

HOUSE FINANCE COMMITTEE  
March 23, 2017  
9:21 a.m.

9:21:24 AM

CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 9:21 a.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair  
Representative Paul Seaton, Co-Chair  
Representative Les Gara, Vice-Chair  
Representative Jason Grenn  
Representative David Guttenberg  
Representative Scott Kawasaki  
Representative Dan Ortiz  
Representative Lance Pruitt  
Representative Cathy Tilton  
Representative Tammie Wilson

MEMBERS ABSENT

Representative Steve Thompson

ALSO PRESENT

Taneeka Hansen, Staff, Representative Paul Seaton; Brandon S. Spanos, Deputy Director, Tax Division, Department of Revenue; Representative Colleen Sullivan-Leonard.

PRESENT VIA TELECONFERENCE

SUMMARY

HB 115 INCOME TAX; PFD CREDIT; PERM FUND INCOME

#hb115

HOUSE BILL NO. 115

"An Act relating to the permanent fund dividend; relating to the appropriation of certain amounts of the earnings reserve account; relating to the taxation of income of individuals; relating to a payment

against the individual income tax from the permanent fund dividend disbursement; repealing tax credits applied against the tax on individuals under the Alaska Net Income Tax Act; and providing for an effective date."

[9:22:16 AM](#)

Co-Chair Seaton MOVED to ADOPT proposed committee substitute for HB 115, Work Draft (30-LS0125\L, Nauman, 3/22/17).

Representative Guttenberg OBJECTED for discussion.

[9:22:59 AM](#)

TANEEKA HANSEN, STAFF, REPRESENTATIVE PAUL SEATON, reported that the CS incorporated the amendments adopted by the committee. There were several new sections. She read the Summary of Changes (copy on file) from version E to version L:

Title - On line one the title has been expanded to include "relating to the permanent fund; relating to the procurement by the Alaska Permanent Fund Corporation; relating to the management of the budget reserve fund" and on line five "individuals, partners, shareholders in S corporations, trusts, and estates."

New Section 2 - Add a new subsection (1) to AS 36.30.015 to direct the trustees of the Alaska Permanent Fund Corporation to adopt regulations regarding procurement.

She reported that new sections 2 and 3 were related to Amendment 11 offered by Representative Pruitt and continued to read the summary of changes:

New Section 3 - Amends AS 36.30.990(1) to add the Alaska Permanent Fund Corporation to the list of entities excluded from the definition of 'agency' for the purposes of the state procurement code. This exempts the corporation from the requirements in the state procurement code.

New Section 4 - Amends AS Sec. 37.05.055(b) to conform to the changes made in section 6.

Ms. Hansen elaborated that section 6 had to do with Amendment 5 that took the royalties above the constitutionally required 25 percent and deposited them in the general fund (GF). She read New Section 5:

New Section 5 - Amends AS 37.10.430(c), relating to the subaccount in the constitutional budget reserve fund, to remove the requirement that any funds invested in the subaccount shall be invested under the assumption that those funds will not be needed for at least five years.

Ms. Hansen related that Section 5 was related to Amendment 12. She turned to the following sections:

New Section 6 - Amends AS 37.13.010(a) and deletes AS 37.13.010(a)(2). The resulting change means that the Alaska Permanent fund will be filled by the constitutionally required 25 percent of all mineral lease rentals, royalties, royalty sale proceeds, and net profit shares. The additional 25% of royalties from leases issued after December 1, 1979, which are above the constitutionally required 25%, will now remain in the general fund and will not be deposited into the permanent fund.

Section 8 - Amends AS 37.13.140(b), created by this act, to change the amount available for distribution from the earnings reserve to be 5.25% of the average market value (POMV) of the permanent fund. [This rate of distribution will be in effect from July 1, 2018 through the June 30, 2019. Also adds a technical change to include the fiscal year just ended in the average market value of the fund instead of excluding the fiscal year just ended.

Ms. Hansen noted that section 8 and section 9 was related to Amendment 1.

Section 9 - Adds a new section to further amend AS 37.13.140(b) which will reduce the amount available for distribution from 5.25% to 5% of the average market value (POMV) of the permanent fund. This change is effective July 1, 2019 and will replace the distribution rate created in the previous section.

Section 10 -Adds a new subsection to AS 37.13.145(b) which states that each fiscal year the legislature will transfer an amount equal to 0.25 percent of the market value from the earnings reserve account to the principal of the fund. Includes a technical amendment on lines 16 and 17 to change "income" to "amount."

Ms. Hansen delineated that the transfer was an internal transfer from the fund and not taken from the 5.25 percent POMV calculation. Section 10 was related to Amendment 1. She continued with section 12 related to Amendment 7:

Section 12 - Amends AS 37.13.145(e), created by this act, to clarify that the amount available for appropriation to the principal of the fund when the earnings reserve account exceeds four times the amount calculated in AS 37.13.145(b) is the lesser of the amount in excess of that calculation or the amount necessary offset the cumulative effect of inflation since the last inflation-proofing transfer occurred.

New Subsection (f) is added to AS 37.13.145 to state that the legislature shall appropriate from the earnings reserve account the additional amount, if necessary, to provide for a per person dividend of \$1,250 per eligible Alaskan. This additional appropriation is in effect for fiscal years 2018 and 2019. [This subsection is repealed at the end of fiscal year 2019.]

Ms. Hansen reviewed the following sections:

Section 13 - Further amends AS 37.13.145(e), previously created by this act, to remove references to subsection (f). Subsection (f), created in the previous section, is repealed on June 30, 2020 (the last day of fiscal year 2019). This new version of AS 37.13.145(e), without the references to (f), becomes effective on that date.

Ms. Hansen reported that subsection (f) and Section 13, which conformed to the repeal of the two-year minimum dividend were related to Amendment 3.

-----Start of Income Tax section-----

Section 16 - This section, allowing an exemption from the requirement to file a tax return electronically, was previously included in the bill. It has been amended to reference AS 43.22.070(h), which is now the section of statute which exempts individuals from the electronic filing requirement.

Section 17 - Previous section 11 of the bill, which created an individual income tax based on federal tax liability in AS 43, has been replaced with section 17. Section 17 creates an individual income tax based on adjusted gross income. The subsections of this chapter have been modified to reflect this change in tax base and to include certain administrative authorities.

Ms. Hansen explained that section 16 and section 17 were not related to prior amendments.

-----End of Income Tax section-----

[9:30:27 AM](#)

Representative Wilson asked where the Section 17 language originated. Ms. Hansen reported that she worked with the Department of Revenue and was derived from and in response to the testimony of Mr. Ed King and the Institute of Social and Economic Research (ISER). She summarized that the testimony warned against an income tax based on federal liability, which made revenue vulnerable to changes to the federal tax code. In addition, some public members had expressed concern with certain deductions and credits associated with the federal tax liability. Finally, in the original version of the bill there was a 10 percent tax on capital gains to address a disparity between long-term capital gains and other income. The tax did not accomplish its intent and by changing to adjusted gross, capital gains were treated like any other income. Therefore, a separate tax was not necessary.

Co-Chair Seaton noted prior testimony that recommended an income tax based on adjusted gross income. He interjected that when crafting the CS, he worked with the Department of Revenue (DOR) who had previously hired a national consultant to draft income tax legislation based on adjusted gross income. The CS incorporated some of the language.

Representative Wilson remarked that the testimony he referred to was invited and not public testimony. She referred to a document ["State Personal Income Tax Revenue as a Share of Personal Income in States with Broad-Based Personal Income Taxes" by the Institute on Taxation and Economic Policy (ITEP) (copy on file)] that ranked the state the fourth highest in the nation with the proposed income tax.

Ms. Hansen corrected Representative Wilson's statement and reported that the proposed income tax ranked Alaska the 4th lowest income tax in the nation, the same as the previous version based on federal liability.

[9:34:48 AM](#)

Vice-Chair Gara referred to page 7 of the CS that contained the proposed tax brackets. He indicated that if income is less than \$10.3 thousand the tax is zero. However, a tax was not owed if income was under \$14.3 thousand. He asked her to explain why. Ms. Hansen responded that the brackets applied to the income considered taxable and the bill included a personal deduction of \$4 thousand per person.

Co-Chair Seaton acknowledged Representative Colleen Sullivan-Leonard in the audience.

Vice-Chair Gara clarified that taxes were calculated on the amount of income over the tax bracket limit. He exemplified that taxes were owed on the amount of income above \$14.3 thousand; the \$14.3 thousand remained tax free. Ms. Hansen replied in the affirmative and added that it was the same as how the federal income tax was calculated.

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Ms. Hansen continued to read the summary of changes:

New Section 18 - Adds a new subsection (c) to AS 43.23.025, relating to the calculation of the permanent fund dividend, to state that for fiscal years 2018 and 2019 the amount of the permanent fund dividend shall be at least \$1250. [This section is repealed at the end of fiscal year 2019].

New Section 19 - Amends AS 43.23.055(1) to clarify that the department of revenue will annually pay

permanent fund dividends from the dividend fund without further appropriation.

Ms. Hansen stated that Amendment 6 was related to section 19 and read New Section 23:

New Section 23 - AS 37.13.145(f) and AS 43.23.025(c), both created by this act, are repealed on June 30, 2020. These subsections relate to the minimum dividend of \$1250 which is set of fiscal years 2018 and 2019 only.

Representative Guttenberg asked about new section 20. He wondered whether the ballot initiative on voter registration was affected by the provision. Ms. Hansen replied in the negative and added that section 20 was renumbered in the CS. She offered that the section authorized a tax payer to use their dividend to pay income tax liability via a check box on the tax form.

[9:42:13 AM](#)

Ms. Hansen continued reviewing the summary of changes:

New Section 24 - Creates a new section in uncodified law which sets the amount the legislature may appropriate from the earnings reserve account for fiscal year 2017. The amount is equal to 5.25 percent of the average market value of the fund, minus \$695,650,000 which is the value of the permanent fund dividends already paid from the earnings reserve account for fiscal year 2017.

Ms. Hansen noted that section 24 was related to Amendment 2. She addressed Section 26:

Section 26 - Additional transition language is included in new subsection (b) to allow the commissioner of revenue and the Alaska Permanent Fund Corporation to adopt the necessary regulations to implement this act.

Ms. Hansen reported that Section 26 correlated to Amendment 11 and was related to the Procurement Act. She read the following:

Sections 27 - 33 -Effective dates: Various conforming amendments are made to the effective date sections to

reflect the new sections that have been added to this bill. The effective date of section 17, addressing the income tax, is now January 1, 2019. Unless otherwise specified, this bill now has an effective date of July 1, 2017.

Ms. Hansen indicated that currently the only section that had an immediate effective date was section 24 and related sections and section 1. The effective date of the remainder of the provisions was July 1, 2017. She related that the 2019 effective date for the income tax was DOR's preferred effective date.

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Representative Wilson could not find the section referring to personal exemptions. Ms. Hansen responded that the provisions were found in AS 43.22.030 beginning on page 12, line 8 of the bill. Representative Wilson wondered why the deductions applied to both residents and non-residents. Ms. Hansen responded that the exemption fell under equal protection guidelines and had to be offered to both. However, on certain items like the deduction of the Permanent Fund Dividend (PFD) a resident only reduction was allowable. She reported that Vermont had residential only deductions related to property owners, but the tax system was extremely complicated. She was examining whether the value of a non-residents exemption may be reduced.

[9:48:36 AM](#)

Ms. Hansen turned to a higher-level discussion of the income tax portion of the bill. She believed adjusted gross income was a much simpler way of approaching a capital gains tax. She addressed a brief history of the original income tax put into place in the 1970s. She relayed that in 1975, the state switched to a tax system similar to the current proposal, in response to significant changes to the federal tax brackets that had reduced Alaska's tax revenue. One of the benefits of changing to an adjusted gross income tax was the allowable exemption of the PFD from a state tax.

Representative Wilson alerted the sponsor that she would be asking how the income tax related to trusts. She indicated that Alaska had been an attractive state for entities to do business because of its tax structure regarding trusts. She

noted that native corporations were exempt because of federal law. She wanted to ensure some parity existed for non-native corporations. Ms. Hansen added that "C" corporations would not be taxed, but S corporations or pass through corporations and partnerships were subject to a tax.

Co-Chair Seaton interjected that that the tax was a personal income tax and not a corporate income tax. He explained that "S" corporations passed income through to individuals. He asked Ms. Hansen to proceed to the sectional analysis ["HB 115: State Revenue Restructuring Act Version: L Sectional Analysis- Long Version" (copy on file)] and discuss the personal income tax and how the tax was structured. Ms. Hansen reminded the committee that the income brackets applied after deductions. She highlighted that the key sections of the income tax portion of the bill were: AS 43.22.010 that established the tax brackets, AS 43.22.30, which defined the taxable income and contained the exemption language, AS 43.22.045 that defined Alaska sourced income specifying the taxable income of nonresidents, and 43.22.150 that contained the section's definitions. She furthered that sections 070 through sections 095 were the administrative sections and were similar to the sections contained in the original version. Finally, sections 040, 050, 055, 060, and 065 provided guidance and authority to DOR for specific situations of taxable groups.

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Ms. Hansen moved to the sectional analysis and began with Section 17 beginning on page 7 of the CS:

-----Start of Income Tax section-----

Section 16 (page 7, line 5) - AS 43.05.045(a) clarifies that there is a penalty if a state income form is not filed is not filed electronically. However, individual filers are exempt from this penalty as noted later in AS 43.22.070(h) - (see page 20, line 27).

Section 17 (page 7, line 15) - Creates the Individual Income Tax within AS 43.22  
Sec. 43.22.010 (page 7, line 17) - Imposes a progressive income tax on residents and nonresidents

on their taxable income. Taxable income, defined later in this chapter, is based on federal adjusted gross income with some state specific modifications. Residents are taxed on all taxable income, while nonresident individuals will be taxed on income from a source within the state.

Subsection (b) outlines the income tax brackets for an individual.

Ms. Hansen described how the tax brackets worked listed on page 8 of the CS. She expounded that the brackets worked the same as the federal tax brackets.

Vice-Chair Gara asked whether the \$4 thousand deduction applied to all dependents. Ms. Hansen responded in the affirmative. Ms. Hansen continued with subsection (c):

Subsection (c) outlines the income tax brackets for two individuals who file jointly; those who are eligible to file a joint federal income tax return are eligible to file jointly in the state. Under subsection (d) and (e), those that are eligible to file a joint return federally but do not do so are directed how to file on the state level.

Ms. Hansen pointed to an error on page 8, line 8 of the bill that listed the tax brackets for joint filers. She noted that instead of \$22.6 thousand the correct number was \$20.6 thousand. The \$2 thousand error carried through to each subsequent bracket. Ms. Hansen continued with subsection (d) and (e).

In response to a question by, Representative Guttenberg, Ms. Hansen replied that a couple must choose whether they want to file jointly or each individually. She continued with subsection (f):

Subsection (f) describes how two individuals who filed a joint federal return but who are not both residents of Alaska shall file with the state. They may choose to file separately, as nonresidents, under the tax brackets described in (b) of this section, or they may elect to file jointly under the brackets in (c) but only if both choose to be taxed as residents.

Sec. 43.22.015 (page 9, line 1) - Describes how a nonresident individual will determine their Alaska

state income tax due. Their tax is determined on all of their taxable income, using the brackets in 43.22.010(b). That tax is then reduced by a ratio based on how much of the nonresident's taxable income is from a source within the state. [Nonresidents who choose to file jointly are not eligible to use this allocation of income, and are instead considered as residents.]

Representative Guttenberg read the definition of "nonresident individual" on page 25, line 10 through 11 of the bill:

"nonresident individual" means an individual who is not a resident of the state for any portion of the taxable year.

Representative Guttenberg wondered how that applied to individuals who worked in the state for more than 30 days and were then considered a resident. Ms. Hansen relayed that the definition of residency was dependent upon the definition of "domiciled."

Representative Wilson wondered whether non-residents and resident could choose whether to file jointly or as individuals. Ms. Hansen responded that both non-residents and residents had the same choice. She explained that whether a nonresident couple filed jointly was affected by the allocation of income determined by the ratio for an individual or file jointly as residents eligible for the resident credit against income taxes paid in other states. She continued with Sec. 43.22.020.

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Sec. 43.22.020 (page 9, line 11) -Defines the tax on trusts and estates. Resident trusts are taxed at 7%, except for Alaska Native Settlement trusts. Alaska Native Settlement trusts receive alternative federal tax treatment and are taxed at 2.5% by this state income tax. Nonresident trusts are also taxed at 7% but only on their income that is connected to a source in the state.

Ms. Hansen elaborated that subsection (b) on page 9, line 18, applied to trusts that were "housed" in Alaska but lacked a taxable connection in the state and were not

subject to a tax. She noted that the provision was added in response to concerns raised in public testimony.

Co-Chair Foster asked for clarification regarding Alaska Native Settlement trusts. Ms. Hansen answered that the trusts were outlined specifically in the federal code. She deferred to DOR for a definitive answer. Ms. Hansen continued with the sectional analysis.

Sec. 43.22.025 (page 9, line 28) - Provides a credit to residents for taxes paid to another state based on income earned in that other state (so someone is not taxed twice on the same income). A credit for income taxes paid in another state cannot reduce the tax due to Alaska below what it would have been if the out of state income was never included in the calculation of the tax due. This means that regardless of the amount of income tax the resident paid in other states, the credit cannot reduce the amount of income tax due to Alaska below what the resident individual would owe on just the income that is not taxed by other states.

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Sec. 43.22.030 (page 11, line 9) - Defines the income that is considered taxable income under this chapter. This is based on the federal adjusted gross income with specific few items added and subtracted. Specific to Alaska, this section allows a per person exemption of \$4000 and also allows the permanent fund dividend to be deducted from state tax.

Items added into federal adjusted gross income include: interest and income from state and municipal bonds and certain United States bonds which are not taxed by the federal government but which are taxable by the states; deductions from federal adjusted gross income for Alaska income taxes (normally deducted *after* adjusted gross income); gain from a trade of like-kind properties which is not federally recognized or taken as a gain; and any deductions allowed to federal adjusted gross income which relate to income that is not being taxed under this chapter.

Items subtracted from federal adjusted gross income include: interest or income from federal bonds which are not legally taxable by the states; refunds for

overpayment of an income tax; expenses that are not deducted from federal adjusted gross income but that relate to income taxed under this chapter; a gain from a trade of like-kind properties that is federally recognized as a gain; nonresident pension income under 4 U.S.C. 114; military compensation for nonresidents; the permanent fund dividend; and \$4000 per individual claimed that is an exemption on the federal income tax forms.

Subsection (b) states that expenses not used in the tax year they were incurred may not be carried back to previous year returns, and may only be carried forward for a total of five years.

Ms. Hansen relayed that subsection (D) under this subsection on page 11, line 20 of the bill would tax "a gain realized but not recognized under 26 U.S.C. 1031 (Internal Revenue Code). She added that the provision allowed an individual to trade a piece of property or asset and the state would similarly not tax the transaction. Subsection (E) on page 11, line 22 provided that "a deduction allowed in the determination for the federal adjusted gross income that is related to income that is not taxable under this chapter" meant that the state would disallow the deduction. She delineated that Section (2) of Section 43.22.030 specified items that were prohibited from taxation under federal law. She communicated that federal bonds, Alaska pensions received by nonresidents and income from nonresident military personnel were exempted. Two additional exemptions were added including the Permanent Fund Dividend (PFD) and the \$4 thousand personal exemption.

Representative Wilson asked for clarification regarding taxing pensions. Ms. Hansen explained that a pension was taxable in another state other than the state it originated in. She exemplified that if an individual with a pension from Washington state moved to Alaska, Washington was prohibited from taxing the pension, but Alaska could tax the pension. Representative Wilson asked about social security. Ms. Hansen replied that a portion of social security was exempted from adjusted gross income as defined by the federal level.

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Representative Pruitt asked for a list of all the potential exemptions. He wondered if the proposed income tax base was an individual's federal adjusted gross income. Ms. Hansen responded that federal adjusted gross income was the base including the exemptions specifically listed in Section 43.22.030. She added that HB 115's taxable income was defined as federal adjusted gross income with the specific Alaska changes in the bill. Representative Pruitt asked about mortgage interest. Ms. Hansen responded that mortgage interest was deducted at the federal level. Representative Pruitt deduced that mortgage interest was not an allowable deduction under the proposed Alaskan income tax. Representative Pruitt ascertained that charitable deductions were also not deductible. Ms. Hansen replied in the affirmative. Representative Pruitt asked whether wealthy people in Alaska could reduce their taxes to a very low liability. Ms. Hansen answered that capital gains income was considered equal to other forms of income under an adjusted gross tax and one reason the bill was changed to a federal adjusted gross income system.

Representative Grenn asked where military pensions fell under in the bill. Ms. Hansen replied that it would depend on the person's residency status. If a person was an Alaska resident, the federally taxable portion of the military pension included in the federal adjusted gross income was taxable in Alaska. She furthered that the tax was not relative to where the pension was generated.

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Vice-Chair Gara thought that the limited list of deductions was a "smarter" way to administer the tax. He remarked that under the federal method with numerous deductions, many interest groups would want exemptions "and HB 115 would become a free-for-all." He favored the income tax approach in the CS. Ms. Hansen replied that some of the public comments the sponsor had received were concerns about loopholes in the tax and was the reason the deduction list was short.

Representative Wilson referenced the chart [titled "State Personal Income Tax Revenue as a Share of Personal Income in States with Broad-Based Personal Income Taxes" (copy on file)]. She used Missouri as an example - it allowed numerous deductions and was ranked 16 with a 2.33 percent effective tax rate. She wondered whether the same

deductions were considered. Ms. Hansen answered that the chart had been generated by the Institute on Taxation and Economic Policy (ITEP) and the percentage was based on the amount of personal income in the state and the amount of revenue from the tax; the percentage of tax revenue out of the total personal income. She furthered that it did not matter what the tax rate was, it mattered how much revenue was generated and how it compared to the amount of overall income in the state. Representative Wilson thought the information was entirely different than she had initially believed. She thought that the chart's ranking meant that Alaskans had a lower tax liability than Missourians. She was not sure the chart was accurate. Ms. Hansen answered that "on average" the chart was true, however because the proposed income tax had multiple tax brackets, in some cases the tax bracket may be higher or lower than another state. She delineated that the bill directed the department to inflation adjust the brackets and exemption every two years. Many states did not inflation adjust, and many residents ended up paying under higher brackets. Representative Wilson reiterated that she understood the chart differently than represented.

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Ms. Hansen answered that Carl Davis from ITEP had generated the chart and they planned to have him address the issue later next week.

Vice-Chair Gara pointed to the footnote on the chart and detailed that the data accounted for the differences. Ms. Hansen replied that her understanding was the model was based on the overall effect and the deductions were removed.

Co-Chair Seaton stated the chart was on the effective tax rate and not the statutory tax rate. He noted that a tax system could include a statutory tax rate with numerous deductions to account for the effective tax rate. The chart represented the effect on the entire population and the amount of income tax paid. He explained that "personal income was divided by the total number of taxes collected in the state based on distribution."

Ms. Hansen continued with the following sections:

[10:28:13 AM](#)

Sec 43.22.035 (page 12, line 23) - Describes how income from a partnership or an s-corporation shall be adjusted based the additions and subtractions of taxable income under 43.22.030. Subsection (c) states that if partnership income is allocated with the specific purpose of evading taxes, that allocation shall be disregarded.

Sec. 43.22.040 (page 13, line 17) - Describes how income from a trust or estate shall be adjusted based the additions and subtractions of taxable income under 43.22.030. Taxable income is reduced by the amount distributed to the beneficiaries, in accordance with U.S.C 661. The Department of Revenue may determine in regulation how the adjustments to income will be allocated between the trust or estate and the beneficiary of that trust or estate. Subsection (b) states that if income or loss is distributed with the specific purpose of evading taxes, that distribution shall be disregarded.

Ms. Hansen noted that the regulations for both sections would be written by the department.

Sec. 43.22.045 (page 13, line 31) -Identifies items of income that are included as being derived from or connected with a source in the state. This is the income on which nonresidents will be taxed.

Ms. Hansen reported having a similar section in the original version of HB 115 to better define the range of income connected with a source in the state.

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Representative Pruitt reverted to "S" corporations and asked whether deductions for losses were allowable. Ms. Hansen responded that if the S corporations could not carry the loss back, but the operating losses could be carried forward for 5 years. Representative Pruitt mentioned a scenario where an "S" Corporations requested an extension to file taxes and paid an estimated amount upfront. He asked whether the corporation could request a refund for overpayment under the scenario. Ms. Hansen surmised that the provision was related to prior tax years rather than pre-payments made. She noted that the bill defined "calendar year" as calendar year or fiscal year in

recognition that S corporations and partnerships file on a fiscal year.

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Representative Pruitt queried what would happen if an S corporation adjusted a past return and were owed a refund. Ms. Hansen responded that the administrative section of the bill specified that if the corporation filed an amended return with the federal government the amended return would be transmitted to the state and DOR would adjust the return. She clarified that the provision he referred to stated that an expense from the current year could not be applied to profit from two years ago.

Ms. Hansen added that Florida did not have a personal income tax but expanded their corporate income tax to include S corporations and partnerships. She shared that Alaska's exemption for S corporations and partnerships in corporate tax law was included when the state had an individual income tax. When the state repealed the individual income tax it did not repeal the exemption. She continued to Section 43.22.050.

Sec. 43.22.050 (page 18, line 9) - Directs the Department of Revenue to create regulations determining what is considered income from a source in the state for business conducted by a nonresident. The regulations must be consistent with AS 43.19, the multistate compact. This provision will allow the department to create regulations to allocate what income is taxable under this chapter when an out of state business is conducting business both in and out of state.

Sec. 43.22.055 (page 18, line 18) - Directs the department to create regulations to detail what income from a nonresident trust or estate is considered derived from or connected with a source within the state. This regulation shall be consistent with 43.22.045, which identifies income from a source within the state.

Ms. Hansen moved to the next section:

[10:36:21 AM](#)

Sec. 43.22.060 (page 19, line 2) - Provides that the taxable income for a part-year resident, trust, or estate shall be the sum of all taxable income associated with the part of the year that the individual or entity was a resident of Alaska and the income from a source in the state for the part of the year that the individual or entity was not a resident of the state.

Representative Wilson thought a resident was defined by a person's domicile. She asked whether a person was required to have homes in two states to be a resident of two states at once. Ms. Hansen explained that the provision applied to a taxpayer who moved in the middle of the year. There were also some residents that lived half of the year in one state and then the other half of the year in Alaska. She continued with the following section:

Sec. 43.22.65 (page 19, line 17) - States that taxpayer's taxable year and method of accounting for the state income tax shall be the same as for the taxpayer's federal income tax. The department shall adopt regulations addressing situations where a taxpayer changes methods of accounting. [For most individuals, the taxable year is the calendar year. However, entities such as partnerships that file an individual income tax return may use a fiscal year in place of a calendar year, and may have different methods of accounting for their income.]

Sec. 43.22.070 (page 19, line 26) - Establishes how taxpayers will submit tax returns and make payments for the individual income tax. It clarifies that this tax is due and payable to the department at the same time and in the same manner as the tax payable to the U.S. IRS for federal taxes. The section also outlines procedures in case there are changes to the taxpayer's federal income tax return. Any overpayments will be reimbursed by the department out of the general fund. As noted above, (h) exempts an individual from the penalty for not filing their income tax electronically. However, a person paid to file returns is not exempt, and must file electronically.

Ms. Hansen explained the provision. An individual would not face a penalty for not filing electronically but tax preparers were required to file electronically. She

summarized that the provision was related to the prevention of tax fraud by preparers. She reported that electronic filing made it more difficult for a preparer to file a fraudulent return and "skim some of the return."

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Representative Pruitt agreed with the provision but wanted to raise the question about the difficulty of access to electronic filing for some, especially rural Alaskans. He also raised the concern about people who volunteer to prepare tax returns. Ms. Hansen deferred the question to Mr. Spanos from DOR.

Co-Chair Foster appreciated the question and shared Representative Pruitt's concern. He related that in small villages, volunteer or hired tax preparers might be affected by the provision.

[10:43:26 AM](#)

BRANDON S. SPANOS, DEPUTY DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE, had volunteered as a tax preparer in some of the state's small villages. He relayed that many villagers who decided not to use the free service traveled to Bethel for tax services. The free tax filing services allowed paper filing. He reported that some paid tax preparers traveled to the villages and used a computer for data input then filed electronically from their business location upon return. He reminded the committee that the statute that required electronic filing offered a renewable five-year waiver provision. Representative Wilson stated that she always filed her taxes on paper. She wondered how the state could track how the taxes were filed. Mr. Spanos indicated that federal law required paid preparers to sign the tax return and provide their federal identification number.

Ms. Hansen interjected that the fraudulent return issue she mentioned earlier did not apply to tax returns prepared by individuals.

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Ms. Hansen continued with the next section that addressed tax withholding on wages of individuals and independent contractors.

Sec. 43.22.075 (page 20, line 30) - Establishes how taxes will be withheld by employers making payment of wages or salaries. The employer shall deduct and withhold the amount of tax, remit the tax to the department, and provide a written statement to the employee by January 31 of the succeeding year showing the amount deducted and other necessary information, similar to the federal W2. The Department of Revenue shall publish the rate of withholding required by this section. Withholding is also required for payments made to independent contractors.

Ms. Hansen reported that other states did not withhold taxes on payments made to contractors and planned to remove the section. The provision proved to be administratively "burdensome."

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Ms. Hansen moved to the next section and remarked that it applied to withholding on nonresident partners' composite return. She elucidated that the provision was very specific to partners required to file an annual information return to the federal government under subchapter K of the internal revenue code.

Sec. 43.22.080 (page 21, line 25) - States that partnerships that are required to file an annual return with the federal government shall also file a partnership return with the Department of Revenue, and shall withhold income tax from a nonresident partner.

Ms. Hansen briefly summarized the following sections:

Sec. 43.22.085 (page 22, line 5) - Allows a resident the option to apply some or all of their PFD as a refundable tax payment to their upcoming state income tax due, less any garnishment, levy, donations to Pick Click Give or college funds, etc., as allowed under other sections of statute. For example, a person may apply some or all of their 2018 PFD to their 2018 taxes due. If a person's Refundable Tax payment of their dividend is more than the amount of their state income tax due, any remaining amount will be reimbursed to the person as a tax refund, after the person has filed their state income taxes.

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Sec. 43.22.090 (page 22, line 15) - Authorizes the department to create all necessary forms and adopt regulations to implement this tax, including regulations for online filing and online payment and prepayment of taxes due, and forms for itemizing deductions. This section allows the department to adopt Internal Revenue Code regulations, as long as they do not conflict with this chapter.

Subsection (b) clarifies that transactions or payments between related parties must have a reason other than the purpose of lowering taxes. The department may determine and adjust the tax due on such a payment as necessary.

Subsection (d) directs the department to adjust the tax brackets and the personal exemption every two years, based on the Anchorage rate of inflation.

Sec. 43.22.095 (page 23, line 18) allows the provisions of the Internal Revenue Code that are mentioned in this chapter to be considered as if they are fully set out and defined in the chapter itself, unless the provision is inconsistent with the chapter.

Sec. 43.22.150 (page 23, line 29) - Defines terms used in this chapter. Key terms include 'domiciled', 'resident', and 'resident trust'. Resident is defined as an individual who: lives in the state for the entire calendar year; receives an Alaska permanent fund dividend; or receives a tax benefit such as a property tax exemption only available to a resident individual.

Ms. Hansen referred to page 26 of the bill and explained that a person domiciled in another state who was in Alaska for less than 30 days did not fall under the provision. Ms. Hansen moved to Section 20.

Section 20 (page 29, line 6) - AS 43.23 is amended by adding a new section which directs the Permanent Fund Division Department of Revenue to create a place on the PFD application where an applicant may apply some or all of their PFD to their upcoming state income tax due.

Ms. Hansen indicated that Section 20 was included in the original version of HB 115.

Representative Guttenberg WITHDREW his OBJECTION.

Representative Pruitt OBJECTED. He thought that the bill was going to undergo changes through an amendment process rather than through a committee substitute. He WITHDREW his OBJECTION.

Representative Wilson OBJECTED. She elaborated that the bill was changed substantially and requested additional public testimony hearings on the CS. She WITHDREW her OBJECTION.

There being NO OBJECTION, the proposed committee substitute for HB 115, Work Draft (30-LS0125\L, Nauman, 3/22/17) was ADOPTED.

Co-Chair Seaton noted that earlier in the week he had announced that a new CS would be introduced that included the previously adopted permanent fund amendments and other changes.

Ms. Hansen explained that "S" corporations and partnerships were included in the previous draft versions of the bill and that trusts were not dealt with properly. The department informed the sponsor that trust income was federally taxable and the bill needed to provide DOR clarity on how to tax trust income.

Representative Wilson wanted to determine how the provisions in the CS affected Alaskan trusts.

Co-Chair Seaton reported that public testimony for the CS was scheduled the following Wednesday.

Co-Chair Seaton reviewed the agenda for the afternoon meeting.

#  
ADJOURNMENT

[11:02:03 AM](#)

The meeting was adjourned at 11:02 a.m.