



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

DRAFT

Date Amended:	06/28/09	Bill No:	ABx3 40
Tax:	Fuel User Fee Law	Author:	Evans
Related Bills:	SBx3 31 (Ducheny) ABx3 2 (Evans) ABx3 39 (Evans)		

This analysis only addresses the provisions that impact the Board.

BILL SUMMARY

This budget trailer bill makes various statutory changes necessary to implement modifications to the 2009-10 Budget Act. As related to the Board, this bill would require, on and after October 1, 2009, a person purchasing fuel for use to pay a user fee in the amount of eighteen cents (\$0.18) per gallon of fuel used.

ANALYSIS

CURRENT LAW

Current federal law (Section 4081 of the Internal Revenue Code) imposes an excise tax on producers of \$0.184 per gallon on the removal of gasoline from a terminal or refinery, or upon importers for the entry of gasoline into the United States. This section also imposes an excise tax on undyed diesel fuel at a rate of \$0.244 per gallon. The federal excise tax rate on jet fuel intended for noncommercial use is \$0.219, except under specified circumstances.

Under the Motor Vehicle Fuel (MVF) Tax Law (Part 2 (commencing with Section 7301) of Division 2 of the Revenue and Taxation Code), the state imposes an excise tax of \$0.18 per gallon on the removal of motor vehicle fuel at the terminal rack level, upon entry into the state, and upon other occurrence. The Aircraft Jet Fuel Tax, which is a state excise tax of \$0.02 imposed on the aircraft jet fuel dealer for each gallon of aircraft jet fuel sold to an aircraft jet fuel user, or used by the dealer as an aircraft jet fuel user, is also included in the MVF Tax Law.

Under the Diesel Fuel Tax Law (Part 31 (commencing with Section 60001) of Division 2 of the Revenue and Taxation Code), the state imposes an excise tax of \$0.18 per gallon on the removal of diesel fuel at the terminal rack level, upon entry into the state, and upon other occurrences.

The Sales and Use Tax Law imposes a sales or use tax on the gross receipts from the sale of, and on the sales price of, tangible personal property, unless specifically exempted by statute. Existing law expressly *includes* within the definition of “gross receipts” and “sales price” the amount of any tax imposed by the United States upon producers and importers and the amount of any tax imposed by the state under the MVF Tax Law. Included in the MVF Tax Law is the Aircraft Jet Fuel Tax. The law expressly *excludes* from the definition of “gross receipts” and “sales price” the amount of any tax imposed upon diesel fuel pursuant to the Diesel Fuel Tax Law.

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Therefore, under the existing Sales and Use Tax Law, the computation of sales tax on the sale of gasoline includes the 18.4 cents per gallon imposed at the federal level and the 18 cents per gallon imposed by the State. With respect to sales of diesel fuel and aircraft jet fuel, the computation of sales and use tax includes the federal excise tax of \$0.244 per gallon on diesel fuel and the state excise tax of \$0.02 per gallon for jet fuel and the federal excise tax of \$0.219 per gallon for jet fuel.

PROPOSED LAW

This bill would add Part 32 (commencing with Section 61001) to Division 2 of the Revenue and Taxation Code to enact the Fuel User Fee Law, which would require a person purchasing fuel for use to pay an eighteen cent (\$0.18) per gallon user fee for each gallon of fuel used.

License. This bill would require every retailer and every supplier to be licensed. It would be unlawful for any person to be a retailer or supplier without first securing such a license.

Fee Collection. Every retailer would be required to collect the user fee from each user at the time the fuel is sold or delivered to the user. A supplier would be required to pre-collect the user fee on specified occurrences, and, if a sale does not occur at the time of imposition of the pre-collection obligation, the supplier would be required to pay the user fee required to be pre-collected.

Returns and Payments. Each retailer would be required to file with the Board monthly returns, which may include, but not be limited to, electronic media showing the number of gallons of fuel received, by transaction, and the total number of gallons of fuel sold within this state during each calendar month, the amount of pre-collected user fee paid during the month and the amount of user fee collected or otherwise required to be collected during the month covered by the return, and other information as the Board deems necessary.

Each supplier would be required to prepare and file electronically with the Board a monthly return showing, by transaction, the number of gallons of fuel received and the number of gallons of fuel removed, sold for resale, or entered within this state, the amount of pre-collected user fee collected or otherwise required to be pre-collected for the month covered by the return, and other information as the Board deems necessary.

Each retailer and supplier would be required to file a return on or before the last day of the month following the monthly period to which it relates, together with a remittance payable to the Board for the amount of the fee due.

Every user would be liable for the user fee until the user fee has been paid to the state and directly remitted to the board; however, payment to a registered retailer would be sufficient to relieve the user from further liability for the user fee.

Administration. The Board would be required to administer and collect the fee in accordance with the Fee Collection Procedures Law (Part 30 (commencing with Section 55001) of Division 2 of the Revenue and Taxation Code. Where an administrative provision in the Fee Collection Procedures Law is inconsistent with an administrative provision under the Fuel User Fee Law, the administrative provision Fuel User Fee Law would be applicable.

The Fee Collection Procedures Law contains "generic" administrative provisions for the administration and collection of fee programs to be administered by the Board. It was added to the Revenue and Taxation Code to allow bills establishing a new fee to reference this law, thereby only requiring a minimal number of sections within the bill to provide the necessary administrative provisions. Among other things, the Fee Collection Procedures Law includes collection, reporting, refund, and appeals provisions, as well as providing the Board the authority to adopt regulations relating to the administration and enforcement of the Fee Collection Procedures Law.

The Board would be authorized to adopt regulations to implement the Fuel User Fee Law.

Disposition of Proceeds. Revenues generated from the proposed fee would be deposited in the State Treasury and credited to the MVF Account in the Transportation Revenue Fund. Upon appropriation, these funds would be available for expenditure, allocation, or transfer, as provided, including expenditures for the following purposes:

- To pay authorized refunds, including refunds due on account of judgments for the return of fees illegally collected.
- To the Controller, to carry out any duties imposed upon him or her by the Fuel User Fee Law.
- To the Board, to carry out any duties imposed upon it by the Fuel User Fee Law.
- To pay the pro rata share of the overhead and general administrative expense of the Controller and the Board attributable to duties imposed by the Fuel User Fee Law. The pro rata share is payable upon presentation of a claim against any appropriation from the MVF Account for the support of the Controller or the Board, as the case may be.

Subject to specified provisions, the money deposited to the credit of the MVF Account would be transferred to the State Transportation Fund, which would be continued in existence, as provided.

Operative Date. The bill would become effective the 91st day after adjournment of the Third Extraordinary Session; however, the fuel user fee would become operative October 1, 2009.

BACKGROUND

Governor Arnold Schwarzenegger vetoed a pair of budget bills last winter that contained a similar fuel tax and fee scheme. The bills were as follows:

Assembly Bill x1 2 (Evans, 2008) would have repealed both the MVF and Diesel Fuel Tax Laws. This was a budget trailer bill that, as discussed below, had a companion measure to impose a fuel user fee on both gasoline and diesel fuels.

Senate Bill x1 11 (Ducheny, 2008) would have imposed a user fee of \$0.39 per gallon on gasoline and a user fee of \$0.31 per gallon on diesel fuel.

Although passed by the Legislature, the Governor vetoed both bills. In his veto messages the Governor cited the following similar message:

"I am returning Senate Bill x1 11 without my signature because it is part of a package of bills that does not deal with California's current budget and economic crisis. This package of bills punishes Californians by raising revenue without providing permanent and ongoing cuts, does not create jobs or stimulate our economy, does not allow government to run more efficiently in California, and makes no attempt to keep people in their homes."

COMMENTS

1. **This bill should contain a specific appropriation to the Board.** This bill proposes a fee to be imposed as of October 1, 2009, which is in the middle of the state's fiscal year. In order to begin to develop the feepayer base, reporting forms, and computer programs, an adequate appropriation would be required to cover the Board's administrative start-up costs that would not be identified in the Board's 2009-10 budget.

2. **Would the Board have sufficient time to implement the new fee program?** To effectively implement this bill, it would be necessary for the Board to notify and register feepayers (approximately 750 wholesalers and 12,000 retailers to identify and register, in addition to our existing taxpayer base), develop computer programs, hire and train key staff, create necessary forms and schedules, and answer taxpayer inquiries. These functions should take place before the fee becomes operative. Board staff estimates that it would take approximately six months to implement the new fee program proposed by this bill.

This bill currently provides the Board approximately three months to implement the new fee program. As such, Board staff has serious concerns about successfully implementing the new fee program in such a short amount of time. It is suggested that the bill be amended to provide for a delayed operative date to the first day of the month six months after the bill is enacted. This would provide the Board with sufficient lead-time to successfully implement the bill.

Furthermore, the bill should be amended to authorize the Board to adopt emergency regulations as necessary to implement the proposed fuel user fee program.

3. **Suggested technical amendments.** There are numerous technical concerns with this bill that need to be addressed in order for the Board to successfully administer the proposed fee program. In part, these concerns are as follows:

- There are two additional bills within the budget package that propose to repeal the MVF Tax Law and Diesel Fuel Tax Law (ABx3 2 and ABx3 39). With those tax laws repealed, the following provisions should be amended into the proposed fuel fee law:
 - Chapters 4 (commencing with Section 60110) and 4.5 (commencing with Section 60130) of Diesel Fuel Tax Law to apply to all interstate users. These provisions are necessary within the fee law for the Board to administer the International Fuel Tax Agreement (IFTA).
 - Provisions related to dyed diesel fuel, including exemptions, penalties, and notices, from Chapter 3(commencing with Section 60100) of the Diesel Fuel Tax Law.

- Seizure and sale and notice of qualified motor vehicles from Article 3 (commencing with Section 60441) of Chapter 7 of the Diesel Fuel Tax Law.
 - All the backup tax provisions provided in Chapter 2 of the MVF and Diesel Fuel Tax Laws and related liability provisions in Sections 7727 and 60361.5, and including exemptions from the backup tax. Since these provisions are repealed by AB3x 39, the Board would have no authority to pursue a user of dyed diesel on the highway, or fuel for which a claim for the fee has been refunded or the product was converted for use as a fuel and used on the highway.
 - The various licensing and reporting requirements for non-suppliers and non-retailers (i.e., train operators, terminal operators, government entities, exempt bus operators, qualified highway vehicle operators, and pipeline and vessel operators). These provisions are necessary for matching and refund purposes.
- Regarding Section 61004: Refine definition of “alcohol” to indicate that the ethanol or methanol is denatured to make it a fuel-grade product.
 - Add a definition for “Alcohol Fuel” to mean all blends of gasoline, and alcohol containing 15 percent or less gasoline. In addition, all other references to alcohol should also be changed to alcohol fuel to avoid assessing tax on E85-type fuel twice (once under the existing Use Fuel Tax Law and again under the proposed fuel user fee).
 - Add a definition for gasohol to mean all blends of gasoline, and alcohol containing more than 15 percent gasoline.
 - Add a definition for government entity similar to existing Section 60043 to mean this state and its political subdivisions except for a political subdivision that is only an exempt bus operator.
 - Regarding Section 61301: Remove the exemptions for diesel in paragraphs (14)(A) through (D), which apply to exemptions from the back-up tax and not blanket exemptions. These categories are required of users to either register and file periodic claims for refund or report their dyed fuel usage.
 - Regarding Section 61301: Subdivision (a)(5) should only address motor vehicle fuel, and not all fuel.
 - Regarding Section 61630: Subdivisions (a), (e), (f) and (g) should apply to all fuel, not just motor vehicle fuel. Also, subdivision (b) should include fuel carried from this state in the fuel tank of an aircraft.
 - Add a provision for sales of diesel fuel to the US Government, similar to Diesel Fuel Tax Law Section 60501(a)(4)(H).
 - Add a provision for sales of diesel fuel lost in the ordinary course of handling, transportation, or storage, similar to Diesel Fuel Tax Section 60501 (a)(4)(G).
 - Add a section similar to MVF Tax Law Section 8101.1, which allows a refund of the fuel fee for fuel used in the operation of a motor vehicle on United States Department of Agriculture roads.

- Add a section similar to MVF Tax Law Section 8101.5, which would prevent a refund of the fee for motor vehicle fuel used in propelling aircraft.
 - Add a section similar to MVF Tax Law Section 8101.6, which would allow for a partial refund of the motor vehicle fee (\$0.06) for public transportation.
 - Add a section similar to MVF Tax Law Section 8101.7, which would prevent a refund of the fee for motor vehicle fuel used in vessels.
4. **State sales tax revenues.** Sales and use tax is due based on the gross receipts from, or sales price of, tangible personal property in this state. The proposed fee would be imposed upon persons purchasing fuel for use, and not the retailers who sell the fuel. If retailers separately state the fee on the receipts they issue to their customers, the retailers are not passing on expenses to the purchaser but are instead collecting the fee from the purchaser as required by statute. Therefore, the fee would not be included in gross receipts and not subject to the sales or use tax.
- In addition to separately stating the user fee on receipts, retailers have the option to post on the service station premises, in a location visible to purchasers, a notice to the effect that the user fee required to be collected by the retailer is included in the price of the fuel, and it shall be presumed that the user fee is included in the cost of the fuel. In this case it also appears that such amounts would not be included in gross receipts and not subject to the sales or use tax.
5. **How would this bill impact tax-paid fuel in inventory?** The excise tax is imposed on the removal of motor vehicle fuel and diesel fuel at the terminal rack. The terminal rack level is a level in the distribution chain at a refinery or at a storage and distribution facility at the end of a pipeline where diesel fuel is 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.
- AB x3 2 (Evans) and ABx3 39 (Evans) propose to make the MVF and Diesel Fuel Tax Laws inoperative on and after October 1, 2009. Also on this date, this measure would impose a fuel user fee. As such, all tax-paid fuel in inventory within the distribution chain would be subject to the proposed fee at the time the fuel is sold or delivered to the user. Since this measure is silent with respect to credits for tax-paid fuel, it is unclear whether any credit for the excise tax would be allowed on the sale or delivery of tax-paid fuel to a user and upon which the fuel user fee would be due.
6. **Tax evasion.** With the transition from a tax to a fee the Board is concerned that there could be increased instances of abuse and evasion schemes. The bill does not limit who may issue an exemption certificate, only that it be issued for exempt purposes. In order to address possible abuse of the exemption certificates, the Board would suggest limiting those who may issue an exemption certificate and require other users of fuel in an exempt manner to file periodic claims for refunds. Additionally, with the new reporting structure, from a supplier to a retailer to a consumer, the Board will see a substantial increase in the number of registrants and therefore increased opportunities for evasion. To assist in deterring and combating evasion efforts, the Board would suggest adding both misdemeanor and felony provisions as punishments for evasion.
7. **Legal challenges of any new fee program might be made on the grounds that the fee is a tax.** In July 1997, the California Supreme Court held in *Sinclair Paint*

Company v. State Board of Equalization (1997) 15 Cal.4th 866 that the Childhood Lead Poisoning Prevention Act of 1991 imposed bona fide regulatory fees and not taxes requiring a two-thirds vote of the Legislature under Proposition 13. In summary, the Court found that while the Act did not directly regulate by conferring a specific benefit on, or granting a privilege to, those who pay the fee, it nevertheless imposed regulatory fees under the police power by requiring manufacturers and others whose products have exposed children to lead contamination to bear a fair share of the cost of mitigating those products' adverse health effects.

Although this measure has been keyed by the Legislative Counsel as a majority vote bill, opponents of this measure might question whether the fee imposed is in legal effect "taxes" required to be enacted by a two-thirds vote of the Legislature.

8. **Related legislation.** SBx3 31 (Ducheny) contains provisions identical to this bill (ABx3 40). In addition, ABx3 2 (Evans) and ABx3 39 (Evans), which are companion measures to this bill and SBx3 31, would make the MVF Tax Law and Diesel Fuel Tax Law inoperative on October 1, 2009, and repeal both laws on January 1, 2010. The fuel user fee proposed by this bill is intended to replace the excise fuel tax revenue structure for the state's primary transportation fuels. If ABx3 2 or ABx3 39 is successfully signed into law, thus repealing the MVF and Diesel Fuel Tax Law, would the state have the proper statutory authority to impose any tax or fee upon MVF or diesel fuel, if the fuel user fee proposed by this measure is found to be invalid?

COST ESTIMATE

The Board would incur substantial non-absorbable costs to adequately develop and administer a new fee program. Costs could be related to identifying and registering new fuel retailers and wholesalers, developing related computer programs, processing returns, payments, claims for refunds, exemption forms, and carrying out compliance and audit efforts to ensure proper reporting, along with developing regulations, training staff, and answering inquiries from the public.

Furthermore, this bill would eliminate the Controller's motor vehicle fuel collection and refund functions, which would be added to the Board's workload. Therefore, the Board would incur additional costs to develop computer programs and for additional staff to administer these new responsibilities along with the resources needed to maintain, collect, audit, and process refunds for the new feepayers.

The costs associated with administering the provisions in this bill, operative October 1, 2009, are estimated to be \$8.57 million for fiscal year 2009-10, \$12 million for fiscal year 2010-11, \$14.3 million for fiscal year 2011-12, and \$14.4 million for each fiscal year thereafter.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Current state law imposes an excise tax of \$0.18 per gallon on the removal of motor vehicle fuel and diesel fuel at the terminal rack level. State law also imposes an excise tax of \$0.02 per gallon on the aircraft jet fuel. Current federal law imposes an excise tax on producers of \$0.184 per gallon on the removal of gasoline from a terminal or refinery, or upon importers for the entry of gasoline into the United States. Federal law also

imposes an excise tax on undyed diesel fuel at a rate of \$0.244 per gallon and a federal excise tax of \$0.219 on jet fuel intended for noncommercial use.

Under current Sales and Use Tax Law, the current state excise tax of \$0.18 per gallon on gasoline and the federal excise tax on producers of \$0.184 per gallon are subject to the sales tax, as is the state and federal excise tax on jet fuel. In relation to diesel fuel, only the federal excise tax of \$0.244 per gallon is subject to the sales tax.

Under this proposal, a retailer would be required to collect the \$0.18 per gallon user fee from each user, at the time the fuel is sold to the user, and would require the fee to be pre-collected by a supplier on specified occurrences. Suppliers and retailers would need to be licensed by the Board. The sales and use tax would not apply to the proposed fee. Under the related proposal, ABx3 39 (Budget Comm.), the MVF Tax Law, which includes the Aircraft Jet Fuel Tax, is repealed.

Gasoline: According to the Board’s FY 2007-08 Annual Report, Table 2, total gasoline excise taxes (\$0.18 per gallon) revenue was \$2.8 billion, a decrease from the FY 2006-07, which had gasoline excise tax revenue of \$2.85 billion. We are using this data as a basis for our estimate because the proposed user fee is also \$0.18 per gallon.

For FY 2008-09, we estimated total gasoline excises tax revenue to be \$2.7 billion; this is about a 5% decline from FY 2007-08. We used the same ratio decline for FY 2009-10 and estimated \$2.5 billion in user fee revenues. Since the proposal’s operative date is on and after October 1, 2009, user fee revenues in FY 2009-10 (9 months) is estimated to be \$1.9 billion (75% × \$2.5 billion = \$1.9 billion).

With respect to 2010-11 and 2011-12, we used the Department of Finance’s (DOF) taxable sales forecast as the basis; an increase of 5.1% and 8.1% is forecasted respectively.

Diesel: Based on the Board’s diesel consumption data, we estimated \$483 million in diesel user fee revenues in FY 2008-09. This is about a 10% decline from FY 2007-08. We used the same ratio decline for FY 2009-10 and estimated \$434 million in user fee revenues. Since the proposal takes effect on or after October 1, 2009, user fee revenues in FY 2009-10 (9 months) is estimated to be \$325 million (75% × \$434 million = \$325 million). The DOF forecast ratios used for gasoline were also used to estimate diesel revenues for FY 2010-11 and FY 2011-12.

<u>User Fee Revenue Estimate</u>			
(in millions)			
	Gasoline	Diesel	Total Revenue
FY 2009-10	\$1,885	\$325	\$2,210
FY 2010-11	\$2,641	\$456	\$3,097
FY 2011-12	\$2,855	\$493	\$3,348

Sales & Use Tax Loss – Gasoline & Jet Fuel:

The sales and use tax would not apply to the fee proposed. The following table depicts the estimated amount of sales and use tax loss related to the repeal of the MVF Tax (gasoline and jet fuel):

<u>Sales & Use Tax Revenue Loss (Gasoline & Jet Fuel)</u>				
(in millions)				
	State (6%)	Fiscal Recovery (0.25%)	Local (2.75%)	Total Loss
FY 2009-10	\$113	\$5	\$52	\$170
FY 2010-11	\$159	\$7	\$73	\$238
FY 2011-12	\$171	\$7	\$79	\$257

Jet Fuel Tax Loss:

<u>Jet Fuel Tax Revenue Loss</u>	
(in millions)	
	Total Loss
FY 2009-10	\$2.1
FY 2010-11	\$3.0
FY 2011-12	\$3.2

REVENUE SUMMARY

This bill would generate an estimated \$2.2 billion in fee revenues in 2009-10 (9 months), \$3.1 billion in 2010-11 and \$3.4 billion in 2011-12.

This measure would indirectly incur an estimated \$170 million loss in sales and use tax (gasoline and jet fuel) in 2009-10 (9 months), \$238 million in 2010-11 and \$257 in 2011-12. Further, this measure would also indirectly result in an estimated loss of \$2.1 million in jet fuel excise tax revenues in 2009-10 (9 months), \$3 million in 2010-11 and \$3.2 million in 2011-12.

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