



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

Date Amended:	<b>7/05/01</b>	Bill No:	<b>AB 309</b>
Tax:	<b>Sales and Use Diesel Fuel Motor Vehicle Fuel</b>	Author:	<b>Longville</b>
Board Position:	<b>Support - Board-sponsored provisions. No position on remainder.</b>	Related Bills:	<b>AB 2114 (2000)</b>

**BILL SUMMARY**

This bill would move the first point of retail sales tax prepayment on fuel to the rack to coincide with the imposition of the motor vehicle fuel tax. This bill would also make various technical and housekeeping changes to the Motor Vehicle Fuel Tax Law and the Diesel Fuel Tax Law.

**ANALYSIS**

***Sales tax prepayment provisions***

**(Sections 1 – 11)**

**Current Law**

Under existing law, any distributor or broker (seller) of motor vehicle fuel, as defined in Part 2 (commencing with Section 7301) of the Revenue and Taxation Code, or any aircraft jet fuel dealer who sells aircraft jet fuel as defined by Section 7372 of the Revenue and Taxation Code, or any producer, importer or jobber (seller) who makes a sale of diesel fuel, as defined in Part 3 (commencing with Section 8601) or Part 31 (commencing with Section 60001) of the Revenue and Taxation Code, is required to collect prepayment of retail sales tax from the person to whom the fuel is sold. Generally, the types of fuels subject to the prepayment provisions include gasoline, aircraft jet fuel and diesel fuel. The prepayment rates for the period April 1, 2001 through March 31, 2002 are \$0.095 per gallon on gasoline, \$0.05 per gallon on aircraft jet fuel, and \$0.08 per gallon on diesel fuel. With the exception of the person making the retail sale of the fuel to the consumer, each seller of fuel is required to report and pay the prepayment amounts to the Board. Also, when the seller of fuel reports and pays his or her prepayment to the Board, the seller of fuel is allowed to claim a credit for the prepayment amount paid to his or her vendor. The person making the retail sale of the fuel to the consumer is allowed to claim a credit for the prepayment amount paid to his or her vendor when reporting the retail sales tax due on the retail sale of the fuel.

**Proposed Law**

This bill would move the first point of retail sales tax prepayment on fuel to the rack to coincide with the imposition of the motor vehicle fuel tax.

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## **Background**

The prepayment of retail sales tax on motor vehicle fuel was added by the passage of Senate Bill 1610 (Ch. 214, Stats. 1986). Prior to the passage of SB 1610, sales tax on fuel was only collected on the final retail sale. Before the prepayment of retail sales tax on motor vehicle fuel requirement, tax evasion by service stations was a problem. Due to the number of retail service stations in the state, and the nature of operations, many service stations would either fail to obtain the necessary seller's permit, or they would obtain the permit but fail to report the entire tax liability from their retail sales. By requiring the prepayment of the retail sales tax on motor vehicle fuel, 80 percent of the retail sales tax is collected in advance. Since the retailer is required to prepay a large portion of its sales tax liability, each retailer has an incentive to report the correct sales amount and recoup the tax already paid to its supplier. Also, information on how many gallons of fuel are sold to each vendor is documented. Board staff uses this information to trace the flow of fuel from seller to seller and ultimately reconcile those numbers with the final retail sale.

Until January 1, 2002, the excise tax on gasoline is imposed upon distributors for the privilege of distributing gasoline in this state. Distribution includes refining, producing, blending, or compounding gasoline in this state coupled with the sale, donation, consignment for sale, barter, or use of the fuel in this state. Distribution also includes importing into this state, coupled with the sale, donation, consignment for sale, barter, or use of the fuel in this state. The first distribution of gasoline generally occurs at the highest point in the distribution chain, before the gasoline leaves the refinery by way of a terminal rack or pipeline.

By contrast, the collection point of the excise tax on diesel fuel is at the refinery or terminal rack level. The rack is a level in the distribution chain at a refinery or at a storage and distribution facility at the end of a pipeline where gasoline, aircraft jet fuel, or diesel fuel are delivered through a mechanism (the rack as it leaves the refinery or storage facility) into ground transportation, such as a truck, trailer, or railroad car.

Beginning January 1, 2002, Assembly Bill 2114 (Ch. 1053, Stats 2000) shifts the imposition of the excise tax on gasoline from the point of first distribution to the rack. Moving the point of taxation to the rack will have several benefits. First, the point of taxation will be consistent with the diesel fuel tax law and the federal excise tax law. Also, with the implementation of the Excise Fuel Information Reporting System (ExFIRS) by the Internal Revenue Service, there is a federal tracking system that will be a tremendous aid in deterring tax evasion for any state that taxes fuel at the rack.

### ***Motor vehicle fuel and diesel fuel tax provisions***

#### **(Sections 12 – 79)**

#### **Current Law**

Under current law, an excise tax of \$0.18 per gallon is imposed on both motor vehicle fuel (gasoline) and diesel fuel. For use fuels such as liquefied petroleum gas, compressed natural gas, ethanol, and methanol, the excise tax rates are \$0.06, \$0.07, \$0.09 and \$0.09, respectively.

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The revenues generated from these excise taxes are deposited in the Transportation Tax Fund.

### Proposed Law

This measure would make the following changes to the Motor Vehicle Fuel Tax Law and the Diesel Fuel Tax Law:

**Sections 7320, 7364 and 7727:** Conform the Motor Vehicle Fuel Tax Law to the Diesel Fuel Tax Law for purposes of the definition of “highway vehicle operator/fueler”, the backup tax and the penalty for the backup tax.

**Sections 7326 and 60022:** Delete the reference to inflammable/combustible liquid and explosion type engine in the definition of “motor vehicle fuel” and “diesel fuel.”

**Sections 7330, 7343, 7344, 60047, 60047.1, 60049, 60049.1, 60135, and 60204.5:** Add definitions to the Diesel Fuel Tax Law and revise Motor Vehicle Fuel Tax Law definitions for the purpose of utilizing the Internal Revenue Service’s Excise Summary Terminal Activity Reporting System (ExSTARS).

**Sections 7337, 7345, 60025, 60048 and 60048.1:** Add definitions for the terms “tax-paid fuel” and “gallon”, and revise the definition of “sale” in the Motor Vehicle Fuel Tax Law.

**Sections 7372 and 60063:** Allow the Board to accept from a person who receives motor vehicle fuel or diesel fuel removed at a refinery or terminal rack an amount equal to the tax due which is required to be paid by the refiner or position holder upon removal of the fuel from a refinery or terminal rack. This section would only be operative if the Internal Revenue Service authorizes payment of federal fuel taxes by the receiving party under a two-party exchange agreement or similar arrangement.

**Sections 7373 and 60064:** Add a presumption of removal or sale to prevent the evasion of the excise tax.

**Sections 7404, 60106.2 and 60503.1:** Correct the process of the collection of the tax and penalty for the misuse of an exemption certificate.

**Sections 7405, 60106.3 and 60503.2:** Conform and correct the penalty amount for misuse of exemption certificate.

**Sections 7453, 7486, 7487 and 60401:** Align the security requirement provisions in the Motor Vehicle Fuel Tax Law and the Diesel Fuel Tax Law and require the Board to release security held after a three-year period in which the person has filed all returns and paid all tax to the state.

**Sections 7652 and 60203:** Repeal the requirement to file a throughput informational report.

**Section 7653:** Allows for a credit on the storage tax return or the supplier tax return for tax-paid motor vehicle fuel in the bulk transfer/terminal system on January 1, 2002. This provision assures that previously taxed fuel in the bulk/transfer system on January 1, 2002 is not subject to the floor stock tax.

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**Section 7654 and 7657:** Remove \$50 penalty for failure to file an information report and for filing an inaccurate or improper information report, and require the Board to establish criteria that provide for efficient resolution of requests for relief of penalty for failure to make a timely report, return or payment.

**Sections 7659.93 and 60253:** Allow the Board to accept and authenticate any return, report, declaration or statement filed using electronic media, and allow the Board to be provided with returns filed with ExSTARS if a terminal operator provides consent and authorization.

**Sections 7659.94 and 60254:** Require any person who is notified to file using electronic media files but who instead files by paper, to pay the additional costs incurred by the Board for processing the paper returns, reports or other documents.

**Sections 8101, 8106.8, 60501 and 60508.4:** Allow a supplier to claim a refund or credit on its return for fuel on which the state excise tax has been paid twice, but only to the extent that the supplier can show that tax on the same amount of motor vehicle fuel has been paid more than one time by the same supplier.

**Section 8126 and 60521:** Allow the Board to recommend a credit or a refund of amounts overpaid by any person, not just a licensed supplier.

**Sections 60015, 60107, 60211 and 60605:** Conform the Diesel Fuel Tax Law to the Motor Vehicle Fuel Tax Law for the purpose of administration of the train operator return, terminal operator records, adding throughput as a diesel fuel registrant, adding sale to remove or sale to an unregistered person and adding relief of jeopardy interest.

**Sections 60027, 60056, 60101, 60161, 60163, 60181, 60206 and 60360:** Rename "highway vehicle operator" to "qualified highway vehicle operator" to allow for specified persons to use dyed diesel fuel on the highway and report the tax without being subject to the dyed fuel penalty, and require qualified highway vehicle operators to pay the backup tax for the use of dyed diesel fuel on the highway. Under federal law, persons defined as qualified highway vehicle operators are allowed to use dyed diesel fuel on the highway.

**Sections 60034, 60057, 60058 and 60361.5:** Conform the Diesel Fuel Tax Law to the Motor Vehicle Fuel Tax Law by adding the highway vehicle operator/fueler as the person liable for the backup tax, making certain sales subject to the backup tax, adding a penalty for the backup tax, and adding a determination for assessing the backup tax.

**Section 60105:** Update Diesel Fuel Tax Law penalty provisions relating to dyed diesel fuel to conform to recently revised Federal Fuel Regulation definitions.

### **Background**

In 2000, Assembly Bill 2114 (Longville, Chapter 1053) made significant revisions to the motor vehicle fuel tax law. Operative January 1, 2002, AB 2114 will revise the Motor Vehicle Fuel Tax Law to conform to the state Diesel Fuel Tax Law and Federal Fuel Tax Law by moving the collection point of the tax from the first distribution level to the

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refinery or terminal rack level. Additionally, AB 2114 will conform the Motor Vehicle Fuel Tax Law to the state Diesel Fuel Tax Law and Federal Fuel Tax Law with respect to definitions and exemptions.

## COMMENTS

- 1. Sponsors and Purpose.** The purpose of the Board-sponsored provisions are to simplify the payment and reporting of the prepaid sales tax on fuel.

The motor vehicle fuel and diesel fuel tax law provisions are sponsored by the Western Petroleum States Association (WSPA) and are intended to further align the motor vehicle fuel tax law, the diesel fuel tax law and the federal fuel tax law. WSPA states that these provisions would allow the state to enhance detection of tax evasion, increase compliance and lower the eventual costs for both the state and industry to accomplish these mutually desirable goals.

- 2. Summary of July 5 amendments.** These amendments, which are sponsored by WSPA, make various technical changes to the Motor Vehicle Fuel Tax Law and the Diesel Fuel Tax Law. These amendments include incorporating provisions into the Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law to allow the Board to accept and authenticate any return, report, declaration or statement filed using electronic media. The amendments would also allow the Board to be provided with returns filed with the Internal Revenue Service's Excise Summary Terminal Activity Reporting System (ExSTARS) if a terminal operator provides consent and authorization.

ExSTARS is a fuel reporting system developed with the cooperation of the IRS, Department of Transportation, States, and Motor Fuel Industry, which details the movement of any liquid product into or out of an IRS approved terminal. The ExSTARS system, which officially started on March 31, 2001, will track all fuel products through terminals and capture destination state information when the fuel is disbursed through the terminal rack. By allowing the Board to be provided with returns filed with the ExSTARS system, California will be able to make a direct comparison between the ExSTARS data, which is reported by terminal operator, and the state tax returns that are filed. This system will gather and analyze motor fuel industry records to determine where and by which entity, federal and state motor fuel taxes are not being remitted and will be a tremendous aid in deterring fuel tax evasion for any state that taxes fuel at the rack.

In addition, the July 5, 2001 amendments also:

- Further align the Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law to the Federal Fuel Tax Law and Federal Fuel Regulations, including authorizing two-party exchange agreements if authorized by the IRS,
- Amend and repeal sections throughout the Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law to allow for the ease of administration for both the state and taxpayer and to add consistency between the two programs,
- Incorporate additional definitions based on Federal Fuel Regulations into the Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law for clarification purposes, and

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- Update Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law definitions that were revised in Federal Fuel Regulations, upon which the state definitions are based.
  - Allow the Board to recommend a refund of amounts overpaid by any person, not just a licensed supplier.
  - Require any person, who after being notified that the person is required to file using electronic media files by means other than the required electronic media, to pay the Board for the costs incurred for processing the returns, reports or other documents.
3. **Summary of May 21 amendments.** An amendment to Section 6471.4 was added to include diesel fuel and aircraft jet fuel with motor vehicle fuel to ensure that taxpayers are not required to make any additional monthly prepayments of the sales tax above what they are already required to report under current law.
  4. **Summary of March 26 amendments.** After discussing the language of the bill with industry representatives, minor amendments were made to address their concerns which consisted of replacing the term “jobber” with “wholesaler,” revising the definition of a sale, adding credit provisions for situations where tax is paid twice or is not due, and adding language to clarify when a bad debt deduction may be taken.
  5. **This bill will simplify reporting for fuel sellers.** Imposing the retail sales tax prepayment on fuel at the same point as the motor vehicle fuel tax would simplify payment and reporting since the imposition of the prepayment of sales tax would coincide with the imposition of the state motor vehicle fuel tax and the federal excise tax imposed on motor vehicle fuel.
  6. **The Motor Vehicle Fuel Tax Law and Diesel Fuel Tax Law provisions would not be problematic to administer.** Board staff provided technical assistance for the drafting of the excise tax amendments to make it possible for the Board to properly administer the tax law changes in the event this bill becomes law.
  7. **The provisions of this bill could help reduce tax evasion.** The Board would be able to utilize ExSTARS (and its component, ExFIRS), a federal tracking system, to gather and analyze motor fuel industry records to determine where and by which entity, federal and state motor fuel taxes are not being remitted. In addition, the Board would use the federal tracking system to track the prepayment of retail sales tax on fuel to prevent tax evasion.

### **COST ESTIMATE**

Some additional administrative workload would be realized as a result of notifying affected sellers, responding to inquiries and revising returns and regulations. These costs would be absorbable.

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**REVENUE ESTIMATE**

The provisions of this bill would have no direct revenue impact. However, the ability to utilize ExSTARS would safeguard the state's revenue against tax evasion.

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