The International Fuel Tax Agreement:
What It Is and How It Works

The International Fuel Tax Agreement (IFTA) is an organization of states and the Canadian provinces under which the fuel use tax obligations of interstate and international motor carriers are administered. IFTA first went into effect in a few jurisdictions more than 20 years ago, and has since been implemented in 48 states and all ten provinces of Canada.

IFTA ensures that state and provincial fuel tax requirements on the trucking industry are administered in both nations with a high degree of uniformity. It has been estimated that this saves administrative costs to business of hundreds of millions of dollars annually. With its sister organization, the International Registration Plan, a similar organization for the administration of U.S. and Canadian vehicle registration programs for motor carriers, IFTA represents a unique development in our federal system, one that may find imitators in other fields of government regulation. Despite its importance for motor carriers and state and provincial tax administration, however, IFTA is relatively little known and understood outside these immediate areas.

<u>Fuel Purchase Taxes and</u>
<u>Fuel Use Taxes</u>

Every state imposes a tax on the sale of highway fuels such as gasoline and diesel fuel. This is the tax with which car drivers are familiar, and which they pay at the pump when they purchase fuel at a service station. Operators of heavy trucks also pay the fuel purchase tax where they buy fuel, either at retail from a service station or truck stop or on wholesale purchases of highway fuel in bulk. However, whereas the driver of a passenger car may fuel up in one state, pay that state's tax, and then drive the car across the state line without further tax obligation, this is not true of an operator of a heavy truck. An interstate motor carrier is also subject to what is called a fuel use tax.

A heavier commercial vehicle uses more fuel in its operations than a passenger car, and pays a correspondingly larger amount of fuel tax. States and provinces long ago recognized that under a simple fuel purchase tax regime, some states would get less tax from heavy trucks and buses, proportionate to the operations of those vehicles, than would other states. This would be due in part to differential tax rates, and the effect this has on fueling patterns, but in part also to fueling patterns that have more to do with simple geography. Some states are more apt to be the destination of freight shipments, while others are what are often called pass-through states. Truck and bus operators are likelier to fill their tanks – and to pay fuel purchase tax – in destination states.

States began in the 1940s to enact a remedy for what they perceived as a misallocation of fuel taxes paid by truck and bus operators. This has come to be known as the fuel use tax, and is now imposed by practically all states. The fuel use tax may be considered a supplement – imposed on heavy commercial vehicles only - to the fuel purchase tax. It aims at the reallocation of fuel taxes based not on where truck and bus operators buy fuel (and pay fuel purchase tax) but on where they consume fuel in their operations.

A fuel use tax requires a trucking company or a bus line to report to the state, generally on a quarterly basis, how much fuel it consumed in the state (calculated by the use of a miles-per-gallon factor), and how much fuel purchase tax it paid on its purchases of fuel in the state. The tax on the fuel consumed in the state is then compared to the tax on the fuel actually purchased in the state, and the carrier pays any tax due on underpurchases or the state pays the carrier any tax it paid on overpurchases, as the case may be.

IFTA's Origins

By the early 1980s, most of the states had enacted fuel use taxes on motor carriers. However, since each state had imposed the tax under slightly different requirements, the area had become a serious and very expensive compliance burden for interstate operators. IFTA was designed as a way of allowing states to continue to collect fuel taxes in proportion to the use of their roads by heavier commercial vehicles while at the same time introducing a level of uniformity in fuel use tax requirements to reduce industry's costs.

IFTA first went into effect in three states in 1983. Thereafter, its membership grew steadily, until in 1991 the U.S. Congress passed a law that effectively required a state to join IFTA by 1996 if it wished to continue to collect a fuel use tax on interstate carriers. Since 1997, therefore, all the 48 contiguous states have belonged to IFTA, and the Canadian provinces have joined as well.

How IFTA Works

Under IFTA, the basic form and function of a fuel use tax is retained, but instead of a motor carrier being obligated to make reports to each state in which its vehicles travel, it reports on all of its operations to its base state alone. The base state, in its turn, (1) processes the carrier's return, (2) collects from or refunds to the carrier a net fuel use tax representing the taxes owed to or from *all* the states in which the carrier operates, (3) distributes to the other states (or receives from them, as the case may be) the amount of fuel use tax the carrier owes each one, and (4) when it comes time to audit the carrier's compliance with fuel use tax requirements, the base audits the carrier on behalf of all the IFTA member jurisdictions. This is all done under rules that ensure that each member of IFTA administers its fuel use tax with a high degree of uniformity. Neither IFTA nor the federal law, however, puts any limit on the rate of fuel use tax a state may impose.

For a state, the key to IFTA's success is that since IFTA preserves the basic form and function of a fuel use tax, each state is kept whole – it continues to receive fuel taxes in the proportion that heavier commercial vehicles consume fuel on its highways.

An Example

An example may be in order here. Suppose that J.R. Todd Trucking, a company based in South Carolina, operates trucks only in North and South Carolina, and accrues 90,000 miles during a calendar quarter in each state. Suppose that the tax rate for diesel fuel in North Carolina is 30 cents a gallon, and that South Carolina's tax rate is 20 cents a gallon. Suppose that Todd Trucking uses 30,000 gallons of fuel in its highway operations in a quarter. And suppose that the company's vehicles fuel up 90 percent of the time in South Carolina. At the end of the first quarter of the year, South Carolina will have collected its *fuel purchase tax* on 27,000 gallons of fuel bought by Todd Trucking, or, at 20 cents a gallon, $5,400. North Carolina, on the other hand, has collected $900 in fuel purchase tax (3,000 gallons @ 30 cents/gal.). Both the states have deposited their collections in the bank, where they earn interest.

On its IFTA report – filed with South Carolina alone – Todd Trucking duly reports the following:

Miles traveled everywhere:	180,000	
Fuel purchased everywhere:	30,000 gallons	
Fleet miles per gallon factor:	6.0 mpg	
Miles traveled in SC:	90,000	
Gallons consumed in SC:	15,000 gallons	(90,000 mis. / 6 mpg)
Gallons purchased tax-paid in SC:	27,000 "	
Gallons overpurchased:	12,000 "	
Tax due from SC:	$2,400	(12,000 gals. x 20 cents/gal.)
Miles traveled in NC:	90,000	
Gallons consumed in NC:	15,000 gallons	(90,000 mis. / 6 mpg)
Gallons purchased tax-paid in NC:	3,000 "	
Gallons underpurchased:	12,000 "	
Tax due to NC:	$3,600	(12,000 gals. X 30 cents/gal.)
Net tax due:	$1,200	($3,600 to NC less $2,400 from SC)

And Todd Trucking includes with its return, filed with South Carolina by April 30 (that is, by the end of the month following the conclusion of the calendar quarter) a check for $1,200. South Carolina also deposits this check in the bank, where it earns interest.

The final step in the process comes with the transmittal by South Carolina to North Carolina of Todd Trucking's $1,200, bundled in with all the rest of the funds collected by South Carolina and due to North Carolina. South Carolina is required by IFTA to make this transmittal by the end of May. *It does not pay North Carolina any interest* – although it has held some of the money it collected on the overpurchases of Todd Trucking for as much as five months (from January at the beginning of the quarter, through May when it renders up the money to North Carolina).

Loser – or Winner?

Let us further suppose that, perhaps because of its relatively low tax rate, South Carolina makes IFTA transmittals at the end of the quarter that exceed the amount that South Carolina receives from all the other IFTA states. Can it truthfully be said then that South Carolina is a loser under IFTA? By no means. The fuel use tax administered under IFTA is not the whole picture: the fuel purchase tax must be considered as well.

As should have been clear from the example of J.R. Todd Trucking, every dollar that South Carolina remits to another state under IFTA has been held by South Carolina for at least two months and perhaps for as much as five months. And the state will have earned interest on that money, interest that under IFTA it is entitled to *keep*. Every one of those dollars represents tax collected on motor carrier overpurchases in South Carolina, of fuel that they did not consume in the state. To be sure, other carriers will have underpurchased in South Carolina compared to their operations there (and the states where they bought the fuel they used in South Carolina will have earned interest on that tax), but as long as under IFTA South Carolina sends more money to other states at the end of a quarter than it receives from those states, South Carolina can count itself a *winner*.