

Department of Finance and Administration

Legislative Impact Statement

Bill: HB1048

Bill Subtitle: TO CONVERT THE MOTOR FUEL, DISTILLATE SPECIAL FUEL, AND LIQUEFIED GAS SPECIAL FUEL TAXES TO A PERCENTAGE OF THE SALES PRICE; TO DEDICATE EXCESS REVENUES TO THE REPAYMENT OF AMENDMENT 91 BONDS; AND TO DECLARE AN EMERGENCY.

Basic Change : Sponsor: Rep. Hendren

The bill would amend current Arkansas laws to levy Motor Fuel (Gasoline) taxes and Special Motor Fuel (Diesel, Dyed Diesel and Liquefied Petroleum Gas (LPG)) taxes based on a percentage applied to price versus the existing method of tax due per gallon. The proposal would levy tax at the rate of 10.75 % of price for Motor Fuel (Gasoline) vs. the current tax rate of \$.215 per gallon. The tax is currently reported by Arkansas licensed refineries, importers, and motor fuel distributors. Diesel fuel would be taxed at 11.25% of price vs. the current tax rate of \$.225 per gallon. The tax is reported by Arkansas licensed refineries, importers, and motor fuel suppliers.

For Dyed Diesel fuel, the tax would be levied at 3% of price vs. the current tax rate of \$.06 per gallon. The tax is reported by Arkansas licensed motor fuel suppliers and is primarily sold to farmers for use in off-road equipment. The tax is distributed to General Revenues, the Property Tax Relief Trust Fund, and the Education Adequacy Fund. Liquefied Petroleum Gas (LPG) would be taxed at 8.25% of price vs. the current tax rate of \$.165 per gallon. The current per gallon tax is reported by LPG suppliers who consume LPG from their inventory to fuel their own trucks. The proposal would continue that practice. Other users of LPG do not report the gallonage tax but pay a vehicle annual licensing fees and purchase LPG without paying a gallonage tax. The proposal would also maintain that method of taxation.

Other changes in the proposal include a change in the distribution of tax collections. After established thresholds are met, additional revenues would be used for repayment of Amendment 91 bonds. The 3% shrinkage allowance on the first 1 million gallons per month provided to motor fuel (gasoline) distributors when filing their monthly tax reports is also eliminated. Current Arkansas law provides the 3% allowance to offset losses resulting from evaporation, shrinkage, and other types of losses.

In order to comply with the International Fuel Tax Agreement and to provide additional administrative and procedural guidance, amendment to the current language for taxation based on fuel pricing is necessary. Issues include:

Motor Fuel (Gasoline) and Special Motor Fuel (Highway Use Diesel Fuel)

- The proposal does not conform to the provisions of the International Fuel Tax Agreement (IFTA) which provides for fuels taxation for interstate truckers on a per gallon basis and is due based on where fuels are used versus where the fuel is actually purchased. A per gallon tax rate must be established in order to file quarterly IFTA tax reports. IFTA requires each state to establish a tax rate per gallon in order to perform these calculations. States that levy taxes based on pricing use methods to convert the percentage tax rate to a per gallon tax rate
- The proposal does not provide direction as to the which sales transaction price is to be used when calculating taxes due – It is unclear whether the tax will be due on the sales price from the refinery / importer will be due based on the sales price from the Arkansas distributor and supplier when selling to the Arkansas retailer? Current law provides that the distributors and suppliers are the taxpayers responsible for reporting the fuel taxes to DFA. Retailers selling to consumers do not currently report the fuels taxes. Clarification should be provided.

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- The proposal does not provide a definition of sales price for purposes of the taxation. Clarification is needed regarding whether the sales price subject to tax includes the federal gallonage tax paid on the motor fuel.
- The proposal does not provide clarity for taxes due when distributors and suppliers consume fuel from their own inventory. Additional language is needed to establish the price upon which tax would be due.

The bill contains an Emergency Clause with an effective date for the legislation of July 1, 2015.

Revenue Impact :

Revenue impact resulting from a change in the method of taxation for motor fuels would be dependent on the price point (wholesale or retail) for purposes of the calculation and the specific definition of sales price to be used.

Example Calculation

Using the wholesale level fuel prices when selling to retailers as the price point for the percentage tax levy; not including the federal gallonage taxes within the definition of sales price; and using the wholesale spot petroleum prices as of January 12, 2015 on sales by fuel wholesalers to fuel retailers as provided by the U.S. Energy Information Administration reflecting gasoline at \$1.11 per gallon; diesel at \$1.48 per gallon; and LPG at \$.45 and applying those price points to the FY2014 annual fuel consumption, taxation would be impacted as follows:

Gasoline

FY2014 Arkansas taxable gasoline gallons - 1,381,734,019
Tax due at \$.215 per gallon - \$297.1 million
Tax due at 10.75% of wholesale price - \$167.6 million
Reduced Tax - \$129.5 million

Diesel

FY2014 Arkansas taxable diesel gallons - 553,696,100
Tax due at \$.225 per gallon - \$124.6 million
Tax Due at 11.25% of wholesale price - \$92.2 million
Reduced Tax - \$32.4 million

Liquid Propane Gas (LPG)

FY2014 Arkansas taxable LPG gallons - 75,175
Tax due at \$.165 per gallon - \$12,400
Tax due at 8.25 % of wholesale price - \$2,800
Reduced Tax - \$9,600

Dyed (Off-Road) Diesel

FY2014 Arkansas taxable dyed diesel gallons - 209,831,058

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Tax due at \$.06 per gallon - \$12.5 million

Tax due at 3% of wholesale price - \$9.3 million

Reduced Tax - \$3.3 million

An actual impact statement cannot be prepared with accuracy with no absolute knowledge of future fuel prices.

Taxpayer Impact :

Changes in the proprietary computer systems currently used by Arkansas distributors and suppliers to file their monthly electronic tax schedules and reports with DFA will require modification to add features to allow for taxation by price. Gasoline wholesale distributors would no longer receive the 3% allowance on the 1st million gallons of gasoline sold each month. This will increase the tax paid by fuel distributors by as much as \$77,400 annually.

Resources Required :

Computer systems changes will require additional, unanticipated budgetary resources for DFA in order to modify the existing computer AIRS tax system. Project estimate costs for systems requirements gathering, development and programming and final testing totals \$259,000.00. DFA computer system modifications can be completed by January 1, 2016 if additional budget allocations are available.

Time Required :

An effective date of January 1, 2016 is needed to comply with the required changes.

Procedural Changes :

DFA will develop new guidelines in order for taxpayers reporting the fuels taxes to modify their Electronic Data Interchange (EDI) computer software used by taxpayers to report and remit taxes. New rules may be required and DFA staff personnel would be trained of the change in filing method and procedures.

Other Comments :

The Petroleum Environmental Fee (PEF) is a fee collected for environmental cleanup involving any type of petroleum received, shipped, and stored within the State. This fee is collected on a per gallon basis and reported by fuel distributors and suppliers on their monthly tax reports. The Fee would not be changed by the proposal.

Legal Analysis :

Motor Fuel taxes are currently collected by on a gallonage basis – the tax is applied per gallon of fuel at a set rate. Additionally, revenue from motor fuel taxes can be pledged as part of a GARVEE bond program in anticipation of future federal funds to underwrite highway and transportation construction projects. HB1048 would change the method of taxation for gasoline, diesel fuel, farm and off-road diesel and LP gas.

HB1048 would conflict with The International Fuel Tax Agreement (IFTA), codified in Ark. Code Ann. § 26-55-1102. IFTA is a tax collection agreement between all states and 10 Canadian provinces. IFTA's purpose is to report motor fuel use taxes imposed by each jurisdiction on the consumption of motor fuel in qualified motor vehicles, generally commercial trucks. Membership in IFTA ensures Arkansas collects tax revenue from other states when commercial trucks use Arkansas

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roads but do not buy motor fuel in Arkansas. Modifying the tax of motor fuel from gallonage taxes to gross receipts taxes would disrupt the uniform administration of IFTA, which will create a compliance issue for Arkansas. Complying with IFTA requires the tax assessment to be based on miles traveled and gallons of fuel purchased and consumed by qualified vehicles. Removing the gallonage component of the tax computation would conflict with the requirements of how IFTA taxes are to be assessed, collected, and audited. Non-compliance with IFTA could result in expulsion pursuant to Article XV of IFTA. Expulsion would result in loss of tax revenue submitted to Arkansas from other states and Canada. Expulsion would also negatively impact the trucking industry of Arkansas and interstate commerce. With regards to IFTA, this bill is problematic in two areas:

- (1) IFTA reporting requires a gallonage based reporting standard. To further comply with IFTA, a gross receipts based motor fuel tax must be converted to a gallonage equivalent and updated periodically.
- (2) Compliance with the IFTA under a gross receipts standard could require significant regulatory increases. Every vendor of distillate special fuel would be required to have an account with the DFA on the Distillate Special Fuel tax which would also require additional employees and appropriations to administer the program.

The provisions limiting the motor fuel tax revenue that may be credited to the Arkansas Highway Revenue Distribution Law reduce the amount distributed in Ark. Code Ann. § 27-70-206(1) to the State Central Services/Constitutional Officers Fund in Ark. Code Ann. § 19-5-205 used to fund the General Assembly, the Governor's Office and other Constitutional Officers.

HB1048 maintains a specific dollar amount pledged for existing bonds under Ark. Code Ann. §§ 27-64-101 through -514 despite changing the taxes to gross receipts based calculations. The proportion of tax revenue available will fluctuate with the amount of the tax without any guarantee that the pledged amount will be maintained if the retail price of motor fuel continues to drop.

Additionally, DFA is required by Amendment 91 to the Arkansas Constitution to designate \$.01 per gallon of revenue in the Arkansas Highway Revenue Distribution Act for the State Aid Street Fund in Ark. Code Ann. § 27-70-207(e). Additional administrative burdens are created by changing the motor fuels taxes to gross receipts while being constitutionally required to designate a gallonage based amount to the State Aid Street Fund.

Section 20 contains a drafting error where it reads "The refund for purchases of distillate special fuel tax shall does not include . . ." Page 16, Lines 1-2. The Section is likely meant to read, "The refund for purchases of distillate special fuel tax ~~shall~~ does not include . . ."

HB1048 repeals the provisions of Arkansas law allowing for GARVEE bonds, Ark. Code Ann. §§ 27-64-205, -305, -405, and -605. It is unclear why GARVEE bonds would be repealed and no mention of this is in the title or emergency clause of the bill. HB1048 would leave only Amendment 91 bonds available for funding highway and transportation bond issues.

The Emergency Clause for HB1048 would make the effective date July 1, 2015. The additional regulatory requirements may not be able to be in place by July 1, 2015 as described above.