OPTIONS TO ADDRESS REVENUE ADEQUACY FOR FUNDING OF HIGHWAY MAINTENANCE AND CONSTRUCTION AND TO IMPROVE EQUITY

BLUE RIBBON TAX REFORM COMMISSION
September 11-12, 2003

INTRODUCTION

From the testimony presented, it appears the revenues devoted to highway maintenance and construction are not adequate. The issue, then, becomes how to fund the deferred maintenance on existing roads, construction of new roads and other inter-modal development. This clearly has economic development implications.

If the commission determines that current revenues are insufficient to meet New Mexico's highway maintenance and construction and other transportation needs, there are a number of options for increasing revenues and reforming the road-funding tax structure. These options are in the areas of motor fuel excise taxes, the weight-distance tax, overweight and oversize fees and vehicle registration fees. The commission may also want to consider some options providing relief from the leased vehicle surcharge.

Revenue impacts for the various options are in the Revenue Impact Table attached. There is also additional background information on the various options in the report to the commission from the Selective Excise Tax Committee.

Arguments for and against the various proposals follow the discussion of the options in each area.

MOTOR FUEL EXCISE TAXES

OPTIONS
GASOLINE TAX

OPTION 1. Increase the Gasoline Tax Rate.
The gasoline tax rate may be increased in increments of one or more cents and increases of more than one cent could be phased in over several years. Each one cent of gasoline tax raises about $8.4 million on a full-year basis. Assuming about 950 to 1,000 gallons per year per household, the impact of each one-cent tax increase would be $9.50 to $10.00 per household per year.

ISSUES

- Will the increased revenue be directed 100 percent to the state road fund or distributed as it is now, with varying percentages of the tax directed to local governments and various funds, including the state road fund?
- Will the increase be implemented at one time or phased in over several years?

OPTION 2. Index the Gasoline Tax Rate.
Increase the gasoline tax rate over time by adding an indexing feature. Assuming the indexes grow at between two percent and four percent per year, index calculations would tend to add about 1/3 of a cent to 9/10 of a cent per year. Thus, given a provision requiring rounding down to the nearest whole cent, the tax rate would probably be revised by one cent every two or three years.

ISSUES

- What index should be used and which agency should compute, monitor and certify the tax rate indexing provision?
- How often should an indexing adjustment be allowed?
- What rounding convention will be used in the calculation?
- Will the increased revenue be directed 100 percent to the state road fund or distributed as it is now, with varying percentages of the tax revenue directed to local governments and various funds, including the state road fund?

OPTION 3. Eliminate Gross Receipts Tax Deduction for Gasoline.
Because gasoline is taxed under the Gasoline Tax Act, receipts from selling are exempt from the gross receipts tax. This proposal would remove the exemption, making gasoline subject to the gross receipts tax as well as the gasoline tax. The increased revenue from this option, for both state and local governments, is in the Revenue Impact Table.

ISSUES

- If this option is enacted, a decision will need to be made about distribution of revenues. Currently, gasoline tax revenues are all directed to state and local road funds and purposes. Gross receipts tax revenues are distributed between the state and local governments and, unless earmarked otherwise, may be used for general purposes.

OPTION 4. Remove the Gross Receipts Deduction for Gasoline but Create a New Deduction for Federal and State Gasoline Taxes.
This is nearly the same as the previous option. The difference is that a new gross receipts deduction would be created for the federal and state gasoline taxes paid on the gasoline sold. For the fiscal impact of this option, see the Revenue Impact Table.

ISSUES

- As for the previous option, a decision will need to be made about distribution of revenues. Currently, gasoline tax revenues are all directed to state and local road funds and purposes. Gross receipts tax revenues are distributed between the state and local governments and, unless earmarked otherwise, may be used for general purposes.

OPTION 5. Exempt from the Gasoline Tax the Gasoline Sold for Use in Boats.
This option proposes to exempt gasoline sold for use in boats from the gasoline tax. This is similar to the treatment of aviation gasoline and, like aviation gasoline, would be subject to the compensating tax. For the fiscal impact of this option, see the Revenue Impact Table attached.

ISSUES

- If motorboats are exempt from the gasoline tax, it would probably be appropriate to repeal the current gasoline tax distribution to the motorboat fuel tax fund. The fund is administered by the State Parks Division, with 75 percent of the money being used for construction, improvement and maintenance of boating facilities and 25 percent of the money used for other boating-related purposes.

OPTION 6. Develop a More Functional Fuel Tax Processing and Reporting System.
Absent tax at "the rack", increased enforcement efforts should be funded through the Taxation and Revenue Department to improve collection and enforcement of fuel taxes by developing and implementing a more functional fuel tax processing and reporting system that will provide support for adequate audit activity to stem noncompliance known as "leakage".

SPECIAL FUELS EXCISE TAX

OPTION 1. Increase the Special Fuels Excise Tax Rate.
The special fuels excise tax rate may be increased in increments of one or more cents, and

increases of more than one cent may be phased in over several years. Each one cent of special fuel tax raises about $4.4 million on a full-year basis.

ISSUES

- Will the increased revenue be directed 100 percent to the state road fund or distributed as it is now, with some of the revenue distributed to the local governments road fund?

- Will the tax increase take effect immediately or be phased in over time?

OPTION 2. Index the Special Fuels Excise Tax.
Assuming the indexes grow at between two percent and four percent per year, index calculations would tend to add about 1/3 of a cent to 9/10 of a cent per year. Thus, given a provision requiring rounding down to the nearest whole cent, the tax rate would probably be revised by one cent every two or three years.

The tax burden impact of a one-cent tax increase would tend to range from about $6.67 to $13.33 per year for a diesel pickup, assuming 15 mpg and from 10,000 to 20,000 miles driven per year.

The tax burden impact of a one-cent tax increase would tend to range from about $40.00 to $160.00 per year for a commercial heavy vehicle, assuming 5 mpg and from 20,000 to 80,000 miles driven per year.

ISSUES

- What index should be used and which agency should be responsible for computing, monitoring and certifying the tax rate indexing provision?

- What rounding convention will be used in the calculation?

- How often should an indexing adjustment be allowed?

- Will the increased revenue be directed 100 percent to the state road fund or distributed as it is now, with some of the revenue distributed to the local governments road fund?

OPTION 3. Eliminate the Gross Receipts Tax Deduction for Special Fuel.
Because special fuel is taxed under the Special Fuels Supplier Tax Act, receipts from selling are exempt from the gross receipts tax. This proposal would remove the exemption, making special fuel subject to the gross receipts tax as well as the special fuel excise tax. For the fiscal impact of this option, see the Revenue Impact Table.

ISSUES

- If this option is enacted, a decision will need to be made about distribution of revenues. Currently, special fuel excise tax revenues are all directed to state and local road funds and purposes. Gross receipts tax revenues are distributed between the state and local governments and, unless earmarked otherwise, may be used for general purposes.

OPTION 4. Remove the Gross Receipts Deduction for Special Fuel but Create a New Deduction for Federal and State Special Fuel Taxes.

This is nearly the same as the previous option. The difference is that a new gross receipts deduction would be created for the federal and state special fuel excise taxes paid on the special fuel sold. For the fiscal impact of this option, see the Revenue Impact Table.

ISSUES

- As for the previous option, a decision will need to be made about distribution of revenues. Currently, special fuel excise tax revenues are all directed to state and local road funds and purposes. Gross receipts tax revenues are distributed between the state and local governments, and, unless earmarked otherwise, may be used for general purposes.

PROS

- The motor fuel taxes are benefits taxes — those who use the system must pay for the system. If additional revenues are needed, it is appropriate for road users to pay additional taxes for their use of those roads.

- A number of states with low tax rates per gallon also impose additional sales taxes on gasoline.

- The benefits of motor fuel taxes are widely accepted by the public, and opposition to motor fuel tax increases typically is less vociferous than with other state taxes if the taxes are specifically earmarked for the roads.

- Motor fuel excise taxes generally are easier to administer and collect than other state taxes because the point of taxation may be limited to a few hundred distributors.

- Gasoline and special fuel taxes are a charge for the construction and maintenance of the public highways; they are user fees. Gross receipts tax is a tax to support the general activities of government. There is no reason why gross receipts tax should not apply to user fees such as the gasoline tax and special fuel excise tax. Receipts from selling other commodities subject to special excise taxes are also subject to the gross receipts tax. Examples include cigarettes and beer.

- If the option to impose gross receipts tax on gasoline or special fuel is adopted, the version that allows state and federal taxes to be deducted may be the better idea. This variation eliminates a tax-on-tax.

- Exempting gasoline used for boats from the gasoline tax is appropriate, since the gasoline tax is meant to be a charge for the use of the highways. However, the exemption should be accompanied by repeal of distribution of the revenues to the motorboat fuel tax fund.

- Without imposing fuel taxes at the rack, it is crucial to develop a more functional fuel tax processing and reporting system, especially for gasoline, to reduce the noncompliance problems that are referred to as leakage. Option 6 will maximize revenues from existing taxes.

CONS

- The motor fuel excise taxes are an inelastic state revenue source, that is, revenue is dependent upon gallons consumed, which is influenced by oil prices, motor vehicle fuel efficiency, alternative fuel sources and consumer driving patterns. Other road user taxes and fees are better sources of revenue.

- Some argue that drivers of passenger automobiles pay a disproportionately large share of highway costs when measured by their contribution to highway wear and tear. It is argued that motor fuel taxes violate equity because heavy trucks generate a disproportionate share of highway maintenance costs and those users should bear a higher proportion of the cost.

- Truckers argue that all consumers benefit from the current system because higher taxes on the industry would be passed to consumers through higher prices on consumer goods.

- There are good reasons not to impose the gross receipts tax on the sale of gasoline or special fuel. The popular will seems to be that any tax on gasoline must be earmarked for the highways. Unless the receipts from the gross receipts tax on gasoline are so earmarked, it will not be accepted by the public. If the receipts are to be earmarked, why not directly raise the unit gasoline tax by an equivalent amount?

- An argument against exempting gasoline for use in boats from the gasoline tax is that for the small benefit conferred, a large amount of time and effort will be involved in claiming and verifying the exemption. This exemption will be expensive to administer, if indeed enforcement is practicable.

- The motor fuel tax is a regressive tax, particularly in poor rural areas where residents must commute longer distances for work, shopping and other necessary activities.

WEIGHT-DISTANCE TAX AND OVERWEIGHT/OVERSIZE FEES

Adequacy continues to be an issue in funding the state road fund, and the weight-distance tax offers an alternative revenue source. Weight-distance tax, a unit tax, generates approximately $50 million per year. This tax provides a means to collect a user fee on heavy commercial vehicles doing the most damage to highways without imposing it on the public at large.

New Mexico has not adjusted the weight-distance rates for over 20 years. There also appear to be significant compliance problems involving reporting the weight-distance tax, including failure to file tax returns and pay tax. There are enforcement deficiencies as well. In fact, it seems the state has limited its enforcement efforts in the wake of the C.R. England Trucking lawsuit that questioned the validity of the $5.00 "cab card" fee imposed under the weight-distance tax.

Oversize permits are available to vehicles exceeding the state's height and width restrictions, for a fee of $15.00 per single trip or $60.00 per year. Transporters of manufactured homes are required to obtain single trip permits. Generally, the oversize vehicles are of less concern than overweight vehicles since most damage to the highways results from the weight, rather than the size, of a vehicle. These revenues are earmarked for the state road fund.

Overweight permits are available to vehicles exceeding the state's maximum weight restriction of 86,400 pounds for a fee of $15.00 per single trip. In some cases a $60.00 annual permit may be obtained "if the operation is to be within the vicinity of a municipality". Special overweight permits are available to liquid haulers, authorizing an increase of up to 25 percent in axle weight for liquid hauling tank vehicles, for a fee of $35.00 per single trip or $120 for an annual permit. These revenues are earmarked for the state road fund.

Options for raising revenues from the weight-distance tax and overweight/oversize permit fees follow. Pros and cons of those proposals follow the options.

OPTIONS

WEIGHT-DISTANCE TAX

OPTION 1. Increase the Weight-Distance Tax.
The Department of Transportation (DOT) suggested that a weight-distance tax increase of up to 80 percent could be justified on the basis of inflation since the tax rate was last adjusted some 20 years ago. Such an analysis, in isolation, does not take into account other taxes imposed on the trucking industry. While considering a tax increase scenario, it should be kept in mind that the gross receipts tax burden on trucking should also be considered. In-state trucking companies might benefit more from a tax reform package that raises weight-distance tax and provides gross

receipts tax relief. A 10.48 percent increase in weight-distance tax rates would raise about $5.5 million for a full year.

OVERWEIGHT/OVERSIZE VEHICLES

OPTION 1. Increase the Fee Schedule.

There is evidence that the current fixed fee schedule represents an inadequate tax structure, and that increased fee amounts are warranted. It is suggested that the commission consider the option of increasing all permit fees be equal to the liquid hauler annual permit of $120. The average fee for an annual permit in other states is seven to 10 times greater than the fee for a single trip permit.

ISSUES

- Does the commission wish to maintain oversize fees at present level and modify only the overweight schedule?

OPTION 2. Permit Fee Structural Modification.

Based on information provided by the state DOT, a fixed permit fee does not adequately compensate the state for damage inflicted on the roads by overweight vehicles. To address this, overweight permit fees should be structured to capture increased fees for increased weight and increased mileage.

A number of states impose a fixed permit fee plus an additional permit fee based on weight or distance traveled by an overweight commercial vehicle. The additional permit fee commonly takes the form of a fee imposed on overweight tonnage and miles traveled. State overweight fees imposed on each ton-mile range from a low of 0.9 cents per ton-mile in Illinois to 20 cents per ton-mile in Washington on weights in excess of 180,000 pounds.

The state DOT has suggested a fixed fee charge of $30.00 per trip and an additional ton-mile tax rate of five cents per ton-mile. The fee for a 200-mile trip at a weight of 150,000 pounds would be $30.00 + $318. A 200-mile trip at a weight of 120,000 pounds would be $30.00 + $168, and at a weight of 100,000 pounds would be $30.00 + $68.

ISSUES

- The commission would need to resolve issues regarding the treatment of liquid hauler and wrecker vehicles that make frequent or unforeseen overweight trips.

PROS

- The weight-distance tax is a benefits tax that assesses a user fee on the commercial vehicles that do the most harm to the highway infrastructure. It is, therefore, an appropriate tax to raise for additional road maintenance and construction revenue.

- All weight-distance tax revenues are currently deposited in the state road fund and increased revenues would automatically accrue to the state road fund.

- An estimated 80 percent of the weight-distance tax is exported to out-of-state users, because New Mexico is considered a "bridge" state, i.e. where most shipments neither originate nor terminate in the state, but where trucks merely cross through the state.

- Continued improvement in New Mexico's transportation system aids in economic development and competitive positioning. The trucks and trucking companies who pay the taxes and fees will benefit from that economic development.

CONS

- The weight-distance tax schedule has not been adjusted for over 20 years.

- An increase in weight-distance tax would increase the overall tax burden imposed on the trucking industry.

- Oversize and overweight fees are granted without regard to the amount a vehicle is overweight or oversize, which does not meet the adequacy standard.

- New Mexico is only one of four states imposing a weight-distance tax. Therefore, it is does not meet the "uniform" standard.

- Compliance problems have impaired the full implementation and collection of the weight-distance and trip tax.

VEHICLE REGISTRATION FEES

Vehicle registration fees are an area that may be appropriate for fee increases to help fund needed highway construction and maintenance. New Mexico vehicle registration fees average about $38.00 per vehicle per year and are generally low in comparison to other states. Registration fee levels were last adjusted in 1987.

OPTIONS

OPTION 1. Increase Vehicle Registration Fees.
Vehicle registration fees could be raised by any amount, with suggestions of 50 to 100 percent increases proposed. Each 10 percent increase in registration fees raises about $6.2 million on a full-year basis. Current passenger car fees range from $16.00 to $42.00, with an average of $38.00 per year. Each 10 percent increase in fees would cost vehicle owners from $1.60 to $4.20 per year.

ISSUES

- Will all of the increased revenue be distributed to the state road fund or shared with local governments?
- How will the increase be implemented in regard to two-year registrations?
- Should a similar increase be imposed on heavy trucks (over 26,000 pounds) by means of a weight-distance tax increase?

OPTION 2. Impose an Annual Value-Based Tax on Vehicles in Conjunction with Registration Fees.
Eleven western states impose some type of value-based annual tax on vehicles at rates ranging from 0.3 percent to 4.2 percent per year. A one percent tax would cost vehicles owners from $20.00 a year on a $2,000 vehicle to $300 a year on a $30,000 vehicle.

ISSUES

- What standard method of valuing vehicles should be chosen?
- Should some minimum amount be assessed against older vehicles?
- Will all of the increased revenue be directed to the state road fund or shared with local governments?

OPTION 3. Simplify the Distribution of Registration Fee Revenue to Local Governments.
The current distribution rules for vehicle registration fees and other miscellaneous fees collected by the Motor Vehicle Division appear to be needlessly complex. It would be much more efficient to simplify the current revenue distribution specifications, while holding harmless the current recipients. Although this proposal is attractive, no specific distribution simplification proposal has been put forward.

ISSUES
- Should earmarking of the local government revenue for particular uses be eliminated (i.e. distinctions between local government general fund and road funds)?

PROS
- A number of states impose some form of annual tax on the value of vehicles that is considerably higher than New Mexico's registration fees. Imposing such a value tax or imposing some increase in our registration fees would not put us at a disadvantage with surrounding states. In fact, it would align us more with rates in other states.

- Vehicle registration fees are a form of benefits tax — those who use the road system pay for the system.

- Vehicle registration fees generally are easy to administer and collect since vehicle owners must request a license plate and validation sticker that must be prominently displayed on the vehicle.

CONS
- Vehicle registration fees are an inelastic state revenue source, that is, revenue is dependent upon the number of vehicles, and the revenue tends to grow slower than the cost of providing services to the public.

- Vehicle registration fees may not accurately reflect the actual amount of use of the system by individuals.

- Some argue that drivers of passenger automobiles pay a disproportionately large share of highway costs when measured by their contribution to highway wear and tear. It is argued that heavy trucks generate a disproportionate share of highway maintenance costs.

- Truckers argue that all consumers benefit from the current system because higher taxes on the industry would be passed to consumers through higher prices on consumer goods.

- Vehicle registration fees probably exhibit the characteristics of a regressive tax.

LEASED VEHICLE GROSS RECEIPTS TAX SURCHARGE

In addition to imposition of the leased vehicle gross receipts tax, New Mexico also imposes a leased vehicle surcharge at a rate of $2.00 per day on short-term vehicle rentals. While many states or local governments have a similar tax, this is an area where the commission is considering tax relief.

OPTIONS

OPTION 1. Repeal the Leased Vehicle Surcharge.
This option proposes to repeal the leased vehicle surcharge on every vehicle rental.

OPTION 2. Exempt Certain Rentals from the Leased Vehicle Surcharge.
This proposal would exempt "replacement car rentals" from the leased vehicle surcharge. "Replacement car rentals" are those rentals that are paid for by an auto insurance company on behalf of the person renting the vehicle as a temporary replacement for a vehicle that is being repaired. Such rentals typically extend for periods of a week or more.

PROS

- Taxes imposed on rental vehicles — the gross receipts tax, leased vehicle gross receipts tax and leased vehicle surcharge — can total over 18 percent. This is a large burden, especially on those who must rent a vehicle for a long period.

- The leased vehicle surcharge was initially imposed as a way to export the tax burden to tourists and business travelers, who were assumed to be the predominate users of rental cars. In practice, it also applies in situations where a resident must rent a vehicle to replace a wrecked vehicle for a long period of time. It seems appropriate to exempt those replacement rentals from the surcharge.

- Industry representatives report that seven states currently exempt replacement car rentals from similar taxes or surcharges — Maryland, Oklahoma, Indiana, Louisiana, Rhode Island, Utah and Wisconsin.

CONS

- Most states impose a similar tax to help pay for state and local services.

- The tax is needed to support the highway infrastructure fund and the local governments road fund.