

Department of Finance and Administration

Legislative Impact Statement

Bill: HB1259

Bill Subtitle: TO CREATE A SALES AND USE TAX EXEMPTION FOR PARTS FOR AND REPAIR OF AGRICULTURAL EQUIPMENT AND MACHINERY.

Basic Change : Sponsor: Representative Jett

The bill provides a sales and use tax exemption for repair and replacement parts and repair services used to repair agricultural machinery and equipment used in commercial agricultural production in Arkansas. The exemption would be effective on the first day of the calendar quarter following the effective date of the act. (Revenue Impact calculated assuming October 1, 2015 effective date.)

Revenue Impact :

FY16 Tax Decrease

Total Impact to State Revenues - \$11.6 million
[8 Months of Reduced Tax Collections -- 10/1/2015 Effective Date]

- \$ 7.8 million --- State General Revenue (4.5%)
- \$ 1.5 million --- Educational Adequacy (.875% tax)
- \$.9 million --- Property Tax Relief Trust Fund (.5%)
- \$.2 million --- Conservation Tax (.125%)
- \$.9 million --- Highway Fund (.5%)
- \$ 0 million --- Educational Excellence Trust Fund
- \$ 0 million --- Educational Adequacy (GR transfer)
- \$.3 million --- State Central Services
- \$.1 million --- Constitutional Officers

Total Loss to City and County Sales Taxes - \$5.4 million

FY17 Tax Decrease

Total Impact to State Revenues - \$17.7 million

- \$ 10.1 million --- State General Revenue (4.5%)
- \$ 2.3 million --- Educational Adequacy (.875% tax)
- \$ 1.3 million --- Property Tax Relief Trust Fund (.5%)
- \$.3 million --- Conservation Tax (.125%)
- \$ 1.3 million --- Highway Fund (.5%)
- \$ 1.6 million --- Educational Excellence Trust Fund
- \$.1 million --- Educational Adequacy (GR transfer)
- \$.3 million --- State Central Services
- \$.1 million --- Constitutional Officers

Total Loss to City and County Sales Taxes - \$5.5 million

Taxpayer Impact :

Sellers would discontinue collection of sales tax on sales of repair and replacement parts used to repair farm machinery and equipment and repair services for such equipment by purchasers using the equipment in commercial agricultural production. Sellers would change their accounting and tax collection systems and processes to provide the tax exemption and to maintain records to substantiate their exempted sales to maintain records to substantiate the exemptions they granted.

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Resources Required :

No resources will be required if the exemption is fully administered by sellers of these products and services. The purchaser would have to substantiate to the seller that they were entitled to the exemption and the seller would maintain the records for future audit. Limited resources may be required if Arkansas registers commercial farmers and provides an exemption certificate and number for the farmer to present to the seller when purchasing their exempt products and services.

Time Required :

Adequate time is provided for implementation unless registration of commercial farmers is required. To register the Arkansas commercial farmers, a January 1, 2016 or July 1, 2016 effective date would be required.

Procedural Changes :

Education of taxpayers and DFA staff regarding enactment of the sales and use tax exemption. Modification of Sales Tax Rules will be required and possible farmer registrations

Other Comments :

The proposal does not provide definitions for agricultural machinery and equipment and for repair and replacement parts. Under Ark. Code Ann. § 26-52-403, the exemption for farm machinery and equipment is limited to implements used exclusively and directly in farming. Farming is further defined as the agricultural production of food or fiber as a business. This proposal does not limit the exemption for repairs and replacement parts to the same farm machinery and equipment exempt under §26-52-403.

Specific definitions for repair and replacement parts is necessary. Items such as motor oil, grease, and lubricants, replacement oil and air filters, tires, batteries, belts, and sparkplugs could be considered maintenance items and subject to tax versus replacements and entitled to exemption.

The proposal would exempt sales of repairs and services for the equipment that is used in commercial agricultural production in Arkansas only. Out-of-state purchasers would continue to pay tax on the repairs and services they purchase from Arkansas sellers. Treating out-of-state purchasers in a different manner than Arkansas purchasers would have constitutional concerns, would be problematic for sellers in making a determination of state of residence for exemption purposes, and would create a different tax base dependent on the purchaser's state of residence which would violate the provisions of the Streamlined Sales Tax Agreement. The proposal should be amended to remove the requirement that the exemption only applies for repairs of equipment that is used in Arkansas.

With a broad range of products and services that would be subject to the exemption, sellers may need clear documentation presented by the purchaser to substantiate their exemption claim. Depending on the definition established for the eligible parts and services subject to exemption, companies such as discount stores, auto parts suppliers, tire retailers, engine repair service providers, and many other types of retailers will be administering a sales tax exemption for farm related repair and replacement purchases for the first time. A purchaser providing a state issued exemption certificate would assist the retailer in properly determining if a sale is exempt. Neighboring states of Tennessee, Missouri, Oklahoma, Texas and Louisiana require exempt farm purchasers to present a state issued certificate to claim exemptions.

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Legal Analysis :

Under current law, repair and replacement parts and labor do not qualify for the farm equipment and machinery sales tax exemption. This bill establishes a broad exemption that reaches beyond repair and replacement parts and labor. The exemption for parts also includes parts purchased to modify a piece of farm equipment or machinery. The exemption for labor also includes initial installation, alteration, addition, cleaning and refinishing of farm equipment or machinery.

The bill has no emergency clause and will become effective on the first day of the calendar quarter following the effective date of this act.