



January 30, 2004

Ms. Diane Johnston, General Counsel
California Air Resources Board
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Sacramento, California 95814
regreview@arb.ca.gov

Subject: CARB regulations and their impact to CIOMA members.

Dear Ms. Johnston:

We wish to thank the Air Resources Board for the opportunity to comment on regulations which have had an adverse impact, or may have an adverse impact, on businesses in this state. Before getting into the specific regulatory programs we would like to comment on CARB's regulatory program in general. CARB has established a sophisticated regulatory development program. While we are at odds with you in many instances, we will exercise our continued involvement with regulations that directly (and indirectly) affect our members. As we have expressed recently, we are very concerned with the role that settlement agreements are playing in the accomplishment of public priorities. When settlement agreements are entered into there is a specific **exclusion** of interested and affected parties from both the negotiations leading to settlements, and their implementation. This practice raises serious legal, moral and due process issues and we urge the Board to resist this avenue. If agreements *are* pursued, then the inclusion of all parties potentially affected by the agreement(s) should be included in negotiation and implementation of the document(s). If not, then, as a prophylactic strategy, parties will be encouraged to initiate their own lawsuits to insure that their interests are being protected through separate agreements. This is a worse-case manner in which to accomplish effective public policy. We acknowledge the receipt of the recent letter from Executive Officer Witherspoon and will respond to it in a separate communication. We thank her for writing us about our concerns.

Now for our specific comments:

CARB Fuel Specification Regulations

CIOMA has had a long-standing interest in communicating our concerns on the development and implementation of state fuel specifications. As we have expressed frequently, and which is now backed by numerous public and private studies, California's high fuel prices are specifically driven by the supply isolation these requirements impose on our fuels. We are already physically isolated, but the implementation of unique fuel requirements has exacerbated this condition into a situation where our fuel prices are the highest in the contiguous 48 states and are significantly more volatile. For the independent fuel marketer this poses a special economic threat. Large oil companies have the financial resources and market flexibility to weather these conditions. Indeed, the fuel suppliers in this state actually

are advantaged by these conditions, as is witnessed by the higher-than-other-states refinery “crack spreads” (a measure of determining refinery profitability) California refiners enjoy. Small businesses, which comprise our membership, are much less able to withstand periodic market conditions where supply costs are greater than sales costs – termed “inversion” – which occur more frequently in these volatile conditions. Further, these conditions create difficult-to-predict market conditions which confound our members in obtaining needed loans to make frequent and expensive upgrades mandated by CARB and other California agencies. And these regulations, by tightening the overall supply of fuels in the state, have created especially volatile conditions in the unbranded market, as well as more frequent shortages, where most of our members obtain their primary supply.

The independent oil marketer provides a valuable component to the state fuels market. First, independent marketers provide convenience to California motorists. They operate and supply small independent stations that serve neighborhoods and rural areas, where larger firms will not operate due to low volume conditions. Further, our members serve small bulk purchasers such as local governments, school districts, emergency services, agriculture, construction sites and small fleets. Finally, our members generally participate at the lower end of the price spectrum, providing downward pressure on fuel costs and assuring choice by participating in toe-to-toe competition with the major oil companies. We fill important niches in the fuels market place, and without our participation, many fuel purchasers will have to create more expensive and more logistically complex fuel supply arrangements. The economic conditions created by California’s unique fuel recipes create harm and significant impact to our members and their continued viability.

However, even with our continued good-faith input to CARB’s regulatory process, the Board continues to conclude that there is “no impact” to small businesses from these regulations. We have a well-documented set of communications with CARB on this issue. Most recently we raised concerns early in the development of the Phase III gasoline regulations – at the earliest point during workshops – which have been continually ignored throughout the adoption and amendment of the Phase III regulations. We would be glad to share the full set of documents and chronology, but, in short, we have had 3 years of communication with CARB on this issue, carefully pointing out how the regulations had the potential to impact our members, and small businesses, to no avail. If CARB continues to ignore the economic impact on small businesses resulting from their regulations, as legally mandated, we will be forced to pursue this discussion in court.

Proposed solutions:

- ✓ Retain a consultant to develop model(s) that effectively predict the costs to small businesses from CARB regulations, especially noting the limitations created by having to finance, on limited assets and incomes, the costs of proposed regulations. Further, other costs to businesses, such as insurance, other mandated expenses (such as enhanced vapor recovery, underground storage tanks upgrades, etc) and the like should be included to determine if small businesses can afford, or qualify for financing, the regulation at hand.
- ✓ Develop the ability to quantify both direct and indirect costs of regulations. For example, the cost of fuel to a marketer will not only be influenced by possible

increases in manufacturing, it will also be affected by the strains the regulations put on the overall supply system. Increased costs in fuel supplies, such as these, need to be taken into account.

- ✓ Respond in good faith to concerns raised by affected parties during the course of regulation comment and consideration.

CARB Enhanced Vapor Recovery Regulations

We have provided a jointly developed comment on a portion of the Enhanced Vapor Recovery (EVR) regulatory package with the Western States Petroleum Association, - that letter is being delivered under separate cover. It addresses a critical issue regarding the timing of various regulations in this complex package, and a proposed solution to the ORVR/EVR requirements as they currently stand.

Beyond the comments included in that letter we have the following comments on the overall EVR package. First, as we have commented previously in adoption proceedings and public comment opportunities, we believe CARB has not sufficiently addressed the issues of cost to small businesses in the economic analysis of the requirements. Small businesses have unique and difficult hurdles in attempting to comply with CARB requirements, especially significantly expensive EVR mandates. The federal Small Business Administration has documented that small businesses face financial burdens 60% higher than larger firms in achieving compliance with environmental regulations. For example, small businesses do not have large quantities of ready capital available to pay for expensive improvements. So, they have to obtain financing to accomplish these ends. First, the owner must be able to demonstrate the ability to repay the loan based upon income and liabilities. Obviously an independent operator does not have the asset base of a major oil company. And, as has been the recent experience of service station owners, these expensive requirements come along at disturbingly frequent intervals, in many cases more frequent than the normal operating life of equipment or supporting infrastructure.

A particularly difficult problem the small owner has is that the station is likely a smaller volume location (the major oil companies have "cherry-picked" the prime locations and govern competition through branded supply contracts) so it is more difficult to establish adequate financial basis to obtain loans. Second, independent operators do not have the ability to purchase in volume, as do the major oil companies, so their unit price for equipment and services is higher. Finally, every day of non-operation creates a more significant impact to the independent operator due to the lack of reserve capital.

Another area of concern is that financial impact analysis is never updated. Specifically, with the EVR regulations, there have been amendment opportunities to re-evaluate the original cost estimates and recalculate them based upon more current information. A growing concern we have is that as companies continue to struggle with certification of a Phase II system the R&D costs are dramatically increasing. This will lead to higher priced systems than originally projected. Inflationary impacts on equipment and services must also be considered. CARB should schedule regular updates to its original costs estimates so that the real costs of implementation are identified, and if costs become significantly greater than

originally anticipated, a hearing should be scheduled to re-examine the requirements and their cost-benefit.

CARB financial impact analysis has not taken into account these various problems. The analysis is usually based on very preliminary cost estimates. And then the costs are evenly spread over the population of service stations, without weighting for “ability to pay.” This provides a distorted and unrealistic view of economic impact and provides decision makers with inaccurate information. CARB is obligated, by law, to specifically evaluate the impact to small businesses. This has not been done in an accurate manner. And, although staff at times asks us to provide them with this analysis, it is an expensive undertaking that our small number of members and limited resources cannot provide. After all, it is CARB’s obligation to perform this analysis, not ours. And our members are the ones being burdened with the cost of the regulation results. Clearly the moral, legal and financial obligation is the proposing agency’s.

Another issue we have communicated to CARB and others is the potential situation of having sole-source vendors approved for equipment and systems. We believe that at least three vendors should be certified for equipment and systems to assure adequate competition for required materials. We suggest that CARB examine the recent problems station owners have had with “enhanced leak detection” testing, where only one certified testing company exists, and there have been order-of-magnitude price jumps on the testing costs, as a good example of how sole-source provision can lead to serious problems.

Proposed Solutions

- ✓ As suggested in the previous item, CARB should retain a consultant to develop economic impact models on small businesses.
- ✓ CARB should regularly update their economic impact analyses to determine whether original estimates are correct, and identify thresholds of increase that would trigger new hearings if costs were escalating significantly.
- ✓ CARB should adopt a policy that at least three vendors/suppliers be certified before requirement timelines are established.

CARB Enhanced Vapor Recovery Regulations on Aboveground Storage Tanks

This is a regulation package currently under development. Since we have not seen the final requirements, nor final cost information, we cannot make definitive comments on costs or potential impacts to our members or their customers. However, our involvement so far has led us to some preliminary conclusions. First, it appears that staff is spending a significant amount of time in designing a very complex and costly set of requirements, akin to the EVR requirements for service stations. And, this complex construct is being applied to the entire universe of aboveground storage tanks, for large commercial and fleet tanks to small, remotely located farm tanks. There appears to be a fixation with a “Cadillac” solution regardless of cost, practicability or need.

From our preliminary assessment it looks like there are two primary sources of fugitive emissions from AST’s – faulty pressure relief valves and faulty or cracked fuel content

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gauges. There may be a very cost-effective way to eliminate a substantial portion of the emissions by requiring retrofit of these elements and simple annual maintenance requirements, rather than having to put in entire new systems. But we continue to review intricate mechanical information on insulated tanks, complex vapor recovery systems and support equipment. And, to our knowledge, there is no system that meets the proposed requirements currently in use.

This brings another issue into play. The retrofit program for AST's is very different than that for service stations. Retrofit of service stations with vapor recovery equipment occurred over a long period of time. The AST program will require retrofit of all tanks (depending on APCD application of the rules) at one time. This could create significant equipment supply and servicing issues for the regulated community. Further, these new, experimental systems could easily run into certification problems similar to the service station EVR program. By requiring new, untested and increasingly complex requirements CARB is adding delay and uncertainty to emission controls. Further it places the person paying for and employing the new technology in a high liability position.

This occurs in two ways. First, the owner/operator becomes the "lab rat" for the new equipment. Although certified by CARB, the owner/operator is responsible for *utilizing* the new systems or equipment. If equipment fails, if systems don't operate as predicted, or if false readings are generated, the owner/operator must bear the cost for fixing the problem. CARB staff frequently asserts that the owner/operator should make the installers and manufacturers provide warranties or other obligations to fix the problems. This is fallacious - it is like a customer telling Bill Gates that Windows should be responsible for work losses related to computer software glitches. The bottom line is that our members are held ultimately responsible for the field testing and eventual finalization of equipment and system designs. (We refrain, here, from discussing the fact that CARB adopted flawed certification of the previous vapor recovery equipment absent *any* liability.)

Second, the owner/operator is held liable for air quality violations while field testing the equipment. So, to add insult to injury, the owner/operator is provided the "opportunity" to pay for equipment repairs and to argue over, and in many cases pay, fines for equipment or system malfunction. There is a serious equity issue here, as well as an important economic consideration.

Proposed Solutions:

- ✓ Direct staff to prepare "stair-step" proposals to emission controls rather than take-it-or-leave-it packages. This would provide decision makers the ability to evaluate various compliance scenarios and their respective costs and emission reduction capabilities without having to send staff back for complete redesign of regulatory initiatives. It also provides more flexibility in establishing requirements based upon ability to pay.
- ✓ Require staff to provide at least one workshop, prior to "closing" the final regulatory package - one that fully discloses to the regulated community and other parties the estimated costs, economic impacts and emission controls achieved. In the current situation the public's only opportunity to fully comprehend what staff ultimately

recommends is during the final 45-day review period. These documents can entail months, or years, of staff work that must be digested by reviewers in significantly less time than it took to prepare. And, reviewers are compelled not only to digest the information, but comment on it and engage in communications with staff, Board members and others during this compressed timeframe.

- ✓ Provide economic assistance, especially to small businesses, to subsidize the costs of “burning-in” systems and equipment. CARB may come to a significantly different realization of what they are requiring if they have to allocate budget to helping implement their requirements. And this may be the only way small businesses can afford increasingly expensive and complex mandates.
- ✓ Provide emission violation amnesty during “burn-in” periods. We understand that this requires cooperation of the local districts, but in the final analysis businesses that are assisting in achieving reliable emission control equipment/systems should NOT be held liable for failures beyond their control.

CARB Consideration of Regulation on Cargo Tank Trucks and Fuel Delivery Practices

This is another regulatory package under development, although not as far along as the AST/EVR program. Since this program is still in the information-gathering stages there is not much specific to comment upon, but we do have some general observations. First, we have not yet commented on the value of the Ombudsperson Office in negotiating the myriad avenues of CARB regulatory initiatives. Kathleen Tschogl and her staff provide a critical and essential role in helping the regulated community understand what is being proposed, and in facilitating communications between staff, CARB leadership and those who are going to have to pay for compliance. This is truly a “feather” in CARB’s cap - providing resources to those who do not have staff resources dedicated, day-in and day-out to the limited aspect of air quality requirements (in relation to the overall responsibilities of keeping a business profitable, employees paid, and benefits provided). We urge CARB to maintain this office and their role in helping us provide useful, timely information and participation.

Second, we urge the Board to truly “partner” with the regulated community in developing practical and cost-effective regulations. Here is a quandary we have run into. CARB asks us as an association, and our members individually, to participate in data gathering exercises. Staff indicates that without adequate information invalid emission estimates will occur, with the possibility of emission over-statement (leading to more severe requirements). This is a valid point. However, from the regulated vantage, there are some immediate reactions to these data-gathering exercises: 1) How much rope do I give a regulatory agency to hang me with?; 2) How much time and expense is involved in providing this information, in relation to the other pressing needs of my business?; 3) Will this information, many times proprietary, be kept secured and unavailable to anyone but CARB staff working on this issue?; and 4) Will the information be used in models or other estimating calculations that are not suitably designed to provide accurate outputs? With these questions in mind, there is a strong hesitancy to incur the costs and inconvenience of gathering and submitting the data. When these issues are added onto a history of CARB generating expensive and cumbersome regulatory requirements, it is very understandable that the regulated community is hesitant

to cooperate in these situations. Thus, the need to truly partner with the regulated community in regulation development.

We have experienced some encouraging signs from CARB staff in regulatory development programs – and the way the cargo tank program is beginning gives us hope. There have been early meetings and full disclosure of the potential path for regulation development, as well as participation in emission estimate workplan development. This is a good starting point. However, to achieve a true *partnership* with the regulated community there needs to be a buy-in to the final regulatory proposals. Some level of agreement among work group participants needs to be reached in the proposal to be submitted to the Board. If, after extended participation in meetings, data provision and workshops, the staff and/or executive branch come up with proposals that meet the strenuous objection of process participants, the question legitimately posed is, “Why have I wasted all this time and effort to have someone ignore my concerns?”

Therefore we urge the Board and staff to develop, as much as possible, consensus in moving forward with recommendations on regulatory proposals. This is a new model, at least from our perspective. It will lead to greater cooperation, and trust, from the regulated community and will provide dividends through a greater willingness to comply. The opposite is true if regulations keep getting rammed down our throats.

Proposed Solutions:

- ✓ Retain the Ombudsperson Office as a valuable and essential asset in the CARB regulatory process.
- ✓ Strive to achieve consensus with the regulated community for recommendations to the Board, especially when the regulated community is expected to put “sweat equity” into the development of the proposals.

CARB Consideration of Retrofit Requirements to Fuel Delivery Truck Engines

We believe this regulatory endeavor has been temporarily shelved by CARB. In many ways the previous discussion on cargo tank regulations is relevant to our involvement with this initiative. Our involvement with staff was positive and constructive, until a proposal that was developed in a consensus manner was brought back with changes from the administrative branch. At that time it appeared that an unreasonably short time frame was proposed, to the distress of working group participants.

This program contained a reliance on new, untested technology with fuel delivery truck owners and operators having to employ technology in early stages of development. High costs and unanswered questions regarding liability, operating durability, and deployment prior to common availability of ultra low sulfur diesel were legitimate concerns expressed by the regulated community. As has been stated previously, this type of regulatory outcome poses unique and negative impacts to our members. Those impacts must be adequately identified, and hopefully mitigated through careful construct of the requirements.

A particular concern with this proposal is that it is listed in a settlement agreement. Although we have heard that there are attempts in working with agreement parties in removing this requirement we have not been asked to participate in discussions about that effort. Since this program materially affects our members we ask to be included in those discussions.

Proposed Solutions:

- ✓ Careful design of requirements to insure they are employed using reliable and well-tested technology, with minimal liability to the person employing it.
- ✓ Inclusion of parties directly affected by settlement agreement conditions.

Conclusion

After participating in the January "SIP Summit" it is clear that the state has a daunting task of reducing emissions to comply with SIP commitments. We are now encountering the law of diminishing returns, where additional emission controls are becoming increasingly expensive and difficult to attain. The Board must perform the difficult task of balancing air quality improvement needs with the potential economic harm those requirements impose. Especially vulnerable to this situation are small businesses. It is important to remember that small businesses provide essential employment and benefits to their localities. Health effect benefits from air emission reductions should be tempered with potential loss of employment and health coverage for the state's population, as small businesses are adversely affected by regulatory mandates. We thank you for this opportunity to express our views.

Sincerely,



Jay McKeeman
Executive Vice President

Cc: All Members of the Air Resources Board
Deputy Cabinet Secretary Dan Skopec, Governor's Office
Cal/EPA Secretary Terry Tamminen
Executive Officer Catherine Witherspoon, CARB
Kathleen Tschogl - CARB, Ombudsperson