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FISCAL IMPACT REPORT

ORIGINAL DATE 2/22/17

SPONSOR Townsend LAST UPDATED _____ HB 487

SHORT TITLE Tax Gas At The Rack SB _____

ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					R or NR **	Fund Affected
FY17	FY18	FY19	FY20	FY21		
\$0.0	\$0.0	Up to \$3,000.0	Up to \$3,000.0	Up to \$3,000.0	Recurring	Gasoline Tax beneficiaries (gasoline tax compliance gain)
\$0.0	\$0.0	Up to \$2,200.0	Up to \$2,200.0	Up to \$2,200.0	Recurring	Special Fuels Tax beneficiaries (special fuels tax compliance gain)
\$0.0	\$0.0	\$3,000.0	\$3,000.0	\$3,000.0	Recurring	Gasoline Tax beneficiaries (repeal of deductions for gasoline gallons sold on Indian land to <u>non-Indian</u> members)
\$0.0	\$0.0	Delayed	Delayed	Delayed	Recurring	Gasoline Tax beneficiaries (cancel tribal gas tax sharing agreements)
\$0.0	\$0.0	(\$6,000.0)	(\$6,000.0)	(\$6,000.0)	Recurring	Special Fuels Tax beneficiaries (repeal of special fuel users tax and permits)
\$0.0	\$0.0	Up to (\$3,100.0)	Up to (\$3,100.0)	Up to (\$3,100.0)	Recurring	Gasoline and Special Fuels Tax beneficiaries (state agency gasoline tax exemption)
\$0.0	\$0.0	Unknown (negative)	Unknown (negative)	Unknown (negative)	Recurring	Gasoline and Special Fuels Tax beneficiaries (local governments gasoline tax exemption)

Parenthesis () indicate expenditure decreases. ** R = recurring; NR = non-recurring

Partially duplicates HB 509

SOURCES OF INFORMATION

LFC Files

Responses Received From

Department of Transportation (DOT)
Indian Affairs Department (IAD)

Responses Not Received From

Taxation and Revenue Department

SUMMARY

Synopsis of Bill

House Bill 487 moves the collection point of the gasoline excise tax, the special fuel excise tax and the petroleum products loading fee from the “distributor level” to the “terminal rack level” or to the point when the fuels are imported into New Mexico, beginning July 1, 2018. This bill also replaces the Gasoline Tax Act and the Special Fuels Supplier Tax Act with a new Motor Fuel Taxes Act.

The bill identifies the following transactions as exempt from the motor fuels tax:

- Fuel sold to the United States for exclusive use by the government;
- Fuel sold to the State of New Mexico, all local governments and any agency or instrumentality thereof, for exclusive use by those governments;
- Fuel sold by an Indian nation, tribe or pueblo for the exclusive use by the member;
- Exported fuel;
- Fuel moved between suppliers;
- Dyed special fuel sold or delivered between suppliers;
- Dyed special fuel sold by a supplier or permissive supplier to a distributor or by a distributor to another distributor; and
- Dyed special fuel delivered by a license holder into the fuel supply tanks of railway engines, motorboats or refrigeration units or other stationary equipment powered by a separate motor from a separate fuel supply tank.

More specifically, this bill cancels the gas tax sharing agreement between New Mexico Department of Transportation (DOT) and the Pueblos of Santo Domingo and Nambe, and eliminates deductions for gasoline gallons sold at retail on Indian land. As stated above, gasoline gallons sold by an Indian nation to a member of the Indian nation would be exempted. The bill also cancels the monthly transfer of \$33,333 to the General Fund.

This bill does not provide any exemption for dyed gasoline used, and allows a new provision that a licensed distributor or importer “*that makes timely payments of the taxes ... is entitled to retain an amount equal to one and seventy-five thousandths percent of the total taxes to be paid to the supplier or permissive supplier to cover administrative expenses.*” Both these provisions are a departure from existing law.

By repealing the Special Fuels Supplier Tax Act and replacing it with the Motor Fuel Taxes Act, this bill also repeals the special fuel user tax (Sections 7-16A-11 through 7-16A-16), which is currently regulated by the International Fuel Tax Agreement (IFTA) to which the State of New Mexico is a party. Under the current law, all commercial vehicles (that are all the vehicles in excess of 26,000 pounds) pay the special fuel user tax. The tax paid by special fuel “users” is based on the miles travelled in New Mexico, no matter if the special fuel was purchased in another state, or how much fuel was actually consumed in New Mexico.

This bill also repeals the temporary special user fuel permits (Sections 7-16A-19 through 7-16A-21) which apply to all special fuel users that are not enrolled into the IFTA program. This permit fee, along with a special fuel user tax, is mainly collected at the Ports of Entry.

The bill includes various requirements and procedures for licensing, reporting, bonding and other security for taxes, tax remittance, record-keeping, filing returns, credits and refunds, and enforcement. Additionally, the bill cleans up references to the repealed fuel tax acts and replaces them with references to the Motor Fuel Taxes Act.

FISCAL IMPLICATIONS

Currently, gasoline and special fuel taxes are imposed upon distributors when fuel is loaded at the rack or imported into the state. The taxes are currently paid by fuel distributors who file monthly Combined Fuel Tax returns with the Taxation and Revenue Department. The bill proposes that, beginning in July 2018, the fuel taxes would be imposed on rack operators for any fuel removed from the bulk terminal. The taxes imposed on imports into New Mexico would be similar to existing provisions.

DOT notes this bill substantially changes all the motor fuel tax regulation and definitions, and mostly adopts what appears to be Texas statutory language for establishing new provisions on licenses, returns and payments, refunds, etc. Because legislative changes are extensive and complex, DOT's bill analysis does not address the administrative changes, as this will require a more careful analysis and more time, but their analysis intends to point out the most relevant changes and impacts.

By moving to a system of motor fuel taxation at the rack, only a handful of taxpayers (about 10 major) will report and pay the tax, rather than the roughly 150 distributors under current law. Since tax would be imposed at the first, highest level, and since there are few taxpayers involved, DOT points out voluntary compliance is maximized, and audited compliance is attainable. The traditional, ballpark estimate for tax compliance gains by moving to tax at the rack is in the 2 to 5 percent range; however, this gain would be dependent on how compliant taxpayers are already within the existing tax system prior to implementation of tax at the rack.

In New Mexico's case, DOT indicates tax compliance gains might well be toward the low end of that range. A 2 percent compliance gain would be worth about \$3 million for gasoline tax (\$2.2 million road fund) and about \$2.2 million for special fuels tax (\$2 million road fund). Although taxation at the rack could presumably increase compliance and ease audit burdens, the total potential \$5.2 million in revenue gains would depend on the current degree of tax compliance.

This bill exempts the State of New Mexico, all local governments and any agency or instrumentality from paying the gasoline excise tax, whereas current law only exempts special fuel consumed by state and local governments. This exemption will result in a revenue loss for gasoline taxes currently paid by state agencies and local governments. The FY18 operating budget total for transportation fuel was about \$18 million. Applying the current gasoline tax rate to this total, there is potential for a revenue loss of up to \$3.1 million in unpaid fuel taxes by state agencies. There will be an additional unknown but negative revenue impact of local governments' gasoline tax exemption. DOT points out this revenue loss could offset any compliance gains from moving to a system of taxation at the rack.

HB 487 eliminates deductions for gasoline gallons sold on Indian land, while gasoline gallons sold by an Indian nation to an Indian member will be exempted. Based on the 2010 Census population data, the New Mexico total tribal population was about 138,800, representing 6.7

percent of the total New Mexico population.¹ Assuming an average per capita gasoline consumption of 400 gallons per year, DOT estimates about 55 million of gallons might not be taxed. In FY 2016, the total amount of gasoline that was deducted under the tribal retail deduction was about 72 million of gallons. DOT estimates this new provision would be worth about \$3 million in revenue gain under the gasoline tax.

DOT indicates this bill does not reimpose the special fuel users tax (Sections 7-16A-11 through 7-16A-16), which includes reference to New Mexico's participation in the International Fuel Tax Agreement (IFTA), and does not reimpose the temporary special user fuel permits (Sections 7-16A-19 through 7-16A-21), resulting in a revenue loss of about \$6 million per year.

As noted above, this bill cancels the gas tax sharing agreements between DOT, TRD and the Pueblos of Santo Domingo and Nambe. According to DOT, pursuant to the gasoline tax sharing agreements, the two Pueblos are entitled to receive an amount equal to 40 percent of the net receipts attributable to the gasoline tax paid to DOT on 2.5 million gallons of gasoline each month, which represents about \$2 million per Pueblo, or \$4.1 million total. A decennial agreement with the two Pueblos was signed in 2014, and consequently DOT may be obliged to continue paying the two Pueblos until 2024, thus delaying any revenue gain from this source.

While this bill does not provide any exemption for dyed gasoline, DOT states cancelling the dyed gasoline exemption should not have any significant impact on gasoline revenue. In FY16, less than 1,000 gallons of gasoline were reported as dyed, so the revenue gain associated with disallowing dyed gasoline would be insignificant.

Overall, because of the bill's exemption for gasoline used by state and local governments, and the lack of a special fuel user tax, DOT states the overall fiscal impact of the bill is a revenue loss, probably in the range of a few million dollars. Recipient entities sharing the impact of the revenue loss include the State Road Fund, the state-administered Local Governments Road Fund, local governments, and other state funds receiving gasoline tax revenue.

SIGNIFICANT ISSUES

The Federal Highway Administration (FHWA), as well as the literature (*Identifying and Quantifying Rates of State Motor Fuel Tax Evasion*, NCHRP - Report 623), indicate taxing at the terminal rack for motor fuel is one key measure a government can take towards increasing motor fuel excise tax compliance. Moving the point of taxation to the terminal rack decreases the opportunity for tax evasion and reduces the numbers of taxpayers, decreasing the administrative and enforcement burden on the collection agency (i.e., the Taxation and Revenue Department).

Approximately 20 states have imposed a tax at the rack, including the surrounding states of Arizona, Texas, and Oklahoma. Many of those states have moved to this system of taxation in the last 10 years. Taxing at the rack has long been the method of taxation recommended by federal tax officials as a means to minimize tax evasion.

The New Mexico Indian Affairs Department (IAD) notes in *Oklahoma Tax Commission v. Chickasaw Nation*, 515 U.S. 450 [1995], the U.S. Supreme Court held that a state cannot tax gasoline purchased by Indians in Indian country absent congressional authorization. IAD points

¹ Published on BBER website, http://bber.unm.edu/tribal_tables.

out there is verbiage throughout the bill that exempts members of Indian nations, tribes and pueblos from the imposition of taxes regarding fuel and identifies that license holders will be given a tax credit for fuel sold to sovereign Indian nations as long as the sale occurs on tribal lands.

ADMINISTRATIVE IMPLICATIONS

While there is a presumed administrative impact to TRD, a response from the department is needed to determine the degree and cost.

DUPLICATION

This bill partially duplicates HB509, which also moves to a tax-at-the-rack system and increases the fuel excise tax rates.

TECHNICAL ISSUES

DOT points out the revenue distribution language for the new Motor Fuel Taxes Act is revised in Sections 45 and 46 and the changes do have a fiscal impact that may not be intended. Currently, only distributions from the gasoline tax are made to the state aviation fund and to municipalities and counties. However, this bill would make distributions to the funds from the motor fuels tax (including gasoline and special fuels). Consideration might be given to amending Section 45, Subsection B (on page 74, line 5) to reference the taxes “*imposed on gasoline* [~~collected~~] pursuant to the”. Similarly, in Section 46, Subsection A (on page 75, line 4) the reference might be to the “... taxes imposed on gasoline pursuant to the ...”.

DOT also indicates a number of other statutory revenue distributions under the current gasoline tax are not included or adjusted in this bill.

In Section 63, Subsection F (on page 111, lines 12 and 13) the references to “Gasoline Tax Act” and “Special Fuels Supplier Tax Act” should be “Motor Fuel Taxes Act”.

OTHER SUBSTANTIVE ISSUES

Large, complex bills such as this increase the possibility for errors to be introduced in either drafting or in theory regarding implementation and effects. New Mexico has experienced such errors before in far smaller bills that had serious negative consequences for the general fund, such as a prior attempt to “fix” the high-wage jobs tax credit that created a new loophole, leading to costs rising by more than an order of magnitude. The significant number of interactive effects in this bill could have unanticipated consequences that could lead to revenue shortfalls for the state and local governments or unanticipated tax increases for certain groups of taxpayers.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy:** Revenue should be adequate to fund needed government services.
2. **Efficiency:** Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity:** Different taxpayers should be treated fairly.
4. **Simplicity:** Collection should be simple and easily understood.
5. **Accountability:** Preferences should be easy to monitor and evaluate