

SUMMARY OF PROPOSAL #11
for consideration by the
ARKANSAS TAX REFORM AND RELIEF LEGISLATIVE TASK FORCE

TOPIC: Fuel Taxes; Indexing Based on Construction Costs

Summary of Proposal for Consideration

To index motor fuel and distillate special fuel tax rates based on construction costs, with the minimum tax rate set at the current tax rate and the maximum tax rate set at three percent (3%) over the tax rate of the previous year.

Fiscal Analysis

Without a specific guidance on the construction costs and how to adjust the motor fuel taxes, the Department of Finance and Administration (DFA) is unable to provide a fiscal impact statement or analysis. Arkansas is a party to the International Fuel Tax Agreement (IFTA), which provides a method by which commercial interstate motor carriers are able to allocate motor fuel tax based on the miles driven within each jurisdiction. IFTA requires that the tax on motor fuel be a definite amount per gallon rather than a sales tax percentage of the receipts, be levied at the wholesale level, and that the tax rate only be changed on a set time table, such as quarterly. Any adjustments to be made based on these variables would need to be made in compliance with IFTA.

DFA could publish on a quarterly, biannual, or annual basis, the amount of the adjustment to the motor fuel, distillate special fuel, and other related taxes based on a defined formula provided by legislation. The fiscal impact will be dependent on the inflationary measure chosen by the General Assembly. Additionally, the General Assembly should consider whether such a proposal will set a floor below which the motor fuel taxes will not drop or whether such an indexing could allow for a reduction in the motor fuel tax in certain circumstances.

Legal Analysis

Current Law

Arkansas imposes excise taxes on motor fuel at a rate of twenty-one and one-half cents (21.5¢) per gallon and on distillate special fuel at a rate of twenty-two and one-half cents (22.5¢) per gallon.¹ Arkansas does not currently provide a mechanism for the motor fuel or distillate special fuel tax rates to automatically adjust based on one (1) or more economic indicators, including construction costs.

¹ The motor fuel taxes may be found in Arkansas Code §§ 26-55-205, 26-55-1002, 26-55-1006, 26-55-1201, and 26-56-601. The distillate special fuel taxes may be found in Arkansas Code §§ 26-56-201, 26-56-502, 26-56-601, and 26-56-802.

Most of the revenues generated by the taxes on motor fuel and distillate special fuel are special revenues distributed under the Arkansas Highway Revenue Distribution Law.² However, the additional tax of one cent (1¢) on motor fuel and distillate special fuel levied by Act 445 of 1973 is credited to the State Highway Special Construction Account, which is transferred to the State Aid Road Fund, and Arkansas Constitution, Amendment 91, distributes one cent (1¢) per gallon from motor fuel and distillate special fuel to the State Aid Street Fund.

History

Act 606 of 1921 enacted a tax on motor fuel and distillate special fuel at a rate of one cent (1¢) per gallon. The rate was increased twice in 1923, first to three cents (3¢) and then to four cents (4¢) per gallon. In 1927, the rate increased to five cents (5¢) per gallon, and it was increased again in 1931 to six cents (6¢) per gallon.

Act 383 of 1941 separated the tax on motor fuel and the tax on distillate special fuel and levied a tax on each of six and one-half cents (6.5¢) per gallon.

Acts 40 and 41 of 1965 (1st Ex. Sess.) increased the tax rate for motor fuel to seven and one-half cents (7.5¢) per gallon and increased the tax on distillate special fuel to eight and one-half cents (8.5¢) per gallon.

Act 445 of 1973 levied an additional tax of one cent (1¢) per gallon on motor fuel and distillate special fuel.

Act 437 of 1979 increased the motor fuel tax and the distillate special fuel tax by another one cent (1¢) per gallon, bringing the total tax rate to nine and one-half cents (9.5¢) per gallon for motor fuel and ten and one-half cents (10.5¢) per gallon for distillate special fuel.

Act 456 of 1985 added a tax of four cents (4¢) per gallon on motor fuel and two cents (2¢) per gallon on distillate special fuel.

Act 219 of 1991 levied an additional tax of four cents (4¢) per gallon on distillate special fuel.

Acts 364 and 382 of 1991 levied an additional tax of five cents (5¢) per gallon on motor fuel and two cents (2¢) per gallon on distillate special fuel, bringing the tax to a total of eighteen and one-half cents (18.5¢) per gallon on both motor fuel and distillate special fuel.

² Under Arkansas Code § 27-70-206, the funds would be distributed as follows:

- First, three percent (3%) would be credited to the Constitutional Officers Fund and the State Central Services Fund;
- Second, up to two million five hundred thousand dollars (\$2,500,000) may be credited to the Gasoline Tax Refund Fund, if certified by the Director of the Department of Finance and Administration as necessary to pay approved gasoline tax refund claims; and
- Third, the remainder would be distributed as follows: seventy percent (70%) to the State Highway and Transportation Department Fund, fifteen percent (15%) to the County Aid Fund, and fifteen percent (15%) to the Municipal Aid Fund.

Act 1028 of 1999 phased in an additional tax of three cents (3¢) per gallon on motor fuel over three (3) years and an additional tax of four cents (4¢) per gallon on distillate special fuel, which resulted in the current total tax rates for motor fuel and distillate special fuel.

Potential Legal Issues

Amendment 19 to the Arkansas Constitution (incorporated at Article 5, § 38) requires an emergency clause and a $\frac{3}{4}$ -vote of the legislature to increase the rate of certain taxes.³ The motor fuel and distillate special fuel taxes are generally considered to fall under the Amendment 19 requirements. Accordingly, increasing the motor fuel and distillate special fuel tax rates through indexing would require an emergency clause and a $\frac{3}{4}$ -vote of the legislature.

³ Amendment 19 also allows for the General Assembly to refer such tax rate increases to the voters for their approval, in which case the bill would require only a majority vote of each house.