

Agenda Item F

Re-Visit of Proposed Exemptions

June 23, 2010



From House Bill 2186:

SECTION 6.

- (2)(a) The Environmental Quality Commission may adopt by rule low carbon fuel standards for gasoline, diesel and fuels used as substitutes for gasoline or diesel.
- (2)(b) The commission may adopt the following related to the standards, including but not limited to:
- (2)(b)(E) Exemptions for liquefied petroleum gas and other alternative fuels that are used in volumes below thresholds established by the commission;
- (4) The provisions of this section do not apply to:
- (4)(a) Motor vehicles registered as farm vehicles under the provisions of ORS 805.300.
- (4)(b) Farm tractors, as defined in ORS 801.265.
- (4)(c) Implements of husbandry, as defined in ORS 801.310.
- (4)(d) Motor trucks, as defined in ORS 801.355, used primarily to transport logs.

Note: An exemption for home heating oil is not explicitly included in the HB2186 statute; however, DEQ understands the Legislature's intent to be that Oregon's low carbon fuel standard applies only to transportation fuels, not home heating fuels.

The purpose of this document is to provide the rationale for the proposed fuel use exemptions to the low carbon fuel standard. This document also proposes thresholds for such fuel exemptions, where appropriate.

Section 1: Overview and Discussion of Exemptions

HB2186 specifically exempts certain fuel uses from the Oregon LCFS, namely liquefied petroleum gas, and fuels used in farm vehicles, tractors and implements of husbandry, as well as log trucks. HB2186 also authorizes the Environmental Quality Commission to exempt liquefied petroleum gas and other alternative fuels used in volumes below thresholds established by the Environmental Quality Commission.

The Environmental Quality Commission also has the authority to establish additional exemptions, as appropriate. Additional exemptions proposed by DEQ include fuels used in the following applications:

- Ocean-going vessels;
- Aircraft;

- Racing vehicles;
- Military tactical vehicles; and
- Military tactical support equipment.
- Interstate locomotives;

Exemptions to the Oregon Low Carbon Fuel Standard apply to volumes of fuel used in Oregon that meet certain criteria. In order to claim an exemption from the low carbon fuel standard, a regulated party must track the volume of exempted fuel sold in a verifiable and traceable manner, and report such volumes to DEQ. A regulated party can subtract exempt fuel volumes from the total volume of fuel subject to the low carbon fuel standard.

Section 2: Rationale for Proposed Fuel Use Exemptions

Exemptions required by HB2186

The following section provides the rationale for the proposed fuel use exemptions listed in statute:

Liquefied Petroleum Gas

HB 2186 explicitly exempts liquefied petroleum gas (propane) from the low carbon fuel standards. Therefore, DEQ proposes to exempt liquefied petroleum gas used as a transportation fuel under the low carbon fuel standard.

Farm Vehicles, Tractors and Implements of Husbandry

HB 2186 explicitly exempts farm vehicles, tractors, and implements of husbandry, as defined in statute. Therefore, DEQ proposes that owners and operators of farm vehicles and equipment meeting the definitions in Oregon Revised Statutes (ORS 805.300, 801.265, 801.310, respectively) may have in their possession fuel that does not meet the low carbon fuel standard(s).

Paperwork documenting farm uses of diesel and biodiesel blends is currently generated for fuel tax purposes and submitted to the Oregon Department of Transportation. Regulated parties could use similar or, in most cases, the same documentation for tracking exempted fuel volumes under the low carbon fuel standard (LCFS). For example, users of diesel and biodiesel blends are not required to pay tax on the fuel they purchase if they are registered with the Oregon Department of Transportation as a Use Fuel User and complete and submit to the fuel provider an Oregon Exemption Certificate. The Exemption Certificate indicates the reason for which the user is allowed to purchase fuel without tax (known as *ex-tax* sales). For each *ex-tax* transaction, an invoice is generated that includes the type and volume of fuel sold. This existing information could be used by a regulated party to quantify the amount of fuel sold to exempt farm uses under the low carbon fuel standard.

Trucks used primarily to transport logs (log trucks)

HB 2186 explicitly exempts motor trucks used primarily to haul logs, as defined in statute. Therefore, DEQ proposes that owners and operators of motor trucks which meet the definition in Oregon Revised Statute (ORS 801.355) and are used primarily to haul logs, may have in

their possession fuel that does not meet the low carbon fuel standard(s). The regulated party will be responsible for collecting verifiable and traceable documentation certifying that exempted fuel volumes were used in log trucks in order to claim an exemption from the low carbon fuel standard.

As proposed, DEQ understands the exemptions for farm equipment and vehicles and log trucks to apply to the fuel provided to various users, not the users themselves (as those users are not proposed to be regulated by the LCFS). For example, the exemption for “log trucks” applies to the fuel provided to those trucks by a regulated party such as a fuel distributor/provider. In order to exempt the fuel sold for farm or log truck use (or any other exempt use), the regulated party providing the fuel will be required to furnish to DEQ traceable and verifiable documentation of fuel volumes sold for exempted uses in order to calculate credits and deficits under the LCFS program. Those amounts could then be subtracted from (but shown in) annual compliance calculations.

In addition to the exemptions proposed above, HB2186 allows the Environmental Quality Commission (EQC) to approve exemptions to the low carbon fuel standard based on volumetric thresholds. In determining what, if any additional exemptions should be allowed, DEQ staff looked to the California Low Carbon Fuel Standard for other possible exemptions to implement in Oregon. The following are proposed volumetric exemptions to the low carbon fuel standard:

Fuels used in volumes below thresholds established by the Commission

HB 2186 allows fuels used in volumes below a threshold established by the Environmental Quality Commission to be exempt from the LCFS. Volume exemption thresholds for alternative fuels could facilitate the production of fuels with low carbon intensities and provide producers of these fuels adequate lead time to develop the technologies needed to make these fuels viable for transportation applications. DEQ proposes the following two volume-based exemptions for determining whether a fuel is subject to the low carbon fuel standard:

Fuels Used for Transportation - Statewide Total:

California’s LCFS allows an exemption for fuels used for transportation in volumes (total for the entire sector) less than 3.6 million *gasoline gallon equivalent* (gge) per year. Oregon proportionately uses approximately 10 percent, by volume, of the fuel used in California. Therefore, DEQ proposes an exemption threshold of 360,000 gge (total volume, per year) for any single type of fuel used in Oregon for transportation purposes. **Under this exemption, any single type of fuel may qualify for an exemption from the low carbon fuel standard if the total volume used within Oregon in any given year is less than 360,000 gasoline gallons equivalent.**

Small Volume Fuels - Individual Producers:

Producers of low carbon fuels may also be eligible for exemptions from the low carbon fuel standard if the volumes they produce fall into one of the following categories:

- **A fuel producer’s production volume in any year is less than 10,000 gallons.** This exemption threshold is intended to facilitate start-up and small-scale companies entering into the alternative fuels market,
- **A fuel producer’s production volume is between 10,000 to 50,000 gasoline gallons equivalent, and the total volume is used in its entirety by the fuel producer.** This exemption threshold is intended to facilitate the on-site production and use of low carbon fuels. For example, a farm owner may choose to produce biodiesel and operate their farm equipment with that fuel. Such an exemption would allow for the use of self-produced fuels at the same location, and would not require such fuels to meet the low carbon fuel standard.

Other proposed exemptions

In California, fuels used in interstate locomotives (i.e., trains that travel across multiple states), ocean-going vessels, aircraft, racing vehicles, military tactical vehicles and tactical support equipment are exempt from the California low carbon fuel standard. DEQ staff believes that an approach similar to that of California makes sense for implementation of a low carbon fuel standard in Oregon and proposes the following additional exemptions:

Interstate locomotives: Interstate rail operations are covered by federal laws that restrict the regulation of interstate railroads by individual states. DEQ proposes that fuels used in the operation of interstate locomotives are not required to meet the low carbon fuel standard(s).¹

Ocean-going vessels: Ocean-going vessels travel long distances and could avoid regulation simply by changing their purchasing patterns. Those changes could disrupt local fuel markets with no emissions reduction benefit. Ocean-going vessels are exempted under California’s LCFS for that reason. DEQ staff proposes that fuels used in ocean-going vessels be exempt from the Oregon low carbon fuel standard, while fuels used in all other water craft would be subject to the requirements of the standard.

Aircraft, Racing Vehicles, Military Tactical Vehicles, and Tactical Support Equipment: Certain types of specialized equipment have demanding performance characteristics and may have special fuel needs. Vehicles that operate at extreme temperatures, pressures or other conditions may be more likely to experience problems with fuel modifications that would go unnoticed in normal applications. Fuels used for aircraft, racing vehicles, military tactical vehicles, and tactical support equipment represent relatively small volumes and are exempted from California’s LCFS. DEQ proposes that Oregon’s LCFS also exempt fuels used in these specialized applications to avoid any unintended effects.

¹ DEQ is still evaluating how to classify fuels used in intrastate, or short-haul locomotive applications.

Section 3: Consideration of Exemptions under a Low Carbon Fuel Standard

Claiming exemptions under the low carbon fuel standard

It is important to note that a regulated party who sells a blended fuel to an exempt user (e.g. 98% diesel and 2% biodiesel), must either exclude that entire volume of blended fuel from their compliance obligation or include the entire volume. What they cannot do is split the blend apart, and deduct the exempt diesel from their compliance obligation and at the same time take credit for the biodiesel fraction of the blend. This would be in effect “double counting” the carbon reduction value of that exempt fuel. For example, under the Renewable Fuel Standard, all diesel² sold in Oregon (except for marine and locomotive) is currently required to contain 2% biodiesel by volume (known as B2). This approach would also keep the LCFS program neutral on the sale of bio-fuels to exempt users.

² Both on- and off-road diesel fuel