



Submitted Via eRulemaking Portal

August 17, 2018

Acting Administrator Andrew Wheeler
U.S. Environmental Protection Agency
1200 Pennsylvania Ave., N.W.
Mail Code 28221T
Washington, D.C. 20460

Attn: Docket ID No. EPA-HQ-OAR-2018-0167

Re: Renewable Fuel Standard: Proposed RVOs for 2019 and Biomass-based Diesel Volume for 2020

Dear Acting Administrator Wheeler:

The Valero Energy Corporation and its subsidiaries (collectively, “Valero”) submit these comments on EPA’s proposed renewable volume obligations (“RVOs”) for 2019 and for biomass-based diesel for 2020 under the renewable fuel standard (“RFS”) program. In the proposal, EPA seeks comment on several issues in the RFS program in addition to the RVO. Valero’s unique position as a refiner, importer, exporter, marketer and biodiesel and ethanol producer means that Valero views the RFS program from several perspectives that can be particularly helpful to EPA on the issues raised in the proposal. Valero urges EPA to consider its unique frame of reference in evaluating the views and recommendations presented in these comments.

As the largest petroleum refining company in the U.S. and the world’s largest independent refiner, Valero employs approximately 10,000 employees and operates 15 petroleum refineries in the U.S., Canada and the U.K. Valero therefore has a large RFS obligation and has the perspective of an obligated party and a merchant refiner. Valero is also a fuel importer, exporter, and a major fuel wholesaler. Important also from Valero’s perspective is Valero’s experience as a biofuel producer. Valero was the first traditional petroleum refiner to enter large-scale ethanol production and has 11 state-of-the-art plants making Valero the third largest ethanol producer in the U.S. Valero’s investment in Diamond Green Diesel makes Valero also the largest renewable diesel producer in the U.S.

Due to these diverse business interests, Valero is a member of several different trade associations that themselves represent diverse interests. To the extent that these associations submit comments on this proposal, they should not be construed as necessarily representing Valero’s viewpoints, particularly when such comments (or lack of comments) may conflict with our statements herein.

Valero is concerned that EPA has yet again proposed RVOs that are not reasonably attainable and EPA has declined to make use of available authorities to reduce harms caused by the program and the volatile RIN market. In addition to our concerns about the volumes, in these comments, we

identify corrections to the RFS that will substantially improve the program and ensure that it continues to meet the statutory goals set by Congress: to support growth in renewable fuels in the U.S. and to enhance U.S. energy security and independence. As noted in these comments, Valero has provided information and recommendations to EPA in previous comments. Valero has separately submitted its prior comments and other centrally relevant documents to this docket and asks EPA to consider that information as well as these comments in considering how to reduce the unintended and unnecessary harms caused by the RFS.

I. Introduction and Summary

Since 2013, the RFS program has been fraught with challenges, yet EPA has set annual mandates every year at aspirational levels. In that time, EPA has made decisions based on interpretations of the statute that conflict with the goals and the structure of the statute. EPA has acknowledged that the RFS has resulted in renewable fuel entering the market in volumes that increasingly exceed the blendwall and that the statutory goals for biofuel volumes are not achievable. Yet, EPA has not exercised all the authority available under the statute to minimize harm that arises from well-documented market constraints. One of EPA's fundamental obligations under the statute is to set volumes at levels that do not cause unnecessary harm. EPA fails to meet these obligations with the proposal. Valero urges EPA to reconsider the proposed volumes and to reconsider statutory interpretations made in prior rules that EPA relies upon in this proposal.

Despite having numerous tools at its disposal, EPA continues to fail to address the harm to merchant refiners that became apparent before 2015. Although EPA has recently granted waivers to small refineries, the small refinery exemption is not EPA's only tool to address harm in the market nor is it sufficient to remedy harm to all merchant refiners, since many refineries that are harmed do not qualify for the waiver. Valero urges EPA to change course from relying on the same theory-based assessments on which it has relied in each of last three RVO rulemakings and instead undertake a serious and robust evaluation of evidence in the past year that support EPA using more tools to reduce distortions in the RIN market and the fuel market.

Valero asks that EPA reduce mandates for total renewable fuels and advanced renewable fuel so that they are reasonably attainable. EPA admits that the mandate relies on biomass-based diesel volumes that are not reasonably attainable. EPA must also consider domestic supply of biomass-based diesel ("BBD") in setting a reasonably attainable 2020 standard. Valero supports EPA's intention to preserve the RIN carry-over bank and urges EPA to consider that the proposed RVO might result in drawing down the RIN bank because the mandates are not reasonably attainable.

Recent developments provide overwhelming evidence that the current RFS is causing economic harm; thus, Valero urges EPA to reduce the harm by using the general waiver authority to reduce volumes. EPA should use both general waivers: (i) EPA should define "domestic supply" to mean only renewable fuel produced in the U.S. and find that there is an inadequate domestic supply of advanced renewable fuel and (ii) EPA should undertake a robust evaluation of the harms identified by states, by merchant refiners and small retailers and reduce the volumes to prevent the severe economic harm otherwise caused. EPA must not re-allocate volumes attributable to exempt small refineries among the other obligated parties; to do so would exceed

statutory authority, violate due process of obligated parties and cause additional harm to merchant refiners who do not qualify for small refinery waivers.

Additional tools available to EPA to provide relief in the RIN market include changing the status of exported renewable fuel, changing the point of obligation and implementing trading reforms. EPA can increase the supply of RINs in the market and provide additional RIN liquidity and RIN price stability if EPA changes the RFS to ensure that all renewable fuel produced in the U.S. for transportation fuel is available for compliance credits. EPA should ensure that exported renewable fuel can also be used for compliance with the RVO. In response to EPA’s request for recommendations to address RIN market problems, Valero suggests several measures that might address problems in the RIN market but Valero must remind EPA that the primary cause of RIN market problems is the definition of obligated party and the fact that blenders are not obligated parties.

II. The Proposed Volumes Are Not Reasonably Attainable

A. EPA Must Set Reasonably Attainable Volumes for Total Renewable Fuel

The RFS volumes must be reasonably attainable. To determine reasonably attainable volumes of total renewable fuel under the current structure, EPA must assess markets for conventional ethanol. In the proposal for the 2019 RVO, EPA did not provide an assessment of the E0, E15, and E85 markets to determine what levels of conventional ethanol are reasonably attainable for 2019. Rather, EPA assumed ethanol use in 2019 will be as high as actual used in 2017—10.11%. This amounts to 14.527 billion gallons of ethanol consumption for 2019, falling short of the implied conventional ethanol volume of 15 billion gallons.¹

Even assuming EPA’s projections are accurate for 2019, the implied conventional fuel mandate of 15 billion gallons is not achieved and 3.2 billion gallons of other renewable fuel, such as advanced and conventional biodiesel and renewable diesel, are needed to satisfy the total renewable fuel volume. According to EPA, 3.2 billion gallons is approximately 300 million gallons higher than the volume EPA projected for biodiesel needed in 2017 and in 2018. This is above and beyond the volume needed to achieve the advanced fuel volumes. In order to achieve the implied conventional fuel mandate of 15 billion gallons, the ethanol content would have to average

¹ David Korotney, EPA, Market impacts of biofuels in 2019 at 3 (Nov. 27, 2017) (EPA-HQ-OAR-2018-0167-0025). Determination of Volume of Biodiesel and Renewable Diesel Needed in 2019 to Achieve 19,880 Million Gallons of Total Renewable Fuel

Total renewable fuel volume	19,880
Ethanol	14,527
Non-ethanol cellulosic biofuel	362
Other non-ethanol renewable fuels	40
Biodiesel and renewable diesel needed (ethanol-equivalent volume/physical volume)	4,951 / 3,194

10.45%. This is a significant increase beyond historical levels. Currently, the ethanol content is ~9.96% for the first 6 months of 2018.² These requirements are not reasonably attainable.

B. EPA Must Set Reasonably Attainable Volumes for Advanced Renewable Fuel

EPA should not finalize its proposed advanced renewable fuel volume because EPA fails to consider the costs and uncertainty associated with importing renewable fuel and account for reduced volumes of renewable fuel imports due to increased costs and because the volumes of advanced ethanol, other advanced biofuels, and advanced biodiesel and renewable diesel EPA estimates will be reasonably attainable are insufficient to meet its proposed requirement.

EPA has proposed to find that “100 million gallons of advanced ethanol, 60 million gallons of other advanced biofuels, and 2.65 billion gallons of advanced biodiesel and renewable diesel are reasonably attainable.”³ However, the Agency concludes that, combined with its estimate of 381 million gallons of reasonably attainable cellulosic biofuel, “the sum of these volumes falls short of 4.88 billion gallons, which is lowest advanced biofuel requirement that EPA can determine under the cellulosic waiver authority.”⁴ To make up the difference, EPA suggests there may be as much as 2.8 billion gallons of advanced biofuel available in 2019, but admits that this is a risky bet because of “likely feedstock/fuel diversions.”⁵ If this bet fails, EPA suggests that carryover RINs can serve as a backstop,⁶ but acknowledges that compliance using carry-over RINs is not practical.⁷

EPA must consider the costs and uncertainty associated with reliance on imported BBD to meet the RVO. Historically imported BBD accounted for ~30% of generated RINs. Through May 2018, imported BBD accounts for ~18% of the generated BBD RINs. EPA's projection of 4.34 billion advanced biodiesel and renewable diesel RINs in 2019 is overly optimistic. Given tariffs on imported biodiesel from Argentina and Indonesia, EPA proposes an RVO that requires unreasonably high growth in domestic production and imports from other countries. Current domestic BBD capacity is 2.4 billion gallons and utilization is ~70% through May 2018.⁸ Biodiesel imports are significantly down so far in 2018. Actual imports of BBD are down 52% from last year (296 vs. 614 mbpm). Based on the year-to-date average, 2018 imports of BBD are expected to have a 62% decrease from last year (296 vs. 781 mbpm).⁹ Domestic production of biodiesel is higher in 2018, but not high enough to meet 4.34 billion RINs in 2019 with meager

² According to EIA's July STEO report (Table 4a), motor gasoline consumption was on average 9.23 million barrels/day for 1H18. Fuel ethanol blended into gasoline averaged 0.92 million barrels/day. EIA, July 2018 Short-Term Energy Outlook at 41, <https://www.eia.gov/outlooks/steo/archives/jul18.pdf>.

³ *Id.* at 32,040.

⁴ *Id.*

⁵ *Id.*

⁶ *Id.* at 32,047.

⁷ *Id.* at 32,048

⁸ EIA, Monthly Biodiesel Production Report, Table 1: U.S. Biodiesel production capacity and production, <https://www.eia.gov/biofuels/biodiesel/production/table1.pdf>.

⁹ EIA, Petroleum & Other Liquids, U.S. Imports of Biomass-Based Diesel Fuel, https://www.eia.gov/dnav/pet/hist/LeafHandler.ashx?n=PET&s=M_EPOORDB_IM0_NUS-Z00_MBBL&f=M (July 31, 2018 release date).

imports. EPA's "Determination of Volume of Biodiesel and Renewable Needed in 2019" effectively requires 100% utilization rates and zero exports. This is completely unrealistic.

EPA also assumes unrealistically that higher domestic production is reasonably achievable. The registered domestic capacity totaling 4.1 billion gallons of total biodiesel and renewable diesel is irrelevant in this discussion as this volume is not reflective of actual domestic production. EPA should be relying on the EIA production capacity of 2.4 billion gallons. EPA acknowledges in the preamble "domestic production of advanced biodiesel and renewable diesel in 2016 and 2017 was approximately 1.85 billion gallons. Of this total, approximately 150 million gallons of domestically produced biodiesel was exported in 2016 and 2017."¹⁰ It is irrational for EPA to count on significantly higher production than in years past and no exports.

In short, EPA cannot finalize the proposed 4.88 billion gallons when that is premised on the uncertainty of attaining 2.8 billion gallons of BBD to achieve the advanced fuel mandate, "notwithstanding likely feedstock/fuel diversions."¹¹ If there is substantial doubt as to whether a quantity of renewable fuel is reasonably attainable, it is unreasonable for EPA to set the volume at that level. Valero agrees that EPA should not "propose to set the 2019 volume requirements at levels that would envision an intentional drawdown in the bank of carryover RINs."¹² 2.8 billion gallons of advanced biodiesel and renewable diesel for 2019 for the calculation of advanced biofuels is an unattainable volume and, therefore, is an intentional drawdown of the RIN bank balance. EPA should avoid this by using the general waivers to ensure that all RVOs are reasonably attainable without drawing down the RIN bank.

C. EPA Proposes Biomass-Based Diesel Volumes that Are Not Reasonably Attainable and Are Not Based on Domestic Supply

As described in previous comments and again below, EPA should define "domestic supply" to mean produced within the U.S. Thus, in its determination of what volume for BBD is reasonably attainable, EPA should consider domestic supply and not set the standard based on uncertain and costly imports. The promotion of imports is not consistent with the statutory purpose of protecting national security and promoting domestic resource development.

The domestic production capacity of BBD is 2.4 billion gallons/year at 100% utilization. While utilization is currently up year over year from 2017, it is not averaging near 2.4 billion gallons this year. In fact, annualized BBD domestic production is approximately 1.7 billion gallons for 2018. Excluding imports from "domestic supply," the proposed BBD RVO for 2020 is aspirational, not reasonably attainable.

¹⁰ 83 Fed. Reg. at 32,047.

¹¹ *Id.* at 32,040

¹² *Id.* at 32,030.

D. Marine Ultra-low sulfur diesel Impact on Available Supply and Compliance Issues

In setting the applicable BBD volume for 2020, EPA must account for U.S. produced biofuel that is blended into ultra-low sulfur diesel (“ULSD”) and used as a marine fuel oil cutter stock and reduce the mandated volume by that amount. With a January 1, 2020 compliance date for 0.5wt% sulfur IMO marine fuel oil, ULSD may be an optimum blend component to achieve the more stringent sulfur specification for marine fuel oil. Since marine fuel oil does not meet the definition of “transportation fuel,” any biofuel blended into ULSD that is subsequently used as a fuel oil cutter stock will not qualify for RFS compliance. This scenario also creates an opportunity for errors in RIN generation and accounting as well as fraud.

III. EPA Should Preserve the RIN Carry-Over Bank

Valero agrees with EPA that EPA should not set the RVO at a level that would result in a reduction of the RIN bank. The RIN bank should be maintained at 14 percent or higher. In the proposal, EPA has noted that the RIN bank is currently at 15 percent of the proposed total renewable fuel standards and 14 percent of the proposed advanced biofuel standard.¹³ This level is below the 20 percent “rollover” limit specified in EPA regulations. EPA has previously determined that such a limit is consistent with the structure of the RFS while recognizing that credits must be available in the year generated and the year thereafter. When EPA set the 20 percent limitation, EPA stated that “the 20 percent cap provides the appropriate balance between, on the one hand, allowing legitimate RIN carryovers and protecting against potential supply shortfalls that could limit the availability of RINs, and on the other hand ensuring an annual demand for renewable fuels as envisioned by the Act.”¹⁴ Valero does not dispute the 20 percent limit but recommends that EPA consider that the stability of the RIN market and improve the RFS so that the RIN bank is not drawn down and remains available to serve the purposes for which it was intended. EPA acknowledges that there are a number of uncertainties regarding how the RIN bank will be impacted in 2019. Therefore, EPA should not do anything in the 2019 RVO that is intended to or could be anticipated to result in drawing down the RIN bank.

Despite assurances not to set RVOs at levels that would draw down the RIN bank, EPA nonetheless proposes to set the advanced biofuel standard at a level that EPA suggests a large number of carry-over RINs may be necessary. If EPA's concerns about “likely fuel/feedstock diversions” come to fruition, the proposed volume for advanced biofuel will not be reasonably attainable and obligated parties will have to draw down the carryover RIN bank. As EPA recognizes, “a bank of carryover RINs is extremely important in providing obligated parties compliance flexibility in the face of substantial uncertainties in the transportation fuel marketplace, and in providing a liquid and well-functioning RIN market....”¹⁵ Preserving the RIN bank ensures compliance flexibility and depleting it can disrupt the functioning of the RFS program.¹⁶

¹³ 83 Fed. Reg. at 32,030

¹⁴ 72 Fed. Reg. 23,000, 23,934-35 (May 1, 2007)

¹⁵ 83 Fed. Reg. at 32,029.

¹⁶ *Id.* (“An adequate RIN bank serves to make the RIN market liquid...[W]e believe the RFS program functions best when sufficient carryover RINs are held in reserve....”).

EPA can avoid the potentially significant negative consequences of depleting the RIN bank by considering whether the use of one or both general waiver authorities is appropriate. This is one “circumstance[]...that would warrant further reductions in volumes through the exercise of the general waiver authority.”¹⁷ EPA has already determined that the volumes that will be reasonably attainable will fall short of the proposed advanced biofuel RVO. Using either or both general waiver authorities can correct this. As described further below, EPA should consider only the domestically produced renewable fuel to determine whether there is adequate domestic supply for meeting statutory mandates and EPA must consider the economic harm on refineries and refinery communities in evaluating use of the waiver for severe economic harm. EPA should not rely on the carry-over RIN bank to increase the RVO when the circumstances support use of one or both of the general waivers.

A sufficient volume in the RIN bank does not necessarily reduce economic harm. The RIN bank accounts for RINs that RIN-long parties and unobligated parties might still hold. As long as RIN-long parties and unobligated parties hoard RINs, the amount in the RIN bank does not reduce economic harm of the RFS. To improve the functioning of the RIN bank to relieve the economic harm under the RFS, EPA must address the RIN market problems that are due to the inequitable distribution of RINs among obligated parties. EPA could right the RFS and eliminate the inequitable distribution of RINs by adjusting the point of obligation. Short of this correction to the program, EPA must consider additional measures recommended below to reduce the harm that comes from RIN hoarding and other market manipulation. Without a market correction and an adequate RIN bank, the RFS will cause severe economic harm that demands EPA reducing the RVO through use of the general waiver.

IV. Recent Developments Should Compel EPA to Conduct a Full-fledged Analysis of Whether to Use the General Waivers

In the proposal, EPA summarily dismisses consideration of using general waivers for severe economic harm or inadequate domestic supply. Yet, in the past year, several developments demand that EPA evaluate use of the waiver for severe economic harm, including: (1) petitions to EPA requesting EPA grant waivers based on severe economic harm; (2) the bankruptcy of the PES refinery, the largest east coast refinery; (3) exemptions granted to over 30 small refineries; and (4) the court decision in *Ergon-West Virginia, Inc. v. EPA* rejecting EPA's reliance on analysis showing that the cost of the RIN passes through to conclude that a small refinery suffered no disproportionate economic hardship.¹⁸ Furthermore, irrationally high RIN prices continue to reflect a poorly-functioning RFS program. High RIN prices do not promote higher blends of renewable fuel¹⁹ and will continue to cause disproportionate economic harm not only to small refineries but to merchant refiners who are not eligible to seek small refinery exemptions.

¹⁷ 83 Fed. Reg. at 32,048

¹⁸ No. 17-1839, 2018 WL 3483282 (4th Cir. July 20, 2018).

¹⁹ See NERA Economic Consulting, Effects of Moving the Compliance Obligation under RFS2 to Suppliers of Finished Products 15-23 (2015), Attachment A; Ron Minsk, Comments on Proposed 2014, 2015, and 2016 RVO 2-4, 6-8 (June 24, 2015), Attachment B.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

Additionally, in response to EPA's expressed concerns about biofuel imports and tariffs imposed on biodiesel imports, EPA received numerous comments in 2017 about the definition of "domestic supply" and how to account for biofuel imports in the RFS. A year later, the market has experienced the initial impacts of these tariffs, proving the validity of some of the comments. Valero and others requested that EPA define "domestic supply" to include only renewable fuel produced in the United States.²⁰ EPA must determine whether there is adequate domestic supply of renewable fuel to meet the statutory volumes. Including only domestically produced renewable fuel as domestic supply for setting the RVO is a better means for ensuring that the RVO will be reasonably attainable; it eliminates the uncertainty and costs of imports. It is also consistent with congressional intent. Nonetheless, imported renewable fuel must still be available for compliance with the RVO and thus would only serve the purposes of the RFS to the extent imported renewable fuel is more economical than domestically produced renewable fuel.

A. EPA's Criteria for Identifying Severe Economic Harm is Too Limited, Unsupported by the Statute and Disregards the Reality of the Impacts of the RFS Program

Before 2017, EPA's review of economic harm caused by the RFS was limited to evaluation of production and prices of corn and ethanol; food expenditures for households, feed costs for cattle, pigs, poultry and dairy; and gasoline prices and expenditures for households.²¹ In the 2018 final RVO, EPA assessed economic harm in 2017 by looking again only at very limited criteria instead of considering information submitted by commenters during the comment period and submitted well before the comment period.²² EPA admitted that its 2017 analysis had significant limitations, which EPA attributed to time limits. Yet Congress gave EPA a time limit of 90 days to approve or disapprove petitions for waivers based on severe economic harm.²³ Congress did not authorize EPA to disapprove petitions or refuse to properly evaluate petitions on the basis of time constraints.

EPA's own characterization of its review was that of a "high level investigation of a number of broad economic indicators" that "may not be as useful in assessing the possibility that the RFS program would cause severe economic harm on a State or regional level, as compared to a national level."²⁴ Since 2017, EPA has had more than enough time to undertake a more in-depth investigation. Even in 2017, EPA was given early notice that small refineries and merchant refineries had incurred severe harm under the RFS and that small retailers also experienced substantial harm. EPA should not continue to hide behind the limited time between proposal and final annual rulemakings to shirk its responsibility to evaluate the evidence of economic harm provided in comments to every RVO rulemaking since 2015.

²⁰ See, e.g., Valero Comments on Proposed 2018 RVO (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-3988), Attachment C.

²¹ 83 Fed. Reg. at 32,048

²² 82 Fed. Reg. 58,364, 58,518 (Dec. 12, 2017).

²³ 42 U.S.C. § 7545(o)(7)(B).

²⁴ David Korotney, EPA, Assessment of waivers for severe economic harm or BBD prices for 2018 at § A.2 (Nov. 30, 2017) (EPA-HQ-OAR-2017-0091-4925) ("Korotney Memo").

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

EPA must evaluate whether economic harm would occur at the State or regional level and cannot rest a decision regarding economic harm only on evaluation at the national level based on broad criteria that has little relevance for the actual harms arising from the rule. EPA must also evaluate actual evidence and not rely on economic theory.

As further described below, EPA disregarded warnings of harm that already existed but were likely to become more apparent in 2018. For 2018, the only new information EPA considered was crop-based feedstock futures, projected gasoline demand and market impacts of ethanol and biodiesel consumption. EPA disregarded evidence provided by refineries impacted by the standard and small businesses losing to disruptive unfair advantages made possible by the RFS. In this rulemaking, EPA should not commit the same errors disregarding the evidence provided in 2018 of economic harm and disregarding pleas by states and impacted entities to provide relief from harm.

B. EPA Should Consider Evidence of Severe Economic Harm and Undertake Evaluation of Economic Harm Concerns

EPA received several requests to waive RVO volumes to reduce severe economic harm. The states of Texas, New Mexico, Delaware and Pennsylvania sent EPA requests²⁵ and several companies²⁶ and the Small Retailers Coalition made requests²⁷ in response to EPA's Notice of Data Availability in October 2017.²⁸ In addition, PES filed for bankruptcy in January 2018, directly contradicting EPA's claim that the RFS and the RVOs were not adversely impacting refineries.²⁹ Valero sent to EPA a Petition for Reconsideration³⁰ requesting EPA reconsider its decision to deny the Point of Obligations Petitions based on EPA's determination that there was no harm under the RFS. In that petition, Valero requested that EPA provide any other remedy to relieve the harm. Valero attaches the Petition for Reconsideration to these comments and incorporates it as part of these comments on the proposed RVO.

²⁵ EPA made these letters and its responses to them available to the public at <https://www.epa.gov/renewable-fuel-standard-program/learn-more-about-letters-seeking-additional-information-related>. They are included here as Attachments D, E, F, and G for convenience.

²⁶ AFPM Comments on 2018 Supplemental Notice 18 (Oct. 19, 2017) (EPA-HQ-OAR-2017-0091-4703) (requesting a 3.3-billion-gallon reduction of total renewable fuel and advanced biofuel volumes due to past reliance on now uncertain supply of imported renewable fuel); Valero Comments on 2018 Supplemental Notice 14 (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-4885) (requesting reduction in requirements for advanced and total renewable fuel), Attachment H; HollyFrontier Comments on Proposed 2018 RVO 9-10 (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-2547); PES Comments on Proposed 2018 RVO 3 (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-3887).

²⁷ Small Retailers Coalition Comments on Proposed 2018 RVO 1-8 (Oct. 19, 2017) (EPA-HQ-OAR-2017-0091-4687).

²⁸ 82 Fed. Reg. 46,174 (Oct. 4, 2017).

²⁹ Disclosure Statement for the Joint Prepackaged Chapter 11 Plan of Reorganization of PES Holdings, LLC and Its Debtor Affiliates, *In re PES Holdings, LLC*, No. 18-10122-KG (Bankr. D. Del. Jan. 22, 2018) ("PES Disclosure Statement"), Attachment I. Energy Ventures Analysis examined the circumstances that led to PES's bankruptcy and concluded that "the actual costs of the RFS are significant compared to its realized benefits, that [PES] and other east coast merchant refiners are absorbing the cost, and that the dramatic changes in energy markets since 2007 have rendered moot most of the goals of the RFS." EVA Comments on PES Holdings, LLC Proposed Consent Decree 1 (Mar. 26, 2018), Attachment J.

³⁰ Valero Petition for Reconsideration (Mar. 22, 2018), Attachment K.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards
for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

EPA's conclusion that the RFS does not cause harm to refineries or small retailers is based primarily on EPA's conclusion that the RIN costs are passed through in the wholesale price of petroleum fuels. The recent court decision in *Ergon-West Virginia, Inc. v. EPA*³¹ rejects EPA's reliance on this conclusion to determine disproportionate economic harm to individual refineries and challenges its utility to conclude that the RFS does not cause severe economic harm in any state, Region or the nation.³² EPA must undertake a new evaluation of the economic harm of the RFS and determine whether the harm is severe. It is inconsistent for EPA to ignore the waiver when granting over 30 small refinery exemptions based on economic harm and reaching a settlement with PES, which in total represent as much as 2.25 billion gallons.³³ That same kind of harm is affecting both regional economies and refineries that don't qualify for exemptions and don't declare bankruptcies. It is arbitrary and capricious for EPA to deny that there is harm arising from the RFS because of RIN value pass-through while EPA grants hardship exemptions based on disproportionate economic harm. By doing so, EPA is wading neck deep in the market distortion.

1. To date, EPA has interpreted the waiver provision too narrowly

To date, EPA's statutory interpretation of the severe economic harm waiver provision has been an unreasonable interpretation. EPA narrowly interpreted the provision to require proof that a single market factor—RFS volume requirements—is the sole cause of the harm.³⁴ EPA's interpretation undermines the purpose and utility of the statutory waiver. It is hard to imagine how EPA's test might ever be met, given that the RFS requirements interact with many factors contributing to the economy of the nation, a state, or a region. EPA cannot, through interpretation, nullify the effect or purpose of a statute.

Various factors make states and regions uniquely vulnerable to harm from implementing RFS requirements and cause those areas to experience such harm more acutely. For example, economic analysis identified East Coast and Mid-continent refiners as facing the "most risk" from the RFS Program due to "their higher operating costs, significant logistical challenges in sourcing crude oil, and direct competition from large foreign based refiners..."³⁵ EPA unreasonably interpreted the statute to make those factors disqualifiers that precluded a finding of severe harm. EPA should reconsider this interpretation and consider the evidence already available of economic harm caused by the RFS.

³¹ No. 17-1839, 2018 WL 3483282, at *8.

³² In addition, EPA's previous analyses on pass-through "ignores the fact that different entities are differentially situated at the rack. EPA fails to explain...how a merchant refiner such as [PES] can recover RIN costs when competing at the rack with a blender or marketer that has no obligation under the RFS. Merchant refiners would be similarly disadvantaged when competing against an integrated refiner which blends in excess of its RFS obligation and thus would not face the same costs at the rack...These competitive dynamics leave merchant refiners...to disproportionately bear the cost of increasing RIN obligations." EVA Comments 6.

³³ 83 Fed. Reg. at 32,029 (explaining that the 3.06 billion carryover RIN bank includes 1.460 million RINs attributable to small refinery hardship exemptions for 2017 and 790 million RINs attributable to small refinery hardship exemptions for 2016 and the PES bankruptcy settlement).

³⁴ Korotney Memo at § A.3.

³⁵ Alex Holcomb, *Market Analysis of the Proposed Change to the RFS Point of Obligation* 15 (Feb. 22, 2017) (EPA-HQ-OAR-2017-0091-3988), Attachment L.

Valero Comments on EPA’s Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

This is not a theoretical problem. A month after EPA published the 2018 RVO, Philadelphia Energy Solutions (“PES”), the largest refiner on the East Coast, declared bankruptcy. PES identified the primary event precipitating the bankruptcy as RFS compliance costs.³⁶ Comments on the 2018 Rule foreshadowed this, explaining that RIN volatility had caused rating agencies to downgrade PES’s credit and classify its outlook as “negative.”³⁷ Comments further detailed that, by any metric, economic harm resulting from shutdown of PES refineries would be “severe.”³⁸ “[F]or every 100 jobs lost, Pennsylvania would lose over \$128 million in labor income, \$21 million in state and local taxes, and over \$797 million in output.”³⁹ Pennsylvania’s Governor Tom Wolf put it succinctly: “The current and proposed Renewable Volume Obligations are putting thousands of good paying jobs in my state and elsewhere at risk.”⁴⁰ EPA categorically dismissed these real concerns as lacking “sufficient evidence that the purchase of RINs, as opposed to other market factors, is responsible for the company’s difficult economic circumstances”⁴¹ EPA should not dismiss these concerns and the evidence provided in comments submitted in 2017 and additional evidence of harm in 2018.

EPA’s restrictive interpretation is inconsistent with the statute. In *Americans for Clean Energy v. EPA* (“ACE”),⁴² the D.C. Circuit invalidated EPA’s overly broad interpretation of “supply” in the general waiver provisions, concluding that breadth was unnecessary because the severe economic harm waiver protected against harmful volume requirements.⁴³ Interpreting that protection too narrowly, as EPA did in the 2018 RVO rule, equally offends the statutory language and purpose.

2. *EPA must undertake analysis of harm at the state and regional levels*

In the 2018 RVO rulemaking, EPA admittedly undertook no independent analysis of harm at the state or regional level because “an analysis tailored to assessing State or regional impacts was not practical to accomplish within the timeframe”⁴⁴ Aside from EPA’s “high-level” review, which admittedly “has limitations,”⁴⁵ EPA’s determination rests on “belie[f]” that 2018 market conditions are unlikely to make RFS compliance “more economically challenging,” and assurance that 2018 standards are “very similar” to the 2017 standards.⁴⁶ The evidence of harm in 2018 demonstrates that EPA’s assumptions were wrong. EPA should take a closer look at the evidence provided and undertake a more robust evaluation.

³⁶ PES Disclosure Statement 25, Attachment I.

³⁷ PES Comments on Proposed 2018 RVO 2-3.

³⁸ *Id.* at 3.

³⁹ *Id.*

⁴⁰ Gov. Tom Wolf, Petition for RFS Waiver Under CAA Section 211(o)(7)(A)(i) at 2 (Nov. 2, 2017), Attachment D.

⁴¹ 82 Fed. Reg. at 58,517.

⁴² 864 F.3d 691, 737 (D.C. Cir. July 28, 2017) (“ACE”).

⁴³ *ACE*, 864 F.3d at 714.

⁴⁴ Korotney Memo § A.2.

⁴⁵ *Id.*

⁴⁶ 82 Fed. Reg. at 58,518.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

3. *The basis of EPA's determination of harm has been rejected by a federal court*

To find an absence of harm, EPA relies on a 2015 theoretical assessment of RIN-price effects on the market as a whole,⁴⁷ while disregarding specific evidence of actual harm. EPA's conclusory reliance on the same preliminary assessment in denying a small refiner exemption was recently held arbitrary and capricious. In *Ergon-West Virginia, Inc. v. EPA*, the Fourth Circuit ruled that "EPA's analysis of the effect of RIN prices on Ergon's refining facility was arbitrary...because EPA ignored specific evidence suggesting that those prices had a negative effect."⁴⁸ As in *Ergon*, in its determination in 2017 and in this proposal, EPA ignores actual data regarding state and regional economic jeopardy and dramatically skyrocketing refinery operating costs.⁴⁹

The decision in *Ergon* applies here to EPA's evaluation of whether there is severe economic harm arising from the RFS. EPA cannot rely on an industry-wide study and a non-specific nationwide trend:

Insomuch as the EPA cited generally to an industry-wide study and a nonspecific nationwide trend to find that RIN prices would not harm Ergon although Ergon provided specific, contradictory evidence of hardship particular to its refinery due to RIN costs, the EPA failed to squarely address Ergon's petition with regards to RIN costs and "explain[ed] its decision in a manner contrary to the evidence before it."

Furthermore, the EPA's disregard for Ergon's RIN arguments appears inconsistent with its statement earlier in the 2016 decision that the EPA considers "RIN prices [] and the cost of compliance through RIN purchases" in making its determination. J.A. 327; accord J.A. 201 (explaining in a December 2016 memorandum that the EPA considers "RIN prices [] and the cost of compliance through RIN purchases" in evaluating a petition). Consequently, the EPA's cursory consideration and failure to address Ergon's specific evidence regarding RIN costs was an arbitrary and capricious action.⁵⁰

⁴⁷ Kortoney Memo § A.2.b n.20.

⁴⁸ No. 17-1839, 2018 WL 3483282, at *8 (4th Cir. July 20, 2018)

⁴⁹ PES Comments on 2018 Proposed RVO 2 (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-3387) (PES "needs to spend another \$369 million [on RINs] by March 31, 2018"); Valero Comments on 2018 Supplemental Notice 10 (Oct. 19, 2017) (EPA-HQ-OAR-2017-0091-4885) ("The harm to Valero that can be expected from the 2018 RVO is over \$850 million."), Attachment H; Monroe Energy Co. Comments on 2018 Supplemental Notice 18 (Oct. 19, 2017) (EPA-HQ-OAR-2017-0091-4645) ("RIN costs currently exceed every category of expense other than the crude oil Monroe purchases to refine.").

⁵⁰ *Ergon*, No. 17-1839, 2018 WL 3483282, at *26.

4. *EPA must also consider the harm to small retailers and the effect of the RIN market in creating or contributing to dramatically unfair competition in the retail market*

EPA must not continue to ignore the severe economic harm nationally that threatens the viability of small petroleum retailers, which comprise approximately 75% of fuel retailers nationwide. Comments in 2017 explained that excluding blenders from RFS obligations has allowed large, integrated retailers to use billions of dollars in RIN profits to push small retailers, who cannot recoup finished-fuel costs by selling RINs, out of business.⁵¹ EPA must not only consider the harm occurring in recent years, every year, but also what that harm means for changes in the marketplace for small businesses, communities relying on small businesses, and, in the long-term, what it is likely to mean for consumers. With the unfair competition made easier by the RIN market, large retailers have experienced growth and are squeezing out small businesses and small retailers, reducing the competition in the market for consumers. This increased consolidation is not good for consumers. Unfortunately, if EPA waits to see more absolute proof of the harm, it will be too late to correct.

EPA should not continue to act arbitrarily and contrary to the statute by failing to exercise the severe economic harm waiver.

C. EPA Must Give Meaning to the Statutory Definition of “Inadequate Domestic Supply”

Even after the D.C. Circuit's decision in *ACE*, EPA retains substantial discretion to use the general waiver authority for inadequate domestic supply. EPA should appropriately define “domestic supply” as the supply of renewable fuel produced in the U.S. and evaluate whether that supply, in terms of both its existence and its cost, is adequate to support annual requirements. EPA may define “inadequate” to include consideration of the cost of compliance. In other words, “domestic supply” means the amount of renewable fuel produced within the United States and the determination of whether that supply is “inadequate” includes not simply domestic supply but also the expected costs to obligated parties for using that supply and any other sources of renewable fuel for compliance. EPA must consider RIN prices as evidence of the costs of compliance and the costs of the renewable fuel supply used for compliance.

1. *EPA should reconsider the interpretation of the provision and decisions made in 2017*

In the 2017 Supplemental Notice for the 2018 RVO, EPA expressed “concern[] about the high cost of advanced biofuels” and the impact of imports and exports on the nation's energy independence and security.⁵² EPA enumerated several reasons to interpret “domestic supply” as referring to “volumes of domestically-produced renewable fuels.”⁵³ Under that interpretation,

⁵¹ Small Retailers Comments on Proposed 2018 RVO 3-6 (Aug. 31, 2017) (EPA-HQ-OAR-2017-0091-3572).

⁵² 82 Fed. Reg. 46,177.

⁵³ *Id.* at 46,177-78.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

EPA would “consider only whether there was an adequate supply of domestically produced volumes to satisfy the statutory volume targets.”⁵⁴ EPA reasoned:

- This interpretation is “consistent with a straightforward reading of the term ‘domestic supply’ as referring to volumes of domestically-produced renewable fuels”;
- It “may better meet the energy independence and security purposes of EISA”; and
- History demonstrates that projecting supplies of foreign-produced renewable fuel available for import “is extremely difficult.”⁵⁵

EPA invited comments on this interpretation and the possibility of applying it to reduce advanced biofuel and total renewable fuel volume requirements.⁵⁶ Just two months later, however, EPA found it “unnecessary”⁵⁷ to adopt the interpretation that Notice suggested was “appropriate.”⁵⁸ We urge EPA to reconsider the interpretation to align more closely with the statute and the plain meaning of the terms.

“Domestic” is defined as originating in, pertaining to, or relating to a country’s internal affairs. A “domestic” orange is one grown in the United States, not one grown in Brazil and transported here for sale. Likewise, the “domestic supply” of renewable fuel does not encompass fuel imported from abroad. “Domestic” must be given meaning. The statutory context of the phrase “inadequate domestic supply” reflects a focus on events within the United States. The waiver is paired in the same subsection with a waiver focused on harm to “a State, a region, or the United States.”⁵⁹ Other RFS provisions likewise emphasize domestic concerns.⁶⁰ The legislative history also indicates Congress was focused on domestic production of renewable fuels.

Comments in 2017 addressed a number of issues regarding EPA’s interpretation of the waiver provision. We urge EPA to review those comments as part of this 2019 RVO rulemaking and interpret the provision consistent with the goals and plain meaning of the statute. Commenters explained how treating foreign imports as “domestic supply” would negatively affect energy security and independence. Reliance on imports invites supply chain risk, does not ensure that lifecycle greenhouse gas requirements are met, and incentivizes additional foreign production to the detriment of domestic producers.⁶¹ Commenters provided ample evidence that, properly

⁵⁴ *Id.* at 46,177.

⁵⁵ *Id.* at 46,178.

⁵⁶ *Id.*

⁵⁷ 82 Fed. Reg. at 58,516.

⁵⁸ 82 Fed. Reg. at 46,178.

⁵⁹ 42 U.S.C. § 7545(o)(7)(A).

⁶⁰ *See, e.g., id.* § 7545(o)(2)(B)(ii) (when setting volume requirements after 2022, EPA must consider “energy security of the United States...infrastructure of the United States...job creation...rural economic development, and food prices”).

⁶¹ Valero Comments on Proposed 2018 RVO 7-9, Attachment C; *see also* AFPM/API Comments on Proposed 2018 RVO 31-33 (Aug. 31, 2018) (EPA-HQ-OAR-2017-0091-3645); AFPM Comments on 2018 Supplemental Notice (providing additional data on biomass-based diesel and proper interpretation of EPA’s waiver authorities).

interpreted, “domestic supply” was inadequate to meet statutorily-required volumes. Imports of foreign-produced fuel are not de minimis. EPA determined that imported advanced biofuel and biomass-based diesel contributed 2.298 billion RINs to total supply in 2016, or over 12.5% of that year’s total renewable fuel requirement.⁶² And EPA admitted “uncertainty” regarding whether domestic advanced biofuel could “compensate...for volumes that would not be provided through imports.”⁶³ The same conditions still exist today.

EPA must first resolve the issue of whether the term “domestic supply” should include consideration of imports *and then* consider whether use of the inadequate domestic supply waiver is necessary.

2. *EPA Must Include Only Domestically-Produced Biofuel to Determine Whether There is Adequate Domestic Supply for Meeting Statutory Volumes*

EPA should not include foreign produced biofuel imports as “domestic supply.” The RFS should not be designed to mandate fuel imports as it currently does for cellulosic, BBD, and advanced renewable fuel. EPA should set the RVO for cellulosic, BBD, and advanced renewable fuel to promote the domestic production of advanced renewable fuel but not to promote or mandate renewable fuel production in other countries. In implementing the D.C. Circuit’s directive to consider only “domestic supply” for setting the RVO and determining whether to use waiver authority, EPA must interpret the statute in a manner that is consistent with the goals of the statute—energy independence and security. Promoting or mandating renewable fuel imports to replace domestically produced petroleum fuels is not consistent with the goals of the statute. The RVO for cellulosic, BBD, and advanced renewable fuels must be set at levels that can be met with domestic production, not foreign production.

In addition, imports should not be included because of the difficulty in predicting with any confidence how much the U.S. will import in a given year as well as the difficulty in overseeing foreign production to ensure that imported fuel counted toward RFS compliance in fact meets the statute’s requirements.

a. Excluding imports is consistent with the statutory text and goals

The “inadequate domestic supply” waiver provision allows EPA to waive RFS statutory applicable volume requirements upon a determination that there is an “inadequate domestic supply” of renewable fuel.⁶⁴ The logical corollary is that EPA must consider the adequacy of domestic supply when setting the RVO each year. Neither Congress nor EPA has defined “domestic supply.” In the past, EPA has interpreted “domestic supply” to mean the amount of fuel available in the United States for consumption by the consumer.⁶⁵ The D.C. Circuit invalidated EPA’s interpretation of “supply” to mean “supply to the ultimate consumer.”⁶⁶ Because Congress chose to include the term “domestic” to modify “supply,” EPA must consider giving some meaning

⁶² 82 Fed. Reg. at 46,177, Tbls. III-1, III-2.

⁶³ *Id.* at 58,517.

⁶⁴ 42 U.S.C. § 7545(o)(7)(A), (D).

⁶⁵ 80 Fed. Reg. 77,420, 77,435 (Dec. 14, 2015).

⁶⁶ *ACE*, 834 F.3d at 696.

to “domestic” rather than assuming all “supply” of renewable fuel means “domestic supply.” In light of the D.C. Circuit’s views limiting EPA’s overreach in defining “supply,” EPA should consider how to define “domestic” to align with the purposes of the statute. EPA includes within its estimation of the available domestic supply projected volumes of imported renewable fuel.⁶⁷ EPA’s interpretation of “domestic supply” to include imported renewable fuel is contrary to the statutory purpose of the RFS.⁶⁸

Congress enacted the RFS program in an effort to promote energy security by reducing America’s dependence on fuel imports; it also wanted to promote growth in domestic energy jobs and domestic renewable fuel production. Given those goals, including foreign production of renewable fuels in the calculation of the domestic supply makes no sense, because foreign production and imports are an obstacle to energy independence, not an aid to it. Consequently, when assessing the adequacy of the domestic supply of renewable fuel, EPA should focus only on domestic production so that it does not obligate domestic refiners to purchase foreign renewable fuel. Failing to do so could lead to unintended consequences, as previously described by API:

A direct implication of setting renewable fuel volume standards that exceed the ethanol blendwall is that it encourages imported biodiesel that is produced from palm oil. EPA’s own analysis finds that biodiesel produced from palm oil fails to meet GHG emission reduction requirements of the RFS, except it is allowed if it meets grandfathering provisions of [the Energy Independence and Security Act of 2007 (“EISA”)]. Biodiesel imports into the U.S. from Indonesia, a leading palm oil producing country, have increased from zero in 2012 to 73 million gallons in 2015. This outcome of increased palm oil biodiesel consumption in the U.S. is another inconsistency with EISA’s stated purpose to [sic] “...to increase the production of clean renewable fuels”⁶⁹

b. Foreign supply available for import is difficult to predict and to oversee

Reliance on imports subjects obligated parties to unnecessary supply risks. The quantity of renewable fuel that can be imported is very difficult to predict. Market forces could direct volumes of exported renewable fuels to countries other than the United States. When projecting available supplies of renewable fuel for future compliance years, EPA typically relies on production in previous years. Thus, inclusion of foreign supplies in the volumetric requirements for any one year tends to increase the volume of renewable fuel that EPA projects is available in the future. Relying

⁶⁷ See, e.g., 81 Fed. Reg. 89,746, 89,783 (Dec. 12, 2016).

⁶⁸ This assertion is not counter the court’s statement in *ACE v. EPA* that its “interpretation of supply allows EPA to consider the amount of renewable fuel available through import...” *ACE*, 864 F.3d at 711. There, the court was construing the term “supply” as it relates to the person being supplied. In addressing an argument by EPA, the court pointed out that interpreting “supply” to mean supply to the obligated party does not make “supply” synonymous with “production.” *Id.* The court noted that, “for example,” “supply” could include imported fuel and not only fuel production. *Id.* The court was not construing the term “domestic” and did not have before it any question as to the appropriateness of including imported fuel in a determination of “domestic” supply. *Id.* at 34-35. The court’s comment is dicta and has no bearing on the construction of statutory terms not before it in that case.

⁶⁹ API, Comments Proposed 2017 RVO 23 (Aug. 10, 2016) (EPA-HQ-OAR-2016-0004-3512) (internal citations omitted).

on past performance as indicative of future performance risks improperly “locking in” such production, increasing future dependence on that foreign production.

Furthermore, EPA lacks the ability to oversee production outside of the United States and thus, cannot confirm that the renewable fuel produced abroad satisfies the greenhouse gas reduction and other requirements in the statute. Furthermore, EPA cannot easily enforce the requirements of the statute against the foreign producer even if it discovered a violation. Despite this, at least two Indonesian biodiesel producers have qualified for RINs even though their biodiesel generally does not meet the RFS program's minimum greenhouse gas reduction threshold.⁷⁰

3. The Determination of “Inadequate” Must Consider the Costs to Obligated Parties for Compliance

Since EPA designed the RFS so that compliance can be met by either purchasing renewable fuel and blending or through the purchase of separated RINs, EPA must consider the adequacy of domestic supply of renewable fuel in this context. In evaluating whether the supply of renewable fuel is adequate for purposes of a reasonable RVO, EPA must consider not only the costs of compliance by purchasing and blending renewable fuel into transportation fuel in the U.S. but must also consider whether the supply is adequate to ensure that RIN prices are stable and reasonable. Where the domestic supply is not sufficient to ensure stable and reasonable RIN prices, the supply is inadequate. As evidenced by RIN price history since 2014, the supply of RINs has demonstrated that the supply of renewable fuel is inadequate. EPA should waive statutory volumes to reduce the costs of compliance with the RFS.

V. EPA Cannot Re-Allocate RFS Obligations to Account for Small Refinery Exemptions

In designing the RFS, Congress made it clear that EPA was to set annual standards by November 30 prior to the year for which the standards would apply.⁷¹ Congress also provided EPA authority to exempt small refineries from the standards if meeting the standards would cause disproportionate economic harm for a small refinery.⁷² If EPA issues exemptions after EPA has set the annual standard, the statute does not allow EPA to adjust the annual standard for that year or the percentage requirements to account for exemptions granted for that year's annual standard. To do so would be contrary to the statute as well as run afoul of the due process owed to obligated parties who might bear a greater burden of the annual standard. It would also run afoul of the presumption against retroactive regulation.

The CAA establishes statutory targets for four nested types of renewable fuel.⁷³ EPA's responsibility is to annually publish “the renewable fuel obligation” in percentage form that

⁷⁰ 82 Fed. Reg. 40,748 (Aug. 28, 2017).

⁷¹ 42 U.S.C. § 7545(o)(3)(B)(i).

⁷² *Id.* § 7545(o)(9).

⁷³ *Id.* § 7545(o)(2)(B)(i).

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards
for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

“ensures” these requirements are met.⁷⁴ In doing so, EPA considers whether to use one or more waiver authorities to reduce the applicable volumes established by Congress.⁷⁵ EPA must consider different criteria in deciding whether to use its waiver authorities, but *none* of them allows EPA to *increase* an annual standard to account for volumes not met in prior years either because of waiver or because of volumes attributable to exempt small refineries. In fact, nothing in the statute permits EPA to increase volumes in any year to account for the waiver or exemptions granted for previous year RVOs. To do so would be contrary to the statute as well as run afoul of the due process owed to obligated parties who might bear a greater burden of the annual standard.

In addition, Congress also designed the RFS to mandate no more than 15 billion gallons of conventional ethanol in any year and no more than 4.5 billion gallons of non-cellulosic advanced biofuel in 2019.⁷⁶ EPA would be in danger of violating these limitations in a given year if it were to re-allocate exempt small refinery volumes from the prior year.

Although Congress provided EPA authority to exempt small refineries that may experience disproportionate economic hardship, nothing in these provisions authorizes EPA to re-allocate these volumes.⁷⁷ The only adjustment the statute allows EPA to make to account for small refinery exemptions is an adjustment to the applicable percentage to account for use of renewable fuel by small refineries that were exempt in the prior year.⁷⁸ In other words, when exempt refineries still use renewable fuel, those volumes should count toward compliance with the mandate and EPA can reduce the annual percentage applicable to obligated parties in setting the next year's RVO to account for “the use of renewable fuel during the previous calendar year by small refineries that are exempt.”⁷⁹

Moreover, Congress also recognized that the RFS might cause broader economic harm that may not be remedied with small refinery exemptions.⁸⁰ Re-allocation of RVO volumes to non-exempt obligated parties will cause broader economic harm and amount to unreasonable compliance burdens for non-exempt refineries. As discussed above, EPA has noted that the RIN carry-over bank is important for compliance flexibility. The RIN carry-over bank has increased from 11% for 2017 to 14% for 2018. Without the small refinery exemptions and the PES settlement, which account for as much as 2.25 billion RINs, the RIN carry-over bank would not currently hold 3.06 billion RINs; there would have been a drawdown of the RIN carry-over bank. It would no longer serve the critical role that EPA claims it must serve. Re-allocation of the RVO obligation to non-exempt refineries would also mean drawing down the RIN bank, an action that

⁷⁴ *Id.* § 7545(o)(3)(B)(ii)(II). EPA must also obligate the “appropriate parties” as a “required element” of its annual rulemaking. *Id.* § 7545(o)(3)(B)(ii)(I).

⁷⁵ *Id.* § 7545(o)(7).

⁷⁶ The annual cap on conventional biofuels—*i.e.*, ethanol—is implied. It is the difference between the total renewable fuel and advanced biofuel volumes. The cap on non-cellulosic advanced biofuels is 4.5 billion gallons in 2019. It is the difference between the advanced biofuel and the cellulosic biofuel volumes. *See* 83 Fed. Reg. at 32,028 n.10.

⁷⁷ 42 U.S.C. § 7545(o)(9)(B)(i).

⁷⁸ *Id.* § 7545(o)(3)(C)(ii).

⁷⁹ *Id.* § 7545(o)(3)(C)(ii).

⁸⁰ *See*, EPA's authority to reduce the applicable volumes when the Agency determines they would “severely harm the economy or environment of a State, a region, or the United States,” *id.* § 7545(o)(7)(A)(i); or when there is an “inadequate domestic supply,” *id.* § 7545(o)(7)(A)(ii); or when there is a “significant renewable feedstock disruption or other market circumstances” that would increase the price of BBD, *id.* § 7545(o)(7)(E)(ii).

EPA has repeatedly said is not what EPA intends to do when setting the RVO, bringing the system to the brink of illiquidity (further complicating the placement of the obligation in the wrong location in the system).

VI. EPA Should Remove the Export RVO and Treat All Domestically-Produced Renewable Fuel Equally

EPA should revise the RFS to allow all domestically produced biofuel to be used for compliance under the RFS, including ethanol exported for use as transportation fuel and exported biodiesel. EPA should eliminate the export RVO, eliminate the denaturant prerequisite for RINs for renewable fuel, and allow RINs for all exported biofuels. These revisions will promote the purposes of the RFS by supporting domestic renewable fuel production, correct EPA's punitive treatment of exports under the current program rules, and add much-needed liquidity to the RIN market.

Such changes more closely adhere to the text of the RFS statute and contrary to assertions by some, the changes will not destroy demand for ethanol or biodiesel or for renewable fuel feedstocks at home.

A. The current system is inconsistent with the RFS statute

From the start of the RFS program, EPA treated exported renewable volumes outside the realm of the program. EPA devised a parallel program under which RINs attached to renewable fuel that is exported cannot be used by a party to comply with its RVO.⁸¹ Instead, the RINs must be retired with no compliance benefit under a separate export RVO ("ERVO").⁸² In this way, the RFS program has historically kept off-the-books volumes of renewable fuel *produced in the United States* that otherwise would count toward compliance under the RIN accounting system.

This anomalous treatment of exported renewable volumes has no basis in the statute, which focuses on the introduction into commerce of renewable fuel, not on the geography of disposition or consumption of the fuel.⁸³ The plain language of 42 U.S.C. § 7545(o)(2) and (o)(3) requires EPA "ensure that transportation fuel sold or introduced into commerce in the United States . . . , on an annual average basis, contains at least the applicable volume of renewable fuel, advanced biofuel, cellulosic biofuel, and biomass-based diesel" provided in § 7545(o)(2)(B).⁸⁴ Under the statute, renewable fuel is by definition transportation fuel, whether ultimately used in or outside the United States.⁸⁵ "Introduction" into commerce is not synonymous with "used" or

⁸¹ 40 C.F.R. § 80.1130 (replaced under RFS2 with the very similar 40 C.F.R. § 80.1430); *see also* 40 C.F.R. § 1427(c).

⁸² EPA accomplishes this by imposing a parallel regulatory obligation applicable only to exported volumes, known as an Export Renewable Volume Obligation ("ERVO"). Meeting an ERVO has no relation to the statutory compliance obligation required by the statute.

⁸³ In fact, there are indications in the statute to the contrary, that Congress intended to place no restriction on the geographic distribution of renewable fuel. *See* 42 U.S.C. § 7545(o)(2)(A)(iii)(II)(aa) (prohibiting any regulations that "restrict geographic areas in which renewable fuel may be used.").

⁸⁴ 42 U.S.C. § 7545(o)(2)(A).

⁸⁵ *See id.* § 7545(o)(1)(J) ("The term 'renewable fuel' means fuel that is produced from renewable biomass and that is used to replace or reduce the quantity of fossil fuel present in a transportation fuel.").

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards
for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

“consumed.”⁸⁶ Therefore, if the renewable fuel is produced and offered for sale to anyone while the fuel is physically in the U.S., then it would be “introduced in commerce in the United States,” regardless of whether it is destined for export. As a result, this plain language calls for providing that all renewable fuel introduced in the U.S. can generate credits toward compliance with the renewable fuel mandate in the statute.

There is nothing in the text of the statute that forecloses this interpretation. Nor does the legislative history indicate that Congress intended to create a disparity between domestically produced renewable fuel that is exported and renewable fuel used in the United States.

The ERVO is contrary to how the RFS program is supposed to work—incentivizing increased renewable fuel production year-over-year. As the D.C. Circuit recently observed, “[T]he Renewable Fuel Program’s increasing requirements are designed to force the market to create ways to produce and use greater and greater volumes of renewable fuel each year.”⁸⁷ EPA’s interpretation of § 7545(o) to treat consumption as the measurement of compliance with the statutory volumes “flouts that statutory design” because instead of forcing greater production, the ERVO creates a disincentive for further domestic production.⁸⁸ EPA cannot continue with such a “goal-defying (much less that text-defying) statutory construction.”⁸⁹ Designed correctly, the RFS can promote continued growth in domestic biofuel production. Eliminating the ERVO would remove the burden on exports and incentivize further increases in production—a conclusion supported by a recent report issued by Charles River Associates.⁹⁰

That EPA has previously *misinterpreted* the statute does not mean the Agency is forever required to maintain its faulty interpretation. The agency can change course to one consistent with the statute as long as it provides a reasoned explanation for doing so.⁹¹ “[P]revious statutory violations,” of course, “cannot excuse” new ones.⁹² Regardless of EPA’s policy preference for encouraging the domestic consumption of renewable fuel, exported renewable fuel is part of the U.S. supply of renewable fuel. Therefore, to be true to the statutory text, RINs associated with exported renewable volumes should also be available for compliance with the annual RVO.

⁸⁶ See, e.g., *United States v. Hill*, 248 U.S. 420 (1919) (“Commerce includes the transportation of persons and property no less than the purchase, sale, and exchange of commodities.”); *Bell v. Porter*, 159 F.2d 117, 119 (7th Cir. 1946), *cert. denied*, 330 U.S. 813 (1947) (Goods may move in commerce though they never enter the field of commercial competition).

⁸⁷ *ACE*, 864 F.3d at 710.

⁸⁸ *Id.*

⁸⁹ *Id.* (quoting *Advocate Health Care Network v. Stapleton*, 137 S. Ct. 1652, 1662 (2017)).

⁹⁰ Charles River Associates, *Balancing the Treatment of Ethanol Exports, Imports, and Consumption in the Renewable Fuel Standard 2* (Aug. 2017), provided here as Attachment M.

⁹¹ *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009). In fact, a “change in administration brought about by the people casting their votes is a perfectly reasonable basis for an executive agency’s reappraisal” of its regulations and programs. *Nat’l Ass’n of Home Builders v. EPA*, 682 F.3d 1032, 1038 & 1043 (D.C. Cir. 2012) (citing *Fox*, 556 U.S. at 514-15 (Rehnquist, J., concurring in part and dissenting in part)).

⁹² *New Jersey v. EPA*, 517 F.3d 574, 583 (D.C. Cir. 2008).

B. Eliminating the ERVO Makes Policy Sense and Serves the Goals of the Program

Eliminating the ERVO is not only consistent with the statute, it is good public policy because it better serves the purposes of the RFS—domestic job creation, energy independence and security, and increased domestic production of renewable fuels—than the program's current punitive treatment of exports. The proposed change will also remove a distortion that makes America less competitive in global markets without undermining the greenhouse gas-reduction benefits of the RFS. Such a change has already been suggested by the Bipartisan Policy Center in a 2014 report, which suggested that “eliminat[ing] the exporters' RVO” could allow “the export of biofuels [to] meaningfully contribute to satisfying the RFS mandates.”⁹³

1. Allowing RINs for exported renewable fuel corrects the distorted position of exports in comparison to domestically-consumed fuels and in global markets

The ERVO creates a disparity between volumes of domestic renewable fuel that remain in the United States and those that do not and it gives preferential treatment to imports. Because RINs associated with exported renewable fuel must be retired against a fictional RVO, this fuel is disadvantaged in comparison with domestically-produced renewable fuel that remains in the United States. This distinction is not rational when *all* domestically-produced renewable fuel serves the purposes of the RFS statute and benefits domestic producers. Treating domestically consumed ethanol and exported ethanol equally will drive up ethanol production, increase demand for corn, generate additional value for ethanol producers, create jobs and support American energy dominance—a goal of the current administration.⁹⁴

Similarly, EPA's current regulations have a punitive effect on exports. Imported renewable fuel does not serve the purposes of the program, but foreign-produced volumes imported into the United States receive preferential treatment in the form of a RIN that can be separated upon blending and either used for annual compliance purposes or sold. Meanwhile, and at the expense of greater energy independence and security, biofuels produced in the U.S. that are ultimately used in place of petroleum-based transportation fuel abroad do not generate a RIN. Eliminating the ERVO so that these volumes generate RINs that can be used for RFS compliance would remove this penalty on exports. Such a regulatory change would improve the competitive price position of U.S.-produced ethanol in global markets⁹⁵ and drive additional demand for U.S. corn. The value of the RIN would assist exporters in overcoming protective tariffs of importing countries, making increased mandates in other countries more economical.⁹⁶

⁹³ Bipartisan Policy Center, *Options for Reforming the Renewable Fuel Standard* 30 (Dec. 2014), Attachment N.

⁹⁴ President Trump Vows to Usher in Golden Era of American Energy Dominance, <https://www.whitehouse.gov/articles/president-trump-vows-usher-golden-era-american-energy-dominance/> (June 30, 2017).

⁹⁵ Charles River Associates, *Unobligated RINs for Renewable Fuel Exports: Impact on Ethanol Volumes* (Oct. 16, 2017), Attachment O.

⁹⁶ Charles River Associates, *Balancing the Treatment of Ethanol Exports* 2, Attachment M.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

By increasing demand for American ethanol, export RINs will support the price of ethanol and allow plants to run at higher rates. This will help maintain America's position as the best ethanol manufacturer in the world. Most importantly, smaller producers and co-ops will, for the first time, be able to capture the economic upside of RINs. Historically, separating and selling a RIN by biofuel producers generally required direct control of gasoline blending infrastructure. Going forward, ethanol producers who export their products can capture RIN values for themselves.

2. *Eliminating the ERVO supports the goals of the RFS program*

Allowing RINs for exported renewable fuel would better support the statutory goals of the RFS than the current regulatory regime. Those goals are chiefly (1) job creation;⁹⁷ (2) "greater energy independence and security"; and (3) "increase[d] . . . production of clean renewable fuels."⁹⁸

The U.S. exported nearly 1.5 billion gallons of renewable fuel in 2017, setting a new record for ethanol exports.⁹⁹ This represents *actual* domestic production but this fuel does not generate RINs. EPA acknowledges that

the rate of growth in the use of ethanol in the U.S. has decreased in recent years as a result of a number of factors, including that the gasoline market has to a large degree become saturated with gasoline that contains 10 volume percent ethanol (E10), favorable blending economics diminish for gasoline-ethanol blends beyond E10, gasoline demand has leveled off, and efforts to expand the use of higher ethanol blends such as E15 and E85 have not been sufficient to maintain past growth rates in total ethanol use.¹⁰⁰

This means that continued growth in domestic ethanol production depends in large part on appropriately incentivizing exports of ethanol.¹⁰¹ Currently, EPA discourages exports by creating a fictional RVO against export RINs that must be retired. Eliminating the ERVO would make exporting more attractive to domestic producers by giving them access to additional markets for their products without the burden of retiring the RIN just because they export. Ensuring that RINs can be generated for compliance by *all* renewable fuel produced in the U.S. would provide

⁹⁷ Energy and Policy Act of 2005, Pub. L. 109-58, 119 Stat. at 659.

⁹⁸ See *ACE*, 864 F.3d at 697 (quoting Preamble to Energy Independence and Security Act of 2007, Pub. L. No. 110-140, 121 Stat. at 1492.)

⁹⁹ EIA, Today In Energy, *U.S. exported a record amount of fuel ethanol in 2017* (Apr. 27, 2018), <https://www.eia.gov/todayinenergy/detail.php?id=35972>.

¹⁰⁰ David Korotney, EPA, Market impacts of biofuels in 2019 (June 26, 2018) (EPA-HQ-OAR-2018-0167-0025).

¹⁰¹ EVA's analysis concluded that "the 'benefit' of the RFS program going forward is effectively limited to pushing the ethanol blend percentage beyond 10% in an attempt to incentivize demand for that fuel. . . . If ethanol can be sold to blenders at a lower price than wholesale gasoline, there is no reason blending would *not* occur up to the 10% blend wall." Consequently, allowing RINs for exports supports additional markets for domestic ethanol produced in excess of 10% of the U.S. motor gasoline pool. See EVA Comments 4, 5.

opportunities for expanded domestic production, estimated to be as much as an additional 1.2 billion gallons per year (greater than baseline export levels).¹⁰²

In addition, exporting renewable fuels positively impacts the U.S. economy and protects jobs in the biofuels industry, which helps to satisfy the RFS program's goal of job creation. The increased demand for domestic production that would result from eliminating the ERVO would add 26,000 jobs annually, which will contribute to regional and national economic growth.¹⁰³ As many as 1,200 additional temporary jobs could be created over the next three years as a result of specific investments in capacity expansion.¹⁰⁴ This will undoubtedly benefit American corn farmers and rural farming communities in addition to renewable fuel producers.

The proposed change would also enhance our energy and economic security by reinforcing our growing role as an energy superpower. Given that one of the goals of the RFS is to enhance the United States' energy security, it is difficult to imagine that Congress intended the program to replace import of petroleum with imports of renewable fuel, reinforcing the nation's dependence on foreign fuel. Allowing RINs associated with exported renewable fuel to be used for compliance with the RVO would restore the proper balance between renewable fuel imports and exports in the market and support the RFS program's purpose of increased energy independence and security. This change is entirely consistent with President Trump's recommitment to national energy security and special emphasis on U.S. energy exports.¹⁰⁵

C. Eliminating the ERVO Would Ensure Greater Liquidity in the RIN Market

A significant consideration in setting annual RVOs is ensuring a "liquid and well-functioning RIN market upon which success of the entire program depends."¹⁰⁶ In the proposal, EPA explains the gravity of its concern that the RIN bank remain healthy:

An adequate RIN bank serves to make the RIN market liquid. Just as the economy as a whole functions best when individuals and businesses prudently plan for unforeseen events by maintaining inventories and reserve money accounts, we believe that the RFS program functions best when sufficient carryover RINs are held in reserve for potential use by the RIN holders themselves, or for possible sale to others that may not have established their own carryover RIN reserves. Were

¹⁰² See Charles River Associates, *Unobligated RINs for Renewable Fuel Exports* 2. That number represents preventing a loss of 600 million gallons a year based on current policy, and an additional 600 million gallons of production capacity expansion.

¹⁰³ Charles River Associates, *Balancing the Treatment of Ethanol Exports* 3, 10, Attachment M. While assigning unobligated RINs to ethanol exports will contribute to the economy, it does not follow that higher RIN prices increase total economic activity. In fact, the opposite is likely true given the volume of ethanol exports compared to domestic ethanol consumption. RIN costs are mostly borne by US businesses and consumers. Therefore, the proposed regulatory change adds the most value when RINs for ethanol exports do not include expanded RFS obligations. *Id.* at 3.

¹⁰⁴ *Id.* at 11.

¹⁰⁵ President Trump Vows to Usher in Golden Era of American Energy Dominance, <https://www.whitehouse.gov/articles/president-trump-vows-usher-golden-era-american-energy-dominance/> (June 30, 2017).

¹⁰⁶ 83 Fed. Reg. at 32,029.

there to be no RINs in reserve, then even minor disruptions causing shortfalls in renewable fuel production or distribution, or higher than expected transportation fuel demand (requiring greater volumes of renewable fuel to comply with the percentage standards that apply to all volumes of transportation fuel, including the unexpected volumes) could lead to the need for a new waiver of the standards, undermining the market certainty so critical to the RFS program.¹⁰⁷

Revising the regulatory treatment of exported renewables would help to resolve the RIN liquidity concern in both the short- and long-term. As ethanol exports continue to increase, the RINs from such exports would become part of the RINs market, increasing liquidity and ameliorating the potential for RINs price spikes that occur when renewable blending capacity is constricted.

Economic studies have demonstrated that a significant share of the burden of higher RIN prices fall on merchant and other non-integrated refiners.¹⁰⁸ This is due to blenders capturing margins from RINs. Relief from this burden is possible through providing unobligated RINs for ethanol exports,¹⁰⁹ as the change would make an estimated 1.2 billion RINs available in the market in every compliance year, and it would incentivize domestic renewable production to meet growing demand abroad.

D. Eliminating the ERVO Would Not Undermine Demand at Home for Renewable Fuels or for Corn As A Feedstock

If the export RINs policy were enacted, domestic consumption of ethanol and demand for corn as a feedstock would not be harmed as ethanol volumes increased.

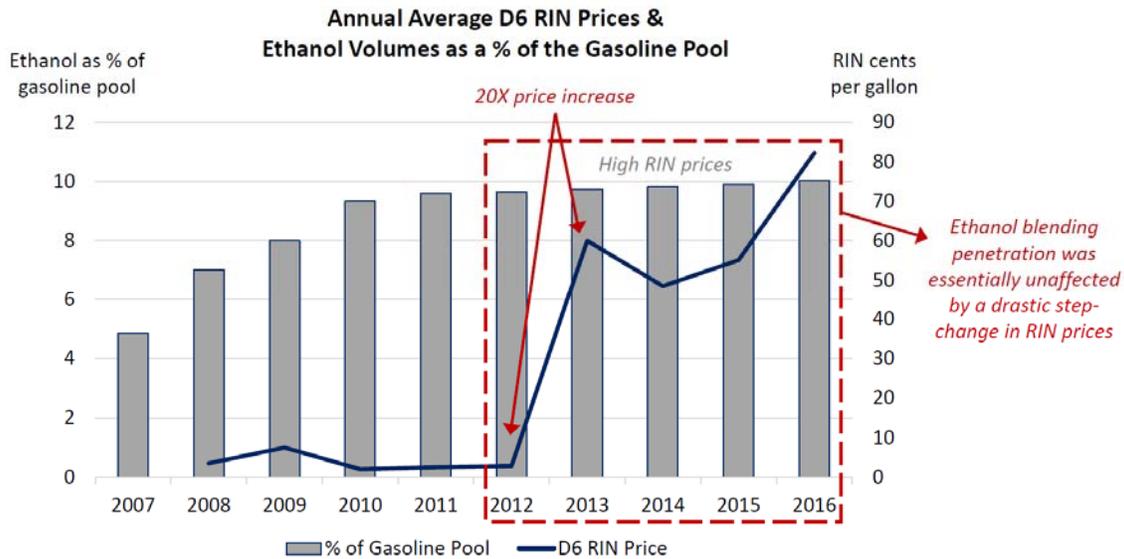
The addition of export RINs to the market are likely to decrease the price of RINs. However, this will not have a negative impact on the domestic consumption of renewables. The following chart (based on RVO and ethanol volumes from EIA and RIN pricing from Argus) shows that high RIN prices do not correlate with increased ethanol blending.

¹⁰⁷ *Id.*

¹⁰⁸ Charles River Associates, *RINs Market Frictions and the RFS Point of Obligation* (2017), Attachment P.

¹⁰⁹ Charles River Associates, *Balancing the Treatment of Ethanol Exports* 3, Attachment M.

Valero Comments on EPA’s Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167



Between 2012 and 2013, RIN prices increased by 20 times. Yet, during the same time, the volume of ethanol in the gasoline pool was nearly unchanged.¹¹⁰ In fact, EIA recently confirmed that lower RIN prices (such as would result from the increasing RINs pool if this proposal were enacted) do not impact domestic ethanol consumption.

This regulatory change would not cannibalize domestic consumption because ethanol is the most economic option for octane enhancement (a dynamic that would be expected to persist if the ERVO were eliminated).¹¹¹ Overall, continued domestic use of ethanol for octane and increased exports would result in a net increase in ethanol demand.¹¹²

E. Eliminating the ERVO is Consistent with International Trade Agreements

Critics of the proposal to allow RINs assigned to exported volumes to be separated and used for compliance argue that the proposal may present problems with the United States’ trading partners. Arguments that the change could lead to dumping in foreign markets, create a subsidy that is prohibited by international trade agreements (including those under the auspices of the World Trade Organization (“WTO”)), or result in countervailing duties are speculative at best for several reasons.

¹¹⁰ Critics of the proposal to allow RINs for exported volumes argue that it will not cure the blendwall. This is a strawman. The proposed change to the treatment of renewable fuel exports is not intended to cure the blendwall. Rather, it is intended to add liquidity to the RINs market by allowing all biofuel produced in the U.S. to count toward compliance, resulting in reasonable RINs prices and RFS compliance costs that do not subject merchant and, small retailers, and others among the fuel value chain to harm.

¹¹¹ Charles River Associates, *Unobligated RINs for Renewable Fuel Exports* 4, Attachment O.

¹¹² *Id.* at 3.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

First, WTO rules typically do not apply to environmental conservation measures. Article XX of General Agreement on Tariffs and Trade ("GATT") provides

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures ... relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.¹¹³

This exception has been used to except the RFS program in general from WTO restrictions. The proposed regulatory change would be adopted in order to allow that overall program to operate more efficiently and effectively—very likely making it exempt from WTO concerns. In addition, demonstrating a WTO violation would require evidence of harm to foreign biofuels producers which would be difficult. There is no evidence that treating exported ethanol the same as domestically consumed ethanol (including imports) would result in the loss of existing ethanol production capacity in countries that would purchase U.S. ethanol.

Moreover, the current treatment of exported volumes under the RFS may be considered to be a violation of international trade agreements. The proposal to eliminate the ERVO would rectify these concerns. These issues are discussed in brief below, but Valero incorporates into its comments analysis conducted by Sidley Austin LLP.¹¹⁴

1. Modifying the export treatment within the RFS would not constitute a violation of GATT 1994

Modifying the treatment of exported renewable fuels would not violate the WTO's General Agreement on Tariffs and Trade 1994 ("GATT 1994").¹¹⁵ In fact, in modifying the RFS to allow exported renewable fuel volumes to enjoy the same RIN benefit as volumes consumed at home, EPA will be viewed as addressing compliance flaws posed by the current ERVO and will bring the RFS program into compliance with international trade laws.

Article XI:1 of GATT 1994 bars "prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences [*stet*] or other measures" that are "instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party." As Sidley Austin explained,

Today's RFS discriminates against U.S. exports of renewable fuels by not allowing those volumes to receive the same benefits as volumes consumed (blended)

¹¹³ See GATT Art. XX(g) (exempting

¹¹⁴ See Letter from Andrew W. Shoyer, Sidley Austin, to EPA Admin. Scott Pruitt (Oct. 19, 2017) (EPA-HQ-OAR-2017-0091-4716), Attachment Q.

¹¹⁵ *Id.* at 1.

domestically....Currently, the EPA requires that a person exporting renewable fuel from the United States surrender RINs. On the other hand, if the renewable fuel is sold in the domestic market, the sale does not attract an obligation to surrender RINs. In the domestic market, the obligation to surrender a RIN is at the point that it is blended with hydrocarbon-based fuels. Thus, the existing requirements create an artificial disincentive for exporting renewable fuels, and creates an incentive for selling renewable fuel in the domestic market. This is indeed a distortion of the market through government intervention, and...appears to amount to a violation of Article XI:1 of GATT 1994.¹¹⁶

For purposes of compliance with international trade agreements, the proposed modification would remove an artificially created disincentive against exportation rather than creating an incentive for exportation.¹¹⁷ By eliminating the ERVO, EPA would allow exported renewable fuel volumes to enjoy the same RIN benefit as volumes consumed at home, which would be viewed as rectifying these concerns.¹¹⁸

2. *Allowing export RINs to be used for compliance should not result in “dumping”*

Allowing export RINs to be used for RFS compliance purposes should not result in dumping, which is prohibited by Article VI of GATT 1994. “Dumping, by which products of one country are introduced into the commerce of another country at less than the normal value of the products is to be condemned if it causes or threatens material injury to an established industry.”¹¹⁹

There is no reasonable argument that allowing the RINs to attach to exports would allow for exports to occur at a price that is artificially lower than the “normal price” for domestic sale of ethanol. The proposed change would not provide any financial benefits to exports of ethanol above and beyond domestic consumption (for which RINs already attach). In addition, the scope of the RFS program as a whole means that the price implications of the proposed change would be negligible. And, to the extent that the international ethanol market is influenced by U.S. policy, that influence is dominated by the overall RFS program, the vast majority of which is unaffected by this proposed change.

As discussed above, the change would support the functioning of the RFS program, which is exempt as an environmental conservation measure, and there is no evidence that the change would harm foreign producers of renewable fuel.

¹¹⁶ *Id.* at 1, 3.

¹¹⁷ *Id.* at 3.

¹¹⁸ *Id.* at 1, 3. Although GATT 1994’s general prohibition on restricting trade “is generally viewed as a prohibition to disadvantage imports, the WTO has applied this prohibition to government measures that restrict exports as well.” *Id.* at 4.

¹¹⁹ GATT Art. VI:1.

3. *The proposed change does not create a prohibited subsidy or result in countervailing duties*

The WTO's Subsidies and Countervailing Measures Agreement ("SCM Agreement") prohibits subsidies contingent on exports and subsidies that cause adverse effects to the interests of other WTO members.¹²⁰ Annex I of the SCM Agreement lists a variety of prohibited subsidies, and the proposed change is not similar to any of the listed subsidies. The proposed change would result in exported ethanol being treated the same as domestically consumed ethanol. It would rectify an existing obstacle to exports, and would not create any scheme to privilege or promote exports above and beyond domestic use. Again, the change would be covered by the exception for environmental conservation measures, and there is no evidence that treating exported ethanol the same as domestically consumed exports would result in the loss of existing ethanol production capacity in countries that would purchase U.S. ethanol. And, it is likely the proposed change would be considered part of the overall program and therefore subject to the general exception for environmental conservation measures in GATT Article XX.

VII. EPA must consider the point of obligation each time it establishes the annual percentage standards

Although EPA may attempt to declare (as it has in the last two annual rulemakings) issues related to who is "appropriately" charged with ensuring that the annual volumes of renewable fuel required by the statute are met are beyond the scope of rulemaking, EPA does not have the option to exclude such comments aimed at informing the agency of its failure to satisfy a required element of this rulemaking. Valero's comments on the point of obligation are not outside the scope of this rulemaking and must be given full consideration by EPA despite the Agency's insistence that it is not "reopening" this issue. The D.C. Circuit in *ACE*¹²¹ did not address this issue because the court had already decided to remand the 2014-2016 RVO rule to EPA. The fact that the court left EPA with only the choice of venue for its consideration of the point of obligation—on remand or in response to a rulemaking petition¹²²—indicates that the court does not consider the point of obligation outside the scope of the RVO.

As presented in the various administrative petitions submitted to the agency and in briefs to the D.C. Circuit, the statute requires that EPA (1) regulate refiners, importers and blenders "as appropriate" to ensure transportation fuels contain renewable fuels and (2) consider the appropriateness of the entities regulated under the RFS every time it sets the RVO. The primary statutory goals of the RFS are "greater energy independence and security and increasing production of clean renewable fuels."¹²³ To meet these goals, the statute assigns EPA certain duties. First, it requires EPA to promulgate regulations that regulate the appropriate parties to

¹²⁰ *SCM Agreement*, Article 3.1, available at https://www.wto.org/english/docs_e/legal_e/24-scm.pdf ("the following subsidies, . . . shall be prohibited: (a) subsidies contingent . . . upon export performance; (b) subsidies contingent . . . upon the use of domestic over imported goods").

¹²¹ 864 F.3d at 737.

¹²² *Id.* at 85.

¹²³ Energy Independence and Security Act of 2007 ("EISA"), Pub. L. No. 110-140, tit. X, § 1001-1002, 121 Stat. 1492 (2007).

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

ensure that transportation fuel introduced into commerce contains renewable fuel.¹²⁴ Second, it assigns EPA an annual, mandatory duty to evaluate whether the appropriate parties are regulated:

- Not later than November 30 of each calendar year, EPA “shall determine and publish...the renewable fuel obligation that ensures the requirements of paragraph (2) are met.”¹²⁵
- The renewable fuel obligation shall “be applicable to refineries, blenders, and importers, *as appropriate*.”¹²⁶

It is clear that this is not a one-time requirement, but rather, an annual obligation because EPA cannot fulfill its duty to ensure that the renewable volumes prescribed by the statute for a given year are met without considering whether it has regulated the appropriate parties at that point in time.¹²⁷ It is not sufficient to regulate the parties that were appropriate at one point in time or continue with the parties regulated at one time when a change would improve the performance of the program.

EPA acknowledged the need to reevaluate the appropriateness of the regulation related to “appropriate” parties when the agency committed to reevaluate the point of obligation as circumstances change.¹²⁸ It is equally clear that EPA must fulfill its annual duty to consider the point of obligation within sufficient time to publish a final rule every November.¹²⁹ EPA has not fulfilled its duty with regard to the annual percentage standards for 2019 in this proposal.

Considering the point of obligation each time EPA sets the annual percentage standards serves the statute's goals of “increasing production of clean renewable fuels” and “greater energy independence and security.” EPA cannot ignore the positive effect that changing the point of obligation would have on consumption of all renewable fuels. Nor can EPA ignore how the current point of obligation promotes fuel exports and supports biofuel imports. Neither can EPA continue to rely on a regulation that amounts to restructuring a segment of the U.S. economy on the basis of administrative convenience or because some economic sectors are profiting from the regulatory structure in a way that does not serve the statutory purposes. When EPA “lay[s] claim to extravagant statutory power over the national economy while at the same time strenuously

¹²⁴ 42 U.S.C. § 7545(o)(2)(A)(iii).

¹²⁵ *Id.* § 7545(o)(3)(B)(i).

¹²⁶ *Id.* § 7545(o)(3)(B)(ii)(I).

¹²⁷ In disclaiming this duty, EPA has in other contexts attempted to rely on *Valero Energy Corp. v. EPA*, No. 7:17-CV-00004, 2017 WL 8780888 (N.D. Tex. Nov. 28, 2017), but the district court in that case did not address EPA's annual rulemakings or whether EPA must consider comments regarding the point of obligation in that context. That court's analysis was also flawed. It conflated the general requirement in § 7545(o)(2)(A)(iii) to promulgate “compliance provisions” with the specific requirements applicable to annual determinations in § 7545(o)(3)(B). It failed to explain what purpose the annual requirement would serve if it were met merely by the compliance provision. And it treated the first “required element” of EPA's annual determination differently from the other two. 2017 WL 8780888, at *4-*6.

¹²⁸ 75 Fed. Reg. 14,670, 14,722 (Mar. 26, 2010) (“We will continue to evaluate the functionality of the RIN market. Should we determine that the RIN market is not operating as intended, driving up prices for obligated parties and fuel prices for consumers, we will consider revisiting this provision in future regulatory efforts.”).

¹²⁹ 42 U.S.C. § 7545(o)(3)(B)(i); 40 C.F.R. § 80.1405(b).

asserting that the authority claimed would render the statute unrecognizable to the Congress that designed it," such an announcement should be greeted with skepticism.¹³⁰

Moreover, EPA itself has recognized a "guiding principle" of the RFS is that "the program should preserve existing business practices for the production, distribution, and use of both conventional and renewable fuels."¹³¹ In failing to consider the point of obligation, EPA has flouted this principle, preferring instead to try to force merchant refiners to change their business practices in order to add blending facilities and to risk further consolidation in the fuel industry rather than fix the underlying flaws in the structure of the RFS.

In the context of EPA's proposed denial of their administrative petitions regarding the definition of "obligated parties" and in the context of other annual rulemakings, Valero and many other parties have explained the numerous, significant benefits that would result from EPA defining "obligated party" consistent with the federal excise tax definition of "position holder." These benefits include (but are not limited to) reducing (1) administrative burden on EPA; (2) harm to obligated parties that must purchase RINs on the market to satisfy their annual RVOs; (3) market frictions that undermine the program's ability to increase renewable fuel penetration; (4) volatility in the RIN market; (5) unfair competition experienced by small retailers; and (6) opportunities for speculation and fraud in the RINs market.¹³² These benefits would still be achieved today if EPA were to properly align the point of obligation with position holders.

IX. RIN Market

While we commend the EPA for opening the dialogue on market reforms, Valero nevertheless believes that RFS implementation reforms of the sort discussed elsewhere in these comments (including counting RINs generated by exports and shifting the point of obligation) are necessary prerequisites to resolving the structural causes of manipulation and speculation.¹³³ Valero is also very concerned that EPA has already delayed taking action to reduce the harms arising from the RIN market problems. Valero urges EPA to advance its multi-year discussion of RIN market concerns by issuing concrete rule proposals designed to protect the integrity and orderly, efficient functioning of the market. EPA has received comments, information and

¹³⁰ *Util. Air Regulatory Grp. v. EPA*, 134 S. Ct. 2427, 2444 (2014) (internal citations omitted).

¹³¹ 71 Fed. Reg. 55,552, 55,557 (Sept. 22, 2006).

¹³² *See, e.g.*, Valero Comments on Proposed Denial of Petitions for Rulemaking to Change the RFS Point of Obligation (Feb. 22, 2017) (EPA-HQ-OAR-2016-0544-0274), Attachment R; PBF Energy Comments on Proposed Denial (Feb. 22, 2017) (EPA-HQ-OAR-2016-0544-0373); Small Retailers Coalition Comments on Proposed Denial (Feb. 22, 2017) (EPA-HQ-OAR-2016-0544-0344); Small Refiners Coalition Comments on Proposed Denial (Feb. 22, 2017) (EPA-HQ-OAR-2016-0544-0406); Monroe Energy Comments on Proposed Denial (Feb. 22, 2017) (EPA-HQ-OAR-2016-0544-0368); Valero Comments on Proposed 2017 RVO (July 11, 2016) (EPA-HQ-OAR-2016-0004-1746), Attachment S; Valero Comments on Proposed 2018 RVO, Attachment C.

¹³³ Some have argued that the RFS credit trading program is not consistent with the statute. However, the appropriate placement of the point of obligation, by obligating blenders as well as refiners and importers, would alleviate the harm caused by alleged statutory violation.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards
for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

recommendations regarding this issue in prior rulemakings; EPA should consider those comments as well as ones submitting in this docket and not delay in taking action.¹³⁴

The RIN market is susceptible to manipulation and other market abuses, such as hoarding, which contribute to volatility, price spikes, and uncertainty that increase costs and threaten economic stability for RFS program participants. By taking steps to improve transparency, liquidity, and implementing certain basic market protections, the EPA can ensure that the market is not susceptible to excessive speculation or abusive market practices.

A. The Similarity of the RIN Market and Commodity Markets

RIN trading is very similar to trading in commodities and commodity derivative financial instruments like futures. There is a finite deliverable supply of both commodities and RINs, and temporal differences in supply and demand can lead to episodic volatility and price spikes. As with commodity futures contracts, RINs have a specific expiration date. Just as the seller of a commodity futures contract has an obligation to deliver at a future contract expiry date, most RINs are traded on a forward basis with a title transfer date tailored to meet periodic RVO compliance dates. RIN two-year expiration cycles and periodic compliance retirements resemble both literal expiration cycles for agricultural commodities and contractual tenor expiration cycles for commodity futures contracts.

The RIN market is a largely unregulated over-the-counter¹³⁵ commodity derivatives market subject to market frictions and opacity in trading, an inelastic demand curve, as well as illiquidity, scarcity, and volatility. As regulators have long observed in similar markets in the commodities space, these factors can create obstacles to efficient price discovery and can create incentives to undermine market integrity by engaging in manipulative behaviors. Due to the practical similarities between RIN markets and commodity derivative and spot markets, a number of the proposed reforms discussed below are modeled after existing regulations designed to protect market participants, promote market integrity, and foster efficient price discovery that have been implemented by federal agencies, such as the Commodity Futures Trading Commission (“CFTC”), which have many decades of experience in regulating markets.¹³⁶ Valero addresses below topics

¹³⁴ Valero has submitted comments and recommendations in EPA RFS rulemaking dockets aimed at improving RIN market transparency and reducing market manipulation on previous occasions. Concerns raised by Valero in these submissions remain valid, in that no market reforms have been adopted to address the concerns and the issues persist. In June 2016, Valero indicated that potential RIN speculation and fraud might undermine the RFS program, including with reference to experts who described the failure of the RIN system to function as intended. *See* Valero Petition for Rulemaking: Renewable Fuel Standard Definition of Obligated Party – 40 C.F.R. § 80.1406 at 24 (June 13, 2016), Attachment T. In February 2017, Valero described harms under the current RFS arising from RIN fraud, RIN speculation, and volatility and the impacts on small and independent refiners and small retailers and the harm to the program, renewable producers, and ultimately consumers. *See* Valero Comments on Proposed Denial 9, 15, 26, Attachment R. In August 2017, Valero identified potential market manipulation occurring in the RIN market and other RIN market operational problems, explained why the RIN market is vulnerable to manipulation, and recommended a number of fundamental changes and other measures that EPA should implement to resolve the problems with the RIN market. *See* Valero Comments 2018 Proposed RVO 14-18, Attachment C.

¹³⁵ Over-the counter refers to commodities, stocks, etc. that are traded off an exchange.

¹³⁶ Valero supports EPA's ongoing dialogue with the CFTC to develop techniques that could be employed to minimize fraud, market abuses or other violations, and to conduct appropriate oversight of the RIN market. *See* “Memorandum of Understanding Between the Environmental Protection Agency and the Commodity Futures Trading Commission

raised by EPA in its comment solicitation to help EPA better understand the illiquidity, instability, price discovery problems, potential manipulation, and lack of transparency in the RIN market.

B. Illiquidity

1. The RIN market is often illiquid

RIN markets are often very illiquid. This is due in part to the finite production of RINs over time, which limits the possibility of a substantial oversupply and creates a high floor for demand. There also is the potential for hoarding behavior by some market participants.

As a result of the mismatch between the RFS point of obligation and RIN production, there are not enough RINs available in the market to satisfy RVOs at any given time. Only RINs available in the market contribute to liquidity; warehoused RINs do not contribute to short- or medium-term supply curves relevant for the next RVO.

2. Illiquidity undermines price discovery and market stability

It is widely accepted in the financial economics literature that liquidity enhances price discovery—*i.e.*, the incorporation of new information into asset pricing. In an illiquid market, bid-ask spreads tend to be wider, raising the transaction costs to an informed trader and creating a friction against the placement and execution of informed orders. Moreover, in illiquid markets, it can be difficult for an informed trader to place and execute large orders without substantially affecting market prices, reducing the potential reward for informed trading. Illiquidity can thus undermine price discovery.

Illiquidity also undermines market stability. Markets with relatively few and/or relatively small providers of liquidity at any given point in time tend to be more subject to extreme price movements in the event of large order placements. Large orders, particularly those of commercial market participants, may contain information about their supply and demand, which can affect prices. Price changes should relate to supply and demand. But if those orders are purely speculative and therefore not reflective of true supply and demand, other traders can misinterpret those orders as informed trades, and price spikes can occur and thereby impact price discovery. Further, economic experience demonstrates that illiquid markets often have characteristically high volatility, which not only undermines price discovery but also creates uncertainty for market participants regarding the true economic value of the asset in question.

3. Recommendations to enhance RIN market liquidity and prevent excessive speculation

Valero recommends that EPA implement reforms to increase market liquidity and discourage excessive warehousing or hoarding of RINs. These reforms could be pursued

on the Sharing of Information Available to EPA Related to the Functioning of Renewable Fuel and Related Markets” (Mar. 15, 2016), available at <https://www.epa.gov/sites/production/files/2016-03/documents/epa-cftc-mou-2016-03-16.pdf>.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

independently or in tandem. These reforms would require additional position and/or transaction data reporting to regulators, discussed in detail below.

First, Valero recommends that EPA implement position limits. Position limits are an important tool used by market regulators, such as the CFTC, to prevent excessive speculation and the potential for manipulation while ensuring sufficient market liquidity for bona fide market participants and protecting the price discovery process.¹³⁷ Speculative position limits have been used as a tool to regulate futures markets for over seventy years and Congress has repeatedly expressed confidence in the use of speculative position limits as an effective means of preventing unreasonable and unwarranted price fluctuations that undermine market stability.¹³⁸

EPA requested comment on whether it should change the duration for which RINs could be held and require obligated parties to retire RINs for compliance on a more frequent basis. Valero believes that EPA can discourage hoarding and encourage liquidity by implementing position limits subject to a durational component.

In addition to position limits, Valero recommends that EPA establish carryover limits relative to a RIN holder's compliance obligations and that such proportional limits be tightened to reduce the excess RINs a firm is permitted to carry over and bank for the following compliance period. The limits would include carryover allowances such that market participants with RVO obligations would qualify for exemptions enabling them to carry over a greater number of RINs as a function of the entity's requirements to hedge future RVO obligations. Limits could be structured to discourage hoarding by net RIN-long parties and encourage unobligated net RIN-long parties to make more RINs available to the market, thereby increasing liquidity.¹³⁹ The limits also should become more restrictive as RINs approach expiration, analogous to telescoping position limits commonly applied to commodities markets, with RVOs operating as hedge exemptions.

Valero also recommends that EPA create a central RIN repository and auction process for excess carryover RINs. In a tight market with a limited supply of RINs, some net long market participants could be motivated to allow RINs to expire rather than to sell them in order to restrict available market supply and drive up the price of their remaining positions. In order to eliminate such behavior, RINs that would otherwise exceed carryover limits would be transferred to a central RIN repository where they could then be made available for purchase via a public auction.

¹³⁷ For information on the CFTC's position limit framework, see CFTC, *Speculative Limits*, <https://www.cftc.gov/IndustryOversight/MarketSurveillance/SpeculativeLimits/index.htm> (last visited Aug. 15, 2018).

¹³⁸ See 78 Fed. Reg. 75,680, 75,681 (Dec. 12, 2013). See also H.R. Rep. No. 421, 74th Cong., 1st Sess. 1 (1935); H.R. Rep. No. 624, 99th Cong., 2d Sess. 44 (1986). The Commodity Exchange Act ("CEA") provides criteria for the CFTC to address with respect to position limits: (i) to diminish, eliminate, or prevent excessive speculation as described under this section; (ii) to deter and prevent market manipulation, squeezes, and corners; (iii) to ensure sufficient market liquidity for bona fide hedgers; and (iv) to ensure that the price discovery function of the underlying market is not disrupted. See 7 U.S.C. § 6a(a)(3)(B).

¹³⁹ See 83 Fed. Reg. 32,024, 32,029 (July 10, 2018).

C. The RIN Market Is Susceptible to Manipulation, Which Undermines Price Discovery and Market Integrity

1. The RIN market is susceptible to manipulation

The RIN market is virtually unregulated. Due to the structure of the RFS, obligated parties—particularly RIN-short parties—are a captive market for RINs. They must purchase a government mandated and publicly known quantity of RINs every year regardless of the price. Thus, RIN-short obligated parties are captive buyers while sellers can dictate trade terms. This dynamic, which results in an inelastic demand curve, combined with a lack of regulation, no restrictions on who can participate in the market, and no limits on the size of positions a participant can accumulate, provides for a market highly susceptible to abuse by participants engaged in manipulative and disruptive trading behavior.

The susceptibility of RIN markets to manipulation can be analyzed through the frameworks used to analyze commodity and commodity derivative markets. The finite supply of RINs, in conjunction with the inelastic demand curve for RINs created by defined RVOs and a single, universally known compliance schedule, creates opportunities for RIN-long parties in RIN markets—akin to the suppliers in a commodity market—to “squeeze” those with a net short position into paying higher prices, especially as RVO deadlines loom.¹⁴⁰ Also analogous to commodity markets, traders with larger positions are proportionately more capable of effectuating squeezes by withholding a greater portion of the total RIN supply from the market and keeping them warehoused. Such withholding and warehousing directly reduces liquidity in RIN markets, and can lead to increased volatility.¹⁴¹ Unlike most commodity markets, the RFS program does not currently restrict or prohibit large positions, meaning RIN squeezes can be even more effective than commodity market squeezes, with a lower risk of detection and punishment.

Moreover, in addition to an inelastic demand curve that is the result of the RVO for obligated parties, Charles River Associates has found that supply for RINs is “relatively inelastic.”¹⁴² This allows net long RIN market participants to withhold and warehouse larger positions with less concern that another party will increase RIN supply and devalue their long position.

¹⁴⁰ See Frank H. Easterbrook, *Monopoly, Manipulation, and the Regulation of Futures Markets* at S106, 59 *Journal of Business*, Issue 2 (Apr. 1986) (“The party may acquire a large portion of the existing contracts, thus under-cutting the usual assumption that every trader is ‘small’ in relation to the market. Or the party may simply decline to liquidate his position, so that at the very close of trading a formerly small holding becomes large in relation to the open contracts. The holder of these contracts then demands or tenders delivery (depending on whether he is long or short). Holders of opposite positions, surprised by the sudden demand or tender, unable either to make or take delivery without incurring large costs, and unable to find other parties with whom to close out their positions, must pay a premium to negotiate around the demand.”).

¹⁴¹ See Allen et al., *Large Investors, Price Manipulation, and Limits to Arbitrage: An Anatomy of Market Corners* at 647, *Review of Finance* (2006) (“We show that market corners tend to increase market volatility and have an adverse price impact on other assets.”)

¹⁴² See Charles River Associates, *RINs Market Frictions and the RFS Point of Obligation 3* (“[T]he relatively inelastic supply of RINs due to the characteristics of the RFS program and supply conditions past the “blendwall” tends to make manipulation issues more serious.”), Attachment P.

2. *The hoarding problem*

The prevalent market abuse existing in the RIN market today is hoarding—the intentional withholding of RIN supplies from obligated parties to create short squeezes and force obligated parties to purchase RINs at higher prices. Hoarding has been a significant concern to Valero and other market participants since the development of the RFS program and remains a real and costly issue today. Hoarding continues to have an increasingly significant impact on Valero's business—Valero attributes a portion of its increasing RIN expenditures, which have more than doubled since 2015 and almost quadrupled since 2014, to artificially high RIN prices supported by hoarding behavior.¹⁴³

Hoarding imposes large costs on all RIN-short parties in the RIN market. A Columbia University study listed high and volatile RIN prices as a failure of the program: “RIN prices under the RFS have been both high and volatile. Since February 2013, the price of the D6 RIN...has fluctuated from less than \$0.20 per gallon to more than \$1.40 per gallon.”¹⁴⁴ One of the listed sources for such price inflation and volatility stated: “Because RINs are bankable, expectations of future changes in the conventional [price] gap induce changes in current RIN prices. Thus, RIN prices are sensitive to rumors and market guesses about shifts in future RFS policy.”¹⁴⁵

Another concern is that financial speculators—parties with no RVOs—can buy RINs and engage in hoarding to reduce liquidity and benefit from illiquidity-induced volatility, selling RINs only at peak price spikes. RIN hoarding has an adverse effect on market liquidity, market stability, price discovery, and, ultimately, market integrity, creating great uncertainty for obligated parties. Hoarding reduces RIN supplies from the marketplace, thereby reducing liquidity. Less liquidity, in turn, increases volatility, which makes the RIN market more susceptible to other types of manipulative conduct and interferes with efficient price discovery.

3. *Recommendations to discourage hoarding*

Valero recommends that EPA establish rolling compliance dates and/or shorten the shelf life of a RIN to prevent short squeezes. By allowing for more flexibility regarding compliance dates and/or shortening the shelf life of a RIN, short squeezes could be made less profitable and liquidity could be more evenly spread throughout the year, particularly if pursued in tandem with position limits and/or a central RIN repository and periodic auctions.

Valero also recommends that EPA continue to work with other federal agencies and other regulators responsible for overseeing established trading markets to adopt clear anti-manipulation requirements that explicitly identify and prohibit hoarding and other abusive market practices occurring in the RIN market (*e.g.*, spoofing, violations of bids or offers, and artificial price floors).¹⁴⁶ The CFTC has a long history of administering rules, such as position limits, and

¹⁴³ See Seeking Alpha, *Valero Almost Broke The \$1B Threshold On RINs in 2017*, <https://seekingalpha.com/article/4155058-valero-almost-broke-1b-threshold-rins-2017> (Mar. 9, 2018).

¹⁴⁴ See James Stock, Columbia University, *Reforming the Renewable Fuel Standard* (Feb. 2018), Attachment U.

¹⁴⁵ *Id.*

¹⁴⁶ Spoofing occurs when traders place bids or offers with the intent to cancel their quotes before execution, in order to attract other traders to the market and induce a particular market price; violations of bids or offers occur when

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

enforcing those rules to prevent market manipulation and attempts to corner or hoard the market. For example:

- The CFTC stated in the final rule released on Position Limits for Futures and Swaps that the “long-standing statutory mandate [to limit trading] is based on Congressional findings that market disruptions can result from excessive speculative trading. In the 1920s and into the 1930s, a series of studies and reports found that large speculative positions in the futures markets for grain, even without manipulative intent, can cause ‘disturbances’ and ‘wild and erratic’ price fluctuations. To address such market disturbances, Congress was urged to adopt position limits to restrict speculative trading notwithstanding the absence of manipulation. In 1936, based upon such reports and testimony, Congress provided the Commodity Exchange Authority (the predecessor of the Commission) with the authority to impose Federal speculative position limits.”¹⁴⁷
- The CFTC stated in its prior proposal that “Large concentrated positions in the physical commodity markets can potentially facilitate price distortions given that the capacity of any market to absorb the establishment and liquidation of large positions in an orderly manner is related to the size of such positions relative to the market and the market’s structure and is, therefore, not unlimited.”¹⁴⁸
- In its Cost-Benefit Analysis of the proposed post Dodd-Frank Position Limits for Derivatives, the CFTC concluded that in addition to volatility reduction benefits of position limits, “visibility levels and associated reporting requirements of proposed [position limit rules] would enable the Commission to better understand generally the portfolio compositions, including *bona fide* hedging needs, of the largest position holders of referenced contracts. This data would enable the Commission to determine whether to readjust the speculative position limits to continue to ensure the statutory objectives are met. Visibility reports would allow the Commission to have a better sense of the relative distribution of speculative versus non-speculative positions and activity, as well as the nature and effect of the largest speculative traders in referenced contracts.”¹⁴⁹

traders buy at a price higher than the lowest available offer price and/or sell at a price that is lower than the highest available bid price; and artificial price floors are the result of RIN-long dominant parties sending blanket offers to purchase RINs to all known large sellers below a certain target price. See Valero Comments on Proposed 2017 RVO 15, Attachment S; see also 7 U.S.C. § 6c(a)(5)(A). The Dodd-Frank Act amended the CEA to prohibit “spoofing,” making it “unlawful for any person to engage in any trading, practice, or conduct on or subject to the rules of a registered entity that is of the character of, or is commonly known to the trade as, ‘spoofing’ (bidding or offering with the intent to cancel the bid or offer before execution).” See 7 U.S.C. § 6c(a)(5)(C).

¹⁴⁷ 76 Fed. Reg. 71,626, 76,127 n.10 (Nov. 18, 2011).

¹⁴⁸ 76 Fed. Reg. 4,752, 4,755 (Jan. 26, 2011).

¹⁴⁹ *Id.* at 4,764.

EPA should provide legislative recommendations to Congress if it determines that additional oversight authority is needed to implement appropriate market reforms, such as those currently utilized by the CFTC to protect market integrity.

Valero's recommendations to increase market liquidity noted above, *e.g.*, position limits, carryover limits, and a central RIN repository and auction process for excess carryover RINs, have the added benefit of reducing incentives to manipulate the RIN market. Consequently, Valero repeats its recommendation that EPA implement these requirements to discourage RIN hoarding and increase market liquidity, from the additional perspective of enhancing market integrity.

D. Transparency

1. Transparency in the RIN market

Manipulation and transparency are obviously related, in that a lack of transparency opens the door to fraud and other misconduct. Valero agrees with the statement of one former CFTC Commissioner that “[t]ransparency is the cornerstone of a well functioning regulatory system,”¹⁵⁰ and strongly believes that improving transparency in the RIN market will help EPA identify and eliminate manipulative behavior, which in turn will benefit RFS program participants and protect the program's integrity. Notwithstanding the above, transparency improvements alone will not fix the RIN market; they will only be effective if they are accompanied by reforms implementing position limits, carry-over limits (with exemptions), and enhancing liquidity of the RIN pool.

Unlike the commodities and securities markets, the RIN market is not transparent—prices are not disclosed and there is no obligation to accurately report prices. Because there is no requirement for accurately reporting RIN trading information, information is spread thin and across many brokers contributing to chaotic trading with no natural order to trade flow. There is also no centralized validation of RIN volumes or RIN prices and no trader accountability.

Although RIN market participants are required to enter certain transaction information in the EPA Moderated Transaction System (“EMTS”) within prescribed time frames, the current EMTS reporting regime does not inform regulators about net positions and forward contracts in real time, and instead reports prices at the time of deliveries.¹⁵¹ Since the RIN market is primarily a forward market, regulators cannot engage in effective market surveillance in the ways that other agencies are able to do so.

¹⁵⁰ See “Integrity of the Futures Markets and the Role of Transparency,” Remarks by CFTC Commissioner Jill E. Sommers Before the FIA Asia Derivatives Conference Tokyo, Japan (Sep. 19, 2008), *available at* <https://www.cftc.gov/PressRoom/SpeechesTestimony/opasommers-5>.

¹⁵¹ According to an expert report, “the EMTS is inadequate for tracking the price of RINs because it collects price data on either a per-RIN or per-gallon basis. In addition, recording such data is subject to human error, so it is nearly impossible to identify and assess the cause of RIN volatility where the recorder incorrectly enters the data. Furthermore, several of the data fields in EMTS are voluntary; therefore, this information is often incomplete or in many cases misleading because there is no regulatory requirement to collect or analyze that data.” Ramon Benavides, Global Renewable Strategies and Consulting, LLC, *The US Renewable Identification Number: RINs Trading Market* 5 (2017), Attachment V.

Moreover, regulators are unable to monitor the RIN markets in real time to ensure that the markets function in an efficient manner, *i.e.*, one in which there are a sufficient number of reasonably available RINs for obligated parties seeking to purchase them.¹⁵² Thus, if a market participant intentionally withholds supplies to squeeze RIN short parties, regulators would not have the means to anticipate the temporary shortage or assess whether a squeeze is occurring.

2. *Transparency reforms*

EPA requested comment on a number of transparency reforms for the RIN market, including whether EPA should consider increasing the frequency at which currently available information is posted; post regular updates to the number of RINs it anticipates will be required for compliance; post average RIN prices based on the price information submitted to EPA through EMTS; and require public disclosure if a party holds a certain percentage of the RIN market. EPA also sought comment on whether it would be helpful to have access to aggregated information related to the number of RINs held by different categories of entities, such as renewable fuel producers, obligated parties, and parties that neither produce renewable fuel nor have an RVO under the RFS program.

In considering how to improve RIN market transparency, it remains important for EPA to obtain basic transaction information through EMTS that will enable it to conduct effective surveillance across the RIN market and detect, analyze, and sanction manipulative behavior. According to recent press reports, RIN data was not adequate for the CFTC to examine the market for the presence of manipulation. The proposals below include components of the CFTC's transparency framework to improve the adequacy of data collected by EPA.¹⁵³

EPA should consider reforming EMTS reporting requirements to capture more transaction data (including forward transactions) and net position data prerequisite to effective market surveillance. For example, EPA can require parties to report RIN transactions to EMTS within a short period of time after market participants agree to the transaction (*e.g.*, same day, t+1, or t+2), rather than upon delivery. Public posting of anonymized aggregates of reported data also should be considered to increase market transparency to the public and reduce information asymmetry across market participants.

One of the more important tools used by the CFTC to surveil markets is its large trader reporting program, pursuant to which it collects daily market data and position information from exchanges, clearing members, futures commission merchants, foreign brokers, and traders.¹⁵⁴ The large trader reporting program works as follows:

¹⁵² 83 Fed. Reg. at 32,029.

¹⁵³ Chris Clayton, *EPA RIN Market Data Poor* (Feb. 15, 2018), <https://www.dtnpf.com/agriculture/web/ag/news/business-inputs/article/2018/02/15/cftc-draw-conclusion-rin-market-epa-2>.

¹⁵⁴ See CFTC, *Large Trader Reporting Program*, <https://www.cftc.gov/IndustryOversight/MarketSurveillance/LargeTraderReportingProgram/index.htm> (last visited Aug. 15, 2018). To ensure privacy of the information they provide, the CFTC assigns confidential reporting numbers to reporting firms and traders.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

- “Under the Commission’s LTRS, clearing members, FCMs, and foreign brokers (collectively called reporting firms) file daily reports with the Commission under Part 17 of the CFTC’s regulations. The reports show futures and option positions of traders with positions at or above specific reporting levels as set by the Commission....If, at the daily market close, a reporting firm has a trader with a position at or above the Commission’s reporting level in any single futures or option expiration month, the firm reports that trader’s entire position in all futures and options expiration months in that commodity, regardless of size.”¹⁵⁵
- The CFTC collects data directly from exchanges, but such data have limitations which are addressed by the Large Trader Reporting System: “Each day, exchanges report each clearing member’s open long and short positions, purchases and sales, exchanges of futures for cash, and futures delivery notices for the previous trading day. This data is reported separately by proprietary and customer accounts by futures month, and for options by puts and calls, expiration date and strike price....Clearing member data, however, do not directly identify the beneficial owners of positions. The aggregate customer position reported for a clearing member could represent either a single trader or numerous traders. Also, the data would not reveal a circumstance where a single trader controls substantial portions of the customer positions with more than one clearing member, and therefore, could control a substantial portion of the market. To address such a limitation on clearing member data, the Commission’s market surveillance program uses large trader data.”¹⁵⁶
- “The aggregate of all large trader positions reported to the Commission usually represents 70 to 90 percent of the total open interest in any given market. The reporting level for large trader reports can range from 25 contracts to over 1,000 contracts. The level for any given market is based on the total open positions in that market, the size of positions held by traders in the market, and the size of deliverable supplies for physical delivery markets.”¹⁵⁷
- “The Commission has the discretion to raise or lower the reporting levels in specific markets to strike a balance between collecting sufficient information to oversee the markets and minimizing the reporting burden on traders that are reportable.”¹⁵⁸

These reports enable the CFTC to view activities of large traders to determine when their positions pose a threat by exceeding position limits or accountability levels. EPA should consider

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*

¹⁵⁷ *Id.*

¹⁵⁸ *Id.*

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

implementing similar reporting by large and active RIN traders, to provide EPA with information needed to prevent or at least detect manipulation or short squeezes.

EPA also should consider public reporting of anonymized net position data to help market participants and the public understand market dynamics similar to the CFTC's Commitments of Trader Reports.¹⁵⁹ Such public data could come in two forms. This could involve reporting periodic aggregate positions for the general categories of renewable fuel producers, obligated parties, and parties that neither produce renewable fuel nor have an RVO under the RFS program, but should also include positions of large traders, speculative positions, and those with high volumes of transactions, again with an eye toward allowing regulators the information needed to prevent manipulation or short squeezes. Since some large traders are reporting as obligated parties because they import small amounts of fuel, in developing rules to report by categories, EPA should carefully design the rules to appropriately classify traders who are genuinely obligated parties separate from those that are chosen to be obligated merely to be able to trade and report as obligated parties.

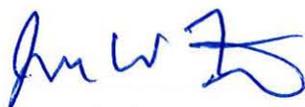
EPA also should consider more frequent public posting of data that is already made available on EMTS (*e.g.*, in real-time to the extent possible) and public posting of periodic stock and flow data relating to aggregate RIN obligations to ensure that market participants have appropriate data to forecast RIN demand and information regarding when RINs are retired. Each market participant can estimate its own RIN obligations, but may not have a strong sense for market-wide RIN obligation changes that should define the demand curve. Similarly, regulators may not be aware of short-term RIN obligation developments. Because of this, EPA should consider requiring market participants to report their estimated RIN obligations to the EPA periodically, such as monthly or quarterly.

¹⁵⁹ See CFTC, Commitment of Traders, <https://www.cftc.gov/MarketReports/CommitmentsofTraders/index.htm> (last visited Aug. 15, 2018). These reports provide a breakdown of each Tuesday's open interest for futures and options on futures markets in which 20 or more traders hold positions equal to or above the reporting levels established by the CFTC.

Valero Comments on EPA's Proposed Rule for Renewable Fuel Standard Program: Standards
for 2019 and Biomass-based Diesel Volume for 2020
Docket ID No. EPA-HQ-OAR-2018-0167

Valero is committed to working with EPA in a constructive way that will further the goals of the RFS program. I am available at your convenience to discuss the issues raised in these comments and the recommendations. Please contact me at (210) 345-2000 should you have any questions.

Sincerely,



Jason W. Fraser,
Senior Vice President & Counsel,
Public Policy, Strategy & External Communications
Valero Energy Corporation