

HOUSE FINANCE COMMITTEE
October 26, 2017
1:03 p.m.
FOURTH SPECIAL SESSION

1:03:10 PM

CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:03 p.m.

MEMBERS PRESENT

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

MEMBERS ABSENT

None

ALSO PRESENT

Ken Alper, Director, Tax Division, Department of Revenue;
Sheldon Fisher, Commissioner, Department of Revenue;
Brandon S. Spanos, Deputy Director, Tax Division,
Department of Revenue.

PRESENT VIA TELECONFERENCE

Representative Tammie Wilson

SUMMARY

HB 4001 EMPLOYMENT TAX

HB 4001 was HEARD and HELD in committee for further consideration.

Co-Chair Foster reviewed the meeting agenda.

#hb4001

HOUSE BILL NO. 4001

"An Act imposing a tax on wages and net earnings from self-employment; relating to the administration and enforcement of the wages and net earnings from self-employment tax; and providing for an effective date."

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KEN ALPER, DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled "Capped Payroll Tax - Bill Introduction HB 4001 by Governor Walker" dated October 26, 2017 (copy on file). He pointed to the bill title on slide 2 of the bill. He shared that it was partial income tax. He moved to slide 4 of the legislation and provided detail on unrestricted general funds (UGF) and other projections. He referred to SB 26 that was in conference committee and would still leave a shortfall of \$0.6 to \$0.9 billion. He stated that HB 4001 was to partially fill that gap.

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Mr. Alper moved to slide 5 and addressed that the primary issue was a reduction in oil revenue. The slide contained a chart showing UGF oil revenue, the GF budget and oil surplus from 2010 to 2018. He turned to slide 6 and discussed that it was the budget per capita adjusted for inflation and population. Operating budget spending was currently comparable to spending in the 1990s. The budget had been cut substantially based on historic levels.

Representative Ortiz asked for a restatement of the testimony related to inflation and population growth.

Mr. Alper replied that the chart on slide 6 reflected the budget adjusted for inflation and population. The graph captured all of the information he listed. He referred to healthcare and pointed to the growth in healthcare cost in light blue. The dark blue portion represented the overall agency budgets (without health and education).

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Mr. Alper moved to slide 7 and discussed the Office of Management and Budget (OMB) 10-year plan:

- Not a policy document- an extrapolation of current trends
- Updated to include Preliminary Fall revenue forecast
- After the \$300+ million increase from FY18-19, subsequent years mainly reflect inflation plus known actual liabilities (i.e. debt, retirement funding)
- Status Quo Budget increases from \$4.7 billion to \$5.5 billion in FY2027 (+\$800 million)
- UGF revenue increases from \$2.0 billion to \$2.8 billion in FY2027 (+\$800 million)

Structural budget deficit is still \$2.7 billion in 2027

Mr. Alper turned to slide 8, "OMB 10-year Plan":

- Apparent closing of budget gap in later forecast years is primarily based on the expectation of continuing steady Permanent Fund growth
 - o The SB26 models assume the overall fund continues to grow due to indirect inflation proofing, plus deposits of new royalties
 - o Annual sustainable "POMV" draw therefore increases to \$2.5 - \$2.8 billion by FY2027
 - o Although the budget potentially comes into balance in 2026, deficits before that date will drive the CBRF to an unacceptably low level

Mr. Alper the overall fund would continue to grow with a 7 percent growth rate. Additionally, there were new deposits made annually from royalties. The deficits were looking smaller because the annual draw would go to \$2.5 billion to \$2.8 billion by FY 27. Although the budget potentially

comes into balance in 2026, deficits before that date will drive the CBRF to an unacceptably low level.

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Vice-Chair Gara asked whether slide 6 included all general funds.

Mr. Alper replied that the slide included unrestricted general fund (UGF). He remarked that designated general funds (DGF) were "pretty much a zero sum operation."

Vice-Chair Gara stated that one of his concerns was that the legislature had delayed revenue for so long that it would either be necessary to go below the save Constitutional Budget Reserve (CBR), and implemented tax would take one year to implement.

Mr. Alper replied in the affirmative related to the tax implementation. He agreed that the fiscal cliff was rapidly approaching.

Vice-Chair Gara surmised that the administration would have to propose over drawing from the Permanent Fund or use more from the CBR than recommended.

SHELDON FISHER, COMMISSIONER, DEPARTMENT OF REVENUE, replied that a threshold should be maintained in the CBR for safety measures. The options were cutting more or taking more from the Permanent Fund Earnings Reserve Account (ERA).

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Representative Kawasaki referred to slide 6 and challenged the assertion that the budget deficit was \$2.5 billion. He referred to deferred maintenance and other costs.

Mr. Alper was not sure whether the correct way to refer to the needs was "deficit," but he agreed there were numerous expenditures. All of the capital items brought forward in the early 1980s were aging and would need rooves, siding, and upgrades. There was a much higher capital base than the state had 30 to 40 years earlier.

Representative Kawasaki queried the anticipated GF spend for the ten years.

Mr. Alper replied that the one-time adjustments from FY 18 to FY 19 was inflation. He stated that the FY 18 was unusual, because it only had approximately \$120 million in GF. He furthered that there was approximately \$110 in reappropriation. He stated that the real number was closer to \$230 million. He furthered that the Office of Management and Budget (OMB) ten-year plan utilized the FY 18 budget as the base and increased it as inflation starting with the \$230 million.

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Representative Pruitt referred to the statement that the CBR would be at an unacceptably low level. He asked for the level that should not be surpassed.

Mr. Alper replied \$2 billion. The state need a reserve in case of a natural disaster and other.

Representative Pruitt observed in the presentation that the budget would be balanced by FY 2026. He believed the public's concern was that once a tax was started that it would continue on in perpetuity. He wondered why the bill did not contain a sunset clause.

Mr. Alper replied that if the state had sufficient funds that would make sense to end the tax, but he did not believe it was prudent to include it in the bill.

Representative Pruitt thought a sunset would force the conversation.

Mr. Alper did not believe he was the appropriate person to answer the question.

Representative Pruitt stated that the state had spent a significant amount on capital. He wondered about a conversation regarding whether the state should continue to own all of the assets. He asked if there was an effort to look at the substantial amount of assets tied up in facilities to use elsewhere.

Commissioner Fisher replied that the question of the sunset was appropriate. He remarked that there were assets in "a couple of different buckets." Some of those assets were underutilized, and there was some effort to determine

whether to dispose of some of the assets. He stated that some of those assets were in locations that did not have a market to dispose. He furthered that there was tremendous value in holding some other assets, such as the Atwood Building. He stated that the Atwood Building was a large asset and heavily utilized. The advantage of owning that asset was that the current lease rate was between \$75 to \$80 per square foot. He stressed that the building was completely paid off. He remarked that leasing a space ended up paying the capital cost.

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Representative Pruitt believed the land in Alaska should be available for land. He noted that there had been pressure to get land into the hands of Alaskans. He believed it would bridge the gap for a number of years. He asked if the administration was willing to get DNR working on the issues.

Commissioner Fisher would follow up on the question.

Representative Guttenberg asked about the disposal of state assets. He believed that many of the facilities owned by the state cost the state more when they were privatized. He remarked there were many things the state should or should not be doing.

Commissioner Fisher shared that the savings were achieved by owning. He did not believe the state received inferior service when leasing. He could discuss whether it was beneficial to own or lease.

Representative Thompson pointed to the chart on slide 6 and asked if the tax credits, the Permanent Fund Dividend, and GO bonds were included in the graph.

Mr. Alper answered that the red section included debt service such as GO bonds and oil and gas tax credits. The wedge had become large in 2010 due to oil and gas tax credits. The Permanent Fund had never been part of that graph. He referred to a presentation earlier in the week, and stated that once there was a Permanent Fund restructuring bill, the administration may make the changes.

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Mr. Alper advanced to slide 9 and referred to balancing of the budget by FY 26. He explained that numerous things had to align to obtain a balanced budget at that time.

For this to work out, several things all need to happen:

1. Oil production meets the new, more aggressive preliminary fall forecast scenario
2. Oil prices stabilize in the \$60 range, adjusted for inflation
3. Flat state budgets that can be contained within the OMB 10-year plan despite deferred maintenance and other needs
4. Senate version of SB26 with 75 percent / 25 percent POMV split
5. Permanent Fund grows at a steady 6.95 percent per year without a major market correction

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Representative Ortiz referred to slide 9, item 3. He asked if it assumed that the capital budget continued to be funded as in the current year.

Mr. Alper answered replied that the reappropriations were drawing down some leftover money from the very large capital budgets from five years prior. He remarked that the GF capital budget, but inserting the reappropriations and assuming replications with new GF, the \$230 million was the correct starting point.

Representative Pruitt remarked that the Permanent Fund had grown at an 8 percent average.

Mr. Alper deferred to Commissioner Fisher.

Commissioner Fisher replied that the Permanent Fund had a target that grew at a real return of 5 percent.

Vice-Chair Gara referenced slide 9, item 4 related to the Senate version of SB 26. He asked whether the dividend had to go down to \$1,000.

Mr. Alper answered that the Percent of Market Value (POMV) was the flip side of the \$250 was about \$175 million into the GF.

Vice-Chair Gara was trying to determine when the state would run out of money before the assumptions on slide 9 worked out. He referred back to slide 4 and noted that there would still be a \$600 million deficit. He thought the CBR would run out in three years, much sooner than FY 26.

Mr. Alper answered that if everything worked out exactly right it would balance in FY 26.

Vice-Chair Gara asked about the dividend amount.

Mr. Alper answered the proposal would shorten the time before an absolute zero

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Representative Wilson asked if the management of the Permanent Fund would change if the legislature began using it in the operating budget.

Commissioner Fisher stated his understanding of the question.

Representative Wilson replied that she believed the Permanent Fund was invested currently in long-term assets. She thought it would change if the legislature used it as a fund source.

Commissioner Fisher addressed liquidity of the assets in the fund. He noted that publicly traded securities could be sold, but private equity did not share the characteristic.

Representative Wilson asked if the fund would still receive a high return if the use was shifted.

Commissioner Fisher answered that the Permanent Fund did anticipate a reduction.

Representative Wilson asked if the \$300 million the bill would bring in would be all necessary because the Permanent Fund would be used for the remainder.

Commissioner Fisher answered that he had spoken with numerous leaders of different areas in the state. The administration's plan would take the gap from \$2.6 billion to \$300 million approximately. He acknowledged there were legislators and members of the public that still believed the budget needed to be cut. The bill was not a final solution, but it gave a framework with more certainty of how the state would move forward. The bill would give ratings agencies comfort in the state's financial stability.

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Representative Wilson remarked that there was a desire to lower budget than passed the previous year.

Commissioner Fisher answered that the budget presented and the OMB. He referred to UGF and DGF had been reduced by about 20 percent. The administration was looking at other ways to make reductions like a shared services program, which included consolidating information technology (IT) in the state departments. The departments were conducting efficiency improvements on a regular basis. He believed the state needed to keep thinking about healthcare. He referred to talk about a healthcare authority.

Representative Wilson looked forward to seeing a lower budget.

Co-Chair Foster noted the committee would hear from the Alaska Permanent Fund Corporation (APFC) the following week.

Mr. Alper moved to slide 10 and addressed elasticity.

The following items increase or decrease the size of the future deficits (\$millions):

- House Permanent Fund bill (higher dividend) \$175
- \$10 oil price shift \$300
- Federal health care changes \$100
- Near term major market correction \$300
- Increases to capital budget \$50+
- Major disaster response Indeterminate

Representative Grenn pointed to page 9 and 10 and remarked that they did not include oil credits owed by the state.

Mr. Alper agreed.

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Representative Guttenberg noted that the dividend rose if the population dropped. He asked about the population projections built into the presentation.

Mr. Alper did not know what had been built into the data by the Department of Labor and Workforce Development. He remarked that all of the items would provide a positive benefit to the state, but not direct revenue to the state.

Mr. Alper turned to slide 11, "Earnings Reserve Account Volatility":

- The Earnings Reserve Account is the only portion of the Permanent Fund that may be spent
- It holds the gains and losses of the whole Permanent Fund; the corpus is always made whole from losses
- In the FY08-09 market crash, the ERA balance fell to just \$420 million
- If markets experienced similar results this year, there would only be enough funds in the ERA to cover a single year's deficit

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Mr. Alper summarized the first section of the presentation on slide 12 regarding why a broad-based tax was needed:

- Even a small tax as proposed in HB4001 covers roughly half the forecasted ongoing deficits
- This buys the state time in case of various contingencies
- A tax combined with PF restructuring and continued budget discipline makes a complete fiscal plan
- If we get to where the CBRF is gone in a couple of years and don't have a revenue measure in place, it takes over a year to collect a new tax
- At that point, the remaining alternative of additional unstructured Earnings Reserve draw could

establish a potentially catastrophic long term precedent

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Mr. Alper turned to slide 14 and addressed the tax proposal summary:

- 1.5 percent tax on wages and self-employment income
- Tax paid by individuals earning income in Alaska; two income families would pay for each person
- Does not tax investments, retirement income, rental income, etc.
- Tax is capped at \$2,200 or twice the previous year's PFD, whichever is greater
 - Cap applies to incomes over \$147,000 / year
- Revenue about \$320 million at full implementation
- About 15 percent of revenue will come from nonresidents

Vice-Chair Gara agreed that if the budget gap was not solved the economy would shrink and Alaskans would be harmed. He did not want to pass something that would negatively impact lower income and middle class families. He asked about the tax rate under the bill.

Mr. Alper answered that there were 600 Alaskans with an income over \$1 million per year. The bill became a bit regressive in the 5 percent.

Vice-Chair Gara remarked that at an income of \$1 million it seemed to be a benefit to the wealthiest. He added that higher income individuals were able to deduct from their federal taxes, but lower income individuals did not.

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Mr. Alper replied that about 30 percent of Alaskans itemized their tax returns. It was possible to deduct local income taxes or local sales taxes, but not both.

Vice-Chair Gara felt that the proposal had a negative impact on lower income people. He felt that there should be an exemption for the first \$25,000 for the extremely poor. He wondered whether the proposal taxed every level of income.

Mr. Alper replied that the bill as written taxed the first dollar earned. He remarked that the origins of the bill were in the school head tax.

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Representative Grenn asked if it was gross or net on the federal form.

Mr. Alper answered that ideally the administration would like to see definitions in the bill, but some would have to be dealt with in regulation. He stressed that the tax would be deducted from the check as a percentage of wages or salary, similar to the state's unemployment insurance was deducted from the checks. He furthered that a self-employed person did not have the details within the bill.

Representative Grenn wondered whether the person paying the cap would be less or more than what they would pay with a statewide 2 percent sales tax.

Mr. Alper referred to impacts of different tax types on different income levels. A person would probably pay a bit less under a sales tax.

Representative Grenn requested to see the data.

Representative Pruitt referred to the current tax proposal before Congress. He asked for the administration to "burn" everything received from ITEP [Institute on Taxation and Economic Policy]. He did not want to use information from East Coast liberals. He wondered what the \$320 million was based on, and the year's tax information.

Mr. Alper replied that the most recent complete IRS data set was 2015. He shared that the bill was built on the 2014 data. The data set was reverse engineered to update it to 2015.

Representative Pruitt queried the number of people who had left Alaska since 2015, and what jobs and average salary had decreased.

Mr. Alper answered that he did not have information about how many people had left the state. The unemployment rate

was currently about 3 percent higher than it had been when the current recession started.

Mr. Alper referred to 15 percent from nonresidents. He asked if the percentage was higher was because the tax would apply to individuals who would not have paid the tax under a prior proposed tax structure.

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Mr. Alper had not seen numbers of 7 or 8 percent or that low. He remarked that 12.5 percent was a net from non-residents. He stated that a certain number of Alaskans had an income, but earned all their money out of state.

Co-Chair Seaton clarified that the number was 608 people in Alaska made \$1 million per year; it could not be included in the tax before the committee.

Mr. Alper agreed.

Representative Thompson looked at taxes capped at \$2,200 (slide 14). He pointed to a change in the cap to \$4,800. He wondered if the administration had done the calculation.

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Mr. Alper answered in the affirmative. He guessed they would scoop up three-quarters. It did not affect 95 percent of taxpayers.

Representative Guttenberg asked who collected data on revenue. He wondered if the information was broken out.

Mr. Alper answered it was not his area of expertise. The Department of Labor and Workforce Development kept a good data set at the job classification level. He recommended hearing from DLWD if the committee wanted the information.

Vice-Chair Gara asked at what level of wealth the tax rate started going below the 1.5 percent.

Mr. Alper answered \$147,333.

Representative Pruitt asked if the \$147,333 was taxable.

Mr. Alper answered that it was top line income.

Representative Pruitt spoke to cases with contractors. He wondered if it would rest on the contractor (e.g. deckhand or other). He wondered where the onus rested.

Mr. Alper responded that an employer would have to report on a federal 1099 form.

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Mr. Alper spoke to slide 15: "Tax Proposal Summary":

- For most Alaskans the tax is less than the PFD
- Out-of-state residents will pay the highest effective rate because they do not receive PFDs

Mr. Alper provided a background of how the state got to the current point of looking at a tax. He explained slide 17: "Alaska History of Taxes based on Income and Wages":

- Began in 1949 at 10 percent of federal tax liability
- By 1961, the tax was 16 percent of federal tax liability
- In 1975, Alaska switched from federal tax liability to its own tax brackets
- Ranged from 3 percent to 14.5 percent on taxable income
- Alaska repealed personal income tax in 1980 after oil revenue boom
- "Alaska Fair Tax" (HB303) passed House in 2002. This was an income tax designed to match the effective tax rates of a Sales Tax
- Various bills 2015-17 leading to HB115

Mr. Alper discussed the idea of a broad-based tax turning to slide 18: "Broad Based Tax Analysis":

Since the 2016 session, multiple analyses have been done that look at the relative impact of different taxes, cuts, and Permanent Fund restructuring plans:

- Institute of Social and Economic Research at UAA
- Institute for Taxation and Economic Policy
- Tax Foundation
- Northern Economics
- Brad Keithley
- Department of Revenue internal analyses, including Chapter 3 of Fall 2016 Revenue Sources Book

You will likely hear from many of these resources

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Mr. Alper specified a number of bills that were introduced from 2015 - 2017. The list of legislation was revealed on slide 19: "Income Tax Legislation, 2015-2017":

- Approximate revenue from recent bills

29th Legislature

- o House 2015-16 bills; \$650 million
- o Governor's 2016 bills; \$200 million

30th Legislature

- o SB12, Bishop "School Head Tax"; \$70 million
- o HB146, Claman "School Head Tax"; \$540 million
- o HB115, passed House 2017, \$700 million

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Mr. Alper continued on slide 20: "HB 4001 is different from a true income tax":

- Does not tax several key types of income:
 - Capital gains
 - Retirement earnings
 - S-corp distributions
- Much less complex administration and staffing need
- Does not require individual filing for typical wage earners

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Mr. Alper noted that Nevada did not have an income tax. He mentioned a few other states that did not have an income tax. However, states had a similar payroll tax.

Mr. Alper looked at slide 21, "HB 4001 is different from a true income tax":

Nevada is one of the seven states that do not have an income tax. Nevada does, however, have a similar payroll tax.

"Nevada's Modified Business Tax (MBT), which is remitted by employers (not individuals) on aggregate gross wages (of all employees) above \$50,000 per quarter at a rate of 1.475 percent is currently the only somewhat comparable statewide example."

-Jared Walczak, Tax Foundation, "Could a Payroll Tax Work for Alaska," October 20, 2017

Mr. Alper reviewed slide 22:" Process since Senate voted down HB115 (5/12/17)":

- June 5, Governor proposes "compromise"
 - Included budget, SB26, oil tax credits
 - New revenue based on Sen. Bishop's school head tax bill SB12, for at least \$100 million

- o Bishop bill actually raised only about \$60-\$70 million, had had no hearings, and had some technical issues
- June-July, several informal efforts to build a viable compromise bill based on SB12 before adjournment
- Internal administration discussion of multiple revenue options, and outreach to both legislative bodies, led to decision to use a similar structure
- Converted from stair-step to flat-rate to avoid high marginal tax issues at bracket crossovers
- September 22, bill released at time of current special session call

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Vice-Chair Gara remarked that there was an estimate of the state's deficit. He stated that the bill would raise almost one-half of the deficit, leaving a significant deficit. He wondered why only part of the deficit was addressed.

Commissioner Fisher replied that there was a narrowing of the gap over time, based on the expected growth of the Permanent Fund. He remarked that the governor wanted to present a proposal that would be accepted politically.

Mr. Alper moved to slide 23 titled "Thought behind the "cap".":

- Substantial number of Alaskans ask, in essence, "why are we collecting a tax with one agency while paying a dividend with another?"
 - o Certain people, while opposing a tax, are prepared to give up their PFD to help operate government
- Actually eliminating the dividend would be very bad policy for many Alaskans throughout the state, and it is highly unlikely to imagine a majority approving a full elimination

- The structure of the HB 4001 "cap" acknowledges the concerns of those people- basically taxing the dividend back from higher income Alaskans
- The hope is, a tax with this structure will be more broadly acceptable than a full income tax

Representative Pruitt stated that hope was not a method and the word should never be used. He asked for the administration to never include it in a presentation.

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Mr. Alper agreed that if a person chose to not receive a dividend it would make everyone else's share higher.

Mr. Alper relayed that one of the pieces necessary to build was a mechanism for refunds. He provided detail. He moved to slide 24, "Technical Language in HB 4001":

Bill is about 1/3 the length of HB 115.

Language is adequate to establish, or authorizes regulations to define, many key issues:

- Defining "self-employment" and "from a source in the state" plus other key terms
- Interpretations must be consistent with Multistate Tax Compact
- Incorporates IRS code to a limited degree where needed, state can require a copy of federal return
- Process for withholding and remitting tax by employers
- Filing of reports for payments to self-employed individuals and contract employees
- Individual returns by those required to do so, mainly the self-employed
- Refunds for overpayment

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Representative Kawasaki asked about the penalty for not filing taxes.

Mr. Alper did not believe there was a penalty for not filing in the bill. He stated that there was a penalty within the regulation. He deferred to Mr. Spanos. He stated that there was some standard penalty language in the general tax statutes, which would likely apply. He stated that, barring any other direction, the general tax authorities would be used for penalties.

Co-Chair Seaton referred to line 3 of the self-employment. He remarked that the line was only from a source within the state. He wondered how it would be delineated for a resident or non-resident.

Mr. Alper replied that an income tax was a tax on all the income, and a credit was back for tax paid in other states. He stated that the bill was written that the tax was only paid on what was earned in Alaska, whether one was a resident or non-resident. He stated that without a 1099 form in a small business, there would be a self-reporting requirement with an audit follow through. He hoped that the definitions in the bill would give tools to assist in what was counted as self-employed income. He deferred to Mr. Spanos.

BRANDON S. SPANOS, DEPUTY DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE, stated that the bill only taxed income made within the state. He stressed that a resident who earned income outside of Alaska would not be taxed on that income. He remarked that the self-employed would point to the multi-state tax compact.

Co-Chair Seaton asked for verification it was on net income and not self-employment.

Mr. Spanos replied in the affirmative.

Vice-Chair Gara asked if the distribution was counted as self-employment income under the bill.

Mr. Alper replied in the affirmative.

Mr. Spanos answered that the bill referenced a section of the Internal Revenue Code - he would have to research it and follow up.

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Representative Wilson looked at self-employment and schedule C. She stated that if she was a sole proprietor with no actual income from the business, would she go to line 31 with the net profit and loss to utilize as the income.

Mr. Alper answered in the affirmative.

Mr. Spanos concurred with Mr. Alper's reply.

Representative Wilson did not believe a person could take deductions off of self-employed income under the legislation.

Mr. Spanos agreed, if a person had a loss, the bill would allow the loss.

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Mr. Alper advanced to slide 26, "Revenue Impact":

- DOR estimates \$160 million in FY2019 due to the tax taking effect in January 2019*
- This amount is from withholding / employer payments
- No tax returns filed until April 2020
*(Assumes 1/1/19 effective date as proposed)
- DOR estimates \$320 million in FY2020 based on modeling using aggregated federal income data for Alaska residents

Mr. Alper moved to slide 27 titled "Revenue Details":

Revenue estimates are based on 2015 IRS Data

- About 440,000 total resident taxpayers, revenue \$280-\$290 million

68,000 below \$10,000 income

62,000 between \$10 and \$20,000
161,000 between \$20 and \$50,000
107,000 between \$50 and \$100,000
38,000 between \$100 and \$250,000
4,000 above \$250,000

- Net nonresident (after subtracting Alaskans who earn all their income outside) 12.5 percent, revenue \$40 million
- Without the cap, total revenue would be \$10 to \$20 million higher (foregone from high income individuals)

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Representative Pruitt asked how to deal with nonresident individuals.

Mr. Alper answered that the bill included a definition and regulations would flush the issue out. He detailed that from nonresidents it was a bit easier when they were wage employees.

Representative Pruitt provided a scenario where a company was located in Alaska but did business outside of the state. He asked if the income was considered derived from the state if the business was physically in Alaska.

Mr. Spanos replied that state's usually taxed residents on all of their income, and residents and nonresidents would be taxed the same. He furthered that for a wage earner it would be physical presence and wages would be taxed.

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Co-Chair Seaton asked if Mr. Spanos was talking about property, not rents.

Mr. Spanos answered that the property would not be taxable.

Mr. Alper noted that it was a parallel structure. The consideration would be what percentage of income was considered Alaskan for tax purposes.

Representative Pruitt referred to individuals earning money in another state, but who lived in Alaska. He wondered if

it depended on whether the individual paid tax in another state.

Mr. Alper responded that the individual would only be taxed if the work was in Alaska.

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Co-Chair Seaton asked about the difference between a taxpayer and a tax filer. He asked how the bill treated joint filers. He asked if distributions were broken out 50/50.

Mr. Alper answered that every person was considered a filer, there was no joint filer. It was an individual tax only; there was no mechanism in the bill to create a joint tax.

Co-Chair Seaton wondered if both spouses had the \$2,200 cap.

Mr. Alper answered that the taxes would be paid in the dual income household.

Co-Chair Seaton referred to partner distributions or self-employment tax. He wondered if it was only assigned to one of the household members.

Mr. Alper answered that he did not know. He deferred to Mr. Spanos.

Mr. Spanos restated his understanding of the question.

Co-Chair Seaton replied in the affirmative and asked about a single cap.

Mr. Spanos answered he had not researched the issue, but believed that a partnership could choose to distribute whatever amount it wanted.

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Mr. Alper believed it meant there were circumstances where a couple would have to pay two caps.

Co-Chair Seaton stressed that he was attempting to understand how the joint filing would occur.

Mr. Alper relayed that the questions were easy for a payroll or wage tax. He stated that the broadening a footprint into self-employment required the special provisions.

Co-Chair Seaton believed it was important to have a delineation showing how the joint filer impacted the proposed tax.

Mr. Spanos responded that the joint filing definition in the federal code, and noted that there was no definition for a married couple in the bill, so each employed individual would owe their own tax. In order to calculate your own returns, they had to know their individual earnings.

Representative Guttenberg used a scenario where Oregon had an income tax. He asked if Oregon currently was taxed on the entire income. He remarked that the employer would remove the tax in Alaska.

Mr. Alper agreed. He stated that a resident of a state that had an income tax, who earned income in Alaska, would pay the tax to Oregon on all their income. He stated that living in Oregon and working in California initiated the credit.

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Vice-Chair Gara understood the difficulty of implementing the tax immediately. He asked about the modest payroll tax and wondered if it would be possible to implement.

Mr. Alper answered that he was really talking about a voluntary taxation if it occurred before the effective date. He would not want to implement the tax in the middle of a calendar year and believed they were stuck waiting until April 2019.

Vice-Chair Gara did not mean to implement the tax prior to the bill's effective date. He meant implementing it prior to dealing with regulations in the department. He asked if it would be possible to ask the effective date to be January 1.

[3:22:11 PM](#)

Mr. Alper answered there was no staff currently attached to the bill; the department would have to hire the staff. He could not imagine getting anything functional between Thanksgiving and New Year's.

Mr. Alper moved to slide 28 titled "Fiscal note implementation cost":

- Implementing an individual income tax in 14 months will be a significant logistical challenge
 - Need to draft regulations
 - Need to design, develop, and test technology to administer tax system for over 400,000 taxpayers
- Estimated \$300,000 supplemental appropriation request for a contractor to work with DOR on an implementation plan
- Estimated \$10,000,000 one-time capital appropriation to build income tax into our current tax revenue system
 - Includes withholding, filing, and refunds
- Gradual ramp-up of staffing; eventual annual management cost estimate is \$5.2 million with 40 employees
- Total cost over six-year fiscal note period is about 2.5 percent of projected revenue.

[3:25:34 PM](#)

Mr. Alper advanced to slide 29 and continued to address the fiscal note implementation cost.

The Department of Revenue's Fiscal Note is somewhat conservative (meaning too high, we hope)

- Assumes stand-alone system built within the Tax Division
- Items that need to be pinned down (partial list):

- o How much can we limit individual reporting needs vs. relying on employer filing?
- o Process for self-employment filing system
- o Degree of electronic vs. paper filing
- o Potential coordination with Department of Labor (Employment Security Tax). This would have substantial challenges due to federal funding

Mr. Alper provided additional detail on slide 29. He hoped to do the work with 30 or less people. In comparison the full income tax bill that had passed the House called for 60 employees.

[3:27:41 PM](#)

Mr. Alper looked at slide 31, "Impact of Recession on Alaska's Economy":

Per the Alaska Department of Labor, since the peak:

- Overall economic activity in the state down 17 percent (much of this due to the reduction in the value of every barrel of oil)
- Total job losses 11,900 positions (3.3 percent)
- State government job losses 2,700 positions (>10 percent)
- State facility closures throughout the state

[3:29:30 PM](#)

Vice-Chair Gara stated that the DLWD had told committee members that the lost jobs were 13,500 in the last two years. He asked Mr. Alper to confirm the number.

Mr. Alper replied that he would provide that information. He stressed that there was an inherent seasonality.

Mr. Alper turned to slide 32 titled "ISER - Job Impact of Different Options." Each of the options would cost jobs in varying degrees. He moved to slide 33 and addressed multiple tax options that would each raise \$500 million. It

started to taper out because the highest earning individuals tended to get their income from things other than wages.

[3:34:17 PM](#)

Mr. Alper addressed the final slide titled "Comparable Tax Burden." The chart had been produced by Institute of Social and Economic Research (ISER). He detailed that Alaska mostly collected select sales taxes such as alcohol and other. The average Alaskan paid \$500 per year to the state; the average state was about \$2,700 and the highest were over \$4,000. If the bill passed it would mean Alaska's total taxation would be around \$1,000 and Alaska would still remain the lowest tax regime. He did not believe it would be material enough to make Alaskans move.

Representative Grenn referred to the last slide. He referred to the state's high property taxes and cost of living. He wondered if ISER had a comparative study including local taxation.

Mr. Alper replied he believed so; it would be worth layering into the presentation. Alaska was also unique in its over 400 municipal sales taxes; the weighted average was about 1.7 percent because Anchorage did not have a sales tax.

[3:38:13 PM](#)

Representative Pruitt referred to the earlier discussion about some people not wanting to take the Permanent Fund. He wondered if there was a way to come up with a way to use the money for state use.

Mr. Alper replied that it was a legal question. He stated that if a person chose to take the dividend and donate it to the state that person could do that.

Representative Pruitt wondered if there was a way for a person to choose not to claim their dividend. He stated that it came up all of the time. He believed there should be a way to provide the opportunity for individuals wanting to give their PFD. He did not want to penalize others in the process.

Commissioner Fisher would look into the issue.

Vice-Chair Gara stated he had asked the question for two years. He believed Legislative Legal Services agreed that if the dividend was made an offer for people to either accept or deny, it would mean it was not income.

Commissioner Fisher would look into the issue.

Mr. Alper added that APFC would testify the following week and could possibly weigh in on the issue.

Commissioner Fisher would follow up.

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

#

ADJOURNMENT

3:43:48 PM

The meeting was adjourned at 3:43 p.m.