

Montana Department of Transportation  
Report on Dyed Fuel Enforcement  
Submitted to the Revenue and Transportation Committee  
December 8, 2011

**Background**

Motor fuel tax, including the tax on diesel fuel is the primary funding source for the construction, maintenance, and administration of the highway system in Montana, including the state match for over \$300 million in federal revenue received each year. Diesel fuel is taxed at the rate of \$0.2775 per gallon and all diesel powered vehicles traveling on public roads in Montana are subject to this tax.

Untaxed diesel fuel is available in Montana for off-road use and other non-taxable activities. To distinguish untaxed fuel from taxed fuel, a red dye is added to the untaxed fuel at the refinery. Dyed fuel is exempt from both Montana and Federal taxes and can be purchased through petroleum distributors or at many retail stations.

**Vehicle Inspections**

Montana law allows for the inspection of motor vehicle supply tanks to ensure that dyed fuel is not being consumed on Montana roadways. MDT's Motor Carriers Services Officers routinely check for dyed fuel during motor carrier safety inspections. Additionally, they may pull vehicles over specifically to check for dyed fuel if probable cause exists to suspect dyed fuel abuse.

Civil penalties of up to \$1,000 for first offenses and \$5,000 for second and subsequent offenses are imposed on the driver if a concentration of dye of 2 parts per million or greater is found through such an inspection. The below table demonstrates the number of vehicles checked for dyed fuel and the number of violations found.

Fiscal Year	Vehicles Inspected	First Offense (\$1,000)	Second Offense (5,000)
2008	17,194	106	9
2009	27,377	84	2
2010	23,230	95	2
2011	25,474	59	3
TOTAL	93,275	344	16

## Appeals

Once a citation has been issued, the driver may file an appeal to the Department, either through an informal review or formal appeal. If the penalty is upheld at the Department level, the driver may wish to elevate to the State Tax Appeal Board (STAB) and ultimately to District Court.

During the informal review, the penalty may be upheld at the full, \$1,000, dismissed completely, or reduced based on the circumstances. The below table summarizes the dyed fuel citations that have been appealed.

Fiscal Year	Informal Appeal	Formal Appeal	STAB	District Court
2008	61	7	2	2
2009	29	3	1	0
2010	47	5	0	0
2011	28	4	1	1
TOTAL	165	19	4	3

## Special Fuel Users

Montana law requires that any contractors who work on public road projects (city, county, state, or federal) be licensed as a Special Fuel User (SU). SU's are required to use clear (taxed) diesel fuel on all operations and file tax returns to the department.

The intent of the SU license requirement is to level the playing field for all contractors bidding on public road projects by ensuring that fuel costs are relatively equal. A recent statutory change now requires contractors to include their SU license number as part of the bid submission.

MDT staff recently completed a state-wide fuel tax training program which provided educational opportunities for current and potential Special Fuel Users as well as petroleum distributors, International Fuel Tax Agreement (IFTA) carriers and International Registration Plan (IRP) carriers. Training was provided in more than 30 communities and nearly all public works offices were contacted to provide information relative to the SU requirements for public road projects.

The number of SU's has increased from 284 in 2008 to 393 in 2011.

## Internal Audit

MDT's Internal Audit Unit regularly performs audits on Special Fuel Users. These audits are prompted by either random selection or by referral from other MDT staff. The below table reflects the audit activity since FY2008.

<b>FY</b>	<b>Number of Audits</b>	<b>Total Audit Assessments</b>	<b>Final Assessment</b>
2008	1	\$ 180	\$ 180
2009	3	\$ 38,352	\$ 7,977
2010	3	\$ (5,085)	\$ (5,085)
2011	8	\$ 54,375	\$ 5,016

## Legislative Performance Audit

In September 2011, the Legislative Fiscal Division completed a performance audit entitled (Controls over Dyed Diesel Use in Montana." The report contained 6 recommendations, each concurred in by the Department.

This audit report can be found at: <http://leg.mt.gov/content/Publications/Audit/Report/11P-01.pdf> .

The goals of the audit were to:

- Determine if public road contracts comply with special fuel permitting requirements mandated by state law.
- Evaluate the effectiveness of enforcement of dyed diesel fuel on public roads.
- Assess management controls over MDT's dyed diesel enforcement activities.

Below is the current status of MDT's implementation of the 6 audit recommendations:

Audit Recommendation	Corrective Action Plan	Implementation Status
<b>Recommendation #1</b> We recommend the Montana Department of Transportation expand contractor reviews to include subcontractors working on department road contracts to ensure they have the statutorily required special fuel users permit.	Develop a process to check whether subcontractors have an SU license.	Implementation Complete
<b>Recommendation #2</b> We recommend the Montana Department of Transportation provide training to local and federal government contracting personnel regarding special fuel users permit requirements.	MDT representatives will stop by all 56 County offices, 64 public works offices and 7 federal offices across Montana	Implementation Complete
<b>Recommendation #3</b> We recommend the Montana Department of Transportation define its process and expectations for public road project inspections to help ensure contractors comply with state law related to dyed diesel use.	Develop guidelines for MCS Officers to review and perform public road projects	Target Completion Date 7/31/2012
<b>Recommendation #4</b> We recommend the Montana Department of Transportation establish a risk based vehicle inspection program for its dyed diesel enforcement activities.	Using available data and information for other state jurisdictions to develop guidelines to target high risk areas. These guidelines will also include a mechanism for tracking and documenting any concentrated enforcement efforts.	Target Completion Date 7/31/2012
<b>Recommendation #5</b> We recommend the Montana Department of Transportation design and implement a process to identify high risk areas related to dyed diesel that should be further examined by the Internal Audit Unit.	Gather data from multiple divisions and develop a risk assessment that will be used to help identify which audits to perform in the next plan year.	Implementation Complete
<b>Recommendation #6</b> We recommend the Montana Department of Transportation strengthen dyed diesel enforcement by: A. Using available information to prioritize enforcement activities. B. Compiling data related to inspections for public road projects. C. Tracking the disposition of dyed fuel tip line calls. D. Sharing information related to the department's appeals process.	A. Develop guidelines for fuel inspections. B. Review alternatives for inspections, then develop guidelines. C. Develop a system for tracking dyed fuel tip line calls. D. Develop a system for tracking appeals and their resolution.	Target Completion Date 7/31/2012  (implementation complete on C and D)

### Recommendation #3

MCS is working on guidelines to address this recommendation. To date, the Administration Division had completed training to all county and public works offices. In addition to this, the preliminary discussions include:

- Exploring areas to becoming more educated on all the Public Work projects in the state i.e., web sites.
- Educating the District Captains on how to find the number and locations of the Public Work sites in each district. The Captains could then implement best practices for their officers to check these projects sites.
- Meet with the industry to educate and solicit ideas.
- Implement a tracking system to document the inspection of each project.

The goal is to have these guidelines in place before the 2012 construction season is started.

Recommendations #4 and #6

MCS is working on guidelines to address this recommendation. Our preliminary discussions include:

- Use of inspection sites
- Researching surrounding states practices
- Exploring options to team up with other state agencies on inspections
- Identifying the high risk areas in the state
- Looking at the MCS Enforcement officers resources i.e., scale officers vs. patrol officers
- Exploring possibilities of working with and educating the Industry
- Develop a tracking mechanism of enforcement activities for documentation and determining high risk areas

The goal is to have this complete by July 2012. This will allow time to work with the industry prior to implementing a plan.

## **Impact on State Special Revenue Fund**

Although difficult to quantify, dyed fuel enforcement has had a positive impact to the state special revenue fund.

The following outcomes indicate a greater compliance with dyed fuel laws, resulting in a positive impact to the state special revenue fund.

- The number of vehicle inspections increased from 17,194 in 2008 to 25,474 in 2011 ( up 48%) yet the total number of violations found has decreased from 115 in 2008 to 62 in 2011 (down 46%)
- The number of licensed Special Fuel Users had increased from 284 in 2008 to 393 in 2011 (up 38%)
- Nearly 44% of the diesel fuel sold in FY2008 was dyed, compared to less than 42% in 2011 (FY2012 to date is 39%)

## **Biodiesel Fuel Tax Incentives**

The 2005 Montana Legislature created fuel tax incentives for Biodiesel producers, licensed distributors, and retailers selling Biodiesel. House Bill 756 became effective July 1, 2005 and provides 10 cents per gallon incentive on each gallon increase of Biodiesel production over the previous year. The tax incentive may be claimed for 1) the first year's total production, 2) the production in the second year that exceeds the production in the first year, and 3) the production in the third year that exceeds production in the second year.

Two licensed distributors applied for and qualified for the incentive of \$.10 per gallon. In FY09, \$495.90 was paid to a Belgrade distributor.

In FY10, \$3,536.70 was paid to a Chester distributor.

This incentive expired effective June 30, 2010.

HB 776: Provides a refund of 2 cents per gallon to licensed distributors and 1 cent per gallon to retailers who sell Biodiesel that is produced entirely from Biodiesel ingredients produced in Montana. The refunds must be applied for within 30 days after the quarter ends. The department has never had any person apply for this incentive.

## **Contacts**

If you have questions or comments regarding MDT's dyed fuel enforcement activities, please contact one of the following:

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