THE CALIFORNIA RAILROAD INDUSTRY

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

September 27, 2011

Railroad Industry Comments on the 2nd 15-Day Change Notice for MRR and CTR

On behalf of the Union Pacific Railroad (UP), BNSF Railway (BNSF), and the Association of American Railroads (AAR), collectively "the Railroads," we want to thank the California Air Resources Board (ARB) for the opportunity to comment on the Second Notice of Public Availability of Modified Text (2nd 15-Day Change Notice) for the Mandatory Reporting of Greenhouse Gas Emissions Regulation (the MRR). Furthermore, we want to thank ARB staff for their attention to our issues.

The Mandatory Reporting Rule should be amended to shift the point of regulation for transportation fuels and/or allow the Railroads and fuel suppliers to agree to shift the reporting obligation in order to address the inequitable impact on the railroad industry.

In the fall of 2010, the California Air Resources Board ("ARB" or "Board") released the proposed amended MRR which identified the point of regulation (POR) for transportation fuels to be at the first occasion where the fuel crosses "the rack" at a fuel terminal and required certain position holders in transportation fuels to report greenhouse gas (GHG) emissions starting in 2012. In November and December, the Railroads proposed that ARB shift the point of regulation for transportation fuels to the first point of supply because the proposed rule imposed a significant regulatory burden on one, and only one, end-user of transportation fuels – the Railroads. When such modifications could not be made, we worked cooperatively with ARB to include language in the Board resolution to allow the Railroads to continue to work with Staff on this issue. In addition, the Railroads submitted comments on December 15th that summarized our concerns regarding the inequities created by the rule. (See Attachment 1)

During 2011, the Railroads suggested to the ARB staff that the MRR and CTR compliance burdens should be shifted upstream. The Railroads believe there are two possible options to resolve concerns with the ARB's approach. (See Attachment 2) Under Option 1, the Railroads asked ARB to amend the rules so that suppliers of diesel fuel by pipeline to the Railroads' California fueling facilities would assume the reporting burden under the MRR and the compliance burden under the CTR. Under Option 2, the Railroads asked ARB to amend the MRR to allow agreements between position holders in transportation fuels and fuel suppliers that shift the reporting obligation to the fuel supplier. In spite of both parties' cooperative efforts, neither option is reflected in the (2nd 15-Day Change Notice). The Railroads believe that one or both of the two options should have been included in the 2nd 15-Day Change Notice. We again ask that the rule be amended to include one of our proposed options.

1. **ARB should amend the Mandatory Reporting Rule to shift the point of regulation for California railyards that receive diesel fuel by pipeline to the first point of supply.**

In order to remedy the significant regulatory burden placed on the Railroads, the only end-user of transportation fuel with a reporting requirement under the MRR, the Railroads request that ARB amend the Mandatory Reporting Rule to shift the point of regulation for California railyards that receive diesel fuel by pipeline to the first point of supply. Fuel suppliers are already required to report transportation fuel data to ARB under other AB 32 regulations and could easily comply with such a requirement under the MRR. Furthermore, research performed by the Railroads and provided to ARB staff indicates that, in all instances, the suppliers of diesel fuel to railroad fueling facilities by pipeline already possess data on the number of gallons sold to the Railroads, and would need no additional information to comply with the MRR.

2. **ARB should amend the Mandatory Reporting Rule to allow agreements between position holders in transportation fuels and fuel suppliers that would shift the reporting obligation to the fuel supplier.**

This proposal follows the structure established in ARB's Low Carbon Fuel Standard that allows for the transfer of regulated party status (see LCFS §95484(a)). Under this option, a position holder and its fuel supplier could mutually agree to shift the reporting obligation of the MRR to the fuel supplier. Such an arrangement would allow the position holder and fuel supplier to enter into the most economical arrangement in order to comply with the regulation. Given the complexity of the current and projected regulatory arena for transportation fuel, it only makes sense to allow the parties to mutually agree on how to best comply with the MRR.

Technical Correction

The Railroads have worked closely with ARB staff to identify and correct technical issues, and we thank staff for their attention.

3. **Calibration Requirements.**

Section 95121(c) requires certain operators to meet certain monitoring and QA/QC requirements. As written, it is unclear whether position holders who must calculate emissions based on either the delivering entity's invoiced fuel volume or on a financial transaction meter (per §95121(b)(1)) are exempt from the monitoring and calibration requirements of §95121(c). Since position holders who must calculate emissions based on either the delivering entity's invoiced fuel volume or on a financial transaction meter do not utilize the meters at their fueling racks, it is not reasonable to require these meters to be monitored and calibrated under the MRR. Furthermore, discussions with ARB staff revealed that §95121(c) was not intended to apply to position holders who must calculate emissions based on the delivering entity's invoiced volume for fuel or a financial transaction meter. The Railroads therefore request that ARB clarify that the requirements of §95121 (c) will not apply to the Railroads.

Thank you for the opportunity to provide comments and we look forward to continuing to work cooperatively with staff. If you have any questions, please do not hesitate to call me or Sarah Weldon at 415-421-4213.

Respectfully submitted,

Kirk Marckwald
Principal, California Environmental Associates
On behalf of Union Pacific Railroad, BNSF Railway and Association of American Railroads

cc:
Michael Barr, Pillsbury Winthrop Shaw Pittman LLP
Michael Rush, AAR
Russell Light, BNSF
Melissa Hagan, UPRR

Attachment 1

THE CALIFORNIA RAILROAD INDUSTRY

Kevin Kennedy, Ph.D
Air Resources Board
1001 I Street
PO Box 2815
Sacramento, CA 95814

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

December 15, 2010

Re: Comments of The California Railroad Industry on the Proposed California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms Regulations and Mandatory Reporting Rule

Dear Dr. Kennedy and Clerk of the Board:

This letter provides the comments of BNSF Railway Company and Union Pacific Railroad Company ("the Railroads") on the "Proposed California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms Regulations," adding Article 5 (§§ 95800 et seq.) to Title 17 of the California Code of Regulations ("the Cap-and-Trade Rule" or "the Rule"), as well as the proposed "Amendment to the Regulation for Mandatory Reporting of Greenhouse Gas Emissions (Title 17, §§ 95100 et seq.) ("the MRR"). The Railroads appreciate the opportunity to comment on the Rule and the MRR, as well as the Air Resources Board's consideration of these comments.

As proposed, the Cap-and-Trade Rule would, beginning in 2015, regulate transportation fuels by requiring "suppliers" of certain fuels, including diesel fuel, to purchase compliance instruments (i.e., allowances or offsets) in order to meet the "cap" on greenhouse gas ("GHG") emissions imposed by the Rule. The Railroads understand that, for purposes of diesel fuel, the MRR and Cap-and-Trade Rule are modeled on the reporting requirements of the Board of Equalization ("BOE"). While this approach may have been logical from the standpoint of streamlining existing reporting practices, ARB's decision to rely on the existing BOE reporting forms for defining the first point of supply unwisely places differing compliance burdens on the major transportation companies depending on the method through which they receive fuel from their suppliers, and thus would inhibit the competitiveness of some companies as compared to others within the same market. The fuel producers and fuel importers are the first supplier of fuel for both bulk and non-bulk transfers. Therefore, the fuel producers and fuel importers are the best source of information for purposes of reporting and compliance with AB 32, and it is illogical and overly-complicated to have different points of compliance based strictly on whether the fuels are transferred via the bulk or non-bulk system.

The Railroads submit these comments because, as proposed, the MRR and the Cap-and-Trade Rule create potential inequities for and amongst major fuel consumers in California by treating bulk and non-bulk transfers of fuel differently for purposes of reporting and compliance. Whereas non-bulk transfers will generally be reported by, and the compliance obligation will rest with, upstream fuel producers and fuel importers, the reporting and compliance obligation for bulk transfers is pushed downstream to multiple and various fueling facilities that might qualify as "terminals" under the Rule.

As currently drafted, the Railroads could be determined to be "suppliers" of diesel fuel, and therefore "covered entities," under the proposed Cap-and-Trade Rule. This would mean that the Railroads would be required to acquire compliance instruments in order to supply diesel fuel to locomotives in California. By limiting the number of compliance instruments available to all covered entities in a given year, the Cap-and-Trade Rule would impose a *de facto* regulation on the Railroad's ability to supply diesel fuel to locomotives in California, notwithstanding the preemptive effect of the federal Interstate Commerce Commission Termination Act of 1995 ("ICCTA").[1] The Railroads and Air Resources Board have long recognized this federal preemption of state and local authority to regulate railroads, and should continue to do so when implementing the MRR and Cap-and-Trade Rule.

The Railroads urge that further study of this issue is necessary and warranted to address concerns that many major fuel consumers are unaware that the reporting and compliance obligations under AB 32 have been pushed "downstream" away from the fuel producers and fuel importers. To address this significant issue, the Railroads request and recommend that, in the event the Board elects to approve the Cap-and-Trade Rule, the Executive Officer be authorized and directed to meet with interested stakeholders concerning this issue in order to gather the necessary facts and data, and to amend the regulations in a manner consistent with AB 32.

We look forward to continuing to work cooperatively with ARB staff. Please contact me at 415-421-4213 x 12, or Sarah Weldon at 415-421-4213 x 34 if you have any questions.

Sincerely yours,

Kirk Marckwald
On Behalf of the Association of American Railroads, BNSF Railway, and Union Pacific Railroad

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[1] The ICCTA's preemption of state and local regulations that impose an unreasonable burden on the railroad industry has been upheld in multiple court decisions. *See City of Auburn v United States Government* (154 F.3d 1025, 1029-31 (9th Cir. 1998) ("Congress intended to preempt a wide range of state and local regulation of rail activity"); *Association of American Railroads v South Coast Air Quality Management District* (9th Cir. 2010) 622 F.3d 1094 ("[the] ICCTA preempts those [local and state] rules unless they are rules of general applicability that do not unreasonably burden railroad activity").

Attachment 2

Kirk Marckwald

From: Kirk Marckwald
Sent: Friday, August 26, 2011 4:24 PM
To: 'rfletcher@arb.ca.gov'
Cc: 'gmayeur@arb.ca.gov'; 'scliff@arb.ca.gov'
Subject: Railroads' Proposed Options to Amend CTR and MRR Rules
Attachments: 11_0826_Proposed Draft Options to Amend CTR and MRR Rules.pdf

Bob:

Attached for you and your team's review are two options to amend the proposed Mandatory Reporting and Cap-and-Trade Rules.

Option 1 contains draft proposed regulatory text that shifts the compliance burden upstream to the fuel suppliers. This language was discussed with you on August 2nd and has not been revised since. Option 1 is the Railroads' preferred option.

Option 2 contains draft proposed regulatory text that allows the Railroads to contractually assign the reporting and compliance responsibility to the fuel suppliers, provided the suppliers agree to take it. The text is modeled after similar language in ARB's Low Carbon Fuel Standard (LCFS).

Thank you for your team's consideration of these options. If you have any questions, please call me at 415-215-4213. We look forward to discussing these with you on Thursday at 4 pm.

Kirk

Proposed Draft Options to Amend the Proposed Cap-and-Trade and Mandatory Reporting Rules

Option 1 – Shift the Compliance Burdens to the Upstream Fuel Suppliers

This document compares the Railroads' proposed changes to ARB's proposed regulation.

Proposed Approach regarding fuels delivered by pipeline to Railroads under the proposed amended Mandatory Reporting Rule and the proposed Cap-and-Trade Rule.

1. Amend the definition of "Position Holder" in both the MRR and CTR, as follows:

   "Position holder" means an entity that holds an inventory position in motor vehicle fuel, ethanol, distillate fuel, biodiesel, or renewable diesel as reflected in the records of the terminal operator or a terminal operator that owns motor vehicle fuel or diesel fuel in its terminal. The "Position Holder" for diesel fuel supplied to a railroad fuel storage and distribution facility by pipeline is the supplier of that fuel according to the bill of lading, invoice or other sales document.

2. Amend the definition of "Terminal" in both the proposed revised Mandatory Reporting Rule and the proposed Cap-and-Trade Rule:

   ""Terminal" means a motor vehicle fuel or diesel fuel storage and distribution facility that is supplied by pipeline or vessel, and from which motor vehicle fuel may be removed at a rack. "Terminal" includes a fuel production facility where motor vehicle fuel is produced and stored and from which motor vehicle fuel may be removed at a rack. "Terminal" does not include a railroad fuel storage and distribution facility."

3. Amend §95121(d)(~~1~~9) in the MRR as follows:

   §95121 (d)

   (~~1~~9) California position holders must report the annual quantity in barrels, as reported by the terminal operator, and as corrected to reflect the individual components of the product, for each petroleum product or biomass-derived fuel listed in Tables MM-1 and MM-2 of 40 CFR Part 98 that is delivered across the rack in California, except that distillate fuel oil is limited to diesel fuel and except for products for which a final destination outside California can be demonstrated.

   (A) California position holders who deliver diesel fuel to a railroad fuel storage and distribution facility by pipeline must report the name of the recipient and the volumes delivered according to the bill of lading, invoice or other sales document.

Option 2 – Contractually Assign Reporting and Compliance Obligations in the Mandatory Reporting and Cap-and-Trade Rules

Amend §95103 of the proposed Mandatory Reporting Rule as follows:

§ 95103. General Greenhouse Gas Reporting Requirements.

(c) *Fuel and CO2 Suppliers.* The suppliers listed below, as defined in section 95102(a), are required to report under this article when they produce, import and/or deliver an annual quantity of products that, if completely combusted, oxidized, or used in other processes, would result in the release of greater than or equal to 10,000 metric tons of CO2e in California, unless otherwise specified in this article:

(1) Position holders at terminals and refineries delivering petroleum products and/or biomass-derived fuels, as described in section 95121;

(A) A position holder at a terminal may, by written contract, transfer its regulatory compliance requirements under the Mandatory Reporting Rule and the Cap-and-Trade Rule to the fuel suppliers and/or refiners that supply fuel to the position holder for a period of one calendar year or longer. The procedures for such a transfer are contained in §95121(f)

Amend §95121 of the proposed Mandatory Reporting Rule as follows:

§ 95121. Suppliers of Transportation Fuels.

(f) *Procedures for Transferring Position Holder Obligations by Written Contract.*

A position holder at a terminal may transfer its regulatory compliance requirements under the Mandatory Reporting Rule and the Cap-and-Trade Rule to the fuel suppliers and/or refiners that supply fuel to the position holder for a period of one calendar year or longer by following the procedures specified in this paragraph.

(1) The regulatory compliance requirements for both the Mandatory Reporting Rule and the Cap-and-Trade Rule must be transferred for the entire transfer period. The transfer may not be for one rule and not the other.

(2) The term of the transfer must be at least one calendar year. Transfers longer than one year must be in increments of calendar years.

(3) For transfers of periods less than one complete compliance period, by May 15th of the calendar year following the year for which the compliance obligation is calculated pursuant to §95103, the transferee fuel supplier will surrender one hundred percent (100%) of the required compliance obligation for GHG emissions reported from the calendar year.

Attachment 2 (cont)

(4) For transfer terms that cover any complete compliance period, the transferee fuel supplier may surrender compliance obligations as provided in §95855 of the Cap-and-Trade Rule.

(5) Notification of the Executive Officer.

(A) For each transfer of a Position Holder Obligation under this paragraph, the transferring party and the transferee fuel supplier must submit a joint, signed written notice to the Executive Officer at least 60 days prior to the term of the transfer. The written notice shall be in a form determined by the Executive Officer and shall contain:

1. Names of the transferor and transferee, including current and complete contact information.

2. Signatures of Responsible Officials for each transferor and transferee.

2. Term of the transfer.

3. Estimate of amount of fuel covered.