

HB

472

SFIN

FILE

SENATE FINANCE COMMITTEE REPORT

DATE: 4/9/98

FURTHER: REPORTED OUT OF
4/17/98

DATE TURNED
IN TO OFFICE: 4/17/98

Finance Committee considered HOUSE BILL NO. 472

"An Act relating to apportionment of business income."

and recommends:

- be replaced with 5 CS HB 472 (FIN)
- adopt previous _____ CS _____ (_____)
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to the _____ Committee

- Senate Bill: same title
- new title
- House Bill: same title
- technical title
- new: SCR# _____

SIGNING DO PASS	DP	OTHER RECOMMENDATIONS	NR	DNP	AM
<i>John Ingram</i>	✓	<i>Roll E (HOD)</i>	✓		
		<i>Frank Hamill</i>	X		
		<i>Albert P. Gar</i>		X	
Co-Chair:		Co-Chair: <i>[Signature]</i>	✓		
Co-Chair:		Co-Chair: <i>[Signature]</i>	✓		

NEW FISCAL NOTE(S):

Department Date Zero Fiscal

PREVIOUS FISCAL NOTE(S):*

Department Date Zero Fiscal

Rev./Income + Excise	3/30/98	0	

APPROPRIATION -- no fiscal note

*include fiscal notes accompanying Governor's bill

STATE OF ALASKA
1998 LEGISLATIVE SESSION

FISCAL NOTE

Bill Version: HB 472

(H) Publish Date: 3/31/98

Revision Date: _____ Dep. Affected: _____ Revenue _____
 Title: Apportionment of Business Income BRU: _____ Revenue Operations _____
 Component: _____ Income and Excise Audit 4/1/98
 Sponsor: (H) L&C
 Requestor: (H) L&C COMPONENT SERIAL NO. 113

Expenditures/Revenues: (Thousands of Dollars)

	FY 99	FY 00	FY 01	FY 02	FY 03	FY 04
OPERATING EXPENDITURES						
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL EXPENDITURES						
CHANGE IN REVENUES - Loss	\$3,000.0 - \$8,500.0	\$3,000.0 - \$8,500.0	\$3,000.0 - \$8,500.0	\$3,000.0 - \$8,500.0	\$3,000.0 - \$8,500.0	\$3,000.0 - \$8,500.0

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1001 CBRF						
1048 University of AK receipts						
Other						
TOTAL						

Estimate of any current year cost \$ _____

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary)

Please see attached analysis.

Prepared by: Brett Fried, Economist
 Division: Income and Excise Audit
 Approved by Commissioner: Wilson L. Condon
 Agency: Revenue

Phone: 465-3682
 Date: March 30, 1998
 Date: March 30, 1998

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COMMITTEE COPY

HB 472 (L&C)
Apportionment of Business Income
Fiscal Note Analysis
March 30, 1998
Page 2

HB 472 – Apportionment of Business Income

HB 472 would amend Alaska's Corporate Income Tax to specifically incorporate Section 883 of the Internal Revenue Code. Alaska would exempt from tax the income of foreign owned aircraft and ships, under the legislation.

Overview of Section 883

The Alaska Supreme Court, on February 20, 1998, decided a case that determined that the federal corporate income tax exemption that applies to income from foreign owned ships and aircraft does not apply in Alaska. The federal provision is Section 883 of the Internal Revenue Code. The court held that, while Alaska incorporates much of the code into the Alaska Corporate Income Tax (AS 43.20), Section 883 was "excepted to or modified by" Alaska's choice of the apportionment method of determining taxable income in Alaska. The decision makes it clear that these entities are subject to tax in Alaska.

Revenue Effect

The state will collect less revenue by changing the statutes to exempt income from foreign owned ships and aircraft from Alaska income tax. We have had little time and we have very limited information available to develop projections of potential corporate tax revenue from the recent court decision on the taxation of foreign shipping corporations. Consequently, we have developed a range based on estimates of Alaska corporate income tax revenue from foreign cruise ship corporations, foreign air cargo corporations and foreign corporations shipping fish. We do not have financial information available to review the other segments of the shipping industry (mining and timber). To develop this range we used publicly available financial statements, information from taxpayer returns, and other industry specific data available from State agencies and other sources.

Based on the above paragraph our estimate of the range of potential annual revenue lost due to the passage of this bill is \$3.0 million to \$8.5 million.



Alaska Steamship Association

234 Gold Street • Juneau, Alaska 99801
(907) 586-3107 • Fax (907) 586-1001

MEMORANDUM

April 14, 1998

Sent via fax

To: Deborah Vogt, Department of Revenue
Jeff Bush, Department of Commerce and Economic Development
Representative Norm Rokeberg
Senator Bert Sharp


From: Joe Kyle
Executive Director, Alaska Steamship Association

Subj: Department of State Letter re HB - 472 & SB - 345

Attached, please find a letter from the Department of State relative to the proposed corporate tax on foreign, international air and sea carriers of commerce.

We hope this letter helps place HB - 472 and SB - 345 in context with national policy goals.

Again, we urge that the legislature and the administration act swiftly to prevent the imposition of this new, corporate tax.

Captain John Cox, President •  • James Fernie, Treasurer • Dan Blackmore, Secretary



United States Department of State

Washington, D.C. 20520

April 13, 1998

Honorable Tony Knowles
Governor, State of Alaska
Third Floor, State Capitol
P.O. Box 11001
Juneau, Alaska 99811-0001

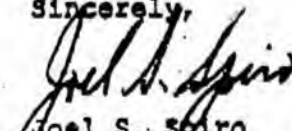
Dear Governor Knowles:

Action by the Alaska State Legislature to prevent the imposition of income taxes on foreign transportation companies has recently come to our attention. This move is consistent with United States policy. We and our international trading partners agree that such taxes are not in our mutual interests. By preventing the imposition of these taxes, Alaska will join other states, most recently, New York, New Jersey, and California, in recognizing that they work against economic growth. Currently, no States apply such taxes.

This is an active area of foreign policy. The U.S. Department of State is currently engaged in maritime and aviation income tax exemption treaty negotiations with several countries. At present, the U.S. Government exempts from federal income tax, on a reciprocal basis, maritime companies and airlines from over ninety countries that accord similar treatment to our transportation companies.

The U.S. Department of State and other government agencies will gladly provide information and other assistance to you, your tax authorities and state legislators who may wish to have more details on this important international trade issue.

Sincerely,


Joel S. Spiro
Deputy Assistant Secretary
for Transportation Affairs



Anchorage Economic Development Corporation
The Center of Opportunity

April 9, 1998

Senator Robin L. Taylor
State Capitol (MS 3100)
Juneau, AK 99801-1182

Dear Senator Taylor:

The Anchorage Economic Development Corporation supports HB 472, An Act Relating to Apportionment of Business Income. This bill will overturn the recent decision of the State Supreme Court to allow the state to tax income from ships and aircraft owned by foreign corporations doing business in Alaska. The Alaska Corporation Net Income Tax would be applied to past, present and future net operating income. The State of Alaska depends on tourism and trade as its principal economic engines. Trade includes the export of oil and gas as well as seafood, timber and air cargo. The AEDC believes the implementation of business income taxes on foreign carriers selectively will have a significant deleterious effect on trade for the State of Alaska far in excess of any direct revenue obtained by the measure.

1. The State of Alaska would be the only state in the nation to impose such a tax. This would send a negative signal to some of Alaska's most important trading partners, such as Japan. The 1972 income tax treaty between Japan and the United States would be compromised. If any American state imposes such a tax, Japan would reciprocate against all American carriers. This principle has already been tested in New Jersey and New York several years ago.
2. Imposing this tax would negate the recently secured U. S. Department of Transportation ruling for Alaskan international airports to allow expanded cargo transfer among international and domestic carriers with traffic rights in Alaska. The recently concluded bilateral aviation agreement would be compromised by this action. The promotion of the air cargo industry and related logistics and value added manufacturing would suffer a severe set back at a crucial time. The market for international cargo trade is extremely competitive, with narrow margins determining the distinctions among competing locations. The imposition of a selective tax on international carriers would have a negative effect on some of Alaska's strongest contributors to cargo trade.
3. The imposition of this tax will discourage high value job development in Alaska. For each \$50 million generated in taxes, approximately 1,000 existing jobs would be lost. Such a tax discourages investment in Alaskan projects and operations because it raises the cost of transportation to foreign destinations. Alaska depends on foreign markets for the economic value of its export products. The Alaska market is not large enough to sustain the economy here alone, and the American domestic market is not the only destination of Alaskan goods.

4. The imposition of this tax retroactively to 1992 connotes a punitive approach to international carriers. This sends the wrong message to foreign corporations and poses troubling questions for all business investors regarding the prospective taxation policies of Alaska toward business.

The growth and diversification of the Alaska economy is essential for the long term viability of the state. A prosperous future will only occur in an environment where taxation and revenue policies are fair and evenly distributed on a sound policy basis. The imposition of a tax on foreign carriers unfairly affects Alaska's most important trading partners. This measure will have a negative effect on Alaska's competitive standing in world trade. This selective foreign carrier tax must not be implemented unilaterally by Alaska.. The AEDC urges your favorable action on HB 472 to remove this impending disaster.

Please feel free to contact me at (907) 258-3700 with any questions or concerns you may have.

Sincerely,



Patricia M. DeMarco, Ph.D.
President

cc: Governor Knowles





International Air Transport Association

IATA Centre, Route de l'Aéroport 33
P. O. Box 416
CH-1215 Geneva 15 Airport
Switzerland

**Facsimile No: +1 (907) 465-2070
(2 Pages)**

Senator Bert Sharp
Co-Chair, Senate Finance Committee
Alaska State Senate
State Capitol, Room 516
Juneau, Alaska 99801-1182
United States of America

6 April 1998
Ref: 045/98

Re: Senate Bill No. 345

Dear Senator Sharp,

On behalf of the International Air Transport Association (IATA), the trade association comprised of 256 member airlines from over 150 countries, I wish to express the strongest support for Senate Bill No. 345. SB 345 would ensure that the income of non-U.S. airlines serving Alaska would be exempt from the state's income tax in accordance with U.S. Intern. l Revenue Code Section 883.

IATA is deeply concerned with the potentially far-reaching ramifications of the recent Alaska Supreme Court decision in *Alaska v. OSG Bulk Ships, Inc.* Indeed, it is our understanding that on the basis of this decision, the Department of Revenue plans to levy Alaska corporate income tax on the income derived by non-U.S. airlines from the operation of their aircraft in international traffic.

It is widely known that U.S. IRC Section 883 exempts the income of non-U.S. airlines at the federal level on the basis of reciprocity. These reciprocal exemptions are generally embodied in numerous U.S. treaties for the avoidance of double taxation. IATA firmly believes that U.S. IRC Section 883 is intended, *inter alia*, to eliminate the risk of multiple taxation of the income derived by the aircraft of both U.S. and non-U.S. airlines in international traffic.

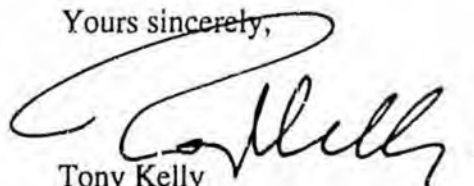
If the State of Alaska chooses not to adhere to the reciprocal tax exemption provisions of U.S. IRC Section 883, non-U.S. airlines will be exposed to double (and even multiple) taxation, as they are already subject to national (and often local) income taxes in their respective countries of domicile. Furthermore, one immediate consequence of this tax

treatment of non-U.S. airlines will be the exposure of U.S. airlines to the reciprocal imposition of similar taxes in the many foreign jurisdictions which they serve. Ultimately, the intricate worldwide network of reciprocal tax regimes will be seriously jeopardized.

IATA also believes that any imposition of an income tax on the international operations of the non-U.S. airlines serving Alaska would ignore the taxes and charges already paid by them for their local operations as well as the significant direct and indirect contributions they make to the economy of the state. We believe that SB 345 sends a strong signal to the international airline community that the State of Alaska encourages their business on the basis of long-established international tax practice.

Based upon the foregoing, IATA strongly urges you to take all necessary steps to ensure the passage of Senate Bill No. 345.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Tony Kelly', with a large, sweeping flourish above the name.

Tony Kelly
Director

Industry Monetary Affairs

AFOGNAK NATIVE CORPORATION



**TIMBER MARKETING OFFICE
104 CENTER ST., SUITE 201B
KODIAK, AK 99615
907-486-5808
FAX 907-486-4262**

April 6, 1998

The Honorable Bert Sharp
Alaska State Senate
State Capitol
Juneau, Alaska 99801-1182

RE: SB 345

Dear Senator Sharp:

We are extremely displeased that the Alaska Department of Revenue is poised, as a result of a recent decision by the Alaska Supreme Court, to implement a new corporation business tax on foreign, international air and sea carriers operating in the State of Alaska.

Our company depends on international shipping to move our products overseas to international markets. The tax will ultimately be passed directly back to us through the carriers we use. Aside from the new tax being passed on to businesses operating in Alaska, it will invite retaliatory taxes on domestic water borne carriers serving the Pacific Rim. Most significantly the tax is impractical to enforce because of the access it requires to the accounting records of foreign ship owners, and is in contravention of international trade practices.

Alaska would be the only state in the Union imposing such a tax if it decides to move forward. Other states have rejected this form of taxation.

Therefore, we strongly urge that you move forward with SB-345 so that the Department of Revenue will be preempted from imposing this onerous, new tax.

Sincerely,

A handwritten signature in black ink that reads "James E. Carmichael". The signature is written in a cursive style.

James E. Carmichael
Marketing Manager



Resource Development Council for Alaska, Inc.

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(907) 276-0700 Fax: (907) 276-3387 e-mail: rdc@aonline.com

Founded 1975

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April 6, 1998

Senator Loren Leman, Chairman
Senate Labor and Commerce Committee
Alaska State Legislature
State Capitol, (MS 3100)
Juneau, AK 99801-1182

Dear Senator Leman:

RE: Support for SB 345

As you are aware, the Alaska Department of Revenue is poised to implement a new tax regime on foreign air and sea carriers as a result of a recent Alaska Supreme Court decision in the OSG Bulk Ships Inc. case.

The Resource Development Council (RDC) is very concerned about new taxes which could impact current and future decisions to do business in Alaska.

Foreign air and water borne carriers move Alaskan products to international markets. Local businesses and consumers also depend on these same carriers to bring our supplies to Alaska. This new tax regime on transportation could stop some carriers from doing business in Alaska and may discourage others from investing here in the future.

Even if companies currently doing business in Alaska do not leave, the additional costs associated with the tax regime will likely be passed along to Alaska industry and consumers. The net effect being an additional tax on Alaskans, not off-shore companies.

Any way you look at it, the new tax regime has an enormous direct and indirect impact on Alaska businesses, consumers and future economic growth in international markets.

It is our understanding Alaska would be the only state in the Union with such a tax. California, New York and New Jersey have recently withdrawn proposals to tax foreign carriers because of the potential impact on business and their economy.



RDC is very concerned about any new taxes on foreign carriers and we support SB 345 which looks to resolve this issue. Thank you for your initiative in introducing this legislation.

Sincerely,

RESOURCE DEVELOPMENT COUNCIL
for Alaska, Inc.

A handwritten signature in cursive script that reads "Ken Freeman".

Ken Freeman
Executive Director

cc. Senate President Mike Miller
Senate Finance Co-Chair Bert Sharp
Senate Finance Co-Chair Drue Pearce

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

TONY KNOWLES, GOVERNOR

P.O. BOX 110400
JUNEAU, ALASKA 99811-0400
TELEPHONE: (907) 465-2300
FACSIMILE: (907) 465-2389

April 7, 1998

The Honorable Dave Donley
Alaska State Legislature
Capitol, Room 508
Juneau, Alaska 99801

Dear Senator Donley,

You asked this morning about the application of the retroactivity provision of SB 345. Specifically, you asked if we could tell you how much money was at stake in cases where the Section 883 exemption was an issue, and whether, if the legislature enacts the retroactive provision, the Department of Revenue would be required to open closed cases and refund taxes.

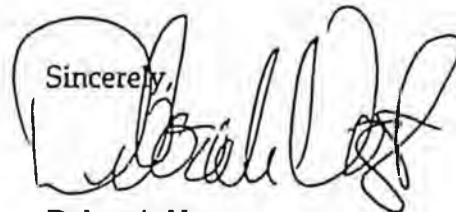
Turning to the second question first, both the Department of Law and this department agree that the retroactive repeal of the tax on foreign carriers would have no effect on closed cases. The cases in which Section 883 taxes have been paid were closed by settlement and closing agreement. They would not be reopened.

One taxpayer, Amerada Hess, has appealed its final Department of Revenue hearing decision to the superior court. The taxpayer has paid the disputed taxes. The taxes it requests refunds on include an assessment of Section 883 taxes of approximately \$1.3 million, exclusive of interest. The tax years at issue in that litigation are 1982 through 1986. The retroactive application of SB 345 will not affect that case because the tax years at issue predate 1993.

As I testified this morning, we cannot calculate the amount of taxes that have been paid on Section 883 income because cases involving collections have always been settled, and settlements necessarily include any number of issues. But, as set out above, these collections would not be disturbed by retroactive application.

I hope this answers your questions.

Sincerely,



Deborah Vogt
Deputy Commissioner

98-022