

Community Forum:
How Other Cities Tax Themselves to Pay for
Public Services

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March 20, 2010

Hosted by the Anchorage Assembly's
Community and Economic Development
Committee

Outline

Part I

Anchorage's contribution to Anchorage's tax burden –
How we fit in with State and Local Taxes

Part II

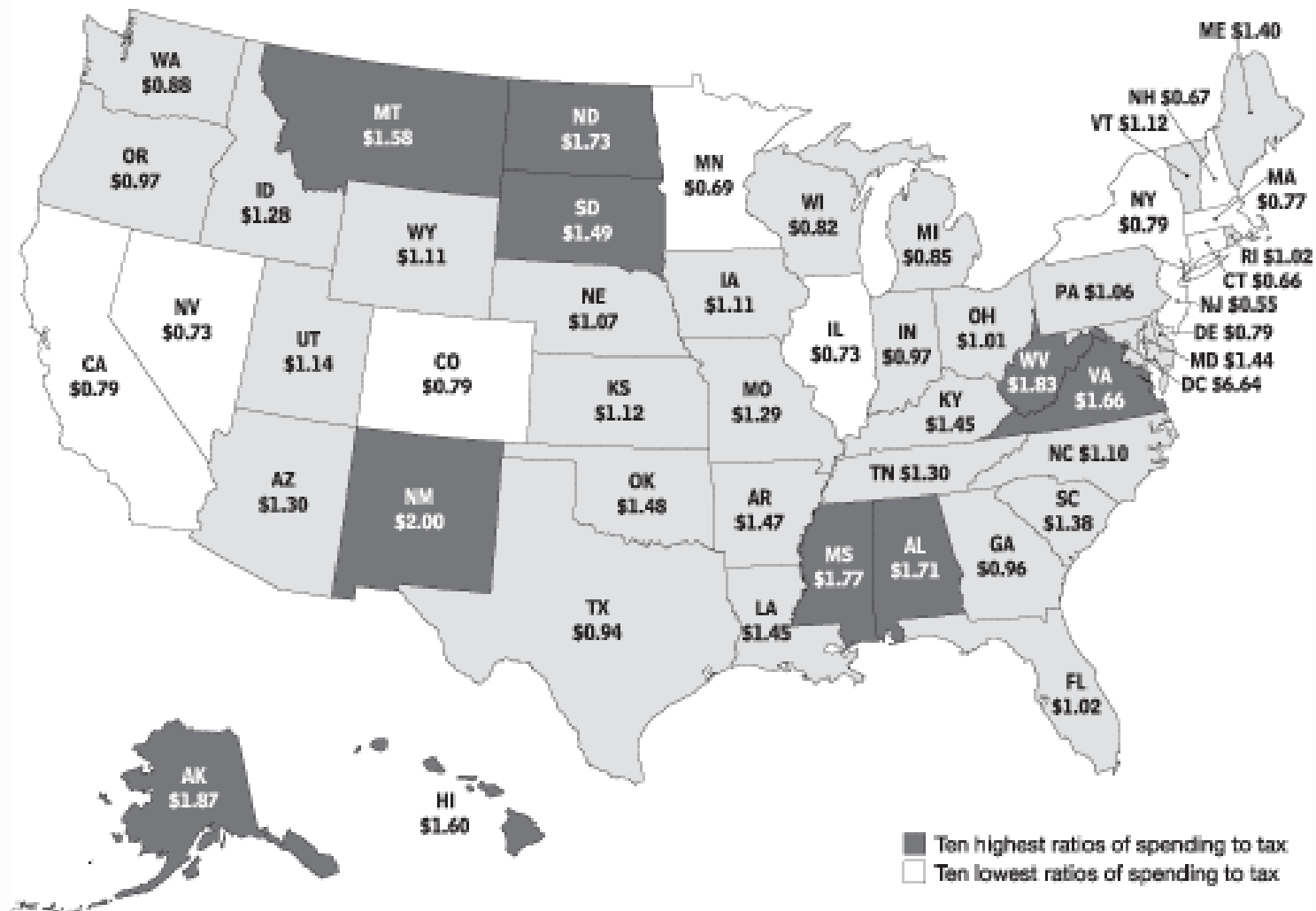
- Anchorage's Local Revenues, and is there a problem with our fiscal system?
 - 5 reasons for change.
- Is a Business Activity Tax the answer?
 - 5 reasons the BAT may be a good fit.
- Property Tax Relief Task Force: “No”
 - 5 reasons the BAT isn't a good fit.

How Heavy is Anchorage's Tax Burden?

- Anchorage Citizen's Tax Burden is composed of
- Federal, State, Local

Alaska Ranks 2nd among States (2004)

Federal Expenditures for Every Dollar of Taxes Sent to Washington



NOTE: Figures for fiscal year 2004. Source: Tax Foundation. Web: <http://taxfoundation.org>

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Where does Alaska's Tax Burden Rank?

- According to the FTA Alaska has the **highest** per capita Tax State Tax burden in the country:

- **2008 State Tax Revenue**

revised June 25, 2009

| | Total Taxes (\$ million) | Per Capita | Rank | % of Pers. Income | Rank |
|---------------|-----------------------------|---------------|----------|----------------------|----------|
| Alabama | 9,071 | 1,946 | 42 | 6.0 | 39 |
| Alaska | 8,425 | 12,276 | 1 | 30.9 | 1 |
| Arizona | 13,706 | 2,109 | 39 | 6.6 | 34 |
| Arkansas | 7,531 | 2,637 | 19 | 8.8 | 7 |
| California | 117,362 | 3,193 | 12 | 7.7 | 14 |
| Colorado | 9,625 | 1,949 | 41 | 4.8 | 48 |
| Connecticut | 13,368 | 3,818 | 5 | 7.0 | 26 |
| Delaware | 2,931 | 3,357 | 10 | 8.5 | 10 |
| Florida | 35,850 | 1,956 | 40 | 5.1 | 46 |

Source: From Federation of Tax Administrators' website taxadmin.org, (accessed March 18 2010)

Where Does Alaska's Tax Burden Rank?

- According to the US Census AK ranks between “Taxachusetts” and New Jersey in per capital state taxes:

| Rank | State | Amount |
|----------|--------------------|-----------------|
| | United States..... | 2,199.11 |
| 1 | Vermont..... | 3,600.16 |
| 2 | Hawaii..... | 3,477.93 |
| 3 | Wyoming..... | 3,417.77 |
| 4 | Connecticut..... | 3,300.49 |
| 5 | Minnesota..... | 3,093.93 |
| 6 | Delaware..... | 3,068.98 |
| 7 | Massachusetts..... | 2,818.39 |
| 8 | Alaska..... | 2,798.66 |
| 9 | New Jersey..... | 2,781.33 |
| 10 | California..... | 2,724.31 |

Where Does Alaska's Tax Burden Rank

- According to the Tax Foundation Alaska has the **lowest** per capita Tax State Tax burden in the country:

Table 1

*State and Local Tax Burden by Rank
Fiscal Year 2008*

| State | State-Local Tax Burden | Rank |
|----------------|------------------------|------|
| US average | 9.7% | — |
| New Jersey | 11.8% | 1 |
| New York | 11.7 | 2 |
| Connecticut | 11.1 | 3 |
| Maryland | 10.8 | 4 |
| Hawaii | 10.6 | 5 |
| California | 10.5% | 6 |
| Ohio | 10.4 | 7 |
| Vermont | 10.3 | 8 |
| Wisconsin | 10.2 | 9 |
| Rhode Island | 10.2 | 10 |
| Pennsylvania | 10.2% | 11 |
| Minnesota | 10.2 | 12 |
| Idaho | 10.1 | 13 |
| Arkansas | 10.0 | 14 |
| Maine | 10.0 | 15 |
| Georgia | 9.9% | 16 |
| Nebraska | 9.8 | 17 |
| Virginia | 9.8 | 18 |
| Oklahoma | 9.8 | 19 |
| North Carolina | 9.8 | 20 |
| Kansas | 9.6% | 21 |
| Utah | 9.6 | 22 |
| Massachusetts | 9.5 | 23 |
| Delaware | 9.5 | 24 |
| Kentucky | 9.4 | 25 |

| | | |
|-------------------|-------|-----|
| Oregon | 9.4% | 26 |
| Michigan | 9.4 | 27 |
| Indiana | 9.4 | 28 |
| West Virginia | 9.3 | 29 |
| Illinois | 9.3 | 30 |
| Iowa | 9.3% | 31 |
| Missouri | 9.2 | 32 |
| North Dakota | 9.2 | 33 |
| Colorado | 9.0 | 34 |
| Washington | 8.9 | 35 |
| Mississippi | 8.8% | 36 |
| South Carolina | 8.8 | 37 |
| Alabama | 8.8 | 38 |
| New Mexico | 8.8 | 39 |
| Montana | 8.8 | 40 |
| Arizona | 8.5% | 41 |
| Louisiana | 8.4 | 42 |
| Texas | 8.4 | 43 |
| Tennessee | 8.3 | 44 |
| South Dakota | 7.9 | 45 |
| New Hampshire | 7.6% | 46 |
| Florida | 7.4 | 47 |
| Wyoming | 7.0 | 48 |
| Nevada | 6.8 | 49 |
| Dist. of Columbia | 10.3% | (8) |

Source: Prante, Gerald Tax Foundation Special Report No. 163 (Aug 2008) page 2

Where Does Alaska's Tax Burden Rank?

Table 6

*State and Local Tax Collections Per Capita
Fiscal Year 2008*

| State | Total State and Local Tax Collections (per capita) | Rank | Taxes Collected from Residents (per capita) | Rank | Taxes Collected from Non-residents (per capita) | Rank |
|------------|--|------|---|------|---|------|
| US average | \$ 4,294 | — | \$ 2,924 | — | \$ 1,370 | — |
| Alabama | \$ 2,949 | 50 | \$ 1,977 | 42 | \$ 972 | 48 |
| Alaska | 7,864 | 1 | 1,433 | 50 | 6,431 | 1 |
| Arizona | 3,286 | 43 | 2,170 | 35 | 1,116 | 36 |
| Arkansas | 3,284 | 44 | 2,315 | 29 | 969 | 49 |
| California | 4,752 | 10 | 3,683 | 6 | 1,069 | 39 |

Source: Prante, Gerald Tax Foundation Special Report No. 163 (Aug 2008) page 9

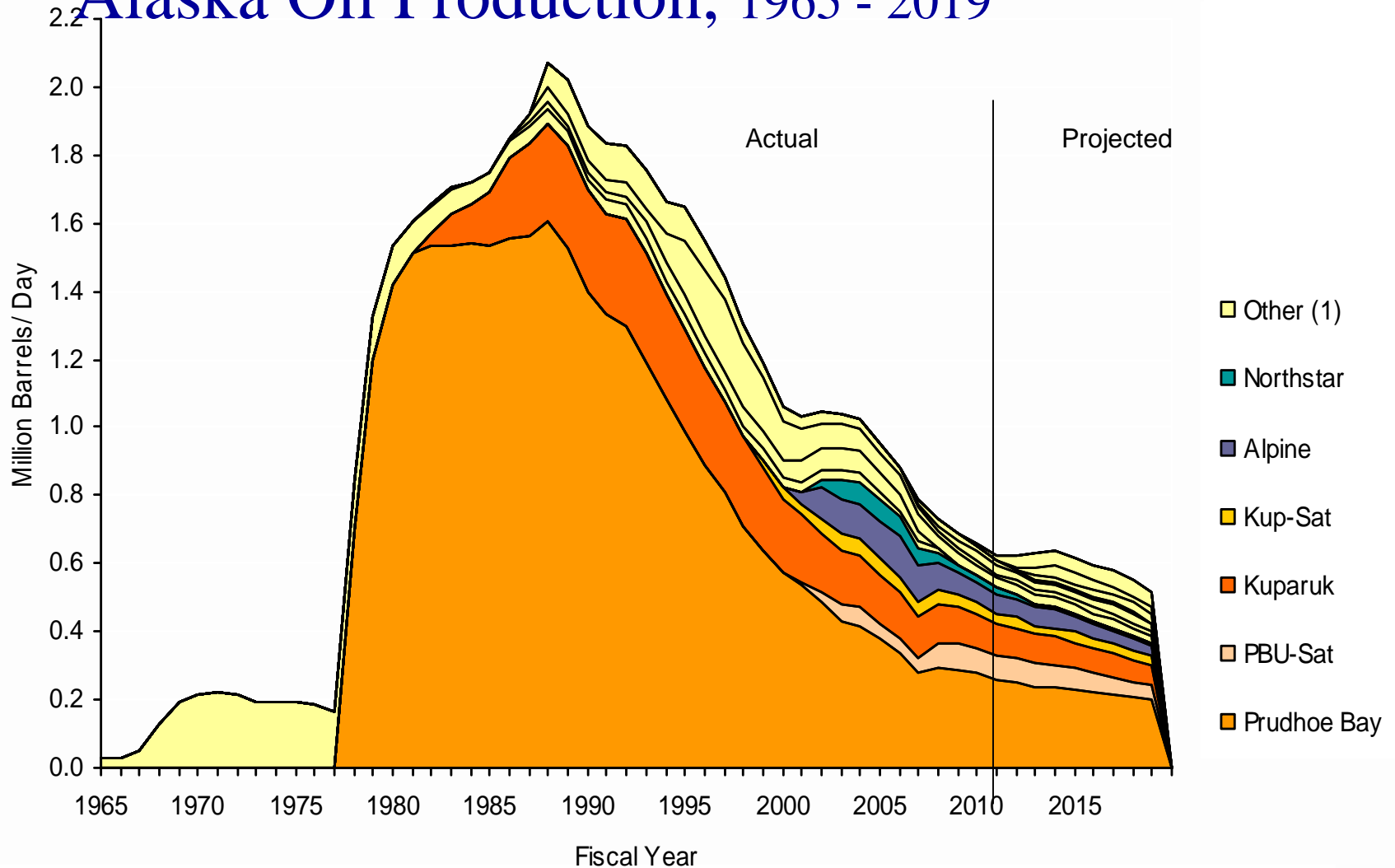
Alaska's Taxes

State of Alaska Taxes (and Oil and Gas Royalties)

| | <u>FY 2008</u> | <u>FY 2009</u> |
|--|--------------------|--------------------|
| Special Oil & Gas Corporate Income Tax | \$ 605.80 | \$ 492.20 |
| Oil & Gas Production Tax | 6,822.60 | 3,112.00 |
| Oil & Gas Property Tax | 81.50 | 111.20 |
| | | |
| Oil and Gas Royalties (Unrestricted) | <u>2,446.10</u> | <u>1,465.60</u> |
| Total Oil & Gas Unrestricted | <u>\$ 9,956.00</u> | <u>\$ 5,181.00</u> |
| | | |
| Other Unrestricted Taxes | \$ 433.20 | \$ 294.70 |

Source: Dept. of Rev. 2008 & 2009 Revenue Sources Books

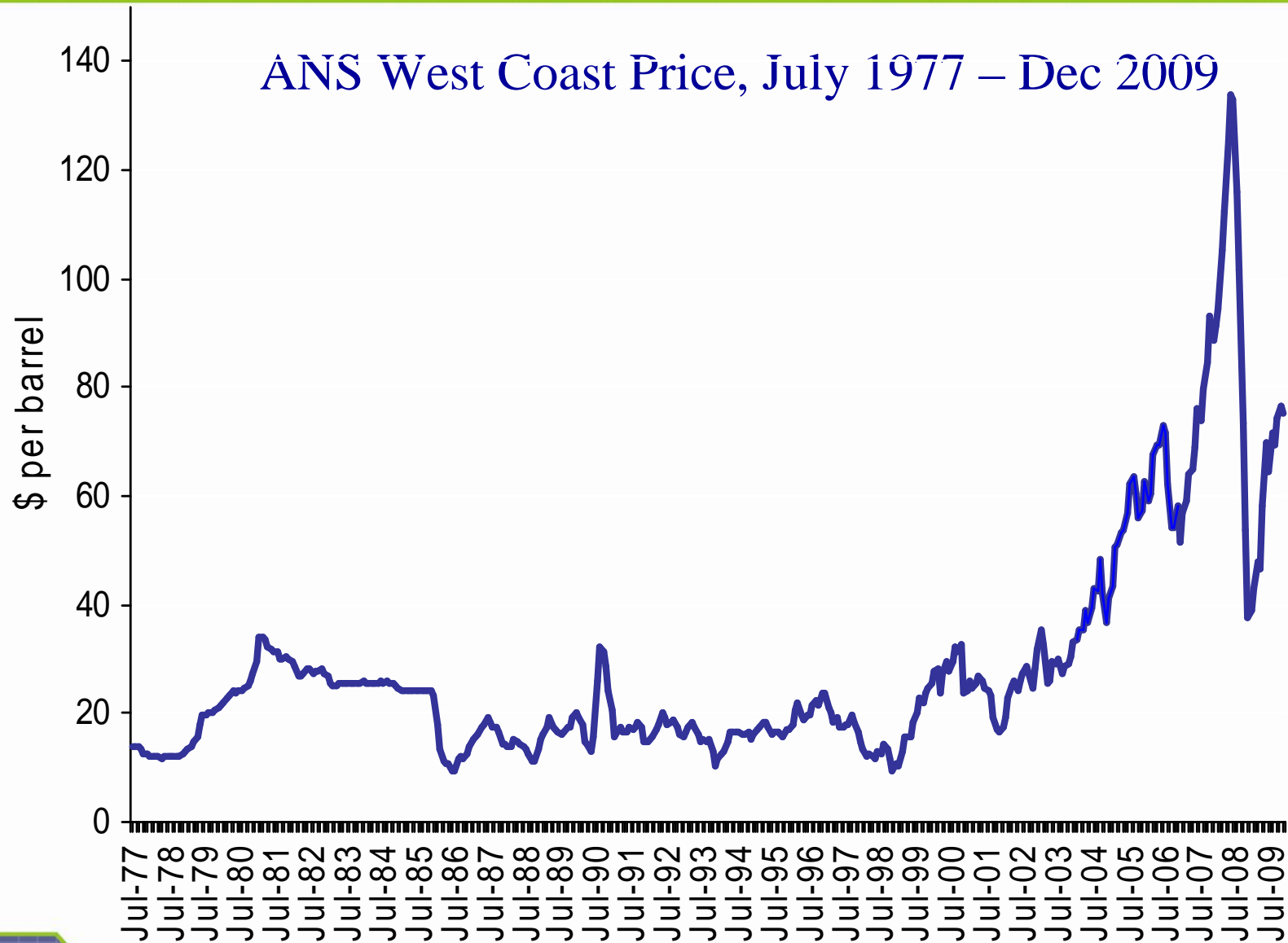
Alaska Oil Production, 1965 - 2019



Source: Alaska Department of Revenue, Fall 2009 Revenue Sources Book. Extrapolated
 (1) Cook Inlet, Duck Island, Milne Point, Greater Point McIntyre, Liberty, Known On & Offshore, Fiord and NPRA.

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ANS West Coast Price, July 1977 – Dec 2009



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Source: Alaska Department of Revenue, Tax Division

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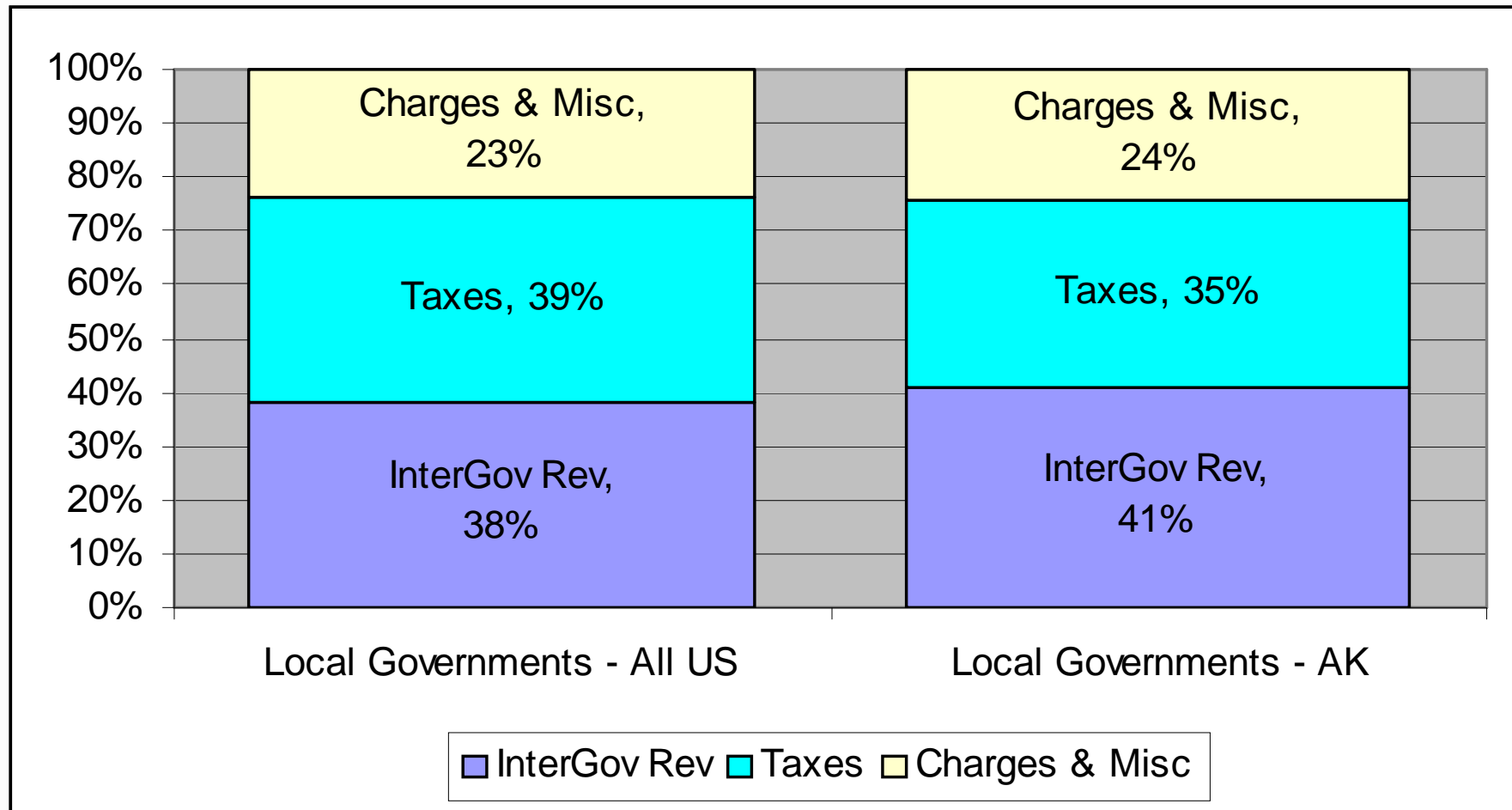
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How would a Gasline effect State Finances?

| | | | |
|--|-------------------------------|---|----------------|
| Barrels A Day | FY 2009 - ANS Oil 0.702 | Billion Cubic Feet of gas a day Billion CF = million mcf | Gas 4.5 |
| ANS West Coast Value | \$ 68.34 | Today's Henry Hub Price | \$ 4.27 |
| Transportation Costs | (6.48) | Tariff ?? | (3.00) |
| ANS Wellhead Value | <u>\$ 61.86</u> | Gas Well Head Value | <u>\$ 1.27</u> |
| Annual Taxable Value (In Millions of Dollars) | 15,850.4 | Annual Taxable Value (In Millions of Dollars) | 2,086.0 |

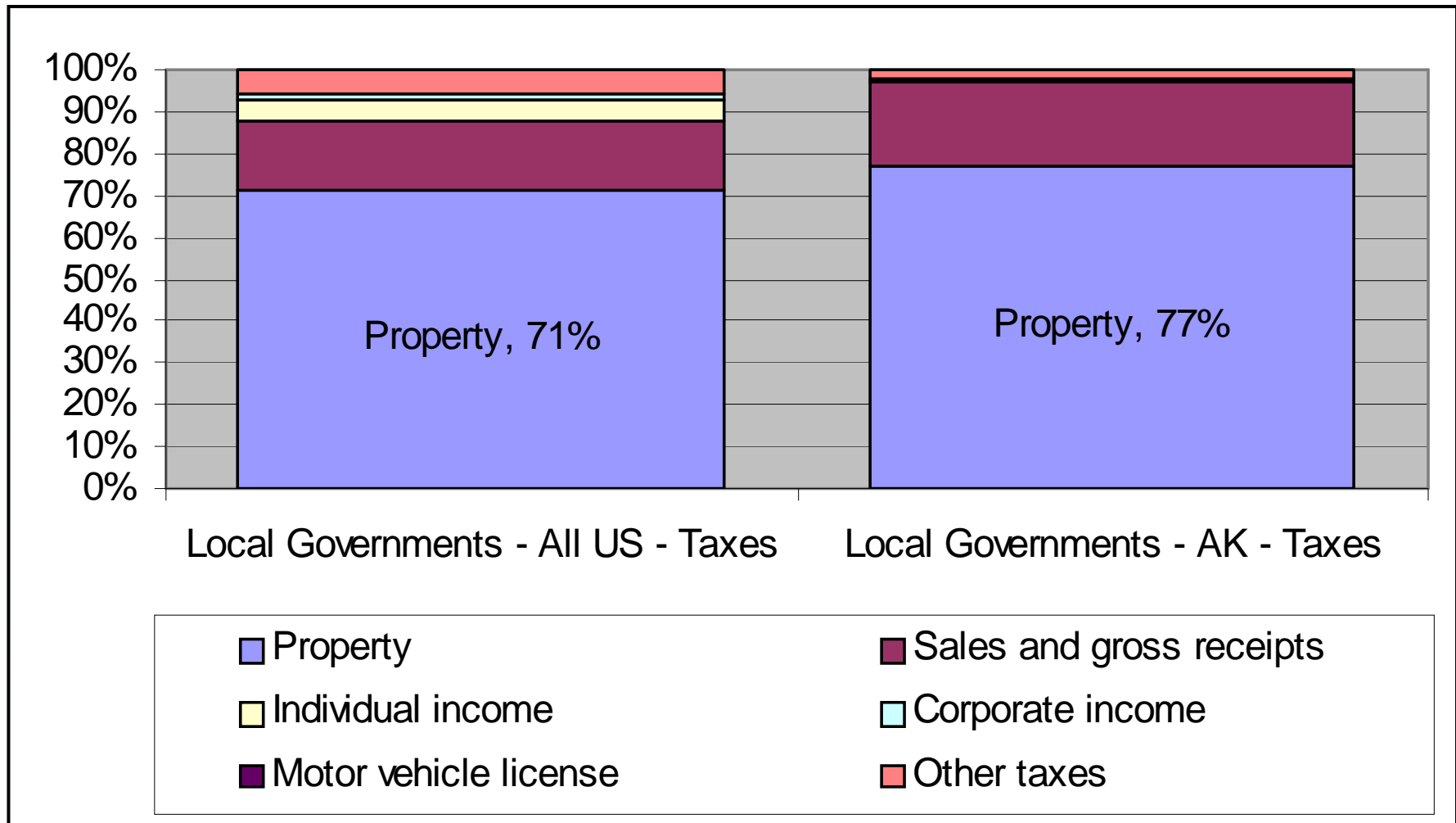
- Take Away on State Taxes
- State's revenues are highly volatile, especially after the 2006 ("PPT") and 2007 ("ACES") reforms
- Mechanisms like the CBRF (Constitutional Budget Reserve fund), Forward funding of education, and perhaps the Permanent Fund will become more important.
- If there is correction in oil prices similar to the recent correction in gas prices, followed by a prolonged period of lower energy prices, state and municipalities may be in competition for revenues.

AK Local Government Looks a lot like US-Wide Local Gov



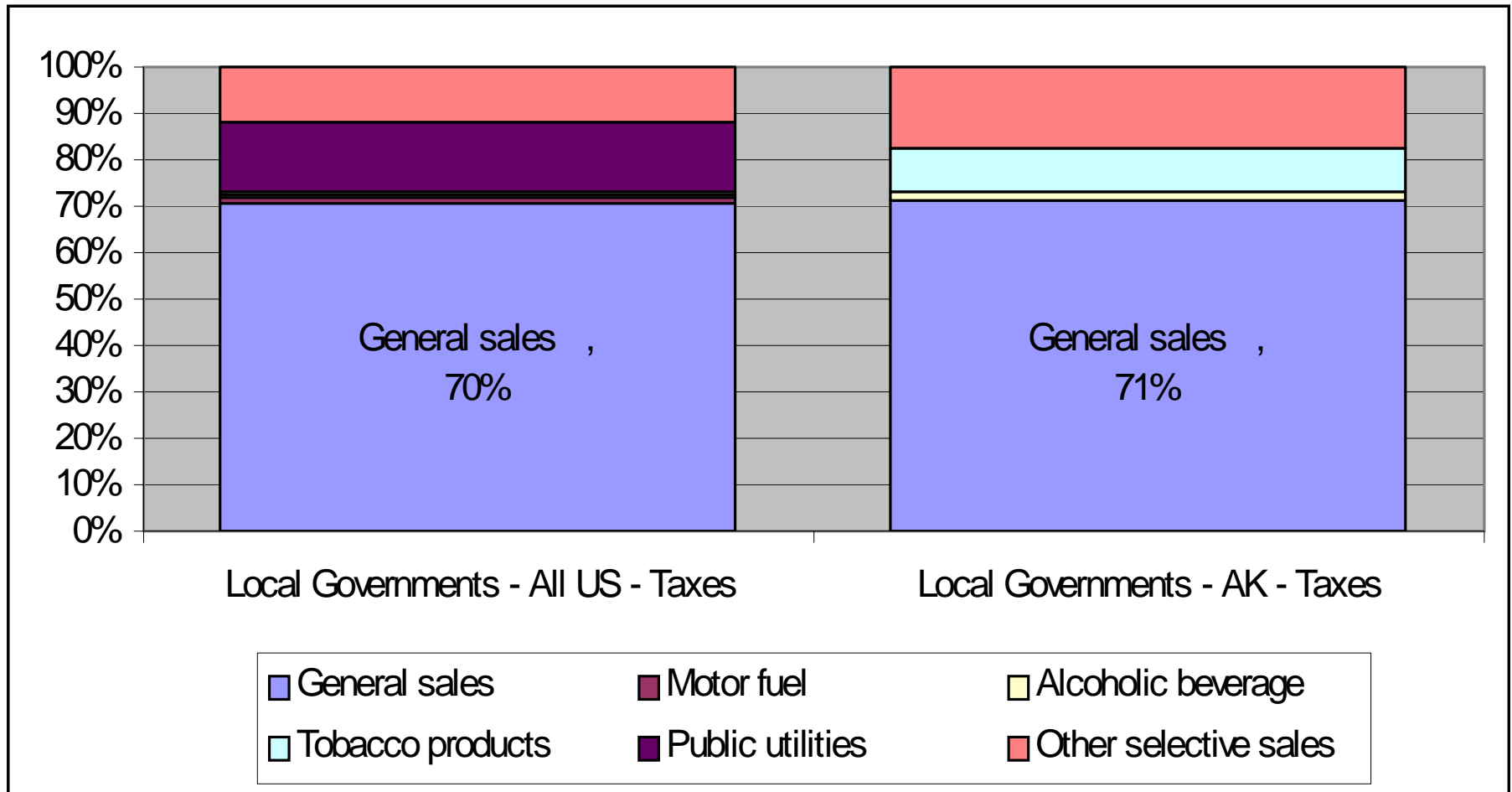
Source: 2007 Census of Government Finance <http://www2.census.gov/govs/estimate> (accessed March 18, 2010)

AK Local Taxes look a little less like US-Wide Local Taxes



Source: 2007 Census of Government Finance <http://www2.census.gov/govs/estimate> (accessed March 18, 2010)

AK Local Sales Taxes vs. US-wide Local sales Taxes



Source: 2007 Census of Government Finance <http://www2.census.gov/govs/estimate> (accessed March 18, 2010)

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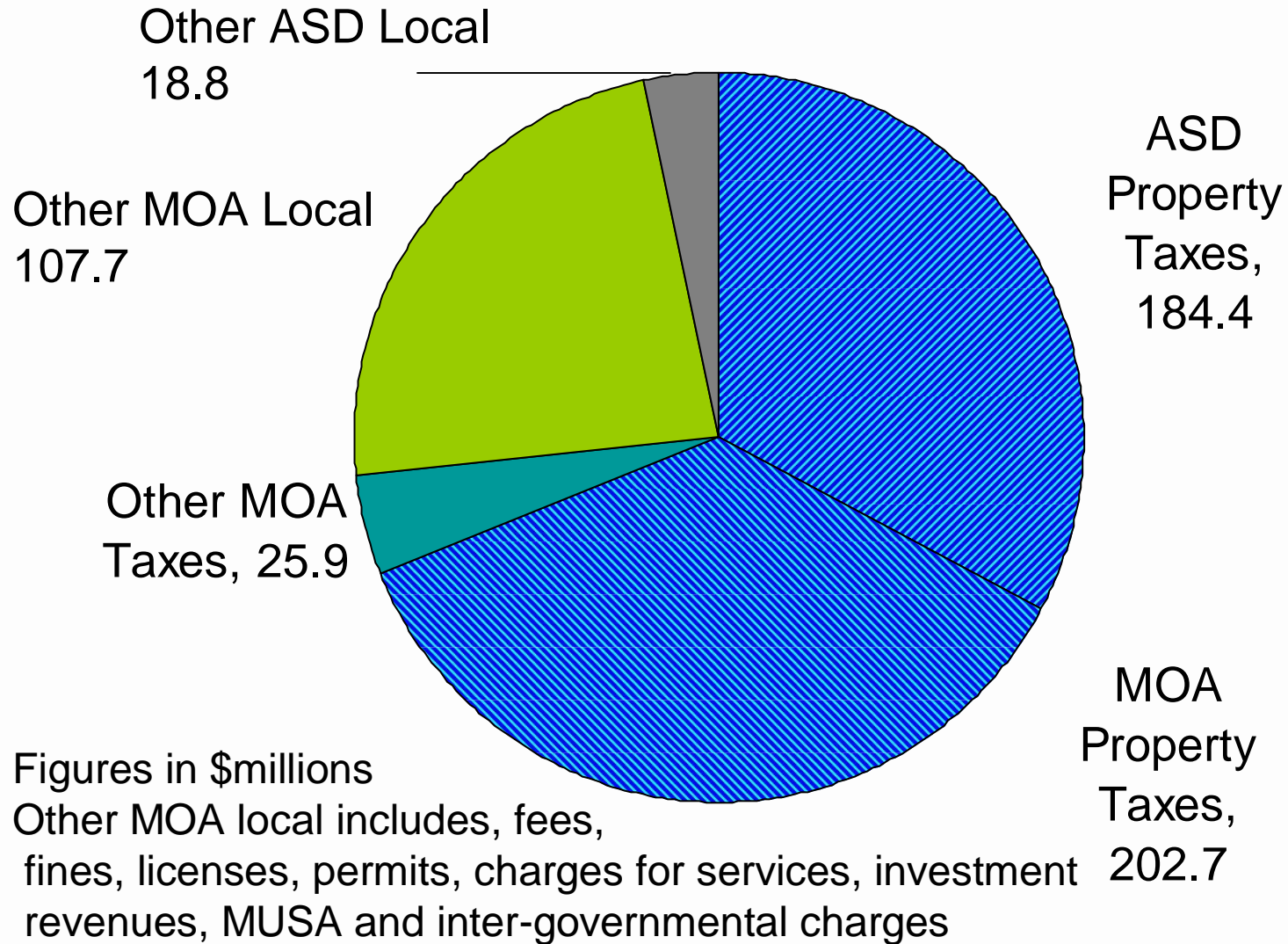
Part I - Conclusions

- The tax burden in Anchorage is among the lowest in the nation
- Primarily because the state tax burden is negligible.
- (Can argue that for state and federal taxes it is negative)
- Therefore local taxes loom very large

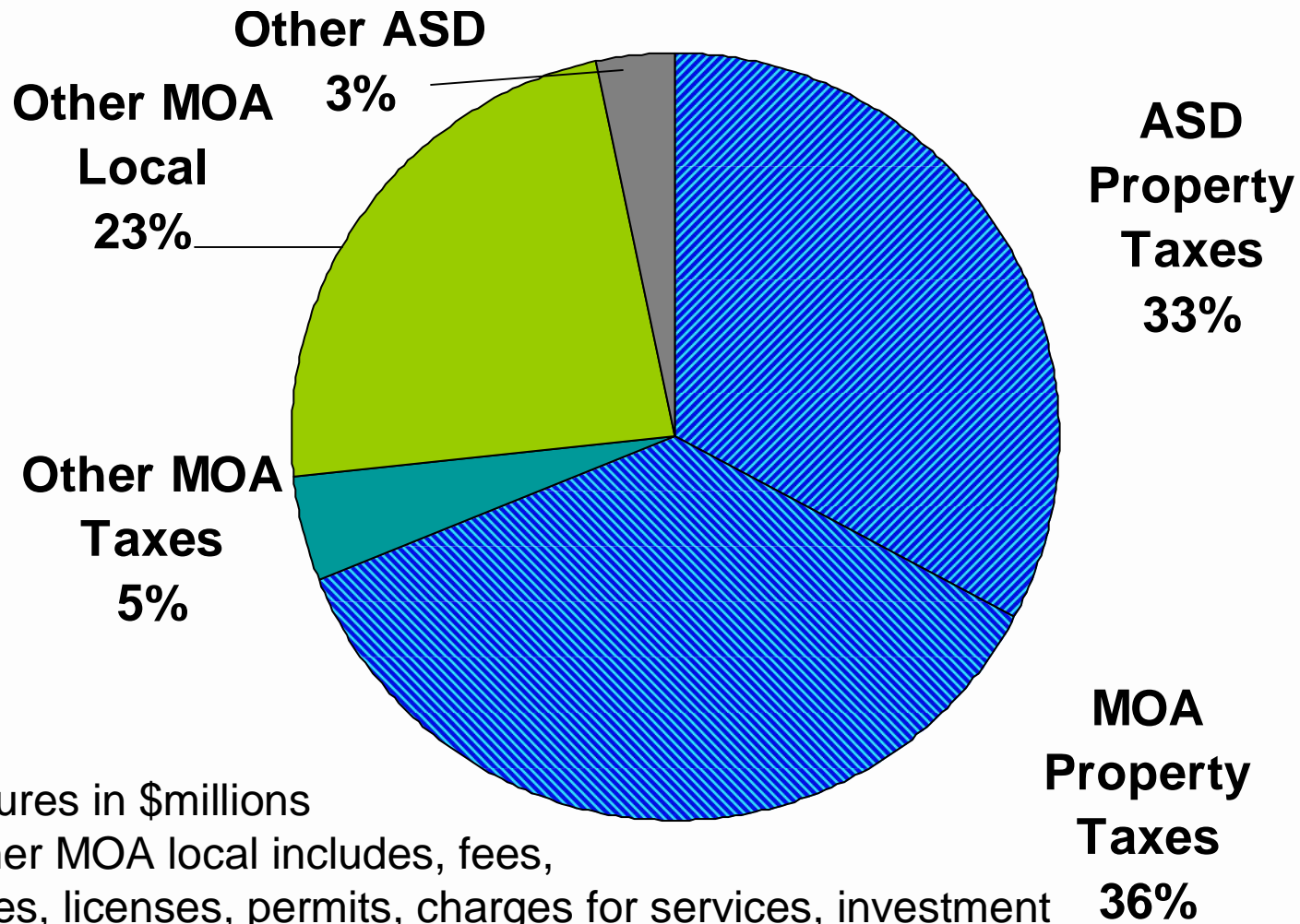
- Because the Property Tax is the primary tax, it looms even larger

- Two Alternatives to the Property Tax for Anchorage were explored in the summer of 2007:
- A Business “Activities Tax” or “Business Opportunity Tax”
- The Property Tax Relief Task Force

2006 Anchorage Combined Local Revenues - \$562.8 million



2006 Anchorage Combined Local Revenues – 2/3 from Property Tax

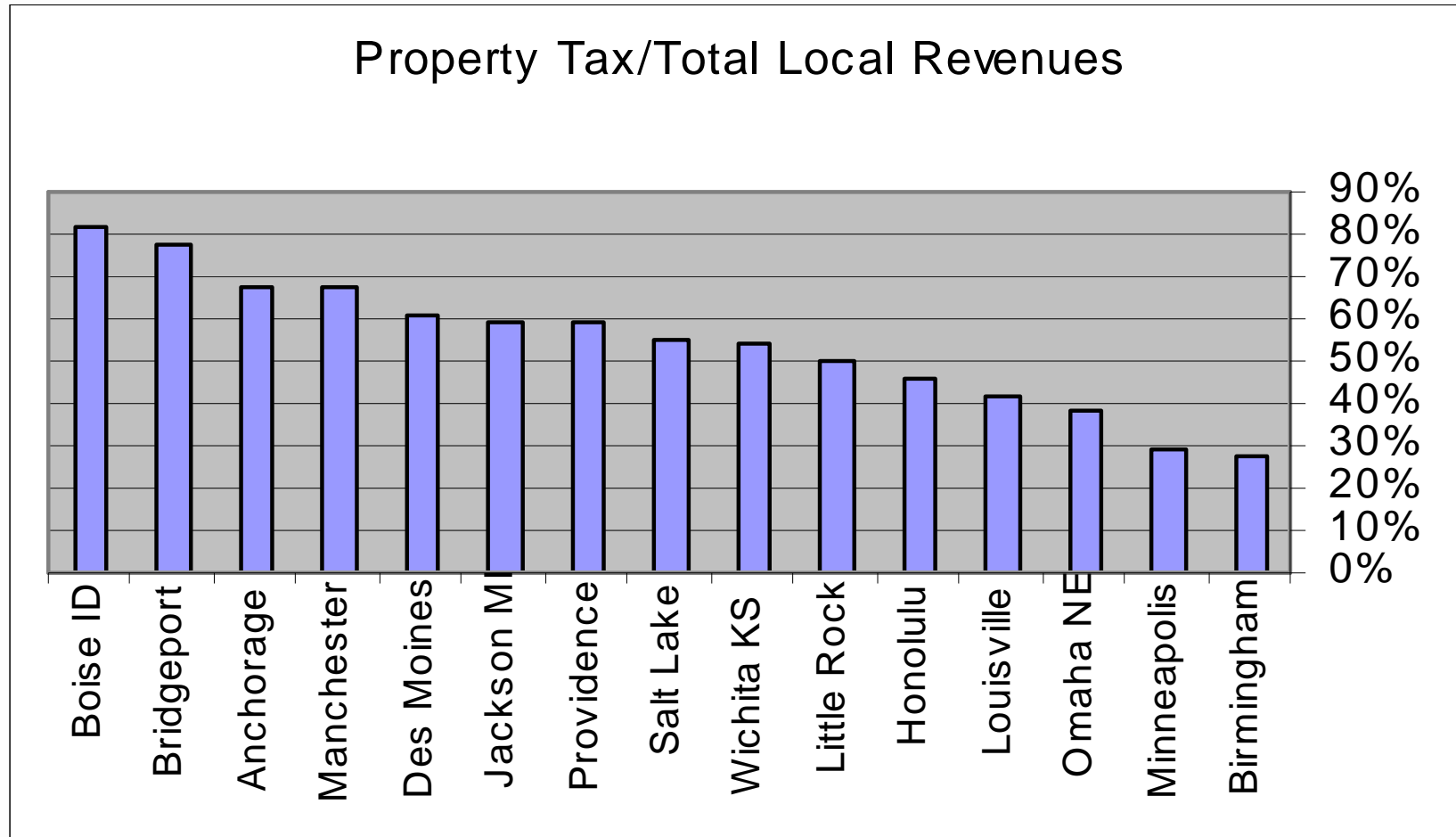


Figures in \$millions

Other MOA local includes, fees, fines, licenses, permits, charges for services, investment revenues, MUSA and inter-governmental charges

Is Anchorage Heavily Reliant on Property Tax?

Comparison for 2006 with Cities in DC study with Like Population



Includes all cities in DC study with populations between 100,000 and 400,000 except Newark NJ, Sioux Falls SD and Columbia SC – Data from Budgets and CAFRS

Why Change Anchorage's Fiscal System

(1) Reliance on one major tax means the rate is higher than if there were two major taxes, each raising less revenue

Are Anchorage Property Taxes High? (First is highest, 51st lowest)

| Annual Income, hypothetical family of 3 | Total tax rank | Property tax rank |
|---|----------------|-------------------------------|
| \$25,000 | 48 | 3rd(estimated as 20% of rent) |
| \$50,000 | 48 | 15 th |
| \$75,000 | 51 | 15 th |
| \$100,000 | 51 | 14 th |
| \$150,000 | 51 | 13 th |

Source: Tax Rates and Tax Burdens in the District of Columbia – A Nationwide Comparison 2005 (Government of the District of Columbia, Issued August 2006)

Why Change Anchorage's Fiscal System?

(2) Do property taxes reflect changes in local (and national) economy?

- Shift from goods to services.
- Shift from investment in capital equipment to investment in human capital.

“There are whole industries today – enormously and profitable industries – that weren't even dreamed of twenty-five years ago. The new economy has been described by many names; service, information, space age, diversified. But our tax structure remains tied to the past, to hard products and assets attached to the ground. -

Report of the Texas Tax Reform Commission (2006, pg 12) advocating property (and income) tax relief coupled with a modified gross receipts tax.

Why Change Anchorage's Fiscal System?

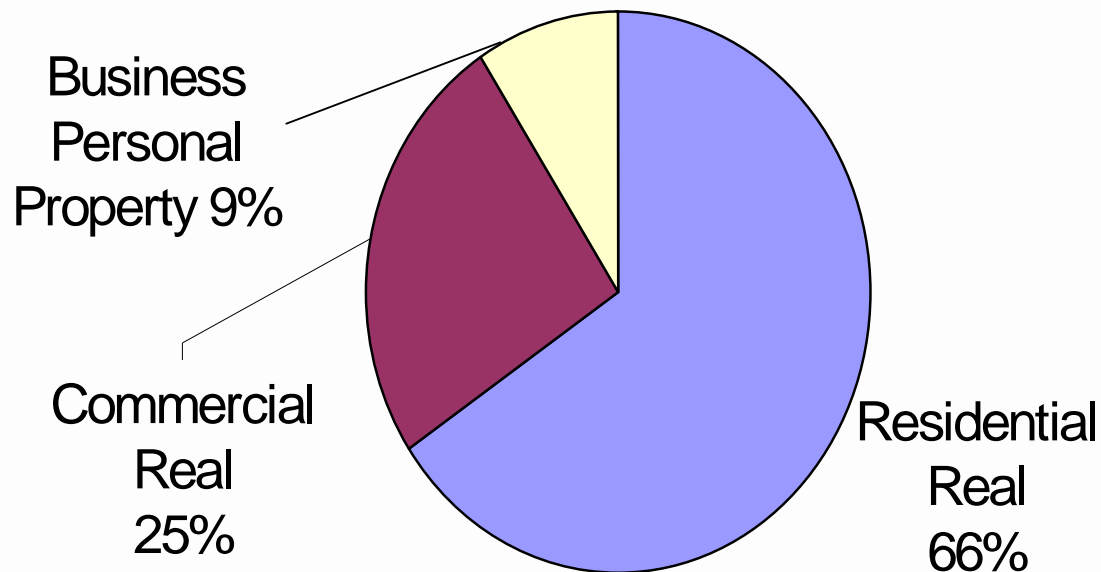
(3) Do citizens see how local government is financed?

- Homeowners know they are paying tax though roughly 45% make monthly escrow payments, and are not aware how much is tax.
- Consumers do not understand if and how property taxes paid by business are passed on to them or how property taxes that move through several business may pyramid.

Why Change Anchorage's Fiscal System?

(4) Is Anchorage bearing too much of its own tax burden?

- Business taxes easier to export than personal taxes and commercial property is 9 billion out 26 billion total in value



Why Change Anchorage's Fiscal System?

(5) Our dependence on Property Taxes may effect City's long term financial health

- Standard and Poor's Municipality of Anchorage, Alaska, General Obligation (April 11, 2007)
- “The municipality’s general fund revenues are derived mainly from the property tax...; this could emerge as a concern if market values for residential and commercial property weaken”

Property Tax Relief Task Force

- Task Force appointed by Mayor Begich and Assembly Chair Coffey
- Eleven Citizens from Business Community
- Chaired by Former Assemblyman Bob Bell
- Asked to recommend a mechanism that could provide significant and lasting property tax relief
- Significant defined as at least one third reduction
- Kick off meeting on July 25, 2007

Is a Business Activity Tax an Answer?

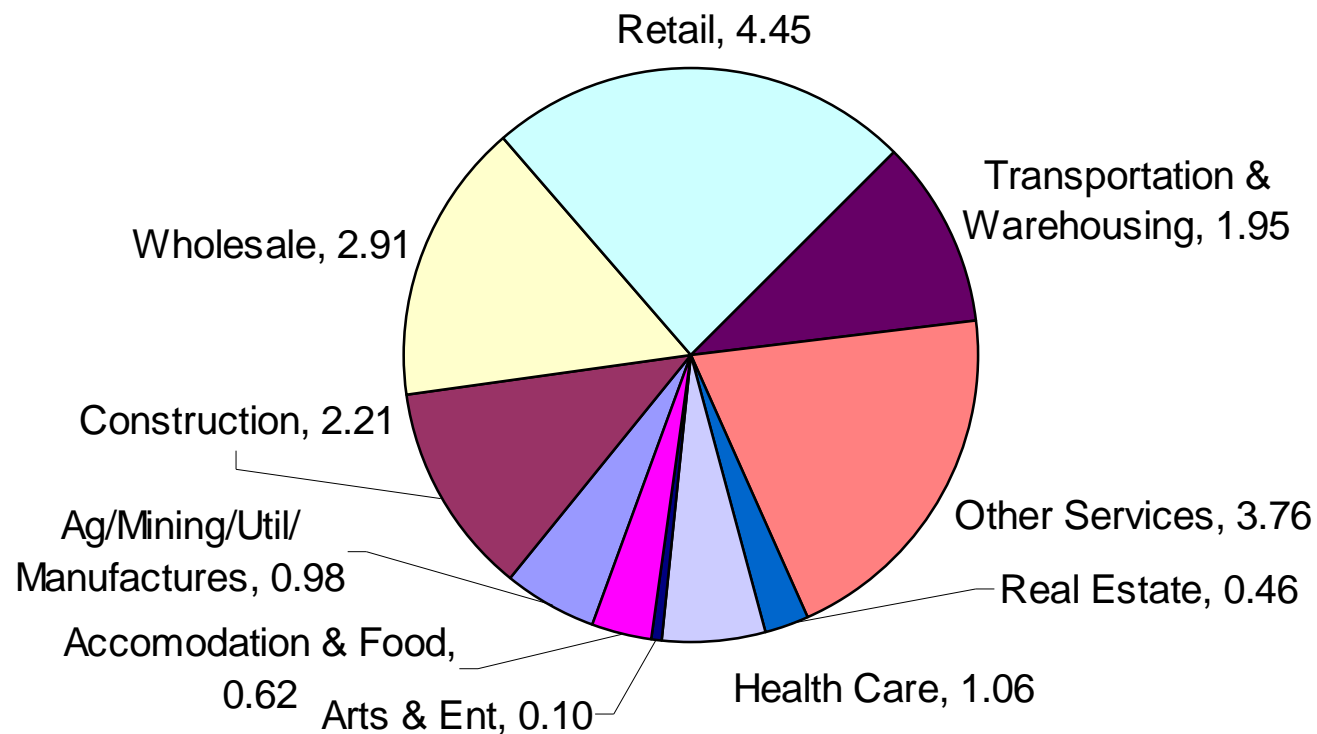
(1) Broad base = low rate

- Would provide the sought after diversity of revenues.
- Would allow property tax rates to fall –
 - Improving the property tax so its broad base is complemented by a lower rate

Broad Base = Low Rate

For most businesses, gross receipts best measure of activity. Businesses sell:

Estimated 2006 Gross receipts of \$18.5 billion



Model of Property Tax Relief From the gross receipts portion of a Business Activity Tax:

If goal were \$130 million dollars, rate of .7%
 (7 tenths of a percent - \$7,000 in tax on a million dollars of receipts. \$.07 cents on a ten dollar sale.)

| | Property Value | Mill Rate | Tax Revenue |
|---|------------------|--------------|-----------------|
| Current (2006): | \$ 26,045 | 14.82 | \$ 386.0 |
| Reform: | | | |
| Reduce Mill Rate by 33% | | 66.7% | |
| Property Taxes: New Mill Rate Applied | \$ 26,045 | 9.88 | \$ 257.3 |
| | Taxable Receipts | Tax Rate | Tax Revenue |
| Add Business Activity Tax | \$ 18,500 | 0.70% | \$ 128.7 |
| Sum of Tax Revenues after Reform | | | \$ 386.0 |
| Figures in Millions of Dollars, "current" ties to 2006 Budget | | | |
| | | | |

Is a Business Activity Tax an Answer:

(1) Broad base = low rate

Other Business measures:

Alternative “headquarters” measure – if costs or a single measured cost is great than sales , then business is probably headquarters, back office or part of logistics chain.

Tax on the alternative measure – (payroll, square footage, # of employees, occupancy costs)

Is a Business Activity Tax an Answer:

- (2) Exportability
- “Only good tax is one someone else pays”
- New Mexico, Hawaii, Arizona, & Montana all design their tax codes so that a business contracting with the federal government pays tax based on that contract.
 - (Federal government exempt from sales tax, however if every bidder on a contract adds BAT to its price, burden of tax is passed to Federal government.)

Is a Business Activity Tax an Answer:

- (3) Responsive
- Every transaction, not just selected transactions taxed. Reaches all areas of economic activity.
 - Compared to a traditional sales tax, base includes services, business to business transactions, and sales to government
 - Task Force rated this a big plus

Is a Business Activity Tax an Answer:

- (4) Takes advantage of Anchorage's status as a "Hub City"
- Anchorage largest commercial hub for many many miles around
- "Agglomeration rents"
- Situs and Nexus issues:
 - Only taxpayers that have nexus can be taxed
 - Only transactions that have situs can be taxed

Is a Business Activity Tax an Answer:

- (5) Widely used, should reassure rating agencies
- States – Historically part of fiscal system in
 - Washington and
 - Delaware.
 - Since 2005 replaced other business taxes in
 - Texas and Michigan (in modified form) and
 - Ohio (“Commercial Activity Tax”)
- Cities – Extensive use in California, post proposition 13 limits on property taxes.

Is a Business Activity Tax an Answer:

- (5) Widely used, should reassure rating agencies
- Cities – used in hundreds of cities across country, primarily with state framework in
 - Pennsylvania
 - Washington
 - Virginia
 - South Dakota (limited)
 - Georgia (limited)
 - Alabama
 - Tennessee
- * Note – Washington on both lists (and they have a sales tax). So same transaction may be taxed three times – gross receipts once by city, once by state and once by sales tax.

Property Tax Relief Task Force

- Met seven times July – September
- Final report issued September 19, 2007
 - Task force did not opt for a business activity tax
 - Task force recommended a sales and use tax which included tax on services

Property Tax Relief Task Force: "No"

- (1) Agreed that Business Activity Tax was responsive to the economy

Property Tax Relief Task Force: "No"

- (2) Agreed that Business Activity Tax burden could be exported – but noted that mechanism put burden on contracting businesses.

Property Tax Relief Task Force: "No"

- (3) Didn't like the exportability
 - Citizens don't understand cost of government when others pay.
 - Citizens are not engaged with government when others pay.
- Personal Observation: When "others" pay, "they" demand a say in tax policy which can appear profoundly undemocratic.

Property Tax Relief Task Force: "No"

- (4) Business Activity Tax shifts the initial burden to the business community.
 - “we can’t raise our prices in this competitive environment”
 - Discussion revolved around
 - unfair effect on low margin businesses
 - Pyramiding and cascading
 - Discourages outsourcing and
 - Encourages integration and large business that have internal transfers, not b2b sales

Property Tax Relief Task Force: "No"

- (5) Didn't like the lack of visibility and transparency of a Business Activity Tax for those final consumers to whom the burden was passed.
 - Focus and discussion on arguments about comparative transparency of property tax, Business Activity Tax and sales tax on those paying vs. those who might bear the final burden.

Other Task Force Conclusions

- Fiscal system and reliance on Property Tax not broken – even though it could be improved.
- Overall tax burden is low in Anchorage and any changes should be approached with caution.
- Best solution is a sales tax including services but excluding staples— rate (to achieve 1/3 reduction in property taxes) probably under 3%.

Property Tax Relief

- Task Force Conclusions compared with votes
- Sales Tax requires a vote of the people
 - 1993 30% Yes 70% No
 - 2001 29% Yes 71% No
 - 2006 30% Yes 70% No
- 60% approval required under charter
 - Charter amendment requires 50%
- Note: Implication of possible state sales tax?

Other Learnings

- No one has a good model of where the final burden of many taxes fall, and if or to what degree business tax burdens are passed on consumers.
 - “Businesses don’t pay taxes, they just collect them.”
 - V.
 - “We can’t raise our prices in this competitive environment”

Thank You

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