

# EPA's Proposed Rulemaking: RFS Renewable Identification Number (RIN) Quality Assurance Program



Meetings with OMB  
January 4 and 7, 2013

# Background – The Issue

- The U.S. "Renewable Fuel Standard" (RFS) requires that:
  - Renewable fuel producers and importers generate fuel credits, Renewable Identification Numbers (RINs), in proportion to the amount and type of renewable fuel produced / imported.
  - Petroleum refiners and importers ("obligated parties") must acquire sufficient RINs to demonstrate compliance based on the amount of fuel they refine or import.
- RINs can be either *assigned* (transferred with the biofuel volume) or *separated*
  - RINs are separated by obligated parties, renewable fuel exporters, blenders, and producers who introduce the renewable fuel as *neat* transportation fuel
  - Separated RINs can be transferred any number of times
- RINs system design focused on maximizing flexibility; did not adequately comprehend RIN validity
- Between November 2011 and May 2012, EPA deemed 140 million biodiesel RINs to be invalid and issued Notices of Violation and fines not only to those creating invalid RINs, but also to refiners as purchasers of invalid RINs

# Background – The Industry’s Approach

- RIN integrity is key to the success of the RFS - impacts all parties involved in the program and EPA
  - An efficient, cost effective solution that avoids unnecessary complexity is needed to ensure RIN market liquidity for the benefit for all participants
- AFPM, API formed a joint industry working group in early 2012 to address the issue of RIN validity
  - Proposal: Regulatory amendment to the RFS for a new EPA-approved, third party RIN validation process that minimizes risk for invalid RINs through audits, and provides affirmative defense for purchases of validated RINs
  - Process: Sought multi-stakeholder involvement that included the biofuel industry and EPA
    - All stakeholders agreed that an affirmative defense mechanism would help ensure liquidity in the RIN market; alignment on specifics of RIN validation process not achieved

# Industry Position

- API & AFPM support EPA's proposed rulemaking to establish an EPA approved Quality Assurance Program (QAP) to address RIN validity that is:
  - Voluntary, producer-initiated, and provides for an affirmative defense
  - Efficient, cost effective and has a positive impact on RIN liquidity
- Key program elements :
  - *Independent* third party validation – EPA publishes QAP performance standards and approves validator submitted plans
  - Affirmative defense: validated RINs later deemed invalid are not subject to violation (provided the party did not have actual knowledge of a RIN's invalidity prior to acquisition or was the cause of the invalidity)
  - EPA explained three options for the market to choose from
    1. Status quo: does not provide affirmative defense
    2. "Simpler" QAP: provides affirmative defense – refiners may have obligation to replace RINs
    3. "Enhanced" QAP: provides affirmative defense with no obligation for a refiner to replace RINs
  - Validated RINs covered by a QAP are differentiated in EMTS
  - Program can be applied to all biofuel categories
  - RIN separation needs to be addressed

# Unknowns and Concerns:

## Program components

- Elements of the QAP – EPA’s draft guidance document was posted on October 31<sup>st</sup>
- AFPM and API provided detailed comments to EPA
- EPA proposes two types of QAPs based data monitoring frequency (e.g. quarterly)
  - EPA should clarify differences between the two QAPs (“simpler” vs. “enhanced”) and with the current RFS requirements
- QAP data elements should be streamlined and cost-effective
- QAP data collection and verification
  - Statistically significant data samples should be used; not all data collected
    - EPA to draw from experience with the successful Reformulated Gasoline (RFG) program which uses statistically significant sampling - not every gallon is tested
  - Proposal should clarify the difference between data *collection* and data *verification*

# Unknowns and Concerns:

## Program components

- Validation process should preserve RIN market liquidity for all market participants; high complexity and cost could jeopardize liquidity
- Current system functionality that allows for the efficient purchase and sale of RINs should be preserved
  - Changes to EMTS are necessary to identify type of RIN QAP tier
  - EPA should avoid unnecessary complexity and strive for clarity, transparency
    - No manual entries (similar to RFS1)
    - EPA could publish QAP validated RINs as an interim solution, if necessary
- Imports are within the scope of the QAP program
  - Foreign biofuels producers and biofuel importers may generate RINs and need to be able to participate in the program (potentially tailored to address imports)
- Exports are outside the scope of the QAP program
  - QAP focus is on RIN generation, not on tracking RINs through the system
  - EPA should use RFS regulations to address potential import/export fraud (e.g. consider requiring retirement of RINs upon export, rather than at year end)
  - QAP program complexity would increase exponentially should exports or RIN tracking be covered (likely including costs)

# Unknowns and Concerns:

## Program components

- Affordability – Liability protection at a reasonable cost is important for parties to participate in the program
  - The program has to be more efficient than existing options to gain widespread acceptance by biofuel producers and obligated parties
  - There is a risk reduction and cost associated with each QAP element; at some point the incremental risk reduction is outweighed by the cost of the additional QAP elements beyond the following:
    - Site visit and analysis to verify the potential production capacity
    - Utility bills
    - Feedstock receipts
  - Unnecessary requirements should be avoided (e.g. workforce size, process controls, attestation report), as they increase cost without reducing the risk
  - EPA cost estimates need to be realistic – the agency should be using true costs based on Agency discussions with QAP providers
  - Cost concerns have already been raised with EPA by various stakeholders, and should be closely scrutinized by OMB

# Unknowns and Concerns:

## Program components

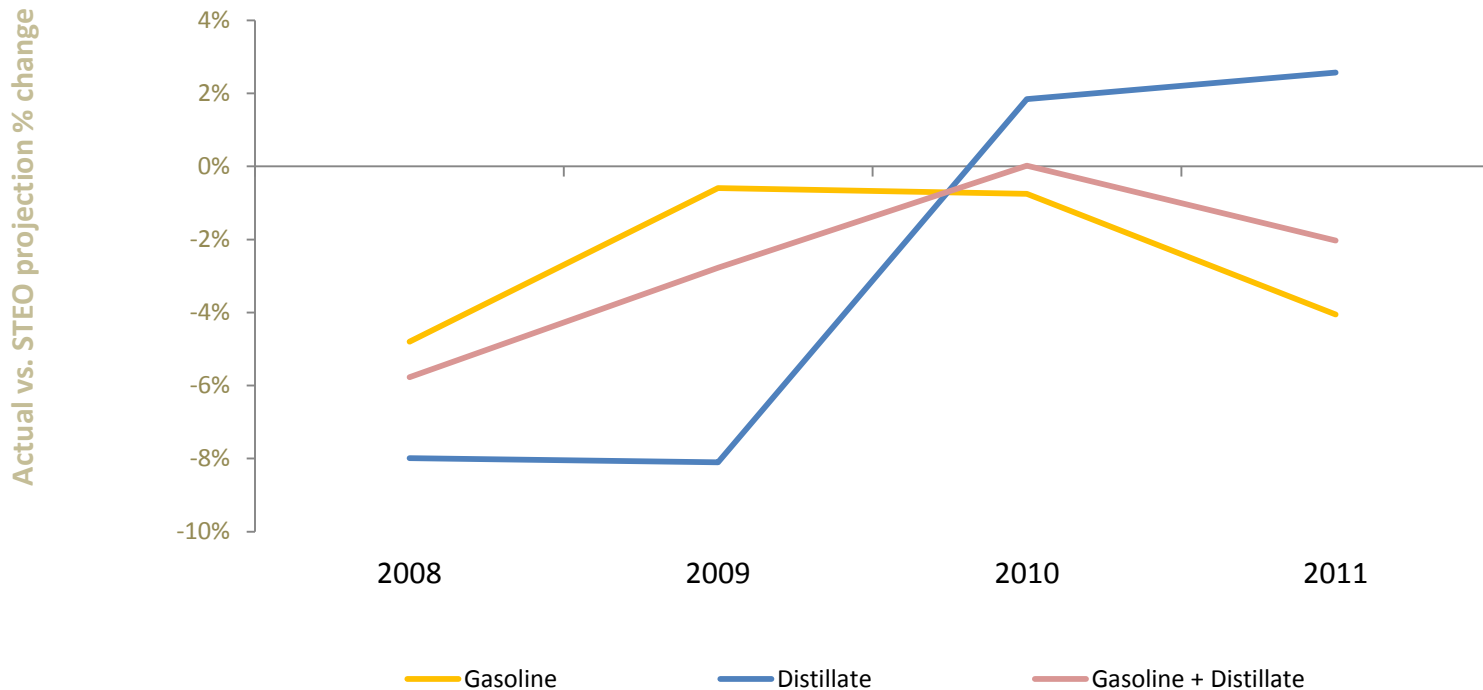
- Proposed RIN validation process is expected to reduce risk for invalid RINs significantly
- Replacement RINs – Obligated parties submitting validated RINs for compliance should not be liable for replacement of RINs that are later deemed by EPA to be invalid
  - Liability for addressing RIN invalidity should be limited to the party(ies) that caused the invalidity
    - RIN generators or parties committing fraud should be first in line for any RIN replacement
    - Requiring refiners to replace validated RINs potentially undermines the value of the QAP program and may not help RIN liquidity
  - RFS standards (e.g., biomass-based diesel, cellulosic) are set based on EPA's estimate of the maximum feasible volumes for the year
    - Replacing RINs from a previous year is impossible unless there are surplus RINs; cannot incentivize production for a prior year
    - Requiring future year RIN replacement could result in demand exceeding supply



# Unknowns and Concerns:

## Program components

- Limited threshold exemption (de minimis) below which no replacement RINs are required
  - Should not be less than 3% of each obligated party's RVO
  - 3% minimum is supported by variability inherent in the RFS program (EIA projections vs. actual demand)



# Unknowns and Concerns:

## Interim Solution

- 2013 is already here – QAP criteria not finalized, validators not yet approved, EMTS must be revised
- Industry remains concerned and needs to understand the specifics of the mechanism that would enable EPA to make the program effective upon proposal

# Unknowns and Concerns:

## Interim Solution Until Final Rule is Effective

- EPA Enforcement should exercise its authority to issue a “No Action Assurance” letter until the final rule is effective
- Alternately, EPA needs to extend the March 2012 Interim Enforcement Policy for 2012 RINs and 2013 RINs until final rule is effective <sup>1</sup>
  - EPA established maximum penalties for RIN violations that did not extend past 2011
  - Many obligated parties took additional steps independently in 2012 to investigate the validity of RINs procured
  - The policy should be extended to cover 2012 and 2013 RINs generated prior to the issuance of a final rule
  - EPA should also extend the policy to cover all RIN types beyond biodiesel
- API and AFPM requested such an extension in a November 27<sup>th</sup> letter to the Agency

<sup>1</sup><http://www.epa.gov/compliance/resources/policies/civil/erp/erp-invalidrins.pdf>

Thank you

