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FISCAL IMPACT REPORT

ORIGINAL DATE 03/09/21

SPONSOR SFC LAST UPDATED _____ HB _____

SHORT TITLE Clean Fuel Standard Act SB 11/SFCS

ANALYST Wan

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	NFI	NFI	NFI			

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Environment Department (NMED)

Economic Development Department (EDD)

SUMMARY

Synopsis of Bill

The Senate Finance Committee substitute for Senate Bill 11 would enact the Clean Fuel Standards Act and proposes a clean fuel standard (CFS) using performance- and market-based incentives to reduce the carbon intensity of transportation fuels. SB11/SFCS directs the Environmental Improvement Board (EIB) to adopt a CFS that applies to transportation fuels, requiring that such fuels meet the following reductions in carbon intensity (CI) values: a reduction of the CI of transportation fuels in New Mexico by a minimum of 10 percent from 2018 levels by 2030 and by a minimum of 28 percent from 2018 levels by 2040. After 2040, the EIB shall determine further reduction requirements and timeframes for achieving them. The CFS would only apply to fuels used in motor vehicles and businesses that produce or import those fuels (referred to as “providers” in the bill).

SB11/SFCS defines “carbon intensity” as “the quantity of fuel lifecycle emissions per unit of fuel energy, expressed in grams of carbon dioxide equivalent per megajoule.” The Environment Department (NMED) explains that CI “is calculated by a life-cycle analysis that estimates the greenhouse gas (GHG) emissions for the fuel over its entire life cycle, including emissions from producing, processing, transporting, storing, and burning the fuel.”

SB11/SFCS directs NMED to petition the EIB to enact rules implementing the CFS within 24

months of the effective date of the legislation. The central mechanism for implementation established by the bill is a system, to be developed through rulemaking, whereby individuals can earn “credits” by reducing eligible GHG emissions and may sell those credits to providers who are in a “deficit” – providers of a transportation fuel that has a CI greater than the applicable standard. A credit and a deficit are each equal to one metric ton of carbon dioxide equivalent.

The bill requires the EIB’s rules to establish a fair market for credit transactions, managed by NMED or a third party. The market would be governed by EIB rules, which will enable credits to be traded or saved by providers for future compliance periods. Providers would demonstrate compliance with the CFS by balancing credits and deficits annually and submitting “fuel pathway” applications, fuel transactions, and CI data to NMED. “Fuel pathway” is defined in the bill as “a detailed description of all stages of production and uses for a transportation fuel...that is used to calculate the fuel lifecycle emissions of a transportation fuel.”

The EIB rules will specify how credits are generated, and SB11/SFCS requires the rules to prioritize mechanisms for credit generation that benefit disproportionately impacted, environmental justice, and rural communities. The bill also requires electric utilities that generate credits from electricity used as transportation fuel to reinvest at least 50 percent of credit-generated revenues into transportation electrification projects, rebates for electric vehicle purchases, or direct benefits for current electric vehicle customers. Of these investments, 30 percent of the funds in year one, 40 percent in year two, and 50 percent in subsequent years must be directed toward transportation electrification projects that primarily benefit disproportionately impacted, environmental justice, and rural communities.

Under SB11, NMED would be responsible for administration and enforcement of the CFS and associated credits. The bill requires the department to develop, in consultation with the Department of Agriculture (NMDA), an emergency deferral process, to be conducted with the input of stakeholders, for temporarily suspending CFS implementation to address market conditions. Details of this process will be established through the EIB’s CFS rulemaking, but must include a requirement that NMED consider a provider’s request for emergency deferral.

SB11/SFCS would create the “clean fuel standard fund,” to consist of annual registration fees charged to providers and any person generating credits under the CFS. Appropriations from the fund shall be used for NMED staffing and resources needed for administration and enforcement of transportation fuel regulations.

There is no effective date of this bill. It is assumed that the effective date is 90 days following adjournment of the Legislature.

FISCAL IMPLICATIONS

NMED reports 6 FTE would be required to develop proposed rules, conduct stakeholder and public outreach, petition the EIB, and participate in the rulemaking hearing process. In addition, the agency projects expenditures of \$1.64 million over two years for contracts with outside technical experts who would conduct additional analyses and assist in the preparation of EIB hearing exhibits and testimony. NMED anticipates contractual services will include: calculation of carbon intensities of existing transportation fuels; rule-drafting legal assistance, including review of legislation from other states; development of market trading rules and software platforms; development of a platform for permitting, certification, and compliance; and identifying specific

mechanisms and rules for credit generation. An appropriation included in HB2/HAFCS would cover these expenses in FY22-23, the expected timeline needed for the EIB to consider and promulgate rules.

However, NMED expects it will need those 6 FTE after the EIB rulemaking process as well, to manage the administrative responsibilities of implementing the regulations. Annual recurring costs for the required FTE (which would include three technical staff, two economists, and one attorney) and associated expenses, plus ongoing contractual services for trading platform software subscription and maintenance, carbon intensity determination, and analyses, are estimated to be \$1.15 million. These expenditures would be a recurring cost to the agency beginning in FY24.

SB11/SFCS requires the CFS rules to include registration fees on providers and any person generating credits in an amount sufficient to cover the reasonable costs of NMED's administration and enforcement of the rules. Therefore, NMED expects to generate \$1.15 million in annual revenue to fund program expenses beginning in FY24, once the process of developing, proposing, and adopting rules is complete.

This bill creates a new fund and provides for continuing appropriations. The LFC has concerns with including continuing appropriation language in the statutory provisions for newly created funds, as earmarking reduces the ability of the Legislature to establish spending priorities.

SIGNIFICANT ISSUES

According to the U.S. Environmental Protection Agency, transportation is the economic sector that generates the largest proportion of GHG emissions in the United States. As a result, most states have adopted policies to target emissions reductions in the transportation sector, primarily focused on clean vehicle programs and incentives. Six states have alternative fuel standards, which require a certain percentage of gasoline or diesel sold in a state to be sourced from alternative fuels such as ethanol and biodiesel.¹ California and Oregon have low carbon or clean fuel standards similar to the one proposed by SB11/SFCS, which set reduction targets for the CI of fuels rather than prescribing the types of fuels to be sold.

While the credit generation and marketplace mechanisms established by SB11/SFCS bear similarities to cap and trade programs, there are a few distinctions that set a CFS apart. First, a CFS only requires fuel producers and importers to reduce the CI of their fuels, while a cap and trade program places a limit on GHG emissions from any given sector or the economy as a whole. Furthermore, in a cap and trade program, the government distributes or auctions emissions allowances to companies; under this bill's proposed CFS, any company or individual in a variety of economic sectors to which the CFS does not apply can earn credits by reducing their GHG emissions and sell those credits to fuel providers who must comply with the CFS. As a result, while the policy targets GHG emissions from transportation fuels, it also provides an opportunity for individuals and businesses in other sectors to benefit economically from reducing their own emissions.

NMED's analysis posits that a CFS and credit market as proposed by SB11/SFCS "will allow New Mexico to decarbonize the transportation sector while driving innovation across industries, diversifying the state's economy, and creating jobs." The agency further states,

¹ Center for Climate and Energy Solutions, <https://www.c2es.org/document/low-carbon-fuel-standard/>.

“The creation of a CFS, tied to CI, invites the oil and gas industry to participate in waste recovery mandates (pending rulemaking before the Oil Conservation Commission) and ozone precursor emission controls (pending proposed rulemaking before the EIB) into economically recoverable, CI-reducing innovations. These new opportunities can generate credits. The predictable schedule of the decreasing CI standard allows for [businesses to] fund projects based on the credit market. The market process allows the project that delivers the greatest reduction in CI to be most valued, regardless of the industry sector in which it occurs.”

The Economic Development Department (EDD) also anticipates SB11/SFCS will promote statewide economic development and diversification by “supporting the expansion and location of new businesses, job creation, innovation in research and development and new alternative fuel technologies, and incentivizing capital investment into New Mexico, thereby increasing the tax base.” Consequently, EDD believes this will have a positive revenue impact of unknown magnitude for the state general fund. EDD also states that the presence of national research laboratories in New Mexico give the state the potential to be an “innovation hub” for new clean energy technologies.

On the issue of how SB11/SFCS might affect the cost of fuel for consumers, EDD says data from other states indicates New Mexico could see an increase in gas prices of less than 5 percent. Over time, however, the cost of alternative fuel vehicles is expected to decrease, increasing demand for those vehicles and alternative fuels, and reducing alternative fuel prices.

PERFORMANCE IMPLICATIONS

SB11/SFCS would lower emissions from transportation fuels, resulting in improved air quality which may increase the number of days with an air quality index of moderate or good, one of NMED’s key performance measures.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

In NMED’s estimation, if SB11/SFCS is not enacted, New Mexico will need to seek out other strategies to reduce emissions from the transportation sector in order to meet the state’s reduction requirements.

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