SUNOCO INC
Form 10-Q
May 05, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2011

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission file number 1-6841

SUNOCO, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**23-1743282**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
1818 Market Street, Suite 1500, Philadelphia, PA	**19103**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (215) 977-3000

(Former name, former address and former fiscal year, if changed since last report): Not Applicable

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x NO ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES x NO ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	Accelerated filer	¨
Non-accelerated filer	¨ (do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ¨ NO x

At March 31, 2011, there were 121,106,529 shares of Common Stock, $1 par value outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

SUNOCO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Millions of Dollars and Shares, Except Per-Share Amounts)

	For the Three Months Ended March 31, 2011	2010
	(UNAUDITED)	
Revenues		
Sales and other operating revenue (including consumer excise taxes)	$ 10,609	$ 8,166
Interest income	4	
Other income, net	25	26
	10,638	8,192
Costs and Expenses		
Cost of products sold and operating expenses	9,819	7,311
Consumer excise taxes	548	530
Selling, general and administrative expenses	145	146
Depreciation, depletion and amortization	112	114
Payroll, property and other taxes	37	34
Provision for asset write-downs and other matters (Note 3)	6	45
Interest cost and debt expense	43	39
Interest capitalized	(6)	(3)
	10,704	8,216
Loss from continuing operations before income tax expense (benefit)	(66)	(24)
Income tax expense (benefit) (Note 4)	14	(9)
Loss from continuing operations	(80)	(15)
Loss from discontinued operations, net of income taxes (Note 2)		(23)
Net loss	(80)	(38)
Less: Net income attributable to noncontrolling interests	21	25
Net loss attributable to Sunoco, Inc. shareholders	$ (101)	$ (63)
Earnings (loss) attributable to Sunoco, Inc. shareholders per share of common stock:		
Basic:		
Loss from continuing operations	$ (0.84)	$ (0.34)
Loss from discontinued operations		(0.19)

Net loss	$ (0.84)	$ (0.53)
Diluted:		
Loss from continuing operations	$ (0.84)	$ (0.34)
Loss from discontinued operations		(0.19)
Net loss	$ (0.84)	$ (0.53)
Weighted average number of shares outstanding (Note 5):		
Basic	120.9	118.8
Diluted	120.9	118.8
Cash dividends paid per share of common stock	$ 0.15	$ 0.15

(See Accompanying Notes)

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SUNOCO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Millions of Dollars)

	At March 31, 2011 (UNAUDITED)	At December 31, 2010
Assets		
Cash and cash equivalents	$ 1,480	$ 1,485
Accounts and notes receivable, net	2,875	2,679
Note receivable from sale of Toledo refinery (Note 3)	285	
Inventories:		
Crude oil	822	98
Petroleum and chemical products	151	126
Coal and coke	89	83
Materials, supplies and other	103	97
Deferred income taxes	74	129
Toledo refinery and related assets held for sale (Note 3)		1,029
Total current assets	5,879	5,726
Investments and long term receivables	163	160
Note receivable from sale of Toledo refinery (Note 3)	200	
Properties, plants and equipment, cost	10,968	11,263
Less: accumulated depreciation, depletion and amortization	3,820	4,208
Properties, plants and equipment, net	7,148	7,055
Deferred charges and other assets	396	356
Total assets	$ 13,786	$ 13,297
Liabilities and Equity		
Accounts payable	$ 4,512	$ 3,912
Accrued liabilities (Note 6)	511	554
Short-term borrowings	115	115
Current portion of long-term debt	205	178
Taxes payable	317	170
Total current liabilities	5,660	4,929
Long-term debt	2,152	2,136
Retirement benefit liabilities (Note 7)	483	481
Deferred income taxes	1,226	1,390
Other deferred credits and liabilities (Note 6)	571	562
Commitments and contingent liabilities (Note 6)		
Total liabilities	10,092	9,498
Equity (Note 9)		
Sunoco, Inc. shareholders equity	2,950	3,046

Noncontrolling interests		744		753
Total equity		3,694		3,799
Total liabilities and equity	$	13,786	$	13,297

(See Accompanying Notes)

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SUNOCO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Millions of Dollars)

	For the Three Months Ended March 31, 2011	2010
	(UNAUDITED)	
Cash Flows from Operating Activities:		
Net loss	$ (80)	$ (38)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Loss on divestment of discontinued polypropylene operations		169
Provision for asset write-downs and other matters	6	45
Depreciation, depletion and amortization	112	117
Deferred income tax benefit	(133)	(48)
Payments less than (in excess of) expense for retirement plans	3	(134)
Changes in working capital pertaining to operating activities:		
Accounts and notes receivable	(200)	(11)
Inventories	(743)	(248)
Accounts payable and accrued liabilities	559	341
Income tax refund receivable and taxes payable	149	319
Other	(41)	(11)
Net cash provided by (used in) operating activities	(368)	501
Cash Flows from Investing Activities:		
Capital expenditures	(150)	(161)
Acquisitions	(36)	
Proceeds from divestments:		
Toledo refinery and related inventory	546	
Other divestments	6	8
Other	(6)	
Net cash provided by (used in) investing activities	360	(153)
Cash Flows from Financing Activities:		
Net repayments of short-term borrowings		(282)
Net proceeds from issuance of long-term debt	70	571
Repayments of long-term debt	(23)	(303)
Net proceeds from sale of Sunoco Logistics Partners L.P. limited partnership units		145
Cash distributions to noncontrolling interests	(30)	(27)
Cash dividend payments	(18)	(18)
Other	4	1
Net cash provided by financing activities	3	87
Net increase (decrease) in cash and cash equivalents	(5)	435
Cash and cash equivalents at beginning of period	1,485	377
Cash and cash equivalents at end of period	$ 1,480	$ 812

(See Accompanying Notes)

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. General.

The accompanying condensed consolidated financial statements are presented in accordance with the requirements of Form 10-Q and U.S. generally accepted accounting principles for interim financial reporting. They do not include all disclosures normally made in financial statements contained in Form 10-K. In management s opinion, all adjustments necessary for a fair presentation of the results of operations, financial position and cash flows for the periods shown have been made. All such adjustments are of a normal recurring nature, except for the gain on divestment of the Toledo refinery and related inventory, the gain resulting from the reduction of crude oil and refined product inventories at the Toledo refinery prior to its sale and the provision for asset write-downs and other matters (Notes 3 and 11). Results for the three months ended March 31, 2011 are not necessarily indicative of results for the full-year 2011.

2. Discontinued Polypropylene Operations.

On March 31, 2010, Sunoco completed the sale of the common stock of its polypropylene chemicals business to Braskem S.A. The assets sold as part of this transaction included the polypropylene manufacturing facilities in LaPorte, TX, Neal, WV, and Marcus Hook, PA, a propylene supply agreement and related inventory. Cash proceeds from this divestment of $348 million were received in the second quarter of 2010. As a result of the sale of the polypropylene chemicals business, such operations have been classified as discontinued operations in the condensed consolidated statements of operations. Sunoco recognized a net loss of $169 million ($44 million after tax) related to the divestment which was reflected as a component of the loss from discontinued operations in the first quarter of 2010.

The following is a summary of the loss from discontinued operations for the three-month period ended March 31, 2010 (in millions of dollars):

Loss before income tax benefit	$ (136)
Income tax benefit	(113)
Loss from discontinued operations*	$ (23)

* Attributable to Sunoco, Inc. shareholders.

Sales and other operating revenue (including consumer excise taxes) from discontinued operations totaled $313 million for the three months ended March 31, 2010.

3. Changes in Business and Other Matters.

Divestment

On March 1, 2011, Sunoco completed the previously announced sale of its Toledo refinery and related crude and refined product inventories to a wholly owned subsidiary of PBF Holding Company LLC. The Company received $1,037 million in net proceeds consisting of $546 million in cash, a $285 million note receivable due in 90 days, a $200 million two-year note receivable, and a $6 million net receivable related to working capital adjustments subsequent to closing. In addition, the purchase agreement also includes a participation payment of up to $125 million based on the future profitability of the refinery. Sunoco has not recorded any amount related to the contingent consideration in accordance with its accounting policy election on such amounts. In connection with this transaction, the Company recognized a $15 million net pretax gain ($4 million after tax) in the first quarter of 2011. This gain includes an estimated pretax gain of $535 million attributable to the sale of crude and refined product inventories. The gain on this divestment was recognized in other income, net in the condensed consolidated statement of operations. The results of operations for the Toledo refinery have not been classified as discontinued operations due to Sunoco s continuing involvement with the Toledo refinery through a three-year agreement for the purchase of gasoline and distillate to supply Sunoco retail sites in this area.

Prior to the sale, Sunoco reduced crude oil and refined product inventories at the Toledo refinery which resulted in LIFO inventory profits of $42 million ($26 million after tax) during the first quarter of 2011.

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Acquisitions

In January 2011, SunCoke Energy acquired Harold Keene Coal Co., Inc., based in Honaker, VA, for approximately $51 million. The purchase price included a net cash payment of $36 million and contingent consideration totaling $15 million primarily related to the estimated fair value of contingent royalty payments to the seller if certain minimum production levels are met for a period of up to 20 years. The assets acquired, which are adjacent to SunCoke s existing mining operations, include two active underground mines and one active surface and highwall mine currently producing between 250 and 300 thousand tons of coal annually. Proven and probable coal reserve estimates for this acquisition total approximately 21 million tons. No pro forma information has been presented since the acquisition was not material in relation to Sunoco s consolidated results of operations.

Asset Write-Downs and Other Matters

The following table summarizes information regarding the provision for asset write-downs and other matters recognized during the three months ended March 31, 2011 and 2010 (in millions of dollars):

	Pretax	After-tax
2011		
Business improvement initiatives	$ 6	$ 4
2010		
Eagle Point Refinery	$ 33	$ 20
Business improvement initiatives	12	7
	$ 45	$ 27

In connection with ongoing business improvement initiatives to reduce costs and improve business processes, the Company recorded provisions of $6 and $12 million ($4 and $7 million after tax) in the first quarter of 2011 and 2010, respectively, primarily for pension settlement losses.

In the first quarter of 2010, Sunoco recorded a $33 million accrual ($20 million after tax) primarily for contract losses in connection with excess barge capacity resulting from the shutdown of the Eagle Point refining operations in December 2009.

The following table summarizes the changes in the liability for employee terminations and other exit costs (in millions of dollars):

	Three Months Ended March 31,	
	2011	2010
Balance at beginning of period	$ 72	$ 68
Additional accruals	2	35
Payments charged against the accruals	(9)	(17)
Balance at end of period	$ 65	$ 86

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4. Income Taxes.
The following table summarizes the components of pretax income and income tax expense from continuing operations for the three months ended March 31, 2011 and 2010 (in millions of dollars):

	2011 Pretax Income (Loss)	2011 Tax Expense (Benefit)	2011 After-Tax Income (Loss)	2010 Pretax Income (Loss)	2010 Tax Expense (Benefit)	2010 After-Tax Income (Loss)
Income attributable to Sunoco, Inc. shareholders before discrete items	$ (141)	$ (24)	$ (117)	$ (3)	$ (1)	$ (2)
Discrete items:						
Sale of Toledo refinery	15	11	4			
LIFO inventory gains	42	16	26			
Provision for asset write-downs and other matters	(6)	(2)	(4)	(45)	(18)	(27)
State deferred income tax adjustment		5	(5)		9	(9)
Other		5	(5)	(1)	1	(2)
Income attributable to noncontrolling interests	24	3	21	25		25
	$ (66)	$ 14	$ (80)	$ (24)	$ (9)	$ (15)

The following table reconciles the U.S. statutory rate to the effective tax rates applicable to income attributable to Sunoco, Inc. shareholders before discrete items for the three months ended March 31, 2011 and 2010:

	2011	2010
U.S. statutory rate	35 %	35 %
Increase (reduction) resulting from:		
Nonconventional fuel credits	(9)%	(5)%
Depletion	(2)%	%
Manufacturers deduction	(4)%	(3)%
State income taxes (net of federal income tax effects)	1 %	4 %
Other	(4)%	%
	17 %	31 %

In the first quarter of 2011, Sunoco recorded a $5 million increase to deferred income taxes in part due to apportionment changes as a result of the sale of the Toledo refinery. In the first quarter of 2010, Sunoco recorded a $9 million increase in deferred state income taxes attributable to the transfer of assets related to its continuing phenol chemicals operations to a different legal entity subsequent to the sale of the stock of the discontinued polypropylene business.

The Company received a federal income tax refund totaling $394 million in March 2010 for the carryback of its 2009 net operating loss.

5. Earnings Per Share Data.
The following table sets forth the reconciliation of the weighted-average number of common shares used to compute basic earnings per share (EPS) to those used to compute diluted EPS (in millions):

	Three Months Ended March 31,

	2011	2010
Weighted-average number of common shares outstanding-basic	120.9	118.8
Add effect of dilutive stock incentive awards*		
Weighted-average number of shares-diluted	120.9	118.8

* Since the assumed issuance of common stock under stock incentive awards would not have been dilutive, the weighted-average number of shares used to compute diluted EPS is equal to the weighted-average number of shares used in the basic EPS computation.

6. Commitments and Contingent Liabilities.

Commitments

Over the years, Sunoco has sold thousands of retail gasoline outlets as well as refineries, terminals, coal mines, oil and gas properties and various other assets. In connection with these sales, the Company has indemnified the purchasers for potential environmental and other contingent liabilities related to the periods prior to the transaction dates. In most cases, the effect of these arrangements was to afford protection for the purchasers with respect to obligations for which the Company was already primarily liable. While some of these indemnities have spending thresholds which must be exceeded before they become operative, or limits on Sunoco s maximum exposure, they generally are not limited. The Company recognizes the fair value of the obligations undertaken for all guarantees entered into or modified after January 1, 2003. In addition, the Company accrues for any obligations under these agreements when a loss is probable and reasonably estimable. The Company cannot reasonably estimate the maximum potential amount of future payments under these agreements.

Environmental Remediation Activities

Sunoco is subject to extensive and frequently changing federal, state and local laws and regulations, including, but not limited to, those relating to the discharge of materials into the environment or that otherwise relate to the protection of the environment, waste management and the characteristics and composition of fuels. As with the industry generally, compliance with existing and anticipated laws and regulations increases the overall cost of operating Sunoco s businesses, including remediation, operating costs and capital costs to construct, maintain and upgrade equipment and facilities.

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Existing laws and regulations result in liabilities and loss contingencies for remediation at Sunoco s facilities and at formerly owned or third-party sites. The accrued liability for environmental remediation is classified in the condensed consolidated balance sheets as follows (in millions of dollars):

	At March 31, 2011	At December 31, 2010
Accrued liabilities	$ 29	$ 29
Other deferred credits and liabilities	86	86
	$ 115	$ 115

The following table summarizes the changes in the accrued liability for environmental remediation activities by category (in millions of dollars):

	Refineries	Retail Sites	Pipelines and Terminals	Chemicals Facilities	Hazardous Waste Sites	Other	Total
Balance at January 1, 2010	$ 30	$ 66	$ 12	$ 4	$ 3	$ 1	$ 116
Accruals	1	4	1				6
Payments	(2)	(4)	(1)		(1)		(8)
Other		2					2
Balance at March 31, 2010	$ 29	$ 68	$ 12	$ 4	$ 2	$ 1	$ 116
Balance at January 1, 2011	$ 31	$ 65	$ 12	$ 3	$ 3	$ 1	$ 115
Accruals	1	3	1				5
Payments	(2)	(4)	(1)				(7)
Other		2					2
Balance at March 31, 2011	$ 30	$ 66	$ 12	$ 3	$ 3	$ 1	$ 115

Sunoco s accruals for environmental remediation activities reflect management s estimates of the most likely costs that will be incurred over an extended period to remediate identified conditions for which the costs are both probable and reasonably estimable. Engineering studies, historical experience and other factors are used to identify and evaluate remediation alternatives and their related costs in determining the estimated accruals for environmental remediation activities. Losses attributable to unasserted claims are also reflected in the accruals to the extent they are probable of occurrence and reasonably estimable.

Total future costs for the environmental remediation activities identified above will depend upon, among other things, the identification of any additional sites, the determination of the extent of the contamination at each site, the timing and nature of required remedial actions, the nature of operations at each site, the technology available and needed to meet the various existing legal requirements, the nature and terms of cost-sharing arrangements with other potentially responsible parties, the availability of insurance coverage, the nature and extent of future environmental laws and regulations, inflation rates, terms of consent agreements or remediation permits with regulatory agencies and the determination of Sunoco s liability at the sites, if any, in light of the number, participation level and financial viability of the other parties. Management believes it is reasonably possible (i.e., less than probable but greater than remote) that additional environmental remediation losses will be incurred. At March 31, 2011, the aggregate of the estimated maximum additional reasonably possible losses, which relate to numerous individual sites, totaled approximately $90 million. However, the Company believes it is very unlikely that it will realize the maximum reasonably possible loss at every site. Furthermore, the recognition of additional losses, if and when they were to occur, would likely extend over many years and, therefore, likely would not have a material impact on the Company s financial position.

Under various environmental laws, including the Resource Conservation and Recovery Act (RCRA) (which relates to solid and hazardous waste treatment, storage and disposal), Sunoco has initiated corrective remedial action at its facilities, formerly owned facilities and third-party sites. At the Company s major manufacturing facilities, Sunoco has consistently assumed continued industrial use and a containment/remediation strategy focused on eliminating unacceptable risks to human health or the environment. The remediation accruals for these sites reflect that strategy. Accruals include amounts to prevent off-site migration and to contain the impact on the facility property, as well as to address known, discrete areas requiring remediation within the plants. Activities include closure of RCRA solid waste management units, recovery of hydrocarbons, handling of impacted soil, mitigation of surface water impacts and prevention of off-site migration.

Many of Sunoco s current terminals are being addressed with the above containment/remediation strategy. At some smaller or less impacted facilities and some previously divested terminals, the focus is on remediating discrete interior areas to attain regulatory closure.

Sunoco owns or operates certain retail gasoline outlets where releases of petroleum products have occurred. Federal and state laws and regulations require that contamination caused by such releases at these sites and at formerly owned sites be assessed and remediated to meet the applicable standards. The obligation for Sunoco to remediate this type of contamination varies, depending on the extent of the release and the applicable laws and regulations. A portion of the remediation costs may be recoverable from the reimbursement fund of the applicable state, after any deductible has been met.

The accrued liability for hazardous waste sites is attributable to potential obligations to remove or mitigate the environmental effects of the disposal or release of certain pollutants at third-party sites pursuant to the Comprehensive Environmental Response Compensation and Liability Act (CERCLA) (which relates to releases and remediation of hazardous substances) and similar state laws. Under CERCLA, Sunoco is potentially subject to joint and several liability for the costs of remediation at sites at which it has been identified as a potentially responsible party (PRP). As of March 31, 2011, Sunoco had been named as a PRP at 33 sites identified or potentially identifiable as Superfund sites under federal and state law. The Company is usually one of a number of companies identified as a PRP at a site. Sunoco has reviewed the nature and extent of its involvement at each site and other relevant circumstances and, based upon the other parties involved or Sunoco s level of participation therein, believes that its potential liability associated with such sites will not be significant.

Management believes that none of the current remediation locations, which are in various stages of ongoing remediation, are individually material to Sunoco as its largest accrual for any one Superfund site, operable unit or remediation area was less than $12 million at March 31, 2011. As a result, Sunoco s exposure to adverse developments with respect to any individual site is not expected to be material. However, if changes in environmental laws or regulations occur, such changes could impact multiple Sunoco facilities, formerly owned facilities and third-party sites at the same time. As a result, from time to time, significant charges against income for environmental remediation may occur.

The Company maintains insurance programs that cover certain of its existing or potential environmental liabilities, which programs vary by year, type and extent of coverage. For underground storage tank remediations, the Company can also seek reimbursement through various state funds of certain remediation costs above a deductible amount. For certain acquired properties, the Company has entered into arrangements with the sellers or others that allocate environmental liabilities and provide indemnities to the Company for remediating contamination that occurred prior to the acquisition dates. Some of these environmental indemnifications are subject to caps and limits. No accruals have been recorded for any potential contingent liabilities that will be funded by the prior owners as management does not believe, based on current information, that it is likely that any of the former owners will not perform under any of these agreements. Other than the preceding arrangements, the Company has not entered into any arrangements with third parties to mitigate its exposure to loss from environmental contamination. Claims for recovery of environmental liabilities that are probable of realization totaled $13 million at March 31, 2011 and are included principally in deferred charges and other assets in the condensed consolidated balance sheet.

Regulatory Matters

Under a 2005 Consent Decree which settled certain alleged violations under the Clean Air Act, Sunoco was required to make capital outlays totaling approximately $150-$200 million related to projects at the Marcus Hook refinery prior to June 30, 2013. During the first quarter of 2011, the Company reached an agreement with the U.S. Environmental Protection Agency (EPA), Pennsylvania Department of Environmental Protection, and Philadelphia Air Management Services regarding the terms of a two-year extension of the capital requirements at Marcus Hook. This extension will still require a public comment period and court approval.

Through the operation of its refining and chemical facilities, marketing facilities, coke plants and coal mines, Sunoco s operations emit greenhouse gases (GHG), including carbon dioxide. There are various legislative and regulatory measures to address GHG emissions which are in various stages of review, discussion or implementation. Current proposals being considered by Congress include cap and trade legislation and carbon taxation legislation. One current cap and trade bill proposes a system that would begin in 2012 which would require the Company to provide carbon emission allowances for emissions at its manufacturing facilities as well as emissions caused by the use of fuels it sells. The cap and trade program would require affected businesses to buy emission credits from the government, other businesses or through an auction

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process. The exact amount of such costs, as well as those that could result from any carbon taxation would not be established until the future. However, the Company believes that these costs could be material, and there is no assurance that the Company would be able to recover them in the sale of its products. Other federal and state actions to develop programs for the reduction of GHG emissions are also being considered. In addition, during 2009, the EPA indicated that it intends to regulate carbon dioxide emissions. While it is currently not possible to predict the impact, if any, that these issues will have on the Company or the industry in general, they could result in increases in costs to operate and maintain the Company s facilities, as well as capital outlays for new emission control equipment at these facilities. In addition, regulations limiting GHG emissions or carbon content of products, which target specific industries such as petroleum refining or chemical or coke manufacturing could adversely affect the Company s ability to conduct its business and also may reduce demand for its products.

National Ambient Air Quality Standards (NAAQS) for ozone and fine particles promulgated by the EPA have resulted in identification of non-attainment areas throughout the country, including Texas, Pennsylvania, and Ohio, where Sunoco operates facilities. Areas designated by the EPA as moderate non-attainment for ozone, including Philadelphia and the Houston/Galveston/Brazoria area, were required to meet the ozone requirements by 2010 before currently mandated federal control programs were to take effect. In January 2009, the EPA issued a finding that the Pennsylvania and Texas State Implementation Plans (SIPs) failed to demonstrate attainment for the Philadelphia and Houston/Galveston/Brazoria airsheds by the 2010 deadline. This finding is expected to result in more stringent offset requirements and could result in other negative consequences. Texas petitioned the EPA to redesignate the Houston area as severe non-attainment for ozone and in 2009 the EPA granted the petition. Under this designation, Houston s SIP was due in 2010 and attainment must be achieved by 2019. In September 2006, the EPA issued a final rule tightening the standard for fine particles. This standard is currently being challenged in federal court by various states and environmental groups. In March 2007, the EPA issued final rules to implement the 1997 fine particle matter (PM 2.5) standards. States had until April 2008 to submit plans to the EPA demonstrating attainment by 2010 or, at the latest, 2015. However, the March 2007 rule does not address attainment of the September 2006 standard. In March 2008, the EPA promulgated a new, more stringent ozone standard, which was challenged in a lawsuit in May 2008 by environmental organizations. Regulatory programs, when established to implement the EPA s air quality standards, could have an impact on Sunoco and its operations. However, the potential financial impact cannot be reasonably estimated until the lawsuit is resolved, the EPA promulgates regulatory programs to attain the standards, and the states, as necessary, develop and implement revised SIPs to respond to the new regulations.