

SB

83

<TARGET><BILL>SB 83</BILL><SUBJECT>SB
83</SUBJECT><COMM>SFIN28</COMM></TARGET>

SENATE FINANCE COMMITTEE REPORT First Committee of Referral

DATE: 3/20/13

FURTHER:

Date of 5-Day Notice: _____
(in accordance with Uniform Rule 23)

DATE TURNED
IN TO OFFICE: _____

Finance Committee considered SENATE BILL NO. 83

SB 83-INTEREST ON CORPORATION INCOME TAX

"An Act relating to the corporation income tax; and relating to the computation of interest under the look-back method applicable to long-term contracts in the Internal Revenue Code."

and recommends:

- be replaced with CS SB 83 (FIN) [] Same Title New Title
- [] adopt previous CS _____ (_____) [] Same Title [] New Title
- [] attached amendment(s)
- [] adopt _____ Letter of Intent
- [] further referral to _____ Committee

Dept Abbr.	
ADM	LWF
CED	LAW
COR	LEG
CRT	MVA
EED	DNR
DEC	DPS
DFG	REV
GOV	DOT
DHS	UA

NEW FISCAL NOTE(S)				
Dept.	Fiscal	Indet.	Zero	FN #
REV		X		

PREVIOUS FISCAL NOTE(S)				
Dept.	Fiscal	Indet.	Zero	FN #

[] APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	PRINTED LAST NAME	Do PASS	Do NOT PASS	No REC	AMEND
<i>[Signature]</i>	DUALRAY			✓	
<i>[Signature]</i>	BISHOP	✓			
<i>[Signature]</i>	HOFFMAN	✓			
<i>[Signature]</i>	OLSON			✓	
<i>[Signature]</i>	FAIRCLOUGH	✓			
CO-CHAIR: <i>[Signature]</i>	Meyer	✓			
CO-CHAIR:					

Fiscal Note

State of Alaska
2013 Legislative Session

Bill Version: SB 83
Fiscal Note Number: _____
() Publish Date: _____

Identifier: SB083-DOR-TAX-03-21-13
Title: INTEREST ON CORPORATION INCOME TAX
Sponsor: MICCICHE
Requester: (S) FIN

Department: Department of Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2014	Included in	Out-Year Cost Estimates				
	Appropriation Requested	Governor's FY2014 Request	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
OPERATING EXPENDITURES	FY 2014	FY 2014					
Personal Services							
Travel							
Services							
Commodities							
Capital Outlay							
Grants & Benefits							
Miscellaneous							
Total Operating	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Fund Source (Operating Only)

None							
Total	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Positions

Full-time							
Part-time							
Temporary							

Change in Revenues		***	***	***	***	***	***
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Estimated SUPPLEMENTAL (FY2013) cost: 0.0

Estimated CAPITAL (FY2014) cost: 0.0

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? No
If yes, by what date are the regulations to be adopted, amended or repealed?

Why this fiscal note differs from previous version:

Initial version.

Prepared By:	Johanna Bales, Deputy Director	Phone:	(907)269-6628
Division	Tax	Date:	03/25/2013 04:00 PM
Approved By:	Alicia Egan, Legislative Liaison	Date:	03/21/13
	Department of Revenue		

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2013 LEGISLATIVE SESSION

BILL NO. SB 83

Analysis

Bill Language:

This bill would allow Alaska corporations that are required to report income from long-term contracts using the percentage of completion method, to calculate the additional tax due, on this income, using the current federal interest rates, instead of the current Alaska interest rates. Alaska's interest rate is significantly higher than the current federal rate and this bill would result in a tax savings to those companies that have income from long-term contracts. This bill would primarily affect those corporations engaged in the construction business.

Revenues:

There is a provision within the Internal Revenue Code that requires corporations to use the percentage of completion method to report income from long-term contracts. As part of this requirement, corporations must calculate interest on the difference between actual income received and estimated income reported. The interest is then included as an additional tax or a reduction in tax (if the estimated income is higher than actual income) on their corporate tax return. Since Alaska adopts the Internal Revenue Code, this provision is applicable to Alaska corporate income taxpayers as well. However, Alaska law requires that we substitute Alaska's interest rate in place of the federal interest rate. Over the past 22 years, Alaska's interest rate has been significantly higher than the federal interest rate. Currently, Alaska's interest rate is 11% and the federal interest rate under 26 U.S.C. 460 (Internal Revenue Code) is only 2%. This provision proposes to change Alaska's law and allow the use of the lower federal interest rate when calculating this additional tax due.

There are some corporations in Alaska that are subject to this provision. However, since we do not currently have an automated system from which we can pull this specific information, it is difficult for us to determine the full fiscal impact of this provision. However, the division conducted a manual review of tax returns filed by approximately 100 construction companies for calendar years 2010 and 2011. Based on this review, the division discovered that more than 50% of these companies filed S Corporation tax returns and, therefore, were exempt from Alaska corporate income tax. Of the remaining corporations, the division found that only a few had ever reported additional income tax due to the federal provision described above. Of those that had reported additional tax, the division found the difference in the tax due calculated using Alaska's interest rate and calculated using the federal corporate interest rate was less than \$50,000 in the last two calendar years. Although it is possible that there are other corporations subject to this provision that were not identified during the manual review, we believe that the effect of this bill on Alaska's corporate income tax revenues will be minimal.

Expenditures:

The department can implement the provisions of this bill using existing resources.

CS FOR SENATE BILL NO. 83(FIN)

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-EIGHTH LEGISLATURE - FIRST SESSION

BY THE SENATE FINANCE COMMITTEE

Offered:

Referred:

Sponsor(s): SENATOR MICCICHE

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to the corporation income tax; relating to the computation of interest**
2 **under the look-back method applicable to long-term contracts in the Internal Revenue**
3 **Code; and providing for an effective date."**

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 *** Section 1.** AS 43.20.021 is amended by adding a new subsection to read:

6 (j) For purposes of calculating interest under the look-back method in 26
7 U.S.C. 460 (Internal Revenue Code), the rate of interest shall be as provided in that
8 section.

9 *** Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to
10 read:

11 **RETROACTIVITY.** Section 1 of this Act is retroactive to January 1, 2013.

12 *** Sec. 3.** This Act takes effect immediately under AS 01.10.070(c).

Adopted 3/28/13

28-LS0634\U
Bullock
3/27/13

CS FOR SENATE BILL NO. 83()

IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-EIGHTH LEGISLATURE - FIRST SESSION

BY

**Offered:
Referred:**

Sponsor(s): SENATOR MICCICHE

A BILL

FOR AN ACT ENTITLED

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12 *** Sec. 3.** This Act takes effect immediately under AS 01.10.070(c).



ALASKA STATE LEGISLATURE

Senator Peter A. Micciche

State Capitol, Room 125
Juneau, AK 99801-1182
(907) 465-2828 Fax 465-4779

MEMORANDUM

Date: March 20, 2013

To: Senator Kevin Meyer
Senator Pete Kelly
Co-Chairs, Senate Finance Committee

From: Senator Peter Micciche

RE: SB 83 Hearing Request

Please schedule the following resolution for a hearing in the Senate Resources Committee:

SB 83-INTEREST ON CORPORATION INCOME TAX

Attached is the backup information.

SB 83, Version A

Sponsor Statement

Excerpt of Title 26 Internal Revenue Code

"Interest on Underpayments and Overpayments of Federal Taxes"

The Senate Finance Committee is the first committee of referral and therefore the bill does not have a fiscal note yet.

If you have any questions or need additional information, please contact Mindy Rowland in my office at 465-4989.

ALASKA STATE LEGISLATURE

SESSION ADDRESS:
Alaska State Capitol, Rm. 125
Juneau, Alaska 99801-1182
Phone: (907) 465-2828
Fax: (907) 465-4779
Toll Free: (800) 964-5733



INTERIM ADDRESSES:
145 Main St. Loop #226
Kenai, AK 99611
Phone: (907) 283-7996

270 W. Pioneer Ave.
Homer, AK 99603
Phone: (907) 235-0690

SENATOR PETER A. MICCICHE

DISTRICTS

Anchor Point
Clam Gulch
Cohoe
Diamond Ridge
Fox River
Fritz Creek
Funny River
Halibut Cove
Happy Valley
Homer
Kachemak City
Kachemak Selo
Kalifornsky
Kasilof
Kenai
Nikolaevsk
Ninilchik
Razdolna
Ridgeway
Seldovia
Soldotna
Voznesenka

Sponsor Statement

SB 83-INTEREST ON CORPORATION INCOME TAX

Under AS 43.05.225, the State of Alaska is required to charge contractors undertaking long-term projects an interest rate on all delinquent taxes of 5 points above the current annual rate charged by banks for advances or 11%, whichever is greater. Due to low interest rates, the rate in effect has been 11% for a number of years.

The application of this delinquent tax penalty to the construction industry has created a negative impact, due to the way contractors are required to account for long-term contracts by the IRS and Generally Accepted Accounting Principles (GAAP).

Many of our larger construction projects in Alaska are multi-year projects. They are accounted for as long-term contracts and are required to use a percentage of completion reporting method. Specifically, contractors calculate the estimated profit of a project that is completed within a single tax year and pay the tax on the estimated profit. This process is detailed in Title 26, Section 460 of the IRS Code.

Although contractors do their best to estimate project costs and potential profits at the beginning of a project, as the project progresses and the risks are reduced, estimated profits can rise. At the end of a project when the actual profit is known, contractors are required to file look-back taxes and either pay on the increased profit or receive a refund on any overpayment. It is common practice within the construction business is to estimate conservatively and thus have additional taxes to pay when "looking back." These payments under long-term contracts should be considered amended tax returns not delinquent payments subject to such severe penalty.

Under the same IRS code which requires long-term contracts to be based upon a percentage of completion method, interest rates are established for both overpayments and underpayments. Overpayments and underpayments are assessed an interest rate of the Federal short-term rate plus 2 percent if under \$10,000, and plus .5 percent if over \$10,000.

For the purposes of paying state corporate income taxes, this bill applies the interest rates established under 26 U.S.C. 460 on all long-term contracts covered by 26 U.S.C. 460. This is accomplished by adding a new subsection to AS 43.20.021, the Department of Revenue's statutes governing the adoption of IRS code by reference.



First National Bank
A L A S K A

March 26, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau AK, 99801

RE: Senate Bill 83

Dear Senator Micciche,

I work for First National Bank Alaska, a community bank which has served Alaskans for over 90 years with a legacy of helping build strong families, homes and businesses in our great state. As a commercial loan officer, I work with general contractors of all sizes who play major roles in our local construction industry. With respects to Senate Bill 83 regarding the issue of interest charged on look back taxes, I believe conformance to Federal standards would be appropriate.

When we provide financing to contractors, whether it is for working capital or major capital expenditures, we rely on a lot of information to help us make a credit decision. We look at a contractor's performance over time, competency of management, bonding capacity, quality of financial information and financial strength of the business and its owners. A bank line of credit to fund payroll or a term loan to purchase equipment for a project can be an essential part of a contractor's success in completing projects on time and within budget.

With respects to financial information, CPA Prepared financial statements rely on many assumptions and estimates in accordance with Generally Accepted Accounting Principles. In my experience, responsible contractors will be conservative in their estimates of profits on uncompleted jobs. The bank encourages conservative estimates in order to avoid downward swings in profitability from one year to the next because actual financial performance below estimates could have a negative on the bank's willingness to provide future financing. There would be a very high likelihood that it would also negatively impact a contractor's bonding capacity which the bank relies on in many cases when providing financing.

From my perspective, the difference in profitability can be attributed to conservative estimates that are in the best interest of contractors and the current rate of interest charged by the State on look back taxes feels more like a penalty against responsible contractors.

In closing, I would like to thank and applaud you for your support of Senate Bill 83 with respects to the interest rate charged on look back taxes and feel alignment with the Federal rate charged is more appropriate.

Respectfully,

Stacy Tomuro
Vice President

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Interest on Underpayments and Overpayments of Federal Taxes

(Current through March 2013)

Interest on underpayments of federal tax must accrue interest, compounded daily, at rates published quarterly by the Internal Revenue Service in accordance with section 6621 of the Internal Revenue Code. (See Rev. Proc. 95-17, 1995-1 C.B. 556, for rules on how to calculate compounded interest.)

The rates for the most recent twelve calendar quarters are as follows:

Rates for Underpayments and Overpayments of Tax

Calendar Quarter	Underpayments	Noncorporate Overpayments	Corporate Overpayments	Large Corp. Overpayments	Large Corp. Underpayments
Apr-Jun 2010	4%	4%	3%	1.5%	6%
Jul-Sep 2010	4%	4%	3%	1.5%	6%
Oct-Dec 2010	4%	4%	3%	1.5%	6%
Jan-Mar 2011	3%	3%	2%	0.5%	5%
Apr-Jun 2011	4%	4%	3%	1.5%	6%
Jul-Sep 2011	4%	4%	3%	1.5%	6%
Oct-Dec 2011	3%	3%	2%	0.5%	5%
Jan-Mar 2012	3%	3%	2%	0.5%	5%
Apr-Jun 2012	3%	3%	2%	0.5%	5%
Jul-Sep 2012	3%	3%	2%	0.5%	5%
Oct-Dec 2012	3%	3%	2%	0.5%	5%
Jan-Mar 2013	3%	3%	2%	0.5%	5%

As can be seen from the above table, the interest rate that applies to overpayments of tax by individuals (and other noncorporate taxpayers) is the same rate that applies to underpayments of tax.

For corporations, the interest rate on overpayments of \$10,000 or less is 1 point less than the rate for underpayments, and the interest rate on the portion of the overpayment in excess of \$10,000 (i.e., "large" overpayments) is 2.5 points less than the rate on underpayments. Corporations also pay interest that is 2 points higher for "large corporate underpayments" (i.e., underpayments of more than \$100,000).

The underpayment interest rates that have applied since 1987 are shown below.

Rates for Underpayments

Year	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1987	9%	9%	9%	10%
1988	11%	10%	10%	11%
1989	11%	12%	12%	11%
1990	11%	11%	11%	11%
1991	11%	10%	10%	10%
1992	9%	8%	8%	7%
1993	7%	7%	7%	7%
1994	7%	7%	8%	9%
1995	9%	10%	9%	9%
1996	9%	8%	9%	9%
1997	9%	9%	9%	9%
1998	9%	8%	8%	8%
1999	7%	8%	8%	8%
2000	8%	9%	9%	9%
2001	9%	8%	7%	7%
2002	6%	6%	6%	6%
2003	5%	5%	5%	4%
2004	4%	5%	4%	5%
2005	5%	6%	6%	7%
2006	7%	7%	8%	8%
2007	8%	8%	8%	8%
2008	7%	6%	5%	6%
2009	5%	4%	4%	4%
2010	4%	4%	4%	4%
2011	3%	4%	4%	3%
2012	3%	3%	3%	3%
2013	3%			

The Pennsylvania Estate and Trust Cybrary

Daniel B. Evans, Attorney at Law

P.O. Box 27370

Philadelphia, PA 19118

Telephone: (866) 348-4250

Email: dan@evans-legal.com

respect to which the taxpayer has made the election.

(3) Period to which election applies

An election under this section shall be effective for the taxable year for which it is made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election.

(4) Treatment as method of accounting

Except to the extent inconsistent with the provisions of this section, for purposes of this subtitle, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

(d) 5-year spread of transitional adjustments for magazines

In applying section 481(c) with respect to any election under this section which applies to magazines, the period for taking into account any decrease in taxable income resulting from the application of section 481(a)(2) shall be the taxable year for which the election is made and the 4 succeeding taxable years.

(e) Suspense account for paperbacks and records

(1) In general

In the case of any election under this section which applies to paperbacks or records, in lieu of applying section 481, the taxpayer shall establish a suspense account for the trade or business for the taxable year for which the election is made.

(2) Initial opening balance

The opening balance of the account described in paragraph (1) for the first taxable year to which the election applies shall be the largest dollar amount of returned merchandise which would have been taken into account under this section for any of the 3 immediately preceding taxable years if this section had applied to such preceding 3 taxable years. This paragraph and paragraph (3) shall be applied by taking into account only amounts attributable to the trade or business for which such account is established.

(3) Adjustments in suspense account

At the close of each taxable year the suspense account shall be—

(A) reduced the excess (if any) of—

- (i) the opening balance of the suspense account for the taxable year, over
- (ii) the amount excluded from gross income for the taxable year under subsection (a), or

(B) increased (but not in excess of the initial opening balance) by the excess (if any) of—

- (i) the amount excluded from gross income for the taxable year under subsection (a), over
- (ii) the opening balance of the account for the taxable year.

(4) Gross income adjustments

(A) Reductions excluded from gross income

In the case of any reduction under paragraph (3)(A) in the account for the taxable

year, an amount equal to such reduction shall be excluded from gross income for such taxable year.

(B) Increases added to gross income

In the case of any increase under paragraph (3)(B) in the account for the taxable year, an amount equal to such increase shall be included in gross income for such taxable year.

If the initial opening balance exceeds the dollar amount of returned merchandise which would have been taken into account under subsection (a) for the taxable year preceding the first taxable year for which the election is effective if this section had applied to such preceding taxable year, then an amount equal to the amount of such excess shall be included in gross income for such first taxable year.

(5) Subchapter C transactions

The application of this subsection with respect to a taxpayer which is a party to any transaction with respect to which there is nonrecognition of gain or loss to any party to the transaction by reason of subchapter C shall be determined under regulations prescribed by the Secretary.

(Added Pub. L. 95-600, title III, §372(a), Nov. 6, 1978, 92 Stat. 2880.)

EFFECTIVE DATE

Section 372(c) of Pub. L. 95-600 provided that: "The amendments made by this section (enacting this section) shall apply to taxable years beginning after September 30, 1979."

§490. Special rules for long-term contracts

(a) Requirement that percentage of completion method be used

In the case of any long-term contract, the taxable income from such contract shall be determined under the percentage of completion method (as modified by subsection (b)).

(b) Percentage of completion method

(1) Requirements of percentage of completion method

Except as provided in paragraph (3), in the case of any long-term contract with respect to which the percentage of completion method is used—

(A) the percentage of completion shall be determined by comparing costs allocated to the contract under subsection (c) and incurred before the close of the taxable year with the estimated total contract costs, and

(B) upon completion of the contract (or, with respect to any amount properly taken into account after completion of the contract, when such amount is so properly taken into account), the taxpayer shall pay (or shall be entitled to receive) interest computed under the look-back method of paragraph (2).

In the case of any long-term contract with respect to which the percentage of completion method is used, except for purposes of applying the look-back method of paragraph (2), any income under the contract (to the extent

not previously includible in gross income) shall be included in gross income for the taxable year following the taxable year in which the contract was completed. For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under subparagraph (B) shall be treated as an increase in the tax imposed by this chapter for the taxable year in which the contract is completed (or, in the case of interest payable with respect to any amount properly taken into account after completion of the contract, for the taxable year in which the amount is so properly taken into account).

(X) Look-back method

The interest computed under the look-back method of this paragraph shall be determined by—

(A) first¹ allocating income under the contract among taxable years before the year in which the contract is completed on the basis of the actual contract price and costs instead of the estimated contract price and costs,

(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each taxable year referred to in subparagraph (A) which would result solely from the application of subparagraph (A), and

(C) then using the adjusted overpayment rate (as defined in paragraph (7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any amount properly taken into account after completion of the contract shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such amount was properly taken into account) such amount to its value as of the completion of the contract. The taxpayer may elect with respect to any contract to have the preceding sentence not apply to such contract.

(3) Special rules

(A) Simplified method of cost allocation

In the case of any long-term contract, the Secretary may prescribe a simplified procedure for allocation of costs to such contract in lieu of the method of allocation under subsection (c).

(B) Look-back method not to apply to certain contracts

Paragraph (1)(B) shall not apply to any contract—

(i) the gross price of which (as of the completion of the contract) does not exceed the lesser of—

(I) \$1,000,000, or

(II) 1 percent of the average annual gross receipts of the taxpayer for the 3 taxable years preceding the taxable year in which the contract was completed, and

(ii) which is completed within 2 years of the contract commencement date.

For purposes of this subparagraph, rules similar to the rules of subsections (e)(2) and (f)(3) shall apply.

(4) Simplified look-back method for pass-thru entities

(A) In general

In the case of a pass-thru entity—

(i) the look-back method of paragraph (2) shall be applied at the entity level,

(ii) in determining overpayments and underpayments for purposes of applying paragraph (2)(B)—

(I) any increase in the income under the contract for any taxable year by reason of the allocation under paragraph (2)(A) shall be treated as giving rise to an underpayment determined by applying the highest rate for such year to such increase, and

(II) any decrease in such income for any taxable year by reason of such allocation shall be treated as giving rise to an overpayment determined by applying the highest rate for such year to such decrease, and

(iii) any interest required to be paid by the taxpayer under paragraph (2) shall be paid by such entity (and any interest entitled to be received by the taxpayer under paragraph (2) shall be paid to such entity).

(B) Exceptions

(i) Closely held pass-thru entities

This paragraph shall not apply to any closely held pass-thru entity.

(ii) Foreign contracts

This paragraph shall not apply to any contract unless substantially all of the income from such contract is from sources in the United States.

(C) Other definitions

For purposes of this paragraph—

(i) Highest rate

The term "highest rate" means—

(I) the highest rate of tax specified in section 11, or

(II) if at all times during the year involved more than 50 percent of the interests in the entity are held by individuals directly or through 1 or more other pass-thru entities, the highest rate of tax specified in section 1.

(ii) Pass-thru entity

The term "pass-thru entity" means any—

- (I) partnership,
- (II) S corporation, or
- (III) trust.

(iii) Closely held pass-thru entity

The term "closely held pass-thru entity" means any pass-thru entity if, at any time during any taxable year for which there is income under the contract, 50 percent or more (by value) of the beneficial interests

¹ So in original. Probably should be followed by a comma.

in such entity are held (directly or indirectly) by or for 5 or fewer persons. For purposes of the preceding sentence, rules similar to the constructive ownership rules of section 1563(e) shall apply.

(5) Election to use 10-percent method

(A) General rule

In the case of any long-term contract with respect to which an election under this paragraph is in effect, the 10-percent method shall apply in determining the taxable income from such contract.

(B) 10-percent method

For purposes of this paragraph—

(i) In general

The 10-percent method is the percentage of completion method, modified so that any item which would otherwise be taken into account in computing taxable income with respect to a contract for any taxable year before the 10-percent year is taken into account in the 10-percent year.

(ii) 10-percent year

The term "10-percent year" means the 1st taxable year as of the close of which at least 10 percent of the estimated total contract costs have been incurred.

(C) Election

An election under this paragraph shall apply to all long-term contracts of the taxpayer which are entered into during the taxable year in which the election is made or any subsequent taxable year.

(D) Coordination with other provisions

(i) Simplified method of cost allocation

This paragraph shall not apply to any taxpayer which uses a simplified procedure for allocation of costs under paragraph (3)(A).

(ii) Look-back method

The 10-percent method shall be taken into account for purposes of applying the look-back method of paragraph (2) to any taxpayer making an election under this paragraph.

(6) Election to have look-back method not apply in de minimis cases

(A) Amounts taken into account after completion of contract

Paragraph (1)(B) shall not apply with respect to any taxable year (beginning after the taxable year in which the contract is completed) if—

(i) the cumulative taxable income (or loss) under the contract as of the close of such taxable year, is within

(ii) 10 percent of the cumulative look-back taxable income (or loss) under the contract as of the close of the most recent taxable year to which paragraph (1)(B) applied (or would have applied but for subparagraph (B)).

(B) De minimis discrepancies

Paragraph (1)(B) shall not apply in any case to which it would otherwise apply if—

(i) the cumulative taxable income (or loss) under the contract as of the close of each prior contract year, is within

(ii) 10 percent of the cumulative look-back income (or loss) under the contract as of the close of such prior contract year.

(C) Definitions

For purposes of this paragraph—

(i) Contract year

The term "contract year" means any taxable year for which income is taken into account under the contract.

(ii) Look-back income or loss

The look-back income (or loss) is the amount which would be the taxable income (or loss) under the contract if the allocation method set forth in paragraph (2)(A) were used in determining taxable income.

(iii) Discounting not applicable

The amounts taken into account after the completion of the contract shall be determined without regard to any discounting under the 2nd sentence of paragraph (2).

(D) Contracts to which paragraph applies

This paragraph shall only apply if the taxpayer makes an election under this subparagraph. Unless revoked with the consent of the Secretary, such an election shall apply to all long-term contracts completed during the taxable year for which election is made or during any subsequent taxable year.

(7) Adjusted overpayment rate

(A) In general

The adjusted overpayment rate for any interest accrual period is the overpayment rate in effect under section 6621 for the calendar quarter in which such interest accrual period begins.

(B) Interest accrual period

For purposes of subparagraph (A), the term "interest accrual period" means the period—

(i) beginning on the day after the return due date for any taxable year of the taxpayer, and

(ii) ending on the return due date for the following taxable year.

For purposes of the preceding sentence, the term "return due date" means the date prescribed for filing the return of the tax imposed by this chapter (determined without regard to extensions).

(e) Allocation of costs to contract

(1) Direct and certain indirect costs

In the case of a long-term contract, all costs (including research and experimental costs) which directly benefit, or are incurred by reason of, the long-term contract activities of the taxpayer shall be allocated to such contract in the same manner as costs are allocated to extended period long-term contracts under section 451 and the regulations thereunder.

(2) Costs identified under cost-plus and certain Federal contracts

In the case of a cost-plus long-term contract or a Federal long-term contract, any cost not

68A Stat. 454, as amended, which is classified generally to chapter 23 (§ 3301 et seq.) of this title. For complete classification of this Act to the Code, see section 3311 of this title and Tables.

AMENDMENTS

2001—Subsec. (c), Pub. L. 107-18, §§ 532(c)(12), 901, temporarily struck out "section 2011(c) (relating to refunds due to credit for State taxes)," after "see". See Effective and Termination Dates of 2001 Amendment note below.

1956—Subsec. (c), Act June 29, 1956, inserted reference to section 6421 of this title.

Act Apr. 2, 1956, inserted reference to section 6420 of this title.

EFFECTIVE AND TERMINATION DATES OF 2001 AMENDMENT

Amendment by Pub. L. 107-18 applicable to estates of decedents dying, and generation-skipping transfers, after Dec. 31, 2004, see section 532(d) of Pub. L. 107-18, set out as a note under section 2011 of this title.

Amendment by Pub. L. 107-18 inapplicable to estates of decedents dying, gifts made, or generation skipping transfers, after Dec. 31, 2012, and the Internal Revenue Code of 1996 to be applied and administered to such estates, gifts, and transfers as if such amendment had never been enacted, see section 901 of Pub. L. 107-18, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1956 AMENDMENT

Amendment by act June 29, 1956, effective June 29, 1956, see section 211 of act June 29, 1956, set out as an Effective Date note under section 4041 of this title.

Subchapter C—Determination of Interest Rate; Compounding of Interest

Sec.	
6621.	Determination of rate of interest.
6622.	Interest compounded daily.

AMENDMENTS

1982—Pub. L. 97-248, title III, § 344(b)(3)(A), Sept. 3, 1982, 96 Stat. 638, inserted "; Compounding of Interest" after "Rate" in heading for subchapter C.

Pub. L. 97-248, title III, § 344(b)(2), Sept. 3, 1982, 96 Stat. 638, added item 6622.

§ 6631. Determination of rate of interest

(a) General rule

(1) Overpayment rate

The overpayment rate established under this section shall be the sum of—

- (A) the Federal short-term rate determined under subsection (b), plus
- (B) 3 percentage points (3 percentage points in the case of a corporation).

To the extent that an overpayment of tax by a corporation for any taxable period (as defined in subsection (c)(3), applied by substituting "overpayment" for "underpayment") exceeds \$10,000, subparagraph (B) shall be applied by substituting "0.5 percentage point" for "2 percentage points".

(2) Underpayment rate

The underpayment rate established under this section shall be the sum of—

- (A) the Federal short-term rate determined under subsection (b), plus
- (B) 3 percentage points.

(b) Federal short-term rate

For purposes of this section—

(1) General rule

The Secretary shall determine the Federal short-term rate for the first month in each calendar quarter.

(2) Period during which rate applies

(A) In general

Except as provided in subparagraph (B), the Federal short-term rate determined under paragraph (1) for any month shall apply during the first calendar quarter beginning after such month.

(B) Special rule for individual estimated tax

In determining the addition to tax under section 6654 for failure to pay estimated tax for any taxable year, the Federal short-term rate which applies during the 3rd month following such taxable year shall also apply during the first 15 days of the 4th month following such taxable year.

(3) Federal short-term rate

The Federal short-term rate for any month shall be the Federal short-term rate determined during such month by the Secretary in accordance with section 1274(d). Any such rate shall be rounded to the nearest full percent (or, if a multiple of $\frac{1}{4}$ of 1 percent, such rate shall be increased to the next highest full percent).

(c) Increase in underpayment rate for large corporate underpayments

(1) In general

For purposes of determining the amount of interest payable under section 6601 on any large corporate underpayment for periods after the applicable date, paragraph (2) of subsection (a) shall be applied by substituting "5 percentage points" for "3 percentage points".

(2) Applicable date

For purposes of this subsection—

(A) In general

The applicable date is the 30th day after the earlier of—

- (i) the date on which the 1st letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals is sent, or
- (ii) the date on which the deficiency notice under section 6212 is sent.

The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary.

(B) Special rules

(i) Nondeficiency procedures

In the case of any underpayment of any tax imposed by this title to which the deficiency procedures do not apply, subparagraph (A) shall be applied by taking into account any letter or notice provided by the Secretary which notifies the taxpayer of the assessment or proposed assessment of the tax.

(ii) Exception where amounts paid in full

For purposes of subparagraph (A), a letter or notice shall be disregarded if, during

SENATE BILL NO. 83

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-EIGHTH LEGISLATURE - FIRST SESSION

BY SENATOR MICCICHE

Introduced: 3/20/13

Referred: Finance

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the corporation income tax; and relating to the computation of
2 interest under the look-back method applicable to long-term contracts in the Internal
3 Revenue Code."

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 * **Section 1.** AS 43.20.021 is amended by adding a new subsection to read:

6 (j) For purposes of calculating interest under the look-back method in 26
7 U.S.C. 460 (Internal Revenue Code), the rate of interest shall be as provided in that
8 section.

9 * **Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to
10 read:

11 **APPLICABILITY.** The rate of interest provided for in AS 43.20.021(j), enacted by
12 sec. 1 of this Act, applies on and after the effective date of this Act.



UDELHOVEN

Oilfield System Services, Incorporated

184 East 53rd Ave.
Anchorage, Alaska 99518-1222
Fax (907) 522-2541
Phone (907) 344-1577

March 27, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau, Alaska 99501

Dear Senator Micciche

I am writing to you with deep concern in general with our legislators in Juneau. It concerns me to see so many laws, rules and statutes on the books that are simply put not good for the State and not business friendly. Thank you for sponsoring Senate Bill 83 and attempting to rectify one of the problem areas.

Alaska statute sets the rate for look-back interest at the same rate as if the taxes were delinquent. This look-back rate charged to us by the State of Alaska is far in excess of the federal rate. The rate imposed by the State of Alaska on look-back taxes is usurious at 11 percent, when even unsecured bank loans are available for much less. I ask you: Is that our goal to collect more interest from good contractors trying to do the right thing than the federal government does?

We as "C" Corps follow GAAP and are required to report income on a percentage of completion method. Often, projects will continue for extended periods of time. Generally we would report conservatively and correctly. At times, if we are lucky, we do a little better than originally planned. Many times we do not do as well.

There is no way we are able to know the actual outcome of a project that would extend over the end of the year with 100% accuracy. The only way to avoid the penalty imposed by the State's look-back interest rate would be to overestimate profits and give the State tax dollars that may or may not be due far in advance. Although the state would owe us interest at the same 11 percent, this practice would take funds away from the company for extended periods of time that could be used to start new projects, create jobs, and make purchases, etc which is what the State really needs. Also, our bonding companies and bankers would not be happy to see such poor performance as our estimated profits faded away at the end of the job.

We adamantly support Senate Bill 83 which will bring the rates down to match the federal rates and thank you for your efforts in bringing this bill forward.

Sincerely

Cathy Duxbury
Controller

An Alaskan Corporation
Established 1970

North District
P.O. Box 340103
Prudhoe Bay, AK 99734
(907) 659-8093

South District
P.O. Box 8349
Nikiski, AK 99635
(907) 776-5185

F.M. STRAND & ASSOCIATES

A PROFESSIONAL CORPORATION

3201 C Street, Suite 601
Anchorage, AK 99503
Tel: (907) 563-4425
Fax: (907) 561-0563
www.fmstrandcpas.com

Certified Public Accountants

Serving clients throughout
Alaska since 1973.

March 27, 2013

Senator Peter Micciche
State Capitol, Room 125
Juneau, Alaska 99801

Re: Senate Bill No. 83 House Bill No. 185

Dear Senator Micciche:

F. M. Strand & Associates, P.C. is an Anchorage-based CPA firm serving many Alaskan general contractors. We request your support for Senate Bill No. 83, which would bring the Alaska interest rate used for the computation of interest under the look-back method applicable to long-term contracts in line with the federal interest rate used in that calculation.

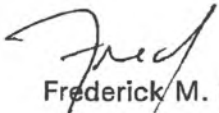
Look-back interest is not income tax. It is the interest on a hypothetical under or over payment of income tax using actual cost rather than estimates for recognition of income from long-term contracts reported with the percentage of completion method. It can be owed to the State or be due from the State, depending on the accuracy of the estimates the contractor used.

Currently, the Alaska interest rate is 11 percent. Federal law sets interest rates for look-back purposes based on the Federal short-term rate. The Federal rate reflects current economic conditions more accurately and is updated quarterly.

Thus, we believe the interest rate used by the State of Alaska for the look-back interest computations should be lowered to match the Federal rates. Please support Senate Bill No. 83.

Very truly yours,

F. M. STRAND & ASSOCIATES, P.C.



Frederick M. Strand

FMS:cb

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**davis
constructors
& engineers inc.**

740 Bonanza Avenue • Anchorage, Alaska 99518
Phone (907) 562-2336 Fax (907) 561-3620
www.davisconstructors.com

March 27, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau, Alaska 99801

Dear Senator Micciche

Davis Constructors & Engineers, Inc. is strongly in support of Senate Bill 83 and appreciates your efforts to address the issue of look-back interest rates charged by the State of Alaska. We employ hundreds of Alaskans, construct government and private buildings in this great state and are proud to direct a portion of our profits to charitable causes that assist members of the communities we work in.

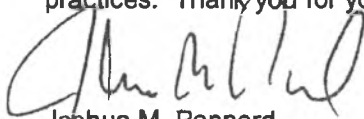
The State of Alaska assesses interest on look-back taxes due from construction contractors on long-term contracts at the delinquent tax rate, set by statute with a floor of 11 percent. The problem is that these taxes due are not "delinquent", but are the result of a successful contractor performing well on a project that bridges multiple years.

Large contractors are required to use the percentage of completion method to account for taxable contract income. Taxes are paid based on income calculated using estimated gross profits until the project is complete. If the estimated gross profit increases over the life of the job, the taxes due for prior periods are recalculated and paid with interest.

Good business practices dictate that contractors are conservative in their initial estimates of long-term projects. As you might imagine, there are many uncertainties in the beginning stages of a project and good contractors will include contingencies for the unexpected. As the project progresses and risks are managed, the gross profit often goes up and that is something that shareholders, banks and bonding companies like to see.

The federal government charges a look-back tax interest rate that fluctuates with the current state of the economy and is subject to change each quarter. The current federal interest rate assessed on look-back taxes is substantially lower than the state's 11 percent and reflects the fact that contractors pay taxes based on estimates. When actual amounts are known and paid, a reasonable interest rate is paid to the federal government to account for the fact that they're paid in later years.

Senate Bill 83 will tie Alaska look-back tax interest rates to the federal rates and help to level the playing field for C Corporation construction contractors in Alaska. We choose to pay state income tax and should not be penalized for having sound business practices. Thank you for your support of Senate Bill 83.


Joshua M. Pepper
President


Idonna Pieper Nelson
CFO

General • Commercial • Design Build • Construction Management



2964 Commercial Drive
Anchorage, AK 99501

(907) 258-2425 Fax: (907) 278-8018

March 26, 2013


**Alaska State Legislature
State Capitol
Juneau, Alaska 99801**

Dear Legislator:

K-C Corporation is an Alaskan contractor who has been active in the construction field for the past 27 years. We are what is known as a C type corporation and as such account for our long term contracts under the percentage of completion method of accounting as required by the IRS. We estimate our profits at the beginning of each contract and on completion of the first year of work we project what we will earn for that period and pay taxes based on these figures. Upon completion of the contract we frequently find our profits are greater than expected and end up paying additional taxes on the earnings plus what is known as "look back interest" on these earnings. We have no problem with this.

Our problem comes when we see the great variance in the rate or means used by the Internal Revenue Service to determine "look back Interest" charges versus the fixed rate of (11%) charged by the State of Alaska. We would like to see this changed in the state statute to reflect what the IRS has established as a basis for calculating their rates. This is the purpose of Senate Bill 83 which we feel reflects a much fairer basis for establishing the rate. Please support Senate Bill 83.

Sincerely
K-C CORPORATION


Byron D. Kohfield
President



ASSOCIATED GENERAL CONTRACTORS of ALASKA

8005 Schoon Street • Anchorage, Alaska 99518
Telephone (907) 561-5354 • Fax (907) 562-6118

3750 Bonita Street • Fairbanks, Alaska 99706
Telephone (907) 452-1809 • Fax (907) 456-8599

Senator Peter Micciche
State Capitol Building, Room 125
Juneau, AK 99801

March 27, 2013

RE: SB 83

Dear Senator Micciche *Peter*

On behalf of the Associated General Contractors of Alaska, a construction industry trade association of 660 construction industry business members, we heartily support SB 83.

As an advocate for our members and the Alaska construction industry, we look for ways to help contractors and other construction related businesses stay competitive and to stay in business. Helping to improve laws on the books is just one of the ways we do that. SB 83 is an excellent example of such an improvement.

Without getting into the complexities of look-back taxes, changing the interest charged on taxes due is a benefit to those contractors who choose to be C-corporations and pay state corporate income tax. While 11% interest rate set in statute may have been a reasonable rate over thirty years ago when it was put in statute, that rate today is considered usurious. Making it consistent with the IRS rate and standards is fair.

I wish this legislation was a benefit to a large number of contractors, but the truth is, it probably benefits less than two dozen. The benefit may be to relatively few, but the benefit to them is big. It helps even the playing field between them and their competitors who are not C-corps and do not pay state corporate income taxes.

This is good legislation and needs to move forward. Thank you for sponsoring SB 83.

Sincerely,

John MacKinnon
Executive Director
Associated General Contractors of Alaska



CONSOLIDATED ENTERPRISES, INC.

633 E. 81ST AVENUE • ANCHORAGE, ALASKA 99518-3145
TELEPHONE (907) 344-4567 • FAX (907) 349-6390

March 27, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau, Alaska 99801

Re: Senate Bill No. 83

Dear Senator Micciche:

Consolidated Enterprises was incorporated as a general contractor in the State of Alaska in 1974. Since that time we have employed many great people and pride ourselves on the successful completion of thousands of projects throughout our great State.

We believe that one of the many reasons we have maintained a strong, successful Company is that our approach has always been a conservative one. As a contractor we account for our long term projects under the percentage of completion method. This approach is extremely appealing to both our bonding company and our bank. Being conservative on our gross profits in one fiscal year, carries forward into the new fiscal year with gross profit gains that the readers of our financial statements desire.

As you are aware, the State of Alaska is currently charging 11% look back interest for taxes due on gross profit gains! The federal government is currently charging 2% interest for increases or decreases in tax of \$10,000 or less and are charging .5% interest if the increase or decrease in tax exceeds \$10,000. Additionally, the State does not currently make a distinction between the IRS required process of estimating taxes based upon the contractor's best knowledge and a tax payer who does not make a timely filing.

In our current economic climate, The State of Alaska's level of interest is extremely high. It has significant financial impact on our Company and most importantly negatively affects the conservative guideline that makes for a successful, profitable Company.


Therefore, our company respectfully requests that you pass Senate Bill No. 83. We believe this bill is fair, promotes conservative estimates and does not penalize corporations that are complying with all tax requirements.

Thank you for your time in this matter and if you should require any additional information, please do not hesitate to contact us.

Sincerely,
CONSOLIDATED ENTERPRISES, INC.


Chris Layson
President

Sincerely,
CONSOLIDATED ENTERPRISES, INC.


Destry Lind
Vice-President



PARKER | SMITH | FEEK

celebrating 75 years

March 26, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau AK, 99801

RE: SB 83

Dear Senator Micciche,

As a surety bond broker who works with many of the largest and most active general contractors in Alaska, and who represents all of the major sureties actively writing bonds in Alaska, I deal with the issue embodied in SB 83 on a regular basis. The issue of interest on look back taxes deals with one of the core elements of the surety underwriting process - reliable, consistent and conservative accounting.

Privately held contractors who are required to post bonds on projects rely on CPA-prepared financial statements to provide a credible third party confirmation of a contractor's financial performance. A contractor's performance is assessed over time, and due to the uncertainties inherent in contracting, namely the constant re-pricing from project to project due to bidding and the inability to fix costs due to differences in suppliers, subcontractors, project locations and other general conditions, determination of profitability on any one project before completion is by definition an estimate.

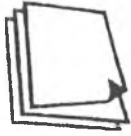
Every responsible contractor will be conservative in these estimates, and their surety demands it, since the contractor who underperforms expectations is a contractor who will not get the full support of their surety. Bonding is the lifeblood of many contractors, and the penalty of underperformance, that is not getting all the bonding that is needed, is simply too great.

Since the difference in profitability is generally due to legitimately conservative estimating, the interest on look back taxes should be considered as a tool to true up, not penalize. The State of Alaska would do well to conform to the Federal Government on this issue.

Respectfully,

Parker Smith & Feek, Inc.

Scott Fisher
Principal, Construction Practice Group Leader



THOMAS, HEAD & GREISEN, PC
CERTIFIED PUBLIC ACCOUNTANTS

Kevin E. Branson, CPA
John A. Letourneau, CPA
Debra K. Mason, CPA/CFF, CFE
Erich R. Lamirand, CPA
Cindy L. Hulquist, CPA
Ronald E. Greisen, CPA/ABV/CFF

March 27, 2013

Senator Peter Micciche
State Capitol Room 125
Juneau, AK 99801

RE: HB 83

Dear Senator Micciche:

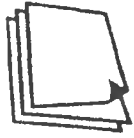
I am writing to you today to encourage you to support Senate Bill 83. Contractors that have elected to be C Corporations pay state corporate taxes. The IRS code has a provision to determine "look back" interest charges, but the Alaska state law of a fixed rate of 11% supersedes the IRS code. This 11% rate penalizes C Corporations as the current rates are far below 11%. We would like Alaska to adopt the IRS rate under 26 U.S.C. 460 for "look back" interest charges. The federal rate is variable as it fluctuates with the current state of the economy.

Senate Bill 83 promotes conservative estimates and would not penalize C Corporations in the State of Alaska that are complying with all tax requirements governing long-term contracts.

Please support HB 83.

Very Truly Yours,

Kevin E. Branson, CPA



THOMAS, HEAD & GREISEN, PC
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Debra K. Mason, CPA/CFF, CFE