



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

DRAFT

Date:	08/04/14	Bill No:	<u>Assembly Bill 2756</u>
Tax Program:	Diesel Fuel	Author:	Committee on Revenue and Taxation
Sponsor:	Author	Code Sections:	RTC 60501 & 60505.5
Related Bills:	AB 2757 (Bocanegra)	Effective Date:	01/01/15

BILL SUMMARY

This bill allows a diesel fuel tax refund to a supplier for that portion of tax-paid biodiesel fuel removed from the terminal rack as a dyed biodiesel blend.

Summary of Amendments

This bill previously imposed certification and annual training requirements on state and county employees responsible for property tax change in ownership and exemption decisions. Those provisions were deleted and replaced by the current provisions.

ANALYSIS

CURRENT LAW

Under the Diesel Fuel Tax Law (DFTL),¹ a \$0.11 per gallon excise tax² is imposed on the removal of diesel fuel at the refinery or terminal rack,³ upon entry into the state, and upon sale to an unlicensed person. This tax is adjusted annually to balance the revenues from the additional sales taxes on diesel fuel against the diesel fuel excise tax rate reduction that occurred as a result of the Fuel Tax Swap.⁴

Existing law defines a terminal⁵ as a distribution facility supplied by pipeline or vessel (i.e., by bulk transfer), from which the diesel fuel may be removed at a rack. It also includes a diesel fuel production facility with storage that is not supplied by pipeline or vessel, from which the fuel produced may be removed at a rack. These diesel fuel production facilities have the same licensing and reporting requirements as distribution facilities currently supplied by pipeline or vessel.

Generally, the diesel fuel supplier owes excise tax at the time the diesel fuel is removed from the terminal rack.⁶ If the diesel fuel enters California outside the bulk transfer/terminal system (“below the rack”), for instance by train or truck, the excise tax is due once it enters California.⁷

A supplier includes, among others, a person who owns the fuel in a terminal (position holder), a refiner, an enterer (importer), a blender, and a terminal operator. The Board

¹ Part 31 (commencing with Section 60001) of Division 2 of the Revenue and Taxation Code (RTC).
² The Board set the excise tax rate on diesel fuel at \$0.11 per gallon for the period of July 1, 2014, to June 30, 2015.
³ RTC Section 60006 refers to a series of pipes, a “rack,” as a mechanism for delivering fuel from a refinery or terminal into a truck, trailer, or other means of nonbulk transfer.
⁴ Additional sales and use tax rate on sales of diesel fuel imposed by AB 105 (Ch. 6, Stats. 2011): <http://www.boe.ca.gov/legdiv/pdf/0105abenrolledstw.pdf>
⁵ RTC Section 60003
⁶ RTC Section 60051
⁷ RTC Section 60052

of Equalization (BOE) requires a supplier to be licensed and file monthly returns or information reports that detail the amount of fuel entered, received, removed, and stored.

Exemptions and Refunds. Certain sales by diesel fuel suppliers are exempt from the excise tax, such as export for use outside the state, fuel used off-highway, or dyed diesel fuel.⁸

Certain persons may claim a credit or refund for the tax paid on fuel that is subsequently used in a nontaxable manner. Current law⁹ authorizes reimbursement of the tax paid on diesel fuel that meets any of the following conditions:

- Used for purposes other than operating motor vehicle on public highways of the state.
- Exported for use outside of this state.
- Used in construction equipment that is exempt from vehicle registration and operated on a construction project.
- Used in a vehicle on any highway under the jurisdiction of the United States (U.S.) Department of Agriculture. To qualify for a refund, the user must have paid for or contributed to the construction or maintenance of the highway.
- Used in a motor vehicle owned and operated by a public agency or political subdivision of the state on highways constructed and maintained by the U.S. within a military reservation in California.
- Sold by a supplier to a consulate officer or employee under circumstances where the supplier would have been entitled to an exemption if the fuel had been sold directly to the consulate.
- Lost in the ordinary course of handling, transportation, or storage.
- Sold to the U.S. and its agents and instrumentalities under conditions that would have otherwise allowed a supplier to qualify for an exemption had that fuel been sold directly to the U.S.
- Sold to a train operator for use in a diesel-powered train or for other off-highway use under conditions that would have otherwise allowed a supplier to qualify for an exemption had that fuel been sold directly to the train operator.
- Removed from the terminal rack, but only to the extent that the supplier can show that tax on that same diesel fuel has been paid more than once by that supplier.

Biodiesel. California tax laws consider biodiesel to be a diesel fuel¹⁰ and subject to the diesel fuel excise tax rate. The fuel industry generally describes biodiesel by its percentage of biodiesel blended with petro diesel. For instance, a 100% biodiesel is described as B100 and a 5% biodiesel is B5, in which petro diesel represents 95% of the blend.

PROPOSED LAW

This bill allows a diesel fuel tax refund to a supplier for that portion of tax-paid biodiesel fuel removed from the terminal rack as a dyed biodiesel blend.

⁸ RTC Section 60100

⁹ RTC Section 60501

¹⁰ RTC Section 60022

BACKGROUND

Most U.S. produced biodiesel comes from the Midwest region. Since this biodiesel distribution occurs outside the normal bulk transfer/terminal system it is subject to the diesel fuel tax upon entry into the state. As the biodiesel products enter the market from outside California, the enterer¹¹ is responsible for the diesel fuel tax when it enters the state. Biodiesel that is produced in California (in-state), is generally taxed upon removal from the fuel production facilities rack, or, when the biodiesel “enters” the California market if removed from below the rack.¹²

In either of those cases, when another supplier makes a subsequent purchase of this tax-paid biodiesel to create a blended diesel fuel, the tax-paid biodiesel fuel is blended with ex-tax diesel fuel. When this blended diesel fuel is subsequently removed at the terminal rack, it may result in tax assessed twice on the biodiesel portion. In the case of a taxable removal, the state allows the supplier to claim a credit on their return as tax-paid twice by the same supplier.

However, some suppliers have been unable to receive a credit or refund for tax paid on biodiesel that enters the state, or is produced in-state, and is delivered into their terminals as tax-paid, but subsequently is removed at the terminal racks for a *nontaxable* purpose. While the current statute allows reimbursement for the second tax paid on diesel fuel by the same supplier, the statute does not account for tax-paid diesel fuel that is taxed coming into the terminal but removed for nontaxable purposes (e.g. dyed biodiesel blends). The supplier is unable to recover the tax from the customer and is also unable to seek reimbursement for the tax from the BOE. Since the tax-paid biodiesel is blended with ex-tax dyed diesel fuel, it is not subject to tax when it is removed from the terminal rack. Because there is no subsequent taxable event, the current statute does not provide for a reimbursement of the tax-paid portion of the biodiesel.

COMMENTS

- 1. Sponsor and Purpose.** This bill is sponsored by the Committee on Revenue and Taxation and is intended to address a diesel fuel tax issue wherein a supplier is unable to be reimbursed for excise taxes paid on fuel subsequently sold as a dyed biodiesel blend, which is not subject to tax when removed at the terminal rack.
- 2. The BOE would not have administrative issues with the refund provisions.** The BOE administers all provisions of the DFTL, including the exemption and refund provisions. BOE staff works closely with the fuel industry to be aware of industry trends and practices, and provides information and assistance in the form of [special notices, publications and reports](#), answers to [frequently asked questions](#), and [newsletters](#). The BOE has previously provided guidance to suppliers that refunds are not allowed for tax-pad biodiesel fuel converted to dyed biodiesel fuel.¹³
- 3. Related legislation.** AB 2757 (Bocanegra) contained identical provisions before being amended In Senate Appropriations.

COST ESTIMATE

The BOE administrative costs are absorbable.

¹¹ Importer of record or owner of the fuel; RTC Section 60013

¹² “Below the rack” from outside the normal bulk transfer/terminal system means from outside the normal bulk transfer/terminal system.

¹³ http://www.boe.ca.gov/pdf/pub201_Dec_2012.pdf. See especially pp. 3 & 4, “Diesel Fuel Tax.”

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

REVENUE ESTIMATE**BACKGROUND, METHODOLOGY, AND ASSUMPTIONS**

As explained in the Background section, current law allows a supplier to claim a credit or refund for tax-paid twice on the biodiesel portion that has been assessed tax twice. Since current statute does not allow a credit or refund to address the blended dyed biodiesel issue that this bill seeks to address, we cannot be certain how diesel fuel suppliers (taxpayers) are currently blending, or will be blending, the dyed biodiesel. Therefore, for purposes of this estimate, we assume the ratio of blending for tax-paid twice biodiesel (based on the refund data) is the same for blended dyed biodiesel. The revenue impact per fiscal year (FY) is as follows:

For FY 2011-12:

- Taxable biodiesel removed totaled 94.9 million gallons.
- Taxpayers filed a claim for refund on 3.0 million gallons of tax-paid biodiesel.
- Tax rate for FY 2011/12 was \$0.13 per gallon.
- Up to 3.2% (3 million /94.9 million = 3.2%) of exempt dyed diesel fuel may be subject to a refund of excise taxes paid.
- Estimated refunds would amount to approximately \$395,000 (94.9 million x 3.2% x \$0.13 excise tax = \$394,784).

For FY 2012-13:

- Taxable biodiesel removed totaled 228.9 million gallons.
- Taxpayers filed claims for refund on 7.9 million gallons of tax-paid biodiesel.
- Tax rate for FY 2012/13 was \$0.10 per gallon
- Up to 3.5% (7.9 million /228.9 million = 3.5%) of ex-tax dyed diesel fuel may be subject to a refund of excise taxes paid.
- Estimated refunds would amount to approximately \$800,000 (228.9 million x 3.5% x \$0.10 excise tax = \$801,150)

REVENUE SUMMARY

BOE staff estimates the potential overpayment of diesel fuel tax, applied to the data for FY's 2011-12 and 2012-13, is \$395,000 and \$800,000, respectively.

Qualifying Remarks.

- In the future, we can expect taxpayers to blend up to 5% biodiesel into all petroleum diesels to meet the required California Air Resources Board Low Carbon Fuel Standards mitigation measures.
- Diesel fuel tax rate is subject to an annual rate change effective July 1 of each fiscal year. The rate for FY 2014-15 will be \$.011 per gallon.¹⁴
- This revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.

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¹⁴ This rate was effective July 1, 2014. See here for more detailed information:
http://www.boe.ca.gov/meetings/pdf/022514_P1_1_Fuel_Tax_Swap_Memo.pdf

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