



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended	04/06/06	Bill No:	AB 2325
Tax:	Motor Vehicle Fuel	Author:	Nation
Related Bills:			

BILL SUMMARY

This bill would provide for an excise tax rate increase on motor vehicle fuel (gasoline) by 5 cents (\$0.05) per gallon, beginning January 1, 2007, and would increase the tax rate in 5 cent (\$0.05) increments each year for five years for a total increase of 25 cents (\$0.25).

ANALYSIS

Current Law

Under the Motor Vehicle Fuel Tax Law (Part 2 of Division 2 of the Revenue and Taxation Code, commencing with section 7301), the state imposes an excise tax of \$0.18 per gallon on the removal of motor vehicle fuel (gasoline) at the refinery or terminal rack, upon entry into the state, and upon sale to an unlicensed person.

The Sales and Use Tax Law expressly includes within the definition of “sales price” and “gross receipts” 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 Motor Vehicle Fuel Tax Law.

Proposed Law

This bill would add Section 7361.1 of the Motor Vehicle Fuel Tax Law to provide for an increase in the excise tax imposed on gasoline as follows:

- On and after January 1, 2007, and before January 1, 2008, the additional tax shall be five cents (\$0.05) per gallon.
- On and after January 1, 2008, and before January 1, 2009, the additional tax shall be ten cents (\$0.10) per gallon.
- On and after January 1, 2009, and before January 1, 2010, the additional tax shall be fifteen cents (\$0.15) per gallon.
- On and after January 1, 2010, and before January 1, 2011, the additional tax shall be twenty cents (\$0.20) per gallon.
- On and after January 1, 2011, the additional tax shall be twenty-five cents (\$0.25) per gallon.

The revenues imposed by the rate increase would be deposited into the State Highway Account, the California Energy Independence Fund, and the California Energy Independence Rebate Fund, the latter two established in the Treasury by this bill, according to the following formula:

- Fifty percent allocated to the State Highway Account for the specific purpose of funding projects nominated by regional transportation planning agencies for the Regional Transportation Improvement Program (RTIP). The distribution would mimic the current process established under the State Transportation Improvement Program, but with 100 percent funding allocated to the RTIP. None of the new revenue would be used for the Interregional Transportation Improvement Program.

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- Twenty-five percent allocated to the California Energy Independence Fund, which shall be used only for the purpose of funding the research and development of alternative energy resources.
- Twenty-five percent allocated to the California Energy Independence Rebate Fund, which shall be used only for the purpose of providing rebates to any consumer of an alternative fuel vehicle.

For purposes of this section, “alternative fuel vehicle” means either a vehicle that runs on nonpetroleum fuel, including electricity, ethanol, biodiesel, hydrogen, methanol, or natural gas that has been determined by the State Air Resources Board to meet applicable vehicular emission standards, or a hybrid vehicle, a plug-in hybrid vehicle, and vehicles that can run on petroleum fuel blended with nonpetroleum ingredients such as E85 or B20.

Background

In 1990, voters approved Senate Constitutional Amendment 1 (Proposition 111) in the June direct primary election. Approval of this measure made operative Assembly Bill 471 (Ch. 106, Stats. 1989) and Senate Bill 300 (Ch. 105, Stats. 1989). These bills, among other things, increased the rate of tax imposed on most motor vehicle fuels from \$0.09 to \$0.14 per gallon, effective August 1, 1990. Further, on January 1, 1991, and each January 1 thereafter through 1994, the excise tax increased by \$0.01 per gallon to the current \$0.18 per gallon.

In 2000, Assembly Bill 2114 (Ch. 1053, Longville) changed the point of imposition of the tax up the chain of distribution from the first distribution of the fuel to the removal of the fuel from the refinery or terminal rack. The bill also provided for a backup tax, which applies to the sale and/or delivery of gasoline into the fuel tank of a motor vehicle on which the tax has not been paid or the tax on the fuel has been refunded. The bill also provided for a floor stock tax.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author and is intended to provide a dedicated source of funding for regional transportation projects and to fund alternative energy solutions to fossil fuels, as well as to provide rebates to encourage the purchase of alternative fuel vehicles.
2. **The bill should contain a floor stock tax.** A floor stock tax serves to equalize the excise tax paid on those gallons of fuel held on inventory by a wholesaler or retailer prior to the effective date of a tax increase and on those gallons purchased after the tax increase. Having a large gasoline inventory before a tax rate increase takes effect can bring about a small windfall to a seller, who can raise the selling price of the gasoline purchased prior to the increase and attribute the increase in price to the tax rate increase. However, the additional funds collected are profit to the seller and not excise tax paid to the state. A floor stock tax mitigates this windfall.
3. **Suggested technical amendments.** Board staff is available to work with the author’s office in drafting appropriate amendments to address the following concerns:
 - According to the author’s staff, it is the intent of the bill to provide for an exemption from the increase in the fuel tax rate for certain taxpayers. Currently, the bill is adding an exemption to the Personal Income Tax Law to exempt a

taxpayer with an unspecified income from the income tax. It has been explained to the author's staff that the fuel excise tax is imposed upon the supplier at the time the fuel is removed from the rack. It is not imposed directly on an individual who purchases gasoline at a retail station.

- The Board has concerns regarding the deposit, appropriation, fund expenditure, and transfer of funds with respect to the California Energy Independence Fund and the California Energy Independence Rebate Fund. The bill should also specify which agencies would administer these proposed funds.
4. **This measure would not affect diesel or alternative fuels.** Diesel fuel is taxed under the Diesel Fuel Tax Law. Alternative fuels, such as liquefied petroleum gas, compressed natural gas, ethanol, and methanol are taxed under the Use Fuel Tax Law. This bill is not intended to increase the tax rate for any of those fuels.
 5. **State sales tax revenues.** Existing Sales and Use Tax 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 tax imposed by the state under the Motor Vehicle Fuel Tax Law. Accordingly, the sales tax applies to both the federal and the state excise tax in addition to the sales price of the gasoline itself.

The following is an example of the price per gallon of gasoline computed on a tax-included basis:

Sales price per gallon of gasoline net of all taxes	\$2.240
Federal excise Tax	.184
State excise Tax	.180
Total	\$2.604
Sales tax reimbursement computed at 7¼% of \$2.604	.189
Total tax-included price per gallon	\$2.793

Therefore, if, as a result of this bill, the excise tax on gasoline is increased, then the state sales tax on gasoline would generate corresponding additional revenues.

6. **An increase in the gasoline tax typically increases evasion.** The Board assumes that an increase of 25 cents per gallon, which would more than double the present state tax rate and increase the price of fuel, would cause a significant increase in the incidence of tax evasion.

COST ESTIMATE

A detailed cost estimate is pending. However, the Board would incur significant costs as a result of passage of this measure for notifying taxpayers, developing returns, computer programming, developing and carrying out compliance and audit efforts to ensure proper reporting, and increasing investigative activities. From experience, the Board would anticipate the increase in fuel excise tax rates to invite riskier tax evasion schemes. In order to properly protect the state's revenue from increased incidences of

tax evasion, the Board would incur higher audit and compliance staff costs with each additional increase in the excise tax rate.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

The Motor Vehicle Fuel Tax Law imposes a tax of \$0.18 per gallon of fuel and requires, if the federal fuel tax is reduced below the rate of \$0.09 per gallon and federal financial allocations to this state are reduced or eliminated, that the state tax rate be increased so that the combined state and federal tax rate per gallon equals 27 cents. This bill would increase the excise tax on motor vehicle fuel by five cents (\$0.05) per gallon beginning January 1, 2007, and increase the motor vehicle fuel tax each subsequent calendar year (CY) in five cent increments to a total of 25 cents per gallon as of January 1, 2011, and thereafter.

In calendar year 2005, taxable distribution of motor vehicle fuel amounted to 15.9 billion gallons. Over the past five years, taxable distribution has increased at an average annual rate of 1.5%. We estimate that the taxable distribution in CY 2007 will amount to 16.4 billion gallons of motor vehicle fuel and will increase by 1.5% per year to 17.4 billion gallons in CY 2011. Since the excise tax on fuel is included in the gross receipts from the retail sale of the fuel, as tangible personal property, an increase in fuel excise tax will result in additional sales and use tax revenue. The revenue impact of this bill is as follows:

Revenue Summary

	CY 2007	CY 2008	CY 2009	CY 2010	CY 2011
	(unless otherwise stated, all the amounts are in millions)				
Estimated growth increase		1.5%	1.5%	1.5%	1.5%
Estimated taxable distribution (gallons)	16,399	16,645	16,895	17,148	17,406
Rate increase	5¢	10¢	15¢	20¢	25¢
Fuel tax revenue increase	\$ 820	\$ 1,665	\$ 2,534	\$ 3,430	\$ 4,351
State Sales Tax (5.00%)	\$ 41	\$ 83	\$ 127	\$ 171	\$ 218
Fiscal Recovery Fund (0.25%)	2	4	6	9	11
Local Tax (2.00%)	16	33	51	69	87
District Tax (0.68%)	6	11	17	23	30
State and local tax revenue	\$ 65	\$ 131	\$ 201	\$ 272	\$ 346
Total revenue increase	\$ 885	\$ 1,796	\$ 2,735	\$ 3,702	\$ 4,697

For calendar year 2012 and beyond, the increased motor vehicle fuel tax revenue would amount to \$4.4 billion that would be increasing at an annual rate of 1.5% and result in \$350 million in additional State and local sales and use tax revenue on gasoline.

Analysis prepared by:	John Cortez	916-445-6662	04/20/06
Revenue estimate by:	Bill Benson, Jr.	916-445-0840	
Contact:	Margaret S. Shedd	916-322-2376	

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