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Clerk of the Board, Air Resources Board
1001 I Street
Sacramento, CA 95814

RE: Phillips 66 Company Comments on Proposed 45-day Modifications to the California Cap and Trade Regulations and Response to October 7, 2013 oral CARB Staff Refinery Workshop Presentation and PowerPoint

Phillips 66 Company (P66) submits this single set of comments addressing both the proposed 45-day modifications package of the Cap and Trade Regulations proposed on September 4, 2013, and the staff presentation from the October 7, 2013 workshop on refinery benchmarking and coke calcining which reflects "staff thinking". These proposals both relate to the California Air Resources Board (CARB) adoption of benchmarking under the state's Cap and Trade Program (Program). We would like to offer our support for much of the publically vetted items contained in the 45-day package, and are also in support of others' related comments including the Western States Petroleum Association, Coalition for Fair and Equitable Allocation and the Blue Green Alliance.

We appreciate the time and effort that staff has put into the vetted and publically noticed portions of this rulemaking including the Second Compliance Period Assistance Factor adjustment; use of the CWB methodology, including the treatment of "offsites"; the fresh look at the Calciner benchmark and Cap Adjustment Factor (CAF) assignment, and establishment of additional refinery benchmarks. Significant progress has been made in the last year.

P66 has significant operations in California that are included under the Program including four separate oil refining facilities in four different cities and a petroleum coke calciner. P66 has proactively participated in every opportunity under this rulemaking process. And since 2008 we have attended workshops, had our refinery managers testify at board hearings, met with staff, met with Board Members, leadership and provided staff and Board Members company sensitive information. This is all for the specific purpose to help craft a workable regulation that does not cause inequities within the State which could disproportionately harm certain refiners, including our own operations in California and jeopardize the livelihoods of our 2,500 employees who live and work here.

While we support a large portion of the publicly noticed portions of this rulemaking that indeed significantly improve the existing Program, there are a variety of new, substantive issues that as of the Board hearing date were not in writing. In fact, "staff thinking" was only recently shared at the recent October 7, 2013 workshop over 30 days into the 45-day public comment period. These eleventh and a half-hour proposals have not been a meaningful part of the regulatory process leading up to, or including, the 45-day comment period. It is unfortunate that we have not been able to fully analyze the operational and economic impacts of these proposals.

P66 has concern over the following issues and formally requests more time to consider their impact on our business:

1. The non-Atypical Refinery benchmark proposal
2. Staff proposal over "jointly-operated" facilities (Definition of refinery)
3. Hydrogen production benchmark
4. Calciner benchmark
5. Calciner Cap Adjustment Factor

These benchmarking and allocation issues need to be thoroughly discussed, and will require adequate time for evaluation and comment. We are asking that the Board bring back these substantive issues to a future CARB hearing.

On top of creating in-state competitive issues, any cost burden added to a California refinery makes it less competitive versus refineries outside California who can import into California without cap and trade compliance costs. Without any protection from the import of finished or intermediate products, and with real world barge shipping costs to import fuel averaging out at only 3-6 cents per gallon, P66 recommends that CARB step back and take a fresh look at what the staff is proposing from in-state refining,.

With this in mind, P66 has concerns that certain benchmarking proposals will have the unintended consequences of tilting the in-state competitive balance. If CARB proceeds with their current single "typical" benchmarking proposal, some in-state refiners will be required to purchase 25% of their allowances while other refiners will have virtually no obligation to purchase in the Program because most of their allowances are given to them for free.

These issues have significant costs associated with them and are items that deserve full stakeholder vetting before they are adopted in the required 15-day amendment package. As of right now you only have concepts before you but they are yet-to-be drafted, or seen by stakeholders.

We are particularly concerned that the Board hasn't been given time to provide its critical oversight to these last minute issues, such as the competitive typical refinery benchmark. Unlike the Atypical benchmark which has been seriously considered by staff, Ecofys and Solomon in workshops and studies, the non-Atypical category (larger refineries) has not had this type of data analysis by staff or stakeholders. The single "typical" benchmark conflicts with both Solomon's six EDC categories as well as EPA's six categories for refining energy efficiency under Energy Star Program. Moving ahead with adoption of the this one benchmark would be premature and eliminates any Board review or stakeholder participation. We struggled to carry out a thorough analysis and develop definitive conclusions on principles that are not in writing. We believe CARB and the process would benefit from careful stakeholder analysis of new last minute additions to the typical refinery benchmarking proposal.

We are concerned that the current "staff thinking" will create immediate competitive issues within the refining industry in California. We have previously asked the Board, and do so again, to benchmark refineries against those of similar size and complexity. It is clear that larger industrial facilities are, and can be, more efficient through economies of scale.

The Board needs to determine its goal for refinery benchmarking. If the goal is to set the benchmark based on the most efficient refineries in California, regardless of size, the result is an immediate competitive disadvantage for the relatively smaller refineries. This competitive disadvantage comes from raising their cost of business by requiring them to purchase additional allowances. We cannot rebuild our refineries to be double their size to achieve the same efficiency as the largest refineries in the state. We cannot combine our two Southern California refineries that are five miles apart or our two other refineries in central and northern California that are 200 miles apart. What we can do is maintain or improve efficiency to a well established benchmark against similar refineries of size and complexity.

We have consistently recommended a benchmark that incorporates size and complexity. This can be an equation or a set of groups. The federal EPA took this very approach when it developed its Energy Star Program. It benchmarked refineries against similar size and complexity refineries to determine Energy Star Eligibility. Otherwise there would have been very few small Energy Star Refineries.

Solomon Associates, who staff selected to calculate refinery carbon efficiency, also benchmarks by refinery size and complexity. Our industry benchmarks our refineries using the Solomon methodology of six distinct "EDC" groups.

We believe there is sufficient time for careful analysis of the newly issued written proposal and subsequent dedicated Board hearing since refinery benchmarking for the Second Compliance Period are note needed before October 2014. A similar scenario of "deadline rulemaking" transpired on October 20, 2011, during the initial adoption of the Cap and Trade Regulations. However, in contrast to 2011, when the program faced possible expiration and the potential for re-review of the entire program in another regulatory process, there is no such constraint this time.

Providing a transparent and data driven process so that stakeholders can fully analyze the "new concepts" and more intricate parts of new proposals placed before you and respond will achieve a more solid program with fewer unintended consequences. New concepts introduced more than one month into a 45 day comment period is a recipe for unintended consequences. Because a 15-day amendment package will be needed, the regulatory mechanisms are already in place to direct staff to take the time needed, and P66 respectfully requests that the items of Opposition listed below are allowed to be fully vetted after being put in writing, and properly noticed prior to a final vote by the Board.

Summary of Support

1. Phillips 66 supports extending the First Compliance Period's industrial assistance factor through the Second Compliance Period;
2. Phillips 66 supports the use of the Complexity-Weighted Barrel (CWB) approach to refinery benchmarking;
3. Phillips 66 supports the inclusion of "offsite and non-energy utilities" and "non-crude sensible heat" factors in the CWB methodology;
4. Phillips 66 supports the establishment of separate benchmarks for "Atypical" refineries and the existing definition of facility contained in all portions of the Program;
5. Phillips 66 supports the current definitions of "Refinery" and "Facility" which reflect national and local definitions for stationary sources.
6. Phillips 66 supports the amendments related to allowance True-Up provisions;

   Recommendation: Approve the above mentioned measures.

Summary of Opposition

1. P66 opposes "staff thinking" regarding a new component for defining a facility under the allocation process. This concept of "jointly-operated" is not appropriate and does not meet the plain English criteria for Atypical refining operations.

   Recommendation: Abandon this new concept and regulate refineries instead of refiners. Recognize facilities which reflect national and local definitions for stationary sources.

2. P66 opposes the proposed "typical" refinery benchmark because it places an immediate competitive disadvantage on smaller refineries.
3. P66 opposes the adoption of the recently proposed and yet unjustified Calciner benchmark and requests that this issue be left open while the data and calculation methodology are analyzed.
4. Phillips 66 opposes staff's failure to place Coke Calcining operation into the greater than 50% emissions category in Table 9-2 and requests that this issue be left open while additional data is collected and analyzed.

5. Phillips 66 opposes the new staff proposal to establish a separate Hydrogen benchmark outside of the CWB methodology;

   Recommendation: Prior to release of the 15-day package, ensure that these elements are put into writing with policy and data justifications, a formal workshop is held, and new items are brought before the full board for adoption at a new hearing

P66 appreciates the opportunity to provide our recommendations to help assure a successful Program. Please do not hesitate to call me for further information and clarification at (916) 447-5572.

Sincerely,

Ste Will

Stephanie Williams, State Government Affairs Manager
Western and Rocky Mountain Region

Cc: CARB Board Members
Mary Nichols, Chairperson CARB
Richard Corey, CARB Executive Officer

Phillips 66 Company (P66) Comments on Proposed 45-day Modifications to the California Cap and Trade Regulations and Response to oral October 7, 2013 CARB Staff Refinery Workshop Presentation and Power Point

1. Definition of Refinery: **CARB has introduced a new definition of "facility" as it applies to the atypical refinery benchmark that is arbitrary, inconsistent policy treatment and targets the Phillips 66 Santa Maria Refinery more than 30 days into the 45-day comment period.**

Phillips 66 operates five distinct facilities in four different cities in the state of California (four refineries and a Calciner) subject to Cap and Trade. While not in writing to evaluate prior to the CARB hearing on October 25, 2013, CARB staff floated a new definition of facility. The long standing definition of "facility" is well known in stationary source permitting and federal GHG reporting. However, staff's newly proposed definition for "jointly operated" to be included in the "atypical" refinery category is a new concept. Trying to link facilities above and beyond the current definitions in Cap and Trade and MRR is inconsistent and has no policy justification. Since the term "jointly-operated" has not yet been defined, it is nearly impossible to draft intelligible comments for the Board while in concept with no written language.CARB staff made it very clear at the October 7 workshop that staff our Santa Maria facility was targeted for exclusion when creating the definition. The Phillips 66 Santa Maria and Rodeo refineries are separated by xx miles within the state. Santa Maria's intermediate product is shipped by common carrier pipeline to the San Joaquin Valley where it is transferred for further processing. Because it only produces intermediate products, much of its production can be replaced by international-sourced waterborne shipments to the Rodeo facility. As a result, the current staff "staff thinking" regarding "jointly operated" facilities will favor importation over in state manufacturing of intermediates.

A key objective behind the free allowance mechanism is to prevent leakage but staff's current path seems counter to that objective. As such, we are struggling to understand the policy argument for staff's proposal.

CARB's contractor Ecofys reported this information to CARB in the August 2012 Ecofys report on benchmarking. CARB's utilized Ecofys as its expert on benchmarking. On several occasions they list Santa Maria as a separate facility from Rodeo. See footnote "c" on page 7 (pdf pg 12) and then in Appendix C on page 72 (pdf pg 77)

The footnote cites P66 corporate documents and says: "*Became Phillips 66 in May 2012. The San Francisco Refinery comprises two facilities linked by a 200-mile pipeline: the Santa Maria facility located in Arroyo Grande and the Rodeo facility in the San Francisco Bay Area. The Santa Maria facility upgrades heavy crude oil for final processing in the San Francisco Bay facility. The Los Angeles Refinery Complex is composed of two facilities linked by a five-mile pipeline. The Carson facility serves as the front end of the refinery by processing crude oil, and Wilmington serves as the back end by upgrading the products (source: 10-K forms)*"

Recommendation 1: Abandon "staff thinking" regarding a new specific definition of facility and continue with the existing definition.

2. **Refinery Benchmarking: CARB should continue its work to establish and recommend refinery benchmarks that recognize refinery size, complexity and configuration.**

We are particularly concerned that the Board give critical oversight to the last minute competitive typical refinery benchmark. Unlike the Atypical benchmark which has been seriously considered by staff and Ecofys and Solomon in workshops and studies, the non-Atypical category (larger refineries) has not had this type of data analysis by staff or stakeholders. The "typical" benchmark conflicts with both Solomon's six EDC categories as well as EPA's six categories for refinery energy efficiency under the Energy Star Program. Moving ahead with adoption of this benchmark would be premature and eliminates any Board review or stakeholder participation. We struggle to carry out a thorough analysis and develop conclusions on principles that are not in writing. We believe CARB would benefit from careful stakeholder analysis of new last minute additions to the typical refinery benchmarking proposal.

We are concerned that the current "staff thinking" will create immediate competitive issues within the refining industry in California. We have asked the board previously and ask the board again to benchmark refineries against refineries of similar size and complexity. It is clear that larger industrial facilities are, and can be, more efficient through economies of scale.

The board needs to determine its goal is for refinery benchmarking. If the goal is to set the benchmark based on the most efficient refineries in California, regardless of size, the result is an immediate competitive disadvantage for the relatively smaller refineries. This competitive disadvantage comes from raising their cost of business by requiring them to purchase additional allowances. We cannot rebuild our refineries to be double their size to achieve the same efficiency as the largest refineries in the state. We cannot combine our two Southern California refineries that are five miles apart or our two other refineries in central and northern California that are 200 miles apart. We can maintain or improve efficiency to benchmark well against similar size and complexity refineries.

We have consistently recommended a benchmark that incorporates size and complexity. This can be an equation or a set of groups. The federal EPA took this very approach when it developed its Energy Star Program. It benchmarked refineries against similar size and complexity refineries to determine Energy Star Eligibility. Otherwise there would have been very few small Energy Star Refineries.

Solomon Associates, who staff selected to calculate refinery carbon efficiency, also benchmarks by refinery size and complexity. Our industry benchmarks our refineries using the Solomon methodology of six distinct "EDC" groups.

Recommendation 2: Phillips 66 supports staff's recommendation to recognize "Atypical" refineries in the benchmarking process. Staff should continue this work and establish additional benchmarks based on refinery size, complexity and configuration.

3. **CARB has failed to justify its proposed benchmark for coke calcining and has not properly assigned calcining to the list of industries in Table 9-2 and Table K-10 with emissions greater than 50%, with the corresponding cap adjustment factor.**

Phillips 66 opposes the adoption of the newly introduced and unjustified Calciner benchmark. We were surprised by seeing it the October 7th Workshop PowerPoint without any supporting data or discussion.

Unfortunately, there has not been opportunity to understand and review CARB's underlying data and assumptions, which eliminates our company ability to participate in this rulemaking.

There are only two calciners in the state making this decision poor public policy and one that is still unanswered by CARB. As part of the further discussions, we will want to discuss and understand the basis for the current and proposed benchmarks, confirm that the metrics of the benchmark are understood and identify possible technology and operational differences in the two Calciners operating in California.

Recommendation 3A: Develop a coke calcining benchmark that properly represents coke calcining in California and the technology used, and that does not subject calcining to leakage. Share all assumptions and benchmark basis with stakeholders.

We are also not clear on why CARB has not yet designated coke calcining as an industrial operation with greater than 50% process emissions. Our coke calciner clearly meets this criteria. Phillips 66 has provided supporting information as to why calciners should be added to Table 9-2 where other "Process with Greater than 50% Emissions" industries are listed and assigned an appropriate cap reduction factor.

CARB staff has also suggested that part of this evaluation is evaluating calcining's risk as EITE (Energy Intensive, Trade Exposed) industry. In this review, we do not understand CARB's rationale for designating calcining as part of a three digit NAICS code that covers all petroleum products, when there is a objective six digit custom description for Calcining (NAICS Code 324199) found in the Emission Intensity Table K-10. CARB is arbitrarily recommending a more general code that would result in our Calciner failing to qualify for the alternative and appropriate cap adjustment factor

Table K-10 in Appendix K has a listing of Emission Intensities. The calciner NAICS code 324199 indicates an intensity of 9,754 which is greater than the necessary threshold for the 50% process emission declining cap factor of 5,000 MT/$M. If there is uncertainty in the industries included in the original survey P66 can provide ARB with the necessary information to further support an emissions intensity >5,000 MT/$M.

Recommendation 3B: Utilize the NAISC Code that reflects Calcining (324199) and then insert it and coke calcining into Table 9-2 and Table K-10 for adoption in the 15 day package, with the corresponding cap reduction factor.

4. **Phillips 66 opposes the "staff thinking" proposal to establish a separate Hydrogen benchmark outside of the CWB methodology.**

Phillips 66 supports the comments submitted by the Western States Petroleum Association on this issue.

Recommendation 3: Abandon "staff thinking" regarding establishment of a separate Hydrogen benchmark outside of the CWB methodology and continue with the existing policy path that was released as part of the 45 day comment package.

Comments on the Process

Refinery benchmarking is a very significant policy decision which not only establishes the foundation of the Cap and Trade Regulation, but our competitive position within California based on the number of allowances we will need to purchase to continue operating in the state.

P66 is in the awkward position of commenting on oral presentation held at the October 7, 2013 workshop announcing significant benchmarking policy more than a month into the already limited 45-day review period. In 2011, we faced a similar truncated timing scenario on the initial Cap and Trade proceeding. The previous administrative process was truncated due to the clock running out on the original Cap and Trade rulemaking resulting in the Board directing staff on October 20, 2011 to re-evaluate the refining sector in-state competitiveness. The in-state competitiveness was not evaluated, the resolution ignored and here we are today, with an even more truncated process, literally 30 plus days into a 45-day package with only a October 7, 2013 PowerPoint to make assumptions from. Understanding what CARB staff might or might not think on decisions that will cost P66 tens of millions of dollars is not an acceptable process.

Significant decisions that impact the viability of our operations have been twice truncated and rushed to the end of a 45 day comment period. Multi- million dollar decisions are being made without the needed data analysis and, as a result, the policy justifications are unclear. These decisions impact how many allowances a facility will be provided and directly affect the California refining sector. Our testimony and position must be extracted from presentations and staff discussions on a very short time line with only the promise of detailed language to come to the Board. By taking a rushed approach to this rulemaking, the state risks placing negative unintended consequenses on the refining sector, which could result in unnecessary job loss,, increased importation of intermediate and finished product from outside California, and increased overall carbon emissions. Benchmarking is too important to get it wrong.

Because the actual language of the proposal has yet to be provided to stakeholders the evening before the hearing, we request that the process leading up to the required 15-day regulatory amendment package be brought back to the board for review and additional justification.

Other Comments re: the October 7 Workshop presentation:

1. P66 supports the staff's proposal to adopt the CWB allocation methodology. We also support including CWB terms for off-sites and non-energy utilities, and non-crude sensible heat. The CWB methodology, however, should be applied carefully in establishing efficiency benchmarks that recognize refinery size, complexity and configuration. When an individual facility operates with smaller size and fewer process units (lower CWB), there is less opportunity for heat exchange, the distribution of allowances would suffer from not recognizing these realities.

2. The October 7, 2013 oral presentation and corresponding PowerPoint recognize two benchmarks, one for atypical and typical refineries. The distinction is based on having less than 12 process units and less than 20 million barrels crude through the atmospheric distiller during an allocation year. While this is a step in the right direction in setting a benchmark that recognizes less complex or atypical refineries, the arbitrary policy decision to "require jointly operated facilities" to be considered as a single facility is not. This policy specifically excludes our smallest refinery, located in San Luis Obispo County, from the designation of atypical. CARB justification was vague with oral explanation alluding that facilities linked by pipelines mean that one refinery cannot operate without the other. The San Francisco refinery located in Contra Costa County, is 250 miles in distance from the Santa Maria Refinery.

   CARB must not arbitrarily discriminate against certain refineries. While the Santa Maria Refinery refines intermediate products that are utilized by Rodeo to make finished product, Rodeo could operate without the intermediate made by Santa Maria and shipped by pipeline. Intermediate products are commodities that could be brought to Rodeo by ship, barge, rail or other pipeline purchased from another source. Penalizing both facilities by entertaining the concept that a single refinery can consist of pieces within a 250 mile radius undermines the future viability of the facility and improperly treats the combined facility as a single typical refinery which it clearly is not. If the goal of the cap-and-trade program is to attract investment at the least cost, comparable facilities would benchmark with 'like against like' based on their refined products, size and configuration. Incentives should instead be to encourage a facility to be the best that it can be.

3. CARB's oral proposal and corresponding PowerPoint suggests fundamental changes to the longstanding definition of a stationary source facility. By requiring jointly operated facilities to be considered as single facility for purposes of an atypical determination, CARB is modifying the overarching policy definition of federal and state stationary source permitting. Many refineries are accessible by underground pipeline to receive or deliver a multitude of refining feed stocks. Facilities can be jointly operated by company ownership, long-term contract, or commodity streams. The definition of facility embedded in the CARB MRR regulation definition is why we report our 5 operating sites separately to CARB.

   "Facility," unless otherwise specified in relation to natural gas distribution facilities and onshore petroleum and natural gas production facilities as defined in section 95102(a), means any physical property, plant, building, structure, source, or stationary **equipment located on one or more contiguous or adjacent properties in actual physical contact** or separated solely by a public roadway or other public right-of-way and under common ownership or common control, that emits or may emit any greenhouse gas....".

The key words here are "continuous or adjacent". Modifying the regulation to capture refiners instead of refineries will create competitive disadvantages for only Phillips 66. The policy justification and objective is punitive and will not result in improved energy efficiency on-site.