

November 18, 2008

**Memorandum For: Mr. Phill Swagel, Assistant Secretary of the Treasury for Economic Policy
Mr. Jeb Mason, Deputy Assistant Secretary Secretary of the Treasury for Business Affairs and Public Liaison
Mr. King Mueller, Deputy Assistant Secretary Secretary of the Treasury for Legislative Affairs**

**From: Independent Connecticut Petroleum Assn.
Fuel Merchants Association of New Jersey
Oil Heat Institute of Long Island
Oil Heat Institute of New Hampshire
Oil Heat Institute of Rhode Island
Maine Oil Dealers Association
Massachusetts Oilheat Council
New England Fuel Institute
Vermont Fuel Dealers Assn.**

Subject: Credit Markets and the Needs of Home Heating Oil Retailers and Consumers

Background

The heating oil retailers we represent purchase their product from wholesale suppliers who require payment from retailers in 30 days, 10 days, upon loading, or in some cases, in advance of loading. Retailers then deliver the fuel to consumers who routinely take 30 or more days to pay for their retail deliveries. The cash-flow gap between when a retailer pays a wholesaler and when a consumer pays the retailer has traditionally been borne by wholesalers issuing lines of credit. Over the past few years wholesalers have gradually begun constricting their credit lines, making private financing more necessary to fill the gap.

An additional complexity this year was witnessed in the spring and early summer with widely reported price projections of \$200 per barrel crude oil, and \$5, or even \$6 per gallon retail heating oil,. This resulted in dramatic increases in consumer demand to be “locked-in” with contracts between consumers and retailers at fixed prices. This demand resulted in retailers turning to wholesalers for similar instruments to “lock-in” supply and price to meet consumer demand. In the spring and early summer the cost of futures contracts by retailers of fuel, with wholesale suppliers were generally over \$4 a gallon, most between \$4 and \$4.25 per gallon for 42,000 gallon contracts sold for delivery in November, December, January, February and March.

Beginning in mid-July with a peak of \$147 per barrel crude, the commodities market began a collapse to the \$60 per barrel crude oil range in October, and then \$2 +/- for wholesaler heating

oil. This collapse had the two-fold impact of significant margin calls on contracts, as well as consumer revolt against program purchases made earlier in the year.

Issue 1.

The pressures on the nation's credit markets seen prior to August were difficult, and now are significantly more so given the recent "seizing up" of credit markets both nationally and internationally. The intent of the Emergency Economic Stabilization Act is to address those concerns. While the underlying purpose of the EESA was to stimulate lending by the nation's credit markets, we generally find that these markets have yet to respond to the needs of heating fuel retailers. Access to credit is the very lifeblood of this industry, as without access to credit the system described above fails.

Several surveys of heating fuel dealers were conducted this summer to determine difficulty in accessing credit. All show a problem made worse by the current credit crisis.

- A New England Fuel Institute survey of nearly 200 dealers found about a 1/4 of dealers estimated a shortfall over \$300,000 in their winter credit requirements.
- A survey conducted in Connecticut found that 53% of the retailers face \$120,100,000 in identifiable credit need that may go unmet in just Connecticut. Finally, retailers' report 88% will need credit beyond that extended by their wholesalers and only 12% believed they have adequate credit.
- In Vermont a similar survey shows that 40% of the state's 125 heating oil retailers have had difficulty extending their existing line of credit.
- In Massachusetts there are 750 heating oil retailers who supply 2 billion gallons of heating oil to commercial and residential users including 1 million homes.
- In Rhode Island there are 120 heating oil retailers who supply 211 million gallons to 171,000 households. Most of the state's retailers face difficulty with access to adequate credit.

Issue 2.

Many heating oil consumers across the Northeast "lock-in" their winter fuel when it is warm. Approximately a third of heating oil consumers purchase their heating oil in the summer through fixed price contracts with their retailers. In Connecticut, approximately 112,000 consumers locked-in an estimated 95,200,000 gallons in heating oil purchases this summer, 75% of which averaged \$4.50 a gallon. Consumers in other states are in a similar predicament. Heating oil retailers in Connecticut had to make financial commitments to wholesale suppliers for an estimated \$385,560,000 of heating oil contracts to meet this demand. With the collapse of commodity prices seen since mid-July, retailers now find forward months at prices half of what they had available pre-mid-July and consumers see retail prices similarly half of what was available at that same time. Wholesalers will only allow retailers out of their supply

arrangements if the retailer literally buys his or her way out of the contract[s], and then the retailer could make new arrangements at currently available prices. Wholesalers can only accommodate a retailer buy-out for no longer than a year to pay for the contract[s]. On a mark to market basis, a large, northeast regional wholesale supplier of heating oil believes that as many as one-half of its retailer customers are technically bankrupt. Another large, northeastern regional wholesaler believes the period of January and February to be of critical timing as their view is many retailers will have exhausted their credit lines. This condition arises from having entered into wholesale supply arrangements in early summer for winter delivery that are now too expensive given the 55% decline in commodity prices since mid-summer.

Retailers were heavily leveraged with asset-based commitments and personal guarantees (i.e., mortgaging their homes in some cases) to enter into their original supply agreements. Financing retailer's way out of these positions to provide relief for themselves and consumers alike is not an option given the enormous debt that would require of retailers. Finding a solution to assist consumers will take exceptional creativity.

Partial Solution Unrealized

Thanks to changes in the rule making process this summer by the U.S. Small Business Administration, a majority of the dealers in the Northeast fall under the SBA definition of a small business. Our hope this past summer was that the SBA rule change from \$11.5 million in gross receipts over three years to **companies of 50 or fewer employees** would make private lending easier and that the credit problem seen to that point would be significantly lessened. Unfortunately, private lenders still have to cover the 25% of each loan that would not be covered by an SBA guarantee. The SBA 7 [a] loan program only allows a maximum guarantee of 75% of loans over \$150,000 up to a maximum of \$2 million. For SBA guarantees to play a role, banks need to step up and provide lending, which many are unable or unwilling to do at this time. Temporarily lifting the underwriting requirement for private lenders and raising the employee limit to 100 would help more heating fuel dealer's access SBA loans

Request

We are now entering the cold weather demand season, **making access to capital markets critical for our businesses**. With the intended purpose of the EESA to spur lending, and the Department of the Treasury's clear emphasis on that outcome, we restate not only our capital borrowing needs, but of equal, associated concern, are widely reported stories involving the use of TARP assets by the banking community to engage in acquisitions, rather than increasing their lending. The Treasury recently transferred \$400 million to Webster Bank. Webster then announced the new capital would assist the bank in acquiring other banks to become the largest bank in New England. One would have hoped Webster's emphasis would have been more appropriately on expanding its lending and becoming more creative in meeting the needs of borrowers in the economy. Banks are, in fact, further constricting their lending, not expanding their lending. While already a source of difficulty for heating fuel retailers, the problem of access to adequate credit will be exacerbated should the Northeast be subject to a prolonged cold snap, a spike in the wholesale price, or both.

We seek the Department of the Treasury's considerable influence under the Emergency Economic Stabilization Act to strongly encourage lenders to the heating oil industry to be more willing to lend and work with agencies such as the Small Business Administration toward that end. Losing access to adequate credit will mean interruptions in fuel deliveries for potentially millions of consumers.

One other potential option concerning the issue of fixed price contracts would be an interface between the Department of the Treasury and the Department of Energy under DOE's Northeast Strategic Heating Oil Reserve. The DOE operates a 2 million barrel strategic heating oil reserve wherein DOE purchases fuel for storage in the event of supply disruptions. As the DOE has existing authorization for acquisition, and has "swapped" contracts of fuel from time to time, it is at least theoretically possible for DOE to swap higher-cost wholesale contracts sold in the summer for the reserve, relieving at least some pressure and allowing wholesalers to replace those contracts sold to retailers with lower cost contracts of benefit to retailers and then consumers.

It is our hope that the federal government recognizes the impact that the loss of liquidity could have on our industry and on the millions of Americans that depend on us to stay warm this winter.

We look forward to exploring these issues more fully when we meet.