

i. Designate and Track as a Replacement for the Non-Highway Baseline Approach

Under the designate and track approach, a refiner or importer would designate its 500 ppm diesel fuel as highway diesel fuel or NRLM diesel fuel and this refiner designation would be used to differentiate highway fuel and NRLM fuel instead of the non-highway baseline. For example, the highway 80/20 requirement would only apply to the amount of diesel fuel designated by the refinery or importer as highway diesel fuel. A marker would still be used to segregate heating oil, but the dye requirement for NRLM at the refinery gate would be removed. As with the baseline approach, undyed 500 ppm highway and 500 ppm NRLM could be fungibly distributed up until the point the NRLM diesel fuel is dyed. These refiner designations would have to follow the fuels through the distribution system. Under this designate and track approach, fuel distributors would be required to ensure that they did not sell more diesel fuel to the highway market than they took in as highway fuel. For example, if 60% of the fuel they took in was originally designated by the refineries as NRLM, they could not sell more than 40% to the highway market. The refiner or importer would have no obligation to ensure this occurred and no liability if it did not occur.

This approach shifts the focus from monitoring and enforcement of production at the refinery gate to monitoring and enforcement of the volumes of fuel handled by each party in the distribution system. Under the designation and track approach, refiners and importers would have complete flexibility to designate individual batches of diesel fuel or even portions of batches as either highway fuel or NRLM fuel. A pipeline could mix undyed highway 500 ppm and NRLM diesel fuels and ship them fungibly as a single physical batch as in the non-highway baseline approach. However, two sets of records would be kept, one applicable to the highway fuel portion and one applicable to the NRLM fuel portion. Whenever all or a portion of the fungible batch was split off or sold, that portion would have to carry one of the two designations, highway or NRLM. The sum of the volumes designated as either fuel would always be required to add up to the volumes designated in the original batch. A combination of fungibly mixed batches would be handled similarly, with the total volumes of each designation of volume split off or sold equaling the sum of the volumes of each designation of the original batches, respectively.

Each party in the distribution system beyond the refinery gate would be required to reconcile the volumes taken in and the volumes discharged, based on the designations of the diesel fuel, annually. For example, assume that over a year a pipeline received a total of 100,000,000 gallons of undyed 500 ppm diesel fuel from various refineries, with 70% of what it received being designated by the refineries as highway and 30% designated as NRLM. Over the year the pipeline would also designate what it discharged at various terminals or other points as either highway or NRLM. The pipeline would have to ensure that over a year's time it did not discharge more than 70% of the volume of this entire pool of 500 ppm diesel fuel as highway diesel fuel, to ensure that fuel designated as NRLM was not inappropriately converted to highway use. It could not discharge more 500 ppm fuel as highway than it took in as highway, and it would have to discharge at least as much 500 ppm diesel fuel designated as NRLM as it took in. This same reconciliation process would apply to every party in the distribution system.

A primary advantage of this designate and track approach for refiners is that it would allow them complete flexibility in deciding how much 15 ppm highway diesel fuel to produce, allowing them to react to changing market conditions. As long as 80 percent of whatever volume they designated as highway was 15 ppm, they would be in compliance. However, in order to maintain the integrity of the highway program, EPA would have to ensure that all diesel fuel designated as NRLM eventually was dyed and sold to the NRLM market. Otherwise, for example, refiners and importers could simply designate diesel fuel under the more lenient NRLM diesel fuel program while downstream in the distribution system the fuel was shifted to the highway diesel fuel market. Such shifting would compromise the required 80/20 split between 15 ppm and 500 ppm highway diesel fuel and undermine the benefits and integrity of the highway program. Various refiners proposed that EPA compare the volume of all diesel fuel designated as NRLM by the refineries and importers nationwide and compare that with the volume dyed nationwide to determine whether the approach was working. Unfortunately, this approach is not feasible, since EPA could not determine and take corrective action against refiners, importers, or distributors if the designated and dyed volumes did not reconcile. To locate the cause of a discrepancy between the

designated and dyed volumes, EPA would have to audit the records of every party in the distribution system nationwide. The refiners and importers would not face any liability under this approach for any downstream discrepancy unless there was evidence of collusion with downstream entities.

Thus, under this designate and track approach, EPA would need to require that all parties handling undyed diesel fuel designated as NRLM maintain records for each batch of fuel shipped and received and submit reports periodically demonstrating that the volume of undyed NRLM designated fuel that they dyed plus that transferred undyed to another fuel distributor equaled or exceeded the volume of undyed NRLM designated fuel that they received.²⁴⁸ We would also need to require that all parties handling dyed or undyed NRLM diesel fuel maintain records and submit reports demonstrating that the volume of NRLM designated fuel that they received was sold for use in nonroad, locomotive or marine diesel engines or transferred with the same designation to another fuel distributor. These requirements would be applied on an annual basis, providing fuel distributors with flexibility to shift fuel designated for one use to the other market and vice versa to address short term supply fluctuations of each fuel but still maintain overall program integrity.

Given the large number of entities involved in distributing diesel fuel and the number of transactions, there are a number of serious practical concerns regarding the enforceability of such an approach. Under the baseline approach described above, enforcement is focused on the roughly 128 refineries producing either highway or NRLM diesel fuel. This designation and track approach would add the various entities in the distribution system. In order to improve the chances of effectively enforcing the program, we would at a minimum have to limit the scope of the entities involved to bulk terminals and entities upstream. Thus, all NRLM diesel fuel would have to exhibit visible evidence of dye after leaving a large bulk terminal. Even with this limitation, there would be as many as 100 pipelines and 1000 terminals reporting. Enforcement of such an approach would be difficult because to determine whether inappropriate changes in

²⁴⁸ If the volume of dyed NRLM fuel exceeded the designated volume, this would imply that some highway 500 ppm fuel was dyed. This would not compromise the required 80/20 split between 15 ppm and 500 ppm fuel under the highway program, although the total social cost of producing the fuel would be higher.