

Property Tax Relief Project Drilldown I

Mission:

By Sept. 4, 2007 bring forth a recommendation for significant and lasting property tax relief to Anchorage's citizens and businesses, including a workable, broad-based, alternative revenue mechanism for the Municipality of Anchorage and the Anchorage School District to fund that relief.

Mission (cont.):

- The Solution should meet the following criteria:
 - Diversify municipal revenues to obtain significant and lasting relief
 - Keep current spending caps in place
 - Build on Anchorage's unique role as the economic and commercial hub of the region while recognizing the dynamics of a changing economic environment
 - Incorporate best administrative practices

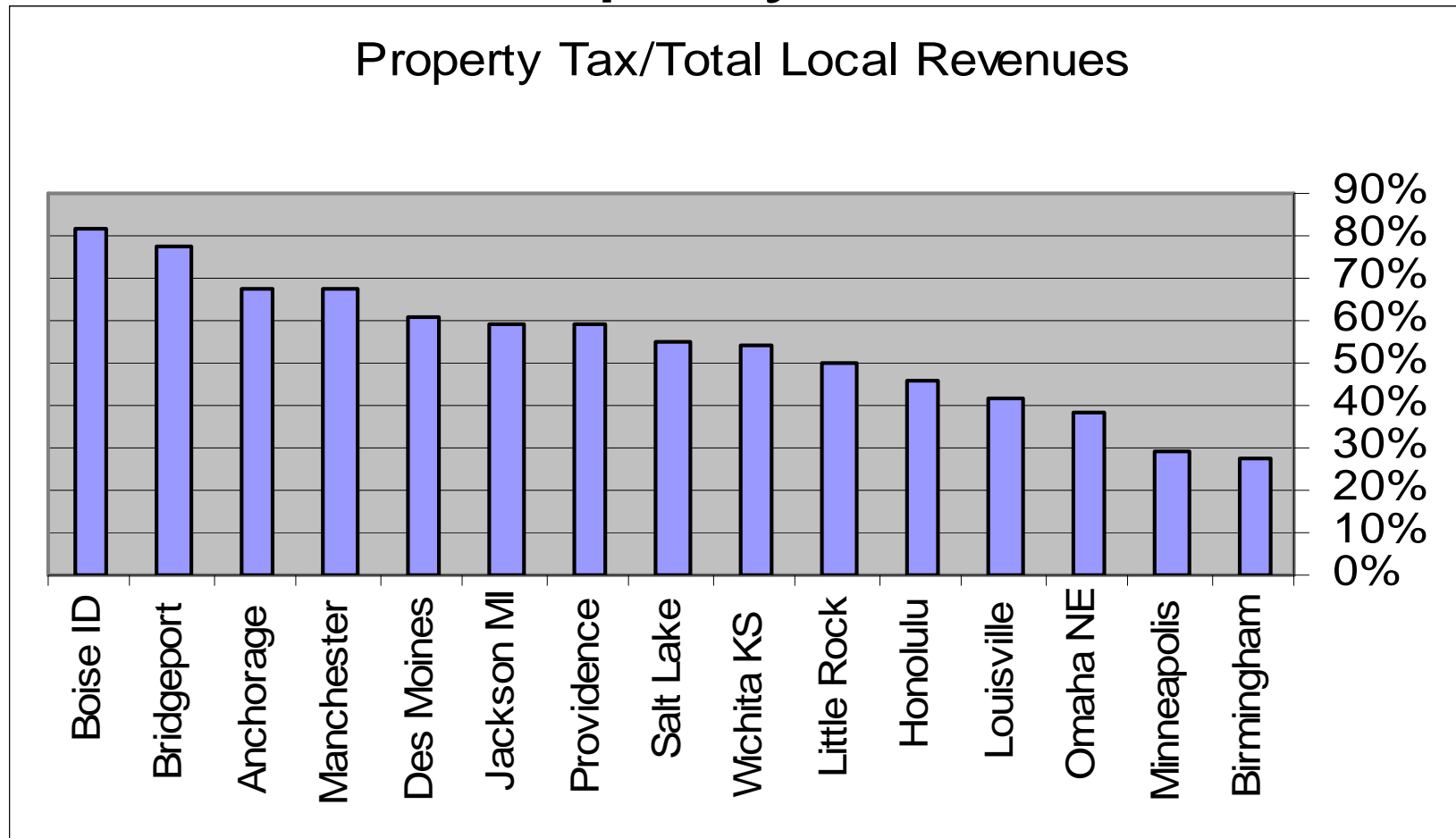
Mission - Why?

- Problem is not property tax
- Even after the relief envisioned by this project, property tax will still be Anchorage's largest source of local revenues.
- Problem is over-reliance on a single source, which happens to be property tax.

How Does Anchorage Rank?

- Concentration of Property Tax
- Level of Taxation

Is Anchorage Heavily Reliant on Property Tax?



July 25, 2007
 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
 Property Tax Relier Project
 Dhillon

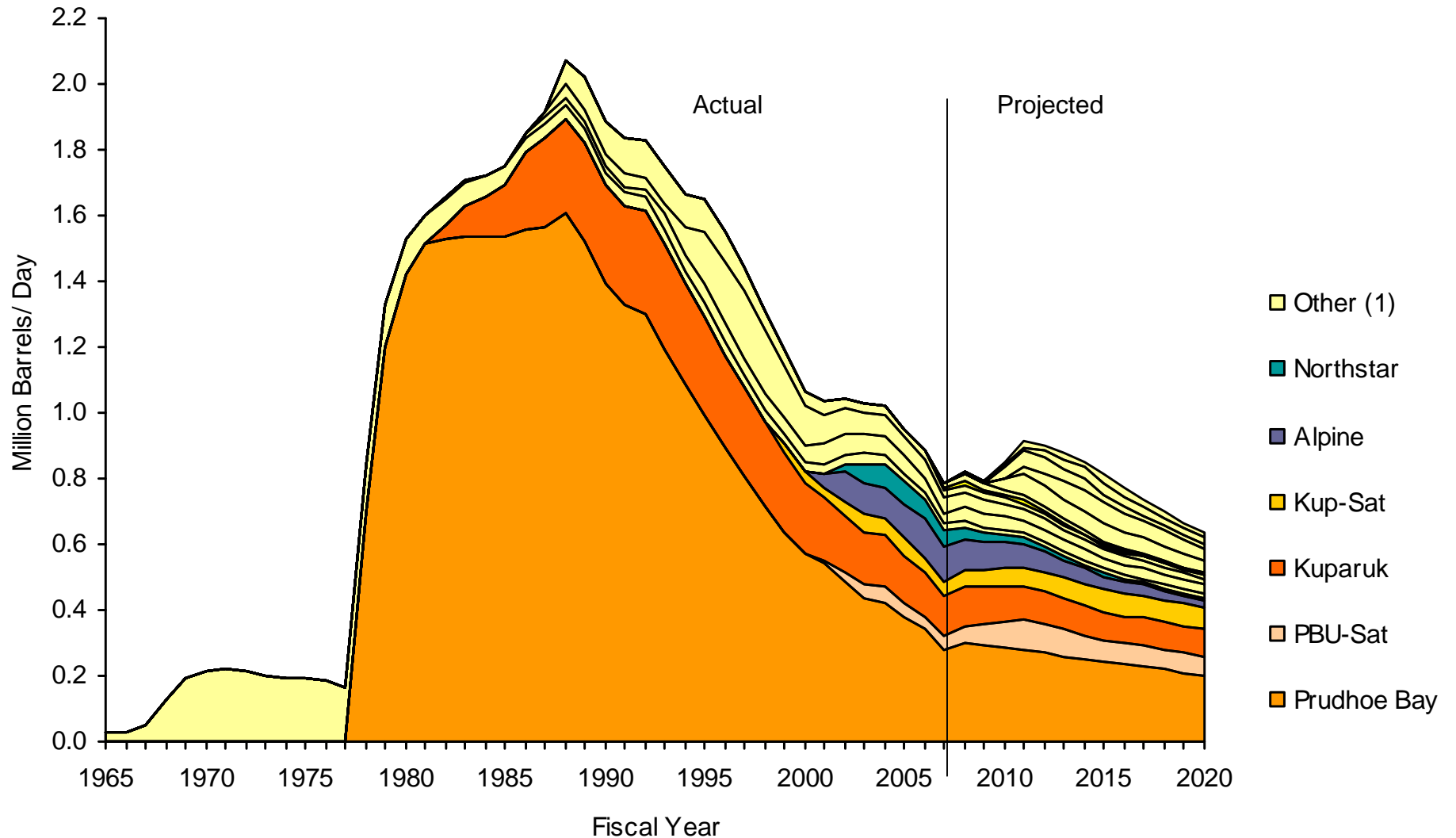
Are Anchorage Property Taxes High? (First is highest, 51st lowest)

| 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
 July 29, 2007
 2005 (Government of the District of Columbia, Property Tax Relief Project
 2005 (Government of the District of Columbia, Issued August 2006)
 Drilldown

Context of State Revenues

Alaska Oil Production, 1965 - 2020



Source: Alaska Department of Revenue, Fall 2006 Revenue Sources Book. extrapolated

(1) Cook Inlet, Duck Island, Milne Point, Greater Point McIntyre, Liberty, Known On & Offshore, Fiord and NPRA.

July 23, 2007

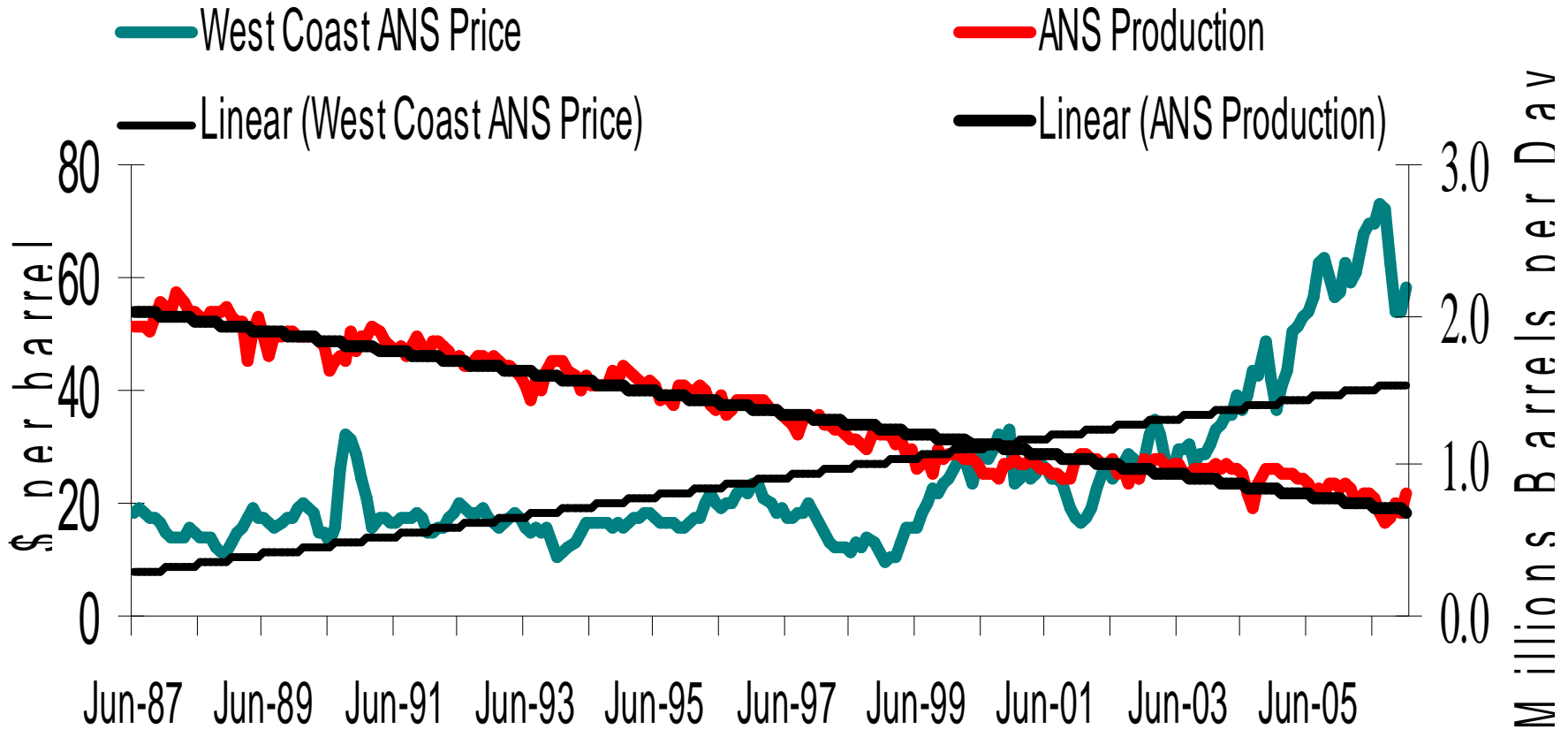
PROPERTY TAX RELIEF PROJECT
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Significant – State Context

- Historical Moment: State has relied on oil and gas taxes. Volumes fallen, but rising prices overcompensate:
 - 1998: 2 million bbl/day @ \$15/bbl = \$30 million
 - 2007: 750,000 bbl/day @ \$45/bbl = \$30 million
 - Yesterdays close was \$75/bbl, PPT with built in progressivity
 - ?: 750,000 bbl/day @ 15/bbl = \$8.25 million

ANS West Coast Price and Oil Production



Source: Alaska Department of Revenue, Tax Division

July 25, 2007

Property Tax Relief Project
Drilldown

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Significant – State Context

- If the company which decides to build the pipeline started now, and time schedules did not slip, first gas is 2016.
- If application process goes smoothly, 9 year clock could start running as soon as summer of 2008, first gas 2017.
- Smaller project could be quicker but will have smaller revenues.
- 4.5 bcf a day producer project that derailed last year was equivalent of shipping 750,000 bbls a day through the pipeline

Significant – State Context

- If there is a price correction State may look at
 - sales tax,
 - use of Permanent Fund earnings,
 - income tax,
 - or eliminating state provided services and jobs or support for programs including education.

Significant

- Significant Property Tax relief is at least a one third reduction in property taxes from what they would have been:
- 2006: \$130 million
- 2009 (estimate) \$150 million

- Property Taxes currently $\frac{2}{3}$ of total local revenues so a $\frac{1}{3}$ reduction would leave them at just under 50% ($\frac{4}{9}$ ths) of local revenues.

What are the Obvious Alternatives to a Business Activity Tax?

- Sales Tax – been on the ballot three times since 1993 – always rejected. Voters clearly do not want an add on at the cash register.
- Income Tax/Payroll Tax– Most cities that have these type of taxes head toward the simple end so we typically see flat payroll taxes on all employees.
- Head Tax – To generate same amount as revenue as proposed reform would require over 700 from each Anchorage adult (visitors pay nothing.)

What are the obvious alternatives employed by other cities?

- Utility Taxes – These typically are allowed to be billed through to customers.
- Sin taxes, such as on alcohol (already have tobacco tax)

Business Activity Tax101: Gross Receipts Portion

- Tax on gross receipts for the period with no deductions for the cost of doing business
- Typically at a much lower rate (less than 1%, and frequently less than a half a percent) than an income tax or sales taxes on a much broader base.

Business Activity Tax 101

- States:
 - DE (“Merchants & Manufacturers Tax”) since 1913
 - WA (“Business & Occupations Tax”) since 1933 – WA also has sales (but no income tax) – transaction taxed from both sides
 - also local option used by 40 WA cities -
 - OH (“Commercial Activities Tax”) since 2005
 - Also sales and income tax, transactions taxed from both sides– replaces corporate income tax
 - MI A modified gross receipts tax & a corporate income tax replaced the “Single Business Tax” – enacted in 2007

Business Activity Tax 101

- TX in 2005 replaced its corporate income tax with Business Activity Tax/modified Gross Receipts tax
 - Taxpayer can deduct
 - wages and salaries or
 - costs of goods sold or
 - 30% of Gross receipts
 - Relatively high rate of 1%

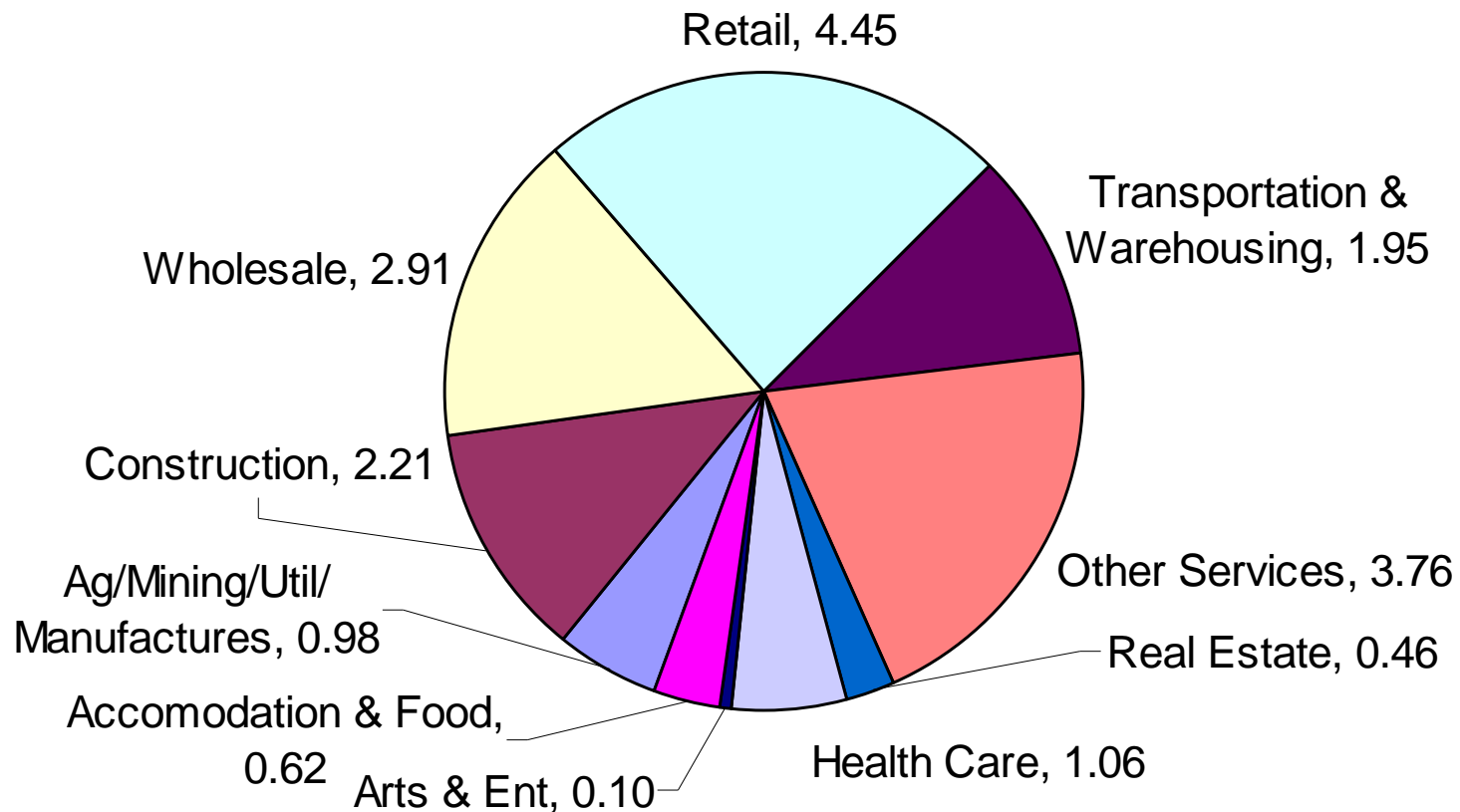
Business Activity Tax 101: “Turnover Tax”

- Widely used in Europe until replaced with VAT
- AZ, NM, HI and AR have “gross receipts taxes” with lots of exemptions that essentially act like retail sales taxes
- WV, IN, MS, NJ have repealed gross receipts taxes.
- KY uses GRT as AMT for CIT

Business Activity Tax 101

- States with local options defined (and constrained by state law):
 - WA including Seattle, Tacoma, Bellingham
 - PA (Mercantile Tax) including Pittsburgh and Philadelphia
 - VA (Business Privilege and Occupational License) including Virginia Beach & Norfolk
 - GA (Just utilities and financial inst?)
 - TN including Knoxville & Chattanooga
- Individual Cities: LA CA, Birmingham AL

2006 Anchorage Gross Receipts Estimate of \$18.5 Billion



2006 Anchorage Gross Receipts Estimate of \$18.5 Billion

What is .75%?

| Gross Receipts | Gross Receipts Tax |
|--|--|
| \$10 | 7.5 cents |
| \$100 | 75 cents |
| \$1,000 | \$7.50 |
| \$10,000 | \$75.00 |
| \$100,000 | \$750 |
| \$1,000,000 | \$7,500 |
| \$10,000,000 | \$75,000 |
| \$100,000,000 | \$750,000 |
| <small>July 25, 2007</small> \$1 billion | <small>Property Tax Relief Project Drilldown</small> \$7.5 million |

Friction in the model: costs

Costs will be incurred setting up new system.

- Decrease in amount of property tax collected may not lead to immediate drop in costs of administering property tax
 - same number of assessments, notices, collections etc.
 - may be a drop in number of appeals or resources city chooses to dedicate to audit

Elimination of business personal property will lower costs – but transition is tricky.

Friction in the model: Compliance levels

- Percent of delinquent Property taxes to tax levy:
 - 1996-2000 3.3%
 - 2001 – 2005 2.5%

- Percent of delinquent GRT taxes:
 - ???

Source: ASD 2006 CAFR (Table LL)

Is this a good idea or not? Tax Dimensions:

- No Perfect tax – may not even be a good tax – just the least worst set of taxes for the situation
- Exportability
- Transparency
- Responsiveness
- Simplicity
- Equity: Who pays the tax?

Exportability and Transparency: Who Pays a Business Tax

- Legal Incidence
 - Should be clear, payment mechanism simple
- Economic Incidence
 - Will be less clear. Can a firm or a landlord reclaim increased costs through higher prices?
 - Competition
 - Time element
 - General equilibrium model & changes in behavior
 - Will property tax relief be passed through to customers in lower prices?
 - What does it mean when firms use tax increases to capture more than the price increase?

Dimension: Transparency

- Pro: Price you see is the price you pay at the cash register: no add ons to estimate in your head
- Con: If business passes tax on, consumer doesn't know who much of price is really recovery of gross receipts tax, (or income tax, property tax, federal income tax, state and federal excise taxes (except gasoline tax) FICA and Medicare payroll taxes on employees, state production taxes on, or "environmental taxes.")

Dimension: Transparency

- Consider a business sector dominated by several large players that pay gross receipts, but with one small player that is too small to pay GRT. All the big players raise their prices to recapture the GRT. The small player raises its prices as well. Has it “collected the tax” for itself?
- What if the smaller firm doesn’t raise prices but captures a larger market share competing on its lower price- are those new revenues “collection of the tax”?
- What if the new revenues that come from not raising prices are enough to propel the firm into the ranks of GRT taxpayers? Has the firm then collected the tax?

Dimension: Transparency

- Transparency favors credit method VAT, where “the price you see is the price you pay” and the VAT is stated on the bill.
- On the one hand transparency disfavors equally “hidden taxes” like income tax, gross receipts tax, property tax, payroll taxes and additive or subtractive VATS, and on the other hand “add-on” taxes like sales tax.

Dimension: Exportability

- Gross Receipts tax capitalizes on Anchorage's position as a hub city
 - Center for government contracting (A government may be exempt from a sales tax, but a firm doing business with a government is not exempt from a gross receipts tax)

Dimension: Exportability

- If businesses pass taxes on to customers, then more of a business tax is exported than a personal or hybrid (combined personal and business) tax
- (a) through sales to US and state governments
- (b) through sales to out of town purchasers and export industries
- (c) through sales to visitors

Dimension: Exportability

- If businesses **don't** pass taxes on to customers, then more of a business tax is exported to the federal government through federal taxes than a personal or hybrid tax because
- (a) all businesses can deduct expenses, not just individual itemizers.
- (b) marginal rates tend to be higher for businesses
 - higher corporate rates,
 - Schedule C and partnership income skewed toward higher brackets
 - FICA on net for sole proprietors.

Dimension: Exportability

- Exportability favors business tax (gross receipts or income tax).
- Exportability disfavors personal taxes like personal income tax, head tax or sales tax and hybrid taxes like current property tax.

Dimension: Responsiveness

- Will reflect underlying 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.

Dimension: Responsiveness

- Responsiveness favors gross receipts because it tracks broad economic activity
- Responsiveness disfavors sales tax on personal tangible property and hybrid taxes like current property tax that track narrower measures.

Dimension: Simplicity

- Corporate income tax far too complex for a city the size of Anchorage
- National trend away from it, driven by a feeling that complexity of the corporate Income tax has overwhelmed its utility and theoretical strengths as a tax.

Dimension: Simplicity

- Simplicity favors gross receipts, property or sales tax
- Simplicity disfavors income tax

Result:

- A gross receipts tax scores well on
 - Exportability
 - Simplicity
 - Responsiveness
 - Transparency

Mission (cont.):

- The Solution should meet the following criteria:
 - Diversity municipal revenues to obtain significant and lasting relief ✓
 - Keep current spending caps in place
 - Build on Anchorage's unique role as the economic and commercial hub of the region while recognizing the dynamics of a changing economic environment ✓
 - Incorporate best administrative practices

Tax Caps

- **Section 14.03. Tax increase limitation.**
- (a) Except as provided in this section, the total amount of municipal tax that can be levied during a fiscal year shall not exceed the total amount approved by the assembly for the preceding year by more than a percentage determined by adding the percentage increase in the Federal Consumer Price Index for Anchorage from the preceding fiscal year plus the average percentage growth or loss in the Anchorage municipal population over the preceding five fiscal years as determined by the state department of community and regional affairs.
- (b) The limitations set forth in subsection (a) do not apply to the following:
 - (1) Taxes on new construction or property improvements which occur during the current fiscal year.
 - (2) Taxes required to fund additional services mandated by voter approved ballot issues.
 - (3) Special taxes authorized by voter approved ballot issues.
 - (4) Taxes required to fund the costs of judgments entered against the municipality or to pay principal or interest on bonds, including revenue bonds.
 - (5) Taxes required to fund the cost of an emergency ordinance enacted pursuant to 10.03 of the Municipal Charter.
- (c) Any tax increases which result from the exceptions set forth in subsection (b)(1)--(3) shall be added to the base amount which is used in subsection (a) for the calculations of the subsequent year tax increase limit.
- (Initiative, prop. 24, 10-4-83)

Spending Caps

- **6.10.037 Spending limitation on general government operating budget.**
- Per capita expenditures in the general government operating budget for tax-supported services shall be increased over the previous year's budget by amount no more than the percentage increase in the July CPI over the previous July CPI and those additional increases necessary to provide voter and legally mandated services.
- (AO No. 83-50(S), 1-1-84)

Mission (cont.):

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 - Keep current spending caps in place ✓
 - Build on Anchorage's unique role as the economic and commercial hub of the region while recognizing the dynamics of a changing economic environment ✓
 - Incorporate best administrative practices

Incorporate Best Administrative Practices

- Avoid the possible costs of a crisis down the road.
 - Flexibility
 - Adaptability
 - Broaden options

Incorporate Best Administrative Practices

- Create clear obligations that are simple to understand and meet:
 - Clarity important for legal incidence.
 - Clarity impossible for economic incidence
 - It can be researched, modeled, and extremely regressive taxes separated from extremely progressive taxes, but ultimately taxes are just one economic force among many
 - Trade off between broad simple rules and detailed specific rules

Incorporate Best Administrative Practices

- Use Modern Technology:
 - Self reporting by taxpayer
 - Can electronic filing be the norm, and paper available as an alternative?

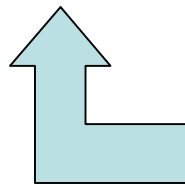
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 - Incorporate best administrative practices ✓

Simple Model of Tax Burden: No Pass Through

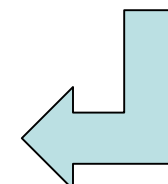
Property tax payers and consumers (including both homeowners and businesses in dual role)

Businesses with gross receipts (some may also pay property taxes and make purchases)



\$130 million in property tax relief

Municipal Government

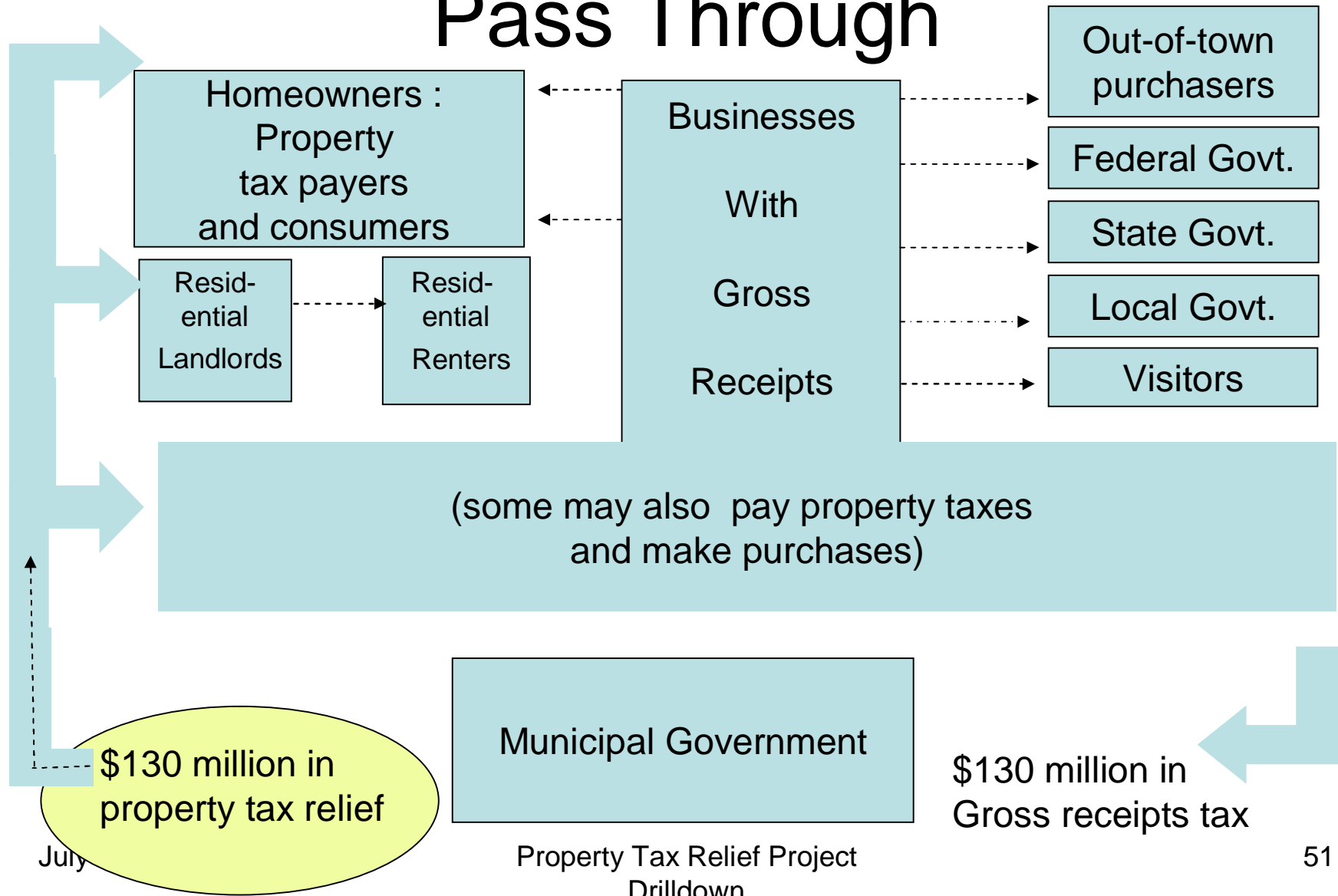


\$130 million in Gross receipts tax

Simple Economic Burden Model i

| | Property Tax | | | | |
|-----------------------|-----------------------|---|--------------|------------|-------------------------|
| | | | No Pass Thru | | |
| | Property Tax Relief % | Property tax relief initially goes to (\$millions): | Fed Tax rate | Fed Tax \$ | Who Ends up with Money: |
| Total: | | 131.40 | | | |
| Owner Occpd Dwlling | 39.0% | 51.20 | 14.0% | (7.20) | 44.00 |
| Residential Landlords | 23.0% | 30.20 | 25.0% | (7.60) | 22.60 |
| Residential Renters | 0.0% | - | | | |
| Misc Res | 3.0% | 3.90 | | | 3.90 |
| Local Gov | | | | | |
| Subtotal | 65.0% | 85.30 | | (14.80) | 70.50 |
| Businesses w/ Real | 26.0% | 34.20 | 31.0% | (10.60) | 23.60 |
| Businesses w/ Pers | 9.0% | 11.80 | 31.0% | (3.70) | 8.10 |
| Non Anch Bus Ownrs | | | | | |
| Subtotal | 35.0% | 46.00 | | (14.30) | 31.70 |
| Feds | | | | 29.10 | 29.10 |
| State | | | | | |
| Export | | | | | |
| Visitors | | | | | |
| Subtotal | 0.0% | - | | 29.10 | 29.10 |
| Sum | | 131.30 | | - | 131.30 |

Simple Model of Tax Burden: Full Pass Through



Modeling Full Pass Through

| | | Total Consumption | Total consumption reallocated on \$18.5 billion base | B to B GRT to final consumer % | Restatement in millions of tax | Just GRT pass through (prices increase) | Allocate just property tax relief (prices decrease) | Both taxes pass through (net price increase) |
|---|------|---------------------|--|--------------------------------|--------------------------------|---|---|--|
| GRT Tax rate: | | | | | 0.710% | | | |
| | | billions of dollars | | | In millions of dollars | | | |
| Household Consumption | | 5.80 | 4.90 | 50% | 34.80 | 65.70 | 23.00 | 42.70 |
| Visitor Consumption | | 0.70 | 0.60 | 6% | 4.30 | 8.10 | 2.80 | 5.30 |
| Government Consumption: | | - | | | - | - | - | - |
| Fed | | 1.50 | 1.30 | 13% | 9.20 | 17.40 | 6.10 | 11.30 |
| Local | | 0.20 | 0.20 | 2% | 1.40 | 2.60 | 0.90 | 1.70 |
| State | | 1.30 | 1.10 | 11% | 7.80 | 14.70 | 5.20 | 9.50 |
| Export Spending | | 2.00 | 1.70 | 17% | 12.10 | 22.80 | 8.00 | 14.80 |
| Subtotal: | | 11.50 | | | | 131.30 | 46.00 | 85.30 |
| Business Spending (Implied Multiplier:) | 1.89 | 10.20 | 8.70 | | 61.80 | | From property tax model | |
| TOTAL | | 21.70 | 18.50 | | 131.40 | | | |
| Tentative exempt. Adj. | | 3.20 | | | | | | |

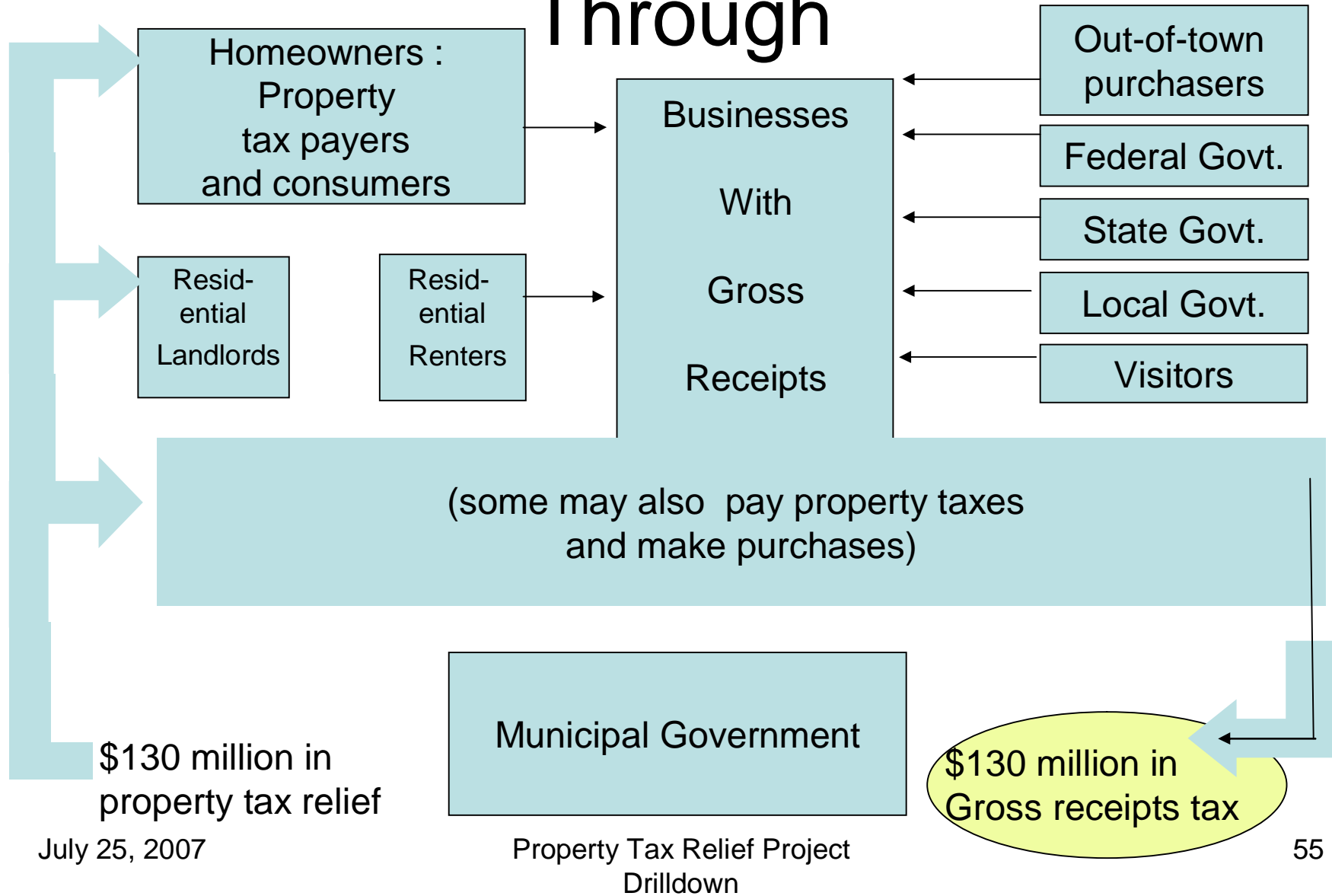
Simple Economic Burden Model ii

| Property Tax | | | | | | | | |
|-----------------------|-----------------------|---|--------------|------------|--|--|---|-------------------------|
| Pass Thru | | | | | | | | |
| | Property Tax Relief % | Property tax relief initially goes to (\$millions): | Fed Tax rate | Fed Tax \$ | Who Ends up with Money before prices lowered | Who receives benefit of property tax relief: Consumption % | Who receives benefit of property tax relief: Consumption \$ | Who Ends up with Money: |
| Total: | | 131.40 | | | | | | |
| Owner Occpd Dwlling | 39.0% | 51.20 | 14.0% | (7.20) | 44.00 | 25.0% | 11.50 | 55.50 |
| Residential Landlords | 23.0% | 30.20 | | | | | | |
| Residential Renters | 0.0% | - | | | 30.20 | 25.0% | 11.50 | 41.70 |
| Misc Res | 3.0% | 3.90 | | | 3.90 | | | 3.90 |
| Local Gov | | | | | | 2.0% | 0.92 | 0.92 |
| Subtotal | 65.0% | 85.30 | | (7.20) | 78.10 | 52.0% | 23.92 | 102.02 |
| Businesses w/ Real | 26.0% | 34.20 | | - | | | - | |
| Businesses w/ Pers | 9.0% | 11.80 | | | | | - | |
| Non Anch Bus Ownrs | | | | | | | n/a | n/a |
| Subtotal | 35.0% | 46.00 | | - | - | 0.0% | - | |
| Feds | | | | 7.20 | 7.20 | 13.0% | 5.98 | 13.18 |
| State | | | | | | 11.0% | 5.06 | 5.06 |
| Export | | | | | | 18.0% | 8.28 | 8.28 |
| Visitors | | | | | | 6.0% | 2.76 | 2.76 |
| Subtotal | 0.0% | - | | 7.20 | 7.20 | 48.0% | 22.08 | 29.28 |
| Sum | | 131.30 | | - | 85.30 | 100% | 46.00 | 131.30 |
| | | | NB: Bus | | 46.00 | | | |
| | | | | | 131.30 | | | |

Simple Economic Burden Model iii

| Gross Receipts Tax | | | | | | |
|-----------------------|-------------------------------------|--------------------|------------|------------------------------|-----------------------|--|
| | Who has legal obligation to pay GRT | No Pass Thru | | | Pas | |
| | | Fed Tax @ 55%*2 5% | Fed Tax \$ | Who Ends up with less money: | Con- - sump- - tion % | |
| Total: | (131.40) | | | | | |
| Owner Occpd Dwlling | | | | | 25.0% | |
| Residential Landlords | | | | | | |
| Residential Renters | | | | | 25.0% | |
| Misc Res | | | | | | |
| Local Gov | | | | | 2.0% | |
| Subtotal | - | | - | - | 52.0% | |
| Businesses w/ Real | 5% (6.60) | 31.0% | 2.00 | (4.60) | | |
| Businesses w/ Pers | 95% (124.80) | 31.0% | 38.70 | (86.10) | | |
| Non Anch Bus Ownrs | | | n/a | n/a | n/a | |
| Subtotal | (131.40) | | 40.70 | (90.70) | | |
| Feds | | | (40.70) | (40.70) | 13.0% | |
| State | | | | | 11.0% | |
| Export | | | | | 18.0% | |
| Visitors | | | | | 6.0% | |
| Subtotal | - | | (40.70) | (40.70) | 48.0% | |
| Sum | (131.40) | | - | (131.40) | 100% | |

Alternate Model of BOT: Full Pass Through



July 25, 2007

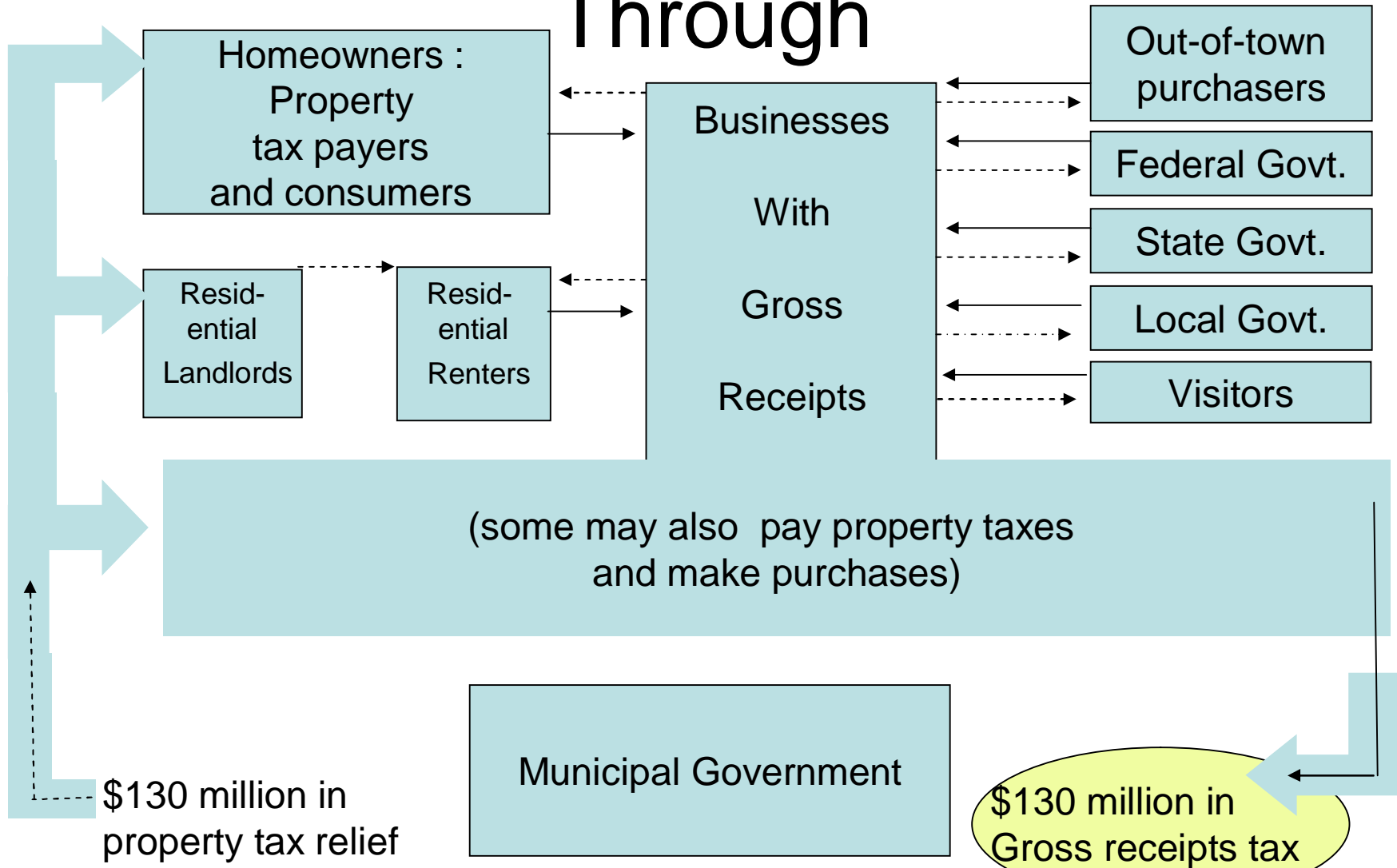
Property Tax Relief Project
Drilldown

Simple Economic Burden Model iv

| Gross Receipts Tax | | | | | | |
|---|-------------------------------------|--------------------|------------|------------------------------|---------------|------------------|
| | | No Pass Thru | | | Pass Thru | |
| | Who has legal obligation to pay GRT | Fed Tax @ 55%*2 5% | Fed Tax \$ | Who Ends up with less money: | Consumption % | GRT Pass Through |
| Total: | (131.40) | | | | | (131.40) |
| Owner Occpd Dwlling Residential Landlords | | | | | 25.0% | (32.90) |
| Residential Renters | | | | | 25.0% | (32.90) |
| Misc Res | | | | | | - |
| Local Gov | | | | | 2.0% | (2.60) |
| Subtotal | - | | - | - | 52.0% | (68.40) |
| Businesses w/ Real | 5% (6.60) | 31.0% | 2.00 | (4.60) | | - |
| Businesses w/ Pers | 95% (124.80) | 31.0% | 38.70 | (86.10) | | - |
| Non Anch Bus Ownrs | | | n/a | n/a | n/a | n/a |
| Subtotal | (131.40) | | 40.70 | (90.70) | | - |
| Feds | | | (40.70) | (40.70) | 13.0% | (17.10) |
| State | | | | | 11.0% | (14.50) |
| Export | | | | | 18.0% | (23.70) |
| Visitors | | | | | 6.0% | (7.90) |
| Subtotal | - | | (40.70) | (40.70) | 48.0% | (63.20) |
| Sum | (131.40) | | - | (131.40) | 100% | (131.60) |

Alternate Model of BOT: Full Pass

Through



July 25, 2007

Property Tax Relief Project Drilldown

Simple Economic Burden Model v: results

| | Percent PT Relief passes through: | Percent GRT passes through: | Percent current PT passes through: | Net Effect reform with elected pass through: | Net Effect |
|-----------------------|--|--------------------------------------|---|---|------------|
| Total: | 50% | 50% | 67% | | |
| Owner Occpd Dwlling | 49.75 | (16.45) | (155.1) | 33.30 | (121.82) |
| Residential Landlords | 11.30 | - | (22.4) | 11.30 | (11.07) |
| Residential Renters | 20.85 | (16.45) | (83.8) | 4.40 | (79.42) |
| Misc Res | 3.90 | - | (11.7) | 3.90 | (7.80) |
| Local Gov | 0.46 | (1.30) | (1.8) | (0.84) | (2.69) |
| Subtotal | 86.26 | (34.20) | (274.9) | 52.06 | (222.80) |
| Businesses w/ Real | 11.80 | (2.30) | (23.4) | 9.50 | (13.86) |
| Businesses w/ Pers | 4.05 | (43.05) | (8.0) | (39.00) | (47.02) |
| Non Anch Bus Ownrs | n/a | n/a | n/a | n/a | n/a |
| Subtotal | 15.85 | (45.35) | (31.4) | (29.50) | (60.88) |
| Feds | 21.14 | (28.90) | (55.3) | (7.76) | (63.06) |
| State | 2.53 | (7.25) | (10.2) | (4.72) | (14.89) |
| Export | 4.14 | (11.85) | (16.6) | (7.71) | (24.35) |
| Visitors | 1.38 | (3.95) | (5.5) | (2.57) | (8.12) |
| Subtotal | 29.19 | (51.95) | (87.7) | (22.76) | (110.42) |
| Sum | 131.30 | (131.50) | (393.9) | (0.20) | (394.10) |

Simple Economic Burden Model vi: results

| | Percent PT Relief passes though: | Percent GRT passes though: | Percent current PT passes though: | Net Effect reform with elected pass through: | Net Effect | Status Quo assuming 50/50 split between local and non local ownership | Adjust assuming 50/50 split between local and non local ownership | Net Effect assuming 50/50 split between local and non local ownership |
|-----------------------|---|-------------------------------------|--|---|------------|---|---|---|
| Total: | 33% | 67% | 67% | | | | | |
| Owner Occpd Dwlling | 47.80 | (22.04) | (155.1) | 25.75 | (129.36) | (187.8) | 30.9 | (156.9) |
| Residential Landlords | 15.14 | - | (22.4) | 15.14 | (7.23) | n/a | n/a | n/a |
| Residential Renters | 13.76 | (22.04) | (83.8) | (8.28) | (92.10) | (83.8) | (8.3) | (92.1) |
| Misc Res | 3.90 | - | (11.7) | 3.90 | (7.80) | n/a | n/a | n/a |
| Local Gov | 0.30 | (1.74) | (1.8) | (1.44) | (3.29) | (1.8) | (1.4) | (3.3) |
| Subtotal | 80.90 | (45.83) | (274.9) | 35.07 | (239.78) | (273.5) | 21.2 | (252.3) |
| Businesses w/ Real | 15.81 | (1.52) | (23.4) | 14.29 | (9.07) | n/a | n/a | n/a |
| Businesses w/ Pers | 5.43 | (28.41) | (8.0) | (22.99) | (31.01) | n/a | n/a | n/a |
| Non Anch Bus Ownrs | n/a | n/a | n/a | n/a | n/a | (32.7) | 5.2 | (27.6) |
| Subtotal | 21.24 | (29.93) | (31.4) | (8.69) | (40.08) | (32.7) | 5.2 | (27.6) |
| Feds | 23.85 | (24.89) | (55.3) | (1.04) | (56.34) | (55.3) | (1.0) | (56.3) |
| State | 1.67 | (9.72) | (10.2) | (8.05) | (18.22) | (10.2) | (8.0) | (18.2) |
| Export | 2.73 | (15.88) | (16.6) | (13.15) | (29.79) | (16.6) | (13.1) | (29.8) |
| Visitors | 0.91 | (5.29) | (5.5) | (4.38) | (9.93) | (5.5) | (4.4) | (9.9) |
| Subtotal | 29.16 | (55.78) | (87.7) | (26.62) | (114.28) | (87.7) | (26.6) | (114.3) |
| Sum | 131.30 | (131.53) | (393.9) | (0.23) | (394.13) | (393.9) | (0.2) | (394.1) |

Issues

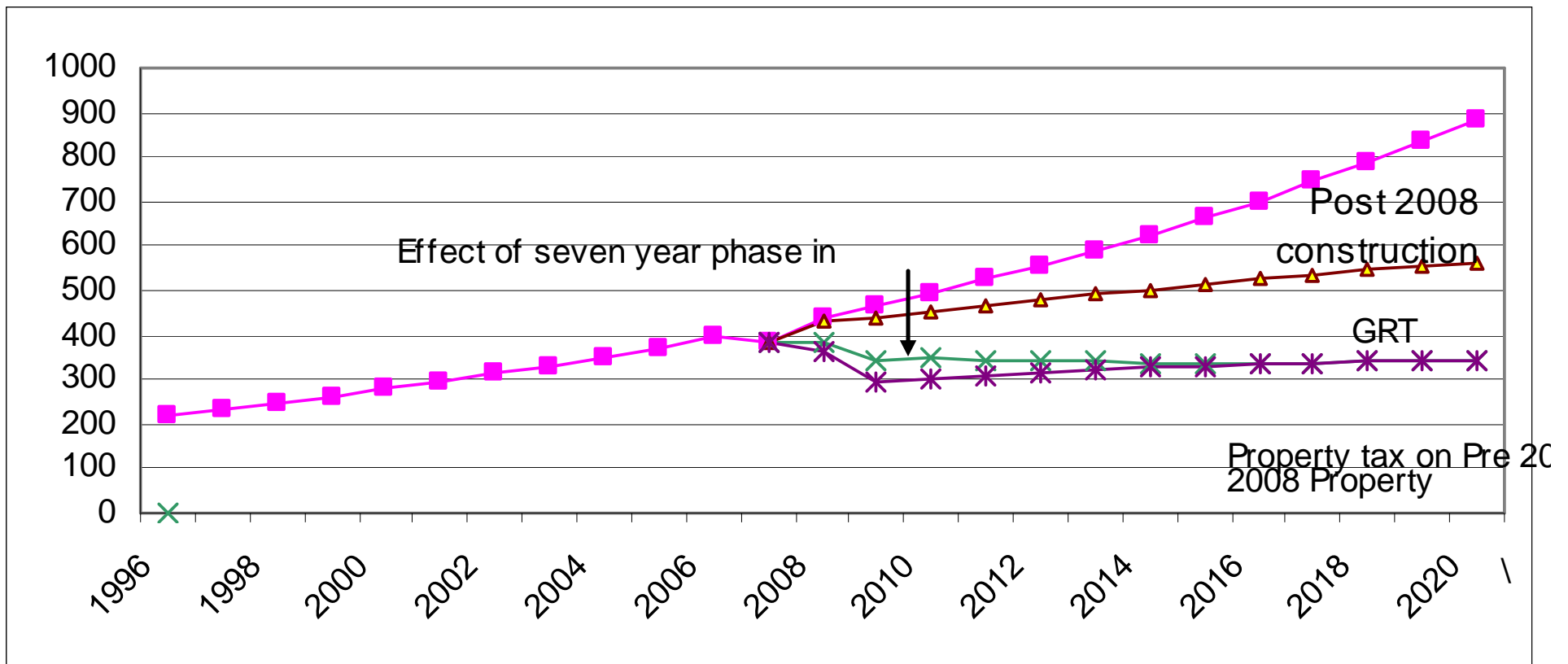
Issue 1: Transition and Rate

- Transition Constraints: Quick imposition of tax
 - Administrative issues for tax payer– ability to identify taxable receipts in real time.
 - Ability to plan and price and sell price changes
 - Administrative issues for city and taxpayer – ability to write rules, and train enough people to be able to answer questions about those rules in time to be helpful.
 - Earliest conceivable transition with a modicum of grace is 10 months from now (August 2007-May 2008) if city can start to prepare as though the tax will be imposed.
 - Means 2008 revenues only 5/12ths of annual.

Issue 1: Transition and Rate

- Suggest other economists review our revenue estimate
- Estimate compliance rate – as a function of cost expended
- Current estimate is in the .70% to .79% range for immediate adoption
- Alternative is .5% for first two years, then seven year phase in to reach full rate.

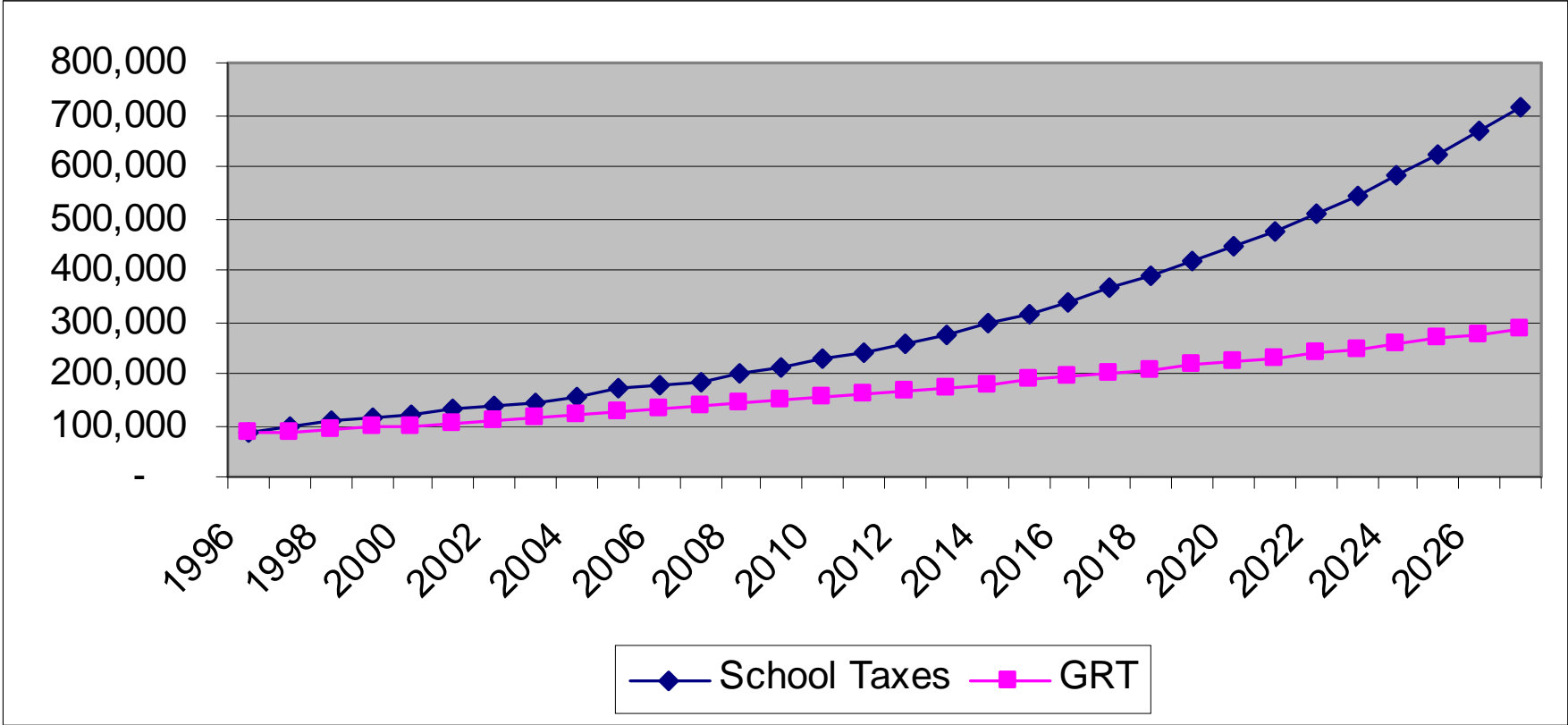
Issue 1: “What have you done for me lately”



Issue 2: Business Personal Property Tax

- Zeroing out means
 - either
 - Higher property taxes on all real property,
 - Higher gross receipts tax on all receipts or,
 - Both.
 - Eliminating one bureaucracy.
- BPPT represents 9% of Property Tax

Issue 3: School District Dedication



Source: School Taxes through 2006 from ASD 2006 CAFR, escalated at 7% Thereafter (historical rate 1996-2006). GRT is 2006 figure escalated or deescalated By ISER 2005 estimate for wage & salary

Issue 4. Small Business Exception: Taxpayer Definition

- How the taxpayer is defined may make clearer who qualifies for small business exemption:
- Pass through entities, S corps, Partnerships?
- One set of rules for corporations focused on defining “intra-company receipts”
- Another set of rules for natural persons?

Issue 4. Small Business Exception: Taxpayer Definition

- Propose that only receipts over a certain amount are taxable:
- Fairbanks proposal \$5/\$10 million
- Ohio “CAT” \$1 million
- Philadelphia: no minimum

Issue 4. Small Business Exception: Taxpayer Definition

- Two issues for corporations and partnerships:
 - What constitutes a single business so that intra-company transactions are not taxed?
 - How many ‘small business exemptions’ does a related group of companies qualify for?
 - Are federal IRC filing rules a good starting place.

Issue 4. Small Business Exception: Taxpayer Definition

- Is a single exemption granted to a natural person, even if they own multiple businesses?

Issue 5. Nexus & Situs

- “Nexus” is the connection required to exist between a taxing jurisdiction and a potential taxpayer such that the state has the constitutional right to impose the tax.
 - US Supreme Court
 - (1976) in Complete Auto Transit requires substantial nexus
 - (1990) in Quill required physical presence for sales tax
 - (2007) declined to hear FIA appeal of economic presence was sufficient nexus for income tax.

Issue 5. Nexus & Situs

- Nexus issues for sales and use taxes and income taxes are vigorously litigated especially with rise of e commerce.
- Can claim broadest nexus allowed under the US and AK constitutions

Issue 5. Nexus & Situs

- “Situs” is the site where something is treated as being for legal purposes.
 - Generally not an issue for retail or restaurants, hotels etc.
 - US Supreme Court (1976) in Complete Auto Transit requires fair apportionment

Issue 5. Nexus & Situs

- “Situs” is the site where something is treated as being for legal purposes.
 - For contracts, services and complex real transactions
 - destination, buyer or benefit rule
 - source or principle place of business of seller rule
 - throwback rule – if not taxed elsewhere

Issue 6: Measurement: when Receipts don't match activity or opportunity

- A firm with a lot of activity but few receipts in Anchorage.
 - Oil industry, Transportation companies that have huge presence here coordinating part of world wide operations, but few “Anchorage” sales.

Issue 6: Measurement: when Receipts don't match activity or opportunity

- Firms where it is difficult to define receipts in Anchorage.
 - Financial services industries where money “changing hands” is not a sale. Loans, insurance, trading.

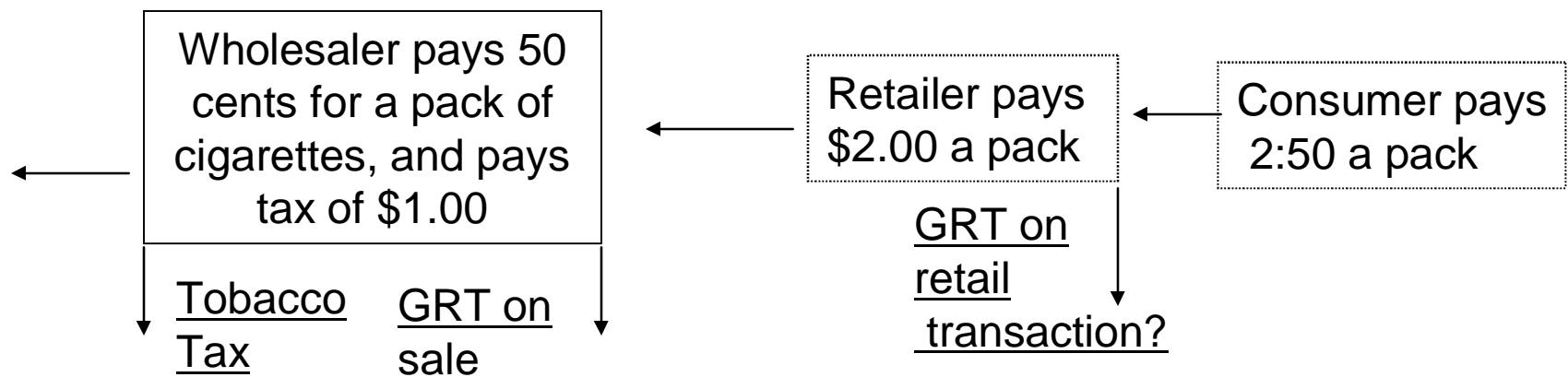
Issue 7: Transactions Already Taxed

| \$ figures in millions | Motor Vehicle Rental | Hotel Room Tax | Tobacco Tax | Sum |
|-------------------------|----------------------|-----------------------------|---|-------|
| 2006 Collections | 5.0 | 19.1 | 17.7 | 41.8 |
| Tax rate | 8% | 12% | 65 mills per cigarette, 45% other tobacco products | |
| Implied Base | 62.6 | 159.1 | 40.0 | 261.7 |
| .75% pro forma tax rate | .5 | 1.2 | .3 | 2.0 |
| July 25, 2007 | | Property Tax Relief Project | | 76 |

Drilldown

Issue 7: Transactions Already Taxed

- Would not apply to?:
- Annual motor vehicle (\$5 million) and airplane registration (\$ 200,000) taxes
- Retail sale of an item for which wholesale tax had been paid



Issue 8: Not-For-Profits

- Seller to a not for profit (or a government) must still pay BAT on that sale.
 - Not a sales tax; nor price discount
- Does a not-for-profit have to pay BAT on its sales:
 - 501(c)(3) charities qualifying for tax deductible contributions
 - 501(c)(4) Civic Leagues, Social Welfare – don't automatically but may qualify for tax deductible contributions
 - 501c other ... not qualifying
 - 527 – political organizations with solicited contributions

Issue 8: Not-For-Profit

- The \$18.5 billion gross receipts estimate is after excluding \$1.2 billion in receipts by establishments that are currently exempt from paying federal income tax:
- Goldsmith (2006) Not for Profit Study estimated total expenditures of \$3.4 billion of which \$1.2 billion was payroll

Issue 8: Not for Profits - Estimate of Not-Profit Anchorage non-donated Receipts

| \$ figures in millions | 501(c)(3) | 501(c)(4) | Other | Sum |
|-------------------------|-----------|-----------|---------|-----------|
| Revenue | \$3,506.4 | \$115.6 | \$869.2 | \$4,491.2 |
| % contributed | 62.6% | 21.0% | 30.0% | |
| \$ not cont | 1,311.4 | 91.3 | 608.4 | 2,011.2 |
| Anch % | 49.5% | 38.4% | 38.4% | |
| Anch \$ | 649.1 | 35.1 | 233.6 | 917.8 |
| .75% pro forma tax rate | 4.9 | .3 | 1.8 | 6.9 |

Source: Goldsmith, The Foraker Group Report on the Alaska Non-Profit Economy December 2006, ISER. Figures generally from 2004.

Issue 9: Web Based Tax

- Tax agencies around the world are spending literally billions of dollars to move from a paper based filing and storage system to more modern data handling methods.
- This tax could skip the paper stage: Need to bring in a champion of web based filing and recognize that up front costs may be higher but will have huge benefits later on.

Issue 10: Enforcement/Structure

- Structure of property tax: Tax is first lien on property. If no one pays tax, city can sell property and collect tax- not cities issue if it can't find owner.
- Structure of Bed, and Car Rental taxes: registration, requirement for bonding (The business is just collecting the tax, handling the taxpayers money.)

Issue 10: Enforcement/Structure

- Structure of business license tax: A license is issued for the privilege of doing business in the jurisdiction. The cost is set by (among other measures), gross receipts. Business can be shut down for failure to pay.(?)
- Structure of Gross Receipts tax; a tax is levied on the gross receipts of an entity.

Issue 10: Is a Business Activity Tax a sales tax?

- A sales tax must be approved by 60% of voters at an election.
- Sales taxes on consumers and Business Activity Taxes/Gross Receipts Taxes on businesses are quite distinct.
- Simplistic argument: “How can a tax measured primarily by sales be anything other than sales tax?”