credits.

Options 1 and 2 should be considered further because they provide a mechanism to ensure that there will not be a shortfall of credits. Options 3 and 4 might result in some additional credits being available, but there is no guarantee that the number of credits will be sufficient. Option 5 is not a solution at all. Option 5 is based on the premise that companies will knowingly violate the law and simply pay penalties. That will not be the case. The likely outcome under Option 5 is that companies will comply with the law and ultimately supplies of gasoline and diesel fuel in the State will be limited leading to potentially severe impacts on consumers and the economy. ARB should not even consider a provision that contemplates obligated parties knowingly violating the law as a potential solution to an infeasible standard.

III. Feasible Standards Combined With An Alternative Compliance Mechanism Can Provide Regulatory Certainty And Incentivize Investments in Low-CI Fuels

We understand that one of ARB's goals is to further incent investments in low-CI fuels. The first step toward increasing investor certainty is for ARB to adjust the standards to feasible levels. As it is, if ARB does not adjust the standards and simply requires obligated parties to purchase a large number of government issued credits, it will likely result in considerable criticism of the program which will undermine investor confidence. ARB should consider the example of EPA's use of cellulosic waiver credits under the Federal RFS program. For several years, EPA set the cellulosic renewable fuel standards at unrealistically high levels causing obligated parties to purchase cellulosic waiver credits from EPA. This ultimately led to wide-spread criticism of EPA for collecting fees for "phantom fuels." Fortunately, now EPA is attempting to set the cellulosic mandates at more realistic levels. If ARB continues to maintain the standards at infeasible levels, it will undoubtedly result in criticism of the program and undermine investor confidence.

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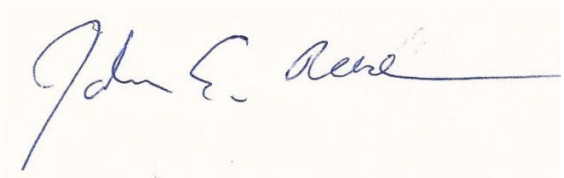
Shell appreciates the opportunity to comment on ARB's White Paper. If you should have any questions concerning these comments, please feel free to contact me at 713.230.5147 or John.Reese@Shell.com.

Sincerely,



John E. Reese
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