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## FISCAL IMPACT REPORT

**SPONSOR** Varela **ORIGINAL DATE** 2-13-09  
**LAST UPDATED** 3/15/09 **HB** 547/aHAFC  
**SHORT TITLE** Investigate Gas Price Increases **SB** \_\_\_\_\_  
**ANALYST** Ortiz

### APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY09	FY10		
	\$50.0	Non-Recurring	Consumer Settlement Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

Responses Received From  
 Attorney General's Office (AGO)

### SUMMARY

#### Synopsis of Bill

The House Appropriations and Finance Committee reduced the appropriation to \$50 thousand and used the consumer settlement fund to finance it.

#### Synopsis of Bill

House Bill 547 appropriates \$100 thousand from the general fund to Attorney General's Office for the purpose of investigating the recent gas price increases and decreases.

### FISCAL IMPLICATIONS

The appropriation of \$50 thousand contained in this bill is a non-recurring expense to the consumer settlement fund. Any unexpended or unencumbered balance remaining at the end of fiscal year 2010 shall revert to the general fund.

According to the December 2008 revenue estimate, FY10 recurring revenue will only support a base expenditure level that is \$293 million, or 2.6 percent, less than the FY09 appropriation. All appropriations outside of the general appropriation act will be viewed in this declining revenue context.

**SIGNIFICANT ISSUES**

Within the past year, explains the Attorney General’s Office, gas prices in New Mexico and across the United States have experienced enormous price swings without any justification by market fundamentals.

For example, within the last 6 months of the year on NYMEX, the futures price for a barrel of oil went from \$140 per barrel to \$33 per barrel, even though demand for gasoline did not drop proportionally. This suggests that speculation may have played a large role in earlier price increases.

In addition, local gas prices immediately increase whenever oil futures increase, even though the cost of current inventories should not be affected by futures prices.

Lastly, when there is a drop in oil futures, the local gas price does not decrease immediately. For example, it is estimated that local gas should sell for less than \$2 when the futures price for a barrel of oil drops below \$40 per barrel. However, in December when the January futures price for a barrel of oil dropped to \$33, the price for local gas stayed at \$2.30 per gallon.

LFC data below indicates the average price per gallon.

<u>\$/gal</u>	
<b>FY 2006</b>	<b>\$2.60</b>
<b>FY 2007</b>	<b>\$2.66</b>
<b>FY 2008</b>	<b>\$3.18</b>
<b>FY09 YTD</b>	<b>\$2.65</b>
<b>CY 2006</b>	<b>\$2.65</b>
<b>CY 2007</b>	<b>\$2.85</b>
<b>CY 2008</b>	<b>\$3.21</b>
<b>CY 2009 YTD</b>	<b>\$1.89</b>

Attached is a document produced by the Energy Information Administration, an independent statistical agency within the U.S. Department of Energy. It addresses the components of retail gas prices and why they fluctuate.

Also attached is the New Mexico Attorney General’s report addressing the 2007 House Joint Memorial 42 request to investigate the disparity between the price of gasoline and diesel fuel.

Attachments

EO/mt

## WHY ARE CALIFORNIA GASOLINE PRICES HIGHER AND MORE VARIABLE THAN OTHERS?

California prices are higher and more variable than prices in other States because there are relatively few supply sources of its unique blend of gasoline outside the State. The State of California's reformulated gasoline program is more stringent than the Federal government's. In addition to the higher cost of this cleaner fuel, there is a State sales tax of 7.25 percent on top of an 18.4 cent-per-gallon Federal excise tax and an 18.0 cent-per-gallon State excise tax.

California refineries need to be running near full capacity to meet the State's gasoline demand. If more than one of its refineries experiences operating problems at the same time, California's gasoline supply may become very tight and prices can soar. Even when supplies can be obtained from some Gulf Coast and foreign refineries, they can take a relatively long time to arrive due to California's substantial distance from those sources. The farther away the necessary relief supplies are, the higher and longer the price spike will be.

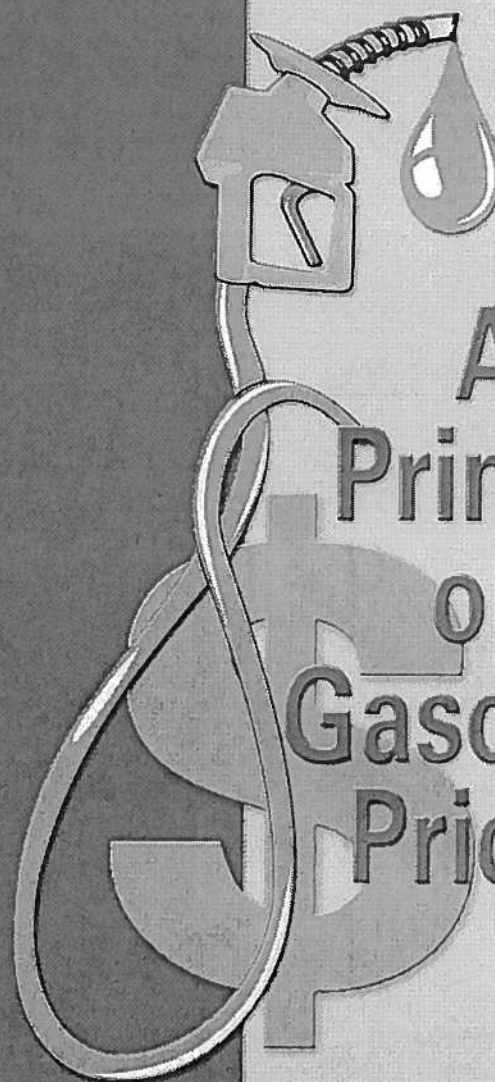
California was one of the first States to ban the gasoline oxygenate additive methyl tertiary butyl ether (MTBE) after it was detected in ground water. Ethanol, a non-petroleum product usually made from corn, is being used in place of MTBE. Gasoline with ethanol requires changes in the way gasoline is produced and distributed. Some supply dislocations and price surges occurred in the summer of 2003 as the State moved to ethanol and away from MTBE. Similar problems have also occurred as a result of other fuel transitions.



This brochure is available at:  
<http://tonto.eia.doe.gov/reports/reportsA.asp?type=other>  
For links to current gasoline prices and analyses, see:  
<http://tonto.eia.doe.gov/oog/info/gdu/gasdiesel.asp>

The Energy Information Administration is an independent statistical agency within the U.S. Department of Energy whose purpose is to provide reliable and unbiased energy information.

For further information, contact:  
National Energy Information Center  
Washington, DC 20585  
Telephone: (202) 586-8800  
E-Mail: [infoctr@eia.doe.gov](mailto:infoctr@eia.doe.gov)  
&  
EIA's Web site at:



# A Primer on Gasoline Prices



## A PRIMER ON GASOLINE PRICES

Gasoline is one of the major fuels consumed in the United States and the main product refined from crude oil. Consumption in 2007 was about 142 billion gallons, an average about 390 million gallons per day and the equivalent of about 61% of all the energy used for transportation, 44% of all petroleum consumption, and 17% of total U.S. energy consumption. About 47 barrels of gasoline are produced in U.S. refineries from every 100 barrels of oil refined to make numerous petroleum products. Most gasoline is used in cars and light trucks. It also fuels boats, recreational vehicles, and farm, construction and landscaping equipment. While gasoline is produced year-round, extra volumes are made and imported to meet higher demand in the summer. Gasoline is delivered from oil refineries mainly through pipelines to an extensive distribution chain serving about 167,500 retail gasoline stations in the United States.<sup>1</sup> There are three main grades of gasoline that are based on octane levels: regular, mid-grade, and premium. Premium grade is the most expensive; the price difference between grades is generally constant at about ten cents per gallon.

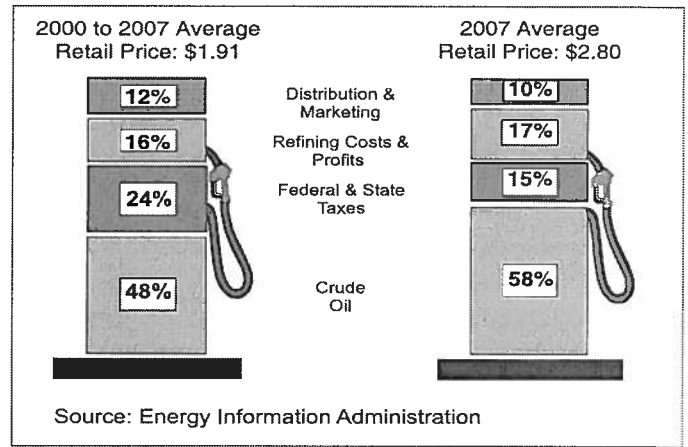
<sup>1</sup>National Petroleum News, 2007 Industry Scorecard.

### WHAT ARE THE COMPONENTS OF THE RETAIL PRICE OF GASOLINE?

The cost to produce and sell gasoline to consumers includes the cost of crude oil to refiners, the costs to refine, market and distribute the gasoline, and finally the retail station costs and taxes. Retail pump prices reflect these costs, as well as the profits (and sometimes losses) of refiners, marketers, distributors and retail station owners.

The cost of crude oil as a share of the retail price varies over time and among regions of the country. In 2007, the price of crude oil averaged about \$68 per barrel and accounted for about 58% of the national average retail price of a gallon of regular grade gasoline (Figure 1). In comparison, in 2005 the average crude oil price was \$50 per barrel and the crude oil cost was 53% of the retail price. From 2000 to 2007 the average crude oil price was about \$39 per barrel and the crude oil cost share of the retail gasoline prices averaged 48%.

Figure 1. What Do We Pay for in a Gallon of Regular Grade?



Source: Energy Information Administration

Federal, State, and local government taxes are the next largest part of the retail price of gasoline. In 2007, taxes (not including county and local taxes) accounted for about 15% of the cost of a gallon of regular gasoline. Federal excise taxes were 18.4 cents per gallon and State excise taxes averaged 21.5 cents per gallon.<sup>2</sup> Eleven States levy additional State sales and other taxes, some of which are applied to the Federal and State excise taxes. Additional county and city taxes can have a significant impact on the price of gasoline in some locations. From 2000 to 2007, taxes averaged about 24% of the retail gasoline price.

<sup>2</sup>Energy Information Administration, Petroleum Marketing Monthly, December 2007, Table EN1 at: [http://www.eia.doe.gov/pub/oil\\_gas/petroleum/data\\_publications/petroleum\\_marketing\\_monthly/historical/2007/2007\\_12/pmm\\_2007\\_12.htm](http://www.eia.doe.gov/pub/oil_gas/petroleum/data_publications/petroleum_marketing_monthly/historical/2007/2007_12/pmm_2007_12.htm)

Refining costs and profits were about 17% of the national average retail price of regular gasoline in 2007, close to the 2000 to 2007 average of 16%. This component's share varies from region to region mainly due to the different gasoline formulations required in different parts of the country.

Distribution, marketing, and retail dealer costs and profits in 2007 were 10% of the gasoline price, down from the 2000 to 2007 average of 12%. Most gasoline is shipped from the refinery first by pipeline to terminals near consuming areas, where it may be blended with other products (such as ethanol) to meet local government and market specifications, and is then delivered by tanker truck to individual stations. Some retail outlets are owned and operated by refiners, while others are

independent businesses that purchase gasoline from refiners and marketers for resale to the public. The price on the pump includes the retailer's cost to purchase the finished gasoline and the costs of operating the service station. It also reflects local market conditions and factors, such as the desirability of the location and the marketing strategy of the owner.

### WHY DO GASOLINE PRICES FLUCTUATE?

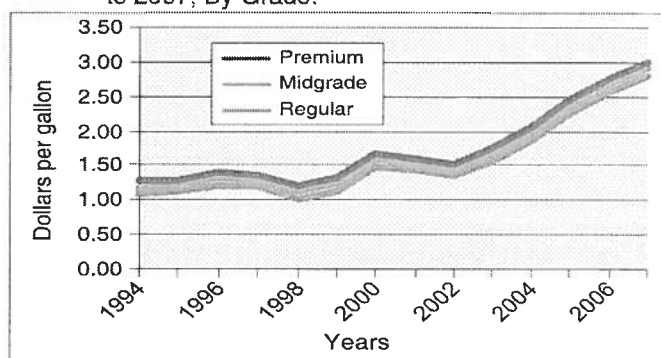
Retail gasoline prices are mainly affected by crude oil prices and the level of gasoline supply relative to demand. Strong and increasing demand for gasoline and other petroleum products in the United States and the rest of the world is exerting intense pressure on available supplies. Even when crude oil prices are stable, gasoline prices fluctuate due to seasonal demand and local retail station competition. Gasoline prices can change rapidly if something disrupts the supply of crude oil or if there are problems at refineries or with delivery pipelines.

**Seasonal demand for gasoline** - Retail gasoline prices tend to gradually rise in the spring and peak in late summer when people drive more, and then drop in the winter. Good weather and vacations cause U.S. summer gasoline demand to average about 5% higher than during the rest of the year. If crude oil prices do not change, gasoline prices typically increase by 10-20 cents from January to the summer.

**Crude oil supply and prices** - Crude oil prices are determined by worldwide supply and demand. Events in crude oil markets that caused spikes in crude oil prices were a major factor in all but one of the five major run-ups in gasoline prices between 1992 and 1997, according to the National Petroleum Council's study "U.S. Petroleum Supply - Inventory Dynamics." Rapid gasoline price increases occurred in response to crude oil shortages caused by the Arab oil embargo in 1973, the Iranian revolution in 1978, the Iran/Iraq war in 1980, and the Persian Gulf conflict in 1990. The cost of crude oil has been the main contributor to the most recent gasoline price increases. World crude oil prices reached record levels in 2007 due mainly to high worldwide oil demand relative to supply. Other factors contributing to higher crude oil prices include political events and conflicts in some major oil producing regions, as well as other factors such as the declining value of the U.S. dollar (the currency at which crude oil is traded globally).

The Organization of Petroleum Exporting Countries (OPEC) has significant influence on world oil prices because its members produce over 40% of the world's crude oil and have more than two-thirds of the world's estimated crude oil reserves. OPEC members are also the only countries that have "spare production capacity" and the ability to bring more oil into production relatively quickly. Since it was organized in 1960, OPEC has tried to keep world oil prices at a target level by setting production levels for its members.

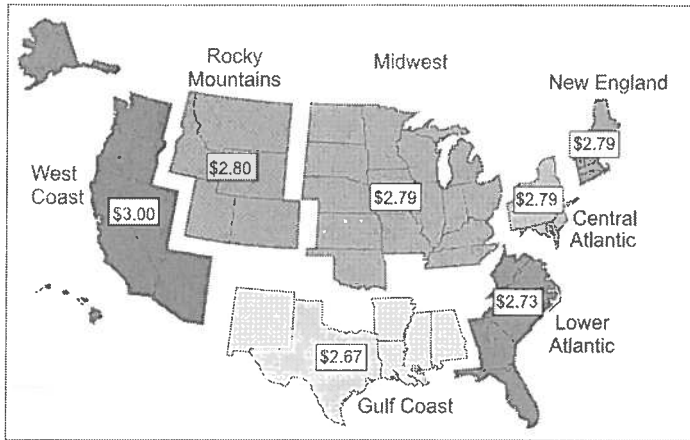
Figure 2. Average Annual U.S. Motor Gasoline Prices, 1994 to 2007, By Grade.



Source: Energy Information Administration

**Gasoline supply and demand imbalances** - Gasoline prices tend to increase as the available supply of gasoline grows smaller relative to real or expected demand or consumption. The supply of gasoline is a function of crude oil supply and refining, imports of refined gasoline, and gasoline inventories (stocks). Stocks are the cushion between major short-term supply and demand imbalances, and their levels can have a significant impact on gasoline prices. If refinery or pipeline problems and/or reductions in imports cause supplies to decline unexpectedly, gasoline inventories (stocks) may drop rapidly. This may cause wholesalers to bid higher for available supply over concern that future supplies may not be adequate. Imbalances have also occurred when a region has changed from one fuel type to another (e.g., to cleaner-burning gasoline) as refiners, distributors, and marketers adjust to the new product. Gasoline may be less expensive in one summer when supplies are plentiful vs. another summer when they are not. Prices for all commodities fluctuate, but gasoline prices are generally more volatile than prices of other goods. For example, consumers generally have options to substitute between food products when prices change but most do not have that option for fueling their vehicles.

Figure 3. 2007 Regular Grade Gasoline Prices at Retail Outlets by Region (dollars per gallon, including taxes).



Source: Energy Information Administration, EIA-878, Motor Gasoline PriceSurvey.

### WHY ARE GASOLINE PRICES HIGHER IN SOME REGIONS THAN IN OTHERS

Although price levels vary over time, Energy Information Administration (EIA) data indicate that average retail gasoline prices are often highest in certain States or regions (Figure 3). Besides taxes, there are other factors that contribute to regional and even local differences in gasoline prices:

**Distance from supply** – Retail gasoline prices tend to be higher with greater distance from the source of supply: ports, refineries, and pipeline and blending terminals. About 66% of the crude oil processed by U.S. refineries in 2007 was imported, with most transported by ocean tankers. The U.S. Gulf Coast is the source of about 40% of the gasoline produced in the United States and the starting point for most major gasoline pipelines.

**Supply disruptions** - Any event that slows or stops production of gasoline for even a short time, such as planned or unplanned refinery maintenance or the refinery shutdowns that occurred when the Hurricanes Katrina and Rita hit the Gulf Coast in 2005, can prompt bidding for available supplies. If the transportation system cannot support the flow of surplus supplies from one region to another, prices will remain comparatively high.

**Retail competition and operating costs** – Pump prices are often highest in locations with few retail gasoline stations.

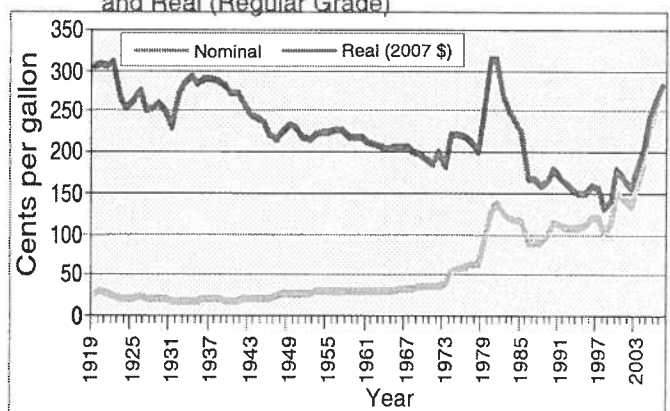
Even stations located close together may have different traffic patterns, rents, and sources of supply that influence their pricing. Drivers face a trade-off between stations with high prices and the inconvenience of driving further to find a station with lower prices.

**Environmental programs** - Some areas of the country are required to use special “reformulated” gasoline with additives to help reduce carbon monoxide, smog, and air toxics that result when gasoline is burned or when gasoline evaporates during fueling. Other environmental programs put restrictions on fuel transportation and storage. These programs tend to add to the cost of producing, storing, and distributing gasoline. About a third of the gasoline sold in the U.S. is reformulated. Each oil company prepares its own formulation to meet Federal emission standards.

### HOW DO GASOLINE PRICES IN 2007 COMPARE WITH HISTORICAL PRICES?

There are two ways to compare recent prices with historical prices. One is to compare the price actually paid at the pump or the “nominal” price. The other is to compare the “real” price, which is the price adjusted for inflation, so that prices in the past are in “today’s” dollar value. The figure below shows the average annual nominal and real prices of regular gasoline from 1919 to 2007, where the real price is based on the value of the dollar in 2007. During that period, consumers paid the highest prices for gasoline in real terms in the early 1920’s and 1980’s.

Figure 4. Historical Average Annual Gasoline Prices – Nominal and Real (Regular Grade)



Source: Energy Information Administration, Short Term Energy Outlook, January 2007.

February 2008

## **The Response of the Attorney General to House Joint Memorial 42**

The New Mexico State Legislature, during its First Session in 2007, adopted House Joint Memorial 42, "A Joint Memorial Requesting the Attorney General to Investigate the Disparity between the Price of Gasoline and Diesel Fuel" (HJM 42). In response to that Memorial, Attorney General Gary K. King directed staff to review gasoline and diesel fuel prices within the state of New Mexico and the market forces affecting those prices.

The Attorney General and his staff developed a set of questions which were submitted in June 2007 to a number of important participants in the New Mexico petroleum market. The respondents replied to the questions in late July and early August 2007. Staff then worked on development of information relating to the market forces involved in a comparison of that information to the responses submitted by the industry.

This report is the product of that work.

### THE MARKETS

The first step in understanding the perceived disparity in the prices of gasoline and diesel fuel is to understand that they are in separate markets and that their apparent price relationship is tenuous at best, despite both being derived from crude oil. Crude oil delivered to a refinery is broken up into numerous of its components. From that crude oil is derived propane, gasoline, diesel fuel, lubricants, paraffin wax, sulfur and sulfuric acid, tar, asphalt and any number of petrochemicals to be processed into other products. That these products all come from crude oil is no basis for assuming that the price to the consumer of one product should be related any more than tangentially to the price of any other product from crude oil. Rather, each of these products has its own demand from the consumer and from industry. That demand, coupled with the available supply, determines what the purchasers of the end products are willing to pay.

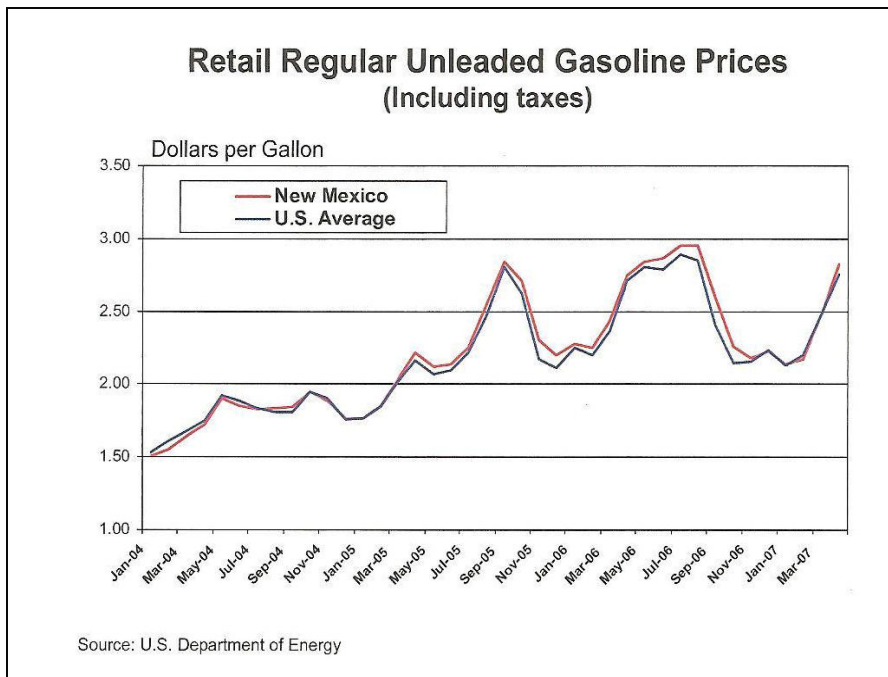
Although gasoline is used almost exclusively for operating vehicles and diesel is used, less exclusively, for operating a wide variety of vehicles, the most fundamental difference is that they are not interchangeable -- one does not operate a gasoline-driven automobile by pouring diesel fuel into it -- and therefore these two fuels do not compete directly with one another.

The other major difference was aptly noted by the Legislature in the preamble of HJM 42:

WHEREAS, the price and availability of diesel fuel is important to New Mexico as it is the primary fuel for semitrucks, delivery vehicles, buses, trains and farming construction equipment....

While both gasoline and diesel fuels are used to drive engines and equipment, the use for diesel fuel is overwhelmingly in the commercial field; similarly, the noncommercial transportation fuel of choice is virtually all gasoline. J.D. Powers & Associates found that noncommercial vehicles purchased in 2006 were 0.5% hybrid, 3% diesel and the rest gasoline fueled. In the same year, the study reports that only 12% potential new non-commercial vehicle purchasers were even considering a diesel purchase.<sup>1</sup> Staff believes it is safe to assert that these two fuels constitute separate and distinct markets for the timeframe addressed herein.

#### NATIONAL AND GLOBAL TRENDS IN THE GASOLINE AND DIESEL FUEL MARKETS



A short review of national and global trends for these two fuels is beneficial to the understanding of what is happening in those markets in New Mexico itself. As is well known, in recent years retail gasoline prices have risen in New Mexico, as well as the rest of the nation. Indeed, the New Mexico average for retail

regular unleaded gasoline has moved up and down in lockstep with the US average. See the accompanying chart.

Numerous factors affect the prices of gasoline, diesel fuel and sometimes both. Some of the most important are set forth below.

**Crude Oil Prices.** In the year since HJM 42 was promulgated, crude oil prices have nearly doubled. In January 2007 the price was \$54.35/bbl and in July \$71.41/bbl. In the last month, the price very briefly exceeded \$100/bbl before settling back to \$90.13/bbl by

<sup>1</sup> J.D. Power and Associates Press Release, "Toyota, Honda, Ford and Nissan Have the Most Models in the Top 30 of the Automotive Environmental Index", July 16, 2007.



January 18, 2008.<sup>2</sup> As HJM 42 noted, both diesel fuel and gasoline are products of crude oil.

Planned Maintenance Issues. Planned maintenance turnarounds are required for the continuing reliable operation of refineries. Turnarounds are normally planned a year or more in advance and are intentionally initiated in advance of the driving season so the refineries will be able to run at full capacity during peak demand. The US Department of Energy noted in March of 2007 that "the size and complexity of a refinery turnaround leaves little flexibility to change plans. The large commitments for labor, equipment, and materials needed for process improvements make changes very costly at best, and safety concerns can override all other considerations."<sup>3</sup> Shortages in skilled labor and delays in obtaining equipment have sometimes extended turnarounds in the last year. This factor is common to both diesel fuel and gasoline. A planned maintenance issue of major importance in 2006 was the modification of refineries to accommodate the federally-mandated switch to ultra low sulfur diesel fuel (ULSD).

Unplanned Maintenance Issues. Unplanned refinery outages in the United States disproportionately impact gasoline production, but also have adverse effects on diesel production. The 2006 changeover to ultra low sulfur diesel fuel also precipitated more unplanned maintenance issues as the refinery operators learned how to use the equipment, react to unexpected shutdowns and failures, and to adjust properly.

Ethanol. Increased blending of ethanol, with a lower BTU content than conventional gasoline, into gasoline requires that additional fuel supplies be provided to offset the fuel efficiency loss.

Global Demand. This factor particularly applies to the diesel market, but still somewhat to the gasoline market. Throughout the world, greater industrialization has resulted in a strong increase in the demand for diesel. Particularly in China, the demand for diesel fuel has risen drastically over the last decade. In the European Union, there has been a tax-driven movement that has converted much of the noncommercial fleet into ultra low sulfur diesel fuel.<sup>4</sup> This has reduced demand pressure on gasoline prices, and increased it on diesel fuel prices globally. See the accompanying chart, "Spot Gasoline Prices," on the following page.

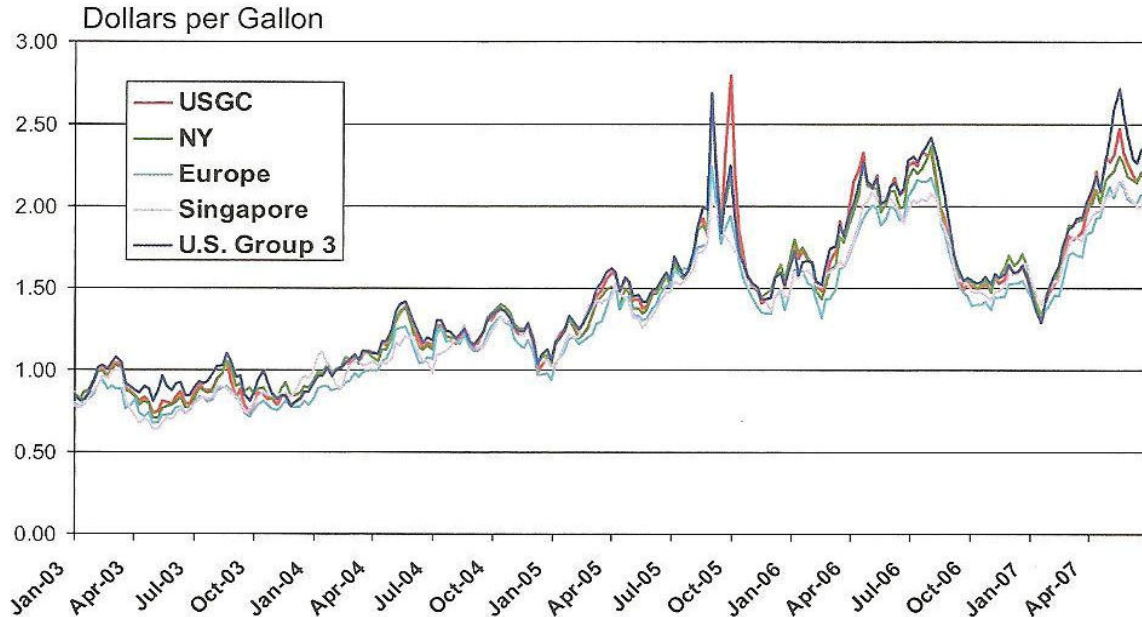
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<sup>2</sup> <http://www.wtrg.com/daily/crudeoilprice.html>. The US Federal Trade Commission in 2004 concluded that changes in crude prices account for 85% of the change in product prices over the past 20 years. US Federal Trade Commission Bureau of Economics, "The Petroleum Industry: Mergers, Structural Change and Antitrust Enforcement," August 2004, p. 1.

<sup>3</sup> US Department of Energy, Energy Information Administration, "Refinery Outages: Description and Potential Impact on Petroleum Prices," March 2007, Page v Is.

<sup>4</sup> See, e.g., "Restructuring Taxes to Protect the Environment", Bernie Fischlowitz-Roberts, Earth Policy Institute, July 25, 2002-10 (describing the effect on vehicle fleets in the United Kingdom of a tax policy strongly encouraging use of ULSD").

## Spot Gasoline Prices



Source: Platts

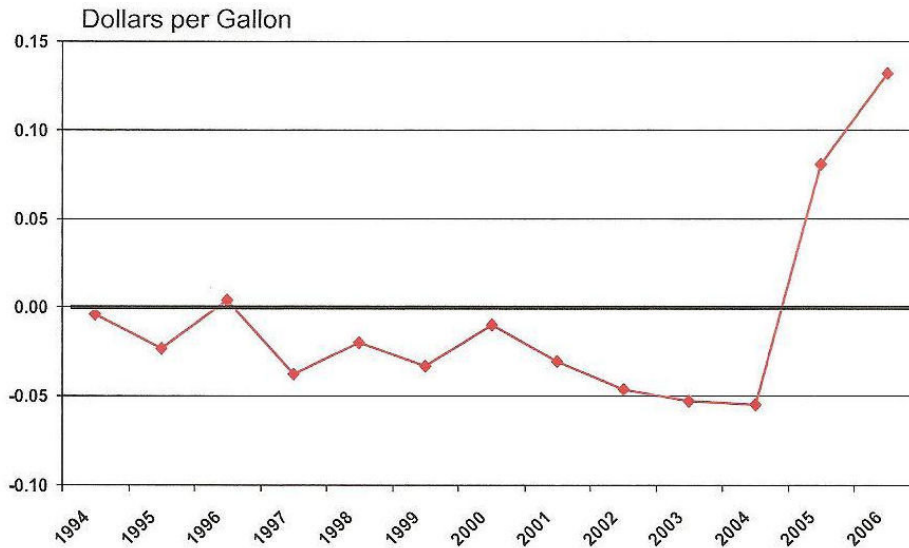
Consequently, there has been a reduction in diesel imports to the United States, which puts demand pressure to drive up the price of diesel fuel here. In addition, US restrictions on ultra low sulfur diesel fuel keep much diesel from being imported into this country. A growth in the global demand for gasoline, combined with quality restraints on imported gasoline, also led to a 7% reduction in imports to the US between mid-2006 and mid-2007, leading to somewhat increased prices for gasoline.

### GASOLINE VERSUS DIESEL PRICE TRENDS.

There has been a global and national trend towards diesel fuel prices strengthening relative to gasoline prices and a reversal is unlikely to be sustained. The chart below shows how in the major refining area of the Gulf Coast, spot prices for diesel, that have traditionally been below gasoline prices, have now risen well above the gasoline prices. One should note in particular the spike in the diesel price beginning in 2004, more than a year before Hurricane Katrina struck the Gulf Coast. By early 2006, the spot price increase had risen from a nickel less than gasoline to thirteen cents above. If one would apply this difference to the national average for regular unleaded gasoline on July 3, 2006, the expected cost per gallon of diesel fuel would be \$3.064, only 4.4% more than the cost of gasoline. Since then, of course, the demand for diesel has continued to increase in strength and the upward pressure on its price, further demonstrating that diesel

and gasoline are in separate markets and are simply responding to supply and demand market pressures for their particular purposes. The next diagram describes visually the movement of diesel prices, measured against a constant gasoline price.

### Diesel Minus Gasoline Spot Prices U.S. Gulf Coast



Source: Platts - pipeline, mid; low sulfur diesel before May 1, 2006 and ultra low sulfur diesel thereafter as mandated

The strengthening of diesel versus gasoline prices is the result of a longer-term structural change in product markets globally, within the United States, and presumably within the state of New Mexico. Diesel demand has been increasing at a faster rate than gasoline demand in recent years, due primarily to increased industrialization in China, India and elsewhere. In the United States, diesel demand growth has been strong due to robust economic growth in the use of diesel fuel to transport products that are sold in the United States. Europe has had strong diesel demand growth as a result of the tax-driven dieselization of the passenger vehicle fleet. Gasoline demand in Europe is declining as a result. Due to strong economic growth, Asia has taken a greater share of the world oil demand. It has traditionally had stronger diesel demand growth than gasoline demand growth in that diesel fuel is used in the shipment of products and for generating electricity while gasoline use is primarily for personal transport. Globally, this has resulted in the demand for diesel fuel increasing at a rate of 2.5% per year for the last 10 years, while demand for a gasoline increased only at 1.5% per year in that decade.

In some respects, one may look at this issue as a war of technology in which gasoline and diesel fuel each serve as a component of a competing technology. The stronger technology seems to be the one based on diesel fuel and, as it becomes cleaner and more efficient, more consumers, businesses and governments adopt its use. At the same time those users are giving up their gasoline-based equipment.

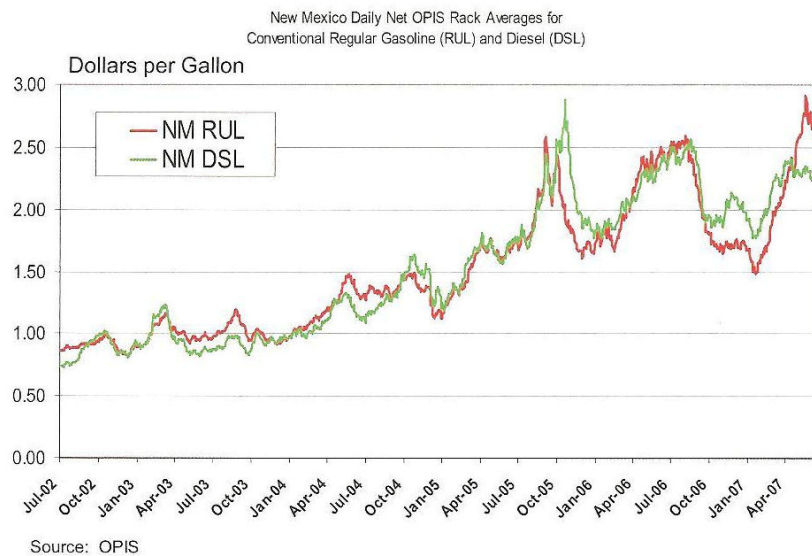
There is an additional constraint on the production of diesel in the United States. Refineries are generally configured to maximize gasoline production. The typical distillate<sup>5</sup> yield in the United States is only about 25%. To reconfigure a refinery would have two adverse effects on the production of that refinery -- first, it would take a significant amount of downtime and investment and, secondly, it would reduce the amount of gasoline available to the driving public.

Another reason for rising diesel prices is that the US and Europe have substantially lowered the sulfur content of their fuels in recent years. In addition to costing more to manufacture a lower sulfur product, other potential suppliers around the world can no longer meet US and European diesel specifications. In addition, the production of ultra low sulfur diesel can reduce the amount of diesel that can be produced from some refineries. Thus, acceptable diesel supplies are more limited and cost more than they did a few years ago.

## NEW MEXICO

Several years ago, diesel was normally somewhat lower in price per gallon than gasoline; now the situation is reversed, as costs of production and demand for diesel have increased. A good example is the contrast between the consumer retail prices, including state and federal taxes, for Conoco-Philips regular unleaded gasoline and diesel fuels in the Albuquerque market from January 2006 through the end of June 2007, as set forth in the next chart. These prices show that diesel fuel was more expensive in twenty-three of the thirty months during that period. This pattern reflects not only the pattern of price changes within the state but also within the nation.

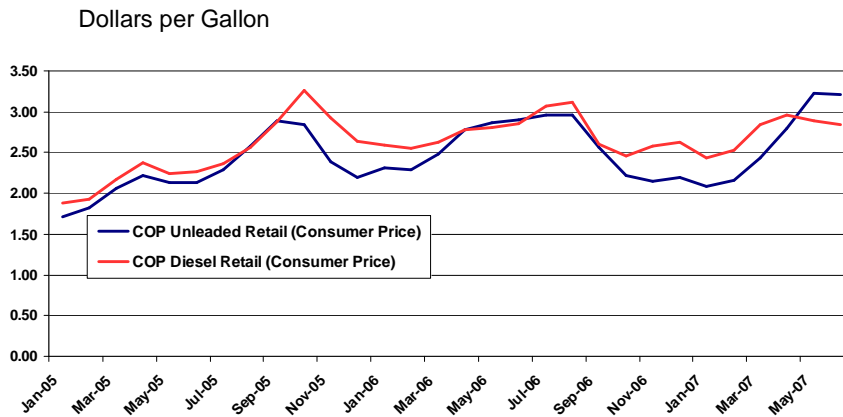
### New Mexico OPIS Rack Averages – Gasoline vs. Diesel



<sup>5</sup> "Distillates" include both diesel fuel and heating oil.

The outcome in New Mexico is shown in the rack averages of gasoline and diesel in the chart above. The chart below shows the retail consumer prices for ConocoPhillips customers in the Albuquerque area

### Albuquerque Retail Consumer Prices (Includes applicable state/federal taxes)



Source: COP Unleaded retail or COP Diesel Retail = July 2002 – March 2004 = Comets as reported by LOPS database. April 2004 – June 2007 = LOPS database

### CONCLUSION

The change in the apparent relationship between the prices of gasoline and of diesel fuel in New Mexico generally reflects similar changes in the national and global markets for the two products. A significant increase in the demand for diesel fuel globally, particularly in China and Europe, has placed steady pressure upward on the price of diesel, both here and abroad. Similarly, the lower degree of demand for gasoline has placed less pressure upon its price. (As noted above, the demand for gasoline does continue to increase in the world, but only at 60% of the rate of diesel's demand increase.)

Changed conditions in the national and New Mexico markets reflect, among other things, the governmentally-imposed stiffer sulfur standards and increasing demands from outside these two markets for diesel fuel. Those conditions include the volatility of international politics in the price and availability of significant amounts of imported crude oil. Overall, the businesses and consumers in New Mexico may expect to see diesel fuel at an increasingly higher cost compared to gasoline, which itself may continue to increase slowly.

These outcomes are the results of a growing population, the global market's increased pace of industrialization, especially in Asia, and the natural depletion of easily obtained crude oil. These factors do not suggest deliberate or malicious tinkering with the New Mexico petroleum marketplace.