

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672
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COWPER ADMINISTRATION - BUDGET TRANSITION TEAM
BUDGET TRANSITION REPORT
ALASKA DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

OVERVIEW OF DCED OPERATING BUDGET

	<u>FY 86 ACT</u>	<u>FY 87 REV</u>	<u>FY 88 SFL *</u>	<u>FY 88 PRO</u>
Commissioner/Admin Services	1,838.3	1,880.4	1,465.5	
Measurement Standards	2,090.7	2,125.5	2,122.5	
Banking, Securities & Cor	1,280.4	1,287.0	1,234.6	
Insurance	1,052.7	964.7	888.3	
Occupational Licensing	1,747.0	1,877.8	1,856.6	
Retirement Incentive Prog	0.0	0.0	138.6	
AK Transportation Commission	8.2	0.0	0.0	
AK Public Utilities Comm	4,052.7	3,564.2	3,731.2	
Real Estate Commission	456.9	546.8	546.8	
Oil and Gas Conservation	1,846.3	1,613.9	1,580.7	
Alaska Power Authority	25,882.8	23,544.2	20,626.8	
Economic Development Advo	3,031.5	2,656.3	2,466.8	
Investments	1,268.8	1,349.6	1,349.6	
Accounting and Collection	1,544.5	1,834.5	1,834.5	
Fish Enhancement Tax Rece	3,186.6	4,435.3	3,284.0	
Tourism	6,599.8	6,312.2	8,200.0	
AIDA	1,187.8	1,714.4	1,868.3	
AK Seafood Marketing Inst	3,601.4	3,132.7	3,132.7	
TOTAL	60,686.5	58,839.5	56,438.7	

* Sheffield Proposed FY 88

KEY BUDGET ISSUES CONFRONTING DCED

Alaska Power Authority

Power Cost Equalization

Description: The Power Cost Equalization program represents the largest operating budget expenditure made within the APA's budget as well as the operating budget of the entire Department. This program should be reviewed in depth to determine if it is effectively meeting its intended purpose and whether changes can be made to the structure of the program to improve its effectiveness and to reduce the program's cost to the State.

Discussion: The Power Cost Equalization program is based on a formula which averages the price paid per kilowatt hour in Juneau, Anchorage and Fairbanks. This average rate is then made available to participating rural communities through State subsidies.

This program may not have had the result that was originally intended. While the program has led to the electrification of several rural communities it may have also promoted the inefficient use of more power with no consideration given to the use of conservation measures. Since no cap exists on how much electric energy will be subsidized for each household the demand for electric power at the current rates becomes almost limitless. In addition, since local utility costs, for the most part, will be subsidized through the program there is little incentive for the local utilities to generate and distribute power in a cost effective manner.

and economic means of distributing power throughout the region. Others contend that neither intertie enhancement project is, at present, economic and therefore the REF should be used for other projects.

Regarding the construction of Bradley Lake, many utilities feel that it is a good project and that it should probably be constructed. However there is no concensus of opinion that the project construction and operation should be managed by the AFA. Some utilities have suggested that a portion of the REF be used to complete the financing of the Bradley Lake project. Still others have suggested that the entire REF be appropriated to the Alaska Electric Generation and Transmission (AEG&T), the only recognized Railbelt generation and transmission entity presently recognized by the APUC, and place them in charge of the Bradley Lake project as well as the intertie enhancement projects.

Recommendation: The issues discussed above are complex ones. There exists no unanimous opinion on what action should be taken. In the past the Railbelt utilities have had a difficult time agreeing on many issues, but many utilities feel that by making them responsible for the REF and for planning to meet the future energy needs of the Railbelt a successful organization of these utilities can result.

The long term existence of the APA should be closely examined with the perspective that, at least in the Railbelt, the utilities stand ready to begin planning and developing the energy future for their ratepayers. Strong consideration should be given to placing the Railbelt utilities in charge of the Bradley Lake project and the Railbelt Energy Fund. In addition, the other functions now performed within APA should be moved into a Division of Energy which should be located in the Department of Commerce and Economic Development.

Other APA Programs

Description: In spite of the criticism that APA has received over the recent past, there are several functions performed by the APA which are viewed as important to Alaskan residents. These functions, to the extent possible, should still be provided by the State regardless of the future for the APA.

Discussion: The Alaska Power Authority was formed to provide some key functions in developing electric energy resources within Alaska. Among the functions provided by APA, the following is brief list of some that are often mentioned by utilities as ones they would not wish to lose if APA were eliminated;

1. The APA serves as financing vehicle which has the full faith and credit of the State of Alaska behind it. This can result in significantly better financing arrangements for power projects than would otherwise be available to Alaskan utilities if they were forced to obtain financing for projects entirely on their own.

2. The APA has been providing valuable technical advice to rural communities who are developing their own power generation facilities.
3. The APA has traditionally provided energy planning assistance in Alaska.

Recommendation: These functions, currently provided by the APA, should be strongly considered for inclusion in a Division of Energy contained within the Department of Commerce and Economic Development.

Accounting and Collections / Investments

Description: One of the one-time revenue options proposed in the first section of the Budget Transition Report was for the State to divest itself of its present loan programs. Two of the organizations who are chiefly responsible for these portfolios are the Division of Accounting and Collections and Division Investments which are both contained in the Department of Commerce and Economic Development.

Discussion: If the Governor chooses to raise one-time revenue for the State by divesting the various loan programs which are managed by the Department of Commerce and Economic Development, then there will not be a need for either the Division of Investments or the Division of Accounting and Collections. However, other options may exist to reduce the operating expenses associated with these two divisions.

One option which may be considered is to stop making any additional loans in these loan programs but continue to service the loans and continue to receive the income generated by these loan portfolios. Under this scenario, the Division of Investments would no longer be needed since no new loans were being made, but the Division of Accounting and Collections would be required to continue to service these loan portfolios.

Another option may be, in addition to closing the loan programs down in terms of making new loans, contract out to a financial institution to service the loan portfolio. This second option may have additional merit considering the relatively good condition of the financial records for these loan portfolios and that the state's financial institutions are currently eager to find ways to generate additional cash flow.

Recommendation: Further action regarding the budget of these two divisions should be predicated on a decision by the Governor to begin divestiture of the loan programs managed by the Department of Commerce and Economic Development. There appear to be potential savings which can accrue to the General Fund under any of the scenarios described above. The Cowper Administration should give close consideration regarding the future existence of these organizations in light of the current State revenue picture.

Tourism / Economic Development Advocates / AK Seafood Marketing Institute

Description: As discussed by Governor Cowper throughout his campaign, the future of Alaska is dependent on further economic development and diversification. The above organizations have as their primary function to promote the economic development of the State. Given this perspective it will be important to provide additional support to these organizations even in times of low revenues in order to stimulate future economic development opportunities.

Discussion: One common complaint about these types of organizations is that it is difficult to determine how effective they have really been in stimulating the economy. It is very important that these organizations be held responsible for meeting their goals and objectives. In order to measure the productivity of these organizations, measurable objectives must be established and be used regularly to evaluate performance of the program. It is very important that the performance measurements not be based on how many applications were received or amounts of paper processed, but rather on how successful they were in stimulating new business (i.e., new sales arrangements with Pacific Rim countries, seminars presented on dealing with foreign countries, etc.).

Recommendation: In light of the need for further economic development and diversification in Alaska, now is not the time to cut the budgets of the State organizations which are responsible to help stimulate new business. The budgets of the economic development advocates should be reviewed to see if a further injection of money could have real benefits to the economy. All State organizations who have similar economic stimulation functions should be consolidated under the Economic Development Advocates section in DCED. Finally, these organizations should establish measurable objectives against which their performance can be judged, and the measurements should be evaluated regularly.

Alaska Industrial Development Authority

Description: As described in the text associated with the committee's suggestions for possible revenue generation options, the Governor may want to consider moving the liquid assets of AIDA into the General Fund and asking the legislature to appropriate the earnings from AIDA assets back to the General Fund.

Discussion: AIDA has \$ 162.0 million in unencumbered assets held in short term government securities which can be moved into the General fund through a variety of approaches which are discussed in the section of this report on possible revenue options. AIDA can also provide an annual income to the General Fund of \$ 18.8 million on earnings from its current portfolio.

Recommendation: The Governor should look closely at the revenue opportunities presented by AIDA. These actions will require legislative cooperation and should be done only after careful consideration has been given to the role that AIDA should play in developing the economic future of Alaska.

12. The state cannot afford to implement the new procurement code this year. Legislation should be proposed to defer and/or amend the procurement code passed last year to reduce implementation costs.
13. Additional funding is necessary for catastrophic losses because the state is self-insured to higher levels than in the past. A self insurance fund for payment of losses should be established, or legislation should be passed allowing the administration to use the budget reserve fund for extraordinary losses.
14. While the Supreme Court has ruled that the public defender and public advocacy offices cannot be administered by the court system, the general fund budget for these offices should be transferred to the court system, which would then bear the costs of these offices through RSA to the department.
15. The Alaska Public Broadcasting Commission should examine the feasibility of providing public broadcast services statewide from a small number of broadcast origination sites, including the feasibility of a single statewide public radio and single statewide television station rebroadcast at all existing public broadcasting sites.
16. The telecommunications divisions should continue to consolidate audio and data circuits statewide to minimize costs of communications.
17. The RATNET entertainment channel should be eliminated.
18. Public service programs currently housed in the department should be transferred to more appropriate agencies. The longevity bonus program and other senior programs should be transferred to health and social services; public broadcasting to education; and public offices to elections.
19. There should be a greater degree of coordination between the division of finance and the department of revenue's treasury functions.
20. Additional work is necessary in the division of finance to ensure that the state has an accurate picture of its financial status at all times. Greater coordination between the state accounting system and departmental accounting systems, particularly those in the department of transportation and public facilities, is essential.
21. In keeping with its statutory mandate, the department needs to take a more active role in ensuring that the staff of other agencies have the necessary training to use the new statewide accounting system and that microcomputer systems are being used effectively. Constant attention should be paid to the relative merits of microcomputer systems versus mainframe systems.

Department of Revenue

The subcommittee did not review the department's activities in depth. However, preliminary budget and fiscal analysis leads us to the following recommendations:

1. The permanent fund dividend program is charged for costs of staff who administer the program. The size of this staff and the appropriateness of all charges against the dividend program should be examined.
2. The tax audit staff is critical to state collections of tax revenues. The department should examine the audit division to determine if procedures and staffing levels are appropriate.

**Budget Transition Team
Subcommittee on General Government**

Brian Rogers, Chairman
Richard Fineberg
Robert Poe

Department of Administration

The subcommittee did not review the department's far-reaching activities in depth. However, preliminary budget analysis leads us to the following recommendations:

1. Six collective bargaining contracts expire by the end of FY87. Additional funding may be necessary to hire additional skilled negotiators for what is likely to be a difficult bargaining process.
2. Per diem entitlements should be revised to pay for meals only on the last day of state travel. This revision must be negotiated for all collective bargaining units. Total savings should reach \$1 million annually.
3. State travel policies should be revised to ensure that all frequent flier bonuses accrued for state-paid travel benefit the state. Negotiations may be necessary with the major Alaskan airlines to achieve these benefits, which could reach in excess of \$1 million annually.
4. The classification study should be implemented as soon as possible to avoid future litigation and costs. Changes in pay for affected employees should be implemented at the same time as any general pay reductions.
5. Geographic differential changes should be implemented with collective bargaining units during the current negotiations.
6. TRS Match funding should be eliminated in the state budget; costs of the entire non-employee share should be transferred to school districts and the University.
7. The state Supplemental Benefits System should be revised in legislation which would decrease the state payment by any amounts required by federal law to be paid for Social Security or Medicare.
8. The FY88 budget for all state agencies should reflect anticipated savings in PERS and TRS employer costs based on actions by the retirement systems boards in January 1987.
9. The state cannot afford to operate the Juneau Pioneers' Home. Construction contracts should be cancelled; even with damages paid to affected companies, the state will save money.
10. A major revision to the state's payroll computer system is needed. A search for an appropriate software package should start immediately.
11. Appropriations for leasing of state facilities are insufficient for FY87; a supplemental appropriation will be necessary. The department should actively work toward a reduction of leased space as contracts expire. Departmental needs for leased space should decrease as budgets decline and layoffs continue. The department should attempt to negotiate lease cost reductions with current contractors.

3. Collections functions of state agencies should be consolidated in the department.
4. Licensing functions of state government should be considered for consolidation in the department to allow greater coordination of licenses and permits and to reduce both costs to the state and time demands on the individuals/companies being licensed.
5. The trust functions of the Permanent Fund Corporation and those of the PERS and TRS systems, the mental health trust, and the university trust are similar. Consideration should be given to merging all the trust investing functions of the state under the Permanent Fund Corporation, with policies set for investment of PERS and TRS funds by the appropriate retirement system boards.
6. With appropriate safeguards, confidential petroleum industry data necessary for use in projecting state revenues must be available for use by certain legislators and governor's office staff. Additionally, the department should take steps to ensure that the maximum amount of non-confidential information on Prudhoe Bay economics is available to all for scrutiny. As noted elsewhere in this transition report, changes are needed in the revenue forecasting system.
7. Annual revenues of the Alaska Industrial Development Authority and the Alaska Housing Finance Corporation should be deposited in the general fund, becoming available for appropriation by the legislature.

Department of Law, Governor's Office

The subcommittee did not review these offices in depth. Based on information available, we recommend:

1. The department of law should review the costs and benefits of major criminal cases which involve significant costs to the state. It should be a general policy that supplemental appropriations will not be available for the criminal division to encourage the division to prioritize cases on both policy and budget grounds.
2. The governor and legislature should consider revisions to the presumptive sentencing law, and should consider allowing plea-bargaining in appropriate cases to reduce costs throughout the criminal justice system. Increased use of pre-trial diversion and suspended imposition of sentences will also decrease costs of the justice system.
3. To save state employee time, increase effectiveness, and promote better public information, the governor's office should play a lead role in establishing clear, comprehensive and compatible budget accounting, and revenue reporting systems.

**Budget Transition Team
Subcommittee on Public Protection**

Department of Public Safety

1. Contract negotiations with the Public Safety Employees Association begin immediately. The state should seek significant concessions from this high-cost employee group.
2. The department should consolidate divisions to reduce the number of division directors and deputy directors. The Records and Identification unit should be consolidated in Anchorage.
3. Fish and Wildlife Protection employees should be hired on a seasonal basis for many functions, reducing personnel costs significantly.
4. Greater efforts should be made to put uniformed troopers in the field, transferring clerical and other office functions to civilian employees who require less professional training.
5. The governor should consider transferring domestic violence programs from public safety to health and social services.
6. The department should be given statutory authority to increase fees for motor vehicles, criminal history records, crime laboratory functions, security guard applications, and fire safety inspections. As noted above, inspection functions of several departments should be consolidated.
7. State troopers currently providing principal police functions in organized municipalities, such as Anchorage's Hillside area, should be laid off or transferred to other posts. Municipal governments with police powers should assume these functions.
8. The state should actively work to coordinate dispatch efforts with local governments wherever possible to save costs.
9. The Commission on the Administration of Justice should be abolished.
10. Administrative overhead costs on the Village Public Safety Officer contracts should be reduced. VPSOs should assume additional public protection functions in villages, including inspection functions of various departments.
11. Administration costs of the Police Academy should be reduced.

**Budget Transition Team
Subcommittee on Public Protection**

Senator John Sackett, Chairman
Brian Rogers

Department of Labor

The subcommittee did not conduct an in-depth review of the Department of Labor budget. Based on a brief review, we offer the following recommendations:

1. Costs of administration of the Second Injury Fund should be borne by the fund, rather than by the general fund. This requires a statutory change to return to the pre-1981 method of funding these administrative costs.
2. The department should review fees for inspection services (such as mechanical inspection) and should revise fees to more adequately cover costs of these services. The department should work with other departments which conduct inspections (public safety, transportation and public facilities, environmental conservation, etc.) to consolidate functions.
3. The Youth Employment Service (YES) should be examined in conjunction with youth programs in other state agencies to determine which programs are of highest priority to the state.
4. The department should examine methods of funding workers compensation administration from non-state sources, including a premium tax on workers compensation insurance.
5. The functions of the Governor's Commission on Employment of the Handicapped may be appropriately handled by the Commissioner of Labor and staff.
6. The state demographic functions performed by the Research and Analysis section should be more heavily used by other state agencies in planning and budgeting. The governor should consider moving the Research and Analysis section, or at least the state demographer, to the Office of Management and Budget policy office.

Department of Military and Veterans Affairs

1. The department may not be able to afford opening of the Kotzebue Armory.
2. There may be savings in retirement benefits for the Alaska National Guard due to new PERS rates likely to be adopted by the PERS Board in January.

3. Cost of hold harmless for non-need based programs.

Both Longevity Bonus recipients and Permanent Fund Dividend recipients are held harmless. As the new administration reviews the continuation of all non-needs based programs, it needs to examine this policy.

4. Facilities not in use.

Two youth corrections facilities (Bethel and Fairbanks) have been constructed but not opened, while the Nome facility has been converted to a day program only. The fate of these facilities needs to be examined.

5. Consolidation or coordination of services.

A number of programs in other agencies should be examined for potential transfer to the Department of Health and Social Services:

Youth in Detention in Dept. of Education
Schools for the Handicapped in Dept. of Education
Adult Basic Education in Dept. of Education
Employment Training Grants in Department of Education
Vocational Rehabilitation in Dept. of Education
Environmental Health in Dept. of Environmental Conservation
Senior Citizen's Tax Relief in Dept. of Community & Regional Affairs
Renter's Equivalency Rebate in Dept. of Community & Regional Affairs
Child Care in Dept. of Community & Regional Affairs
Head Start Grants in Dept. of Community & Regional Affairs
Job Training Partnership Act in Dept. of Community & Regional Affairs
Housing Assistance in Dept. of Community & Regional Affairs
Domestic Violence & Sexual Assault in Dept. of Public Safety
Longevity Bonus in Dept. of Administration
Pioneers Homes in Dept. of Administration
Older Alaskans Commission in Dept. of Administration

Under the current structure, the State has several separate agencies responsible for direct social and educational services to people. The new administration should examine ways in which to ensure that those services are provided in a coordinated, holistic way.

This report was prepared by the Health and Social Services Subcommittee: Mary Halloran and John Sackett.

December 15, 1986

DEPARTMENT OF HEALTH & SOCIAL SERVICES
BUDGET REVIEW

BUDGET NUMBERS

FY 87 Authorized	\$345,709.4
FY87 General Fund Only	235,243.9
FY87 Revised General Fund Only	219,574.2

FISCAL ISSUES

1. Lack of flexibility.

The nature of the Department's programs makes it difficult to reach lower budget levels quickly. About half of the department's funding goes to entitlement programs, such as AFDC, while much of the balance funds institutions such as API. The major cost of the institutions is employee compensation. To reach further savings in the institutions, salary reductions and longer work weeks appear crucial, as reductions in the number of staff is not a viable option. Two options have been suggested for funding the entitlement programs: (1) prorating payments after issuing emergency regulations; or (2) seeking supplemental funding. These issues are discussed in detail in the Department's transition report.

2. Increased public assistance caseload (Supplemental request).

As noted above, the Department may be seeking a supplemental to meet rising entitlement program costs. The caseload is increasing 4 to 5% above earlier projections. The Department has yet to see outmigration of its clients -- they may be too poor to move. In addition, three other programs are in deficit spending: API, youth facilities, and foster care. The supplemental request may be more than \$4 million.

At this time, the Department is examining a return to the approach used in 1970, the instructional unit method. Any approach will have to be closely examined for equity and for final cost effects. (See also Educator Salaries, No. 2). A proposal for foundation formula revisions should be available sometime in January.

2. Educator salaries and benefits, TRS Match, and tenure provisions.

About 70% of the foundation formula goes to salaries. These costs have tripled in the last decade, and Alaska educator salary costs exceed those of every other state. The high level of the costs stems, in large part, from educator salary increases over the cost of living. School operating fund expenditures (federal, state and local dollars) have jumped from \$201 million in FY76 to \$606 million in FY84, an increase of \$405 million. According to a 1986 House Research report, in city and borough schools, the cost per student has increased sixty percent (after adjustment for inflation) from FY76 to FY84, and sixty-two percent for rural districts during the same period.

The collective bargaining process has not resulted in significant salary reductions thus far, although it may in the future. A number of approaches have been offered, based on the recognition that Alaska's K-12 educators are, in essence, state employees. One approach to educator salaries might be the implementation of a statewide salary schedule, with its provisions applying only to newly hired teachers. Another approach could be to place a limit on the use of State funds for compensation of individual positions, as proposed in legislation during the 1986 session. Another approach would be to rollback individual compensation ten percent across the board by legislative action. Every one percent rollback would result in approximately \$4.4 million in reduced costs. All these approaches would narrow the collective bargaining process, a major policy step.

Unless a reduction in teacher and administrator compensation is obtained -- and obtained in short time -- education costs will be out of control in relation to state revenues. School districts in organized cities and boroughs can presumably cope to some extent by raising local property and sales taxes. REAAs and school districts in smaller cities are limited in their tax base -- and thus constrained in their capacity to deal with the crisis.

A related issue to examine is teacher tenure, currently granted after only two years of service. Another related issue is TRS Match, a contribution annually by the state to local district and University of Alaska labor costs, and estimated at \$26 million for FY88. The TRS Board recommends that the State discontinue splitting the cost with the employer and that the employer and employee only share contributions to teacher retirement.

December 15, 1986

DEPARTMENT OF EDUCATION BUDGET REVIEW

The Public School Foundation appropriation is the largest single appropriation in the state operating budget; student loans is the largest component of the loans budget; and school debt retirement now almost equals the annual state general obligation debt appropriation. Reduced state aid to local education has brought the fiscal issues inherent in funding for public schools into sharp focus.

THE BUDGET NUMBERS

FY87 Revised Budget General Fund is as follows:¹

K-12 Support	\$423,954.7
Additional Grants	11,020.6
TRS Match	26,856.3
Department Operations	10,769.8
Dept. Operated Schools ²	6,205.5
Boards & Commissions ³	7,262.8
School Debt Retirement	129,837.3
Student Loans	54,100.0

Total	\$670,007.0
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FISCAL ISSUES

1. Education Foundation Formula

The complexity of the current formula, as well as its perceived inequities, need to be addressed. Now, the formula seems to drive district policy and program decisions. That is, districts may make decisions about which programs to offer based on the dollars which the decisions generate -- not on the needs of the students.

Equity is a fundamental consideration, both in terms of policy and for practical reasons. For example, federal funding (PL81-874 receipts) depend on the state meeting federal equalization criteria. Litigation challenging the current formula is already underway.

1. Amount is adjusted for one-time items.

2. Mt. Edgecumbe, AVTEC

3. Arts Council, Professional Teaching Practices Commission, Alaska
Student Activities Association, Postsecondary Commission

3. Fiscal accountability.

Local school districts appear to have differing degrees of fiscal sophistication. Because of legal restrictions hampering districts' efforts to reduce staff, some districts are using current fund balances to absorb this year's state funding reductions. Districts without such fund balances may face early closure or seek supplemental funds this legislative session.

It is not clear at this point how much of the 10% restriction (\$42 million in foundation formula, plus other monies) school districts will be able to handle. A related issue is the lack of comprehensiveness in budget procedures for school districts: There is no requirement that the proposed budget has to be balanced, for example. Nor are school district membership counts audited, although these counts are the basis for distribution of over \$400 million in general funds. Department-level capability to assist districts with fiscal management is limited.

4. Arbitrary deadlines.

Two deadlines drastically affect districts' ability to cope with funding problems: first, the districts must notify teachers of pending layoffs by March 15 of the preceding year. Second, districts are unable to establish their funding level until mid-fall of the school year. With funding levels falling, districts get squeezed between these two timelines. Districts need legislation allowing layoffs after March 15 of the preceding year for financial hardship. The legislation would need to define the term "financial hardship."

5. Pupil transportation costs.

Lack of appropriate data make it difficult to fund pupil transportation except in a reactive manner. More fundamentally, the policy issue remains unexamined: What is the state role in providing transportation for students? Now district contracts drive the cost, with the State simply reimbursing a portion of the cost after the fact. When sufficient data is gathered to construct a defensible equation, this cost should be moved into the foundation formula, so that local districts deal with transportation as part of their overall costs.

6. Duplicative services.- Centralized Correspondence Study

Centralized Correspondence Study provides elementary and secondary programs not only for students in isolated areas, but also to students living in urban settings. A review of the policy needs to take place: Is the program for "real" correspondence study or is it alternative schooling? If the cost of centralized correspondence study exceeds the average cost per student in regular school, should the parents pay the difference if the program is functioning as alternative schooling for their child? Or should the program simply be narrowed to only providing schooling for "real" correspondence study students?

7. Student loan program.

The policy issue is: Does the state want to stay in the loans business, particularly a subsidized non-needs based loans program? If the policy decision is to continue a student loan program, then one approach would be to establish a revenue bonding program. One investment firm has suggested issuing \$25 million in revenue bonds annually for several years to capitalize the program. For the revenue bonding approach to work, the "forgiveness" provision would have to be deleted. Another alternative would be to investigate the possibility of switching to the already-established federal student loans program. This alternative would allow the collections function for the current loans to be shifted to the Department of Revenue, reducing the overhead costs of the program and, in effect, allowing the Postsecondary Commission to be dismantled.

8. Vocational rehabilitation programs - centralization & coordination with Depts. of Labor and HSS.

As dollars become more limited, a thorough interdepartmental review should take place, aimed at providing better delivery of services by the three involved departments.

Federal "maintenance of effort" requirements for vocational education may present another fiscal problem, limiting the state's flexibility in dealing with administrative costs for vocational rehabilitation. Instead of accepting the federal mandate, perhaps the State should explore congressional action to provide Alaska and other states with more flexibility.

9. "Nice but not necessary" programs

Community Schools, RSVP, Alaska State Council on the Arts, Alaska School Activities Association, Professional Teaching Practices Commission, Alaska Career Information System, and the Blue Book -- each of these programs has its advocates and certainly its benefits. Whether they are "necessary" in times of greater fiscal restraint needs to be examined closely.

10. School debt retirement.

A consistent level of state reimbursement for local school debt needs to be determined. School districts, local governments, and the public need to know precisely who is going to pay which portion of the costs before those costs are entered into. One suggestion is that the state's obligation be limited to a specific amount of the principal, with no state dollars going towards reimbursement of the interest accumulated on the school debt. This issue needs to be considered in conjunction with the overriding issue of all debt management.

11. Division of Education Program Support.

Originally, this division primarily passed through federal funds to local districts, and performed monitoring and compliance for federal purposes. As state dollars became more plentiful, monies were added for special program grants and curriculum development. The division should be reviewed to determine the impact of returning to a fully federally funded program.

12. School district consolidation.

Alaska has a number of very small school districts with high administrative costs. The consolidation of administrative functions should be analyzed to see if districts can be combined for administrative purposes while local boards retain program control in local schools.

This report was prepared by the Education Subcommittee: Mary Halloran and John Sackett.

December 15, 1986

UNIVERSITY OF ALASKA
BUDGET REVIEW

BUDGET NUMBERS

FY87 Authorized	\$263,073.2
FY87 Revised	255,098.6

FISCAL ISSUES

1. Restructuring university statewide system.

The proposed restructuring plan is based on the recognition "that the University's administrative structure is extremely complex, extensive, and costly in relation to the size of the University and the clientele that it serves." The proposal is conceptual at this stage, with "numbers" to be worked out later. The core issue is the future role of Alaska's community colleges. By national standards only Kenai, Anchorage, Fairbanks and MatSu have a sufficient population base to maintain a strong community college. Should Alaska continue to strive to be different? And, if so, how can the community colleges be cost-effective?

2. Inability to respond quickly to fiscal problems.

The university has a long lead time for making most personnel changes. Although this policy is part of academic tradition, it leads the university into taking inappropriate measures in dealing with budget cuts. This year, for example, the university absorbed much of its budget reduction by taking one-time cuts in equipment and maintenance. It should be recognized that the university is also constrained in making rapid program changes because of legal obligations to students already in degree programs.

3. Focus on programs important to Alaska's economic future.

The university should be encouraged in its intent to focus on fisheries, international trade, arctic health, and arctic research.

4. Employee compensation and benefits.

The university should investigate the possibility of pay reductions for faculty commensurate to those taken by state agency personnel, with the national market taken into consideration. Any new salary schedule should also take into consideration the Department of Administration's geographic differential study results.

The university should proceed to implement its classification study to remove perceived inequities in its personnel system.

The full costs of TRS match should be absorbed by the university rather than supplemented by an additional appropriation.

Another angle to the employee compensation issue is the student-faculty ratio. The university teaching load is currently 9 credits per semester, versus a nationwide average of 12 credits per semester. Cost-cutting measures need to include an analysis of the appropriateness of the current teaching load versus the need for both basic and applied research.

5. Availability of information.

A frequently expressed concern among both executive and legislative staff was the vagueness of fiscal information provided by the university. The university has its own accounting system and its own personnel system, separate from those of the state. The lack of financial integration with the state system means that fiscal details are not readily available. Apparently the university does not prepare an annual financial report as required, for example. The real issue here is not who governs the university, but the public's right to know what is being purchased with state dollars. The university should be encouraged to increase its provision of detailed information on its fiscal matters.

6. Instate contracting.

State agencies currently contract for research and other services with firms outside Alaska. Some of that work could be performed in Alaska, providing training for Alaska graduate students in practical aspects of their area of study. The state needs to consider adopting a firm policy of granting a contracting priority to the university.

7. "Nice but not necessary."

The university budget funds, as do all state budgets, many programs which need to be reconsidered from the perspective of necessity: KUAC, the University Alumni Association, some cooperative extension service functions, for example.

8. Other issues.

High costs of insurance, falling interest rates, decline of federal research money, lack of sufficient funding for data processing projects already underway, the status of the statewide administration building in Fairbanks -- these and other issues need to be examined.

This report was prepared by the University Subcommittee: Mary Halloran and John Sackett.

December 15, 1986

DEPARTMENT OF CORRECTIONS
BUDGET REVIEW

BUDGET NUMBERS

FY87 Authorized	\$83,919.1
General Fund Only	82,579.6
FY87 Revised	80,631.4
General Fund Only	79,291.9

FISCAL ISSUES

1. Legal and policy changes.

The attached memorandum from the Department of Corrections identifies possible ways to reduce the cost of the corrections system, and provides cost estimates for each item. The proposals must be analyzed in light of their impact on the public, the court system and the rest of the legal system, including the Department of Public Safety.

2. Other issues.

Other issues with fiscal impact have been identified but not researched. They include: level of staffing at each institution; availability of malpractice insurance; scarcity of bed space; leasing rather than building correctional institutions. Underlying the Department's management and fiscal problems is the lack of a longterm plan. Such a plan could, for example, delineate institutions by offender groups, allowing more flexibility in supervision in some institutions.

This report was prepared by the Corrections Subcommittee: Mary Halloran and John Sackett.

MEMORANDUM

State of Alaska

TO: Mary Halloran
Budget Transition Team
Office of the Governor

THRU:

FROM: William W. Ladwig *WJ*
Acting Commissioner
Department of Corrections

DATE: December 10, 1986

FILE NO.:

TELEPHONE NO.: 465-3376

SUBJECT: Cost Implication of Law
and Policy Changes

The attached, Law and Policy Changes Under Review, was presented by the Corrections' Mini-Cabinet to Governor Sheffield for the purpose of identifying some possible ways to reduce the cost of operating the Alaska Correctional System. It was also provided to Governor Cowper's Transition Team for their consideration.

The following is our preliminary estimate, on a point-by-point basis, of the financial impact on this department should some or all of these items be brought to fruition. We cannot comment on the extent, if any, of the financial impact on other executive branch agencies.

1. ~~SAVINGS FROM CITATIONS INSTEAD OF BOOKING~~

There appears to be savings in this policy change. During November 1986, there were 595 persons statewide, who could have been served citations and released instead of being booked. Extrapolating this data for 12 months and assuming an average 8 hour hold, we could save 2,380 mandays per year at an average cost of \$74.97 per day (not including medical or statewide program costs) or \$178,400. By also enforcing the offenses of Failure to Appear and Failure to Satisfy Judgment by making them subject to citation instead of incarceration, an additional 698 mandays could be saved. This would represent an additional savings of \$51,600.

It appears that the Alaska State Troopers and the local police departments are making use of citations in such a way that they are not overburdening the Department of Corrections.

The per year statewide impact could be the saving of \$230,000 and reducing our population count by 8-9 full time persons.

2. ~~DEVELOPING A BAIL SCHEDULE~~

We cannot provide any data regarding the actual bail amounts on which people are being released around the state, only the original amount of bail set, but we do know that varying policies and rates are set by the presiding judge in each jurisdiction. In many instances, bail schedules do not exist or are flexible and judicial intervention is required so people are held until they are arraigned, assigned a Public Defender, have a bail hearing, arrange bail with the bondsman and are released.

This is an issue to be decided by the courts through the advice of the Chief Justice and Art Snowden, Administrative Director for the Court System. They are generally receptive to all suggestions.

3. Significantly increase the number of probation and parole cases.

This proposal refers to the maintenance of people on probation or parole who are doing well and no longer need supervision. If it can be determined that supervision is no longer needed, it is suggested that the court or the Parole Board be petitioned for approval of termination of supervision. Currently 665 of the 2753 probation/ paroles are on minimum supervision for an average of 5 years. If the court or Parole Board could be approached for termination after one year, considerable probation officer time in aggregate could be saved and applied to additional intensive supervision cases who could then be released from institutional custody. These 665 cases require .8 work unit hours/mo. $\times 12 = 6,384$ units per year. Intensive supervision cases requires about 120 hours per year. Thus $6,384 \div 120 = 53$ intensive supervision clients that could then be released from institutional care. Savings:

Cost of institutional care:	$53 \times \$86.33^* \times 365 =$	\$1,670,100
Cost of intensive supervision probation care:	$53 \times \$15.98 \times 365 =$	309,100
	Savings	\$1,361,000

4. Move all sentenced misdemeanants to private sector contract beds.

This would free up approximately 130 institutional beds. It is assumed that the private sector can provide these minimum security beds at a lower cost than the state though the actual cost per day is unknown.

Current average cost of 130 beds = $130 \times \$86.33^* \times 365 = \$4,096,359$
Private sector beds @ \$35.00/day $\times 130 \times 365 = \$1,660,750$ for a saving of \$2,435,609 or
Private sector beds @ \$40.00/day $\times 130 \times 365 = \$1,898,000$ for a saving of \$2,198,359

The cost variable is provided as some or all of these 130 offenders may require some treatment programming such as alcohol or substance abuse.

* This average daily cost of care includes average statewide cost of institutional care of \$74.97 plus average daily cost of medical care of \$6.02 and other statewide programs of \$5.34.

5. Reinstate the pre-trial diversion program.

There is no real savings to us with this program since the tight screening process diverts very few people and these are then likely to be picked up on probation. Thus any savings are offset by cost of misdemeanor supervision, the considerable cost of preparation of misdemeanor pre-sentence reports on all eligibles, and the cost of collection of restitution and supervision of community service work.

6. Return parole eligibility to all first felony offenders sentenced presumptively.

The impact of this is very substantial; the estimated 247 first-time felons admitted to serve presumptive sentences in FY88 will serve 990 prisoner-years, whereas if this suggestion was implemented, they would serve a total of 792; 198 fewer, with parole eligibility. Since the average cost of incarceration is \$86.33 X 365 or \$31,510 per year per offender and the average cost of probation/parole supervision is \$5.20 X 365 or \$1898 per offender year, there is an average savings of \$29,612 per offender year. Thus savings in FY88 could be as much as \$29,612 X 198 or \$5,863,200 if it were possible for this change to affect current population. Should this change be implemented it would take place over time. The savings per year are shown here to show the magnitude that could be achieved.

7. Amend Title 33 to allow placement of felons in contract housing at the discretion of the Department of Corrections.

There are currently 427 felons classified as minimum custody and 74 classified as community custody or a total of 501 felons who could be eligible for placement in contract beds. The savings:

501 inmates X \$31,510/year in institutions	=	\$15,786,500
501 inmates X \$17,611 /year		
specialized contract beds	=	8,823,200
Saving		\$ 6,963,300

** Currently paying \$48.25 per day for specialized CRC beds

8. Amend Title 33 to permit placement of some "violent" offenders in restitution centers.

There are currently 240 inmates classified as minimum or community custody serving sentences for sexual offenses and other violent crimes.

Cost of institutional care: 240 X \$31,510/year	=	\$7,562,400
Cost of specialized CRC beds: 240 X \$17,611/year	=	4,226,600
Savings		\$3,335,800

9. Replace the five-member Parole Board with a Parole Commission of three full-time professionally qualified members.

The many legal and policy changes suggested will greatly effect the work load of the Parole Board. Cost implications for the Parole Board are dependent upon which, if any, of these items are implemented. It is quite possible that their cost of operation will be increased.

10. Permit mandatory releasees with probation sentences to serve the mandatory release and probation time concurrently.

Current population will serve 6 months mandatory release parole plus 3 years' probation. The above change in the statutes would reduce this period of supervision from a total of 3.5 years to 3.0 years. The savings could be: 2500 clients X .5 years X \$1,898/year (at an average cost of \$5.20 per day) or \$2,372,500 over three years or \$790,800 per year.

11. Amend the Good Time portion of Title 33 to remove Parole Board discretion in regard to 1/3 vs. 1/4 award.

The saving from this change is in staff time, i.e., the time required for institutional Probation Officers completing screening forms for the Parole Board and Parole Board review time. The Parole Board has only exercised this discretion three times and those resulted in the persons serving approximately one month additional time.

12. Review all sentencing practices implemented since the criminal code implementation of 1980 with particular attention to judicial and prosecutorial discretion.

According to a study made during November of 1984, felons sentenced presumptively for Class A, B and C felonies were serving 29% more man-years than those who had been sentenced non-presumptively. Felons sentenced presumptively for unclassified crimes will serve 39% more man-years than those sentenced non-presumptively. At the time of this study, 368 felons were serving a total of 2,210 man-years of presumptive sentences. Had they been eligible for early release, they would serve 1,714 man-years, a difference of 496 man-years. The average FY86 cost of 496 man-years at \$31,510 per year is \$15,629,000.

13. Establish a criminal justice sentencing commission which annually balances justice system resources, i.e., police, prosecution, judiciary, corrections, defense.

The cost effect of this proposal is not known at this time.

14. Develop a fast track prosecution program for implementation as soon as possible.

We cannot estimate cost impact at this time for this item. It would allow offenders to move through the Criminal Justice System faster at least up to the point of incarceration. Financial impact here appears to be in the Department of Law and the Court System.

Mary Halloran
Page 5
December 10, 1986

15. Provide alternative to incarceration for Title 47 non-criminal bookings/detainees.

There were a total of 2,724 non-criminal bookings from 12/85 through 11/86, 66% of the statewide bookings were at Yukon-Kuskokwim and Anchorage Annex; 44% of which were at Bethel (the second highest cost institution in the state). These non-criminal bookings when costed by institution represent \$253,400 during that one year period of time, not including medical costs. Savings to the Department of Corrections would be offset by the cost of alternative care.

16. Return the 6th and "C" Correctional Center to the Municipality of Anchorage for the purpose of holding municipal offenders.

The "savings" from this is to allow the department to channel 53 staff and \$3,142.5 to other uses thereby making future budget requests for this department smaller. The distribution of these resources is detailed in our FY88 budget request in lieu of requesting "new" dollars.

The above items portray a course of action that could have substantial impact, over time, on the State's operating budget. Also, by diverting offenders to probation or less costly housing, the State will be able to avoid the necessity for capital expenditures of millions of dollars required to build new prison facilities.

None of the above can be accomplished without the full participation of the Legislature, Court System, Executive Branch and last, but not least, the public.

WWL:cc
Attachment
cc w/attachment:
Pete Jeans
Mike Maher

Law and Policy Changes Under Review:

1. Increase the use of citations in lieu of arrest for minor offenses.
2. Develop and implement a statewide bail schedule.
3. Significantly increase the number of probation and parole releases.
4. Move all sentenced misdemeanants to private sector contract beds. This would free up approximately 130 institutional beds.
5. Reinstitute the pre-trial diversion program.
6. Return parole eligibility to all first felony offenders sentenced presumptively.
7. Amend Title 33 to allow placement of felons in contract housing. (Corrections' discretion).
8. Amend Title 33, restitution center statute, to permit placement of some "violent" offenders in restitution centers.
9. Develop a Parole Commission of three full time professionally qualified members.
10. Permit mandatory releasees with probation sentences to serve the mandatory release and probation time concurrently.
11. Amend the Good Time portion of Title 33 to remove Parole Board discretion in regard to 1/3 vs. 1/4 award.
12. Review all sentencing practices implemented since the criminal code implementation of 1980, with particular attention to judicial and prosecutorial discretion.



ALASKA MINERAL TAXATION

**Compared to Taxes on
Mines in Eleven States**

**January
1982**

Prepared for the Alaska Department of Commerce and Economic Development

Office of Mineral Development

**Governor
Jay S. Hammond**

**Commissioner
Charles R. Webber**

**Director
John F. M. Sims**

**Prepared by: Whitney & Whitney, Inc.
1755 East Plumb Lane, Suite 135
Post Office Box 11647
Reno, Nevada 89510**

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PREFACE

The Alaska Mineral Taxation report is an extension of a study done for the Wisconsin Association of Manufacturers & Commerce completed in January 1981. The Wisconsin study provided an opportunity to quickly and inexpensively compare Alaska's tax structure with the tax structures of eleven other states.

Whitney & Whitney, Inc., of Reno, Nevada, who prepared the Wisconsin study, was contracted by the Office of Mineral Development to "plug" Alaska tax data into the identical computer mine models used in the Wisconsin study. While there are some qualifications necessary in evaluating the results, the study gives a reliable comparison of Alaska's present mineral taxation structure with the taxation structure of states with viable mining industries.

Section 1

INTRODUCTION

GENERAL COMMENTS

This report was prepared by Whitney & Whitney, Inc., at the request of the Office of Minerals Development, Department of Commerce & Economic Development in Alaska. The report provides a review of the mineral tax structure for the State of Alaska and a comparison of that structure with eleven other mining states. Since its inception in 1977, Whitney & Whitney, Inc., has specialized in economic modeling of mining projects. Corporate studies have included the analysis of mineral policy and the effects of mineral taxation on mining company profitability in a number of different countries in different parts of the world. In the course of this work, Whitney & Whitney, Inc. developed the MINeral ECONomic ANALysis (MINECAN) Mine Project Cash Flow modeling system. The system has been licensed by Control Data's CYBERNET Timesharing System, and three country specific tax modules: South Africa, Western Canada, and the United States are available worldwide for use by resource analysts on a timesharing basis. The MINECAN System was designed specifically for modeling mining projects, has been extensively tested, and is available to experienced mine project analysts for use via timesharing. Thus, experienced analysts who may be interested in the results presented herein may use the modeling system to prepare similar analyses for other types of deposits, or different assumptions as to tax regimes.

The Office of Minerals Development requested that Whitney & Whitney, Inc., use a comparative tax study prepared for the Wisconsin Association of Manufacturers (WMC) in late 1980 as the basis for the analysis. That study, titled "Wisconsin Taxation of Metallic Mining as Compared to 10 Major Mining States," was published by the WMC in January, 1981. In the WMC study, Whitney & Whitney, Inc., used discounted cash flow mine model economic analysis to determine the effect of state tax structure on a specified deposit type and a defined range of mine sizes. The modeling methodology is described in the WMC report, and the reader should contact them for a copy if he is interested in the details of the mine models, mine model construction methods, and the underlying assumptions.

It should be noted that the models developed for the WMC report include capital and operating cost assumptions which were based on information relative to mining activity in "the lower 48" states, particularly those states included in the study. Therefore, a number of these cost assumptions do not hold true for Alaska, especially the costs of exploration and mine development. In addition, infrastructure costs have not been included since infrastructure consisting of power, roads, railroads, etc., are generally available in the lower 48 states.

The results of this study demonstrate that, based on the WMC mine models, the Alaska mineral tax structure provides a relatively attractive tax environment for mining investment. However, this conclusion should be reconsidered in light of higher exploration and development costs throughout Alaska. Suggestions for further study, including revision of the existing WMC models, are addressed in the final section of this report.

SCOPE OF WORK

In comparing the Alaska mineral tax structure with that of the eleven other states, a number of tasks were completed. These tasks are listed below and are discussed in detail in succeeding section of this report.

- Methods used and the base models developed in the WMC study were reviewed;
- The Alaska mineral tax structure was researched and the Alaska tax input was added to the existing WMC models;
- Tax input was checked and the models were run;
- Generated output included in Appendix A was analyzed;
- Comparative tax burden bar charts and mining investment tables were updated to include Alaska;
- A discussion of the study results was completed.

Section 2

BACKGROUND ON THE WMC STUDY

GENERAL DESCRIPTION

In January 1981, a report on the "Wisconsin Taxation of Metallic Mining as Compared to 10 Major Mining States" was prepared by Whitney & Whitney, Inc. for the Wisconsin Association of Manufacturers and Commerce. In the WMC study, mine models were used to provide an analysis of exploration, development and mine construction investment levels, annual sales levels, and tax revenues generated for the federal, state and local governments.

Six mine models for each site were prepared: three underground and three open pit. Three mine sizes were used: 10,000, 5,000, and 3,000 tons of ore production per day. A "base case" for each of the six models was developed which required decisions concerning deposit type and geometry, mining and milling assumptions are included in Table 1 and capital cost assumptions are listed in Table 2.

The analysis differed significantly from previous studies in that detailed inflation forecasts were incorporated and a detailed investment timing schedule was prepared for each mine model. A brief overview of study methods is included in Table 3.

WMC TAX TYPES

Since state tax is the focus of the Alaska study, a review of state tax types defined in the WMC study is necessary. State taxes used for the comparative analysis were divided into five types: (1) severance tax; (2) net proceeds tax; (3) property tax; (4) sales and use tax; and (5) state income tax. The functional definition of each of these tax types is given below.

Severance Tax

This tax is variously described as a tax on the privilege of mining and may be called a severance tax, a production tax, a mining license tax, or an occupation tax. Method of application: it may be a tax on the gross value of ore extracted; a tax on the units of ore extracted; or a tax on the gross value of production less certain allocable costs.

Net Proceeds Tax

As used in many states, this tax is a tax in lieu of property tax on ore reserves contained in the orebody being mined. It may be described as a property tax and is assessed on the basis of defined gross proceeds, or net proceeds. Method of application: the tax basis may be the net present value of future cash flows and the Hoskold formula or present value formula may be used; the tax basis may be gross proceeds (gross value of sales less certain allowable costs); the tax basis may be net proceeds (gross sales less defined costs that typically include marketing, processing, transportation to a smelter or refinery, milling costs, mining costs, and depreciation; depletion may or may not be allowed, and federal income tax may or may not be allowed). The tax is generally assessed on the defined measure of value at the property tax rate for the location.

TABLE 1 - BASIC ASSUMPTIONS FOR WMC BASE CASE MINE MODELS

DEPOSIT TYPE: A zinc-copper massive sulfide deposit.

ORE RESERVES: 10,000 TPD Mines - 102 million tons
5,000 TPD Mines - 51 million tons
3,000 TPD Mines - 30.6 million tons

MINE LIFE: 42 years with a productive life of 30 years

GRADES: 1% copper, 5% zinc, 1.1 oz. per ton silver and .029 oz. per ton gold, 0.4% lead

NET RECOVERY: Copper .7923, Zinc .6804, Silver .5816, Gold .4618, Lead .239

DISCOUNT RATE: 18%

COST ESCALATION FACTOR: 7%

ORE MINING COSTS:

10,000 TPD UG - \$16.476/ton
5,000 TPD UG - \$18.54/ton
3,000 TPD UG - \$21.92/ton

All open pit mines - \$1.165/ton

MILL SPENDING COST:

10,000 TPD UG - 11.176/ton
5,000 TPD UG - \$12.52/ton
3,000 TPD UG - \$13.152/ton

10,000 TPD OP - \$11.15/ton
5,000 TPD OP - \$12.494/ton
3,000 TPD OP - \$13.152/ton

OVERHEAD COSTS:

10,000 TPD UG - \$4.284/year
5,000 TPD UG - \$5.44/year
3,000 TPD UG - \$6.966/year

10,000 TPD OP - \$3.78/year
5,000 TPD OP - \$4.795/year
3,000 TPD OP - \$6.151/year

RECLAMATION EXPENSES:

10,000 TPD UG - \$685,000/year Start Year 12
5,000 TPD UG - \$685,000/year Start Year 12
3,000 TPD UG - \$685,000/year Start Year 11

10,000 TPD OP - \$1,370,000/year Start Year 11
5,000 TPD OP - \$1,370,000/year Start Year 11
3,000 TPD OP - \$1,370,000/year Start Year 10

ROYALTY PAYMENTS: 7% of net smelter return

STATE TAXES: Dependent on State under consideration

FEDERAL TAXES: 46%

TABLE 2 - WMC BASE CASE SELECTED CAPITAL COST ASSUMPTIONS

TOTAL EXPLORATION COST:

10,000 TPD UG - \$3.010 million
 5,000 TPD UG - \$2.733 million
 3,000 TPD UG - \$2.6 million

10,000 TPD OP - \$3.010 million
 5,000 TPD OP - \$3.010 million
 3,000 TPD OP - \$2.6 million

TOTAL DEVELOPMENT EXPENSE:

10,000 TPD UG - \$344.795 million
 5,000 TPD UG - \$259.99 million
 3,000 TPD UG - \$202.33 million

10,000 TPD OP - \$131.07 million
 5,000 TPD OP - \$ 95.79 million
 3,000 TPD OP - \$ 73.33 million

INFRASTRUCTURE INVESTMENT: None

TOTAL MINE & PLANT INVESTMENT:

10,000 TPD UG - \$681.84 million
 5,000 TPD UG - \$461.55 million
 3,000 TPD UG - \$321.93 million

10,000 TPD OP - \$588.82 million
 5,000 TPD OP - \$400.89 million
 3,000 TPD OP - \$278.08 million

REPLACEMENT EQUIPMENT:

10,000 TPD UG - \$715.47 million
 5,000 TPD UG - \$337.543 million
 3,000 TPD UG - \$327.204 million

10,000 TPD OP - \$1118.119 million
 5,000 TPD OP - \$693.912 million
 3,000 TPD OP - \$369.448 million

WORKING CAPITAL:

10,000 TPD UG - \$56 million/year**
 5,000 TPD UG - \$33 million/year**
 3,000 TPD UG - \$20 million/year**

10,000 TPD OP - \$41 million/year*
 5,000 TPD OP - \$12 million/year*
 3,000 TPD OP - \$15 million/year*

* Start Year 10

** Start Year 11

TABLE 3 - MINE MODELING METHODOLOGY OVERVIEW

1. Choice of States and deposit type;
2. Three underground mine models prepared;
3. Three open pit mine models prepared;
4. Six mill models prepared;
5. Smelter schedules examined;
6. Inflation and price forecasts prepared;
7. Detailed state tax analysis conducted;
8. WMC mining tax proposal reviewed;
9. All input data reviewed;
10. Total of seventy-two models run;
11. Analytical results studied.

Property Tax

As used in most states this is the tax that is assessed on real property such as equipment and buildings. It is assessed at the prevailing property tax rate. The tax basis in many states is the depreciated value.

Sales and Use Tax

Sales and use taxes are generally levied on mine supplies, and on equipment and materials. Sales and use taxes are also levied on materials and equipment used in mine construction. Use taxes are levied on equipment and supplies purchased out-of-state but used within the state. This is to eliminate tax avoidance through out-of-state purchases. Method of application: the tax base is the purchase price of the item before addition of tax which is usually a percentage rate.

State Income Tax

Income taxes are levied by most states and they often use the federal income tax base, although a different method of depreciation may be specified, and depletion may or may not be allowed. Method of application: the tax base is defined net income which is usually taxed at a percentage rate; some states have graduated tax rates. Most mining operations fall into the top bracket because the dollar volume of income may be large even though the mine may not be profitable from a "return on investment" point of view. Some states allow deduction of federal income tax before calculation of net income for state tax purposes. States may have both net proceeds taxes and net income taxes. The tax rates may be additive if the net proceeds tax is defined so that it equates to an income tax.

Historically, property taxes have provided a major source of income for states and municipalities. Special taxes have been devised for mines due to the difficulty of defining a value for an orebody. In addition, at times taxes have been applied to mining to compensate the state for depletion of a state's natural resources, without consideration of the economic benefits that the state realizes from the incremental and related economic activities generated by mining. For example, it has been estimated that in Arizona the economic activity resulting from copper mining is at least four times the value of the copper metal extracted and sold as a result of the mining activity. Another reason for imposing special taxes on mining has been to provide monies to local municipalities and state agencies to offset negative economic impacts that may result from new mine developments during the pre-production stages.

A summary of states included in the WMC report and their tax types is listed in Table 4. Alaska has been added to the summary.

TABLE 4 - SUMMARY OF STATE TAX TYPES

STATES	SEVERANCE	NET PROCEEDS	PROPERTY TAX	SALES TAX	INCOME TAX
Alaska		x	x		x
Arizona	x	Special type	x	x	x
Colorado		x	x	x	x
Idaho		2 types	x	x	x
Michigan	special type	special type	x	x	x
Minnesota	x	x	x	x	x
Missouri			x	x	x
Montana	x	x	x	x	x
New Mexico	2 types	x	see net proceeds	x	x
Tennessee		special type	x	x	x
Utah	x	x	x	x	x
Wisconsin		x	x	x	x

Section 3

ALASKA MINERAL TAX STRUCTURE

ALASKA TAX TYPES

Mining operations in Alaska are subject to three different taxes: a mining license tax, a state corporate income tax, and local property taxes. Each of these taxes is described below.

Mining License Tax

This is a special tax on mining activity in Alaska which requires that all new mine operators obtain licenses. New operations are exempt from the tax for three and one-half years after production begins (except for sand and gravel operations). (AS Sec. 43.65.010(a))

The tax is based on net income. Deductions allowed in the calculation of net income include: operating costs, royalties, depreciation, depletion, development costs, and taxes except mining license tax and federal income tax. (AS Sec. 43.65.010(c))

Depletion is a percentage of the gross income from the property during the tax year. The percentage allowed is:

Coal Mines	10%
Metal mines, fluorspar, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, ball and sagger clay, or rock asphalt mines and potash mines or deposits	15%
Sulphur Mines or Deposits (AS Sec. 43.65.010(e))	23%

The depletion allowance may not exceed 50% of the net income of the taxpayer without allowance for the depletion. (AS Sec. 43.65.010(f))

Net income is taxed at the following rates:

Over \$40,000 and not over \$50,000 - 3%
Over \$50,000 and not over \$100,000 - 5% of the excess over \$50,000 plus \$1,500
Over \$100,000 - 7% of the excess over \$100,000 plus \$4,000

The mining license tax is essentially a net proceeds tax.

Corporate Income Tax

Corporations operating in Alaska are taxed on net income derived from sources within the state. (AS Sec. 43.20.011) Net income does not include an allowance for federal income taxes. The Alaska corporate tax rates, which were recently revised, are included in Table 5.

TABLE 5 - ALASKA CORPORATION TAX RATE TABLE

Effective 1-1-78

The tax is 5.4% times taxable income (TI), plus 4% times the remainder of TI less \$50,000 i.e.

$$\text{Tax} = (5.4\% \times \text{TI}) + (4\% \times [\text{TI} - \$50,000.00]).$$

Effective 1-1-81

If TI is:	\$ 10,000 or more, but less than:	\$ 20,000 then tax is:	\$ 100 plus:	2% of TI over:	\$ 10,000
	20,000	30,000	300	3%	20,000
	30,000	40,000	600	4%	30,000
	40,000	50,000	1,000	5%	40,000
	50,000	60,000	1,500	6%	50,000
	60,000	70,000	2,100	7%	60,000
	70,000	80,000	2,800	8%	70,000
	80,000	90,000	3,600	9%	80,000
	90,000	1,000,000	4,500	9.4%	90,000
	1,000,000	4,000,000	90,040	10%	1,000,000
	4,000,000 or more	then tax is:	390,040	11%	4,000,000

Effective 1-1-82

If TI is:	\$ 0 or more, but less than:	\$10,000 then tax is:	\$ 0 plus:	1% of TI over:	\$ 0
	10,000	20,000	100	2%	10,000
	20,000	30,000	300	3%	20,000
	30,000	40,000	600	4%	30,000
	40,000	50,000	1,000	5%	40,000
	50,000	60,000	1,500	6%	50,000
	60,000	70,000	2,100	7%	60,000
	70,000	80,000	2,800	8%	70,000
	80,000	90,000	3,600	9%	80,000
	90,000 or more	then tax is:	4,500	9.4%	90,000

Source: Department of Revenue, State of Alaska

Property Tax

The state administers no general property tax but municipalities and boroughs are authorized to levy taxes on real and personal property. Property is assessed January 1st of each year at its "full and true value" which is defined as "the estimated price which the property would bring in an open market and under the prevailing market conditions in a sale between a willing seller and a willing buyer both conversant with the property and with prevailing general price levels." (AS Sec. 29.53.060)

The tax rates are fixed locally with a maximum rate of 3% for cities. The different borough and city tax rates can vary substantially from year to year.

TAX DATA INPUT

The previously defined tax information which was compiled by an outside expert for Whitney & Whitney, Inc. was adjusted to the data input format required by the mineral economic analysis (MINECAN) program used to run the WMC models.

For the purposes of this study, the mining license tax was included in the "net proceeds" tax type. The mining license tax rate of 7% was added to each WMC base case since the lower tax rates were not applicable to the levels of net income generated in each of the models. An adjustment was made for the 3½ year exemption period and a depletion rate of 15% was used. The input record for each of the models is included in Appendix A. Lines 01030 and 01032 are for the net proceeds tax.

The 1982 state corporate income tax rate of 9.4% for income exceeding \$90,000 was used in running the six Alaska models. The 1980 and 1981 tax rate schedules were not considered since there was no income reported during those years. The input records for state corporate income tax for each model are included in Appendix A, Line 01040.

A statewide conservative estimate of 3% was used to assess the effects of property tax on mining profit. These rates are set locally and will vary from year to year to meet budget needs. Mines are typically located in areas outside the cities where the lower tax rates apply. The input record for property tax is Line 01010 for each of the six models in Appendix A.

Section 4

COMPARATIVE MINERAL TAX ANALYSIS

COMPARISON OF STATE TAX BURDENS

Total taxes generated by each of the models over the project life were calculated and aggregated into three categories for presentation purposes: (1) income tax, (2) other tax which includes property and sales tax, and (3) mining specific tax which is composed of net proceeds and severance taxes. The comparative state tax burdens for each of the six mines are illustrated in Figures 1 through 6. The total amount of tax over the project life for each of the mines is summarized by state in Table 6.

Taxes in Alaska range from \$.4 billion for the 3,000 TPD open pit mine to \$2.4 billion for the 10,000 TPD underground mine. For the six models, income tax generally represents 35%-40% of the total burden. The mine license tax ranges from 20% of total taxes for the smaller mines to just over 35% for the large underground mine.

Examination of Figures 1 through 6 and Table 6 illustrates that Alaska's total tax burden is average when compared with that of other states. The total state tax burden for the life of the six mines is generally higher in Alaska than in Idaho, Michigan, Montana, New Mexico, and Tennessee. Tax burdens in Alaska are generally lower than in Arizona, Colorado, Utah and Wisconsin. Minnesota and Missouri taxes are similar to those in Alaska.

MINING INVESTMENT IN ALASKA

Measures used to assess competition for mining business among states include: tax on mining as a percent of sales; effective state tax rates; effective state and federal tax rates; and rate of return on investment. Each of these measures is discussed below.

Tax as a Percentage of Sales

States that have the lowest tax on mining as a percent of sales are deemed to be most competitive in terms of attracting mining investment. Table 7 provides a summary of mineral specific taxes as a percent of sales for each of the states studied. The most attractive state with the lowest percentage is Missouri. The next most attractive states are Minnesota and Idaho followed by Tennessee and Alaska.

Effective Rates and Taxation

Another measure of business competitiveness is the effective rate of taxation. Two measures of effective taxes are defined: (1) effective rate of total state taxes, and (2) effective rate of combined state and federal taxes. The effective tax rates as a percent of operating (book) income were calculated and are presented in Tables 8 and 9. For this study, the effective rate of state taxation in Table 8 is most important.

Alaska's effective tax rate (tax as a percent of operating income) for each of the six models ranges from 11.16% to 13.83%. At the 10,000 TPD levels, the Alaska tax system is less competitive than at the lower levels of production. For example, for the 10,000 TPD underground mine, Alaska has higher taxes than all the other states except Utah, Wis-

FIGURE 1

TOTAL STATE TAX BURDEN

(UNDERGROUND 10,000 TPD MODEL)

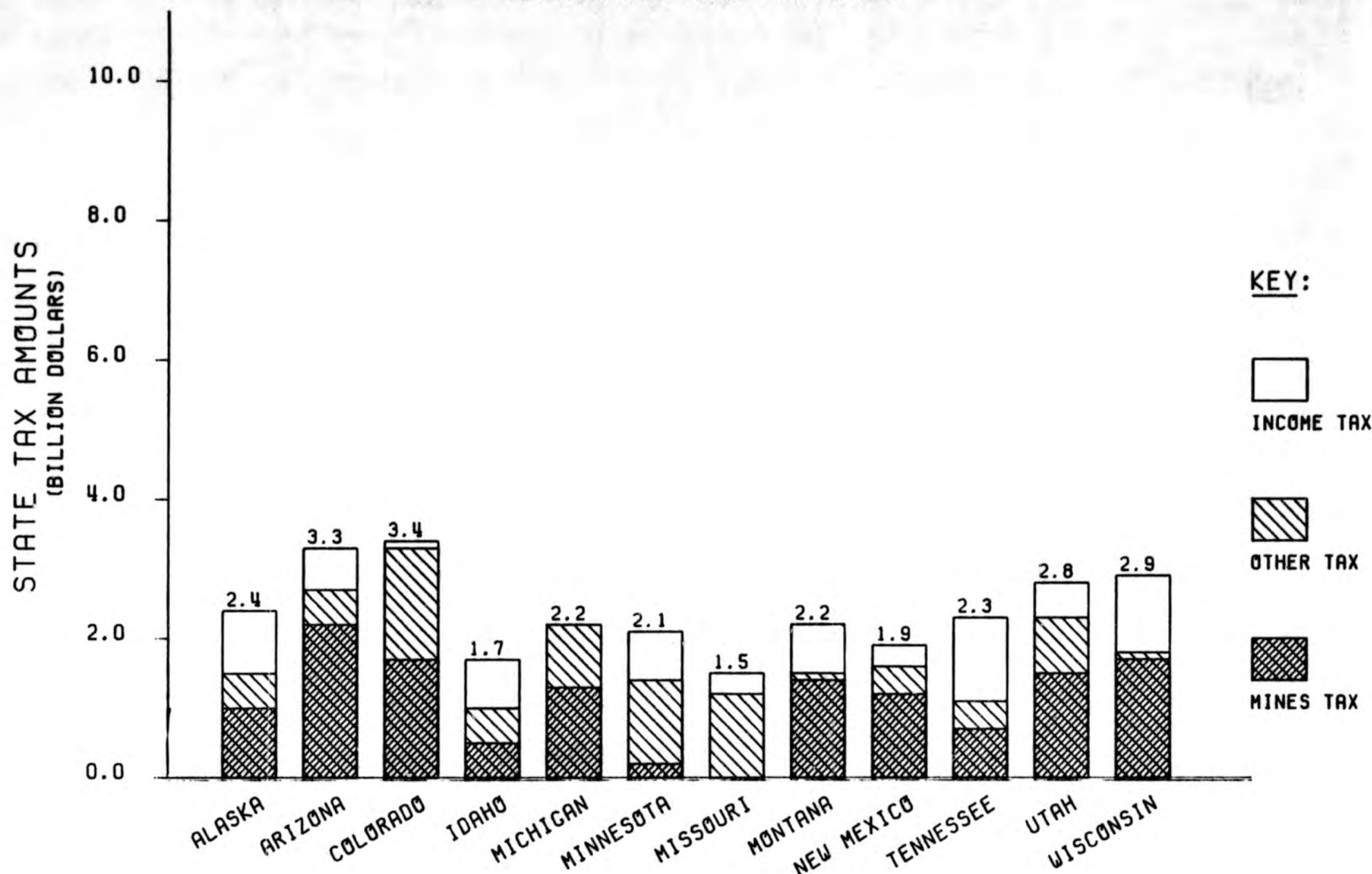


FIGURE 2

TOTAL STATE TAX BURDEN

(UNDERGROUND 5,000 TPD MODEL)

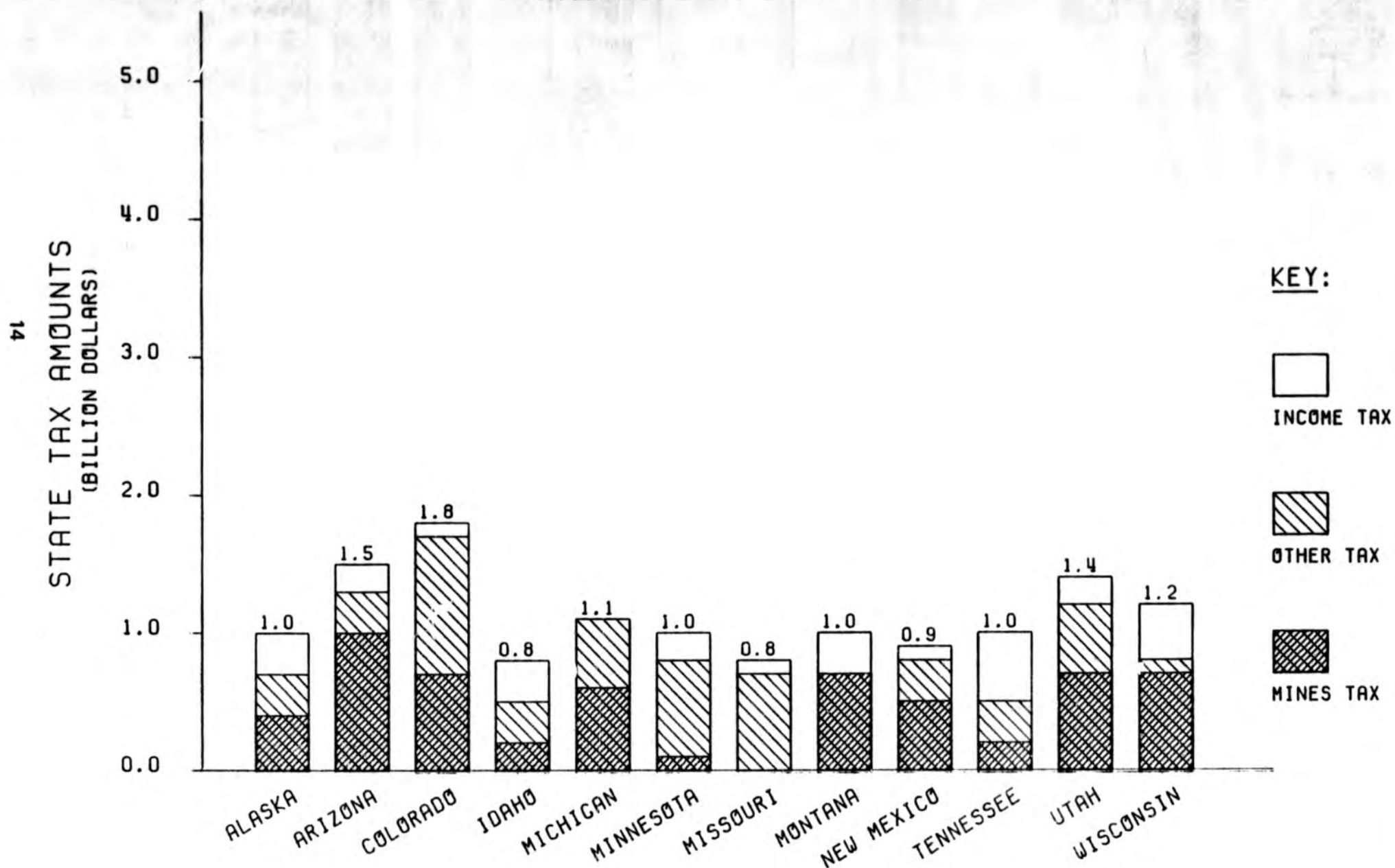


FIGURE 3

TOTAL STATE TAX BURDEN

(UNDERGROUND 3,000 TPD MODEL)

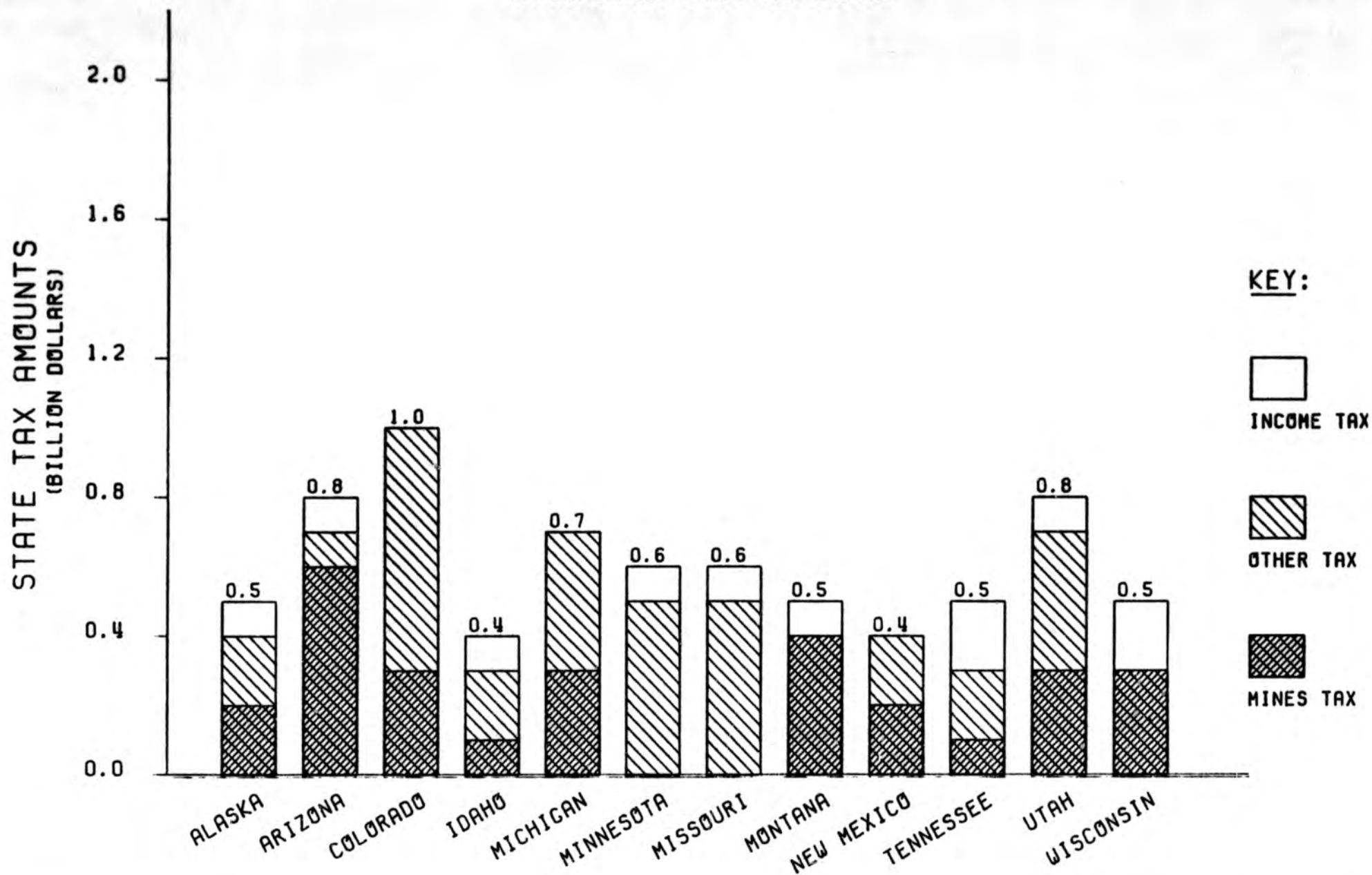


FIGURE 4

TOTAL STATE TAX BURDEN

(OPEN PIT 10,000 TPD MODEL)

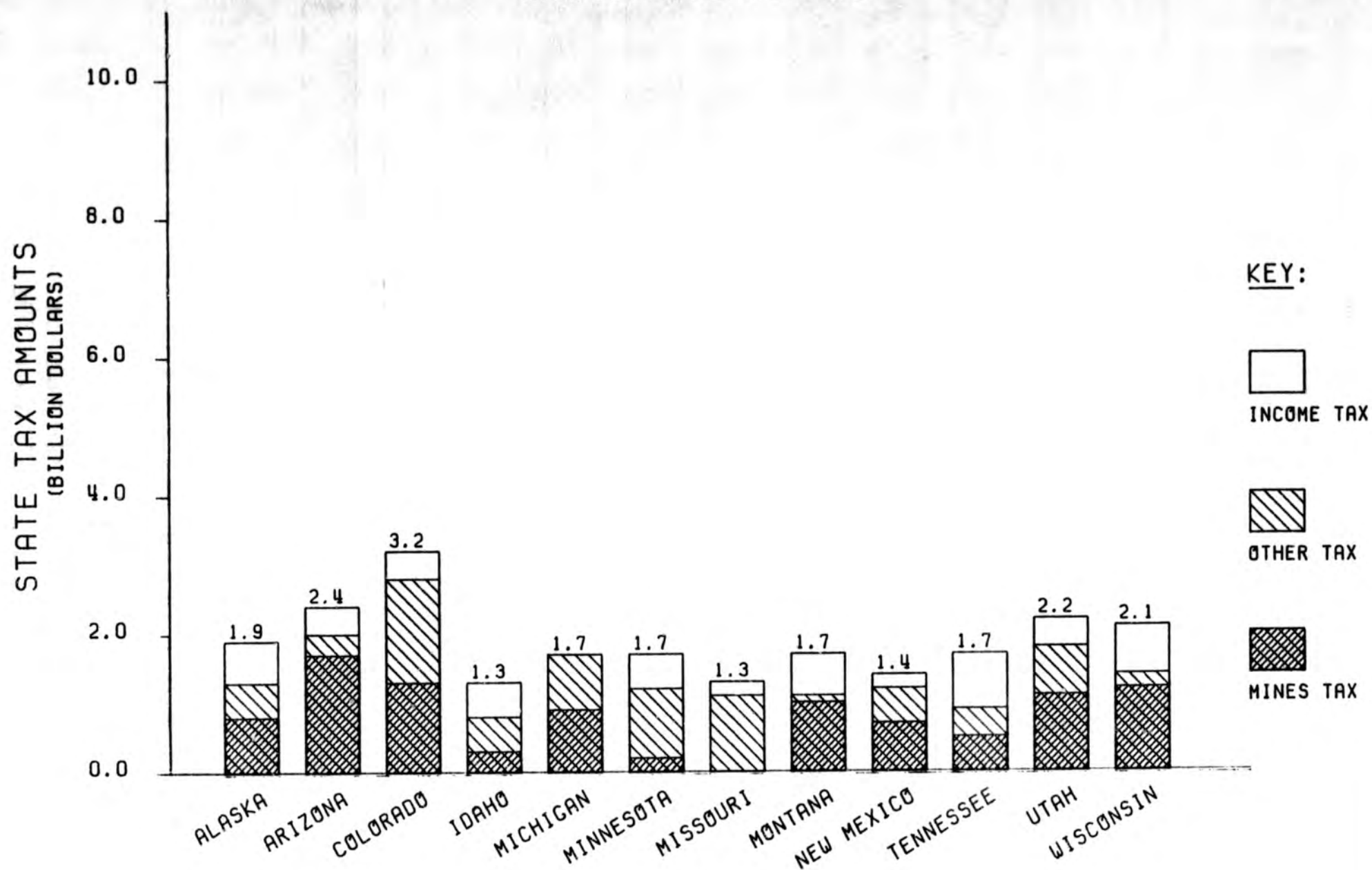


FIGURE 5

TOTAL STATE TAX BURDEN

(OPEN PIT 5,000 TPD MODEL)

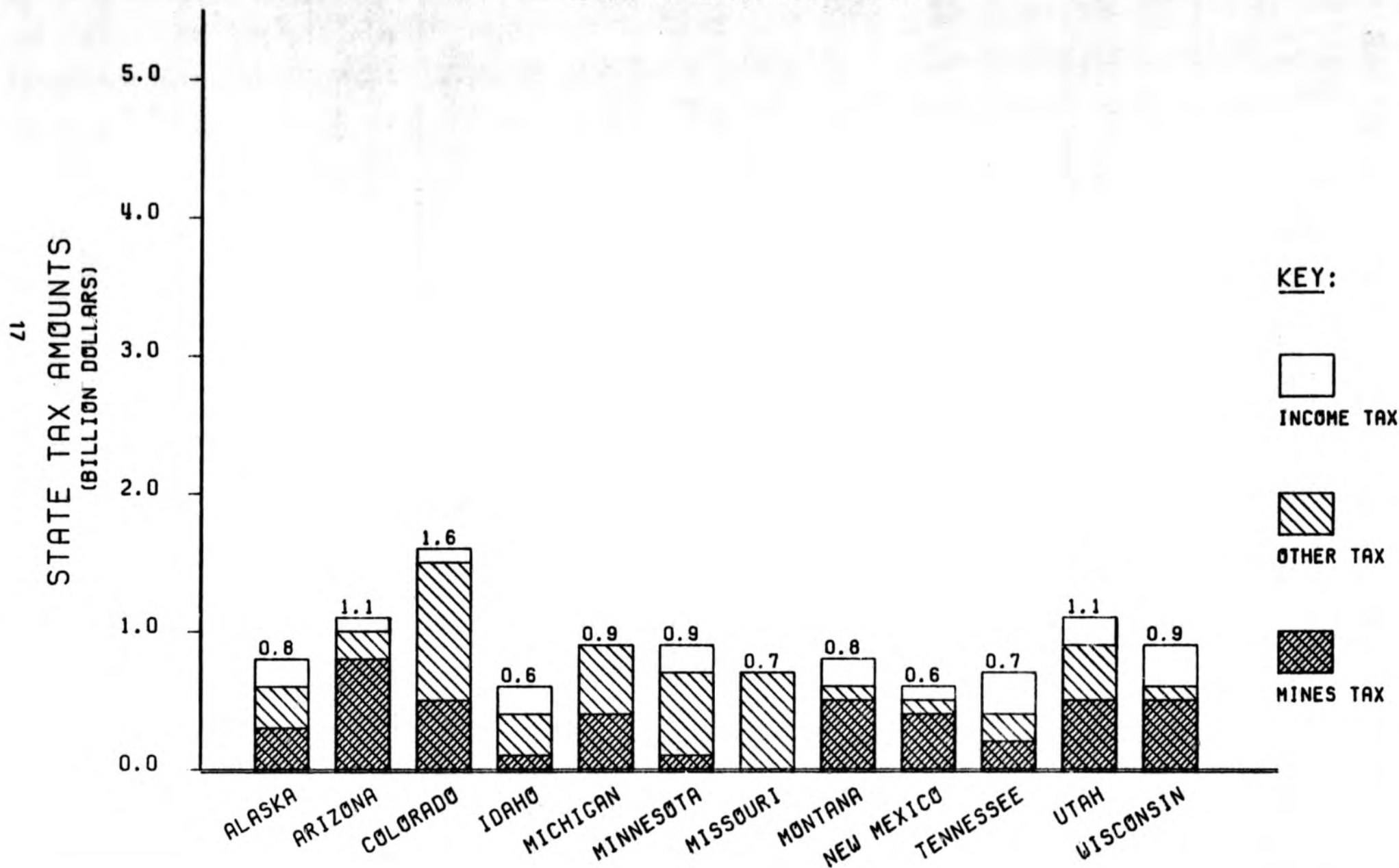


FIGURE 6

TOTAL STATE TAX BURDEN

(OPEN PIT 3,000 TPD MODEL)

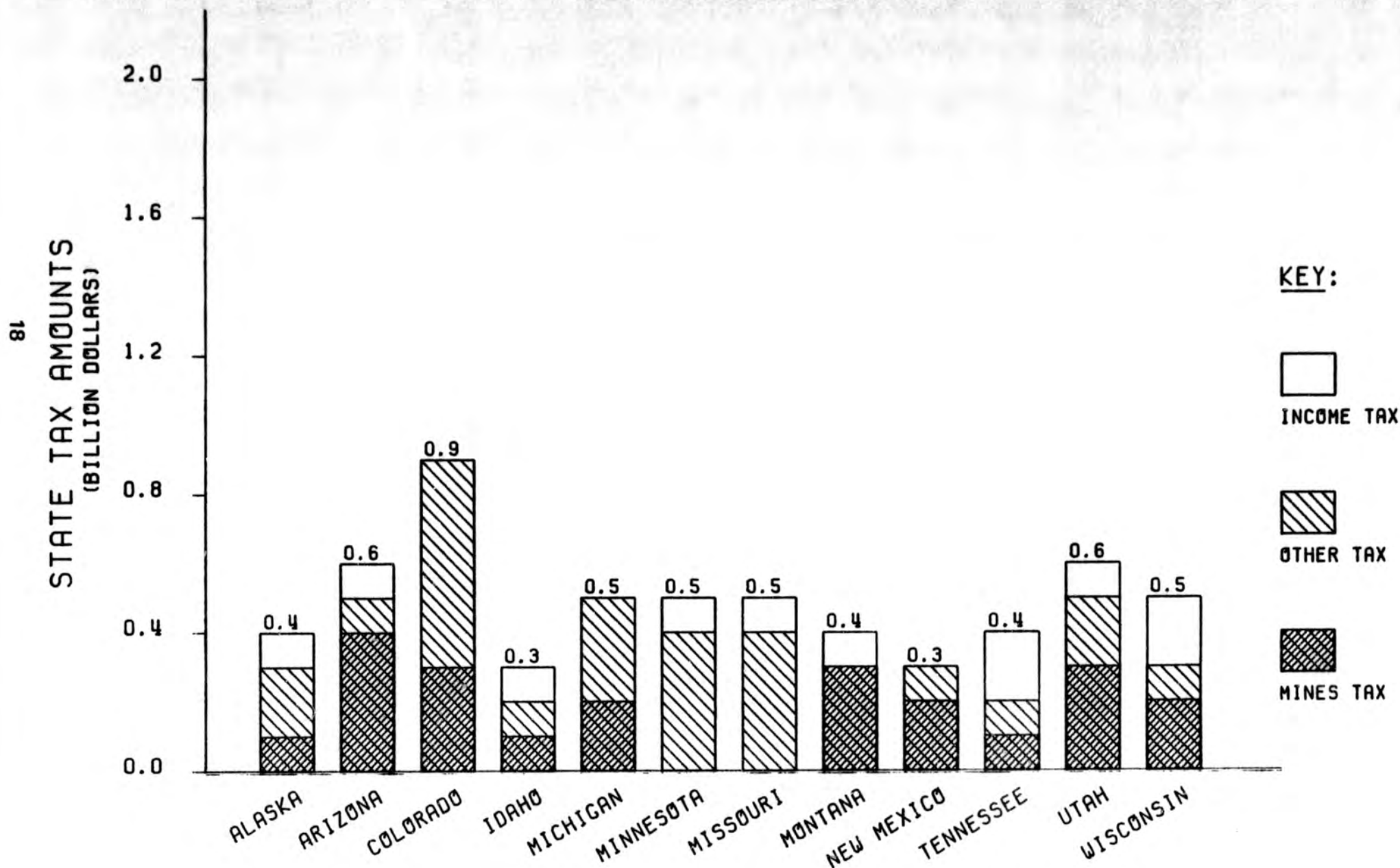


TABLE 6 - MINE LIFE TOTAL STATE TAX BURDEN (\$ BILLION)

STATE	UNDERGROUND MODELS			OPEN PIT MODELS		
	10,000	5,000	3,000	10,000	5,000	3,000
Alaska	2.4	1.0	0.5	1.9	0.8	0.4
Arizona	3.3	1.5	0.8	2.4	1.1	0.6
Colorado	3.8	1.8	1.1	3.2	1.6	0.9
Idaho	1.7	0.8	0.4	1.3	0.6	0.3
Michigan	2.2	1.1	0.7	1.7	0.9	0.5
Minnesota	2.1	1.0	0.6	1.7	0.9	0.5
Missouri	1.5	0.8	0.6	1.3	0.7	0.5
Montana	2.2	1.0	0.5	1.7	0.8	0.4
New Mexico	1.9	0.9	0.4	1.4	0.6	0.3
Tennessee	2.3	1.0	0.5	1.7	0.7	0.4
Utah	2.8	1.4	0.8	2.2	1.1	0.6
Wisconsin	2.9	1.2	0.5	2.1	0.9	0.5

TABLE 7 - STATE MINERAL SPECIFIC TAXES AS A PERCENT OF SALES

STATE	UNDERGROUND MODELS			OPEN PIT MODELS		
	10,000	5,000	3,000	10,000	5,000	3,000
Alaska	1.22	.88	.57	1.23	.93	.71
Arizona	3.15	2.96	2.96	3.25	3.05	2.95
Colorado	2.38	1.96	1.43	2.44	2.08	1.81
Idaho	.66	.50	.35	.67	.54	.45
Michigan	1.76	1.64	1.49	1.68	1.56	1.48
Minnesota	.30	.24	.17	.30	.25	.21
Missouri	.000	.000	.000	.000	.000	.000
Montana	1.97	1.94	1.89	1.97	1.94	1.92
New Mexico	1.69	1.49	1.23	1.68	1.50	1.36
Tennessee	.92	.67	.44	.94	.73	.58
Utah	2.09	1.91	1.71	2.18	2.05	1.93
Wisconsin	2.33	1.96	1.36	2.32	1.96	1.64

TABLE 8 - EFFECTIVE STATE TAX RATE*

STATE	UNDERGROUND MODELS			OPEN PIT MODELS		
	10,000	5,000	3,000	10,000	5,000	3,000
Alaska	11.16	11.32	13.85	12.01	12.47	13.63
Arizona	15.43	17.60	24.05	15.46	17.06	19.40
Colorado	17.77	21.16	31.06	20.03	23.87	29.36
Idaho	8.19	8.75	11.16	8.40	8.92	9.80
Michigan	10.26	13.07	20.22	10.60	13.12	16.34
Minnesota	9.79	11.93	18.40	10.90	13.18	16.40
Missouri	7.22	9.70	16.60	8.50	11.16	14.74
Montana	10.58	11.70	15.37	10.70	11.65	13.02
New Mexico	8.93	9.97	13.06	8.76	9.52	10.55
Tennessee	10.67	11.33	13.54	10.65	11.14	11.96
Utah	13.38	15.75	22.28	14.03	16.36	19.25
Wisconsin	13.49	14.39	15.63	13.54	14.16	14.84

*Tax as a percent of operating income

TABLE 9 - EFFECTIVE STATE AND FEDERAL TAX RATE*

STATE	UNDERGROUND MODELS			OPEN PIT MODELS		
	10,000	5,000	3,000	10,000	5,000	3,000
Alaska	33.71	30.42	29.76	34.39	31.94	30.57
Arizona	36.06	34.83	37.77	36.26	34.61	35.17
Colorado	37.61	37.16	42.33	39.11	39.48	42.13
Idaho	32.07	28.84	27.82	32.37	29.77	27.76
Michigan	33.25	31.51	34.53	33.64	32.33	32.58
Minnesota	33.01	30.87	31.64	33.84	32.45	32.55
Missouri	31.57	29.48	31.88	32.46	31.15	31.42
Montana	33.39	30.59	31.12	33.63	31.32	30.23
New Mexico	32.47	29.49	29.34	32.56	30.06	28.36
Tennessee	33.42	30.30	29.61	33.59	30.98	29.39
Utah	34.95	33.28	36.15	35.52	34.20	34.84
Wisconsin	34.94	32.32	31.20	35.16	32.68	31.58

*Tax as a percent of operating income

consin, Arizona and Colorado. However, for the 3,000 TPD underground mine, only Idaho, New Mexico and Tennessee have lower effective tax rates. This suggests that the Alaska tax structure is less regressive than a number of the other state tax systems; that is, the effective rate of state taxation is not significantly higher for the small mines than it is for the large mines. The slight regressiveness of the state tax system is shown in Table 10. Two of the three major taxes in Alaska are based on net income, so mines are only taxed when they are profitable. The combined federal and state effective tax rates for Alaska shown in Table 9 are progressive: taxes increase as the level of net income increases. This is important since when prices fall and mines become unprofitable, mines in states where taxes do not decline proportionately will be shut down sooner than mines in states where the tax burden declines as the mine's profitability declines. Thus, those states that have progressive tax structures and whose tax burdens are otherwise comparable will keep their mines in production longer under adverse conditions than those states which have regressive tax structures.

For purposes of this comparative analysis, it should be pointed out that Idaho, Missouri and Tennessee are states that are characterized by active mining industries and whose mines are typically underground mines. These states have a relatively low tax burden on mining. In the case of Idaho and Tennessee, the combined federal and state tax structure is progressive; that is, small mines are treated no less favorably than large mines.

Previous studies on the Alaska mineral tax structure report that the state mining license tax and the state corporate income tax in Alaska represent 34% of net income after depletion and taxes. Whitney & Whitney calculations using this measure resulted in a range of 32% to 34% for the six models. When local property taxes are included, the total tax revenue generated as a percent of net income ranges between 40% and 61%.

Rate of Return on Investment

The rate of return as used here is the implicit return on investment provided by the project out of cash flows generated over the project life.

Using this measure, Alaska is compared to the eleven states in the WMC study in Table 11. This table illustrates that the most attractive state in terms of rate of return is Idaho, followed by New Mexico, Montana, Tennessee, Missouri, Wisconsin and Alaska. Alaska's rates of return range from 18.9 to 10.2. This measure of business competitiveness indicates that Alaska is not as attractive in terms of return on investment as six of the other states studied. The WMC study suggests that states which provide the highest rate of return on mining are generally the states that have the most mining activity.

It has been argued that metal prices are a greater determinant of investment decisions than a specific tax regime. While that may be partially true, it should be remembered that when prices rise the comparative tax burden will remain about the same. Other things being equal, investment dollars will still flow to those areas where the best return can be obtained.

TABLE 10 - DISTRIBUTION OF TOTAL BOOK INCOME (\$ MILLION AND % OF INCOME BEFORE TAX)

	UNDERGROUND MODELS						OPEN PIT MODELS					
	10,000 TPD		5,000 TPD		3,000 TPD		10,000 TPD		5,000 TPD		3,000 TPD	
	\$ Million	%	\$ Million	%	\$ Million	%	\$ Million	%	\$ Million	%	\$ Million	%
Book Income*	21,219		8,666		3,397		15,814		6,693		3,195	
State Taxes												
Mining License	869	4	316	4	114	3	643	4	243	4	104	3
Property	456	2	281	3	212	6	479	3	292	4	197	6
State Income	1,045	5	385	4	145	5	779	5	300	5	134	4
Total State Taxes	2,370	11	982	11	471	14	1,901	12	835	13	436**	14**
Federal Income Taxes	4,785	23	1,655	19	540	16	3,539	22	1,303	19	541	17
Total Taxes	7,155	34	2,637	30	1,011	30	5,440	34	2,138	32	977	31
Income After Tax	14,064	66	6,029	70	2,386	70	10,374	66	4,555	68	2,218	69

*BI = Gross Sales - PC Charges - Royalties - Operating Expense - Depreciation

**Rounding errors

TABLE 11 - MINING INVESTMENT ATTRACTIVENESS OF 12 STATES

State	Zinc	% of U.S. Production			RATE OF RETURN (%)					
		Copper	Lead	Silver	UNDERGROUND MODELS			OPEN PIT MODELS		
					10,000 TPD	5,000 TPD	3,000 TPD	10,000 TPD	5,000 TPD	3,000 TPD
Alaska	-	-	-	-	18.6	14.3	10.2	18.9	15.9	12.1
Arizona	-	65	-	17	18.5	14.1	10.0	19.0	15.6	12.1
Colorado	-	-	3	11	16.8	12.5	8.4	16.8	13.3	10.0
Idaho	10	-	8	47	19.0	14.7	10.7	19.6	16.1	12.8
Michigan	*	2	*	-	18.3	13.9	9.7	18.7	15.2	11.8
Minnesota	*	*	*	*	18.2	13.8	9.6	18.5	15.0	11.5
Missouri	19	-	78	-	18.8	14.3	10.1	19.3	15.7	12.1
Montana	-	5	-	-	18.9	14.6	10.5	19.5	16.0	12.6
New Mexico	-	9	-	-	19.0	14.6	10.7	19.6	16.2	12.9
Tennessee	29	-	-	-	18.8	14.5	10.6	19.4	16.0	12.7
Utah	-	14	1	-	18.2	13.8	9.6	18.6	15.0	11.7
Wisconsin	*	*	*	*	18.6	14.3	10.5	19.2	15.8	12.5

Source: U.S. Bureau of Mines, **Commodity Data Summaries, 1979.**

Note a (-) indicates that the production is either not significant or that the information is not available.

A (*) indicates that there is no production.

Section 5

CONCLUSIONS AND RECOMMENDATIONS

Discounted cash flow analysis has been used to compare six different models for a zinc-copper deposit in Alaska with those same models in eleven other states including: Arizona, Colorado, Idaho, Michigan, Minnesota, Missouri, Montana, New Mexico, Tennessee, Utah, and Wisconsin. The Alaskan computer printouts generated by Whitney & Whitney's MINE-CAN program used for these analyses appear in Appendix A. The parameters used to differentiate between the six base models were: the size of the mine (large or small); and the mining method (underground or open pit). The parameter used to differentiate between the sets of models for each state was the individual states' mineral tax structure. The models used were the base cases from the WMC study and the basic assumptions used in the modeling are listed in Tables 1 and 2. Results of the analyses are summarized below.

Mining operations in Alaska are subject to three taxes: a mining license tax, a state corporate income tax, and local property taxes.

Alaska's total mineral tax burden is average compared with the eleven states in the WMC study. Measures of competitiveness among the twelve states indicate that Alaska is surpassed by approximately one-half the states in terms of its ability to attract mining investment.

Given the constraints of this study, it might be suggested that the Alaska mineral tax structure acts as neither a deterrent nor an incentive in attracting mining investment. However, one important factor must be considered. The WMC modeling effort did not include the higher costs of mining activity in Alaska which stem in part from the colder climate, the frequently remote locations of mineral deposits, and the general lack of a developed infrastructure.

Cost assumptions for the WMC study were developed for the lower 48 states using flow-sheets and standard cost estimation methods. A number of these assumptions are subject to revision when the deposit location is changed to Alaska.

Previous studies have shown that operating and capital costs of mining activities are substantially higher in Alaska than for the lower 48 states. Higher capital costs relate to the remote location of deposits and the need for construction of support facilities including power, townsites and transportation. Greater operating costs result from the higher wage rates, corresponding higher payroll costs, and the greater number of staff needed for maintenance of facilities. Property tax levels may also be higher depending on infrastructure requirements. Cost levels vary depending on the location of the deposit within the state.

Whitney & Whitney, Inc. recommends that the economic viability of mining investment in Alaska be studied further to provide a more realistic assessment of mine profitability, effective tax rates and rates of return on investment.

The optimal study would include a total of 18 models, 3 sets of 6 models. The parameter used to differentiate between the sets would be deposit location. Set 1 would be located in the southeastern part of Alaska. Set 2 would be located in the central part of the state, and Set 3 would be located in northern Alaska. Each set would include the 6 WMC models

which vary according to size and mining method. Capital and operating costs would be adjusted in each model depending on regional location. Whitney & Whitney preliminary estimates suggest that costs in southeastern Alaska range from one to two times more than costs in the lower 48 states; costs in central Alaska range from 1½ to 2½ times more than costs in the lower 48 states; and costs in the northern part of the state range from two to three times more than costs in the lower 48 states.

Results of the study would be useful to investors, businessmen, and planners at the state, borough and city levels. If the revised models indicate that mine development in Alaska is not competitive due to cost factors which are only partially controllable, then the Alaska tax system which presently seems competitive may require incentives if increased mine development is desired.

Disputed Taxes

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

POUCH S
JUNEAU, ALASKA 99811
PHONE: (907) 465-2300

January 30, 1986

The Honorable Al Adams
Chairman
House Finance Subcommittee on Oil and Gas
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Re: Expedite Collection of
Disputed Taxes

Dear Representative Adams:

A proposal has been raised in the Interim Report of the House Finance Subcommittee on Oil and Gas (January 17, 1986) to require prepayment of disputed taxes at some stage in the appeal process in order to expedite the collection of disputed taxes. We appreciate the opportunity afforded us to comment on this issue.

The Department of Revenue is concerned that the proposal will have a detrimental impact on its operations, emphasis, and ability to litigate tax challenges. Rather than expedite resolution of tax disputes, it is the Department's view that the prepayment requirement concerning disputed taxes will create delays. The adverse impact will be greater the earlier the prepayment requirement is imposed. Additionally, the prepayment proposal will affect taxpayers other than oil and gas companies if it is imposed on the corporation net income tax under AS 43.20 et. seq.

Instead, we believe the collection of disputed taxes can be expedited more successfully through approaches other than the prepayment requirement. These approaches have been recently adopted and their effect is already being felt.

In this letter, we outline the handling of disputed tax controversies by examining the assessment and appeal process, discussing the reasons for delays, and the effect the prepayment requirement may have on the various levels of the Department's appeal process.

I. The Assessment And Appeal Process

There are two levels of administrative appeal within the Department, the informal conference and the formal hearing. Appeal after the formal hearing decision is to Alaska Superior Court. The appeal process can proceed through the 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.

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

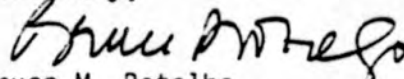
We have strong concerns that the requirement to prepay disputed taxes at some level in the review process will not expedite the resolution of disputed tax cases. Rather, we think it could impair the strategy and ability of the Department to defend its assessments and may create an adversary relationship 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,

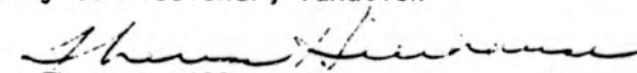
The Honorable Al Adams
January 30, 1986
Page 6

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

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.

Representative Al Adams
166-268-86

January 29, 1986
Page 3

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.

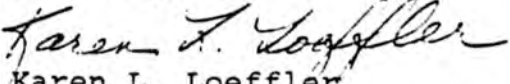
As to the first part of your question, we have found nothing that would require the state to escrow disputed tax liabilities. The federal government, for example, does not escrow the amounts it collects pending district court tax proceedings. ^{7/} Moreover, the contrary view, if applied to all tax disputes,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

File: Policy Committee
Hunt
July 24, 1986

Re: Department of Revenue
Accounts Receivable

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 CORPORATION	AS 43.55	163,313,107.90	2,390,349.13	160,921,864.21	894.56	.00
INDIVIDUAL INCOME	AS 43.20	56,079,918.77	1,285,177.53	53,560,820.38	1,093,383.91	140,536.95
FISHERIES	AS 43.20	12,937,939.83	972,441.42	3,793,773.08	7,705,312.74	466,412.59
MOTOR FUEL	AS 43.75	10,525,556.47	327,826.72	2,406,472.69	6,467,260.51	1,323,996.55
BUSINESS LIC GR RCPT	AS 43.40	3,156,188.63	41,340.60	462,445.05	2,651,510.02	892.96
MINING	AS 43.70	2,779,306.42	.00	2,313,682.53	320,952.66	144,671.23
WITHHOLDING	AS 43.65	1,990,328.47	7,653.26	1,978,935.78	3,739.43	.00
OIL & GAS PROPERTY	AS 43.20	1,730,964.17	.00	955.84	1,533,025.91	196,982.42
SEAFOOD MARKETING	AS 43.56	647,211.56	.00	.00	452,135.57	195,075.99
ALCOHOLIC BEVERAGE	AS 16.51	266,532.75	41,797.17	71,761.95	147,797.90	5,175.73
ESTATE	AS 43.60	57,095.45	3,482.08	.00	53,613.37	.00
AVERAGE WHOLESALE	AS 43.31	38,333.30	353.00	32,360.69	5,619.61	.00
CIGARETTE	AS 43.80	2,950.00	.00	1,300.00	1,650.00	.00
COIN OPERATED DEVICE	AS 43.50	2,731.61	.00	.00	2,731.61	.00
	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.

ALASKA DEPARTMENT OF REVENUE
DIVISION OF AUDIT
BRIEFING TO JOINT SPECIAL COMMITTEE ON STATE'S TAX POLICY
ANCHORAGE SEPTEMBER 11, 1986

THE APPEALS PROCESS AND DISPUTED TAX DOLLARS

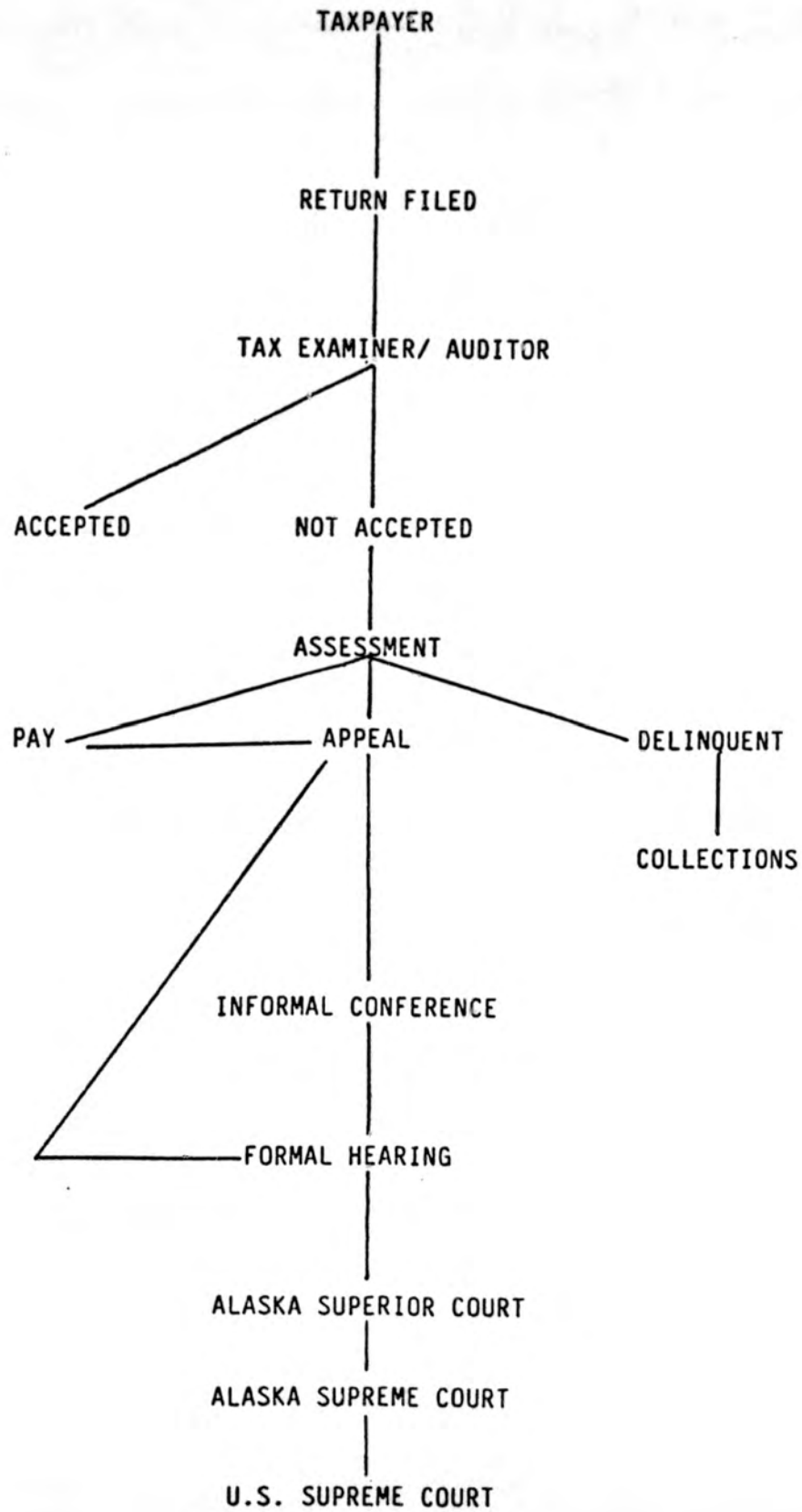
- 
1. Introduction
 2. An Overview of the Audit and Appeals Process
 3. An Overview and Explanation of the Accounts Receivable
 4. Time Frames for Resolution of Appealed Assessments
 5. Current Efforts to Resolve Outstanding Appeals
 6. Audit issues of major impact

Prepared By:

Division of Audit
September 8, 1986

DEPARTMENT OF REVENUE

APPEAL PROCESS



ALASKA DEPARTMENT OF REVENUE
TAX ACCOUNTS RECEIVABLE SUMMARY
September 8, 1986

TAX TYPE	STATUTE	VALUE OF ACCOUNTS	NOTICES OF ASSESSMENT	APPEALED	DELINQUENT AND ASSIGNED	CURRENTLY NOT COLLECTABLE
OIL & GAS CORP INC	AS 43.21	\$ 796,082,574.95	\$.00	\$ 796,082,574.95	\$.00	\$.00
OIL & GAS PRODUCTION	AS 43.55	162,364,658.57	.00	162,363,756.03	902.54	.00
CORPORATE INCOME	AS 43.20	53,228,126.63	441,076.07	50,115,569.11	2,529,105.92	142,375.53
INDIVIDUAL INCOME	AS 43.20	13,069,990.76	289,982.60	3,813,588.26	8,492,500.07	473,919.83
FISHERIES—PRE FY87	AS 43.75	9,581,615.38	9,213.91	1,561,787.27	6,678,940.56	1,331,673.64
MOTOR FUEL—PRE FY87	AS 43.40	3,163,030.85	47,170.92	469,560.47	2,644,666.77	1,632.69
BUSINESS LIC GR RCPT	AS 43.70	2,671,333.27	.00	2,245,258.35	308,545.52	117,529.40
MINING	AS 43.65	2,257,196.66	210,233.12	2,046,963.54	.00	.00
WITHHOLDING	AS 43.20	1,630,804.08	.00	.00	1,492,345.84	138,458.24
SALMON ENHAN—PRE FY87	AS 43.76	955,871.26	.00	490,542.97	382,598.01	82,730.28
OIL & GAS PROPERTY	AS 43.56	375,463.31	5,759.49	.00	173,438.04	196,265.78
SEAFOOD MARKETING	AS 16.51	200,258.68	105.35	50,429.32	144,495.15	5,228.86
ESTATE	AS 43.31	132,871.76	97,956.59	29,243.96	5,671.21	.00
ALCOHOLIC BEVERAGE	AS 43.60	57,793.31	.00	.00	57,793.31	.00
CIGARETTE	AS 43.50	2,756.53	.00	.00	2,756.53	.00
AVERAGE WHOLESALE	AS 43.80	2,300.00	.00	.00	2,300.00	.00
MOTOR FUEL - AV.	AS 43.40	2,287.00	2,287.00	.00	.00	.00
COIN OPERATED DEVICE	AS 43.35	2,126.08	.00	.00	1,986.32	139.76
SALMON ENHAN. - NSE	AS 43.76	1,492.26	.00	.00	1,492.26	.00

TOTAL TAX RECEIVABLE (A)	\$1,045,782,551.34	\$1,103,785.05	\$1,019,269,274.23	\$22,919,538.05	\$2,489,954.01
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PERCENT OF TOTAL VALUE	100.00%	0.11%	97.46%	2.19%	0.24%
PERCENT OF WORKABLE VALUE				90.20%	9.80%

TAX TYPE	STATUTE	NUMBER OF ACCOUNTS	NOTICES OF ASSESSMENT	APPEALED	DELINQUENT AND ASSIGNED	CURRENTLY NOT COLLECTABLE
INDIVIDUAL INCOME	AS 43.20	1,314	45	234	871	164
CORPORATE INCOME	AS 43.20	671	92	374	168	37
OIL & GAS PRODUCTION	AS 43.55	580	0	579	1	0
WITHHOLDING	AS 43.20	363	0	0	271	92
MOTOR FUEL—PRE FY87	AS 43.40	268	15	110	137	6
FISHERIES—PRE FY87	AS 43.75	219	1	25	139	54
BUSINESS LIC GR RCPT	AS 43.70	108	0	33	46	29
SALMON ENHAN—PRE FY87	AS 43.76	87	0	14	68	5
SEAFOOD MARKETING	AS 16.51	54	1	8	43	2
OIL & GAS CORP INC	AS 43.21	34	0	34	0	0
MINING	AS 43.65	29	15	14	0	0
OIL & GAS PROPERTY	AS 43.56	19	3	0	15	1
ALCOHOLIC BEVERAGE	AS 43.60	9	0	0	9	0
COIN OPERATED DEVICE	AS 43.35	6	0	0	4	2
ESTATE	AS 43.31	6	2	1	3	0
AVERAGE WHOLESALE	AS 43.80	2	0	0	2	0
CIGARETTE	AS 43.50	1	0	0	1	0
MOTOR FUEL - AV.	AS 43.40	1	1	0	0	0
SALMON ENHAN. - NSE	AS 43.76	1	0	0	1	0

TOTAL TAX ACCOUNTS (B)	3,772	175	1,426	1,779	392
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PERCENT OF TOTAL ACCOUNTS	100.00%	4.64%	37.80%	47.16%	10.39%
PERCENT OF WORKABLE ACCOUNTS				81.94%	18.06%

ALASKA DEPARTMENT OF REVENUE
APPEALED TAX ASSESSMENTS BY APPEAL LEVEL
 September 8, 1986

<u>TAX TYPE</u>	<u>STATUTE</u>	<u>VALUE OF ACCOUNTS</u>	<u>CONFERENCE</u>	<u>FORMAL</u>	<u>COURT</u>
OIL & GAS CORP INC	AS 43.21	\$ 796,082,574.95	\$415,735,726.42	\$380,346,848.53	\$.00
GAS PRODUCTION CORPORATION	AS 43.55	162,363,756.03	155,815,089.12	6,171,496.34	377,170.57
INDIVIDUAL	AS 43.20	50,115,569.11	32,888,824.73	9,034,818.38	8,191,926.00
BUSINESS LIC GR RCPT	AS 43.70	3,813,588.26	3,753,923.70	59,664.56	.00
MINING	AS 43.65	2,245,258.35	1,420,740.46	603,726.17	220,791.72
FISH, FREEZER SHIP	AS 43.75	2,046,963.54	2,046,963.54	.00	.00
SALMON ENHAN. - COOK	AS 43.76	1,561,787.27	1,103,109.89	454,507.73	4,169.65
MOTOR FUEL - HWY	AS 43.40	490,542.97	490,542.97	.00	.00
SEAFOOD MARKETING	AS 16.51	469,560.47	424,262.28	45,258.19	.00
ESTATE	AS 43.31	50,429.32	50,164.84	264.48	.00
		29,243.96	29,243.96	.00	.00
TOTAL TAX RECEIVABLE (A)		<u>\$1,019,269,274.23</u>	<u>\$613,758,591.91</u>	<u>\$396,716,624.38</u>	<u>\$8,794,057.94</u>
PERCENT OF TOTAL VALUE		100.00%	60.22%	38.92%	0.86%

<u>TAX TYPE</u>	<u>STATUTE</u>	<u>NUMBER OF ACCOUNTS</u>	<u>CONFERENCE</u>	<u>FORMAL</u>	<u>COURT</u>
INDIVIDUAL INCOME	AS 43.20	234	226	8	0
CORPORATE INCOME	AS 43.20	374	297	56	21
BUSINESS LIC GR RCPT	AS 43.70	33	19	12	2
FISHERIES—PRE FY87	AS 43.75	25	14	10	1
MOTOR FUEL—PRE FY87	AS 43.40	110	107	3	0
SEAFOOD MARKETING	AS 16.51	8	7	1	0
OIL & GAS CORP INC	AS 43.21	34	21	13	0
MINING	AS 43.65	14	14	0	0
ESTATE	AS 43.31	1	1	0	0
OIL & GAS PRODUCTION	AS 43.55	579	504	73	2
SALMON ENHAN. - COOK	AS 43.76	14	14	0	0
TOTAL TAX ACCOUNTS (B)		<u>1,426</u>	<u>1,224</u>	<u>176</u>	<u>26</u>
PERCENT OF TOTAL ACCOUNTS		100.00%	85.83%	12.34%	1.82%

ALASKA DEPARTMENT OF REVENUE
AGING OF APPEALED TAX ASSESSMENTS
September 8, 1986

TAX TYPE	STATUTE	VALUE OF ACCOUNTS	LESS THAN 1 YEAR	1 YEAR TO LESS THAN 2 YEARS	2 YEAR TO LESS THAN 5 YEARS	5 YEARS OR OLDER
OIL & GAS CORP INC	AS 43.21	\$ 796,082,574.95	\$275,237,156.20	\$436,778,244.98	\$ 60,039,980.49	\$24,027,193.28
OIL & GAS PRODUCTION	AS 43.55	162,363,756.03	2,413,708.33	121,859,592.48	20,741,532.20	17,348,923.02
CORPORATE INCOME	AS 43.20	50,115,569.11	3,430,983.75	18,160,728.86	19,353,962.71	9,169,893.79
INDIVIDUAL INCOME	AS 43.20	3,813,588.26	490,971.23	925,106.34	2,325,156.56	72,354.13
BUSINESS LIC GR RCPT	AS 43.70	2,245,258.35	.00	305,598.75	1,662,028.28	277,631.32
MINING	AS 43.65	2,046,963.54	1,036,507.95	411,742.76	598,712.83	.00
FISHERIES—PRE FY87	AS 43.75	1,561,787.27	906,953.25	.00	577,841.02	76,993.00
SALMON ENHAN—PRE FY87	AS 43.76	490,542.97	475,546.66	11,256.39	3,739.92	.00
MOTOR FUEL—PRE FY87	AS 43.40	469,560.47	49,396.46	374,865.82	.00	45,298.19
SEAFOOD MARKETING	AS 16.51	50,429.32	43,129.73	.00	7,299.59	.00
ESTATE	AS 43.31	29,243.96	29,243.96	.00	.00	.00
TOTAL APPEALED		\$1,019,269,274.23	\$284,113,597.52	\$578,827,136.38	\$105,310,253.60	\$51,018,286.73
PERCENT OF TOTAL VALUE		100.00%	27.87%	56.79%	10.33%	5.01%

TAX TYPE	STATUTE	VALUE OF ACCOUNTS	LESS THAN 1 YEAR	1 YEAR TO LESS THAN 2 YEARS	2 YEAR TO LESS THAN 5 YEARS	5 YEARS OR OLDER
OIL & GAS PRODUCTION	AS 43.55	579	93	8	437	41
CORPORATE INCOME	AS 43.20	374	152	41	141	40
INDIVIDUAL INCOME	AS 43.20	234	42	47	130	15
MOTOR FUEL—PRE FY87	AS 43.40	110	12	95	0	3
OIL & GAS CORP INC	AS 43.21	34	6	9	15	4
BUSINESS LIC GR RCPT	AS 43.70	33	0	12	18	3
FISHERIES—PRE FY87	AS 43.75	25	6	0	18	1
MINING	AS 43.65	14	2	2	10	0
SALMON ENHAN—PRE FY87	AS 43.76	14	4	7	3	0
SEAFOOD MARKETING	AS 16.51	8	5	0	3	0
ESTATE	AS 43.31	1	1	0	0	0
TOTAL APPEALED		1,426	323	221	775	107
PERCENT OF TOTAL ACCOUNTS		100.00%	22.65%	15.50%	54.35%	7.50%

OIL AND GAS TAXES OUTSTANDING
ON SEPTEMBER 2, 1986

INCOME TAX (CHPT. 21)	\$489,158,736
PRODUCTION TAX (CHPT. 55)	<u>94,760,523</u>
TOTAL OIL AND GAS TAXES	\$583,919,259

TAX ASSESSED WITHIN:

6 MONTHS	\$170,086,196	29.19%	
12 MONTHS	2,248,117	.37%	
18 MONTHS	6,997,314	1.19%	
24 MONTHS	335,097,693	<u>57.37%</u>	88.12%
36 MONTHS	10,722,320	1.83%	
OVER 36 MONTHS	<u>58,767,619</u>	<u>10.05%</u>	
	\$583,919,259	100.00%	

NUMBER OF ALL TAX ACCOUNTS	1,426	100.00%
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OIL & GAS ACCOUNTS:

INFORMAL CONFERENCE	525	36.81%
FORMAL HEARING	<u>86</u>	<u>6.03%</u>
TOTAL	611	42.84%

Prepared By:
Division of Audit
September 2, 1986

STATE OF ALASKA

DEPARTMENT OF REVENUE

BILL SHEFFIELD, GOVERNOR

STATE OFFICE BUILDING
POUCH SA
JUNEAU, ALASKA 99811

February 19, 1986

The Honorable Al Adams
Chairman, House Finance Committee
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Re: Time Frames From Audit Through Appeal and Estimates for
Resolution of Appealed Assessments

Dear Representative Adams:

The Division of Audit was requested to provide an outline of the period of time required to perform the audit process in a typical oil and gas case and estimates for the resolution of appealed assessments.

TIME FRAMES

Following is the outline of the process from the filing of the return through the completion of the formal hearing proceedings:

Three Year Audit Period

It has been the practice of the Division of Audit to audit every oil and gas return filed under Chapters 20, 21, and 55, with certain exceptions related to revenue materiality. Each return filed under these chapters is initially reviewed when received to determine whether an adjustment is necessary for errors or omissions apparent on the face of the return. The return is then assigned to the lead auditor of the audit team that is responsible for that particular taxpayer. Information pertaining to the return is then data captured at the direction of the audit team for analysis and eventual use for the audit of that and other taxpayers. Generally, the audit team will examine Chapter 21 and 55 returns for the same periods in tandem.

AS 43.05.260(a) prescribes a three year period for the assessment of tax following the filing of the return. The assessment of additional tax will, with only few exceptions, take place at the end of this three year period or later pursuant to an extension of the assessment period under AS

43.05.260(c)(3). This is attributable to the fact that audits must be designed to conclude within this statute of limitations period. Thus, the Division must allocate all resources to those cases that are otherwise approaching the end of the three year period. The audit depth and complexity of the issues, as well as the voluminous books and records involved in these audits, is in large part governed by the three year period. The Division requires the full three years under normal circumstances to perform a standard audit and, regardless, would utilize any otherwise available time to increase the audit scope. Therefore, in all cases the audit scope would increase rather than the audit period decrease.

As indicated previously, the Notice of Assessment will be issued approximately three years from the filing of the return. The taxpayer then has a period of 60 days in which to file a written protest to the assessment action. In many cases, taxpayers may request additional time in which to complete this filing. The case enters an appeal status with the filing of the protest.

One Year Conference Mode

An Appeals Officer is assigned the case upon conclusion of the normal processing function performed by the control unit. This may take about one month. A one year period is then required to conclude the informal conference proceedings with the issuance of the written conference decision. During this one year period, the Appeals Officer will generally correspond and meet with the taxpayer and its representatives. The function of the Appeals Officer is to review the assessment action and to receive, or further develop as the case may be, further facts, information, and argument with relevance to the matters in dispute. The taxpayer is fully afforded the right to present facts and information pertaining to each of the many audit issues and, generally, will require additional time to submit information and documentation requested by the Appeals Officer. The Appeals Officer will attempt to narrow the issues during the conference and, following a full review of all accumulated evidence and argument, will perform technical research as may be necessary to render a decision. The decision is conveyed to the taxpayer in the form of a comprehensive written report addressing each of the issues raised during the conference.

One Year Formal Hearing Mode

The taxpayer then has 30 days in which to appeal the informal conference decision to the formal hearing level of the administrative appeal process. We can generally estimate a one year period in which to complete the closing of the hearing record. It will then take about another six months for the Hearing Officer to render a written decision.

The formal hearing is equivalent to a trial court of original jurisdiction since the record must be presented at this level. Functions the Appeals Officer performs at this level include the preparation and response to motions, legal research, utilization of discovery devices, negotiation, drafting, review and critique of proposed stipulations, verification or reconciliation of factual information, negotiation with opposing counsel, and participation in pre-hearing conferences. Upon conclusion of those matters the actual hearing can be conducted. The Appeals Officer is responsible for the presentation of the audit case and will make opening and closing statements as well as conduct direct and cross examination of witnesses. A legal brief may then be required to be filed before the hearing record can close.

Six Months to Formal Hearing Decision

The Hearing Officer will then take the case under advisement following the closing of the record. The hearing officers project a six month period from the closing of the record to the issuance of the formal hearing decision. The Hearing Officer must consider the evidence presented, the arguments made by both parties, and conduct independent legal research to support the decision to be rendered.

A taxpayer has 30 days from which to appeal the formal hearing decision to Superior Court. The tax must be paid or a bond filed pursuant to the court rules at that point.

Summary

In summary, we are projecting approximately a five and one-half year period from the filing of the tax return to the completion of the administrative processes. This assumes there is no change in the overall appeal considerations nor in the staffing of Appeals Officers and Hearing Officers.

RESOLUTION OF CHAPTER 21 INCOME TAXES APPEALED

In conjunction with the time frames for finalization of tax disputes, we were asked to provide an estimate showing the time periods in which the assessed oil and gas separate accounting income taxes might be finalized. We are projecting the following:

The Honorable Al Adams
February 19, 1986
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	<u>TAX</u>
Within One and One-Half Years	1%
Within Two Years	6%
Within Two and One-Half Years	93%
Total	<u>100%</u>

The percentages shown above do not include penalty or interest but are instead intended to reflect only the amount of the tax deficiencies. The penalty and interest figures will follow the underlying tax assessment. Of the total assessed, approximately 72% entered the appeal process in the 1985 calendar year.

Cordially,



Martin J. Richard
Director of Audit

cc: Members of the House Finance Committee

86-45