

FISCAL NOTE

STATE OF ALASKA
2004 LEGISLATIVE SESSION

Fiscal Note Number: 1
 Bill Version: CSSB 366(FIN)
 (S) Publish Date: 5/7/04

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue
 Title State Sales Tax RDU Revenue Programs & Services
 Component Tax Division
 Sponsor Senate Finance Committee
 Requester Senate Finance Committee Component No. 2476

Expenditures/Revenues (Thousands of Dollars)

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

OPERATING EXPENDITURES	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	*	*	*	*	*	*
CAPITAL EXPENDITURES	*					
CHANGE IN REVENUES ()	*	*	*	*	*	*

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	*	*	*	*	*	*

Estimate of any current year (FY2004) cost: 0.0

Check this box (X) if funding for this bill is included in the Governor's FY 2005 budget proposal:

POSITIONS

Full-time	*	*	*	*	*	*
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

* See page 2 and 3

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 Division Tax Division Date/Time 5/7/04 4:33 PM
 Approved by: Steve Porter, Deputy Commissioner Date 5/7/2004
 Agency Department of Revenue

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ANALYSIS CONTINUATION

Cost Discussion

We estimate that there will be approximately 50,000 taxpayers under the bill generating just under 500,000 returns each year. We estimate ongoing operational costs of \$5.9 million per fiscal year. The projected staffing is 79 full time employees. We have not developed cost estimates for specific fiscal years that reflect program start-up and maturity. Based on this estimate, and our analysis of other broad based tax proposals, we expect that operational costs for FY05 will be between \$2.0 and \$3.0 million after which operating costs are expected to peak during the second year of the program then decline and stabilize at the \$5.9 million estimate as the program matures. Capital investment in information systems and specialized equipment are estimated at \$7.5 million.

These operational and capital cost estimates assume that the \$60 tax cap under the bill is a \$60 cap on the state tax and an independent \$60 cap on each municipal tax that may apply to a transaction. This is how we interpret the bill as written. If however, the cap is intended to be a limit of \$60 on state and municipal taxes combined, then detailed reporting of individual transactions would be necessary to determine the portion of the \$60 attributable to the state and municipal taxes. The cost of transactional reporting are significant for taxpayers and the department. If the bill is modified to impose a cap on the combined state and municipal tax, we recommend that the revenue distribution and tax sharing provisions of the bill be modified to provide for revenue sharing based on the ratio of state to municipal tax rates in order to avoid these costs and complexities.

Revenue Discussion

Estimating the revenue from a proposed sales tax is fraught with potential pitfalls. These include the difficulty of obtaining current and applicable data and identifying the potential effects on consumers and businesses. Besides these estimation difficulties, the maximum allowable tax per single sale and municipal share provisions in this bill make it even more difficult to develop a plausible estimate.

Sales

The U.S. Economic Census estimates that the total value of all sales, receipts or revenue for Alaska establishments in 1997 was over \$35 billion. However, HB 366 exempts certain goods and services, including the following:

- (1) the sale of property for resale
- (2) financial services
- (3) prescription drugs
- (4) health care services
- (5) the sale, lease or rental of real property
- (6) sale of natural gas or diesel fuel for home heating
- (7) water, sewer, electricity steam or refuse and garbage collection
- (8) transportation of passengers and tangible personal property
- (9) property and services used for the exploration, extraction and production of natural resources.
- (10) the sale, transfer or use of motor fuel taxed under AS 43.40.010;
- (11) sales, leases, or rentals made in a municipality or unincorporated community with a population of less than 500.

We tried as much as possible to match goods and service classified as exempt in the Bill to census definitions so that we could exclude them from the estimated tax base. We then updated the tax base by sector using personal income statistics. The result is a tax base of about \$12.5 billion. If we ignore for the time being the municipal share, allowable maximum tax and exemption for sales made in small communities provisions in the Bill, then the total estimated revenue at three percent would be about \$375 million. Additionally, at no point in this analysis do we estimate how any of the provisions in this bill will change behavior.

The Cap

We are not aware of any direct method to estimate the reduction in revenue as a result of the exclusion of single sales, leases or rentals that exceed the tax cap of \$60. There is no statewide estimate of the volume of sales or the amount of each sale that would exceed the cap. A community that defines its maximum tax per sale in a similar fashion to HB 366 is the Kenai Peninsula Borough. The Kenai Peninsula Borough allows the tax to be applied "only to the first \$500 of each separate sale, rent or service transaction with some exceptions."

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These exceptions include a provision that defines room rentals on a per room per night basis. This is to prevent a person from bundling rooms together over time and using the bundled transaction as a single sale. There is no such provision in this Bill.

The Kenai Peninsula Borough used a random sampling of their 1999 returns to do an analysis of their tax cap. The result of their analysis shows that the cap lowers the Kenai Peninsula Borough's taxable sales by approximately 35 percent. Although this percentage seems very high when applied to the state there would be a large incentive to bundle goods and services and to invoice as infrequently as possible. This will be particularly true of services which account for almost 50 percent of the total estimated revenue from this tax. Unlike the Kenai Peninsula Borough, this bill also does not have any restrictions such as the "per room per night" restriction in the Borough ordinance. In 1999, this ordinance also specified that a single sale of a service could not be invoiced over more than 30 days. This provision was recently repealed. Using the Kenai Peninsula Borough's experience the cap could reduce the statewide sales tax base to \$8.1 billion. Our very rough revenue estimate at the three percent tax rate would then be about \$243 million.

Communities with less than 500 individuals

We estimate that approximately three percent of the population lives in cities with less than 500 people. Although these individuals may have completely different spending habits than other individuals in the state, as a very rough estimate we could reduce the tax base by three percent. The tax base would then be about \$7.9 billion and our very rough estimate at the three percent tax rate would be \$235 million.

The Municipal Share

It is not possible to estimate how many municipalities (cities and boroughs) would choose to impose sales taxes or change their rates as a result of HB 366. However, we do know that approximately 70 municipalities in Alaska already have sales tax rates equal to or higher than three percent. If we use population as a proxy for sales and adjust for cities that currently have population less than 500 and levy sales taxes, then at a minimum, 19 percent of one percent of the tax base would go to cities, or about \$15 million using the above rough estimate. The maximum municipal share, if all communities with populations greater than 500 adopted a three percent or higher tax rate, would be about \$79 million using the above estimate. The rough estimate of revenue to the state would then be somewhere between \$156 to \$220 million at the 3 percent rate.

Intersection of Tax Cap and Municipal Share

The Bill says that if a borough levies a "general" sales tax then a "borough must conform exactly to the statewide sales and use tax." In addition, "a city may levy sales and use taxes in the manner provided for boroughs." We interpret this to be that the \$60 tax cap would apply separately at the borough, city and statewide level. That is, the total effective tax cap for sales made in a city with a sales tax within a Borough with a sales tax, would be \$180. If, however, the total tax cap on the sale is \$60 and it is shared back to municipalities and boroughs with sales taxes then the revenue estimate would be lower.

Other Assumptions or Exclusions

We did not include any adjustments for consumers or businesses lowering their tax burden by changing their behavior. Also, we did not include estimates for use taxes collected from buyers and out-of-state sellers. Additionally, we did not exclude the sales of services by or to the state or a political subdivision of the state.