

Legislative Analysis



SALES TAX EXEMPTION: GASOLINE

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House Bill 4204 (Substitute H-3)

Sponsor: Rep. Robert Gosselin

Committee: Tax Policy

First Analysis (3-24-05)

BRIEF SUMMARY: The bill would exempt the amount of the sales price of gasoline exceeding \$1.99 per gallon (before the imposition of state taxes) from the sales tax. (As a practical matter, this would mean no state sales tax would be charged on a gallon of gasoline for the amount of the price exceeding \$2.30 at the pump.)

FISCAL IMPACT: For each one cent that the retail price of gasoline (the price at the pump) rises above \$2.30, sales tax revenue would decline by approximately \$2.95 million on an annual basis. If the retail price remained at \$2.35 for a period of one week, sales tax revenue would decline by nearly \$285,000. The most significant impact resulting from the reduction in sales tax revenue would fall on the School Aid Fund, which receives nearly 73 percent of sales tax revenue. In addition, constitutional revenue sharing, which receives 10 percent of all sales tax revenue, would also decline.

THE APPARENT PROBLEM:

Gas prices in Michigan are up, and are now at near-record levels. This week, the price for a gallon of regular gasoline is about \$2.136, compared to \$1.739 a year ago at this time. Moreover, gas prices have increased 38.5 cents since the start of the year, and are not expected to recede dramatically in the near future, particularly as the summer driving season starts and as refiners start producing cleaner summer blends.

The reasons for the sudden surge in gas prices are quite varied, though they are largely not something individual consumers or the state can control. A barrel of crude oil futures on the New York Mercantile Exchange closed on Monday at \$56.62, about 50 percent higher than a year ago, in part because of political unrest in the world's oil producing regions and increasing worldwide demand.

Higher gas prices ultimately affect drivers and businesses and can be a drag on consumer spending. As gas prices continue to increase, consumers have fewer dollars to spend on other items, such as groceries and utilities, and look to ways of cutting back on their gasoline consumption. Moreover, businesses are faced with increased costs, which can be substantial, because of higher motor fuel prices. Service stations, which rely on fuel sales, often see significant drops in sales of non-gasoline items such as beverages and food.

With people having little choice in the cost of gas, and with there being little the state can do in terms of affecting the base price of a gallon of gas, some people have suggested the

state influence gas prices through tax policy. The state imposes the six percent sales tax and, on top of that, an excise tax on the sales of gasoline in the state. Legislation has been introduced to exempt a portion of gasoline sales from the sales tax when prices increase above a certain level.

THE CONTENT OF THE BILL:

The bill would amend the General Sales Tax Act to exempt from taxation, the amount of the sales price of a gallon of gasoline that exceeds \$1.99 per gallon.

Currently, the federal government imposes an excise tax of 18.4 cents per gallon of gasoline, and the state imposes an excise tax of 19 cents per gallon. The sales tax is imposed on sales of gasoline, including the federal gas tax, but excluding the state gas tax. The "sales price" of \$1.99 per gallon referenced in the bill, then, would be the actual cost of a gallon and the federal gas tax. Added to that cost would be 11.94 cents in sales tax and the 19 cents for the state gas tax. The bill, then, would apply to gasoline with a retail selling price exceeding \$2.30 per gallon.

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ARGUMENTS:

For:

By exempting a portion of the cost of a gallon of gasoline, the bill provides Michigan taxpayers (individuals and businesses) with some much-needed tax (and price) relief as gas prices continue to increase. With the cost of a gallon of gasoline at the pump continuing to increase to near-record levels, Michigan drivers are facing greater financial strain as they must continue to pay utilities, the rent or mortgage, and other necessary household or business expenses. Moreover, taxpayers must pay the sales tax on top of the federal gas tax, which amounts to double taxation and further increases the price of gasoline in the state. (Some people question the practice of applying taxes on top of taxes.)

The cost of gasoline is felt not only at the service station, but in the price of goods and services throughout the economy. Limiting the sales tax is one way state government can help lessen the blow. With this proposal, the state will forego collecting a windfall from higher gasoline taxes.

Supporters say this bill benefits lower-income drivers since they often must drive older, less fuel efficient vehicles.

Against:

The bill provides individual taxpayers with very little tax relief while depriving schools and local governments of revenue. When a gallon of gas retails for \$2.30, that price includes the federal gas tax (\$0.19), the state gas tax (\$0.184), the sales tax (\$0.119), and the actual cost (\$1.81). If the retail cost of a gallon were to increase to \$3.00, that price

would include about 15.9 cents in sales tax, and the actual cost would be about \$2.47. Under the provisions of the bill, the taxpayer would save four cents on that gallon of gasoline. A taxpayer who drives 15,000 miles in a year in a vehicle that averages 20 miles per gallon purchases 750 gallons. Even if gas prices were \$3 per gallon for an entire year, total taxpayer savings would only be about \$30 for the year. At \$2.50 per gallon retail, the sales tax would be about 13 cents, resulting in a per gallon savings of about one penny. At 750 gallons a year, the total savings would be \$7.50.

The bill, at present, makes no distinction between the various grades of fuel sold and phases in the tax relief, starting with arguably wealthier individuals who purchase premium gasoline. Premium grade gasoline could easily exceed \$2.30 per gallon in the immediate future, if it isn't already at that price now. That may not, however, necessarily be the case for the lowest grade of fuel, which is likely the gasoline of choice for people on low or fixed incomes. The bill, then, seems to provide tax relief to individuals who are likely to purchase higher priced gasoline regardless of its costs. If the intent is to provide tax relief to individuals in need, a means tested income tax credit based on gasoline purchases could be established instead.

Against:

Representatives of schools and local governments testified the bill goes against the tenets of Proposal A and the shift in school funding from local property taxes to the state sales tax. It was pointed out that reductions in state revenue collected through the imposition of the sales tax often necessitate higher local property taxes. However, voters in 1994 clearly expressed their desire to fund schools through the sales tax, not the property tax. Moreover, it is a bad precedent to apply the sale tax unevenly in this way: a variable amount based on the price of goods. The "slippery slope" question is, why not apply the policy to other goods as well?

Response:

On the other hand, it could be argued that the revenue schools and local governments would be foregoing are not revenues they are receiving now; they are "windfall" revenues derived from extraordinarily high gas prices. Few other goods are so central to people's lives.

Against:

The bill reportedly creates administrative problems for the Department of Treasury. Purchasers of gasoline from a refiner or pipeline terminal operator must prepay the sales tax equal to six percent of the statewide average retail price of a gallon of self-service unleaded regular gasoline, as determined by the department. (Pursuant to Revenue Administrative Bulletin 2005-1, that rate is 9.9 cents per gallon, beginning April 1, 2005.) Subsequent purchasers pass that prepayment along until reaching the retailer, who must reconcile any differences in prepaid sales tax and actual sales tax liability on the retailer's sales tax return. The bill, then, seems to require the department to rebate retailers for the exempted portion of gasoline sales. Also, the Department of Treasury testified that the bill could put the state out of compliance with the Streamlined Sales Tax Project, into which the state only recently entered. The project is intended to ease sales and use tax

collection by businesses partly by creating uniformity among the states in terms of what is taxable and how the tax is administered.

POSITIONS:

Taxpayers United testified in support of the bill. (3-23-05)

The Department of Treasury opposes the bill. (3-23-05)

The Michigan Townships Association opposes the bill. (3-23-05)

The Michigan Small and Rural Schools Association opposes the bill. (3-23-05)

The Michigan Education Association opposes the bill. (3-23-05)

The Middle Cities Education Association opposes the bill. (3-23-05)

The Michigan Federation of Teachers opposes the bill. (3-23-05)

The Michigan Environmental Council opposes the bill. (3-23-05)

The Michigan Association of School Administrators opposes the bill. (3-23-05)

Oakland Schools opposes the bill. (3-23-05)

The Allegan County ISD opposes the bill. (3-23-05)

The Ottawa Area ISD opposes the bill. (3-23-05)

The Wayne RESA opposes the bill. (3-23-05)

The Tri-County Alliance opposes the bill. (3-23-05)

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■ 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.