

STATE OF ALASKA

DEPARTMENT OF REVENUE

Tax Division

Sean Parnell, Governor

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March 16, 2010

The Honorable Paul Seaton, Chair
House Education Committee
House of Representatives
Capitol Building Room 102
Juneau, Alaska 99811

Re: HB 367

Dear Chairman Seaton and Committee Members:

During the last meeting of the House Education Committee, we were asked to provide the following information regarding the Alaska Education Credit:

1. The tax effect of a contribution for which an Income Tax Education Credit may be claimed, under two scenarios:
 - a. Charitable contribution is claimed
 - b. Income Tax Education Credit is claimed
2. Two scenarios demonstrating the difference in ordering credits.
3. Alaska Education Tax Credits claimed in the Fiscal Years 2007--2009
4. Any technical suggestions

Please find attached several worksheets that answer the questions posed. On Attachment 1, we have provided a comparison of claiming a charitable contribution to claiming a credit for a contribution to university.

Attachments 2 and 3 are provided to show the difference resulting from alternatives in credit ordering. Attachment 2 assumes that the Income Tax Education Credit is prioritized over the

Film Production Tax Credit. Attachment 3 assumes that the Film Production Tax Credit is prioritized over the Income Tax Education Credit.

Ordering of credits is clearly a policy decision. From a technical standpoint, it is important that the policy be made clear. Alaska statute currently requires that the Gas Exploration & Development Credit (AS 43.20.043) be applied against the corporate income tax first, before all other credits. However, Alaska statute is silent on how other credits are applied. On Attachment 6, we have provided some alternative language for lawmakers to consider.


Our second suggestion concerns the application of the Education Credit. Current law restricts the credit to \$150,000 per "taxpayer." In the area of income tax, it is unclear whether this refers to an individual corporation, or to the group of corporations where there is an affiliated group. AS 43.20.340(10) defines "taxpayer" as "a person [corporation] subject to a tax imposed by this chapter." Where there is an affiliated group of taxpayers, they may file one consolidated tax return. For example, if a multi-state oil company is doing business in Alaska, it commonly has separate corporations for its E&P operations, its marketing operations, and its transportation operations. Such a company commonly files a single consolidated Alaska tax return. It is unclear whether there is one \$150,000 credit allowed for a consolidated tax return, or multiple \$150,000 credits allowed for each member represented in the consolidated return. Hearing minutes from the year the credit was initially enacted indicate that the credit limit was intended to apply per corporate group and not to individual taxpayers within the group. It would be helpful to have this clarified in statute. Attachment 6 also presents some language to clarify this.

Attachment 4 shows the Education Credits claimed for the last three fiscal years. Please note that these statistics are provided based on tax returns filed during each fiscal year. Thus, the FY09 statistics include most of the income tax returns filed for the calendar year 2007 and any fiscal year tax returns filed during FY09.

Attachment 5 shows the contributions upon which the Education Credits were claimed for each respective fiscal year. Please note that these statistics are based on the tax returns, as filed, and do not include any similar contributions for which a taxpayer may have claimed a charitable contribution, rather than claiming a credit.

Thank you for the opportunity to provide this information.

Sincerely,

A handwritten signature in black ink, appearing to read "Johanna Bales".

Johanna Bales
Deputy Director, Tax Division

Purpose: To compare the tax benefit of an income tax "deduction" to the benefit of a "credit" for contribution of \$50,000,000 to a university

A deduction is an expense taken to reduce total taxable income.

A credit reduces income tax directly.

| | | deduction | credit |
|--|-------|--------------------------|-----------------------------|
| Gross income | A | 300,000,000 | 300,000,000 |
| Expenses: | | | |
| Other expenses | | 10,000,000 | 10,000,000 |
| Deduction for contribution to university | B | <u>50,000,000</u> | <u> </u> |
| Total expenses | C | 60,000,000 | 10,000,000 |
| Taxable income | A - C | <u>240,000,000</u> | <u>290,000,000</u> |
| Tax rate | | <u>* 9.4%</u> | <u>* 9.4%</u> |
| Tax | | 22,560,000 | 27,260,000 |
| Credit | | <u>0</u> | <u>B * 50% (25,000,000)</u> |
| Tax after credit | | <u><u>22,560,000</u></u> | <u><u>2,260,000</u></u> |

This analysis examines the benefit of the next marginal contribution after \$200,000.

Assumptions:

- charitable contribution is not limited by taxable income limit.
- highest marginal tax rate
- company does all of its business in Alaska

Purpose: to compare ordering of credits

Priority: Income Tax Education Credit

Assumptions:

company does business only in Alaska

| | | available credits | tax application limit | carryover |
|--|--------------|----------------------|--------------------------|------------------|
| Income Tax Education Credit | AS 43.20.014 | 1,000,000 | no limit | no carryover |
| Gas Exploration & Development Tax Credit | AS 43.20.043 | 1,000,000 | 50% tax | 5 year carryover |
| Film Production Tax Credit | AS 43.98.030 | 1,000,000 | no limit | 3 year carryover |
| Total potential credits | | <u>3,000,000</u> | | |

**** AS 43.20.043(c) requires application first of Gas Exploration & Development Tax Credit**

Scenario 1: apply Income Tax Education Credit next

| | | |
|--|----------------------|------------------|
| Tax before credits | (assumed) | 1,200,000 |
| Gas Exploration & Development Tax Credit | (limited to 50% tax) | (600,000) |
| Income Tax Education Credit | | <u>(600,000)</u> |
| Tax after credits: | | <u>0</u> |

Credits utilized

| | |
|--|------------------|
| Gas Exploration & Development Tax Credit | 600,000 |
| Income Tax Education Credit | 600,000 |
| Total credit utilized | <u>1,200,000</u> |

Credits lost

| | |
|-----------------------------|----------------|
| Income Tax Education Credit | 400,000 |
| Total credits lost | <u>400,000</u> |

Credits available for future utilization

| | |
|--|------------------|
| Gas Exploration & Development Tax Credit | 400,000 |
| Film Production Tax Credit | <u>1,000,000</u> |
| Total credits available for future utilization | <u>1,400,000</u> |

Purpose: to compare ordering of credits

Priority: Film Production Tax Credit

Assumptions:

company does business only in Alaska

| | | available | tax application | carryover |
|--|--------------|------------------|-----------------|------------------|
| | | credits | limit | |
| Income Tax Education Credit | AS 43.20.014 | 1,000,000 | no limit | no carryover |
| Gas Exploration & Development Tax Credit | AS 43.20.043 | 1,000,000 | 50% tax | 5 year carryover |
| Film Production Tax Credit | AS 43.98.030 | 1,000,000 | no limit | 3 year carryover |
| Total potential credits | | <u>3,000,000</u> | | |

**** AS 43.20.043(c) requires application first of Gas Exploration & Development Tax Credit**

Scenario 2: apply Film Production Tax Credit next

| | | |
|--|----------------------|-----------|
| Tax before credits | (assumption) | 1,200,000 |
| Gas Exploration & Development Tax Credit | (limited to 50% tax) | (600,000) |
| Film Production Tax Credit | | (600,000) |
| Tax after credits: | | <u>0</u> |

Credits utilized/monetized

| | |
|--|------------------|
| Gas Exploration & Development Tax Credit | 600,000 |
| Film Production Tax Credit | 600,000 |
| Total credit utilized | <u>1,200,000</u> |

Credits lost

| | |
|-----------------------------|------------------|
| Income Tax Education Credit | 1,000,000 |
| Total credits lost | <u>1,000,000</u> |

Credits available for future utilization

| | |
|--|----------------|
| Gas Exploration & Development Tax Credit | 400,000 |
| Film Production Tax Credit | 400,000 |
| Total credits available for future utilization | <u>800,000</u> |

Alaska Education Tax Credit
Credits Claimed
FY 07--09

| <u>Tax Type</u> | FY 09 | FY 08 | FY 07 |
|------------------------------------|------------------|------------------|------------------|
| Corporate Income Tax | 1,064,019 | 1,314,499 | 1,196,972 |
| Insurance Premiums Tax | 450,000 | 425,000 | 300,000 |
| Fishery Resource Landing Tax | 150,000 | 1,050,000 | 1,200,000 |
| Mining License Tax | 0 | 10,814 | 250,626 |
| Fisheries Business Tax | 450,000 | 450,000 | 300,000 |
| Total Education Tax Credit claimed | <u>2,114,019</u> | <u>3,250,313</u> | <u>3,247,598</u> |

Contributions generating Alaska Education Tax Credit

FY 07--09

| | FY 09 | FY 08 | FY 07 |
|--|------------------|------------------|------------------|
| <u>Tax Types</u> | | | |
| Corporate Income Tax | 1,624,326 | 5,197,425 | 5,047,485 |
| Insurance Premiums Tax | 600,000 | 575,000 | 400,000 |
| Fishery Resource Landing Tax | 200,000 | 1,400,000 | 1,600,000 |
| Mining License Tax | 0 | 21,628 | 391,802 |
| Fisheries Business Tax | 600,000 | 200,000 | 200,000 |
| Total contributions for Education Tax Credit | <u>3,024,326</u> | <u>7,394,053</u> | <u>7,639,287</u> |

** Note: These amounts do not include contributions that would have enjoyed the Education Tax Credit, but for which taxpayer did not claim a credit, but claimed a deduction instead.

Letter to House Education Committee
March 16, 2010
Attachment 6

Suggested edits for HB 367

If intent is to prioritize Education Credit before other credits:

A new paragraph:

AS 43.20.014(e)(2) “tax due under this chapter” means the tax liability after application of the credit under AS 43.20.043 and before application of any other credits allowable under this chapter.

To clarify taxpayer credit limit:

Amend AS 43.20.014(d)(3)

(3) when combined with credits taken during the taxpayer’s tax year under AS 21.89.070, 21.89.075, AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, exceed \$150,000. **If the taxpayer is a member of an affiliated group, then the credit may not exceed \$150,000 for the affiliated group.**

Add a new paragraph:

AS 43.20.014(e)(3) “affiliated group” means a group of two or more corporations in which 50 percent or more of the voting stock of each member of the group is directly or indirectly owned by one or more corporate or noncorporate common owners, or by one or more of the members of the group.

Similar language to be added in AS 21.89.070, 21.89.075, AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045