

MINUTES
SENATE FINANCE COMMITTEE
March 24, 2004
9:04 AM

TAPES

SFC-04 # 55, Side A
SFC 04 # 55, Side B
SFC 04 # 56, Side A

CALL TO ORDER

Co-Chair Gary Wilken convened the meeting at approximately 9:04 AM.

PRESENT

Senator Gary Wilken, Co-Chair
Senator Lyda Green, Co-Chair
Senator Con Bunde, Vice Chair
Senator Fred Dyson
Senator Ben Stevens
Senator Lyman Hoffman

Also Attending: SENATOR BERT STEDMAN; IAN FISK, Staff to Senator Bert Stedman; KATHY HANSEN, Executive Director, Southeast Alaska Fishermen's Alliance; DICK COOSE, Staff to Senator Bert Stedman; LUCKY SCHULTZ, Staff to Senator Fred Dyson; CHERYL FRASCA, Director, Office of Management and Budget, Office of the Governor; PHELAN STRAUBE, Staff to Senator Ben Stevens; KEVIN RITCHIE, Executive Director, Alaska Municipal League

Attending via Teleconference: From an Offnet site: ROBIN WILSON, Tax Division, Department of Revenue

SUMMARY INFORMATION

SB 286-DIRECT MARKETING FISHERIES BUSINESS

The Committee heard from the sponsor and the industry. A committee substitute was adopted and the bill reported from Committee.

SB 328-NATIONAL FOREST INCOME PROGRAM/DCED REGS

The Committee heard from the sponsor, adopted one amendment and held the bill in Committee.

SJR 3-CONST AM: APPROPRIATION/SPENDING LIMIT

The Committee heard from the sponsor, the Office of Management and Budget, adopted one amendment, one amendment was offered but withdrawn from consideration, and the bill was held in Committee.

SB 366-STATE SALES TAX

The Committee heard from the sponsor, the Office of Management and Budget, the Department of Revenue, and the Alaska Municipal League. A committee substitute was adopted and the bill was held in Committee.

#sb286

CS FOR SENATE BILL NO. 286(L&C)

"An Act relating to direct marketing fisheries businesses, to the fisheries business tax, and to liability for payment of taxes and assessments on the sale or transfer of fishery resources; and providing for an effective date."

This was the first hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken explained that this legislation would reduce "the fisheries business tax rate for direct marketers from five to three percent." A direct marketer is defined "as a fisherman who owns a vessel of at least 65-feet or less and catches, processes, and sells both processed and unprocessed fish product" in or outside of the State.

Senator Bunde moved to adopt the Finance committee substitute, Version 23-LS0738\Z as the working document.

Co-Chair Wilken objected for explanation.

SENATOR BERT STEDMAN, the bill's sponsor, explained that this legislation would affect the direct marketing business sector of the fishing industry. The fisheries business, which was implemented in 1913, is the oldest tax in Alaska. Currently, a three-percent tax is assessed on the "the grounds price," which is the price paid upon delivery of raw fish to the dock. The tax rate on fish sold to a floating processor, "which is a large mobile processing facility" is currently five-percent. This bill focuses on the group of fishermen who no longer fit these "old" fisheries business tax definitions, for, as the industry has developed, circumstances have

changed and more independent, small boat fishermen are conducting their own processing and marketing. Unlike the large scale floating processors, these business "are primarily Alaskans resident fishermen who operate out of our ports, buy our fuel, and supplies" and own property in the State.

Senator Stedman stated that this bill would correct current tax inequities by charging these small direct marketing vessels a three-percent rather than five-percent fisheries business tax. It would also alter the value upon which the direct marketers' tax is based. Rather than the value being determined by the grounds price, which is the floating processors' first point of sale, the direct marketers' "first point of sale is the second wholesale or retail price because these businesses are selling their fish to supermarkets, restaurants," or directly to the customer. Therefore, this bill would clarify "that direct marketers would be taxed on the 'prevailing' ground price."

Senator Stedman stated that, while some fisheries are required to pay taxes on a monthly basis, this legislation would specify that all taxes due by direct market vessels would be due each April first in order to allow them to take care "of their accounting comprehensively at the end of the season."

Senator Stedman summarized that this legislation would "remove the current disincentive in our tax system" by recognizing that the direct marketing industry is providing quality fish products, is responding to marketing demands, and is taking more responsibility to ensure the success of their operation. He stated that passage of this legislation would provide a level playing field to direct marketers by providing tax fairness. He reiterated that the vessels addressed in this legislation are less than 65 feet in length.

IAN FISK, Staff to Senator Bert Stedman, informed the Committee that the Version "Z" differs from the previous bill version in that it adds the word "unprocessed" into the definition of value in Sec. 5, page four, line five as follows.

(A) the market value of the fishery resource as determined by the prevailing price paid to fishermen for the unprocessed fishery resource of the same kind and quality by fisheries business in the same region or market areas where the fishery resource was taken if

New Text Underlined [DELETED TEXT BRACKETED]

Co-Chair Wilken removed his objection.

There being no further objection, the Version "Z" committee substitute was ADOPTED as the working draft.

Co-Chair Wilken noted that the sponsor has provided a "Short Definitions of Terms" handout [copy on file] that defines fishing terminologies.

Senator Olson inquired to the reason that April first is specified as the date the tax would be due. That date might place a hardship on the fishing industry.

Mr. Fisk responded that, historically, the Fisheries Business Tax has been due on April first, due to the fact that oftentimes "fishermen receive retroactive payments over the course of the winter." In an effort to make taxation filing easier, this legislation would consolidate a variety of taxes, including the hatchery assessment tax and the marketing tax, by making them uniformly due at the same time.

Senator Olson asked what impact would occur were the price of fish to lower and negate the retroactive payments.

Mr. Fisk could not recall any situation wherein a fisherman was required to pay back a company due to a reduction in price.

Senator Olson asked the burden were no retroactive funds forthcoming during the winter months.

Mr. Fisk responded that absent any retroactive checks, the fisherman would be required to pay based upon the price received at the time of delivery.

KATHY HANSEN, Executive Director, Southeast Alaska Fishermen's Alliance, testified in support of the bill as it would address "a tax clarity and tax fairness issue." Noting that she had been a participant in the development of this legislation, she shared that the bill is "a tightly woven compromise" resulting from discussion "between the industry, processors, and all the agencies that are involved in direct marketing licensing."

Co-Chair Wilken noted that Members' packets contain several letters in support of the legislation, including one from the Alliance, [copy on file] dated March 22, 2004.

Senator Stedman noted that the legislation was initiated and furthered by the Salmon Task Force, which is comprised of fishermen and processors. This issue has required attention for several years.

Co-Chair Green asked whether the legislation's new subsections contain any further language that should be addressed.

Senator Stedman responded in the negative. He stated that work has been conducted in regards to this issue for several years. Both the fishing and processing industries support it.

Co-Chair Green asked whether the new language in the bill would disadvantage any agency or group.

Senator Stedman responded no. The intent of the legislation is to "conceptually enhance" the State's value-added fisheries products, assist the industry in their modernization efforts and response to market conditions, enhance the product price, and address some tax reporting issues. The hope is that these efforts would result in increased revenue to both the State and the industry.

Senator Dyson moved to report the bill from Committee with individual recommendations and accompanying fiscal notes.

There being no objection, CS SB 286 (FIN) was REPORTED from Committee with indeterminate fiscal note #1 from the Department of Revenue and zero fiscal note #2 from the Department of Fish and Game.

#sb328

SPONSOR SUBSTITUTE FOR SENATE BILL NO. 328

"An Act relating to the national forest income program in the Department of Community and Economic Development and to the authority of the department to adopt regulations; making conforming amendments; and providing for an effective date."

This was the first hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken explained that this bill would provide the Department of Community and Economic Development with the necessary authority to adopt regulations required "to implement a federal program commonly know as National Forest Receipts."

SENATOR BERT STEDMAN, the bill's sponsor, stated that this legislation would allow the State to align with federal changes to the National Forest Receipts (NFR) program.

DICK COOSE, Staff to Senator Stedman, read the SB 328 introduction

statement as follows.

Historically, the distribution of funds under the National Forest Receipts Program was authorized under a 1908 federal law (16 USC 500) where 25% of the annual income earned from activities within a national forest was shared with the State for distribution to boroughs, cities, and regional education attendance areas located within the national forest. With the passage of the "Secure Rural Schools and Self-Determination Act of 2000" (P.L. 106-393), National Forest Receipts payments to the State for fiscal years 2002 - 2007 will be based upon the average of the three highest annual payments made to the State during the "eligibility period" of fiscal years 1987 - 2000.

Payments to the State under the Secure Rural Schools and Community Self-Determination Act stabilized for the period 2002-2007 rather than fluctuate and significantly dropping due mainly to the drastic reduction in national forest timber harvest the past several years. Distribution to the boroughs, cities, and rural education attendance areas changed only in that the federal act required that at least 15% but no more than 20 % of each local entities payment be spent on "special projects" with the balance to be spent on the traditional schools and roads categories. The special projects are defined in the Federal act.

SB 328 allows the Department of Community and Economic Development to prepare regulations to reflect the distribution and accounting for the 15-20% special projects distributions required by the Federal act.

Senator Stedman reminded that it would be beneficial to align the State with federal forestry statutes, particularly were the NFR receipt program to continue into the future.

Co-Chair Wilken asked when the current NFR program would expire.

Mr. Coose responded that the current authorization is in effect through the year 2007.

Co-Chair Wilken asked whether extending the NFR program beyond that date would require federal re-authorization.

Mr. Coose affirmed that it would.

Co-Chair Green understood therefore that the primary purpose of this legislation is to conform to federal changes.

Co-Chair Wilken understood that some of the statutory issues being addressed occurred when the State combined two departments.

Senator Stedman clarified that the legislation is required due to federal changes.

Mr. Coose explained that one of the federal regulations that changed was the mandate that 20-percent of the receipts be spent in support of special projects. The Department must receive authorization to rewrite regulations in that regard. He also noted that the Department could further respond to Co-Chair Wilken's comment regarding the departments' consolidation issue.

Co-Chair Green asked for an example of what would constitute a special project.

Mr. Coose explained that there are two kinds of special projects: one being a local government or community project such as the construction of a community shelter at Ward Lake in Ketchikan or a project to enhance search and rescue endeavors in Juneau, Sitka, and Ketchikan as well as some forestry service education projects. He expressed that the projects are clearly defined in federal law.

Amendment #1: This amendment inserts new language in Section 1, page two, following line two, as follows.

(m) In this section, "number of children in average daily membership" means that the number of full-time equivalent students enrolled and residing in the city school district or regional education attendance area that receives a share of the income from the public schools allocation of the fund created in (b) of this section.

Co-Chair Wilken moved to adopt Amendment #1 and objected for explanation.

Senator Stedman explained that the forest service receipts are shared based upon acreage. In addition to the major boroughs such as the City & Borough of Sitka and the City and Borough of Juneau, some of the unorganized communities are grouped together and then the receipts are shared. Currently, however, some communities are including correspondence study students in their calculations, which adversely weighs their school district over another. Amendment #1 "would level the playing field" by eliminating this disparity.

Senator Dyson asked for further explanation regarding these

correspondence school enrollment calculations.

Senator Stedman responded that one school in particular has expanded its distance correspondence school enrollment. This has served to increase their average daily student count. This amendment would allow only those students residing in and attending the community school to be factored into the equation. This would correct this current inequity.

Co-Chair Wilken stated that the intent of the NFR was to assist individual school districts in the operation of their schools by utilizing a funding formula based upon "students actually in seats." As depicted in the Department of Education and Early Development chart dated March 11, 2004 and titled "Correspondence History FY99-FY05 Projected" [copy on file] the community of Craig had eight students enrolled in its correspondence program in FY 2000. 574 were enrolled in FY 2004. The NFR is being used to fund those 574 correspondence students who do not physically participate in the school district. The amendment would serve to allocate the NFR, as intended, based upon those students who are physically present in the schools.

Senator Stedman stated that the communities that are embedded in the Tongass National Forest are unable to tax federal forest service lands, are unable "to expand into other resource based areas or do economic expansions to keep their population employed." He voiced appreciation for the efforts being exerted by Alaska's Congressional delegation in Washington to extend the NFR program.

Senator Dyson asked for confirmation that the City of Craig has a correspondence school program.

Senator Stedman affirmed that the school has a substantial amount of correspondence students.

Co-Chair Wilken referred Members to the aforementioned Department of Education and Early Development correspondence program chart.

Senator Dyson asked whether the students enrolled in Craig's correspondence program are from Craig, are from elsewhere, or are a combination of both.

Senator Stedman understood that the students are from around the State.

Senator Dyson asked for confirmation that the correspondence program being referenced could include students who live in Craig.

Senator Stedman responded that the program is a combination of students both within and outside of Craig.

Senator Dyson asked, therefore, whether the amendment would exclude students who reside in Craig but are enrolled in the correspondence program from being counted as part of the Craig school enrollment.

Co-Chair Wilken expressed that further information in this regard must be acquired.

Senator Stedman acknowledged.

Senator Dyson declared that students who live in Craig but who are enrolled in the correspondence program should be counted as Craig school students.

Co-Chair Green interjected that the amendment would not exclude in-district correspondence students as it specifies that those who enroll and reside in Craig would qualify.

Co-Chair Wilken agreed that the amendment's language does address Senator Dyson's concern.

Co-Chair Wilken requested that a breakout of the in-district students be specified in the chart.

Senator Olson asked how the adoption of this amendment would affect the Craig School District. He opined that the amendment should be held until that information is available.

Co-Chair Wilken stated that the amendment could be adopted prior to receipt of that information.

Senator Olson asked whether this amendment would affect charter schools.

Senator Stedman stated that the answer would be forthcoming.

Co-Chair Green commented that charter school students who are enrolled and reside in the school district would not be affected by the adoption of this amendment.

Senator Olson acknowledged.

Co-Chair Green stated that the purpose of NFR is to provide assistance to local communities within the national forest based upon residency.

Senator Hoffman asked whether any of the 574 students who are enrolled in the Craig correspondence program were counted in the receipt of NFR dollars in any other district.

Senator Stedman understood the question to be whether any of the students are being "double counted" in that they might be counted as being enrolled in both a correspondence program and in the community in which they reside. He assured that further information in this regard would be forthcoming.

Co-Chair Wilken declared, "that if they are, they shouldn't be." He suspected that this is not the case.

Senator Hoffman therefore asked how the students who are not residents of Craig would be accounted for were the amendment adopted.

Co-Chair Wilken understood that they would get State support through the State Student Foundation Formula which is a separate accounting. The NFR is additional funding to the State Foundation Formula.

Co-Chair Wilken removed his objection to the Amendment.

There being no further objection, Amendment #1 was adopted.

Co-Chair Wilken ordered the bill to be HELD in Committee.

#sjr3

CS FOR SENATE JOINT RESOLUTION NO. 3(JUD)

Proposing an amendment to the Constitution of the State of Alaska relating to an appropriation limit and a spending limit.

This was the fourth hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken stated that this legislation would allow a Constitutional spending limit proposal to be placed on a Statewide election ballot.

Amendment #1: This amendment deletes language in Section 1, page two, subsection (c)(3) and replaces it with new language as follows.

(3) of money received by the State from a source other than

the State or federal government that is restricted to a specific use by the terms of a gift, grant, bequest, or contract;

In addition, following ";" in Section 1, subsection (c)(8) on page two, line 21 the word "and" is deleted and a new paragraph is inserted to read as follows.

(9) of money for expenditure by a State agency to provide services to another State agency that has also received an appropriation of the same money; and

LUCKY SHULTZ, Staff to Senator Dyson, explained that in response to Members' concerns regarding the appropriateness of language in Version 23-LS0296\B pertaining to the appropriation calculation exemption "of donations, gift, and grants to the State for specific purposes," Amendment #1 would replace that language "with more appropriate language" pertaining to the exemption of such statutory designated program receipts as gifts, grants, bequests, and specifically, contracts.

Senator Dyson moved to adopt Amendment #1.

Co-Chair Wilken objected for explanation.

CHERYL FRASCA, Director, Office of Management and Budget, Office of the Governor, clarified that this amendment would align the bill's language with current State Statutes pertaining to statutory designated program receipts.

Mr. Schultz continued that the amendment would also incorporate a new exemption into the bill in order to allow for an exchange of interagency receipts in that one State agency could expend money in order to provide services to another State agency. This is not additional income and should therefore be appropriately reflected. The amendment would also address reimbursable agreements.

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Senator Hoffman inquired as to the necessity of addressing the interagency receipt language, as, were the funds already included in one department's budget, they would be incorporated into the allocation base.

Ms. Frasca responded that the amendment would address the issue of duplicated expenditures. She explained that when developing a fiscal summary that compares one year's budget to the next, there is a line item element through which to identify components that

should be backed out or would reduce duplicated expenditures that had been appropriated twice. The proposed language would serve "to exclude the duplication so they count only once under the limit." Examples would include "highway working capital fund appropriations to the Internal Services Fund for telecommunications" as well as interagency receipts.

Co-Chair Green asked regarding a component of the Department of Health and Social Services budget that would be affected by the proposed statutory designated program receipts language.

Ms. Frasca responded that the amendment would address the pro-share/fair share component in the Department as these funds are categorized as a contractual relationship between a health facility through which federal Medicaid funds are received and then returned to the State. The amendment would address this contractual issue.

Co-Chair Green asked whether "this implies that it is a contract with the State."

Ms. Frasca clarified that it is a contractual agreement between a hospital and the State.

Co-Chair Green understood therefore that it is not a contractual agreement between the hospital and the federal government.

Ms. Frasca affirmed that, when pertaining to the fair share/pro share arrangement, it is not.

Co-Chair Wilken removed his objection.

There being no further objection, Amendment #1 was ADOPTED.

Amendment #2: This amendment inserts new language into Section 2, subsection (d) on page three, line three following the word "fund" as follows.

if the balance in the fund is less than \$2,000,000,000. The amount deposited into the budget reserve fund under this subsection shall not exceed the amount that, when added to the balance in the fund before the deposit, equals \$2,000,000,000. After deposit is made under this subsection, any excess general fund money shall be deposited into a budget reserve fund established by statute

Senator Dyson moved to adopt Amendment #2.

Co-Chair Wilken objected for explanation.

Senator Dyson explained that this amendment would address the question of how to deal with excess funds were the money available for appropriation to exceed the limit. The original version of the bill decreed that the excess funds must be deposited into the Constitutional Budget Reserve (CBR). However, utilizing these funds to rebuild the CBR to approximately a seven billion dollar level has not been viewed as the "wisest public policy." Therefore, rebuilding the CBR to some acceptable or prudent level would serve to strengthen the State's bond rating and provide flexibility with which to respond "to foreseen and unforeseen fluctuations in revenue." This Amendment would specify a CBR limit of two billion dollars. This would be one billion dollars beyond Governor Frank Murkowski's recommendation that a one billion dollar minimum balance be established. Additional revenue beyond the two billion dollars would be deposited into the existing Statutory Budget Reserve (SBR) fund. He voiced support for the amendment.

Co-Chair Wilken recalled that prior to the State's withdrawing funds from the CBR beginning in 1994, money from the SBR was utilized between 1990 and 1994. The balance currently is the SBR is minimal.

Senator Dyson read Section 2, subsection (d), as it would read were the amendment adopted.

(d) The amount of money in the general fund available for appropriation at the end of each fiscal year shall be deposited in the budget reserve fund if the balance in the fund is less than \$2,000,000,000. The amount deposited into the budget reserve fund under this subsection shall not exceed the amount that, when added to the balance in the fund before the deposit, equals \$2,000,000,000. After deposit is made under this subsection, any excess general fund money shall be deposited into a budget reserve fund established by statute.

Co-Chair Wilken understood that adoption of the amendment would limit the CBR balance to two billion dollars and anything beyond that amount would be deposited into the SBR. He asked whether the language stating that, "any excess general fund money shall be deposited into a budget reserve fund established by statute" should be amended to clarify that this fund is the SBR.

Ms. Frasca suggested that amendment language specifying the general fund also be deleted, as such things as excess Permanent Fund earnings should also be deposited into the budget reserve fund.

Senator B. Stevens noted that, in response to his question as to

whether the Permanent Fund Earnings Reserve Account was a subaccount of the general fund or the Permanent Fund, the position of the Department of Revenue's Commissioner was that it was a subaccount of the Permanent Fund. As a result of the Commissioner's remarks, he understood that those earnings would not be available for appropriation as a general fund subaccount. Therefore, the Permanent Fund earnings reserve account would not be a consideration in this bill.

Ms. Frasca agreed that this would be the case "in terms of the categorization;" however, she stated that a future Legislature could appropriate the balance of the Permanent Fund earnings reserve account into the general fund.

Senator B. Stevens acknowledged. He noted that this legislation differs from separate earnings reserve account legislation that he has proposed, in that, by specifying that excess general funds would fund the earnings reserve account, there is a different funding mechanism.

Co-Chair Wilken suggested therefore that the general fund language in the amendment remain as is with the option of revisiting it as the bill progresses.

Senator Dyson stated that amending the language to specifically denote SBR is worthy of consideration.

Senator Dyson asked Ms. Frasca whether the language specifying that general fund money would be available for appropriation should be revisited.

Ms. Frasca asked that additional time be provided before that determination is made.

Senator Dyson asked the Members and Ms. Frasca to reflect upon whether two billion dollars is an appropriate CBR limit.

Ms. Frasca requested that she be provided sufficient time to be able to confer with the Department of Revenue in that regard.

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Senator Bunde asked the rationale behind designating two billion dollars as the CBR limit, particularly as the State typically requires, annually, half a billion to provide for cash flow issues aside from sufficient funding with which to provide for such things

as a downturn in revenue or a catastrophic event. In addition, the fact that the State borrowed five billion dollars from the CBR and has yet to fully reimburse that amount is an irritant.

Senator Dyson voiced appreciation for that concern. He also voiced appreciation for the efforts being exerted by Senator B. Stevens to present legislation to reimburse the CBR.

Senator Dyson voiced the understanding that the ability of the CBR to reach a five billion balance was unanticipated, and that the Governor's recommendation that a one billion dollar CBR limit be specified as the account "floor" or level that must not be breached was the amount required to maintain such things as the State's bond rating. In addition, he referenced separate testimony pertaining to loan rates, inflation, the financial market and the impact that such things incur on the State's financial situation.

Senator B. Stevens expressed the hope that someday the Legislature could face the problem of what to do with an excess balance in the CBR. He also stressed that reimbursing the CBR is "a constitutional obligation" and unless that issue were resolved, either by changing the Constitution or by repaying the amount borrowed, the establishment of a one billion dollar floor as recommended by the Governor or a two billion dollar floor as suggested in this amendment would serve to prohibit that reimbursement as future Legislators could appropriate excess funds elsewhere.

Senator Dyson clarified that rather than establishing a two billion dollar floor, this amendment would establish that amount as the maximum CBR "ceiling" or limit.

Senator B. Stevens understood that this limit would only apply to the amount of general fund contributions to the CBR.

Senator Dyson clarified that the two billion dollar limit would apply to total funds in the account regardless of where they originated. He requested Members to contemplate whether a two billion dollar balance in the CBR combined with the money that might be deposited into the SBR would qualify as a reimbursement of the money the State has borrowed from the budget reserve.

Senator B. Stevens responded that time would be required to appropriately consider the situation. However, he voiced discomfort that the Legislature might allocate funds in excess of the proposed two billion dollar mark to other savings accounts rather than repaying the entirety of the money owed to the CBR. This mechanism could displace the State's debt obligation to the CBR.

Senator Hoffman asked whether this language would serve to repeal the CBR repayment language. This would be contrary to the original intent of Legislators who, acting upon a vote of the people, allowed funds to be borrowed from the CBR with the understanding that the money would be repaid. He stated that, years ago, the Legislature, without success, inquired of the Administration at the time, as to whether settlement money the State received from oil companies could be utilized to repay the CBR. Therefore, he agreed with Senator B. Stevens that the entire amount of money that has been borrowed from the CBR should be repaid. This bill, he continued, in addition to establishing a spending limit, would also attempt to amend, by establishing a spending cap, a vote of the people that specified that the CBR should be reimbursed.

Senator Olson asked whether a majority vote of the Legislature would be required in order to access funds from the SBR as opposed to the three-quarter vote that is required to access the CBR.

Co-Chair Wilken affirmed that a majority vote could access the SBR.

Senator Dyson, in response to Senator Hoffman's concern, asked for clarification regarding whether the adoption of this amendment would eliminate the Constitutional requirement that the CBR be reimbursed to the level it was at the time the Constitution was amended to allow funds to be borrowed from the CBR.

Mr. Schultz responded that the Version "B" committee substitute contains language that would repeal Article IX, Section 17(d) of the Constitutional budget language that specifies that any withdrawal of funds from the CBR must be repaid. Amendment #2 would add new language to Section 17(d).

Senator Dyson therefore stated that it must be clarified that were the people of the State to approve language as presented in this legislation, the voters would be changing language that they had previously approved in this regard. He stated that, provided that it is clearly communicated to the people of the State, Legislators have the right to determine an appropriate CBR fund level. The real discussion should be what is an appropriate level for the CBR.

Senator Hoffman stated that the single subject rule should be applied in this instance, as the language contained in the Amendment regarding a specified CBR level is a completely different topic that should require a separate Constitutional amendment aside from the spending limit. While it does pertain to managing the State's funds, aligning it with a spending limit might be a stretch.

Senator Bunde understood that the reason that a two billion dollar limitation is being presented is to provide sufficient funding above the Governor's one billion dollar "floor" recommendation that supports the State's credit rating. Therefore, in addition to maintaining a one billion dollar floor, \$500,000,000 is required to support cash flow issues throughout the year and another \$500,000,000 would be available to address claustrophobic events or such things as financial market fluctuations and oil price declines.

Senator Bunde stated that the position of maintaining a one billion dollar floor to insure the State's credit rating has also been questioned as the State has other options through which to support its bond ratings such as acquiring a line of credit from a financial institution. The problem with doing that, he professed, is that it would incur additional debt service whereas maintaining one billion dollar balance in the CBR would not cost the State anything. It would also garner interest earnings even though utilizing the CBR in this manner would tie up a lot of money. Knowing which position to advance is a dilemma.

Co-Chair Wilken asked that Senator Dyson consider holding this amendment for further discussion.

Senator Dyson agreed. He also acknowledged Senator Hoffman's point about the single subject rule and stated that further research in that regard would be undertaken.

Senator Dyson stated that an amendment that would specify a four-year termination date on this proposal is being considered, with a provision that it could be re-authorized.

Co-Chair Wilken asked what the fee might be were the State to arrange for a one billion or half a billion dollar line of credit with a major financial institution. He considered this a viable option and suggested that it might be less expensive than the cost associated with investing the CBR on a short-term rather than long-term basis. With \$28 billion in the bank, the fee for a line of credit should be "relatively" reasonable. Perhaps an informal inquiry could be made.

Ms. Frasca stated that information in this regard would be forthcoming.

Senator Dyson voiced uncertainty as to whether providing \$500,000,000 to address such things as fluctuations in the financial markets or the price of oil is sufficient. He asked Ms. Frasca or the Department of Revenue to provide further information

to the Committee in this regard.

Senator Dyson moved to withdraw the motion to adopt Amendment #2.

There being no objection, Amendment #2 was WITHDRAWN from consideration.

Co-Chair Wilken ordered the bill HELD in Committee.

#sb366

SENATE BILL NO. 366

"An Act relating to the levy and collection of sales and use taxes, to the levy and collection of municipal sales and use taxes, and to municipal sales and use taxes on alcoholic beverages; and providing for an effective date."

This was the first hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken stated that this bill, which is sponsored by the Senate Finance Committee, would institute a statewide four-percent sales tax on sales, lease, rental, and use of tangible property and services within the State.

Senator B. Stevens moved to adopt committee substitute, Version 23-LS1051\U as the working document. He then objected to the motion in order to explain the changes in the committee substitute.

Co-Chair Wilken noted that Kathryn Kurtz, Legislative Counsel, Division of Legislative Legal and Research Services, has provided a Version "U" Sectional Analysis [copy on file], dated March 24, 2004.

Senator B. Stevens stressed that this is a working document and as such would continue to evolve over time. Changes in Version "U" include: the addition of three new sections to the list of limitations on the powers of Home Rule municipalities to Section 5, on page two, beginning on line seven.

Co-Chair Wilken interjected that numerous individuals have indicated the desire to testify regarding this bill.

Senator B. Stevens expressed the understanding that this would be a Committee work session with the goal of developing a new committee substitute based upon Department and Member input. Therefore, he asked that the hearing be limited to Committee discussion.

Co-Chair Wilken apologized for not clarifying that this hearing would be a work session, as it is the bill's first hearing and "a foundation on what we are talking about" must be established. The Version "U" committee substitute was distributed to the public with the understanding that public testimony would be taken at a later date.

Senator B. Stevens explained that some of the changes incorporated into the committee substitute would address concerns presented by State departments, specifically the Department of Revenue. However, not all of the concerns have been addressed, as this is a continuing work in progress. In addition to changes in Section 5, other changes include: language in Section 12, page three, line 27, that would allow municipalities to adjust their local tax system in order to qualify for the one-percent return the State would rebate to the municipality; language in Section 16, subsection (7) on page five, line 29 would provide an exemption for goods for resale by the mining and manufacturing industry was added because it was inadvertently omitted in the original committee substitute; the reference to a local bed tax, were it separate from the local sales tax, as specified under AS 29.45.700, in Section 16, subsection Sec. 43.44.060. Relationship to municipal levies. on page six, line 29 would allow it to remain in place; language in Section 16, Sec. 43.44.060, subsection (c) on page seven, beginning on line 18 would address the situation of two different taxation rates resulting from a city within a borough by combining the two rates and then splitting the revenue rebated to that taxing regime proportionately between the two entities.

Senator Hoffman asked for further information regarding how the State's one-percent tax rebate would be split between a municipality and a borough.

Senator B. Stevens responded that the one-percent rebate would be divided between the two entities depending on their individual tax levies. A five-percent tax on behalf of the local entities would be collected were a municipality to levy a two-percent tax and the borough to levy a three-percent tax. One percent of the five percent tax would be rebated and prorated proportionately between the two.

Senator Hoffman understood therefore that the language specifically defines how the split would occur as opposed to it being an optional situation.

Senator B. Stevens responded that this would be the guideline for any community that that a dual city/municipality taxation system.

Senator B. Stevens explained that other changes in Version "U" include language in Section 16, Sec. 43.44.130. Authority to enter streamlined sales and use tax agreement. on page nine, beginning on line nine that "would permit the State to enter into a multi-state sales agreements for catalog sales," and, were any agreement to occur on the federal Congressional level regarding Internet sales, this would allow the State to participate in that agreement. In addition, this language would allow the purchase of a large ticket item that is taxed in one of certain participating states to be exempt from taxation in Alaska. He noted that this would prevent "dual taxation," and he noted that these types of agreements currently exist between some states.

Senator B. Stevens further explained that some issues not addressed in this committee substitute include whether or not to establish a sales tax limitation; or whether or not to exempt such things as industrial equipment that is used in development or exploration or transportation expenses as exemplified by taxing items shipped on the Alaska Railroad that would probably be taxed again when sold at the retail level. He voiced support for exempting both of these components. Another issue not addressed is whether or not to incorporate penalties for non-compliance or non-enforcement language.

Co-Chair Wilken asked whether Version "U" addresses the entirety of the Department of Revenue concerns as detailed in the Department's March 19, 2004 memorandum [copy on file] signed by Deputy Commissioner, Steve Porter, and addressed to Senator B. Stevens.

Senator B. Stevens responded that Version "U" addresses most but not all of the concerns. Efforts on how to address the remaining concerns are continuing.

PHELAN STRAUBE, Staff to Senator Ben Stevens, informed the Committee that efforts are continuing in regards to incorporating into the bill, language, as suggested by Senator Hoffman, that would allow a small business to withhold from submitting a tax every 30 days as required, until such a time that the tax owed amounted to a minimum of \$250.

Senator B. Stevens noted that another area requiring further discussion would pertain to a sixty dollar per transaction limitation, specifically how it would affect existing local revenue streams. He also noted that language exempting wages and interest from taxation was also inadvertently omitted from the bill's exemption list.

Senator Bunde asked whether the intent of the bill is to limit the collection of tax to only those entities holding a State business license as enforcing collection of the tax on such things as garage sales would be an administrative nightmare.

Senator B. Stevens responded that Section 16, subsection (6)(A) on page five, beginning on lines 25 would exempt the resale of property if a purchaser resells the property, by itself or in combination with other property, "in the ordinary course of business."

Senator Hoffman stated that such things as garage sales could also be exempted by language in Section 16, subsection (3) on page five, line 17 that would exempt "occasional sales."

Senator B. Stevens concurred.

Senator Hoffman asked about his request to provide a senior citizen sales tax exemption in the bill.

Senator B. Stevens responded that while this issue was discussed, it was determined that the municipalities that currently exempt senior citizens from taxation could address this on the local level by utilizing the one-percent rebate to assist seniors or by providing them a tax credit.

Senator Hoffman stated that he would support a senior citizen tax exemption. For clarification, he pointed out that while one of his requests was to exempt diesel fuel utilized in the generation of electricity, the language in Section 16, subsection (5) on page five, line 22, that exempts "the sale of natural gas, diesel fuel, heating oil, water, electricity, steam, or refuse and garbage collection service" would serve to exempt diesel fuel in its entirety. He voiced that his suggestion limited the diesel fuel exemption whereas the language as written would serve to provide a disparity between gas users and diesel users.

Senator B. Stevens acknowledged the comment and stated that this exemption would be revisited.

Senator Dyson opined that the endeavor to exempt industrial machinery would be difficult as it would be a challenge to provide this exemption to a specific industry such as the oil industry and large construction projects but not consider exempting such things as commercial fisherman or fish processors.

Senator B. Stevens responded that this had been considered without resolution. However, it should be noted that while the four percent

tax might apply to every purchase, there is a maximum \$60 tax limit. This "ceiling," which could be described as an invoice sales tax rather than an itemized sales tax, was included in the bill in an attempt to address this concern.

Senator Dyson acknowledged the explanation.

Senator Olson asked how the tax would be applied to harvesters of products, be it either fishermen harvesting from the sea or farmers harvesting potatoes who might sell their products either on a wholesale or retail basis.

Mr. Straube interjected that were a fisherman to purchase cans that would be utilized in the process of his harvest, the purchase of those cans would be exempt from the sales tax. Manufacturing components would also be exempt from taxation under provisions of this bill.

Senator B. Stevens continued that, the concept "is that any item that is either sold or purchased in the process for total resale is exempt." A borough would have the ability to implement a landed raw fish tax, whereas the State would have the ability to tax the final product where that product sold in the State. This sales tax would not apply to a product manufactured in the State but sold outside of the State.

Co-Chair Wilken suggested that the word "sewer" be added to the list of exemptions in the aforementioned Section 16, subsection (5) on page five, line 22.

Senator B. Stevens agreed that some of the activities specified in that section might not be owned by a municipality.

Co-Chair Wilken affirmed that this is the case in the City of Fairbanks.

Co-Chair Wilken asked regarding the status of the bill's fiscal notes.

Senator B. Stevens responded that the adoption of the Version "U" committee substitute would provide the Department of Revenue with significant information with which to develop a fiscal note. However, he requested that development of the fiscal note be delayed until a new committee substitute that encompasses the items that were inadvertently omitted from Version "U" is developed.

Co-Chair Wilken suggested that a separate estimate be developed that would depict how much sales tax would be lost were senior

citizens exempted.

Senator Bunde asked the anticipated annual expense of administering the program, as he was concerned that these expenses might outweigh the revenue the tax would generate.

Senator B. Stevens understood that the Department has calculated those figures.

ROBIN WILSON, Tax Division, Department of Revenue, testified via teleconference from an offnet site and stated that while the Department would work with Senator B. Stevens to develop a fiscal note, it could not provide one at this time as the Committee has some important decisions yet to make. The Version "U" committee substitute has not been reviewed by the Department and language regarding such things as the tax limitation could complicate the development as it would affect costs. She assured however, that once the exemption structure is clarified, a fiscal note would be developed.

Senator B. Stevens withdrew his objection to the committee substitute, with the understanding that a new committee substitute would be provided in short order.

There being no further objection, the Version "U" committee substitute was ADOPTED as the working document.

Co-Chair Wilken asked that the handout titled "State Sales Tax Issue Primer" [copy on file], dated March 2004, that was developed by the Alaska Municipal League (AML) be explained.

KEVIN RITCHIE, Executive Director, Alaska Municipal League, voiced appreciation for the Committee's endeavors to address the State's fiscal dilemma by considering a variety of revenue generating options including a State sales tax.

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Mr. Ritchie stated that the AML would be available to assist the Committee in this endeavor. He noted that the intent of the "State Sales Tax Issue Primer" is to examine some of the impacts that would result were a State sales tax implemented as well as to acknowledge that this State is different from other states. Since Statehood, even when times were tough, sales taxes have been reserved to be a municipal tax, as it is recognized that many small communities do not have any other viable option through which to

generate revenue aside from property taxation. He also noted the wide costs of living variations in the differing regions of the State is a consideration in this issue.

Mr. Ritchie noted that in response to questions pertaining to revenue sources, AML would first recommend the use of the earnings of the Permanent Fund and the adoption of the Percent of Market Value (POMV) Program.

Mr. Ritchie declared that a "direct partnership" between municipalities and the State must be sought regarding the development of the fiscal notes, as the exemption list provided in the bill is "a huge issue" that would affect both the State and municipalities' sales tax revenues. He noted that the Kenai Peninsula Borough and the City and Borough of Juneau currently are the largest sales tax collection organizations.

Mr. Ritchie concluded his remarks by stating that AML would be available to answer questions regarding the Sales Tax Primer and would welcome participation in the continuing development of the bill.

Co-Chair Wilken voiced appreciation for AML's assistance, the Primer, and the suggestion to develop a Sales Tax Exemption Commission.

Senator Olson assumed that from "the negative approach" presented in the Primer that AML has a negative view of the State Sales Tax. He asked whether the exemption approach would be more palatable to municipalities were it to mirror exemptions currently in place at the local level.

Mr. Ritchie responded that each area of the State is different and that difference is reflected in each area's specific exemptions. Beginning on page 16 of the Primer, there is a definition and an overview of various communities' tax exemptions, and in short, there are no common or uniform tax exemptions. He also clarified that this non-uniformity also pertains to the tax limitation as some municipalities have a limit on a total invoice while others might apply it to a single purchase.

Senator B. Stevens complimented Mr. Ritchie and AML on the information provided in the booklet. Continuing, he spoke to the issue as depicted on page ten of the Primer in the section titled "A State Sales Tax in Not Fair to Alaskans" which bases its anti-tax position on the fact that the price of goods in rural communities is substantially higher than that of urban communities. While labeling this as a major policy call, he declared that he has

"yet to rationalize within my mind" a justification as to why it is acceptable on the local level to tax products to fund local government but it is labeled "unfair" for the State to tax those same products. On the same subject, he noted that urban areas use property taxes as a mechanism through which to fund government. He noted that the State provides goods and services, including education, "at a equal level" to all areas of the State be it urban or rural.

Senator Bunde opined that the information on this page intimates that the proposed Sales Tax would be unfair due to the fact that because the price of an object such as milk is more expensive in one area of the State, the purchaser would be required to pay more tax. Continuing, he recalled testimony to the affect that, in one areas of the State, a Permanent Fund Dividend check equates to approximately 30-percent of the household income. Therefore, were an income tax implemented, that area of the State would be paying little or no income tax while another area of the State would be paying substantially more. He opined, however, that the income tax scenario is fairer than the sales tax scenario.

Senator Hoffman, furthering Senator Bunde's comments, stated that what is relevant in an income tax scenario is that everyone in the State is treated equally whether they are in an economically depressed area or not. The problem with a State sales tax is that the State would be receiving additional dollars from communities where the price of things such as milk is higher. This differs from the local tax scenario in that everyone in the community would pay the local government the same tax amount. He stated that there is fairness in a local sales tax as the individuals living within those boundaries are treated equally. In conclusion, he agreed that Rural areas would be treated unfairly were a Statewide sales tax implemented.

Senator B. Stevens proclaimed that these discussions would continue; however, he argued that the State sales tax would be fair because it would be applied equally in all parts of the State regardless of the different pay scales, expenses, and other amenities. A State sales tax would be the most equitable thing that could be applied across the State and furthermore, the areas that are more affluent, spend more money and therefore would contribute more money.

Senator Hoffman declared that it would be fair to tax on a per gallon basis rather than a price per gallon basis. Therefore, whatever one consumes, one pays for whether it be marine, aviation, or motor fuel. He recognized this as being a fair taxation method as opposed to the inequities presented by a State sales tax based

on price.

Senator Olson noted that contrary to State programs that provide cost of living allowance considerations for the price of services or employment, private business employees are not provided these benefits.

Senator B. Stevens countered that private industry employees would also not have the option to not pay local sales or property taxes on such things as rent.

Senator B. Stevens stated that a new committee substitute would be forthcoming.

Co-Chair Wilken stated that an opportunity for public testimony on this bill would be forthcoming.

Co-Chair Wilken ordered the bill HELD in Committee.

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ADJOURNMENT

Co-Chair Gary Wilken adjourned the meeting at 10:54 AM.