

Department of Finance and Administration

Legislative Impact Statement

Bill: HB1263

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

HB1263 would provide a state and local 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 bill would be effective on the first day of the calendar quarter following the effective date of this act.

Revenue Impact :

FY18 Tax Decrease

Total Impact to State Revenues **- \$12.6 million**
[8 Months of Reduced Tax Collections -- 10/01/2017 Effective Date]
-\$ 8.4 million --- State General Revenue (4.5%)
-\$ 1.6 million --- Educational Adequacy (.875% tax)
-\$ 1.0 million --- Property Tax Relief Trust Fund (.5%)
-\$.2 million --- Conservation Tax (.125%)
-\$ 1.0 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 **- \$4.4 million**

FY19 Tax Decrease

Total Impact to State Revenues **- \$19.4 million**
-\$ 11.7 million --- State General Revenue (4.5%)
-\$ 2.5 million --- Educational Adequacy (.875% tax)
-\$ 1.4 million --- Property Tax Relief Trust Fund (.5%)
-\$.4 million --- Conservation Tax (.125%)
-\$ 1.4 million --- Highway Fund (.5%)
-\$ 1.2 million --- Educational Excellence Trust Fund
-\$.1 million --- Educational Adequacy (GR transfer)
-\$.4 million --- State Central Services
-\$.2 million --- Constitutional Officers
Total Loss to City and County Sales Taxes **- \$6.7 million**

Taxpayer Impact :

Sellers would discontinue collection of state and local 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 be required to maintain records to substantiate their exempted sales.

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Resources Required :

None.

Time Required :

Adequate time is provided for implementation.

Procedural Changes :

None.

Other Comments :

None.

Legal Analysis :

HB1263 creates an exemption from gross receipts tax for tangible personal property purchased to modify or repair agricultural machinery and for the service of installing, altering, adding, cleaning, refinishing, replacing, or repairing agricultural equipment. The bill does not provide definitions for "agricultural machinery and equipment" and for "repair and replacement parts" and the chapter under which the new section will be contained has no definition for agricultural machinery and equipment. Under § 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.

Because the bill does not define "agricultural machinery and equipment", it is unclear what will be encompassed by the exemption. For example, "agriculture" could include timber harvesting, which has traditionally been excluded from the definition of "farm equipment." Pursuant to § 26-52-431(c), the purchase of repair or replacement parts for timber machinery are specifically not exempt from collection of gross receipts tax. If timber harvesting is considered agriculture, then HB1263 could conflict with § 26-52-431(c).

Specific definitions for "repair and replacement parts" is also necessary. Items such as motor oil, grease, 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. There is also no specific definition of "aviation machinery and equipment." Without a specific definition, this term could include aircraft, drones, flight navigation equipment, geographical information systems (GIS), flow controls, real time meteorological systems, and precision-calibrated spray equipment.

The bill 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

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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. It is recommended the bill 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.