

ARIZONA HOUSE OF REPRESENTATIVES
Fiftieth Legislature – First Regular Session

COMMITTEE ON WAYS AND MEANS

Minutes of Meeting
Monday, March 14, 2011
House Hearing Room 1 -- 2:00 p.m.

Chairman Harper called the meeting to order at 2:49 p.m. and attendance was noted by the secretary.

Members Present

Mr. Chabin
Mr. Farley
Mr. Gallego

Mr. Gray R
Mrs. Lesko
Mr. Mesnard

Mr. Olson
Mr. Vogt, Vice-Chairman
Mr. Harper, Chairman

Members Absent

None

Committee Action

SB1226 - DPA S/E (5-3-0-1)
SB1502 - NOT ASSIGNED

SB1512 - DP (8-0-0-1)
SB1552 - DP (7-1-0-1)

CONSIDERATION OF BILLS

SB1502 - fire districts; merger; consolidation - NOT ASSIGNED

Chairman Harper announced that SB1502 was not assigned to the Committee on Ways and Means and will not be heard.

SB1512 - technical correction; light pollution(now: bond election; informational pamphlet) - DO PASS

Alexander Blount, Majority Intern, stated that SB1512 modifies the information required to be included in a bond election pamphlet (Attachment 1). He explained the bill's provisions:

- Requires the informational pamphlet to include the estimated tax impact of debt service for the bonds on agricultural or other vacant property (Class 2).
 - Specifies that the estimated tax impact on Class 2 property be based on a value of \$100,000.
- Decreases the value for which the estimated tax impact on certain Class 1 property is based from \$2,500,000 to \$1,000,000.

Vice-Chairman Vogt moved that SB1512 do pass. The motion carried by a roll call vote of 8-0-0-1 (Attachment 2).

SB1552 - corporate tax allocation; sales factor - DO PASS

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that SB1552 allows a multistate service provider to elect to treat sales from services as being in this state to the extent that the purchaser of the service received the benefit of the service in Arizona (Attachment 3). Mr. Gonzalez-Plumhoff explained the following provisions of SB1552:

- Allows a multistate service provider to elect to treat sales from services as being in this state to the extent that the purchaser of the service received the benefit of the service in Arizona, beginning in tax year 2012.
- Specifies that the election must be made on the taxpayer's income tax return.
 - Stipulates that the election is effective retroactively for the full taxable year of the income tax return on which the election is made.
 - Stipulates that the election is binding on the taxpayer for at least five consecutive taxable years, regardless of whether the taxpayer no longer derives more than 85 percent of their sales from services provided to purchasers who receive the benefit of the service outside Arizona.
- Allows termination of the in-state election without the permission of the Department of Revenue (DOR) after the election has been in effect for five consecutive taxable years or on the acquisition or merger of the taxpayer.
- Allows termination of the in-state election prior to the expiration of the five taxable years with the permission of DOR.
- States that the termination must be made on the taxpayer's income tax return for the first taxable year in which the election is terminated.
- Defines *multistate service provider* to mean a taxpayer that derives more than 85 percent of its sales from services provided to purchasers who receive the benefit of the service outside this state in the taxable year of election.
 - Includes corporations that are owned or controlled directly or indirectly by the same interests or an affiliated group that are required by DOR to file a combined return, or who elect to, or are required to file a consolidated return.
 - Excludes sales to students receiving educational services at campuses physically located in Arizona from the 85 percent calculation.
- Defines *received the benefit of the service in this state* to mean that the services are received by the purchaser in this state.
 - Specifies that if the state where the services are received cannot be determined, the services are considered to be received at the home of the customer or at the office of the customer from which the services were ordered in the regular course of the customer's trade or business.
 - Specifies that if the ordering location cannot be determined, the services are considered to be received at the home or office of the customer to which the services were billed.
- States that the measure's provisions are not intended to affect, and shall not be cited or considered in the construction or interpretation of statute for taxable periods prior to the effective date of the legislation.

Chairman Harper announced the names of those who signed up in support of SB1552 but did not speak:

Matt Beckler, Vice President Tax, Apollo Group
Joseph Abate, Counsel, A T & T
Michael DiMaria, Director of Legal Issues, Qwest Communications
Jason Bagley, Government Affairs Manager, Intel Corporation
F. Rockne "Roc" Arnett, President, East Valley Partnership
Norman Moore, Attorney, Independent Colleges and Universities of Arizona (ICUA)
Courtney Gilstrap LeVinus, Tucson Metropolitan Chamber of Commerce
Lorna Romero, Director of Government Relations, Arizona Chamber of Commerce & Industry
Kevin McCarthy, President, Arizona Tax Research Association
Don Isaacson, Independent Colleges and Universities of Arizona (ICUA)
Matt Salmon, Lobbyist, Grand Canyon University
Brad Wright, Corporate Counsel, Apollo Group
Tom Dorn, Lobbyist, East Valley Chambers of Commerce Alliance
Ellen Poole, Executive Director, South West Region Government Relations, USAA
Wendy Briggs, Lobbyist, American Express
Michelle Bolton, Vice President of Public Affairs, Greater Phoenix Chamber of Commerce

Chairman Harper announced the names of those who signed up as neutral on SB1552 but did not speak:

Susan Anable, Manager, Government Relations, Cox Communications
Sean Laux, Legislative Liaison, Department of Revenue

Senator Rick Murphy, sponsor, requested the Members' support of SB1552.

Chairman Harper stated that he has not always been a supporter of the concept of the bill.

Vice-Chairman Vogt moved that SB1552 do pass. The motion carried by a roll call vote of 7-1-0-1 (Attachment 4).

Chairman Harper excused himself from the meeting and announced that Vice-Chairman Vogt will be acting as Chairman for the remainder of the meeting.

PRESENTATION: Two-tiered Diesel Tax

Arizona Department of Transportation

Kitty Decker, Senior Division Administrator, Arizona Department of Transportation (ADOT), introduced accompanying staff and provided the Members with a copy of the presentation (Attachment 5). The following information was included in the presentation:

Use Fuel (Diesel) Tax Two Rates:

- 18 cents per gallon for "light class" vehicles
 - Weigh 26,000 pounds or less OR
 - Not more than 2 axles
- 26 cents per gallon for "use class" vehicles

- Weigh more than 26,000 pounds OR
- More than 2 axles
- Approximately 93 percent of tax is collected from use class vehicles
- Arizona is the only state with two diesel tax rates at the pump

Two-tiered Use Fuel Tax History:

- 1997 to present - Use Fuel Vendor licensing required
- 1/1/98 - Two rates of tax: \$.27/\$.18 for Use Class/ Light Class
 - Implemented in response to elimination of the weight/distance tax
- 7/1/00 - Use class rate reduced to \$.26
- 8/9/01 - Tax rate labels required on pumps
- 9/21/06 - Penalty for misuse assessed against end-user

Two-tiered Use Fuel Tax ADOT Responsibilities:

- Licensing
- Refunds
- Compliance
- Accounting and Audits
- Other Administrative Issues

Fuel Tax Licensing Unit:

- Fuel Tax Licensing Unit issues three different types of licenses
 - Suppliers
 - Restricted distributors
 - Vendors (retailers)
- Vendor Licenses are required solely for the enforcement of diesel differential tax rate
- Vendor Licenses
 - 87 percent of all licenses issued
 - Approximately 60 percent of workload per week
 - More frequent and continuous activity
 - Decal requests/posting issues
 - Updated applications for new or closed locations
 - Miscellaneous tax issues

Fuel Tax Refund Compliance Unit:

- Arizona is a “pay and refund” state
 - Use Fuel tax is reported and paid on a monthly basis
 - Refunds granted upon request for exemptions
- Use Fuel refunds for diesel differential are the largest component of unit
- Other types of refunds:
 - Exports
 - Off-road use
 - Native American Exemptions
 - Miscellaneous
- Over 4,000 diesel differential refund requests
 - Average process time: 53 minutes

- Estimated man-hours per year: 3,566
- Refunds must be completed in 60 days or 11 percent interest applied (A.R.S. 28-5612)

Fuel Tax Evasion Unit:

- Enforcement of fuel tax laws and requirements
 - Only 5 enforcement officers for entire state
- Duties include:
 - Discovery of illegal imports/illegal blending
 - Use of dyed diesel on highways and streets
 - Misuse of diesel differential and vendor licensing
- Misuse and Vendor Licensing:
 - Inspections; surveillance; tips/reports
 - 25 percent -30 percent of time spent on enforcement of vendor requirements
- Increased enforcement since January, 2003
- Fiscal Year (FY) 2010:
 - Vendor license violations: 29
 - Vendor decal violations: 227
- Fiscal Year (FY) 2009:
 - Vendor license violations: 41
 - Vendor decal violations: 242
- End users - low level of awareness

Use Fuel Vendor Penalties:

- Decal penalties:
 - Civil penalty of \$100 per day/per pump for each day that diesel fuel is sold in fuel dispensers that are not properly labeled
 - If discovered; then vendor is given decals to come into compliance
- License Violations:
 - If vendor is discovered to be unlicensed, then cannot sell diesel until license is obtained
 - If selling of diesel continues while unlicensed, then \$100 per day penalty
 - No refunds for unlicensed vendors
- Civil Penalty on the end-user, not vendor:
 - \$1000 or \$10/gallon, whichever is greater; subsequent violation is the amount of the civil penalty times the number of violations
 - Plus the amount of the tax for the differential rate (8 cents per gallon)

Revenue Functions:

- Revenue Accounting Section
 - Daily accounting reports
 - Monthly accounting reports
- Receipts Accounting System
 - Processing of actual refunds
 - Work with State Treasurer's Office to have approximately 4,000 checks issued per year

Revenue Audit and Analysis:

- Audit leads; sampling
- Diesel differential:
 - Save at least 1,000 man-hours per year
 - 2010: 248 card lock assessments; \$382,000

Other Administrative Tasks:

- Time spent on:
 - Forms and Notices
 - Policies, procedures, rules and regulations
 - Miscellaneous responses to inquiries
 - Personnel requirements
- Storage/space requirements:
 - Retention schedules
 - Starting to eliminate these issues through electronic means

Use Fuel (Diesel) Gallons Sold:

- 736.8 million total gallons in FY 2010
- 747.3 million total gallons in FY 2009
- 882.4 million total gallons in FY 2008

Net Use Fuel Tax Collections:

- FY 2010 - \$171,308,245
- FY 2009 - \$173,930,895
- FY 2008 - \$207,859,050
- FY 2007 - \$210,281,755
- FY 2006 - \$213,460,036
- FY 2005 - \$194,368,181

Ms. Decker answered questions regarding the following:

- Weight fees
- Enforcement responsibilities
- ADOT proposals
- Indian reservation tax assessment
- Single tax projected savings

Arizona Petroleum Marketers Association

Andrea Martincic, Executive Director, Arizona Petroleum Marketers Association, provided the Members with a copy of the presentation (Attachment 6) and conveyed the following information:

Arizona - Pay and Refund State

- All diesel fuel is taxed at the higher diesel rate of 26 cents when it breaks bulk at the loading rack.
- Arizona's diesel fuel tax is collected and remitted by the fuel supplier to ADOT.

- The fuel supplier must add the tax to the price of the fuel to recover it from the consumer.
- Diesel suppliers and diesel vendors apply for refunds from ADOT.

Classes of Trade Affected by Two Diesel Tax Rates

- Bulk Tank Owners (no use fuel vendor license)
- Retail
 - All diesel pumps labeled 18 cents, or
 - All diesel pumps labeled 26 cents, or
 - Pumps labeled 18 cents and 26 cents
- Card lock facilities
- On-site mobile fueling

Bulk Tank Owner

- Must submit for refunds to ADOT for any light class vehicle fueling.
 - Refund process is time consuming, particularly for small businesses.
 - Must compile copies of all delivery invoices to show taxes paid and fueling records of light duty vehicles (This can be quite significant- usually all handwritten records).
 - Receive reimbursement from ADOT about 45 days later.

Use Fuel Vendors

- Retail sites with pumps labeled only at 18 cents
- Retail sites with pumps labeled only at 26 cents
- Truck stops with separated islands with pumps labeled at 18 cents and 26 cents
- Card lock facilities
- On-site mobile fueling

18-Cent Diesel Retailers

- These retailers have their diesel pumps labeled at 18 cents.
- Most canopies at these retail sites can NOT accommodate a heavy-duty vehicle.
- If a heavy-duty vehicle misfuels, ADOT can prosecute the vehicle owner.
- These retailers must still put in for ADOT refunds for all of the gallons of diesel sold at the 18-cent rate, since they had to pay the supplier the 26-cent rate.

26-Cent Diesel Retailers

- These retailers choose to post all of their diesel pumps at the 26-cent rate.
- If a light-duty user fuels here, they must go inside the store and receive their 8-cent tax differential from the clerk and fill out a store log to record the transaction.
- The retailer must use this log to file for a refund with ADOT.
- ADOT uses the same 50-gallon threshold in these audits, making it difficult for retailers to get a refund at times.

Truck Stops

- Many truck stops have separated islands with the pumps labeled 18 cents and 26 cents to accommodate different customers.
- Must constantly educate tourists (light-duty users) that there are two rates for diesel fuel in Arizona.

- Must track the light-duty gallons to put in for refunds and again run into audit issues with the 50-gallon threshold.
- Many trucks now have gasoline generators to run the electric in the cab due to new regulations restricting idling to less than 5 minutes.
- There are legitimate times when a heavy-duty vehicle needs to be on the “other side” of the island to fuel these generators.
- Can cause confusion for retailers and the customers.

Card Lock

- Card lock users can have potential difficulties with the two tax rates depending on how their card lock system is setup.
- If the fuel card is tied only to the driver and not the vehicle there is a greater potential for tax fraud.
- Out-of-state light class users have no way to get the tax differential back. The card host would not be an Arizona licensed supplier.

On-Site Mobile Fueling

- Delivering diesel into vehicles- usually commercial fleets.
- Charge the 26-cent rate unless a customer has a light class declaration on file.
- Most customers do not bother and are paying the 26-cent rate.
- Mobile fuel vendor only puts in for refunds if they are charging the customer 18 cents.

Use Fuel Vendor Audits

- ADOT audits go back three years but can go back further if records are available.
 - ADOT uses a 50-gallon threshold to determine if a purchase may have been at the improper rate.
 - Extremely problematic since many light-duty diesel vehicles have saddle tanks.
 - Audits - time consuming and a hassle.
 - Suppliers forced to turn over customer lists so that ADOT can investigate/prosecute end users based on the number of gallons the supplier sold.

End User Awareness - LOW

- Many customers with mixed fleets (light and heavy-duty) do not want to mess with tracking mileage of various vehicles and never put in for their differential payment - choose to pay 26 cents for everything.
- Out-of-state diesel drivers (problematic at retail level and card lock facilities).
- Even large Arizona companies with fleet have claimed they did not know Arizona had two tax rates.

Possible Solutions

- One rate of tax at the pump
 - No need for Motor Vehicle Division (MVD)/vendor interactions - savings for both.
 - Fairness: proper tax rate collected; level playing field.
- Could move to one rate at the pump 26 cents: Light-duty end user could get an 8-cent refund from the MVD (or income tax offset for registration of a diesel vehicle fuel efficiency):
 - No need for MVD/vendor interactions - savings for both.
 - Fairness: Proper tax rate likely collected; level playing field.

- Could move to one rate at the pump 18 cents: create a fuel surcharge on heavy-duty use class vehicles.
 - Would require additional monthly reporting and licensing with ADOT for intrastate users.

Ms. Martincic answered questions regarding the following:

- Differential Reimbursement
- Auditing
- Revenue neutrality projection for 24.5 cents flat rate

CONSIDERATION OF BILLS (CONTINUED)

SB1226 - county treasurers; investments; warrants; notice(now: city; town; levy limit override) - DO PASS AMENDED S/E **S/E: same subject**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, explained that the proposed Harper two-page strike-everything amendment dated 03/09/2011 (Attachment 7) to SB1226 allows certain municipalities to levy an additional secondary property tax to fund specific purposes called for and voted on by the public, through December 31, 2012 (Attachment 8).

Mrs. Lesko asked what other cities or towns are able to levy an additional secondary property tax as SB1226 allows; Mr. Gonzalez-Plumhoff replied none. Mrs. Lesko asked if the City of El Mirage has other options. Mr. Gonzalez-Plumhoff deferred to a representative from the City of El Mirage and offered that the ability to raise the municipal sales tax or primary property tax levies, if the limit has not already been reached, would be potential options.

Senator John Nelson, sponsor, stated that SB1226 is a simple bill and was not created by the present El Mirage City Council. Senator Nelson provided a brief history of the bill and the events leading to its drafting.

Lana Mook, Mayor, City of El Mirage, testified in support of SB1226, stating that the bill and the Harper strike-everything amendment are critical to El Mirage. She explained that the City's proximity to Luke Air Force Base limits economic development and asserted that a local Wal-Mart is the extent of the commercial tax base for the City. She stated that new City Council leadership has shifted the City's focus from fighting Luke Air Force Base to actively exploring methods of working around zoning challenges to create a more diverse and sustainable tax base. She stated that in three months, the City has begun to overcome its challenges and three new businesses are scheduled to break ground. Ms. Mook cited that a \$5 million budget deficit has been reduced by half. She described the many ways that the City has improved methods of cutting spending; these efforts still fall short and additional help is required. She urged the Members to support the bill and strike-everything amendment.

Vice-Chairman Vogt announced the names of those who signed up in support of SB1226 but did not speak:

Steve Campbell, Police Chief, City of El Mirage

Leah Hubbard, Special Assistant to the City Manager, City of El Mirage

David Moss, President and CEO, Surprise Regional Chamber of Commerce
Jack Lunsford, President and CEO, representing self
Joseph Brehm, Management Intern, City of Prescott

Vice-Chairman Vogt announced the names of those who signed up in opposition to SB1226 but did not speak:

Jose Borrajero, representing self
Lynne Weaver, Prop 13 Arizona

Mrs. Lesko moved that SB1226 do pass.

Mrs. Lesko moved that the Harper two-page strike-everything amendment dated 02/08/2011 be adopted. The motion carried.

Without objection, Mrs. Lesko withdrew the motion that the Harper two-page strike-everything amendment dated 02/08/2011 be adopted.

Mrs. Lesko moved that the Harper two-page strike-everything amendment dated 03/09/2011 (Attachment 8) be adopted. The motion carried.

Mrs. Lesko moved that SB1226 as amended do pass. The motion carried by a roll call vote of 5-3-0-1 (Attachment 9).

Without objection, the meeting adjourned at 3:45 p.m.

Charly Laube, Committee Secretary
May 23, 2011

(Original minutes, attachments and audio on file in the Office of the Chief Clerk; video archives available at <http://www.azleg.gov>)