

# Fiscal Note

State of Alaska  
2021 Legislative Session

Bill Version:	CSHB 37(W&M)
Fiscal Note Number:	3
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Identifier: HB037-DOR-TAX-5-11-21  
Title: INCOME TAX; PERMANENT FUND; EARNINGS RES.  
Sponsor: WOOL  
Requester: (H) Ways & Means

Department: Department of Revenue  
Appropriation: Taxation and Treasury  
Allocation: Tax Division  
OMB Component Number: 2476

## Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below.

(Thousands of Dollars)

	FY2022 Appropriation Requested	Included in Governor's FY2022 Request	Out-Year Cost Estimates				
OPERATING EXPENDITURES	FY 2022	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
Personal Services	6,371.7		6,371.7	6,371.7	6,371.7	6,371.7	6,371.7
Travel	25.0		12.5				
Services	264.1		1,764.1	2,514.1	1,914.1	1,914.1	1,914.1
Commodities	215.9		6.9	6.9	6.9	6.9	6.9
Capital Outlay							
Grants & Benefits							
Miscellaneous							
<b>Total Operating</b>	<b>6,876.7</b>	<b>0.0</b>	<b>8,155.2</b>	<b>8,892.7</b>	<b>8,292.7</b>	<b>8,292.7</b>	<b>8,292.7</b>

## Fund Source (Operating Only)

1004 Gen Fund (UGF)	6,876.7		8,155.2	8,892.7	8,292.7	8,292.7	8,292.7
<b>Total</b>	<b>6,876.7</b>	<b>0.0</b>	<b>8,155.2</b>	<b>8,892.7</b>	<b>8,292.7</b>	<b>8,292.7</b>	<b>8,292.7</b>

## Positions

Full-time	69.0		69.0	69.0	69.0	69.0	69.0
Part-time							
Temporary							

## Change in Revenues

1004 Gen Fund (UGF)	290,000.0		580,000.0	580,000.0	580,000.0	580,000.0	580,000.0
<b>Total</b>	<b>290,000.0</b>	<b>0.0</b>	<b>580,000.0</b>	<b>580,000.0</b>	<b>580,000.0</b>	<b>580,000.0</b>	<b>580,000.0</b>

**Estimated SUPPLEMENTAL (FY2021) cost:** 0.0 (separate supplemental appropriation required)

**Estimated CAPITAL (FY2022) cost:** 8,500.0 (separate capital appropriation required)

**Does the bill create or modify a new fund or account?** No  
(Supplemental/Capital/New Fund - discuss reasons and fund source(s) in analysis section)

## ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? Yes  
If yes, by what date are the regulations to be adopted, amended or repealed? 12/31/21

## Why this fiscal note differs from previous version/comments:

Corrected to add positions inadvertently omitted from prior version.

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Agency: Department of Revenue

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## FISCAL NOTE ANALYSIS

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## Analysis

**Bill Analysis**

This bill creates a new broad-based income tax that would apply to resident and nonresident individuals, trusts, and estates, including partners or shareholders of partnerships or S-Corporations, who derive income from, or where income is connected with, a source in Alaska. The Department of Revenue, Tax Division (Department) estimates that there will be approximately 468,000 resident taxpayers and approximately 70,000 non-resident taxpayers. These estimates are rough. The tax rate would be 2.5% of the taxpayer's federal adjusted gross income (AGI).

Taxes paid to other states, based on income derived in those states, can be credited from this tax. The bill would exclude from the definition of Alaska taxable income a Permanent Fund Dividend (PFD) received by the taxpayer. The bill would also allow an individual eligible for a PFD to direct the Department to hold all or a part of the amount of the PFD to pay the tax due under this bill. This tax will be effective January 1, 2022.

Lastly, the bill would allow for another exception to the requirement that taxpayers file reports and returns electronically, which will cause an additional administrative burden on the Department.

**Revenue Impact**

At full implementation, revenue will be about \$580 million annually. Assuming that AGI is earned evenly across the fiscal year, revenue in FY2022 would be approximately \$290 million, earned in the second half of the fiscal year. Depending on the timing of tax implementation and estimated payments, it is possible that some of the revenue projected for FY2022 could be shifted into FY2023. As the impact is proportionate to each household's income, actual impact by household will vary widely. Any impact will be partially mitigated, as state individual income taxes are deductible from federal taxes. Thus, Alaskans who itemize their federal taxes would reduce their federal tax liability by the amount of their state tax multiplied by their marginal federal tax rate.

The Department's income tax revenue model is based on aggregated federal income data for Alaska residents. It is assumed that income from nonresidents will increase Alaska AGI by approximately 5%. This 5% adjustment is an estimate of the net nonresident earnings (nonresident income in Alaska less Alaska resident income taxed elsewhere) developed through consultation with the Alaska Department of Labor and influenced by Bureau of Economic Analysis "adjustment for residence" historical values. The model does not address long term population growth, inflation, or impacts on the economy from implementing an income tax.

In producing this revenue estimate, the existing income tax revenue model was adjusted to incorporate estimated impacts of the personal exemptions and Permanent Fund Dividend exemptions in this bill.

**Implementation Cost**

The cost and time required to implement a new broad-based tax is directly related to its complexity. For a more robust tax such as the one envisioned in this bill an 8-month implementation process should be expected. The Department is currently using Version 9 of its Tax Revenue Management System (TRMS). The Department expects to engage FAST Enterprises, the TRMS contractor, to build an income tax module into TRMS. The \$8,500.0 capital project reflects an estimated initial implementation cost for FAST to add the income tax module and a Fast Identity Verification Services (FIVS) module. This estimate assumes that the Department will receive capital funding for a TRMS Update (version 12) in the FY2022 budget. If that does not occur, this estimate will need to be increased by \$5 million.

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After initial implementation, continued maintenance and support by FAST is estimated to be \$2.2 million in calendar year (CY) CY2023 and \$1 million in CY2024 and beyond for the individual income tax module, and \$500,000 per year for the FIVS module.

Adding a fully functional income tax module is a multi-year process. The initial fast-track need will be to build and implement a tax withholding system, which will need to be in operation by January 1, 2022. The Department will also need to adopt regulations by January 1, 2022. Since the bill allows taxpayers to elect to apply their PFD to their tax liability, the Department will work with FAST to interface the TRMS system with the PFD Division's PFD management system in an effort to automate the PFD offset provisions of this bill. In addition to the software development, this bill will require a rapid and robust outreach to the business community throughout Alaska, and this fiscal note includes funding for travel needs. Additionally, this bill will require integration with national accounting and tax software vendors in order to update programs such as TurboTax and QuickBooks to incorporate Alaska.

Once the withholding system and PFD interfaces are in place, FAST and Tax Division staff will begin building the tax return filing and examination modules, with their associated databases, communications, and integration with our existing imaging, accounting, and collections systems. The legislation creates an annual tax, meaning that the first tax returns will be filed in January 2023, with a filing due date of April 15, 2023. Taxpayers who request and receive extensions would have filing deadlines in October 2023. The Department estimates that this bill will generate approximately 405,500 returns. This estimate is based on the number of Alaska resident individual returns and partnership/S-Corporation returns filed in 2018 as publicly reported by the Internal Revenue Service, multiplied by 15% to adjust for estimated nonresident returns.

As part of the Department's research into the potential costs to administer this tax, we spoke with tax administrators in the States of Montana and Vermont. Each have population sizes close to Alaska's and impose individual income taxes. Montana and Vermont employ approximately 102 and 60 people, respectively, to administer each state's individual income taxes. Using a simple per-capita adjustment, these numbers translate to 68 and 70 employees needed to administer an individual income tax in Alaska. Given the complexities that come with administering nonresident and pass-through corporation returns, and the sheer volume of estimated new taxpayers and returns, the Department expects to need 69 people to administer an individual income tax in Alaska. The new staff would be roughly split between the Juneau and Anchorage offices. The Department will continue to look for ways to automate administration of this tax and look for efficiencies.

We expect to replicate the online filing percentages of the PFD Division, currently at 85%. However, the 15% of paper filers will require manual handling and data entry for approximately 60,825 paper returns out of the 405,500 total estimated returns. In contrast, the Department currently processes approximately 2,700 paper returns out of 38,000 total returns across all tax programs the Department administers each year.

Additional travel is largely for public education efforts, as well as the need to train new staff on the tax management system. The cost for services reflects primarily internal core service rates paid to other state agencies, due to additional staff within the Tax Division, as well as ongoing maintenance and support costs for FAST. Commodities reflect the initial outfit for new employees for office and computer furnishings.

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**Analysis**

An initial analysis of the staff needs within the Tax Division to implement an individual income tax is as follows:

- (1) Deputy Director
- (2) Audit Supervisors
- (2) Income Tax Specialists
- (18) Auditors
- (5) Accounting Technicians
- (3) IT Analysts/Programmers
- (5) Appeals Officers
- (15) Tax Technicians
- (16) Imaging & Office Assistants
- (2) Administrative Assistants