

## Rising Gasoline Prices Benefit a Few States

By

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### Introduction

Every day, news headlines highlight the rising price of crude oil. An article on the determinants of oil prices, ominously titled “The Price of Fear,” was the top story in a recent edition of *The Economist*.<sup>1</sup> Federal Reserve Chairman Ben Bernanke testified before both houses of Congress that “concerns about unrest in the Middle East and North Africa and the possible effects on global oil supplies have led oil and gasoline prices to rise further.”<sup>2</sup> And a paper coauthored by Berkeley economist Severin Borenstein found that rising oil prices translate into a real financial burden at the pump, estimating that for every \$1.00 increase in a barrel of oil there is a 1.31 cent increase in a gallon of gasoline.<sup>3</sup>

Over the past year, the average price of gasoline in the United States has increased by almost 75 cents per gallon.<sup>4</sup> Every state and the federal government impose an excise tax on the sale of gasoline as a fixed number of cents per gallon. Therefore, as gas prices rise, states will see no increase in gas excise tax revenue since the tax rate is fixed regardless of price. In fact, states may even see a drop in revenue if demand decreases due to the higher prices.

Some states, however, apply a sales tax (or a similar tax) to gasoline, in addition to their excise tax. When gas prices go up, these states will receive additional tax revenue; For example, Indiana levies a 7 percent sales tax on gasoline in addition to its gasoline excise tax. Due to higher gas prices relative to a year ago, Indiana is currently collecting an additional 5 cents for every gallon of gasoline purchased. This amounts to over \$202 million in tax revenue for Indiana in just the past year, purely because of the increased price of gasoline. The following table shows the states that charge a percentage-based tax on gasoline:

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<sup>1</sup> “The Price of Fear.” *The Economist* 3 Mar. 2011: 29-32. <http://www.economist.com/node/18285768>.

<sup>2</sup> Ben S. Bernanke, “Semiannual Monetary Policy Report to the Congress.” 1 Mar. 2011.

<http://www.federalreserve.gov/newsevents/testimony/bernanke20110301a.htm>.

<sup>3</sup> Severin Borenstein, et al. “Do Gasoline Prices Respond Asymmetrically to Crude Oil Price Changes?” *Quarterly Journal of Economics*, February 1997.

<sup>4</sup> “Weekly U.S. Retail Gasoline Prices, Regular Grade.” U.S. Energy Information Administration, [http://www.eia.gov/oil\\_gas/petroleum/data\\_publications/wrgp/mogas\\_home\\_page.html](http://www.eia.gov/oil_gas/petroleum/data_publications/wrgp/mogas_home_page.html)

**Table1: State Sales Tax on Gasoline**

State	Tax	Comments
<b>California</b>	2.35% - 3.25% Sales Tax	State share 2.25%; district share 0.1%-1.0%
<b>Connecticut</b>	7% Gross Income Tax	Paid by the distributor
<b>Georgia</b>	4% Prepaid Sales Tax	Prepaid rate is determined on a semiannual basis
<b>Hawaii</b>	4% Gross Income Tax	Paid by the distributor
<b>Illinois</b>	6.25% - 9.25% Sales Tax	State share 5%; local/county share 1.25%-4.25%
<b>Indiana</b>	7% Sales Tax	
<b>Michigan</b>	6% Sales Tax	
<b>New York</b>	3%-4.75% Sales Tax	Depends on the county
<b>Virginia</b>	2% Sales Tax	Only in counties with public transportation

Source: State revenue departments

### Per Gallon Excise Tax

Currently, every state levies an excise tax on gasoline, ranging from 4 to 35.3 cents per gallon.<sup>5</sup> An excise tax is a tax levied on a narrow range of goods, generally dependent on the quantity purchased—in this case,  $x$  cents per gallon. Revenue generated from excise taxes is dependent on the quantity of goods purchased, and not the fluctuating market prices of goods. States charge an excise tax because the quantity of gasoline purchased is fairly constant, providing a steady stream of revenue.

### Ad Valorem Sales Tax

In contrast to an excise tax, an *ad valorem* tax is dependent on the price of the goods, and the tax is calculated as a percentage of that price. State and local sales taxes are the most common example of *ad valorem* taxes. Nine states levy some form of ad valorem tax on gasoline. Four states charge a simple sales tax on the final purchase. Indiana has the highest rate at 7 percent, followed by Illinois at 6.25 percent, Michigan at 6 percent, and California at 2.25 percent (districts can also charge between .1 percent and 1 percent on top of the state rate). Two others levy a gross income tax on the distributor: Connecticut at 7 percent and Hawaii at 4 percent. Georgia charges a 4 percent sales tax to the distributor based on a semiannual rate set by the Georgia Department of Revenue. Additionally, two other states have some form of ad valorem tax on gasoline: while New York exempts gasoline from its state sales tax, individual counties impose their respective sales taxes (between 3 percent and 4.75 percent) on gasoline. Likewise, counties in Virginia with public transportation systems charge a 2 percent sales tax on gasoline. States and localities that tax gasoline based on price as opposed to quantity will likely experience revenue gains based on recent gas prices.

### Methodology

All calculations in this paper involving the price of gasoline use data from the U.S. Energy Information Association, and estimates of quantity purchased come from the Federal Highway Administration. Information regarding excise taxes on gasoline can be found on our website at [www.taxfoundation.org/taxdata/show/26079.html](http://www.taxfoundation.org/taxdata/show/26079.html) as well as in the Tax Foundation's *Facts and Figures* booklet. Information on which states levy a sales tax is found on individual state governments' websites.

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<sup>5</sup> "2011 Facts and Figures: How Does Your State Compare?" *Tax Foundation*, 2011.  
<http://taxfoundation.org/files/ff2011.pdf>

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