

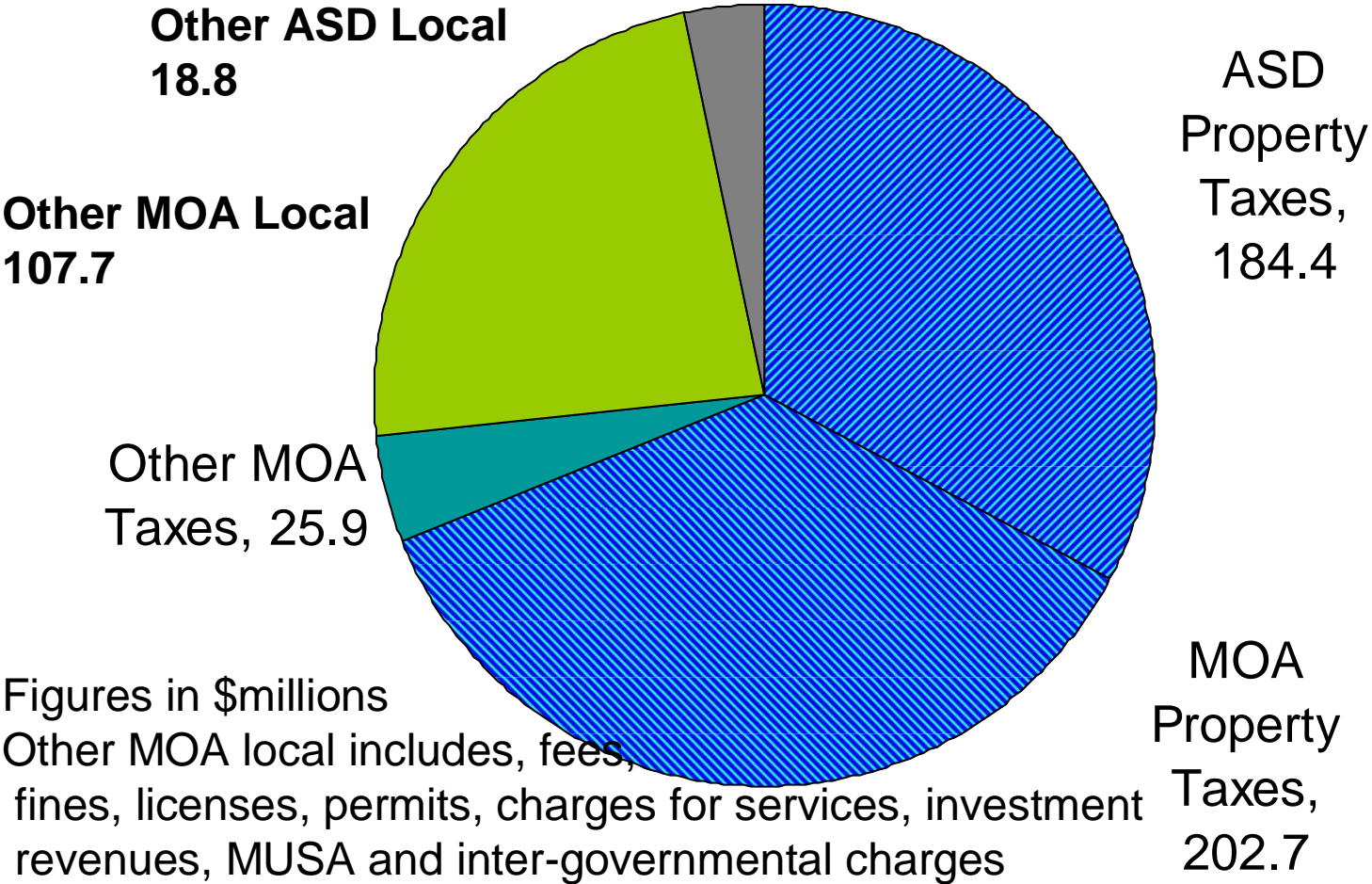
Assembly Work Session on  
The Property Tax Relief /  
Business Activity Tax Project  
Summer 2007

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Anchorage  
April – September 2007

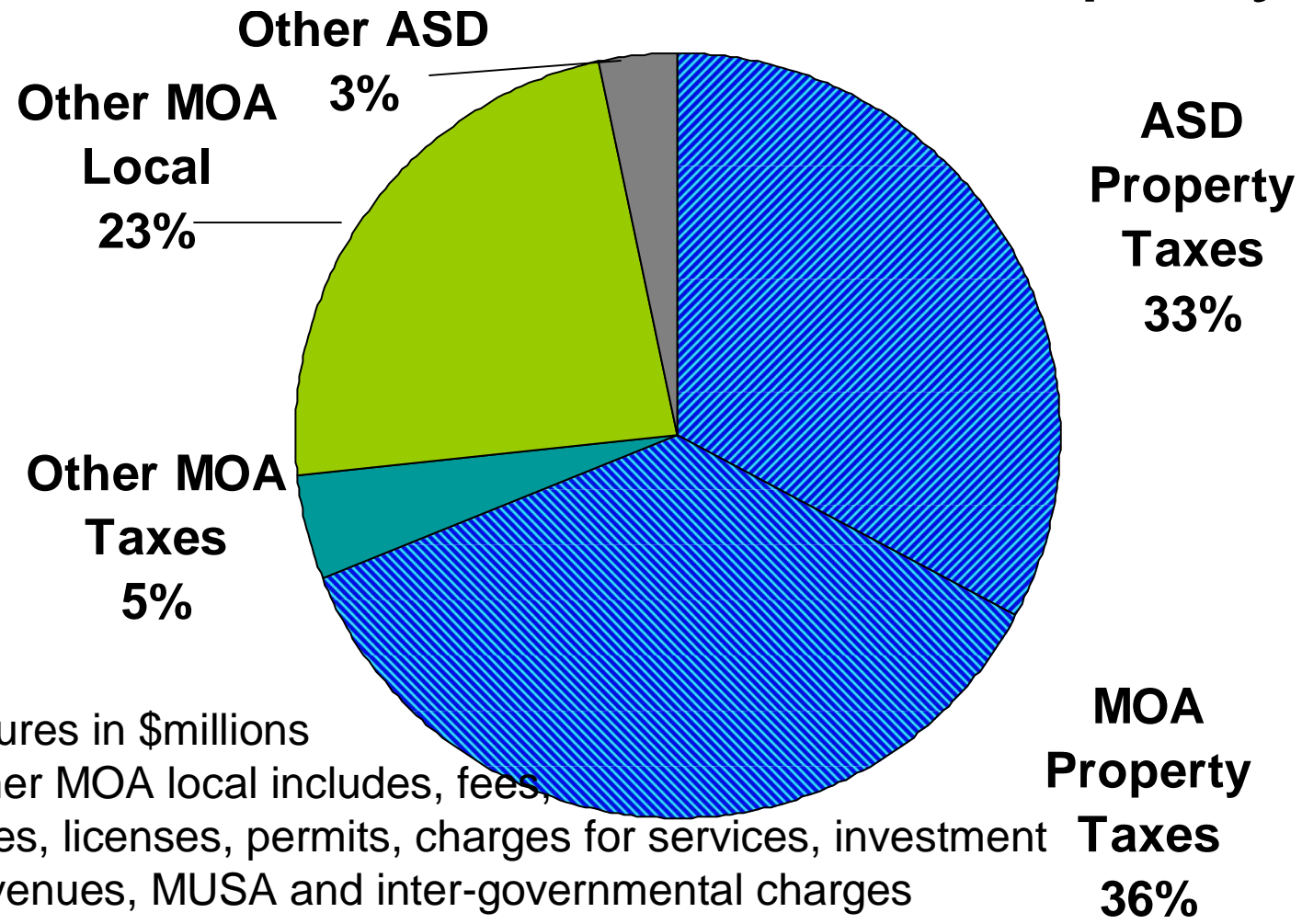
# Outline

- 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.

# 2006 Anchorage Combined Local Revenues - \$562.8 million

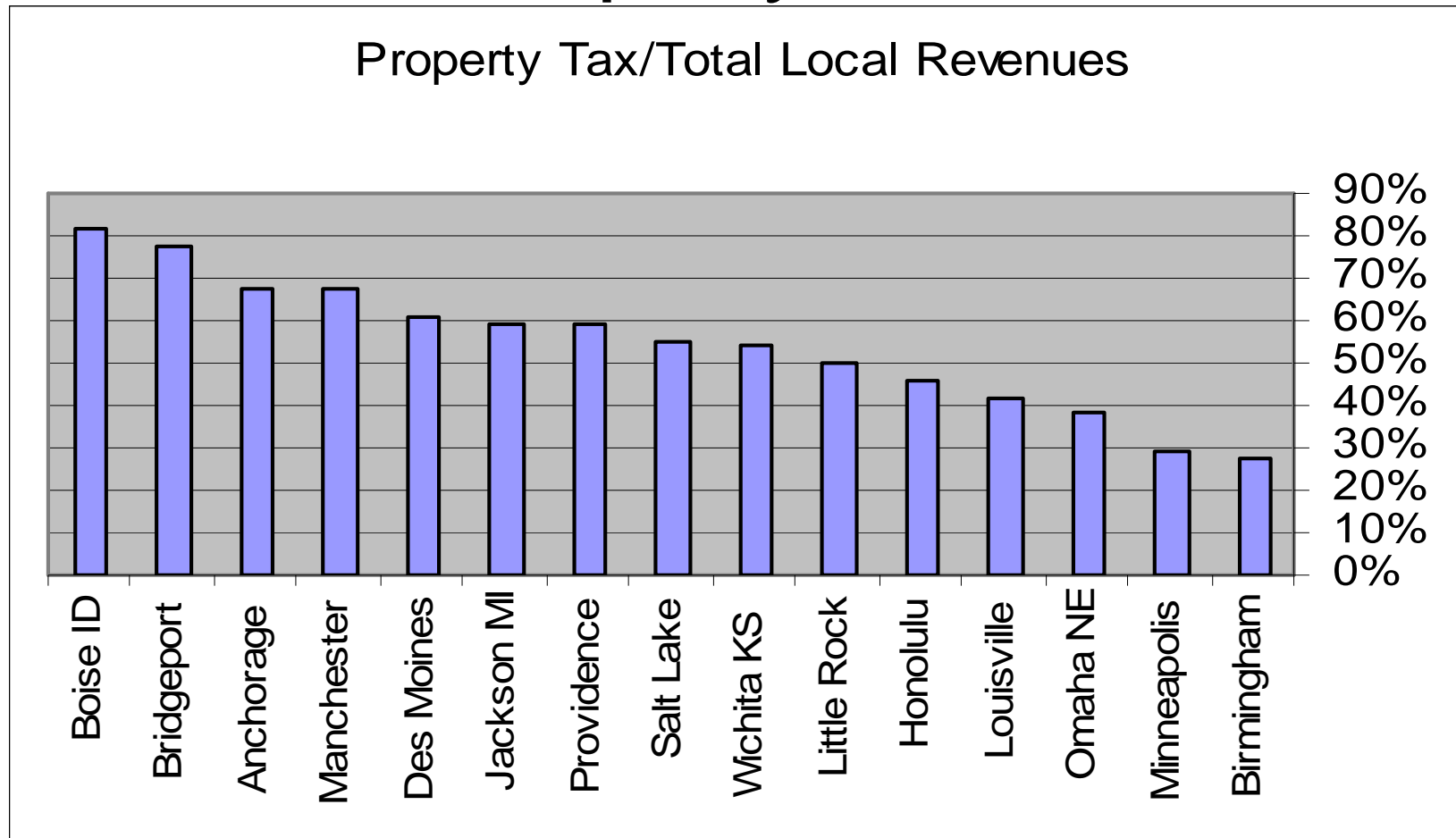


# 2006 Anchorage Combined Local Revenues – 2/3 from Property Tax



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?



10/5/2007 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  
Assembly Work Session

# 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, 51<sup>st</sup> 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 <sup>th</sup>
\$75,000	51	15 <sup>th</sup>
\$100,000	51	14 <sup>th</sup>
\$150,000	51	13 <sup>th</sup>

Source: Tax Rates and Tax Burdens in the District of Columbia – A Nationwide Comparison  
 10/5/2007 Assembly Work Session  
 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.



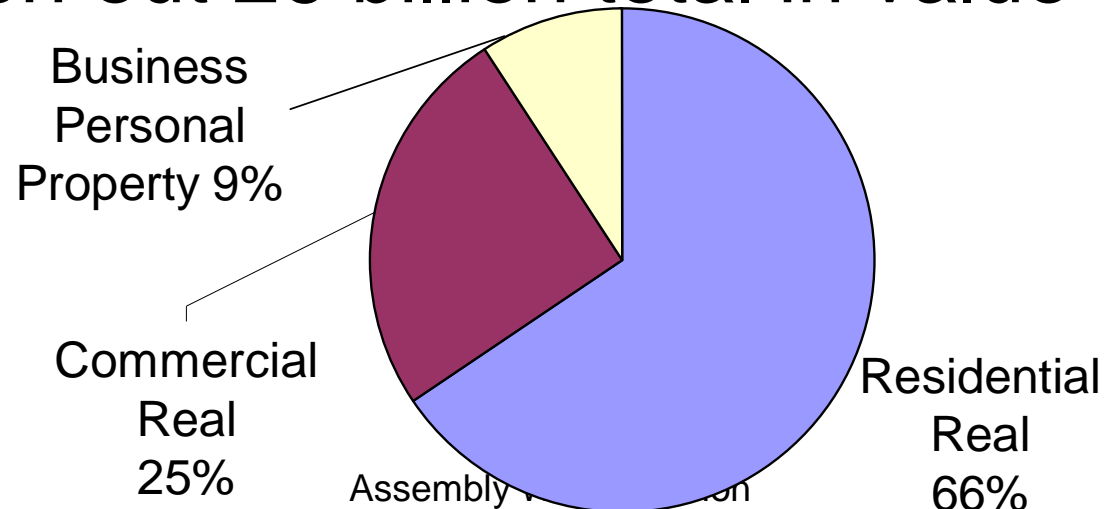
# Why Change Anchorage's Fiscal System?

- (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 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

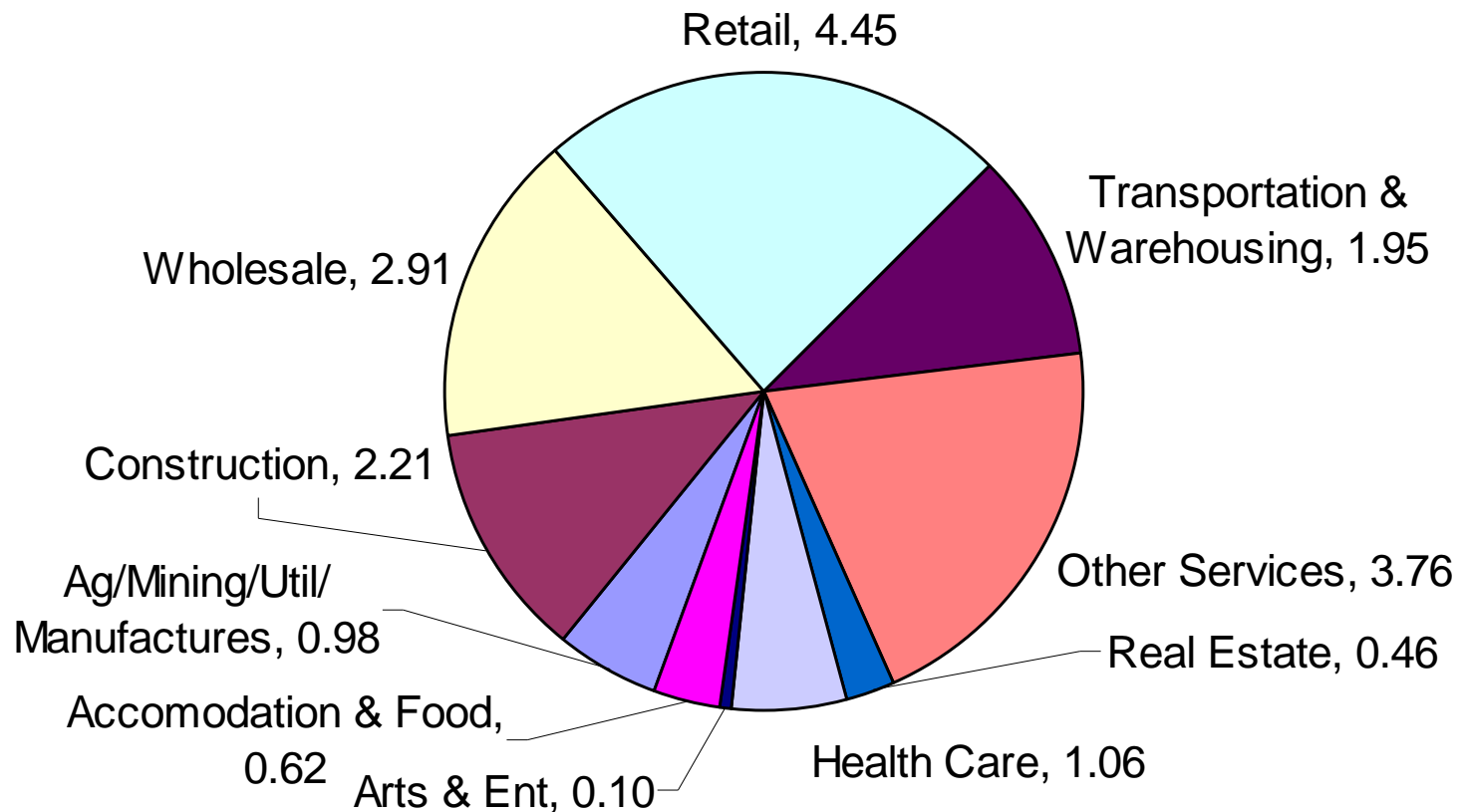
# Is a Business Activity Tax an Answer: (1) Broad base low rate

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

Estimated 2006 tax base in Anchorage:  
18.5 billion dollars in sales

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.)

# 2006 Anchorage Gross Receipts of \$18.5 Billion



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

	Property Value	Mill Rate	Tax Revenue
<b>Current (2006):</b>	\$ 26,045	14.82	\$ 386.0
<b>Reform:</b>			
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	<b>0.70%</b>	\$ 128.7
<b>Sum of Tax Revenues after Reform</b>			\$ 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 taxes. 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”)

# 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

# Is a Business Activity Tax an Answer: (5) Widely used, should reassure rating agencies

- Cities – Extensive use in California, post proposition 13 limits on property taxes.
- \* 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 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.
  - 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%.

# 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”