Statement of Mr. Joseph Sparano
On behalf of the
Western States Petroleum Association
Before the Congressional Government Reform Subcommittee
on Energy Policy, Natural Resources and Regulatory Affairs
July 2, 2003 –10:00 a.m.

Good morning. My name is Joe Sparano. I am President of the Western States Petroleum Association or, WSPA. Our trade association represents approximately 30 petroleum companies that explore, produce, manufacture, transport and market petroleum products in six western US states – California, Arizona, Nevada, Washington, Oregon and Hawaii.

I am pleased to be invited to speak to you today. As I mentioned, WSPA supports petroleum companies in western states. The association typically confines its activities and advocacy to the state level, and does not engage in federal issues.

However, California as usual seems to be the bell-weather state for our nation when new and improved products and advanced regulatory programs are involved. In this case, our members have already started transitioning from one gasoline oxygenate (MTBE), to another, (ethanol). I understand you would like to hear some details today about our experiences so far.

Before I address the subject of our industry's California oxygenate transition, I would like to provide the panel with some background information for those not familiar with the make-up of our state's petroleum industry and California's gasoline specification history.

First, our industry: WSPA members' California activities currently directly employ over 300,000 Californians and those jobs are indirectly responsible for another 700,000 jobs. That results in more than one million total people employed because of investments and operations of our state's petroleum industry.

Also, our members currently produce almost 1 million barrels per day of crude oil from reserves located in the state. They also operate 12 highly complex refineries that produce over 1 million barrels per day of the cleanest burning grades of gasoline on the planet.

Next, some history: in 1990, the federal Clean Air Act Amendments required the use of cleaner burning, reformulated gasoline (or, RFG) containing a specified minimum amount of oxygen in areas with the worst ozone pollution. Los Angeles, the San Joaquin Valley and the Sacramento area are among the sections of California that have been part of that program.

Methyl Tertiary Butyl Ether (or MTBE) was widely used as an oxygenate that would promote cleaner burning gasoline. Unfortunately, traces of MTBE have since been found in groundwater, leading to the decision to phase-out this oxygenate.

These clean fuels, along with emission control equipment on vehicles, have played a major role in the dramatic air quality improvements that have occurred in California. In fact, the biggest gains in air quality have occurred right here in southern California.

And, throughout California, air quality is about twice as good today as it was in 1975, as measured by statewide ozone smog levels. Perhaps even more impressive is that our state has reduced pollution while at the same time California's population has grown by 43% and the number of vehicle miles traveled has nearly doubled.

Now, let me address our recently started and continuing transition to ethanol-blended gasoline. At this point, we have gained several months of manufacturing, distribution and marketing experience, using gasoline blended with ethanol. And, a majority of our industry members have made the voluntary transition to ethanol.

Although California was one of the first states to ban MTBE, effective January 1, 2003, our state government delayed the ban date by one year to January 2004. This was partially due to the state's early concerns about the availability of and price associated with ethanol supply, and the possible market volatility impacts on California's driving public, of an abrupt change in product composition.

There was also some concern by government agencies and others that segregation of the marketplace into gasoline blended with ethanol and gasoline blended with MTBE during a transition phase might, by itself, lead to market tightness and price spikes. That concern has thus far not really materialized, and all our member companies have publicly reported that they plan to have the transition completed by the January 2004 deadline.

One of the conclusions contained in a May 2003 Energy Information Administration (EIA) report on California's early transition states that, in general, the transition to ethanol has gone remarkably well. It further indicates that this seems to be due in part to several years of preparation (and collaborative efforts) by the private sector and state government agencies.

We also believe this type of collaborative effort, including detailed dialogue and adequate lead-time, is critical to ensure that logistics issues are worked out before a transition. Ethanol supplies were adequate this spring, and the infrastructure to deliver, store and blend ethanol at terminals was developed in a timely manner.

While the transition to ethanol-blended gasoline is going relatively smoothly in California, there was a gasoline price spike this spring. It is important to recognize that the price of gasoline is determined by a variety of market conditions at any given point in time, and those conditions are constantly changing.

According to the EIA and others, the gasoline price spike experienced this spring in California, as elsewhere in the nation, was due largely to the following factors:

- An exponential increase in the cost of crude oil;
- Refinery maintenance activities and unplanned outages at several California plants;
- The higher cost of manufacturing California's more-difficult-to-produce, special cleaner burning gasoline; and,
- The continuing increase in demand versus supply of CARB gasoline.

Coincidentally, the price spike was concurrent with the timing of the transition from winter grade to summertime gasoline. This transition results in the requirement for a lower vapor pressure product that typically is more difficult to produce, and that must be distributed throughout the same delivery system, displacing entirely the previous supplies of winter gasoline over a short period of time.

Also, in California, as noted by the Federal Trade Commission and others, retail prices tend to run higher even under the best of circumstances, due to our unique cleaner-burning gasoline formula – the cleanest in the world – and the fact that our state has the third highest combined taxes on gasoline in the country – over 50 cents per gallon.

It seems clear from this information that no individual factor, including the transition from MTBE blended to ethanol-blended gasoline, should be singled out as the cause of last spring's spike in California retail prices. However, there is an effort underway by the Energy Commission to determine the causes of periodic swings in California gasoline prices and to recommend measures to the legislature to help stabilize the situation.

While WSPA and its member companies are actively involved in this evaluation process, we oppose any direct government intervention to "fix" energy markets. There is ample historical data that reminds us those types of government mandates are almost always counterproductive. The free market actually works very well.

There are some specific actions, however, that could help as this nation moves to an ethanol-blended gasoline.

First, WSPA strongly encourages repeal of the current federal RFG 2% oxygen mandate, and has been engaged with other parties in advocating elimination of the requirement for California. Mandating an arbitrary amount of oxygenate in RFG provides no added environmental benefits, and reduces flexibility.

What I want to make clear is that even if an oxygenate waiver is granted, it is likely many of our members will continue to use ethanol. Our companies simply want the flexibility to use oxygenates where they make the most economic and environmental sense. It is essential for supply and efficiency reasons that refiners have maximum flexibility in the way they manufacture gasoline.

Second, WSPA supports adoption of a provision limiting product defect liability for manufacturers or sellers of any product approved for use by Congress or any of the regulatory agencies.

Third, there needs to be an overhaul of the permitting process in many states – definitely in California. Obtaining permits in a timely and efficient manner is a significant hurdle to ensuring a sufficient infrastructure is in place.

WSPA supports the government identifying and removing impediments to investments that will improve an already efficiently functioning marketplace, while not impacting negatively the many improvements to the environment already gained through investments and other actions by the petroleum industry.

Generally speaking, I want to caution you that the jury is still out, as it were, on the long-term consequences of an ethanol mandate in California and elsewhere. As the transition is completed here, and as other states shift to ethanol as the preferred oxygenate, there may be logistic, supply, environmental or other issues that were not initially anticipated.

It is essential, therefore, that the industry be provided with maximum flexibility to use ethanol where it makes the most sense. Repealing the RFG oxygen content requirement would provide such flexibility.

Let me be clear – WSPA's companies fully support free markets, energy diversification and fuel choice. We maintain that government standards should be performance-based, and allow for maximum flexibility to meet the desired goals.

We believe that a strong and efficient petroleum industry also has an important part to play in ensuring a healthy economy. We are interested in government policies that will facilitate that role by supporting a more favorable business climate in California and elsewhere.

In closing, I'd like to thank this committee for your interest in ensuring that there have been minimal disruptions as many of our companies have transitioned to the use of an ethanol based oxygenate. WSPA and its members are prepared to work with you as the remaining companies complete the transition from MTBE by California's year-end 2003 deadline.

As always, our industry will continue its longstanding commitment to complying with government regulations as safely, cleanly and cost-effectively as possible.