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of C O M M E R C E

**Anchorage's Tax Cap:
After 25 Years, How Are Taxpayers Doing?**

*Prepared by the Anchorage Chamber of Commerce
State/National Affairs Committee*

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Anchorage's Tax Cap: After 25 Years, How Are Taxpayers Doing?

Stable fiscal policies—both at a State and local level—are necessary for a healthy business climate. For nearly a decade the Anchorage Chamber of Commerce has advocated that the State of Alaska formally adopt a long-range fiscal plan (Attachment A is the Anchorage Chamber board of director's resolution).

With this in mind, the Anchorage Chamber's State/National Affairs committee researched the tools by which governments work to limit spending. The result is this white paper that focuses on a tool used in Anchorage—a limit on tax revenue that was approved by Anchorage voters in 1983.

Revenue Limit Alaska-Style: Municipality of Anchorage's Tax Limitation

Special thanks for assistance to the State/National Affairs committee in advancing our understanding the Municipality's Tax Limit to:

- *Larry Baker, a committee member and former Anchorage Chamber board member, who served on the Anchorage Assembly when this Tax Limitation was implemented;*
- *Joe Griffith, past Anchorage Chamber chair, who was the Anchorage Assembly's budget analyst and wrote the ordinance that implemented the Tax Limit; and*
- *Municipality of Anchorage Manager Mike Abbott and Chief Financial Officer Sharon Weddleton for their background information and technical assistance about operating within the Tax Limit.*

History of Anchorage's Tax Limit

In the early 1980s spending by local government was increasing at an alarming rate, which was being fueled by an unprecedented level of state spending due to the start of North Slope oil production. Anchorage businesses and citizens were concerned that they would be unable to afford the property taxes that would be required in the future to support the spending decisions being made at that time.

The business community and Anchorage citizens expressed these concerns to local officials. The Anchorage Chamber of Commerce, along with the FREE Committee of the Anchorage Women's Club, led an initiative process to put a tax limitation before voters. The purpose was to establish a mechanism that would limit how much taxes could increase each year. The Anchorage Chamber established a speakers bureau and took the initiative directly to service clubs, community groups, and the citizens of Anchorage.

Sufficient signatures were collected and the Municipal Charter amendment (Attachment B) was placed on the October 4, 1983 ballot. It was approved by 58 percent of the voters.

The Tax Limit was straightforward. It placed a ceiling on how much revenue from all

taxes¹ could increase from one year to the next. The limit applied to all² taxes—not just property taxes. Because it applied to total tax revenue, it meant that revenue from a new tax (i.e. the vehicle rental tax implemented in 2001) meant less in property taxes could be collected. As intended, by including all taxes in the limit, it meant a new tax would not give government more money to spend and instead, would reduce the amount of property taxes that could be collected.

The Tax Cap also recognized Anchorage would grow in the future and provided mechanisms by which the total tax revenue could grow annually:

- The limit increases by changes in population, inflation, property improvements, and new construction; and
- It also increases to pay for decisions made by voters, such as general obligation bonds and corresponding operation and maintenance costs.

One year after voters approved the Tax Limitation (also known as the Tax Cap), the Anchorage Assembly approved an “interpretive ordinance” (Attachment C) that prescribed how to calculate the new limit. This ordinance served as the template for calculating the limit each year—until 2003.

Since that time there have been changes that weakened the protection the limit originally provided taxpayers. One substantive change excludes payments by municipal-owned utilities from the Tax Cap and the second changes the base used to calculate the limit each year.

Issue: Municipal Utility, Enterprise Payments

A payment in lieu of taxes, or a PILT, is the equivalent of property taxes usually paid to a government by another government or government-owned entity. The Federal and State governments pay a PILT to Municipality of Anchorage for government-owned buildings or land within the Municipality.

A PILT also is paid by municipal-owned utilities (Municipal Light and Power, Anchorage Water and Wastewater) and enterprises (Port of Anchorage, Merrill Field). These payments are based on the idea that if these utilities were in private hands, these “businesses” would be paying property taxes to the Municipality for the public benefits they receive (i.e. roads, public safety, etc.). The Municipality of Anchorage has named these as a “Municipal Utility Service Assessment,” or MUSA, and “Municipal Enterprise Service Assessment,” or MESA.

From 1984 to 2003, utility and enterprise payments (MUSA and MESA) were considered a payment in lieu of taxes and accordingly, fell under the Tax Limit. The practical effect from a property taxpayer point of view is that these payments reduced the amount of property taxes that could be collected—for every dollar paid by a utility, it meant a dollar less in property taxes would be collected.

¹ Taxes collected by the Municipality are for automobile registration, tobacco, aircraft registration, and motor vehicle rentals.

² There was one tax excluded from the limit—the hotel/motel bed tax.

In 2003 this changed. The Mayor proposed and the Assembly approved Assembly Ordinance 2003-160 (Attachment D), that made two substantive changes: increased how much utilities paid (especially AWWU) and then excluded the payments from the Tax Cap. The practical effect was that this revenue no longer offset property taxes and gave municipal government more money to spend.

The impact of this change has been substantial (keep in mind that utilities collect from ratepayers the revenue to pay their MUSA/MESA):

- In Fiscal Year 2004, MUSA/MESA payments totaled \$9.3 million;
- In FY 2007, a total of \$23.3 million³ was paid by utilities, of which \$16.5 million was from MUSA/MESA (Attachment E details these revenues).

If MUSA/MESA payments still were under the Tax Cap, in FY 2007 \$16.5 million less in property taxes could have been collected. Instead, property owners paid \$16.5 million in taxes; utility rater payers paid \$16.5 million more, which gave the municipality \$16.5 million more to spend.

According to former Assembly member Larry Baker and former Assembly Budget Analyst Joe Griffith, MUSA and MESA payments were to be included in the Tax Cap because they were a property tax equivalent. The decision to remove these payments from the Tax Cap was contrary to the original intent of the Charter amendment.

Notwithstanding the original intent, the Municipal Attorney opined in November 2003 (Attachment F) that an Assembly has the authority to override how MUSA/MESA revenue fits under the Tax Cap—regardless of the Assembly’s intent in 1984. We are not agreeing or disagreeing that the Assembly had the authority to make this change (even though the committee was told prior Municipal Attorneys have advised that an Assembly did not have this authority). Regardless, this demonstrates that if Anchorage citizens want to give binding direction to municipal government, it needs to be in the Municipal Charter. For this reason the Anchorage Chamber State/National Affairs committee recommends that the Municipal Charter be amended to specify that MUSA/MESA revenue falls under the Tax Cap. The Anchorage Chamber committee also recommends that there be a transition period for full implementation of this change in order to minimize the impact of spending reductions that may be required.

Issue: Tax Cap’s Base Calculation

Each year the Tax Cap is recalculated. The amount of taxes collected the prior year serves as the base for the next year. This base is adjusted for several factors including changes in population and inflation, construction that was not taxed the prior year, and voter approved spending such as debt service on bonds. (Attachment G is the tax cap calculations for Fiscal Years 1998 to 2008).

³ In FY 2005, the municipality also re-started collection of a “Utility Revenue Distribution,” that totaled nearly \$1.1 million (another “non-tax revenue” that provided increased revenue to the Municipality).

From 1984 to 2006 there were two numbers that significantly impacted how much in property taxes could be collected. The first was the *maximum amount of property taxes allowed* and the second was the amount of property taxes *to be collected*. Political deference was given to the significance of these two numbers. Mayors and Assemblies first established the maximum amount and then worked to craft a budget that collected less in property taxes than the maximum amount allowed.

This political goal was important because the amount of property taxes *collected* was the base on which the following year’s Tax Cap was built. If \$2 million less in property taxes was collected one year, the base for the following year’s Tax Cap was \$2 million lower. But as some pointed out, using the lower number also meant that the Municipality lost \$2 million in “taxing capacity” in future years.

During this period of time the Municipality also used State general assistance to lower the amount of property taxes to be *collected*. As illustrated in Chart 1, this meant that the base was even lower for the next year—and if a similar level of state assistance were not received the following year, the Municipality would be unable to increase taxes (because of the based used) to make up for the shortfall.

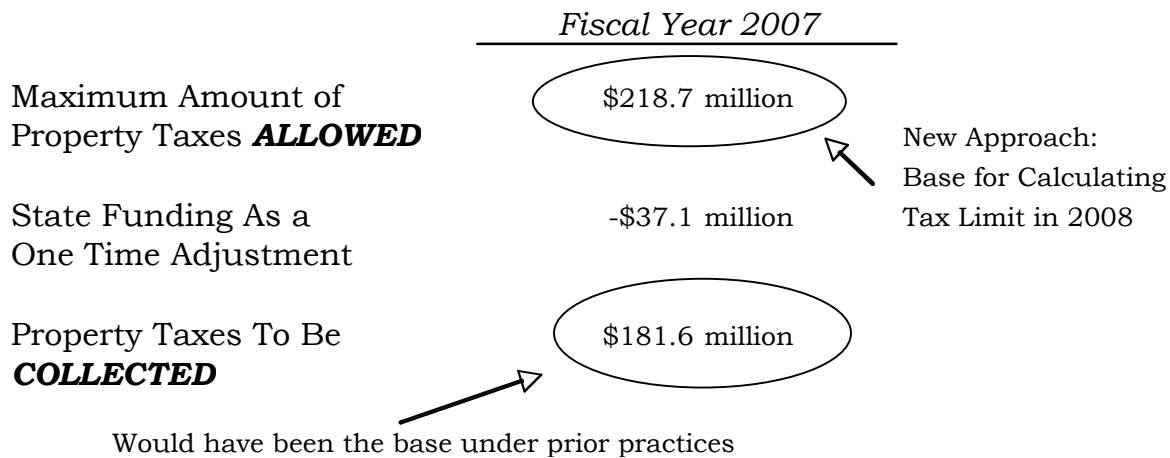
Chart 1.
Base for Calculating Tax Cap Prior to 2007

	<u>Fiscal Year 2000</u>
Maximum Amount of Property Taxes ALLOWED	\$154.4 million
Lowered by Applying State Funding	-\$14.7 million
Property Taxes To Be COLLECTED	\$139.7 million

Base for calculating Tax Limit in 2001

In 2007 and 2008 the Municipality changed the base for calculating the Tax Cap. As illustrated in Chart 2, instead of using the amount *collected*, it used the *maximum* amount that *could have been collected* as the base to calculate the following year’s Tax Cap. To do this it categorized state assistance as a “one-time adjustment” to the amount of property taxes to be collected that one year. This approach meant state funding would not reduce the base to be used in future years—therefore protecting the Municipality’s future “taxing capacity”.

Chart 2.
Change in Base to Calculate Tax Cap



The Anchorage Chamber State/National Affairs was concerned with these recent changes—but we decided not to recommend reverting back to using the amount of property taxes *collected* as the base. While the Anchorage Chamber committee is concerned that these changes could expose taxpayers to substantial increases in the future should state revenues decline substantially, it concluded that officials will need to have options available to make responsible fiscal decisions for which citizens and business will hold them accountable.

Having said that, the Anchorage Chamber committee does believe it important that state financial assistance is judiciously used to minimize the potential for dramatic swings in property taxes. Suggestions include using state revenue for one-time expenses that taxpayers otherwise would pay, retirement of bonded indebtedness, as well as general tax relief.

Issue: Tax Cap’s Inflation Adjustment

The current Tax Cap calculation uses the *one-year* change in the Anchorage Consumer Price Index (CPI) to adjust the Cap. This contrasts with the *five-year average* for population changes that also is used.

Use of a one-year CPI change is challenging because the data is not available on a timely basis. The Municipal Budget must be approved by December even though the Federal government does not release CPI data until the following April. It was suggested during our discussions that there would be benefit to change the inflation adjustment to the same five-year average. This would have a smoothing effect on the impact of this variable each year and minimize the impact of when this information is available.

Issue: Property Tax Exemptions

Anchorage has several widely used residential property tax exemptions. These include a Senior Citizen Property Tax Exemption that excludes the first \$150,000 in assessed valuation from property taxes and a \$20,000 exemption available for owner-

occupied properties.

For understandable reasons, these exemptions are quite popular with those that benefit from them. Residential property tax exemptions, however, impact taxes paid by Anchorage's business community. Because the overarching Tax Cap does not decrease when exemptions are granted to certain groups, the burden to make up for "lost" tax revenue shifts to those property tax payers that are not getting the tax break—business and non-residential property owners.

Some local government officials are advocating that state law be changed to increase the maximum residential tax credit. A statewide initiative (Attachment H) was circulated to increase the residential property tax exemption to \$100,000. The signatures were submitted to the State Division of Elections in April 2008 but the initiative was denied for not having a sufficient number of eligible signatures. Also, legislation has been introduced in the past to expand the current exemption. Such efforts merit close monitoring due to their impact to Anchorage businesses that own property.

Issue: Non-Tax Revenue

There also has been a dramatic increase in non-tax revenue (Attachment I), such as user fees and fines. Between 1998 and 2008:

- Program generated revenue (i.e. user fees, fines) increased 146%—to \$59.8 million from \$24.3 million.
- Non-property tax revenue, interest and MUSA/MESA revenue increased 163%--to \$93.5 million from \$35.5 million.

While the Anchorage Chamber committee recognized that user fees are another way that government "taxes" citizens and is concerned with these dramatic increases, it decided to not study this issue as part of this review—but future increases merit monitoring.

Recommendations

The Anchorage Chamber's State/National Affairs committee recommends that changes be made to ensure the Tax Cap provides taxpayers—including businesses—with a stable tax environment. These recommendations are:

1. Amend the Municipal Charter to specifically state that payments in lieu of taxes, including those paid by utilities, fall within the Tax Cap. If necessary, this change should be phased in order to budgetary minimize impact on municipal services.
2. Amend the Municipal Charter to set aside general financial assistance from the State of Alaska for tax relief measures as appropriate, such as non-recurring obligations and debt service.

3. Amend Chapter 12.25 (Tax Increase Limitation) to prescribe the use of a five-year average for the inflation adjustment.

In addition:

4. The Anchorage Chamber of Commerce should monitor efforts to increase tax exemptions to ensure they are fair to all taxpayers and do not place an unfair burden on Anchorage businesses.
5. The Anchorage Chamber of Commerce should monitor changes in non-tax revenues to ensure they are fair and do not place an unfair burden on the business community and hinder Anchorage's business climate.

Impact of Recommendations

The changes proposed to the tax cap will have a budget impact on the Municipality and the Anchorage School District (ASD). For example, ASD has calculated that, if the five-year average for inflation had been in place over the past five years, ASD would have realized a cumulative loss of \$1.8 million out of a total \$2.4 billion received, though ASD would have received nearly \$1 million more in FY 08/09 (see Attachment M).

Additionally, while it has been the practice of the most recent administration to offset general fund expenses with MUSA/MESA revenues, there is no way to predict how future administrations might allocate budget cuts as a result of bringing those revenues back under the Tax Cap or whether any such budget cuts or impact on services would be material if this white paper's recommendation to phase-in the change over several years is adopted. Attachment E demonstrates MUSA/MESA fees collected over the past ten years to put potential impacts in perspective.

Clearly, if the proposed changes to the tax cap are adopted, policy makers, the public and the Anchorage business community will need to carefully evaluate both the phase-in period over which the changes are adopted and the resulting expected impact on budgets and services.



**Anchorage Chamber of Commerce
Board of Directors
Resolution 2008/09-02
A Resolution Regarding the State/National Affairs Committee Report
“Anchorage’s Tax Cap: After 25 Years, How Are Taxpayers Doing?”**

WHEREAS, the Anchorage Chamber of Commerce recognizes that stability in government fiscal policies are critical to a healthy business environment; and

WHEREAS, the Anchorage Chamber’s State/National Affairs Committee studied tools by which governments provide such stability through limits on spending and revenue; and

WHEREAS, the committee included in its study the Municipality of Anchorage’s Tax Limitation that was created by voters in 1983 as a result of an initiative led by the Anchorage Chamber of Commerce and the FREE Committee of the Anchorage Women’s Club; and

WHEREAS, after substantial analysis of Anchorage’s Tax Limit the committee identified several issues and concerns related to the current application of the Tax Limitation that impact property tax stability for Anchorage business and residential property owners; and

WHEREAS, these issues are addressed through recommendations included in the final report “Anchorage’s Tax Cap: After 25 Years, How Are Anchorage Taxpayers Doing?” and are of importance to Anchorage tax payers; and

WHEREAS, this board has reviewed the report and endorses the recommendations therein; and

NOW THEREFORE BE IT RESOLVED, the Anchorage Chamber board of directors resolves:

1. That the report of the Anchorage Chamber State/National Affairs committee as submitted November 14, 2008 is approved and endorsed by this board.
2. That this resolution and report should be delivered to members of the Anchorage Assembly, Mayor, School Board, and School Superintendent.

Approved the 12th Day of December, 2008

A handwritten signature in black ink, appearing to read 'Phil Okeson'.

Phil Okeson, chair
Anchorage Chamber of Commerce

A handwritten signature in black ink, appearing to read 'Stacy Schubert'.

Stacy Schubert, IOM, president
Anchorage Chamber of Commerce

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Attachments

*Available via the Anchorage Chamber of Commerce's Web site at
Anchoragechamber.org*

- A "In Support of Economic Growth and Long-Term Fiscal Stability", Anchorage Chamber of Commerce Board of Directors Resolution 2006/07-01
- B Municipal Charter Amendment, Section 14.03, Tax Increase Limitation
- C Anchorage Ordinance, Chapter 12.25, Tax Increase Limitation
- D Anchorage Ordinance 2003-160 and Assembly Memorandum 939-2003, "An Ordinance Amending Anchorage Municipal Code Sections 26.10.025 and 12.25.040 Regarding Calculation and Application of Municipal Utility Service Assessments (MUSA); Adding a New Section and Deleting References to Anchorage Telephone Utility"
- E Data: MUSA/MESA Revenue 1998-2008
- F Municipal Attorney Memorandum, November 4, 2003, Concerning MUSA and the Tax Cap
- G Data: Tax Cap Calculations 1998-2008
- H The Residential Tax Exemption Initiative, "An Act Increasing the Maximum Residential Exemption and Providing for Annual Adjustments"
- I Data: Municipal Non-Property Tax Revenue 1998-2008
- J State Tax and Expenditures Limits 2007
- K Constitutional Limit
- L Statutory Budget Reserve
- M Anchorage School District Response and Possible Budget Impact
- N Municipality of Anchorage Response Memo