

New RFS Program Requirements

Beveridge & Diamond, P.C. Client Alert, July 18, 2007

Beginning September 1, 2007, new U.S. Environmental Protection Agency (“EPA”) registration, recordkeeping and reporting requirements will become effective for all producers and importers of renewable fuels in the United States as part of EPA’s implementation of the Renewable Fuel Standard (“RFS”) program. The program will also involve the establishment of a new trading market in renewable fuel credits. An overview of these new requirements and the new market is provided below.

I. What is the Renewable Fuel Standard Program?

The Energy Policy Act of 2005 required EPA to establish a program to ensure that the pool of gasoline sold in the contiguous 48 states contains specific volumes of renewable fuel for each calendar year, starting with 2006. Each year, EPA must set an annual standard representing the amount of renewable fuel that must be used by each gasoline refiner, blender (other than oxygenate blenders), or importer (known as “obligated parties”). The standard is expressed as a percentage of gasoline sold or introduced into commerce, and an obligated party’s required renewable fuel volume is determined by multiplying its annual gasoline production by the annual standard.¹

The standard set by EPA for 2007 is 4.02 percent, which represents the volume of renewable fuel that each obligated party is responsible for introducing into the domestic gasoline pool in 2007. As described below, compliance with the RFS program is demonstrated through the acquisition of unique Renewable Identification Numbers (“RINs”), which are assigned by the producer or importer to every batch of renewable fuel produced or imported.²

Under the Energy Policy Act, EPA must continue setting specific increased renewable fuel standards annually through 2012, at which point it must begin establishing its own volumes on an annual basis. EPA has indicated that it intends to continue using the main elements of its RFS program in its post-2013 program. In a May 15, 2007 announcement, President Bush announced an intention to develop regulations that will build upon his “20-in-10” proposal from the 2007 State of the Union address. That proposal would reduce the amount of gasoline usage in the United States by 20 percent in the next 10 years, including by establishing a

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¹ Renewable fuel producers or importers that do not produce or import gasoline must comply with the requirements highlighted in this memorandum, but are not themselves considered “obligated parties” under the RFS.

² EPA published its final rule promulgating the RFS Program requirements at 72 Fed. Reg. 23,900 (May 1, 2007). Additional information, including guidance documents, is available online at EPA’s website: <http://www.epa.gov/otaq/renewablefuels/>.

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mandatory fuel standard that requires 35 billion gallons of renewable and other alternative fuels by 2017. EPA has acknowledged that this new regulatory effort (and continued attention by the Congress) may affect its RFS program in the future, but the Agency has suggested that the RFS program elements might be incorporated into an expanded renewable and alternative fuels program.

II. What Qualifies as Renewable Fuel?

Generally, renewable fuels must be produced from plant or animal products or wastes, as opposed to fossil fuel sources. Valid renewable fuels include:

- ◆ ethanol made from starch seeds, sugar, or cellulosic materials;
- ◆ biodiesel (mono-alkyl esters); and
- ◆ non-ester renewable diesel.

For purposes of compliance with the RFS, EPA has established the following “Equivalence Values” for specific renewable fuels:

1 gallon of corn ethanol	=	1 gallon-RINs
1 gallon of biobutanol	=	1.3 gallon-RINs
1 gallon of biodiesel (mono-alkyl ester)	=	1.5 gallon-RINs
1 gallon of non-ester renewable diesel	=	1.7 gallon-RINs
1 gallon of cellulosic ethanol	=	2.5 gallon-RINs
1 gallon of waste-derived ethanol	=	2.5 gallon-RINs

In effect, every physical gallon of corn ethanol (with an Equivalence Value of 1 gallon-RINs) will count as one gallon for RFS compliance purposes, while every physical gallon of cellulosic ethanol (with an Equivalence Value of 2.5 gallon-RINs) will count as two and a half gallons for RFS compliance purposes.

III. How Will the RIN Trading Program Work?

Pursuant to the Energy Policy Act, EPA has promulgated a credit trading program, allowing obligated parties to generate or acquire credits to demonstrate compliance with their annual renewable fuel volume obligations. Credits can also be used by an obligated party to meet its requirements in the following year, or traded for use by another obligated party.

RINs form the basic “currency” for the RFS program: currency for trades, currency for credits, and currency for compliance. A RIN must be generated for all renewable fuel produced or imported into the United States, and RINs must be acquired by obligated parties for use in demonstrating compliance with the RFS annual requirements. EPA’s program requires RINs to be transferred with renewable fuel until the point at which the renewable fuel is either: (a) purchased by an obligated

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party, or (b) blended into gasoline or diesel fuel by a blender. At such time, RINs are “separated” from the volumes.

Separation of a RIN from a volume of renewable fuel means that the RIN can be traded independently from the volume to which it had originally been assigned; in effect, RINs become freely transferable once they are separated from a batch of renewable fuel. Each RIN may be held by any party, and transferred between parties any number of times. Because RINs are generated by non-obligated parties (namely, renewable fuel producers and importers), and many non-obligated parties will own RINs, EPA’s approach to RINs differs from other Agency credit trading programs in two fundamental ways:

- ◆ First, unlike other EPA programs where credits are distributed to regulated parties and then traded by those parties that manage to achieve compliance before using all of their credits, under the RFS program RINs are themselves the fundamental unit for demonstrating compliance. Every obligated party must generate or acquire enough RINs to satisfy its annual obligations.
- ◆ Second, obligated parties are typically not the ones producing the renewable fuels and generating the RINs, nor blending the renewable fuels into gasoline, which means that trades must occur between obligated parties and non-obligated parties. As a result, the RIN trading program permits any party to hold RINs, and allows for RINs to be traded any number of times.

Once a RIN is separated from a volume of renewable fuel, it can be used for compliance purposes, banked, or traded to another party. Obligated parties can thus acquire RINs directly through the purchase of renewable fuel with assigned RINs, or through the open market for separated RINs. The means through which RIN trades will occur will be at the discretion of the parties involved, but may include open auctions, direct contracts, brokered purchases, or simple transfers. RINs not used in the year they are generated or in the subsequent year will expire, and no more than 20 percent of a current year’s RFS obligation can be satisfied using RINs from the previous year.

IV. What are the New Requirements for Renewable Fuel Producers and Importers?

A. Registration

Renewable fuel producers and importers must register under the RFS program before generating, transferring or owning RINs. Registration forms are available at: <http://www.epa.gov/otaq/regs/fuels/fuelsregistration.htm> . A party may not own RINs, or engage in any activities regarding RINs, as of September 1, 2007 unless it

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has registered and received a unique four-digit EPA company number and unique five-digit facility identification numbers.

Parties who are already registered with EPA under the Agency's reformulated and conventional gasoline or diesel fuel programs will use their existing EPA company and facility numbers and do not need to separately register under the RFS program. Registrations never expire and do not have to be renewed.³

B. RIN Generation and Transfer Requirements

Renewable fuel producers and importers must assign a unique RIN to each batch of renewable fuel. A batch may equal any volume of renewable fuel up to 99,999,999 gallon-RINs and/or the maximum volume that is produced or imported by the producer or importer within a calendar month. The RIN must be assigned to a batch no later than the point in time when ownership of the batch is transferred from the producer or importer to another party.

The RIN transfer must be recorded on a new or existing product transfer document ("PTD"). RINs are represented by a 38-character numeric code in a specified format describing assignment status, year of production/importation, company registration, facility registration, batch number, equivalence value, renewable type (cellulosic/non-cellulosic), block starting number and block ending number.

An obligated party must separate a RIN from a batch (change an assigned RIN to an unassigned RIN) as soon as it gains ownership of that batch. Renewable fuel blenders also separate RINs upon blending. Unassigned RINs can then be transferred freely without volumes of renewable fuel to obligated parties or to any other party. Once a RIN is separated from a volume of renewable fuel, the PTD associated with that volume can no longer list the RIN but should include a notation that the assigned RIN has been removed.

C. Reporting

Renewable fuel producers and importers are responsible for the submission of three reports to EPA on a quarterly basis:⁴

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³ EPA's regulations provide that a foreign entity may apply to EPA for approval to own RINs. As an approved foreign RIN owner, the foreign entity will be able to obtain, sell, transfer and hold both assigned and separated RINs, and the entity will be required to comply with all requirements that apply to domestic RIN owners. In addition, an approved foreign RIN owner will be required to comply with additional requirements to ensure that enforcement of the RFS regulations at the foreign RIN owner's place of business will not be compromised.

⁴ In addition, obligated parties and exporters of renewable fuel must submit an annual compliance report, demonstrating RFS compliance.

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1. **Quarterly RIN Generation Reports.** Producers and importers must submit quarterly RIN generation reports providing information on all batches of renewable fuel produced and imported, and all RINs generated.
2. **RIN Transaction Reports.** Producers and importers must submit RIN transaction reports, providing information on individual RIN purchases, RIN sales, retired RINs (no longer valid because of the passage of time), and expired RINs (no longer valid due to the reportable spillage of their assigned volumes, RINs used to satisfy an enforcement action, or RINs used to effect an import volume correction). A separate RIN transaction report is required to be submitted for each RIN purchase and sale, and for each retired or expired RIN. A RIN transaction report must be submitted by the end of the quarter in which the activity occurred.
3. **Quarterly Gallon-RIN Activity Reports.** Producers and importers must submit quarterly gallon-RIN activity reports, providing the total number of gallon-RINs owned at the start and end of the quarter, and the total number of gallon-RINs purchased, sold, retired and expired during the quarter, as well as end-of-quarter renewable fuel volumes.

The reports must be submitted to EPA by May 31 (for the January-March quarter), August 31 (for the April-June quarter), November 30 (for the July-September quarter), and February 28 (for the October-December quarter). Reports may be submitted electronically through EPA's Central Data Exchange ("CDX"), which allows EPA to accept reports that are electronically signed by the submitter in a secure and encrypted fashion. Information may be designated as confidential business information ("CBI").

Finally, producers and importers of renewable fuels are subject to an annual attest engagement requirement under the RFS program. Attest engagements consist of an independent, professional review of compliance records and reports.

D. Recordkeeping

In addition to documentation related to RIN transfers, parties must keep records related to the sale, purchase, brokering and trading of RINs, and any copies of any reports they submit to EPA for compliance reports. Additional recordkeeping requirements apply to producers of cellulosic and waste-derived ethanol.

Parties must keep copies of all record for five years.

For more information, or if you have questions about RFS compliance requirements, please contact Russ LaMotte (rlamotte@bdlaw.com, (202) 789-6080) or Alan Sachs (asachs@bdlaw.com, (410) 230-1345).

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