

Bond Case Briefs

Municipal Finance Law Since 1971

Disputes Over State Taxes on Railroad Fuel Simmer Before Supreme Court.

The court on Monday asked for the U.S. government to submit views on an Alabama case.

Alabama for about a decade now has been battling in court over whether a tax the state levies on the diesel fuel that railroads purchase to power their locomotives discriminates against the industry and is therefore in violation of federal law.

In the latest chapter of this long-running dispute, two [linked petitions](#) concerning the same case are pending before the U.S. Supreme Court. So far, the high court hasn't decided to hear the matter. But on Monday justices [asked](#) for the Trump administration to submit views on it.

Alabama's lawyers describe the case as the "de facto bellwether" for other related disputes.

They add that state and federal courts across the federal 11th Circuit, which covers Alabama and Georgia, have stayed over 30 actions in the two states for tax refunds and injunctions while awaiting resolution in the case, which pits Alabama against CSX Transportation, Inc.

The Alabama legal fight hinges on claims by CSX, one of the nation's largest rail carriers, that the state discriminates against it by requiring railroads to pay a 4 percent sales and use tax on diesel purchases. In contrast, trucks and interstate water carriers are exempt from the tax.

Alabama says eight railroads have sued seeking refunds for tax payments on fuel totaling about \$24 million, not including interest, and that CSX stopped paying the state tax in 2011. Most of the state's sales and use tax revenue goes to fund public schools, the state adds.

It also notes that CSX is seeking to clawback similar taxes in Georgia totaling upwards of \$34 million.

CSX agrees there are public dollars at stake.

But the company says the state "ignores the victim of its illegal taxing scheme" and that "the railroads have been in the past, and continue to be, beleaguered by what Congress determined was 'widespread, long-standing and deliberate' discriminatory state and local taxation."

Claims Under the '4-R Act'

The federal law at the center of the controversy is the [Railroad Revitalization and Regulatory Reform Act](#), or "4-R Act."

Enacted in 1976, it prohibits three types of state tax practices related to property taxes. The law also contains a clause that blocks states from imposing other types of taxes that discriminate against rail carriers under the jurisdiction of the federal government.

On two other occasions, Alabama's fuel tax feud with CSX has reached to the Supreme Court—most

recently in [late 2014](#).

That time around, the court sent the case back to the 11th U.S. Circuit Court of Appeals to determine whether Alabama could justify the tax exemptions for trucks and water carriers, like barges.

In the wake of the ruling, Alabama now says the Supreme Court should hear the case to “definitively” clarify whether and when sales and use tax exemptions violate the 4-R Act.

The state’s petition asking the court to take up the case describes how railroads, citing the federal law, began bringing litigation in the 1990s against state taxes on diesel fuel. These claims began in Alabama in 2008, with seven rail carriers filing four lawsuits.

“States have been waiting for an answer for more than 20 years; years we have spent litigating cases that have cost taxpayers millions of dollars,” the state’s filing with the Supreme Court says.

“Granting review to answer the decades-old question thus provides the opportunity to resolve multiple pending cases and prevent new ones.”

The railroad says it’s inaccurate to characterize the case as the culmination of two decades of litigation because there has not been a string of prior cases with unsettled questions about when tax exemptions for water carriers are justified.

CSX, in a linked “cross-petition,” is asking the Supreme Court to review the portion of the 11th Circuit decision related to trucks if it green-lights the state’s petition focused on water carriers.

While truckers don’t pay the sales and use tax on fuel in Alabama, they do pay a 19 cent per gallon state excise tax on diesel, along with a roughly 24 cent per gallon federal tax. Cargo vessels traveling in and out of the state on waterways don’t pay a state fuel tax in Alabama, but do pay a per gallon federal tax of about 29-cents.

Fuel for CSX trains is not subject to any of those taxes, the state court filing notes. Alabama says that between 2007 and 2016 its state and local taxes for train fuel totaled about 23-cents per-gallon.

The company counters that while water carriers pay no Alabama state fuel taxes, CSX in Birmingham and Montgomery, where it buys most of its fuel in the state, faces a combined state and local tax rate of 10 percent, and statewide owes about \$5 million in the tax costs annually.

The state’s tax exemption for fuel used by water carriers dates back to 1939 and the state says that, while it’s not entirely clear, it was likely enacted to comply with federal laws and court decisions.

“Alabama did not exempt water carriers to disadvantage trains,” its court petition says.

The state also makes a case that the federal government has jurisdiction over waters used for interstate shipping, and because vessel operators pay federal fuel tax to support projects and policing on those waters, states should be able to forego taxing fuel for ships.

CSX argues that the federal taxes are “irrelevant” and points out that the 11th Circuit rejected arguments tied to the fact that shipping on interstate waters is within the federal domain.

The company says in the 1970s, when lawmakers passed the 4-R Act, many railroads were on the brink of financial collapse, partly due to state and local tax burdens, and that the federal law was meant to help boost competition between freight trains and other types of haulers.

“The Eleventh Circuit’s water carrier ruling does just that,” the company says. “A state should not be heard to complain of ‘lost tax revenue’ from its own discriminatory tax.”

The 11th Circuit ruling, which preceded the current petition and cross-petition before the Supreme Court, gave Alabama two options to fix the discrimination it found: stop collecting sales and use taxes on fuel from the railroad, or revoke the water carrier exemption.

Under the first option, CSX would pay zero taxes on fuel in the state, Alabama says. With the second, it would face a total tax burden in the state for diesel of about 23 cents per gallon, while for trucks the figure would be around 47 cents, and for barges about 52 cents.

Use of Tax Proceeds

Another company, Illinois Central Railroad Co., on Jan. 2, filed a petition asking the Supreme Court to hear a similar but separate case dealing with a Tennessee tax law.

In the Illinois Central case, the company is asking the court to consider whether a state fuel tax on diesel for trains, that truckers are exempt from, discriminates against railroads under the 4-R Act. The 6th U.S. Circuit Court of Appeals upheld the tax, deeming it “roughly equivalent” to the fuel taxes that motor carriers do pay in the state.

Illinois Central zeros in on the idea that the way tax revenues are spent can factor into whether a tax is discriminatory. Sure, truckers pay fuel taxes in the state, the railroad says, but that money helps pay for highway construction and maintenance, which they benefit from.

Railroads on the other hand, according to Illinois Central, receive “minimal direct benefit” from the fuel taxes they pay and must pony up for their own infrastructure, like tracks and bridges.

This gives an advantage to trucking firms, the company claims. Illinois Central says the case presents the court with a chance to resolve whether the way a state uses tax revenue is relevant when it comes to determining if a tax is allowable under the 4-R Act.

CSX’s cross-petition, urging the Supreme Court to weigh in on the 11th Circuit’s blessing of Alabama’s diesel sales and use tax exclusion for trucks, features similar arguments.

Alabama’s lawyers [say the court should grant](#) the railroad’s cross-petition to resolve questions about the “truck issue” as well.

They also say the Illinois Central case does not present the same issues surrounding the justification for the water carrier exemption and that the court should take its case instead. “The one it knows best,” the state adds, “and thanks to Alabama’s acquiescence to CSX’s cross-petition, the only one that tees up all necessary issues.”

Route Fifty

By Bill Lucia,
Senior Reporter

JANUARY 14, 2019