EXHIBIT C

Arkansas Excise Taxes

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About ITEP

The Institute on Taxation and Economic Policy (ITEP)

Non-profit

Non-partisan research organization

Federal, state, and local tax policy issues

Mission:

Ensure elected officials, media, and general public have access to accurate, timely, and straightforward information that allows them to understand the effects of current and proposed tax policies with an emphasis on taxincidence analysis.



Overview

About Excise Taxes

Excise Tax Stats in Arkansas

• Trends: Cigarette, Soda

• Major Opportunity for Reform: Gas Tax



Excise Taxes 101

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How They Work

• Sales taxes that apply to particular products (tobacco, alcohol, gasoline)

• Usually applied on a per-unit basis instead of as a percentage of purchase price (per pack cigarettes, per gallon of gasoline)



How They Work

- Tend to be less visible than general sales taxes since not itemized on consumer receipts; generally reflected in sticker price
- Every state levies excise taxes on tobacco, alcohol, and gasoline

• Assumption: consumers of these products are not similar to other consumers, and are thus deserving of differential treatment under the tax law



• Reason 1: Discourage consumption of different types of products deemed to be harmful to individuals and society ("sin taxes")



• Reason 2: Correct for the failure of negative externalities that result from the consumption of certain types of products



• Reason 3: Proxy for a user fee (e.g., gas tax)

Regressivity

- Sales taxes inherently regressive because the lower a family's income, the more of its income the family must spend on things subject to the tax
- Excise taxes often even more regressive than general sales taxes because taxes paid on units sold rather than purchase price, so same amount of the tax is due whether consumer is purchasing premium alcohol and cigarettes or much lowercost versions of these same products



Sustainability

- o Grow very slowly, which makes them an inadequate source of revenue over the long run
 - Can be a politically expedient option for shoring up budgets in the short term
- o Sources of Instability
 - × Per-unit rates don't adjust with inflation. As inflation erodes flat value of the tax, state's ability to provide a consistent level of services suffers
 - Declining consumption of goods subject to excise taxes



- Both can be mitigated, but not eliminated
 - o Switch to a percentage-based tax instead of tax per unit for less volatile goods (e.g., cigarettes and alcohol)
 - o Index tax per unit rate for inflation for more volatile goods or build in mechanisms for regular adjustments (e.g., gas)
 - Rely on low-income tax credits to offset the effects of excise taxes on individuals least able to afford them (e.g., EITC)





o Regressive and unsustainable nature make them weaker taxes that shouldn't be relied too heavily upon

Excise Taxes in Arkansas

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General Stats

- Major Excise Taxes in Arkansas:
 - oGasoline Tax
 - oCigarette Tax
 - oTaxes on Insurance Premiums
 - oAlcohol and Soda Taxes
 - oPublic Utility Taxes



General Stats

- Selective sales and excise taxes as a share of total state and local tax revenues
 - 8.8% compared to 7.8% national average (13% higher)
- Selective sales and excise taxes as a share of personal income compared to national average
 - ×1.3% compared to 1.2% (9% higher)



Incidence of Arkansas Excise Taxes

Regressivity

Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
Income Range	Less than	\$16,000 -	\$28,000 -	\$47,000 -	\$75,000 -	\$155,000 -	\$357,000
	\$16,000	\$28,000	\$47,000	\$75,000	\$155,000	\$357,000	or more
Average Income in Group	\$9,600	\$22,600	\$36,500	\$58,200	\$99,900	\$209,800	\$909,100
Sales & Excise Taxes	9.2%	8.8%	7.5%	5.8%	4.5%	2.7%	1.3%
General Sales—Individuals	5.2%	5.2%	4.7%	3.6%	2.9%	1.8%	1.0%
Other Sales & Excise—Ind.	1.8%	1.4%	1.0%	0.8%	0.5%	0.3%	0.1%

Incidence of Arkansas Excise Taxes

ARKANSAS STATE & LOCAL SALES & EXCISE TAXES AS A SHARE OF INCOME



Trends: Cigarettes & Soda

Cigarette Taxes

About

- O Historically easier for lawmakers to raise compared to broad-based taxes like sales or income tax
- o Nearly every state has enacted an increase since 2002
- o Various motivations: fund health care, discourage smoking, raise state and local revenue



Cons of Cigarette Taxes

- Regressivity
 - Cigarette taxes fall disproportionately on lowincome taxpayers
 - Fixed amount of tax on a pack of cigarettes represents a larger share of income for low-income smokers
 - O Prevalence of smoking is higher among individuals living below the poverty line



Cons of Cigarette Taxes

- Sustainability: Declining Tax
 - o Flat-per-pack tax
 - o Smoking rate has been in decline for decades
 - o Substitution effects with e-cigarettes and "vaping"
 - o Tax evasion and smuggling



Pros of Cigarette Tax

- Relatively stable revenue source that can be a supplemental source of funding to serve short-term needs
- Health benefits
 - O Deters smoking particularly among children and young adults
 - O Long-term health benefits
 - ▼Impacts medical costs, worker productivity



Soda Taxes

- Increased activity around/interest in taxing sugar consumption
- Can generate meaningful revenues for public services
- Similar cons as cigarette taxes:
 - o Regressive
 - o Sustainability



Opportunity for Reform: Gas Tax

Arkansas Gas Tax

• Single most important source of transportation revenue under the control of state lawmakers

• Challenge: State's motor fuel taxes have been falling increasingly short of meeting infrastructure needs



Erosion of the Gas Tax

As designed, unsustainable revenue source
Flat rates

Arkansas Motor Fuel Tax Rates					
Gasoline	.215 per gallon				
Clear Diesel	.225 per gallon				
Biodiesel Mixture*	.225 per gallon				
Gasohol	.215 per gallon				
Liquid Petroleum Gas (LPG)	.165 per gallon				
Natural Gas (CNG)	.05 per gallon				
Ethanol/Methanol	.215 per gallon				
Petroleum Environmental Fee **	.003 per gallon				
Arkansas Excise Tax Rate					
Dyed Diesel	.06 per gallon				

Erosion of the Gas Tax

- As designed, unsustainable revenue source
 - o Construction cost inflation
 - Costs of asphalt, concrete and machinery grow almost constantly
 - Construction costs are 66.6% higher than in 2000.
 - A \$5M project in 2000 costs \$8.3M in 2016
 - ▼ Rising construction costs put additional strain on whatever revenue is being raised



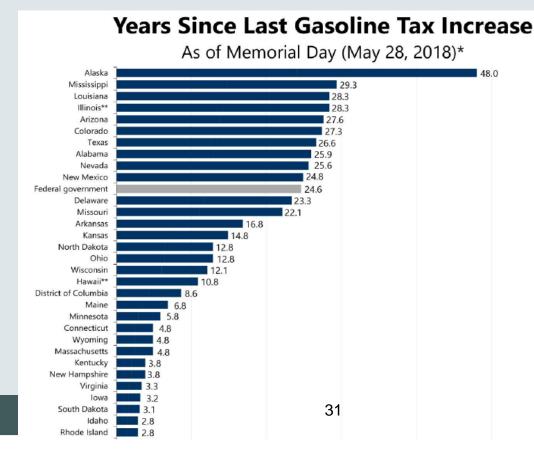
Erosion of the Gas Tax

- As designed, unsustainable revenue source
 - o Fuel Efficiency
 - × Has been on the rise since 2004
 - ▼ Travel further on each tank of gas; extra miles essentially tax-free relative to what drivers had previously been paying
 - O Positive development overall, but creates undeniable problem for the gas tax



It's Time!

• As of Memorial Day 2018, it has been 16.8 years since Arkansas adjusted its gas tax





Cost in Lost Revenue

- If AR had reformed its gas tax to grow alongside construction costs the last time lawmakers raised the tax, the state would be bringing in \$422 million in additional gas tax revenue every year
- To put it another way, the purchasing power of Arkansas's gas tax has been cut roughly in half by two entirely predictable developments: inflation and improving vehicle fuel efficiency

Responses: Wait on Gas Tax Reform

- Retain status quo re: gas tax and either don't fund or look to other revenue sources to address infrastructure needs
- Consequences
 - Continue to have an inadequate budget to repair and expand economically vital transportation infrastructure
 - Structurally deficient or obsolete bridges
 - Poor or mediocre condition of major roads
 - Congestion on major urban highways
 - Lack of access to bus or rail transit
 - ▼ Travel delays
 - Increased vehicle operating costs



Responses: Short-Term Fix

• First and most obvious step: Reverse losses in gas tax purchasing power by increasing gas tax rate

• \$422 million on the table

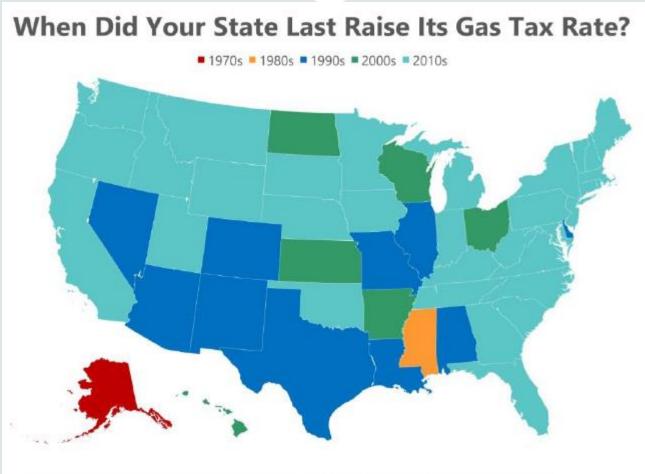


Cost in Lost Revenue

- If AR had reformed its gas tax to grow alongside construction costs the last time lawmakers raised the tax,
 - Gasoline tax rate would grown over time from 21.5 cent per gallon to 42.0 cents per gallon
 - O Diesel tax rate would have grown over time from 22.5 to 43.9 cents per gallon
- Increases of this size would result in an above-average gas tax rate, but not the highest in the country.
 - o Fairly close to rates in Indiana and Michigan
 - o Lower than CA, HI, NJ, NY, PA, and WA



It's Time!



Source: Institute on Taxation and Economic Policy, May 2018. Reflects year in which gasoline tax increase took effect.

Responses: Long-Term Fix

• Fix past problems by raising gas tax rate and plan for the future by opting for smarter, variable gas tax structures that will raise sustainable gas tax revenues for the long haul

• Restructuring state gas tax rates so that they grow over time can help alleviate the challenges posed by increases in fuel efficiency and construction costs

Options for Variable Gas Tax Rates

- Restructuring gas tax rates can come in a variety of forms
- Currently, there are more than half a dozen broad types of economic measures used in variable-rate formulas across the country
 - Fuel prices, energy prices, inflation, personal income growth, population growth, vehicle fuel-efficiency, revenue targets, and legislative spending decisions



Options for Variable Gas Tax Rates

- Indexing options:
 - O Link the gas rate to transportation cost growth
 - The most direct route for ensuring that increases in the price of asphalt, machinery, and other transportation inputs do not prevent states from adequately maintaining their transportation networks.
 - o Link the gas rate to the Consumer Price Index (CPI)
 - * Rate of growth in the price of items purchased by a typical consumer.
 - Improvement over a fixed rate, but can be inadequate in years where growth in cost of transportation inputs exceeds that of other goods (as it did throughout most of the 2000s).



Options for Variable Gas Tax Rates

- Indexing options, cont'd:
 - o Link the gas rate to the price of gasoline
 - More familiar to and comfortable for lawmakers since resembles sales tax, but highly volatile.
 - ➤ Several states have abandoned this approach or intervened in order to ensure there isn't dramatic rising and falling.
 - ➤ Options for offsetting volatility:
 - Link to average price over previous 12 months instead of price at the pump
 - Limit maximum rate changes
 - Impose floors or ceilings



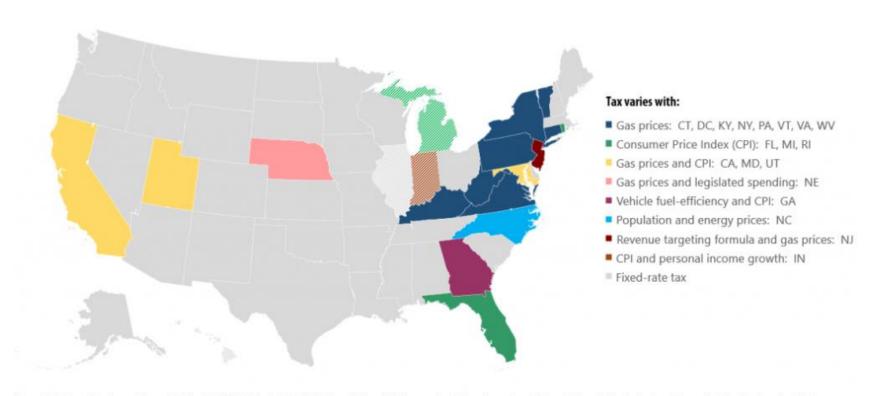
Growing Recognition of Need for Variable Rates

- Since 2013, six states (MD, NJ, PA, RI, UT, and VA) as well as the District of Columbia (DC) have abandoned their old gas tax structures in favor of more sustainable, variable-rate designs
- Over this same period, states such as CA, GA, IN, MI, and NC have made significant improvements to their existing variable-rate tax structures
- Because of these reforms, a majority (57 percent) of the U.S. population now lives in states where the gas tax rate automatically varies over time



Growing Recognition of the Need for Variable Rates

States with Variable-Rate Gasoline Taxes



Source: Institute on Taxation and Economic Policy, July 2017. Striped states (HI, IL, IN, and MI) apply their general sales taxes to gasoline, which results in variations in the tax paid per gallon based on the price of fuel.

Gas Tax Regressivity

- Like most taxes on consumption, state gas taxes are inevitably regressive—impacting low-income families far more heavily than any other group
- When raising and modernizing the gas tax, lawmakers can provide meaningful relief to these families via targeted low-income tax credits (like EITC), without having to starve states' transportation revenue streams

In Good Company

• 27 states have raised or reformed their gas taxes since 2013, including:

- 2018
 - o Oklahoma
- 2017
 - o Indiana
 - o South Carolina
 - o Tennessee
 - o West Virginia

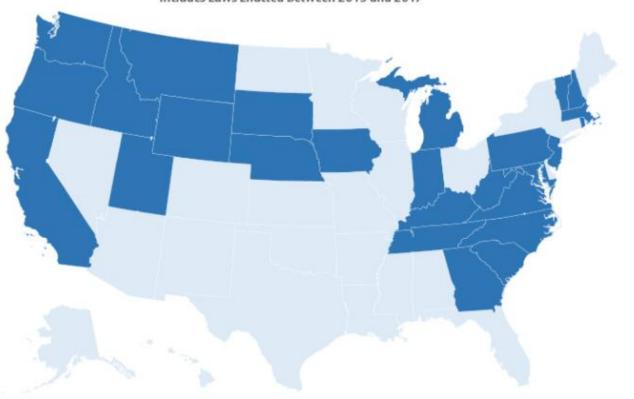
- 2015
 - o Georgia
 - o Idaho
 - o Iowa
 - o Kentucky
 - o North Carolina
- 2013
 - o Virginia



In Good Company

Recent State Gasoline Tax Increases & Reforms

Includes Laws Enacted Between 2013 and 2017



Source: Institute on Taxation and Economic Policy. Reflects laws enacted by July 12, 2017, plus legislation awaiting the governor's signature in Oregon.

Summary



Summary

- Regressivity and unsustainability of excise taxes can be mitigated, but not eliminated
 - o Refundable low-income tax credits (e.g., EITC)
 - o Variable instead of fixed per unit rates
- Heavy reliance generally on excise taxes discouraged
- Modernize your gas tax!
 - o Critical for funding economically vital infrastructure investments
 - o Increase rate, make variable to prevent future erosion
 - Offset regressive increases with refundable low-income tax credits (e.g, EITC)



Questions?

Thank you for your time and attention!

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