RENEWABLE FUELS ASSOCIATION

June 27, 2016

Jim Aguila
Air Resources Board
1001 I Street
Sacramento, CA 95814
Via email: LCFSWorkshop@arb.ca.gov

RE: Comments of the Renewable Fuels Association (RFA) on California Air Resources Board (ARB) Workshop Regarding Proposed Amendments to LCFS (June 2, 2016)

Dear Mr. Aguila,

The Renewable Fuels Association (RFA) appreciates the opportunity to provide comments in response to the potential proposed amendments to the Low Carbon Fuels Standard (LCFS) that were the subject of an Air Resources Board (ARB) workshop on June 2, 2016. The proposed regulatory amendments discussed at the workshop relate primarily to the development of a mandatory verification program.

RFA is the leading national trade association representing U.S. ethanol producers. Many of our members are active participants in the LCFS program and are responsible for providing billions of gallons of low-carbon fuel to the California market since implementation began in 2011.

In summary, ARB has not sufficiently demonstrated that such amendments to the program are warranted. The LCFS regulation's existing validation and verification measures have provided adequate assurance to the marketplace that the current fuel pathway certification process is accurately reflecting the daily operations of fuel producers and carbon intensity of the fuels they supply to the state. Moreover, the current program structure is providing participants the assurance that credits are being properly generated and transacted. In short, the LCFS program's "buyer beware" approach has worked effectively. Not a single instance of fraud, purposeful misrepresentation of a fuel pathway, or willful generation of invalid credits has been documented since LCFS enforcement began more than five years ago. Further, many of the measures proposed by ARB would be duplicative of current regulatory and voluntary provisions that are already providing the market with the level of assurance it desires.

The new verification measures proposed by ARB would add enormous cost and administrative burden to the LCFS without providing a meaningful benefit to the program. In addition, the proposal to move the point of obligation marks a fundamental change to the structure of the regulation and we question whether the implications of such a modification have been fully considered. It is of great concern to us that ARB has not conducted any reasonable cost-benefit analysis of these potential amendments; the

Agency has stated only that the "cost impacts [of non-verification amendments] are expected to be minimal" and the likely costs of new verification-related amendments will not be known until ARB conducts an "informal survey to solicit representative cost information."Moreover, we are alarmed by the proposal's obvious overreach regarding information and data that clearly qualify as confidential business information and confidential personal information.

Finally, many of the new verification and validation requirements proposed by ARB are not only duplicative of existing LCFS provisions, but they also overlap with existing regulatory and voluntary verification and validation schemes that are in place as the result of other state and federal regulatory programs. Before embarking on the development of an entirely new verification program, ARB should carefully consider how existing programs can be used to meet perceived needs for additional assurance around fuel pathway validity and LCFS credit generation.

At the June 2 workshop, ARB staff presented proposed changes to the LCFS in three parts: Non-Regulatory Amendments; Proposed Regulatory Amendments; and Proposed LCFS Verification Program. We provide more detailed comments in response to each of these topics below.

1. NON-REGULATORY AMENDMENTS

Unique Identifiers

ARB staff presented the concept of introducing "Unique Identifiers (UIDs)" for LCFS credits. In theory, UIDs would be assigned to each credit upon generation in the LRT-CBTS. ARB staff suggested UIDs would provide parties the ability to track specific credits throughout the supply chain and ensure "effective monitoring, verification and enforcement for LCFS."

We do not believe UIDs are necessary to facilitate efficient transaction of LCFS credits in the LRT-CBTS system. A UID program would be extraneous and duplicative of the proposed "LCFS Verification Program" discussed elsewhere in these comments. Further, detailed information is already available within the LRT-CBTS regarding the fuel types, volumes, and carbon intensities associated with the credits and deficits generated under the LCFS. While this information may not allow all LRT-CBTS users to identify specific credits with specific gallons of fuel, it does provide the marketplace with valuable knowledge regarding the feedstocks and fuels being used to generate credits and deficits under the program. ARB periodically publishes this data in aggregate and makes it available to the public.

In the end, if ARB further pursues a UID program, we strongly recommend that it abandon the proposed verification program; implementing both programs would be repetitive, burdensome, and unnecessary. While we believe neither a UID program nor the proposed new verification program are necessary, the UID program is preferable to the verification program should ARB decide to further pursue some form of additional verification.

If ARB moves forward with the UID concept, we believe the code should be limited just to the most critical information needed by LCFS participants (which is generally already available to counterparties in LRT-CBTS). For example, the vintage of a credit or deficit is completely irrelevant and should be excluded from a UID, as LCFS credits have no expiration. Information contained in a UID should be limited to just those elements that are important to transacting parties, such as the fuel type, volume, carbon intensity, and originating company/facility associated with the credit or deficit.

Finally, we are not convinced that adding a UID to the LCFS credit program would in fact qualify as a "non-regulatory amendment." Adding a UID would fundamentally alter the LCFS credit program and we believe formal amendments would be necessary to the sections of the regulation governing how credits are generated and transacted. We encourage ARB to further consider whether a UID program would truly constitute a "non-regulatory" change.

2. PROPOSED REGULATORY AMENDMENTS

Point of Obligation for Petroleum Fuels

While we can appreciate the desire to harmonize the point of obligation under the LCFS and MRR regulations, we see compelling fundamental reasons for leaving the initial obligation where it is (i.e., with the refiner or importer). In addition, it does not appear that ARB staff has fully considered the potential ramifications of this proposal.

First, refiners and importers are the parties ultimately responsible for producing and supplying petroleum fuels to the California market. Because refiners and importers are currently the initial regulated parties, they are compelled by the regulation to reduce the production of deficit-generating high-carbon intensity (CI) fuels and facilitate increased use of low-CI fuels that generate credits. If refiners and importers are relieved of their compliance obligation, they will have little or no incentive to supplant the production or importation of high-CI fuels. Instead, that responsibility would now fall to the position holders at the terminal rack, who historically have had very little leverage to influence what fuels are produced and supplied by upstream refiners. In essence, moving the point of obligation results in position holders being "held hostage" by refiners and importers and subject to the whims of the refiners who have ultimate control over what fuels are supplied to the market.

Second, refiners and importers *already have the ability to pass their obligation down to the rack* if there are sufficient reasons to do so. Thus, if the marketplace determines that the rack is the most appropriate point for the obligation, the current regulation already allows this to happen. The proposed amendment would needlessly remove this flexibility.

Third, ARB provided absolutely no analysis of the costs and benefits associated with this proposal, other than to suggest that it would benefit staff by "requir[ing] only one verification process under both regulations." We believe moving the point of obligation could have important consequences for the

operability of the LCFS program, compliance costs, and California fuel markets; thus, we strongly encourage ARB to conduct more rigorous analysis on the potential impacts of this proposal.

"Know Your Customer" Check

We strongly oppose the "Know Your Customer" check concept as presented at the workshop. While such a program may make sense under the California Cap and Trade regulation, it does not make sense for the LCFS. The LCFS credit market operates strictly as a compliance market and access is generally limited only to regulated parties and fuel producers/suppliers. Unlike the Cap and Trade program, speculators, brokers, and traders who have no interest in the underlying fuel commodities generally are not participants in the LCFS credit market. This makes the "Know Your Customer" concept unnecessary for the LCFS.

In addition, the entities having legal responsibility for accurate registration, reporting, and recordkeeping under the LCFS are the companies involved in fuel production and distribution—not individual employees who serve as LRT-CBTS account administrators. We vehemently oppose any regulatory requirement for individual employees to provide copies of government-issued identification cards, passports, criminal history, bank account information, personal addresses, and other personal information. ARB's proposal constitutes an invasion of privacy that is completely unnecessary to ensure the efficient operation of the LCFS program. Sufficient information pertaining to the companies participating in the LCFS credit market is already available via existing regulatory requirements related to program registration and reporting.

Reporting

ARB has not justified its proposal to shorten the number of days to report credit transfers from 10 days (current) to just three days. The current allowance of 10 days has worked efficiently through the first five-plus years of the program and we see no compelling reason to change the credit transfer timeframe. Given the long transportation times for many low-carbon fuels entering California, and given the complex accounting systems employed by buyers and sellers of low-carbon fuels, the 10-day window provides more flexibility and time to ensure proper transfer and reporting procedures are used.

Third-Party Pathway Validation

We agree with ARB's view that the current regulation requiring pathway applicants to submit invoices and receipts for energy consumption, feedstock purchases, fuel and co-product sales, and other information is overly burdensome. However, the proposal to retain these records for inspection by a third-party auditor or ARB staff for a period of *10 years* is unreasonable, especially if ARB expects validation audits to be conducted annually. As ARB staff knows, the invoices, receipts and other documentation associated with even one year of operations at a typical biofuel facility is voluminous. Keeping these records on hand for a full decade provides no apparent regulatory benefit and puts an onerous recordkeeping requirement on producers. A 2- or 3-year period for recordkeeping is more

manageable and sensible. Additional comments on ARB's other verification and validation proposals are found in the next section.

3. PROPOSED LCFS VERIFICATION PROGRAM

Purpose and Scope

As stated elsewhere in these comments, we do not believe ARB has sufficiently justified the need for the additional verification and validation processes described at the workshop. To date, there have been no instances of fraudulent credit generation under the LCFS, and participation in the LCFS credit market is primarily limited to only those parties who use it to facilitate and demonstrate compliance. This is different than other credit markets (e.g., California Cap & Trade, RFS2), where speculators and other outside participants have the ability to buy, sell, and trade credits as financial instruments.

As such, the additional verification and validation requirements proposed by ARB go too far and are in many cases unnecessary. We have seen no evidence whatsoever from ARB that the benefits of these additional requirements outweigh the costs and administrative burden to both fuel suppliers and ARB staff.

Proposed Changes to Fuel Pathway Validation

ARB proposes to add a number of additional steps to the current fuel pathway application process. Many of these proposed additions appear duplicative with current requirements or unnecessary to ensure the validity of fuel pathway information and credit generation.

For example, the elements of the proposed "monitoring plan," including flow diagrams, metering/instrumentation information, calculations related to monitoring CI, measurement accuracy, etc., are already submitted to ARB with the fuel pathway application. Current regulations already require producers to ensure the CI of their fuel stays under an approved "cap" level, and they must notify ARB of any process/equipment changes that would potentially alter the CI of the fuel. In this sense, fuel producers are already performing constant monitoring to ensure their operations conform to those described in their approved pathway applications.

Further, the proposal to add a requirement for "validation statements" to the existing pathway validation process is redundant with current checks and balances already present in the regulation. The current LRT-CBTS transaction verification system ensures transacting parties reconcile all of the pertinent information related to a batch of fuel that is changing hands. If the buyer seeks additional assurance that the information provided by the seller is accurate and reliable, there are already private-sector due diligence solutions available to secure that additional certainty.

ARB's proposal that credits may only be issued quarterly after a "positive" verification statement is issued could wreak havoc on the credit market by greatly reducing liquidity. If parties must wait for

quarterly verification statements before credits are issued, significant interruptions in the free flow of credits between buyers and sellers could occur. There is no need for quarterly verification statements since ARB effectively requires constant monitoring of production processes to ensure conformity to the approved fuel pathway. Thus, if ARB proceeds with the proposed validation program, we strongly recommend eliminating the quarterly verification statement requirement and allow the market to continue to transact credits as it does today. If the annual verification audit results in an "adverse" outcome, ARB could require the retroactive replacement of any improperly generated credits. Alternatively, if ARB proceeds with the quarterly audit concept, it should eliminate the annual audit requirement as it would be redundant with the fourth quarter audit each year.

At the workshop, ARB staff made several references to focusing on "high risk pathway contributors," but never specifically defined what is meant by "high risk" and failed to present any criteria for determining the level of credit validity "risk" posed by various fuel pathways. While we do not believe the proposed additional verification measures are necessary, if ARB proceeds with the proposed verification program we agree that it should focus only on pathways that present the most risk for invalid credit generation. However, ARB should work with stakeholders to develop science-based criteria for determining with specificity what constitutes "high risk" pathways and/or pathway contributors.

ARB staff stated that additional reporting requirements related to "high risk pathway contributors" could include traceability for feedstocks, co-products, and finished fuels. Depending on the breadth and applicability envisioned by ARB, these potential traceability requirements could be unachievable and unreasonable. Further, the UID concept discussed by ARB would already include traceability elements and thus would be duplicative.

4. SOME OF ARB'S PROPOSED MEASURES ARE DUPLICATIVE WITH OTHER REGUALTORY AND VOLUNTARY PROGRAMS

Low carbon fuel producers who participate in the California LCFS are already subject to a number of other verification and validation requirements as a result of other state and federal regulatory programs. For example, the federal Renewable Fuel Standard (RFS2) requires regular attestation audits, third-party engineering reviews, a detailed application process for new pathways, pathway compliance monitoring plans, compliance reporting, and other measures. In addition, some producers who may be perceived as presenting a "higher risk" participate in a voluntary Quality Assurance Program (QAP) under the RFS to provide potential buyers with additional assurance that RIN credits are properly generated. Finally, as stated elsewhere, a number of voluntary market-based solutions and programs exist to assist potential buyers of low carbon fuels and/or credits with additional quality assurance. Before proceeding with the development of an entirely new verification program, we strongly encourage ARB to consider how existing regulatory- and market-based verification schemes may be used to fill any perceived gaps in the LCFS regulation's existing verification, monitoring, and validation programs.

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RFA appreciates the opportunity to provide comment on the proposed amendments discussed at the June 2 workshop. We look forward to working with ARB and other stakeholders on this and other issues related to the LCFS.

Sincerely,

Geoff Cooper

cc:
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