

# Department of Finance and Administration

## Legislative Impact Statement

**Bill: SB261**

**Bill Subtitle: TO PROVIDE A SALES AND USE TAX EXEMPTION FOR TIMBER MACHINERY AND EQUIPMENT.**

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### Basic Change :

**Sponsor: Sen. Garner**

SB261 would add an additional section, § 26-52-452, to Arkansas sales and use tax code provisions to provide an exemption for "timber machinery and equipment" when sold to a "member of the timber industry". A "member of the timber industry" is defined to be a person who is engaged primarily in the commercial production, harvesting, or processing of timber. The current sales tax exemption for "timber harvesting machinery and equipment" as provided in § 26-52-431 is not amended by the bill and is not included within the definition of "timber machinery and equipment".

To be exempt from tax as "timber machinery and equipment", the implements purchased must be used exclusively in the production, harvesting and processing of timber. Included without limitation within the types of machinery and equipment eligible for the exemption are "all-terrain vehicles".

Members of the timber industry would claim the sales tax exemption at the time of purchase from the retailer on all eligible implements except for purchases of all-terrain vehicles. To claim the exemption for all-terrain vehicles, the purchaser would pay the tax to the retailer and subsequently file a claim for a tax rebate from the Department of Finance and Administration (DFA).

The act would be effective on the first day of the calendar quarter following the effective date of the act (October 1, 2019).

### Revenue Impact :

Unable to determine impact to State General Revenues .

SB261 provides a sales and use tax exemption for all machinery and equipment purchased by "members of the timber industry" for use in the "commercial production, harvesting, or processing of timber". Definitions are not provided in the bill for these terms. Arkansas timber production and related industrial manufacturing of timber is significant and additional clarity would be necessary to determine revenue impact of the proposal.

### Taxpayer Impact :

Taxpayers who are "members of the timber industry" as defined in the bill and engaged primarily in the commercial production, harvesting, or processing of timber will be eligible for sales and use tax exemption on purchases of machinery and equipment. If purchasing an eligible all-terrain vehicle, the taxpayer would file a claim for a state and local sales tax rebate from DFA.

Taxpayers currently eligible for the exemption for "timber harvesting machinery and equipment" and the exemption for "manufacturing machinery and equipment" may be eligible for additional sales tax exemptions.

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### **Resources Required :**

DFA would require one additional accountant and one additional auditor – Accountant II GS08, Auditor II GS09 -- \$120,000 annually in salary and matching; supplies, equipment, postage, etc. -- \$25,000 annually. In order to issue state and local sales tax rebates, it will be necessary to provide necessary taxpayer support in initiating the process; register all taxpayers submitting claims; review all claims and taxpayer submitted copies of invoices, documents and forms; conduct an audit to determine eligibility, accuracy and correctness of the claim and the state and local tax calculations; prepare and post an audit report to the DFA tax processing system; and request authorization for issuance of a tax rebate payment through the State Treasurer.

### **Time Required :**

Time would be needed to develop rebate forms as well as a mechanism for receiving the new rebates within the State's database.

### **Procedural Changes :**

Updates to the sales tax rules will need to be promulgated.

### **Other Comments :**

"Timber machinery and equipment" include all-terrain vehicles if the vehicle is used exclusively in the production, harvesting or processing timber. It is not clear how an all-terrain vehicle would be utilized in producing, harvesting or processing timber. If the intent of the bill is to exempt all-terrain vehicles used as a transportation device while a person is actively producing, harvesting or processing timber, a specific exemption reflecting this specific fact may be preferred language for the bill.

The bill provides an exemption for timber machinery and equipment used exclusively by persons producing, harvesting and processing timber. Manufacturers who process timber into lumber, paper products, plywood, etc. may have machinery and equipment that is not currently exempt under the "manufacturers exemption" of § 26-52-402 that may become eligible for exemption as "timber machinery and equipment".

The bill provides a sales tax exemption if the machinery and equipment is used exclusively in timber production, harvesting, or processing. The bill does not require the machinery and equipment to be used "directly" in timber producing, harvesting, and processing. Other sales tax exemptions for machinery and equipment and used by Arkansas industrial manufacturers and in commercial farm production require "direct use".

The current sales tax exemption for "timber harvesting machinery and equipment" only applies to complete systems or units of machinery that operate exclusively and directly in harvesting. The exemption provided in the bill may expand on eligible exempt items when purchased for use while timber harvesting.

It is not clear if off-road use motorized vehicles, trucks, trailers, or other self-propelled off-road

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machines and vehicles, other than the specific ATVs of the size and features referenced in the bill, would be eligible "timber machinery and equipment" for purposes of the sales tax exemption. If the intent of the bill is to exclude other types of off-road motorized vehicles, trucks, trailers, etc. from the exemption, amending language may be recommended to add or exclude this type of machinery and equipment.

Under current law, § 26-52-431 provides a definition as to the type of activity that is considered "harvesting of timber". The bill does not provide similar language to provide that meaning. It may be recommended that similar language be provided in the bill.

The bill also does not provide a definition for the term "implements" in reference to the meaning of this term in relation to the timber industry. It may be recommended that the bill be amended to include a specific definition to provide guidance as to the use of this term when determining which types of products and items that will eligible for exemption as "timber machinery and equipment".

The bill also does not provide definitions for the terms "production" and "processing" in reference to the meaning of these terms in relation to the timber industry. It may be recommended that the bill be amended to provide specific definitions to include the types of activities being performed that are being referenced by the use of these terms and which will result in the eligibility for the sales tax exemption.

The bill provides an exemption for timber machinery and equipment used exclusively by persons producing, harvesting and processing timber. The bill does not provide definitions for the terms "producing" "harvesting" or "processing" in order to determine the types of business activities for which machinery and equipment may be purchased exempt from sales tax.

### Legal Analysis :

This bill creates a sales and use tax exemption for certain timber equipment and machinery purchased by a "member of the timber industry" in the "producing, harvesting, and producing" of timber. This bill specifically provides for a person engaged in the timber industry to obtain an all-terrain vehicle exempt from sales and use tax. The bill provides that the exemption on the all-terrain vehicles will be administered as a rebate. This bill removes from its definition of "timber machinery and equipment" any machinery and equipment exempted by § 26-52-431.

An exemption for timber harvesting already exists at § 26-52-431. That section exempts the sale of machinery, new and used equipment, and related attachments sold to or used by a person engaged primarily in the harvesting of timber. The section requires that the machinery and equipment be used exclusively and directly in the harvesting of timber and provides specific definitions for "equipment," "machinery," "harvesting of timber," "off-road equipment," and "primary activity." This bill appears to mirror some language from § 26-52-431 and specifically references that section. It is unclear how the exemption in this bill will work in concert and be administered with § 26-52-431.

SB261 presents several issues for administration of the exemption. First, the bill provides no definitions for key terms, including "primary activity," "implements," "producing," "harvesting," and "processing." Without these definitions, it is unclear what types of machinery equipment will be exempted and who will be entitled to claim the exemption. As currently drafted, this bill may allow for wide exemptions on behalf of manufacturers who "process" timber into a final form. This may allow for these manufacturers

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to take exemptions in addition to those provided by the manufacturing exemptions currently allowed by law.

The bill does not provide a requirement for the exempted machinery to be used directly in the production, harvesting, and processing of timber. A “direct use” requirement is reflected in the existing sales and use tax exemptions for agriculture, timber harvesting, and manufacturing. Lack of a “direct” requirement will exempt items that may only be used tangentially in timber production, harvesting, and processing of timber.

Finally, the specific allowance for all-terrain vehicles causes confusion with the bill’s intent and application. The bill provides that timber machinery and equipment are “implements used exclusively in the production, harvesting, or processing of timber” and then provides that the definition includes, without limitation, all-terrain vehicles. It is unclear how an all-terrain vehicle would meet the definition of timber machinery and equipment as it is typically used for transportation and not exclusively in production, harvesting, or processing of timber.