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Congress Should Streamline Regulatory Impediments to Refinery Expansions

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High oil prices, currently triple the average of the 1990s, are the main cause of today's high gasoline prices. But they are not the only cause. The cost of refining oil into gasoline has also risen, due in part to unnecessarily costly and onerous federal refinery regulations. One pending bill, The Refinery Permit Process Schedule Act (H.R. 5254), takes steps to streamline the regulatory process. Reining in refinery regulations should lead to increased refining capacity and thus lower prices.

Inadequate Domestic Refining Capacity

No new refinery has been built in the U.S. since the 1970s, and even expansions of existing refineries have not kept pace with growing demand for gasoline in recent years. Consequently, the price consumers pay at the pump reflects not only high oil prices due to tight supplies, but also high refining costs due to tight refining capacity.

Domestic gasoline output and gasoline imports together are barely adequate even under the best of circumstances, and the lack of spare refining capacity leaves little margin for error. This is especially true during the high-demand summer months. In fact, there is so little cushion that even minor incidents that knock a single refinery offline can boost prices nationwide. More major events—such as Hurricane like Katrina, which impacted 14 percent of refining capacity—can send prices skyrocketing.

Part of the reason that capacity is so tight is costly and time-consuming regulations affecting refinery operations. Most stem from the Clean Air Act and became much more stringent after that statute's 1990 rewrite. According to the Federal Trade Commission, "[E]nvironmental laws and regulations have required substantial and expensive refinery upgrades, particularly over the past 15 years."[1]

The need for these additional environmental measures is questionable, given that air pollution from refineries and other sources was already in sharp decline before they were enacted.[2] Nonetheless, the existing statutory requirements and Environmental Protection Agency (EPA) rules remain in place, and the EPA continues to promulgate new rules.

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By some estimates, as much as 25 percent of capital outlays in the refining sector goes to environmental regulatory compliance. This investment, several billion dollars annually, is money that is spent maintaining existing capacity, rather than expanding it. And not only do these costly regulations siphon resources away from refinery expansions, but they also make those expansions more expensive and protracted.

According to the projections through 2030 from the Department of Energy's Energy Information Administration (EIA), "[D]emand for refined products continues to increase more rapidly than refining capacity…."[3] Though increased imports of gasoline, currently near 10 percent and rising, can partially fill the gap created by inadequate domestic capacity, this trend does not bode well for future gasoline prices.

A Modest Pro-Capacity Step

H.R. 5254 is a modest attempt to rein in this regulatory excess. It seeks only to expedite the permitting process and judicial review for refinery expansions. It does not make substantive changes to the underlying regulations.

To be sure, substantive regulatory changes would be well justified. For example, the costly and environmentally unnecessary New Source Review program creates massive costs and delays for refinery expansions, accomplishes little for air quality, and in some instances is counterproductive, leading to higher levels of pollution. Unreasonable deadlines in EPA's new ozone standards will create operational problems for many refineries and should be modified. Overall, there is ample room to prune or discard many refinery regulations that are outdated, redundant, unnecessarily complex, or overly time consuming. Many could be cut back, and these changes would not jeopardize air quality.

Nonetheless, speeding the permit process is a good first step in an area where little has been accomplished. Measures that sought to remove regulatory impediments to refinery expansion were considered in last year's energy bill, but many in Congress opposed them, claiming that they were either giveaways to big oil or environmental rollbacks. Though these allegations are questionable, they were persuasive enough so that the final version of the Energy Policy Act of 2005 did little to streamline refinery regulations.

H.R. 5254 also has provisions that would make closed military bases available as potential sites for new refineries. This is an interesting idea, but it is unclear whether any such facilities are suitable for a new refinery. Many experts think provisions facilitating expansions of existing refineries are more promising than efforts to build new ones.

In sum, H.R. 5254 addresses one of the contributors to today's high gasoline prices – excessive regulations that block hamper needed additions to refinery capacity – and as such could be part of the solution to the pain at the pump.

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[1] Federal Trade Commission, "Gasoline Price Changes: The Dynamic of Supply Demand, and Competition," June 2005.

[2] See, Environmental Protection Agency, "Air Emissions Trends – Continued Progress Through 2004," 2005.

[3] Energy Information Administration, "Annual Energy Outlook: With Projections to 2030," February 2006, p. 96.