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HOUSE COMMITTEES ON ENERGY & ENVIRONMENTAL PROTECTION AND AGRICULTURE

TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING HB 470 RELATING TO TAXATION

WRITTEN TESTIMONY ONLY

TESTIFIER: FREDERICK D. PABLO, INTERIM DIRECTOR OF
TAXATION (OR DESIGNEE)
COMMITTEE: EEP-AGR
DATE: FEBRUARY 9, 2011
TIME: 8:30AM
POSITION: NO POSITION

This measure amends the incidence of the Environmental Response, Energy, and Food Security Tax, from the distributor of petroleum products to the point of origin in Hawaii, that being a marine terminal operator.

The Department of Taxation (Department) takes **no position** on this legislation; however is not opposed to imposing the Environmental Response Tax at the earliest point that the petroleum product becomes subject to Hawaii's taxing authority.

The Department supports efforts where third-parties collect and pay the taxes of another, similar to a sales tax or withheld income tax. Because the terminal operator "collects" and pays the tax, the Committee may want to consider adding a provision similar to HRS § 235-64, which holds the collected amounts in trust for the State.

Assuming this measure does not result in revenue loss by shifting the point of taxation, the Department is not opposed to this measure.

TAXBILLSERVICE

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SUBJECT: FUEL, Collection of environmental response tax

BILL NUMBER: HB 470

INTRODUCED BY: Wooley, Awana, Choy, Keith-Agaran, C. Lee, Nakashima and 2 Democrats

BRIEF SUMMARY: Amends HRS section 243-3.5 to provide that the marine terminal operator located within or outside the state, instead of the distributor, shall collect the environmental response tax from the owner of petroleum products at the time the products are received at the terminal.

Defines "marine terminal" as any facility used for transferring oil or petroleum products to or from a tank ship or tank barge. Defines "operator" as any person who owns, has an ownership interest in, or operates a marine terminal. That does not include the owner of land underlying a marine terminal or the owner of the marine terminal itself if that person is not involved in the operation of the marine terminal.

Repeals the sunset date of Act 73, SLH 2010.

EFFECTIVE DATE: Upon approval

STAFF COMMENTS: Currently, the state environmental response tax per barrel of petroleum product is paid by the distributor of the petroleum product. The proposed measure would require the marine terminal operator, rather than the distributor, to collect the environmental response tax from the owner at the time the product is received at the terminal.

It appears that this measure is proposed to ensure the payment of the environmental response tax on each barrel of petroleum product at the time the products are received at the terminal. It should be remembered that there are situations where the product may be delivered through a marine terminal located physically within the boundaries of the state, but the product itself may technically never enter the United States or for that matter the state of Hawaii. Such is the case of product that is delivered from a foreign country into a Foreign Trade Zone (FTZ) to be processed or refined and then shipped to a foreign destination. Technically that product has never entered the jurisdiction of the state and is not subject to federal, state, or local taxes or regulations. Thus, while the marine terminal operator may know of petroleum products, or the quantity thereof, off loaded from a tanker or barge through a marine terminal; until the product enters the United States, and more specifically the state of Hawaii, the marine terminal operator may be reporting quantities that technically are not subject to the environmental response tax.

It is the distributor who tracks how much petroleum product actually enters the state and, therefore, how many barrels for which the tax is due and payable. For example, a refiner may have raw petroleum product shipped into the FTZ for refining purposes, some of which is refined into gasoline for automobiles, some of the raw product is further refined for jet fuel and rest is a lower quality "bunker" fuel used to power surface vessels. Until any of the product that has been refined leaves the FTZ, it has

technically not entered the country or the state. The jet fuel can be transported from the FTZ to Honolulu International Airport through bonded lines for delivery to and to be used by, say, Japan Airlines. Since Japan Airlines flies internationally, that fuel would never be subject to federal or state taxes. The use of that fuel will only be known by the distributor as it is the distributor who knows when the product will enter the taxing jurisdiction of the United State and Hawaii and not the marine terminal operator.

This measure also repeals the sunset date of Act 73, SLH 2010. Act 73, SLH 2010, renamed the environmental response tax the environmental response, energy and food security tax. It also increased the rate of tax from 5 cents per barrel to \$1.05 on each barrel with 5 cents of the tax deposited into the environmental response revolving fund, 15 cents deposited into the energy security special fund, 10 cents deposited into the energy systems development special fund; and 15 cents deposited into the agricultural development and food security special fund with the residual of 60 cents deposited into the general fund between 7/1/10 and 6/30/15. While this act is scheduled to sunset on 6/30/15, the proposed measure would make it permanent.

It should be remembered that the environmental response tax was initially adopted for the purpose of setting up a reserve should an oil spill occur on the ocean waters that would affect Hawaii's shoreline. The nexus was between the oil importers and the possibility that a spill might occur as the oil product was being imported into the state. Now that the fund has become a cash cow, lawmakers have placed other responsibilities on the fund, including environmental protection and natural resource protection programs, such as energy conservation and alternative energy development, to address concerns related to air quality, global warming, clean water, polluted runoff, solid and hazardous waste, drinking water, and underground storage tanks, including support for the underground storage tank program of the department of health.

It should be noted that the enactment of the barrel tax for the environmental response revolving fund is the classic effort of getting one's foot in the door as it was initially enacted with a palatable and acceptable tax rate of 5 cents and subsequently increasing the tax rate once it was enacted which is what it has morphed into as evidenced by the \$1.05 tax rate. Because the tax is imposed at the front end of the product chain, the final consumer does not know that the higher cost of the product is due to the tax. Thus, there is little, if any, accountability between the lawmakers who enacted the tax and the vast majority of the public that ends up paying the tax albeit indirectly. Proponents ought to be ashamed that they are promoting a less than transparent tax increase in the burden on families all in the name of environmental protection and food security. Much as lawmakers last year said this tax increase was a commitment to energy independence and food security, by the time the lights were turned out on the 2010 legislative session 60 cents of the new dollar per barrel tax went into the general fund to fund such things as education and social services. So much for commitment, the measure was nothing more than smoke and mirrors to shore up the state general fund because lawmakers could not cut enough spending to balance the general fund budget.

It should be remembered that the State Auditor has singled out the environmental response revolving fund as not meeting the criteria established and recommended that it be repealed. The Auditor criticized the use of such funds as they hide various sums of money from policymakers as they are not available for any other use and tend to be tacitly acknowledged in the budget process. More importantly, it should be recognized that it is not only the users of petroleum products who benefit from a cleaner environment, but it is the public who benefits. If this point can be accepted, then the public, as a whole,

should be asked to pay for the clean up and preservation of the environment.

Funds deposited into a revolving fund are not subject to close scrutiny as an assumption is made that such funds are self-sustaining. It should be remembered that earmarking of funds for a specific program represents poor public finance policy as it is difficult to determine the adequacy of the revenue source for the purposes of the program. To the extent that earmarking carves out revenues before policymakers can evaluate the appropriateness of the amount earmarked and spent, it removes the accountability for those funds. There is no reason why such programs should not compete for general funds like all other programs that benefit the community as a whole.

It should be noted that the measure to increase the environmental response, energy, and food security tax was vetoed by the governor and subsequently overridden by the legislature. The governor's message stated that the measure was vetoed "because it raises taxes on Hawaii residents and businesses by an estimated \$22 million per year at a time when the community cannot afford these taxes, and deceptively implies these funds will be used to address the state's dependence on imported fuel and food. This tax will impact virtually everything we do or use in Hawaii including electricity, gasoline, trucking, shipping, retail goods, food, and even the propane for our backyard barbeques. The impacts will ripple through our entire economic system. I am particularly concerned that the tax increase occurs at a precarious moment when the State economy is beginning to stabilize and progress out of the slump created by the global recession."

Rather than perpetuating the problems of the barrel tax, it should be repealed and all programs that are funded out of the environmental response fund should be funded through the general fund. At least program managers would then have to justify their need for these funds. By continuing to special fund these programs, it makes a statement that such programs are not a high priority for state government. This sort of proliferation of public programs needs to be checked as it appears to be growing out of hand and at the expense of the taxpayer. Supporters of the barrel tax have little regard for the poor who will end up bearing most of the burden as most of a low-income family's paycheck will be spent on goods and services that are affected by the barrel tax.

Digested 2/8/11



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HOUSE COMMITTEE ON ENERGY & ENVIRONMENTAL PROTECTION HOUSE COMMITTEE ON AGRICULTURE

February 9, 2011, 8:00 A.M.
(*Testimony is 1 page long*)

TESTIMONY IN SUPPORT OF HB 470

Aloha Chair Morita, Chair Tsuji, and Committee Members -

The Sierra Club, Hawai'i Chapter, *supports* HB 470, which changes who will collect the Environmental Response, Energy, and Food Security Tax.

This change appears to be attempting to close a loophole that may allow some petroleum products to potentially enter the state without paying the Environmental Response, Energy, and Food Security Tax. It furthers this Legislature's smart tax-shifting policy designed to foster greater food and energy independence by tapping into the source of our problem (over reliance on dirty, imported oil). In order to ensure the State receives the full benefit of the historic fee passed last year, this measure should be approved by the Committees.

Thank you for the opportunity to testify.



Western States Petroleum Association

House Committee on Energy & Environmental Protection
and
House Committee on Agriculture

DATE: Wednesday, February 9, 2011
TIME: 8:30 a.m.
PLACE: Conference Room 312
RE: HB470: Relating to Taxation

I am testifying on behalf of the Western States Petroleum Association (known as WSPA) in opposition to HB 470. WSPA is a non-profit trade association representing a broad spectrum of petroleum industry companies in Hawaii and five other western states.

HB 470 requires a marine terminal operator, rather than a distributor, to collect the Environmental Response, Energy, and Food Security Tax from the owner of petroleum products at the time those products are received at the terminal and repeals the sunset date of Act 73, SLH 2010.

The Import-Export Clause of the U.S. Constitution prohibits a state from imposing taxes or duties on imports: No State shall, without the Consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws. In addition, the Commerce Clause of the U.S. Constitution directly limits the power of the states to discriminate against interstate commerce. The U.S. Supreme Court has previously struck down discriminatory tax laws enacted by Hawaii.

Thank you for giving WSPA the opportunity to testify today.

