

[Senate Bill 321](#) (Beall)

Date: 03/26/15

Program: Motor Vehicle Fuel Tax

Sponsor: Author

Revenue and Taxation Code Section 7360

Effective: Immediately

Michele Pielsticker (Chief) 916.322.2376

John Cortez (Analyst) 916.445.6662

**Summary:** Authorizes the BOE to make specified adjustments to the motor vehicle fuel (gasoline) tax swap rate using a five-year average fuel price estimate. Authorizes partial adjustments to the true-up portion of the rate up to a consecutive three-year period, and under specified conditions, authorizes more frequent rate adjustments, but no more frequently than every six-months.

**Purpose:** To reduce volatility of the revenues generated by the gasoline tax to assist state and local governments in preparing multiyear transportation budgets.

**Fiscal Impact Summary:** Does not affect revenues.

**Existing Law:** In 2010, the Legislature enacted two “fuel tax swap” measures<sup>1</sup> that changed the imposition and rates of state taxes on gasoline and diesel fuel, and require the Board of Equalization (BOE) to determine the appropriate excise tax rate adjustments to maintain revenue neutrality. The gasoline tax changes became operative on July 1, 2010, and the diesel fuel tax changes became operative July 1, 2011.

These provisions<sup>2</sup> exempt sales and purchases of gasoline from the state General Fund sales and use tax rate. To offset the revenue loss related to this partial exemption, the law increased the gasoline excise tax rate from \$0.18 per gallon to \$0.353 per gallon.<sup>3</sup> Conversely, the statute<sup>4</sup> reduced the diesel fuel excise tax rate from \$0.18 to \$0.13 per gallon but increased<sup>5</sup> the sales and use tax rate on diesel fuel sales and purchases to offset the loss related to the diesel fuel excise tax rate reduction, resulting in the following rates:

1.87% effective July 1, 2011

2.17% effective July 1, 2012

1.94% effective July 1, 2013

1.75% effective July 1, 2014, and thereafter.

The fuel tax swap provisions require the BOE to maintain revenue neutrality, so that the revenues derived from the increased gasoline excise tax and the increased diesel sales and use tax equals the revenues that would have been derived had the gasoline sales and use tax partial exemption and the diesel fuel excise tax reduction, respectively, not occurred.

Revenue and Taxation Code Sections 7360 and 60050 require the BOE to adjust the gasoline and diesel fuel excise tax rates, respectively, either upward or downward, to maintain revenue neutrality. For gasoline, the BOE determines: (1) whether the sales and use tax revenue loss related to the partial exemption was fully offset by the adjusted rate, and (2) the projected sales and use tax revenue loss for the next fiscal year, considering forecasted gasoline prices and consumption.

---

<sup>1</sup> [ABx8 6](#), (Ch. 11, Stats. 2010) and [SB 70](#) (Ch. 9, Stats. 2010). These provisions were re-enacted in 2011 by [AB 105](#) (Ch. 6, Statutes 2011).

<sup>2</sup> RTC Section 6357.7.

<sup>3</sup> RTC Section 7360.

<sup>4</sup> RTC Section 60050.

<sup>5</sup> RTC Sections 6051.8 and 6201.8.

For diesel fuel, the BOE determines: (1) whether the revenue gain from the increased sales and use tax rate on diesel fuel sales and purchases was fully offset by the adjusted diesel fuel excise tax rate, and (2) the projected sales and use tax revenue gain for the next fiscal year, considering forecasted diesel fuel prices and consumption.

By March 1 each year, the BOE must determine the rate adjustments and the adjusted rate applies on the following July 1.

**Proposed Law:** This bill amends RTC Section 7360, with respect to the forecasted revenue projections, to do the following:

- For Fiscal Year (FY) 2015-16, requires the BOE to adjust the excise tax rate based on a five-year average fuel price estimate that relies on fuel price data from the immediately preceding four years and estimated fuel prices for the current fiscal year so as to generate a forecasted fuel price that is weighted primarily by the known fuel price data. That adjusted rate shall be determined by July 1, 2015, and that rate would be effective for FY 2015-16.
- For FY 2016-17, and each FY thereafter, the BOE would follow the same estimate methodology as FY 2015-16, but the rate would be adjusted by March 1 of the fiscal year immediately preceding the applicable FY, and that rate would be effective for the state's next FY.
- For true-up rate adjustments made after January 1, 2015, the BOE could make partial adjustments over a three-year period to take into account the net revenue gain or loss of any fiscal year in order to reduce potential revenue volatility.
- If, due to clear changes in either fuel prices or consumption in the state, the BOE determines that the revenue being generated by the adjusted excise tax will be significantly different than the earlier estimates, then the BOE may adjust the rate before the March 1 date, but not sooner than six months between the intervening adjustments.

This bill contains an urgency clause and becomes effective immediately.

**Background:** The fuel tax swap requires the BOE to determine the excise tax rates for gasoline and diesel fuel on an annual basis. The legislation set the excise tax rate for the first year of the swap and required the BOE to adopt a "revenue-neutral" excise tax rate for each ensuing fiscal year. The calculation requires the BOE staff to develop a forecast of both consumption and price for both gasoline and diesel fuel. Staff works closely with DOF and adopts DOF's consumption forecasts.

BOE's rate calculation also takes into account the "true-up" portion, which is the one-year look back period to determine the difference between what was estimated for the previous fiscal year and what was actually collected.

Since enactment of the "fuel tax swap," the BOE staff has referred to the Department of Finance's (DOF) estimates of fuel consumption and forecasted prices to determine the necessary rate adjustment to achieve revenue neutrality. As the Governor's chief fiscal policy advisor, the DOF ensures financial integrity of the state. It prepares economic forecasts and analyses of various economic developments, and uses the most widely accepted forecasting methodology. The BOE has adjusted the gasoline excise tax rates to maintain the required revenue neutrality through incremental increases and decreases as follows:

July 1, 2011: Increase of \$0.004

July 1, 2012: Increase of \$0.003

July 1, 2013: Increase of \$0.035

July 1, 2014: Decrease of \$0.035

July 1, 2015: Decrease of \$0.060

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.

The BOE adjusted the diesel fuel excise tax rate with both increases and decreases, as follows:

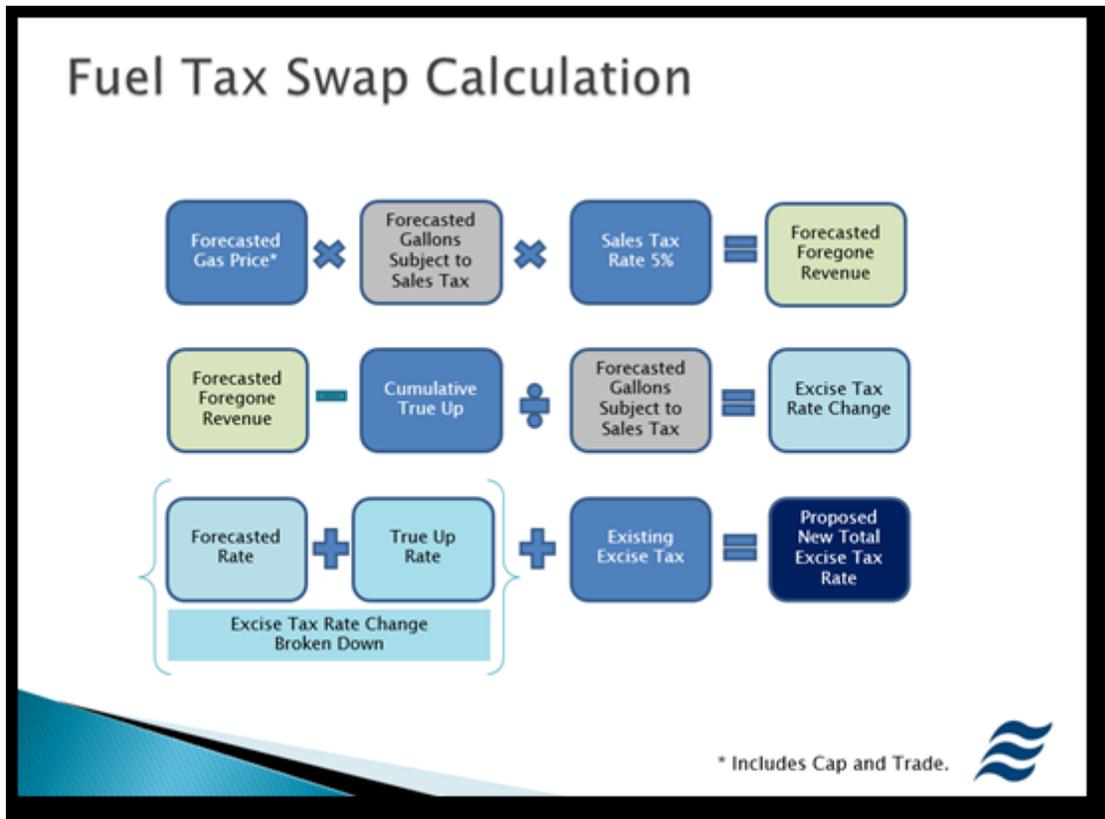
July 1, 2012: Decrease of \$0.03

July 1, 2013: Retain July 1, 2012 rate

July 1, 2014: Increase of \$0.01

July 1, 2015: Increase of \$0.02

The following chart depicts the fuel tax swap calculation:



### Commentary:

- 1. Effect of the bill.** This bill is intended to reduce potential volatility of the revenues generated by the gasoline tax by specifying the forecast method for fuel prices and allowing more frequent excise tax rate adjustments.
- 2. No administrative difficulties with the forecast provisions.** Under the current fuel tax swap rate calculation, the two main components are the forecast and the true-up. The forecast is comprised of two factors: fuel price and fuel consumption quantity. The BOE's rate adjustments are expected to be revenue neutral and any out-year adjustments are intended to maintain revenue neutrality. Since this bill provides specifics to assist with the forecast of fuel prices, and adjustments as needed, it maintains the goal of revenue neutrality. Therefore, BOE staff does not foresee administrative difficulty with the forecast portion of the fuel tax swap rate adjustments.
- 3. BOE staff suggests a 60-day delayed operative date.** As required by current statute, the BOE set the FY 2015-16 excise tax rate before March 1, 2015, and that rate takes effect July 1, 2015. The delay allows the BOE time to notify the affected industry and make necessary administrative changes to the returns and computer programs. Moreover, an excise tax rate change would need to be calculated by BOE staff and then placed on a BOE hearing agenda for the BOE members to consider and take appropriate action. BOE staff are available to assist the author with a delayed operative date.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.

4. **Is a rolling three year true-up needed?** The adjusted gasoline excise tax rate is composed of a forecast portion, and the true-up portion. Over the last three fiscal years the forecast portion accounted for an average 89% of the excise tax rate change. Up until the 2015-16 FY rate change, the forecast accounted for 94% of the rate change. Over the three-year period, the true-up has averaged less than two cents (\$0.0163 cents). BOE staff believes the proposed adjustments to the forecast would only continue to make the true-up portion a smaller percentage of the total gasoline excise tax rate change.
5. **A rolling true-up of up to three years would only complicate an already complex process.** This bill allows the true-up to be spread out for up to three years in order to avoid dramatic tax rate changes. The current true-up is intended to maintain revenue neutrality by looking back one-year to determine the difference between the estimated fiscal year revenues and the actual revenues collected. As previously explained, the true-up accounts for one portion of the total fuel tax rate adjustment; the other component being the next fiscal year's forecasted rate. Per the statutes and inevitable fuel price changes, a true-up component was necessary for the last two fiscal years.<sup>6</sup> If a true-up component was based on a partial year adjustment, would the BOE have to deviate from a fiscal year calculation to some arbitrary annual period to determine the true-up period? Would the BOE need to consider the carryover "gain or loss" when the next fiscal year true-up is calculated? The bill's legislative intent language strives for revenue neutrality over a reasonable number of fiscal years, but adding another layer of calculations and forecasting may only exacerbate the current confusion for local government revenue projections.
6. **Related bills.** [SB 433](#) (Berryhill) would require the DOF, instead of the BOE, to determine the annual excise tax rate adjustment for gasoline and diesel fuel under the "fuel tax swap" provisions.

**Administrative Costs:** The BOE's administrative costs are absorbable. These costs include the fuel tax swap calculations, review, presentation, and decision making. The BOE would also continue to notify the affected industry and respond to inquiries regarding the excise tax rate adjustments.

**Revenue Impact:** The intention of this bill is to reduce potential revenue volatility by smoothing out forecasted fuel prices and maintain the original bill's revenue neutrality. Accordingly, this bill does not affect motor vehicle fuel tax revenues.

---

<sup>6</sup> As previously footnoted, the enacting statutes established the initial surtax rate, beginning July 1, 2010, and required the BOE to adjust that rate beginning July 1, 2011, with a forecast. A true-up was not required until July 1, 2012, which compared the actual revenues with the forecasted estimates.