

Senate Labor & Commerce

HB 115 - Education Funding Act

Version K.A

30th Alaska Legislature

What does the bill do?

HB 115 creates the Alaska school based income tax and designates revenue to the Public Education Fund.

- Applies to residents and non-residents;
- Includes personal exemption of \$4,000 per person;
- Includes exemption for the permanent fund dividend;
- Creates brackets based on Adjusted Gross Income (AGI);
- Income from S-Corporations will be taxed on the individual partner or owner's tax return;
- Planned implementation is January 1, 2019.

Why do we need the bill?

- Creates consistent stream of funding for education;
- Diversifies revenue to minimize volatility;
- Prioritizes education;
- Progressive (income tax) vs. Regressive (PFD reduction);
- Gives Alaskans a voice in their government's decisions;
- Creates an incentive for the State to grow our economy.

Why Adjusted Gross Income?

***Volatility of federal tax liability** – If federal tax rates change this automatically impacts state revenue levels, with no state input. Issue is addressed by using adjusted gross income instead of tax liability;

***Exemptions & credits** – Using adjusted gross gives a clean slate instead of automatically adopting all federal credits and deductions;

***Equity between capital gains & wages** – All income is treated the same in computing adjusted gross income;

***Administrative ease** – Calculating non-resident taxable income is simpler under adjusted gross income than under federal tax liability;

***Alaska Specific** – Alaska taxable income now includes a \$4,000 personal deduction and a deduction for the permanent fund dividend, which cannot be deducted from federal tax liability.

History of Tax in Alaska

Before oil started flowing, Alaskans were accustomed to participating in their state economy through a structured tax program. The income and school taxes created stability for basic programs – education, health, public safety, infrastructure, and more.

- School tax Implemented in 1949 during territorial days;
- Alaska Territorial Legislature also passed income tax in 1949 (in 11 days);
- Alaskans paid both taxes from 1949-1980;
- In 1975 the income tax had changed from 16% of federal tax liability to a tax with brackets from 3 to 14.5%;
- Alaska income tax provided 40% of all state revenue.

CSHB 115

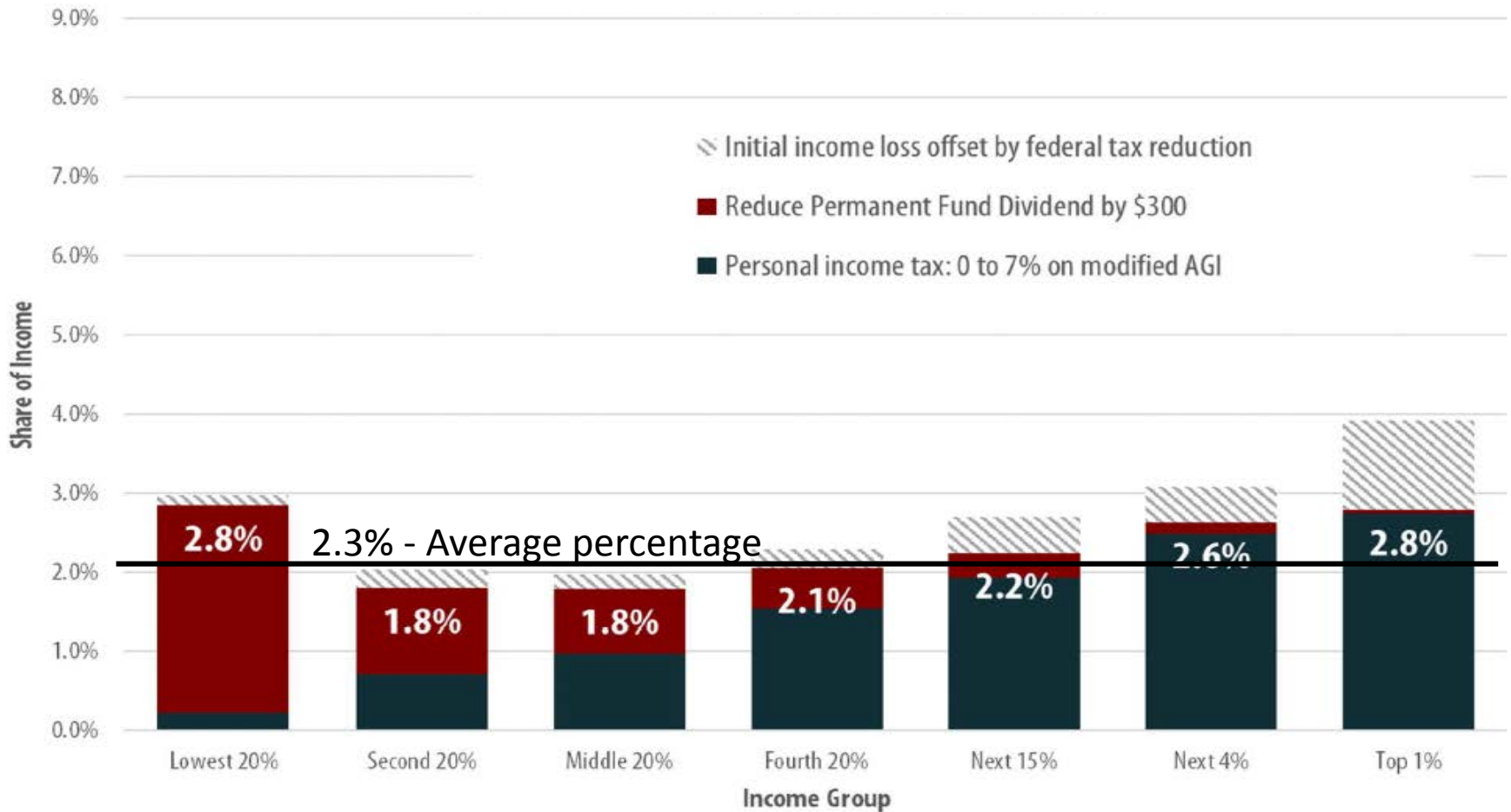
Education Funding Act

Estimated revenue based on effective date of
January 1, 2019

| | |
|---------------------------------|---------------|
| FY2019 - Half year | \$341 million |
| FY2020 - First full year | \$687 million |

*Alaska school tax starts with the federal AGI – Line 37 on Schedule 40.
Approximately \$80 million will come from non-residents when fully
implemented.*

Future impact across income brackets, based on CSHB 115 (Education Tax) & restructure PFD resulting from HCS SB 26.



Source: Institute on Taxation and Economic Policy, March 2017. Modeled in a Tax Year 2016 economy, modified to assume a baseline Permanent Fund Dividend payout of \$1,700 per person.

**Long term combined impact of HB 115 and HCS SB 26 across income groups. Short term impact has a greater effect on the lowest 20% due to immediate & larger change to the Permanent Fund Dividend in the first few years.*

How does Alaska compare to other States?

*State and Local Tax Burden by Rank



| | State-Local Tax Burden as Percent of State Income | Rank | Income | Income Rank |
|---------------|---|------|----------|-------------|
| Alaska | 6.5% | 50 | \$49,780 | 10 |

*Tax Burden includes all state and local taxes paid directly by residents, but also includes indirect taxes which may be passed to the consumer, such as severance taxes.

Chart from Tax Foundation website:

<http://taxfoundation.org/article/state-local-tax-burden-rankings-fy-2012>. Table 12 for FY 2012

State Personal Income Tax Revenue as a Share of Personal Income in States with Broad-Based Personal Income Taxes

2015, dollar amounts in thousands

| Rank (1 = lowest) | State | Effective Tax Rate (tax / income) | State Personal Income Tax Revenue | Personal Income |
|----------------------|-----------------|--------------------------------------|--------------------------------------|-----------------|
| 1 | North Dakota | 1.19% | \$504,394 | \$42,349,688 |
| 2 | Arizona | 1.45% | \$3,868,234 | \$267,361,132 |
| 3 | Louisiana | 1.46% | \$2,922,499 | \$200,594,438 |
| 4 (proposed) | Alaska (HB115)* | 1.66% | \$681,006 | \$40,907,753 |
| 4 | Kansas | 1.70% | \$2,335,804 | \$137,316,497 |
| 5 | New Mexico | 1.72% | \$1,358,702 | \$79,104,093 |
| 6 | Mississippi | 1.73% | \$1,798,699 | \$104,045,259 |
| 7 | Ohio | 1.77% | \$8,950,232 | \$505,950,314 |
| 8 | Oklahoma | 1.80% | \$3,209,442 | \$178,250,475 |
| 9 | Pennsylvania | 1.84% | \$11,735,689 | \$636,857,158 |
| 10 | Alabama | 1.84% | \$3,407,750 | \$184,784,917 |
| 11 | South Carolina | 2.03% | \$3,802,638 | \$187,532,342 |

Source: Analysis by the Institute on Taxation and Economic Policy (ITEP) of Calendar Year 2015 state income tax data from the U.S. Census Bureau and personal income data from the Bureau of Economic Analysis (BEA).

Sample of Other State Income Brackets based on AGI

| | | | |
|--|-------|---|----------|
| Hawaii | 1.40% | > | \$0 |
| | 3.20% | > | \$2,400 |
| <i>Hawaii does not adjust brackets for inflation</i> | 5.50% | > | \$4,800 |
| | 6.40% | > | \$9,600 |
| | 6.80% | > | \$14,400 |
| | 7.20% | > | \$19,200 |
| | 7.60% | > | \$24,000 |
| | 7.90% | > | \$36,000 |
| | 8.25% | > | \$48,000 |

| | | | |
|---|--------|---|-----------|
| Ohio | 0.495% | > | \$0 |
| (b, c, e, g) | 0.990% | > | \$5,250 |
| | 1.980% | > | \$10,500 |
| <i>Has additional income taxes at local level averaging 2.25%</i> | 2.476% | > | \$15,800 |
| | 2.969% | > | \$21,100 |
| | 3.465% | > | \$42,100 |
| | 3.960% | > | \$84,200 |
| | 4.597% | > | \$105,300 |
| | 4.997% | > | \$210,600 |

Source: Tax Foundation "Facts & Figures 2017: How Does Your State Compare?" www.taxfoundation.org/publications/facts-and-figures/

| | | | |
|---|------|---|----------|
| Mont. | 1.0% | > | \$0 |
| (a, e, g) | 2.0% | > | \$2,900 |
| <i>Allows deduction for some of federal taxes</i> | 3.0% | > | \$5,200 |
| | 4.0% | > | \$7,900 |
| | 5.0% | > | \$10,600 |
| | 6.0% | > | \$13,600 |
| | 6.9% | > | \$17,600 |

| | | | |
|--|------|---|----------|
| Ky. (b) | 2.0% | > | \$0 |
| | 3.0% | > | \$3,000 |
| <i>Kentucky does not adjust brackets for inflation</i> | 4.0% | > | \$4,000 |
| | 5.0% | > | \$5,000 |
| <i>Has additional income taxes at local level averaging 2%</i> | 5.8% | > | \$8,000 |
| | 6.0% | > | \$75,000 |

Alaska: 2.5% starting at \$10,300 of taxable income. When including the personal exemption and PFD deduction, this means \$15,550 for a single person and \$31,100 for a married couple is tax exempt.

5 Workers and Wages, Major and Selected Industry Categories

Alaska, 2015

| Industry | Total | | Nonresident | | | |
|---|---------|-------------|-------------|---------|-------------|---------|
| | Workers | Wages (mil) | Workers | Percent | Wages (mil) | Percent |
| Agriculture, Forestry, Fishing and Hunting | 2,507 | \$55.8 | 1,354 | 54.0% | \$28.0 | 50.2% |
| Mining | 22,349 | \$2,416.4 | 7,937 | 35.5% | \$805.2 | 33.3% |
| Oil and Gas | 4,702 | \$910.8 | 1,385 | 29.5% | \$252.8 | 27.8% |
| Oilfield Services* | 13,777 | \$1,184.4 | 5,343 | 38.8% | \$454.7 | 38.4% |
| Utilities | 2,596 | \$201.1 | 133 | 5.1% | \$6.7 | 3.3% |
| Construction | 26,868 | \$1,338.0 | 5,932 | 22.1% | \$217.8 | 16.3% |
| Manufacturing | 28,481 | \$646.7 | 18,005 | 63.2% | \$295.4 | 45.7% |
| Seafood Processing | 23,131 | \$413.8 | 17,024 | 73.6% | \$267.5 | 64.6% |
| Wholesale Trade | 7,315 | \$358.0 | 713 | 9.7% | \$22.8 | 6.4% |
| Retail Trade | 49,499 | \$1,154.1 | 8,176 | 16.5% | \$101.1 | 8.8% |
| Transportation and Warehousing | 25,515 | \$1,222.1 | 6,704 | 26.3% | \$288.3 | 23.6% |
| Air Transportation | 7,718 | \$336.3 | 2,001 | 25.9% | \$62.3 | 18.5% |
| Information | 7,551 | \$419.0 | 766 | 10.1% | \$29.0 | 6.9% |
| Finance and Insurance | 8,130 | \$453.0 | 665 | 8.2% | \$19.2 | 4.2% |
| Real Estate and Rental and Leasing | 7,108 | \$220.1 | 837 | 11.8% | \$17.0 | 7.7% |
| Professional, Scientific, and Technical Services | 18,186 | \$1,022.2 | 4,367 | 24.0% | \$226.8 | 22.2% |
| Management of Companies and Enterprises | 2,823 | \$195.6 | 566 | 20.0% | \$29.1 | 14.9% |
| Administrative Support/Waste Management and Remediation | 17,460 | \$545.8 | 4,171 | 23.9% | \$101.3 | 18.6% |
| Educational Services | 2,873 | \$68.6 | 648 | 22.6% | \$7.4 | 10.8% |
| Health Care and Social Assistance | 50,996 | \$2,232.5 | 5,457 | 10.7% | \$183.5 | 8.2% |
| Arts, Entertainment, and Recreation | 7,405 | \$97.0 | 2,416 | 32.6% | \$23.2 | 23.9% |
| Accommodation and Food Services | 43,801 | \$676.4 | 13,822 | 31.6% | \$147.4 | 21.8% |
| Accommodation | 12,858 | \$211.1 | 6,080 | 47.3% | \$68.5 | 32.4% |
| Food Services and Drinking Places | 30,430 | \$460.5 | 7,565 | 24.9% | \$77.6 | 16.8% |
| Other Services | 12,971 | \$388.8 | 1,880 | 14.5% | \$37.1 | 9.5% |
| Other/Unknown | 653 | \$13.3 | 257 | 39.4% | \$4.6 | 34.5% |
| Local Government | 50,138 | \$1,878.0 | 3,553 | 7.1% | \$77.5 | 4.1% |
| State Government | 27,625 | \$1,341.8 | 1,908 | 6.9% | \$48.0 | 3.6% |

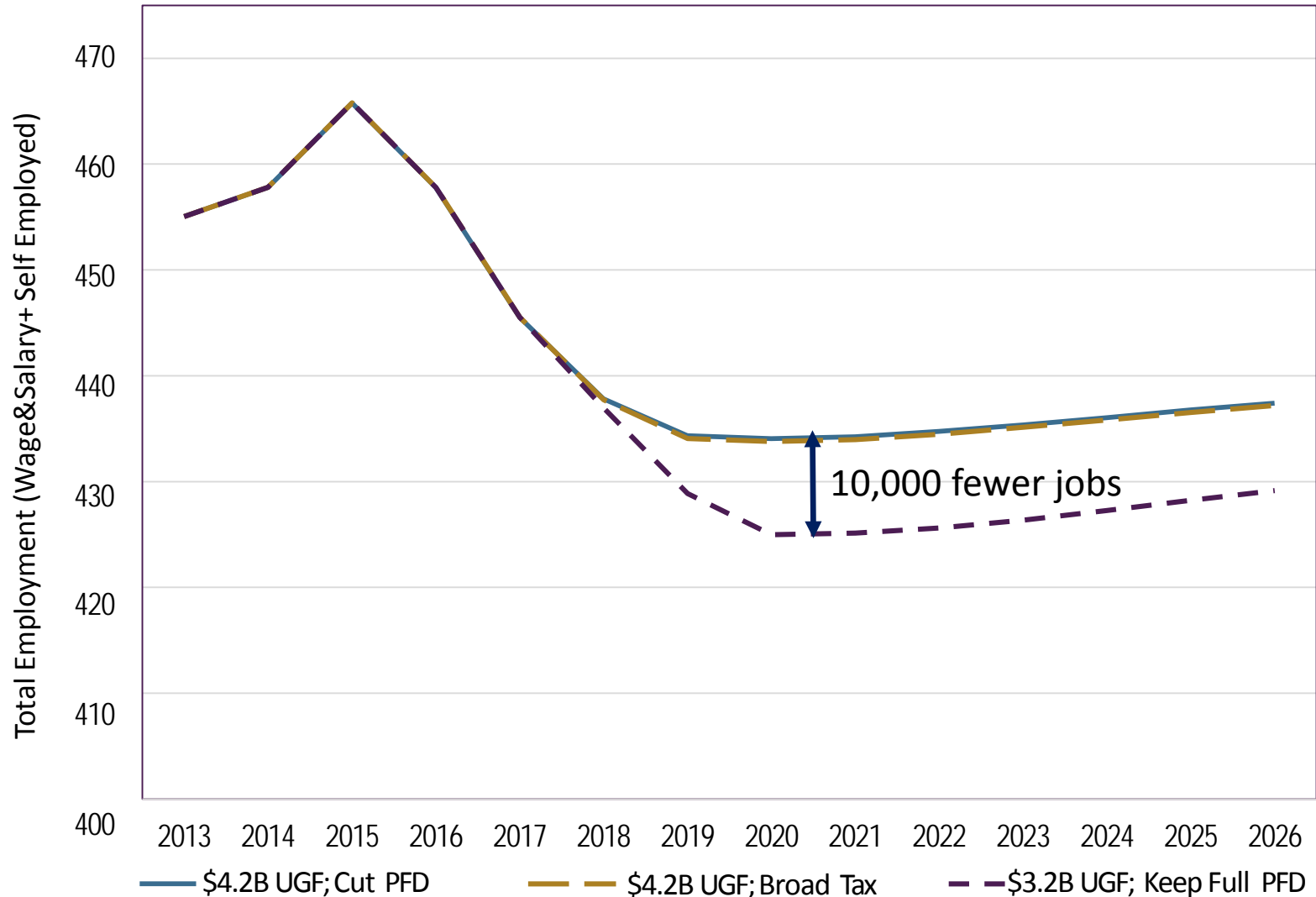
Total

422,850 \$16,944.3 90,267 21.3% \$2,716.0 16%

Note: Data exclude the self-employed, fishermen, and other agricultural workers, and private household workers. For estimates of fish harvesting employment, go to labor.alaska.gov/research/seafood/seafood.htm.

Source: Alaska Department of Labor and Workforce Development, Research and Analysis Section, 2015 Nonresidents Working in Alaska report.

2017-2026 Employment Forecast under Three Budget Scenarios



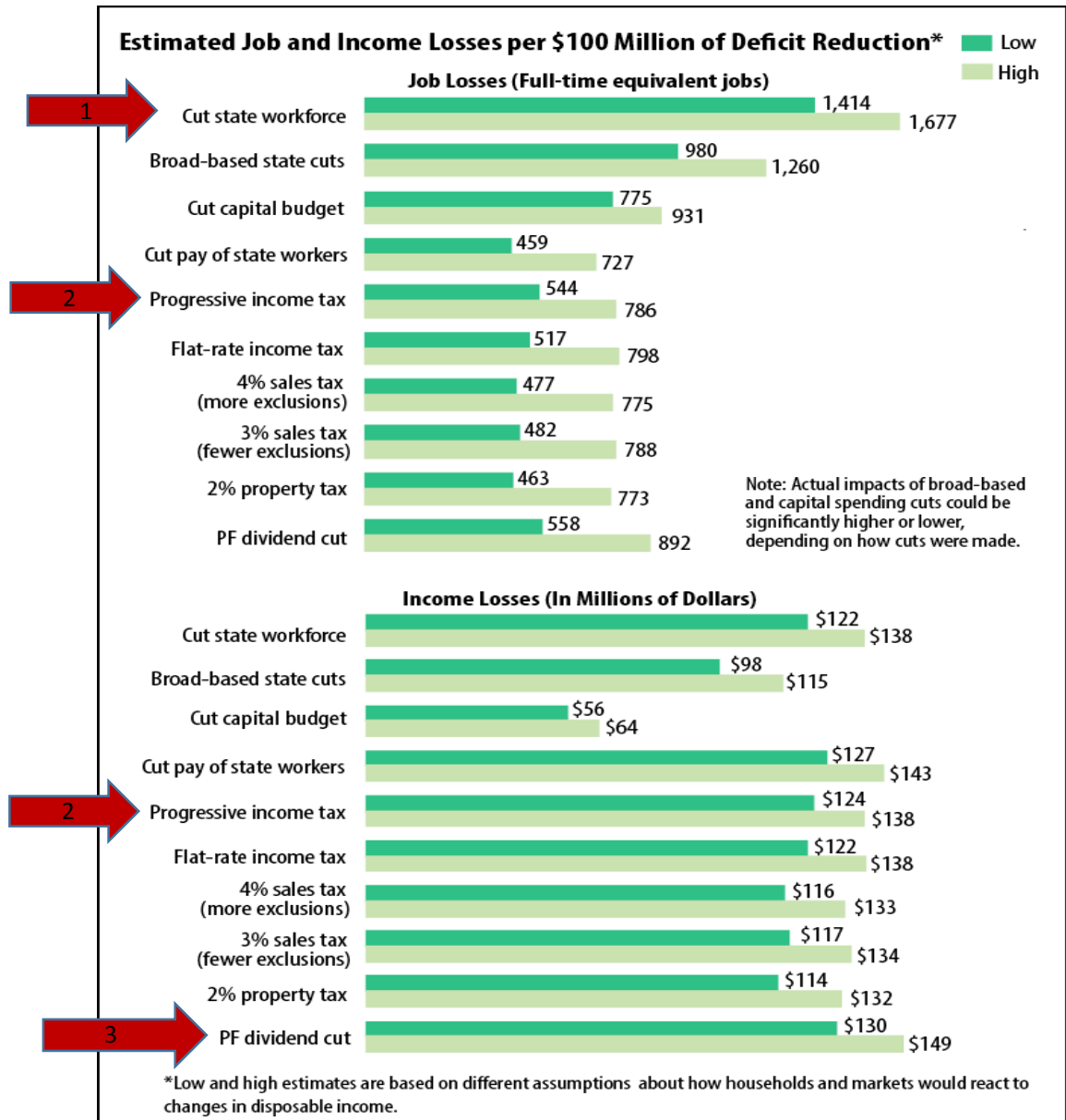
Source: Northern Economics "Forecasting Alaska's Economy: 2016-2017".
By Jonathan King

Impacts of cuts on Alaska's workforce

1. Closing the deficit just by cutting state jobs would cost the economy the most jobs.

2. Progressive income tax has a smaller impact on job losses, and would be partly paid by non-residents, so they have smaller direct impacts on incomes.

3. Dividend cuts would have the greatest short-run effects on Income.



For the year (Jan. 1–Dec. 31, 2015, or other tax year beginning . . . , 2015, ending . . . , 20 . . .) See separate instructions.

Your first name and initial . . . Last name . . . Your social security number . . .

If a joint return, spouse's first name and initial . . . Last name . . . Spouse's social security number . . .

Home address (number and street). If you have a P.O. box, see instructions. . . Apt. no. . .

City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions).

Foreign country name . . . Foreign province/state/country . . . Foreign postal code . . .

Presidential Election Campaign: Check here if you, or your spouse if filing jointly, want \$3 to go to this fund. Checking a box below will not change your tax or refund. You Spouse

Filing Status

Check only one box.

1 Single

2 Married filing jointly (even if only one had income)

3 Married filing separately. Enter spouse's SSN above and full name here. ▶

4 Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶

5 Qualifying widow(or) with dependent child

Exemptions

6a Yourself. If someone can claim you as a dependent, do not check box 6a

b Spouse

| c Dependents: | | (2) Dependent's social security number | (3) Dependent's relationship to you | (4) <input type="checkbox"/> If child under age 17 qualifying for child tax credit (see instructions) |
|----------------|-----------|--|-------------------------------------|---|
| (1) First name | Last name | | | |
| | | | | <input type="checkbox"/> |
| | | | | <input type="checkbox"/> |
| | | | | <input type="checkbox"/> |
| | | | | <input type="checkbox"/> |

d Total number of exemptions claimed

Boxes checked on 6a and 6b

No. of children on 6c who: • lived with you • did not live with you due to divorce or separation (see instructions)

Dependents on 6c not entered above

Add numbers on lines above ▶

Income

7 Wages, salaries, tips, etc. Attach Form(s) W-2 7

8a Taxable interest. Attach Schedule B if required 8a

8b Tax-exempt interest. Do not include on line 8a 8b

9a Ordinary dividends. Attach Schedule B if required 9a

9b Qualified dividends 9b

10 Taxable refunds, credits, or offsets of state and local income taxes 10

11 Alimony received 11

12 Business income or (loss). Attach Schedule C or C-EZ 12

13 Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ 13

14 Other gains or (losses). Attach Form 4797 14

15a IRA distributions 15a

b Taxable amount 15b

16a Pensions and annuities 16a

b Taxable amount 16b

17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E 17

18 Farm income or (loss). Attach Schedule F 18

19 Unemployment compensation 19

20a Social security benefits 20a

b Taxable amount 20b

21 Other income. List type and amount 21

22 Combine the amounts in the far right column for lines 7 through 21. This is your total income ▶ 22

Adjusted Gross Income

23 Educator expenses 23

24 Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ 24

25 Health savings account deduction. Attach Form 8889 25

26 Moving expenses. Attach Form 3903 26

27 Deductible part of self-employment tax. Attach Schedule SE 27

28 Self-employed SEP, SIMPLE, and qualified plans 28

29 Self-employed health insurance deduction 29

30 Penalty on early withdrawal of savings 30

31a Alimony paid b Recipient's SSN ▶ 31a

32 IRA deduction 32

33 Student loan interest deduction 33

34 Tuition and fees. Attach Form 8917 34

35 Domestic production activities deduction. Attach Form 8903 35

36 Add lines 23 through 35 36

37 Subtract line 36 from line 22. This is your adjusted gross income ▶ 37

Multiply by \$4000 for AK personal exemption

Adjusted Gross Income line 37

“I feel we are running out of time... savings are draining out at \$10 million a day... In an ideal world it would be good to go slowly, carefully, but there is not enough time left for that.”

-Gunnar Knapp

House Finance Presentation

January 25, 2017