**DEPARTMENT OF AGRICULTURE**
**STATE OF NEW MEXICO**

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SUSANA MARTINEZ
*Governor*

JEFF M. WITTE
*Secretary*

May 12, 2017

MEMORANDUM

TO: Petroleum Refiners, Marketers, and Biodiesel Suppliers

FROM: Jeff M. Witte, Secretary of Agriculture

SUBJECT: Temporary Suspension of New Mexico's Biodiesel Mandate

In accordance with Section 57-19-28, paragraph C of the Petroleum Products Standards Act NMSA 1978 and in consultation with the secretary of the Energy, Minerals and Natural Resources Department and pursuant to regular, periodic monitoring of biodiesel supplies and price differentials, the New Mexico Department of Agriculture has issued a "Temporary Suspension of New Mexico's Biodiesel Mandate."

Section 57-19-29, paragraph C of the Petroleum Products Standards Act will be suspended for a period of six months effective May 16, 2017 through November 15, 2017.

Attached is the concurrence letter from Secretary McQueen with the Energy, Minerals and Natural Resources Department which details the justification for the suspension.

If you have any questions or need additional information, please contact Mr. David Turning, assistant division director for Standards and Consumer Services Division, at (575) 646-1616 or dturning@nmda.nmsu.edu.

Attachment: Secretary McQueen Letter, May 10, 2017

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May 10, 2017

The Honorable Ken McQueen, Secretary
Energy, Minerals and Natural Resources
1220 South St. Francis Drive
Santa Fe, NM 87505

RE: Biodiesel Mandate

Dear Secretary McQueen:

In accordance with the Petroleum Products Standards Act:

**57-19-28. Duties of the board; authority of the director**

*C. If in consultation with the secretary of energy, minerals and natural resources and pursuant to regular, periodic monitoring,* ***the director determines that sufficient amounts of biodiesel are not available*** *to meet the requirements of Section 57-19-29 NMSA 1978* ***or that the price of the biodiesel blend significantly exceeds the price of diesel fuel for at least two months,*** *the director shall suspend those requirements for a period of up to six months.*

**57-19-29. Quality standards**

*C. On or after July 1, 2012, all diesel fuel sold to consumers for use in motor vehicles on the streets and highways of this state shall contain five percent biodiesel, except that this standard may be temporarily suspended by the director in accordance with Section 57-19-28 NMSA 1978.*

Availability and pricing have been evaluated, the following information has been compiled:

**Diesel sold in the New Mexico Market:**

In 2016, New Mexico sold 495,261,557 [1] qualifying gallons of diesel for a monthly average of 41,271,796. In 2017 (through February) there has been 81,310,624 qualifying gallons of diesel sold for a monthly average of 40,655,312. Based on the information provided, in 2016, 63.8 percent of the diesel sold in the state was supplied by New Mexico terminals and 36.2 percent of the diesel sold in the state was imported. For 2017 the trend is similar with 63 percent of the

[1] Qualifying gallons are calculated by New Mexico Tax and Revenue on reported special fuel sales (New Mexico Terminals 2A plus Import schedule 3 minus Export schedule 7 minus US Government schedule 8).

diesel sold in New Mexico being supplied by New Mexico terminals and 37 percent being imported (see Attachement 1).

**Biodiesel sold in the New Mexico Market:**

Based on information provided by the New Mexico Tax and Revenue Department (NMTRD), the New Mexico Department of Agriculture (NMDA) received a breakdown of biodiesel sold by category (B100, B99, B02, B05, B20 and category 170). For categories B100, B99, B02, B05 and B20, NMTRD was able to calculate the biodiesel used from reported data.

For category 170, NMTRD is unable to determine a biodiesel usage number as this reporting line could be a combination of B02, B05 or a B20. To address the omission of data, through a statistical analysis using historical sampling data, NMDA calculated a distribution of product by percentage to category 170 which resulted in the following:

| Biodiesel Present Per Sample | Percent of Biodiesel present per Sample | |
|---|---|---|
| | **2015** | **2016** |
| <0 – 1 | 55% | 46% |
| 1 – 2 | 5% | 6% |
| 2 – 3 | 5% | 5% |
| 3 – 4 | 12% | 14% |
| 4 – 5 | 17% | 18% |
| 5 – 6 | 2% | 7% |
| 6 - 100 | 2% | 3% |

January 2017 category 170 calculations are as follows:

- 90% or 3,819,322 gallons X 5% = 190,966 gallons
- 10% or 424,369 gallons X 20% = 84,879 gallons
- 190,966+ 84,879 = 275845 total gallons

February 2017 category 170 calculations are as follows:

- 90% or 3,500,923 gallons X 5% = 175,046 gallons
- 10% or 388,991 gallons X 20% = 77,798 gallons
- 175,046 + 77,798 = 252,844 total gallons

Biodiesel gallons sold in the New Mexico market during 2017 was derived from the NMTRD reporting biodiesel data plus the statistical distribution of category 170:

- January 908,838 (CFT Biodiesel report) plus 275,845 (Calculated category 170)= 1,184,228
- February 1,245,495 (CFT Biodiesel report) plus 252,844 (Calculated category 170 = 1,498,339 (See attachment 2).

**Identified supply points and their ability to blend biodiesel:**

NMDA obtained the information on supply points and their ability to blend biodiesel by contacting the various terminals, refiners and biodiesel producers directly for those located within New Mexico. The out-of-state terminals, refiners and biodiesel producers self-reported.

The information was compiled and initially presented at a biodiesel task force meeting held in Albuquerque on June 4, 2015. The information from the initial report was updated in January 2017 and distributed during the New Mexico legislative session.

New Mexico (9 supply points):

- (1) Bloomfield (blends seasonally during the warmer months- product (B5) is shipped via Holly pipeline from Moriarty)
- (1) Ciniza (splash blends seasonally during the warmer months- does not have the infrastructure to in-line blend)
- (5) Albuquerque (1 terminal blends year round, 3 terminals have no blending (infrastructure is lacking), 1 biodiesel producer blends year round- offers splash blending)
- (1) Artesia (has the ability to blend year round)
- (1) Moriarty (blends seasonally during the warmer months- has infrastructure to in-line blend, does not have infrastructure to blend during winter months)
    a. Three or 33 percent have year round blending capability
    b. Three or 33 percent have seasonal blending capability (during the warm months)
    c. Three or 33 percent have zero blending capability

Texas (9 supply points):

- (2) Amarillo (1 terminal blends year round, 1 terminal blends seasonally during the warmer months)
- (1) Abernathy (blends seasonally during the warmer months)
- (1) Big Spring (blends year round)
- (5) El Paso (1 terminal blends year round, 3 terminals have no blending, 1 biodiesel producer blends year round)
    a. Four or 44 percent have year round blending capability
    b. Two or 22 percent have seasonal blending capability (during the warm months)
    c. Three or 33 percent have zero blending capability

Colorado (2 supply points):

- (1) Alamosa (blends year round)
- (1) La Junta (blends seasonally during the warmer months)
    a. One or 50 percent have year round blending capability
    b. One or 50 percent have seasonal blending capability (during the warm months)

Out-of-state percentages for blending:

a. Five or 45 percent have year round blending capability
b. Three or 27 percent have seasonal blending capability (during the warm months)
c. Three or 27 percent have zero blending capability

<u>** None of the out-of-state sources will guarantee product availability</u> (see attachment 3).

**<u>Contracts:</u>**

When marketers purchase fuel, they do so through contracts or agreements with suppliers. Suppliers can be branded or unbranded (Chevron, Shell, etc.), and these suppliers can be the owner/operators of terminals/racks they are receiving fuel from or they contract storage space at a location where they don't own any infrastructure. Purchase and sale contracts/agreements require customers to comply with all laws and ordinances orders or regulations relating to the handling, use, sale and transportation of products sold to them on the contract/agreement. Additional blending outside the terminal could potentially violate this part of the contract/agreement should the blended biodiesel product not meet specifications and violate laws and/or regulations. Due to the terms of contracts/agreements, most do not have the flexibility to purchase outside their contract terms.

- New Mexico Petroleum Marketers Association: "The marketer signs a supply contract with a supplier, and he is then obligated by contract to the supplier. The marketer cannot co-mingle product under terms of the contract, if he does he is subject to termination of the contract" (see attachment 4).
- HollyFrontier Refining & Marketing LLC: "HollyFrontier does not currently sell branded ULSD in NM and is not subject to branded contract concerns, but HollyFrontier's purchase and sale agreements require customers to comply with all laws, ordinances orders or regulations relating to the handling, use sale and transportation of products sold to them on the agreement. Additional blending outside the terminal could potentially violate this part of the agreement should the blended biodiesel product not meet specifications and violate laws and/or regulations" (see attachment 5).

**Splash Blending:**

Although splash blending is not a prohibited practice in the petroleum business, splash blending isn't the ideal method for blending biodiesel into petroleum diesel. Branded customers (Chevron, Shell, etc.) are usually restricted from splash blending altogether because those companies have to maintain control over what is marketed with their name brand. Additionally, marketers are prohibited through contract/agreements or company policies to splash blend due to concerns of fuel quality.

Identified splash blending concerns:

- Stratification of the denser biodiesel layer, as loading velocities, volumes or sequencing can be inadequate for proper mixing;
- Mixing is dependent on the length of time which a tank truck travels down a particular type of road;
- If the ambient temperature is low, then the biodiesel can gel when in contact with the sides of a metal tank and not mix with the diesel fuel;
- If the loading temperature of the biodiesel is low, then the biodiesel can gel before it mixes with the diesel fuel;
- And if there is any remaining heel volume in the tank truck, then the full quantity of second blend component or fuel may not be able to be loaded (see attachments 4, 5, 6).

**Availability and price differentials:**

- In New Mexico, out of nine (9) terminals, we have three (3) or 33 percent of the terminals with no infrastructure to blend, and out of the 11 out-of-state terminals, there are three (3) or 27 percent that do not have infrastructure to blend. Lack of infrastructure does cause availability issues by not having product available in the market where it is needed. In most cases, the retailer who is selling the product has a contract or agreement that limits what terminal/terminals they can purchase fuel from and what they can do to the fuel once it has been purchased. For some retailers who can amend the product after it has been picked up at a terminal, those retailers become solely responsible for the quality of the product- this is an option none of the retailers are willing to undertake.

- Additionally, lack of infrastructure in-state and out-of-state creates price differential issues due to the need to source product from non-local terminals. For example: In the Albuquerque market there are a number of terminals (3) that do not have the infrastructure to blend biodiesel. In order to meet the needs of the mandate, customers of those terminals will have to source their B5 diesel from other terminals that do have the infrastructure to blend biodiesel. The terminals for the Albuquerque market are located in El Paso (288 miles away) or Amarillo (265 miles away), this would undoubtedly add an additional freight cost to the product to the tune of ~14 cents per gallon or more. The additional driving distances limit the number of deliveries that could be pulled from those terminals and would create the need for more trucks, drivers and an increased demand on out-of- state terminals which they may not have the capacity to handle. The economics created by this action would be detrimental to the markets in New Mexico as well as increased prices for the drivers in New Mexico (see attachments 4, 5, 6, 7).
- Pricing data obtained from Oil Price Information Service (OPIS) and the U.S. Energy department both are reporting price differentials that will negatively affect the consumers in New Mexico. Pricing data from OPIS from the Albuquerque and El Paso markets for 2017 shows a price differential between diesel and biodiesel, the same trend is mirrored by the U.S. Energy report (see attachment 9).

To meet the requirements of the mandate, New Mexico needs on average 2 million gallons of biodiesel per month. For 2017, the monthly average usage of biodiesel has been 1.3 million gallons. The prevailing issue in New Mexico is that in order to deliver more biodiesel into the marketplace, i.e. make it available to the end consumer, that it is tied to the lack of infrastructure at terminals that supply the New Mexico market at both the in-state and out-of-state terminals. Although Biodiesel is available by suppliers, the distribution terminals infrastructure is not in place in order to blend biodiesel into the diesel supply that is delivered to the consumer, thus creating an availability issue.

Price differentials were sourced from:

- U.S. Department of Energy- Clean cities Alternative Fuel price report (see attachment 8)
- HollyFrontier- Biodiesel, RIN and ULSD price quotes from Oil Price Information Service (OPIS) for 2017 (see attachment 9).
- Global Alternative Fuels, LLC/ Rio Valley Biofuels LLC (See Attachement 10).

**Recommendation:**

Based on the following impeding issues:

1. Current and historical reporting from the NMTRD indicates that supply of biodiesel into the state is 700,000 gallons or 35 percent short on a monthly basis to fulfill the requirement of the mandate.
2. Infrastructure at 30 percent of distribution points lack the ability to blend on an annual basis. Of the remaining distribution points, 30 percent can only blend during warm months.

Based on discussions with the petroleum industry (Chevron, Valero, Western, HollyFrontier, Phillips 66 and Vercenergy) to build infrastructure would require 24 to 30 months to accomplish; however, there is not an economic incentive to undergo the construction.

3. The ability to deliver diesel via pipeline requires that it be delivered via truck or rail infusing additional transportation costs as a result of the mandate
4. Implementation of the mandate without infrastructure would cause availability issues in the state, driving up costs to the end consumer and making New Mexico a drive through state for the trucking industry, removing the tax base from the New Mexico economy.

It is my recommendation that the implementation of the biodiesel mandate be suspended until such a time that there is sufficient infrastructure to support the mandate and OPIS pricing as well as U.S. Energy reports support implementation. Factors that need to be addressed would be infrastructure necessary to delivery biodiesel into the New Mexico market and pricing reports generated by the U.S. Energy department showing that price differentials do not exist that impede implementation. As such, the suspension should remain in place based on reviews completed in six month intervals. I request your concurrence in issuing a temporary suspension of the biodiesel mandate as spelled out in section 57-19-28 of the Petroleum Products Standards Act effective May 16, 2017, through November 15, 2017.

Sincerely,

Jeff M. White

JMW/dt

Secretary Ken McQueen
Energy, Minerals and Natural Resources

I concur in issuing a temporary suspension effective May 16, 2017, of the biodiesel mandate as spelled out in Section 57-19-28 of the Petroleum Products Standards Act.