California Independent Oil Marketers Association
3831 N. Freeway Blvd. #130 • Sacramento, CA 95834
(916) 646-5999 • (916) 646-5985-fax
www.cioma.com

DOCKET
07-HFS-1
DATE JAN 05 2009
RECD. JAN 05 2009

January 5, 2009

California Energy Commission
Dockets Office, MS-4
Re: Docket No. 07-HFS-01
1516 Ninth Street
Sacramento, CA 95814-5512

Subject: CIOMA comments on Draft AB 868 Fuel Delivery Temperature Study, Docket No. 07-HFS-01

To Whom It May Concern:

The California Independent Oil Marketers Association (CIOMA) by this letter is transmitting their comments on the Energy Commission's Draft AB 868 Fuel Delivery Temperature Study, Docket No. 07-HFS-01. We commend the Energy Commission for providing the first objective and independent review of issues and economics surrounding the controversy of mandatory or permissive fuel temperature compensation at petroleum retail facilities. CIOMA and its members have repeatedly contended that automatic fuel temperature compensation at retail locations will only result in higher costs to California fuel consumers, without corresponding benefit. The Energy Commission report correctly concludes that the various forms of fuel temperature compensation will *not* benefit fuel consumers, or society in general.

CIOMA represents independent marketers who purchase gasoline and other petroleum products from refiners and sell the products to independent gasoline retailers, businesses, and government agencies, as well as representing branded "jobbers" who supply branded retail outlets, especially in rural areas. Our members are primarily small, family owned businesses who encounter unique difficulties in meeting California's complex and increasingly expensive environmental requirements. We represent approximately 400 members, about half of whom are actively engaged in the marketing and distribution of petroleum products and fuels.

Although we agree with the general direction taken in the draft study, we have serious concerns that the study incorrectly (and insufficiently) quantifies the costs and highly overestimates theoretical benefits to the consumer. An independently commissioned study by Mike Flynn, LECG, is being submitted which goes into significant detail regarding the areas of the report which need bolstering. With the inclusion of information taken from the LECG report, we conclude that temperature compensation at retail outlets will *only entail costs* to the consumer – and that the consumer will derive *absolutely no benefit* from temperature compensation. The following points summarize how we reach this conclusion:

- Fuel temperature is already taken into account in fuel transactions and distribution – The LECG study correctly demonstrates that fuel temperature is already taken into account during fuel transactions and that competition prohibits the garnering of "mystery profits" from "mystery gallons". As such, there is *absolutely zero benefit to consumers* in the requirement of additional, costly temperature compensation technology since it "corrects" a problem in need of no solution.
- No evidence of "mystery gallon profits" – The LECG study also shows, beyond a doubt, that service station operators have *not* achieved compensation due to higher fuel temperatures. The significant dollars calculated in the "hot fuel rip-off" arguments should be easily detectable in California station margins and profits. LECG's analysis shows there is no detectable trace of mystery profits from mystery gallons, so there are no mystery gallons. This also suggests that there are only costs, and no benefits for fuel temperature compensation.
- A gallon is a gallon – A flaw in the Energy Commission's analysis is the inconsistency in evaluating how fuel is delivered from the rack to the service station. Under current practices gross gallons are received by the delivery truck at the rack, gross gallons are deposited into the retail storage tank, and gross gallons are distributed to the customer. Therefore, there is internal and harmonic consistency in the use of gross gallons as distribution accuracy metric. Where the Energy Commission report confuses this situation is that sales at the rack are *priced* on a net (temperature and gravity-adjusted) basis. However, the delivery of fuel into the tanker is on a *gross gallon* basis.

  The pricing of gallons at the rack in net terms is the result of two important factors. First, as indicated by API, the use of net pricing at the terminal is necessary to make "oranges to oranges" terms between fuel suppliers in different locations, such as exchanges, providing an equivalent basis for transaction pricing and value. Second, a net-gallon price is used to determine a snapshot for application of state excise tax using both temperature and fuel gravity since excise taxes are based on per-gallon basis. The important factor to remember is that *only the price is adjusted, not the amount of fuel.*

  The retailer pays a delivered price for his or her fuel. That may include the net gallon (or gross gallon) wholesale price of the fuel as well as other variables such as delivery costs, liability protection, taxes and wholesaler mark-up. But the retailer is paying a price *per gross gallon delivered.* That is a factor that is used by the retailer to determine gross gallon price, and why the LECG report correctly concludes that switching to a net distributed gallon will merely create a change in the price to accommodate the changes in the distributed volume (equivalent to a change from gallons to liters, for example). This switch also creates inconsistency in the accuracy measurement of fuel along the transaction chain.
- No "for free" fuel sales – The LECG report also accurately addresses the contention that service stations will provide higher volume ATC-corrected fuel at a loss, or for free. Competition will provide the stimulus to incorporate costs related to equipment and additional fuel volumes as quickly as possible, especially in the situation where all stations are required to perform the same function(s) at the same time. Service stations will not be selling "free" gallons in the short-, medium- or long-term.

- No "twinkie" offset - The LECG report addresses the fundamental problem in assigning loss of fuel margin by increasing in-store product prices. In-store product pricing is based on an entirely separate set of factors, and pricing of in-store products above competitive levels (to offset lower fuel margins) will harm such sales. CEC correctly notes that "society" will wind up a net loser in this case as higher prices are paid by all consumers of such goods.
- We agree with the report's concerns regarding regulation of permissive temperature compensation - We agree that there is an apparent gap in authority to adequately regulate ATC equipment if it were installed. However, we do not agree with the report's conclusion that ATC is permissively authorized under current state law. We agree with the analysis submitted by Latham & Watkins that state law currently *precludes* allowance of ATC by specifying that distribution of petroleum fuels must be in gallons, and a gallon is defined as "231 cubic inches (exactly)".[1] And, that it will take additional legislation to allow ATC in either a permissive or mandated manner.

In conclusion, we are very pleased that the Energy Commission has performed a commendable job in exploring the costs and benefits of this complicated topic. It is the first, broad-based, objective analysis of the issues and economics involved in fuel temperature compensation. While we strongly disagree that the net cost to society is "slight", we do agree that fuel consumers and society will receive no offsetting benefit from temperature compensation requirements. In fact we argue that consumers and society will *only* be confronted by higher costs.

If you have any questions or need additional information, please feel free to contact me at your earliest convenience.

Sincerely

Jay McKeeman, CIOMA Vice President of Government Relations & Communications

cc: Assemblyman Mike Davis
Assembly Speaker Karen Bass
Energy Commissioner Jim Boyd
Energy Commissioner Karen Douglas
Ed Williams, Director, Division of Measurement Standards
Gordon Schremp, Energy Commission
John Moffat, Governor's Office

[1] Page 8, CEC Draft AB 868 Fuel Delivery Temperature Study and Sec. 12107, Business & Professions Code.