

# OFF-ROAD FUEL USE EXCISE TAX EXEMPTIONS EVALUATION SUMMARY



THIS EVALUATION WILL BE INCLUDED IN COMPILATION REPORT SEPTEMBER 2019

YEAR ENACTED	1931
REPEAL/EXPIRATION DATE	None
REVENUE IMPACT	\$7.3 million CALENDAR YEAR 2017
NUMBER OF TAXPAYERS	Could not determine
AVERAGE TAXPAYER BENEFIT	Could not determine
IS IT MEETING ITS PURPOSE?	Yes

## WHAT DO THESE TAX EXPENDITURES DO?

The Off-Road Fuel Use Excise Tax Exemptions include seven different tax expenditures that exempt gasoline and special fuels used for off-road purposes from the state fuel excise tax.

## WHAT IS THE PURPOSE OF THESE TAX EXPENDITURES?

Statute does not explicitly state a purpose for the exemptions. Based on our review of statute, we inferred that the purpose is to prevent individuals and businesses from having to pay taxes on fuel that is not used to operate vehicles on state highways.

## WHAT DID THE EVALUATION FIND?

We found that the exemptions are meeting their purpose because they prevent individuals and businesses from paying the excise tax on fuel that is purchased, but not used on state highways, although it appears that some eligible taxpayers are not claiming it.

## WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations related to the exemptions.

# OFF-ROAD FUEL USE EXCISE TAX EXEMPTIONS

## EVALUATION RESULTS

### WHAT ARE THESE TAX EXPENDITURES?

This evaluation covers seven fuel excise tax exemptions for fuel used for off-road purposes. All of these expenditures were established in 1931, and there have been no significant changes made to statute [Section 39-27-103(3)(a)(I), C.R.S.] since their enactment. EXHIBIT 1.1 provides information about each of these expenditures, which we refer to collectively as the Off-Road Fuel Use Excise Tax Exemptions (Off-Road Fuel Use Exemptions).

EXHIBIT 1.1. OFF-ROAD FUEL USE EXEMPTIONS		
DESCRIPTION OF USE QUALIFYING FOR EXEMPTION	STATUTE	YEAR ENACTED
Operating a stationary gas engine	39-27-103(3)(a)(I)(A)	1931
Operating a motor vehicle on or over fixed rails	39-27-103(3)(a)(I)(B)	1931
Operating a tractor, truck, or other farm implement or machine for agricultural purposes on a farm or ranch	39-27-103(3)(a)(I)(C)	1931
Operating a motor boat	39-27-103(3)(a)(I)(E)	1931
Cleaning or dyeing fuel	39-27-103(3)(a)(I)(G)	1931
Any commercial use other than the operation of a motor vehicle upon state highways	39-27-103(3)(I)(H)	1931
Any other use that entitles a person to a refund under the provisions of this part 1 or federal law	39-27-103(3)(a)(I)(I)	1931

SOURCE: Office of the State Auditor review of Colorado Revised Statutes.

Colorado first imposed an excise tax on motor fuel in 1919. In 1935, Article X, Section 18 of the Colorado Constitution was enacted, which requires that all excise taxes collected on motor fuel be used for the construction and maintenance of Colorado's highways. The fuel excise tax is assessed on the number of gallons of gasoline or special fuel acquired, sold, or offered for sale in Colorado for any purpose. Special fuel includes diesel engine fuel, kerosene, compressed natural gas, and

liquefied natural gas [Section 39-27-101(29), C.R.S.]; statute specifically excludes liquefied petroleum gas as a special fuel for this purpose [Section 39-27-102(1)(a)(I)(A), C.R.S.].

EXHIBIT 1.2 shows the fuel excise tax rates for Calendar Year 2019. Overall, Colorado collected \$630 million in fuel excise taxes in Fiscal Year 2017.

EXHIBIT 1.2. EXCISE TAX RATES BY FUEL TYPE CALENDAR YEAR 2019	
FUEL TYPE	RATE PER GALLON
Gasoline	\$0.22
Diesel	\$0.205
Compressed Natural Gas	\$0.183
Liquefied Natural Gas	\$0.12
SOURCE: Office of the State Auditor analysis of Department of Revenue's data on excise tax rates.	

The Off-Road Fuel Use Exemptions are limited to fuel purchases of 20 gallons or more and by industry-specific fuel use percentages, as determined by the Department of Revenue and established in rule [Section 39-27-103(3)(a)(II) and (III), C.R.S.]. The percentages are based on the amount of fuel typically used in a particular industry for off-road purposes. According to information provided by the Department of Revenue, industry-specific refund percentages ranged from 0 to 100 percent, as shown in EXHIBIT 1.3.

EXHIBIT 1.3. INDUSTRY SPECIFIC OFF-ROAD FUEL USE REFUND PERCENTAGES ESTABLISHED BY DEPARTMENT OF REVENUE CALENDAR YEAR 2019		
INDUSTRY	AVERAGE REFUND PERCENTAGE GASOLINE	AVERAGE REFUND PERCENTAGE SPECIAL FUEL
Agriculture/Forestry/Fishing	71.18%	71.05%
Transportation–Commercial	45.88%	29.89%
Public Administration (Government)	100%	100%
Services–Commercial	57.86%	48.23%
Construction	32.5%	62.94%
Other	28.57%	14.29%
Mining/Oil & Gas Products	31.54%	40.68%
Manufacturing	41.71%	38.74%
Tribal Use	0%	0%
SOURCE: Department of Revenue's GenTax data on the default industry percentages available to be refunded for excise taxes paid.		

To claim the refund, taxpayers must apply to the Department of Revenue for a refund for the excise tax paid using the Fuel Tax Refund Claim Form (Form DR 7118). According to Department of Revenue rules [1 CCR 201-16], the Department of Revenue will process the claim and apply the default industry percentage, which can be adjusted based on additional information provided by the taxpayer to justify a different percentage for the specific claim.

#### WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURES?

Statute does not specifically identify the intended beneficiaries of the Off-Road Fuel Use Exemptions. We inferred, based on the statutory language, that the intended beneficiaries are individuals or businesses that use gasoline or special fuel for off-highway purposes, including farmers and ranchers, construction companies for equipment used to repair roads, motor boat users, and any others needing fuel for off-highway purposes. We also inferred that consumers may indirectly benefit from these refunds since the businesses receiving the refund may pass the savings on to consumers through lower prices on goods and services.

#### WHAT ARE THE PURPOSES OF THE TAX EXPENDITURES?

Statute does not explicitly state a purpose for the Off-Road Fuel Use Exemptions. Based on our review of statute, we inferred that the purpose of the expenditures is to prevent individuals and businesses that purchase fuel for off-road use from having to pay the excise tax when the fuel is not used to propel vehicles on state highways. The State's fuel excise tax is intended to place part of the cost of building and maintaining state highways onto highway users when they purchase fuel. Since the fuel purchased for off-road purposes is not used to operate vehicles on the State's highways, it is not contributing to their deterioration.

#### ARE THE TAX EXPENDITURES MEETING THEIR PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We found that the Off-Road Fuel Use Exemptions are meeting their

purpose because they prevent individuals and businesses from paying the fuel excise tax on fuel that is purchased, but not used on state highways, although it appears that some eligible taxpayers are not claiming it.

Statute does not provide quantifiable performance measures for the tax expenditures. Therefore, we created and applied the following performance measure to determine whether the Off-Road Fuel Use Exemptions are meeting their inferred purpose:

**PERFORMANCE MEASURE:** *To what extent are individuals and businesses claiming the Off-Road Fuel Use Exemptions for fuel purchases for eligible off-road uses?*

**RESULT:** We determined that some taxpayers who purchase fuel for off-road purposes claim the refund, but there is likely a large percentage who do not, especially in certain industries. Specifically, in Calendar Year 2017, there were 5,275 refund claims for a total of \$7.3 million. Of these, 57 percent were from the agricultural industry, followed by commercial transportation and government, as shown in EXHIBIT 1.4. According to the Colorado Livestock Association and the Colorado Wyoming Petroleum Marketers Association, the agricultural industry is generally aware of the refunds and as an industry, they advocate for retaining them. Representatives from other industries that we spoke with, including construction and railway operations, did not appear to have the same awareness of the refunds.

**EXHIBIT 1.4.**  
**INDUSTRIES CLAIMING OFF-ROAD FUEL USE REFUNDS**  
**CALENDAR YEAR 2017**

ITEM	TOTAL FILINGS	PERCENTAGE
Agriculture/Forestry/Fishing	3,022	57%
Transportation–Commercial	724	14%
Public Administration (Government)	678	13%
Services–Commercial	304	6%
Construction	264	5%
Other	155	3%
Mining/Oil & Gas Products	63	1%
Manufacturing	61	1%
Tribal Use	4	<1%
<b>TOTAL</b>	<b>5,275</b>	<b>100%</b>

SOURCE: Office of the State Auditor analysis of data from the Department of Revenue.

Although the agricultural industry accounted for the majority of refund claims, it appears that only a small percentage of taxpayers in the agricultural industry submitted a claim. According to the U.S. Department of Agriculture, there are 33,800 taxpayers in the agricultural industry in Colorado that are potentially eligible for one of the Off-Road Fuel Use Exemptions. Furthermore, since taxpayers can file quarterly for a refund, there may have been fewer than 3,022 distinct taxpayers claiming the exemption, although we were unable to confirm the exact number. This means that only up to 9 percent of potentially eligible taxpayers submitted a claim if each taxpayer only made a single claim during the year. If all of these taxpayers submitted claims each quarter, the percentage of agricultural taxpayers would be about 2 percent. Although we do not have comparable data for other industries, we would expect similar results based on our discussions with stakeholders.

#### WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURES?

We estimate that the Off-Road Fuel Use Exemptions had a total state revenue impact of about \$7.3 million in Calendar Year 2017, with an equal amount saved by eligible Colorado taxpayers. We estimated this revenue impact based on data provided by the Department of Revenue. EXHIBIT 1.5 shows the total revenue impact by industry and the average refund per taxpayer in each industry.

EXHIBIT 1.5. ESTIMATE OF THE STATE REVENUE IMPACT FROM ITEMS INCLUDED IN THE OFF-ROAD FUEL USE CREDITS CALENDAR YEAR 2017			
INDUSTRY	STATE REVENUE IMPACT (ESTIMATED)	TOTAL FILINGS	AVERAGE REFUND/FILING
Agriculture/Forestry/Fishing	\$ 690,100	3022	\$ 228
Transportation–Commercial	1,158,300	724	1,600
Public Administration	3,318,700	678	4,895
Services–Commercial	333,500	304	1,097
Construction	817,200	264	3,096
Other	110,300	155	712
Mining/Oil & Gas Products	723,600	63	11,486
Manufacturing	61,700	61	1,011
Tribal Use	70,500	4	17,627
<b>TOTAL</b>	<b>\$ 7,283,800</b>	<b>5,275</b>	<b>\$ 1,381</b>

SOURCE: Office of the State Auditor analysis of data from the Department of Revenue.

If a larger percentage of eligible taxpayers claimed the refunds, the revenue impact to the State would increase. For example, we calculated the potential state revenue impact if all taxpayers in the agricultural industry claimed the refunds. For our calculations, we used data from the U.S. Department of Agriculture's 2018 *Farm Production Expenditures Summary* report and their 2018 *Agricultural Statistics* reports on the total number of farms and ranches in Colorado and the amount of gasoline and diesel fuel used by the agricultural industry that could be eligible for the Off-Road Fuel Use Refunds. According to industry representatives, only about 20 percent of the diesel fuel purchased by the agricultural industry is eligible for the Off-Road Fuel Use Refunds; most of the diesel fuel purchased for agricultural purposes is dyed diesel, which is exempt from the fuel excise tax under another tax expenditure. Therefore, we based our estimate on 20 percent of the total agricultural diesel fuel purchases being eligible.

As shown in EXHIBIT 1.6, we estimate that the state revenue impact due to the Off-Road Fuel Use Refunds could increase by about \$3.6 million if all of the agricultural industry claimed the refunds.

EXHIBIT 1.6. ESTIMATE OF THE STATE REVENUE IMPACT IN THE OFF-ROAD FUEL USE CREDITS BASED ON USE BY THE AGRICULTURAL INDUSTRY CALENDAR YEAR 2017		
CREDIT ITEM	TAXPAYERS	ESTIMATED STATE REVENUE IMPACT
Agriculture (less estimated 80 percent dyed diesel purchased) <sup>1</sup>	33,800	\$4,316,000
Agriculture (actual number filed based on Department of Revenue data)	3,022 <sup>2</sup>	- \$690,100 <sup>3</sup>
Potential Additional Revenue Impact		\$3,625,900

SOURCE: Office of the State Auditor analysis of data from the U.S. Department of Agriculture, Colorado Department of Agriculture, and Department of Revenue. Estimated total taxpayers is equivalent to the number of farms and ranches in Colorado.

<sup>1</sup> Estimate based on gasoline and diesel fuel only and accounts for the default agriculture industry percentage, where 71 percent of excise tax on diesel and gasoline can be refunded.

<sup>2</sup> This total assumes that the number of actual filings for Calendar Year 2017 equals the number of taxpayers. However, we do not have data to confirm this.

<sup>3</sup> The Department of Revenue reports industry revenue impacts in aggregate, so the revenue impact for agriculture reported by the Department also includes excise tax refunds for fuel used for forestry and fishing industries.

## WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURES HAVE ON BENEFICIARIES?

Eliminating the Off-Road Fuel Use Exemptions would increase taxes for individuals and businesses that purchase gasoline and special fuels for off-road use. Without these exemptions, eligible taxpayers would have been subject to over \$7 million in additional taxes in Calendar Year 2017. According to stakeholders in the agricultural and construction industries, these increased costs would likely be passed on to consumers to the extent the current beneficiaries are able to do so. However, many agricultural producers may not be able to pass the costs on to consumers because they must often sell at established market prices for agricultural commodities. Thus, agricultural producers would likely have to absorb the additional cost, which could have a significant impact since the agricultural industry already tends to operate on small profit margins.

## ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We identified similar tax expenditures in the seven states surrounding Colorado, including Arizona, Kansas, Oklahoma, Nebraska, New Mexico, Utah, and Wyoming. Unlike Colorado, all of these other states refund 100 percent of the amount of fuel taxes paid for eligible fuel types. See EXHIBIT 1.7 for comparison:



EXHIBIT 1.7. OTHER STATES WITH SIMILAR OFF-ROAD FUEL USE TAX EXPENDITURES				
STATE	ORGANIZATION TYPES	FUEL TYPE(S)	TYPE OF EXPENDITURE	AMOUNT OF SAVINGS
Colorado	Motorized vehicles operating off Colorado roads	Motor and special fuel	Refund	Up to 100% of excise tax depending on industry type
Arizona	Off-highway use	Motor fuel	Refund	100% of excise tax
Kansas	Any off-highway or use in school buses	Motor and special fuel	Refund	100% of excise tax
Nebraska	Agricultural, quarrying, industrial, or any other usage in unlicensed vehicles or equipment	Motor fuel	Refund	100% of excise tax
New Mexico	Off-highway use	Motor and special fuel	Refund	100% of excise tax
Oklahoma	Agricultural use and off-highway use	-Diesel for non-highway use -Motor fuel for agricultural use	Refund	100% of excise tax on diesel for all except (\$0.0208) per gallon of gasoline used for agricultural purposes must be paid
Utah	Agricultural and off-highway uses	-Special fuel used for any purpose other than to operate a motor vehicle on public highways -Motor fuel used for agricultural purposes	Refund	100% of excise tax
Wyoming	Off-highway use	Motor fuel	Exemption	100% of excise tax

SOURCE: Office of the State Auditor analysis of similar tax expenditures in other states.

### ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

The Dyed Diesel Fuel Excise Tax Exemption [Section 39-27-102.5, C.R.S.] is similar to the Off-Road Fuel Use Exemptions. Dyed diesel is tax exempt when purchased (as opposed to the Off-Road Fuel Use Exemptions, which allow taxpayers to claim a refund for taxes already paid on the fuel) and is used primarily for off-highway equipment, government transportation vehicles, transit buses, and highway construction. We discuss the Dyed Diesel Fuel Tax Exemption in its own report.

### WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURES?

The Department of Revenue was not able to provide information on the total number of taxpayers claiming the Off-Road Fuel Use Exemptions.

The only information that could be extracted from GenTax, the Department of Revenue's tax processing and information system, was the number of exemption filings and the total amount claimed for the exemptions. To have data on the number of taxpayers claiming the exemptions, the Department of Revenue would have to make programming changes in GenTax to collect this information, which would require additional resources (see the Tax Expenditures Overview Section of the Office of the State Auditor's *September 2018 Tax Expenditures Compilation Report* for additional details on the limitations of Department of Revenue data and the potential costs of addressing the limitations).

#### WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations related to the Off-Road Fuel Use Exemptions.