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**George Andrew Sprague
311 South Morgan Street
Morganfield, KY 42437-1729
270-952-1850**

**Union County Biodiesel Company, LLC
5700 Prospect Drive
Newburgh, IN 47630
812-842-2960**

**Midwest Biodiesel Products, LLC
7350 State Route 111
South Roxana, IL 62087
618-254-2920**

**CONGRESS OF THE UNITED STATES
House of Representatives
Committee on Energy and Commerce
2125 Rayburn House Office Building
Washington, DC 20515-6115**

**The Honorable Cliff Stearns, Chairman
Subcommittee on Oversight and Investigation
Hearing: "RIN Fraud: EPA's Efforts to Ensure Market Integrity in the Renewable Fuels Program."**

Dear Mr. Stearns,

My name is George Andrew Sprague; I am the owner of Union County Biodiesel Company, LLC (UCBC) and Midwest Biodiesel Products, LLC (MBP), along with my partner Terry Zintel. I am a 5th generation farmer, Licensed Civil Engineer and Land Surveyor, and most importantly for the purposes of this hearing and my testimony, I am a Biodiesel Entrepreneur. I started UCBC in 2004 and MBP in 2006, as a direct result of my interest in alternative fuels which grew from my time as a Director on the Kentucky Soybean Association.

My background in engineering and construction led me to believe that I could develop the technology to produce biodiesel and to construct and operate a small biodiesel manufacturing facility on my family farm in Kentucky. My on-farm biodiesel manufacturing facility was operated as a technology testing and manufacturing prototype facility from 2004 through June 2009. In 2006, I partnered with Terry Zintel of St. Louis, MO to design and construct a 12 million gallon per year biodiesel manufacturing facility located in South Roxanna, IL called Midwest Biodiesel Products, LLC. In 2009, we designed and constructed an 18 million gallon per year biodiesel manufacturing facility in Newburgh, IN named UCBC.

Terry Zintel and I are small businessmen and entrepreneurs. Every dollar we have invested in our biodiesel businesses has come from our savings or from banks where we have borrowed the money. We have no corporate war chests to weather market or government policy calamities. When unforeseen cash demands occur in our businesses, we borrow the money or liquidate other personal assets to keep our businesses afloat. It should also be understood that borrowing money in the current banking climate, and in particular with the current state of the biodiesel industry, is very simply impossible. Our greatest long term fear is that Congress and the EPA will take a position of inaction or lack of positive

corrective action and this course will most certainly doom the vast majority of small and midsized biodiesel manufacturers in our Country to a path of elimination and bankruptcy.

Congress enacted the Energy Policy Act of 2005 and the subsequent Energy Independence and Security Act of 2007, and the rules promulgated by EPA most recently revised in July, 2010. One of the basic premises of the RFS program is to displace hydrocarbon based fossil fuels, with renewable fuels, and thereby lessen the U.S. dependence upon foreign oil. To achieve the goals set forth by Congress, the EPA created a RIN-based program. The Renewable Fuel Identification Number (RIN) represents a gallon of renewable fuel and is attached to each gallon upon production of the fuel. The RIN has become the currency of the RFS program with RINs being attached to liquid gallons of renewable fuel, separated off once owned by the Obligated Parties or blended with transportation fuel, fuel oil, or jet fuel, and subsequently used to document the U.S. displacement of our fossil fuels. The RINs provide incentives for blending of renewable fuels and allows the EPA to track production and use in the USA.

The RIN program has been successful in many ways. First, it has allowed Obligated Parties (Refiners, Importers, and Blenders of refined fuel) to access RINs when the renewable fuel was not readily accessible. For example, the Midwest States have multiple renewable fuel production facilities; however, the transport of the renewable fuel to the markets on the coasts can be expensive. Rather than being forced to absorb the costs of the transportation of ethanol and biodiesel from long distances, the Obligated Parties have the flexibility to simply purchase RINs from gallons that have been blend in the Midwest. This has saved Obligated Parties billions of dollars in infrastructure, capital expenses and transportation costs. Furthermore, the RFS2 program allows the Obligated Parties to have the flexibility of importing and exporting renewable fuels to help them balance their market and financial plans. Very simply, the RINs are the currency of the RFS2 program and as such, have created the necessary economic incentives to continue blending renewable fuels in a profitable manner.

To monitor the generation, transfer, and use of renewable fuels, the EPA created the Moderated Transaction System (EMTS). The EMTS system is capable of tracking all transactions and allows the EPA and the renewable fuels industry to adjust to the changing economics and market demands surrounding the renewable fuels industry and their respective RINs. Unfortunately, the EMTS system has no way to validate or monitor renewable fuel production and EPA is blind to potential fraud until the end-of-year required audits which are due by February 28th of the following year of production. At the inception of the EMTS program the majority of the renewable fuel industry believed that the EPA would be the entity providing oversight, guidance and validation of all RINs transactions in the EMTS system. The industry believed the EPA was in control of the validity of the RINs being generated within their controlled system. Every single participant in the system was certified by the EPA. Every participant provided documentation to the EPA, was reviewed by the EPA, allowed access to the system by the EPA, was monitored by the EPA, and most importantly, approved by the EPA. It was quickly pointed out after the fact by EPA that this is not the case and that a "buyer beware" policy would be followed even though every single transaction surrounding RINs takes place within the EPA's controlled and monitored system.

The EPA now expects the renewable fuels industry to resolve the issues of fraud through the use of generally accepted industry practices and independent third party validation programs with little or no guidance or input from the EPA. This enormous gap of oversight from the EPA and their lack of direct involvement in monitoring the RIN program have allowed the abuse of an otherwise productive RIN program. Without either the EPA's participation in RIN validation or a completely independent third party industry validation for RIN integrity, the renewable fuels industry will continue to be at the mercy of the EPA for their "after the fact - buyer beware" method of enforcement and monitoring. The

renewable fuels industry will greatly suffer under this type of policy as it create an environment where blending renewable fuels no longer makes financial sense.

After much debate and lengthy rule writing, the RFS program, was launched in the 3rd Quarter of 2007. Most participants in the program only vaguely understood the rules and there was little help offered by the EPA in understanding the rules or knowing where the obstacles in the program would be encountered. For the first couple of years of the biodiesel RFS program, biodiesel RIN pricing was in the range of \$0.10 to \$0.50 and this range did not significantly influence the overall marketing of biodiesel due to the combined existence of the \$1.00 per gallon Excise Tax Credit. The way the economics worked was the difference between the cost of production and the market price of the biodiesel, after the \$1.00 per gallon Excise Tax Credit, was what determined the value of the biodiesel RINs. RINs began to have a significant value in 2010, continuing into 2011 where they reached a maximum value of \$2 per RIN. With the value of RINs soaring in 2011, biodiesel was being produced and sold at record levels, and the young startup industry was well on its way to establishing itself in the overall fuel industry. The RIN markets appeared to be working well and it appeared Congress and the EPA had established an efficient and functional monitoring system for the renewable fuels industry. Most participants complained about the added document filings and cost of reporting, but were enjoying the financial benefits of a fluid and functional market. As a whole, the industry appeared to be following the course set forth by Congress and implemented by EPA.

Both UCBC's Newburgh facility and our facility in South Roxana, IL experienced their best year of production in 2011 along with their most profitable year in 2011. The EPA rules and their controlled system require all biodiesel manufactures to transfer all RINs to our downstream fuel customers. Our customers were selling UCBC and MBP RINs without difficulty throughout all of 2011. When these same customers returned to the RINs marketplace on January 2, 2012, every single customer of UCBC and most of the customers of MBP were told that small producer RINs were undesirable and furthermore, some of our customers were told they could not sell RINs because the RINs came from small or mid-sized biodiesel producers. We were informed by RIN Brokers and Buyers that the Obligated Parties only would purchase RINs from large biodiesel producers. We were even provided a list from one Broker that named 15 of the largest producers in the country and only RIN from these 15 plants were acceptable. We were told that the EPA's "Buyer Beware" methodology was being enforced on the Obligated Parties in response to the pending Notice of Violations which were to be issued in the near future by the EPA. We were also informed by RIN Brokers and Buyers that the Obligated Parties would be performing some kind of due diligence with all biodiesel producers that they wanted to purchase RINs from and that no transactions would occur until the Obligated Parties were confident that no potential invalid RINs could be created by the producers.

On January 2, 2012, we were effectively put out of business by the lack of confidence in the EPA's RIN program. Without the ability of our customers to sell our RINs, we could not sell our biodiesel. UCBC sold only a couple of truckloads of biodiesel in January and February of 2012, and Midwest Biodiesel did not sell much more. We have been facing financial ruin and the closure of our businesses because everyone in the biodiesel industry feared what action the EPA was going take on the innocent participants of the EPA's own RIN system. By March 2012, we had initiated direct contact with several Obligated Parties and re-established some sales of UCBC and MBP RINs. Unfortunately, the sale of biodiesel was extremely slow due to the overall uncertainty in the RIN market and the continued fear of what action the EPA was going to take. As an example, we have one customer who bought a total of 60 million gallons of biodiesel last year from multiple biodiesel manufacturers that decided to not buy a single gallon of biodiesel in 2012 until the RIN crisis is solved and the EPA determines how it is going to penalize the innocent participants in its own RIN system. Today, we are continuing to work with our

customers to assure them we are producing valid RINs and we are exploring every possible avenue to find ways to sell our biodiesel and help our customers move our RINs until the EPA finalizes their approach to the current RIN situation.

In January of 2012, I contacted my Congressman, Ed Whitfield to assist me in contacting EPA about this RIN situation. I am pleased to say that all of the conversations I have had with the EPA staff were very informative and helpful, the EPA personnel I have interacted with have been concerned about my personal situation and the root problem with their regulations. The EPA has sought my opinion about the problems and my opinion about potential solutions to make a better RIN program for all of the participants.

Listed below are my thoughts and ideas on how to correct the RIN program and handle the RIN fraud situation. Below are the primary issues as I see them and solutions to those issues:

1. All biodiesel RIN program participants assumed the EMTS system was safe and was being controlled, managed and monitored by the EPA. No one, including the Obligated Parties or even the EPA saw the fraud coming. When RINs became as valuable as they were in 2010-2011, criminals began to devise plans to defraud the system, the EPA, and our Federal Government. This type of fraud did not happen in the ethanol industry because ethanol RINs are only worth a few cents per gallon – apparently not enough money to attract the criminals.

SOLUTION: The EPA could adopt a presumptive liability policy. Like the EPA Ultra Low Sulfur Diesel Rules, the EPA should adopt rules that allow innocent, non-complicit parties protection from EPA enforcement actions. In other words, if a party is purchasing biodiesel RINs through the EPA's own system and they are not directly involved with the creation of an invalid RIN; the innocent parties should be protected from EPA enforcement penalties. Furthermore, if RIN generators, owners, and obligated parties invest in a RIN quality assurance program, this likewise should afford the parties protection from EPA enforcement penalties.

2. Currently, RINs can be separated from wet gallons prior to being blended at the consumer level. As a matter of fact, we know of many biodiesel manufacturers that are currently separating RINs at the instant a biodiesel sale takes place – long before the separation should happen. To my knowledge, all of the biodiesel RIN fraud happened with RINs separated from the wet gallon of fuel. Obligated Parties prefer the flexibility of early separation but this is exactly what has caused all of the biodiesel RIN fraud.

SOLUTION: RINs must remain connected to the wet gallon biodiesel from creation at the biodiesel manufacturer to final blending at the consumer's level. This process would most certainly eliminate the current biodiesel RIN fraud since most of the current RIN fraud is perpetuated by an isolated single party with a prematurely separated RIN. If RINs were required to remain with the wet gallon of biodiesel until final consumer blending, passing fraud forward to downstream participants would be extremely difficult and much less likely to be executed without immediate detection. This method would also stop the improper RIN separation for non-transportation fuel uses and the practice of exportation after RINs separated without properly retiring the RINs. If the Obligated Parties demand the freedom to separate RINs from wet gallons before they are blended at the consumer level, then the RIN program should require the biodiesel producers to sell RINs directly to the Obligated

Parties based upon the EPA biodiesel mandate and the actual gallons of biodiesel manufactured.

3. No “Due Diligence” was being performed by the Obligated Parties. EPA made it very clear, after the RIN fraud problem was discovered, that the Obligated Parties were responsible for verifying and certifying the quality of the RINs with the EPA’s own RIN program. Everyone in the biodiesel industry assumed that the EPA was responsible for this function and furthermore that the Year End Attestment process would keep the system clean.

SOLUTION: Biodiesel Producers and Biodiesel Marketers must create an independent RIN Integrity or RIN Verification Program which the EPA and the Obligated Parties accept as proof that RIN compliance is being adhered to by every biodiesel manufacturer which participates in the Program. This method does not need to be overly burdensome, but thorough enough to provide transparency in the Obligated Parties and the EPA. Because this effort will be paid by the biodiesel producers, it should have requirements that do not create unreasonable cost for the biodiesel producer.

4. There is no method to fix a problem with RINs once a situation or inadvertent problem occurs. Currently, the EPA issues a Notice of Violation once a problem occurs and does not provide a method or opportunity to correct the situation or problem. This type of methodology creates severe heartburn for the Obligated Parties.

SOLUTION: The EPA should take the position that any unintended violation is fixable and provide a sufficient window of time to correct the situation. If corrective action is not taken, then a violation has occurred and the EPA should proceed with its normal enforcement procedures.

There are other problems with the EPA’s RIN program that have no RIN fraud impact but are adversely affecting the small and mid-sized biodiesel manufacturer. Listed below are several suggested enhancements to the current RIN program that will significantly help small and mid-sized biodiesel manufacturers remain profitable and ensure the continued growth of this young industry.

5. Obligated Parties are required to meet their mandated RIN obligations on an annual basis. Obligated Parties even have the latitude to be non-compliant in one year if they correct the shortage and are compliant within the following year. This allows the Obligated Parties to be passive in the marketplace for extremely long periods of time. We have been informed that several of the largest Obligated Parties have bought very limited numbers of RINs in the first 6 months of 2012. The lack of regular purchasing of RINs invalidates the laws of supply and demand and quite simply, the Obligated Parties can manipulate the market in their favor and create non-market driven biodiesel pricing and RIN pricing scenarios.

SOLUTION: The Obligated Parties should be required to meet their anticipated annual mandate of RINs on a monthly or quarterly reporting basis. This very simple change to the EPA’s program rules would ensure a more stabilized biodiesel manufacturing environment and it would bring fewer extreme high and extreme low demands for biodiesel RINs. In turn, small and mid-sized biodiesel manufacturers would be operating in a more normalized demand market and it would pave the path for further expansion of the small and mid-sized biodiesel manufacturers in our Country.

6. The EPA's EMTS system was created to track RINs from their creation to final separation, as well as to preserve the integrity and identity of the RIN throughout the lifecycle of the process. If the Obligated Parties are allowed to isolate compliant biodiesel manufacturers thereby choosing and selecting which biodiesel manufacturer's RINs they obtain, the Obligated Parties will in fact have the power to put small and mid-sized biodiesel manufacturers out of business. The Obligated Parties will be free to collude with the handful of large biodiesel manufacturers to force out of business the small and mid-sized biodiesel manufacturers.

SOLUTION: RINs verified by an independent verification program and properly entered into the EPA's EMTS system must always be considered valid for use by the Obligated Parties and priced at the same level as all other RINs. If the RINs were to be determined invalid at a later time by audit or EPA inspection, the Obligated Parties should not be subject to fines, penalties, or the requirement to purchase replacement RINs. Providing the Obligated Parties assurances that RINs obtained through the EPA's own EMTS system will ensure an environment where small and mid-sized biodiesel manufacturers can survive and grow.

7. Obligated Parties prefer to buy RINs in large batch sizes due to the cost of completing a financial transaction with RIN Brokers and RIN providers. Small producers and blenders receive a lower price for their RINs than do large producers due to this market force. The lower prices offered to the small and mid-sized biodiesel manufacturer creates another economic disadvantage for the small and mid-sized biodiesel manufacturer who already struggles with the issues competition against the larger biodiesel manufacturer.

SOLUTION: The EPA must endorse privately operated RIN exchanges to allow all RINs to be sold, without the discrimination of whether or not the RIN was generated at a large biodiesel manufacturer or a small biodiesel manufacturer. This very simple process will level the field for all biodiesel manufacturers and ensure the fluid movement of RINs.

I believe that all of the suggested corrections listed above are capable of immediate implementation by the EPA. This Committee, Congress and the EPA must immediately act to preserve the biodiesel industry and to preserve the small to mid-sized biodiesel manufacturer. The Obligated Parties and large biodiesel manufacturers can play the waiting game to see what policy transpires, small biodiesel manufacturers cannot wait. Please take action now; please direct the EPA to implement these simple yet effective changes to save jobs, save investments, and to save our biodiesel industry.

Respectively,

George A. Sprague

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Summary Outline

George A. Sprague:

1. Farmer, Engineer & Biodiesel Entrepreneur.
2. Formed Biodiesel Companies; UCBC in 2004 and MBP in 2006.
3. Biodiesel Companies are small producers with limited cash resources.
4. Inconsistent Government policies create severe cash shortages for my businesses.

RFS Program and RINs:

1. Congress created RFS program to lower dependence on foreign oil, strengthen US Alternative Fuel Industry, and to reduce pollution to our environment.
2. EPA created EMTS program for tracking and monitoring RIN activity.
3. EPA did not include the necessary program safeguards.
4. EMTS program worked well in past years but currently provides no assurances of RIN integrity to the renewable fuels industry.

RIN Fraud:

1. Neither the EPA nor the Obligated Parties anticipated current fraud situation.
2. EPA allowed RIN separation too early in the process which was a major contributing factor to the current fraud situation.
3. EPA's "Buyer Beware" policy and lack of "Due Diligence" by Obligated Parties created an opportunity for RIN fraud.
4. EPA rules result in violations and fines in lieu of positive corrective actions.

Solutions

1. Obligated Parties should be granted "Presumptive Liability".
2. Independent RIN Verification by Producers must be endorsed by the EPA.
3. No RIN separation should take place until the biodiesel is sold as transportation fuel.
4. All RINs must be considered valid once verified and entered into the EMTS system by the biodiesel producer.