



March 4, 2004

Ms. Althea Henry, Contract Administrator
State of Delaware
Division of Support Services
Department of Administrative Services
820 Silver Lake Boulevard
Dover, Delaware 19904

**Re: Contract #03-009-AH
Motor Oil, Re-refined Motor Oil, Lubricant and Anti-Freeze**

Dear Ms. Henry:

The Independent Lubricant Manufacturers Association (“ILMA”) requests that the State of Delaware revise its “specifications” for the above-referenced contract, as well as for any extensions of this contract or for other State contracts for “motor oil, re-refined motor oil, lubricant and anti-freeze,” by deleting the prohibition on “non-nationally recognized compound blenders.” This prohibition is discriminatory, is not related to product quality, is not reflective of today’s lubricant market, and is costly to Delaware taxpayers.

Introduction of ILMA

ILMA, established in 1948, is a national trade association of 142 manufacturing member companies, consisting largely of small businesses, ranging in size from fewer than 10 to more than 200 employees. As a group, ILMA member companies blend, compound and sell over 25 percent of the United States’ lubricant needs and over 75 percent of the metal removal fluids utilized in the country. According to industry surveys, ILMA members produce approximately 30 percent of the engine oils sold in the United States.

In order to manufacture a lubricant, ILMA member companies purchase oil, re-refined oil and synthetic lubricant base stocks and a wide range of additives. ILMA member companies then compound and blend the base stocks with the correct additives in the proper proportions to produce a lubricant with the desired characteristics for a particular job.

ILMA members are diverse. A large proportion of our membership manufactures automotive lubricants for original equipment manufacturers and for the retail market, either under their own labels or through contract packaging arrangements. As discussed more fully below, most refiners contract with ILMA members to produce, package and distribute some percentage of their branded lubricant products. Many ILMA members produce lubricants for metalworking and heavy industrial machines, while others supply lubricants for mining, textiles, food processing, electronics, as well as many other industries.

Independent lubricant manufacturers by definition are neither owned nor controlled by companies that explore for or refine crude oil to produce lubricant base stocks. Base oils are purchased from refiners, who are also competitors in the sale of finished products. Independent lubricant manufacturers succeed by manufacturing and marketing high-quality, often specialized, lubricants. Their success in this competitive market also is directly attributable to their tradition of providing excellent, individualized service to their customers.

ILMA members historically have marketed motor oils, transmission fluids and other lubricants that meet and/or exceed the automakers' or original equipment manufacturers' performance and warranty requirements. ILMA members have provided quality products through competitive bids to State, local and other governmental agencies throughout the Association's 55-year history.

The Specification is Discriminatory

The prohibition against "non-nationally recognized compound blenders" discriminates against ILMA members doing business in Delaware. As an initial matter, the State does not define in its contract what it means to be "nationally recognized." Many ILMA members who likely would bid on the contract are nationally-recognized "players" within the lubricants industry, although they may have a strong regional presence, but their lubricant products may not be "household names."

However, ILMA assumes that the State's intent is that the *brand* of lubricant products supplied under the contract be nationally recognized. Yet, some of the manufacturers (*i.e.*, refiners) listed under the "acceptable manufacturers guide" either never had (*e.g.*, California Oil Company and Pure Oil Company) or no longer have (*e.g.*, Arco) nationally-recognized brands.¹ In such instances, ILMA fails to see how the State can make a distinction unless it is attempting to discriminate against independent lubricant manufacturers.

¹ Moreover, the State's chart of "acceptable manufacturers" is woefully out of date. For example, Exxon and Mobil merged well before the 2003 contract, as well as the American Oil Company (Amoco), Arco and BP Oil Company. Further, Texaco and Chevron have merged, while Cities Service Oil Company has been Citgo Petroleum for a number of years. Phillips Petroleum recently merged with Conoco Oil Corporation.

As noted above in the introduction of ILMA, independent compound blenders as a group have a sizeable market share in producing engine oils (*i.e.*, approximately 30 percent).² Further, many ILMA members manufacture, package and distribute lubricant products for the refiners that the State deems “acceptable” under the contract. Refiners have closed blending and other owned, lubricant manufacturing facilities in recent years, instead relying on ILMA members the State deems to be non-nationally recognized to manufacture, package and distribute their branded lubricant products in defined geographical areas. ILMA fails to see how on one hand its members can make the refiner’s lubricants meeting the contract’s specifications, while on the other hand they cannot bid on the same contract with their own competing products with the same components.

The contract specifications allow for “re-packing agreements,” although such agreements are not defined. The industry usage for this term largely involves petroleum jobbers (*i.e.*, primarily gasoline and heating oil distributors) who purchase bulk lubricants and anti-freeze and then re-package the products in 55-gallon drums and smaller containers. Many of the refiner-branded, bulk lubricants are delivered to these petroleum jobbers by ILMA members.

Moreover, ILMA is not aware that the American Petroleum Institute (“API”) approves “repackaging contractors.” API, however, licenses lubricant manufacturers, including ILMA members, to use its “donut” and “starburst” symbols under its Engine Oil Classification and Licensing System on engine oil labels. Accordingly, even if a non-nationally recognized compound blender had a “repackaging agreement” with an “acceptable manufacturer,” it could not bid on the contract because there is no API approval process or program.

The Specification is not Related to Product Quality

The State incorrectly assumes that refiner-branded products are the only lubricants that can satisfy the State’s contract needs from a quality perspective. ILMA members and refiners manufacture their lubricant products, particularly engine oils, to standards set by third-party organizations, including API. For example, in the engine oil area, there are “read across” guidelines which match different base stocks with chemical additive packages to produce the lubricant with the required performance characteristics. The key for the State in its contract is that the lubricant products sold and delivered meet these stated industry-wide performance standards.³

² Further, as also noted in the introduction of ILMA, independents are the predominant market leaders in other lubricant areas, specifically metalworking fluids.

³ The contract specification states that “(n)ormal industry-wide manufacturing tolerances will be acceptable.” This provision should be rewritten to allow for lubricant products that meet industry-recognized and developed performance standards.

Ms. Althea Henry
March 4, 2004
Page 4 of 5

Without an industry-wide performance standard, the State has no guarantee that the refiner's lubricant product will perform as promised. Perhaps, the only "insurance" for the State in such a situation is the refiner's "deep pockets." Nonetheless, recognition as either a national brand or as a national compounder blender is not critical to the State in receiving quality lubricant products.

The Specification Does Not Reflect Today's Market

The contract's specification does not reflect today's lubricants market. As noted above, refiners have reduced significantly their lubricant manufacturing operations, relying instead on ILMA members in many geographical areas to manufacture, package and distribute their branded products. Further, as also previously noted, the list of acceptable manufacturers is out of date as is the use of the repackaging contractors.

More importantly, given these consolidations, ILMA's members play an even more critical role in the lubricants business and in satisfying the demanding needs of end-users. The State should recognize in its contract independent compounder blenders who manufacture high-quality lubricant products and who are more proximate to and can better serve their customers.

Delaware's Taxpayers are not Getting the Best Deal

More importantly, as the result of recent refiner mergers and consolidations and if the contract specification is literally adhered to, there are fewer companies that can competitively bid today on the State's lubricant needs. As a result, the State and the taxpayers are not getting the best possible pricing for the lubricant products being purchased by the State. A specification that allows for a larger group of bidders, including ILMA members, who are quoting an industry-wide performance requirement will result in a lower cost of goods to the State.

* * * *

ILMA appreciates your consideration on this matter. We are interested in assisting you with a contract specification for lubricant products that will provide for fair competition among all participants in the lubricants industry to provide Delaware with high-quality, lower-cost products.

Sincerely,

Celeste M. Powers, CAE
Executive Director

cc: Board of Directors

Ms. Althea Henry
March 4, 2004
Page 5 of 5

Jeffrey L. Leiter, Esq.