185.

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

----In the Matter of----	)	
	)	
PUBLIC UTILITIES COMMISSION	)	DOCKET NO. 05-0002
	)	
Instituting a Proceeding to Investigate the Issues and Requirements Raised by, and and Contained in, Hawaii Revised Statutes 486H, as Amended.	)	

DECISION AND ORDER NO. 22451

Filed May 3, 2006

At 3:10 o'clock P .M.

Karen Higashi

Chief Clerk of the Commission

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

----In the Matter of---- PUBLIC UTILITIES COMMISSION Instituting a Proceeding to Investigate the Issues and Requirements Raised by, and and Contained in, Hawaii Revised Statutes 486H, as Amended.	)	Docket No. 05-0002 Decision and Order No. 22451

DECISION AND ORDER

By this Decision and Order, the commission exercises its discretion under Hawaii Revised Statutes ("HRS") Chapter 486H (the "Hawaii Gas Cap Law") to modify the maximum pre-tax wholesale price of gasoline ("gas price caps" or "gas caps") to reflect the requirements of HRS § 486J-10 and Hawaii Administrative Rules ("HAR") § 15-35-3 (2004) (the "Ethanol Mandate"). The Ethanol Mandate requires that a minimum of 85% of the gasoline sold in Hawaii contain at least 10% ethanol.[1] Thus, with the advent of the Ethanol Mandate, a large portion of the gasoline in Hawaii will be gasoline that contains 10% ethanol ("E-10 gasoline"). Because E-10 gasoline is a different product from non-ethanol conventional gasoline (as was sold prior to the Ethanol Mandate), the commission issues this Decision and Order to set forth: (1) the gas price caps for E-10 gasoline ("E-10 gas price caps" or "E-10 gas caps"), (2) the commission's publication procedures for the maximum pre-tax wholesale price of E-10 gasoline; and (3) the continued

[1] See HAR § 15-35-3 (2004); HRS § 486J-10.

monitoring by the commission of matters related to HRS Chapter 486H.

As described in greater detail below, the E-10 gas price caps differ from the non-ethanol conventional gas price caps in two significant respects: (1) the baseline price of E-10 incorporates an indexed ethanol component, and (2) the zone price adjustments for E-10 are increased to include capital, inventory, barging, and other operational costs. Pursuant to Decision and Order No. 21952 in Docket No. 05-0002, filed on August 1, 2005, the commission will continue to calculate and publish non-ethanol conventional gas price caps, as applicable. The E-10 gas price caps and the applicable non-ethanol conventional gas price caps will be issued together.

The methodology adopted by the commission in this order constitutes the commission's best efforts to accurately and reasonably implement the current Hawaii Gas Cap Law alongside the Ethanol Mandate, within the spirit and intent of the Gas Cap Law.[2]

I.

Background

The procedural background was extensively laid out in Decision and Order No. 21952 and is hereby incorporated by reference. Currently, Chevron U.S.A. Inc. ("Chevron"), Tesoro Hawaii Corporation ("Tesoro"), Shell Oil Company ("Shell"), members of the Hawaii Petroleum Marketers Association

[2]The commission is aware that HB 3115, if passed into law, would dramatically amend the Hawaii Gas Cap Law. At such time, the commission will make the necessary adjustments, including but not limited to issuing another Order or Decision and Order.

("HPMA"), and the Division of Consumer Advocacy are parties to this proceeding (collectively "Parties"). ICF Consulting, LLC ("ICF") was retained by the commission to review and evaluate the issues and requirements raised by, and contained in, HRS Chapter 486H, as amended.

In Decision and Order No. 21952, the commission set forth:

> (1) the maximum pre-tax wholesale price of non-ethanol conventional gasoline;
>
> (2) the procedures for filing petitions and complaints with the commission;
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> (3) the procedures for publishing the gas price caps; and
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> (4) the risks identified in implementing HRS Chapter 486H.[3]

The commission concluded that the following factors should be used in determining the conventional (non-ethanol) gas price caps:

> (a) the HRS Chapter 486H baseline price and location adjustment factor established by the Legislature;
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> (b) the HRS Chapter 486H marketing margin factor established by the Legislature;
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> (c) the HRS Chapter 486H Premium and Mid-grade adjustments established by the Legislature; and
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> (d) the zone price adjustments recommended by ICF, except that the highest actual transportation costs would be used rather than the average transportation costs proposed by ICF.[4]

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[3] See Decision and Order No. 21952, filed Aug. 1, 2005, at 1-2.

[4] See id. at 2.

In Decision and Order No. 21952, the commission stated that it would establish the subsequent schedules and procedures in Docket No. 21952, including, but not limited to, "adjusting the maximum pre-tax wholesale price formula or factor to include ethanol."[5]

Following Decision and Order No. 21952, the commission gathered information from the Parties related to the Ethanol Mandate. On September 21, 2005, consistent with Decision and Order No. 21952, the commission issued Order No. 22056, which in part, ordered the Parties to submit proposals to adjust the HRS § 486H-13 factors to include the addition of ethanol blending requirements.[6] In addition, on December 22, 2005, the commission issued information requests, PUC-IR-42 through -50, regarding ethanol.[7] Finally, on March 2 and 3, 2006, by request of certain

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[5]See id. at 40.

[6]See Division of Consumer Advocacy's Submission in Response to Commission Order No. 22056, filed Nov. 1, 2005; Chevron U.S.A. Inc.'s Response to Order No. 22056, filed Nov. 1, 2005; Tesoro Hawaii Corporation's Response to Order No. 22056, filed Nov. 1, 2005; Sealed envelope from Akana Petroleum, filed Nov. 29, 2005; Aloha Petroleum, Ltd.'s Estimated Ethanol Conversion Costs, filed Dec. 1, 2005; Mid Pac Petroleum's Submission in Response to Order No. 22056, filed Dec. 1, 2005; Shell Oil Company's Response to Order No. 22056, filed Dec. 1, 2005; HPMA's Proposals to (I) Create Marketing Margin Factors for Different Classes of Trade and (II) Adjust Gas Cap Factors for Ethanol Requirements, filed Dec. 1, 2005; Mid Pac Petroleum, LLC's Submission in Response to Order No. 22056, filed Jan. 6, 2006; Chevron U.S.A. Inc.'s Supplemental Response to Order No. 22056, filed Feb. 24, 2006; Chevron's revised Exhibit A, which was originally filed on Feb. 24, 2006, filed Mar. 1, 2006.

[7]See Hawaii & Maui Petroleum Inc.'s Responses to PUC IRs 42-50, filed Jan. 6, 2006; Aloha Petroleum, Ltd.'s Response to PUC-IR-45 to IR-50, filed Jan. 6, 2006; Shell Oil Company's Responses to the Public Utilities Commission's Information Requests PUC-IR-42 to IR-50, filed Jan. 6, 2006; Tesoro Hawaii Corporation's Confidential Responses to Public Utilities Commission Information Requests, PUC-IR-42 to PUC-IR-50, filed

parties and with no objection from the Parties, Mid Pac Petroleum, LLC (HMPA member), Aloha Petroleum, Ltd. (HPMA member), Chevron, and Tesoro made confidential presentations to the commission on issues related to ethanol blending.

The commission provided ICF with the information it had obtained from the Parties, and asked ICF to prepare a report to the commission on the effect of the Ethanol Mandate on Hawaii's Gas Cap Law. On March 23, 2006, ICF submitted the report entitled "Recommendations to Modify Hawaii Revised Statutes Chapter 486H, Gasoline Price Cap Legislation, for the Ethanol Mandate, Hawaii Administrative Rules, Title 15, Chapter 35" ("ICF Report"). In its Report, ICF explains:

> The transition to a gasoline market which requires a minimum 85% of the gasoline sold to contain 10% ethanol will have a significant impact on the Hawaii gasoline market. There are several primary reasons for this, including:

Jan. 6, 2006; Chevron U.S.A. Inc.'s Responses to Public Utilities Commission's Information Requests, filed Jan. 6, 2006; Akana Petroleum's Responses to PUC-IR-42 to IR-50, filed Jan. 11, 2006; Chevron U.S.A. Inc.'s Responses to Public Utilities Commission's Information Requests, filed Feb. 7, 2006; Tesoro Hawaii Corporation's Confidential Responses to Public Utilities Commission Information Requests, PUC-IR-42 to IR-50, filed Feb. 9, 2006; Shell Oil Company's Supplemental Response to the Public Utilities Commission's Information Requests PUC-IR-45 to IR-50, filed Feb. 15, 2006; Mid Pac Petroleum LLC's presentation materials regarding confidential company data responsive to PUC-IR-42 to IR-50, filed Mar. 2, 2006; Aloha Petroleum, Ltd.'s presentation materials regarding confidential company data responsive to PUC-IR-42 to IR-50, filed Mar. 2, 2006; Tesoro Hawaii Corporation's confidential supplemental responses to Public Utilities Commission information requests and confidential PowerPoint slides presented at the ethanol presentation to the commission on March 3, 2006, filed Mar. 8, 2006; Chevron U.S.A. Inc.'s revised confidential responses to PUC-IR-42 and PUC-IR-49 and copies of Chevron's confidential PowerPoint presentation on the ethanol issue on March 3, 2006, filed Mar. 10, 2006.

ethanol by the importer to other Parties. The average cost of ethanol supply would then be reduced by the 51 cpg Federal tax credit applicable to registered blenders of ethanol into gasoline. This net average ethanol price ("industry aggregated ethanol pool price") would be a 10% component of the E-10 gas cap.

3. Increases to the current zone price adjustments to account for increased costs related to capital, operational, and inventory changes resulting from the Ethanol Mandate. This would be a fixed increase to the zone price adjustments for the applicable zones as follows:

Zone 1 (Oahu)	1.1 cpg
Zone 2 (Kauai)	3.3 cpg
Zone 3 (Maui)	2.4 cpg
Zone 4 (Hana)	2.4 cpg
Zone 5 (Molokai)	no change
Zone 6 (Lanai)	no change
Zone 7 (Hilo)	2.2 cpg
Zone 8 (Kona)	2.9 cpg[9]

On March 23, 2006, the commission provided copies of the ICF Report to the Parties, and requested that the Parties provide their written comments (if any) regarding the ICF Report no later than noon on March 28, 2006. On March 28, 2006, Tesoro, Shell, and HPMA filed their written comments.[10] On March 29,

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[9] See ICF Report at 4-5.

[10] See Tesoro Hawaii Corporation's Comments to ICF Recommendations for the Ethanol Mandate, filed Mar. 28, 2006 ("Tesoro's comments to the ICF Report"); Shell Oil Company's Preliminary Comments on the ICF Consulting Report Regarding Recommendations to Modify Hawaii Revised Statutes Chapter 486H, Gasoline Price Cap Legislation, for the Ethanol Mandate, Hawaii Administrative Rules, Title 15, Chapter 35, filed Mar. 28, 2006 ("Shell's comments to the ICF Report"); HPMA's Comments to Report: Recommendations to Modify Hawaii Revised Statutes Chapter 486H, Gasoline Price Cap Legislation, For the Ethanol Mandate, Hawaii Administrative Rules, Title 15, Chapter 35, dated March 23, 2006 submitted by ICF Consulting, LLC ("ICF"), filed Mar. 28, 2006 ("HPMA's comments to the ICF Report").

With respect to an alternative to the ethanol pool approach, ICF states:

> If the direct utilization of the delivered cargo prices to Hawaii is not feasible because all Parties submitting confidential information would not consent to the disclosure of a pool price average, ICF believes that an appropriate alternative would be to determine the weekly ethanol price in the gas cap formula as follows:
>
> 1. Calculate the average OPIS ethanol prices in New York, Chicago, and Los Angeles on a weekly basis
>
> 2. Add 4 cpg location differential or location adjustment factor
>
> 3. Deduct the 51 cpg Federal Ethanol tax credit for so long as it is applicable
>
> 4. The resulting delivered ethanol cost, inclusive of the blender's tax credit, should be added into the gas cap at 10% of the calculated E10 price (the other 90% is the HIBOB price).[17]

With respect to the use of the OPIS conventional unleaded gasoline spot prices as a benchmark for HIBOB, ICF states:

> [A]part from the costs specific to Hawaii refiners to export gasoline or naphtha, or meet distillation specifications, a conventional BOB product such as HIBOB should be cheaper to produce than an RBOB product. Furthermore, and again apart from the costs specific to Hawaii refiners to export gasoline or naphtha, or meet distillation specifications, generally speaking the cost

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2. Comment on the possible use of the OPIS Conventional gasoline prices as a baseline for the HIBOB market price given the relative tradeoff between the cost of the required reduction in vapor pressure to manufacture HIBOB gasoline blendstock, and the benefit of lower octane requirements to manufacture the HIBOB blendstock.

See ICF Supplement 1 at 2.

[17] See ICF Supplement 1 at 2.

II.

Discussion

A.

The Maximum Pre-Tax Wholesale Price for the Sale of E-10 Gasoline

Under HRS § 486H-13(b), "the commission shall determine the maximum pre-tax wholesale price of regular unleaded, mid-grade, and premium gasoline . . . such that the maximum pre-tax wholesale gasoline prices reflect and correlate with competitive market conditions." Indeed, in Act 242, Session Laws of Hawaii (2004), the Legislature stated that the objective of the Hawaii Gas Cap Law is "not to guarantee lower gasoline prices," but rather to "enhance consumer welfare by fostering the opportunity for prices that reflect and correlate with competitive market conditions." As such, the gas caps are designed to fluctuate with a virtual competitive market for gasoline in Hawaii. It is axiomatic that in determining prices that "reflect and correlate with competitive market conditions," the Hawaii Gas Cap Law was not intended as a mechanism to guarantee the petroleum industry recovery of its actual costs.

1.

The baseline price for E-10 gasoline

HRS § 486H-13(c) provides that the baseline price for regular unleaded gasoline shall be determined on a weekly basis and shall be equal to the average of three U.S. Mainland price points (Los Angeles, New York Harbor, and the U.S. Gulf Coast). However, HRS § 486H-13(c) also provides that "the commission, in its discretion, may determine a more appropriate baseline[.]"

2.

The HIBOB portion (including the Chapter 486H location adjustment factor) of the E-10 baseline price

In Decision and Order No. 21952, the commission determined that it would use the three U.S. Mainland price points identified in HRS Chapter 486H to calculate the baseline price for non-BOB conventional gasoline. As ICF explains, "[t]he current gasoline price cap determination uses OPIS market pricing for conventional gasoline as a means to determine a reasonably competitive alternative market source cost of supply into Hawaii."[25] Indeed, "[t]he OPIS benchmarks used in the current gas cap formula are necessary because there is no sustained history of imported gasoline into Hawaii to use as a credible basis."[26] However, with the Ethanol Mandate, HIBOB (as opposed to conventional gasoline) will be blended into E-10 gasoline. Therefore, the commission must first determine whether the OPIS spot prices for non-BOB conventional gasoline may be used as a benchmark for HIBOB.

In Supplement 1, ICF acknowledges that "it may be plausible to consider a benchmark that estimates the cost of HIBOB (or, conventional "BOB") gasoline as equivalent to the current conventional gasoline prices in use in the gas cap formula."[27] ICF explains,

> [A]part from the costs specific to Hawaii refiners to export gasoline or naphtha, or meet distillation specifications, generally

[25] See ICF Report at 16.

[26] See ICF Report at 18.

[27] See ICF Supplement 1 at 4.

> speaking the cost to produce a conventional BOB product such as HIBOB is likely lower than the cost of producing conventional gasoline. The reasons for this are:
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> 1. The lower octane is a cost savings; the lower vapor pressure is an increased cost to the refiner. Therefore they do tend to offset each other.
>
> 2. The degree of these offsets is based on the relative premium of octanes in the marketplace (as determined by the premium/unleaded spread), and the relative value of the butane uplift to gasoline (lowering vapor pressure by 1 psi RVP reduces butane blending by roughly 2% in gasoline)[.]
>
> 3. The economies of each of these offsets can vary widely based on prevailing markets, but the octane impact of reducing the unleaded octane level 2-3 numbers to allow for ethanol blending at the terminals could be 3-5 cpg lower cost. This is based on the 9 cpg premium in the gas cap formulation for premium vs unleaded price, or roughly 1.8 cpg per octane number. The offsetting impact of a 1 RVP reduction for butane, even with butane at fuel price levels, would likely be more in the 2 cpg higher cost range.[28]

None of the Parties stated or provided evidence to dispute that the cost for mainland refineries to produce HIBOB would be the same or lower than the cost to produce conventional gasoline.[29] Although some of the Parties did reference higher costs for Hawaii refineries,[30] the determination of "competitive market

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[28] See ICF Supplement 1 at 3-4.

[29] See Chevron's comments to Supplement 1; Tesoro's comments to Supplement 1; Shell's comments to Supplement 1; see also HPMA's comments to Supplement 1 (late filed).

[30] See Tesoro's comments to Supplement 1 at 3-7 ("ICF appears to argue that because an importer of BOB would not need a production cost adjustment, refiners are not entitled to one. ICF ignores reality when it attributes a cost savings to refiners

not on "competitive market conditions" as required by HRS § 486H-13(b).

As indicated above, the appropriate methodology for determining the cost of HIBOB is the cost of importing the appropriately blended product from the mainland. As ICF states, "apart from the costs specific to Hawaii refiners to export gasoline or naphtha, or meet distillation specifications, generally speaking the cost to produce a conventional BOB product such as HIBOB is likely lower than the cost of producing conventional gasoline."[33] Moreover, after reviewing the Hawaii refineries' costs, ICF finds that "[t]he information submitted to the Commission by the refiners does not, however, provide a clear, compelling, and specific basis to allow ICF to directly recommend to the Commission the costs submitted by the refiners."[34] Thus, the commission finds that the cost of acquiring HIBOB under competitive market conditions (i.e., from mainland refineries, as reflected under the OPIS benchmarks) would be approximately the same as the cost of acquiring non-BOB conventional gasoline. Accordingly, the commission determines that no adjustment should be made to reflect the higher costs experienced by Hawaii refineries.

The Parties' argument regarding the reduced demand for the refineries' gasoline product as a result of the Ethanol Mandate is equally unavailing. The commission understands that ICF recommends the inclusion of "a fixed 4 cpg

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[33] See ICF Supplement 1 at 3.

[34] See ICF Report at 13-14.

premium to the current conventional gasoline baseline price"[35] to account for the reduced demand for the refineries' gasoline product. ICF's recommendation is based on its assessment that "Supply increases by 10% ethanol addition, and Demand increases by 3% due to lower gasoline mileage per gallon with a 10% ethanol blend. Net supply increase is 7%."[36] ICF explains, "since ethanol will be increasing the supply of gasoline in Hawaii by a net 7%, the Hawaii refineries will incur costs to either reduce gasoline production or export gasoline or gasoline blendstocks, since there will be less demand for the refiner[ies]' gasoline product as a result of the mandate."[37] Based on the 7% increase in gasoline supply, ICF recommends "a fixed adjustment of 4 cpg to reflect the cost to produce HIBOB blendstock in Hawaii refineries above the current baseline price calculation of conventional gasoline price in New York, Los Angeles, and the Gulf Coast."[38] ICF recommends this approach because it believes that this method would more "fully recognize the costs to Hawaii wholesalers."[39] Indeed, ICF states that it "strongly believes that the use of a fixed price adjustment to recognize the HIBOB cost provides a mechanism that more closely aligns with the true cost of Hawaii refiners to manufacture HIBOB and re-balance the

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[35] See ICF Report at 4.

[36] See ICF Report at 11 n.3.

[37] See ICF Report at 11.

[38] See ICF Report at 15. In ICF's calculation, because HIBOB is "a 90% component of the delivered baseline price for E-10 gasoline sales," this results in "a net 3.6 cpg addition to the E-10 gas cap." See ICF Report at 4.

[39] See ICF Report at 12.

gasoline supply resulting from the Ethanol Mandate."[40] However, as stated above, HRS Chapter 486H requires the commission to set the gas price caps to "reflect and correlate with competitive market conditions," not necessarily to ensure that wholesalers recover their costs.[41] Accordingly, the commission determines that no adjustment should be made to reflect the reduced demand for the refineries' gasoline product as a result of the Ethanol Mandate.

Finally, with respect to the location adjustment factor, HRS § 486H-13(d) provides that "[t]he location adjustment factor . . . shall be $.04 per gallon or as otherwise determined by the commission and shall thereafter be subject to adjustment pursuant to section 486H-16(a)." In Decision and Order No. 21952, the commission determined that it would use the HRS Chapter 486H location adjustment factor. At this time, the commission has not found sufficient justification to deviate from the location adjustment factor established by the Legislature in HRS § 486H-13(d). Thus, the commission will continue to use the HRS § 486H-13(d) location adjustment factor in its calculations of the HIBOB portion of the E-10 baseline price.

Accordingly, the HIBOB portion of the E-10 baseline price will be the HRS Chapter 486H baseline, plus the 4 cpg location adjustment factor established by the Legislature in HRS § 486H-13(d).

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[40] See ICF Report at 16.

[41] The commission continues to acknowledge the possible adverse effects, such as gasoline supply shortages, that could occur if businesses operating under the price caps are not able to earn normal returns operating in Hawaii. See Decision and Order No. 21952, at 35-38.

1. Calculate the average OPIS ethanol prices in New York, Chicago, and Los Angeles on a weekly basis

2. Add 4 cpg location differential or location adjustment factor

3. Deduct the 51 cpg Federal Ethanol tax credit for so long as it is applicable

4. The resulting delivered ethanol cost, inclusive of the blender's tax credit, should be added into the gas cap at 10% of the calculated E10 price (the other 90% is the HIBOB price).[45]

With respect to the first step of ICF's alternative recommendation above, ICF explains that "[t]his formula uses the OPIS prices in the three primary Mainland markets in which ethanol is competitively traded in reasonable volumes."[46] Under HRS § 486H-13(b), the baseline is an average of the weekly average of the daily spot prices for regular unleaded gasoline in Los Angeles, New York Harbor, and the U.S. Gulf Coast. Because there is currently no ethanol spot price for the U.S. Gulf Coast, the Chicago spot price for ethanol is a reasonable proxy for the U.S. Gulf Coast.[47] ICF further explains that "the markets (in

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[45]See ICF Supplement 1 at 2.

[46]See ICF Supplement 1 at 2.

[47]In its comments to ICF Supplement 1, Shell stated that "Chicago has a completely different supply route from Hawaii. Product cannot be directly exported to Hawaii from Chicago. Product must first be railed to Los Angeles or New York before it can be shipped to Hawaii." See Shell's comments to Supplement 1 at 1. However, the location adjustment factor is the average cost to ship product to Oahu. See HRS § 486H-16(a)(2) (stating that the location adjustment factor is "the average of the actual acquisition cost to non-refiner marketers to obtain gasoline from refiners or importers for sale on Oahu . . . ."). Because HRS § 486H-13(d) applies the 4 cpg location adjustment to the HRS § 486H-13(c) baseline of Los Angeles, New York, and the U.S. Gulf Coast, the Legislature's location adjustment factor addresses Shell's concern. Furthermore, the commission notes that Shell's

particular New York and Los Angeles) are increasingly influenced by imported cargoes from Brazil and other markets, and therefore are a reasonable assessment of the Mainland market."[48] Thus, the commission determines that it will use the OPIS spot prices for ethanol in New York Harbor, Chicago, and Los Angeles in calculating the ethanol portion of the E-10 baseline price.

The commission, however, will also adopt ICF's recommendation to gather information for all imports and cargo-based resales of ethanol. ICF recommends that "should the Commission adopt this alternative ethanol price determination, all ethanol import and resale transactions continue to be provided by the Parties to the Commission, and that the Commission track and monitor the average price of the ethanol cargoes delivered and resold."[49] In addition, the commission will also gather information related to the volume of ethanol that is blended.[50] This information will be valuable to the commission in monitoring the efficacy of the benchmarks and the appropriateness of further adjustments, if necessary.[51]

With respect to the second step of ICF's alternative recommendation above, ICF explains that "[t]he location

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suggestion to eliminate Chicago from the baseline price for ethanol, and thereby rely on two spot prices as opposed to three spot prices, would likely result in increased volatility.

[48]See ICF Supplement 1 at 2.

[49]See ICF Supplement 1 at 2.

[50]See ICF Report at 21.

[51]ICF's recommendation is for an adjustment every 3 or 6 months if a pattern of significant differences is identified between ethanol delivered costs and resales versus the OPIS benchmark. See ICF Supplement 1 at 3.

adjustment of 4 cpg is used to be consistent with the legislated adjustment of the existing gas caps."[52] The commission adopts ICF's recommendation and determines that it will use the HRS § 486H-13(d) location adjustment factor in calculating the ethanol portion of the E-10 baseline price.[53]

With respect to the third step of ICF's alternative recommendation above, ICF explains that "[t]he average cost of ethanol supply will be reduced by the 51 cpg Federal tax credit which applies to the blender of the E-10 gasoline. This net ethanol weekly price will be a 10% component of the gas cap price for E-10 gasoline."[54] ICF states that "the calculated delivered price includes a 51 cpg Federal tax credit component for all gasoline blended with ethanol. This credit will accrue to the party that actually blends the ethanol into gasoline for sale; therefore it needs to be recognized in the allowable gas cap price for any sale to a party that will purchase the HIBOB/ethanol blended gasoline."[55] The commission adopts ICF's recommendation to deduct the 51 cpg Federal tax credit from the

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[52]See ICF Supplement 1 at 2.

[53]The commission notes that more than one Party argued that a higher location adjustment factor is warranted. See, e.g., Tesoro's comments to Supplement 1 at 3; Shell's comments to Supplement 1 at 2. However, HRS § 486H-16(a)(2) provides that the location adjustment factor should "reflect the average of the actual acquisition cost to non-refiner marketers to obtain gasoline from refiners or importers for sale on the island of Oahu over the prior twelve-month period . . . ." At the present time, the commission does not yet have a twelve-month period of actual acquisition costs. Nonetheless, as indicated above, the commission will be gathering data and monitoring costs, and may make further adjustments, as necessary and appropriate.

[54]See ICF Report at 5.

[55]See ICF Report at 22.

operational costs in Zones 1 through 4, 7 and 8.[57] Further, ICF recommends, "Zones 5 and 6 will not be marketing E-10 gasoline, so there should be no E-10 gas cap related adjustments for those zones."[58]

First, with respect to the capital costs for investments in terminals and other supply and distribution facilities, the commission adopts ICF's recommendation that "an 11 year capital recovery period be applied to the ethanol mandate capital costs."[59] ICF states that "[i]nformation provided by the Parties indicates that Ethanol Mandate-related capital costs of about $35 million dollars are being expended by the Parties throughout the state, with about half the costs on Oahu."[60] ICF further states: "To recover the cost of the capital investments for the Ethanol Mandate, the additional $35 million dollars expended will require an increase in the gas cap formula to permit Parties the opportunity to pass through the added costs of compliance with the Ethanol Mandate."[61] ICF explains that "[f]or evaluation of terminal and pipeline projects for economic reasons (as opposed to mandated reasons), the Parties indicated a diverse range of capital recovery periods ranging from 1 to 15 years, and averaging about 11.3 years based on a weighted average

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[57] See ICF Report at 33-34.

[58] See ICF Report at 29.

[59] See ICF Report at 26.

[60] See ICF Report at 25.

[61] See ICF Report at 25.

of capital spent and amortization periods used."[62] Thus, the commission determines that ICF's recommendation of an 11-year capital costs recovery period for the Ethanol Mandate capital costs is reasonable and appropriate, and the commission adopts ICF's recommendation that "the capital recovery adjustment be applied for an 11 year period, and then be removed from the calculation."[63]

The commission also adopts ICF's recommendation to use a 6% interest rate, which ICF bases on the March 3, 2006 London Interbank Offered Rate (LIBOR) of 4.99% for 6 months, increased by 1% to reflect potentially higher costs for commercial borrowers.[64] The commission notes that one of the Parties recommended that a higher interest rate be utilized.[65] At this time, the commission has not found sufficient justification to deviate from the interest rate that ICF recommends. Accordingly, the commission adopts ICF's recommendation that the commission apply a 6% interest rate.

Second, with respect to inventory costs, the commission adopts ICF's recommendation to increase the zone price adjustments to reflect the increased costs related to the increased inventory necessitated by the Ethanol Mandate. ICF states: "One additional cost factor that is necessitated by the Ethanol Mandate is the need for Parties to increase overall inventory levels of gasoline [products] in Hawaii. The primary

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[62] See ICF Report at 25.

[63] See ICF Report at 33.

[64] See ICF Report at 26 and n.6.

[65] See HPMA's comments to the ICF Report at 1-2.

In sum, the commission adopts ICF's recommendations for E-10 zone price adjustments as follows: Zone 1: Oahu 7.6 cpg; Zone 2: Kauai 23.9 cpg; Zone 3: Maui, except the district of Hana 22.8 cpg; Zone 4: The district of Hana on the island of Maui 30.8 cpg; Zone 5: Molokai (none); Zone 6: Lanai (none); Zone 7: The districts of Puna, south Hilo, north Hilo, and Hamakua on the island of Hawaii 23.4 cpg; Zone 8: The districts of north Kohala, south Kohala, north Kona 26.1 cpg.

6.

The Chapter 486H mid-grade and premium adjustment factors

HRS §§ 486H-13(f) and (g) provide that the mid-grade and premium adjustment factors are 5 cpg and 9 cpg, respectively. In its Decision and Order No. 21952, the commission determined that it would use the HRS Chapter 486H mid-grade and premium adjustment factors. On March 22, 2006, HPMA filed a Motion for Adjustment of the Premium and Mid-Grade Price Adjustment Factors.[75] At this time, the commission has not determined whether a change should be made to the mid-grade and premium adjustment factors in HRS §§ 486H-13(f) and (g), and if so, what that change should be. Because any change to the mid-grade and premium adjustment factors does not stem directly from the Ethanol Mandate, the commission will address the mid-grade and premium adjustment factors in a separate Decision and Order. Accordingly, the commission will use the mid-grade and premium

[75]HPMA incorrectly filed its request in the form of a motion, rather than a petition. See, e.g., In re Senter Petroleum, Inc.'s Petition to Adjust the Zone Price Adjustment for Zone 2 (Kauai) Effective September 1-4, 2005 under Haw. Rev. Stat. § 486H-16, in Docket No. 05-0221, filed Aug. 30, 2005.

adjustment factors listed in HRS §§ 486H-13(f) and (g) in its calculations of the pre-tax wholesale price of E-10 gasoline.

B.

Publication and Effective Date of the Gasoline Price Caps

The commission will publish the first E-10 gas price caps, pursuant to HRS § 486H-13(b), on its website, www.hawaii.gov/budget/puc, on Wednesday, May 10, 2006, for all Zones, except Zones 5 and 6. These E-10 gas price caps shall be effective from May 15, 2006 through May 21, 2006. The commission thereafter will publish the E-10 gas caps every Wednesday, to be effective the following Monday through Sunday. For example, the second publication will be published on May 17, 2006, which will be effective for the period May 22, 2006 through May 28, 2006.

The baseline price shall be computed using the spot prices of the five (5) OPIS business days prior to each Wednesday. In the event that a State holiday falls on a Wednesday, the commission will publish the maximum pre-tax wholesale price on the previous business day, using the spot prices of the five (5) OPIS business days immediately prior to the day they are published.

The commission will continue to publish the gas price caps for conventional (non-ethanol) gasoline for all Zones, as applicable.

III.

Orders

THE COMMISSION ORDERS:

1. The following factors shall be used in calculating the HRS Chapter 486H maximum pre-tax wholesale price of E-10 gasoline: (a) 90% of the HRS Chapter 486H baseline price and location adjustment factor established by the Legislature; (b) 10% of the one-week average daily OPIS ethanol spot prices for New York Harbor, Chicago, and Los Angeles, calculated consistent with HRS § 486H-13(c), plus the 4 cpg location adjustment factor established by the Legislature in HRS § 486H-13(d) and minus the 51 cpg Federal ethanol tax credit for so long as it is applicable; (c) the HRS Chapter 486H marketing margin factor established by the Legislature; (d) the following E-10 zone price adjustments recommended by ICF (with an 11 year capital recovery period, the expiration of which will result in the removal of certain applicable portions of the zone price adjustments): Zone 1: Oahu 7.6 cpg; Zone 2: Kauai 23.9 cpg; Zone 3: Maui, except the district of Hana 22.8 cpg; Zone 4: The district of Hana on the island of Maui 30.8 cpg; Zone 5: Molokai (none); Zone 6: Lanai (none); Zone 7: The districts of Puna, south Hilo, north Hilo, and Hamakua on the island of Hawaii 23.4 cpg; Zone 8: The districts of north Kohala, south Kohala, north Kona 26.1 cpg; and (e) the HRS Chapter 486H mid-grade and premium adjustments established by the Legislature.

2. The commission will publish the first E-10 gas price caps, pursuant to HRS § 486H-13(b), on its website, www.hawaii.gov/budget/puc on May 10, 2006 for all Zones, except

CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Decision and Order No. 22451 upon the following parties, by causing a copy hereof to be mailed, postage prepaid, and properly addressed to each such party.

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DATED: MAY - 3 2006