

**MINUTES
NEW REVENUE SUBCOMMITTEE
of the
ARKANSAS BLUE RIBBON COMMITTEE ON HIGHWAY FINANCE**

**Wednesday, October 14, 2009
10:00 a.m.
Room 272, State Capitol
Little Rock, Arkansas**

The New Revenue Subcommittee of the Arkansas Blue Ribbon Committee met Wednesday, October 14, 2009, in Room 272 at the State Capitol in Little Rock, Arkansas.

Subcommittee members in attendance: Jim McKenzie, Chairman; Charles Dains, Bill Fletcher, Mark Lamberth, Bill Lynch, Mark McBryde, Representative Bill Sample and Mike Wilson

Also attending: Representatives Mark Martin, Robert Moore and Ray Kidd

Mr. McKenzie called the meeting to order.

Consideration to approve September 16, 2009, minutes (Exhibit B)

Representative Bill Sample made the motion to approve the September 16, 2009, minutes. The motion was seconded by Mr. Bill Lynch and approved by the Subcommittee.

Acknowledgements

Mr. McKenzie commended Mr. Mark McBryde and staff for volunteering to develop an interactive computer model for alternative analysis. Mr. McBryde stated that a demo should be available for distribution at the November meeting. Mr. McKenzie noted that Mr. Bill Lynch and Mr. McBryde had volunteered to develop a Policy brief on Public Private Partnerships and Tolling.

Review of Draft Policy Briefs (Exhibit E)

Mr. McKenzie stated that during its September meeting, the Subcommittee discussed and considered the listed revenue resources as potential new revenue sources (gasoline excise tax, diesel excise tax, removal of sales tax exemption on motor fuels, indexing motor fuel taxes, carbon tax on motor fuels, vehicle miles traveled tax, weight distance tax, public private partnerships/tolling, general sales tax and income tax). The Subcommittee will develop 2-4 page policy briefs on the revenue options. The intent of the policy brief is to include simplified language describing the revenue option, what it will generate, any legal and administrative issues, and graphs. The information will be entered into the model that Mr. McBryde is developing. General adjustment factors would apply to many of the revenue sources. In order to estimate the net revenue over the 2011-2020 decade, initial revenue projections must be adjusted for several factors that will influence returns over that period, specifically growth in the Vehicle Miles Traveled (VMT), fleet fuel efficiency improvement and fuel prices.

Factor 1. Vehicle Miles Traveled (VMT)

The Arkansas Highway and Transportation Department (AHTD) projects a 1.7% annual VMT growth rate each year from now through 2020, which is consistent with published national trends. This projection assumes a reasonable economic recovery and no oil price shock that would reduce VMT. No attempt was made to differentiate between VMT growth rates of the light duty fleet and heavy trucks.

Factor 2 - Fleet Fuel Efficiency

In 1980, the average miles per gallon (mpg) of the light duty fleet was 16 mpg and by 1990 the rate had increased to 21.1 mpg, or an average increase of 2.68% per year. The 2.68% rate applied to the light duty fleet only with light trucks, pick-up trucks and SUV's, showing more improvement. Mr. McKenzie stated the 2.68% rate would be a conservative estimate in terms of improvement and average fuel efficiency over the coming decade, noting the Subcommittee would be interested in reviewing better data regarding projected absorption rate of high mileage vehicles.

Net Growth Rate

The projected increase in VMT, which would otherwise result in increased motor fuel use, is offset by the improvement in average fleet fuel efficiency resulting in the use of less motor fuel. The net growth assumed for these policy briefs is -1% per year rate of growth in excise tax revenues projected over the decade.

The net growth rate chart indicates the VMT growth results in a 22% increase in revenues from motor fuels by 2020, the New Corporate Average Fuel Economy (CAFÉ) standards without VMT growth would result in a 28% decrease in motor fuel revenue by 2020 and the net growth rate (-1%), results in an 11% reduction in annual revenues from motor fuel taxes by 2020. Assuming a combination of lower VMT and faster absorption of high mileage vehicles into the fleet, there would be a net growth rate of -3.3% per year.

Factor 3 - Fuel Prices

The Subcommittee reviewed annual pump price projections for 2011-2020 for average annual gasoline and diesel prices from Moody's and the Energy Information Agency (EIA). The projections showed that annual pump prices would be significantly higher than they are now. These projected increases could reduce the VMT growth and produce a more rapid increase in fleet turnover to high mileage vehicles. This information has not been factored into the adjustment factors but will be added if a source for the information becomes available. Sales tax is applied to motor fuels at the anticipated rates that generate heavy revenue. Projected pump prices are used to figure sales tax adjustments.

Carbon Tax on Motor Fuels

Mr. McKenzie stated that, to his knowledge, no other state has deployed a carbon tax. A carbon tax would be based upon the carbon content of each motor fuel and would be administered using the same mechanism as the motor fuel excise taxes. Some advantages of the carbon tax include: a new tax requiring only a simple majority vote of the General Assembly to adopt or increase, the rate could be set at 1¢ per gallon, and the gas excise tax increase has the same revenue profile as an excise tax increase. The carbon tax is a way to tax alternative motor fuels with carbon content in an equitable manner and, like the excise tax, is inelastic.

The two major fuels are diesel fuel and motor gasoline. The carbon tax on diesel fuel would be 15% higher. A tax rate of 1¢ per pound of carbon on motor gasoline would yield 19.4¢ per gallon. A carbon tax rate equivalent to 1¢ per gallon for gasoline would generate \$14 million for gasoline and \$6.78 per unit for diesel fuel.

Issues to be resolved include the method of administration for alternative fuels and the impact of a carbon tax on the State's emerging biofuels enterprises. Mr. Lamberth stated that, in conjunction with the carbon tax, other revenue sources would be needed. Mr. McKenzie noted that consistent base measures had been developed to adjust the rate accordingly.

In response to a question, Mr. McKenzie stated the battery powered electrical vehicles would most likely fall under the VMT tax. The VMT tax would directly tax the number of miles driven as opposed to the volume of fuel purchased. Mr. Dains stated the carbon tax is not a use tax and, as it has nothing to do with highway use construction or repairs, the carbon tax should not be considered. Mr. McKenzie suggested the Subcommittee try to focus on solving the problems and reiterated the intent is to raise revenues for highways.

The carbon tax is not a general application for all uses and would be a tax on motor fuels. This alternative would help solve a structural problem in that the main source of revenue requires a 75% vote in the General Assembly. Mr. Dains said there might be a good reason for the 75% requirement and that we should focus on items that can pass a 75% requirement. Mr. McBryde pointed out that after the Committee works through this process to identify different funding sources to solve the problem, the legislature will determine what is appropriate. Mr. Lynch noted the Subcommittee should consider all options. Mr. McKenzie added that after options are identified, the Subcommittee can develop policy briefs which may assist the full Committee in deciding on options to present to the public and those appropriate in drafting legislation.

Mr. McKenzie requested feedback from Subcommittee members regarding policy briefs, if they would like to review any of the discussed agenda items in an appropriate format and if additional charts or graphs are needed. He requested that members review the handouts and email comments and recommendations to him.

Sales Tax on Motor Fuels

Mr. McKenzie addressed the need for clarifications on the sales tax on motor fuels. The Subcommittee could deal with the repeal of the existing exemption on the gross receipts tax of motor fuels. The state sales tax and local sales taxes would apply to motor fuels. According to the National Conference of State Legislatures, at least 9 states (CA, DE, GA, HI, IL, IN, MI, NY, and WV) collect a sales or gross receipts tax as a percent of the retail price. Some states apply the tax at the gas pump, wholesale level, wholesale price of fuel, and wholesale price and state and federal excise tax. There is also the possibility of a new state excise tax on the value of motor fuel as opposed to the volume of motor fuel. Regarding this matter, the Bureau of Legislative Research legal staff will provide information to the Subcommittee within a few weeks.

The Subcommittee also discussed projected unadjusted and adjusted yield for the net growth factor. In 2009, the sales tax on gasoline would initially generate a wholesale price of \$27,168,029 and, by 2020, the projected adjusted price of gasoline would generate \$52,421,276. Mr. Fletcher stated that a percentage of the sales tax could be increased but "don't put a tax on tax; make it clear that we are not taxing the excise tax".

Some of the advantages of a sales tax on gas include it can be passed with a simple majority vote in the General Assembly and that it provides some elasticity to the tax base, increasing with inflation to match rising construction costs. Mr. Fletcher stated the Subcommittee should look at what other states are doing and what works best. Mr. McKenzie noted that a simple repeal of the motor fuels exemption would also apply to local sales taxes unless otherwise restricted by the repeal legislation.

Issues to be resolved

The Subcommittee discussed the following issues: *Tax on Tax*: There is some question on whether a sales tax can be charged on the full price of fuel, including state and federal excise taxes, as it levy a tax on a tax. *Method and Cost Administration*: Input needs to be obtained from petroleum marketers and the Department of Finance and Administration on the preferred method of administration and the cost of administering the tax. *Application of Local Sales*: In either option (repeal exemptions or new sales tax) a determination would need to be made about the application of local sales taxes to motor fuels. Influencing factors will be the method and cost of administration and the method of dividing the state sales tax receipts. *Division of State Sales Tax Receipts or Not*: If the local sales tax is allowed on motor fuels, should the receipts from the state sales tax then be divided 70/15/15 with cities and counties or does the State take all of that and leave it up to the cities to apply their own sales tax? Mr. McKenzie stated this is a policy issue that would significantly affect the amount of revenue that would go to AHTD.

Mr. McBryde stated that regarding the local sales taxes throughout the State, one of the problems in looking at the cash flow associated with it include some of the cities and counties have issued and secured bonds with their local option sales taxes, and, therefore, looking at the available bonds would be a case by case analysis. Mr. Fletcher

stated that he does not understand why it is a simple exemption of the state sales tax when it automatically applies to the exemption of whatever happens in each local county or city. Why not leave them alone and let them do whatever they want to? Mr. McKenzie added the Subcommittee will have to address this issue when recommendations are considered. It has been questioned if a sales tax can be charged on the full price of fuel, including state and federal excise taxes, since it would be levying a tax on a tax.

Other Business

Mr. McKenzie noted the Subcommittee plans to get the remaining policy briefs to the full Committee in a timely manner for review at the November meeting. He added that any changes to the policy briefs based on additional information would be added. Mr. Dains recommended adding an additional 1% to 2% sales tax on new and used vehicles sales that would strictly go to AHTD. Mr. McKenzie will confer with the Revenue Transfer Subcommittee chairman, Representative Lowery, regarding this issue. Mr. Dains recommended the Subcommittee consider prioritizing policy items that would pass with a 75% vote.

Mr. McKenzie informed the Subcommittee that Mr. Wilson has prepared research on the content for indexing and will present it to the full Committee. A brief summary, including a history search, would be presented at the next Subcommittee meeting.

There being no further business, the meeting adjourned at 11:13 a.m.