

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILES 8672

3002 SCOMM 134: HOUSE SPECIAL COMMITTEE ON WAYS & MEANS 2003-04

General Revenue System

- Broad Based Taxes -

- **Income**

- **Consumption**

Economic Growth

- Real Economic Growth -

- Hydrocarbon
- Technology
- Fish
- Finance
- Manufacturing
- Transportation
- Construction
- Executive Services
- Tourism
- ANCSA Corporations
- Mining and Minerals
- Roads

Balanced Budget Mechanism

- **Maintain Cash Reserve**
- **Revolving “Credit Line” Concept**
- **Mitigate Oil Price Volatility**
- **Reduce Broad Based Taxes when Reserves are Adequate**

ALASKA'S FISCAL CROSSROADS

A DISCUSSION

For years Alaskans have heard about the state's "fiscal gap," which is the result of recurring expenses exceeding recurring revenues (if you were a family, you would describe it as "living beyond your means.") The state has been "living beyond its means" in ten of the last 12 years.

This gap has been filled by spending from the Constitutional Budget Reserve (CBR), a savings account created by voters in 1990 that consists of one-time settlements from disputed oil and gas royalties and taxes. Over the years, \$7.9 billion has gone into the fund; today only \$1.9 billion remains. In spite of high oil prices in this current fiscal year that ends June 30, 2003, nearly \$500 million still will be needed to prop up spending.

In developing the FY 04 budget, the challenge was to begin the process by which the state starts to "live within its means" (budget cuts) or gets another job to bring in more income (new revenues). For the long term, the Administration is committed to growing recurring revenues by developing Alaska's resources to pay for appropriate state responsibilities, such as public safety, transportation, and education.

But for the short-term, it is necessary to make different spending decisions. To get that process underway, Administrative Order 202, issued on the Governor's first day in office, outlined a process by which every department evaluated what it does, how it does it, and what results it is getting for the public dollars invested in those services—a "bottom line" for state government. The results from this evaluation formed the basis for many of the budget recommendations reflected in the proposed budget.

Throughout this process the Administration also was very focused on the bigger picture of the need to minimize the draw that will be required from the CBR to help pay for next year's spending. Again, there were two ways to do this—new revenues and budget cuts. The proposed FY 04 budget accomplishes both:

- \$235 in additional revenues, of which \$114 million is primarily user-related fees, and \$121 million is the deposit of one-time monies in the General Fund;

- \$55 million in operating budget cuts. This number understates the level of reductions; nearly \$190 million in cuts were made but were offset by formula-driven increases and debt payment obligations.

Overall, comparing FY 2004 to FY 2003 General Fund spending:

Revenues:	\$82 million higher
Operating Budget:	\$55 million lower
Capital Budget:	\$25 million higher
Debt, Other Appropriations:	\$11 million higher
<u>Total Spending:</u>	<u>\$20 million lower</u>

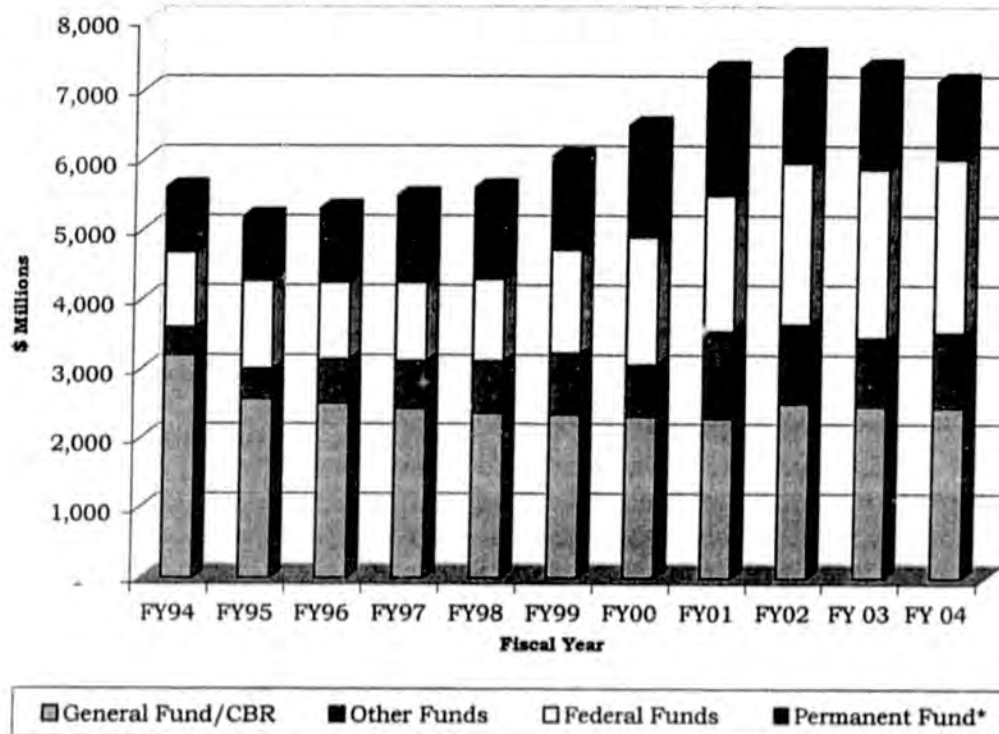
The following information provides background about state spending, revenues, and the context for developing the Fiscal Year 2004 budget.

FISCAL ISSUES

Historical Background

Chart 1 below shows appropriations by fund source for the Governor's FY 04 proposed budget compared to annual budgets in the past decade. What it demonstrates is that the main areas of growth by far in the total state budget have been federal funds and Permanent Fund payments for dividends and inflation proofing.

Chart 1
Appropriations by Revenue Source
Operating and Capital Budgets
FY 1994 - FY 2004 Proposed



Source: Legislative Finance Budget History File

*Permanent Fund includes appropriations for dividends and inflation proofing.

Federal funds have restrictions on how they may be spent and are largely devoted to transportation and health and social service programs. For the most part, the Legislature and Governor do not exercise much control over federal spending. Federal programs also often require a state general fund match (\$356 million in the Governor's proposed FY 04 operating and capital

budgets) or have maintenance of effort requirements. For the past several years, federal match requirements have made up about half of the general fund portion of the state capital budget (\$139 million in fiscal year 2003).

Chart 2 focuses on state-controlled funding sources (excluding Permanent Fund earnings which are discussed in detail in a later section) and shows the relationship between general fund revenue, draws from the constitutional budget reserve (CBR) and other funds during the past decade.

The category of "other funds" in the budget includes such sources as university tuition and Alaska Housing Finance Corporation (AHFC) receipts and has grown as well, mainly to supplement and supplant declining general fund revenue. Beginning in 1992, there has been a concerted effort to separate out services that are fee supported from those that compete for general fund revenues. "Other funds" do not affect the fiscal gap or increase the draw on the CBR. Many fee-supported and self-funding programs have been reclassified from general fund to other state funds, which accounts for some of the growth in the other funds portion of the budget. The other funds portion of the Governor's FY 2004 budget proposal is \$91 million higher than the FY 2003 authorized budget.

General Fund Revenues

The "fiscal gap" between revenues and expenditures is defined solely in terms of state general funds and is the focal point of the Governor's FY 04 budget proposal because reductions in general fund spending help close the gap. The general fund portion of the FY 2004 Governor's proposed budget is \$20 million less than the FY 2003 authorized budget. However what isn't shown in the graph is that nearly \$190 million in built-in general fund cost increases, mostly in formula programs and debt service, had to be cut out of the budget or otherwise accommodated to achieve a \$20 million overall general fund savings.

The state currently produces about half of the 2 million barrels per day of oil that it did at its peak in 1988. The long term decline in production is exacerbated by the fact that new production from smaller fields is taxed at a much lower rate than the declining super-giant Prudhoe Bay and Kuparuk fields. Petroleum royalties and taxes comprise about 84% of general fund revenues. Chart 3 shows historical and projected general fund revenue and demonstrates how the long-term underlying decline in petroleum revenue is affected by periodic spikes and troughs caused by oil price volatility.

Chart 2
State Funding Sources and CBR Draw
Operating and Capital Budgets
FY 1994 - FY 2004 Proposed

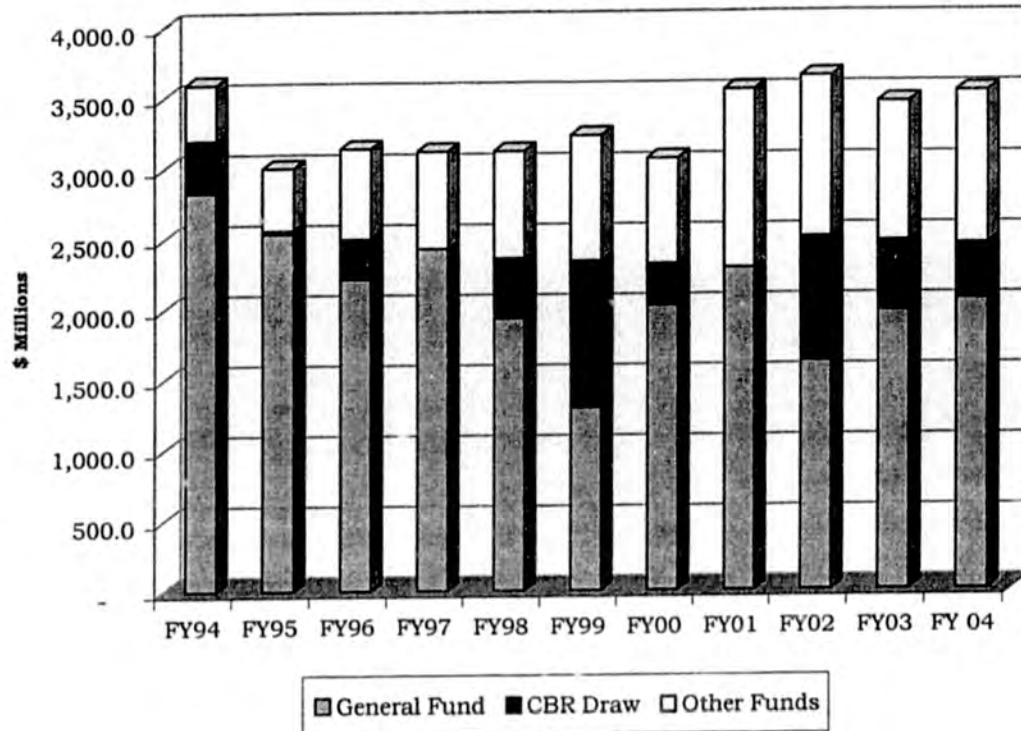
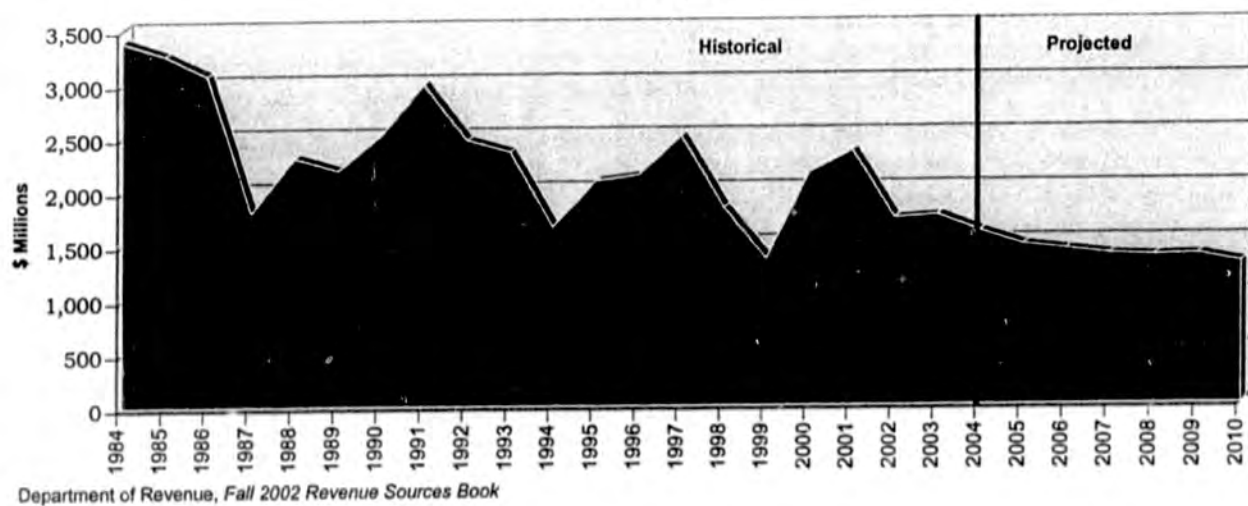


Chart 3
Historical and Projected General Fund Revenue
Status Quo



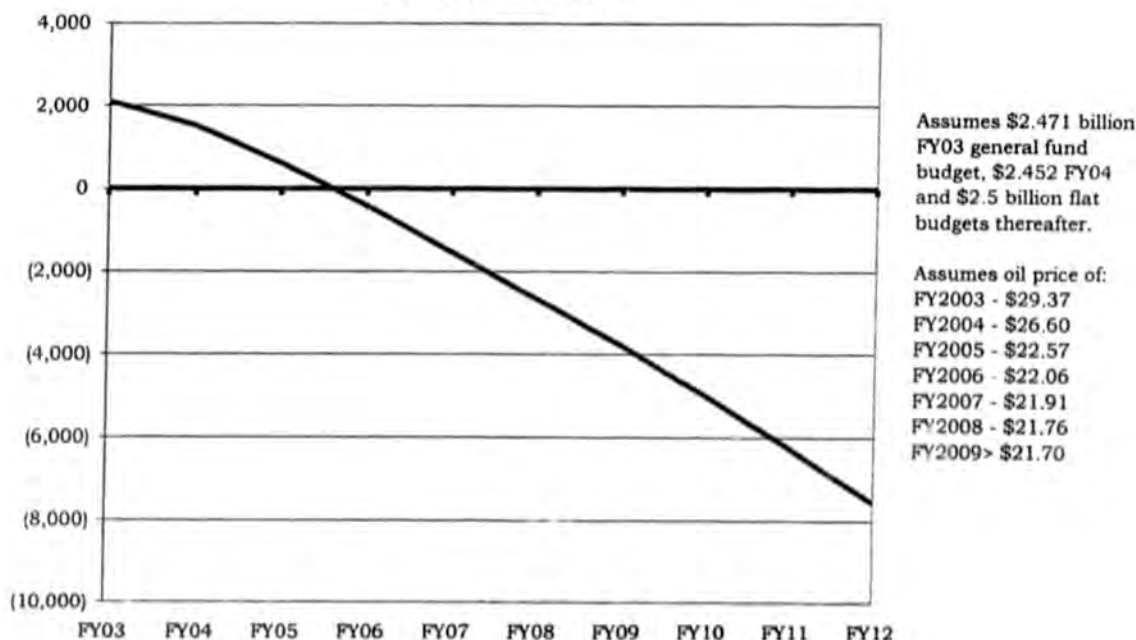
Department of Revenue, Fall 2002 Revenue Sources Book

New oil developments in NPRA and elsewhere on the North Slope will undoubtedly improve the long-term revenue picture but are at least a few years off. (For an excellent discussion of potential oil and gas production opportunities, link to the Department of Revenue *Fall 2002 Revenue Sources Book* at www.tax.state.ak.us.) Likewise the Governor's proposals for industrial roads to mining and other natural resource development prospects will take some time to bring revenue returns to the state treasury. For this reason it is important in the meantime to preserve the balance in the CBR so that it can help bridge until revenues from new development are available.

General Fund Revenues and the CBR Draw

The CBR was established by a constitutional amendment authorized in a statewide vote in the 1990 general election. It was capitalized by oil and gas royalty and tax settlements with petroleum companies and was designed as a buffer to insulate the state general fund from oil price swings that devastated the state economy in the mid '80s. At current production level, every \$1 change in the average price of oil over the fiscal year results in a \$65 million change in revenues. (In the mid-'80s every \$1 change in the price of oil generated \$150 million due to high production in high tax fields.)

Chart 4
CBR Balance
FY 2003 - FY 2012



Virtually all of the large tax and royalty cases have been settled, which means there are no more big deposits to replenish the CBR. During the past decade the CBR has served as a buffer to oil price volatility and it has been used to address the state's structural deficit.

For 10 of the past 12 fiscal years, the state has balanced its budget by drawing money from the CBR – a little over \$5 billion so far of the \$7 billion in total deposits. The FY 03 CBR draw is projected to be \$494 million and the Governor's proposed FY 04 budget projects a \$393 million draw. Even assuming flat general fund budgets and extraordinarily high oil prices, absent any new revenues, the CBR will be depleted in February 2006. If the Legislature approves the Governor's proposed one-time deposits to the general fund (\$121 million) and revenue increases (\$113 million), the date when the CBR is depleted will be delayed by about another 6 months. Chart 4 is a graphical depiction of the Department of Revenue projection of the Governor's FY 04 budget proposal.

The immediate goal expressed in the budget proposal is to slow the rate of CBR decline with a combination of budget cuts, one time fund transfers to the general fund, and new revenue sources so it can continue to function as an oil price buffer. Longer-term, the goal is to close the fiscal gap by balancing expenditures with recurring revenues.

The fiscal summary (*Table 1*) provides a broad outline of the Governor's FY 2004 proposed budget compared to the current year. Individual departmental budget detail is available by following the link:
http://www.gov.state.ak.us/omb/04_OMB/budget/budgethome.htm

Table 1

Fiscal Summary
FY 2003 Authorized Compared to FY 2004 Governor Proposed
(dollars shown in millions)

	General Fund	FY2003 Authorized Federal Funds	Other Funds	Total Funds	General Fund	FY2004 Governor Federal Funds	Other Funds	Total Funds	Difference General Fund	Total
1 Revenues										
2 Unrestricted General Fund Revenues (A)	1,977.0			1,977.0	1,824.0			1,824.0	(153.0)	(153.0)
3 Proposed New Revenues				0.0	113.6			113.6	113.6	113.6
4 One-Time Deposits to the General Fund				0.0	121.2			121.2	121.2	121.2
5 Corporate Dividends (B)			77.4	77.4			52.0	52.0		(25.4)
6 Federal and Other Funds		2,429.9	906.1	3,336.0		2,497.3	1,022.8	3,520.2		184.2
7 Total Revenues	1,977.0	2,429.9	983.5	5,390.4	2,058.8	2,497.3	1,074.8	5,630.9	81.8	240.6
8 Authorization to Spend										
9 Operating	2,222.3	1,416.4	773.2	4,411.9	2,167.3	1,458.9	792.2	4,418.4	(55.0)	6.5
10 Agency Operations (non-formula)	1,116.0	738.1	1,220.1	3,074.1	1,089.0	721.5	1,245.7	3,056.1		
11 Formula Programs	1,106.4	678.3	117.1	1,901.7	1,078.3	737.3	141.0	1,956.6		
12 Duplicated Authorizations (C)			(564.0)	(564.0)			(594.4)	(594.4)		
13 Capital	109.8	947.7	124.5	1,182.0	134.4	1,003.9	209.5	1,347.8	24.6	165.9
14 Project Appropriations & Revised Programs	109.8	947.7	227.5	1,285.0	134.4	1,003.9	268.1	1,406.4		
15 General Obligation Bonds (D)			463.5	463.5				0.0		
16 Duplicated Authorizations (C)			(566.5)	(566.5)			(58.6)	(58.6)		
17 Debt and Other Statewide	139.1	65.9	115.8	290.8	150.1	34.6	73.1	257.7	10.9	(33.1)
18 Debt Service (E)	11.5	0.0	110.5	122.1	48.0	1.7	122.3	172.1	36.5	50.0
19 Loan and non-Debt Fund Capitalization	57.7	25.2	33.4	116.2	67.5	32.9	11.0	111.3	9.7	(5.0)
20 Supplemental Appropriations	69.9	40.7	(8.2)	102.4	33.0			33.0	(36.9)	(69.4)
21 New Legislation				0.0	1.6		0.7	2.3	1.6	2.3
22 Duplicated Authorizations (C)			(50.0)	(50.0)			(60.9)	(60.9)		
23 Total Authorization to Spend (unduplicated)	2,471.2	2,429.9	983.5	5,884.6	2,451.8	2,497.3	1,074.8	6,023.9	(19.5)	139.3
24										
24 AK Permanent Fund Dividends (and PFD division operations)			682.0	802.0			507.0	509.0		(293.0)
25 AK Permanent Fund Inflation Proofing and Other Transfers			205.0	642.0			590.0	594.0		(48.0)
26 Total AK Permanent Fund			887.0	1,444.0			1,097.0	1,103.0		(341.0)
27 Totals with Permanent Fund	2,471.2	2,429.9	1,870.5	7,328.6	2,451.8	2,497.3	2,171.8	7,126.9	(19.5)	(201.7)
28 Draw from Constitutional Budget Reserve	494.2				393.0				(101.3)	

Notes

A FY2003 Unrestricted Revenues are based on an oil price of \$29.37 per barrel and estimated production of 0.994 million barrels per day. FY2004: \$26.60 and 0.997 mbd

B Corporate Dividends include funds made available to the State by the boards of the Alaska Industrial Development and Export Authority (AIDEA), the Alaska Housing Finance Corporation (AHFC), and the Alaska Student Loan Corporation (ASLC). The AIDEA dividend for FY2003 is \$20.1 million. Under current statutes, there will not be an FY2004 AIDEA dividend. The total AHFC transfer for dividend capital projects, loan programs and debt service is \$103 million for FY2003, and \$103 million for FY2004. Since AHFC's debt payments for general government purpose bonds do not require appropriation, the net transfers appropriated here are \$52 million for FY2003 and \$47 million for FY2004. The ASLC Dividend is \$5.25 million in FY2003 and \$5 million for FY2004.

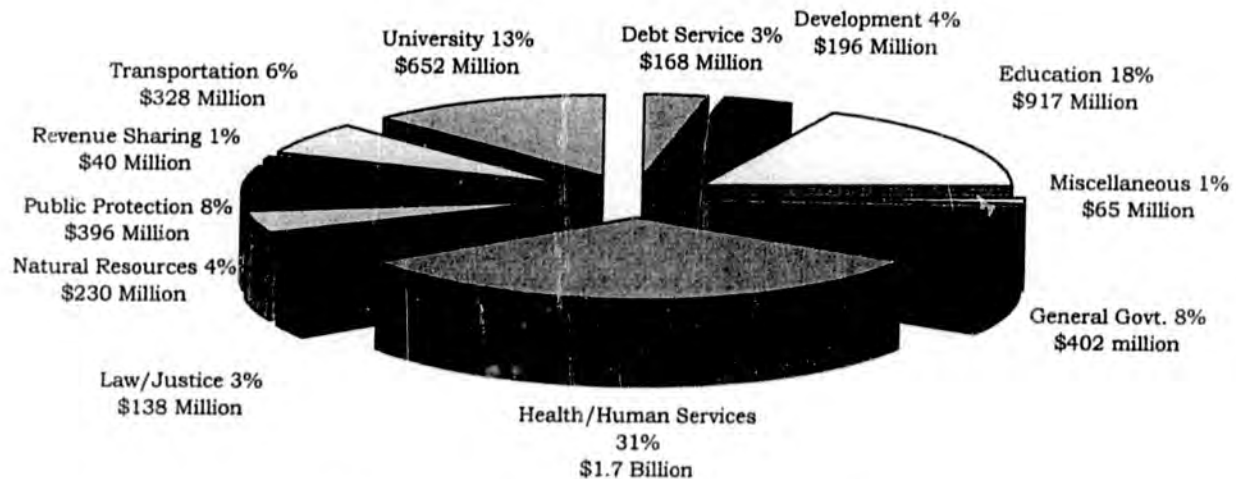
C Duplicated authorizations are in the budget twice, such as when funds flow in and out of a holding account or one agency pays another for services provided.

D General Obligation bonds are included in the FY2003 capital budget, however, are backed out as duplicated authorizations as the actual costs of the bonds will be incurred as debt payments in future years.

E This amount includes capitalization of Debt Retirement Fund. The legislature appropriated \$20.0 million of the general funds amount needed to pay FY2003 debt as an FY2002 supplemental to the Debt Retirement Fund. It was vetoed down to \$11.5 million to match the amount actually needed in FY2003.

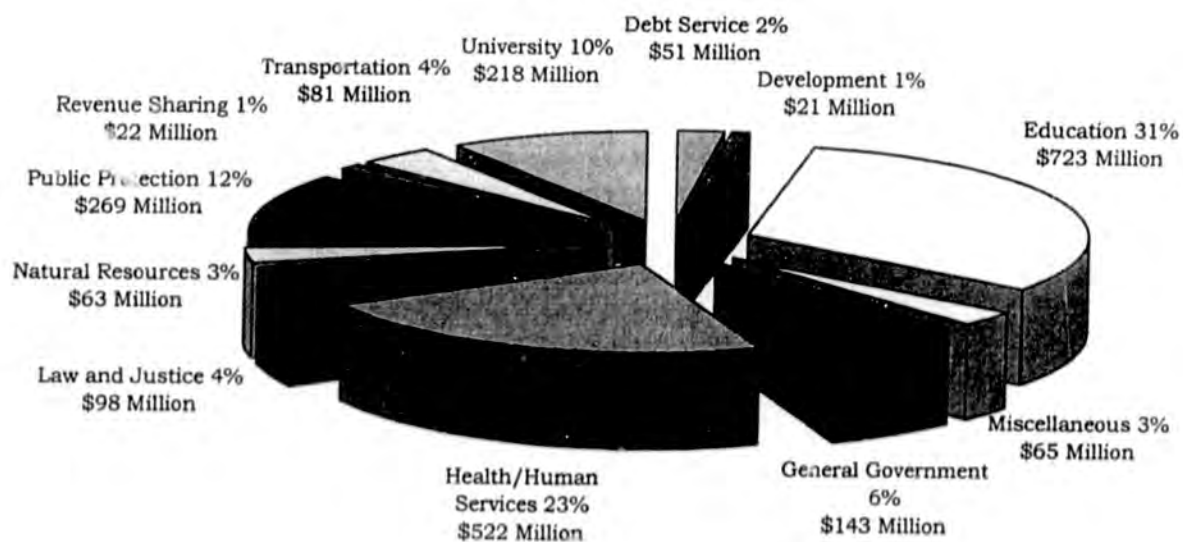
The pie charts (*charts 5 and 6*) provide a sense of the relative share of spending by program area in the FY 04 proposed operating budget in terms of total funds and general funds.

Chart 5
FY 2004 Proposed Operating Budget
All Funds Sources (\$4.4 Billion)
by Program Category*



*Excludes Permanent Fund earnings appropriations for dividends and inflation proofing.

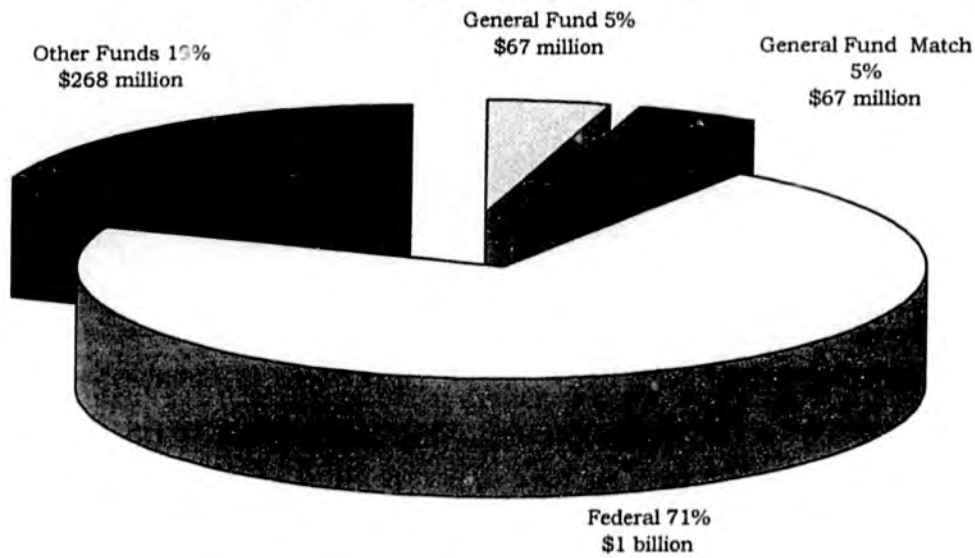
Chart 6
FY2004 Proposed Operating Budget
General Fund (\$2.2 Billion)
by Program Category



*Note that category totals add to more than \$2.2 billion because they include duplications and fund transfers.

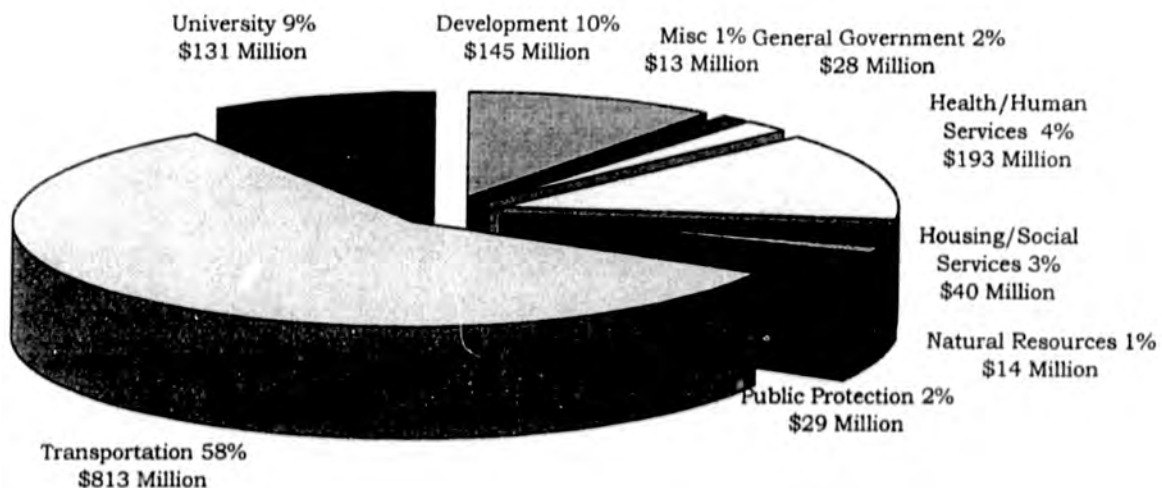
The capital budget is shown in charts 7 and 8 by major funding source and program category.

Chart 7
FY 2004 Proposed Capital Budget
All Fund Sources (\$1.3 Billion)*



*Section dollar totals are greater than total due to rounding.

Chart 8
FY 2004 Proposed Capital Budget
All Fund Sources (\$1.3 Billion)



Spending

In recent years, formula programs and debt service have been primary driving forces in state spending increases. To be successful, any long-term fiscal plan needs to come to grips with these areas of systemic budget growth.

Formula Program Growth

Charts 9 and 10 show formula program growth by fund source and provide some perspective on how their growth affects the state operating budget. Even though the focus here is on *state* spending, it is important to show the growth in federal funding, particularly for Medicaid, because of state match requirements (\$288 million of the \$2.2 billion in general funds for the FY04 operating budget).

Chart 9
Formula Program Growth
by Fund Source
FY 1999 - FY 2003

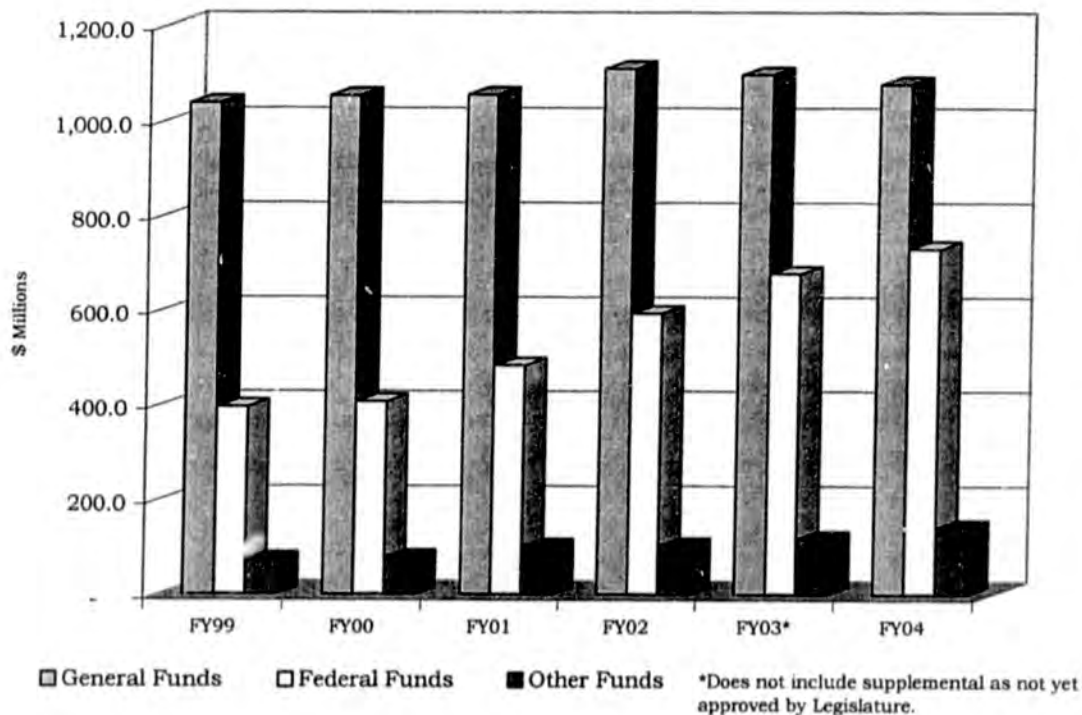


Chart 10
Operating Budgets vs. Formula Programs
General Funds
FY 1994 - FY 2004 Proposed

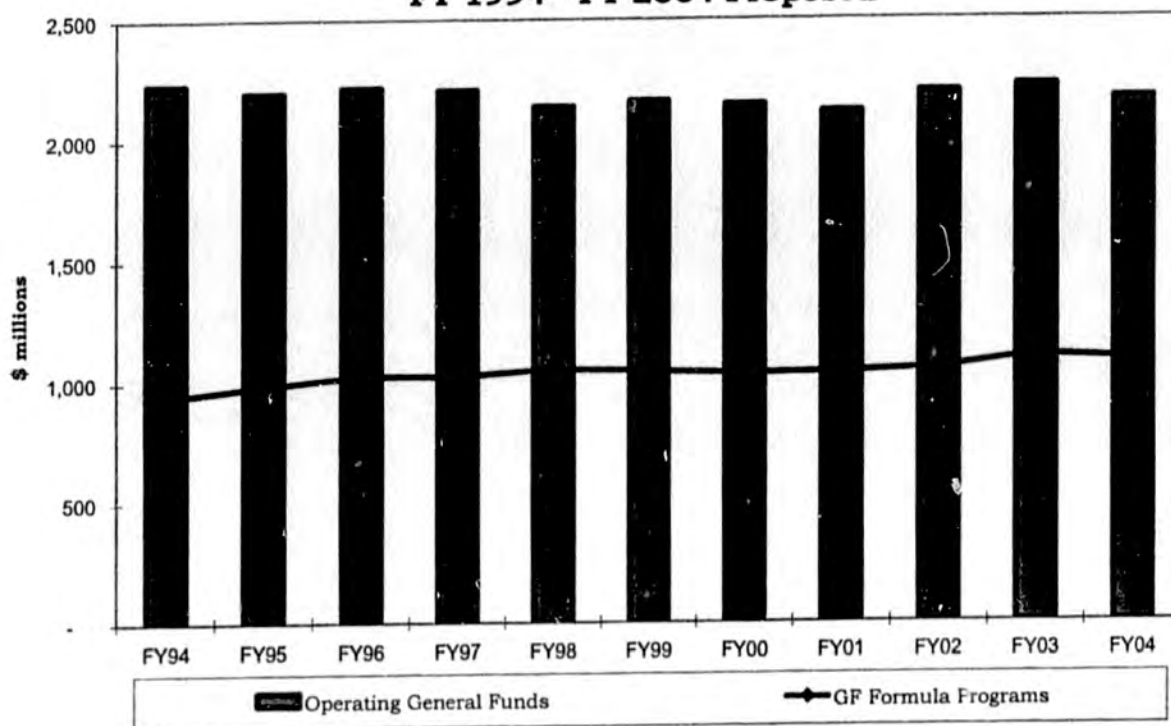


Table 2 is a list of formula programs that highlights changes in the Governor's proposed FY 04 budget. Proposed program cuts eliminate the Longevity Bonus program, reduce Pupil Transportation and the Revenue Sharing/Safe Communities programs. Table 2 highlights formula program changes from FY 03.

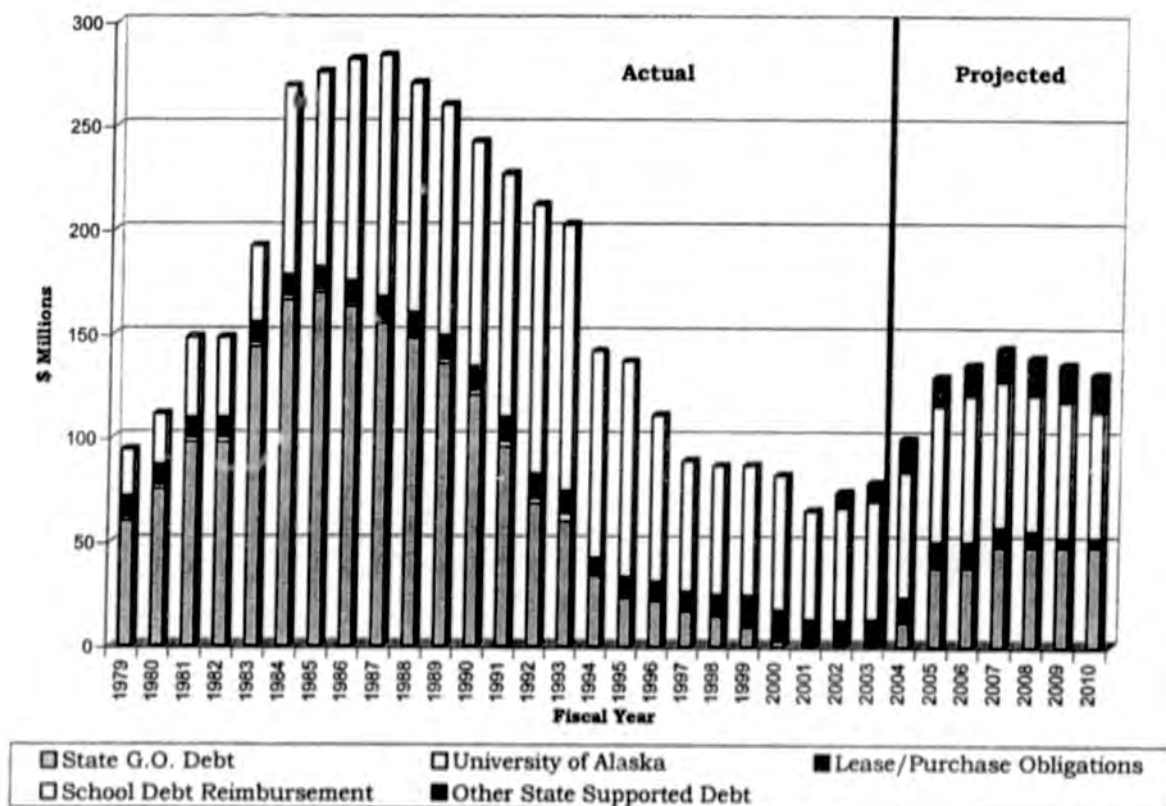
Table 2
Formula Programs
FY 2003 vs. FY 2004 Proposed

Agency	Program	FY 03	FY 04	Change
DOA	Elected Public Officers Retirement System Benefits	1,093.9	1,493.9	400.0
	Unlicensed Vessel Participant Annuity Retirement Plan	75.0	75.0	-
		1,168.9	1,568.9	400.0
DCED	Power Cost Equalization	15,700.0	15,700.0	-
	State Revenue Sharing	12,855.2	9,641.4	(3,213.8)
	Municipal Assistance/Safe Communities	16,775.5	12,581.6	(4,193.9)
	National Program Receipts	15,830.0	15,830.0	-
	Fisheries Business Tax	1,150.0	1,600.0	450.0
		62,310.7	55,353.0	(6,957.7)
Education	Foundation Program	707,324.3	687,668.1	(19,656.2)
	Tuition Students	2,225.0	-	(2,225.0)
	Boarding Home Grants	335.9	185.9	(150.0)
	Youth in Detention	1,100.0	1,100.0	-
	Pupil Transportation	53,933.8	43,188.2	(10,745.6)
	Community Schools	500.0	-	(500.0)
		765,419.0	732,142.2	(33,276.8)
DHSS	AK Temporary Assistance Program	47,653.7	47,653.7	-
	Adult Public Assistance	54,357.5	57,811.5	3,454.0
	General Relief Assistance	1,061.4	1,549.0	487.6
	Longevity Bonus	47,519.3	-	(47,519.3)
	Old Age Assistance-Alaska Longevity Bonus (ALB) Hold Harmless	1,527.9	-	(1,527.9)
	Tribal Assistance	8,612.5	8,612.5	-
	Permanent Fund Dividend Hold Harmless	13,007.9	15,405.5	2,397.6
	Medicaid Services*	820,036.5	930,873.6	110,837.1
	Child Care Benefits	33,102.0	49,836.1	16,734.1
	Foster Care	17,545.8	18,908.9	1,363.1
	Catastrophic and Chronic Illness Assistance	2,000.0	2,000.0	-
	Children's Health Eligibility	2,588.3	2,279.6	(308.7)
	Subsidized Adoptions & Guardianship	14,610.1	19,011.2	4,401.1
	Schools for the Handicapped	6,846.9	6,297.2	(549.7)
		1,070,469.8	1,160,238.8	89,769.0
DMVA	Retirement Benefits	1,322.5	1,322.5	-
				-
	Total	1,900,690.9	1,950,625.4	49,934.5
	General Funds	1,098,588.2	1,078,333.7	(20,254.5)
	Federal Funds	678,301.4	731,314.2	53,012.8
	Other Funds	117,072.1	140,977.5	23,905.4

Debt Service Growth

Another area of recent and future growth in the state budget is debt service. During the past decade, the state was able to leverage non-general fund revenue sources to finance capital projects, e.g., tobacco settlement receipts, and the Alaska Housing Finance Corporation (AHFC) dividend. However that all changed last year when voters approved the first issuance of general obligation bonds since 1980 for transportation and school construction projects. The Legislature also approved a school debt reimbursement program for municipalities and capital project debt reimbursement for various university, harbor and power projects.

Chart 11
State Supported Debt Service
Historical and Projected



The net increase to the state general fund operating budget for debt service in FY 04 is \$36 million. This would have been higher by \$6.6 million if the Governor's proposal had not prorated school debt reimbursement by 10%. (Proration means that if the state approved share of a municipality's debt service is 60%, the Governor's proposal will actually fund it at 54% in the FY

04 budget.) Debt service will increase in the future as additional authorized bonds are sold. Table 3 provides a detailed breakdown of the state's debt obligations and the revenue sources used to meet them.

Table 3
FY2004 Proposed
Debt Obligations and Revenue Sources
(\$ thousands)

Debt	FY2003	FY2004	Inc/(Dec)
School Debt Reimbursement (estimated maximum per school districts)	52,536.0	59,421.7	6,885.7
Lease Finance			
API Replacement	1,635.9	706.0	(929.9)
Palmer Airport Fire Facility	759.7	756.8	(3.0)
Spring Creek Correctional Facility	4,002.0	3,991.2	(10.8)
Palmer Courthouse	415.5		(415.5)
Kenai Courthouse	566.4		(566.4)
Anchorage Times Building	789.4	789.3	(0.1)
Soldotna DOT Maintenance Facility	636.6	639.3	2.7
Anchorage Health Lab	2,287.6	2,319.1	31.5
Fairbanks Courthouse	2,899.5	2,900.3	0.8
Trustee Fees	100.0	100.0	0.0
Total Lease Finance	14,092.7	12,201.9	(1,890.7)
Atwood Building	3,549.4	3,549.4	0.0
AHFC Debt	50,000.0	56,002.0	6,002.0
HB528- University		1,412.9	1,412.9
HB528- Harbors		1,212.1	1,212.1
HB528- Power Projects		3,705.8	3,705.8
General Obligation Bonds- Education and Museum		6,693.5	6,693.5
General Obligation Bonds- GF Transportation		3,211.6	3,211.6
General Obligation Bonds- GARVEE Transportation		2,000.0	2,000.0
Tobacco Securitization- 2000	10,095.8	8,801.7	(1,294.1)
Tobacco Securitization- 2001	10,095.8	8,801.7	(1,294.1)
Total Debt	140,369.6	167,014.3	26,644.7
Fund Sources			
School Fund (Cigarette Tax)	31,600.2	28,600.0	(3,000.2)
AHFC Dividend (corporate debt)	50,000.0	56,002.0	6,002.0
Debt Retirement Fund Balance 1)	2,350.0	7,869.8	5,519.8
Tobacco Securitization- 2000	10,095.8	8,801.7	(1,294.1)
Tobacco Securitization- 2001	10,095.8	8,801.7	(1,294.1)
Investment Loss Trust Fund balance	100.0	2,944.7	2,844.7
ACPE Dividend	783.1		(783.1)
AHFC Dividend (DRF)	18,700.0		(18,700.0)
FY2002 Supplemental to Debt Retirement Fund	11,531.7		(11,531.7)
Atwood Building bond interest earnings		1,636.9	1,636.9
Atwood Building earnings from private tenant rent		1,081.6	1,081.6
Municipal Bond Bank interest on reserve account		775.0	775.0
Lease Retirement Account investment earnings		461.3	461.3
GARVEE Transportation Bonds Federal Revenue (estimate)		1,700.0	1,700.0
GARVEE Transportation Bonds AATP Match (estimate)		300.0	300.0
General Funds Required	5,113.0	48,039.7	42,926.7
Total Fund Sources	140,369.6	167,014.3	26,644.7
General Fund Appropriations			
Appropriation to Debt Retirement Fund	8,000.0	40,877.9	32,877.9
Appropriation to Administration for Atwood Building Debt	3,549.4	830.9	(2,718.5)
Appropriation to University for HB528 Debt		1,412.9	1,412.9
Appropriation to Transportation and Public Facilities for HB528 Debt		1,212.1	1,212.1
Appropriation to Community and Economic Development for HB528 Debt		3,705.8	3,705.8
Subtotal General Fund Appropriations	11,549.4	48,039.7	36,490.3

1) Reduce FY 2003 school debt reimbursement based on actual entitlements, plus increased cigarette tax receipts added \$6,436.3 to the debt retirement fund balance.

The cost to the state for financing future debt is dependent on the state's credit rating. Currently the state enjoys an excellent credit rating – Aa2 Moody's, AA for both Standard and Poors and Fitch. While none of the rating agencies seem disposed towards downgrading the state's credit rating, they are quite aware of Alaska's long term fiscal situation and are watching closely to see how it is addressed. The importance of bringing recurring revenues and expenditures in line will have a significant impact on the state's future bond ratings.

Long Term Fiscal Plan

Some analysts believe that the most viable option under discussion for bridging the fiscal gap is the Percentage of Market Value (POMV) proposal that has been recommended in the past by the Permanent Fund trustees. The trustees say that the POMV payout proposal would solve a major portion of the fiscal gap, guarantee that Permanent Fund dividends will continue and extend the life of the CBR before additional revenue measures need be considered.

The basic elements of the Board's proposal are straightforward: Five percent of the market value of the Permanent Fund would be paid out each year (about \$1.2 billion). The trustees have made no recommendations on how the payout is to be spent. (For modeling purposes we assume it is split evenly between dividends and the general fund.) On average, the Fund is expected to earn about 7.95% per year so the payout rule would add 3% each year to the value of the Fund to offset the effects of inflation and maintain its real value into the future.

The 5% payout rate is at the upper end of what other endowments have found to be sustainable and was chosen by the Fund trustees as a balance between spending for the current generation of Alaskans and maintaining the purchasing power of the Fund for future generations.

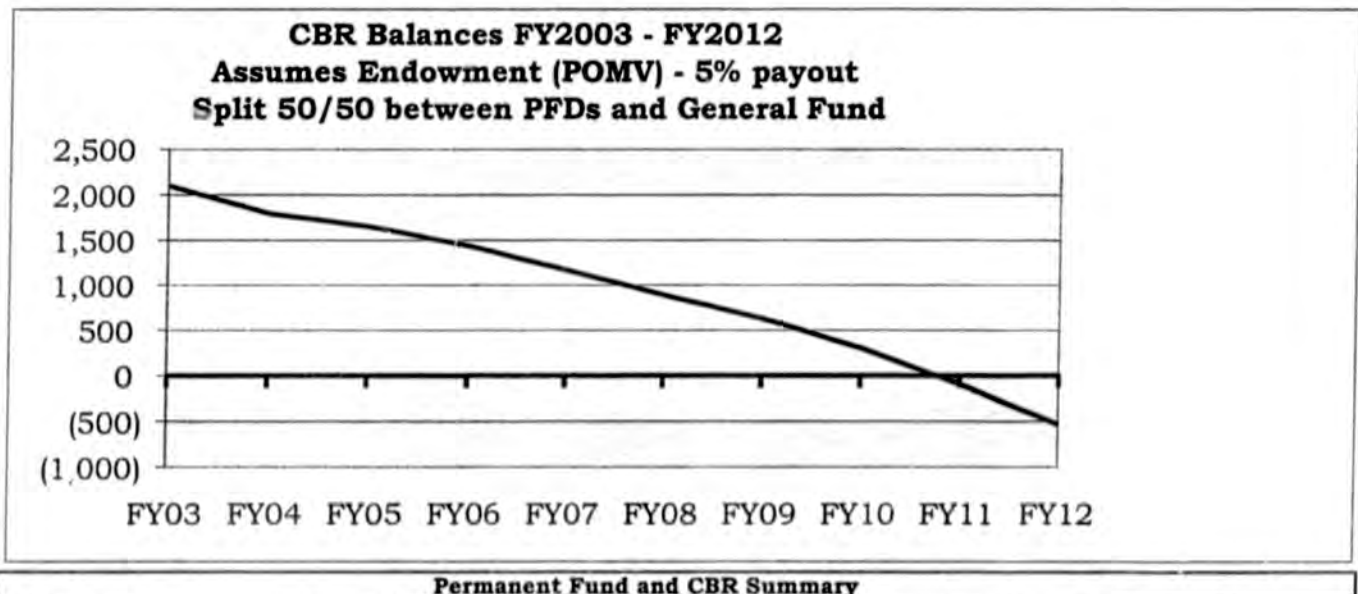
Currently dividends are paid out of the Earnings Reserve Account (ERA) of the Fund. Because of market losses, the balance in the ERA in September 2002 was zero, prompting speculation that funds might not be available to pay a 2003 dividend. A POMV approach would ensure that there would be funding available each year to pay dividends regardless of market volatility.

The Governor has said that no change will be made to the Dividend Program without a vote of the people. If offered as a constitutional amendment, a POMV formula as proposed by the Trustees would require a 2/3 vote approval of each house of the Legislature and then be approved by voters in a statewide election. If approved in 2004 by voters, with an effective date of January 2005, \$623 million would be available for dividends and an equal amount to the general fund.

If the state were not to adopt the POMV approach, but instead continue the status quo, the CBR can be expected to be drained completely by February 2006. Without a major source of new revenue at that time, there would be no choice but to make severe cuts in state programs or use Permanent Fund earnings, which could put both the dividend and inflation-proofing at risk.

The POMV provision by itself would extend the projected depletion date for the CBR to August 2008. Combined with the Governor's FY 04 budget and legislation proposals, the date of CBR depletion is pushed out to April 2011, giving time for additional recurring resource development revenues, such as those that would come from production of natural gas from the North Slope or from ANWR.

Chart 12



Permanent Fund and CBR Summary										
	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12
Permanent Fund Earnings to General Fund	-	-	623	629	646	673	698	719	742	764
Permanent Fund Expected Earnings	(516)	1,651	1,756	1,813	1,872	1,932	1,993	2,054	2,116	2,178
End-of-year market value of Permanent Fund	22,694	24,173	24,953	25,766	26,596	27,425	28,266	29,114	29,967	30,823
End-of-year Earnings Reserve balance	382	614	-	-	-	-	-	-	-	-
End-of-year CBRF balance	2,100	1,796	1,655	1,438	1,169	892	633	304	(88)	(533)
Projected Dividend (by Calendar Year)	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Status Quo	1,120	820	550	700	950	1,220	1,410	1,540	1,660	1,760
POMV 5% Model	1,120	820	1,000	990	1,010	1,040	1,070	1,090	1,120	1,140
Projected Date of CBR Depletion										
Status Quo	February '06									
POMV 5% Model	April '11									
Department of Revenue Shortcut Model										

Summary

The initial focus of the Governor's proposed FY 2004 budget is on the fiscal gap between general fund revenues and expenditures. The first step is to slow the drawdown of the CBR balance to maintain its usefulness as a buffer to oil price volatility. The proposed budget cuts nearly \$190 million in built in general fund cost increases, mostly in formula programs and debt service to achieve \$20 million in overall savings compared to FY 2003. The Governor also proposes \$113 million in new revenues from a variety of sources and one time transfers of \$121 million in funds from other sources to the general fund. Altogether these actions (plus higher oil prices) would decrease the draw on the CBR from \$494 in FY 2003 to \$393 million for the Governor's FY 2004 proposed budget. This compares to the 842 million CBR Draw that was projected when the Legislature approved the current year budget last May.

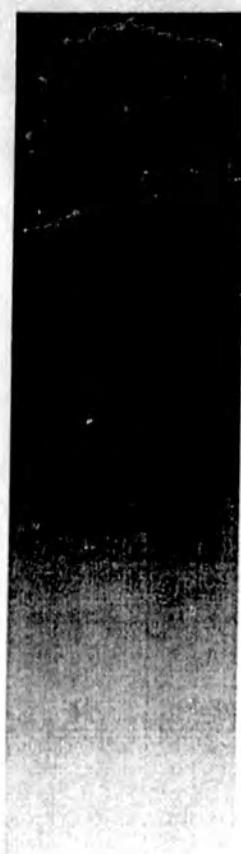
For the longer-term, the Governor has asked the Permanent Fund trustees to make recommendations on how to best protect the Permanent Fund itself as well as how to provide stable and predictable distribution of earnings for dividends. If a similar POMV proposal as that discussed in this overview could extend the life of the CBR to August 2011. This would allow more time for resource development revenues to come on line and postpone the day when broad-based taxes need be considered.

SCOMM

134:3

State of Alaska
Division of Retirement & Benefits
Top 20 TRS employers by salary

Employer Number	Employer Name	Annual Earnings	FY 2004 Employer Rate	Estimated FY 2004 Employer cost	4% Increase Employer Cost	Total Expected FY 05 Employer Cost - 16%
701	Anchorage School District	\$ 174,110,494.00	12.00%	\$ 20,893,259	\$ 6,984,419.76	\$ 27,857,679
706	Fairbanks North Star Borough School District	\$ 57,301,300.00	12.00%	\$ 6,876,156	\$ 2,282,052.00	\$ 9,168,208
722	Matanuska-Susitna Borough School District	\$ 50,380,853.00	12.00%	\$ 6,045,702	\$ 2,016,234.12	\$ 8,060,936
733	University of Alaska	\$ 37,998,991.00	12.00%	\$ 4,559,879	\$ 1,519,959.64	\$ 6,079,839
746	Kenai Peninsula Borough School District	\$ 37,313,528.00	12.00%	\$ 4,477,623	\$ 1,492,541.12	\$ 5,970,164
710	City & Borough of Juneau School District	\$ 19,867,624.00	12.00%	\$ 2,384,115	\$ 794,704.96	\$ 3,178,820
754	Lower Kuskokwim School District	\$ 18,407,816.00	12.00%	\$ 2,208,938	\$ 736,312.64	\$ 2,945,251
736	North Slope Borough School District	\$ 14,173,506.00	12.00%	\$ 1,700,821	\$ 566,940.24	\$ 2,267,761
718	Kodiak Island Borough School District	\$ 12,306,958.00	12.00%	\$ 1,476,835	\$ 492,278.32	\$ 1,969,113
751	Northwest Arctic Borough School District	\$ 12,289,935.00	12.00%	\$ 1,474,792	\$ 491,597.40	\$ 1,966,390
752	Bering Straits School District	\$ 10,819,453.00	12.00%	\$ 1,298,334	\$ 432,778.12	\$ 1,731,112
714	Ketchikan Gateway Borough School District	\$ 9,061,991.00	12.00%	\$ 1,087,439	\$ 362,479.64	\$ 1,449,919
753	Lower Yukon School District	\$ 8,902,384.00	12.00%	\$ 1,068,286	\$ 356,095.36	\$ 1,424,381
727	Sitka School District	\$ 6,727,046.00	12.00%	\$ 807,246	\$ 269,081.84	\$ 1,076,327
737	Alaska Department of Education & Early Dev.	\$ 6,056,768.00	12.00%	\$ 726,812	\$ 242,270.72	\$ 969,083
756	Southwest Region School District	\$ 4,994,756.00	12.00%	\$ 599,371	\$ 199,790.24	\$ 799,161
730	Valdez City School District	\$ 4,609,664.00	12.00%	\$ 553,160	\$ 184,386.56	\$ 737,546
735	Galena City School District	\$ 4,434,404.00	12.00%	\$ 532,128	\$ 177,376.16	\$ 709,505
762	Yukon-Koyukuk School District	\$ 3,767,177.00	12.00%	\$ 452,061	\$ 150,687.08	\$ 602,748
757	Lake and Peninsula Borough School District	\$ 3,174,454.00	12.00%	\$ 380,934	\$ 126,978.16	\$ 507,913



State of Alaska

Public Employees' Retirement System Teachers' Retirement System

Presentation to the House Ways & Means Committee

April 30, 2003



Marsh & McLennan Companies

Alaska Division of Retirement and Benefits
Public Employees' Retirement System (PERS) Plan Comparison Chart

Tier I 1/1/61 - 6/30/86	Tier II Entered on or after 7/1/86	Tier III Entered on or after 7/1/96
After tax employee contribution: 4.25% for all others 5% for police and fire 4.25% for school district employees Contributions changed to Tier II level as noted under Tier II.	Pre-tax employee contribution: 6.75% beginning 1/1/87—all others 7.5% beginning 1/1/87—police and fire 9.6% beginning 7/1/99—school district	No change from Tier II.
Members vest with 5 years of service.	No change.	No change.
Normal retirement age is 55, with early retirement at age 50; police/fire members can retire at any age after 20 years of police/fire service; all other members can retire at any age after 30 years of membership service. 7/1/96—Early retirement reduction changed to Tier III.	Normal retirement age is 60, with early retirement at age 55; police/fire members can retire at any age after 20 years of police/fire service; all other members can retire at any age after 30 years of membership service. 7/1/96—Early retirement reduction changed to Tier III.	No change from Tier II. However, early retirement reduction will be ½% per month or 6% per year for every year less than the required normal retirement age.
Benefit formula was 2% X "years of service" X "average salary" based on the high three consecutive years salaries. Benefit formula changed to Tier II in 1986 applied to all service earned after that effective date. P/F 2% X 10, 2.5% over 10.	Benefit formula is 2% for first 10 years, 2.25% for the next 10 years, and 2.5% per year thereafter. Benefit calculation is determined on the average of the high three consecutive years salary. No change to P/F.	Benefit formulas did not change; however, the benefit calculation for "all others" occupation is determined on the average of the high five consecutive years salary and the Benefit calculation for "P/F" occupational code is high three consecutive years regardless of tier (effective 2002).
An Alaska Cost-of-Living Allowance is payable to benefit recipients who remain domiciled in Alaska after retirement. The allowance is \$50 or 10% of the base benefit, whichever is greater.	An Alaska Cost-of-Living Allowance is payable to benefit recipients 65 or older or disability benefit recipients regardless of age who remain domiciled in Alaska after retirement. The allowance is \$50 or 10% of the base benefit, whichever is greater.	No change from Tier II.
PRPA increases granted on an ad hoc basis. The automatic PRPA legislated in 1986 applied to all members regardless of hire date.	Automatic PRPA adjustments to disabled members, retirees 60 and over, and those who have received benefits for 5 years.	No change from Tier II.
Major medical insurance is provided to all benefit recipients and their eligible dependents at no cost.	Major medical insurance is provided at no cost to disabilitants, regardless of age and benefit recipients over age 60 or • police/fire members with 25 years of police/fire service • all other members with 30 years of membership service and their eligible dependents at no cost. Benefit recipients under 60 must pay the full premium cost.	Same as Tier II. However, employees must accrue a minimum of 10 years of credited service* , to have system-paid coverage at age 60. Employees with less than 10 years must pay the full premiums as long as they wish to continue medical coverage.
Disability benefits for members: nonoccupational disability benefits are calculated as a normal retirement. Occupational disability provides 40% of the gross monthly compensation. Different occupational disability formula available before 7/1/76.	No change.	No change.

Alaska Division of Retirement and Benefits
Teachers' Retirement System (TRS) Plan Comparison Chart

Tier I 7/1/55 - 6/30/90	Tier II Entered on or after 7/1/90
After tax employee contribution: 7% Contributions changed to Tier II level as noted under Tier II.	Pre-tax employee contribution: 8.65% beginning 1/1/91
Members vest with 8 years of service.	No change.
Normal retirement age is 55, with early retirement at age 50; teachers can retire at any age after 20 years of membership service.	Normal retirement age is 60, with early retirement at age 55; teachers can retire at any age after 20 years of membership service.
Benefit formula was 2% X "years of service" X "average of high 3 contract salaries." Benefit formula changed to Tier II in 1990 applied to all service earned after the effective date.	Benefit formula is: 2% for the first 20 years, 2.5% thereafter. Benefit calculation is determined on the average of the high three contract salaries.
An Alaska Cost-of-Living Allowance is payable to benefit recipients who remain domiciled in Alaska after retirement. The allowance is 10% of the base benefit.	An Alaska Cost-of-Living Allowance is payable to benefit recipients 65 or older or disability benefit recipients regardless of age who remain domiciled in Alaska after retirement. The allowance is 10% of the base benefit.
PRPA increases granted on an ad hoc basis. The automatic PRPA legislated in 1990 applied to all members regardless of hire date.	Automatic PRPA adjustments to disabled members, retirees 60 and over, and those who have received benefits for 8 years.
Major medical insurance is provided to all benefit recipients and their eligible dependents at no cost.	Major medical insurance is provided at no cost to disability recipients, regardless of age and retirees and survivors over age 60. Retirees under 60 with less than 25 years of membership service must pay the full premium cost.
Disability benefits are 50% of base salary, plus 10% for each eligible dependent child up to a maximum of 4 children.	No change.

State of Alaska - PERS Key Results
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	<u>FY04</u>	<u>FY05</u>
Average Contribution Rate:	6.77%	24.91%
Board Adopted Rate:	6.77%	11.77%

	<u>June 30</u>	
	<u>2001</u>	<u>2002</u>
Funding Ratio:		
Non-Medical Benefits:	143.7%	120.9%
Total Benefits:	100.9%	75.2%

Plan Assets	\$ 7.412 Billion
Plan Pension Liabilities	\$ 6.133 Billion
Plan Pension/Medical Liabilities:	\$ 9.859 Billion

State of Alaska - TRS Key Results

	<u>FY04</u>	<u>FY05</u>
Total Contribution Rate:	14.44%	35.57%
Board Adopted Rate:	12.00%	16.00%

	<u>June 30</u>	
	<u>2001</u>	<u>2002</u>
Funding Ratio:		
Non-Medical Benefits:	119.7%	93.2%
Total Benefits:	95.0%	68.2%

Plan Assets:	\$ 3.689 Billion
Plan Pension Liabilities:	\$ 3.959 Billion
Plan Pension/Medical Liabilities	\$ 5.411 Billion

Background

Total system costs can be defined by the following equation:

$$\begin{aligned} & \text{Benefits Paid} \\ & \quad (\text{Pension and Medical}) \\ & + \\ & \text{Administration Expenses} \\ & = \\ & \text{Employer and Member Contributions} \\ & \quad (\text{Employer Contribution is Variable/Member Contribution is Fixed}) \\ & + \\ & \text{Net Investment Income/Loss} \\ & \quad (\text{Expected annual rate of return: 8.25\%}) \end{aligned}$$

Background

Actuarial methods are used to allocate system costs over time in an orderly fashion. They do not, however, change the ultimate cost of the system.

System Funding Goals

The following are system funding goals based on observed board discussions:

- Relatively stable contribution rates over time
- Actuarial funding of retiree medical benefits
- 100% funded ratio of assets to accrued liabilities (including retiree medical)
- Pay for benefits during working lifetime



What does an Actuary do?

Goal

**Pay for retirement benefits during
working lifetime of employees**



Age 25
Salary \$40,000

Age 45
20 years of service
annual accrued benefit of \$18,000

Retirement Benefit Calculation

2% of \$40,000 times 10 years = \$ 8,000

2.5% of \$40,000 times 10 years = \$10,000

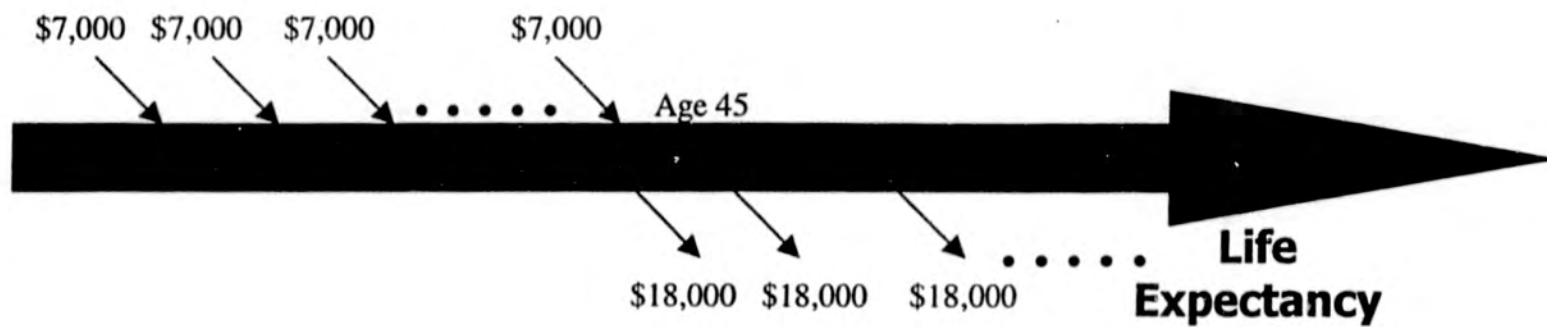
Sum = \$18,000

/ year for life

Goal

**Accumulate \$210,000 during
the employee's 20 year career**

17% of Pay



Additional Assumptions Built into the Model

- **Salary increases**
- **Medical inflation**
- **Employment patterns**
- **Cost of living adjustments**
- **Others**

Entire System

Sum of benefit values for each system participant

\$

Actuarial Cost Method

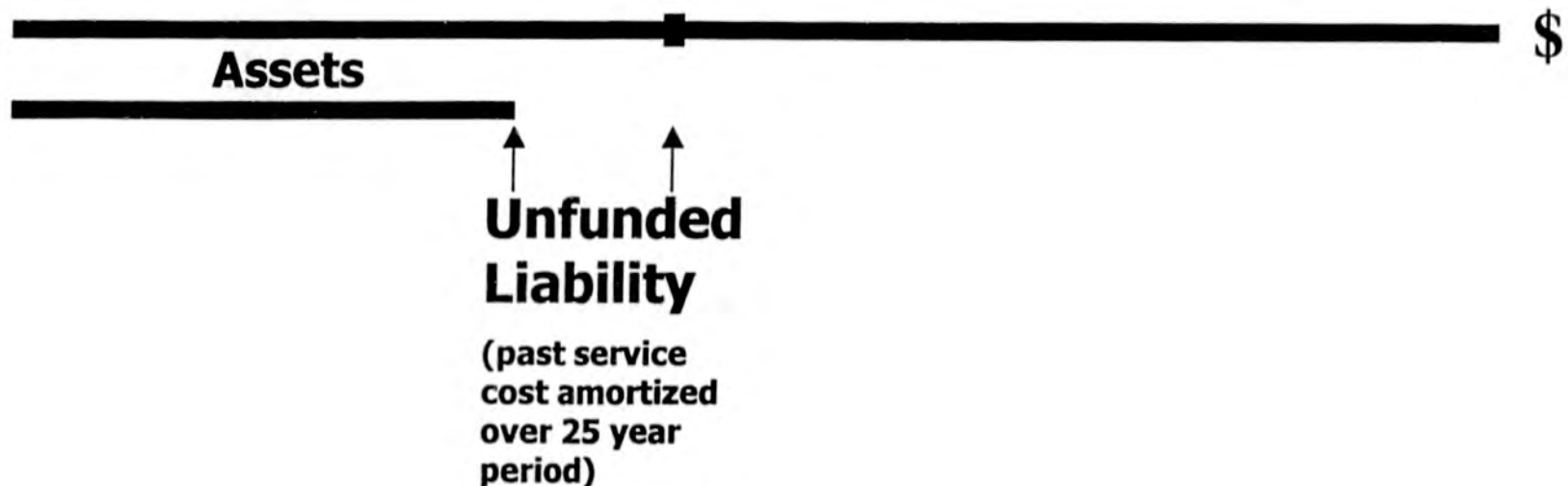
The annual contribution is defined by the following equation:

$$\begin{aligned} &\text{Annual Contribution} \\ &= \\ &\text{This Year's Normal Cost} \\ &+ \\ &\text{Past Service Cost} \end{aligned}$$

Amortization Methods

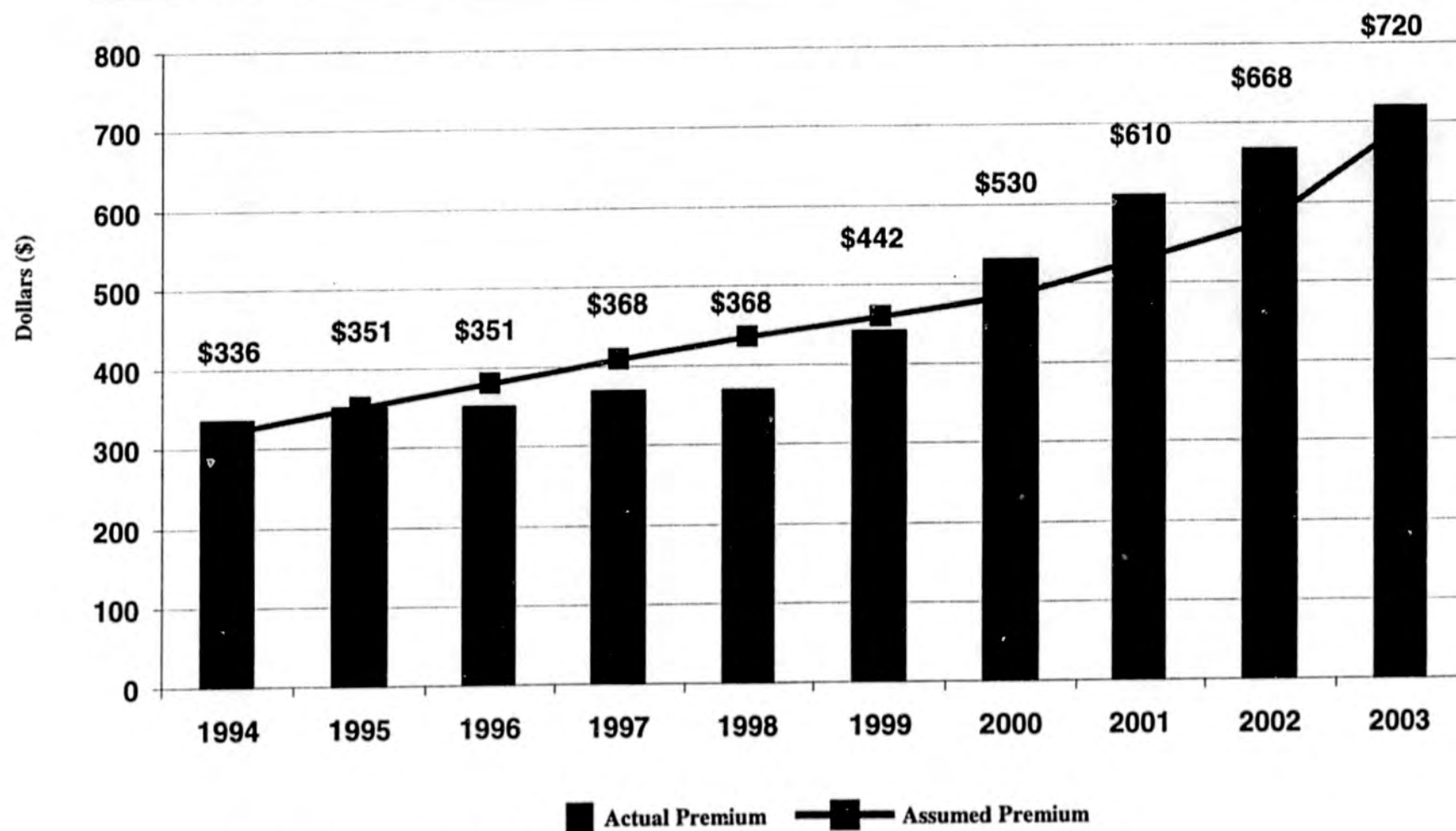
Amortization methods are used to systematically pay off the unfunded liability and achieve 100% funding of the accrued liability

Accrued Liability Future Normal Costs

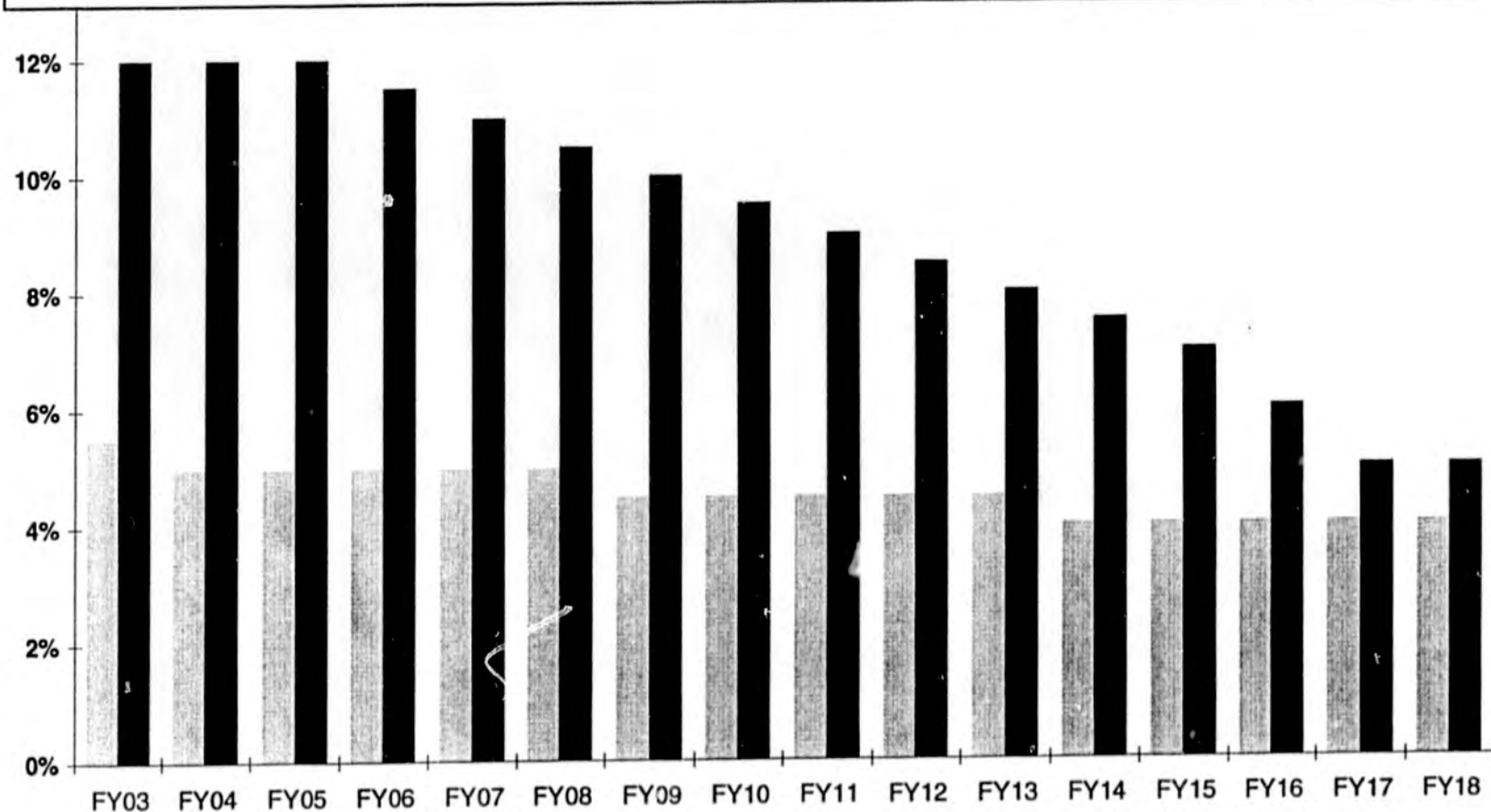


State of Alaska - PERS & TRS

Monthly Blended Premium per Retiree for Health Coverage



State of Alaska PERS & TRS Health Cost Trend Assumption



■ Prior Rates

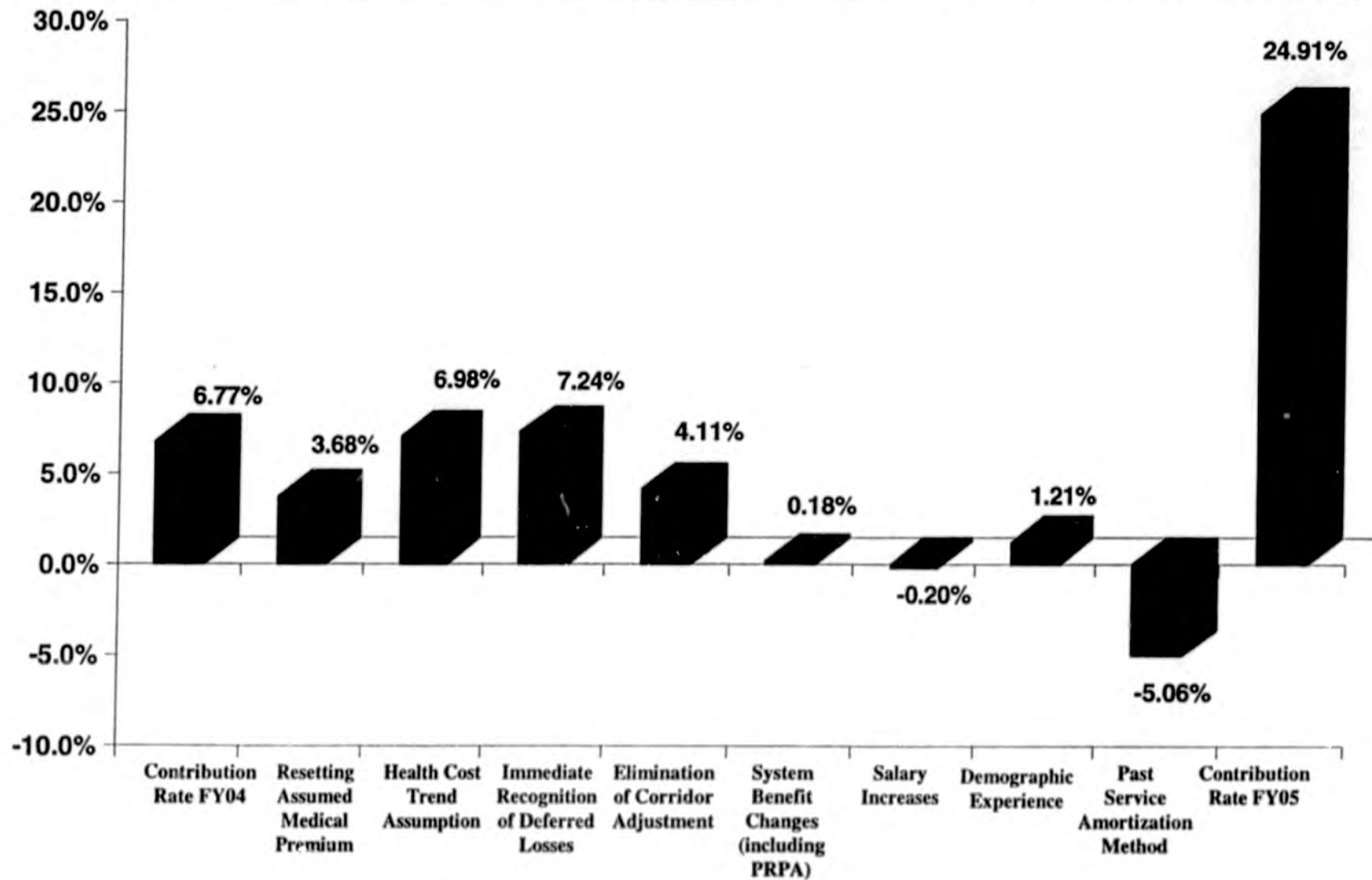
■ Revised Rates

State of Alaska - PERS & TRS Development of Valuation Assets

- Preliminary valuation assets are assumed to return 8.25% per year.
- Asset valuation method recognizes 20% of the investment gain or loss in each of the current and preceding four years.
- The method defines investment gain or loss as the difference between actual investment return (net of expenses) and the expected return (8.25%) on the actuarial value of assets.
- This method will be phased in over the next five years.
- As of June 30, 2002, the actuarial value of assets equals the market value of \$7.413 billion in PERS and \$3.689 billion in TRS.

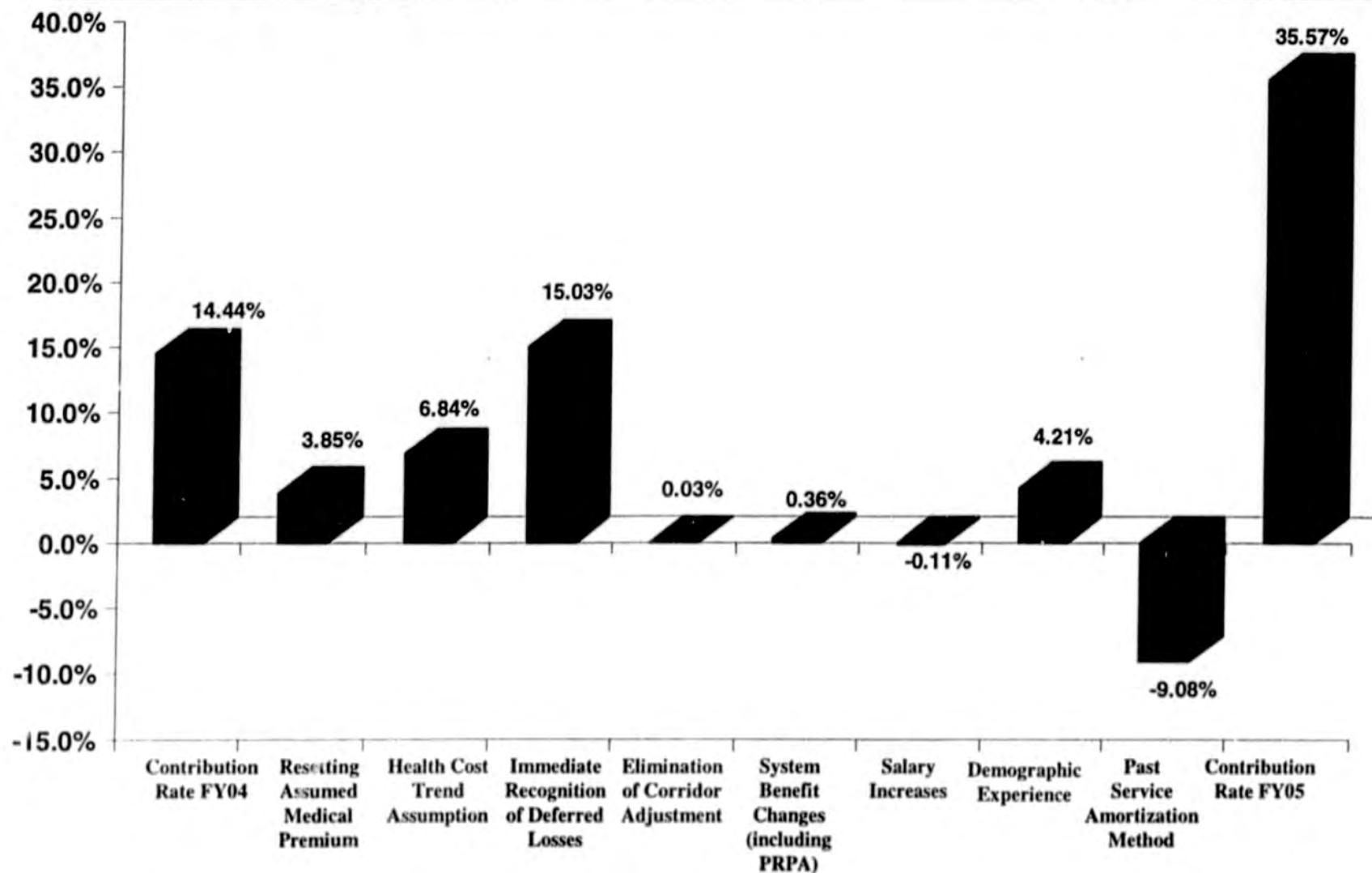
State of Alaska - PERS

Reconciliation of Average Contribution Rate for Fiscal Year 2005

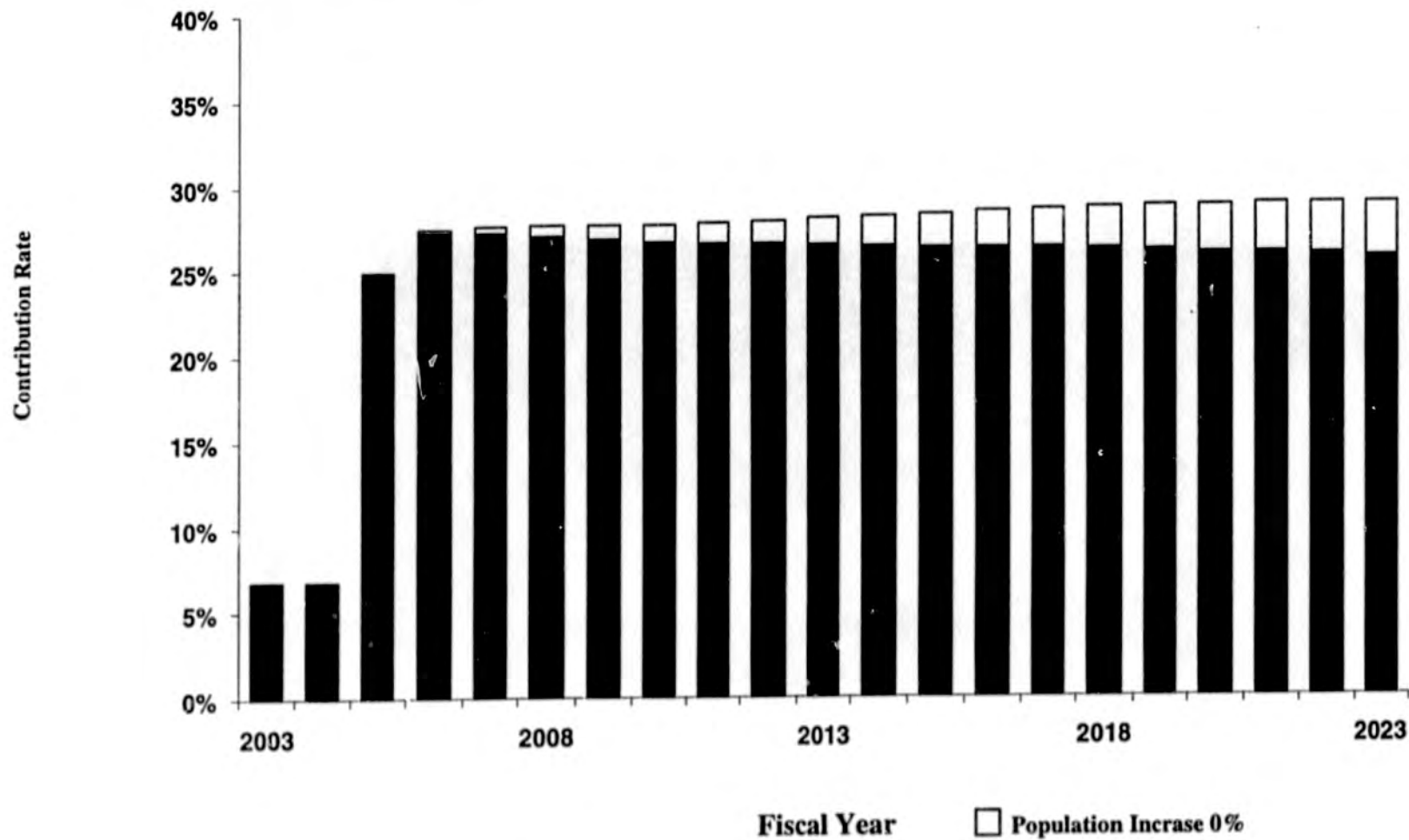


State of Alaska - TRS

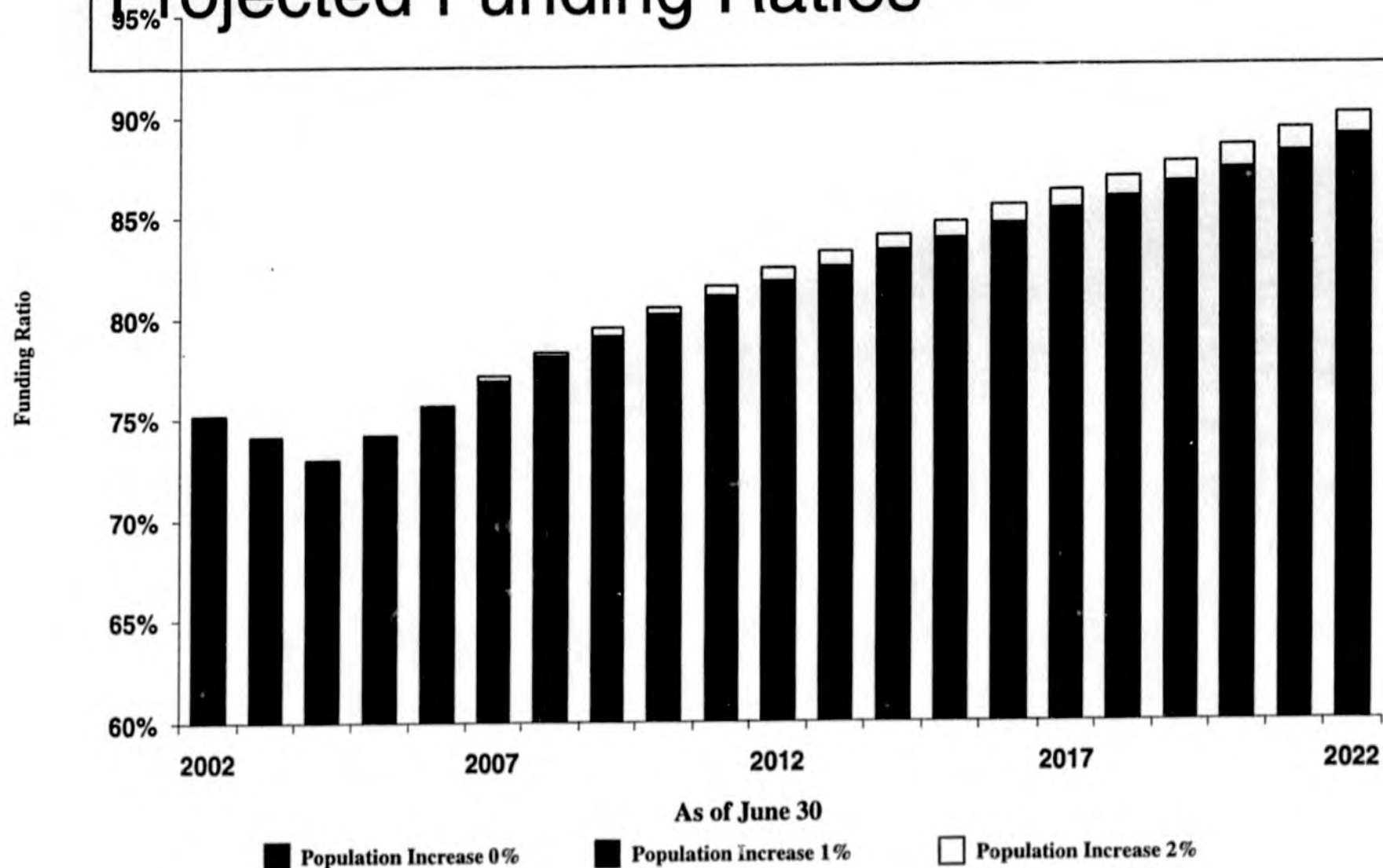
Reconciliation of Total Contribution Rate for Fiscal Year 2005



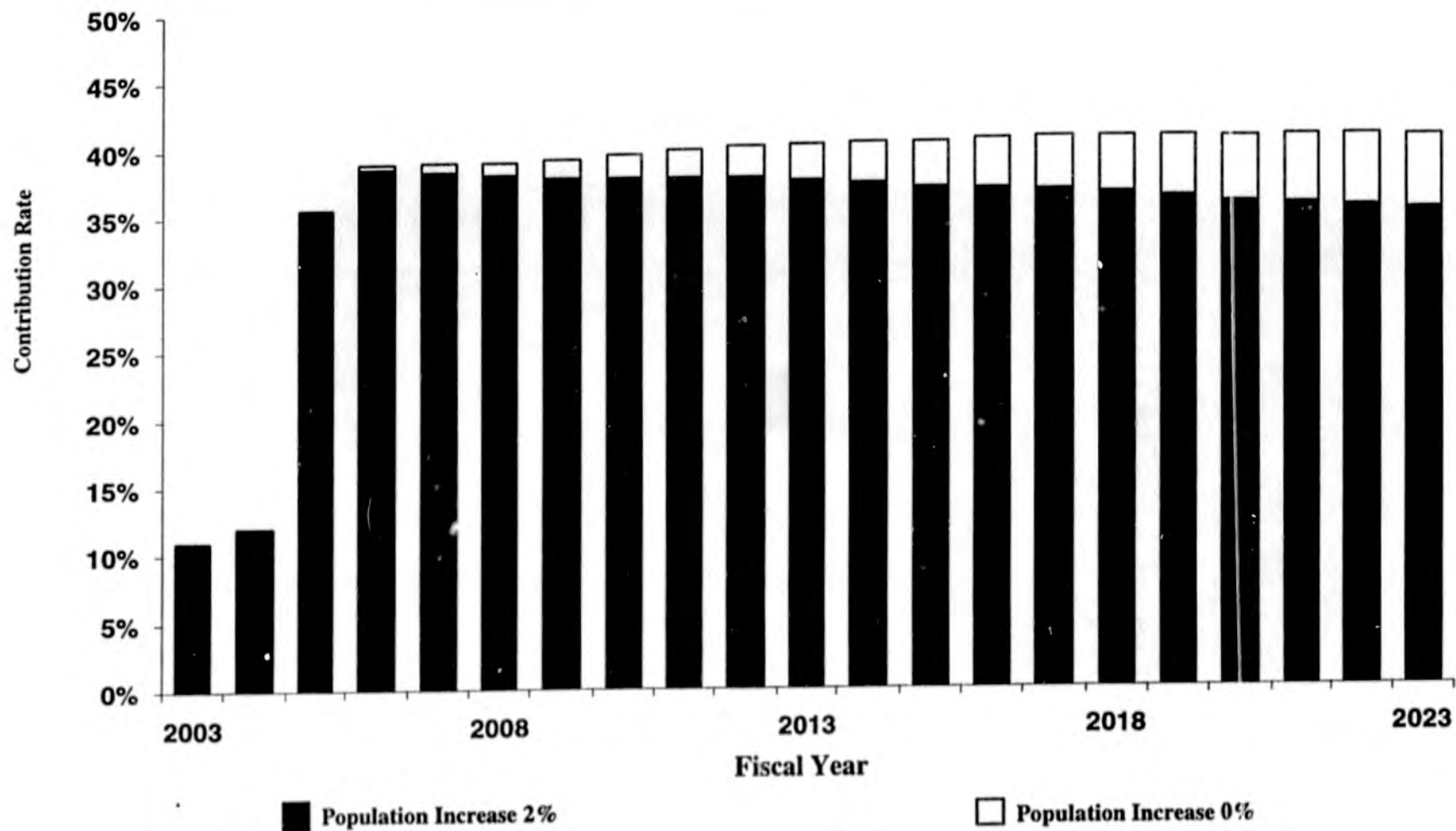
State of Alaska - PERS Projected Contribution Rates



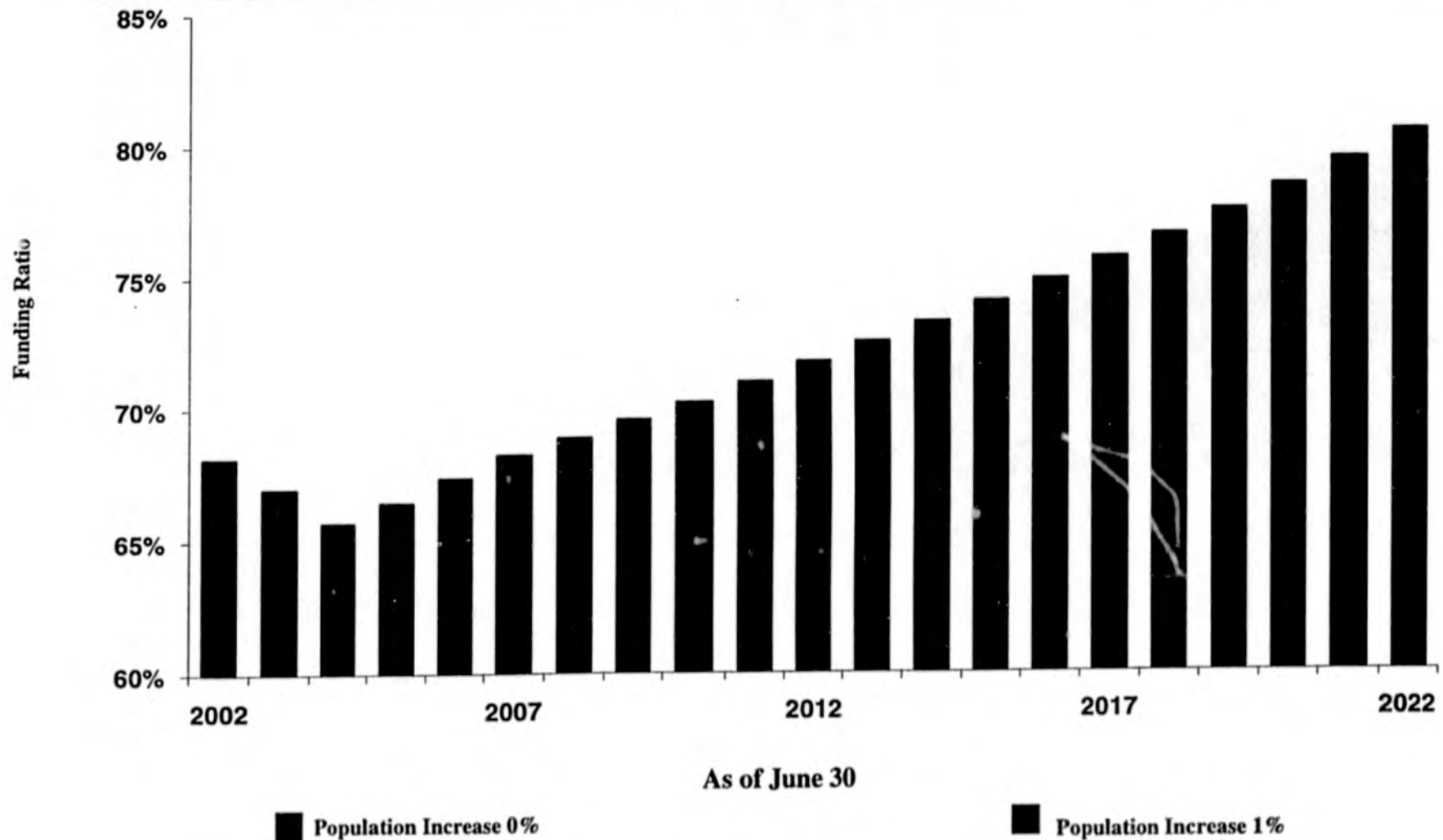
State of Alaska - PERS Projected Funding Ratios



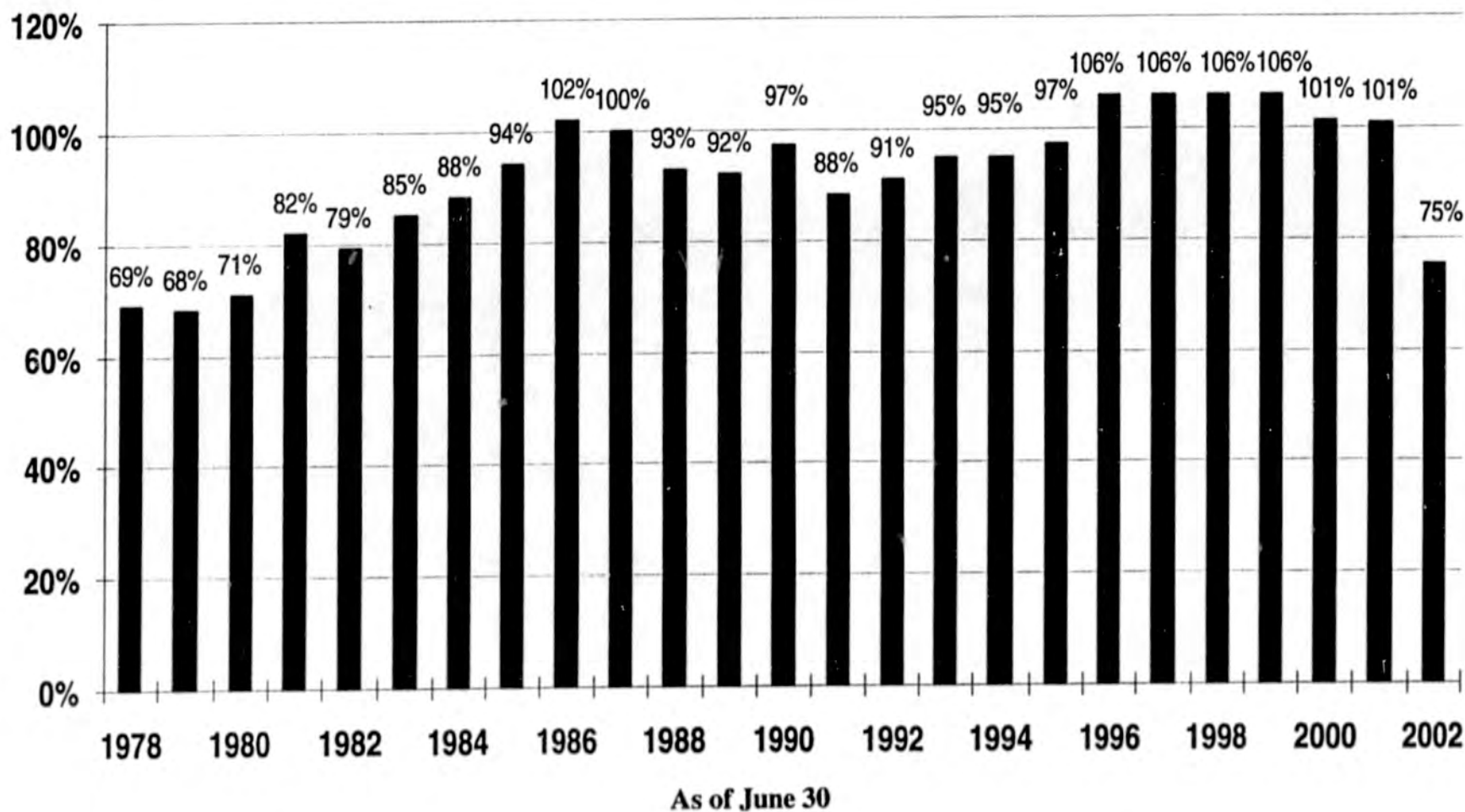
State of Alaska - TRS Projected Contribution Rates



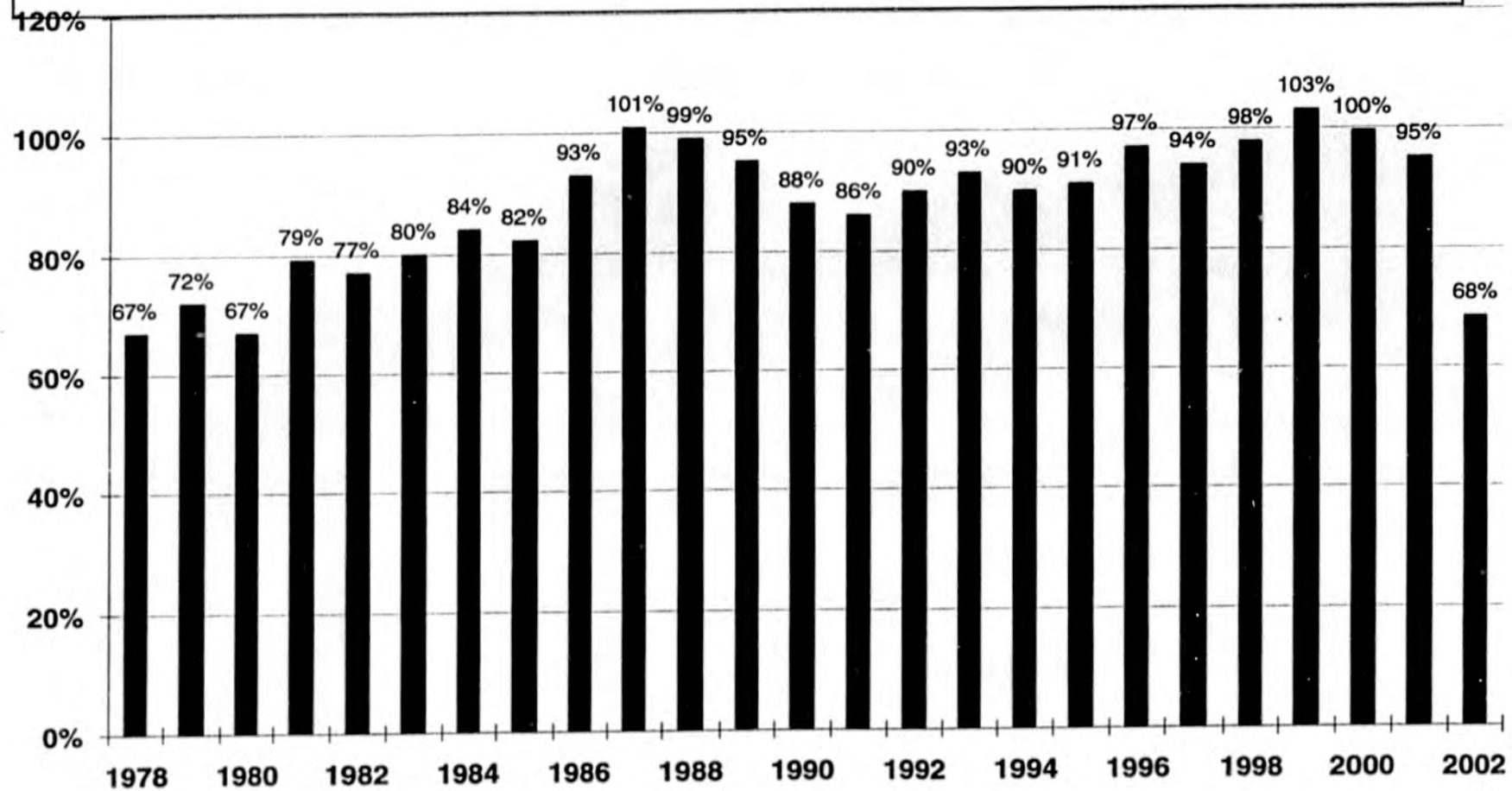
State of Alaska - TRS Projected Funding Ratios



State of Alaska - PERS Funding Ratio History



State of Alaska - TRS Funding Ratio History



State of Alaska - PERS Key Results

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Non-Medical Benefits:	143.7%	120.9%
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Non-Medical Benefits:	119.7%	93.2%
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SCOMM

134:4

Alaska State Legislature

House Special Committee on Ways and Means

Representative Mike Hawker, Chairman

Session Contact:

State Capitol, Room 434

Juneau, AK. 99801

Phone (907) 465-4949

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Staff Contact: Pauly Swanson (907) 465-6820



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Anchorage, AK 99501-2133

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Fax: (907) 269-0248

Sectional Analysis CSHB 236 (W&M)

This Act imposes an education tax on wages and net earnings from self-employment in Alaska and provides that the tax collected be separately accounted for and may be appropriated for education. The tax imposed may not exceed \$100 per calendar year.

Section 1: Provides a short title: Alaska Education Tax Act.

Section 2: Adds the education tax to the list of taxes that are prior, paramount and superior to all other liens upon the real and personal property of the person liable for the tax.

Section 3:

43.45.011: Imposes a tax, not to exceed a combined total of \$100 a calendar year on wages and net earnings from self-employment in excess of \$600. The tax is imposed at a rate of 0% on the first \$600 of earnings, 10% on the next \$1,000 of earnings and 0% on all other earnings. Section 2 also provides that this tax is imposed only in calendar years following a June 30 fiscal year end when the cash balance in the Constitutional Budget Reserve Fund is less than \$1.0 billion. The tax is suspended in a subsequent calendar year following a June 30 fiscal year end when the cash balance in the Constitutional Budget Reserve Fund is greater than \$2.5 billion.

43.45.021: Provides that the education tax is to be collected from wages by employers in accordance with regulations adopted by the Department of Revenue.

43.45.026: Provides that the department may require security deposits from employers who have been delinquent in remitting the education tax.

43.45.031: Provides that self-employed individuals remit their education tax in accordance with regulations adopted by the Department of Revenue.

Committee Members:

Representative Ralph Samuels • Representative Vic Kohring • Representative Norman Rokeberg
Representative Bruce Weyhrauch • Representative Peggy Wilson • Representative Dan Ogg
Representative Max Gruenberg • Representative Carl Moses

43.45.041: Provides for refunds of overpayment of the education tax.

43.45.051: Requires that a person required to report a payment to a self-employed individual to the federal government report the same information to the Department of Revenue.

43.45.061: Provides that the tax collected be accounted for separately and may be used for education.

43.45.099: Defines critical terms by reference to the Internal Revenue Code (26 U.S.C.)

Section 4: Allows the department to develop regulation to implement the Act before the effective date of the Act.

Section 5: Allows Section 4 of the Act to take effect immediately.

Section 6: Allows the other sections of the Act to take effect January 1, 2005, although the education tax will not actually be imposed until the CBR trigger point is reached.

Alaska State Legislature

House Special Committee on Ways and Means

Representative Mike Hawker, Chairman

Session Contact:

State Capitol, Room 434

Juneau, AK. 99801

Phone (907) 465-4949

Fax (907) 465-4979

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23-LS0921\V

Kurtz

3/16/04

CS FOR HOUSE BILL NO. 236()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - SECOND SESSION

BY

Offered:

Referred:

Sponsor(s): REPRESENTATIVE WILSON

A BILL**FOR AN ACT ENTITLED**

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

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

5 * **Section 1.** AS 43.10.042(a) is amended to read:

6 (a) A lien imposed under AS 43.10.010 - 43.10.060 is not valid as against a
7 mortgagee or other lien holder, pledgee, purchaser, or judgment creditor until notice of
8 it is recorded in the records of the recording district where the property subject to the
9 lien is situated. However, regardless of the date the liens are recorded, a lien arising
10 out of a tax due under AS 43.45, AS 43.56, and AS 43.75 [AS 43.55 AND 43.75],
11 including the penalties and interest on the tax, is a lien prior, paramount, and superior
12 to all other liens, mortgages, hypothecations, conveyances, and assignments, upon all
13 the real and personal property of the person liable for the tax, and upon all the real and
14 personal property used with the permission of the owner to carry on the business that

1 is subject to the tax.

2 * **Sec. 2.** AS 43 is amended by adding a new chapter to read:

3 **Chapter 45. Education Tax.**

4 **Sec. 43.45.011. Tax imposed.** (a) There is imposed a tax, not to exceed a
5 combined total of \$100 a calendar year, on wages and net earnings from self-
6 employment in excess of \$600.

7 (b) The rate of the tax is 10 percent.

8 (c) The tax imposed under this section does not apply to wages and net
9 earnings exempt from the tax under federal law.

10 (d) The tax is imposed in a calendar year following a fiscal year during which
11 the cash balance on June 30 of the budget reserve fund created by art. IX, sec. 17,
12 Constitution of the State of Alaska, was less than \$1,500,000,000. Once imposed, the
13 tax remains in effect until suspended under (e) of this section.

14 (e) The tax is suspended in a calendar year following a fiscal year during
15 which the cash balance on June 30 of the budget reserve fund created by art. IX, sec.
16 17, Constitution of the State of Alaska, was equal to or greater than \$2,500,000,000
17 and is not reimposed until the condition in (d) of this section is met.

18 (f) The commissioner shall certify the cash balance of the budget reserve fund
19 on June 30 within one calendar month following the end of each fiscal year.

20 **Sec. 43.45.021. Collection of tax by employer.** (a) An employer shall
21 deduct and withhold 10 percent of an employee's wages subject to withholding under
22 26 U.S.C. 3401 - 3406 on the first regular payroll of the calendar year and from
23 subsequent payrolls until the tax due under this chapter is fully withheld.

24 (b) An employer is liable for the tax required to be withheld from an employee
25 unless the employer can demonstrate that the employer relied on proof provided by the
26 employee that the total tax for the calendar year imposed under AS 43.45.011 had
27 already been withheld under this section or paid under AS 43.45.031. A deduction of
28 the tax may not be made from the wages of an individual who provides proof to the
29 employer that the entire tax imposed under AS 43.45.011 on that individual for the
30 calendar year has already been withheld or paid under AS 43.45.031.

31 (c) Tax withheld by an employer becomes due and shall be paid by an

1 employer to the department in accordance with regulations adopted by the department.

2 (d) An employer shall maintain a record of the amount deducted from the
3 wages of each employee and shall furnish an annual statement of the deductions to
4 each employee and to the department in accordance with regulations adopted by the
5 department.

6 (e) The Department of Revenue may, to the extent practicable, coordinate
7 collection and reporting of the tax imposed in this chapter with the collection and
8 reporting of employment security contributions by the Department of Labor and
9 Workforce Development, including permitting the Department of Labor and
10 Workforce Development to collect the tax payments and remit them to the Department
11 of Revenue.

12 (f) The department may by regulation provide for an incentive to an employer
13 or a self-employed individual for electronically filing returns and making payments or
14 for other use of technology or filing methodologies to improve the efficiency of tax
15 administration. Regulations adopted under this subsection must

16 (1) establish the duration, level, nature, and value of the incentive; the
17 value of an incentive established under this subsection may not exceed \$300 for each
18 return, application, filing, or payment; and

19 (2) require that the incentive be available only if the return,
20 application, filing, or payment is filed timely with the department under this chapter.

21 **Sec. 43.45.026. Employer security.** (a) If the department determines that an
22 employer has been delinquent in remitting the tax imposed under AS 43.45.011 in
23 accordance with regulations adopted by the department, the department may require
24 the employer to deposit and keep on deposit with the department a sum equal to the
25 tax required to be withheld by the employer during the 12 months immediately
26 preceding the determination of delinquency under this subsection by the department.
27 If the employer was not required to withhold tax during the full 12 months
28 immediately preceding the determination of delinquency, the department may require
29 a deposit equal to the employer's estimated liability for a 12-month period based on
30 the actual liability for the period during which the employer was required to withhold
31 tax.

(b) The department may accept a bond or other security equal in value to the deposit required under (a) of this section in lieu of the deposit required under (a) of this section.

(c) The provision of a deposit, bond, or other security under this section does not relieve the employer from any other obligation under this title.

(d) The department may apply all or part of the deposit, bond, or other security to payment of the tax imposed under AS 43.45.011, and to any interest and penalties imposed under AS 43.45.021.

(e) The deposit, bond, or other security provided under this section is exempt from process, attachment, garnishment, or execution unless otherwise provided by law.

(f) The department shall return the deposit, bond, or other security to the employer if the employer is timely in filing and remitting the tax under AS 43.45.021 for a period of 24 consecutive months.

(g) If an employer ceases to be subject to AS 43.45.021, the department shall, after 12 months have elapsed and all liabilities of the employer to the department under this chapter have been satisfied, refund to the employer any remaining deposit, and cancel any bond or other security accepted by the department under this section.

Sec. 43.45.031. Payment of tax by self-employed individual. A self-employed individual shall remit to the department 10 percent of the individual's net earnings from self-employment in accordance with regulations adopted by the department until the entire tax has been paid.

Sec. 43.45.041. Refund of overpayments. (a) If an individual pays to the department, directly or through withholding, an amount exceeding the total tax imposed under this chapter during a calendar year and the individual applies for a refund in accordance with regulations adopted by the department, the department shall refund the overpayment to the individual.

(b) Interest on an overpayment may not be allowed under AS 43.05.280 if the department refunds the overpayment within 90 days after the date the individual correctly files the refund claim.

(c) The Department of Revenue may adopt regulations to coordinate refunds

1 of overpayments under this section with refunds of employment security contributions
2 under AS 23.20.165.

3 (d) An individual may apply for a refund under this section only during the
4 calendar year immediately following the calendar year in which the excess was paid.

5 **Sec. 43.45.051. Report of payments to self-employed individuals.** A person
6 required to report a payment to a self-employed individual to the federal government
7 under 26 U.S.C. shall also report that payment to the department in accordance with
8 regulations adopted by the department.

9 **Sec. 43.45.061. Disposition of tax proceeds.** (a) The tax collected by the
10 department under AS 43.45.021 shall be deposited into the general fund and accounted
11 for separately.

12 (b) The legislature may appropriate the estimated amounts to be collected and
13 separately accounted for under (a) of this section for education.

14 (c) The deposit required and appropriation authorized by this section are not
15 intended to create a dedication in violation of art. IX, sec. 7, Constitution of the State
16 of Alaska.

17 **Sec. 43.45.099. Definitions.** In this chapter,

18 (1) "employee" has the meaning given in 26 U.S.C. 3401;

19 (2) "employer" has the meaning given in 26 U.S.C. 3401;

20 (3) "net earnings from self-employment" has the meaning given in 26
21 U.S.C. 1402;

22 (4) "wages" has the meaning given in 26 U.S.C. 3401.

23 * **Sec. 3.** The uncoded law of the State of Alaska is amended by adding a new section to
24 read:

25 **REGULATIONS.** Notwithstanding sec. 5 of this Act, the Department of Revenue
26 may proceed to adopt regulations to implement sec. 2 of this Act. The regulations take effect
27 under AS 44.62 (Administrative Procedure Act), but not before the effective date of sec. 2 of
28 this Act.

29 * **Sec. 4.** Section 3 of this Act takes effect immediately under AS 01.10.070(c).

30 * **Sec. 5.** Except as provided in sec. 4 of this Act, this Act takes effect January 1, 2005.

Subject: HB 236 Version V

Date: Tue, 16 Mar 2004 16:07:45 -0900

From: "Don Rulien" <drulien@rulienwhitlock.com>

To: <representative_mike_hawker@legis.state.ak.us>

Representative Mike Hawker,

I have read through Version V of HB 236 "Education Tax", the newest version has dealt with many of my concerns regarding who will be taxed. By incorporating the definition of self employment earnings and the W-2 wage earner under this bill, you have successfully taxed all qualified individuals. I hope that the Department of Revenue can mimic the Employment Security Tax regulations regarding the collection and payment of this tax. Small businesses in Alaska would be able to make a simple transition for the collection and payment of this tax, as it would be similar to the current collection of Employment Security Tax.

Thank you,

Don Rulien

Don Rulien

Rulien, Whitlock & Associates, LLC

1407 W. 31st Avenue, Suite 500

Anchorage, AK 99503

email drulien@rulienwhitlock.com

Tel. 907-272-1421

Fax 907-272-8556

LEGAL SERVICES

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LEGISLATIVE AFFAIRS AGENCY
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Mail Stop 3101

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

April 14, 2003

SUBJECT: Employment Tax
(CSHB 236(), Work Draft Version 23-LS0921\H)

TO: Representative Peggy Wilson
Attn: David Jacobs

FROM: Kathryn L. Kurtz 
Legislative Counsel

You have requested a sectional summary of the above-described bill.

As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents. If you would like an interpretation of the bill as it may apply to a particular set of circumstances, please advise.

Section 1. Creates a new chapter in title 43 imposing a tax on employment.

Sec. 43.45.011 imposes a tax of \$100 per year on each individual 19 years or older and employed in the state who receives compensation greater than \$1,000.

Sec. 43.45.021 requires employers to withhold the tax from an employee's pay. Requires the employer to file returns and send the tax money to the department of revenue. Prohibits the withholding of tax from an employee who has already had the tax withheld by another employer, or who is not 19 years of age or older for the entire tax year. Requires individuals subject to the tax who have not had the tax withheld by an employer to file a return.

Sec. 43.45.031 makes employers liable for the tax, unless the employer can demonstrate that the employer relied on proof provided by the employee that the tax had already been withheld, or that the employee was not of an age to be subject to the tax.

Sec. 43.45.041 permits employees who have paid more than \$100 in taxes in a tax year to claim a refund from the department.

Sec. 43.45.051 requires the money collected from the tax to be deposited in the general fund and accounted for separately. Permits the legislature to appropriate the proceeds for education.

Sec. 43.45.099 defines "tax year" as July 1 - June 30.

Section 2. Transitional provision requiring that the initial tax be remitted and a return filed before the 15th day of the fourth month that the tax is in effect.

Representative Peggy Wilson
April 14, 2003
Page 2

Section 3. Provides an effective date of July 1, 2003.

KLK:med
03-394.med

23-LS0921\H

Kurtz

4/14/03

CS FOR HOUSE BILL NO. 236()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:

Referred:

Sponsor(s): REPRESENTATIVE WILSON

A BILL

FOR AN ACT ENTITLED

1 "An Act imposing a tax on employment; and providing for an effective date."

2 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

3 * Section 1. AS 43 is amended by adding a new chapter to read:

4 Chapter 45. Education Tax.

5 Sec. 43.45.011. Tax imposed. There is imposed a tax of \$100 a year on each
6 individual 19 years of age or older who, during the entire tax year, receives
7 compensation greater than \$1,000 in the state.8 (b) For purposes of this section, "compensation" includes wages, salaries,
9 commissions, tips, any other form of remuneration paid for personal services, and
10 gross receipts from a trade or business.11 (c) The tax imposed under this section does not apply to compensation exempt
12 from the tax under federal law.13 Sec. 43.45.021. Collection and payment of tax. (a) An employer shall
14 deduct and withhold \$50 of the tax or 10 percent of the employee's gross
15 compensation, whichever is less, on the first regular payroll in which the employee's

total compensation paid by the employer during the tax year exceeds \$1,000, and from subsequent payrolls until the tax due under this chapter is fully withheld.

(b) An employer shall file a return on a form prescribed by the department and remit the tax withheld to the department on or before the 15th day of the month following the earlier of the last day of

(1) each calendar quarter during which tax was required to be withheld; or

(2) any month in which, on the last day of that month, the employer has withheld but not paid \$500 or more of tax.

(c) A deduction of the tax may not be made in the salary or other compensation of an individual who provides proof to the employer that

(1) the tax imposed under AS 43.45.011 for that tax year has already been withheld by another employer; or

(2) the individual was not 19 years of age or older for the entire tax year.

(d) An individual who has not had the full tax withheld by an employer must file a return on a form prescribed by the department and remit the tax due under this section by June 30 of the tax year.

Sec. 43.45.031. Liability of employer. An employer who pays compensation is liable for the tax required to be withheld from an employee under this section unless the employer can demonstrate that the employer relied on proof provided by the employee that

(1) the tax imposed under AS 43.45.011 had already been withheld by another employer; or

(2) the individual was not 19 years of age or older for the entire tax year.

Sec. 43.45.041. Refund claims. (a) An individual who has paid more than \$100 in tax under this chapter in a tax year, directly or through employer withholding, or both, may claim a refund from the department. The claim must be made on a form prescribed by the department before December 31 of the calendar year immediately following the tax year in which the overpayment was made.

1 (b) Interest on the overpayment may not be allowed under AS 43.05.280 if the
2 department pays the refund within 90 days after the date the individual files the refund
3 claim or the date on which the last payment of the tax by or on behalf of the individual
4 was received by the department, whichever is later.

5 **Sec. 43.45.051. Disposition of tax proceeds.** (a) The tax collected by the
6 department under AS 43.45.021 shall be deposited into the general fund and accounted
7 for separately.

8 (b) The legislature may appropriate the estimated amounts to be collected and
9 separately accounted for under (a) of this section for education.

10 (c) The deposit required and appropriation authorized by this section are not
11 intended to create a dedication in violation of art. IX, sec. 7, Constitution of the State
12 of Alaska.

13 **Sec. 43.45.099. Definition.** In this chapter, "tax year" means the period
14 beginning on July 1 and ending on June 30 of the following calendar year.

15 * **Sec. 2.** The uncoded law of the State of Alaska is amended by adding a new section to
16 read:

17 **TRANSITIONAL PROVISION.** Notwithstanding AS 43.45.021(b)(2), enacted by
18 sec. 1 of this Act, amounts withheld during the first three months that the tax is in effect shall
19 be remitted and a return shall be filed on or before the 15th day of the fourth month that the
20 tax is in effect.

21 * **Sec. 3.** This Act takes effect July 1, 2003.

Edits to convert CSHB 236 (Version H) from a fiscal year tax to a calendar year tax:

- 1) Page 1, line 15. After "payroll" and before "in which..." add "after January 31" **(this edit prevents withholding during January)**
- 2) Page 2, line 18. Delete " by June 30" and replace it with "on or before January 31 after the close of the tax year " **(this change conforms the self-employed filing deadline to the new calendar year AND extends it an additional month from the last day of the tax year to avoid problems that taxpayers may have with filing during the holidays – also, those with end-of-year withholding would have difficulty complying with a year-end filing requirement)**
- 3) Page 3, line 13 and 14. Replace "period beginning on July 1 and ending on June 30 of the following" with "calendar". **This changes the tax year to the calendar year.**
- 4) Page 3, line 21. Delete "July 1, 2003" and substitute "January 1, 2004". **This also conforms the tax year to the calendar year.**

Just a suggestion: The bill might look cleaner if instead of this minimalist approach, all references to "tax year" were removed and at least one reference to the calendar year were added.

LEGAL SERVICES

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FAX (907) 465-2029
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State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

April 7, 2003

SUBJECT: Sectional Summary of CSHB236()
(Work Order No. 23-LS0921\D)

TO: Representative Peggy Wilson
Attn: Jean Ellis

FROM: Kathryn L. Kurtz *KLK*
Legislative Counsel

You have requested a sectional summary of the above-described bill.

As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents. If you would like an interpretation of the bill as it may apply to a particular set of circumstances, please advise.

Section 1. Creates a new chapter in title 43 imposing a tax on employment.

Sec. 43.45.011 imposes a tax of \$100 per year on each individual 19 years or older and employed in the state who receives compensation greater than \$1,000.

Sec. 43.45.021 requires employers to withhold the tax from an employee's first two paychecks after total compensation paid to that employee during the tax year exceeds \$1,000. Requires the employer to file returns and send the tax money to the department of revenue monthly. Prohibits the withholding of tax from an employee who has already had the tax withheld by another employer, or who is not 19 years of age or older for the entire tax year. Requires individuals subject to the tax who have not had the tax withheld by an employer to file a return.

Sec. 43.45.031 makes employers liable for the tax, unless the employer can demonstrate that the employer relied on proof provided by the employee that the tax had already been withheld, or that the employee was not of an age to be subject to the tax.

Sec. 43.45.041 requires the money collected from the tax to be deposited in the general fund and accounted for separately. Permits the legislature to appropriate the proceeds for education.

Sec. 43.45.051 defines "tax year" as July 1 - June 30.

Section 2. Provides an effective date of July 1, 2003.

KLK:lmb
03-142.lmb

JAN 21 2004

23-LS0921\D

Kurtz

4/7/03

CS FOR HOUSE BILL NO. 236()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:

Referred:

Sponsor(s): REPRESENTATIVE WILSON

A BILL

FOR AN ACT ENTITLED

1 "An Act imposing a tax on employment; and providing for an effective date."

2 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

3 * Section 1. AS 43 is amended by adding a new chapter to read:

4 Chapter 45. Education Tax.

5 Sec. 43.45.011. Tax imposed. There is imposed a tax of \$100 a year on each
6 individual 19 years of age or older who, during the entire tax year, receives
7 compensation greater than \$1,000 in the state.

8 (b) For purposes of this section, "compensation" includes wages, salaries,
9 commissions, tips, and any other form of remuneration paid for personal services.

10 (c) The tax imposed under this section does not apply to compensation exempt
11 from the tax under federal law.

12 Sec. 43.45.021. Collection of tax. (a) An employer shall deduct and
13 withhold \$50 of the tax from the employee's salary or other compensation on each of
14 the first two regular payrolls after the employee's total compensation paid by the
15 employer during the tax year has exceeded \$1,000. An employer shall file a return on

1 a form prescribed by the department and send the tax withheld to the department on or
2 before the fifteenth day of the month following the month in which the tax was
3 withheld from the employee.

4 (b) A deduction of the tax may not be made in the salary or other
5 compensation of an individual who provides proof to the employer that

6 (1) the tax imposed under AS 43.45.011 for that tax year has already
7 been withheld by another employer; or

8 (2) the individual was not 19 years of age or older for the entire tax
9 year.

10 (c) An individual who has not had the full tax withheld by an employer must
11 file a return on a form prescribed by the department and remit the tax due under this
12 section by June 30 of the tax year.

13 **Sec. 43.45.031. Liability of employer.** An employer who pays compensation
14 is liable for the tax required to be withheld from an employee under this section unless
15 the employer can demonstrate that the employer relied on proof provided by the
16 employee that

17 (1) the tax imposed under AS 43.45.011 had already been withheld by
18 another employer; or

19 (2) the individual was not 19 years of age or older for the entire tax
20 year.

21 **Sec. 43.45.041. Disposition of tax proceeds.** (a) The tax collected by the
22 department under AS 43.45.021 shall be deposited into the general fund and accounted
23 for separately.

24 (b) The legislature may appropriate the estimated amounts to be collected and
25 separately accounted for under (a) of this section for education.

26 (c) The deposit required and appropriation authorized by this section are not
27 intended to create a dedication in violation of art. IX, sec. 7, Constitution of the State
28 of Alaska.

29 **Sec. 43.45.051. Definition.** In this chapter, "tax year" means the period
30 beginning on July 1 and ending on June 30 of the following calendar year.

31 * **Sec. 2.** This Act takes effect July 1, 2003.