March 24, 2000

The Honorable Carol M. Browner
Administrator, United States Environmental Protection Agency
Ariel Rios Building
1200 Pennsylvania Ave., N.W.
Washington, D.C. 20460

Dear Ms. Browner:

Enclosed for your consideration is the Report of the Small Business Advocacy Review Panel (SBAR Panel or the Panel) convened for the planned proposed rulemaking on **Heavy-duty Engine Standards and Diesel Fuel Sulfur Control** that the Environmental Protection Agency (EPA or the Agency) is currently developing.

On November 12, 1999, EPA=s Small Business Advocacy Chairperson convened this Panel under section 609(b) of the Regulatory Flexibility Act (RFA) as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA). In addition to the Chair, the Panel consisted of the Deputy Director of EPA=s Office of Transportation and Air Quality, the Chief Counsel for Advocacy of the Small Business Administration, and the Deputy Administrator of the Office of Information and Regulatory Affairs within the Office of Management and Budget.

The Report includes a discussion of the options under consideration for the proposed regulation under development, a description of the Panel's outreach to small entity representatives, summary of small entity comments received by the Panel, and the Panel's findings and discussion.

Sincerely,

/S/
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Thomas E. Kelly, Chair
Small Business Advocacy
U.S. Environmental Protection Agency

/S/
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John T. Spotila, Administrator
Office of Information and Regulatory Affairs
Office of Management and Budget

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Jere W. Glover
Chief Counsel for Advocacy
U.S. Small Business Administration

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Christopher H. Grundler, Deputy Director
Office of Transportation and Air Quality
Office of Air and Radiation
U.S. Environmental Protection Agency

Enclosure

Report of the Small Business Advocacy Review Panel on Control of Air Pollution from New Motor Vehicle Engines: Heavy-Duty Engine Standards and Diesel Fuel Sulfur Control Requirements

Executive Summary

This section summarizes the Report of the Small Business Advocacy Review Panel (SBAR Panel or the Panel) convened for the proposed rulemaking on heavy-duty engine standards and diesel fuel sulfur control that the Environmental Protection Agency (EPA or the Agency) is currently developing.

On November 12, 1999, EPA's Small Business Advocacy Chairperson convened this Panel under section 609(b) of the Regulatory Flexibility Act (RFA) as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA). In addition to the Chair, the Panel consisted of the Deputy Director of EPA's Office of Transportation and Air Quality, the Chief Counsel for Advocacy of the Small Business Administration, and the Deputy Administrator of the Office of Information and Regulatory Affairs within the Office of Management and Budget.

The Panel's findings and discussion are based on the information available during the term of the Panel. EPA is continuing to conduct analyses relevant to the proposed rule, and additional information may be developed or obtained during the remainder of the rule development process and from public comment on the proposed rule. Any options the Panel identifies for reducing the rule's regulatory impact on small entities may require further analysis and/or data collection to ensure that the options are practicable, enforceable, environmentally sound and consistent with the Clean Air Act (CAA or the Act).

Industries That May Be Subject to the Proposed Regulation

A program establishing new emission standards for heavy-duty engines and new standards for the sulfur content of highway diesel fuel would directly affect manufacturers of heavy-duty engines and petroleum refiners that produce highway diesel fuel, respectively. In addition, the program potentially could directly affect diesel distributors and marketers. EPA has not identified any manufacturers of heavy-duty engines that meet SBA's definition of a small business. EPA has, however, identified approximately 22 petroleum refiners that meet SBA's definition of a small refiner (1500 or fewer employees) and produce highway diesel fuel. EPA has also identified several thousand businesses in the diesel distribution and marketing industry that meet SBA's definitions of small business.

Summary of Small Entity Outreach

The Panel had several meetings and conversations with small entity representatives (SERs) to discuss the potential diesel sulfur program. In addition, EPA conducted outreach with small entities in the months preceding the Panel process. On November 23, 1999, the Panel sent a package of outreach materials to the SERs, which included an overview of various options for implementing a program for ultra-low sulfur highway diesel fuel, and a set of related questions. On November 30, 1999 the Panel met with the SERs to hear their comments on preliminary options for regulatory flexibility. The Panel also received written comments from the SERs in response to the discussions at this meeting and the outreach materials. The Panel asked SERs to evaluate how they would be affected under a regulatory approach that would establish a national ultra-low standard for all diesel fuel effective at a single point in time ("single fuel" approach), and how they would be affected if such a standard were phased in a manner similar to the introduction of unleaded gasoline ("phase-in" approach).

One of the small refiner SERs, the Gary-Williams Energy Corporation, invited the Panel to tour its refinery in Wynnewood, Oklahoma. Several representatives of the Panel conducted this site visit on December 17, 1999, and were pleased to have this excellent opportunity to visit a small refinery. In addition to touring the refinery, Gary-Williams also arranged with one of its jobbers a tour of a local truck stop. These site visits were valuable for representatives of the Panel to see first hand how a small refinery and a truck stop operate.

Panel Findings and Discussion

Major Topics of Panel Discussion

The Panel discussed each of the issues raised in the outreach meetings and in written comments by the SERs. Regarding small refiner issues, the Panel's key discussions centered around the nature of refining operations, how operations and economics differ between small and larger refiners (and among small refiners), and the kinds of regulatory alternatives that might assist small refiners in complying with a sulfur standard for highway diesel fuel. In regard to small diesel distributors and retailers, the Panel discussed the diversity of businesses within the distribution industry and how they relate to one another, the way in which service stations and truck stops store fuels, how retailers make decisions about which fuels to sell, how they would be affected by a requirement that ultra-low sulfur fuel be made available at retail outlets, and numerous other facets of these operations. The Panel also discussed the relative merits of a "single-fuel" approach and a "phase-in" approach, but did not formulate a recommendation as to which approach EPA should adopt in its proposed rule. Some Panel members did, however, recommend that EPA seek comment on specific flexibility options (described below) that would be suitable to each of the approaches; these recommendations are included in the Report.

Projected Reporting, Recordkeeping, and Other Compliance Requirements of the Proposed Rule

EPA expects that recordkeeping, reporting and compliance provisions of the proposed rule will be fairly consistent with those in place today for other fuel programs, including the current 500 ppm highway diesel regulation. For example, recordkeeping likely would involve the use of product transfer documents, which are already required in some instances under the 500 ppm sulfur rule.

If EPA adopts a provision allowing small refiners to continue selling 500 ppm fuel to the highway market, there would have to be certain safeguards to prevent contamination of the ultra-low sulfur fuel, and to prevent misfueling of new vehicles. Under such a flexibility option, refiners as well as downstream parties could be subject to enforceable measures to prevent contamination and misfueling (e.g., general segregation requirements, labeling at pump stands).

A phase-in approach could include additional compliance requirements for retailers, including a requirement that diesel fuel retailers (e.g., service stations and truck stops) make the ultra-low sulfur grade available at their retail outlets.

Other Relevant Federal Rules Which May Duplicate, Overlap, or Conflict with the Proposed Rule

The regulations EPA expects to propose would be similar in many respects to the existing sulfur standard for highway diesel fuel, but with a lower sulfur standard. The Panel is not aware of any area where the regulations under consideration would directly duplicate or overlap with the existing federal, state, or local regulations. The Panel notes, however, that several small refiners also will be subject to the recently promulgated gasoline sulfur control requirements in approximately the same timeframes as the standards under consideration for highway diesel fuel. The Panel also notes that more stringent diesel sulfur standards might require many refiners to obtain permits from state and local air pollution control agencies under the Clean Air Act's New Source Review program prior to constructing the desulfurization equipment needed to meet the standards.

Under a phase-in approach, many diesel retail outlets might install additional tanks in order to accommodate the ultra-low sulfur fuel as well as the current grade. Such construction would likely require compliance with EPA's underground storage tank program. Similarly, bulk terminals and bulk plants adding new tank capacity to accommodate both grades of diesel fuel would likely be subject to local fire codes and other related codes.

Regulatory Alternatives

The Panel considered a range of options and regulatory alternatives for providing small businesses with flexibility in complying with new sulfur standards for highway diesel fuel. As part of the process, the Panel requested and received comment on several early ideas for flexibility that were suggested by SERs and Panel members. Taking into consideration the comments received on these ideas, as well as additional business and technical information gathered about potentially affected small entities, the Panel summarizes these options below.

Panel Recommendations

1) The Panel recommends that EPA seek comment on an option for small refiner flexibility that would allow small refiners to continue selling their current 500 ppm highway diesel, provided there are adequate safeguards to prevent contamination and misfueling. The Panel further recommends that EPA request comment on an appropriate duration for this option. This option effectively delays the ultra-low sulfur compliance date for small refiners, and allows them to continue selling their current fuel to the highway diesel market. To ensure the environmental benefits of the rule are achieved while implementing this flexibility option, there would have to be certain safeguards with refiners as well as downstream parties to prevent contamination of the ultra-low sulfur fuel, and to prevent misfueling of new vehicles.

2) The Panel recommends that EPA seek comment on an option that would provide a process for refiners to seek case-by-case approval of applications for temporary waivers to the diesel sulfur standards, based on a demonstration of hardship circumstances. Small refiners have told the Panel that there is no "one size fits all" approach to flexibility given the wide variety of refinery circumstances and configurations. The Panel recognizes that there may be case-by-case flexibilities that are feasible, environmentally neutral, and warranted to meet the unique needs of an individual refiner, but that, if applied across the board, might jeopardize the environmental benefits of the program. The Panel envisions that this option would be modeled after a similar provision in the gasoline sulfur program. This option would allow domestic and foreign refiners, including small refiners, to request additional flexibility based on a showing of unusual circumstances that result in extreme hardship and significantly affect the ability to comply by the applicable date, despite their best efforts. The Panel also recommends that EPA seek comment on several issues related to how such a hardship provision could best be implemented.

3) The Panel recommends that EPA seek comment on the appropriate level of the sulfur cap, and on a 50 ppm cap for small refiners. Some Panel members suggest that EPA explore whether an averaging, banking and trading program, appropriately structured, should be used to encourage small refiners to reduce average sulfur levels even further below this cap level, wherever it is inexpensive to do so.

Some Panel members believe that each of the above ideas, individually or in combination, potentially could provide significant relief to small businesses, with minimal environmental impact, and

should be considered in the diesel rulemaking. The SBA Panel member believes that these ideas, taken together, potentially could provide significant relief to small businesses while still meeting statutory objectives and should be considered as a package in the diesel rulemaking. In addition to the above regulatory alternatives, the Panel believes EPA should carefully consider all comments received during the outreach process on these and other issues of concern to small entities.

Other Recommendations

Some Panel members recommend that EPA seek comment on options to provide flexibility under a phase-in approach to implementing more stringent diesel fuel sulfur standards. These Panel members believe that a phase-in approach (where small businesses are exempt from certain requirements) has sufficient merit under the Regulatory Flexibility Act that it merits discussion and a request for comments from the public as part of the proposal. The Panel believes that while a "phase-in" approach would provide greater flexibility to small refiners, it could impose significant burdens on small retailers and distributors, because the industry would have to accommodate a second grade of highway diesel fuel. Therefore, the Report includes recommendations appropriate to a phase-in approach, focused on addressing the burden of both small refiners and small entities in the retail and distribution sectors of the petroleum industry.

1) Some Panel members recommend that the proposed rule request public comment on a phase-in approach that would adopt a requirement, from which small retailers would be exempt, that ultra-low sulfur diesel fuel be made available wherever highway diesel fuel is sold. For example, this availability requirement could be limited to truck stops selling more than 200,000 gallons per month of diesel, and to retail outlets selling more than 10,000 gallons per month of diesel fuel.

2) Some Panel members urge EPA, in developing its proposal, also to explore using a production requirement in lieu of an availability requirement to assure general availability under a phase-in approach. While acknowledging significant concerns with this approach, on the basis of SER comments, these Panel members also recommend that EPA request comment on this alternative within the context of a proposal that includes a phase-in approach. These Panel members further recommend that the proposed rule should also request comment on a small refiner exemption from the production requirement, and on an averaging, banking, and trading provision that would allow small refiners choosing to comply early under a phase-in to earn credits and sell them to other refiners.

A full discussion of comments received and Panel recommendations are included in the Panel's final full Report.