

SUBJECT: Rewriting the motor-fuel tax code and moving the tax collection point

COMMITTEE: Ways and Means — committee substitute recommended

VOTE: 8 ayes — Wilson, McCall, Pitts, Hilderbran, Luna, Paxton, Ritter, Woolley
0 nays
1 absent — J. Keffer

WITNESSES: For — Al Howard
Against — None
On — Robert Nichols, Texas Transportation Commission

BACKGROUND: Tax Code, ch. 153 imposes motor-fuel taxes (MFTs) on the sale of gasoline and diesel fuel and sets forth collection procedures for fuel distributors and the comptroller. The tax rates for both gasoline and diesel fuel are 20 cents per gallon and are paid by motorists and other end users. Tax-free diesel for certain users is dyed to identify it as being used for tax-exempt purposes. Certain agricultural users, however, may buy clear diesel fuel tax-free for off-road use.

Texas collects the gasoline tax from about 850 distributors (monthly) and interstate truckers (quarterly). The state collects the diesel-fuel tax from about 13,500 suppliers (monthly) and interstate truckers (quarterly). About 20 other states collect MFTs at the terminal level, known as the “rack.” Typically, a terminal is a tank farm, underground pipeline outlet, or other facility where distributors fill their tanker trucks with fuel before delivering it to service stations and other retailers.

DIGEST: CSHB 2458 would repeal Tax Code, ch. 153 and replace it with new ch. 162, which would:

- move the MFT collection point from the distributor level to the terminal level;

- replace the existing tax's delivery-based framework with one based on the amount of fuel removed from terminals;
- continue the licensing of motor-fuel retailers and terminal operators;
- set up a new filing allowance schedule for remitting MFTs on gasoline and diesel fuel;
- limit the purchase of tax-free diesel fuel to "dyed" diesel, except for independent school districts and the federal government;
- preserve all existing exceptions, including off-road and agricultural use, and the aviation fuel exemption;
- eliminate refund claims for tax-exempt use of gasoline and diesel fuel in off-road equipment; and
- tighten control of imported and exported fuel and require importers and exporters to register with the state.

Collection point transfer. CSHB 2458 would shift MFT collection from distributors, who buy fuel tax-free from intermediate storage facilities for retail sale, to suppliers, who own either the fuel, the storage terminals, or both. Both distributors and suppliers still would have to file reports and maintain records, but suppliers would remit taxes based on the amount of fuel that distributors obtained for delivery and sale.

Auxiliary highway usage taxes. In order for the comptroller to collect taxes on untaxed fuel being transported or consumed on roadways, an additional tax would be imposed for that purpose at the same 20-cent-per-gallon rate.

Tax payments and credit. Suppliers would have to remit MFTs to the state by the 25th day of the month following the date of fuel sales, as in current law. Distributors could defer their tax payments to suppliers until the 23rd day of the following month. Suppliers would have 60 days to request credits from the comptroller for taxes remitted by suppliers but not paid by distributors.

Diesel exemption refund claims. Users of "clear" diesel for tax-exempt purposes no longer could claim tax refunds. The comptroller would grant refunds only for exempt uses of "dyed" diesel and gasoline.

The bill would take effect September 1, 2003.

**SUPPORTERS
SAY:**

CSHB 2458 would track federal MFT collection policy adopted by 20 other states, enlisting Texas in a nationwide effort to coordinate state fuel-tax systems. This relatively simple change, advocated by Gov. Perry, would increase revenue to the state at a time when it is sorely needed, without raising the MFT rate. The new revenue would include federal matching funds based on gallons taxed, currently an unknown quantity. The bill would eliminate the dual method of collecting from gasoline distributors and interstate truckers and from diesel fuel suppliers and truckers.

It makes good fiscal sense to base MFTs on fuel removal, rather than delivery. This method would reflect more accurately the volumes being sold at the point of assessment. Taxes would be assessed on the amount of fuel that suppliers disbursed from storage facilities at the “loading rack,” the highest point in the petroleum distribution chain.

This change would allow the state to use 111 terminals’ automated systems for tax calculation and remittance, reducing human error. Collection efficiency would increase as the number of tax filers would fall from more than 14,000, based on comptroller reports, to less than 1,000. Enforcement costs should decrease with the filing of mandatory reports by both suppliers and distributors that could be used to verify data without field auditing. When audits were needed, the paper trail would be clearer, because fuel would have changed hands fewer times before being taxed. This should reduce the opportunity for tax evasion and fraud which, along with payment by wire transfer, should increase revenue by \$50 million to \$75 million a year, according to the Texas Department of Transportation (TxDOT).

The collection allowance rate is appropriate and would not change, because distributors as well as suppliers would continue to have responsibilities to the state, especially for auditing purposes. Such allowances are common in the Texas tax system. They provide value for the state by making most tax collection more economical than if the state conducted it. Many businesses believe their actual costs of recordkeeping, remittance, and liability are 6 to 7 percent. The current 2 percent rate would be divided between distributors, who would keep 1.75 percent of collections for continuing to file reports, and suppliers, who would receive 0.25 percent for their new collection costs.

The industry has agreed to the credit and “float” provisions of CSHB 2458. These provisions would not hamper retailers’ ability to do business, hurt their cash flow, or require them to seek alternative sources of credit to cover tax payments.

The conversion to dyed diesel would help track exempt uses. Conversion should not be that difficult or costly for most terminal operators that currently do not offer dyed diesel. Once demand increases from farmers and others who have bought both clear and dyed diesel up to now, availability of dyed diesel should increase.

**OPPONENTS
SAY:**

CSHB 2458 is unnecessary. It seeks to fix a system that is not broken but is performing well. The projections of additional revenue due to rack collection of MFTs are exaggerated. The comptroller, for example, calculated the fiscal note with no revenue gain due to fraud reduction, one of the major reasons touted for changing the collection point. Other states’ revenue gains have been short-lived, tending to level off once new systems are in place.

The bill would retain too large a collection allowance and would not allocate it fairly. Instead of reducing the 2 percent reimbursement rate, it merely would divide it among two different segments of the petroleum marketing chain. Suppliers, many of them multinational integrated oil companies that own terminals, would have to do most of the tax collecting but would keep only 0.25 percent of collections. Distributors, who would do virtually no collecting, would keep 1.75 percent. They also would lose interest earned on cash deposits because the “float” period, the time between tax collections and tax payments, would be shortened by two days.

The omission of language authorizing refund claims for tax-exempt uses of gasoline and diesel fuel could hurt farmers and other agribusinesses. If refund claims for dyed diesel are not reinstated along with refund claims for gasoline and clear diesel, it could force some of the 22 terminals not selling dyed diesel to acquire, activate, or upgrade dye injection equipment.

**OTHER
OPPONENTS
SAY:**

MFTs should be based on price, not volume, so the state could take advantage of inflation and insulate the revenue stream from the effects of improved fuel efficiency and motorists’ driving habits.

The effective date should be changed to September 1, 2004, to give the comptroller sufficient time to retool internal systems and processes and to change applicable rules.

NOTES:

The author plans to offer floor amendments that would add language similar to current law allowing refund claims of MFT tax exemptions for off-road, agricultural, and recreational uses of gasoline and dyed diesel fuel. These changes are estimated to result in a general revenue gain of close to \$1 million in fiscal 2004-05. Among other changes, the amendments also would:

- remove the state's mandatory deferred tax payments involving fuel sold by suppliers to distributors for export;
- allow exporters to use interim payment and proof methods to verify the tax liability of a destination state until other states fully authorize payments by Texas suppliers (sunsets in 2005); and
- change the bill's effective date to January 1, 2004.

According to the bill's fiscal note, the state would gain about \$134.7 million in net revenue during fiscal 2004-05. A projected general revenue loss of about \$21 million would be offset by a gain of about \$117 million for the State Highway Fund and \$39 million for the Available School Fund. Added administrative costs to the comptroller for software revision, processing of refunds for tax overpayment, personnel, and other costs would account for more than \$8 million of the general revenue loss. Most of the gains would result from eliminating the diesel exemption for air conditioning usage and omitting language allowing refund claims for exempt uses of gasoline and dyed diesel, which effectively would route unclaimed exemption allocations to the highway and school funds instead of to general revenue.

The committee substitute changed the filed version of HB 2458 by repealing the existing MFT statute and replacing it with a new chapter; replacing the current usage-based tax with a terminal/refinery removal tax; and imposing an auxiliary highway usage tax applicable if the removal tax was not paid.

The companion bill, SB 1308 by Bivins, has been referred to the Senate Finance Committee.