Economic Impact Analysis
Virginia Department of Planning and Budget

9 VAC 25-640– Aboveground Storage Tank and Pipeline Facility Financial Responsibility Requirements
Department of Environmental Quality
March 17, 2000

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 9-6.14:7.1.G of the Administrative Process Act and Executive Order Number 25 (98). Section 9-6.14:7.1.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

State Water Control Law (Section 62.1-44.34:16 D) requires that operators of aboveground storage tank and pipeline facilities demonstrate financial responsibility as a condition of operation and authorizes the State Water Control Board to promulgate regulations requiring operators of aboveground storage tank (AST) and pipeline facilities to demonstrate financial responsibility. In accordance with the State Water Control Law, the proposed regulation is designed to provide the criteria by which operators can demonstrate that they have adequate financial resources to perform their responsibility to contain and cleanup any oil discharges which may occur at their facilities.

Estimated Economic Impact

Currently, AST facility and pipeline operators are not required to demonstrate their financial wherewithal in order to operate in the Commonwealth. This proposed regulation would require AST operators with statewide storage capacity of greater than 20 million gallons to demonstrate financial responsibility in the amount of $1 million. AST operators with statewide storage capacity between 25,000 and 20 million gallons would need to demonstrate financial responsibility in the amount of five cents per gallon of storage capacity. AST operators with statewide storage capacity of less than 25,000 gallons are exempt from this regulation. Pipeline operators are required to demonstrate $5 million dollars of financial responsibility, regardless of the pipeline's capacity.

Financial responsibility can be demonstrated by: (1) financial test of self-insurance; (2) guarantee; (3) insurance; (4) surety bond; (5) letter of credit; or (6) trust fund. Based on experience with the existing (since 1990) underground storage tank financial assurance requirements and with solid and hazardous waste facility financial assurance requirements, the Department of Environmental Quality anticipates that most operators will use the financial test of self-insurance or a guarantee to meet the financial responsibility requirements. Over 99.5% of underground storage tank operators have consistently used one of those two methods.[1] Under the self-insurance option, the operator provides a financial statement indicating a net worth at least equal to the amount required to demonstrate financial responsibility. The financial statement must either be audited by an independent auditor or have been reported to the Securities Exchange Commission, Energy Information Administration, Rural Electrification Administration or Dun and Bradstreet. The cost for the self-insurance method would be essentially a small amount of staff time in document preparation.

The guarantee method requires that a guarantor provide a letter from its financial officer demonstrating that it has adequate funding to meet the financial test requirements and that it establishes an unfunded standby trust in the event the guarantor must pay on the guarantee. The department provides all the necessary forms. Since the standby trust is unfunded, no trust management fees are incurred. The guarantor does incur costs in that it is accepting contingent

[1] Based on data provided by the Department of Environmental Quality

liability. Presumably the operator will compensate the guarantor for its acceptance of that contingent liability.

According to the department, insurance would cost the average operator $7,500 per year, while a surety bond for an AST operator with 20 million gallons of storage capacity (well above average) would be about $9,000 annually and for a pipeline would be $37,000 annually. It should not be ignored though, that the issuer of the insurance or surety bond assumes the risk of potential future cleanup costs. So, the net cost (including the benefit of elimination of cleanup cost risk) of the insurance or bond to the operator will be substantially less than the amount of the payments to the issuer.

The department presented this proposed regulation to representatives from the Virginia Petroleum Council, the Virginia Petroleum Jobbers Association, the Virginia Asphalt Association, the Virginia Aggregate Association, plus a number of small operators and environmental groups. All three pipeline operators in the Commonwealth were sent copies of the proposed regulation and asked for feedback. There were no objections to the language other than the frequency of paperwork submissions. The proposed regulation was altered to satisfy that objection. Proof of financial responsibility is required once a year. The lack of objection to the cost of the proposed regulation despite the widespread dissemination of its contents provides some evidence to support the department's expectation that most operators would be able to comply at low cost.

This proposed regulation may provide some benefit to the Commonwealth in that it would force some financially unstable operators to cease operations and likely sell their operations to more financially secure entities. Operators that cannot demonstrate financial responsibility would be required to close their facilities. In such cases it seems likely that the operator would sell their facility in order to get some return from their property. If an operator is unable to pay for the costs of oil leaks and declares bankruptcy, the state conducts the cleanup and public funds[2] are used to pay for it. Thus, by decreasing the number of operators that are incapable of paying their share of the costs of potential oil leaks, the proposed regulation decreases the likelihood that the state will be required to pay for the cleanup costs of a bankrupt

operator. This could reduce by a small margin the amount of state funds used to cleanup oil leaks.

It is also possible that the proposed regulation would discourage financially weak operators from purchasing facilities. A firm or an individual may have just enough funds to purchase a facility, but not enough to demonstrate financial responsibility to pay for their share of potential cleanup costs. Such an entity would likely be dissuaded from their purchase since they would not be permitted to operate and earn revenue. In this way the proposed regulation could limit the number of entrants into the industry that are not capable of paying for potential cleanup costs. Again, this could reduce by a small margin the amount of state funds used to cleanup oil leaks.

Reducing the number of operators that are incapable of paying their share of the costs of potential oil leaks would likely also reduce some delays in cleanup. According to the department, situations where operators are unable to pay their share of cleanup costs tend to delay the process of cleanup. Thus, the proposed regulation has the potential to decrease the frequency and length of cleanup delays, which would be beneficial for the environment as well as for third parties affected by the spill.

Additionally, it seems probable that financially troubled operators are less likely to incur the expense of proper maintenance and safety procedures than would more financially secure operators. Thus, reducing the number of operators that are incapable of paying their share of the costs of potential oil leaks may to small degree decrease the likelihood of leaks occurring.

In summary, the benefits of the proposed regulation include the potential for a small decrease in the occurrence of oil spills and the frequency and length of cleanup delays. State expenditures on the cleanup of oil spills and damage to the environment and third party property could potentially be reduced. Demonstrating financial responsibility would involve small net costs for most operators. Though it seems probable that the potential benefits of the proposed regulation outweigh the potential costs, there is insufficient data to determine that conclusively.

[2] The Virginia Petroleum Storage Tank Fund is funded by a fee of $0.006 on every gallon of gas, diesel, heating oil, and kerosene that is sold in Virginia (source: the Department of Environmental Quality).

Businesses and Entities Affected

The proposed changes to the regulation will affect the 727 AST facility operators with 25,000 gallons or more of storage capacity and the 3 pipeline operators in the Commonwealth.

Localities Particularly Affected

The proposed changes to the regulation affect localities throughout the Commonwealth.

Projected Impact on Employment

The proposed changes to this regulation are not expected to significantly affect net employment. A small number of financially weak operators may cease operations. But those facilities would most likely be purchased by more financially secure operators, who would likely employ approximately the same number of workers.

Effects on the Use and Value of Private Property

The value of facilities owned by operators that are unable to demonstrate financial responsibility will decrease from their perspective.