

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672
1512 SCOMM 55: JNT. SPEC. COMM. ON STATE TAX POLICY, 1986-1987, 312

A. The Assessment Level Of Review

The Audit Division is responsible for reviewing tax returns and monitoring taxpayers through audits to insure that taxable income is properly calculated and reported. If the Division determines that an adjustment is required, it will inform the taxpayer that either more taxes are owed or a refund is warranted. If more taxes are due, an assessment notice will be issued.

As a practical matter, assessments are often made as the three year statute of limitations is about to expire. These assessments are often high as compared to the final adjusted assessment made during the appeal period. The reason is that auditors must make an aggressive although reasonable evaluation in order to insure that the State receives the money it is entitled to. They cannot later amend the assessment after the statute of limitations for assessments has expired except under limited circumstances. The taxpayer has the right to appeal an assessment within 60 days of being notified of an assessment.

1. Reasons For Delay

There are two primary reasons for delay during the assessment period. Assessments often are made as the three year statute of limitations is about to expire because audits of taxpayers, especially large multi-state and multi-national taxpayers, can take years to complete. Other audits underway may deal with the same issue or taxpayer. It is not an administratively sound practice to litigate the same issue for each taxpayer for each tax year. Accordingly, a delay may occur to allow a "lead" audit to proceed to completion.

2. Prepayment after Assessment

As a practical matter, if prepayment were required after the assessment, taxpayers might not be as cooperative in providing the information during the three year audit period, or in waiving the statute of limitations. This lack of cooperation would require the department to employ more discovery devices (subpoenas, summons, interrogatories, depositions, etc.), which would be costly in both time and money.

B. Informal Conference

The informal conference is the first level of review of a challenged assessment. A conference officer discusses the assessment with the taxpayer through correspondence, in-person, or through telephone conferences. Unlike the formal hearing in which the Appeals Section does take an adversary role on behalf of the Audit Division, the purpose of the informal conference is to provide an opportunity for discussion. As a result of this nonadversarial approach, the expertise

of the Appeals Section, and its ability to settle cases, nearly 90% of all assessment disputes are resolved at the informal conference level of review.

1. Reasons For Delay

There are a number of reasons for delay at the informal conference level. Many of these reasons are identical to those experienced at the assessment level. The time frame for holding an informal conference may vary, depending on the complexity of the issues, stays and consolidations of appeal, the availability of the pertinent officials of the taxpayer, the number of informal conference officers, etc.. A great deal of the assessment actions have been stayed until resolution of certain basic issues. Staying appeal cases allows the Department to screen similar cases and proceed with the "best" test case.

2. Prepayment after Informal Conference

If prepayment of disputed taxes is required after the informal conference decision, the nature of the informal conference will become adversarial. Part of the reason for this change in atmosphere is that attorneys will be forced to enter the tax appeal process at an earlier stage of review.

C. Formal Hearing

The formal hearing is the administrative trial level for tax disputes. A Department of Revenue hearing examiner is appointed by the Commissioner to serve as a hearing officer for the appeal. A formal hearing is often preceded by a prehearing conference, briefing, and discovery requests. Full due process safeguards are provided with adequate notice and full opportunity to be heard by an impartial hearing officer. A formal hearing decision is issued after the record is closed and reviewed.

1. Delays In The Formal Hearing Process

Delays have occurred in the formal hearing process for some of the same reasons previously mentioned. In addition, the nature of the hearing process in affording both the taxpayer and the Audit Division the full opportunity to explain their respective cases causes delays. Additionally, since the Hearing Examiner Section handles not only tax appeals but other revenue appeals, staff limitations and backlogs of cases contribute to delays. Delays have also resulted because of stays pending resolution of a number of tax cases before the courts, both at the federal and state levels.

2. Prepayment of Disputed Taxes After Formal Hearing

Payment after formal hearing occurs, of course, if the taxpayer does not appeal to the Superior Court. Prepayment as a condition or prerequisite for judicial action may require the creation of a different form of action. In other words, instead of an appeal, a taxpayer would file an original action claiming a refund. The Superior Court would not be limited to review of the formal administrative record, but would, in effect, try the case *de novo*. The Department's concerns about such a procedure are two-fold: one, delays of substantial periods would be encountered; and, two, the Court's decisions on tax issues would not be based upon the administrative record, but upon new findings of fact and conclusions of law. In effect, contested cases will have two trials with potentially differing results, creating confusion in the interpretation of Alaska's tax law.

D. Other State's Assessment And Appeal Processes

We are unaware of any state that requires prepayment of disputed income taxes during the administrative appeal process, although some require payment at later levels of judicial review. State Tax Review Agencies: Organization and Practices, Federation of Tax Administrators Research Report No. 79 (December 1978). The prepayment requirement for disputed taxes is often limited to certain types of taxes that would therefore effect a limited group of taxpayers. See In the Matter of the Tax Appeal of Simpson Mannor, Inc., 548 P.2d 246 (Haw. 1976) (excise taxpayers required to pay before proceeding to Tax Appeals Court, although net income, real property, public service company and bank franchise taxpayers could appeal without prepayment of disputed taxes).

II. Alternative means to Expedite Collections Of Disputed Taxes

There are a number of alternatives to prepayment of disputed taxes, many of which we have implemented to expedite the collection process for appealed taxes.

At the audit level, assessments are progressing at a more rapid rate. The major reason for this change is that through experience, advanced marketing data, familiarity with the various taxpayers' businesses, and clarification of legal issues and positions, audits are shorter in duration and more thorough. Also, resolution of certain issues has resulted in fewer contested issues.

At the informal conference level, a major breakthrough in the dam of backlogged cases was the judicial resolution of the constitutionality of the separate accounting methodology under AS 43.21 et. seq.. ARCO v. State of Alaska, Department of Revenue, Alaska Supreme Ct. Op. No. 2965 (August 16, 1985, appeal dismissed by the U.S. Supreme Ct on January 13, 1986. Now, other issues that were stayed pending the resolution of the constitutional issues are progressing through informal conferences.

Another major change is the transfer of the informal conference functions to the Appeals Section of the Audit Division. The Appeals Section has five conference staff members who are attorneys, CPAs, or audit staff with extensive years of experience in tax matters.

At the formal hearing level, the Alaska Supreme Court's resolution of various tax issues has greatly impacted the number of cases or issues stayed at the formal hearing level of appeal. The reduction in the backlog of cases and additional staff should enable the Hearing Examiner Section to be able to issue a decision within six months of closure of a hearing by the end of 1986.

Another major change affecting the collection of disputed tax monies was the increase in the tax interest rate. AS 43.05.225 was amended in 1982 by raising the interest rate on delinquent taxes from eight percent to twelve percent. As a result, taxpayers no longer have the disincentive to pay and then to use the disputed taxes on other investment opportunities while the appeal is pending.

III. Summation

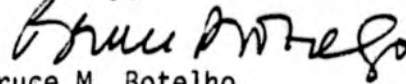
We have strong concerns that the requirement to prepay disputed taxes at some level in the review process will not expedite the resolution of disputed tax cases. Rather, we think it could impair the strategy and ability of the Department to defend its assessments and may create an adversary relationship that could permeate the assessment and appeal process, end the practice of voluntary compliance, hamper the ability of the Department to obtain needed information, diminish the Department's success rate in defending its assessments and decisions, delay the resolution process, and require additional staff at every level of the assessment and appeal process.

We believe that expedition of collecting disputed taxes is better accomplished through other approaches, many of which are currently being implemented. Greater experience and knowledge at the audit level in administering the new tax programs, a more proficient appeals staff, negotiated settlements of cases at the informal conference level,

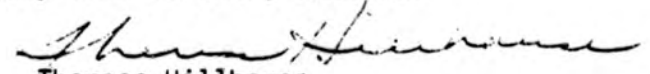
The Honorable Al Adams
January 30, 1986
Page 6

reduction of the backlog of appeals at the formal hearing level, and recent Alaska Supreme Court cases have and will greatly expedite the resolution of disputed tax cases. An increase in the interest rate has already spurred early payment of disputed taxes. These changes should insure earlier payment of taxes owed the State.

Sincerely,



Bruce M. Botelho
Deputy Commissioner, Taxation



Theresa Hillhouse
Revenue Chief Hearing
Examiner

cc: Members of the House Finance Committee

Karen L. Loeffler
Shelly J. Higgins
Oil and Gas Section
Department of Law

BB:TH:mkw
86-14



ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES
RESEARCH AGENCY

Pouch Y. State Capitol
Juneau, Alaska 99811
(907) 465-3991

June 23, 1986

MEMORANDUM

TO: Representative Terry Martin

FROM: Brad Pierce *BP*
Legislative Analyst

RE: Changes to the Operating Budget FY 79 - FY 87
Research Request 86-214

You requested this agency to provide a brief history of changes to the State operating budget since 1979. Specifically you wished to know when loans and debt service were removed from the operating budget. You asked that we provide figures on the "true increase" in the operating budget (which you defined to include loans and debt service) since 1979.

To answer your request, we contacted Richard Fineberg of the Office of Management and Budget (OMB) who recently completed a review of State budget appropriations since 1979. He provided most of the information used in this memorandum. As I am sure you are aware, tracking State appropriations through the maze of reappropriation bills and changing State accounting conventions is a formidable task and it has taken Mr. Fineberg several years to reconcile the numbers. Attached is a table of his State appropriation totals for FY 79 - FY 87 (which include capital appropriations and extraordinary items in addition to the operating appropriations you requested). Also attached is an OMB memorandum explaining what is included in the table.

History of the State Operating Budget

The following table shows that operating appropriations (including debt service and loans) peaked in FY 86 at \$3.026 billion or an increase of 147.1 percent over FY 79. Estimated operating appropriations for FY 87 total \$2.935 billion, or 139.6 percent greater than FY 79 (nominal dollars). Operating budget appropriations (including debt service and all State loans) declined in two years of the FY 79 - FY 87 period: 3.8 percent in FY 84 and 3.1 percent in FY 87.

Much of the difficulty with categorizing State appropriations stems from the fact that there is no definition of the operating budget in the statutes. Alaska Statute 37.07.120, effective January 1, 1984 explicitly defined "capital projects" and "capital improvements" (Attachment B).

Representative Martin
June 23, 1986
Page 2

Operating Budget Appropriations FY 79-FY 87
(in millions)

	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987*</u>
Operating Funds	1,149.0	1,309.0	1,757.8	2,183.0	2,437.7	2,437.4	2,685.7	2,776.9	2,702.0
Debt Service	61.7	77.1	100.0	104.2	145.6	180.6	175.1	168.9	165.2
Loans	<u>14.0</u>	<u>33.5</u>	<u>560.8</u>	<u>472.8</u>	<u>338.0</u>	<u>192.3</u>	<u>140.4</u>	<u>80.4</u>	<u>67.5</u>
Total	1,224.7	1,419.6	2,418.6	2,760.0	2,921.3	2,810.3	3,001.2	3,026.2	2,934.7
Percent Increase		15.9	70.4	41.1	5.8	(3.8)	6.8	0.8	(3.1)

* Estimated.

Source: Richard Fineberg, Senior Analyst--Office of Management and Budget, June 20, 1986.

Prepared by the House Research Agency, June 1986.

Representative Terry Martin
June 23, 1986
Page 3

Since then, the convention has been to list anything that is not a capital project or improvement as an operating budget item or as a separate category. As you pointed out in your request, this makes it very confusing to attempt to track changes in operating expenditures over time.

The debt service portion of the operating budget can be broken into two separate categories: general obligation bond debt and local school debt. Even though general obligation (G.O.) debt service is used to pay for capital projects, it has conventionally been considered part of the operating budget. During FY 79 - FY 81, it was included in the main section of the general appropriations bill by program category. During FY 82 and FY 83, G.O. debt was funded by a statutory continuing debt service appropriation (AS 37.15.012; Attachment C). From FY 84 to the present, it has been included in the front section of the appropriations bill as a separate category, first as an unstated amount in FY 84 and FY 85 then as a stated amount for FY 86 and FY 87.

Local school debt has also been inconsistently recorded and compiled over the years in question. From FY 79 to FY 83 it was included in the Department of Education operating budget. In FY 84, school debt was listed separately in the front section of the general appropriations bill. In FY 85, school debt was removed from the operating budget to avoid the State constitutional appropriations limit passed by voters in 1982 (Article IX Section 16; Attachment D). Thus for the three most recent fiscal years (FY 85 - FY 87), school and G.O. debt have been lumped together and treated as a separate category from operating appropriations in the general appropriations bill.

There is no clear pattern for State loan program funding between FY 79 and FY 87. During this period, most State loan programs were funded in the capital budget, with the notable exception of the student loan program which has usually been funded in the general appropriations bill. Occasionally, there have been special appropriations bills to fund individual loan programs. The extraordinary growth in the loans portion of the operating budget during FY 81 - FY 83 portrayed in the table above, reflects several appropriations for energy development as well as special appropriations to set up new loan programs (e.g. fisheries enhancement loans) during that period. In FY 86 and FY 87, substantial transfers (about \$114 million each year) were made from some loan programs as direct State involvement was scaled back. For example, the Department of Community and Regional Affairs--Housing Assistance Loan Fund (HALF) was transferred to Alaska Housing Finance Corporation (AHFC) which then issued bonds for the purchase and returned the cash from the bond sale to the General Fund. For FY 87, student loans were placed in the capital budget during the final hours of the 1986 legislative session because the operating budget had already been passed by the time the House and Senate Conference Committee decided on the appropriate level of funding.

Representative Martin
June 23, 1986
Page 4

We hope this information is sufficient for your purposes. If you would like greater detail on operating and/or capital appropriations, I would suggest that you call Richard Fineberg at 465-3568 as he is the expert on such matters. Please let us know if we can supply any further information.

BP

Attachments

ATTACHMENT A
STATE APPROPRIATION TOTALS

STATE APPROPRIATION TOTALS
(\$ millions)

	FY 79	FY 80	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87*
Operating Agencies (Auth.)/1									
Unrestricted General Funds	\$ 851.7	\$ 959.6	\$1,364.3	\$1,706.2	\$1,897.8	\$1,958.0	\$2,110.5	\$2,115.0	\$2,015.4
Other Funds	297.3	349.4	393.5	476.8	539.9	479.4	575.2	672.0	686.6
Total Operating Funds	1,149.0	1,309.0	1,757.8	2,183.0	2,437.7	2,437.4	2,685.7	2,787.9	2,702.0
Debt Service /2									
Unrestr. Gen. Fund (G.O. Bond)	59.8	75.2	97.4	102.4	143.6	178.6	169.5	163.3	155.0
Other Funds (Int. Airport R.F.)	1.9	1.9	2.6	1.8	2.0	2.0	5.6	5.6	10.2
Total Debt Service	61.7	77.1	100.0	104.2	145.6	180.6	175.1	168.9	165.2
Capital (Auth.)/3									
Unrestricted General Funds	171.0	92.0	565.2	1,164.9	470.1	778.4	1,241.9	471.4	325.0
Other Funds	338.4	81.7	414.6	72.4	239.7	398.5	192.1	431.7	406.2
Total Capital Funds	509.4	173.7	979.8	1,237.3	709.8	1,176.9	1,434.0	903.1	731.2
Loans Programs (Auth.)/4									
Unrestricted General Funds	14.0	33.5	560.1	471.8	337.0	171.9	140.0	80.4	61.0
Other Funds	0.0	0.0	0.7	1.0	1.0	20.4	0.4	0.0	6.5
Total Loan Funds	14.0	33.5	560.8	472.8	338.0	192.3	140.4	80.4	67.5
Total									
Unrestricted General Funds	1,096.5	1,160.3	2,587.0	3,445.3	2,848.5	3,086.9	3,661.9	2,830.1	2,556.4
Other Funds	637.4	433.0	811.4	552.0	782.6	900.3	773.3	1,109.3	1,109.5
Total Funds	\$1,733.9	\$1,593.3	\$3,398.4	\$3,997.3	\$3,631.1	\$3,987.2	\$4,435.2	\$3,939.4	\$3,665.9
Extraordinary Items/5									
Unrestricted General Funds	0.0	0.0	2,309.5	1,167.0	708.3	300.0	510.0	138.6	0.0
Other Funds	0.0	0.0	0.0	0.0	41.0	198.9	155.1	403.8	544.5
Total Extraordinary Items	0.0	0.0	2,309.5	1,167.0	749.3	498.9	665.1	542.4	544.5
GRAND TOTAL									
Unrestricted General Funds	1,096.5	1,160.3	4,896.5	4,612.3	3,556.8	3,386.9	4,171.9	2,968.7	2,556.4
Other Funds	637.4	433.0	811.4	552.0	823.6	1,099.2	928.9	1,513.1	1,654.0
GRAND TOTAL	\$1,733.9	\$1,593.3	\$5,707.9	\$5,164.3	\$4,380.4	\$4,486.1	\$5,100.8	\$4,481.8	\$4,210.4

/1 Agency "Adjusted Base" totals plus one-time, special and supplemental operating appropriations. This category includes Local School Debt Retirement (Education), Municipal Assistance (Revenue) and Revenue Sharing (DCRA). (FY 79 and FY 80 figures are estimated.)

/2 FY 79-84: Actual payments for G.O. debt retirement allocated to agencies. FY 85-87: Debt service authorizations.

/3 Session totals; OMB has adjusted some figures to reflect repeals and reappropriations and the definition of capital projects enacted in AS 37.07.120(4) (Ch. 34, SLA 83).

/4 See attached memorandum on loan programs.

/5 For a list of extraordinary items see attached memorandum. Where appropriations in this category differ from actual outlay, totals have been adjusted to reflect cash flows.

* Preliminary estimates.

\$3784

File

October 31, 1985
(Rev. June 18, 1986)
86B-90

465-3568

Richard Fineberg, Senior Analyst
Division of Strategic Planning
Office of Management and Budget

Extraordinary Budget
Items

In order to provide a consistent basis for comparative analysis of State budget growth, certain extraordinary items were isolated from operating, capital, debt service and loan appropriations. The extraordinary items category includes items such as:

- FY 81-86 Permanent Fund Dividend payment appropriations;
- FY 81-85 special appropriations from the General Fund to the Permanent Fund (in excess of Constitutionally dedicated resource revenues);
- Alaska Energy Center;
- State Income Tax Refunds (FY 81);
- Legal Settlements (e.g., the FY 81 payment pursuant to the Alaska Native Claims Settlement Act and the FY 83 Settlement of the Marathon Oil dispute);
- FY 81 transfer of General Fund assets to AHFC and AIDA (in excess of the cash appropriations listed in loan program totals);
- One-time entitlement appropriations to municipalities (FY 82-83);
- Establishment of the Rainy Day Fund (FY 81);
- Certain loan guarantee transfers to and from the Rainy Day Fund (see list);
- FY 85 General Fund loan to the Alaska Power Authority for the Four-Dam Pool; and
- Certain repeals of appropriations for income tax refunds, campaign and child care credits, capital projects and loan programs.

The extraordinary category does not include constitutionally dedicated deposits to the Permanent Fund.

The following appropriations comprise the "Extraordinary Items" in the October 31, 1985 tally: (Revised June 18, 1986):

	<u>Unrestricted General Funds</u>	<u>(\$ Millions) Other Funds</u>	<u>Total Funds</u>
<u>Fiscal Year 1979</u>			
<u>Fiscal Year 1980</u>			
<u>Fiscal Year 1981</u>			
Permanent Fund Special Deposit (35/80)	\$900.0		
Permanent Fund Dividend (120/80 FN[SB 122])*	128.5		
ANCSA Payment (120/80 p. 93)	292.6		
Income Tax Refunds (120/80 s25, FN[SB 394], 3/5580)	186.4		
Rainy Day Fund (171/80)	350.0		
Transfer of GF Assets to AIDA (120/80 s9)	166.0		
Transfer of GF Assets to AHFC (120/80 s3,4)	286.0		
CFAB Loan; (33/80 s3)	12.0		
" (lapsed to General Fund)	(12.0)		
	<u>\$2,309.5</u>		
* Excludes 0.8 of this appropriation used for Administration Operations.			
<u>Fiscal Year 1982</u>			
Permanent Fund Special Deposit (61/81 s1,2 am 101/82 s16)	\$800.0		
Permanent Fund Dividend (82/81, p. 106)	150.0		
Permanent Fund Dividend (92/81 s50)	12.5		
Municipal Entitlements (61/81 am 92/81, 141/82)	204.5		
	<u>\$1,167.0</u>		
<u>Fiscal Year 1983</u>			
Permanent Fund Special Deposit (GF Transfer per 61/81, 101/82)	\$400.0		
Permanent Fund Dividend (101/82 s18)	150.4		
" (6/83)		\$41.0	
Marathon Oil Settlement (34/83 s23)	36.2		
University Lands Settlement (21/83)	4.2		
Municipal Entitlements (61/81 am 92/81, 141/82)	101.2		
Fish. Prod. Revenue Loan Guarantee Fund (34/82 s4,5,8,9) (borrowed from and lapsed to Rainy Day Fund)		100.0 (100.0)	
AIDA Enterprise Fund (114/82 s9)	16.3		
	<u>\$708.3</u>	<u>\$41.0</u>	

June 19, 1986

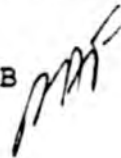
	<u>Unrestricted General Funds</u>	<u>(\$ Millions) Other Funds</u>	<u>Total Funds</u>
<u>Fiscal Year 1984</u>			
Permanent Fund Special Deposit (GF Transfer per 61/81, 101/82)	\$300.0		
Permanent Fund Dividend (107/83 s32)		\$179.0	
Permanent Fund Dividend (122/84 s15)		8.0	
Permanent Fund Dividend (44/84 s1,2)		11.9	
	<u>\$300.0</u>	<u>\$198.9</u>	
<u>Fiscal Year 1985</u>			
Permanent Fund Special Deposit (GF Transfer per 61/81, 101/82)	\$300.0		
Permanent Fund Dividend (122/84 s14)		\$155.1	
GF Loan to APA: 4-Dam Pool (171/84 s313)	210.0		
Forest Product Business Loan Guarantee (130/84) (borrowed from and lapsed to Rainy Day Fund)		25.0 (25.0)	
	<u>\$510.0</u>	<u>\$155.1</u>	
<u>Fiscal Year 1986</u>			
Permanent Fund Dividend (98/85 s14)		\$217.3	
Lapse to General Fund of Misc. Loan, Capital Project and other funds (See <u>1985 Appropriations Digest</u> pp. 6,19)		186.5	
TAPS Settlement to Rainy Day Account (105/85 s762)	138.6		
	<u>\$138.6</u>	<u>\$403.8</u>	
<u>Fiscal Year 1987</u>			
Permanent Fund Dividend (130/86 s13)		\$ 289.9	
Lapse to General Fund of Misc. Loan, Capital Project and other funds (See <u>1986 Appropriations Digest</u> pp. 6,19)		140.3	
Transfer to General Fund of Various Assets (See <u>1986 Appropriations Digest</u>)		114.3	
Transfer Permanent Fund Undistributed Income Account to Permanent Fund (42/86)		(1,129.6) 1,129.6	
Close Rainy Day Account; Create Budget Reserve Account (58/86; 129/86 s301, 538)		(436.0) 436.0	
		<u>\$ 544.5</u>	

MEMORANDUM

Division of Strategic Planning
Office of Management and Budget
465-3568 MS 0164

TO: Brad Pierce
House Research Agency

DATE: June 20, 1986

FROM: R.A. Fineberg, Policy Analyst, OMB 

SUBJECT: FY 79-87 Appropriation Totals

In response to your inquiry concerning historical budget data, enclosed is the update to the packet we provided Jay Livey of your agency Nov. 1, 1985.

Please note that the FY 87 data will change a bit as the 652 sections of this year's repeal and reappropriations bill are recorded officially in accounting records and the complications buried in the bill are resolved. We do not believe that any one of the categories or the net totals in the June 20 estimate will change by more than \$20.0 million; in fact, changes will probably be much smaller than that.

As for the prior-year data: As you know, we are working backwards. Since November 1985 the FY 81 data have been completed and reviewed; although we are still working on compiling FY 79 and FY 80 operating budget agency totals and expect revisions to the estimates in that category, work to date indicates that the estimates we have used from other sources are probably close enough to use for broad comparison purposes. For FY 81-87, the breakdown by agency will be available shortly, but I probably won't get back to the project to complete FY 79-80 data until completion of this year's Appropriations Digest.

ATTACHMENT B

ALASKA STATUTE 37.07.120

Effect of amendments. — The 1983 amendment rewrote the first sentence, added the present second sentence, and

revised a personal pronoun in the present third sentence

NOTES TO DECISIONS

Budgetary system established by statutes implementing Constitution.—Statutory language implementing Alaska Const., art. IX, § 13, establishes a budgetary system in which all appropri-

tions are made by legislative act. *Municipality of Anchorage v. Frohne*, Sup. Ct. Op. No. 1477 (File Nos. 8050, 3104), 568 P.2d 3 (1977).

Sec. 37.07.110. Interpretation of chapter. This chapter shall be construed as supplemental to all other state laws not in conflict with it. If a section or part of a section of this chapter is in conflict with federal requirements for a program for which federal grant-in-aid funds are available, the section or part, to the extent of the conflict, is inoperative. (§ 1 ch 188 SLA 1970)

Sec. 37.07.120. Definitions. In this chapter

(1) "agency" means a department, officer, institution, board, commission, bureau, division, or other administrative unit forming the state government and includes the Alaska Pioneers' Home and the University of Alaska, but does not include the legislature or the judiciary;

(2) "allocation" means an amount set out as a legislative guideline for expenditure by a state agency for a stated purpose within the total amount of an appropriation;

(3) "appropriation" means a maximum amount available for expenditure by a state agency for a stated purpose set out in an appropriation act;

(4) [Effective January 1, 1984] "capital projects" and "capital improvements" mean an allocation or appropriation item for an asset with an anticipated life exceeding one year and a cost exceeding \$25,000 and include land acquisition, construction, structural improvement, engineering and design for the project, and equipment and repair costs.

(5) "fiscal year" means a year beginning on July 1 of one calendar year and ending on June 30 of the following calendar year;

(6) "object of expenditure" means a line item of expenditure within an allocation or an appropriation;

(7) "office" means the Alaska office of management and budget established in the Office of the Governor by AS 44.19.141 (§ 1 ch 188 SLA 1970; am § 4 ch 26 SLA 1976; am § 2 ch 97 SLA 1976; am § 7 ch 46 SLA 1977; am §§ 14, 26 ch 63 SLA 1983)

Revisor's notes. - Reorganized in 1983 to alphabetize the defined terms.

Effect of amendments. The 1983 amendment repealed the definition of

"division" and added the "office," "capital projects, improvements."

Sec. 37.07.130. Sho
Budget Act, (§ 1 ch 18

Cha

Article

1. Custodians of State Funds
2. Accounting §§ 37.10-050
3. Investment and Deposit
4. Recovery of Money or Property

Article

Section

- 10 Disbursements
20 Vouchers to be approved by administrative officer

Sec. 37.10.010. Dis
tion shall (1) disburse
department, establish
employee of it authoriz
an examination of vouc
proper form, certified a
certified; and (3) be h
1949)

Cited in *Munson v. Territo*
16 Alas. 580 (1956)

Collateral references. state to incur indebtedness in distress due to unemployment under unusual conditions. 73 ALR 371

Power of board or officials to

Sec. 37.10.020. Voucher officer. A voucher arising from the issuance of the state shall be subject to the reference to the Department of the Auditor General (ACLA 1949)

ATTACHMENT C

ALASKA STATUTE 37.15.012

Sec. 37.15.010. Full faith and credit for general obligation bonds. The full faith, credit and resources of the state are hereby pledged to the payment of the principal of and interest and redemption premium, if any, on all general obligation bonds of the state authorized pursuant to art. IX, § 8 of the constitution. (§ 1 ch 175 SLA 1960; am. § 1 ch 104 SLA 1967)

Collateral references. — 63
Am.Jur 2d, Public Funds, § 23-32, 64
Am.Jur 2d, Public Securities and Obligations, § 1 et seq.
SLA C.J.S., States, § 250-262
Funding or refunding obligations as

subject to conditions respecting approval by voters, 97 ALR 442

Validity of bond issue in excess of amount permitted by law without authorized debt, tax or voted limit, 125 ALR 52

Sec. 37.15.012. Continuing debt service appropriation. The amounts required annually to pay the principal, interest, and redemption premium on all issued and outstanding general obligation bonds of the state are appropriated on July 1 of each year from the general fund to the state bond committee to make all required payments of principal, interest, and redemption premium. (§ 101 SLA 1981)

Opinions of attorney general. This section does not represent an unconstitutional dedication of public funds under § 7, art. IX, of the state constitution.

tion as that section of the constitution states, in implied exception to obligations November 10, 1982. On Gen.

Sec. 37.15.015. Committee shall publish notice of existing state indebtedness before election. (a) Before a general or special election in which a bond issue is offered for ratification, the state bond committee shall publish a notice of existing state bonded indebtedness at least once a week for three consecutive weeks in a newspaper of general circulation in each of the four judicial districts of the state. The first notice shall be published at least 20 days before the date of the election. A notice shall contain

- (1) the current total bonded indebtedness of the state;
- (2) the cost of the debt service on the current indebtedness.

(b) Neither the failure to publish the notice of existing state bonded indebtedness nor a defect in the publication affects the validity of the bond issue offered for ratification or of a general or special election in which a bond issue is offered for ratification. (§ 2 ch 50 SLA 1964; am. § 1 ch 8 SLA 1969)

Collateral references. Effect of inclusion in call for election or in proposal for bond issue submitted to people of unauthorized method of payment or repayment, 63 ALR 462

Bonds issued by state officer of bond payable solely out of proceeds of sale

gations of political subdivisions pledged or within constitutional or statutory provisions which impose a limit on state indebtedness or require consent of electors, 97 ALR 444

Mistake, ambiguity, or omission of statement as to indebtedness, 97 ALR 444

election or proposal for bond affecting validity of election issued pursuant thereto, 119
Effect of delay after sale of voters on power of government issue bonds, 135 ALR 768

Sec. 37.15.020. Main committee shall sell the series and at the time, state and its inhabitants

Sec. 37.15.030. Interest bonds shall bear interest not to exceed 11 percent of the rate of Average Yields for the whichever is higher. The from date of issue, until statute. (§ 1 ch 175 SLA 1970; am. § 1 ch 110 SLA 1982)

Effect of amendments. amendment substituted, preceding "percent a year" the first sentence.

The 1982 amendment language beginning "11 per

Sec. 37.15.040. Sale bonds, the state bond in such manner as if the bonds offered for bidder. If the state bonds are not satisfactory to reject all bids received am. § 1 ch 43 SLA 1969

Sec. 37.15.050. Re mine whether the bond maturities and may redemption. No bond maturity date unless mentioned on the face SLA 1967; am. § 1 ch

Collateral references. States, § 261

ATTACHMENT D
ARTICLE IX, SECTION 16

f whether dedication prohibi-
s to interest or other income
y money appropriated to
funds and other funds and ac-
November 30, 1982, Op. Att'y

S

state tax or license," within the
of this section, whether or not
assessments fit the definition
assessments." State, N.S.E.
aquaculture Ass'n v. Alex, Sup.
o. 2488 (File Nos. 5065, 5086,
P.2d 203 (1982).

all be contracted unless
or unless authorized by
fied by a majority of the
question. The State may,
n, contract debt for the
surrection, defending the
redeeming indebtedness
comes effective. [Amend-

ans for veterans" in the first

S

S

Section 15. Alaska Permanent Fund.

Cross references.

For statutory provisions concerning per-
manent fund dividends, see AS 43.23.

Opinions of Attorney General. —
Since this section specifically authorizes
dedications to the Permanent Fund of "at
least" 25 percent of certain revenues, any
additional dedication to the fund by stat-
ute or by appropriation is also permissi-
ble. November 30, 1982, Op. Att'y Gen.

If the legislature enacts any other dis-
tribution program which is consistent
with the intent of the permanent fund
dividend law (AS 43.23), any appropria-
tion to implement that program will be
exempt from the appropriation limit of
§ 16, art. IX, of the state constitution.
1983 Op. Att'y Gen. No. 01

NOTES TO DECISIONS

Quoted in Williams v. Zobel, Sup. Ct.
Op. No. 2170 (File Nos. 5400, 5421), 619
P.2d 422 (1980); Alaska Oil Co. v. Alaska,
45 Bankr. 358 (D. Alaska 1985).

Stated in Zobel v. Williams, 50
U.S.L.W. 4613 (U.S. June 14, 1982), rev'g
Sup. Ct. Op. No. 2201 (File No. 5400), 619
P.2d 448 (1980).

Section 16. Appropriation Limit. Except for appropriations for
Alaska permanent fund dividends, appropriations of revenue bond
proceeds, appropriations required to pay the principal and interest on
general obligation bonds, and appropriations of money received from a
non-State source in trust for a specific purpose, including revenues of
a public enterprise or public corporation of the State that issues
revenue bonds, appropriations from the treasury made for a fiscal year
shall not exceed \$2,500,000,000 by more than the cumulative change,
derived from federal indices as prescribed by law, in population and
inflation since July 1, 1981. Within this limit, at least one-third shall
be reserved for capital projects and loan appropriations. The legisla-
ture may exceed this limit in bills for appropriations to the Alaska
permanent fund and in bills for appropriations for capital projects,
whether of bond proceeds or otherwise, if each bill is approved by the
governor, or passed by affirmative vote of three-fourths of the
membership of the legislature over a veto or item veto, or becomes law
without signature, and is also approved by the voters as prescribed by
law. Each bill for appropriations for capital projects in excess of the
limit shall be confined to capital projects of the same type, and the
voters shall, as provided by law, be informed of the cost of operations
and maintenance of the capital projects. No other appropriation in
excess of this limit may be made except to meet a state of disaster
declared by the governor as prescribed by law. The governor shall
cause any unexpended and unappropriated balance to be invested so
as to yield competitive market rates to the treasury. [Amendment
approved November 2, 1982]

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

January 29, 1986

Honorable Al Adams
Alaska State Legislature
Pouch V
State Capital
Juneau, Alaska 99811

Re: Prepayment of disputed taxes
Our file: 166-268-86

Dear Representative Adams:

You have requested our opinion on the constitutionality of requiring payment of disputed taxes from taxpayers pending proper appeal of the assessed amounts. You have also asked our opinion on when in the dispute resolution process such payment would be appropriate and whether the collected sums must be put in escrow pending the outcome of the dispute. You have noted that you are especially interested in these questions as they concern taxes owed to the state by the oil and gas corporations under AS 43.21, AS 43.20 and AS 43.55, since, you have stated, "back taxes under these three statutes currently total about \$900 million." Thus, you are interested in whether any proposed changes in the appeal process to require payment of disputed taxes may be applied to the cases currently pending.

We conclude that a requirement that disputed taxes be paid at some point prior to final resolution of the dispute in the courts is permissible under both the Alaska and United States constitutions. We also believe that a statute requiring that taxes be paid pending appeal could be drafted so as to apply to disputes pending at the administrative level at the time of enactment and further, that the state need not escrow payments of disputed taxes but could enact valid legislation authorizing such procedures.

Finally, although we have found nothing that would bar legislation creating a prepayment requirement, we think that there are some practical and policy concerns that would have to be addressed in connection with any specific proposal to change the procedures for the collection of disputed taxes. The Department of Revenue has a number of comments as to the practical implications of any proposed legislation in this area and will be providing you with a list of their concerns.

BILL SHEFFIELD, GOVERNOR

REPLY TO:

☒ 1031 W 4th AVENUE
SUITE 200
ANCHORAGE, ALASKA 99501
PHONE: (907) 276-3550

☐ 1st NATIONAL CENTER
100 CUSHMAN ST.
SUITE 400
FAIRBANKS, ALASKA 99701
PHONE: (907) 452-1568

☐ POUCH K - STATE CAPITOL
JUNEAU, ALASKA 99811
PHONE: (907) 465-3600

BACKGROUND: EXISTING PROCEDURES AND APPLICABLE STATUTES AND
REGULATIONS

The procedures for taxpayer appeals are currently governed by AS 43.05.240 and Alaska Appellate Rules 602(c) and 204. AS 43.05.240 controls the administrative appeal process and generally provides for a two step process. 1/ In most instances the

1/ AS 43.05.240 provides as follows:

Taxpayer remedies. (a) A person aggrieved by the action of the department in fixing the amount of a tax or in imposing a penalty may apply to the department within 60 days from the date of mailing the notice [of assessment] ... giving notice of the grievance and requesting an informal conference. At the conference the person aggrieved may present arguments and evidence relevant to the amount of tax or penalty due the state. If the department determines that a correction is warranted, the department shall make the correction.

(b) A person aggrieved by the action of the department in fixing the amount of a tax or in imposing a penalty may apply to the department and request a formal hearing

(1) in place of the informal conference provided for in (a) of this section ...or;

(2) within 30 days after decision resulting from an informal conference.

(c) At the formal hearing the department may subpoena witnesses and may administer oaths and make inquiries necessary to determine the amount of the tax or penalty due the state. The person aggrieved may present arguments and evidence relevant to the amount of the tax penalty due the state. If the department determines that a correction is warranted, the department shall make the correction.

(d) Within 30 days after the formal hearing and decision by the department, a person aggrieved by the decision of the department may appeal to the superior court in the judicial district in which the person resides. If after the appeal is heard it appears that the tax was correct, the court shall confirm the tax. If incorrect, the court shall determine the amount of the tax and if the person aggrieved is entitled to recover the tax or part of it,

(footnote continued)

taxpayer who wishes to protest an assessment begins by requesting an informal conference. 2/ The purpose of the informal conference is both to resolve the dispute, if possible, and to clarify those issues left to be resolved at the formal hearing. In fact, many disputes are resolved at this level.

A taxpayer who does not agree with the informal conference decision may then request a formal hearing. However, the taxpayer first pays any part of the assessment that relates to issues resolved at the informal conference level, thus, streamlining the matters to be addressed at the formal hearing.

The formal hearing is conducted by a hearing officer and is governed by trial-type procedures under which the taxpayer and audit staff may call witnesses to testify under oath, cross-examine witnesses, and introduce documentary evidence relevant to determining the amount of tax due. 3/ AS 43.05.240; 15 AAC 05.030.

If, after the formal hearing decision, any part of the assessment is still in dispute, appeal is to the superior court. AS 43.05.240(d) provides that a taxpayer may appeal to superior court within 30 days after the formal hearing decision is issued. This statute does not expressly require the taxpayer to pay the disputed taxes before appealing to a superior court. However, Section 240(d) can reasonably be interpreted to require prepayment prior to judicial review and this interpretation is reflected in the department's regulations. 15 AAC 05.040 requires full payment of

(footnote continued)

the court shall order the repayment and the department shall immediately pay the amount due....

2/ Although the informal conference can be waived, see AS 43.05.240 (b)(1), the department discourages this practice since it often leads to delays in the formal hearing process as numerous pre-conference hearings become necessary to clarify issues and generally accomplish those matters usually accomplished by the informal conference.

3/ According to representatives of the Department of Revenue, at formal hearing taxpayers win at least a partial abatement in approximately 50% of the appeals of assessments under all tax laws.

the amount determined to be due by the final administrative decision of the department pending appeal to the court.

When an appeal is filed in court, the Appellate Rules of the Alaska Courts come into play. Appellate Rules 602(c) and 204(d) grant the appealing taxpayer the right to stay the administrative decision by filing an approved supersedeas bond for the amount of a potential judgment. 4/ Any legislation aimed at removing the superior court's power to approve the filing of a supersedeas bond in lieu of payment of the disputed taxes would have to provide for amending these Appellate Rules. This can be done, but only by a two-thirds vote of the members of each house. Alaska Const. Art. IV, sec. 15.

You should also be aware that a number of other statutory provisions would be affected by a prepayment requirement. An example is AS 43.20.270 which provides that the department may collect taxes by distraint and sale from a taxpayer who has not appealed from the assessment.

I. CONSTITUTIONALITY OF REQUIRING PAYMENT OF DISPUTED TAXES
PRIOR TO FINAL DETERMINATION OF TAX LIABILITY

The obligation to pay taxes is purely a statutory creation. The methods by which the state may assess and collect a tax, as well as taxpayer remedies, are controlled by the express wording of the taxing statutes. The state legislature has discretion to set the conditions precedent to any refund, limited only by constitutional considerations of due process. See generally 71 Am. Jur. 2d, State and Local Taxation, secs. 596,608 (1973).

The due process clause of the Alaska Constitution is set out in Article I, Section 7 and provides: "No person shall be deprived of life, liberty, or property, without due process of law..." The core of this guarantee is the right to notice and a hearing when

4/ This may be why the Department of Revenue has not generally enforced its regulation requiring payment of disputed taxes pending appeal. We know of one case in which the Department asked the superior court to require full payment of taxes in lieu of a supersedeas bond but the court approved a bond in accordance with the Appellate Rules.

state action threatens the deprivation of some material right. Matanuska Maid, Inc. v. State, 620 P.2d 182 (1980). The language of the parallel federal due process guarantee, contained in the fifth and fourteenth amendments, is identical to that contained in the Alaska Constitution.

Under the applicable federal tax procedures, a taxpayer is given the choice of appealing through administrative procedures to Tax Court or going directly to federal district court. A taxpayer may appeal to Tax Court without paying disputed taxes and on to the Court of Appeals upon paying a bond. However, full payment of all disputed taxes is a prerequisite to going directly to federal district court, since jurisdiction over tax matters in the district courts exists only for actions "for the recovery of taxes alleged to have been erroneously or illegally assessed or collected," 28 U.S.C. sec. 1346. The requirement that a taxpayer pay the disputed taxes in full as a precondition of judicial review has been challenged on due process grounds and upheld by the federal courts. Johnston v. Comm'r of Int. Rev., 429 F.2d 804 (6th Cir. 1970) (due process not violated where taxpayer was barred from administrative appeal and had to pay full disputed tax amount to challenge tax in federal court); see, Flora v. United States, 357 U.S. 63 (1958).

Thus, while a taxpayer who disputes an assessment is guaranteed some right to a notice and hearing on the disputed amount, it is unlikely that the hearing must occur prior to any attempt at collection of the taxes assessed by the taxing authority. Both federal courts and courts in other states have held that due process is satisfied by the provision for a hearing after payment of taxes on the taxpayer's liability for taxes it alleges are wrongfully collected. See e.g., Phillips v. Comm'r of Int. Rev., 283 U.S. 589 (1931); Johnston v. Commissioner of Internal Revenue, 429 F.2d 804 (6th Cir. 1970); Cohen v. U.S., 297 F.2d 760 (9th Cir. 1962); State Tax Commission v. Yavapai County, 29 P. 2d 733 (Ariz. 1934); Anderson Bros. Corp. v. Stone, 85 So. 2d 767 (Miss. 1956); see generally 72 Am Jur 2d, State and Local Taxation, sec. 786 (1973).

The Alaska Courts have not addressed the issue of prepayment of taxes. While the Alaska courts certainly look to federal precedent, they are not limited to these rulings, since the provisions of the state constitution may have broader safeguards than the federal standards. Shagloak v. State, 597 P.2d 142 (Alaska 1979). However, based on the federal precedent and other caselaw cited above, we believe that the Alaska Supreme Court would uphold,

against due process challenge, a statutory requirement that taxes be paid at some point in the appeal process as a prerequisite to further review. 5/

You have asked, however, at what point in the process we believe prepayment would be "appropriate". As a matter of policy the choice of when to require full payment is of course up to the legislature. However, as a legal matter, we believe that the likelihood of any successful challenge to a prepayment requirement would decrease in direct proportion to the number of procedural safeguards available for use by the taxpayer prior to required payment. Thus, we believe that imposition of the requirement at the conclusion of the formal hearing is the least vulnerable point. However, we have found nothing to suggest that payment could not be required after the informal conference or possibly even earlier as long as there remains notice and an opportunity for a hearing to challenge the tax at some reasonable stage of the proceedings.

II. APPLICATION OF THE PREPAYMENT REQUIREMENT TO CURRENTLY PENDING CASES

It is our opinion that a change in the taxing procedures to require a prepayment of disputed tax liabilities could legally be applied to appeals that are currently pending at the administrative level. A taxpayer might attempt to challenge the application of any prepayment requirement to existing cases on the grounds that such an application would be unconstitutionally retroactive. However, we do not believe such a challenge would succeed.

5/ We think, however, that a small taxpayer appealing corporate income tax assessments under 43.20 might challenge a prepayment requirement on due process or other grounds. An argument that a specific taxpayer cannot afford to pay the full, assessed amount before appeal and would therefore be irreparably harmed by strict application of the prepayment requirement might be receptively received by a court. In such a case, the court could decide to stay the application of the prepayment statute or reduce the amount required to be paid on due process grounds or as an exercise of its general equitable powers. It would be unlikely, however, to hold the statute unconstitutional on its face.

A retroactive 6/ statute is "one which gives to pre-enactment conduct a different legal effect from that which it would have had without the passage of the statute," Norton v. Alcoholic Beverage Control Board, 695 P. 2d 1090, 1093 (Alaska 1985) citing Hochman, The Supreme Court and the Constitutionality of Retroactive Legislation, 73 Harv. L. Rev. 692 (1960). While this definition might lead to arguments over whether applying a statutory change to require prepayment of disputed taxes to pending cases is a retroactive application, the argument would be largely irrelevant. Procedural changes that do not effect substantive rights may be retroactively applied. Matanuska Maid, Inc. v. State, 620 P.2d 182, 187 (Alaska 1980). The theory behind the constitutional prohibition against retroactivity is that a statute should not operate to deprive a person of vested rights. However, for over a century, the rule has been that no party has a vested right in any statutory remedy. See The Collector (Brainard) v. Hubbard, 79 U.S. 1 (1871) cited in Bidwell V. Scheele, 355 P.2d 584, 586 (Alaska 1960).

Thus, in the Bidwell case, the Alaska Supreme Court held that the repeal of a statute requiring a person bringing a claim of title to lands against the holder of tax title to pay the equivalent of the sale price of the lands into the court should be applied to a pending action. The purchaser had no right in the previous procedure. Similarly, a taxpayer has no right to the present tax appeal procedures that permit a full appeal prior to any requirement to pay disputed liabilities.

The intent to apply a change in the tax appeal procedures to pending cases, however, would have to be stated expressly in the statute. AS 01.10.090 provides: "No statute is retrospective unless expressly declared therein." The statute need not use the specific word, "retrospective" but the legislature must clearly express its intent. See also, AS 01.10.100 (repeal or amendment of a law does not extinguish existing rights unless act expressly so states).

III. ESCROW OF DISPUTED TAX LIABILITIES

While your opinion request asks only whether payments received under a prepayment scheme must be escrowed, further conversations suggest you are also interested in the legislature's

6/ Legislation may be referred to as either retroactive or retrospective; for our purposes the terms are synonymous.

authority to set up some sort of procedure for holding the prepaid amounts for future refund pending resolution of tax disputes. Thus, we perceive your question to be whether or not the decision to escrow these sums may legally be left to the legislature.

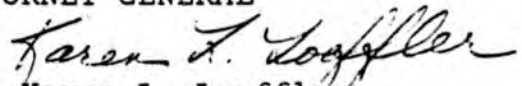
As to the first part of your question, we have found nothing that would require the state to escrow disputed tax liabilities. The federal government, for example, does not escrow the amounts it collects pending district court tax proceedings. ^{7/} Moreover, the contrary view, if applied to all tax disputes, might seriously impair a government's ability to function.

It is more difficult to respond to your inquiry concerning the validity of a mechanism for holding funds for possible repayment in the event the state does not prevail on its tax claims. There are many different methods that could be proposed for holding the disputed funds, and, while we believe that the legislature has broad discretion to choose among these methods, we think that there could be problems associated with some of them. See, e.g., 1982 Op. Att'y Gen. No. 13 (Nov. 30) (discussing dedicated funds prohibition as it applies to various types of funding mechanisms). In short, we think that a valid procedure for holding disputed funds for possible refund could be devised, however, we cannot give any more specific advice without more information.

We hope that this answers your immediate questions. We will be happy to assist you in any further questions you might have.

Sincerely yours,

HAROLD M. BROWN
ATTORNEY GENERAL

By: 
Karen L. Loeffler
Assistant Attorney General

KLL/ma

^{7/} As a practical matter, however, Alaska's situation does not resemble that of the federal government. While the latter operates from a deficit, we do not. Thus, the need to reserve disputed funds could differ.

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

BILL SHEFFIELD, GOVERNOR

P.O. BOX 5
JUNEAU, ALASKA 99811-0400
PHONE: (907) 465-2300

August 13, 1986

Handwritten: H. E. J.

The Honorable John Sund
Alaska State Legislature
2336 Sixth Avenue
Ketchikan, AK 99901

Dear Representative Sund:

At the Joint Special Committee on Tax Policy meeting in Anchorage, you requested clarification of the statement in the Department of Revenue's June 1986 Revenue Forecast that "the magnitude of the recent decline in estimated corporate tax payments was totally unexpected. Unfortunately, the correct revenue picture will not be revealed until the Department conducts audits of the companies involved."

Vince Wright, chief of our petroleum research section, advises me that this statement is correct as written--although perhaps it was not as clearly written as one might wish. Corporate taxpayers are required to make quarterly pre-payments of taxes. See, 15 AAC 21.710. That is, in the year the tax liability is incurred, they pay the State of Alaska what they estimate their tax liability will be, on a quarterly basis. If a corporation estimates that its tax bill for the spring quarter of 1986 will be \$100,000, for example, it must forward to the Department of Revenue that amount at the end of the spring quarter. These are estimated quarterly pre-payments.

As you pointed out at the meeting, the companies do not actually file their tax returns until April of the following year at the earliest. In point of fact, most of the larger taxpayers obtain an automatic extension and do not file their tax returns until September of the following year.

Thus, the Department would receive the hypothetical taxpayer's estimated quarterly pre-payment of \$100,000 in April, 1986; but would not receive the final tax return until September, 1987. At that time, the taxpayer would either request a refund of any overpayments (if the estimated quarterly pre-payments were high), or would send in additional payment (if the estimated quarterly pre-payments were low).

The problem described in the June 1986 Revenue Forecast is an unanticipated decline in the estimated quarterly tax pre-payments for the spring quarter of 1986. The final tax returns covering these estimated quarterly pre-payments will not be received for another year. However, we rely on the estimated quarterly pre-payments for a portion of our current revenue flow.

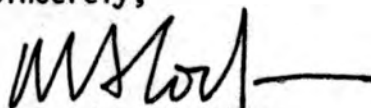
The Honorable John Sund
August 13, 1986
Page 2

It may be that the energy related businesses of many of Alaska's larger corporate taxpayers have suffered as a result of the decline in oil prices. Consequently, their estimates of their ultimate tax liability to the state may have been scaled down, and the quarterly payments reduced commensurately. Whether or not these taxpayers have accurately estimated their tax liabilities will not be known until the Department has audited their final returns.

I hope this answers your question. Enclosed for your information is a brief summary of the audit-assessment-appeal process for tax collection. Also, as requested, is a copy of Dr. Charles Logsdon's analysis of the Jones Act/oil export situation.

Please give me a call if you have any further questions or comments about this or any other matter pending before the Committee.

Sincerely,



Richard D. Monkman
Deputy Commissioner, Taxation

RDM:mkw
86-117

Enclosure

cc: Dr. Charles Logsdon
Vincent Wright
Members of the Committee (w/enclosure)

Assistant Attorney General Deborah Vogt (w/enclosure)
Royce Weller

Department of Revenue
Audit and Appeal Process
August 7, 1986

The Audit Division is responsible for reviewing tax returns and monitoring taxpayers through audits to insure that taxable income is properly calculated and reported. If the Division determines that an adjustment is required, it will inform the taxpayer that either more taxes are owed or a refund is warranted. If more taxes are due, an assessment notice will be issued.

As a practical matter, assessments are often made as the three year statute of limitations for assessments is about to expire. Assessments may be appealed. The taxpayer has the right to appeal an assessment to informal conference within 60 days of being notified of an assessment or waive informal conference and proceed to formal hearing.

There are two levels of administrative appeal within the Department, the informal conference and the formal hearing.

1. Informal Conference

The informal conference is the first level of review of a challenged assessment. A conference officer from the Appeals Section discusses the assessment with the taxpayer in-person, through telephone conference or through correspondence. Unlike the formal hearing in which the Appeals Section takes an adversary role on behalf of the Audit Division, the purpose of the informal conference is to provide an opportunity for discussion. As a result of this nonadversarial approach, the expertise of the Appeals Section, and its ability to settle cases, nerally 90% of all assessment disputes are resolved at the informal conference level of review.

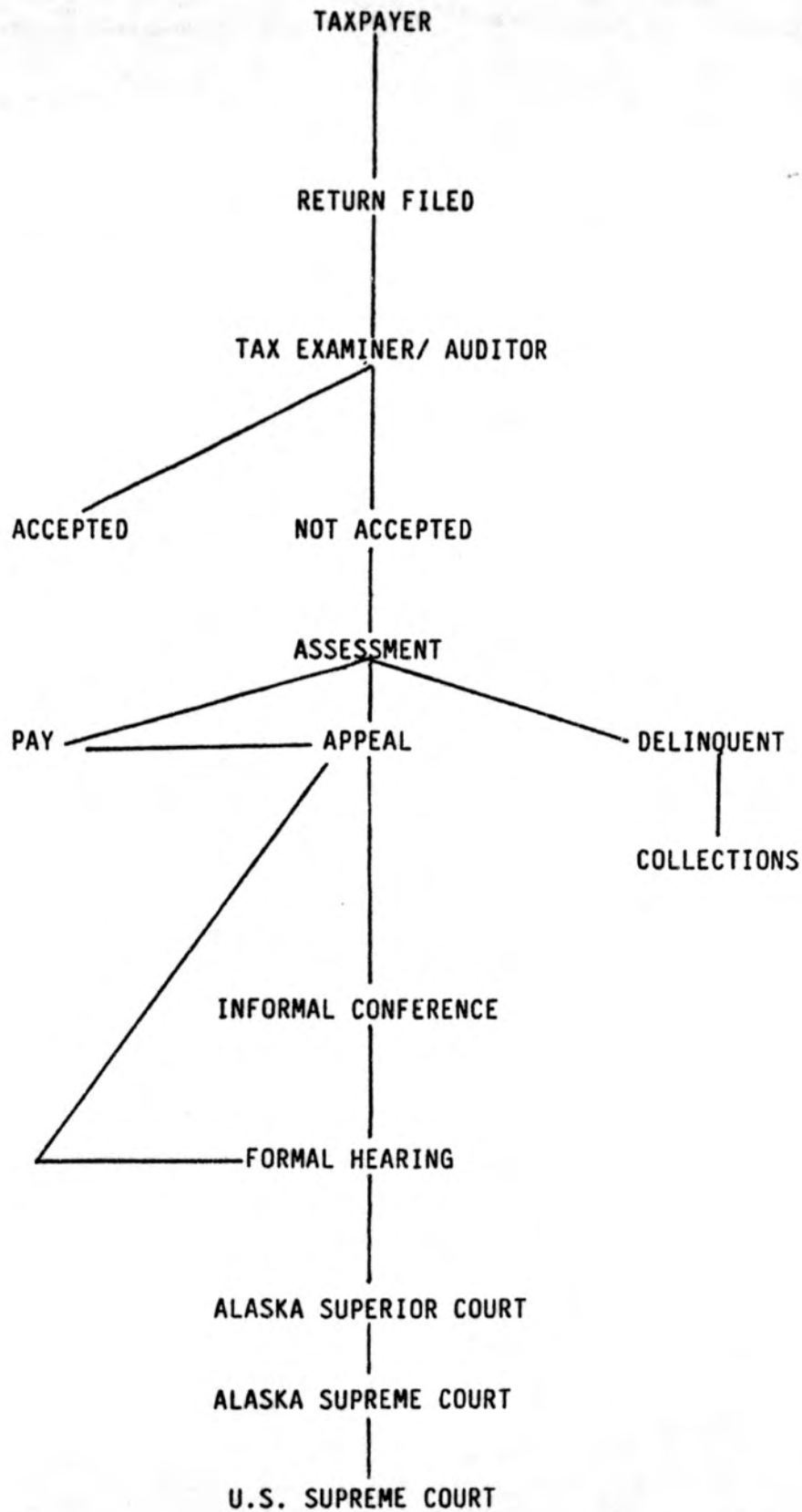
2. Formal Hearing

The formal hearing is the administrative trial level for tax disputes. A Department of Revenue hearing examiner is appointed by the Commissioner to serve as a hearing officer for the appeal. A formal hearing is often preceded by a prehearing conference, motions, briefing, and discovery requests. Full due process safeguards are provided with adequate notice and full opportunity to be heard by an impartial hearing officer. A formal hearing decision is issued after the record is closed and reviewed.

After a formal hearing decision the taxpayer may appeal to the Alaska Superior Court. In rare cases, the appeal process can proceed through Alaskan courts to the U.S. Supreme Court. Final resolution of the appeal occurs after exhaustion or waiver of judicial appeal rights. It is only then that the disputed taxes must be paid if the final determination is against the taxpayer.

DEPARTMENT OF REVENUE

APPEAL PROCESS



MEMORANDUM

State of Alaska

Department of Revenue

TO: Vincent Wright
Chief of Research

DATE: July 18, 1986

FILE NO:

TELEPHONE NO: 276-5364

SUBJECT: ANS Export

FROM: 
Charles Logsdon
Petroleum Economist

I have reviewed the March 1983 analysis that we made of the revenue potential of ANS Export to Japan. The analysis remains essentially correct as the relative transportation cost and relevant price assumptions have not materially changed. I have made a very rough best guess estimate of what ANS export would mean for oil production revenues if it were to go today. The key assumptions and estimates are as follows:

1. Alaska would sell 100,000 b/d of its royalty oil to Japan (Alaska currently has over 120,000 b/d available for export)
2. Major Alaska producers would sell an additional 200,000 b/d to Far East purchasers
3. The price received would not be substantially different than would have been received if the oil were sold at the U.S. Gulf
4. The transportation cost savings due to avoiding the Gulf haul would be \$2.50/bbl if shipped in Jones Act Tankers or \$3.40/bbl if shipped in foreign tankers
5. All cost savings would translate directly into higher wellhead prices. This means that wellhead values would be \$2.50/bbl higher if Jones Act Tankers are used and \$3.40/bbl higher if foreign tankers are used for oil shipped to Japan.

	<u>State of Alaska Gross Revenue Effect</u>	<u>Less State of Alaska Permanent Fund Effect</u>	<u>State of Alaska Net Revenue Effect to General Fund</u>
Jones Act Tankers	\$ 80 million/yr at current prod.	\$ 14.5 million/yr at current prod.	\$65.5 million/yr at current prod.
Foreign Tankers	\$110 million/yr at current prod.	\$ 19.75 million/yr at current prod.	\$90.25 million/yr at current prod.

CL:mkw

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

BILL SHEFFIELD, GOVERNOR

P.O. BOX 5
JUNEAU, ALASKA 99811-0400
PHONE: (907) 465-2300

July 24, 1986

Re: Department of Revenue
Accounts Receivable

File Policy Committee
Hunt
The Honorable Terry Martin
Alaska State Legislature
3960 Reka Dr., B-6
Anchorage, AK 99508

Dear Representative Martin:

Enclosed per your request is a copy of the Department of Revenue's latest accounts receivable list. As you will note, the total assessed and unpaid is \$1.04 billion as of July 21, 1986. The bulk of this (\$1.01 billion) has been assessed by our auditors and is now on appeal. The outstanding amounts are primarily in the oil and gas taxes and in corporate income tax assessments (AS 43.21, AS 43.55, AS 43.20).

I have instructed our hearing officers to process all taxpayer appeals as expeditiously as possible. Due process of law requires that the hearing officers give all taxpayers a fair, unbiased, and complete opportunity to be heard on objections raised to these assessments. Given the large sums involved, some hearings are necessarily complex and lengthy. Nonetheless, the Department of Revenue is working hard to resolve these cases and collect the taxes owed to the people of the State of Alaska.

Sincerely,



Richard D. Monkman
Deputy Commissioner, Taxation

RDM:mkw
86-118

Enclosure

cc: Members of the Committee
Theresa Hillhouse, Chief Hearing Officer

ALASKA DEPARTMENT OF REVENUE
TAX ACCOUNTS RECEIVABLE SUMMARY
July 21, 1986

TAX TYPE	STATUTE	VALUE OF ACCOUNTS	NOTICES OF ASSESSMENT	APPEALED	DELINQUENT AND ASSIGNED	CURRENTLY NOT COLLECTABLE
OIL & GAS CORP INC	AS 43.21	\$ 786,954,201.33	\$.00	\$ 786,954,201.33	\$.00	\$.00
OIL & GAS PRODUCTION	AS 43.55	163,313,107.90	2,390,349.13	160,921,864.21	894.56	.00
CORPORATION	AS 43.20	56,079,918.77	1,285,177.53	53,560,820.38	1,093,383.91	140,536.95
INDIVIDUAL INCOME	AS 43.20	12,937,939.83	972,441.42	3,793,773.08	7,705,312.74	466,412.59
FISHERIES	AS 43.75	10,525,556.47	327,826.72	2,406,472.69	6,467,260.51	1,323,996.55
MOTOR FUEL	AS 43.40	3,156,188.63	41,340.60	462,445.05	2,651,510.02	892.96
BUSINESS LIC GR RCPT	AS 43.70	2,779,306.42	.00	2,313,682.53	320,952.66	144,671.23
MINING	AS 43.65	1,990,328.47	7,653.26	1,978,935.78	3,739.43	.00
WITHHOLDING	AS 43.20	1,730,964.17	.00	955.84	1,533,025.91	196,982.42
OIL & GAS PROPERTY	AS 43.56	647,211.56	.00	.00	452,135.57	195,075.99
SEAFOOD MARKETING	AS 16.51	266,532.75	41,797.17	71,761.95	147,797.90	5,175.73
ALCOHOLIC BEVERAGE	AS 43.60	57,095.45	3,482.08	.00	53,613.37	.00
ESTATE	AS 43.31	38,333.30	353.00	32,360.69	5,619.61	.00
AVERAGE WHOLESALE	AS 43.80	2,950.00	.00	1,300.00	1,650.00	.00
CIGARETTE	AS 43.50	2,731.61	.00	.00	2,731.61	.00
COIN OPERATED DEVICE	AS 43.35	2,107.17	.00	.00	1,968.16	139.01
TOTAL TAX RECEIVABLE (A)		\$1,040,484,473.83	\$ 5,070,420.91	\$1,012,498,573.53	\$20,441,595.96	\$2,473,883.43
PERCENT OF TOTAL VALUE		100.00%	0.49%	97.31%	1.96%	0.24%
PERCENT OF WORKABLE VALUE					89.20%	10.80%

TAX TYPE	STATUTE	NUMBER OF ACCOUNTS	NOTICES OF ASSESSMENT	APPEALED	DELINQUENT AND ASSIGNED	CURRENTLY NOT COLLECTABLE
INDIVIDUAL	AS 43.20	1,343	58	260	859	166
CORPORATION	AS 43.20	675	95	396	147	37
GAS PRODUCTION	AS 43.55	585	93	491	1	0
WITHHOLDING	AS 43.20	418	0	2	288	128
MOTOR FUEL - HWY	AS 43.40	272	15	109	143	5
FISH, FREEZER SHIP	AS 43.75	241	8	37	140	56
BUSINESS LIC GR RCPT	AS 43.70	122	0	35	50	37
SEAFOOD MARKETING	AS 16.51	59	3	10	44	2
OIL & GAS CORP INC	AS 43.21	32	0	32	0	0
OIL & GAS PROPERTY	AS 43.56	18	0	0	17	1
MINING	AS 43.65	17	2	13	2	0
ALCOHOLIC BEVERAGE	AS 43.60	9	3	0	6	0
COIN OPERATED DEVICE	AS 43.35	6	0	0	4	2
ESTATE	AS 43.31	5	1	1	3	0
AVERAGE WHOLESALE	AS 43.80	3	0	2	1	0
CIGARETTE, GENERAL	AS 43.50	1	0	0	1	0
TOTAL TAX ACCOUNTS (B)		3,806	278	1,388	1,706	434
PERCENT OF TOTAL ACCOUNTS		100.00%	7.30%	36.47%	44.82%	11.40%
PERCENT OF WORKABLE ACCOUNTS					79.72%	20.28%

ALASKA DEPARTMENT OF REVENUE
TAX ACCOUNTS RECEIVABLE SUMMARY
July 21, 1986

NOTE: _____

- A. The value of receivables reported, especially those in appeal status, are still subject to some review and correction.

At the end of October, 1985, the Enforcement Division completed the consolidation of all receivables on to a new computer based accounts receivable system, giving the Department the ability to generate summary statistics of tax receivables. Upon review of these statistics, certain anomalies have been identified, some of which have resulted in correction of reported receivables. In a few instances keypunch errors have been identified. In a few other cases unposted payments have been identified, most notably involving those assessments under appeal.

The Enforcement and Audit Divisions are currently working to reconcile what the accounts receivable system shows in appeal status with what Audit's conference staff shows in appeal status. As that reconciliation is conducted the number of accounts and the aggregate value of those accounts may change.

- B. The number of accounts identifies the number of actual billings, not the number of taxpayers. A single taxpayer may have billings for several different tax periods and/or for several different tax types. Accordingly, the actual number of taxpayer appeal cases will be less than the number of accounts identified on this summary.

Attacking the Revenue Decline

To Tax or Not To Tax?

Alaska Department of Revenue forecasts show that total General Fund revenue for fiscal '86 is expected to be down \$400 million from fiscal 1985, and fiscal 1987 revenue is expected to be down another \$460 million.

This projected, sharp revenue decline should be addressed in this session of the Alaska Legislature, whose options include spending cuts, reinstatement of the state income tax, the levying of a state sales tax, elimination of Permanent Fund dividends and higher taxes on oil production. A state lottery has also been suggested, but in an auxiliary role because of its slight revenue raising potential.

Higher Oil-Production Taxes

The idea of raising oil production taxes should be dumped immediately. Alaska desperately needs to generate an economic base in addition to the oil industry. By turning to higher oil-production taxes, we would send a message to other extractive industries that might be considering development in Alaska.

Investments are based on calculations of expected after-tax income. Higher oil-production taxes today will strongly influence such calculations, to the detriment of the economy.

The Income Tax and Permanent Fund Dividends

At a time when falling oil prices and production threaten a prolonged recession in Alaska, a factor in favor of the income tax is its ability to transfer to Alaska more than \$5 million per year in federal money.

State income taxes are likely to continue to be deductible from federal taxable income. For every \$1 raised by the state income tax, federal income tax collections from Alaskans fall by about 15 cents.

If interest rates paid by Alaskans are



By DAVID REAUME

largely determined by national conditions, this deductibility of state income taxes virtually assures that a state tax, with subsequent government spending of the proceeds, will help to shore up the state's economy.

State government can also extract revenue from the federal government by levying a sales tax or by repealing the Permanent Fund dividend. The sales tax option is favorably considered, but repeal of the Permanent Fund dividend clearly ranks below reintroduction of the income tax for one good reason: while dividend repeal would raise substantial revenue (more than \$200 million in fiscal 1986) and would reduce Alaskans' federal income tax payments by about \$10 million, it would do so in a regressive manner.

Indeed, from the point of view of simple fairness, there is no reasonable comparison between the income tax and dividend repeal.

For a family of four with federal taxable income of \$10,000 in 1986, dividend repeal would amount to levying a tax of about 16 percent of taxable income. The same low-income family would lose only 3.4 percent of its taxable income under the old Alaska state income tax.

The break-even point comes at about \$31,000 in taxable income for a family of four (equal to about \$44,000 in federal adjusted gross income).

Families with incomes below that level lose more under dividend repeal than under the state income tax. Families (of four) above that income level fare better under dividend repeal.

For very-high income families the Permanent Fund dividend is more of an annoyance than a benefit.

A State Sales Tax

During the past 15 years consumption-type sales taxes have gained both academic respectability and public favor because of their relative simplicity of administration and their tendency to stimulate savings, but most of all because the perceived burden is less.

Surveys conducted by the Advisory Commission on Intergovernmental Relations consistently show that the public strongly prefers sales taxation to income taxation.

In addition, a state sales tax can be expected to have a net stimulative impact on the economy — both because it is deductible at the federal level and because about 7 percent to 10 percent of its yield would be raised by taxing visitors.

Commonly exempted in an attempt to reduce the comparative burden on low-income households are purchases of (1) food for home consumption, (2) drugs and medicines, (3) heating oil and coal and (4) household purchases of natural gas and electricity.

A good question is, "How high would a sales tax rate need to be if the tax base were consumption less certain exemptions?"

Using Alaska personal income figures and national patterns of consumer expenditure out of income, I have derived some preliminary estimates.

If no exemptions were allowed, a state sales tax rate of between 5 percent and 5.5 percent would have raised the same revenue in 1983 and 1984 as the old income tax.

If only food purchased for home consumption were exempt the sales tax rate needed to achieve parity with the old income tax would be between 5.5 and 6 percent.

If food for home consumption, heating oil and coal, drugs and medicines, and natural gas and electricity were exempt, a sales tax rate of between 6 and 6.5 percent would be required to match the yield of the old income tax.

In all of these calculations, I have assumed that 10 percent of potential revenue is lost to evasion and avoidance.

In addition to exempting certain goods for the benefit of low-income households, higher rates can be levied on goods and services known to be more heavily consumed by high-income households. For example, a higher tax rate can be applied to automobiles costing over a certain amount.

With all of the tax-design options available, a well-designed consumption-

Reaume is owner and president of Alaska Economics Inc., a Juneau-based consulting firm. He has been an economic consultant in Juneau for 10 years and was formerly with the national firm of Data Resources Inc.

tion-type sales tax, coupled with some expenditure reduction, may be the best option we have.

An Alaska State Lottery

A state lottery is not simply a fund raiser but also a consumption item. When a Seattle resident buys a ticket in the Washington lottery, the purchase price consists of a fee for the gaming coupon plus a gambling excise tax.

Because the lottery excise tax falls heavily on low-income players, it is not a foregone conclusion that lotteries are better than general sales taxes or income taxes, *even when yield differences are ignored.*

Even so, it is safe to say that the chief reason lotteries are not more widespread is their rather paltry per capita revenue yield.

In New Jersey and Maryland, two turnpike states that reap considerable revenue from out-of-state motorists, only \$40.87 and \$54.20 per resident was raised through lotteries in fiscal year 1983. (Figures were taken from Census Bureau tabulations.)

In Massachusetts, New York and Washington, per-resident yields were even less, totaling \$18.55, \$16.64 and \$21.33, respectively.

Were Alaska to institute a state-run lottery that yielded Maryland's high of \$54.20 per resident, the total annual yield would be only \$28.5 million, or less than 1 percent of currently projected fiscal year 1985 revenue.

In order to match the yield of the old state income tax, for example, lottery sales would have to total about \$1,450 per resident per year. On average, a lottery's net yield is equal to about 45 percent of total sales, with the remainder given over to prizes (42 percent) and overhead (13 percent).

Because of its slight revenue-raising potential, an Alaska state lottery has to be viewed as only one part of a larger package of spending cuts and revenue increases.

If, for example, a consumption-type sales tax were levied, with exemptions for food and medicine, the statutory rate of the tax could be held down partly by proceeds from a state lottery.

Realistically, an Alaska lottery can be expected to yield something in the range of \$20 to \$30 per resident, given the state's relatively high ratio of visitors-to-residents.

At \$25 per resident, lottery revenue would total about \$13 million and would allow a general sales tax to be levied at a rate of about 1/4 of 1 percentage point lower than otherwise would be the case.

Thus, a combination of solutions, ranging from a state lottery to state sales tax seem to be Alaska's best bet for generating the income it will need in the future. □

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STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

BILL SHEFFIELD, GOVERNOR

P.O. BOX 5
JUNEAU, ALASKA 99811-0400
PHONE: (907) 465-2300

September 4, 1986

The Honorable Terry Martin
Alaska State Legislature
3960 Reka Drive B6
Anchorage, AK 99508

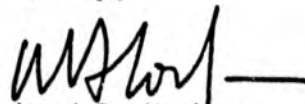
Dear Representative Martin:

In response to your inquiry at the July, 1986 Joint Special Committee on Tax Policy meeting, enclosed are some materials concerning "leakage" of Permanent Fund Dividends to the federal treasury by operation of the federal income tax.

Also enclosed is a study of tax "leakage" to the federal treasury after the repeal of the Alaska income tax in 1979. Of particular interest may be the authors' conclusion that nonresidents accounted for 21% of Alaska income tax returns in 1979 (39,120 out of 187,124 total returns), and that nonresidents paid 11% of the total tax received (\$10,069,565 out of \$92,601,302 total).

Please let me know if you have any further questions or comments.

Sincerely,



Richard D. Monkman
Deputy Commissioner, Taxation

RDM:mkw
86-131

cc: Committee Members

Enclosure

MEMORANDUM

State of Alaska

TO: Vincent D. Wright
Chief of Research
Department of Revenue

DATE: April 3, 1986

FILE NO:

TELEPHONE NO: 465-2300

FROM: Al Zangri
Economist
Research Section
Department of Revenue

SUBJECT: PFD Leakage to Federal
Income Tax

Attached are estimates of the amount of federal income tax leakage resulting from the 1985 permanent fund dividend payment. The estimates were based on a Permanent Fund Dividend amount of \$404 and a total of \$210,617,200 available for distribution. Taxable income for 1985 was estimated by adjusting 1982 data for changes in the average wage and consumer price index between 1982 and 1984. The increase in the number of taxpayers was estimated by using the increase in the number of adult PFD applicants from 1982 to 1985.

Based upon the input assumptions, Table 1 shows that the estimate of total leakage is \$17,957,037.65. This represents approximately 8.5% of the total PFD distribution. Table 2 provides estimates, for various taxable income categories, of the average leakage per income tax return (\$93.30) as well as the average leakage per taxpayer (\$65.47).

AZ:nkw

Attachment

TABLE 1

	NUMBER OF RETURNS	TAXABLE INCOME	INCOME TAX PAYABLE	TAX LEAKAGE
		TOTAL	TOTAL	TOTAL
AGI RANGE				
NO AGI	5406	0.00	0.00	0.00
\$1 TO \$10000	39264	128021179.52	7685762.78	1191645.90
\$10001 TO \$20000	33787	410779344.94	47716496.38	2404717.96
\$20001 TO \$30000	30957	645966358.06	97382247.18	2938037.84
\$30001 TO \$40000	25590	742626786.11	130975949.19	2933693.83
\$40001 TO \$50000	20191	746907727.27	148972418.40	2647211.35
\$50001 TO \$100000	34349	1830273647.64	450867571.63	5295600.03
OVER \$100000	2922	404038892.23	152044211.90	546130.71
TOTAL	192466	4908613935.77	1035644657.45	17957037.63

TABLE 2

		NUMBER OF RETURNS	TAXABLE INCOME	INCOME TAX PAYABLE	TAX LEAKAGE	TAX LEAKAGE
			AVERAGE PER RETURN	AVERAGE PER RETURN	AVERAGE PER RETURN	AVERAGE PER TAXPAYER
AGI RANGE	PFD RECIEVED					
NO AGI	\$404	4107	0.00	0.00	0.00	0.00
	\$808	1299	0.00	0.00	0.00	
\$1 TO \$10000	\$404	34309	3416.89	213.52	32.58	26.95
	\$808	4955	2177.80	58.83	14.88	
\$10001 TO \$20000	\$404	26772	12688.20	1549.45	75.36	58.93
	\$808	7015	10134.11	888.38	55.18	
\$20001 TO \$30000	\$404	21397	21497.06	3455.20	101.67	72.51
	\$808	9560	19455.42	2453.06	79.77	
\$30001 TO \$40000	\$404	14022	29750.56	5683.43	123.92	79.04
	\$808	11568	28134.89	4433.16	103.40	
\$40001 TO \$50000	\$404	8336	37955.63	8252.25	140.84	82.60
	\$808	11855	36314.60	6763.53	124.27	
\$50001 TO \$100000	\$404	10033	53400.38	13933.86	160.99	90.27
	\$808	24316	53236.86	12792.78	151.36	
OVER \$100000	\$404	744	139685.10	53978.43	188.34	107.08
	\$808	2178	137793.01	51370.18	186.41	
TOTAL		192466	25503.80	5380.92	93.30	69.47

MEMORANDUM

State of Alaska

TO: Vincent Wright
Chief of Research
Department of Revenue

DATE: October 25, 1984

FILE NO:

TELEPHONE NO: 465-2175

FROM: Al Zangri
Economist
Research Section
Department of Revenue

SUBJECT: Actual leakage from
1982 PFD distribution

This memo considers only adult PFD distributions, as the dividends issued to children 17 and under are generally not taxable. Of the 233,201 permanent fund dividends distributed to adult residents in 1982, 182,615 were distributed to individuals who filed federal income tax returns in 1982. These 182,615 individuals filed 120,966 tax returns. Strictly speaking, only 124,485 should have been filed since 2,481 people who claimed the 82 PFD on their 82 taxes did not actually receive the dividend until 1983. However, the net effect of this action is to reduce the overall leakage from the 82 and 83 dividend distributions.

Table 1, attached, shows the total taxable income, total income tax paid, and total leakage to the IRS from those 120,966 returns. Table 2 shows the average (per return) taxable income, tax paid and leakage. It also shows the average leakage per taxpayer.

The total leakage was 53,233,939. This compares with our earlier estimate of 60,700,599. Note that the average leakage per taxpayer is very close to the estimate first made last year. The primary error in the total estimate results from over estimating the number of returns that would be filed. The methodology used to estimate the number of returns is not identified in the earlier report so I cannot identify the source of error. The methodology used to estimate the leakage given the number of returns filed was excellent as is evident from comparing the average leakages.

Table 3 shows the total distribution of total taxable income and total income tax payable that would have existed without the PFD distribution. I have included it to illustrate the changes that the PFD introduced into the AGI ranges. It is possible to show exactly how many people were moved into a higher marginal bracket as a result of the dividend distribution. If that would be of interest, I can include it in the report when I look at the 83 leakage.

Given the results of this effort, I suspect that the ICER study over estimated the tax leakage by a fairly large margin.

TABLE 1

AGI RANGE	NUMBER OF RETURNS	TAXABLE INCOME	INCOME TAX PAYABLE	TAX LEAKAGE
		TOTAL	TOTAL	TOTAL
NO AGI	1193	0.00	0.00	0.00
\$1 TO \$10000	23322	85173846.64	5822023.67	1993692.91
\$10001 TO \$20000	22303	275321320.52	37345549.46	5292844.02
\$20001 TO \$30000	21105	447053292.34	79733487.39	7355783.99
\$30001 TO \$40000	17762	522483200.69	108345033.66	8446641.45
\$40001 TO \$50000	14605	547086581.13	127996512.29	9017960.70
\$50001 TO \$100000	24874	1337532934.59	384796908.04	19502811.25
OVER \$100000	1802	248815076.65	102329800.06	1624205.17
TOTAL	126966	3463466252.56	846369314.56	53233939.49

TABLE 2

AGI RANGE	PFD RECIEVED	NUMBER OF RETURNS	TAXABLE INCOME	INCOME TAX PAYABLE	TAX LEAKAGE	TAX LEAKAGE
			AVERAGE PER RETURN	AVERAGE PER RETURN	AVERAGE PER RETURN	AVERAGE PER TAXPAYER
NO AGI	\$1000	638	0.00	0.00	0.00	0.00
	\$2000	555	0.00	0.00	0.00	
\$1 TO \$10000	\$1000	20211	3801.84	275.00	88.35	75.42
	\$2000	3111	2679.13	84.85	66.87	
\$10001 TO \$20000	\$1000	17102	12933.19	1863.79	216.75	192.44
	\$2000	5201	10409.13	1051.92	304.93	
\$20001 TO \$30000	\$1000	14106	21818.43	4185.91	297.73	261.73
	\$2000	6999	19900.34	2955.71	450.93	
\$30001 TO \$40000	\$1000	8826	30114.76	6878.26	361.53	316.38
	\$2000	8936	28725.41	5330.96	588.16	
\$40001 TO \$50000	\$1000	4898	38417.68	10023.61	415.24	370.93
	\$2000	9707	36975.05	8128.24	719.49	
\$50001 TO \$100000	\$1000	5206	53682.89	16569.47	462.05	437.85
	\$2000	19668	53796.00	15178.78	869.30	
OVER \$100000	\$1000	330	141322.48	59535.06	495.30	496.09
	\$2000	1472	137349.63	56170.67	992.36	
TOTAL		126966	27278.69	6666.11	419.28	291.51

TABLE 3

	NUMBER OF RETURNS	PRE PFD TAXABLE INCOME	PRE PFD INCOME TAX PAYABLE	TAX LEAKAGE
		TOTAL	TOTAL	TOTAL
AGI RANGE				
NO AGI	2053	0.00	0.00	0.00
\$1 TO \$10000	25192	81443181.80	5450470.46	2527880.66
\$10001 TO \$20000	22381	274288775.01	37000746.05	5673173.97
\$20001 TO \$30000	21041	440996658.44	77879457.90	7680099.63
\$30001 TO \$40000	17597	512263470.64	105044964.51	8768397.67
\$40001 TO \$50000	14159	526106529.48	122195099.49	9016138.73
\$50001 TO \$100000	22858	1216342192.09	348117360.72	18053242.55
OVER \$100000	1685	236141978.35	97447275.94	1515006.27
TOTAL	126966	3287582785.81	793135375.07	53233939.49

Federal Tax Leakages Associated With 1979 State Income Tax Refunds

By
Lance R. Rovig, Economist
and
Deborah A. Lasher, Research Analyst

The following report is the result of research efforts to ascertain the tax leakages to the Federal government as a result of the repeal of the individual income tax enacted by the 1980 Special Legislative Session.

Federal Tax Leakages Associated With 1979 State Income Tax Refunds

Resident and nonresident Alaskan taxpayers who itemized their Federal deductions in tax year 1979 will have to pay Federal taxes in tax year 1980 on their 1979 State income tax refunds. The refunds must be included on the 1980 Federal Form 1040 as taxable income to the extent that the State tax deduction decreased Federal taxes owed in 1979. Persons who did not claim the State tax as an itemized deduction in tax year 1979 do not have to include the refunds as Federal taxable income for tax year 1980. For reasons explained below, it was assumed throughout this analysis that the same number of returns which itemized at the State level also itemized at the Federal level.

State income taxes recorded to date for tax year 1979 by residents and nonresidents are presented in a series of tables. These tables are based on data captured as of December 1, 1980 and although incomplete do represent the bulk of taxes paid. The basic conclusions of this report, therefore, should not be substantially affected once all the data is captured. Tables I through VI show resident taxes paid by filing status. These are resident returns which itemized their Alaska deductions and which will probably have to pay Federal taxes on their 1979 State income tax refunds. Table B gives a breakdown of resident taxes paid by Federal adjusted gross income categories for returns which itemized and for returns which took the standard deduction. Tables C and D show nonresident taxes paid by Federal adjusted gross income categories for returns which itemized and for returns which took the standard deduction. Nonresident returns were further disaggregated into instate and out of State returns.

Resident and Nonresident Returns:

As shown in Table A, of the \$92,601,302 in taxes paid and refunded on returns for tax year 1979, residents paid \$82,531,737, or 89%, and nonresidents paid \$10,069,565, or 11%. Of the 187,124 total returns, 148,004, or 79%, were resident and 39,120, or 21%, were nonresident returns. This amounts to an average tax paid of \$494.87 for residents and nonresidents combined, or an average tax of \$557.63 for residents and \$257.40 for nonresidents.

As shown on Tables C and D approximately 21,281 nonresident returns, or 54%, itemized their deductions and 17,839, or 46%, took the standard deduction. Table B shows that 92,006, or 62%, of the resident returns took the standard deduction and did not itemize in tax year 1979. And, 55,998, or 38%, of the resident returns itemized their Alaska deductions and probably claimed the State tax as a deduction against their 1979 Federal taxable income.

Itemized Resident Returns:

Although only 38% of the resident returns itemized their deductions they paid 67% of the resident taxes. Resident returns that itemized paid \$55,240,070 of the \$82,531,737 of taxes paid by residents in tax year 1979. This is an average tax paid of \$986 per itemized resident return.

The tax leakage to the Federal government as a result of refunding 1979 taxes paid by Alaskan residents who itemized is estimated to be \$24,186,038. Thus, the average tax leakage is \$432 per itemized resident return. This leakage is 29% of the \$82,531,737 refunded to residents and is 44% of the \$55,240,070 refunded to those residents who itemized deductions on their 1979 tax returns.

Itemized Nonresident Returns:

As explained below, the Federal tax leakage for nonresident returns was determined by using resident returns. Non-resident returns are restricted with regard to the itemized deductions that they can claim on their Alaska tax returns, and these restrictions make it difficult to estimate Federal taxable income from data on the nonresident State returns. Of the \$10,069,565 in nonresident taxes paid in 1979, \$6,355,677, or 63% came from returns which itemized. This is an average tax paid of \$299 per itemized nonresident return. Assuming that 44% of these refunds are paid in Federal taxes, as is the case for resident returns which itemized, then approximately \$2,796,497 would be the tax leakage associated with nonresident returns which itemized. This represents an average tax leakage of \$131 per itemized nonresident return.

Methodology:

Because the State does not collect data on Federal taxable income and since Federal and State taxable income differ somewhat, State taxable income was adjusted to estimate Federal taxable income. For example, State taxable income includes Federal cost of living allowances whereas Federal taxable income does not. Items exempt from State taxation include interest on federal securities, armed services pay, certain pensions and annuities, national guard pay and income from the sale of halibut taken outside of Alaskan waters. In addition, the State tax is not included in Federal taxable income but it is included in State taxable

income. Finally, the standard deduction is included in Federal taxable income because it is subtracted out of taxable income automatically in the tax tables and tax rate schedules. Thus, Federal taxable income was computed as Federal adjusted gross income plus the standard deduction minus 1979 State income taxes withheld minus personal exemptions minus allowable State deductions.

Federal taxes were computed by applying the appropriate tax rate to Federal taxable income. The tax rate that was applied to Federal taxable income was selected according to the taxable income and filing status reported on each return. By adding the 1979 State refund to Federal taxable income the new taxable income and the appropriate new tax rate associated with it was estimated. The new tax rate was then applied to the State refund to calculate the Federal leakage for each return by filing status. For example, a refund of \$800 on an itemized return for a single taxpayer that had \$18,200 in taxable income would result in \$19,000 taxable income. The additional \$800 would be taxed at a rate of 34% or \$272, which is one tax bracket higher than the 30% rate which applied to taxable income over \$15,000 before the tax refund. This \$272 is the federal tax leakage associated with the \$800 State income tax refund. Of the 55,998 itemizing resident returns 49,100 remain in the same tax bracket, 6,838 jump one tax bracket and 60 returns jump two tax brackets as a result of adding 1979 State income tax refunds. Federal tax schedules X, Y and Z were used to make the tax computations for the tables presented in this report.

Accuracy of Estimates:

As shown in Table A, there were 2,405 resident returns and 840 nonresident returns categorized as having zero adjusted gross income (AGI). There are several reasons for this phenomenon. First, some returns may have negative taxable income or income and deductions which are equal. Second, the data on some returns may not have been completely captured (keypunched). And finally, returns received after August either did not contain any tax data other than the amount of tax to be refunded, or in the interest of quick and efficient handling of tax refunds, the data on these returns was not keypunched for the computerized record.

Because State taxes are allowed as a deduction against Federal taxable income but not allowed as a deduction against State taxable income, a few returns which itemized at the Federal level may not have itemized at the State level. Since the number of State resident returns which itemized was used as the surrogate for the number of Federal returns which itemized in 1979, the Federal leakage associated

with 1979 State income tax refunds may be slightly understated. However, Federal individual income tax statistics for tax years 1972 through 1977 indicate that approximately the same percentage of returns itemized in Alaska at the Federal level as were itemized at the State level for tax year 1979.

Some residents who itemized their Federal deductions may file amended returns and claim the standard deduction, if in so doing they can retain more money by keeping the full tax refund as opposed to itemizing deductions on their 1979 Federal tax returns. Finally, since Federal taxable income was computed from State tax data, only resident returns were used in the calculations. Nonresident returns are restricted with regard to the itemized deductions that they may claim on their Alaska tax returns. Itemized deductions are allowed only to the extent that they are paid from income earned in Alaska or directly connected with property having a taxable situs in Alaska. Thus, nonresident State deductions are less than Federal deductions. Consequently, Federal taxable income (and the Federal tax leakage associated with it) if calculated as Federal adjusted gross income plus the standard deduction minus 1979 State income taxes withheld minus personal exemptions minus allowable State deductions, would be overstated for nonresident returns.

TABLE I

1979 Itemizing Residents Estimate Of Tax LeakageSummary

<u>Filing Status</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
Single	12,415	\$ 200,601,536	\$ 9,773,914	\$ 4,173,041
Married-Joint	39,476	1,170,493,498	42,730,912	18,387,549
Married-Separate	838	10,507,790	425,234	198,551
Unmarried-Head of Household	3,168	56,803,812	2,261,403	906,711
Widow(er)	101	1,712,322	48,607	20,187
Totals	<u>55,998</u>	<u>\$1,440,118,959</u>	<u>\$55,240,070</u>	<u>\$24,186,038</u>

TABLE II

1979 Itemizing Residents Estimate Of Tax LeakageFiling Single

<u>Estimated Federal Taxable Income Range</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
\$ 0	247	\$ 0	\$ 0	\$ 0
1- 2,300	2,089	3,047,898	191,298	0
2,301- 3,400	552	1,506,559	39,064	1,273
3,401- 4,400	379	1,467,718	6,462	634
4,401- 6,500	545	2,923,656	13,661	1,502
6,501- 8,500	541	4,025,641	31,706	4,393
8,501- 10,800	527	5,046,188	40,275	8,421
10,801- 12,900	560	6,526,200	120,260	27,676
12,901- 15,000	605	8,260,527	180,407	48,956
15,001- 18,200	1,033	16,627,903	526,945	156,821
18,201- 23,500	1,687	33,834,372	1,367,286	462,111
23,501- 28,800	1,370	33,910,252	1,693,226	652,035
28,801- 34,100	942	27,871,593	1,620,435	699,322
34,101- 41,500	716	25,085,318	1,636,917	787,068
41,501- 55,300	474	20,635,719	1,474,514	798,125
55,301- 81,800	126	7,552,414	593,336	367,967
81,801-108,300	16	1,372,581	131,327	88,496
108,301- +	6	906,994	97,796	68,239
Totals	<u>12,415</u>	<u>\$200,601,536</u>	<u>\$9,773,914</u>	<u>\$4,173,041</u>

TABLE III

1979 Itemizing Residents Estimate Of Tax LeakageFiling Jointly

<u>Estimated Federal Taxable Income Range</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
\$ 0	753	\$ 0	\$ 0	\$ 0
1- 3,400	1,506	1,897,131	551,885	0
3,401- 5,500	626	2,654,946	110,979	3,415
5,501- 7,600	678	4,440,780	28,764	2,741
7,601- 11,900	1,848	18,273,618	48,827	6,550
11,901- 16,000	2,367	33,139,137	79,615	16,536
16,001- 20,200	2,938	53,037,911	397,439	95,086
20,201- 24,600	3,910	86,587,757	1,325,390	367,610
24,601- 29,900	5,235	139,707,838	3,197,448	1,018,301
29,901- 35,200	5,342	168,461,698	5,135,562	1,875,101
35,201- 45,800	8,056	309,911,902	12,136,572	5,174,723
45,801- 60,000	4,456	218,125,352	10,834,659	5,243,567
60,001- 85,600	1,360	87,574,466	5,237,655	2,790,715
85,601-109,400	223	20,102,976	1,391,654	812,280
109,401-162,400	132	15,667,371	1,266,199	800,969
162,401-215,400	26	4,340,635	391,907	262,787
215,401- +	20	6,569,980	596,357	417,167
Totals	<u>39,476</u>	<u>\$1,170,493,498</u>	<u>\$42,730,912</u>	<u>\$18,887,549</u>

TABLE IV

1979 Itemizing Residents Estimate Of Tax LeakageFiling Separately

<u>Estimated Federal Taxable Income Range</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
\$ 0	54	\$ 0	\$ 0	\$ 0
1- 1,700	117	94,954	3,124	0
1,701- 2,750	30	64,934	86	12
2,751- 3,800	34	110,961	33	5
3,801- 5,950	64	308,428	11,794	1,385
5,951- 8,000	57	391,703	813	171
8,001- 10,000	50	446,470	5,644	1,329
10,001- 12,300	57	624,798	10,530	2,938
12,301- 14,950	56	740,845	16,569	5,267
14,951- 17,600	53	827,305	27,139	9,830
17,601- 22,900	115	2,213,209	86,348	36,804
22,901- 30,000	81	2,015,730	98,601	47,615
30,001- 42,800	52	1,746,648	101,264	54,161
42,801- 54,700	10	452,918	28,971	16,888
54,701- 81,200	7	385,366	26,088	16,549
81,201-107,700	1	83,522	8,230	5,596
107,701- +	0	0	0	0
Totals	<u>838</u>	<u>\$10,507,790</u>	<u>\$425,234</u>	<u>\$198,551</u>

TABLE V

1979 Itemizing Residents Estimate Of Tax LeakageFiling Head Of House

<u>Estimated Federal Taxable Income Range</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
\$ 0	110	\$ 0	\$ 0	\$ 0
1- 2,300	180	213,806	11,037	0
2,301- 4,400	103	348,772	7,242	370
4,401- 6,500	140	764,472	714	114
6,501- 8,700	170	1,314,324	2,692	485
8,701- 11,800	314	3,208,540	30,270	6,648
11,801- 15,000	347	4,572,816	85,193	20,396
15,001- 18,200	355	5,729,100	161,623	41,753
18,201- 23,500	509	10,199,334	348,245	107,155
23,501- 28,800	383	9,497,937	396,836	140,806
28,801- 34,100	230	6,871,403	344,876	142,442
34,101- 44,700	219	8,030,576	455,163	207,932
44,701- 60,600	84	3,969,547	248,438	131,115
60,601- 81,800	14	894,503	62,764	36,428
81,801-108,300	6	526,585	41,823	26,322
108,301-161,300	2	227,769	19,907	13,537
161,301- +	2	434,329	44,583	31,208
Totals	<u>3,168</u>	<u>\$56,803,812</u>	<u>\$2,261,403</u>	<u>\$906,711</u>

TABLE VI

1979 Itemizing Residents Estimate Of Tax LeakageFiling Widow

<u>Estimated Federal Taxable Income Range</u>	<u>Returns</u>	<u>Estimated Federal Taxable Income</u>	<u>Alaska State Tax Paid</u>	<u>Estimated Tax Leakage</u>
\$ 0	7	\$ 0	\$ 0	\$ 0
1- 3,400	14	19,837	0	0
3,401- 5,500	6	27,903	5	1
5,501- 7,600	8	54,270	0	0
7,601- 11,900	10	99,159	103	19
11,901- 16,000	9	127,227	727	153
16,001- 20,200	10	176,120	2,593	613
20,201- 24,600	13	282,511	6,433	1,801
24,601- 29,900	5	132,440	3,673	1,150
29,901- 35,200	6	186,045	6,205	2,234
35,201- 45,800	9	349,588	12,159	5,073
45,801- 60,000	2	94,736	4,990	2,445
60,001- 85,600	1	62,180	4,313	2,329
85,601-109,400	1	100,306	7,406	4,370
109,401-215,400	0	0	0	0
215,401- +	0	0	0	0
Totals	<u>101</u>	<u>\$1,712,322</u>	<u>\$48,607</u>	<u>\$20,187</u>

TABLE A

1979 Resident Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	2,405	\$ 190,276	\$ 999,101
1- 5,000	25,751	6,486,443	63,685
5,001- 10,000	20,164	61,262,549	177,703
10,001- 15,000	18,006	112,689,187	1,771,070
15,001- 20,000	15,695	167,264,902	3,758,809
20,001- 25,000	13,111	188,315,241	5,109,024
25,001- 30,000	11,097	207,485,192	6,408,912
30,001- 35,000	9,734	220,577,934	7,354,175
35,001- 40,000	8,318	223,583,054	8,259,171
40,001- 45,000	6,942	215,642,962	8,735,178
45,001- 50,000	5,220	184,580,094	8,159,131
50,001- 60,000	6,597	269,899,159	13,204,322
60,001- 100,000	4,455	239,885,717	13,919,790
100,001- +	509	60,010,940	4,611,756
Subtotal	<u>148,004</u>	<u>\$2,167,873,650</u>	<u>\$82,531,737</u>

1979 Nonresident Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	840	\$ 3,308,470	\$ 176,164
1- 5,000	6,530	3,326,848	61,254
5,001- 10,000	8,648	20,175,524	295,477
10,001- 15,000	6,186	28,239,117	604,111
15,001- 20,000	4,535	29,531,979	715,370
20,001- 25,000	3,187	28,036,155	791,047
25,001- 30,000	2,387	25,939,577	824,290
30,001- 35,000	1,832	24,598,141	867,064
35,001- 40,000	1,361	22,755,027	893,874
40,001- 45,000	999	19,459,837	837,390
45,001- 50,000	665	14,783,572	683,632
50,001- 60,000	909	25,559,573	1,301,446
60,001- 100,000	795	25,223,909	1,438,842
100,001- +	246	7,977,416	579,604
Subtotal	<u>39,120</u>	<u>\$278,915,145</u>	<u>\$10,069,565</u>
Total	<u>187,124</u>	<u>\$2,446,788,795</u>	<u>\$92,601,302</u>

TABLE B

1979 Residents Itemizing Deductions

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	1,769	\$ 27,206	\$ 987,098
1- 5,000	3,196	1,164,575	31,957
5,001- 10,000	2,068	4,084,880	39,273
10,001- 15,000	2,901	13,346,909	138,146
15,001- 20,000	3,943	34,729,763	632,211
20,001- 25,000	4,868	62,258,014	1,487,078
25,001- 30,000	5,547	95,701,706	2,677,870
30,001- 35,000	5,953	126,816,594	3,928,027
35,001- 40,000	5,856	151,429,874	5,313,850
40,001- 45,000	5,383	161,623,207	6,261,470
45,001- 50,000	4,309	148,681,669	6,395,904
50,001- 60,000	5,732	230,444,696	11,079,094
60,001- 100,000	4,017	212,891,786	12,285,905
100,001- +	456	51,856,046	3,982,187
Subtotal	55,998	\$1,295,056,925	\$55,240,070

1979 Residents Taking Standard Deduction

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	636	\$ 163,070	\$ 11,913
1- 5,000	22,555	5,321,868	31,728
5,001- 10,000	18,096	57,177,669	138,430
10,001- 15,000	15,105	109,342,278	1,632,924
15,001- 20,000	11,752	132,535,139	3,126,598
20,001- 25,000	8,243	126,057,227	3,621,946
25,001- 30,000	5,550	111,783,486	3,731,042
30,001- 35,000	3,781	93,761,340	3,425,148
35,001- 40,000	2,462	72,153,180	2,945,321
40,001- 45,000	1,559	54,019,755	2,473,708
45,001- 50,000	911	35,898,425	1,763,227
50,001- 60,000	865	39,454,463	2,125,228
60,001- 100,000	438	26,993,931	1,633,885
100,001- +	53	8,154,894	629,569
Subtotal	92,006	\$872,816,725	\$27,291,667
Total	148,004	\$2,167,873,650	\$82,531,737

TABLE C

1979 Nonresident Itemizing, Out of State Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	8	\$ 144,907	\$ 3,807
1- 5,000	1,957	649,956	7,095
5,001- 10,000	3,240	6,797,436	102,668
10,001- 15,000	2,439	10,104,460	216,445
15,001- 20,000	2,042	12,289,841	288,444
20,001- 25,000	1,501	12,118,852	324,986
25,001- 30,000	1,246	12,474,520	386,331
30,001- 35,000	1,040	12,845,702	429,564
35,001- 40,000	812	13,000,383	492,411
40,001- 45,000	639	11,655,928	484,634
45,001- 50,000	445	9,151,045	406,963
50,001- 60,000	613	15,850,082	779,038
60,001- 100,000	587	17,483,202	952,707
100,001- +	177	6,296,239	456,581
Subtotal	16,746	\$140,862,553	\$5,331,674

1979 Nonresident Itemizing, Instate Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	7	\$ 105,675	\$ 3,863
1- 5,000	408	83,890	250
5,001- 10,000	983	1,715,981	16,097
10,001- 15,000	888	3,310,517	57,319
15,001- 20,000	668	3,765,440	78,015
20,001- 25,000	468	3,679,822	92,624
25,001- 30,000	343	3,737,080	112,379
30,001- 35,000	267	3,511,647	116,887
35,001- 40,000	164	2,770,186	101,793
40,001- 45,000	129	2,598,264	102,551
45,001- 50,000	59	1,256,673	55,350
50,001- 60,000	90	2,594,570	124,180
60,001- 100,000	53	1,980,188	118,452
100,001- +	8	559,177	44,243
Subtotal	4,535	\$31,669,110	\$1,024,003
Total	21,281	\$172,531,663	\$6,355,677

TABLE D

1979 Nonresident Standard Deduction, Out of State Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	623	\$ 2,399,673	\$ 153,012
1- 5,000	3,087	2,050,696	45,693
5,001- 10,000	3,142	8,586,396	137,234
10,001- 15,000	2,050	11,063,999	256,043
15,001- 20,000	1,268	9,629,063	258,569
20,001- 25,000	912	9,238,049	287,859
25,001- 30,000	606	7,375,499	252,090
30,001- 35,000	422	6,417,023	260,253
35,001- 40,000	329	6,064,177	262,288
40,001- 45,000	210	4,720,094	229,446
45,001- 50,000	150	4,117,236	208,263
50,001- 60,000	191	6,680,722	377,045
60,001- 100,000	151	5,577,647	355,354
100,001- +	58	924,223	57,909
Subtotal	<u>13,199</u>	<u>\$84,844,497</u>	<u>\$3,141,058</u>

1979 Nonresident Standard Deduction, Instate Returns

<u>Federal AGI Range</u>	<u>Returns</u>	<u>Alaska Taxable Income</u>	<u>Alaska State Tax Paid</u>
\$ 0	202	\$ 658,215	\$ 15,482
1- 5,000	1,078	542,306	8,216
5,001- 10,000	1,283	3,075,711	39,378
10,001- 15,000	809	3,760,141	74,304
15,001- 20,000	557	3,847,635	90,342
20,001- 25,000	306	2,999,432	85,578
25,001- 30,000	192	2,352,478	73,490
30,001- 35,000	103	1,823,769	60,360
35,001- 40,000	56	920,281	37,382
40,001- 45,000	21	485,551	20,759
45,001- 50,000	11	258,618	13,056
50,001- 60,000	15	434,199	21,183
60,001- 100,000	4	182,872	12,329
100,001- +	3	197,777	20,871
Subtotals	<u>4,640</u>	<u>\$21,538,985</u>	<u>\$572,830</u>
Total	<u>17,839</u>	<u>\$106,383,482</u>	<u>\$3,713,888</u>



ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES
RESEARCH AGENCY

Pouch Y. State Capitol
Juneau, Alaska 99811
(907) 465-3991

April 8, 1986

MEMORANDUM

TO: Representative Mike Davis

ATTN: Mike Welsh

FROM: Mary Jennings *mq*
Legislative Analyst

RE: Commuter Taxes as They Relate to Resident Hire
Research Request 86-147

You requested information regarding commuter taxes; specifically, how do they work, which states have them and whether or not they could be used in Alaska to encourage resident hire.

A number of local governments providing regional services use a wage tax that allows them to tax commuters. A local income tax is allowed by state law in Delaware, Indiana, Kentucky, Michigan, Missouri, New York, Ohio, and Pennsylvania. The tax is withheld from employees' wages and salaries. The rate of taxation for nonresidents (commuters) is either equal to, or in most cases, less than the rate for residents and, depending on the state, it ranges from .5 percent to 4.9 percent. All of the states employing a wage tax have a state income tax which, according to the Pennsylvania Department of Revenue, makes collection and enforcement costs of the commuter tax negligible.

The Pennsylvania Department of Revenue stated that the purpose of the tax is to generate revenue, and not to encourage people to work and live in the same city or county. The department pointed out that in metropolitan Pittsburgh, most cities and towns levy the wage tax, thereby eliminating the incentive of employers to leave the central city for the suburbs. In other states such as Michigan and Ohio, agreements exist between jurisdictions providing that each will receive some income tax revenues from individuals living in one jurisdiction but working in another.

Representative Davis
April 8, 1986
Page Two

Other Nonresident Income Taxation

In 1983, Oregon enacted legislation that changed the way nonresident income was taxed. The law allowed the amount of nonresident income earned in Oregon to be taxed at the rate of the nonresident's total income. In instances where individuals earned only a portion of their income in Oregon, this method of taxation resulted in nonresidents paying higher taxes than residents.¹ According to the Oregon Department of Revenue, this tax legislation set off "border wars" between Oregon and Washington. As a result, Washington, which does not have a state income tax, proposed legislation that would allow border towns in Washington levy a commuter tax on nonresidents working in Washington. Don Smallwood, of the Washington Department of Revenue, stated that Washington proposed this legislation as a threat in order to get Oregon to repeal their new law for taxation of nonresidents. Soon after the Washington proposal, Oregon repealed its law. Although no formal legal opinions resulted, Smallwood stated that the constitutionality of the Oregon law and the proposed Washington legislation was questioned.

Resident Hire in Alaska

The commuter tax as used in other states does not appear to be applicable to encouraging resident hire. In addition, Alaska does not levy a State income tax and the administrative costs of a wage tax would probably be significant. There is also a question of the constitutionality of taxing nonresidents and residents differently. According to Theresa Hillhouse, the Chief Hearing Examiner of the Department of Revenue, in the 1950s, Alaska had instituted a fisheries tax that levied a higher tax on nonresident fisherman. The constitutionality of this law was challenged and it was subsequently repealed.

For your information, I have attached a letter from Mr. William Phillips dealing with this issue. This agency has performed no analysis of Mr. Phillip's proposal, but the concept of credits that favor residents and/or distributions similar to Permanent Fund dividends may have potential as a method for imposing a relatively high tax burden on nonresidents. I hope you find this information useful. Please contact me if you have any questions.

MJ

Attachment

¹The actual tax rate paid by all individuals would be identical. However, by taxing income earned outside Oregon (versus the previous method of taxing only income earned in the state), the amount of tax paid relative to the amount of income earned in Oregon could be higher for nonresidents than for residents.

January 30, 1986

The Honorable Representatives and Senators of the State of Alaska
Pouch V
Juneau, Alaska 99811

Dear Sirs and Madams:

This is a proposal that could deal with two problems facing the state of Alaska; revenue enhancement and local hire. Establish a new state income tax with deductions and tax credits that would just happen to promote living in Alaska. The tax would make it more costly for non-residents to work in Alaska. The non-residents would have the options of moving to Alaska, making a substantial economic investment in Alaska, or seeking work elsewhere.

Establish an income tax with the following rates:

- 5% on the first \$25,000 of taxable income.
- 7.5% on the next \$15,000 of taxable income.
- 10.0% on the next \$20,000 of taxable income.
- 12.5% on all taxable income over \$60,000.

Establish deductions of:

- 25% of the assessed valuation of real property owned in Alaska to a limit of \$30,000.
- Or, rent paid on real property in the state of Alaska to a limit of \$30,000.

Establish tax credits for the following:

- Up to \$500 for donations to the Alaskan Student Loan Fund.
- Up to \$500 for campaign donations made to Alaskan political candidates and/or Alaska political action groups.

Here follow two examples of how this tax plan could work.

Joe Doaks of Tuna, Texas and Sam Resident of Kenai Alaska both own homes with a value of \$120,000 plus personal property of two cars and a boat.

	<u>Doaks</u>	<u>Resident</u>
Income	\$75,000	\$75,000
Deductions	0	30,000
Taxable Income	<u>75,000</u>	<u>45,000</u>
Taxes	6,250	2,875
Credits		
Local Alaskan Real and personal property taxes at 8 mills on \$150,000	0	1,200
Local sales taxes at 5% of 25% of income	0	937.50
Donation to Loan Fund	500	500
Donation to Campaigns	<u>500</u>	<u>500</u>
Total credits	<u>1,000</u>	<u>3,175.50</u>
Taxes owed	5,250	0

Bill Jones of Los Angeles and Don Smith of Fairbanks each own a \$100,000 home and own two cars and a boat.

	<u>Jones</u>	<u>Smith</u>
Income	\$45,000	\$45,000
Deductions	<u>0</u>	<u>25,000</u>
Taxable Income	45,000	20,000
Taxes	2,825	1,000
Credits		
Local Alaskan Real and personal property taxes at 8 mills on \$120,000	0	960
Local sales taxes at 5% of 25% of income	0	0
Donation to Loan Fund	500	0
Donation to Campaigns	<u>500</u>	<u>40</u>
Total Credits	1,000	1,000
Taxes owed	1,825	0

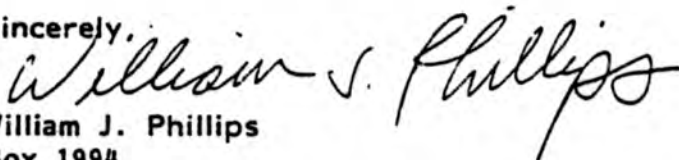
It should be the responsibility of employers to deduct the taxes from earnings. Non-resident contractors should be required to post a \$500,000 bond to guarantee collection and payment of the taxes to the state of Alaska.

Yes, other states would retaliate against the state of Alaska, but then how many Alaskans work out of state while retaining Alaska residency.

A non-resident could buy real property in Alaska or rent Alaskan real property. Nothing would stop them from purchasing and keeping personal property in Alaska. They could buy taxable goods here and take them back home with them. Since a non-resident would be entitled to the same deductions as a resident the tax and deductions would not be discrimination.

While this proposal will not guarantee local hire the additional tax bite should discourage non-residents from working in Alaska. If nothing else the non-residents will start paying their fair share of the costs for services provided to them in the state of Alaska.

Sincerely,


William J. Phillips
Box 1994
Kenai, Alaska 99611

**STATE, FEDERAL AND INDUSTRY SHARES OF ALASKA OIL
RESOURCE INCOME: FISCAL 1982-1985**
(millions of dollars except as noted)

	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]
Fiscal	Total	State	Sever.	Total	Total	Total	Total	Windfall
year	Revenue	Royalty	Conser.	Prop.	Oper.	Deprec.	Acquis.	Profits
			tax	tax	Costs		Costs	Tax
1982	\$16,456	\$1,553	\$1,581	\$276	\$940	\$602	\$1	\$2,018
1983	\$15,470	\$1,448	\$1,494	\$307	\$1,101	\$780	\$1	\$1,018
1984	\$14,955	\$1,409	\$1,393	\$358	\$1,259	\$998	\$1	\$412
1985	\$15,136	\$1,390	\$1,389	\$397	\$1,449	\$1,093	\$1	\$70

	[9]	[10]	[11]	[12]	[13]	[14]	[15]	[16]
Fiscal	Uncap.	Explore.	Admin.	Other	Total	State	Corp.	Federal
Year	Interest	Costs	Costs	Deductions	Deductions	Taxable	Petrol	Taxable
	Expense					Net	Income	Income
1982	\$721	\$191	\$236	\$149	\$8,268	\$8,188	\$669	\$7,519
1983	\$676	\$204	\$252	\$142	\$7,423	\$8,047	\$236	\$7,811
1984	\$614	\$219	\$265	\$136	\$7,064	\$7,891	\$265	\$7,626
1985	\$566	\$234	\$278	\$130	\$6,997	\$8,139	\$169	\$7,970

	[17]	[18]	[19]	[20]	[21]	[22]	[23]
Fiscal	Federal	Oil	Total	Total	----Share of Oil Income----		
Year	Corp.	Industry	Federal	State	State	Federal	Industry
	Income	Alaska	Tax	Tax & Royalty			
1982	\$2,098	\$5,421	\$4,116	\$4,079	30%	30%	40%
1983	\$2,140	\$5,671	\$3,158	\$3,485	28%	26%	46%
1984	\$2,242	\$5,384	\$2,654	\$3,425	30%	23%	47%
1985	\$2,343	\$5,627	\$2,413	\$3,345	29%	21%	49%

SOURCES AND FORMULAS -

Column [1]: Vincent Wright, chief of research, to Mary Nordale, Commissioner of Revenue, Memorandum of October 31, 1985, Table 3.

Columns [2] & [3]: January 1986 DOR Revenue Sources, p. 39.

Columns [4] to [12]: Vincent Wright, loc. cit.

Column [13]: sum of columns [2] through [12]

Column [14]: column [1] - column [13]

Column [15]: Revenue Sources, p. 39.

Column [16]: column [14] - column [15].

Column [17]: column [16] * (production-weighted average tax rate -- 1982 = .279; 1983 = .274; 1984 = .294; 1985 = .294). Company effective rates for '82-84 from R. McIntire and R. Folen, "Corporate Income Taxes in the Reagan Years," Oct. 1984, pp. 32-36; '85 estimated by OMB.

Column [18]: column [16] - column [17].

Column [19]: column [8] + column [17].

Column [20]: sum of columns [2], [3], [4], and [15].

Column [21]: (column [18]) / (sum of columns [18], [19], and [20]).

Column [22]: (column [19]) / (sum of columns [18], [19], and [20]).

Column [23]: (column [20]) / (sum of columns [18], [19], and [20]).

Office of Management and Budget
Division of Strategic Planning
revised April 11, 1986

REVENUE ALTERNATIVES

Excise Taxes
Fisheries Taxes
Licenses and Permits
December 1986

Prepared by

Alaska Department of Revenue
Research Section
Vincent Wright, Chief

Dave Tonkovich, Economist
Bob Elliott, Research Analyst

MEMORANDUM

State of Alaska

TO: Vincent D. Wright
Chief of Research
Department of Revenue

DATE: January 6, 1987

FILE NO.:

THRU:

TELEPHONE NO.: 465-2173

FROM: Dave Tonkovich, Economist ^{ET}
Bob Elliott, Research Analyst ^{BE}
Department of Revenue

SUBJECT: Alternative Means of
Increasing Revenues -
Selective Sales Taxes,
Fisheries Taxes, and
Licenses and Permits

Selective Sales Taxes

Excise taxes are a common form of consumption tax levied on the sale of particular commodities or groups of commodities. Two main types of tax predominate: benefit taxes such as those levied on purchases of motor fuel and sumptuary taxes such as the excises on tobacco and alcohol.

Benefit taxes are rationalized as payments for services which yield measurable benefits to individuals. While it is usually not feasible to charge a motorist a user fee for each mile driven he can be indirectly charged through a tax on the amount of gasoline consumed.

Sumptuary taxes penalize consumption with the hope that this will diminish the use of products such as liquor or cigarettes. However, if such products have low demand elasticities (i.e. consumption responds relatively little when compared to price changes) there is a real question as to whether the sumptuary objective is attained.

Because these taxes have similar characteristics it is helpful to analyze the general features before the review of specific taxes.

Efficiency

Consumption taxes are never levied at a uniform rate on all goods and services and can significantly alter consumer choices and resource allocation. Excise taxes raise the price of the taxed commodity causing consumers to purchase less of the item. The economic effects of the tax depend largely on the demand and supply elasticities of the taxed item.

The burden of these taxes is borne in part by consumers and in part by distributors and producers. Most of the burden will fall on consumers where demand is relatively inelastic (consumption is reduced little relative to an increase in price). The burden will tend to fall on producers if they cannot reduce production as price declines. That is to say supply is inelastic.

Most excise tax revenues are raised from taxes on products for which demand is inelastic - tobacco, alcohol and gasoline. Supply in these industries is relatively elastic so most of the burden falls on

Vincent D. Wright
January 6, 1987
Page 2

consumers. Because consumption of these goods is not reduced much by the price increase the consumer has to reduce consumption of other commodities as well as those which are taxed. Because a wide range of other commodities are involved and because there is little incentive for resources to move out of the taxed industry, resource allocation is not altered significantly by taxes on these goods. This is in sharp contrast to the case of taxes on commodities which are sensitive to price as such levies can substantially alter the pattern of production and consumption. [See Joseph Pechman, Federal Tax Policy, Ch. 6]

Selective excise taxes such as those levied on motor fuel contribute to efficiency in that they collect payments from individuals who benefit from particular public services. When public programs such as the provision and maintenance of highways, airports or docks lower the cost of an activity, that activity is artificially stimulated. This causes more resources to flow into the activity than would occur in the absence of the public program. An excise tax, or some other means of charging for the service, is needed to maintain economic efficiency.

Taxes on items considered socially undesirable are sumptuary taxes and are rationalized on the grounds that their consumption creates additional costs to society which are not reflected in the price of the goods. For instance alcohol consumption leads to lost work time, family problems and accidents while the health hazards of tobacco products are well documented. The argument is made that the excise tax raises prices on these items to more accurately reflect these social costs.

Equity

Excise taxes can be criticized on equity grounds. Burdens are not distributed in accord with established principles of equity such as ability-to-pay. Rather the distribution depends on the proportion of income allocated to taxed items by various income groups. For instance, studies have found excises on beer and cigarettes to be very regressive.

Excise taxes are also criticized for their effects on people with similar incomes (Horizontal equity). Those who prefer the taxed commodities are taxed more than those who prefer other items. This argument is less critical in cases where there are valid social reasons for discouraging consumption or where user charges are impractical.

Finally excise taxes imposed on businesses may be passed onto consumers. Because lower income families spend a larger proportion of their income than do higher income families, this pass through is likely regressive. In summary, equity is frequently the major issue in evaluations of excise taxes.

Elasticity

Excise taxes are not very elastic in that they respond no more than in proportion to changes in income. However the yield of such taxes is relatively stable which makes these taxes popular among state and local governments.

One problem with the taxes as levied in Alaska is that tax rates are expressed as a charge per unit of consumption. When rates are expressed in nominal terms the real tax rate can decline dramatically in periods with significant inflation. Two alternatives to this problem would be the periodic adjustment of rates to reflect inflation or the imposition of the tax as a percentage of sales value. For instance, 11 states employ ad valorem taxes on alcohol. The City of Juneau adds 3% to its 4% sales tax rate for purchases of alcohol.

Administration and Compliance

Probably the main attraction of excise and other consumption taxes is their relative ease of administration. In most cases there are relatively few firms or individuals who need to be monitored by tax authorities. Most difficulties arise in determining if a particular transaction or activity creates a tax liability. In some states problems occur because lower tax rates in bordering states lead to a loss of business and smuggling. Such interstate problems would be minimal in Alaska.

Political Considerations

Private and public concerns about health and problems caused by alcohol consumption generate some support for the sumptuary taxes. Because fuel prices have stabilized or started to decline in the state there is probably less resistance to tax increases on fuels than would have been the case several years ago. Problems could arise if a number of excise taxes were raised simultaneously with other taxes as this could be burdensome particularly for low income groups.

Cigarette Tax

The present cigarette tax is 8 mills per cigarette with 5.5 mills (68.75% of revenues) going to the general fund and 2.5 mills (31.25% of revenues) going to the school fund.

Vincent D. Wright
January 6, 1987
Page 4

The January 1986 revenue forecast used these estimates of cigarette consumption:

Taxable Cigarettes
(Millions of Cigarettes)

<u>FY 87</u>	<u>FY 88</u>	<u>FY 89</u>
1,264.9	1,202.4	1,154.6

General Fund revenues for 1987 should be approximately \$7 million dollars with School Fund revenues of \$3.2 million. For a package of 20 cigarettes the 8 mill rate translates to \$.16 per pack. The highest rate among other states is Maine with a tax of \$.28 per pack. That rate would, in the absence of adjustments for higher, tax-induced declines in consumption, raise about \$17.7 million for Alaska. This is an increase of about \$7 million.

It is useful to examine the elasticity issue for the cigarette tax. The general points made about efficiency, equity and administrative costs pretty well cover the issues usually raised in analyses of cigarette taxes.

Concerns with the health hazards of smoking have tended to decrease cigarette use over time. Figures for 1982 showed that the number of adult smokers nationally had declined by 27 percent since 1965. In Alaska per capita sales peaked at 165 packs per year in 1976, fell during the post pipeline period and rose again to 148 packs in 1982. Since that time consumption has fallen to 129 packs, a decline of 13 percent in 3 years.

Given the economic outlook, it is unlikely that population will increase significantly and the yield of this tax could easily decrease.

Alcoholic Beverage Excise Tax

The January 1986 revenue forecast was based on these estimates of future sales for the three main beverage types:

Gallons of Alcoholic Beverages

	<u>FY 87</u>	<u>FY 88</u>	<u>FY 89</u>	<u>Current Rate/Gal.</u>
Liquor	1,199,863	1,152,205	1,117,870	\$5.60
Wine	1,555,228	1,508,569	1,478,399	.85
Beer	13,585,324	13,177,749	12,914,208	.35
Estimated Present Tax	\$12,796,040	\$12,346,844	\$12,036,684	

Vincent D. Wright
January 6, 1987
Page 5

One approach taken by other states is to equalize the tax on a per ounce of alcohol basis. Consider these figures based on average alcohol content by beverage type (1 gallon = 128 ounces):

	<u>Absolute Alcohol %</u>	<u>Ounces of Alcohol/gal.</u>	<u>Present Tax per ounce of Alcohol</u>	<u>Rate to Equalize Tax per ounce</u>
Liquor	43.0	55.0	\$.1018	\$5.60
Wine	14.0	17.9	.0475	1.82
Beer	4.5	5.76	.0607	.58

On this ounce of alcohol basis the present liquor tax is over twice as high as the tax on wine and is 1.67 times the tax on beer. It is hard to justify the present structure if the goal of tax policy is to reduce alcohol consumption.

Application of the "equalized" rates to FY 87 gallonages would produce revenues of \$17.4 million, an increase of about \$4.6 million. Keep in mind that actual revenues would be somewhat lower because of a decrease in consumption caused by higher prices for wine and beer.

The general arguments made on sumptuary taxes regarding efficiency, equity and administrative costs apply to the alcohol tax. The elasticity issue warrants separate analysis because of the effect of changing lifestyles on liquor consumption.

In 1987, under the present rate structure, over half of alcohol tax revenues will come from the tax on liquor. The national trend has seen per capita consumption of liquor decline by 10 percent over the 5 year period beginning in 1980. This tendency, plus the stagnant outlook for population suggests little if any growth in this source of revenue over the near future.

It is also worthwhile to consider the political and social concerns associated with taxes on alcohol. Taxes on alcohol have appeal for several reasons. The tax is widely used and has been used over long periods of time. The first excise tax on liquor in Alaska was a 1933 levy of 5 cents a gallon on beer and wine. Second, alcoholism is a severe problem in Alaska and there is some evidence that high taxes can discourage drinking by particular groups such as young people. Finally, there are obvious externalities associated with alcohol consumption - broken homes, child abuse, and drunk driving. Public policy aimed at reducing consumption would seem to have a strong justification.

FILE SUMMARY
DEBITES AND CREDITS
MONTH & YEAR: FY 1906

TOTAL	AVIATION GAS			AVIATION JET			MARINE GAS			MARINE DIESEL			OTHER GAS			OTHER DIESEL			
	AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT	RATE	GALLONS AMOUNT				
TOTAL DISTRIBUTIONS			18471847			560656175			15056795			105297514			218042714			663699517	
EXEMPT DISTRIBUTIONS			606828			261678537			307187			6850594			18623962			383241910	
TAXABLE DISTRIBUTIONS PERCENT	653,643,902 100.00%	0.04	17865019	\$714,601 1.33%	0.025	299177038	\$7,479,446 13.89%	0.05	14749608	\$737,480 1.37%	0.05	98446920	\$4,922,346 9.14%	0.08	219418752	\$17,553,500 32.60%	0.08	280457607	\$22,436,609 41.67%
REFUNDS	\$6,636,074																		
EXEMPT DISTRIBUTIONS	\$4,760,225			\$2,379			\$2,725,956			\$125			\$1,367,118			\$21,467			\$663,161
GOVERNMENT	\$10,509	0.04	4025	\$161				0.05	339	\$17	0.05	3180	\$159	0.08	201108	\$16,089	0.08	51037	\$4,083
RENTALS	\$446,220													0.08	150	\$12	0.08	5579041	\$446,323
OTHER	\$4,312,382	0.04	55445	\$2,218	0.025	109038227	\$2,725,956	0.05	2154	\$108	0.05	27339182	\$1,366,959	0.08	67078	\$5,366	0.08	2659689	\$212,775
USE CONVERSIONS	\$1,855,849			\$0			\$227			\$440			\$16,719			\$123,281			\$1,715,162
TO MARINE	\$16,276													0.03	18260	\$546	0.03	922610	\$27,560
TO OFFSHORE	\$1,025,095				0.005	45404	\$227	0.03	14667	\$440	0.03	557200	\$16,719	0.06	2045579	\$122,735	0.06	28037699	\$1,682,274
TO JET	\$5,249																0.055	95410	\$5,248
REFUNDS	\$11,341,774																		
EXEMPT DISTRIBUTIONS	\$659,977			\$0			\$0			\$0			\$26,326			\$7,858			\$635,794
GOVERNMENT	\$1,567													0.08	32087	\$2,567	0.08		\$0
RENTALS	\$11,616													0.08		\$0	0.08	7776230	\$621,618
OTHER	\$45,743										0.05	526526	\$26,326	0.08	66139	\$5,291	0.08	177200	\$14,176
USE CONVERSIONS	\$1,671,745			\$0			\$0			\$0			\$0			\$216,473			\$10,455,323
TO MARINE	\$4,058													0.03	135033	\$4,051	0.03	233	\$7
TO OFFSHORE	\$10,687,737													0.06	3540361	\$212,422	0.06	174255259	\$10,455,316
TO JET	\$0																0.055		\$0
TOTAL PERIODS AND CREDITS	\$17,977,648			\$2,379			\$2,726,183			\$565			\$1,416,163			\$369,074			\$13,469,420
NET TAX	\$15,060,174			\$712,222			\$4,753,263			\$736,916			\$3,512,163			\$17,184,422			\$8,967,128
PERCENT	100.00%			1.99%			13.25%			2.05%			9.79%			47.91%			25.00%

Motor Fuel Taxes

Taxes in Alaska are levied on aviation fuel (4¢ on gas, 2.5¢ on jet) on marine fuel (5¢ on gas and diesel) and on highway fuel (8¢ on gas and diesel, 2¢ for off-highway uses).

Under the Alaska fuel tax system a number of fuel uses are exempt from tax. Sales to government agencies and sales of home heating oil are two examples. Most such exemptions are made outright. However, some fuel is initially taxed but because it is ultimately consumed in an exempt use the tax is fully refunded. In addition, fuel may initially be taxed at one rate but a refund or credit subsequently granted because the fuel is consumed in a use which carries a lower tax. Highway gas, can be used in an outboard motor. In this case the user can apply for a 3 cent per gallon refund, the difference between the highway and marine rates. It is important to understand the refund aspect of the fuel tax system as it has a great influence on the revenue productivity of that system. Consider these figures by fuel category for FY 86:

The table makes a comparison between the nominal revenues for those distributions initially treated as taxable, the levels of refunds and credits for each fuel type and finally shows the net tax collected. For instance the figures for other diesel can be read as follows:

1. Out of 663,699,517 gallons distributed, 280,457,607 gallons were originally put into the taxable category. The remainder went to uses exempt from the tax.
2. Subsequently an additional 8,289,767 gallons were exempted causing \$663,181 to be refunded while 7,947,430 gallons were exempted yielding credits on other fuel taxes owed of \$635,794.
3. Substantial gallonage was consumed in uses carrying lower tax rates than the nominal 8¢ per gallon figure for this category of fuel. Refunds of \$1,715,182 and credits of \$10,455,323 were created through this use conversion.
4. Out of \$22,463,609 in revenues that would have accrued if all taxable distributions were subject to the 8¢ rate, \$8,967,129 was the ultimate tax.

The purpose of this illustration is not to pass judgment on the credit/refund system. To the extent that fuel taxes for some uses (e.g. highway gas) are viewed as indirect payments for the use of publicly constructed facilities (e.g. streets and highways) then it is reasonable that a consumer not pay for this benefit when the fuel use is unrelated (e.g. running a chain saw). The illustration does, however, show how important refunds and credits are to the total fuel tax system. For instance, if total distributions of all fuel types (1,601,424,762 gallons) were the tax base, a tax rate of about 2.2 cents per gallon would raise revenues equivalent to the \$35,866,134 raised in FY 86.

Vincent D. Wright
January 6, 1987
Page 7

To summarize, discussions on ways to increase fuel tax revenues need to be based on more than a simple adjustment of nominal rates. The system of refunds and credits also needs to be considered.

Efficiency and Equity

Fuel taxes are somewhat defensible on efficiency grounds when viewed as indirect user charges paid to cover construction and maintenance of publicly built highways, airports and harbors. Generally these taxes are criticized on equity grounds.

How the burden of motor fuel taxes is distributed depends on what proportion of income is allocated to consumption of motor fuels at various income levels. Consequently, if fuel taxes represent a larger portion of income for low income groups than for high income individuals the tax would be regressive. Phares in his book Who Pays State and Local Taxes finds the motor fuel tax to be quite regressive with average effective tax rates of 2.25% for the under \$3,000 income class falling to .45% for those classes with incomes over \$35,000.

To the extent that the fuel tax is in accord with benefits received the regressive nature of the tax is of less concern. However if the connection to benefits is unclear then the regressive impact is important particularly given the necessity of the journey to work for low income families.

Elasticity

A number of factors in addition to income will influence how revenues from fuel taxes will respond to future changes in personal income. This is true nationally as well as in Alaska where the problem is complicated by uncertain economic conditions.

Nationally, rapid economic growth in 1984 ended a record 5 year downward trend in petroleum product consumption. Uncertainties about petroleum supplies and prices provided incentives for conservation, fuel switching and fuel efficiency improvements. Similarly, the falling oil prices and large inventories of the past year will work to reduce such conservation incentives. OPEC's recent efforts to control production, if successful, will translate into higher prices for petroleum products and will rekindle efforts at fuel conservation. These general uncertainties, combined with Alaska's economic problems, make it difficult to determine how this revenue source will behave in future periods.

It is important to keep in mind that Alaska's motor fuel taxes are expressed in tax per unit terms rather than ad valorem or percentage of value terms. The real tax per gallon is, as a consequence, declining over time. The present 8¢ per gallon tax on highway gasoline (other gas)

Vincent D. Wright
January 6, 1987
Page 8

was first levied in 1970. At that time the Anchorage Consumer Price Index (CPI) was at 109.6. For 1985 the same index had increased to 275.4. Expressed in 1970 dollars the real tax rate on gasoline in 1985 was slightly over 3¢ per gallon. In fairness it needs to be pointed out that the refund for off-highway use was set that same year at \$.06 per gallon. It too has declined dramatically in real terms. At present the lowest tax for gasoline among the 50 states is \$.07 (Missouri) while the highest is \$.18 (Washington).

FISHERIES TAXES

Fisheries Business Tax (AS 43.75)

The fisheries business tax is based upon value to the fisherman by the types of processing operations and the types of fish processed. The tax was substantially increased for all processing types in 1979 with developing commercial fish operations assessed a lower rate to spur development in those species, and floating processors assessed the highest rate in hopes of encouraging permanent shorebased facilities and local employment. In 1986 a shorebased fisheries business tax credit on capital expenditures was enacted to provide an incentive for modernizing facilities and purchasing equipment for development of new fisheries and fishery products. Unfortunately tax credits usually do not generate the economic benefits as initially intended, benefitting the most would be those firms which are financially healthy and in full production. Those firms which are financially distraught and producing little or not at all would receive little or no benefit from tax credits. Furthermore, the credits were not specific in terms of what types of capital expenditures would be allowable as a credit nor was there any provision in the bill which would provide developing species any tax incentive over other species. The present tax credit will be in effect through tax year 1991 and may result in a total estimated loss to the state of approximately \$13.0 million in General Fund unrestricted revenues. However, it should be noted that municipalities will not be affected by the loss in shared revenue since revenue sharing will be calculated on total collections prior to credits. If tax credits were statutorily amended to reflect only specific equipment for only those developing commercial species the state could gain the following estimated revenues:

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Amending Fisheries Business Tax Credit (Millions of Dollars)	1.5	1.5	1.5

Another related topic concerning the fisheries business tax regards the exporting of fishery resources outside of the State's taxing jurisdiction and not filing an Alaska Fisheries Business Tax return. Although some traditional leakages have been closed during the past few years, there still exists a substantial amount of resources illegally avoiding the tax incidence. One possible solution to the problem would require commercial and private air carriers which ship to the lower 48 or overseas to obtain proof of a fisheries business license with any manifest or cargo declaration shipping fishery resources out of state. The carrier would then be subject to substantial fine or payment of the tax due if there was a failure to comply. There are no means possible to accurately predict the amount of leakage; however, past instances which have been documented or have come to light indicate substantial amounts are being illegally shipped out of state. Based on these past events, it is estimated that the following additional revenues could be generated by reducing this leakage:

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Reducing Leakage of Fisheries Business Tax (Millions of Dollars)	1.5	1.5	1.5

Alaska Seafood Marketing Assessment (AS 16.51)

The Alaska Seafood Marketing Assessment is levied upon eligible seafood processors at an elected rate of 0.2% of value. Although the assessment is collected as a gross receipts tax, it is essentially a charge for a governmental service, in this case, the marketing of Alaskan seafood products. Currently, the market assessment funds approximately one-half of the Alaska Seafood Marketing Institute's (ASMI) FY 87 revised budget (\$2.6 million), thus necessitating a General Fund subsidy to cover the difference. If this subsidy was not appropriated each year, the State would realize approximately \$1.4 million annually in General Fund unrestricted revenues. Although by eliminating a source of funding, the industry would have to elect to either keep the current assessment rate with a lowered budget, or vote to double the assessment to a rate of 0.4% (as provided in AS 16.51.120(E)) in order to maintain current ASMI budget levels. It should be noted that the Legislature suggested in the FY 87 operating appropriations bill (Ch. 129, SLA 1986) that "...the ASMI Board schedule a vote of the seafood industry to consider raising the level of the seafood marketing assessment in order to offset anticipated declines in available general funds for FY 88." Accordingly, it would be market forces and industry monitoring which would determine the most efficient funding level for ASMI rather than the political budget process.

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Eliminating the Seafood Marketing Subsidy (Millions of Dollars)	1.4	1.4	1.4

Salmon Enhancement Tax (AS 43.76)

Limited entry holders within qualified regional aquaculture associations elect a levied tax rate of either 2% or 3% of value of salmon. Essentially the State performs collection and regulatory functions for the current four non-profit qualified associations and retains none of the tax receipts for these services. However, the State does collect penalty and interest on the tax returns which offset the current administrative costs. Therefore, there are no current reasonable means to generate additional revenues to the State from this tax source.

In summary, the total additional estimated revenue generated by amending the credit, reducing the leakage, and eliminating the subsidy would amount to the following:

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Total Fish Taxes (Millions of Dollars)	4.4	4.4	4.4

The fisheries business tax is currently inequitable since the assessed tax rates differ due to the method of processing (canned, shorebased, and floating) and the types of species (developing versus traditional). As a result, there is no horizontal equity or neutrality due to this rate differentiation. It should be noted that tax structuring by the type of processing is unique to Alaska. The fisheries business tax must also be considered regressive since it is levied on a commodity which to a high degree is exported outside the state thus passing a significant part of the tax incidence onto the eventual consumer. On the other hand, both the enhancement and marketing tax are elected assessments by those taxpayers who directly benefit from the services provided, and are thus fairly equitable in scope. It should be noted that although sport fishermen will benefit from the stock enhancement and conservation program, they will not be assessed the tax.

Since the fisheries taxes directly depend upon the fisheries resources, there will likely be periods, due to fluctuating market prices and/or catch production, of revenue uncertainty. This can create considerable problems for not only the State but for local municipalities which may depend heavily upon the shared revenues, as well as, play havoc with the budgets of ASMI and the regional aquaculture associations. However, this responsiveness of tax changes to market conditions, or elasticity, can work both ways, being undesirable during poor market conditions but being advantageous during good market conditions and during periods of inflation when the State would be able to receive the same real purchasing power from fish revenues without having to increase

Vincent D. Wright
January 6, 1987
Page 11

rates. Therefore, although the fisheries taxes are quite elastic, they are somewhat inefficient due to their inconsistent revenue flow.

In terms of administrative efficiency, the fisheries tax changes would be minimal. There would be no cost involved administratively in reducing the tax credit or eliminating the subsidy to ASMI since all regulatory and compliance areas are already operational. The tax credit would only require a statutory change to be implemented while the subsidy elimination would involve no cost except omission from the appropriations bill. Actual costs would probably be reduced in regards to the tax credits, since there would be less credits claimed. Although there may be a slight increase in governmental costs due to additional compliance requirements, in terms of reducing the leakage, the actual costs would be borne by the air carriers and most likely passed on to the consumers of those services in higher rates. Consequently, total State administrative costs would be minimal especially given the expected yield.

Politically, the feasibility of enacting the above changes to the fisheries taxes would appear justifiable based on the current financial condition of the state, since it would provide a means of increasing existing fisheries revenues by approximately 18% without increasing any rates. Although processors would lose some funds due to a reduction in the tax credit, the developing species sector of the industry would still benefit. By eliminating ASMI's subsidy, seafood processors would initially lose some product marketing, however, this could be overcome if the industry deemed it necessary. Finally, by reducing the leakage, it would require that all taxpayers would each pay their fair share of the tax burden.

Licenses and Permits

Licenses and permits, including corporation/occupational licensing fees (AS 02.05, AS 08.01.99, AS 10.05.35, AS 21.06.90), motor vehicle fees and permits (AS 05.30, AS 28.10.15, AS 42.10), alcoholic beverage licenses (AS 04.10), amusement and gaming fees (AS 43.35) and fishing and hunting licenses (AS 16.05 and AS 16.43), could be increased. If all the licenses and permits were allowed to increase with inflation, the following additional General Fund and Fish and Game Fund amounts would be realized:

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Licenses & Permits (Millions of Dollars)	1.8	3.7	5.6

If revenues from licenses and permits are still considered insufficient, a vehicle license fee could be enacted. The vehicle

Vinent D. Wright
January 6, 1987
Page 12

license fee could be levied at the time of registration in lieu of a property or ad valorem tax at a rate of 1% of vehicle market value. The following additional revenues could be generated:

	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
Vehicle License Fee (Millions of Dollars)	13.5	13.8	14.0

Regulatory licenses and permits are not generally included in a tax study since they are not imposed for the purpose of raising revenue due to being insufficient revenue generators. On the other hand, license and permit charges by the State should be sufficient to recover the direct costs of administering and policing the regulatory activities. Further, all costs should be considered, not merely those directly incurred by government in the production of the service. Regulatory charges must include those indirect costs to society such as, in the case of motor vehicle licenses, the costs of highway construction and maintenance and, in the case of alcoholic beverage licenses, the costs arising out of excessive use of alcohol.

In terms of equity, license and permit charges are not mandatory use taxes, but are dictated by the principle that persons pay for what they get. Thus, a person can be excluded from the benefits of the service if he does not wish to pay for it. Although license and permit charges by the state do not result in inequities to lower income groups, equity standards require that these lower income groups be assured of obtaining and affording these services.

The use of charges where possible instead of financing by taxation is regarded as justifiable when demand for the services has some elasticity, so that the use of hunting and fishing fees aids resource allocation and lessens waste. Even if services may have inelastic demand, charges may be warranted on equity grounds alone, and by the fact that persons or businesses subject to the provisions generally receive benefits from the State of comparable value.

The use of regulatory charges appears to have less adverse effect upon behavior than taxes (which are mandatory in nature) and therefore may appear more palatable politically. Many licenses and permits for Alaska are either already under review or have been recently increased. In an attempt to equalize the operating budget with revenue, the occupational licensing fee structure was revised (Ch. 26 & 37, SLA 1985) to provide the additional required revenue. Both alcoholic beverage licenses and amusement and gaming fees could be slightly increased to be more in line with other states. The current motor vehicle fees are more than comparable with other states with the recent enactment of Ch. 60, SLA 1986 which increased driver licensing fees and vehicle registration

Vincent D. Wright
January 6, 1987
Page 13

fees effective September 1, 1986. Finally, non-resident fishing and hunting licenses were increased during the past two years, however, resident fees have not increased since 1977. If additional revenue must be generated by substituting regulatory charges for taxes, then the administrative and regulatory costs should be balanced against the charges to determine the desirability of imposing them.

Revenue Potential
of a
General Sales Tax
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Prepared by

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INTRODUCTION AND PURPOSE OF STUDY

Current revenue projections for fiscal years 1988 through 1992 indicate that revenues generated by petroleum related activities (Oil and Gas Corporate Net Income Tax, Oil and Gas Property Tax, Oil and Gas Severance Tax and Oil and Gas Royalties) will comprise over 81.5 percent of total unrestricted General Fund Revenues for the period. Therefore, state government is presently very dependent on these sources of revenue. Finding sources of additional revenue is becoming increasingly important.

Prudhoe Bay oil production has already peaked. Total Alaskan production is currently projected to decline from over 1.848 million b/d in fiscal year 1986 to under 400,000 b/d by fiscal year 2005. This represents a compound annual average rate of decline of 7.9 percent.⁽¹⁾ Other North Slope fields which are currently projected to begin producing will only partially offset this decline. These projections are based only on the development of presently known and economically developable reserves. Additional discoveries may be made in the future, but their development as well as the development of some currently known but high cost reserves is highly dependent on the future growth of real oil prices. In addition, these future discoveries may be made on federal OCS lands from which the state would receive little or no revenues. Future petroleum revenues are therefore both exhaustible and highly uncertain.

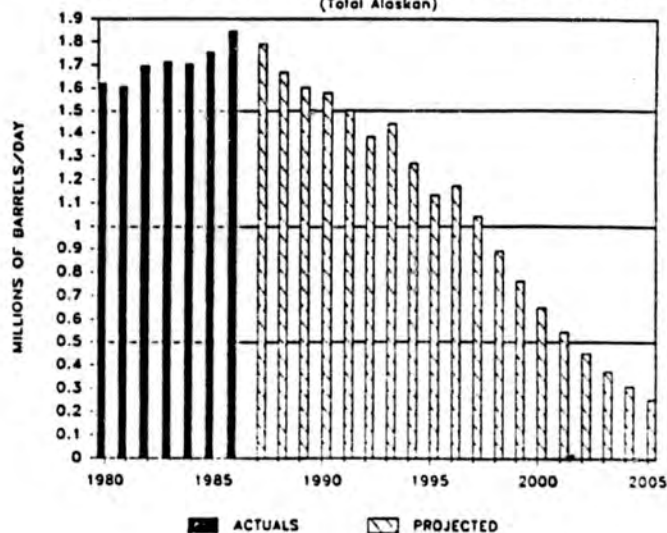
TABLE 1

PETROLEUM PRODUCTIONS PROJECTIONS
(Millions of Barrels/Day)

FISCAL YEAR	TOTAL ALASKAN
1980	1.621
1981	1.609
1982	1.696
1983	1.714
1984	1.704
1985	1.714
1986	1.840
1987	1.842
1988	1.755
1989	1.687
1990	1.520
1991	1.499
1992	1.384
1993	1.207
1994	1.057
1995	1.037
1996	1.095
1997	1.182
1998	1.020
1999	0.895
2000	0.775
2001	0.674
2002	0.593
2003	0.513
2004	0.450
2005	0.384

FIGURE 1

PETROLEUM PRODUCTION PROJECTIONS
(Total Alaskan)



Alaska North Slope oil prices, meanwhile, have dropped from a high in 1981 of \$33.67 per barrel to a 1987 low of \$8.50 (the average is projected to be \$12.59 for the year). These prices have become extremely volatile and difficult to predict. Even if production wasn't declining, this volatility in oil prices and riskiness of oil related revenues could undermine the major source of revenue for this state. To a large extent, this has already happened.

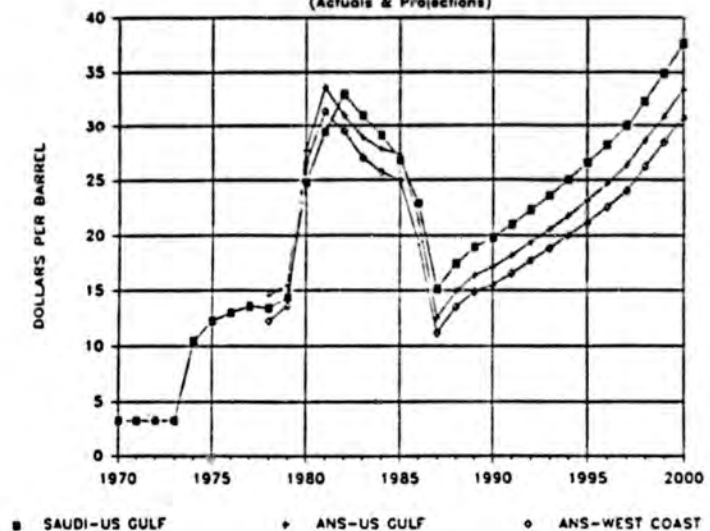
TABLE 2

ACTUAL & PROJECTED CRUDE OIL PRICES
(Dollars per Barrel)

FISCAL YEAR	SAUDI US GULF	ANS US GULF	ANS WEST COAST
1970	3.25		
1971	3.25		
1972	3.25		
1973	3.25		
1974	10.45		
1975	12.30		
1976	13.04		
1977	13.61		
1978	13.46	14.60	12.30
1979	14.41	15.50	13.70
1980	24.75	27.60	26.50
1981	29.45	33.67	21.43
1982	22.99	21.07	29.50
1983	21.05	20.87	27.00
1984	29.10	27.82	25.68
1985	26.80	27.35	24.92
1986	22.90	21.20	19.76
1987	15.15	12.59	11.19
1988	17.39	14.97	13.57
1989	10.95	16.29	14.90
1990	19.77	17.10	15.52
1991	20.76	18.16	16.52
1992	22.21	19.27	17.70
1993	23.62	20.52	18.02
1994	25.03	21.09	19.02
1995	26.55	21.18	21.29
1996	28.10	24.67	22.57
1997	29.92	26.20	24.01
1998	27.76	28.60	26.18
1999	24.91	20.95	20.46
2000	27.62	23.45	20.07

FIGURE 2

CRUDE OIL PRICES
(Actuals & Projections)



The purpose of this study is to develop a model that will allow us to evaluate the revenue potential and burden of general sales tax proposals presented by Legislative and Executive policy makers. We have presented alternative structures here primarily for illustrative purposes, and in no way wish to suggest these are proposals of this Department or section. The value of these alternatives is comparative, illustrating the way different structural elements in a tax can be altered to obtain various results, and to show what scope of information it is possible to generate in response to a proposal. We have evaluated the advantages and disadvantages, as well as preliminary estimates of fiscal impact, for each of our illustrative general sales tax alternatives in order to suggest what kinds of questions could be asked about various proposals.

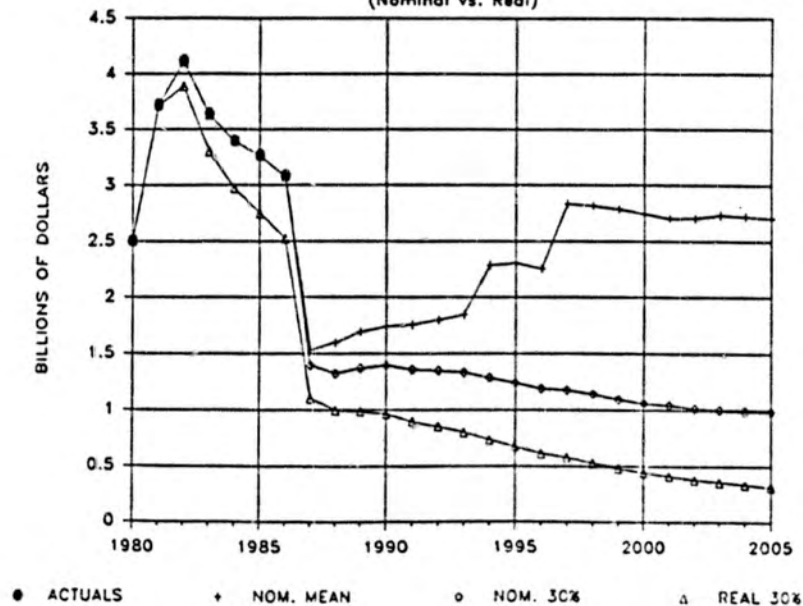
It should be noted at the outset, that it will be practically impossible to replace petroleum revenues with taxes on individuals or other industrial sectors given the present structure of the Alaskan economy. In fiscal year 1984 the gross wellhead value of North Slope oil production was approximately \$10.6 billion⁽²⁾ while the estimated gross production of all other nongovernmental industrial sectors was only \$8.7 billion and total disposable personal income was \$6.8 billion. In addition, oil production has been high profit sector and thus supported much higher levels of taxation than other more marginal industrial sectors. Also, many other industries are currently supported, directly and indirectly through state government spending of oil revenues.

TABLE 3
GENERAL FUND UNRESTRICTED REVENUE PROJECTIONS
(Nominal vs. Real)

FISCAL YEAR	ACTUALS	ESTIMATES MEAN CASE (NOMINAL \$)	ESTIMATES 30 % CASE (NOMINAL \$)	ESTIMATES 30 % CASE (REAL \$/1981)
1980	2.501			
1981	3.710			3.710
1982	4.108			3.891
1983	3.631			3.290
1984	3.390			2.968
1985	3.260			2.746
1986	3.076			2.523
1987		1.535	1.399	1.105
1988		1.601	1.325	1.000
1989		1.697	1.374	0.992
1990		1.748	1.398	0.965
1991		1.763	1.359	0.897
1992		1.802	1.349	0.851
1993		1.851	1.334	0.800
1994		2.290	1.287	0.733
1995		2.307	1.241	0.672
1996		2.254	1.191	0.613
1997		2.830	1.178	0.576
1998		2.810	1.143	0.550
1999		2.779	1.098	0.483
2000		2.738	1.063	0.444
2001		2.698	1.045	0.414
2002		2.699	1.020	0.383
2003		2.730	1.004	0.358
2004		2.718	0.997	0.337
2005		2.699	0.909	0.217

FIGURE 3

GENERAL FUND UNRESTRICTED REVENUES
(Nominal vs. Real)



TAX CAPACITY AND TAX BURDEN ON ALASKANS

The assessment of the burden of taxation is a complicated problem. Statutes determine who is legally responsible for a tax. In contrast the economic incidence of a tax is the change in the distribution of private real income brought about by a tax. Different taxes can be shifted to differing extents from the person or business legally responsible to other individuals or businesses.

In less rigorous terms, concepts such as burden are examined by resorting to state-by-state comparisons of taxes paid usually on a per capita basis or in relation to some measure of revenue capacity. Because measures such as per capita income are poor measures of revenue capacity alternative concepts have been developed. One such measure involves the concept of a representative tax system (RTS).⁽³⁾

"The RTS is designed to answer this question: what would be the total revenue of each of the 50 states if every state applied identical tax rates - national averages - to each of 26 commonly used tax bases?"

Tax effort is a companion concept that indicates the overall tax burden placed on the base as defined by the tax capacity concept. A tax effort index is created by dividing the state's actual tax collections by its estimated tax capacity and multiplying by 100.

"The result may be interpreted as a measure of how much a state chooses to exploit all its potential tax bases relative to other states. If a state has a tax effort beneath the national norm, it will have an effort index under 100. Conversely, if a state has a tax effort in excess of the national average, it will have an effort index over 100."

The most current estimates of these ratios is in an Advisory Commission on Intergovernmental Relations publication Tax Capacity of the 50 States. Dated May 1985, the book is based on tax data for 1982. While aged, the numbers are indicative of Alaska's state and local tax burden relative to other states.⁽⁴⁾

Indexes of this sort can often hide subtleties in the underlying relationships. For instance the effort variables are developed using per capita measures which hide the fact that a substantial portion of the tax may be paid by out-of-state visitors or seasonal workers. Alaska, for instance, shows a high effort for hunting and fishing licenses. Although care has to be exercised in their interpretation, the figures indicate that Alaska residents are taxed at relatively low levels on income and sales when compared to residents of other states.

Overall Alaska shows a high tax effort because of our resource based taxes. However, effort measures are considerably below national norms for several major taxes commonly found in other states. Column two below shows the relative importance of major taxes and column three shows Alaska's effort index for these taxes.

<u>Tax</u>	<u>State-Local Tax Collections as % of U.S. Total</u>	<u>Alaska Effort Index 1982</u>
General Sales	23.5%	29.1
Selected Sales	11.7%	102.0
License Taxes	3.5%	118.0
Individual Income	19.7%	.7
Corporate Income	5.6%	95.0
Property	31.8%	105.0
Estate and Gift	.9%	22.9
Severance	3.4%	278.8

GENERAL DESCRIPTION AND STRUCTURE OF RETAIL SALES TAXES

General Sales Tax

A general sales tax could be enacted at the State level. Alaska currently has no sales tax at the State level, however seven boroughs and at least fifty-two smaller municipalities do levy some form of sales tax. The rates levied range from one percent to five percent. The base upon which these rates are levied also varies with different exemptions being allowed in various communities. If a sales tax were enacted at the State level it would be in addition to the tax at the local level, however, it should be noted that Anchorage and Fairbanks, the two most populous municipalities in the State currently have no sales tax.

Currently forty-five of the fifty states levy some form of sales tax at the state level. Sales taxes are a significant source of state government revenues in most of the states which levy them. Sales taxes account for 48.8 percent of all State tax collections. The sales tax base varies considerably as to exemptions allowed and the degree to which services are taxed from one state to another. Food purchases, except restaurant meals and alcohol, are exempt in twenty-eight of the forty-five states. Prescription drug purchases are exempt in forty-three states. Gas and electric utility bills are exempt to some degree in thirty-two states. Five states exempt clothing purchases to some degree. Also, four states allow some credit for sales taxes paid against state income tax liability. These various exemptions and credits are meant to ameliorate the regressive incidence of the sales tax.

Services are taxed very comprehensively including all personal and professional services in only three states. Twenty-five states either tax no services or tax services very narrowly and selectively such as laundry and cleaning or advertising and selected business services. The remaining seventeen states tax services to a considerable degree although not comprehensively with most exempting professional services.

The rates levied on taxable purchases of goods and services also varies considerably from state to state with a low of three percent to a high of seven and one half percent. The median rate levied by states which exempt food is five percent and by those which do not exempt food is four percent.

Retail sales taxes tax consumer expenditure, thereby taxing income at its use, in contrast to income taxes, which taxes income at its source. The basic elements of any tax structure apply to the retail sales tax. These are tax base, rate(s) and credits against tax owed.

Tax Base

Tax base is characterized by what is included, excluded, and deductible from the base. It is also affected by the presence of exemptions from the tax.

Retail sales are the primary base of state and local sales taxes. Sales for resale generally are excluded to avoid problems of multiple taxation. While a general retail sales tax can logically cover services, in most cases services are excluded. Thus, a substantial portion of consumer expenditure is not taxed. A few services are, however, included in the tax bases of some states. These include admissions, lodging and public utility services.

Equity considerations lead some state to exclude particular retail sales from the tax base. The most common exclusions are prescription drugs and food for consumption at home. Some taxing states allow non resident visitors to obtain exemption certificates for sales tax. All sales tax states have use taxes as part of their sales tax structure. These use provisions apply to goods bought outside the state and brought into the state for consumption.

Tax Rates

Tax rates are applied to the tax base. They can be separated into rate groups for various consumer goods. This can be done to help make the tax more equitable, (i. e. taxing goods more highly that are consumed by higher income taxpayers (luxuries and non health services) or taxing subsistence items (basic food purchases, children's clothing or utilities) at low rates or not at all . The tax rate can also be applied differentially for other social policy goals, i. e. to tax goods with high social cost associated with them, such as alcohol, at higher rates, or to tax goods associated with low tax capacity at low rates or not at all, eg. medications and health services.

Tax Credits

Tax credits against tax owed are deducted after the rate is applied to the tax base. Tax credits are available for special expenditures and can be effective in avoiding penalties for or encouraging those qualifying expenditures. Credits can also be used to offset amounts paid to other government; thereby preventing double taxation of the same transactions.

EVALUATION OF ALTERNATIVES

The tables presented in this report summarize only the projected quantitative impacts of two sales tax proposals. Other issues do arise, however. Each of the elements of the tax structure can be tailored to affect different taxpayers differently (or to try and affect them identically). The alternative tax structures we present will each be analyzed briefly on a number of issues including how they affect taxpayer groups, how easily administered they are and how politically palatable they might be.

In general, the issues which should be considered with respect to measures to increase revenues are as follows.

Economic Efficiency: What effect does the proposed tax have on incentives and economic decision making? How does the tax alter consumption, production or resource allocation decisions?

Equity: Who bears the burden of the tax and how does that burden compare with ability to pay or benefits received? Is the tax progressive or regressive with respect to income and/or wealth?

Elasticity: What is the sensitivity of the tax revenue yield to changes in economic or demographic conditions? As income or population increase or decrease, does tax revenue increase or decrease in greater, lesser or equal proportion?

Administrative Efficiency: How costly is the tax to administer in terms of resources devoted to administration and compliance relative to the revenue yield of the tax? Who bears the burden of administrative cost, the taxpayer, the State or the tax collector (if different from the State)?

Political Feasibility: How acceptable is the proposed tax to the legislature and/or the electorate given existing social, political, and economic conditions? Who benefits, who loses, and who has the most political power?

Additionally, we are concerned with three other issues.

Interstate Capture: How much of the tax owed by nonresident taxpayers who work or travel in Alaska is it possible to capture?

Intergovernmental Effects: Does the tax erode the tax base of higher level (federal) or lower level (local) governments? If such erosion should be mitigated, how can it be done? Do higher level or lower level government taxes erode the State tax base? If such erosion should be mitigated, how can it be done?

Inflation Effects: What is the effect of inflation on the elements of the tax structure and the burden on the taxpayer? If this should be mitigated, how can it be done?