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REVISE MOTOR CARRIER FUEL TAX RATE; REMOVE DIESEL FUEL TAX DISCOUNT

House Bill 5806 (Substitute H-1)
Sponsor: Rep. Jud Gilbert II

House Bill 5807 as introduced
Sponsor: Rep. Rick Johnson

First Analysis (5-23-00)
Committee: Transportation

THE APPARENT PROBLEM:

The diesel discount was enacted twenty years ago, in order to keep the diesel fuel pump price at Michigan truck stops competitive with out-of-state truck stops. (See *BACKGROUND INFORMATION*, "Pump Prices", below.)

According to a report by the Citizen's Research Council of Michigan (CRC) entitled "The Taxation of Diesel Fuel" published in November, 1997, Michigan is one of only a few states in the nation that levies sales taxes on motor fuel sales, and that includes federal motor fuel taxes with the fuel price as part of the sales tax base. As a result, an additional cost must be paid for fuel purchases in Michigan, creating a potential disincentive for buyers.

To compensate for the higher diesel fuel costs, the diesel fuel provisions of the motor fuel tax act were amended in 1980 to establish a six-cent-per-gallon discount (sometimes called the "six-cent credit") for fuel delivered into a vehicle bearing a motor carrier permit. At the same time this discount was added to the diesel fuel tax act, a companion law was enacted. That act, called the Motor Carrier Fuel Tax Act, effectively licenses commercial motor vehicles, describes how the credit is earned, as well as how quarterly tax returns are filed in January, April, July, and October, at which time taxes owed are remitted. This act allows Michigan to collect a tax on the fuel that is <u>used</u> in the state, wherever that fuel is purchased. After these acts were adopted, truckers driving in Michigan could no longer avoid the state tax by purchasing fuel in another, lower cost, state.

The two tax acts constitute the diesel fuel tax program, and both work together, each complementing the other. The discount program is administered by the Department of Treasury Bureau of Revenue, and according to committee testimony, the quarterly tax return and credit process is cumbersome. What is more, the program itself is confusing, since the calculation of the credit varies depending on the type of vehicle, and the use for the fuel. As the CRC report explains in some detail, the precise interaction effects of the two taxes depend on the particular situation: the type of vehicle; whether the fuel is being purchased for travel in Michigan; whether the fuel is being purchased for out-of-state travel; or whether the fuel is being purchased outside Michigan for travel in Michigan. (See *BACKGROUND INFORMATION*, "Website," below). However, generally, the interaction of the two taxes requires motor carriers to pay the diesel fuel tax "at the pump." (Wholesale distributors actually pay motor fuel taxes in Michigan but the additional cost is passed on to the final purchaser, so that the taxes can be considered to be paid at the pump.) To ensure that out-of-state fuel purchasers also pay for the privilege of using Michigan roads, motor carriers pay the Motor Carrier Fuel Tax on fuel used in Michigan but for which no diesel fuel tax has been paid.

The Department of Transportation points out that the current system of diesel fuel tax collection has numerous opportunities for tax avoidance: the tax is not easy to explain; it is difficult for the taxpayer to pay; and, there is small risk of enforcement. Indeed, the department notes that the delinquency rate for motor carriers filing tax returns with the Department of Treasury has increased over the past three years. (According to the department's analysis, the intrastate motor carriers delinquency rates for the years 1997, 1998, and 1999 were 25 percent, 31 percent, and 27 percent, respectively, while the delinquency rates for the Michigan international fuel tax agreement carriers during those same years were seven percent, 13 percent, and 17 percent.) The department has estimated that an additional $8 million could be collected annually if tax collections were streamlined.

THE CONTENT OF THE BILLS:

House Bill 5806 would amend the Motor Carrier Fuel Tax Act (MCL 207.101 et al.) to revise the rate and remove certain of the reporting requirements under the motor carrier fuel tax program.

Under current law a motor carrier licensed under the act pays a road tax calculated on the amount of motor fuel that is consumed in qualified commercial motor vehicles on the public road or highways within the state. The tax is at the rate of 21 cents per gallon. The bill would eliminate this tax rate, and specify instead that the tax be at the rate provided under section 2(2)(c) of Public Act 150 of 1927. [This provision of the Motor Fuel Tax Act specifies that the tax imposed on diesel motor fuel after July 31, 1997 is 15 cents a gallon.]

The bill also would eliminate the provision that allows a motor carrier to credit against the tax imposed by the act an amount equal to six cents per gallon of the sales tax paid on diesel fuel purchased in this state. The credit is claimed on each quarterly return for fuel purchased during the preceding calendar quarter.

The bill would define "motor carrier" to mean a person who operates or causes to be operated a qualified commercial motor vehicle on a public road or highway in this state, and at least one other state or province of Canada, or who is licensed under the international fuel tax agreement. Currently the law defines "motor carrier" more broadly to mean a person who operates or causes to be operated a qualified commercial motor vehicle on a public road or highway in this state. The bill also would modify the definition of "qualified commercial motor vehicle" to specify that it would not include a road tractor, truck, or truck tractor used exclusively in this state. Currently the law specifies that "qualified commercial motor vehicle" does not include a recreational vehicle, or a road tractor, truck, or truck tractor owned by a farmer and used in connection with the farmer's farming operation and not used for hire, or a school bus, a bus defined and certificated under the Motor Bus Transportation Act, or a bus operated by a public transit agency.

House Bill 5807 would amend the Motor Fuel Tax Act (MCL 207.108 et al.) to remove the diesel fuel tax discount, and provide for the allocation of revenue from tax collections under the act.

Currently the law specifies that in the case of diesel motor fuel, the amount of tax payable shall be reduced by the amount of discount allowed under section 22 for each gallon sold by the supplier. Section 22 specifies that there shall be allowed a discount of six cents per gallon of the tax imposed on diesel motor fuel if the diesel motor fuel is delivered into the fuel supply tanks of a commercial motor vehicle licensed under the Motor Carrier Fuel Tax Act. These provisions of the law would be eliminated by House Bill 5807.

Further, current law also specifies that the tax on diesel motor fuel sold and delivered in Michigan is collected by the supplier and paid over monthly to the revenue division of the Department of Treasury, except that the retail dealer shall pay over monthly to the department six cents of the tax imposed for each gallon sold for delivery into or supplied into the fuel supply tanks of a motor vehicle that is not a commercial motor vehicle licensed under the motor carrier fuel tax act, and eligible for the discount allowed. House Bill 5807 also would eliminate this provision.

Finally, House Bill 5807 specifies that all money collected under these provisions would be deposited in the state treasury to the credit of the Michigan Transportation Fund, except $8 million, which would be credited to the State Trunk Line Fund for state trunk line projects. Currently all money collected is credited to the Michigan Transportation Fund.

The bill also would correct an inaccurate date reference in the current law.

BACKGROUND INFORMATION:

Pump prices. According to the Citizens Research Council (CRC), the diesel fuel tax imposed at the pump is effectively a partial prepayment of the final tax owed. Because the diesel fuel tax is paid, and the Motor Carrier Fuel Tax allows a credit for this payment, revenues equal to 9 cents per gallon from motor fuel taxes levied on motor carriers are attributed to diesel fuel taxes. This, in addition to the six cents collected from the Motor Carrier Fuel Tax, yields the total of 15 cents per gallon.

Further, the Republican Programs and Research staff in a memorandum about the diesel fuel tax bills dated 5-18-00, explains that in part, the purpose of collecting from motor carriers a lower diesel fuel tax at the pump (9 cents), then collecting an additional 12 cents per gallon when filing quarterly reports (with a 6 cents refund), is to keep diesel fuel prices at the pump artificially low. That way, truck stops near the state's border with Ohio and Indiana are able to advertise a lower diesel fuel price than truck stops in neighboring states. Under current law, Michigan truck stops advertise a diesel fuel price that includes 15 cents per gallon in state taxes (9 cents diesel fuel tax and 6 cents sales tax) at the pump, while truck stops in Indiana advertise a fuel price that includes 16 cents per gallon in state taxes at the pump. Indiana's system of diesel fuel tax collection is similar to Michigan's, in that the tax collected at the pump is only a partial payment of all taxes due on diesel fuel purchases. In fact, truckers in Michigan eventually pay 21 cents per gallon in state diesel fuel and sales taxes, while truckers in Indiana eventually pay 27 cents in state diesel fuel and sales taxes.

Citizens Research Council Website. A full explanation of the interaction of the two taxes--the diesel fuel tax, and the motor carrier fuel tax--can be found in Memorandum 1047, "The Taxation of Diesel Fuel," published in November 1997. This document is available on the CRC website at http://www.crcmich.org/.

FISCAL IMPLICATIONS:

The House Fiscal Agency notes that it has not yet determined whether House Bill 5806 would have a fiscal impact.

The agency also notes that House Bill 5806 simplifies the collection of the motor carrier fuel tax. The bill would reduce the tax from 21 cents per gallon to 15 cents per gallon but eliminate the six cent sales tax discount, so that effectively there would be no change in the tax rate. The bill references the Motor Fuel Tax Act, linking the two taxes. If both bills were to pass as written, the effective tax rate for both the motor fuel tax and the motor carrier fuel tax would be 15 cents per gallon. Finally, about House Bill 5806, the agency notes that the Department of Treasury has indicated that House Bill 5806 would reduce by six cents per gallon the tax on diesel fuel used in Michigan but purchased outside of Michigan, but would increase by six cents per gallon the tax on diesel fuel used outside Michigan but purchased in Michigan.

The House Fiscal Agency notes that with regard to House Bill 5807, the Department of Transportation has estimated that the bill would increase revenue from the tax by $8 million per year. However, the House Fiscal Agency has not yet independently verified this figure.

About House Bill 5807 the agency also notes that the bill would amend the Motor Fuel Tax act to eliminate the six cent per gallon discount on the diesel fuel tax for commercial vehicles. The elimination of this discount would effectively simplify the collection of this tax.

Further, the House Fiscal Agency notes that the bill would also earmark the $8 million anticipated revenue increase to the State Trunk Line Fund (STF), rather than to the Michigan Transportation Fund (MTF). Currently all diesel taxes collected under the Motor Fuel Tax Act are credited to the MTF. The department has identified this $8 million as one of the new revenue sources needed for debt service on Build Michigan III bonds.

If tax collections did increase by the $8 million per year as estimated by the department, the bill would increase state revenue by $8 million per year with no apparent fiscal impact on state costs or local costs or revenues. However, if tax collections increased by less than the bill's $8 million STF earmark, then state revenues would increase but there would be some decrease in local revenues, since local road agencies receive approximately 60 percent of the MFT distribution under the current Public Act 51 of 1951 formula, but receive no share of the State Trunk Line Fund. (5-18-00)

ARGUMENTS:

For:

These bills have been estimated to increase revenue by $8 million annually, which would allow the state a needed source of revenue for debt service on its new Build Michigan III bond program. They are part of a four-bill package that links the Build Michigan III program with a rewrite of Public Act 51 of 1951, the act that distributes transportation funding among different classes of roads and highways.

For:

The streamlined tax collection system proposed by these bills will provide efficiencies to the Department of Treasury from both a collection and audit standpoint. The current system of diesel fuel tax collection has numerous opportunities for tax avoidance: the tax is not easy to explain; it is difficult for the honest taxpayer to pay; and, there is small risk of enforcement. It is estimated that an additional $8 million will be collected annually. When the state simplifies the diesel fuel tax collection process, by shifting to collections from the wholesaler instead of quarterly from gas stations, it could increase collections substantially. According to the Department of Transportation analysis, a similar shift in the point of collection from the retail to the supplier level on a portion of the tax in 1993 resulted in a revenue increase of $12 million. Likewise, a shift from the retail to supplier as the point of collection in the State of Missouri also increased revenue by millions of dollars.

Against:

Although some have noted these bills would increase the diesel fuel tax collected at the pump (from 15 cents to 21 cents per gallon), they have argued that this would not increase the diesel fuel tax per se. However, according to an analysis done by the House Fiscal Agency and dated 5-22-00, these bills would change the cost of diesel fuel for two classes of commercial truckers: those who are interstate truckers and who purchase fuel in Michigan but who drive most of their miles out of state will experience an *increase* in their net tax of six cents per gallon. Further, interstate carriers who buy their fuel outside of Michigan but drive most of their miles in the state will experience a *decrease* in their net tax by six cents per gallon.

If the state wants to increase compliance in the diesel fuel tax program and raise more revenue through diesel tax collections, then the legislature should pass House Bill 5807. However, House Bill 5806 is not necessary. Indeed, the bill reverses a program that ensures parity among all motor carriers. The legislature put that program in place recently when it enacted Senate Bill 746 of 1995 as Public Act 584 of 1996, in an effort to ensure the same net tax rate for all motor carriers who use diesel fuel in Michigan.

Against:

These bills will cause widespread economic disruptions among truck stop operators, most especially those located in southwest Michigan, and perhaps within much of the diesel retail industry in Michigan's Lower Peninsula. The bills give diesel fuel purchasers the incentive to purchase their fuel elsewhere. This will harm family-owned businesses in Michigan, and likely force some out of business altogether. This is a high price to pay, when the only benefit is to reduce the paperwork for a select few, saving what are likely to be one-time costs in the administration of this program.

Against:

These bills do not address the real policy problem that the diesel discount was designed to eliminate when the program was enacted into law two decades ago. That problem is this: unlike 40 other states, Michigan charges sales tax on diesel fuel purchases. Further, Michigan includes in its sales tax base the federal fuel taxes; in effect the state imposes a tax on a tax. This tax burden increases total diesel fuel costs for buyers, and puts fuel retailers at a disadvantage with their competitors in other states. The focus of the legislature should be to eliminate that sales tax of diesel fuel, and make fuel retailers competitive with those in neighboring states.

POSITIONS:

The Department of Transportation supports the bills. (5-22-00)

The Department of Treasury supports the bills. (5-22-00)

The Michigan Trucking Association supports the bills. (5-22-00)

The Michigan Farm Bureau supports the bills. (5-22-00)

The Michigan Petroleum Association opposes the bills. (5-22-00)

The Hillsdale Policy Group opposes the bills. (5-22-00)

Analyst: J. Hunault

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.