

ALASKA STATE LEGISLATURE
SENATE LABOR AND COMMERCE STANDING COMMITTEE

February 17, 2011

1:31 p.m.

MEMBERS PRESENT

Senator Dennis Egan, Chair
Senator Joe Paskvan, Vice Chair
Senator Linda Menard
Senator Bettye Davis
Senator Cathy Giessel

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

SENATE BILL NO. 23

"An Act relating to transferable film production tax credits; and providing for an effective date by amending the effective dates of secs. 3 and 4, ch. 63, SLA 2008."

- HEARD AND HELD

SENATE BILL NO. 64

"An Act relating to a tax credit for corporate income taxes paid for qualified research and development expenditures; and providing for an effective date."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: SB 23

SHORT TITLE: FILM PRODUCTION TAX CREDIT

SPONSOR(s): SENATOR(s) ELLIS

01/19/11	(S)	PREFILE RELEASED 1/7/11
01/19/11	(S)	READ THE FIRST TIME - REFERRALS
01/19/11	(S)	L&C, FIN
02/17/11	(S)	L&C AT 1:30 PM BELTZ 105 (TSBldg)

BILL: SB 64

SHORT TITLE: RESEARCH AND DEVELOPMENT TAX CREDIT

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

01/24/11 (S) READ THE FIRST TIME - REFERRALS
01/24/11 (S) L&C, FIN
02/17/11 (S) L&C AT 1:30 PM BELTZ 105 (TSBldg)

WITNESS REGISTER

SENATOR JOHNNY ELLIS
Alaska State Legislature
Juneau, AK

POSITION STATEMENT: Sponsor of SB 23.

CURTIS THAYER, Deputy Commissioner
Department of Commerce, Community and Economic Development
(DCCED)
Juneau, AK

POSITION STATEMENT: Introduced Ms. Ayers and said she would present an overview of the Alaska Film Office relative to SB 23.

WANETTA AYERS, Director
Division of Economic Development, Department of Commerce,
Community and Economic Development (DCCED)
Juneau, AK

POSITION STATEMENT: Presented an overview of the Alaska Film Office relative to SB 23.

ROBIN CORNFIELD, Vice President
Communications and Marketing
Nana Development Corporation
Nana Regional Corporation

POSITION STATEMENT: Supported SB 23.

DEBORAH SCHILDT
Alaska Crew Training
Anchorage, AK

POSITION STATEMENT: Supported SB 23.

BRYCE HABEGAR
Alaska Crew Training
Anchorage, AK

POSITION STATEMENT: Supported SB 23.

WOODRUFF LAPUTKA, representing himself
Anchorage, AK

POSITION STATEMENT: Supported SB 23 as a film maker and graduating UAA student.

D.K. JOHNSTON, representing himself

POSITION STATEMENT: Supported SB 23 as an independent Alaskan filmmaker.

ALLEN ERICKSON

White Fox Studios

POSITION STATEMENT: Supported SB 23.

LARRY GOLDEN

Aurora Films

Anchorage, AK

POSITION STATEMENT: Supported SB 23.

JAMES MCLEAN, representing himself

Anchorage, AK

POSITION STATEMENT: Supported SB 23 as an independent screen writer.

CURTIS THAYER, Deputy Commissioner

Department of Commerce, Community and Economic Development (DCCED)

Anchorage, AK

POSITION STATEMENT: Supported SB 64.

WANETTA AYERS, Director

Division of Economic Development, Department of Commerce, Community and Economic Development (DCCED)

Anchorage, AK

POSITION STATEMENT: Supported SB 64.

JOHANNA BALES, Deputy Director

Tax Division

Department of Revenue (DOR)

Anchorage, AK

POSITION STATEMENT: Supported SB 64.

ACTION NARRATIVE

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CHAIR DENNIS EGAN called the Senate Labor and Commerce Standing Committee meeting to order at 1:31 p.m. Present at the call to order were Senators Giessel, Paskvan, and Egan.

SB 23-FILM PRODUCTION TAX CREDIT

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CHAIR EGAN announced SB 23 to be up for consideration.

SENATOR JOHNNY ELLIS, sponsor of SB 23, said the goals are pretty simple: they want to continue the amazing growth and success of Alaska's burgeoning film and TV production industry. Many people thought it was "pie in the sky" and wouldn't happen, but "things are coming along very nicely."

He explained that SB 23 offers to extend the successful tax credits, a signal that the tax incentives are here to stay for a significant period of time. So, investments can be made that will take this industry to the next level - in particular, a sound stage and some other facilities. He said folks in the business community have the resources and are willing to make those investments, but they need to know that the tax credits on the production side will be available long term.

SB 23 would extend the tax credits for 10 years in two \$100-million, five-year increments - not unlike the state does for other industries when they want to incentivize private sector work.

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SENATOR DAVIS joined the committee.

SENATOR ELLIS said it has been hard to find a brand new industry for the state and this film program is successful so far. Extending the incentives would continue bringing new money and investments into the Alaskan economy and put Alaskans to work. He said they have already seen the benefits of recent multi-million dollar productions where hundreds of Alaskans were working as cast and crew in jobs as varied as electricians, carpenters, truck drivers, caterers, security guards, and plumbers. This industry isn't just glamorous; it's real down-to-earth small business and job opportunities for Alaskans.

SENATOR ELLIS added that businesses across the state, both urban and rural, have been able to hire some people and do work during the off season. For instance, commercial fishermen that usually sit around in the winter time were able to work on "Everybody Loves Whales." The original legislation was passed in 2008 and everyone tells him that is why things have gone to the next level. Since its inception in 2008, 15 productions have received tax credits for a total of 910 days and had a total "Alaska spend" of \$15 million. As of January 2011, an additional 28 productions are prequalified for the incentives. If all of these productions are completed, there will be an estimated additional Alaska spend of almost \$84 million. This brings the total projected boost to the Alaskan economy of nearly \$100 million

since 2008. Several people have asked why this should be done if Alaska doesn't already have a trained workforce, but his response is get the industry going and get Alaskans on those jobs!

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CURTIS THAYER, Deputy Commissioner, Department of Commerce, Community and Economic Development (DCCED), introduced Ms. Ayers and said she would present an overview of the Alaska Film Office.

WANETTA AYERS, Director, Division of Economic Development, Department of Commerce, Community and Economic Development (DCCED), said the statutory authority of the Alaska Film Office outlines five responsibilities: to cooperate with the private sector to promote Alaska as a film destination, to provide production assistance, to certify film production internship programs, and to cooperate and co-administer the Alaska Film Production Incentive Program with the Department of Revenue (DOR).

With regard to private sector collaboration, a number of different tactics are being pursued. The first is the website, film.alaska.gov, which provides a variety of information about the program and filming in Alaska. She said they have worked to engage a variety of industry organizations, trade associations, and allied groups to help them find out what the opportunities in the Alaskan film industry are. Outreach to the business community and others that benefit from the film industry is being done so that they are aware of what the opportunities are - and the phone rings every day about this program.

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MS. AYERS said with regard to promoting Alaska, the Film Office is engaged in print advertising in a variety of different industry magazines and directories to make sure the message is out there. They attend a variety of different trade shows and other events to promote Alaska as a film location and talk to producers - and there is a great deal of interest. She showed them a program brochure outlining the incentive program and some of the recent activity that is happening in Alaska.

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She said no industry springs forward fully formed. Now they have this initial interest in this new industry and various state agencies are looking at what their role can be; this includes the Department of Labor, the University, other private sector

efforts for on-the-job training, and other outreach efforts to just help develop the workforce that will meet the needs of this industry.

She said the Film Production Incentive Program has a process of prequalification; that is, going through the production process and submitting the final application; having that approved and then advancing it to the DOR and receiving a tax certificate which in turn gets sold to someone with a corporate tax obligation.

She said two productions were in the queue as this presentation was being developed. One of them may have been approved recently, but overall they have approved 44 pre-qualifications. Over the life of the program (the last three years) 14 approved tax credit applications have been advanced. The total production value for the prequalified applications is about \$34.5 million; those tax credit applications that have been received and approved, about \$4.8 million. And those numbers are changing as the next two productions are approved.

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MS. AYERS said the Film Office has 1.5 full-time equivalent positions. Dave Worrell is their development specialist and he manages the office; Erin Gora is the administrative assistant. Deputy Commissioner Thayer and Special Assistant to the Commissioner Roberta Graham, Communications Coordinator Mark Kelsey, and herself have committed a great deal of time over the last year to this program.

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MS. AYERS said the original fiscal note anticipated operating costs of \$275,000/year, but for this fiscal year they had a \$283,000 budget. The additional support costs are undetermined, and the program has unallocated overhead costs of about \$28,000, for a total of \$310,000.

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ROBIN CORNFIELD, Vice President, Communications and Marketing, Nana Development Corporation, Nana Regional Corporation, said she supported SB 23. It helps create a new industry - that of making movies - in Alaska that is a renewable resource. They support expanding the film tax credit incentive as it will lead to further economic expansion and private sector jobs. Nana Development Corporation's investment in Alaska's film industry is a natural. They are an Alaskan company focused on creating training opportunities and jobs for their shareholders most of

whom live in Alaska. They also have the expertise necessary to support the industry.

She said that Nana is investing in building the infrastructure for a film industry in Alaska, and this expanded tax credit is a key to its success. Last September, they partnered with Evergreen Films that has invested \$10-million in a studio in Anchorage specializing in 3-D films for a general audience, and they are currently filming an animated dinosaur movie there using real Alaska as a backdrop.

She said that in order to support this industry Nana is creating a new company that will provide one-stop shopping for companies making movies in Alaska. Nana already has the expertise in many fields that are necessary for the film industry from catering to security, transportation logistics, construction, mobile surveying and lodging.

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She said WHPacific uses light detection and ranging radar technology, called LIDAR [Light Detection And Ranging], for the purpose of surveying roads, but Evergreen Films found it could be used in developing the animated dinosaur movie. It does surveying faster than the traditional method. She brought this up because it was a surprise to find out that one of their companies had technology that another one of their companies could take advantage of. So, WH Pacific, a Nana company, is now involved in marketing its new-found film services business to other studios and production companies. This is one example of the unknown benefits of Alaskans working with the film industry.

MS. CORNFIELD said Nana spent a long time studying the industry before choosing to invest in it. They discovered that domestic consumer spending for filmed entertainment has grown year over year over the past decade including 2008 and 2009 which were recession years, and that during those years spending also increased. They also analyzed how the industry might grow and found that the US accounts for 6 percent of the world's population and approximately 50 percent of the consumer dollars spent on filmed entertainment worldwide. But international markets are becoming more important and are expected to continue to outpace domestic growth in the near future.

Vancouver is one example of the impact a tax incentive and investment in the film industry can have, she said. Starting with a little TV show in 1994 called "X-Files," it has seen movie production values grow from \$400 million to more than \$1.2

billion, and the industry has helped create more than 20,000 jobs.

MS. CORNFIELD said because they believe so strongly in the future of Alaska's film industry, Nana Evergreen and other private sector partners have begun investigating the possibility for developing a sound stage in Anchorage. This, along with the tax credit, they feel, will encourage more producers to come to Alaska.

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MS. CORNFIELD showed a slide of a five-year period from the beginning of creating a film until it is released. The production takes about three years and then filming begins. So, lengthening the timeline for projects to qualify from 24 to 36 months (included in the legislation) will help attract more producers to use Alaska as a location. Expanding the dollars allowable under the tax credit from \$100 million to \$200 is important as well, as it will allow the industry to grow in Alaska as the infrastructure grows.

She said Nana's mission is to improve the quality of life of its people. It has a simple overall strategy to invest in companies with potential for growth and to look for opportunities that will provide training and jobs for shareholders. She said the foundation for this growing film industry started with the original Alaska film production incentive program, but the future success of the industry is based upon movie producers choosing Alaska over several other states and countries in which to shoot their films. "Everybody Loves Whales" and the economic impact of filming in Alaska is a good success that can be built upon. Alaska resident wages were more than \$4 million; goods and services purchases were above \$7.5 million. Alaskans were in front of and behind the camera, 12,000 hotel rooms were used and more than 8,000 days of rental cars were purchased.

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DEBORAH SCHILDT, Alaska Crew Training, and Bryce Habegar introduced themselves. Ms. Schildt said they both supported SB 23. She said she is a co-founder and program administrator for an educational 501(c)3 called "Alaska Crew Training, Inc." She said their training program would not exist except for the success of Alaska's film incentive bill.

MS. SCHILDT said her background is film school in Canada, then a move to Los Angeles where she started in the film business on features like "Goonies" and "My Girl." After 20 features, 200

commercials and 28 years later, she calls Alaska home. This past year she was one of two Alaskan casting directors on "Everybody Loves Whales."

In 2009 with passage of Alaska's film incentive bill they saw a need for training a larger workforce. AFG wasn't interested at that time, so Alaska Crew Training was formed. Now, according to a recent article in the Anchorage Daily News one would have to watch TV 24 hours a day for two weeks straight to see every new episode of Alaska-based reality programming since "Deadliest Catch" first launched in 2005. No other state has more cable shows per capita than Alaska. "We've entered our next gold rush," she said. "It's Alaskan-based stories shot here and shown around the world."

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She said an executive producer on "Everybody Loves Whales" gave her this list when asked what the industry was lacking:

- a film office fully engaged with a website that really works for producers
- a sound stage, more equipment
- more infrastructure
- and a larger trained workforce

A trained workforce needs a basic understanding of how film production works and on-the-job training opportunities. She said 49 out of 63 speaking roles in "Whales" were cast with Alaskans who earned a combined income of over \$160,000; two Alaskans landed lead roles and earned over \$20,000 in seven weeks, two others over \$16,000. They came from communities across Alaska, not just the big towns.

When "Act 1" formed in 2009 they looked at other film training programs to help them come up with a basic program that could grow with the industry. It was foolish to train workers without projects, so they held off offering classes until they knew there were jobs coming into the state. In 2010 their Production Bootcamp 101 was launched. To date six Bootcamps have been held and nearly 100 people have gone through them. The Bootcamps will be continued in 2011 and they hope to branch out beyond Anchorage with on-line offerings and start Level 1 and Level 2 courses with instructors from the American Film Institute. She related how local people successfully started training and found careers by working on "Whales." She related how many people are taking classes and working on productions like "Ghost Vision."

MS. SCHILDT said many Alaskans have migrated outside of Alaska for schooling, for jobs and careers in the business, but she thought the incentives might give them a chance to come home and find work in the industry here. Their vision is to continually increase their class offerings - starting with entry level jobs because Alaska has a limited pool of seasoned experienced workers. Their Level 1 and Level 2 classes are best suited for individuals who already have some on-the-job training and are looking to increase their skill sets. They are headed toward deepening Alaska's crew base to accommodate two large features at the same time by building up to 500 graduates over the next three years. She said while they have been recognized by the Alaska Film Office as a training resource for crew, all Alaskans can continue to work together on building a workforce.

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WOODRUFF LAPUTKA, film maker and graduating student from UA Anchorage, said he supported SB 23. He described some of the opportunity it has brought about. He was a journalism/public communications major and found he liked working with film making. When he found that there weren't enough programs capable of supporting his interest in filming, he attended the University of Sterling in Scotland for one year working with BBC and Channel 4 professionals to gain that experience. He returned to Anchorage and is now finishing his BA in journalism, but with a vast added interest in the future of Alaska's film industry.

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He said this state has a rich culture in pioneering, and the interesting thing about the film industry up here is that it acts just the same as anything else. You have pioneers who take those "pie in the sky ideas" and make them reality. In Alaska, in particular, the infrastructure is so new that anybody can contribute and become a pioneer. As a graduating student and a young man, Mr. Laputka said, he wants to make his career in Alaska. The opportunities are now here. Plenty of productions came through in the fall and even more are coming through in 2011. A vast amount of material is being developed here.

MR. LAPUTKA said as a film maker, he looks for being able to work in an area that can pay his bills but also that is conducive to what he requires. One thing that will keep him in Alaska is extending the film tax incentives and, for one main reason: it will better enhance the opportunities for establishment of a functioning infrastructure so that they can express not only their art but also their business.

He said the various components of the infrastructure are being pieced together so that it will function well. It is working similarly to the way it happened in Vancouver 20 years ago.

The University of Alaska Anchorage (UAA) doesn't currently have a film program, but there is a proposal to have one at the University of Alaska Fairbanks (UAF). He related that he created his own program and had it signed off by his professors and department heads. When it came down to the brass tacks and he sought that experience he had to go elsewhere. That does not mean that Alaska doesn't have the ability to satisfactorily supply the kind of experience and education needed in order to establish a film program. It only means that it hasn't developed the focus to create a program like that. Now the focus is here, because the tax incentive is here. Now is when the infrastructure is building.

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Foreign interest and foreign investment is going to be the big bolster in what will decide how the growth and future of this film industry will go. In order for that to occur, more time is needed to insure that they have an interest in coming here and the tax incentive. As a young film maker who originally came from Florida, Mr. Laputka said he has a big interest in continuing his career here in Alaska.

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D.K. JOHNSTON, independent filmmaker in Alaska, said he has been an Alaskan resident since 1997. He moved up originally from south Texas, but he has gained a real big foothold in the state as a film maker. He attended middle school here, graduated from Service High School and obtained his Bachelor's degree in journalism/public communication at UAA in 2006. Later he wanted to pursue his passion of film making and had to leave the state where he obtained his MFA degree in film for the New York Film Academy out of Los Angeles. He got to see how the "Hollywood system" works, and he said that "they love us up here." They are intrigued by the kind of landscapes Alaska has to offer and the talent it has to bring to their personal projects.

He said many in the Anchorage LIO can testify to the pros and cons of getting a film production program at UAF. The staff there has been organizing to implement an education program which would open doors for many Alaskans to train and work professionally in the film production industry. If this program is successfully added into the state's education system, it could help increase the number of trained production crew to

compensate for various productions looking to shoot here, and future film makers would be capable of taking on larger roles in production that could potentially increase local production of motion pictures. Right now the majority of educated and experienced production crew in the state receive their training elsewhere and those who have returned are now doing their best to train others interested in making film production a career.

MR. JOHNSTON said he came back to Anchorage to take part in the film industry because as people have said today, Hollywood is a stepping stone for many productions. The major studios are looking to shoot their films in states like Alaska which offer very nice tax incentives. In order to remain competitive, however, with other states and countries establishing professional crew base and a film degree program in the University of Alaska is an important step in the right direction. He hoped extension of the film tax incentive program would encourage branches of the UA system as well as local school districts to increase their education in film and television production. He summarized: "The more education our state can provide in these fields the more likely we are to encourage other Alaskan students to consider continuing their education and training here at home as opposed to going elsewhere."

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ALLEN ERICKSON, White Fox Studios, said he would let another producer, Larry Golden, take his time to testify.

LARRY GOLDEN, Aurora Films, said he had been making films and television in Alaska for 37 years and has witnessed a lot of productions going on by both his colleagues here in the state and some from outside. He said his work has been nominated for two national Emmy awards and it has appeared on PBS in the national prime time schedule several times; he has won many national film festivals and was the executive producer for the most successful locally financed feature film, "Spirit of the Wind."

MR. GOLDEN said he supported the goal of bringing production companies into the state. Every dollar they spend here is another dollar that goes into Alaskans' pockets and those dollars circulate. But he wanted to see something more happen through this program, which is for legislators to use incentive programs to further incentivize or enable local ownership of more media production companies. He explained when a non-resident production company comes here, they spend money, and

that is good, but if an Alaskan production company owns a production, and it's a commercially successful TV series or feature film, the profits from that distribution stay in Alaska, and that is vitally important.

He said New Mexico has found a way in its incentive program to score points for production companies coming into their state and to adjust the tax benefits in such a way that non-resident companies that use local personnel in key creative positions, such as directors and writers, not just positions as crew or truck drivers, that provides a much greater benefit to the state. It helps ensure that the stories that are told and the way they are told are more realistic and more consistent with the real Alaska. That can be enhanced through the incentive program.

MR. GOLDEN added that in 1976, he was the one who proposed to some legislators that the state legislature create a legislative teleconferencing network. That idea was picked up and he was hired as staff to the task force that set up a demonstration project of teleconferences. They held six audio and three video teleconferences. He said it does his heart good to see it being used for the benefit of people around the state.

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JAMES MCLEAN, independent screen writer, Anchorage, said he moved to Alaska in 1976, and that he had seen a lot of films that were allegedly set in Alaska. And as an Alaskan screen writer he winces every time he sees a deputy sheriff in a county in Alaska because there is no such thing.

SENATOR MENARD joined the committee.

MR. MCLEAN said of the six features he has finished, four were optioned, one is in production, and another is in preproduction. They are using Alaskan crews, actors, producers, and Alaskan money for the most part. One of the reasons he can do "Doppelganger Principal" (a film starring Ed Asner) here, is because of the incentive program. It wouldn't happen without it, because it's too speculative for a lot of people. This program is critical for films to be made in Alaska about Alaska and about Alaskan people.

CHAIR EGAN thanked everyone for their comments and said he would hold SB 23 and continue taking testimony next Tuesday.

SB 64-RESEARCH AND DEVELOPMENT TAX CREDIT

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CHAIR EGAN announced SB 64 to be up for consideration.

CURTIS THAYER, Deputy Commissioner, Department of Commerce, Community and Economic Development (DCCED), thanked them for hearing SB 64. It establishes a 20 percent tax credit for qualified research and development (R&D) conducted by corporate taxpayers in Alaska. In effect the R&D tax credit would stimulate private sector investment, entrepreneurial activity and business expansion in the state while bringing opportunity and associated long-term benefits to the state's economy. This legislation will allow Alaska corporations to receive a 20 percent tax credit not to exceed \$10 million per taxpayer per year. The payroll of the employees must take place in Alaska. To qualify for R&D activities it must meet the following requirements:

- The purpose is discovering information
- Information technology in nature, the application of which is intended to be useful in the development of a new or improved component of the taxpayer; all the activities constitute a process or experimentation. The experimentation is for qualifying activity or purpose.

The bill would impose a reporting requirement on the Department of Revenue so the legislature and the public are aware of the fiscal impact and the economic benefits of the R&D credit to the state.

MR. THAYER explained the way the credit would work is that a percentage of qualified R&D expenditures that exceed the average qualified R&D expenditures for three years immediately proceeding that year for which the credit is claimed. Unused credits will be carried forward for up to seven years after the expenditure for which the credit is claimed. In order to prevent a corporate taxpayer from claiming more than one benefit for a single expenditure, the bill would also provide that a credit may not be claimed for expenditures that the corporation deducted in calculating its tax liability or for which it claimed a federal credit that has been apportioned to Alaska. Examples of activities that would qualify for these credits are the development of new and improved product processes and formulas; development of prototypes for models; building or improving manufacturing facilities; developing or improving software technologies; and development or application for patents. Activities that would not qualify are the exploration activity to assertion of the existence, location, extent or quality of any ore or mineral deposit; duplication of existing

business components, surveys or studies such as market research; advertising. Routine data collection and research into social sciences, art or humanities would not qualify.

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WANETTA AYERS, Director, Division of Economic Development, Department of Commerce, Community and Economic Development (DCCED), said she would amplify a couple of points that Mr. Thayer raised. She reiterated that this is modeled after an existing federal R&D tax credit that was established in 1981. It has been reauthorized 14 times and is currently authorized through 2011. There is a great deal of sentiment on a national level to have it reauthorized permanently. The Internal Revenue Code embodies a four-part test to determine what qualifies as research and development. The activity has to be technological in nature; there has to be some level of uncertainty, there has to be a process of experimentation, and it has to be for a permitted purpose. The idea is that there is some level of product or process innovation that will lead to newly commercialized activity or product.

MS. AYERS said on the national level they may be hearing about the concept of the "innovation agenda." Recently the "America Competes Act" made a number of changes about how economic development is addressed on the federal level. Some key components of this are to accelerate the commercialization of new technologies, products, process and services. Within EDA they have established a new Office of Innovation and Entrepreneurship that is to foster innovation and the commercialization of new technologies, products, processes and services with the goal of promoting productivity and economic growth. She explained that President Obama characterized our nation's goal is to "out-build, out-innovate and out-education and out-hustle the rest of the world" so that we would be economic survivors.

She said that 34 other U.S. states have some form of R&D tax credit or incentive. They don't want to necessarily "compete away" R&D activity from them, but to equalize the playing field. For every \$5 increment in R&D expenditures, \$1 would be credited back.

SENATOR PASKVAN said in the last bill with tax credits they dealt with people from a specific industry, and he didn't see anyone in the R&D industry asking for this. He asked if they were working with anyone in particular.

MS. AYERS replied the concept came out of the Council of Economic Advisors that provides advice to Commissioner Bell and the department. A number of members have seen the credit work in other states. A number of businesses could benefit, but they could not be here today.

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JOHANNA BALES, Deputy Director, Tax Division, Department of Revenue (DOR) said the governor is interested in diversifying the state's economy and believes this is a step in the right direction. Maybe in a few years industries will be saying how great this credit is for them, just like the film incentive.

SENATOR PASKVAN said the other bill had a cap for the incentive, but he saw \$10 million per business here and he wanted to know the thought process behind it.

MS. BALES responded that the process is different. The Film Office certifies those expenditures ahead of time and they have a general idea of what they are looking at to create a cap. When comparing it to other types of credits, it's very difficult to pigeonhole R&D expenditures for an entire group of corporate income taxpayers. For instance, they could cap it and then find out after three months that they have run out of money; this type of credit doesn't lend itself to the pre-approval process.

SENATOR PASKVAN said he was trying to get an understanding of what 20 percent is now and what it would be three years from now. As he understands it now they get to deduct 100 percent of their expenditures; so do they get an additional 20 percent credit?

MS. BALES answered no; if they take the credit they can't also take the expenditure. They can't get both. She explained that they are hoping to attract new corporate income tax payers, because the only time they would get the credit is if the R&D activity actually increases in the state. So, if you are someone who is already conducting R&D activity in the state and you increase it this year, you will get a credit for 20 percent of that increase. But if you are someone who has never operated here, your base is going to be zero. So, any new R&D you do, you would get 20 percent of all expenses.

SENATOR GIESSEL said Ms. Bales frequently talks about corporations, and asked if this credit would also apply to an individual.

MS. BALES answered no; just corporations. Individuals don't pay an income tax in Alaska.

SENATOR GIESSEL said she was thinking about Alaska Aerospace Corporation that wants to attract some corporations to Alaska to do some launches. If those corporations are doing some innovative research, would they qualify for this kind of tax credit?

MS. BALES answered they may if they meet the qualifications.

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SENATOR MENARD said it dawned on her that grandfathering in this case is a negative, because if a company already invested and is already going, it won't be given the same credit.

MS. BALES said you could look at it that way, but established companies have been able to enjoy the federal tax credit which Alaska does apportion to their corporate income tax. The intent of this legislation is to increase the activity that is happening right now, if they can partner with those that are already here and also bring new industry to Alaska.

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SENATOR PASKVAN said he assumed a company doing R&D would be deducting the payrolls, rents and all their costs on its federal income taxes, and then they get the credit component. So, if they can't take the deduction and only take the expense, how would that work?

MS. BALES explained that in the calculation of state tax, Alaska starts with federal taxable income. They would be required to add those expenses back, so it would increase their taxable income. Then they would be allowed to take a 20 percent credit but only for those expenses they added back in. So, all of their R&D expenses would be allowed to be deducted. Depending on the tax bracket a taxpayer is in and how they are operating, it might be more beneficial for them to take the deductions and the federal credit that passes through versus the Alaska credit. Generally speaking, credits are more favorable because they are dollar for dollar. She added that Alaska has a 9.4 percent top corporate income tax rate versus a 20 percent tax credit dollar per dollar. To be honest, she said, this is a fairly innocuous credit, and they will see how it works before doing anything else.

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SENATOR MENARD asked what other states do not have a state income tax.

MS. BALES answered Nevada, Wyoming, Florida, South Dakota and Washington.

SENATOR GIESSEL asked why the mineral industry gets no credit for R&D.

MS. BALES explained that this legislation basically piggybacks the qualifications under federal law and that is stipulated in federal law.

SENATOR GIESSEL asked how the credits would work with the petroleum industry and R&D in processing heavy oil since it's an innovative unknown.

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MS. BALES replied if that activity would qualify under federal law, it would qualify here as well. She said they would like to present an amendment.

SENATOR PASKVAN said he was still struggling with understanding the recalculation of gross income under the federal tax, calculate an Alaska percentage and then apply 20 percent of this limited number as a credit, and asked if any other state does that.

MS. BALES replied that the state does this with several other programs as well; for instance, the education tax credit where one is also not allowed to take the contribution deduction if the credit is taken. So, they start with the federal tax and add back that contribution amount. Then they are allowed to take the education credit. There are other modifications to federal taxable income that happen, as well, for differences in federal and state income tax.

SENATOR PASKVAN said he was still trying to understand what the numbers would be and what they would mean.

MS. BALES added this is a corporate income tax that is widely used in most other states. Most corporations are well aware of it, and that is why they have a large tax staff.

SENATOR PASKVAN said he wanted to know if this promotes the attorney's industry more than the R&D industry.

MS. BALES explained that it is truly just a line item on a return that gets added back and recalculated. It is done frequently and most taxpayers are set up to deal with these kinds of anomalies.

MS. BALES said she had an amendment that deletes all of (e) on page 2, lines 12-25 and insert new language.

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SENATOR PASKVAN moved to adopt conceptual Amendment 1.

CONCEPTUAL AMENDMENT 1

TO: SB 64

BY: The Department of Revenue

Page 2, line 12: delete "names" insert "number"

Page 2, line 16: after "credit." insert "The department may only report this information if three or more taxpayers claimed the credit in the prior year."

The subsection would then read:

"(e) Each year, the department shall report the number [NAMES] of taxpayers who claimed credits under this section in the prior year, the total cumulative amount of credits granted to all taxpayers under this section for the prior tax year, and the total cumulative number of employees conducting the research and development for which all taxpayers claim the credit. The department may only report this information if three or more taxpayers claimed the credit in the prior year."

SENATOR DAVIS objected for discussion purposes. She asked why the amendment is needed.

MS. BALES responded that the department does not generally disclose tax information, especially when talking about R&D which could be proprietary. Language would also identify taxpayers and the level of activity they are doing could be disconcerting and actually make them not want to participate in this program. The new language would protect that confidentiality.

CHAIR EGAN said SB 64 would be held for further work.

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There being no further business to come before the committee,
Chair Egan adjourned the meeting at 3:01 p.m.