RENEWABLE FUELS ASSOCIATION

July 24, 2018

The Honorable John Shimkus
Chairman
Subcommittee on the Environment
Committee on Energy and Commerce
U.S. House of Representatives

The Honorable Paul Tonko
Ranking Member
Subcommittee on the Environment
Committee on Energy and Commerce
U.S. House of Representatives

Dear Chairman Shimkus and Ranking Member Tonko:

The Renewable Fuels Association (RFA) is the leading trade association for America's ethanol industry. Its mission is to advance the development, production, and use of fuel ethanol by strengthening America's ethanol industry and raising awareness about the benefits of renewable fuels. Founded in 1981, RFA serves as the premier meeting ground for industry leaders and supporters. RFA's 300-plus members are working to help America become cleaner, safer, more energy secure, and economically vibrant. In advance of the Energy and Commerce Subcommittee on the Environment's hearing this week on "Background on Renewable Identification Numbers (RINs) under the Renewable Fuel Standard (RFS)," we wanted to be sure the Subcommittee was provided the perspective of American ethanol producers.

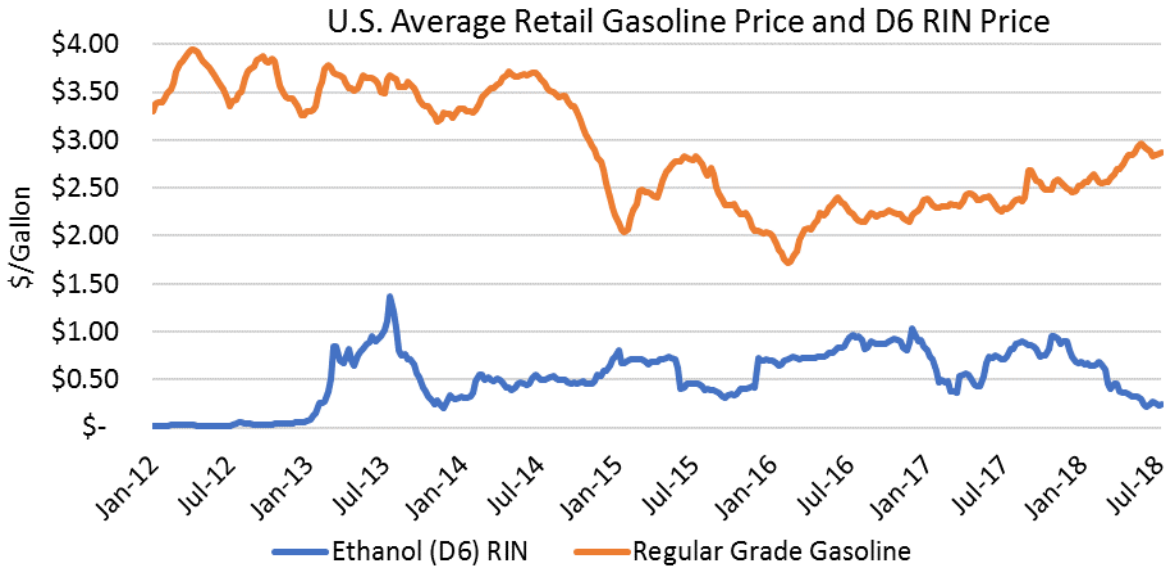
RIN credits are the engine that drives the RFS. Not only are RINs used to demonstrate compliance with annual RFS blending obligations, but they also serve as a critical economic incentive to expand the production and use of renewable fuels. The value of RIN credits is primarily determined by market fundamentals. If the supply of RINs is perceived as being tight relative to the RFS blending obligations, then RIN prices will be relatively high. Conversely, if the supply of RINs is abundant relative to the obligation, then RIN prices will be low. In short, RIN prices reflect the market's understanding of the relative ease or difficulty in meeting annual RFS standards.

Studies show that higher RIN prices facilitate deeper discounting of ethanol-blended fuels (such as E15 and E85) relative to gasoline, and that wider discounts lead to greater consumption of these blends. In turn, greater demand for E15 and E85 stimulates increased production of ethanol, which leads to increased RIN generation and larger supplies. Thus, the most direct and effective way to reduce RIN prices is to let RINs do their job of stimulating increased ethanol production and blending.

It is well understood that merchant refiners who do not blend ethanol **recoup their RIN costs** by slightly marking up their selling price of gasoline blendstock. Thus, RINs are not negatively affecting the financial performance of refining companies, both large and small.

- Petroleum industry consultants at **Turner, Mason & Company** agree that RINs are not affecting margins for refiners, stating, *"RFS compliance costs are substantially passed from refiners"* to wholesale purchasers of gasoline blendstock.
- Under former Administrator Scott Pruitt, the **Environmental Protection Agency** concluded that RINs are not negatively affecting profit margins for oil refiners like PES. According to EPA, *"…obligated parties, including small entities, are generally recovering the cost of acquiring the credits necessary for compliance with the RFS standards through higher sales prices of the petroleum products they sell."*
- Economists from **Harvard University, MIT, and the University of Michigan** also determined that refiners recover the cost of RINs, and thus there is no net impact on margins: *"RIN prices were passed through one-for-one in the prices of bulk petroleum fuels."*
- Economists from **Iowa State University** found *"…added refiner costs from complying with the RFS are passed on to blenders through higher gasoline prices. We show that high RIN prices…have no impact on profits of refiners, blenders, or integrated oil companies."*
- Refiner **Andeavor**, which will become the nation's largest refining company following a planned merger with Marathon, has stated *"RIN costs are passed through at the bulk finished product sales points and provide refiners with coverage of their exposure to them."*
- Even the **API** agrees that *"…RIN costs are largely recovered by refineries, both large and small, through the increased value of gasoline and diesel fuel they supply to the market."*

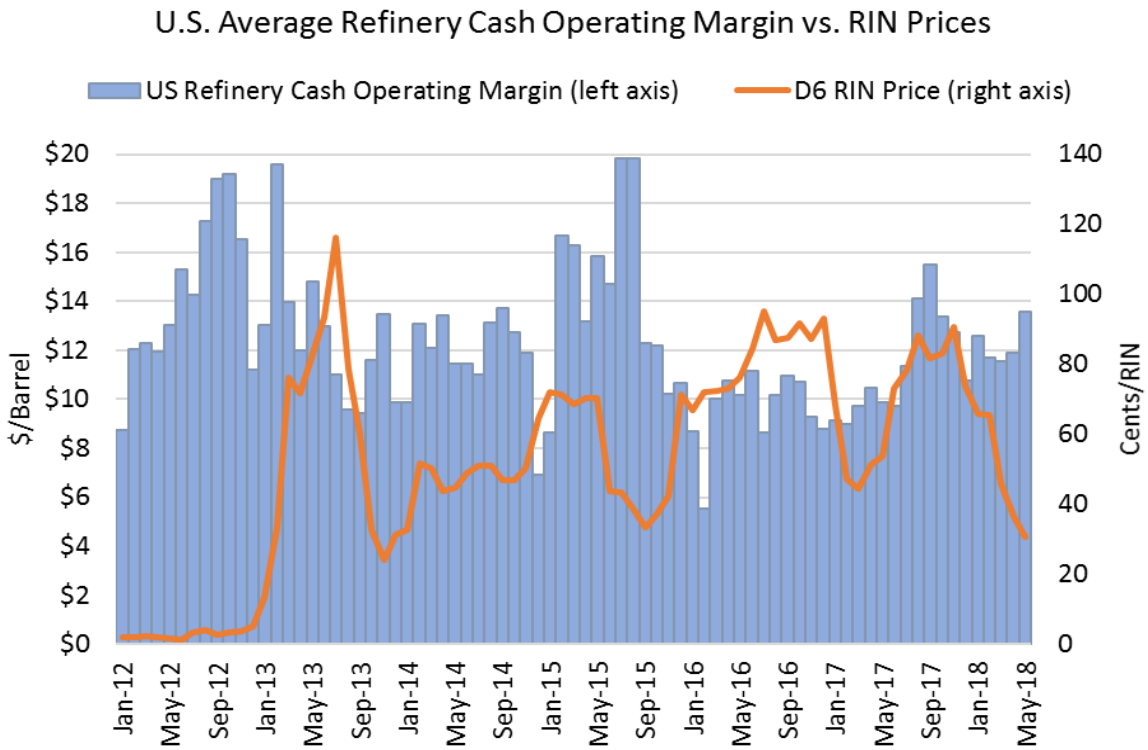
Importantly, there is no evidence to support the notion that RINs push retail gas prices higher. In fact, RINs and retail E10 gas prices tend to be negatively correlated, with periods of high gas prices occurring during periods of low RIN prices and vice versa. According to an **Iowa State** study, "…the net effect on the [retail] price of E10 of high RIN prices is zero: higher gasoline prices are offset by lower ethanol blending costs and the price of E10 remains constant."



Source: OPIS and Energy Information Administration

Moreover, contrary to the rhetoric coming from some in the refining industry, there is **no statistical evidence to support the argument that higher RIN prices negatively affect refiner margins**. In fact, monthly average margins for East Coast refineries have shown a positive correlation with RIN prices in recent years (coefficient=0.71 since January 2017), meaning margins are highest when RIN prices are highest and vice versa (this lends support to the argument that RINs are embedded in the refinery "crack spread").

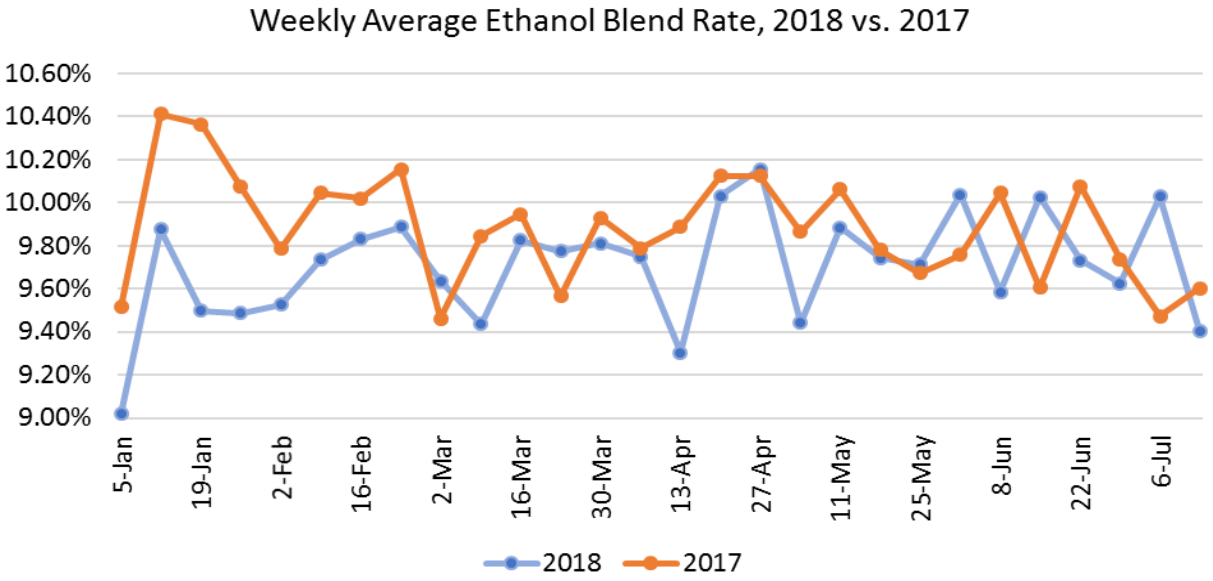
Wells Fargo Securities recently released an analysis to subscribers that examined the potential impacts of RFS compliance costs on merchant refiners, finding that *"Most independent refiners now enjoy a net benefit from RINs, based on our analysis."* The analysis also found that *"RINs costs are being passed along"* and *"investors should not spend much time and effort"* worrying about RINs.

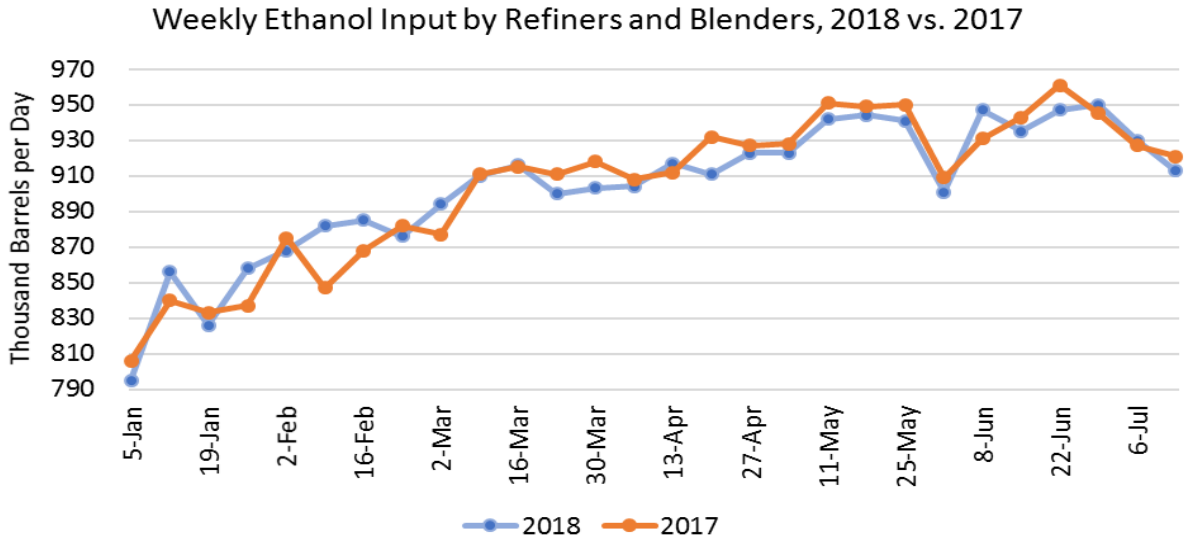


Source: Muse Stancil and OPIS

EPA's recent issuance of approximately 50 small refinery compliance exemptions from 2016 and 2017 RFS requirements has ballooned RIN stocks to nearly 3.1 billion RINs. That is more than double the level of RIN stocks just two years ago. Consequently, RIN prices have plummeted from 95 cents in late November 2017 to just 25 cents today, decreasing the incentive for blenders and refiners to increase volumes of E15 and flex fuels like E85 to push past the so-called E10 "blend wall."

The escalation of RIN stocks and associated collapse of RIN prices has caused demand destruction in the ethanol market. Despite very favorable blending economics (i.e., ethanol is priced 70 cents per gallon below gasoline at the wholesale level), ethanol blending activity has slowed in 2018. Both the absolute volume of ethanol blended and ethanol's share of finished gasoline consumption are lower than year-ago levels. The 2018 weekly ethanol blend rate has been **below year-ago levels in 21 of 28 weeks so far**. Meanwhile absolute blending volumes have lagged year-ago volumes in 18 of 28 weeks, **including 16 of the past 20 weeks**.





Source: Energy Information Administration

U.S. ethanol producers and farmers across the country who have invested in this important value-added market opportunity are extraordinarily concerned by EPA's recent intrusion into the RIN market, and believe it irreparably undermines the integrity of the RFS. The RIN mechanism must remain a market driven instrument for investors. EPA must not be allowed to manipulate the RIN market with specious interpretations of its waiver authorities that arbitrarily and significantly distort RIN supply and demand. Providing waivers from RIN obligations to wealthy oil companies that are recovering RIN costs in the crack spread, creating new RINs not tied to a specific gallon of biofuel to accommodate the retroactive granting of a small refinery waiver, and forgiving the RIN obligations of a certain refinery in bankruptcy proceedings when the source of that refinery's financial distress was well understood to be unrelated to its RFS obligations, are all examples of EPA's wanton disregard for the statute and its biofuel demand destruction campaign. All of this must end. EPA must allow RIN markets to work.

Thank you for the opportunity to comment and I look forward to continuing to work with you on issues related to the RFS.

Sincerely,

Bob Dinneen
President & CEO