HOUSE FINANCE COMMITTEE
April 3, 2017
1:05 p.m.

1:05:38 PM

CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:05 p.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Paul Seaton, Co-Chair
Representative Les Gara, Vice-Chair
Representative Jason Grenn
Representative Dan Ortiz
Representative Lance Pruitt
Representative Steve Thompson
Representative Cathy Tilton
Representative Tammie Wilson
Representative Louise Stutes (Alternate)

MEMBERS ABSENT

Representative David Guttenberg
Representative Scott Kawasaki

ALSO PRESENT

Richard Pomp, Professor of Law, University of Connecticut School of Law; Bethann Chapman, Trust Attorney, Faulkner Banfield, Juneau; Taneeka Hansen, Staff, Representative Paul Seaton; Randall Hoffbeck, Commissioner, Department of Revenue; Representative Jonathan Kreiss-Tomkins.

PRESENT VIA TELECONFERENCE

Brandon S. Spanos, Deputy Director, Tax Division, Department of Revenue.

SUMMARY

HB 115 INCOME TAX; PFD CREDIT; PERM FUND INCOME

HB 115 was HEARD and HELD in committee for further consideration.

Co-Chair Foster addressed the meeting agenda.

#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."

1:07:04 PM

Co-Chair Foster shared that the following speaker, Professor Richard Pomp, had been hired by the Department of Revenue (DOR) to craft the technical elements of a tax based on adjusted gross income. The professor had been hired by the administration based on his expertise on the subject and his contract was for a draft bill. He had not been hired to act as a consultant to the administration or the co-chairs of the House Finance Committee. He elaborated that Professor Pomp had assisted in language interpretation and ensuring the language was accurate. He relayed that the bill before the committee was not Professor Pomp's or the administration's bill; it incorporated many of his technical elements but policy decisions had been made in the co-chairs' offices and the bill had been redrafted by Legislative Legal Services. He furthered that policy decisions such as the tax rates and the allowable deductions had been decided upon by the co-chairs' office.

RICHARD POMP, PROFESSOR OF LAW, UNIVERSITY OF CONNECTICUT SCHOOL OF LAW, provided detail about his professional background. He relayed that the opinions he would share during the meeting were his own and not affiliated with any organization. He shared he had a consulting practice and had worked with Alaska on a fairly large case, involving the Tesoro Corporation, that had gone all the way to the Alaska Supreme Court. He was happy to report the state had won. He also represented other states and some of the

Fortune 500 such as Netflix, AT&T, Toys-R-Us, GE, GM, CBS, and other.

Mr. Pomp noted that he had provided a summary of the rolls of trusts ["Irrevocable Trusts" (copy on file)]. He detailed that the trust section had probably been the most difficult part of the draft legislation, in part because there had been a very conscious attempt to protect Alaska's trust industry. He specified that in 1997 Alaska was one of the first states to start to make its trust laws attractive to nonresidents. Unfortunately, since that time, Alaska had lost its first-to-market advantage because many states had jumped on the bandwagon, including Delaware in 1997. He understood the importance of protecting Alaska's trust industry, which he believed the bill did. A multitude of other states offered high net worth taxpayers a chance to establish trusts and they would not be taxed in those states. He explained the situation was part of the backdrop the legislation had to take into account and deal with. He furthered that unfortunately it was a race to the bottom because once one state provided an attractive environment for the formation of trusts, other states jumped in, which had resulted in numerous competing states offering essentially zero tax on trusts.

Mr. Pomp detailed that the legislation divided trusts into two groups: resident trusts and nonresident trusts. He relayed that trust accounting was among the most complicated of anything dealt with in the bill; it was the province of a fairly small group of specialists - he did not include himself in the category. He continued that it was an opaque and sophisticated area of the law. He had a group of Wall Street practitioners who had been advising him on the topic - he had learned it was very difficult to get ahead of the practitioners who were at the cutting edge and represented powerful, wealthy families. He continued they had the very latest in tax avoidance techniques and the draft tended to deal with the subject, but there were no promises in the particular area of the law that the games being played were known. He was familiar with all of the games played pertaining to other areas of the draft legislation. He expounded that in the trust area, it was very difficult to feel comfortable that everything being done was understood. He explained that sometimes it was necessary to draft with a broad brush to bring numerous things into the tax net and shut down a significant amount of the game playing.

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Co-Chair Seaton relayed that the committee would also hear from a trust attorney later on in the meeting. He referred to a document provided by Mr. Pomp ["Short Summary of rules on trusts in existing version L of HB 115" (copy on file)] that noted investment income would not be considered Alaska source income and cited AS 43.22.045(a)(9). He stated that if there was no Alaska source income at the start of the trust for a nonresident it was fine; however, Alaska trust law required some amount of money to be held in an Alaskan bank. He asked if interest paid on the money in the Alaskan bank make the money Alaska source income and potentially make the entire trust Alaska sourced or taxable.

Mr. Pomp replied that he did not believe so. He read from AS 43.22.045(a)(9):

> ...dividends, interest, payments received under an annuity, gains, other intangible income received from, or attributable to, intangible personal property, including stock, bonds, notes, bank deposits, or annuities, if the intangible personal property is employed in a business, trade, profession, occupation, or employment carried on in the state;

Mr. Pomp elaborated that the latter part of the cited statute was a reference to the nonresident beneficiary and not someone else's business like a trust company. He explained that the prudent question was whether a nonresident beneficiary receiving investment income would be considered employed in a business, trade, profession, occupation, or employment carried on in the state by the nonresident. He believed the answer was probably no. The provision was independent of where the corpus is (where the stocks, bonds, or cash may be located). He stated that had not been made a factor under the draft legislation. He summarized that it would simply be whether "this had anything to do with" a nonresident's business or trade in Alaska. He was sure that in the overwhelming number of cases the answer would be no. He concluded that it would not be Alaska source income and the nonresident beneficiary would not be taxed on the specific items.

Representative Wilson asked about a scenario where a resident and nonresident each had a trust in Alaska with the exact same holdings. She asked if the exception would result in the taxing of residents while nonresidents would not be taxed.

Mr. Pomp replied that the general structure of the draft followed the general structure of the income tax. He detailed that in general, nonresidents were taxed only on Alaska source income, which was a constitutional constraint. A resident of Alaska was taxed on their entire income, which was a pattern followed by every other state with a personal income tax. The answer was yes, a nonresident could be taxed only on Alaska source income - it was the state's only jurisdictional hook with respect to that person. He used himself as an example and explained that Alaska had no jurisdictional hook over him unless the income he had received was attributable to Alaska source income. The draft cast a very broad approach as to what constituted Alaska source income. The draft legislation cast a broad net in reaching nonresidents - it reached the constitutional limit of what a state could do. He relayed that a nonresident could never be taxed on their entire income; it had to have some link with Alaska to be constitutional. He specified it was a bifurcation in the jurisdictional reach between residents and nonresidents. The rules on the trust mirrored the concept - resident trusts were taxable on all of their adjusted gross income and it did not matter whether the income was from an Alaska source or not. Nonresident trusts were taxed only on their Alaska source income, just like nonresident individuals were taxed only on their Alaska source income.

Representative Wilson thought the system would encourage other states to bring their trusts to Alaska, but would encourage Alaskans to go to states like Nevada in order to receive the same kind of breaks Alaska would be giving nonresident trust beneficiaries in Alaska.

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Mr. Pomp replied the point was astute. He explained that all states had to worry about their residents setting up a trust in another location (e.g. Alaska, Nevada, Delaware, and other). He addressed what could be done about the issue. He explained that if it was a grantor trust - trusts came in different sizes and shapes - it was really not

taxed as a trust. He specified that the grantor was the person who was taxed and who set up the trust. He continued that if the trust was revocable (as many were), it would be a grantor trust and the grantor would be taxed on the current income of the trust. He elaborated that the trust did not exist in a sense - the income passed through to the grantor. In that sense, if an Alaska resident set up a grantor trust in another state, the Alaska resident would pick up the income from the trust and it would be taxable to the resident. Any time there was a grantor trust, the problem identified by Representative Wilson went away. There were good tax reasons for grantor trusts because in the past couple of years the rate structure on non-grantor trusts was very compressed - the top bracket was reached at a very low amount of income. At income of $12,000 or $13,000 a person was already at the 39.6 percent bracket when it came to the federal tax rate. He stressed that the rate was very high.

Mr. Pomp continued that many grantors did not want to set up a trust if they did not have to, that would accumulate income and be taxed at the high rate. He elaborated that then the 3.8 percent Medicare tax was added on net investment income. Whereas, if it was set up as a grantor trust, the income would flow through to the Alaska resident grantor and for federal purposes they would receive the benefit of a much lower marginal tax rate. There were very good tax reasons why a grantor trust from a federal perspective was to be preferred. The state benefitted because the income flowed through to the grantor and would be taxed along with the rest of the grantor's income. For a fairly large number of trusts, the problem would go away. The problem pertained only to the non-grantor trusts. He acknowledged the non-grantor trusts could be very large - some people believed the non-grantor trusts were larger than grantor trusts, but he believed it was hard to generalize.

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Representative Wilson asked if the bill contained anything that needed to be altered due to a negative impact a provision would have on a certain group of people (e.g. S corporations, LLCs, and/or individuals).

Mr. Pomp replied that broadly speaking he would not have worried about an inflation adjustment. The state was in a

unique position of having a dividend from the Permanent Fund, which was worth much more than the personal exemptions in the bill. He would probably not have bothered with personal exemptions, given that an adjustment for family size could be done through the distribution from the Permanent Fund. He was aware that the dividend was lower than it had been in the past and that if oil and gas remained at low prices the dividend would probably not be as generous as it once had been. He spoke to economic consequences and noted that everyone worried about the effect of taxation on economic development. He relayed that states such as Kansas had eliminated its income tax with the hope that it would stimulate the economy and more than pay for itself in the long-term. However, the concept did not seem to work at the state level where rates were much lower than at the federal level. The hope was it would work at the federal level because it seemed Congress would do something about lowering rates with the goal of stimulating economic development.

Mr. Pomp continued that someone could say that the bill taxed wages, which it obviously did. An argument could be made that it would discourage people from working. He did not believe there was any empirical evidence for the proposition. When it came to the issues, he wanted to see the data. There were numerous anecdotes floating around, some of which were self-serving and others were ideological in nature. He just wanted to see the evidence and data. He had seen no data that would suggest that the bill would have negative effects on the Alaska economy. He stated that the discussion became even more complicated when considering what negative effects would occur if the money was not available to spend on infrastructure and schools. He furthered that taxes did not go into a black hole; therefore, it would be necessary to finance government services. He questioned what impact cuts to government services would have. He asked if it would attract young entrepreneurs the state may be hoping to attract. He continued that it was difficult to speculate "on any of this." He communicated that in the drafting of the bill he had wanted committee members to see everything. He believed it was much easier for the committee to go through the bill and remove items than to leave items out to begin with. The bill was broad and did not contain anything he thought should not be there.

Co-Chair Foster noted they were coming to the end of Mr. Pomp's speaking time.

Representative Wilson referred to Mr. Pomp's explanation that people were taxed at the time a trust was paid out. She wondered about the purpose of addressing trusts in the legislation if it went to the individual income tax when paid out.

Mr. Pomp answered that there was a level of tax on the trust as it earned income that was not paid out. He detailed that it was not desirable to have a trust used as a mechanism to park their income and receive the benefit of deferral without there being a current tax. When the trust was paid out, double taxation was eliminated - the federal rules were clear there would be one level of taxation. He continued that if it was not taxed at the trust level, it basically equated to a tax-free pocket book.

Representative Wilson did not think that made any sense. She stated that even if money was being made within the trust, if the trust was taxed based on how much money it made and then again when it was paid out, it was double taxation.

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Mr. Pomp responded that Representative Wilson would be correct "if that were so." The federal rules were such that there was no double taxation. To the extent the trust had been taxed on income it distributed, there was no second level of tax on the recipient.

Representative Wilson recounted that she had heard Mr. Pomp state that money in the trust would be taxed before any distribution was made (on capital gains, interest, and other) and at some point once distributions began, the individual would be taxed.

Mr. Pomp answered that the individual would not be taxed if the money had already been taxed at the trust level.

Co-Chair Seaton clarified that a grantor trust was taxed to the individual person. Whereas the nonresident or resident trust was paid by the trust and when a distribution was made it was not taxed again. There were two different

trusts that were taxed in different ways. He compared it to a sub-S corporation and a c corporation.

1:35:28 PM

BETHANN CHAPMAN, TRUST ATTORNEY, FAULKNER BANFIELD, JUNEAU, provided brief detail about her professional career.

TANEEKA HANSEN, STAFF, REPRESENTATIVE PAUL SEATON, agreed with Mr. Pomp's testimony that there was no double taxation. She explained that if a trust accumulated income and paid nothing out in the year it was accumulated, the income was taxed by the trust; it was not taxed a second time when the individual eventually received the income. She detailed that just like with wages, the [tax] withheld was recorded and was not paid a second time. If the trust had income distributed straight to beneficiaries, the trust received a deduction for any income distributed and the trust was not taxed on the income. The rules were clear and set up so the trust was taxed or the beneficiary was taxed.

Representative Wilson did not understand the answer. She believed they were speaking about different types of trusts that worked differently. She asked for further explanation.

1:37:57 PM

Ms. Chapman spoke to fundamental tax law related to trusts. There were several types of trusts "we use." Some were revocable, meaning the person establishing the trust, the grantor, was the beneficiary and could revoke the trust. She detailed that revocable trusts were also called grantor trusts under the Internal Revenue Code, meaning they were completely disregarded for all income tax purposes (they filed no separate tax returns - they could file informational returns, but generally did not) and all of the income was taxed to the individual. The Alaskan that set that type of trust up, was the taxpayer under both federal law and under the legislation. The other type of trust used were irrevocable and involved a grantor transferring assets into the trust without reserving the right to revoke it. Those types of trusts were used frequently for the protection of children, to establish educational accounts for people with disabilities, and other. Under the Internal Revenue Code, the irrevocable trusts could be grantor trusts (even though the grantor had given away the money, they were still the taxpayer). There

were many reasons that was done. She referred to Mr. Pomp's discussion about compressed rates and the federal income tax code, which was one of the reasons a parent may set up a trust and pay the tax annually.

Ms. Chapman discussed the other type of irrevocable trust called a non-grantor irrevocable trust. A person gave away money, but was no longer considered the taxpayer; therefore, the trust would be the taxpayer for all purposes. She continued that those types of non-grantor trusts may or may not pay income tax under the federal code, depending on the structure. One of the types of trusts was called a simple trust that acted as the taxpayer (they were non-grantor trusts) and all of the income had to be distributed out to the beneficiary annually. She detailed that the trust filed a tax return and took a deduction for the distribution paid out and the beneficiary receiving the money paid the tax.

Ms. Chapman relayed that other types of trusts were termed complex non-grantor trusts. She detailed that there may be an accumulation of income that may or may not be distributed (e.g. the income could be distributed by the trustee to one of three children). If there was no distribution of income or capital gains, the trust filed the tax return, which was taxed at the trust rates. If a distribution was made, usually the ordinary income and sometimes the capital gains would come out to the beneficiary on a K-1 (just like a K-1 used for pass through entities, LLCs, partnerships, and S corporations) and the beneficiary would pay the tax. There would not be double taxation. She referred to an example where the tax was paid at the trust level and no distribution was made until four years later. She detailed that under the scenario, anything that was current income would be part of the distribution to the beneficiary and would be taxed to the beneficiary. Anything that had already been taxed was added to principal, which was not taxed. The trust accounting rules were designed to ensure there would not be a tax at both levels.

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Representative Wilson asked if the bill contained provisions that would discourage residents from doing an estate or any other trust.

Ms. Chapman answered it was an income tax bill. She did not believe it would discourage people from doing the same type of planning. She reasoned that parents would still want to protect their children. She affirmed that how something would be taxed would be considered. There would be consideration about whether to make more grantor trusts or just have the tax pay it. She addressed what was typically done to minimize tax. She referred to an amendment that would make the scenario much simpler for people doing trust planning. When there were higher tax rates at the trust level, it discouraged the accumulation of income, which sometimes occurred on the federal level. If tax rates were similar, Alaska would not be discouraging people from saving the money for their children for the future. Additionally, people in Alaska would not be put in a situation where they may have to make distributions just to minimize income taxes. She did not believe the bill would discourage Alaskans from doing what they had been doing all along.

Vice-Chair Gara asked if Ms. Chapman was familiar with special needs trusts. Ms. Chapman replied "very familiar."

Vice-Chair Gara provided a brief description of a special needs trust. He discussed that a person with a disability may need a trust for their living expenses including a special vehicle, a ramp, medicine, and living expenses. He asked for verification his description of a special needs trust was accurate.

Ms. Chapman replied that his description was accurate, but she saw an amendment in the packet that was not quite accurate. She explained that special needs trusts that were established under federal and state law for people with disabilities to keep public assistance were funded with the individual's own money. She detailed that perhaps the individual had received an inheritance or a settlement from a car accident. She furthered that those types of trusts could only be used for supplemental needs such as a van or ramp to a house. However, under social security rules the funds could not be used for housing, medical care that would be provided by Medicaid, and food. The other type of trust used was known as a third-party trust or supplemental needs trust. She used an example of a grandparent wanting to leave a small inheritance to a child with special needs. The grandparent would create a trust that would benefit the child - those trusts were not known as special needs

trusts, but as discretionary trusts. Her only concern [with the amendment] was with references to being used for food and shelter - under social security rules, special needs trusts could not be used in that manner.

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Vice-Chair Gara relayed that Ms. Chapman was referring to his Amendment 18. He stated the amendment was defined more broadly where the trust may also include a disabled person's need for housing. The intention of the amendment was to address situations where a trustee had lost their social security income and wanted to lose their eligibility, the funds in the trust would still be nontaxable as long as used for those things. If a person wanted to keep their social security they would draft it narrowly, but if they did not mind losing their social security, the amendment would give the individual the option to have trust funds tax free. He asked if there was a problem with the proposal.

Ms. Chapman replied no and believed it was a wonderful idea.

^AMENDMENTS

1:47:19 PM

Co-Chair Seaton MOVED to ADOPT Amendment 11, 30-LS0125\L.31 (Nauman, 3/30/17) (copy on file):

> Page 11, line 21:
>
> Delete "and"
>
> Page 11, line 24, following "chapter;":
>
> Insert "and
>
> (F) income of an incomplete gift nongrantor trust to which a taxpayer transferred property, less deductions of the trust, if
>
> (i) the income and deductions of the trust would be taken into account in computing the taxpayer's federal taxable income if the trust in its entirety

was treated as a grantor trust under the Internal Revenue Code;

(ii) the trust is a resident trust;

(iii) the trust does not qualify as a grantor trust under U.S.C. 671 -679 (Internal Revenue Code); and

(iv) the grantor's transfer of assets to the trust is treated as an incomplete gift under 26 U.S.C. 2511 (Internal Revenue Code);"

Representative Wilson OBJECTED.

Ms. Hansen explained that the amendment would add income back into federal adjusted gross income for consideration. She detailed it pertained to an incomplete non-grantor trust. The language had originally come from Mr. Pomp and she had conversations earlier in the day with some trust companies and a trust attorney. The specific trust was complicated and would enable a person to create a trust that for tax purposes was considered a non-grantor trust - a trust that did not come back into a person's income. She continued that it was incomplete, meaning a person did not pay the federal gift tax and still retained certain powers of choosing who, how, and when distributions were made. There would probably not be many Alaskans choosing the particular trust given its complexity. She relayed that New York had already taken action [similar to the amendment] to clarify that in the specific trust where the grantor maintained some control over the income, the income should be considered in the individual's return just like in a normal grantor trust.

1:49:38 PM

Representative Pruitt asked if the amendment provided an exemption to the adjusted gross income category.

Ms. Hansen answered that the income would be added back into adjusted gross income. On the federal level, the specific trust [incomplete non-grantor trust] was not considered a grantor trust. The amendment would designate that for the state level and in the particular circumstance, the trust would be considered a grantor trust and it would be included in adjusted gross income.

Representative Pruitt thought the whole purpose of adjusted gross income was to make the scenario much more simple than it was about to become. He asked why they were considering reversing courses.

Ms. Hansen replied that the chances the item would be necessary were very slim and most residents would not be impacted by the provision. She noted that subsequent amendments would lower the tax rate brackets on trusts in general. The amendment sponsor was supportive of that change because of the many non-grantor trusts that should not be taxed at a 7 percent rate. She explained it was the one example where very high income individuals may potentially move their assets. One of the primary purposes of the specific trust was for state income tax avoidance.

Representative Pruitt asked why they were including the provision if they did not expect it to be used.

Co-Chair Seaton replied that the goal was to establish an income tax without numerous loopholes. The specific loophole had been seen in other states; therefore, the amendment would ensure the specific loophole could not be used in Alaska. The amendment was a preventative measure. Delaware incomplete non-grantor trusts never got completed, but due to tax avoidance, a person had money that did not get taxed. The amendment established that if a person set up one of the specific trusts in Alaska, it would be treated as the individual's own income as if it was a completed grantor trust.

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Representative Pruitt stated there had been a movement from the initial 15 percent to the adjusted gross income. He believed the intent was to make things as simple as possible. He referred to line 37 of the 1040 form [adjusted gross income line on U.S. Individual Income tax Return form (copy on file)]. He added there were not supposed to be any deductions afterwards. He thought the amendment seemed like the start of carving out holes seen as loopholes above and below the adjusted gross income lines. He asked if there had been a departure from trying to keep things simple. He believed they were trying to make their own system that was loosely based on the federal system and it would be subject to change in the future based on whether or not it could bring in more money to pay for state government.

Co-Chair Seaton responded that trusts were very complex subjects. He detailed it was a way in some cases to avoid tax. If the legislature did not want to include loopholes, it should make what was and was not allowable as clear as possible. The amendment attempted to take the experience of other states and make sure people knew they could not use the incomplete trust as a tax loophole in Alaska.

Representative Wilson asked for verification the amendment dealt only with resident trusts.

Ms. Hansen answered that under the amendment the income would come back to the individual resident for taxation.

Representative Wilson pointed out that (F)(ii) of the amendment specified that it pertained to resident trusts that were currently not federally taxed.

Ms. Hansen replied that if it was a nonresident trust, there would not be a way for the state to tax the individual because the money would be going back into the nonresident's income. Therefore, the amendment could only apply to a resident.

Representative Wilson thought the provision would encourage Alaskans to go to states like Nevada because the trust was not federally taxed, but would be taxed in Alaska. She reasoned that if a person moved the trust to Nevada they would not have federal or state taxes.

1:56:17 PM

Ms. Hansen answered that the trust would still be taxable because the income would be added back into the resident's adjusted gross income. She emphasized that the amendment was a preventative measure. The trusts would likely not be seen in Alaska.

Representative Wilson wanted to understand the issue. She was trying to determine if the provision would encourage individuals to have the trusts in another state.

Ms. Hansen responded that it may be possible for an individual to establish the particular type of trust in another state, but all of the income used to establish the trust would need to be from a source outside of Alaska.

Additionally, any trustees and corpus of the trust would have to be out-of-state.

Representative Wilson thought some of the amendments would be hard to vote on. She had spent most of the weekend trying to research what the amendments would do. She did not have the expertise on the issues and had received conflicting answers about what the amendments would do and how they would impact Alaskans. She continued that if they were really talking about income coming out of a trust, S corporation, or an LLC, she believed tax would be recouped based on the existing system. She did not understand why they were discussing trusts at all when the issue was about income tax.

1:59:09 PM

Vice-Chair Gara supported the amendment. He spoke to the discussion that the amendment was complex. He stated that on the federal tax form [1040] it was necessary to make every calculation already prior to getting to the adjusted gross income. Under the bill a person would use the same number they had already calculated on their federal tax, which was not complex. The issue in the amendment was whether the legislature wanted someone to avoid tax if they had a large amount of money. He did not believe a goal of the bill should be to let the wealthiest people hide their money from taxation.

Representative Wilson did not understand how a person would be able to hide their money. She reasoned that when money was taken out, there would be a charge. She asked how someone could be hiding their money. Additionally, if the person was hiding their money in Alaska, she asked if there was any other avenue for the person to do the same thing somewhere else.

Ms. Chapman clarified that they were not talking about hiding money. The issue was about proper tax planning. She stated that Representative Wilson was correct in stating that in almost all instances the state would receive tax because some assets would be distributed out of the trust. The topic addressed by the amendment was an extremely narrow subset of irrevocable trusts that were taxed as separate entities for federal tax purposes. She believed the amendment aimed to address wealthy Alaskans taking money from Alaska and moving it to another state without an

income tax. If the funds were not distributed, Alaska would receive no tax, whereas, if money was distributed, Alaska would receive the tax. The amendment pertained to trusts established by residents in another jurisdiction that did not make distributions from and did not pay state income tax. She noted there were some rulings from the IRS, but she believed whether the trusts worked or not was still in debate. The amendment was trying to specify that the individual would still have to pay tax on the trust in Alaska even if no distribution was made.

2:02:11 PM

Representative Wilson surmised it was about whether a person paid at present or later. She believed Alaska would ultimately receive the tax. She stated that the amendment would mean the trust would be taxed at present versus waiting four or five years when it was paid out. She continued that the money would ultimately be taxed. She did not believe anyone was hiding money anywhere.

Ms. Hansen replied that the beneficiaries of the trusts may not be Alaskans. She continued that it was a very specific type of trust - the Alaskan who created the trust was not the beneficiary, but they maintained control over the money in the way they did not in many of the other non-grantor types of trusts. The individual was not avoiding the tax on a federal level. She clarified that it pertained to planning within the tax law. On the federal level there was no tax avoidance, it was just one way the individual had been able to disassociate that income with their state of residency and therefore avoid the state income tax.

Representative Wilson thought it was important to be careful when referring to tax avoidance and surmised that if an individual was breaking the law the IRS would step in. She wondered how the state would know what a trust earned. She continued that the trust may not be located in Alaska. She surmised that because beneficiaries may not be Alaskan residents, the state wanted to make sure to get its share before the money was distributed. She believed the enforcement system sounded like a nightmare. She wondered how many people the state would need to hire to look into the trusts in other states to determine how to tax individuals. She opined that it was very far reaching in comparison with waiting until a distribution was made [to receive the tax].

2:05:05 PM

Co-Chair Seaton believed that telling people that the issue was not legal would probably solve the problem if people understood it was illegal to have a trust that was never completed, where the individual still controlled the money. He elaborated that the issue was complex and involved attorneys and could involve tax court. The amendment included language to ensure a tax loophole was not created, a loophole that had been found in other states and responded to.

Vice-Chair Gara spoke to his understanding of the concept. He surmised that the federal government did not tax until the distribution occurred - it did not matter what state a person moved to because they were still subject to federal tax. He continued that states had a different issue - states were trying to avoid a situation where someone did not distribute the trust income and then in a year they wanted to distribute the income they moved to a state with no tax. He asked if his understanding was accurate.

Ms. Hansen responded that the federal government did tax trusts that accumulate income. She agreed that it did not matter to the federal government what state of residency a trust was established in - the government would receive the same share out of the trust no matter what. She continued that it did matter to the state whether or not the resident was able to move the asset out-of-state through a trust. She noted the subsequent amendments were simpler.

Representative Wilson MAINTAINED her OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Ortiz, Gara, Grenn, Stutes, Foster, Seaton
OPPOSED: Pruitt, Thompson, Tilton, Wilson

The MOTION PASSED (6/4). There being NO further OBJECTION, Amendment 11 was ADOPTED.

2:08:20 PM

Co-Chair Seaton MOVED to ADOPT Amendment 12, 30-LS0125\L.32 (Nauman, 3/30/17) (copy on file):

Page 26, line 18, following "law;":

Insert "or"

Page 26, line 27, through page 27, line 4:

Delete all material.

Representative Wilson OBJECTED.

Ms. Hansen explained that the amendment would adjust the definition of resident trust to ensure the bill did not overreach and capture nonresident trusts currently administered in Alaska. The amendment sponsor did not want to interfere with the trust industry. She explained that if nonresident trusts were taxed as resident trusts they would move to another state. The original bill draft included a definition that was too broad. The amendment would delete items C, D, and E, which stated [version L]:

> (C) a trust consisting of property that is or will be disposed of or administered under state law;
>
> (D) a trust with a fiduciary or beneficiary other than a beneficiary whose interest in the trust is contingent, that is a resident of the state, and the laws of the state will govern the administration of the trust; the residence of a corporate fiduciary means the principal place where the corporation transacts the administration of the trust; or
>
> (E) a trust that is administered primarily in the state and governed by the laws of the state.

Ms. Hansen elaborated that currently under the trust industry Alaska's trust law required that part of the corpus of the trust be held in-state in order for it to be covered by Alaska trust laws. She explained it was a benefit to Alaska's communities and banking industry because it allowed them to have money deposited in local banks that would not otherwise be there (the money was not from an Alaskan source). The deletion of the items would more closely align Alaska with some other definitions of resident trusts such as New York, and would allow the trust industry to continue.

Representative Wilson did not want to be like New York. She was concerned that the amendment would create two classes of trusts: resident trusts and nonresident trusts. She believed it would make it enticing for nonresidents to come to the state to establish trusts because the state was not going to tax them at the same rate as residents. She continued that it would force Alaskans to go to another state to get the same benefit. She thought it was wrong in every way. She was supportive of the trust industry in Alaska, but providing more advantage to nonresidents did not make sense to her. She asked if the amendments had been added to amendments the committee had heard the previous week.

Co-Chair Foster believed everything was in order.

Ms. Hansen replied that the bill before the committee had been updated to reflect the amendments that had been adopted in the past (to bill version E). The bill was a new version (version L).

Co-Chair Seaton relayed there had been significant concern about the trust industry established in Alaska. The amendment aimed to ensure the trust industry was not impacted and could be maintained in Alaska as it was previously. He explained that Mr. Pomp had a different philosophy, which was to tax everything that was constitutional to tax, including nonresident trusts. The co-chairs felt it had been too broad. He detailed that the committee had heard during public testimony that people wanted to make sure the trust industry, including the nonresident trust industry, was allowed to go forward as it had been.

2:13:31 PM

Representative Wilson MAINTAINED her OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Thompson, Gara, Grenn, Stutes, Ortiz, Seaton, Foster
OPPOSED: Pruitt, Tilton, Wilson

The MOTION PASSED (7/3). There being NO further OBJECTION, Amendment 12 was ADOPTED.

2:14:13 PM

Co-Chair Seaton MOVED to ADOPT Amendment 13, 30-LS0125\L.46 (Nauman, 4/3/17) (copy on file):

Page 9, following line 27:

Insert a new subsection to read:
"(d) A trust that is exempt from federal income tax because of its purpose or activities is not subject to tax under this chapter."

Representative Wilson OBJECTED.

Ms. Hansen explained that the amendment added clarifying language that a trust exempt from federal income tax due to its purpose or activities, was not subject to tax. She relayed that it had already been true because the trust would only be taxed on taxable income, which was based on federally adjusted gross income. Those types of trusts would not have been in that income. She used a charitable remainder trust as an example. She deferred to Ms. Chapman for additional examples.

Representative Wilson asked about the types of trusts that applied.

Ms. Chapman answered that it would also include retirement trusts. For example, a 401k with a private employer had associated qualified trusts and was not subject to federal income tax under Section 401(a).

Representative Wilson asked about union trusts. Ms. Chapman deferred to Ms. Hansen.

Ms. Hansen answered that unions had a type of trust called Taft-Hartley, which was a type of pension trust that was exempt federally. Additionally, some of the union medical trusts were also exempt.

Representative Wilson asked why the trusts had been included if the bill would not tax federally taxed trusts.

Ms. Hansen answered that the amendment included clarifying language only. If someone was reading through the bill section related to tax on trusts they would be able to know

the bill would not levy a tax on trusts exempt on a federal level.

2:17:05 PM

Representative Pruitt stated that Amendment 11 had tried to get as much money as possible by eliminating loopholes. He commented that the current amendment (Amendment 13) would give some people a pass [from taxes]. He asked why the bill went after more money in one case and gave people a pass in another case.

Vice-Chair Gara explained it was a policy call not to tax trusts that currently had an existing no-tax policy. He would listen to an amendment to the amendment to add taxes that were not in the bill, but he would probably oppose it.

Ms. Hansen referenced the committee's earlier discussion about incomplete non-grantor trusts and relayed that those distributions would have been federally taxed at some point; therefore, those trusts did not fit into the category of trusts that were tax exempt for their purpose or activities.

Representative Wilson asked if any of the trusts related to the current amendment would be taxed when they made distributions.

Ms. Chapman replied that charitable trust distributions were made to charities and were never taxed; however, a charitable remainder trust could have interest or income distributions to individuals, which would be taxed. She explained that if she set up a charitable remainder trust where she had the right to receive the income for her life and when she passed away the remainder went to charity, it was an exempt trust under federal law, but she would be taxed on the income because she was an individual. Anything that went to a charitable organization that was exempt under [Internal Revenue Code Section] 501, would never be subject to tax at the federal level.

Representative Wilson asked if it was known how much more money would come into the state if the amendment failed. Alternatively, she wondered how much the state would lose in income if the amendment passed.

Ms. Hansen answered that the bill was not currently taxing the specific trusts, the language was merely clarifying.

Representative Wilson WITHDREW her OBJECTION.

There being NO OBJECTION, Amendment 13 was ADOPTED.

2:20:08 PM

Vice-Chair Gara asked to roll Amendment 17, 30-LS0125\L.37 (Nauman, 3/31/17) (copy on file) to the bottom of the list. He thought the subject may be addressed by a different amendment.

Page 13, following line 26:

Insert a new subsection to read:

"(b) For purposes of this section, the department shall treat the undistributed and distributed income of a trust as income."

Reletter the following subsection accordingly.

Ms. Hansen clarified that the sponsor's office had discussion earlier in the day with a trust taxation expert. Part of the purpose was to avoid people creating multiple trusts just to take advantage of lower tax brackets. On the federal level rule 26 U.S. Code 643(f) specified that if the grantor and beneficiaries were substantially the same person, the trusts were considered the same trust for tax purposes. She believed the intent was already captured in the bill because the state tax would be based on the federally adjusted gross income and the bill specified the trust income should be considered as it was for federal purposes.

Vice-Chair Gara stated that the intent in the amendment was not to have a flat 7 percent tax, but for the tax to be based on the tax brackets based on the amount of income. He asked for verification the intent would be accomplished somewhere else.

Ms. Hansen replied that it was the topic of a future amendment.

Vice-Chair Gara asked to roll the amendment to the bottom of the list and did not believe it would be needed.

There being NO OBJECTION, Amendment 17 was rolled to the bottom of the list.

2:22:23 PM

Vice-Chair Gara MOVED to ADOPT Amendment 18, 30-LS0125\L.41 (Nauman, 3/31/17) (copy on file):

> Page 9, following line 27:
>
> Insert a new subsection to read:
>
> "(d) A special needs trust or other trust established to provide solely for the housing, living expenses, or medical care of a disabled beneficiary is not subject to tax under this chapter. In this subsection,
>
> (1) "disabled beneficiary" means a person who has a physical or mental disability or a physical or mental impairment, as defined in AS 18.80.300;
>
> (2) "special needs trust" has the meaning given in AS 13.36.215(b)."

Representative Wilson OBJECTED.

Vice-Chair Gara explained the amendment. He relayed that in a number of circumstances people with disabilities had a special needs trust created. For example, if a person suffered a terrible brain injury and needed a lift to get in a van, special equipment to get inside their home in order to live independently, medical care, living expenses, and recreational equipment. Trusts were created where the money could only be used for those things - medical related living expenses. He detailed that disability was defined under Alaska Statute 18.80.300 and pertained to a mental or physical disability. The intention of the amendment was to not tax the income from those trusts. The individuals were dealing with very difficult life situations as it is and the money was only spent on things related to the difficult life situation.

Representative Wilson asked about the definition. She assumed the amendment pertained to AS 18.80.300 (14) and

(15). She noted that subsection (14) included a definition of physical and mental disability. She read from the definition "a physical or mental impairment that substantially limits a person's major life activity, only as a result of the attitudes of others toward the impairment; or none of the impairments defined in this paragraph but being treated by others as having such an impairment..." She did not believe the amendment sponsor was addressing that portion of the definition. She believed the amendment should be more specific on whether it pertained to an actual disability or that someone was treating them like they had a disability.

Vice-Chair Gara replied that the language mentioned by Representative Wilson would result in very minor costs. He believed it was doubtful someone would create a trust for a perceived disability; however, if they did, it would be fine with him. He noted it was not very much money and he could not imagine there being a $1 million trust to address the small issue. He surmised it would probably be a matter of thousands of dollars. He was comfortable leaving that portion of the definition in the amendment.

2:25:49 PM

Representative Wilson she believed an individual could not necessarily have what would generally be considered a disability, but still fit under the definition and be allowed to set up a trust for housing and living expenses.

Vice-Chair Gara stated that if Representative Wilson wanted to come back with a clean definition to address the portion of the disability she did not think needed to be addressed, he would be happy to adjust the language. However, on the fly, the kind of disability mentioned by Representative Wilson would not involve very much money. It was a policy call. He could go along with the concern if Representative Wilson had an adjustment to the language. He believed the more important thing was to not tax the trusts. He was happy to work with his colleague if she had a refinement to make.

Representative Wilson suggested limiting Amendment 18 to AS 18.80.300 14(a) "a physical or mental impairment that substantially limits a person's major life activity..." She believed the subsection included the disabilities Vice-Chair Gara was referring to. She furthered that individuals

needing extra assistance would be the ones setting up the trust and utilizing them. She did not believe the other definitions fit the amendment sponsor's description.

Vice-Chair Gara stated that he also wanted to include a condition that may require the use of a prosthesis and special equipment for mobility. He explained that Representative Wilson's proposed language would delete that. He was happy to work on a more narrow definition, but he did not want to exclude individuals who needed help because they had lost a limb or other.

Representative Wilson agreed and stated that subsections (A) and (D) would fit Vice-Chair Gara's description. She MOVED to AMEND Amendment 18 to limit the definition to AS 18.80.300 (14)(A) and (D).

Vice-Chair Gara had no objection to the proposed amendment.

There being NO OBJECTION, Amendment 18 was amended.

2:29:41 PM

Representative Pruitt asked if a special needs trust needed to be established as a special needs trust.

Ms. Chapman replied that the definition of 13.36.215(b) was limited to first-party trusts, which were special needs trusts meeting social security rules. The trusts were established under very specific rules. She believed the amendment also covered other trusts that may be broader for individuals with disabilities.

Representative Pruitt used a trust established for a senior as an example. He asked whether a senior who fit within the rules under discussion would automatically fall under the category. Alternatively, he wondered if the trust had to initially be set up in a manner specifying it would be tax exempt or if the trust could become tax exempt if the individual found themselves fitting within 18.80.300 (14)(A) or (D).

Ms. Chapman answered it would depend on how the trust was written. Typically if an attorney was drafting the trust for someone with a disability, they would include all of the limitations. Sometimes trusts were drafted more broadly, but they may include a provision specifying that

if the events were to occur to the individual beneficiary the definition would be limited at that time. She relayed it would depend on how the trust was drafted, but generally they were always set up with the goal of being special needs trusts or trusts with disabilities.

2:31:35 PM

Representative Pruitt asked if the trust could be amended. For example, if an individual became disabled after a certain period of drawing from a trust, he wondered if the trust could be amended.

Ms. Chapman answered that the trusts under discussion were irrevocable and the individual establishing the trust generally did not have the authority to make amendments. However, under Alaska law there was the ability to go to court to obtain amendments to trusts if it an amendment would be in the best interest of the beneficiary. Additionally, there was a provision that granted trustees in certain circumstances the ability to amend trusts, particularly to create special needs trusts. The definition referenced under 13.36.215(b) was relating to that type of trustee powers. The goal had been to draft the trust laws to be very useful to help people with disabilities.

Vice-Chair Gara stated that a special needs trust was created by a specific class of people. There could also be a trust that did the same thing to help someone with a disability that was not called a special needs trust. The goal was regardless of who created the trust, if it was a special needs trust, it should be tax free. He asked for verification that special needs trusts were, by definition, only those trusts created by a certain class of people.

Ms. Chapman replied in the affirmative. The definition of special needs trust was for people who need to comply with the social security rules to continue to receive their social security and also for Medicaid purposes. The definition in the amendment would be broader. She added that other types of trusts that were not special needs trusts were used, as narrowly defined under federal law, for people with disabilities.

Vice-Chair Gara asked who had to create the trust for it to be a special needs trust.

Ms. Chapman replied that she did not have the definition statute in front of her, but she believed the provision was referring to first-party trusts, which meant it was the individual. Up until recently the trust had to be established by the court, a parent, or a grandparent, but federal law had just recently changed to make them easier to establish.

Representative Wilson asked for verification that an individual would not have the ability to take their irrevocable trust and call it a special needs trust. She surmised that under the amendment the trust would have to be established as a special needs trust.

Ms. Chapman clarified that the individual could call the trust a special needs trust. She detailed it was a name that had been used as a shorthand for the specific type of trust. She continued that the trusts were established with names "like that," but it may not comply with the social security rules. The trust would just not be qualified under social security. An individual could call a trust anything they wanted to. She detailed that special needs trusts were very restrictive under federal law. She concluded that it was okay if a trust did not comply with the federal rules, but they were done for different purposes.

2:35:28 PM

Representative Wilson thought there was something called a special needs trust, which was the reason she was amenable to the amendment and why she wanted to ensure the definition was accurate. However, she now believed that if a person said the trust was special needs and did not want to pay state income tax, the individual would have to fill out paperwork or some proof to show they fell under the statutory definition of disabled. She asked if it would have to take place to abide by the amendment.

Ms. Chapman replied that the way she understood the amendment was that if she had established a trust for a disabled beneficiary that met the requirements, the trust would be exempt.

Representative Wilson asked if it was the intent of the amendment. Her understanding of the amendment was to make sure the state took care of individuals with a disability. She stated that she had mistakenly believed that a special

needs trust was an actual type of trust. She now understood it was merely terminology. She wanted to ensure the amendment would not result in significant regulation so that "something has to be proven that they fall underneath this."

Vice-Chair Gara cited line 3 of the amendment that specified a special needs trust or other trust that did the same thing. He explained that the special needs trust had to be created by the beneficiary. He also wanted the same kind of trusts created by a third party to be covered. He did not care who created the trust, but he did care that the money was used for someone with a disability for their living expenses, including recreational expenses, dignity expenses related to the disability, a lift for a van, and all items related to a person's living because of their disability.

2:38:06 PM

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 18 was ADOPTED as amended.

2:38:26 PM

Co-Chair Seaton MOVED to ADOPT Amendment 24, 30-LSO125\L.48 (Nauman, 4/3/17) (copy on file):

> Page 9, lines 11 - 13:
> Delete "A seven percent tax is imposed for each taxable year or portion of taxable year on the taxable income of a resident or nonresident trust or estate."
> Insert "A tax is imposed for each taxable year or portion of a taxable year on the taxable income of a resident or nonresident trust or estate. Except as provided in (b) of this section, the tax under this section for a trust or estate is determined as follows:
>
> | If the taxable income is | Then the tax is |
> |---|---|
> | Less than $50,000 | 2.5 percent of the amount in excess of $0 |
> | $50,000 but less than $100,000 | $1,250 plus 4 percent of the amount in excess of $50,000 |

$100,000 but less than $200,000	$3,250 plus 5 percent of the amount in excess of $100,000
$200,000 but less than $250,000	$8,250 plus 6 percent of the amount in excess of $200,000
$250,000 or more	$11,250 plus 7 percent of the amount in excess of $250,000.

(b)"

Page 9, line 15, following "Code).":
2Insert "(c)"

Reletter the following subsections accordingly.
Page 9, line 24:
Delete "(b)(1)"
Insert "(d)(1)"

Representative Wilson OBJECTED.

Ms. Hansen explained that the intent of the amendment was to delete the existing flat 7 percent tax currently on trusts and insert the same tax and apply the same tax brackets that were applied to an individual. The one change was that the 2.5 percent tax began on dollar one instead of the $10,300 tax provided to an individual.

Representative Wilson requested an "at ease."

2:39:39 PM
AT EASE

2:40:18 PM
RECONVENED

Representative Wilson WITHDREW her OBJECTION.

Vice-Chair Gara stated that there had originally been a 7 percent tax on trust income. The amendment specified that tax on trust income was based on the income tax schedule in the bill. He elaborated that lower amounts of trust income were taxed at a lower rate and higher amounts of trust income were taxed at a higher rate.

There being NO further OBJECTION, Amendment 24 was ADOPTED.

2:41:20 PM

Co-Chair Seaton MOVED to ADOPT Amendment 1, 30-LSO125\L.4 (Nauman, 3/27/17) (copy on file):

Page 8, lines 6 - 17:

Delete all material and insert:

"If the taxable income is	Then the tax is
Less than $20,600	$0
$20,600 but less than $100,000	2.5 percent of the amount in excess of $20,600
$100,000 but less than $200,000	$1,985 plus 4 percent of the amount in excess of $100,000
$200,000 but less than $400,000	$5,985 plus 5 percent of the amount in excess of $200,000
$400,000 but less than $500,000	$15,985 plus 6 percent of the amount in excess of $400,000
$500,000 or more	$21,985 plus 7 percent of the amount in excess of $500,000."

Representative Pruitt OBJECTED.

Ms. Hansen explained that the amendment would correct an error in the brackets, which was noted when the committee substitute had been introduced. The amendment corrected tax brackets for individuals filing jointly. The intention had been that the minimum (the amount below which the tax was zero) should have been a simple doubling of the minimum for the individual tax brackets. The amount on the individual tax brackets had been $10,300; however, the bottom amount in the committee substitute for the joint brackets was

$22,600. The amendment would amend the brackets for joint filers so that the taxable income began at $20,600 (double the starting amount for individuals).

2:42:29 PM

Representative Pruitt did not support the amendment. He relayed that he was okay with the error that gave $50 extra dollars to married seniors making $30,000. He believed the mistake would be a gain for those individuals. He had recently heard from a senior who had only $127 per month to spare after all of their expenses were paid. He the amendment would mean taking $4 out of that person's $127.

Vice-Chair Gara remarked that there would also be a $4,000 deduction per person. For a couple it would be $28,600 before they were taxed. On top of that there would be two Permanent Fund Dividends (PFD), which would bring the total to over $31,000 before being taxed. He noted it would be the subject of another amendment later on. The person with $1,000 monthly income would not pay tax under the bill.

Representative Pruitt replied that he was well aware of the information relayed by Vice-Chair Gara. He stated the committee had heard $30,000 the previous week and the amendment lowered the amount $2,000 before including dividends. He stated it was a $50 change to some seniors.

Representative Pruitt MAINTAINED his OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Gara, Grenn, Stutes, Ortiz, Foster, Seaton
OPPOSED: Thompson, Tilton, Wilson, Pruitt

The MOTION PASSED (6/4).

There being NO further OBJECTION, Amendment 1 was ADOPTED.

2:45:20 PM

Co-Chair Seaton MOVED to ADOPT Amendment 2, 30-LS0125\L.5 (Nauman, 3/27/17) (copy on file):

Page 21, lines 22 - 24:

Delete "Regulations adopted under this section shall require a person paying an independent contractor to withhold a portion of the amount paid to the independent contractor."

Representative Grenn OBJECTED for discussion.

Ms. Hansen explained the amendment. She relayed that the current committee substitute required the department to establish regulations for withholding on amounts paid to independent contractors. It had later been determined that most states did not do so. The one state that did had determined that about 40 percent of the independent contractors received a refund. The administrative burden of the provision would be higher than any potential revenue.

Representative Grenn WITHDREW his OBJECTION

There being NO further OBJECTION, Amendment 2 WAS ADOPTED.

Co-Chair Seaton MOVED to ADOPT Amendment 3, 30-LS0125\L.6 (Nauman, 3/28/17) (copy on file):

Page 23, following line 28:

Insert a new section to read:

"Sec. 43.22.100. Information released to a banking institution. Notwithstanding AS 43.05.230, information on an individual income tax return may be released to a banking institution to verify the direct deposit of an income tax refund or correct an error in that deposit."

Representative Wilson OBJECTED.

Ms. Hansen explained that the amendment would insert a section that had been included in the original version of the bill. The section was administrative and allowed the release of information on a tax return to a banking institution for them to verify the direct deposit of the refund or an error in the refund.

Representative Wilson asked for verification that if she did not want the government in her banking account she could elect to not have an automatic deposit.

Ms. Hansen answered in the affirmative.

Representative Wilson WITHDREW her OBJECTION.

There being NO further OBJECTION, Amendment 3 was ADOPTED.

2:47:49 PM

Co-Chair Seaton MOVED to ADOPT Amendment 4, 30-LS0125\L.9 (Nauman, 3/29/17) (copy on file). [Note: due to the length of the amendment it has not been included here. See copy on file for details.]

Representative Wilson OBJECTED for discussion.

Ms. Hansen explained that the amendment would make five changes, most of which were technical language changes and related to administration and tax compliance for partnerships and S corporations. There was one change pertaining to trusts. She referred to page 9, line 26, item (C) of the legislation - there had been a drafting error between the original bill and the committee substitute. Under 43.22.020 the tax on trust, item (C) was intended to say that if a trust was considered a nonresident trust and a trustee was a nonresident banking corporation, which was acquired by a resident banking corporation, the banking corporation would remain a nonresident trust for the purposes of the situation. She detailed that the acquisition of the nonresident banking corporation was not something the other trustees or the beneficiary would have any control over.

Ms. Hansen continued explaining the amendment. She directed attention to page 12, lines 27 and 28 of the bill, which described taxable income from a partnership or an S corporation. The amendment made a technical correction. Currently the section read "a partner's or shareholder's distributive share," but it was more accurate to say "a partner's distributive share and a shareholder's pro rata share." She moved to Section 43.22.050 on page 18 where the amendment would insert a new subsection (B). The section was meant to deal with business conducted in Alaska by a nonresident individual or a state, trust, or business. If business was conducted by a nonresident business, the income distributed to individuals needed to be allocated based on the multistate compact. The language was already included, but there was currently no reference in AS

43.22.050 to S corporations or partnerships, which needed to be included.

Ms. Hansen addressed the next change proposed in the amendment. She turned to page 19, following line 16, where a new section would be inserted that dealt with personal service and S corporations formed or used to evade income tax. The language was very similar to existing federal income tax statute language - several other states also had similar language. States that did not have the language had found a significant amount of state income tax avoidance. Technical detail information had been provided by Mr. Pomp, but it had not been included in the original committee substitute in order to take time to sufficiently understand the provision. She noted that renumbering occurred throughout the amendment. The final change appeared on page 22, line 4 - the section related to withholding by partnerships for nonresident partners. The following line was inserted: "The department shall adopt regulations that allow a partnership subject to withholding under this section to file a composite return." She explained that a composite return was used in many states and allowed a nonresident partner to specify that their only income from a state was income from the partnership. The individual certified the withholding amount was accurate and subsequently did not have to personally file an income tax return for that specific state.

2:53:44 PM

Representative Wilson asked if a person with a nonresident trust could not use an Alaska-owned bank. She noted that they were talking about that if a nonresident financial institution was bought out by a resident institution, the state would not charge the nonresident. She asked about a scenario where the bank was an Alaska bank to start with.

Ms. Hansen answered that the intention of the exception was not for nonresident trusts, it was for a trust established by a resident. The definition of resident trust is a trust established based on property that belonged to a resident of the state. She addressed the exemption in the section related to taxing on trusts and explained that if the trust was outside of the state, trustees were all nonresidents, and there was no income or gains from the trust connected with the state, Alaska did not have constitutional authority to tax the trust. The exemption was not about a

nonresident trust placing money in an Alaskan bank or non-Alaskan bank. It pertained to the specific situation under AS 43.22.020 (B) in which a trust created by a resident was not taxable by the state.

Representative Wilson countered that the language read that "a nonresident trustee remains a nonresident trustee even if that banking corporation is later acquired by a resident banking corporation." She asked if a trust started in a resident banking corporation would be taxed differently.

Ms. Hansen replied in the affirmative. She detailed that if a resident trust had an Alaskan banking corporation trustee, it would not qualify for the exemption under [43.22.020] (B); therefore, they would be taxed.

Representative Wilson was trying to figure out what the banking corporation had to do with the issue. She asked for verification that they were specifically talking about the type of banking corporation the trust was started in.

Ms. Hansen answered that it was not about the banking corporation that held the money, it was about whether a banking corporation was a trustee in the trust. She did not know if for example the Peak Trust Company was considered a banking corporation or not. The specific section would apply if a company was considered a banking corporation and also acted as a trustee. She clarified that a trust company or trust using a local bank such as Northrim Bank, did not automatically make the bank a trustee. The topic only pertained to a banking corporation acting as a trustee on behalf of a specific trust.

2:57:45 PM

Representative Wilson was trying to ensure the amendment would not black-ball any resident banking corporation. She did not want to give an unfair advantage to a different type of banking corporation.

Ms. Hansen did not believe it would be the case, because Representative Wilson was speaking about a trustee that was a nonresident banking corporation at the time the banking corporation became a trustee. Once a banking corporation was considered a nonresident trustee, their status would not change.

Representative Wilson read from AS 43.22.050 that dealt with "business conducted in the state by a nonresident and directs the department to regulate what is considered income from a source within the state." She asked why the department would be writing regulation on income from a source within the state. She believed it should be written within the bill so that someone would be able to read the provision and know what income from a source within the state actually meant.

Ms. Hansen answered that the section also specified that "regulations adopted under this subsection must be consistent with AS 43.19 and AS 43.22.045." She explained that AS 43.22.045 fell within the bill and defined income from a source within a state. If an entity had business inside and outside the state, it was necessary to adjust for the multistate compact. The section specified that the state would take the rules on state source income laid out in AS 43.22.045 and the multistate compact rules and would make sure they worked together within the state's regulations.

2:59:49 PM

Representative Wilson referred to the provision where the department would set out regulation for partnerships required to withhold income on a nonresident partner. She asked about the reasoning for the language.

Ms. Hansen responded that there were two circumstances the situation may occur. The first was in the case of a composite return where a nonresident partner may choose to have the partnership withhold for their benefit so they did not have to file an individual income tax return. Second, the partnerships were already filing a Chapter K information return with DOR. She believed it was fairly common practice for the partnerships to withhold on nonresident income.

Representative Wilson was fine with having a report, but she noted that many times when departments were asked to set more regulation, the regulation did not quite fit the legislature's intent. She stated that she would not have a problem if the amendment only pertained to how taxpayers would be recording the information and sending in their returns.

Representative Pruitt spoke to the portion of the amendment pertaining to tax avoidance. He understood the intent, but he referred to subsection (B) where avoidance or evasion was defined. He was trying to understand how the terminology appropriately defined avoidance. He asked how to determine accurately that a taxpayer was actually avoiding tax.

Ms. Hansen replied that the language was very similar to language in federal income tax rules. She believed there were well-defined rules already guiding the subject - the amendment used the same language.

Representative Pruitt asked for verification that the particular section would be defined through regulation.

Ms. Hansen responded that definitions could not be set forth in regulations, which was the reason for the inclusion of subsection (B) that defined the avoidance or evasion of income tax. The way to implement the definition would be set forward by regulation.

3:03:33 PM

Representative Wilson MAINTAINED her OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Gara, Grenn, Stutes, Ortiz, Pruitt, Thompson, Seaton, Foster
OPPOSED: Tilton, Wilson

The MOTION PASSED (8/2). There being NO further OBJECTION, Amendment 4 was ADOPTED.

3:04:12 PM
AT EASE

3:24:43 PM
RECONVENED

Co-Chair Foster noted that the committee would be moving to Amendment 19.

Representative Thompson MOVED to ADOPT Amendment 19, 30-LS0125\L.15 (Nauman, 3/28/17) (copy on file):

Page 4, line 17:

Delete "a new subsection"

Insert "new subsections"
Page 4, following line 26:

Insert a new subsection to read:

"(c) In accordance with AS 37.13.145(b)(2), and subject to appropriation, 33 percent of the amount available for distribution under (b) of this section shall be reserved for dividends. The remainder of the amount calculated to be available for distribution under (b) of this section shall be reduced by the difference between the amount calculated under (1) of this subsection and the amount under (2) of this subsection if the amount calculated under (1) of this subsection exceeds the amount under (2) of this subsection:

(1) the total amount of oil and gas production taxes under AS 43.55.011 - 43.55.180, mineral lease rentals, royalties, royalty sale proceeds, net profit shares under AS 38.05.180(f) and (g), and federal mineral revenue sharing payments and bonuses received by the state from mineral leases that are deposited into the general fund in the current fiscal year;

(2) the sum of $1,200,000,000."

Vice-Chair Gara OBJECTED.

Representative Thompson explained that the amendment with a prepared statement:

Amendment 19 sets a draw limit, it's the mechanism that limits withdrawals from the Permanent Fund when oil revenues increase or recover, or production goes up. It's designated to address oil price volatility. The draw limit is triggered when production taxes and unrestricted royalties reach $1.2 billion. Once triggered the amount calculated by the percent of market value formula and the amount withdrawn from the Permanent Fund is reduced by $1.00 for every $1.00 of oil production tax and royalties that exceed $1.2

billion. This amendment mirrors the provisions that the governor's HB 61 and SB 36 have in them. This is the mechanism that addresses oil price volatility. The draw limit is one of the administration's most must-haves, but the draw limit provides guidance for saving money during times of flush oil revenue. Without the draw limit we would take the full percent of market value draw even though oil revenues were sufficient to cover state spending. If low oil revenue prices are the reason that we are using the Permanent Fund today, why would we continue to take from the fund if oil revenues increase or recover? The draw limit is a commitment to not use today's crisis as an excuse to raid the fund when it isn't needed. Just like a normal person would manage their money, this is the plan for supplementing our paychecks with savings when our paychecks are low, but leaving money in our savings when our income recovers. Leaving money or earnings in the fund when other revenues cover state costs will allow the Permanent Fund to grow. A larger fund means we will have larger Permanent Fund Dividends. A larger fund means we will have larger percent of market value contributions to the General Fund, which means there will be more money for education and capital projects, and smaller deficits in later years.

Representative Thompson relayed that the amendment would protect the state's future and would grow the fund for future generations.

3:28:17 PM

Vice-Chair Gara OBJECTED and noted the committee had previously voted on the topic and had deleted it from the bill. He stressed that at oil prices of $75 per barrel the state would not be flush. He agreed that if the state was able to save, it should. He discussed the $1 billion in deferred maintenance for the University of Alaska alone. He continued that the cost continued to increase because the maintenance continued to be deferred. He did not want to continue to spend money on things that were wasteful and that was in the eye of the beholder. In the past he had opposed unaffordable megaprojects and he would continue to oppose projects such as the Susitna dam and the Knik Arm Bridge. He remarked that at some point there were basic things that needed to be done. He referenced the Seward Highway as an example and discussed the need for

modification to reduce the number of highway deaths. Additionally, there were dangerous roads north of Anchorage. He believed the number $75 per barrel was arbitrary. He would consider proposals like the one in the amendment, but he did not support specifying that additional oil revenue at prices between $75 and $100 per barrel could not be used for things like deferred maintenance or road construction. He had heard people say the concept would be unenforceable, but he did not want to put something in statute that was not enforceable.

Co-Chair Seaton spoke in support of the amendment. He explained that when the amendment had initially been proposed, more modeling and information had been needed. Since that time there had been modeling from the administration showing the cap lowered volatility and depletion of the reserve and made sure the potential failure rate was lowered to less than 1 percent. He added that modeling from the Legislative Finance Division also showed the same results that the action would make things much more stable over time.

3:31:40 PM

Representative Pruitt spoke in support of the amendment. He believed the amendment was a key piece of ensuring the long-term stability of the Permanent Fund. The amendment would mean the failure rate would be minimal in comparison. He clarified that the amendment would not reduce the amount of oil and gas revenues available, it would reduce the Permanent Fund utilization; it was a dollar-for-dollar exchange of oil money for what would have been spent from Permanent Fund money. He reiterated that the amendment would ensure the strength of the Permanent Fund, which he believed was one of the most important things that could be done.

Vice-Chair Gara referred to discussion about the failure rate. He stated that with the amendment there was a failure rate of approximately 1 percent and without it the failure rate was approximately 2 percent over 25 years. He believed the difference was negligible. He did not want anyone to believe the bill as written provided any great danger of failure. He reasoned that under any circumstance the legislature would act if something terrible happened in the stock market.

3:33:24 PM

Co-Chair Seaton asked to hear about the failure rate from the commissioner of DOR. He believed the failure rate was closer to 8 percent without the provision.

RANDALL HOFFBECK, COMMISSIONER, DEPARTMENT OF REVENUE, confirmed that the failure rate without the draw limit was 8.17 percent.

Co-Chair Seaton asked what the failure rate was with the draw limit. Commissioner Hoffbeck answered 0.83 percent.

Representative Wilson asked if there were negative consequences of passing the amendment. Commissioner Hoffbeck replied in the negative and elaborated that the administration supported the amendment.

Representative Wilson asked why. Commissioner Hoffbeck responded that the only reason there was consideration of using Permanent Fund earnings was due to current low oil and gas tax and royalty revenues. If revenues returned, it would no longer make sense to continue to also spend Permanent Fund earnings at that point. The amendment would provide a systematic process for turning off the use of the earnings reserve when it was no longer necessary.

3:35:17 PM

Representative Wilson equated it to a check and balance solution to keep state spending in control. Commissioner Hoffbeck replied in the affirmative.

Vice-Chair Gara referred to a table from the Legislative Finance Division that showed a cumulative failure rate of 2.4 percent over 24 years.

Commissioner Hoffbeck replied that the model Vice-Chair Gara was referencing pertained to SB 26.

Vice-Chair Gara stated that the current bill had additional revenue from income tax (that was not included in SB 26).

Commissioner Hoffbeck replied that when the administration talked about a fiscal plan it assumed that all plans would achieve the full closure of the deficit. All of the plans

without a structural change to close the deficit had failure rates of 50 to 80 percent.

3:36:25 PM

Vice-Chair Gara asked what the total UGF available under HB 115 would be if the limit kicked in at the $1.2 billion. Commissioner Hoffbeck did not have the number on hand.

Vice-Chair Gara asked if anyone on the committee knew. He repeated the question.

Representative Thompson responded that DOR's probabilistic model anticipated that the three affected revenues would provide about $3 billion per year based on a percent of market value of $2 billion in baseline revenue totaling around $1 billion of the production taxes and royalties. He stated it would bring the three revenues up to the $3 billion; the trigger had been moved to $1.2 billion as a compromise.

Vice-Chair Gara wanted to know how much UGF would be available if the amendment passed.

Representative Thompson replied $3 billion with the percent of market value and the other revenues.

Commissioner Hoffbeck added that the UGF at oil of $75 per barrel (about where the trigger would take effect) was about $3.8 billion to $3.9 billion.

Vice-Chair Gara stressed that school funding had not gone up in years; it was $30 million less than it had been three years earlier. He emphasized that people were talking about a $70 million cut to school funding. He elaborated that Anchorage was discussing laying off 99 teachers without the cut - potentially another 200 teachers and staff would be lost. He detailed there were not enough prosecutors; therefore, criminals were walking out on the street. He mentioned other deficiencies such as a lack in troopers, declines in University funding, and insufficient funding for energy projects. He believed the amendment instituted an artificial mechanism. He referenced an explanation that the provision would not have to be followed because it was not constitutionally mandated, which he did not find to be a good reason to pass the amendment. He did not know what would need to be spent five years in the future. He

surmised it was a difference in philosophy on whether or not the legislature should try to address the public's needs annually or whether it should be done with a formula "five years before you know what's going to happen."

3:40:32 PM

Commissioner Hoffbeck clarified that it only included the three categories of income - unrestricted other funds (from taxes and other fees), oil and gas revenue, and the Permanent Fund draw. The total did not include any other new revenues that may be passed. It provided about $600 million in headroom over the current budget prior to kicking in.

Representative Wilson asked for verification it would not include any reforms (e.g. Medicaid reform or other) that may save money. Commissioner Hoffbeck responded that any monies saved with reductions in expenditures could be reappropriated someplace else; it did really impact the calculation. Cuts to one area made money available elsewhere because the amendment would not restrict use of the funds.

Representative Wilson supported the amendment. She commented that the amendment pertained to just one component of the calculation. She continued that they were going into the Permanent Fund for the first time. She continued that the state was in the situation partly due to some of the choices the legislature did not want to make in terms of where to decrease government. She furthered they had also been making smarter choices on legislation that had been passed that would bring savings. She addressed the statement that the state would not have sufficient funds to fix existing infrastructure. She hoped changes would bring a smarter and more efficient government that may not require as much funding. She stated the public had been very clear that it was nervous about how the money was spent. She believed the amendment would act as a check and balance. She spoke to an increase in resource development, corporate taxes, business licensing, and other. She stressed the amendment would not result in a lack of money to fund important items.

Representative Thompson pointed out that when oil prices or production were high, other revenues increased. He cited corporate income tax and investment revenue and other as

examples. He stated that the aforementioned revenues were not impacted by the draw limit. He reasoned there was more money to spend even with the dollar-for-dollar offset.

3:44:04 PM

Representative Pruitt added that if more oil was produced, more royalties were going into the Permanent Fund, meaning there would be more money to make money off of and a larger opportunity for percent of market value dollars to be available. It allowed for growth in several places.

Vice-Chair Gara MAINTAINED his OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Wilson, Grenn, Stutes, Ortiz, Pruitt, Thompson, Tilton, Foster, Seaton
OPPOSED: Gara

The MOTION PASSED (9/1). There being NO further OBJECTION, Amendment 19 was ADOPTED.

3:45:12 PM

Co-Chair Seaton MOVED to ADOPT Amendment 5, 30-LS0125\L.17 (Nauman, 3/29/17) (copy on file):

Page 7, line 6:

Delete "AS 43.22.070(h)"

Insert "AS 43.22.070(i)"

Page 19, lines 26 - 27:

Delete "A person required to pay tax under this chapter"

Insert "A taxpayer"

Page 19, following line 30:

Insert a new subsection to read:

"(b) The department shall determine and publish the federal adjusted gross income below which an

individual is not required to file a tax return under this section."

Reletter the following subsections accordingly.

Representative Wilson OBJECTED for discussion.

Ms. Hansen explained that the amendment would make two administrative changes in Section 43.22.070 (the administrative section of the bill). First, the amendment clarified the language around who was required to file a return with the department. The section currently read "a person required to pay tax under this chapter is required to file a return with the department" and the amendment would change the language to "a taxpayer is required..." She detailed that a taxpayer was anyone subject to the chapter whether or not they actually have a tax due. She characterized the original language as ambiguous because there were some individuals who would not have a tax due. Second, the amendment would add subsection (b), which read "the department shall determine and publish the federal adjusted gross income level below which an individual is not required to file a tax return under this section." The language was similar to what was published and updated annually at the federal level. The federal language specified that a person making less than $10,350 in gross income was not required to file - due to their personal deduction and exemption they did not have a tax liability. The amendment would give the department the same authority to publish the table to prevent people with $1,000 in income from filing.

Representative Wilson referred to the amendment explanation that it would also allow the department to outline when a dependent could file on their parents' return. She asked where it was included in the amendment.

Ms. Hansen replied that she had learned from speaking with DOR that an individual would cover an individual and could also be interpreted to cover a dependent. On the federal level a dependent was able to file under their parents' return when they had less than the amount required for the federal tax level ($10,000 earned income or $1,000 of unearned income). Under the legislation, if the individual did not have a tax due they could be filed under their parents' return.

3:48:36 PM

Representative Wilson understood the concept of including a minimum so people knew when they did not have to file. However, she did not believe it related to whether a person could claim a child as a dependent on their taxes. She did not believe the amendment pertained to when a dependent could be filed on a parent's return. She surmised that the amendment only related to whether a dependent had to file on their own because of their income amount.

Ms. Hansen answered in the affirmative.

Representative Wilson summarized that the amendment merely established a minimum on who had to file, no matter their age.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 5 was ADOPTED.

3:49:32 PM

Co-Chair Seaton MOVED to ADOPT Amendment 6, 30-LS0125\L.18 (Nauman, 3/29/17) (copy on file):

> Page 11, following line 14:
>
> Insert new subparagraphs to read:
>
> "(B) a Joss on the sale or exchange of an obligation issued by or on behalf of
>
> (i) the state;
>
> (ii) a municipality of the state; or
>
> (iii) a public instrumentality, public authority, or public corporation created under state law;
>
> (C) a Joss from the sale or exchange of shares in a unit investment trust if the loss is attributable to an obligation issued by or on behalf of
>
> (i) the state;
>
> (ii) a municipality of the state; or

(iii) a public instrumentality, public authority, or public corporation created under state law;"

Reletter the following subparagraphs accordingly.

Page 12, following line 6:

Insert a new subparagraph to read:

"(G) a gain from the sale or exchange of an obligation issued by or on behalf of

(i) the state;

(ii) a municipality of the state; or

(iii) a public instrumentality, public authority, or public corporation created under state law;"

Reletter the following subparagraphs accordingly. 6

Page 23, line 14:

Delete "AS 43.22.030(a)(2)(H)"

Insert "AS 43.22.030(a)(2){1)"

Representative Wilson OBJECTED.

Ms. Hansen explained the amendment clarified the definition of taxable income under the legislation. The bill already added most municipal obligations into federal adjusted gross income; the items were not taxed by the federal government in most cases, but were taxed by the majority of states. In the definition under AS 43.22.030 (i)(A) it stated "interest on obligations of another state, a political subdivision of another state, a public instrumentality of another state, or the local authority of another state." The language was due to existing case law that a state was allowed to tax obligations issued by other states, but exempt obligations issued by that state. In the language in (i)(a) the bill was already exempting municipal obligations from Alaska or bonds issued by the state or municipalities of Alaska. The amendment helped to clarify that. There were a few cases where Alaska bonds were taxed at the federal level. She furthered that because Alaska

municipal bonds were exempted in (i)(a), the language needed to clarify that in the rare case the federal government taxed Alaska municipal bonds, the state would make adjustments. She detailed that a loss would be added in for an Alaska municipal bond that may have been taken as a deduction from federal gross income and subtracting any gains from Alaska municipal bonds or state bonds that may have been taxed at the federal level.

Representative Wilson asked for verification that if a person had an Alaska bond, it would be a deduction at the state level (just like with the PFD) if it was in the person's federal adjusted gross income, regardless of whether it made money or had to be claimed on federal taxes.

Ms. Hansen answered that any gains included in a person's federal adjusted gross income would not be taxed by the state.

Representative Wilson asked for verification it was a non-starter if a person had to file federally. Ms. Hansen replied in the affirmative.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 6 was ADOPTED.

3:52:52 PM
AT EASE

3:53:21 PM
RECONVENED

Co-Chair Seaton MOVED to ADOPT Amendment 7, 30-LS0125\L.19 (Nauman, 3/29/17) (copy on file). [Note: due to the length of the amendment it has not been included here. See copy on file for details.]

Representative Wilson OBJECTED.

Ms. Hansen explained that the amendment made eight clarifying changes relating to tax rates and taxable income. The primary intention was to increase the clarity of the language. The first was a change to AS 43.22.010 where the tax and tax brackets were laid out. She referred to existing language "derived or connected with a source in the state of a nonresident," which could be interpreted as

saying the state that the nonresident is connected to. The language was changed to make it clear the provision was talking about income that was derived or connected to Alaska. Pages 8 and 9 the title of AS 43.22.015 currently read "allocation of individual income." The amendment would change the titled to read more accurately as "calculation of tax on a nonresident individual." The section addressed the factor used to calculate tax owed by nonresident individuals. Currently the factor was basically all of an individual's taxable income was the denominator of the calculation and any of the taxable income from a source within Alaska was the numerator. The result was applied against the individual's taxes. The amendment clarified that the numerator was the nonresident individual's taxable income and added the language "under 43.22.045," the location where income from a source within the state was defined.

Ms. Hansen moved to page 11 related to allowable deductions. The amendment would add the words "directly or indirectly" to read "income that is related directly or indirectly to income taxable under the state and income exempt under the federal Internal Revenue Code." The goal was to align with established tax law.

3:56:28 PM

Ms. Hansen referred to page 12, line 10 of the legislation where the amendment clarified the trust would not be eligible for the per person exemption; the exemption was intended for people and not entities. She turned to page 15 where state source income was defined for income from a source within the state for nonresidents. The current language was unclear and implied that the activity items listed (including compensation and salary or wages for personal services rendered for employment training; site inspection; research and development; and farming or fishing within the state) were considered ancillary or connected to out-of-state activities. The amendment would reorder the current language to clarify that the activities were considered taxable within the state.

Representative Wilson pointed to page 11, line 23 that the amendment would change to read "adjusted gross income that is directly or indirectly related to income." She asked for an example of indirect.

Ms. Hansen believed indirect would include interest income. She did not receive exact examples; the proposed language matched language of existing tax laws in other states. She deferred to DOR for further detail.

Representative Wilson was concerned about how far reaching indirect income was.

BRANDON S. SPANOS, DEPUTY DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE (via teleconference), answered that indirect income could have multiple meanings. In the business community indirect income could be non-business income (income earned outside the normal course of business). Additionally, indirect income could be from securities or other items that were not normally part of an individual's wages. He cited winning a game of chance or lottery, which would not be a normal course of a person's business income.

4:00:47 PM

Representative Wilson stated she could understand how the scenarios in Mr. Spanos' description would be considered indirect for a business; however, she did not believe the examples would be indirect for an individual. For example, she wondered if she would have to pay income tax on earnings from winning the lottery in another state.

Mr. Spanos replied that if a person was an Alaska resident and won the lottery in another state, the portion of the winnings that were taxable federally would flow through the individual's adjusted gross income and would be taxable in Alaska.

Representative Wilson asked how the scenario was classified as indirect. She asked if anything outside of wages was counted as indirect.

Mr. Spanos replied that it could be. Indirect income was defined as income that was not directly earned through some activity an individual was engaged in. He cited interest on a bank account as an example.

Co-Chair Foster recognized Representative Jonathan Kreiss-Tomkins in the room.

Representative Thompson stated his understanding that if a person won the lottery in California they would be taxed personal income tax the State of California and the federal government would tax the winnings as well. He asked for verification the individual would also have to pay taxes in Alaska.

Mr. Spanos believed that in the specific example the California tax would be higher and therefore the individual's credit would be up to the limit of what they would have paid in Alaska. The individual would not be double taxed. If the individual won the lottery in a state without an income tax, they would pay the full tax in Alaska. Whereas, if the individual won the lottery in a state with a smaller income tax, the individual would get credit for the amount of tax paid in that state and would pay any difference in Alaska.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 7 was ADOPTED.

4:03:13 PM

Co-Chair Seaton MOVED to ADOPT Amendment 8, 30-LS0125\L.23 (Nauman, 3/30/17) (copy on file):

> Page 22, following line 4:
>
> Insert a new subsection to read:
>
> "(c) Withholding under this section is not required by a partnership that
>
> (1) is a publicly traded partnership, as defined in 26 U.S.C. 7704(b) (Internal Revenue Code); and
>
> (2) files with the department an annual information return reporting the name, address, taxpayer identification number, and other information requested by the department concerning each unitholder whose distributive share of partnership income, regardless of source, is more than $1,000."

Representative Wilson OBJECTED.

Ms. Hansen explained the amendment addressed public testimony that publicly traded partnerships should not be

required to withhold for their nonresident partners because they could change hands so quickly. The amendment would provide an exemption for withholding requirements on partnerships that a publicly traded partnership would not be required to withhold.

Representative Wilson appreciated the amendment, but observed it sounded like a report would be required from the companies. She how hard it would be for companies to pull the information together. She noted it would include any source exceeding $1,000. She asked if the amendment pertained to a list that had to include individuals living in-state versus out-of-state. She asked what the report entailed.

Ms. Hansen responded that in terms of in-state versus out-of-state, it was listed as each unit holder whose distributive share of the partnership income was more than $1,000. She believed it was very similar to K-1 information return that was already filed. She referenced testimony by a Tesoro representative who had cited Iowa as an example that also required the information return. She believed companies were likely filing a similar return with the federal government. She did not believe it would be burdensome.

Representative Wilson asked if they knew for a fact that companies filed the same report with the federal government.

Ms. Hansen replied that she knew with certainty that the report was required in Iowa. She knew that partnerships were required to file a K-1 return. She believed the information required for both reports would be very similar. She noted that DOR would be the entity responsible for crafting the actual return a company would be required to file.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 8 was ADOPTED.

4:05:54 PM

Co-Chair Seaton MOVED to ADOPT Amendment 9, 30-LS0125\L.25 (Nauman, 3/30/17) (copy on file). [Note: due to the length of the amendment it has not been included here. See copy on file for details.]

Representative Wilson OBJECTED.

Ms. Hansen explained the amendment. She referred to sections of the bill pertaining to the allocation of income (e.g. distributive shares from a business with income allocated to partners). The amendment would remove the current phrase "income or a gain, loss, or deduction," and would replace it with "an item of income, gain, loss, or deduction." The phrasing was established across all states and was used for allocations, especially related to partnership shares. The amendment would make things easier for interpretation by businesses and the courts if necessary.

Representative Pruitt referred to the language change from income to item. He asked if the language referred to the benefits that could come with being an S corporation. He detailed there were certain times where a shareholder or director of an S corporation may use a company car or receive benefits or "perks." He asked if the amendment was trying to get at that specific situation. He furthered that it reached beyond the salary a person would receive shown on an individual's W-2 form.

Ms. Hansen replied that she did not believe so. She explained that the bill used federally adjusted gross income and only took things that showed up as federally taxable income. She addressed the need to adjust for federal bonds, which the state could not tax, versus municipal bonds, which the state could tax. For example, if a partnership owned a municipal or federal bond that was part of the income source, the income or deduction needed to be adjusted based on how the item (the bond) had been allocated among the partnerships on the federal level. She deferred to DOR for further detail.

4:08:55 PM

Mr. Spanos shared that he had not been involved in the specific language change. He viewed item of income and income as synonymous. He noted that the Internal Revenue Code used the language "item of income" frequently, which was perhaps why other states were using the same language.

Ms. Hansen expanded upon the reason for the change. When drafting legislation, Legislative Legal Services

Legislative tried to be as concise as possible. In the current situation, it was not necessary to use "item" because the income, gain, loss, or deduction were the items. However, the specific language in the amendment was clearly established language used throughout the federal and state tax codes.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 9 was ADOPTED.

4:10:27 PM
AT EASE

4:11:34 PM
RECONVENED

Co-Chair Seaton MOVED to ADOPT Amendment 10, 30-LS0125\L.35 (Nauman, 3/31/17) (copy on file):

Page 19, line 31, following "(b)":

Insert "A person required to file a return under this chapter shall file the return on a form or in a format prescribed by the department. The return is due to the department at the same time and in the same manner, including extensions, as the taxpayer's federal income tax return to the United States Internal Revenue Service."

Page 20, line 27:

Delete "A taxpayer"
Insert "An individual"

Page 20, line 29:

Delete "taxpayers"
Insert "individuals"

Page 20, following line 29:

Insert a new subsection to read:

"(i) The department shall adopt regulations that set out requirements for a spouse, upon request, to be partially or fully relieved from joint and several

liability resulting from the I 9 joint filing of a tax return."

Page 23, following line 22:

"(b) Sections 26 U.S.C. 6654, 6662, 6664, 6694, 6695, 6700 - 6702, 6707, 6713, 7201, 7202, 7206, 7207, 7216, 7407, and 7408 (Internal Revenue Code), as those sections read on January 1, 2017, are adopted by reference as a part of this chapter."

Reletter the following subsection accordingly.

Page 23, line 24, following "(a)":

Insert "and (b)"

Representative Wilson OBJECTED for discussion.

Ms. Hansen explained that the amendment was administrative and had been mentioned by Mr. Spanos earlier in the meeting. The amendment clarified that the tax return was due to DOR at the same time the federal tax returns were due, including any extensions the federal government may offer. The current section "070" in the bill specified that the tax was due at the same time as federal tax, but it did not specify when the return was due. She pointed to page 20, lines 27 and 29 clarified that individual was exempt from electronic filing. She explained that previously the language had used the word "taxpayer," which could apply to partnerships withholding on behalf of their nonresident partners. All corporations were required to file electronically, although there were waivers they could obtain. The amendment would add a subsection on page 20 outlining that the department shall adopt regulations that set out requirements for a spouse to be partially or fully relieved from liability from the tax under the specific chapter. She detailed that normally when a couple filed jointly both spouses were considered liable for the tax, but there were certain circumstances where spouses could apply to be held separately liable.

Ms. Hansen directed attention to page 23 to Section 43.22.095 where definitions from the Internal Revenue Code were adopted as if they were referenced in the chapter. Some of the penalties used by the Internal Revenue Code would also be adopted. She referred to penalties for the

failure to report transactions, failure to collect or pay tax, understatement by a tax preparer, and failing to prevent a tax preparer from engaging in unlawful activities. The amendment would adopt a list of penalties by reference.

4:15:21 PM

Representative Wilson remarked that for almost every state an individual was liable for what their spouse did and typically both individuals were required to sign a tax return. She wondered why they would alleviate the responsibility.

Ms. Hansen answered that in most cases it would still be required. She deferred to Mr. Spanos for additional detail.

Mr. Spanos answered that other states had the type of allowance as well. The specific situation related to a case where an individual had committed fraud and their spouse was unaware of the fraud. Under the scenario, the innocent spouse would not be liable for the penalty in additional taxes imposed. The individual could apply and would have to prove to DOR or the court that they had no knowledge of the fraud.

Representative Wilson believed a person should not sign something they did not believe was accurate. She asked how someone would prove they did not know something.

Mr. Spanos responded that because Alaska did not have individual income tax the issue had not been dealt with in Alaska previously. He provided an example of a husband who owned a business partnership that was committing fraud. Under the scenario the income doubled on the individual income tax return. He explained that the wife had signed the return, but she would have had no knowledge of the fraud taking place. Most states had a provision allowing a person to prove what they would need to provide in order to prove they had no knowledge of the fraud. He would need to speak with other states in order to write the regulation if the amendment passed.

Representative Wilson asked if the federal government had the provision.

4:17:36 PM

Mr. Spanos believed so, but he did not know for certain.

Representative Wilson surmised it would be very hard for a person to prove they did not know something. She detailed that when an individual signed their income tax return they were verifying the information was correct to the best of their knowledge. She thought the amendment language would mean a person would not have to file a significant amount of information in order to be relieved from the liability. She asked if there was someone available from the Department of Law (DOL) who would be responsible for the provision. She thought it could be expensive.

Co-Chair Foster relayed there was no one available from DOL at present.

Representative Wilson could not agree with the portion without knowing the cost and whether it could even be utilized. She would be surprised to learn the federal government had similar loopholes.

Co-Chair Seaton clarified there instances of joint filers where one spouse was a resident and the other was a nonresident. He explained that an individual could be conducting business in Alaska and the spouse could file jointly in another state. He surmised that under the example a spouse may not have knowledge of what had taken place. There were provisions specifying that all of the tax was counted as resident tax - there was not tax avoidance. There may be a non-working spouse who was a nonresident. There could be a reasonable situation where one spouse could claim they had nothing to do with the situation. It had been one of the problems with the previous bill version related to joint filers (one of whom was a resident and the other was a nonresident). He stated that with adjusted gross income the issue had been somewhat solved.

Representative Wilson appreciated the comments, but underscored that the spouse [with no knowledge of the fraud] would still be required to sign. She spoke to her personal experience with tax filing. She continued that even with one person in-state and the other out-of-state, she surmised DOR would still require both individuals to sign. She did not know what the cost would end up being if the issue went to court. She wondered what information the state would require for a person to prove they were not

liable. She stated that in most cases the more people who were responsible for paying increased the likelihood the tax would get paid.

4:22:28 PM

Representative Wilson MAINTAINED her OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Grenn, Stutes, Ortiz, Pruitt, Thompson, Foster, Seaton
OPPOSED: Tilton, Wilson

Vice-Chair Gara was absent from the vote.

The MOTION PASSED (7/2). There being NO further OBJECTION, Amendment 10 was ADOPTED.

4:23:16 PM

Representative Ortiz MOVED to ADOPT Amendment 14, 30-LS0125\L.29 (Nauman, 3/30/17) (copy on file):

> Page 12, line 7:
>
> Delete "and"
>
> Page 12, line 10, following the second occurrence of "individual":
>
> Insert"; and
>
> (I) 50 percent of municipal property taxes paid in the taxable year on the residence in the state of an individual; the deduction under this subparagraph may not be taken for more than one residence for each tax return"

Representative Pruitt OBJECTED.

Representative Ortiz explained that the amendment would allow an individual to deduct up to 50 percent of their local property taxes paid for an Alaskan residence. The deduction would be limited to one residence per return filed. He explained that the concept was fairly simple and spoke to the idea of giving credit to people who were

currently paying property taxes. He detailed there was a 2.65 mill assigned to property taxes that went directly to support state education costs. The amendment would effectively acknowledge that and give credit to the individuals paying that particular tax. The deduction would be put against the federal adjusted gross income line (like the personal income exemption of $4,000 and the PFD deduction); the amendment would enable the individual to add 50 percent of their property tax bill before getting to the Alaska adjusted gross income.

Representative Pruitt clarified that did not object to the amendment, but he planned to offer an amendment to the amendment, which was currently being photocopied.

Co-Chair Foster asked for clarification on the amendment. He referred to Representative Ortiz's explanation that the deduction would be included above the adjusted gross income line. He calculated that if a person had a $4,000 exemption, a $1,000 deduction for the PFD, and a $1,000 property tax deduction. He asked for verification that if the individual earned $50,000, their adjusted gross income would be $44,000.

Representative Ortiz agreed. He added that committee members had received a copy of an email from Mr. Spanos who had done an analysis of the amendment's impact. The amendment would reduce the amount of income taken by an income tax by about $6.3 million. He believed the projected revenue from an income tax was about $65 million, which the amendment would reduce by about $6.3 million.

Representative Wilson remarked that renters paid property taxes. She elaborated that any good landlord would ensure that the costs were included in the rent. She detailed that some states gave credit for renters. She reminded the committee that individuals who may not be able to afford to buy a home were still paying. She believed the amendment would pick one group over another, which she found concerning.

4:27:27 PM

Representative Grenn echoed Representative Wilson's concern and was trying to determine how to draft an amendment to provide a deduction to renters. He used a 10 percent deduction from renters' income per year as an example.

Representative Tilton asked if the definition of residence was included. She noted that the amendment specified a deduction could not be taken from more than one residence and she believed the sponsor was speaking to a residence inside and outside the state. She asked if it was possible to have more than one residence in the state.

Representative Ortiz cited the specific amendment language: "50 percent of municipal property taxes paid in the taxable year on the residence in the state of an individual; the deduction under this subparagraph may not be taken for more than one residence for each tax return." He clarified that if a person had two residences in Alaska they would not be able to take a second deduction.

Representative Tilton asked for clarification that an individual would select the residence that would bring the most beneficial deduction.

Representative Ortiz agreed.

4:29:34 PM
AT EASE

4:41:08 PM
RECONVENED

Representative Pruitt MOVED to ADOPT Amendment 1 to Amendment 14.

Co-Chair Seaton OBJECTED for discussion.

Representative Pruitt explained that the amendment to Amendment 14 would exempt income received from the U.S. government as retirement pay for a retired member of the Armed Services of the U.S. and National Guard of any state. The amendment acknowledged appreciation of the U.S. military personnel and would include in the opportunity from removing it from an individual's adjusted gross income.

Co-Chair Seaton asked for verification that "some of this" was already exempt above adjusted gross income.

Representative Pruitt responded that some of the retirement was exempt, but a portion was considered income.

Mr. Spanos believed some retirement income was already excluded from adjusted gross income, but he did not have the specifics. He offered to get back to the committee.

Co-Chair Seaton objected to the amendment to Amendment 14 because a portion of the retirement income for Armed Services were already excluded under adjusted gross income. He spoke to the amount determined by the federal government for military members for deduction. He imagined there was a worksheet an individual went through and the outcome depended on the person's level of income. He surmised it would all be calculated prior to getting to adjusted gross income.

4:44:00 PM
AT EASE

4:44:54 PM
RECONVENED

Representative Ortiz was not opposed to the idea of the amendment to Amendment 14; however, he believed the issue was separate and that there should be a separate amendment.

Representative Wilson disagreed. She underscored that the door had been opened on things to be included and things to be excluded. She believed there had been testimony on the topic - the committee had heard from military and seniors about their income. She stated that young military members did not make high pay - many were on food stamps and other support. She believed if the committee was going to consider an exemption for one group it needed to consider all groups. She thought the military was important to the state. She also did not believe enough could be done for service members.

4:46:48 PM

Vice-Chair Gara recognized there were military members that did not make much in the way of a pension. He referred to his colleague's statement that some military members were on food stamps. He elaborated that the bill did not tax, with the PFD, income below roughly $15,500 [for an individual] and $31,000 for a joint filer. Additionally, $4,000 was tax free per dependent. He thought the food stamp issue was addressed. He asked what portion of pension income was already excluded from taxation.

Mr. Spanos responded that he had access to the information online and it appeared that military retirement pay, based on age or length of service, was considered taxable income for federal purposes. However, disability retirement pay and veterans benefits were fully excluded from taxable income.

A roll call vote was taken on the motion.

IN FAVOR: Grenn, Stutes, Ortiz, Pruitt, Thompson, Tilton, Wilson, Gara, Foster
OPPOSED: Seaton

The MOTION PASSED (9/1). There being NO OBJECTION, Amendment 1 to Amendment 14 was ADOPTED.

4:50:09 PM
AT EASE

4:50:24 PM
RECONVENED

Representative Pruitt MOVED to ADOPT Amendment 2 Amendment 14.

Representative Wilson OBJECTED.

Representative Pruitt explained that the amendment to Amendment 14 would exempt social security benefits [from an income tax]. He discussed the large and growing population of seniors in Alaska. He had been told by the Alaska Council on Aging that Alaska had the fastest growing population of retired individuals per capita. The amendment would recognize that an income tax would put an undue burden on some of the state's seniors.

Representative Wilson wanted to amend the amendment. She stated there were many individuals who received pensions, but did not receive social security benefits due to the kind of job they had. She opined that if the exemption was given to some seniors it should be given to all seniors. She suggested adding "and pensions" to the amendment.

Representative Pruitt did not have a problem with the suggestion.

4:52:14 PM
AT EASE

4:53:49 PM
RECONVENED

Co-Chair Foster noted the committee would take a break. He asked Representative Pruitt to withdraw his proposed Amendment 2 to Amendment 14 and bring back a written amendment after the break.

Representative Pruitt WITHDREW Amendment 2 to Amendment 14 with the intent to address the issue later.

4:54:45 PM
RECESSED

6:29:30 PM
RECONVENED

Representative Ortiz WITHDREW Amendment 14.

Representative Ortiz WITHDREW Amendment 15, 30-LS0125\L.29 (Nauman, 3/30/17) (copy on file).

6:30:06 PM

Vice-Chair Gara MOVED to ADOPT Amendment 16, 30-LS0125\L.27 (Nauman, 3/30/17) (copy on file). [Note: due to the length of the amendment it has not been included here. See copy on file for details.]

Representative Wilson OBJECTED.

Vice-Chair Gara explained that he had worked with DOR on the amendment language. He stated that sometimes a bill was difficult to read and he believed people had the misimpression they would start getting taxed at $10,000 of salary or pension, which was inaccurate. The amendment included legislative intent language that income as defined under the bill up to $14,300 for an individual and up to $28,600 for joint filers was not subject to the income tax. He added that a $4,000 personal deduction was included. He MOVED to AMEND Amendment 16 for clarity. He noted he had run the amended language by Mr. Spanos for accuracy:

Page 1, line 6:

After “individual”, insert: “, plus income from Permanent Fund Dividends,”

Page 1, line 9:
After “dependents”, insert “, plus income from Permanent Fund Dividends,”

Page 1, Lines 13 and 14:
DELETE:
“(4) in addition to the deductions described in this section, the permanent fund dividend will not be subject to the income tax under AS 43.22.”

Renumber all remaining sections accordingly.

Representative Wilson OBJECTED.

Vice-Chair Gara explained that the amendment to Amendment 16 would move the concept in paragraph 4 into subsections 1 and 2. He read the amendment language. In addition to deductions described in his original amendment explanation, the PFD would not be subject to the income tax. The intent was to include clear language at the beginning of the bill what income would not be taxed by the bill.

Representative Wilson WITHDREW her OBJECTION. There being NO OBJECTION, Amendment 1 to Amendment 16 was ADOPTED.

Representative Wilson understood Amendment 16 pertained to legislative intent. She asked for verification the brackets in the bill were changed, but the amounts were not.

Vice-Chair Gara replied that it was accurate at present, but if the brackets in the bill and the income levels and deductions were changed, the amendment language would need to be rewritten.

Representative Wilson thought there was some inflation proofing in the bill and wondered if that would change any of the amendment's legislative intent.

Vice-Chair Gara responded that the inflation proofing in the future would make less income taxable - there would be a higher income limit. The intent would become part of the uncodified law and would not show up in statute. He detailed that legislative intent could not change the wording of the bill. The legislative intent would not have

an impact when the schedule was taken over by DOR to inflation proof the amount of income that was not taxable.

6:34:50 PM

Representative Wilson asked for verification that the amendment language would just be for people to follow the issue along in the bill. She surmised that if the bill passed and became law any legislative intent would not be included in statute.

Vice-Chair Gara replied that uncodified law did not show up in statute books, but it could be found if someone was looking for intent. The bill was clear that the nontaxable income portion would increase with increases in inflation. He reasoned that if desired it would be possible to include language specifying that the amounts in subsections 1 and 2 would be inflation proofed per the legislation. The amendment would not show up in statute and would not change the meaning of the bill.

Representative Wilson WITHDREW her OBJECTION. There being NO further OBJECTION, Amendment 16 was ADOPTED as amended.

6:36:22 PM

Representative Pruitt MOVED to ADOPT Amendment 18.5, 30-LS0125\L.33 (Nauman, 3/31/17) (copy on file):

> Page 1, lines 4- 8:
>
> Delete "relating to the taxation of income of individuals, partners, shareholders in S corporations, trusts, and estates; 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;"
>
> Page 7, line 5, through page 27, line 14:
>
> Delete all material.
> Renumber the following bill sections accordingly.
>
> Page 29, lines 6- 11:
>
> Delete all material.

Renumber the following bill sections accordingly.

Page 29, line 13:

Delete all material.

Renumber the following bill sections accordingly.

Page 29, lines 25 - 28:

Delete all material.

Renumber the following bill sections accordingly.

Page 29, line 31, through page 30, line 3:

Delete all material.

Page 30, line 4:
Delete "(b)"
Insert "TRANSITION: REGULATIONS."

Page 30, line 10:

Delete "sec. 24" in both places

Insert "sec. 20" in both places 14
Page 30, line 12:

Delete "24, 26, and 27"

Insert "20, 21, and 22"

Page 30, 1ine 15:

Delete all material.

Renumber the following bill sections accordingly. 23
Page 30, line 18:

Delete "sees. 28 - 32"

Insert "sees. 23- 26"

Co-Chair Seaton OBJECTED.

Representative Pruitt explained the amendment would remove the income tax portion of the bill.

Co-Chair Seaton MAINTAINED his OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Pruitt, Thompson, Tilton, Wilson
OPPOSED: Gara, Grenn, Stutes, Ortiz, Seaton, Foster

The MOTION FAILED (4/6).

6:37:57 PM

Co-Chair Seaton MOVED to ADOPT Amendment 20, 30-LS0125\L.12 (Nauman, 3/28/17) (copy on file):

Page 1, lines 2- 3:

Delete "relating to the management of the budget reserve fund;"

Page 3, lines 10- 18:

Delete all material.

Renumber the following bill sections accordingly.

Page 4, line 27:

Delete "sec. 8"
Insert "sec. 7"

Page 6, line 13:

Delete "sec. 12"
Insert "sec. 11"

Page 29, line 27:

Delete "sec. 17"
Insert "sec. 16"

Page 29, line 28:

Delete "sec. 17"
Insert "sec. 16"

Page 30, line 10:

Delete "sec. 24" in both places
Insert "sec. 23" in both places

Page 30, line 12:

Delete "24, 26, and 27"
Insert "23, 25, and 26"

Page 30, line 15:

Delete "Sections 16, 17, 20, 22, and 25"
Insert "Sections 15, 16, 19, 21, and 24"

Page 30, line 16:

Delete "Section 9"
Insert "Section 8"

Page 30, line 17:

Delete "Section 13"
Insert "Section 12"

Page 30, line 18:

Delete "sees. 28 - 32"
Insert "sees. 27 - 31"

Representative Wilson OBJECTED.

Co-Chair Seaton explained that the amendment would delete the following language "relating to the management of the budget reserve fund." He specified that Legislative Legal Services and DOL had expressed that the language caused single subject concern.

Representative Wilson stated that the bill already included two different subjects: the Permanent Fund and an income tax. She believed that at a time when the state was looking for any way to make extra money off of its money, it seemed the state would want to take advantage of the item the amendment would delete.

Representative Pruitt agreed that the bill was already violating the single subject rule with its inclusion of the Permanent Fund and the income tax. He did not understand why the bill could include those subjects but not language pertaining to managing the money in the budget reserve. He stressed that if the committee was going to remove the budget reserve language for that reason, it should also apply the single subject rule to the entire bill. Otherwise, he believed the state would get sued.

Representative Wilson MAINTAINED her OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Gara, Grenn, Stutes, Ortiz, Seaton, Foster
OPPOSED: Pruitt, Thompson, Tilton, Wilson

The MOTION PASSED (6/4). There being NO further OBJECTION, Amendment 20 was ADOPTED.

6:40:39 PM

Co-Chair Seaton MOVED to ADOPT Amendment 21, 30-LS0125\L.11 (Nauman, 3/28/17) (copy on file):

> Page 1, lines 1 - 2:
>
> Delete "relating to the Alaska permanent fund; relating to the procurement by the Alaska Permanent Fund Corporation;"
>
> Page 2, line 1, through page 3, line 2:
>
> Delete all material.
>
> Renumber the following bill sections accordingly.
>
> Page 4, line 27:
>
> Delete "sec. 8"
> Insert "sec. 6"
>
> Page 6, line 13:
>
> Delete "sec. 12"
> 1nsert "sec. 10"

Page 29, line 27:

Delete "sec. 17"
Insert "sec. 15"

Page 29, line 28:

Delete "sec. 17"
Insert "sec. 15"

Page 29, line 31:

Delete "(a)"

Page 30, lines 4 - 7:

Delete all material.

Page 30, line 10:

Delete "sec. 24" in both places
Insert "sec. 22" in both places

Page 30, line 12:

Delete "24, 26, and 27"
Insert "22, 24, and 25"

Page 30, line 14:

Delete all material.

Renumber the following bill sections accordingly.
Page 30, line 15:

Delete "Sections 16, 17, 20, 22, and 25"
Insert "Sections 14, 15, 18, 20, and 23"

Page 30, line 16:

Delete "Section 9"
Insert "Section 7"

Page 30, line 17:

Delete "Section 13"
Insert "Section 11"

Page 30, line 18:

Delete "sees. 28- 32"
Insert "sees. 26 - 29"

Representative Wilson OBJECTED.

Co-Chair Seaton explained that the amendment would delete a provision that violated the single subject rule. He detailed that the bill related to revenues for the state and the bill related to a procurement process by the Permanent Fund, which was quite different.

Representative Pruitt asked if DOL had been asked about its thoughts on the single subject rule before the provision had been added. He stated that the bill was already in violation of the single subject rule. He elaborated that the legislation would use some of the money the Alaska Permanent Fund Corporation (APFC) had wisely been managing for the state and would not give the corporation the tools to manage it appropriately. He continued that APFC had said it needed the language the amendment would delete, which he noted had been included in a bill the previous year and there had been no concerns at that time. He believed there was a double standard going on. He asked what Legislative Legal Services had said about the whole bill. He believed the agency had specified that the whole bill violated the single subject rule.

6:42:35 PM

Representative Wilson wanted to see the legal opinion. She did not recall receiving a legal opinion related to the previous amendment or the current one. She stated that the committee had voted "on it" the previous week and she had never received a call from Legislative Legal Services. She could not imagine the agency would not want to ensure the committee "stayed on the straight and narrow" pertaining to the legislation. It was her understanding that if legislation violated the single subject rule it could result in the entire bill getting thrown out. She thought all committee members would want to be very careful with the single subject rule. She stated that the language the amendments would remove had just been put into the bill and would have violated the rule, compromising the entire bill. She commented on the broadness of the bill title and noted

that during her tenure in the legislature it had been possible to "pretty much stick anything in as long as it's got something in common." She stated that the bill was going after people's hard earned money. She reasoned that the language the amendment would remove would save money and result in more money going to the people if it remained in the bill. She underscored that the language did no damage and gave APFC - that had shown it knew how to invest money - the ability to do its job better and more efficiently. She stated that including the language was smart. She reasoned that when efficiency could be increased and more money could be made on existing funds, the legislature should be doing everything it could to make that happen.

Vice-Chair Gara stated that he would support the concept in a way that could be done constitutionally. He continued that legislators had all sworn to uphold the constitution. He opined that people had been very loose with the constitutional provision on the single subject rule in past years. He relayed that he had taken significant "heat" for trying to follow what he believed was the constitutional role. He stressed that the legislature knew from legal memos that if something was inserted in legislation that violated the constitutional provision it could potentially make the entire bill unconstitutional and the legislature would not find out until a court ruling. He stated that he would love to include a foster care bill in the current legislation, but that was not possible because it would violate the single subject rule. He referred to statements made that including the Permanent Fund and an income tax in one bill was an issue he would also consider. He stated they were both revenue bills, but he would want to be convinced there was no single subject problem - so far he had been convinced there was not. Whereas, the language the amendment would remove seemed to violate the constitutional provision. He would support the subject in other legislation.

Co-Chair Seaton discussed that the bill was a state revenue restructuring act. The provision that Amendment 21 would delete had been added to the bill as an amendment. He did not know whether the maker of the amendment obtained a legal memo stating it would be a violation of the single subject rule. He elaborated that when constructing a bill it was common to receive memos from Legislative Legal Services advising of a problem. He relayed that an income

tax and the Permanent Fund restructuring both fell under the topic of the state revenue restructuring act. He furthered that a procurement process by APFC was outside of revenue restructuring - it was a managerial method.

Representative Pruitt asked if there was a legal opinion specifying the bill did not violate the single subject rule.

Co-Chair Seaton replied he had no legal opinion stating that the bill as introduced (the state revenue restructuring act) violated the single subject rule.

6:48:06 PM

Representative Wilson read from a legal opinion on the single subject rule dated April 16, 2016:

> All that is necessary is that the act should embrace some one general subject; and by this is meant, merely, that all matters treated of should fall under some one general idea, be so connected with or related to each other, either logically or in popular understanding, as to be parts of, or germane to, one general subject.

Representative Wilson stated "talking about the Permanent Fund, this talks about the Permanent Fund - I would say that that would definitely pass the one subject rule."

Co-Chair Seaton explained the bill before the committee was a state revenue restructuring act and a procurement process did not deal with revenue. The procurement process was an internal revenue process by APFC and fell outside of the revenue restructuring topic.

Representative Pruitt MAINTAINED the OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Gara, Grenn, Stutes, Ortiz, Foster, Seaton
OPPOSED: Thompson, Tilton, Wilson, Pruitt

The MOTION PASSED (6/4). There being NO further OBJECTION, Amendment 21 was ADOPTED.

6:49:54 PM

Vice-Chair Gara WITHDREW Amendment 21.5, 30-LS0125\L.38 (Nauman, 3/31/17) (copy on file). He relayed that the amendment had been written before the spending cap had been passed by the committee. The spending cap left no earnings reserve money available to put into a larger dividend; therefore, the amendment no longer worked.

6:50:31 PM

Representative Pruitt WITHDREW Amendment 22, 30-LS0125\L.34 (Nauman, 3/31/17) (copy on file).

Representative Wilson MOVED to ADOPT Amendment 23, 30-LS0125\L.20 (Nauman, 3/31/17) (copy on file). [Note: due to the length of the amendment it has not been included here. See copy on file for details.]

Co-Chair Seaton OBJECTED.

Representative Wilson explained that the amendment would sunset the bill three years after the effective date of the Permanent Fund Act. She elaborated that a separate sunset would be established for the income tax because it would take longer [to take effect]. The sunset would not shut down the program, but it would force the legislature to reevaluate the issue. She reasoned that oil prices could be different at that time and there may be additional revenue resources.

6:51:11 PM

Co-Chair Seaton asked for verification the amendment pertained to 50 percent of all mineral leases offered.

Representative Wilson explained that whenever a sunset occurred it reverted [statute] back to its previous state [prior to the passage of legislation] if the sunset was not extended. If the legislature determined to extend the sunset, the bill would remain the same.

Co-Chair Seaton opposed the amendment. He relayed that the legislature was looking for a long-term, comprehensive, and sustainable fiscal plan. The amendment would mean that would not occur. Without knowing what would happen in the future, the provision would require expensive audits to try to go forward in merely two years [from the present].

Representative Wilson provided wrap up. She underscored that the amendment would include a three-year sunset provision. She stressed that it was not automatic and nothing in the building was automatic. She stated the amendment would force the legislature to determine whether the bill was working. She reasoned the sunset could be extended at any time for as many years as the legislature chose. She believed the provision communicated to the public that the state may not be in the current fiscal crisis forever. The amendment would convey that the legislature would take another look at the issue in three years' time. She emphasized that the amendment did not stop the anything from happening. She believed the amendment would tell the public that the legislature was doing numerous things to make government smarter and to do what it could so state resources would be developed more easily.

Representative Wilson reiterated that the amendment would force the legislature to review the bill; it would not automatically go away, it would merely be reconsidered. She stated that in three years oil may be at $80 to $100 per barrel, mining may be going well, and there may be other industries that were not currently in Alaska. She stated that at that time the legislature may decide that the gap no longer needed to be filled by the provisions in the bill because it had been filled by doing other things. She believed everyone around the committee table wanted to bring in revenue in other ways besides just taxing Alaskans. She stated that the amendment would send a message to the public that the legislature was willing to look at the issue again in three years. She reasoned that if the state still needed the revenue at that time, it would be possible to remove the sunset or extend it. She continued it would allow the legislature to determine whether the appropriate amount of money had been used from the Permanent Fund and whether the state ended up with unintended consequences from the income tax. She explained that the sunset provision would take effect three years after the effective dates of the bill; therefore, because the income tax would not start for another year, the sunset would occur three years after that time. She believed the sunset was the least the legislature could do for the public.

Co-Chair Seaton MAINTAINED his OBJECTION.

A roll call vote was taken on the motion.

IN FAVOR: Tilton, Wilson, Pruitt, Thompson
OPPOSED: Gara, Grenn, Stutes, Ortiz, Seaton, Foster

The MOTION FAILED (4/6).

Vice-Chair Gara WITHDREW Amendment 17, 30-LS0125\L.37 (Nauman, 3/31/17) (copy on file). He believed the contents had been addressed by another amendment.

HB 115 was HEARD and HELD in committee for further consideration.

Co-Chair Foster addressed the schedule for the following day.

#
ADJOURNMENT

6:57:06 PM

The meeting was adjourned at 6:57 p.m.