

**ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON WAYS AND MEANS**

May 11, 2003

5:09 p.m.

MEMBERS PRESENT

Representative Mike Hawker, Co-Chair
Representative Jim Whitaker, Co-Chair
Representative Cheryll Heinze
Representative Vic Kohring
Representative Norman Rokeberg
Representative Bruce Weyhrauch
Representative Peggy Wilson
Representative Max Gruenberg
Representative Carl Moses

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Representative Dan Ogg
Representative Les Gara
Representative Sharon Cissna
Representative Paul Seaton
Representative Ralph Samuels
Representative John Harris

COMMITTEE CALENDAR

HOUSE BILL NO. 293

"An Act levying and collecting a state sales and use tax; and providing for an effective date."

- HEARD AND HELD

PREVIOUS ACTION

BILL: HB 293

SHORT TITLE: STATE SALES AND USE TAX

SPONSOR(S): WAYS & MEANS

Jrn-Date	Jrn-Page		Action
04/30/03	1202	(H)	READ THE FIRST TIME -

			REFERRALS
04/30/03	1202	(H)	W&M, FIN
05/01/03		(H)	W&M AT 7:00 AM HOUSE FINANCE 519
05/01/03		(H)	Heard & Held -- Teleconference -- MINUTE(W&M)
05/06/03		(H)	W&M AT 7:00 AM HOUSE FINANCE 519
05/06/03		(H)	Heard & Held MINUTE(W&M)
05/07/03		(H)	W&M AT 7:00 AM HOUSE FINANCE 519
05/07/03		(H)	Heard & Held -- Recessed to a call of the chair -- MINUTE(W&M)
05/08/03		(H)	W&M AT 7:00 AM HOUSE FINANCE 519
05/08/03		(H)	Heard & Held -- Recessed to a call of the Chair -- MINUTE(W&M)
05/09/03		(H)	W&M AT 7:00 AM HOUSE FINANCE 519
05/09/03		(H)	Heard & Held MINUTE(W&M)
05/10/03		(H)	W&M AT 8:30 AM HOUSE FINANCE 519
05/10/03		(H)	Heard & Held MINUTE(W&M)
05/11/03		(H)	W&M AT 5:00 PM HOUSE FINANCE 519

WITNESS REGISTER

LARRY PERSILY, Deputy Commissioner
Office of the Commissioner
Department of Revenue
Juneau, Alaska

POSITION STATEMENT: Answered questions about the proposed
committee substitute (CS) for HB 293, Version Q.

ACTION NARRATIVE

TAPE 03-29, SIDE A

Number 0001

CO-CHAIR JIM WHITAKER called the House Special Committee on Ways and Means meeting to order at 5:09 p.m. Representatives Hawker, Whitaker, Heinze, Kohring, Weyhrauch, Wilson, Gruenberg, and Moses were present at the call to order. Representative Rokeberg arrived as the meeting was in progress. Representatives Ogg, Gara, Cissna, Seaton, Samuels, and Harris also attended.

HB 293-STATE SALES AND USE TAX

CO-CHAIR WHITAKER announced that the only order of business would be HOUSE BILL NO. 293, "An Act levying and collecting a state sales and use tax; and providing for an effective date."

REPRESENTATIVE HEINZE turned to the Streamlined Sales Tax project and asked if it was in place today, would the state receive taxes on interstate commerce.

Number 0144

LARRY PERSILY, Deputy Commissioner, Office of the Commissioner, Department of Revenue, said that if there was a state sales tax and a business such as Barnes and Noble, which has a store in Anchorage, there would be a nexus in the state. Therefore, if someone in Alaska were to order from Barnes and Noble via the Internet, he believes there would be a nexus and the state could collect sales tax on those businesses with a connection in Alaska. He related his belief that the aforementioned would open the door for additional sales tax collection by the state as well as municipalities.

Number 0311

CO-CHAIR HAWKER moved to adopt the proposed committee substitute (CS) for HB 293, Version 23-LS1064\Q, Kurtz, 5/11/03, as the working document. There being no objections, Version Q was before the committee.

MR. PERSILY explained that Version Q is a flat 3 percent sales tax as specified on page 8, line 29.

CO-CHAIR HAWKER recalled that the intent was to remove all vestiges of seasonality.

MR. PERSILY agreed and noted that there are no seasonal changes encompassed in Version Q. He directed attention to page 3,

lines 11-16, and pointed out that under Version Q the phase-in would end December 31, 2009. Therefore, for the first four years, municipalities will receive all of their sales tax collections within the 8 percent cap, even if the state comes up short. After December 31, 2007, the municipal levy may not exceed 6 percent and after December 31, 2009, the municipal levy may not exceed 5 percent, and thus 3 percent would be left for the state.

Number 0712

REPRESENTATIVE WEYHRAUCH asked if the city sales tax would remain at status quo until completion of the phase-in.

MR. PERSILY confirmed Representative Weyhrauch's understanding and pointed out that on page 3, lines 11-16, the phase-in of the rate occurs, another section addresses the phase-in of the enforcement and collection powers.

CO-CHAIR HAWKER highlighted that there are three components of the phase-in, one of which is the phase-in of overall administration and point of collection. The second portion is the phase-in of the rate integration and the third point is the conformance of the tax base for which a separate phase-in is proposed.

Number 0833

REPRESENTATIVE GRUENBERG surmised that in Anchorage, those municipalities that [do have high local taxes] would lose some revenue.

MR. PERSILY agreed that would eventually be the case. For instance, a city with a 6 percent sales tax could collect 6 percent until December 31, 2009, at which point the city would have to [lower its tax] to 5 percent. He related his understanding that the intent of the legislation, through the phase-in is that such municipalities would have seven to eight years to deal with the fact that the local tax rate would drop.

MR. PERSILY pointed out that the part of the phase-in dealing with rates is located on page 3; the portion of the phase-in dealing with administration and collection is located on the bottom of page 25. Mr. Persily explained that the phase-in beginning at the bottom of page 25 means that basically the municipalities can collect their own money under their own rules

for two years. For the next two years, the municipalities continue to collect the money, but they do so under the state rules. After four years, the state would take over collection under its rules.

Number 1125

REPRESENTATIVE GRUENBERG directed attention to Section 2(b) which begins on page 25, line 31 through page 26, line 2. The language used in this subsection refers to a general sales and use tax. However, he posed a situation in which the municipality doesn't technically meet that requirement such as a bed tax. He inquired as to the rules for that municipality.

MR. PERSILY clarified that this doesn't apply to special municipal taxes such as the fuel transfer tax, the bed tax, the car rental tax, the liquor tax, and the raw fish transfer tax. The aforementioned taxes are outside the 8 percent cap and don't come under state control at any point. In further response to Representative Gruenberg, Mr. Persily said his understanding is that the aforementioned is clear as it is currently drafted.

REPRESENTATIVE GRUENBERG expressed the need for every municipality to be able to understand this so that there is no question.

CO-CHAIR HAWKER pointed out that on page 4, lines 5-8, the language specifies that "a municipality may levy specific excise taxes on single categories of tangible personal property or services, such as bed taxes and fish taxes.

Number 1349

MR. PERSILY, in response to Representative Gruenberg, responded that the term excise tax is broad enough to cover all of the taxes specified earlier because the language is clear that the tax proposed only applies to a general sales and use [tax] of which taxes such as the bed tax are not. Mr. Persily turned to Representative Heinze's earlier question regarding how much money the state will receive, and suggested that the committee keep in mind that this legislation still includes the 12 cents per gallon increase in motor fuel taxes, which amounts to about \$41 million in a full fiscal year. He pointed out that Version Q includes a significant exemption for medical services and prescription drugs. However, Version Q is fairly tight with regard to the manufacturing and transportation exemptions.

Therefore, the sales tax component alone would probably generate \$300-\$375 million, depending on what is ultimately decided with manufacturing.

REPRESENTATIVE HEINZE clarified that her question was in regard to the phase-in period when the state wouldn't receive its full 3 percent.

MR. PERSILY said that he would estimate that it would be less than 10 percent of the state's collection [that would be lost]. He said that needed to be run now that the legislation is using a year round tax that doesn't fluctuate.

Number 1645

MR. PERSILY, upon the request of Co-Chair Whitaker, explained the phase-in again. With regard to the rate, the municipalities keep 100 percent of their rate for the first four years and whatever is left [beyond the municipal tax up to the 8 percent cap] is sent to the state. Therefore, if there isn't anything left or [less than 3 percent is left] under the 8 percent cap, the state would come up short. On December 31, 2007, municipalities can only take 6 percent, and two years later that would be reduced to 5 percent of the 8 percent cap and thus the state would begin to collect its full 3 percent in all municipalities. At that point the phase-in would be complete and some municipalities will have to reduce their rate to 5 percent. He then turned to pages 25-26, which refers to the phase-in of control over collections, auditing, and enforcement. Under this provision, municipalities would collect all their own money under their own rules for two years. During the next two years, the municipalities would continue to collect sales tax under the state's rules.

MR. PERSILY, in response to Co-Chair Whitaker, explained that during the first two years the state would set up a sales tax office within the Tax Division to collect state sales tax statewide. However, all the communities with a sales tax would continue to use their own rules and personnel during the first two years.

Number 1852

CO-CHAIR WHITAKER surmised then that the municipalities or their lobbying group could come to the legislature and identify

specific problems and concerns. There would be two years in which to consider a downside and remedy it.

MR. PERSILY said that the truth is that there are municipalities in the state that have collected sales tax for decades and know how to do it. Therefore, it's very likely that during the two-year transition, the department will learn a lot from the municipalities as the phase-in to state rules occurs.

CO-CHAIR HAWKER emphasized that there doesn't have to be a change for any municipality in any way during the first two years. For the subsequent two years, while working on a consistent base, there is the opportunity to create convergence on administrative matters. Co-Chair Hawker said that it's presumed that there will be a working process between communities and the state during the entire process.

MR. PERSILY pointed out that during that two-year period there may be issues that the Department of Revenue can address by regulation and there may be some that require changes to statutory references, which would mean coming back to the legislature. Hopefully, this wouldn't become an annual event.

Number 2141

REPRESENTATIVE OGG related his understanding that this system will take effect July 1, 2003, and the sales tax would be implemented January 1, 2004. Between those two dates, he surmised that the state would establish a mechanism for collecting the 3 percent tax, separate from the municipal [revenue]. He also surmised that businesses will receive a form from the state and those businesses in the cities with municipal taxes will continue to [fill out the municipal forms]. Representative Ogg indicated the need to include a statement specifying that the state may utilize the municipality as a contractor at the end of 2007 because that may be more efficient.

MR. PERSILY said that such language isn't included, although the matter has been discussed. Mr. Persily noted the [department's] interest in having that as an option.

CO-CHAIR HAWKER asked if [contracting with the municipality at the end of 2007] would be a matter subject to regulation rather than statute.

MR. PERSILY answered that he doesn't believe statutory authority is necessary to do that. Clearly, the direction has been to explore that possibility and, during the phase-in, work with the communities to make the taxes efficient, fair, and easy on the communities and the businesses in those communities. Perhaps the best way to include this notion in legislation would be through a statement of intent.

Number 2431

REPRESENTATIVE OGG said that municipalities and boroughs in his area wanted this as an option that the state may pursue, which is why he suggested the permissive language specifying that "the state may utilize the municipalities as their contracting agent." Therefore, the state wouldn't be forced to contract with the municipality, although it encourages municipalities to approach the state. If it was left to regulation, the legislature's policy wouldn't be there for regulation.

MR. PERSILY emphasized that whatever is done to [encourage] contracting with the municipality would ensure that it doesn't violate the Streamlined Sales Tax Agreement, which is the ultimate goal of this. In response to Co-Chair Whitaker, Mr. Persily confirmed that nothing in the current language prohibits the regulations being developed such that the state could [contract with a municipality].

CO-CHAIR WHITAKER announced that he would be happy to insert intent language in the CS in order to assure the above continues to be a point of discussion.

Number 2644

REPRESENTATIVE OGG said that would be fine. Representative Ogg posed a situation in which a municipality wanted to have a higher sales tax in order to build a hockey rink, for instance. As this process occurred the tax was reduced to 5 percent and the municipality determined the goal [of building a hockey rink] couldn't be accomplished without an additional 1 percent sales tax. Therefore, the question becomes whether a municipality should be prohibited from increasing its portion of the tax so long as there was an election/referendum that authorized the increase above the tax cap.

CO-CHAIR WHITAKER announced that amendments would be addressed tomorrow.

REPRESENTATIVE OGG remarked that [the CS] will move [municipalities] toward meshing [the local and state taxes].

Number 2814

REPRESENTATIVE WILSON inquired as to how many employees will be required to set up and run this state tax system.

MR. PERSILY estimated that when the state's sales tax office is at full staff, there would be about 70 people working on the sales tax. The cost of collection would be about 1.5 percent; 2 percent is viewed as the national benchmark.

REPRESENTATIVE OGG, in response to Representative Heinze, explained that his thought was that when the state tax is in place the municipal tax would be capped at 5 percent. Therefore, if a municipality chose to increase its percentage of sales tax in order to do a project, that municipality's share could be increased through a referendum. He clarified that the aforementioned municipal increase wouldn't carve into the state's share but would be in addition to the [8 percent].

Number 3035

REPRESENTATIVE GRUENBERG turned to the effective dates, which he characterized as complex, specifically in relation to Section 21 on page 26. The current language of Version Q could result in the motor vehicle rental tax provision having its own effective date because technically it isn't covered by any of the other effective dates. Therefore, conceivably, Section 21 could be effective 90 days after [HB 293] is signed into law and even before the legislation establishing motor vehicle rental taxes is signed into law and thus [Section 21 could] result in an immediate effective date of the motor vehicle rental tax.

MR. PERSILY explained that the intent of Section 21 is that if the car rental tax passes, those car rentals wouldn't be subject to the general sales tax. "So, the effective date is the exclusion from sales tax on car rentals takes effect ... on the day the car rental tax takes effect," he said. In response to Co-Chair Whitaker, Mr. Persily explained that if HB 293 were to take effect before the car rental tax does, there would be state sales tax on car rentals and the general [state] sales tax would end the day the car rental tax takes effect.

Number 3249

REPRESENTATIVE GARA recalled during his campaign that he was told that with no exclusions, the [statewide] sales tax would raise close to \$100 million per 1 percent [of tax]. Given rebates municipalities with a higher sales tax are going to receive in the first year and the prescription drug and medical care deduction, does the \$300-\$375 million projection still apply. He inquired as to the bottom line numbers on the various manufacturing scenarios.

CO-CHAIR WHITAKER interjected that the committee isn't sure [what it's doing] with the manufacturing and transportation services. Although there are attempts to obtain specific information, [one must recognize] that [the current information provides] a range of possibilities rather than probabilities.

MR. PERSILY recalled that last year the assumption was that a general sales and use tax with traditional exemptions would amount to about \$100 million a year. In the fall 2002 revenue forecast that number was revised up to \$110 million per 1 percent. The communities with a sales tax of over 5 percent account for only 40,000 residents out of the some 630,000 in the state. Therefore, the state would lose only a small portion of the collections during the phase-in. As mentioned, the language regarding the manufacturing exemption is very tightly written. He acknowledged that the medical care exemption is a large one. Depending upon how the manufacturing exemption is addressed, the legislation could, without the motor fuel tax, still bring in \$300-\$375 million. He estimated that the wide range of \$300-\$375 million is dependent upon the definition of manufacturing, specifically in relation to [the exemption's] impact on the purchase of oil and gas equipment used in exploration and development in Alaska. Under the current tight definition, there wouldn't be an exemption for pumps, drilling rigs, well casings, and drill bits. The industry spends a lot of money on the aforementioned materials. Furthermore, real property is exempted while personal property isn't, which would need to be fully addressed.

Number 3626

CO-CHAIR WHITAKER recalled Representative Heinze's concern relative to oil industry equipment brought in from [out-of-state] versus that manufactured here.

MR. PERSILY clarified that regardless of whether the item is purchased in Alaska or not, if the goods are brought into Alaska for use, they would be subject to tax. Therefore, he agreed with Co-Chair Whitaker that those contractors currently in the business wouldn't find themselves at a competitive disadvantage. Mr. Persily reiterated that this is going to be dependent upon fully addressing the definition of manufacturing.

REPRESENTATIVE HEINZE recalled from yesterday's meeting that the parts of the modules wouldn't be taxed whereas the completed module would be taxed. Therefore, she asked if [under Version Q], [the parts and the completed modules] would all be taxed.

MR. PERSILY pointed out that it would depend upon whether the module is being built [by the company that will use it] or is being built for resale. If the module is being built for resale, the components would be tax exempt. However, when the completed module is sold, it would be taxed as opposed to the company that is building the module for itself and pays tax on the parts as the module is being built because the parts are being used in Alaska.

Number 3929

MR. PERSILY acknowledged Representative Rokeberg's point that there is no manufacturer's list price or receipt for an oil field service module. Therefore, it would pose some enforcement and audit problems.

CO-CHAIR WHITAKER remarked that he didn't expect there to be an answer to this line of discussion before the committee is compelled to report HB 293 from committee. He announced that such a discussion will have to take place at the next committee.

REPRESENTATIVE HEINZE asked if there is a reason why this can't be addressed before the legislation is forwarded. She identified this as one of the biggest concerns she has with the legislation. This is huge, she said. She pointed out that a tax on the Northstar Unit is a \$12 million tax. She said she didn't believe it would be responsible of her to merely let this concern go.

Number 4049

CO-CHAIR WHITAKER remarked that there is no such thing as a perfect bill. The committee is in the midst of a process and

the committee cannot insist that the legislation be perfect before moving it. He pointed out that ultimately there will be the opportunity to amend and vote on final passage of this legislation on the House floor. Co-Chair Whitaker said:

But to think that we, at this point in time, can address that subject adequately and continue the progress that is necessary given the compelling reason for us being here in the first place is simply not possible. It is our intention; it is the wish of the House leadership, the Senate leadership, and the administration, that this bill move from this committee tomorrow morning. We have done good work here. We cannot continue to keep this bill in this committee in the hope that it reach perfection before it moves on. We are part of a process; we are the first committee of purview and that is the manner in which we intend to operate. Certainly, if we do not have the votes to move this ... bill from this committee, then it will not move and each of you have that power to exercise.

Number 4217

CO-CHAIR HAWKER turned to the current provisions for manufacturing and asked if it would be correct to characterize these as tight provisions with few loopholes.

MR. PERSILY replied yes.

CO-CHAIR HAWKER characterized [Version Q] as a very tight bill with few exemptions. He acknowledged that as the legislation moves through the process, special interests may attempt to negotiate exemptions.

Number 4358

CO-CHAIR HAWKER, in response to Representative Wilson, suggested that the provisions are tight throughout the legislation. The scope of the exemption for the manufacturing industry and the mining industry is found on page 12. However, the parameters surrounding the assessments would apply in other areas and the definitions that would apply are throughout the legislation.

MR. PERSILY pointed out that page 22, line 29, contains the definition of manufacturing, which specifically states that manufacturing doesn't include construction.

REPRESENTATIVE WEYHRAUCH informed the committee that when Alabama moved from state tax administration to local tax administration, there were dramatic collection increases for the local jurisdictions. He asked if that would argue for a decentralized collection effort in the localities.

MR. PERSILY said he has heard the same about Alabama, but he doesn't quite believe it. Therefore, someone has been assigned the task of researching what happened in Alabama.

REPRESENTATIVE HEINZE mentioned the difficulty she is going to have with the decision [regarding whether to vote to forward the legislation or not]. She commented that she wants to be a good team player.

TAPE 03-29, SIDE B

REPRESENTATIVE HEINZE acknowledged all the hard work that has gone into this legislation, but emphasized, "Moving this thing out tomorrow morning just blows me away. ... I can't go there tomorrow. I'm already feeling the discord inside me. I was elected to be here to try to put something out. If I give my vote on this, then that's saying I agreed to this and then I go home to my constituents. Then who am I doing the disservice to?"

Number 4612

CO-CHAIR WHITAKER clarified that Representative Heinze will have the option tomorrow of objecting or not objecting and signing [the bill report with] a do not pass, pass, or amend. The aforementioned options recognize that legislation must progress, but be changed. Furthermore, everyone can work on changing the legislation as it goes through the process. [Version Q] won't be the finished product, he said.

REPRESENTATIVE HEINZE said that she understood those options, but she questioned where she is assured the matter will be addressed after the legislation leaves this committee.

CO-CHAIR WHITAKER explained that Representative Heinze would gain that assurance through her own efforts. He acknowledged that this is a huge policy issue.

Number 4348

CO-CHAIR HAWKER reminded the committee that one of the committee's charges is to review and consider manners in which state revenues could be increased. The purview of this committee is revenue issues. The next committee of referral is the House Finance Committee, which is charged with the purview of all financial matters, including revenue and expenditures. Co-Chair Hawker related his belief that the House Finance Committee will exercise due diligence in reconciling the revenue aspects of this [legislation] with the state's expenditure requirements. He opined that the House Finance Committee is the appropriate committee to continue with the next level of discussion in this legislation. He commented that it is appropriate to move this legislation forward, especially considering the constraints that arise as the session ends.

REPRESENTATIVE GRUENBERG directed attention to page 12, line 27, and the following language: "ingredient or component part of the product". He pointed out that there is no definition and thus he wasn't sure of the language's meaning when applied to various businesses. Therefore, perhaps it should be defined in some manner. He said he didn't believe there was the desire to spawn a new industry, a generation of tax lawyers.

CO-CHAIR WHITAKER announced that the drafters will be available tomorrow.

REPRESENTATIVE GRUENBERG then turned to the definition of manufacturing, which is defined on page 22, line 29 through page 23, line 1. Representative Gruenberg expressed concern that the terms "combining or processing components or materials" is broad enough. Furthermore, Representative Gruenberg said that he, too, is concerned about passing this legislation out of committee tomorrow because the committee has only heard from one segment of Alaska, the municipal governments. The committee really hasn't heard from the business community or the oil industry. He opined that the policy decision to not involve real property is worthy of discussion; the question is whether the [legislature] wants to exclude, from a general tax, intangible property.

REPRESENTATIVE WILSON asked if any of the language defining manufacturing includes oil.

MR. PERSILY answered that if the oil is processed at a refinery, the definition of manufacturing would include oil. However, if the oil is merely lifted from the ground, put in a pipe, and sold, it wouldn't really be considered manufacturing under the definition in [Version Q]. Mr. Persily clarified that he was referring to the equipment used [in the oil industry].

CO-CHAIR WHITAKER specified that under the current language, oil "stuff" is taxable.

MR. PERSILY clarified that under this definition of manufacturing, all of the equipment [used to drill for oil] would be subject to the sales tax. However, he noted that this interpretation would be subject to further clarification from the legislature.

MR. PERSILY, in response to Representative Rokeberg, said that the exemption of real property is in the definition that this legislation only applies to tangible personal property, and therefore real property would be exempt.

CO-CHAIR HAWKER pointed out that the related language is on page 8, line 19.

MR. PERSILY explained that [Version Q] doesn't specify an exemption for real property because it is not defined as a taxable item.

REPRESENTATIVE ROKEBERG inquired as to [how this legislation deals] with the easements to real property. [Indisc.].

MR. PERSILY remarked that it would depend upon whether those improvements become a permanent part of the real property as opposed to fixtures and equipment that wouldn't. He said that Representative Rokeberg's question is worthy of further research and clarification.

REPRESENTATIVE ROKEBERG turned to the intrastate transportation of petroleum products and asked if the transportation itself would be taxed similar to the pipeline tariff.

MR. PERSILY explained that under Version Q if it's subject to a single contract for the transportation interstate, it would be

exempt. Under Version Q, intrastate [transportation] would be subject to the tax.

REPRESENTATIVE ROKEBERG pointed out that from the North Slope to the North Pole is intrastate transportation.

MR. PERSILY, in further response to Representative Rokeberg, said that if the state is selling the oil at the wellhead from Prudhoe Bay to Williams, then he surmised it would be Williams' oil. Mr. Persily said that he would add this matter to the list of questions to consider.

REPRESENTATIVE ROKEBERG recalled that currently there is a ceiling on the real property tax mill rate in the state. He asked if there is a statewide cap on that.

MR. PERSILY said that he wasn't knowledgeable in that area.

Number 3009

REPRESENTATIVE ROKEBERG expressed concern that if there is too low of a cap [on the tax], municipalities may raise their real property tax in order to make up for the loss of cash flow due to the 8 percent tax cap. He indicated the need to research this. Representative Rokeberg asked if the statute prohibits a municipal government from imposing an income tax.

MR. PERSILY answered that he didn't know Title 29 well enough to know whether it gives municipal governments the authority to impose an income tax, although he did know that it does give them the authority to impose a sales and use tax, property tax, and special excise tax. He said that he has never seen the words "income tax" in a municipality's specific authority. Therefore, he surmised that the question becomes whether a municipality can impose an income tax absent a specific authority or prohibition against it. He said he would probably defer to Legislative Legal and Research Services.

MR. PERSILY, in response to Representative Rokeberg, said that Representative Rokeberg's amendment tying the sales tax rate to natural resource revenue is on someone's list to offer assistance.

Number 2846

REPRESENTATIVE SEATON turned attention to page 12, line 10, which provides a \$5,000 exemption on motor vehicles, watercraft, aircraft, and mobile homes. Representative Seaton acknowledged that some view a sales tax as fair due to an individual's choice to buy or not. However, in this legislation the individual purchasing an economical motor vehicle will actually subsidize the purchases of high-end vehicles. This cap says that if an individual purchases expensive items, that individual doesn't pay much tax whereas those who purchase an economical item will pay a higher percentage of tax. He inquired as to why there is a cap on these [exempt items].

REPRESENTATIVE GRUENBERG inquired as to why that language is there.

CO-CHAIR WHITAKER ruled that the above wouldn't be discussed tonight.

Number 2609

REPRESENTATIVE OGG directed attention to page 4, line 5, and requested that it be explained with examples that include fish and perhaps products in a store, for which the city would want to levy a specific excise tax. He asked if the state would have a 3 percent tax on these items and then the city could also have a tax on it.

MR. PERSILY said that municipalities throughout the state have special taxes such as the bed tax, the fuel transfer tax, the raw fish tax, the car rental tax, tobacco products, and alcohol. He said he understood page 4, line 5, to mean that a municipality, city, or borough could levy a specific tax on any single category in addition to the general sales and use tax.

REPRESENTATIVE OGG surmised that the municipality, city, or borough would continue to have existing exemptions under the sales tax. He further surmised that these entities could have an excise tax on clothing, for example, even though it was taxed generally as a sales product.

MR. PERSILY explained that the entity would continue the general sales and use tax with an additional [special] excise tax on the specified item.

REPRESENTATIVE OGG turned attention to page 12 and specified that he was going to refer to the fishing industry, the largest

employer in state. He pointed out that on page 12, line 24, "**Exemption for a sale to a miner or manufacturer**" and asked if the seafood processing industry would be included under that.

MR. PERSILY answered that he believes it would, but only to the extent of the ingredients or components. The equipment that operates the canning line wouldn't be under this tight definition. With regard to the question of what the definition of "manufacturing" includes, Mr. Persily confirmed that it would include the timber and fishing industry.

Number 2212

REPRESENTATIVE ROKEBERG continued with the discussion regarding manufacturing. He posed an example in which the manufacturer, Red Dog [Teck Cominco Alaska, Inc.], exports ore to a warehouse within the company's facility and doesn't sell the ore. He posed another example in which a fish packer cans fish then moves it from Alaska to Seattle, Washington, to store it for resale. He asked if there is an incidence of sales (indisc.) at any of those points.

MR. PERSILY said he didn't believe so as currently written. Again, the equipment used [would be taxed] while the transfer from one storage to another wouldn't [be taxed] because it's not the final sale and thus wouldn't be subject to a sales tax. If a natural resource is being sold to be processed for eventual resale, it wouldn't fall under this because there would be a resale exemption certificate.

REPRESENTATIVE ROKEBERG posed a situation in which some Copper River reds are sent to the Pike's Place Market in Seattle, Washington, they wouldn't be [taxed] because they're going to be resold.

MR. PERSILY said that would be his understanding.

Number 2033

CO-CHAIR HAWKER related that the intent was to craft a document that taxes something only once. Co-Chair Hawker recognized that as this legislation moves through the process, there will certainly be a lot of "carve outs" and clarifications in statute as well as regulatory interpretations.

REPRESENTATIVE SEATON asked if it's possible to craft something in this legislation as an export tax. Generally, Alaska exports natural resources and yet those items aren't being taxed.

CO-CHAIR WHITAKER said he didn't have an answer, but he opined that [natural resources] would be a separate class that would be subject to a policy call.

REPRESENTATIVE ROKEBERG mentioned that international treaties address those issues.

REPRESENTATIVE OGG reminded the committee that the state already has a 3 percent raw fish tax.

Number 1708

REPRESENTATIVE GARA turned to the exemptions in Version Q. With regard to rental exemptions, he related his understanding that an apartment or house that is rented won't be taxed.

MR. PERSILY indicated that to be the case because it's real property. The same would apply to commercial office rentals and land rentals. In further response to Representative Gara, he specified that housekeeping services and private school tuition would be taxed unless provided by an Internal Revenue Service 501(c)(3) nonprofit, in which case those would be tax exempt.

REPRESENTATIVE GARA turned to the mining and manufacturing exemption. He recalled that the two examples have been regarding purchases by an oil company and purchases of services by a pipeline company. He used ConocoPhillips Alaska, Inc., as an example and inquired as to what portion of the things the company is purchasing will be taxed under this exemption and what portion of things won't.

MR. PERSILY answered that most everything will be taxed. If ConocoPhillips Alaska, Inc., was running a manufacturing facility, the components or ingredients [would fall under the exemption]. He noted that a refinery would be a manufacturing facility. Under this legislation, the equipment - from the office copier to the drilling rigs - would be subject to the tax.

REPRESENTATIVE GARA continued with the disparity in pipeline transportation services.

Number 1440

MR. PERSILY clarified that transportation is a service, whether the goods are being put on a truck, on a railroad, or in a pipeline. If the aforementioned is an instate service, it's subject to the sales and use tax on the service under the current legislation.

REPRESENTATIVE GARA inquired as to why the interstate service isn't being taxed.

MR. PERSILY opined that there are more complex legal questions when one reviews taxing interstate commerce. The question becomes how far the state can reach to tax something that isn't in the state. Mr. Persily confirmed that the interstate pipeline services won't be taxed, which is referenced on page 13, line 21.

Number 1316

MR. PERSILY, in response to Representative Heinze, confirmed that under the [recent amendments to the] Stranded Gas Development Act the sales tax is negotiable. Therefore, the sales tax may negotiate a contract for payment in lieu of taxes and would nullify any state or municipal sales tax that might otherwise apply. He related his belief that it has to be a single contract. Furthermore, this Act only applies to natural gas regardless of how the gas is eventually exported from the state.

REPRESENTATIVE HEINZE highlighted her interest in how this sales tax would impact the industry, especially in this time when more exploration is desired.

CO-CHAIR WHITAKER pointed out that the Stranded Gas Development Act allows for exemptions through negotiation for virtually any gas project. Nothing here will inhibit a project. As the legislation stands, it will have a significant affect on all economic activity in the state, and therefore the committee needs to be sure not to prohibit future economic growth.

Number 0839

REPRESENTATIVE WILSON surmised that Co-Chair Whitaker is saying that "we don't have to put it in here because the Stranded Gas Act ... takes care of that."

CO-CHAIR WHITAKER answered, "Specifically relative to a potential gas project. The Stranded Gas Act allows, through negotiation, an exemption given that the proposers of a project can convince the administration and then convince the legislature."

REPRESENTATIVE GRUENBERG remarked that on page 10, lines 23-24, seem to be a clear infringement on [freedom of] speech. He asked if there was a reason the provision was drafted in that manner.

MR. PERSILY related that [the department] views this as a consumer protection measure allowing the consumer to know the advertised price of an item [does not include] tax.

Number 0620

REPRESENTATIVE GRUENBERG suggested that if the above is the intent, then the language needs to be drafted to specify that there's nothing to prohibit [including the tax in the price], but the consumer must be informed either way. He mentioned that he would work on the aforementioned. Representative Gruenberg turned to page 11 and pointed out that on line 4 transactions involving the United States are exempt while line 6 specifies that transactions involving an instrumentality of the state is exempt. However, he inquired as to whether the intent is to exempt transactions involving the state.

MR. PERSILY related his understanding that the intent of the provision would be to apply the tax to state and municipal entities.

CO-CHAIR HAWKER noted that he has spent a fair amount of time with an attorney on this matter. He pointed out that AS 39.52.960 "(12) 'instrumentality of the state' means a state agency or administrative unit, whether in the legislative, judicial, or executive branch, including such entities as the University of Alaska, the Alaska Railroad, and any public or quasi-public corporations, boards, or commissions; the term includes municipalities;".

REPRESENTATIVE GRUENBERG pointed out that Title 39 deals with public contracts whereas this is in Title 43. Although he recognized that most of these would be contracts, he suggested that it may need to be specified in this legislation.

Representative Gruenberg returned to the exemption on page 8, line 20, which specifies that the sales and use tax would involve tangible personal property. However on page 11, line 19, there is an exemption for intangibles. He asked if the intent was to tax those intangibles that aren't listed as such in this legislation.

MR. PERSILY explained that [the language on page 11, line 19] specifies that the state specifically exempts those items listed even if construed as tangible personal property.

REPRESENTATIVE GRUENBERG referred to page 13, line 25, and inquired as to why it has to be a single contract because one could combine or break up contracts to receive an exemption.

MR. PERSILY said he would work on obtaining Representative Gruenberg some answers on that. Mr. Persily acknowledged that the transportation services and interstate provisions need clarification.

Number 0122

REPRESENTATIVE SEATON turned attention to pages 11-12, which address isolated and occasional sales. He expressed the need to tighten this language such that it refers to occasional sales by individuals rather than large stocks from companies.

TAPE 03-30, SIDE A

REPRESENTATIVE SEATON indicated that he viewed the current language [on page 11-12] to be a loophole.

Number 0133

REPRESENTATIVE WILSON inquired as to what communities without any property that is taxable for property tax would do once [the state sales tax] is in place and the community reaches the 8 percent cap.

CO-CHAIR WHITAKER said that although that has been discussed, there isn't any language that addresses it in the legislation. He mentioned that Co-Chair Hawker is probably going to offer an amendment to deal with that.

MR. PERSILY explained that although a community could run up against the cap on the general sales and use tax, the community could impose any special tax on specific goods or services.

CO-CHAIR HAWKER pointed out that such a situation wouldn't come into play for four years, which would seem to allow for time to achieve some consensus from both the state and municipalities. He indicated that there are many ways to tax a community outside of this legislation.

REPRESENTATIVE ROKEBERG related his understanding that municipalities could impose a special assessment on a particular item, such as perhaps a toilet.

MR. PERSILY replied that such could be the case.

Number 0433

REPRESENTATIVE SEATON inquired as to the reason [the tax cap] was set at 8 percent.

MR. PERSILY opined that the intent of the drafters was to use 8 percent so that during the phase-in period, each community - even those such as Wrangell - would pay something to the state.

CO-CHAIR WHITAKER agreed and added that the intent was to provide "as much leeway as possible."

CO-CHAIR HAWKER informed the committee that during research and analysis there was nationwide review of the level of caps in states. Typically, those maximum rates were in the 7 percent range. As a matter of judgment, 8 percent seemed defensible and a rationale basis. Particular consideration was given to the fact that Alaska doesn't have a tandem income tax.

REPRESENTATIVE WILSON recalled reading somewhere that when an income and sales tax are in place, economist specify that beyond the 8 percent level, the economic viability of the community is put in jeopardy.

Number 0750

REPRESENTATIVE KOHRING expressed the need for the committee to consider sunseting this legislation in 3-5 years in order to evaluate if it works or whether a new route is necessary. Furthermore, Representative Kohring expressed his belief that

the public should vote on legislation of this nature because this is spending the public's money. He announced that he would be amenable to amendments on the aforementioned issues.

REPRESENTATIVE GARA asked if there has been assessment regarding the affect on sales and the decrease in sales to local business that might follow the implementation of a state sales tax.

MR. PERSILY replied no and added that the Tax Division doesn't have research staff large enough [to address that].

CO-CHAIR WHITAKER commented that it would probably be fair to conjecture that there may be some impact. It would also be fair, he said, to point out that 45 states have sales tax and commerce continues.

REPRESENTATIVE GARA interjected that Alaska's prices are already high and thus Alaska isn't like every other state, which is the source of his concern.

Number 0955

REPRESENTATIVE MOSES inquired as to how [the state] would obtain sales tax from a nonresident employee working on the North Slope who receives meals, housing, and a vehicle [from the company].

MR. PERSILY replied that the sales tax would only be collected on the purchases made in Alaska by the nonresident employee.

[HB 293 was held over.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Ways and Means meeting was adjourned at 6:55 p.m.