

SENATE FINANCE COMMITTEE
January 31, 2017
9:01 a.m.

[9:01:35 AM](#)

CALL TO ORDER

Co-Chair MacKinnon called the Senate Finance Committee meeting to order at 9:01 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Anna MacKinnon, Co-Chair
Senator Click Bishop, Vice-Chair
Senator Mike Dunleavy
Senator Peter Micciche
Senator Donny Olson
Senator Natasha von Imhof

MEMBERS ABSENT

None

ALSO PRESENT

Dan Stickel, Chief Economist, Economic Research Group, Department of Revenue; Ky Clark, Economist, Economic Research Group, Department of Revenue; Alexei Painter, Fiscal Analyst, Legislative Finance Division.

PRESENT VIA TELECONFERENCE

SUMMARY

PRESENTATION: INDIRECT EXPENDITURES COST AND
RECOMMENDATIONS

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RECOMMENDATIONS

[9:02:20 AM](#)

Co-Chair MacKinnon discussed housekeeping.

DAN STICKEL, CHIEF ECONOMIST, ECONOMIC RESEARCH GROUP, DEPARTMENT OF REVENUE, introduced himself.

KY CLARK, ECONOMIST, ECONOMIC RESEARCH GROUP, DEPARTMENT OF REVENUE, discussed the presentation "Overview of DOR's Indirect Expenditure Report, Preliminary Report for FY 2011-FY 2015," (copy on file).

Mr. Clark addressed Slide 4, "Indirect Expenditure Report Overview":

- Passed in 2014 and signed on July 7, 2014 (House Bill 306)
- **Requires DOR to submit a report to the Legislature biennially on July 1 detailing indirect expenditures of all agencies in the State (AS 43.05.095)**
- Requires the Legislative Finance Division to provide a report to the Legislature on the indirect expenditures of certain agencies before the start of Legislative Session following the release of DOR's biennial report
- The first DOR Indirect Expenditure Report was released the day after the bill was signed, July 8, 2014
- The second DOR Indirect Expenditure Report was released July 1, 2016

[9:05:56 AM](#)

Mr. Clark showed Slide 5, "Indirect Expenditures Defined":

Indirect expenditure: Any foregone revenue by the state designed to encourage an activity to benefit the public in the form of a credit, exemption, deduction, deferral, discount, exclusion, or other differential allowance.

As defined by AS 43.05.095(d):

- An **express provision of state law** that results in foregone revenue for the state by providing:
- A tax credit or other credit
- An exemption, but does not include federal tax exemptions adopted by reference in AS 43.20.021
- A discount

- A deduction, but does not include costs incurred in the ordinary course of business that are deducted in the calculation of a tax under this title or in the calculation of a royalty or net profit share payment for a lease issued under AS 38
- A differential allowance

[9:06:46 AM](#)

AT EASE

[9:06:53 AM](#)

RECONVENED

Co-Chair MacKinnon conveyed that the documents discussed during the meeting could be found on the Division of Legislative Finance webpage, as well as BASIS.

Co-Chair MacKinnon whether the foregone revenue noted on Slide 5, was revenue that the state was not receiving, based on what was described in state statute.

Mr. Clark answered in the affirmative. He said that an indirect expenditure would be described as foregone revenue.

Co-Chair MacKinnon clarified for the public that what this meant was that the state was not receiving money for a particular item. She explained that the money was money the state could be receiving, were it not for the exclusions written into statute, which are called indirect expenditures.

[9:08:08 AM](#)

Mr. Clark reviewed Slide 6, "DOR Indirect Expenditure Report":

- Released July 1, 2016 by DOR
- Provides details on 231 indirect expenditures across 11 departments and agencies, including 78 provisions administered by DOR
- A cooperative effort between 10 departments and other participating agencies, coordinated by DOR

- Followed process established in 2014, with improved presentation and some refinements

Mr. Clark indicated that the indirect expenditure report had been a collaborative effort between state agencies, and had been facilitated by the Department of Revenue (DOR). He specified that the report supplied details on 231 indirect expenditures across 11 state departments and agencies, 78 of the 231 total expenditures were administered by DOR. He explained that the department had followed the same process that had been established in 2014 with the first indirect expenditure report produced by DOR. He said that minor improvements had been made to the process, including an improved presentation that included a more expansive introduction. He stated that the consistency of the reporting methodology had been improved.

[9:09:59 AM](#)

Mr. Clark turned to Slide 8, "Methodology-Internally":

- Surveyed all Tax Division workgroups and all divisions within DOR to ensure complete list
- Developed tax database reports to generate DOR data for the Indirect Expenditure Report
- Developed consistent definition for "Fiscal Year" given that tax types are mostly on a monthly, quarterly, or calendar year basis
 - Necessary because of time lag in receiving information for certain tax types (corporate, mining, et cetera)
 - Production tax not impacted by this issue, since we receive detailed monthly data for production tax.

Mr. Clark said that the development of the tax database had been helpful to the department internally by securing all the data in one place.

[9:12:32 AM](#)

Mr. Clark reviewed Slide 9, "Methodology-Internally":

- Internally: Addressing Fiscal Year Issue, cont.

- o Determined that the Fiscal Year includes any tax periods beginning during the fiscal year, using the "tax period beginning" date
 - For example: FY* 2015 corporate tax data will include any returns for periods beginning July 2014 -June 2015 (primarily 15 calendar-year returns)
 - Similar to how federal tax data is reports by the Internal Revenue Service
- o Because of new parameters, some FY 2015 DOR data is "unavailable"
 - Some fiscal year filer returns are not received until spring 2017
 - For example, a corporate tax return beginning June 2015, with extension, would be due in March 2017

[9:14:34 AM](#)

Co-Chair MacKinnon asked whether revenue foregone inside of the report was reflected conservatively inside the report, thus increasing the reporting number for cost savings.

Mr. Stickel responded that the way that FY 15 had been defined for the indirect expenditure report had resulted in an amount of revenue impact beyond what was reflected in the report. He provided education credits as an example; for FY 15, there had been approximately \$5 million in education credits claimed in the system, which was an incomplete number and was above and beyond what was shown in the book.

Co-Chair MacKinnon referred to Page 51 of the Indirect Expenditure Report, January 2017, Legislative Finance Division, www.legfin.akleg.gov. She noted that the page showed that the Department of Education and Early Development, Alaska Student Loan Corp, Alaska Commission on Postsecondary Education WWAMI Graduate Medical Education Program had nearly \$1.6 million in foregone revenue. She understood that state statute required that students in the program be encouraged to come back to Alaska to practice medicine. She relayed that 50 percent of the financial support provided by the program would have to be paid back to the state. She asked whether the number was complete, or whether there could be trailing numbers that could increase the cost or revenue impact.

Mr. Stickel thought the LFD number was complete. He pointed to the committee that there were two indirect expenditure reports, one was created by DOR, the other by LFD. He shared that the DOR report was posted at www.tax.alaska.gov.

[9:18:05 AM](#)

Co-Chair MacKinnon asked whether the DOR report was reviewed in the LFD report.

Mr. Stickel answered in the affirmative.

Co-Chair MacKinnon reiterated that the LFD report offered a legislative perspective based in the information provided by DOR.

Mr. Stickel answered in the affirmative. He elaborated that the administration surveyed all the agencies within state government and then produced a report in July of every other year. He said that LFD then would produce a report of the DOR report, examining in greater detail the indirect expenditures for a certain set of departments each year, making recommendations about the indirect expenditures.

Co-Chair MacKinnon understood that an overview of all credits would have been posted to the DOR website from year-to-year.

Mr. Stickel replied in the affirmative.

[9:19:11 AM](#)

Mr. Clark discussed Slide 10, "Methodology-Externally":

Externally:

- DOR met with other departments and agencies and sent out a survey for the report
- Each agency examined their operations to identify indirect expenditures and report the required information
- A few departments identified provisions that did not actually meet the definition of an "indirect expenditure"
 - Submissions from other departments and agencies are not independently verified

Mr. Clark relayed that the following slide would show items that could be confused for indirect expenditures that were in fact not.

[9:20:29 AM](#)

Mr. Clark showed Slide 11, "Methodology-Externally cont.":

Examples of provisions not meeting definition of "Indirect Expenditure":

- Alaska Housing Finance Corporation (AHFC)
 - Identified one potential indirect expenditure; reduced loan rates. But, it was part of their normal operations and not "required by statute." Statutorily, AHFC can set the rates.
- Department of Commerce, Community, and Economic Development (DCCED):
 - Has certain licensing fees, which are set by statute to cover program costs, that were reduced for residents vs. non-residents. It was determined not be foregone revenue, because the fee differential doesn't affect total revenue.
- University of Alaska (UA):
 - Addressed tuition waivers to employees and dependents; they are a part of the employee's benefit package, so are not considered foregone revenue.
 - Non-resident vs. Resident tuition; UA is not discounting the resident tuition rate, rather the out-of-state student is paying a non-resident surcharge (so no foregone revenue).

[9:22:20 AM](#)

Co-Chair MacKinnon asked whether the DOR report provided a list of the different agencies, including any feedback, that had not met the definition of foregone revenue.

Mr. Clark answered in the affirmative. He lamented that the list had not been included in the report. He shared that the report contained a list of state agencies that the department had reached out to who had responded to the survey, and a list of agencies that had completed the survey but had reported no indirect expenditures.

Co-Chair MacKinnon understood there was no definitive list, only the examples provided in the report.

Mr. Clark answered in the affirmative.

[9:23:46 AM](#)

Mr. Clark turned to Slide 12, "Reported Information":

Each department was required to report the following information:

- The name of the indirect expenditure
- A brief description
- The statutory authority
- The repeal date, if applicable
- The intent of the legislature in enacting the statute authorizing the indirect expenditure
- The public purpose served by the indirect expenditure
- The estimated revenue impact of the indirect expenditure for the previous five fiscal years (excluding the fiscal year immediately preceding the date the report is due)
- The estimated cost to administer the indirect expenditure, if applicable
- The number of beneficiaries of the indirect expenditure and who benefits

Mr. Clark noted that the above items were required by statute to be reported; additionally, the department had required 2 additional items of information including the year that the indirect expenditure was enacted, and the type of indirect expenditure. He said that the department defined direct expenditures differently, whether a credit, deduction, or discount, based on the information provided by the departments.

[9:25:36 AM](#)

Senator Micciche spoke to Page 117 of the LFD report, which listed the indirect expenditure for the royalty modification for Oogururk Unit. He said that although the costs were substantial, the likely revenue impacts would be considerable. He wondered whether offsetting benefits to the state should be considered in future projections.

Mr. Stickel acknowledged that both sides of the equation should be examined when evaluating indirect expenditures.

He shared that the department had broadly captured the benefit of the expenditures in the "public purpose" line on Page 117, which was to "stimulate increased production on ANS." He thought that delving into deeper detail to quantify the benefit would be prudent when considering making changes to the indirect expenditure.

Senator Micciche felt that there should be a line that listed the offset financial benefit to the state, and offered to provide DOR with a list of instances. He thought that this could replace the "public purpose" line, and was a valuable benefit that had not been captured in the report.

Co-Chair MacKinnon wondered how the numbers varied under Alaska's Clear and Equitable Share (ACES) versus the Petroleum Production Tax (PPT).

Senator Micciche said that he would have to research the question.

Co-Chair MacKinnon asked whether statutory change would be needed to include the revenue offset of each indirect expenditure. She noted that some of the projects listed were foregoing revenue in order to produce a product that generated revenue. She thought that it was fair to say that if the indirect expenditure were eliminated for the project on Page 117, the \$26 million could be used for government operations, but then she countered that consequently the state would lose the revenue that the credit had been intended to help generate.

[9:29:49 AM](#)

Senator Micciche thought that the numbers in the report could be more nuanced.

Co-Chair MacKinnon concurred that there were specific items that had been put into place to create a long-term benefit for the state and should be noted.

Mr. Stickel concurred, and noted that future slides would discuss future plans. He shared that DOR was actively soliciting ideas for how the report could be more useful to the legislature. He said that DOR was planning to meet with LFD over summer 2017, to work on improvements to the report.

[9:31:12 AM](#)

Mr. Clark moved to Slide 13, "Overview of DOR's Indirect Expenditure Report":

- Introduction, discussing the purpose of the report, what is included in the report, and an explanation of the limitations of the report
- The indirect expenditures are organized by:
 - Departments, alphabetically
 - Divisions, alphabetically
 - Grouped by Program Name (if applicable)

[9:32:51 AM](#)

Mr. Clark viewed Slide 14, "Future Plans":

- Reaching out to the Office of Management and Budget and the Legislative Finance Division concerning the next Indirect Expenditure Report
- Compiling feedback and suggestions which may be incorporated into the next report in Summer 2018
- Discussion with agencies of their ability to provide more information for certain indirect expenditures

[9:33:53 AM](#)

Mr. Stickel reviewed Slide 16, "Recommendations and Considerations":

- DOR was asked to provide the committee with recommendations regarding indirect expenditures
- DOR identified several areas for the committee to consider:
 - House Bill 155 from 2015-2016
 - Largest indirect expenditures overall
 - Largest indirect expenditures by department
 - Review of recommendations produced by the Legislative Finance Division
 - Indirect Expenditures were reviewed in both January 2015 and January 2017
 - Fee Setting Authority

Mr. Stickel reminded the committee that the suggestions were not formal recommendations to change or repeal any individual indirect expenditures.

[9:34:32 AM](#)

Mr. Stickel looked at Slide 17, "House Bill 155 from 2015-2016":

- The following indirect expenditures were addressed in a proposed bill:
 - Tobacco Products Tax
 - Gives a four-tenths of one percent deduction to cover the expense of account and filing the return for the tobacco tax
 - FY 2015 revenue impact of \$54,053
 - Cigarette Tax
 - Gives a discount of up to \$50,000 as compensation for affixing stamps to packs of cigarettes
 - FY 2015 revenue impact of \$360,326
 - Motor Fuel Tax
 - Gives a timely filing credits of 1% of the total monthly tax due to a maximum of \$100
 - FY 2015 revenue impact of \$62,590
 - Large Passenger Vessel Gambling Tax Deduction
 - Allows a deduction of federal and municipal taxes paid from gambling gross income
 - Revenue impact is unknown

[9:36:14 AM](#)

Mr. Stickel turned to Slide 18, "Largest Indirect Expenditures":

- Oil & Gas Tax Credits (FY16 = \$598 million)
- Mining License Tax -Depletion Deduction (FY14 = \$32 million)
- Insurance: all programs -Lower Tax Rate (DCCED*) (FY15 = \$13 million)
- Insurance: all programs -Deduction from premiums written for claims paid (DCCED*) (FY15 = \$13 million)
- Commercial Passenger Vessel Taxes -Tax Reduction for Local Levies (FY15 = \$13 million)

- Multiple Tax Programs -Film Production Credit (FY15 = \$9 million; credit phasing out under current law)
- Motor Fuel Tax -Foreign Flight Exemption (FY15 = \$8.6 million)
- Sport Fishing, Hunting & Trapping Senior Discount (FY15 = \$6.8 million)

Mr. Stickel informed the committee that the Film Production Credit had been repealed, with credits still working their way through the system.

[9:38:16 AM](#)

Co-Chair MacKinnon shared that the committee was crafting a tax credit bill, and asked that Mr. Stickel forward any ideas to her office.

[9:38:45 AM](#)

Mr. Stickel discussed Slide 19, "Recommendations from Legislative Finance":

- There are recommendations made by Legislative Finance Division in both their 2015 & 2017 Indirect Expenditure Reports
- 2015 Report
 - Recommended 17 indirect expenditures be terminated
 - Recommended 33 indirect expenditures be reconsidered
 - Recommended 24 indirect expenditures be reviewed
 - Recommended 37 indirect expenditures be continued
- 2017 Report
 - Recommended 2 indirect expenditures be terminated
 - Recommended 13 indirect expenditures be reconsidered
 - Recommended 3 indirect expenditures be reviewed
 - Recommended 48 indirect expenditures be continued

Mr. Stickel expanded that in total, LFD had identified 92 indirect expenditures had been recommended for review in some capacity.

[9:39:33 AM](#)

Senator von Imhof asked whether there was a way to compile the recommendations into an easily navigable spreadsheet.

Co-Chair MacKinnon indicated that a spreadsheet for some of the items had already been established, but agreed that it would be helpful if the department provided an Excel spreadsheet for easier review of the recommendations.

[9:41:34 AM](#)

Vice-Chair Bishop queried how many hours it took the department to prepare the indirect expenditure report.

Mr. Stickel specified that the task required a couple of months of dedicated work by one economist, and then a part-time project for the remainder of the year. He stated that the report took several hundred employee hours within the department.

[9:42:11 AM](#)

Senator von Imhof lauded the report as easy to navigate and informative.

Co-Chair MacKinnon commented that all the information contained in the report was very important. She reiterated that an Excel spreadsheet could make the book even more useful.

Mr. Stickel reported that the division had the data in an Excel spreadsheet, and would be happy to work with the committee to create a finely tuned document that met committee specifications.

Co-Chair MacKinnon said that she would request the spreadsheet from LFD.

[9:44:18 AM](#)

Senator Micciche commented that some recommendations were based on what was currently known. He noted Page 69, which listed the indirect expenditure of the inspection fee exemption for hair and nail salon operators. He pointed out that DOR had recommended charging a fee, he thought that a

policy of self-compliance, and self-inspection, would be more appropriate.

[9:45:10 AM](#)

AT EASE

[9:46:03 AM](#)

RECONVENED

Senator Micciche stated that DOR had provided a valuable report, but that the committee had suggestions for making it more effective. He said that the legislature could explore different ways to fund programs that were of less cost to the state and to licensees.

Mr. Stickel clarified that the division's role at DOR was to identify the universe of indirect expenditures, while the LFD drilled down into a certain subset of that universe for each of their reports and then made recommendations. He differed conversation to any specific recommendation to LFD.

[9:47:29 AM](#)

Mr. Stickel looked at Slide 20, "Fee Setting Authority":

- Legislature has granted fee setting authority to certain agencies, for example:
 - o Department of Transportation and Public Facilities
 - Alaska Marine Highway (AMHS): foregone revenue related to AMHS discounts amounted to over \$4.7 million in FY 2015
 - o University of Alaska
 - Scholarship awarding authority
 - Western Undergraduate Exchange
 - Senior Citizen Tuition Waiver
 - o A comprehensive review would likely identify other examples
- Discounts offered by agencies with fee setting authority may not qualify as "indirect expenditures" since they are not an "express provision of state law"

Mr. Stickel relayed that DOR was aware of areas of foregone revenue in the state that did not meet the statutory definition of indirect expenditure, one of which was fee setting authority.

[9:49:15 AM](#)

Senator Micciche thought a large area of revenue impact was discounted loan rates [page 88 - 91 in the 2017 LFD IER]. He thought there was likely a federal program that could help with to offset the cost of the program.

Co-Chair MacKinnon suggested that the issue could be discussed with LFD to further the understanding of how the state's revenue stream was being affected by different state statutes that had been implemented over time.

[9:51:30 AM](#)

Co-Chair MacKinnon thanked the testifiers for their presentation.

[9:52:02 AM](#)

AT EASE

[10:00:19 AM](#)

RECONVENED

ALEXEI PAINTER, FISCAL ANALYST, LEGISLATIVE FINANCE DIVISION, addressed questions that had been raised by the committee during the previous presentation. He confirmed that LFD had a sortable Excel document that had been prepared for the report issue two years prior, which he could resend to committee members. He said that the same document could be updated to reflect the most current report and distributed to members. He noted that the DEC provisions identified by Senator Micciche were a good example of provisions that had an offset; the federal government required the state to have the discount, and funded it, in order for the state to offer the loan program. He furthered that it was not revenue that the state could receive because it was a condition of the federal program. He felt it should not have been in the report, but that DEC had included it in an attempt to be thorough. He added that due to budget cuts DEC no longer provided inspections for hair and nail salons, which was why the recommendation had been made to reconsider the structure that statutorily mandated inspection without offering a funding source.

[10:02:13 AM](#)

Senator Micciche thought that the report could be "scrubbed" for clarity. He believed that self-certification would take the cost away from the state and the licensee.

Co-Chair MacKinnon commented that creation of a table that highlighted the offset funding could be helpful.

[10:03:57 AM](#)

Mr. Painter discussed the presentation "Overview of Legislative Finance Division Indirect Expenditure Reports," (copy on file).

Mr. Painter addressed Slide 2, "Agencies in 2015 Report":

- Commerce, Community and Economic Development
- Fish and Game
- Health and Social Services
- Labor and Workforce Development
- Revenue Legislative

Mr. Painter detailed that LFD made their recommendations for select agencies, every two years, based on the DOR reports.

[10:04:31 AM](#)

Mr. Painter discussed Slide 3, "Summary of 2015 Recommendations":

- Terminate: 17 provisions
 - Total known revenue impact of \$5 million (in FY14)
 - Three provisions had unknown revenue impact
- Modify or review: 59 provisions
- Continue: 37 provisions
- No recommendation: 25 provisions

Mr. Painter noted that there had been some area of statute that LFD had felt deserved a closer look of the entire fee structure, which added to the 59 provisions suggested for modification or review. He noted that the legislature had modified the fee schedule since the report was issued. He added that many of the provisions of the Mining License Tax dated back to statehood, which made it difficult to determine whether they met current legislative intent as the structure as most likely out-of-date. He detailed that

the 25 provisions that had no recommendation were because LFD did not believe that the item was an actual indirect expenditure, or because there had been insufficient information. He noted that, for example, some of the tax credits with very few recipients, had confidential revenue impacts.

[10:06:40 AM](#)

Mr. Painter turned to Slide 4, "2015 Report Key Points":

- Did not review oil tax credits, which had been modified a year before
- 1 "terminate" item (obsolete exploration incentive) repealed in HB 247
- 4 other "terminate" items were in HB 155, which passed House in 2016 but not Senate
- 6 "terminate" items are in Corporate Income Tax
- 3 "terminate" items are in Commercial Fisheries Entry Commission

Mr. Painter detailed that LFD had prepared the report in the fall of 2014, at which time the oil tax structure had been undergoing a referendum, and had recently been modified by the legislature.

[10:07:50 AM](#)

Mr. Painter spoke to Slide 5, "Agencies in 2017 Report":

- Administration
- Education and Early Development (including Alaska Student Loan Corporation and Alaska Commission on Postsecondary Education)
- Natural Resources
- Transportation
- Judiciary
- Plus review of the Education Tax Credit, which is scheduled to sunset at the end of 2018.

Mr. Painter noted that he had overlooked putting Department of Environmental Conservation on the list on Slide 5. He pointed out that the Education Tax Credit had been reviewed because LFD felt that it was important that a detailed recommendation be made for the credit which was scheduled to sunset at the end of 2018. He shared that the credit had not been reviewed in the first report because it had been

modified by the legislature that year, making it too early to evaluate the impact.

[10:08:27 AM](#)

Mr. Painter showed Slide 6, "Summary of 2017 Recommendations":

- Terminate: 2 provisions
 - Unknown revenue impact
- Modify or review: 13 provisions
- Continue: 56 provisions
- No recommendation: 6 provisions

[10:08:52 AM](#)

Mr. Painter discussed Slide 7, "2017 Report Key Points":

- Some items do not have revenue generation as a goal ("fix-it" tickets)
- Others have authority to set fee structure (Marine Highway)
- Remainder are mostly routine (senior discounts, fee waivers for disabled veterans, etc.)
- Some provisions in DEC and DNR could be reviewed

Mr. Painter explained that some items were not considered indirect expenditures because their main goal was not to generate revenue. He said that in 2019, all the remaining agencies were up for indirect expenditure review; however, there were no remaining agencies that had identified indirect expenditures. He announced that LFD would not produce a 2019 report, but would begin the cycle over again in 2021 - starting with DOR.

[10:11:00 AM](#)

Senator Micciche appreciated the recommendation to review the Alaska Marine Highway System children's discounted tariffs, employee and annual passes, and the underage discounted tariffs. He thought that more cuts should be made to the Alaska Marine Highway System.

Co-Chair MacKinnon asked whether any of the provisions for the marine highway were part the employee bargaining unit.

Senator Micciche did not believe that the three he mentioned were related to a bargaining unit.

10:13:27 AM
AT EASE

10:14:38 AM
RECONVENED

Co-Chair MacKinnon discussed housekeeping.

ADJOURNMENT
10:15:39 AM

The meeting was adjourned at 10:15 a.m.