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May 23, 2016

The Honorable Kevin Meyer
President of the Senate
Alaska State Legislature
State Capitol, Room 111
Juneau, AK 99801-1182

Dear President Meyer:

Under the authority of Article III, Section 18, of the Alaska Constitution, I am transmitting a bill relating to revenue measures, including the establishment of an individual income tax, tax measures on fisheries business tax and fisheries landing tax, the mining license tax, the excise tax on alcoholic beverages, raising the tax on tobacco products and taxing electronic smoking products, fees for commercial fisheries entry or interim use permits, regarding the administration and enforcement of the marijuana excise tax.

This is a necessary measure to address our fiscal situation. My approach is a broad-based tax bill to address the need as our current revenues decrease. This has made it necessary to update our tax laws. My proposed measures, while modest, will make a significant difference to the State's fiscal situation.

First, the bill would establish a personal income tax of six percent of total federal tax liability. Because the tax would be calculated based on federal tax liability rather than on income, the bill effectively incorporates federal brackets and exemptions. This permits this bill, and the Alaska personal income tax system it would create, to be as simple and transparent as possible and minimizes administrative burdens both for the State and for taxpayers. This portion of the bill has a delayed effective date, and would apply to income earned on or after January 1, 2018. In addition, the bill would repeal a set of orphaned individual tax credits from the former income tax.

The relatively modest tax is expected to raise approximately \$200,000,000. Because, for those who itemize federal tax deductions, the tax would be deductible from federal income tax, the deduction from federal taxes would offset the actual burden of this tax to Alaska taxpayers by 20 – 25 percent.

Next, the bill would update our cigarette taxes and include newer electronic smoking products. Smoking technology has advanced to include multiple use electronic smoking products which are currently untaxed in Alaska. Therefore, our tobacco tax statutes (AS 43.50 Cigarette Tax Act) should be revised to include this new smoking product. To further update our outdated tobacco tax structure, I propose to amend the additional tax levy on cigarettes – which has not been raised since

2007 – from 62 mills to 112 mills. This change will increase the total State tax per standard cigarette pack from \$2.00 to \$3.00. I also propose increasing the tax rate on tobacco products (other than cigarettes) from 75 percent of the wholesale price to 100 percent of the wholesale price. These reasonable adjustments will bring our tax structure up to date.

The alcoholic beverage tax rates have not been raised for many years. Therefore, the bill would increase the tax rates on alcoholic beverages under AS 43.60 (excise tax on alcoholic beverages). Alcoholic beverage excise taxes are levied on malt beverages, cider with at least 0.5 percent alcohol, wine, and other beverages with a higher alcohol content. The bill would double the tax rates on each gallon or fraction of a gallon. As a result, the excise tax on malt beverages or cider would be \$2.14 a gallon or fraction of a gallon; the tax on wine or other beverages would be \$5.00 a gallon or fraction of a gallon; and the tax on beverages containing more than 21 percent alcohol by volume would be \$25.60 a gallon. The effective tax rate, after these changes, will be 20 cents per standard drink portion. I believe this proposed increase is reasonable, especially considering the high societal cost of alcoholic beverage consumption. Under this bill, the alcoholic beverage industry would bear a fairer share of industry costs to the State, yet still continue as an economically healthy industry.

The bill also would amend AS 43.60.040(a) related to surety bonds. Current law requires a \$25,000 surety bond before a license is issued. This amount is out of date, as many wholesalers require a surety bond much greater than that; at the same time very small brewers and distillers require a smaller surety bond. The bill proposes to amend AS 43.60.040(a) to delete the \$25,000 bond and instead add language that the surety bond amount would be determined by the Department of Revenue.

The mining industry is important to the state, but the taxation rates are too low to maintain. My proposal makes necessary adjustments to the tax imposed on mining operations. Therefore, the bill would change the exemption from paying the mining license tax that currently applies to operations for three and one-half years after production begins to a more reasonable two years. This provides a sustainable balance between assisting new mining operations and taxing revenues from those operations. Additionally, the bill would change the way the mineral and coal deposit exploration incentive credit is determined by removing the ability to apply the credit against mineral royalty production payments. The bill also would increase the mining license tax rate from seven percent to nine percent for that portion of net income in excess of \$100,000 beginning July 1, 2016.

Further, the bill would increase the tax rates of the fisheries business tax (AS 43.75.015) and the fishery resource landing tax (AS 43.77.010). Developing fisheries are exempted from the increase. The tax rates covered by these statutes vary from three percent to five percent, depending on the type of fishery. The bill would increase those tax rates by one percentage point across the board. Currently, the revenue generated by these taxes is split evenly between the State and the municipalities where the fisheries are located. The bill would exempt this one percentage point increase from the revenue sharing arrangement, thereby insuring that the entire increase is applied to the general fund. The bill also would require electronic submission for fishery taxpayers.

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Additionally, the bill removes the existing \$3,000 annual cap for entry permits issued by the Commercial Fisheries Entry Commission.

The bill also addresses the marijuana tax laws, first, by requiring a marijuana cultivation facility to furnish a bond before a license may be issued by the Marijuana Control Board, and by establishing under the Department of Revenue's authority the ability to levy the marijuana excise tax on both persons who are in possession of more marijuana than the amount that is allowable for personal use and possession under our marijuana statute as well as marijuana retail establishments who have purchased product from an unlicensed cultivator.

The citizens of our state are ready to pitch in to solve our fiscal crisis. My measures, by involving a broad base of industries, would result in each industry bearing a small share of needed tax changes. Together we can continue to assure Alaska's strong and stable financial future.

I urge your prompt and favorable action on this measure.

Sincerely,



Bill Walker,
Governor

Enclosure