Cases and Attorney General Opinions (Formal and Informal)
Regarding the Permanent Fund and the Constitutional Budget Reserve

Created by Department of Law
February 3, 2016

The following are the cases and opinions provided to the Senate State Affairs Committee on the topics of the permanent fund and the constitutional budget reserve. Please note these are only representative of the opinions and were selected for relating most closely to the concerns that have been raised relating to the Alaska Permanent Fund Protection Act. More opinions can be provided if further information is needed.

CBR

1. ***Hickel v. Halford*, 872 P.2d 171 (Alaska 1994)** [addresses the definition of "administrative proceeding"]
2. ***Hickel v. Cowper*, 874 P.2d 922 (Alaska 1994)** [seminal case on interpretation of the Constitutional Budget Reserve (CBR) and holding that the earnings reserve account is available for appropriation for purposes of determining what vote is needed to spend from the CBR but the ERA is not included in the pay-back provisions of the CBR]
3. **May 18, 1995, Inf. Op. Att'y Gen., File Nos. 663-95-0475; 663-95-0474** [addressing definition of "administrative proceeding"]

Permanent Fund

4. **August 31, 1977, Inf. Op. Att'y Gen., File No. J-66-106-78** [addresses an extra appropriation to the permanent fund]
5. **September 16, 1977, Inf. Op. Att'y Gen., File No. J-66-107-78** [addresses inflation]
6. **March 10, 1983, Inf. Op. Att'y Gen., File No. 366-484-83** [addresses appropriation of income from and deposits into the permanent fund]
7. **February 6, 1984, Inf. Op. Att'y Gen., File No. 366-405-84** [addresses the appropriation of money from the permanent fund income to replace public assistance payments to individuals lost because of the receipt of permanent fund dividends]
8. **February 12, 1987, Inf. Op. Att'y Gen., File No. 663-87-0356** [addresses an extra appropriation made to the principal of the permanent fund]

9. **June 18, 2003, Op. Att'y Gen., File No. 663-03-0153** [addresses questions concerning the accounting for principal and income of the permanent fund]
10. **June 16, 2009, Op. Att'y Gen., File No. JU2009-200-509** [addresses questions concerning the accounting for principal and income of the permanent fund]

KeyCite Yellow Flag - Negative Treatment
Opinion Amended on Rehearing April 18, 1994
872 P.2d 171
Supreme Court of Alaska.

Walter J. HICKEL, Governor of the State of Alaska, Darrel J. Rexwinkel, Commissioner of the Alaska Department of Revenue, and the State of Alaska, Appellants and Cross-Appellees,
v.
Rick HALFORD, President of the Alaska State Senate, Drue Pearce, Steve Frank, Bert Sharp, Mike Miller, Randy Phillips, Tim Kelly, Loren Leman, George Jacko, Steve Rieger, and Robin Taylor, comprising the Senate Majority of the Eighteenth Alaska Legislative Session, Appellees and Cross-Appellees,
and
Steve Cowper, Appellee and Cross-Appellant.

Nos. S-6124, S-6134.
|
April 4, 1994.
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As Amended on Limited Grant of Rehearing April 18, 1994.

Proceedings were commenced to resolve disputes about the state budget reserve fund containing money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property. The Superior Court, Third Judicial District, Anchorage, John Reese, J., ordered the state to restore funds that had been deposited in the general fund, rather than in the budget reserve fund. Appeal and cross appeal were taken, and expedited review was granted. The Supreme Court, Matthews, J., held that: (1) assessment issued by Department of Revenue (DOR) satisfies all essential elements of an "administrative proceeding" under the state constitutional provision creating the state budget reserve fund; (2) an audit letter was not sufficient to initiate an administrative proceeding; and (3) the decision could be given retroactive effect.

Affirmed and remanded.

West Headnotes (7)

[1] **States**
Special Funds

"Administrative proceeding," as used in state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property, involves adjudication-like proceeding to resolve existing dispute. Const. Art. 9, § 17(a); AS 44.62.360, 44.62.370.

2 Cases that cite this headnote

[2] **States**
Special Funds

"Administrative proceeding," as used in state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property, requires sufficient written notice through document that serves function of complaint to specify nature of dispute and relief requested. Const. Art. 9, § 17(a); U.S.C.A. Const.Amends. 5, 14; AS 44.62.360, 44.62.370.

1 Cases that cite this headnote

[3] **States**
Special Funds

"Administrative proceeding," as used in state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or

litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property, requires that mechanism be set in motion to obtain final and binding resolution of dispute. Const. Art. 9, § 17(a); U.S.C.A. Const.Amends. 5, 14; AS 44.62.360, 44.62.370.

1 Cases that cite this headnote

[4] **States**
Special Funds

Assessment issued by Department of Revenue (DOR) to taxpayer satisfies all essential elements of "administrative proceeding" under state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property; assessment demonstrates existence of dispute, assessment is served on taxpayer, providing notice of dispute, and notice sets in motion mechanisms for resolving dispute. Const. Art. 9, § 17(a); U.S.C.A. Const.Amends. 5, 14; AS 43.05.270, 44.62.360, 44.62.370.

3 Cases that cite this headnote

[5] **States**
Special Funds

Audit letter sent by Department of Revenue (DOR) to taxpayer was insufficient to commence "administrative proceeding" under state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property; letter did not indicate existence of or set in motion mechanism for resolving dispute. Const. Art. 9, § 17(a); U.S.C.A. Const.Amends. 5, 14; AS 43.05.270, 44.62.360, 44.62.370.

Cases that cite this headnote

[6] **Courts**
In General; Retroactive or Prospective Operation

Decision that assessment issued by Department of Revenue (DOR) to taxpayer satisfies all essential elements of administrative proceeding under state constitutional provision creating state budget reserve fund to contain money received by state from termination, through settlement or otherwise, of administrative proceeding or litigation involving mineral lease bonuses, rentals, royalties, or taxes imposed on mineral income, production, or property could be given retroactive effect, despite hardships resulting from repayment of funds that had been deposited in state's general fund. Const. Art. 9, § 17(a-d)

2 Cases that cite this headnote

[7] **Appeal and Error**
Ordering New Trial and Directing Further Proceedings in Lower Court

Remand was necessary for development of record and resolution of scope of protective order against disclosure of information in accounting of receipt and disposition of money under settlement of oil and gas tax dispute which could have divulged identity of individual taxpayer and particulars of its returns. Const. Art. 9, § 17(a); AS 43.05.230, 43.05.230(a).

Cases that cite this headnote

Attorneys and Law Firms

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Before MOORE, C.J., RABINOWITZ, MATTHEWS and COMPTON, JJ., and BRYNER, J., Pro Tem.*

OPINION

MATTHEWS, Justice.

This case requires us to interpret article IX, section 17 of the Alaska Constitution, which establishes the budget reserve fund.[1] ***173** The voters adopted article IX, section 17 in the 1990 general election. It was placed on the ballot after being passed by a legislative resolution approved by a two-thirds vote of each house of the 1990 legislature.

Section 17 requires deposit into the budget reserve fund of all money received by the State after July 1, 1990, "as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation ... involving mineral lease bonuses, rentals, royalties ... or involving taxes imposed on mineral income, production, or property...." § 17(a). Appropriations from the fund require a super legislative majority, *i.e.*, three-fourths of each house. § 17(c). However, if the amount available for appropriation for a given fiscal year is less than the amount appropriated for the previous fiscal year, an appropriation from the budget reserve fund can be made by a majority vote of each house of the legislature. Such an appropriation is limited to the difference between the amount available for appropriation for the fiscal year and the amount appropriated "in the previous calendar year for the previous fiscal year." § 17(b).

The primary issue in this case is the meaning of the term "administrative proceeding" as used in article IX, section 17(a) with respect to mineral taxes. The dispute can only be understood in the context of the applicable statutory and administrative procedures for collection of such taxes.

For all taxes, the tax collection process begins with the filing of the return by the taxpayer. Oil and gas production returns must be filed monthly. AS 43.55.020-.030. Income tax returns must be filed annually. AS 43.20.030. Payments of taxes due must accompany the tax returns. *See* AS 43.20.030; AS 43.55.020. The oil and gas audit division generally audits all taxpayers for all tax periods, with a single audit covering from one to three years, or twelve to thirty-six tax periods. The income and excise audit division also generally audits every oil and gas return filed under AS 43.20. When an audit is complete, the taxpayer is notified of any deficiency by a notice of assessment and demand for payment (hereinafter referred to as the assessment). This is provided for in AS 43.05.245. Assessments must be issued within three years after a return is filed or collection is barred. AS 43.05.260(a).

When a taxpayer receives an assessment, the taxpayer is presented with a number of choices. It may pay the taxes in accordance with the assessment; it may appeal the assessment within sixty days by filing a request for appeal under AS 43.05.240 and 15 AAC 05.010; or it may do nothing. If the taxpayer does nothing, the Department of Revenue (DOR), after the sixty-day period for appeal has expired, may proceed to levy on the taxpayer's property until the tax is collected. AS 43.05.270.

When a taxpayer files a request for appeal with DOR, it may request either an "informal conference" or a "formal hearing." AS 43.05.240(a)(b). If a taxpayer requests an informal conference and the conference does not resolve the dispute to the taxpayer's satisfaction, the taxpayer may request a formal hearing within thirty days after the decision resulting from the informal conference. AS 43.05.240(b)(2). If a taxpayer fails to request a formal hearing within thirty days after the decision of the informal conference, the informal conference decision becomes the final decision of DOR and it may be enforced as such. Informal conference decisions may not be appealed to the courts. AS 43.05.240(d); 15 AAC 05.020(c), .040. Where a formal hearing is requested, either following an informal conference or directly upon filing a request for appeal, the taxpayer is given a formal adjudicatory hearing. 15 AAC 05.030. If the taxpayer is dissatisfied with the result of the formal hearing, the taxpayer may appeal ***174** to the superior court within thirty days after the decision. AS 43.05.240(d).

At any point in this process DOR and the taxpayer may agree on the taxes owed, or the taxpayer may decide to pay the amount claimed by the State either as a result of the assessment, the informal conference decision, or the decision following a formal hearing. DOR has taken the position that funds received after a request for formal hearing must be deposited in the budget reserve fund while funds received before a request for formal hearing are paid into the State general fund. DOR, in other words,

is of the view that an administrative proceeding is not initiated for the purposes of article IX, section 17(a) until a request for formal hearing is made.

During the 1993 legislative session, the legislature appropriated virtually all of the anticipated revenues from the general fund for the fiscal year 1994. Subsequently, a group of legislators who constitute the majority coalition of the Senate (hereafter referred to as the Senate Majority) filed a suit against Governor Walter J. Hickel and Commissioner of Revenue Darrel J. Rexwinkel (hereafter referred to as the State). The suit challenged the deposit into the general fund of funds received after a request for appeal but before a request for formal hearing. Former Governor Steve Cowper filed a similar action. The cases were consolidated. The Senate Majority and Gov. Cowper moved for summary judgment and the State cross-moved for summary judgment.

Following a hearing, the superior court granted the plaintiffs' motions for summary judgment, holding that for the purposes of section 17, administrative proceedings begin once a request for appeal is filed by a taxpayer. The court ordered the State to restore wrongfully allocated funds to the budget reserve fund, with interest, not later than the end of the regular session of the current state legislature.[2] The court noted that preliminary indications were that at least $924,051,580.19 in principal would be required in order to accomplish this. From this order the State has appealed.

The superior court's Final Order and Judgment also ordered the State to provide plaintiffs with an accounting of the receipt and disposition of all monies received after July 1, 1990, as a result of the termination, through settlement or otherwise, of all informal conferences. The accounting is to include the date and amount of money received for each termination. The court also ordered the State to produce its interest computations for settlements received through informal proceedings and "any documents referring to that part of the 1993 settlement of the oil and gas tax dispute with British Petroleum which was allocated to preinformal conference general fund revenues." The court also subjected the accounting and document productions to a protective order, prohibiting the plaintiffs or their attorneys from disclosing the contents of any of the documents.

The State appealed from that portion of the Final Order and Judgment which required the production of the British Petroleum Company (BP) settlement documents.[3] Gov. Cowper cross-appealed, objecting to the confidentiality aspect of the protective order. He also contends that the accounting should include the actual income earned by the State on the settlement funds.

Because of the significant public interest in a speedy resolution of this dispute, we granted the parties' motions for expedited review. Following oral argument on January 26, 1994, we issued an order affirming the first three paragraphs of the Final Order and Judgment of superior court.[4] In addition, we ***175** ordered the parties to brief the question whether an administrative proceeding within the meaning of article IX section 17 begins, in a tax collection context, with the issuance of an assessment. Further, we ordered the parties to brief the question whether, assuming that an administrative proceeding did commence with an assessment, such a ruling should be given prospective effect.[5] We reserved decision on all other issues raised in the appeal and the cross-appeal. In our order we gave summary reasons for our action which we set forth here:

The essential attributes of an "administrative proceeding" as the term is used in article IX, section 17 of the Alaska Constitution are:
1. A dispute must exist.

2. A document reflecting the fact of the dispute which serves a function similar to that of a complaint in a civil action, or an accusation or statement of issues under the Administrative Procedure Act, AS 44.62.360, 370, must be served by one party on the other party.

3. The document must set in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved.

The proceedings which take place after a "request for appeal" is filed under AS 43.05.240(a) and 15 AAC 05.020 clearly have these attributes. For this reason, the first three paragraphs of the judgment of December 14, 1993, are affirmed.

At oral argument, the question was raised whether an assessment marks the beginning point of an administrative proceeding. This question was neither raised nor resolved in the superior court and thus would ordinarily be considered waived for the purpose of this litigation. However, this is a question of substance which can be raised in the future. If it is raised successfully, it could cause fiscal problems of an extremely serious nature. Thus, sound reasons require the consideration of an issue not raised by the parties. *See Vest v. First National Bank of Fairbanks,* 659 P.2d 1233, 1234 n. 2 (Alaska) ("Where ... an issue that has not been raised involves a question of law that is critical to a proper and just decision, we will not hesitate to consider it,

particularly after calling the matter to the attention of the parties and affording them the opportunity to brief the issue."), *reh'g granted*, 670 P.2d 707 (Alaska 1983). For this reason we have ordered supplemental briefing.

Supplemental briefs were submitted by the parties and additional oral argument was held. Both Gov. Cowper and the Senate Majority argue that an assessment begins an administrative proceeding and that a ruling to this effect should not be given only prospective effect. Gov. Cowper argues in addition to the questions ordered briefed that an audit letter which identifies the tax returns to be audited and the information and documents ***176** to be produced at the audit, rather than a subsequently occurring notice of assessment, is the beginning of an administrative proceeding. In addition, Gov. Cowper argues specifically with respect to a settlement with BP which included some years for which no assessment had been issued as well as some years for which an assessment and a notice of appeal had been issued, that, as to the pre-assessment years, the funds received should be included within the budget reserve fund because the funds were received "as a result of the termination ... of an administrative proceeding," even though the particular years in question were not formally part of the administrative proceeding. The State agrees that these questions should be addressed.

The Senate Majority also seeks the resolution of an additional issue. The Senate Majority notes that in our order of January 27, 1994, we indicated that one of the attributes of an administrative proceeding included setting in motion "mechanisms prescribed by statute or regulation under which the dispute would ultimately be resolved." It points out that with respect to royalty disputes as distinct from tax disputes, the State has indicated that the Department of Natural Resources does not have statutory or regulatory procedures by which such disputes are conducted. The State agrees that further guidance on this issue is warranted. Neither party, however, describes the dispute resolution mechanism pertaining to royalties.

We address first the basis for our conclusion that administrative proceedings possess the attributes we identified in the order of January 27th. Next, we conclude that in view of these attributes an administrative proceeding concerning back taxes begins when an assessment is issued. An audit letter does not mark the beginning of an administrative proceeding. We also conclude that our ruling that an administrative proceeding begins with an assessment should not be given solely prospective effect. With respect to the issues characterized by the BP settlement and the questions concerning the procedures used in resolving royalty disputes, we express no opinion as the record before us is insufficient both in terms of underlying facts and development of legal issues for expression of any view. Finally, we hold that on the record before us, the superior court did not abuse its discretion by subjecting the accounting to a protective order, in light of the confidentiality requirements of AS 43.05.230. On remand, however, the superior court remains free to consider whether a more narrow protective order may adequately protect these concerns.

1. *Attributes of an Administrative Proceeding.*

[1] As noted, we set out the following as attributes of an administrative proceeding in our order of January 27, 1994:

1. A dispute must exist.

2. A document reflecting the fact of the dispute which serves a function similar to that of a complaint in a civil action, or an accusation or statement of issues under the Administrative Procedure Act, AS 44.62.360, 370, must be served by one party on the other party.

3. The document must set in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved.

Although there is no single authority which concisely defines an administrative proceeding, examination of case law and Alaska statutes involving adjudicatory administrative proceedings demonstrates that these attributes are common to such proceedings.[6] The context in which the term administrative proceeding is used in section 17, the common meaning of the words, and evidence of legislative and voter intent and purpose also support the recognition of these attributes.

We have previously set forth the appropriate approach to interpreting constitutional language. "Constitutional provisions should be given a reasonable and practical interpretation in accordance with common sense. The court should look to the plain meaning and purpose of the provision and the intent of the framers." ***177** *Arco Alaska, Inc. v. State*, 824 P.2d 708, 710 (Alaska 1992) (citation omitted); *see also Kochutin v. State*, 739 P.2d 170, 171 (Alaska 1987). "Adherence to the common understanding of words is especially important in construing provisions of the Alaska Constitution, because the court must 'look to the meaning that the voters would have placed on its provisions.' " *Division of Elections v. Johnstone*, 669 P.2d 537, 539 (Alaska 1983) (quoting

State v. Lewis, 559 P.2d 630, 637-38 (Alaska), *appeal dismissed*, 432 U.S. 901, 97 S.Ct. 2943, 53 L.Ed.2d 1073 (1977)), *cert. denied*, 465 U.S. 1092, 104 S.Ct. 1580, 80 L.Ed.2d 114 (1984). "Unless the context suggests otherwise, words are to be given their natural, obvious, and ordinary meaning." *Hammond v. Hoffbeck*, 627 P.2d 1052, 1056 n. 7 (Alaska 1981).
Because of our concern for interpreting the constitution as the people ratified it, we generally are reluctant to construe abstrusely any constitutional term that has a plain ordinary meaning. Rather, absent some signs that the term has acquired a peculiar meaning by statutory definition or judicial construction, we defer to the meaning the people themselves probably placed on the provision. Normally, such deference to the intent of the people requires "[a]dherence to the common understanding of words."

Citizens Coalition for Tort Reform, Inc. v. McAlpine, 810 P.2d 162, 169 (Alaska 1991) (citations omitted) (quoting *Johnstone*, 669 P.2d at 539).

Our objective, therefore, is to identify the meaning that the people probably placed on the term "administrative proceeding." We begin by recognizing that administrative agencies today perform a wide range of functions and activities, including supplying services, licensing, investigating, rulemaking, and individualized decision-making in the nature of adjudication. In the proper context investigation, rulemaking, and adjudication all could be labelled "administrative proceedings." In the context of section 17, however, it is extremely unlikely that the people would have understood "administrative proceeding" to mean rulemaking or investigation. First, rulemaking and investigation do not normally terminate "by settlement," as does adjudication, nor would they normally result in the receipt of money as a result of their termination.[7] Second, such an understanding of the term would be contrary to the purpose of the amendment, which was to remove certain unexpected[8] income from the appropriations power of the legislature, and to save that income for future need.[9] Money eventually received as a result of rulemaking, in accordance with the rules adopted, can hardly be called unexpected.

Once we recognize that the people probably understood the term "administrative proceeding" to mean adjudication-like proceedings before administrative agencies, as opposed to rulemaking or investigative actions, our task is to identify the essential attributes of this type of proceeding in order to distinguish between administrative actions which are "administrative proceedings" within the ***178** meaning of section 17 and related administrative actions which are not.[10]

The first attribute an "administrative proceeding" must possess is that a dispute must exist for the proceeding to resolve.[11] This attribute derives from the language of section 17, the voter pamphlet, legislative use of the term, and our recognition that the people understood "administrative proceeding" to mean adjudicatory proceedings.

Article IX, section 17 clearly indicates that an administrative proceeding is a proceeding which may "terminate, through settlement or otherwise." § 17(a). "Settlement," the only specific means listed in the Constitution by which an administrative proceeding may terminate, implies the existence of opposing parties who reach a compromise. "Settlement" thus assumes a preexisting dispute.

This reading is also supported by the voter pamphlet for the 1990 election.[12] Although most of the references in the voter pamphlet to the sources of revenues which would be deposited in the budget reserve fund use language which closely parallels section 17's language,[13] the statement in support of the amendment refers to windfall revenues "that result from pending litigation and tax disputes." When this statement is compared with the constitutional language allocating to the budget reserve fund money received "as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation," it is clear that "tax disputes" refers to administrative proceedings.

The use of the term "administrative proceeding" in the Alaska Statutes also generally supports the existence of a dispute as an essential element in that term's meaning. "Administrative proceeding" is never defined in the Alaska Statutes. In most cases, however, the context in which the term is used demonstrates that an adjudicatory proceeding, usually between an agency of the State and some private individual or entity, is anticipated.[14] As discussed below, such adjudications ***179** are predicated on the existence of an underlying dispute.

Finally, we consider the existence of a dispute to be an essential attribute of an administrative proceeding because it is a common element in all adjudicatory proceedings. For example, *Black's Law Dictionary* defines "adjudication" as "[t]he legal process of resolving a dispute" and "adjudicatory process" as a "[m]ethod of adjudicating factual disputes; used generally in reference to administrative proceedings in contrast to judicial proceedings." *Id.* at 42. Similarly, the formal rules governing administrative adjudications under the

Administrative Procedures Act (APA), AS 44.62.330-.630, clearly anticipate the existence of a dispute before action is taken. For example, an accusation under AS 44.62.360 must set out "the acts or omissions with which the respondent is charged, so that the respondent is able to prepare a defense." AS 44.62.360(1). Both the use of the word "charged" and the recognition of the need for a defense indicate the necessary existence of an underlying controversy or dispute. A statement of issues, as provided for in AS 44.62.370, anticipates that the respondent "must show compliance [with a statute or regulation] by producing proof at the hearing," and must specify "particular matters that have come to the attention of the initiating party and that would authorize a denial of the agency action sought." AS 44.62.370(a)(1)(2). The necessity of one party carrying a burden of production and the possibility that a request for a right or privilege may be denied also indicate the existence of an underlying dispute.[15]

Because a dispute exists in all adjudicatory proceedings, and because the language of section 17 and the voter pamphlet indicate that "administrative proceeding" meant a proceeding involving a dispute, the first essential attribute of an administrative proceeding is that a dispute must exist.

[2] The second essential attribute of an administrative proceeding is that a document reflecting the fact of the dispute, which serves a function similar to that of a complaint in a civil action, or an accusation or statement of issues under the APA, must be served by one party on the other party.[16] This element is required in order to ensure that the procedures we recognize as administrative proceedings meet minimal due process requirements.[17] Although we are not directly concerned in this litigation with the due process rights of the participants in administrative proceedings, minimal due process requirements do define necessary requirements of all adjudicatory proceedings. Without providing at least notice and the ***180** opportunity to participate to those who might be affected, no administrative action can either resolve the dispute to the satisfaction of all of the parties or be considered final despite later objections. *See Wickersham,* 680 P.2d at 1144; *Kerr,* 779 P.2d at 342. Because we conclude that an "administrative proceeding" must be an action capable of finally resolving the issue in dispute, either by the express consent of all of the parties or by reaching a determination which could be accorded finality consistent with due process, we hold that sufficient written notice, specifying the nature of the dispute and the relief requested, is essential to an administrative proceeding. [18]

[3] Our conclusion that an administrative proceeding must be an action which is capable of being accorded finality consistent with the requirements of due process is supported by the language of section 17. The phrase "as a result of the termination, through settlement or otherwise, of an administrative proceeding" clearly implies that an administrative proceeding may terminate with or without the express consent of all of the parties. A party must be aware of the dispute and the existence of the proceedings in order to terminate them by settlement. More importantly, in order for an administrative action to terminate without the consent of all the parties in a manner which may result in the collection of money by the State, individuals affected must have notice and an opportunity to object. Otherwise, no finality will be accorded the administrative agency's decision in any subsequent action.[19]

The third essential attribute of an administrative proceeding-that the document which one party serves on the other must set in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved-derives from the ordinary meaning of the word proceeding and the nature of adjudication.

Webster's Third New International Dictionary 1807 (1969) defines "proceeding" as "a particular step or series of steps adopted for doing or accomplishing something." [20] Our reference to "mechanisms ... under which the dispute will ultimately be resolved" closely parallels the dictionary definition and follows from it.[21]

The two requirements which our "essential attribute" adds to this dictionary definition-that the document served on the other party set these mechanisms in motion and that the mechanisms be prescribed by statute or regulation-follow from the nature of adjudication and from our recognition that a administrative proceeding under section 17 must be capable of being accorded finality.

Adjudicatory proceedings begin with the issuance by one party to the other of a document which serves both as the initiation of the dispute resolution process and as notice ***181** that the process has been initiated.[22] For example, the APA expressly states that filing an accusation or a statement of issues initiates a hearing. AS 44.62.360, .370. Similarly, the civil rules provide that a civil action is commenced by filing a complaint with the court, and that a copy of the complaint must be served on the opposing party. Alaska Rules of Civil Procedure 3, 4. Therefore, it may be said that these documents have legal significance beyond merely providing notice. They also start in motion the coercive force of the law with the ultimate objective

of resolving the dispute. By providing notice, they ensure that the use of this force is fair.

Our recognition that an administrative proceeding necessarily possesses the characteristic of finality requires that the proceeding which is initiated have legal authority to bind the non-initiating party, subject perhaps to further appeal, even if that party disagrees with the solution reached or fails to participate in the resolution. This is a substantive corollary to our earlier recognition that minimum due process is required before binding a party over his objection. Simply put, legal authority to bind a party over his objection, or without his participation in the proceeding, cannot be assumed. Therefore, we require that the mechanisms which attempt to do so be prescribed by law.[23]

This final attribute, more than either of the other two attributes, highlights the difference between the commencement of an administrative proceeding and similar action by a party which does not initiate a proceeding. Unless the document which the first party serves on the opposing party creates a legal obligation on the opposing party to either respond or accept a determination made in the party's absence, then the opposing party is free to ignore the document. If the opposing party is free to ignore the document without consequence, then the document is not part of a proceeding which is capable of finally terminating the dispute without the consent of the opposing party. In other words, so long as the opposing party is free to refuse to participate or to withdraw from any attempt to resolve the dispute without legal consequences, then the attempt may be a settlement negotiation, but it is not an adjudication. By contrast, where the law provides that even an opposing party's complete failure to respond has legal significance and may justify a decision against him or her, then the initial document initiates an adjudication and, provided the other attributes are also present, an administrative proceeding under section 17.

2. *In a tax collection context, an assessment marks the beginning of an administrative proceeding.*

[4] An assessment issued by DOR to a taxpayer under AS 43.05.270 satisfies all of the essential elements of an administrative proceeding.

First, at the time that the State issues an assessment, a dispute does exist. As noted above, a dispute may be defined as "a conflict or controversy; a conflict of claims or rights; an assertion of a right, claim, or demand on one side, met by contrary claims or allegations on the other." *Black's Law Dictionary*, at 472. Prior to the time that an assessment is issued, the taxpayer has either filed or failed to file a return. If the taxpayer has filed a return, this may be considered an assertion by the taxpayer that the amount stated, and only the amount stated, is due. Similarly, if a taxpayer fails to file a return, this may be taken as an implied assertion ***182** that no taxes are due.[24] If DOR then issues an assessment to the taxpayer, demanding additional tax payments (with interest and penalties), then there has been "an assertion of a right, claim or demand on one side, met by contrary claims or allegations on the other" and a dispute exists.[25]

Second, the assessment reflects the fact of the dispute, serves a function similar to a civil complaint or an accusation or statement of issues under the APA, and is served on the taxpayer. The assessment's reflection of the fact of the dispute is self-evident. An assessment is also served on the taxpayer. *See* AS 43.05.245 ("The notice and demand for payment is issued when the notice and demand is delivered to the taxpayer in person or placed in the United States mail, addressed to the last known address of the taxpayer."). The only significant question with respect to this attribute is whether an assessment serves a function similar to a civil complaint or an accusation or statement of issues.

As discussed above, the primary function of each of these documents is to provide written notice to the other party that a matter is being contested and that particular relief is sought. Examination of the assessment notices provided by the State reveal that assessments also serve this function. The assessment letter itself lists a total amount due and demands payment. This constitutes a claim for relief. In addition, computations explaining the amount due are enclosed with the assessment. These constitute specific notice of the matter being contested and the basis for relief. Therefore, the second attribute of an administrative proceeding is present in a notice of assessment.

Third, the notice of an assessment sets in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved. Contrary to the State's arguments, this element does not require that a hearing be convened by the document, so long as the law provides that the document will lead toward a resolution of the dispute regardless of the opposing party's response. It is the legal authority to bind the opposing party, and not the exact means by which that authority is exercised, that is essential.

Therefore, an administrative proceeding can begin before any hearing is initiated, if the law constrains the options of the opposing party on receipt of notice of the

proceeding and provides mechanisms for resolving the dispute irrespective of the opposing party's response. An assessment has this effect. On receipt of an assessment, the taxpayer may 1) pay the assessment; 2) appeal the assessment; or 3) do nothing. If the taxpayer pays, the dispute is resolved. This is similar to a defendant admitting liability in a civil suit. If the taxpayer appeals, the mechanisms provided for by AS 43.05.240 are set in motion to attempt to resolve the dispute. Finally, if the taxpayer does nothing, AS 43.05.270 provides that the State may levy against the taxpayer. Once the sixty-day period for appealing the assessment has expired, however, the taxpayer may no longer challenge the substantive basis of the assessment.[26] The statutory scheme by which an assessment is converted into a debt to the State if no appeal is filed is itself a mechanism for resolving the dispute.

***183** As an assessment possesses each of the essential attributes which we have identified, it marks the beginning of an administrative proceeding in the tax collection process for purposes of Article IX, section 17 of the Alaska Constitution.[27]

3. ***An audit letter does not mark the commencement of an administrative proceeding.***

[5] An audit letter does not satisfy the essential elements of an administrative proceeding. Mere notice of an intention to investigate neither indicates the existence of a dispute nor sets in motion mechanisms for the resolution of a dispute.

No dispute exists when the audit letter is sent. On the contrary, the need for an audit indicates that more information is required before the State can agree or disagree with the taxpayer's return. For this reason, an audit is more properly described as an investigation than an administrative proceeding. *See Mallas v. United States,* 993 F.2d 1111, 1122-24 (4th Cir.1993) (holding that an I.R.S. audit is an investigation and not an "administrative proceeding").

In addition, an audit letter does not set in motion any mechanisms for resolving a dispute, even if a dispute did exist at the time. As an investigative procedure, an audit helps the State to determine what its position is. Nothing in the audit procedure itself can be characterized as an attempt to resolve a dispute.[28]

4. ***Whether our ruling that an administrative proceeding is triggered by an assessment should be given only prospective effect.***

[6] This court set forth the conditions necessary for nonretroactive treatment in *Plumley v. Hale,* 594 P.2d 497, 503 (Alaska 1979):

> 1) the holding is one of first impression, or overrules prior law, and was not foreshadowed in earlier decisions; 2) there has been justifiable reliance on an alternative interpretation of the law; 3) undue hardship would result from retroactive application;[29] and 4) the purpose and intended effect of the holding is best accomplished by prospective application.

We apply these factors both to our initial decision that an informal conference is an administrative proceeding and to our decision today that the notice of assessment marks the beginning of an administrative proceeding in the tax collection process. Although the question of retroactive application arose separately in the course of the proceedings in this case with respect to these two decisions, the analysis is essentially the same.

The first factor is a threshold requirement. *Commercial Fisheries Entry Comm'n v. Byayuk,* 684 P.2d 114, 117 (Alaska 1984). It is satisfied. In *Johnstone,* 669 P.2d at 544, this court held that this requirement was met where "[n]o prior Alaska case has attempted to construe the meaning of the word" and prior nonjudicial opinions "indicated the ***184** presence of real uncertainty." This court has also stated that "if the question answered by the new rule was 'subject to rational disagreement' the threshold showing is met and the court will weigh the remaining criteria." *Truesdell v. Halliburton Co.,* 754 P.2d 236, 239 (Alaska 1988) (quoting *Vienna v. Scott Wetzel Services, Inc.,* 740 P.2d 447, 450 (Alaska 1987)). Although we reject the State's interpretation of "administrative proceeding," we cannot say that it was irrational. Moreover, at the time the State adopted its position, no Alaska case indicated the proper result. We therefore consider the remaining factors.

The second factor-justifiable reliance on an alternative explanation-supports nonretroactive application, but carries relatively little weight. The State has demonstrated that the intended recipients of fiscal year 1994 appropriations have relied on the appropriations. While retroactive application might cause reevaluation of these appropriations, it will not, however, require any specific appropriation to be rescinded. In addition, this reliance is two steps removed from the issue in this case-the proper

allocation of money to the budget reserve fund. The primary focus of concern in weighing this factor is whether the legislative and executive branches justifiably relied on the availability of the monies at issue in this case when making fiscal year 1994 appropriations.

These monies were deposited in the general fund in reliance on a April 24, 1992, Attorney General's Opinion. Even assuming that the State's reliance on the Attorney General's Opinion is an appropriate basis for considering nonretroactive application,[30] at the time that the legislature appropriated the informal conference collection receipts from the general fund, the Attorney General's Opinion had been subject to significant criticism, and the possibility that the money should have been deposited into the budget reserve fund was well recognized.[31] Because the risk of a subsequent judicial decision requiring deposit of these funds in the budget reserve was apparent at the time of the appropriations, we give significantly less weight to this factor.[32]

The third factor-whether retroactive application will result in undue hardship or have a negative effect on the administration of justice-is essentially neutral. Some hardship may be inherent in ordering the State to restore close to one billion dollars, plus interest, to the budget reserve fund after the money has already been allocated. Repayment of this amount could, to a certain extent, require reconsideration of 1994 appropriations. Such reconsideration could, in turn, cause uncertainty and, in some cases, hardship, for those who have relied on the appropriations passed.

Alternatively, however, repayment could be made without hardship from other sources including, most notably, earnings and accumulated earnings from the Alaska Permanent Fund.[33] Moreover, the provisions of section 17 provide the opportunity for significant alleviation or elimination of hardships. First, if and to the extent that removing this amount from the general fund reduces the amount available for appropriation in fiscal year 1994 below the amount appropriated for fiscal year 1993, a simple majority of each house can approve appropriations from the budget reserve fund. Alaska Const. art. IX, § 17(b). Second, to the extent the legislature wishes to continue appropriations for fiscal year 1994 in excess of fiscal year 1993, the legislature can reach the budget reserve fund by an "affirmative vote of three-fourths of the members of each house." ***185** Alaska Const. art. IX, § 17(c). The superior court's decision to effectively stay its order to restore the budget reserve fund until the close of the legislative session, which we affirmed in our January 27 order, allows the State the opportunity to employ these procedures in order to alleviate or avoid hardships.

The final factor to be weighed is whether the purpose and intended effect of the holding is best served by prospective application only. This is "the single most important criterion to use in determining whether to apply a new rule of law retroactively or prospectively." *Byayuk*, 684 P.2d at 118. This factor weighs heavily against nonretroactive application. Where the issue before the court is one of constitutional interpretation, the purpose of the court's holding is to give effect to the purpose of the provision and the intent of the framers. *See, e.g., Citizens Coalition*, 810 P.2d at 168 ("[W]e must never lose sight of another important right of the people implicated in all cases of constitutional construction, namely the right to have the constitution upheld as the people ratified it."); *see also Johnstone*, 669 P.2d at 544 (looking to purpose of constitutional provision in considering this factor).

The purpose of the budget reserve amendment, as well as two of its explicit provisions, would be frustrated or violated by nonretroactive application. The constitutional amendment arose out of concern about a growing gap between spending and revenues. To combat this gap, the reserve fund was proposed to save money against future economic downturns *and* to remove from the current appropriations power certain revenues. Nonretroactive application would frustrate this second purpose by allowing the legislature to appropriate from these revenues close to one billion dollars more than the voters of Alaska intended them to have access to, without meeting the requirements for appropriating out of the budget reserve which are specified in the constitution.

In addition, prospective application would violate the explicit retroactive provision and frustrate the repayment provision of section 17. Section 17 provides that "all money received by the State after July 1, 1990 [from the designated revenues] shall be deposited in the budget reserve fund." Alaska Const. art. IX, § 17(a). The amendment was not voted on until November 1990 and did not become effective until January 1991. At the time it was presented to the voters, therefore, it contained a retroactive provision. By approving the amendment, the voters approved this retroactive provision. Nonretroactive application would ignore the language of the amendment and the intent of the voters.

In addition, nonretroactive application would mean that money which was within the scope of the budget reserve fund, and which should have been deposited into that account, would be subject to allocation without following the procedures required in section 17(b) and (c). Nonretroactive application would also avoid the effect of

section 17(d), which requires that all money appropriated from the budget reserve fund must be repaid out of money remaining in the general fund at the end of a fiscal year. Alaska Const. art. IX, § 17(d).

On consideration of all of these factors, we conclude that nonretroactive application of our decision construing the term "administrative proceeding" and holding that the notice of assessment marks the beginning of an administrative proceeding in the tax collection process would be highly inappropriate. The potential hardships of retroactive application and the State's reliance on a more narrow interpretation than we adopt do not outweigh the importance of giving effect to the constitution as adopted by the people.

5. *The superior court did not abuse its discretion by subjecting the accounting of informal conference settlement receipts to a protective order.*

[7] Alaska Statute 43.05.230 provides that "[i]t is unlawful for a current or former officer, employee, or agent of the state to divulge the amount of income or particulars set out or disclosed in a report or return made under [Title 43]" except under limited circumstances. AS 43.05.230(a). At the time of the superior court's final order, the parties disputed whether the information which would be contained in the accounting, particularly the dates and amounts of individual settlements, would effectively reveal both the identity of individual taxpayers and "particulars" ***186** of their returns. Rather than resolve this dispute on the scant information before it and risk accidentally revealing confidential information, or delay entry of final judgment until the issue could be more fully litigated and thus thwart the strong public interest in a speedy resolution of the underlying dispute over a collateral matter, the superior court granted the protective order and explicitly stated that it was subject to further order of the court. On the record before us, we are unwilling to say that the superior court abused its discretion. On remand, however, the superior court is free to revise this protective order in the light of a more fully developed record.[34]

For the reasons set forth in this opinion, we hold that an administrative proceeding begins, for tax purposes, with the issuance of an assessment to the taxpayer. We express no opinion on the issues characterized by the BP settlement, or on the questions concerning the procedures used in resolving royalty disputes. We remand to the superior court for further proceedings in accordance with this opinion.

All Citations

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Footnotes

* Sitting by assignment made pursuant to article IV, section 16 of the Alaska Constitution.

1 Article IX, section 17 provides as follows:
Budget Reserve Fund. (a) There is established as a separate fund in the State treasury the budget reserve fund. Except for money deposited into the permanent fund under Section 15 of this article, all money received by the State after July 1, 1990, as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation in a State or federal court involving mineral lease bonuses, rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments or bonuses, or involving taxes imposed on mineral income, production, or property, shall be deposited in the budget reserve fund. Money in the budget reserve fund shall be invested so as to yield competitive market rates to the fund. Income of the fund shall be retained in the fund. Section 7 of this article does not apply to deposits made to the fund under this subsection. Money may be appropriated from the fund only as authorized under (b) or (c) of this section.
(b) If the amount available for appropriation for a fiscal year is less than the amount appropriated for the previous fiscal year, an appropriation may be made from the budget reserve fund. However, the amount appropriated from the fund under this subsection may not exceed the amount necessary, when added to other funds available for appropriation, to provide for total appropriations equal to the amount of appropriations made in the previous calendar year for the previous fiscal year.
(c) An appropriation from the budget reserve fund may be made for any public purpose upon affirmative vote of three-fourths of the members of each house of the legislature.
(d) If an appropriation is made from the budget reserve fund, until the amount appropriated is repaid, the amount of money in the general fund available for appropriation at the end of each succeeding fiscal year shall be deposited in the budget reserve fund. The legislature shall implement this subsection by law.

2 It is anticipated that the regular session will end no later than May 10, 1994.

3 At oral argument, the State abandoned this argument as moot, in light of agreement among the parties on the scope of the superior court's production order.

4 These three paragraphs stated:
1. The term "administrative proceeding," as it is used in Article IX, Section 17 of the Alaska Constitution, includes the informal conference process established pursuant to A.S. 43.05.240 and 15 AAC 05.010 and .020.
2. All monies received by the State after July 1, 1990, as a result of the termination, through settlement or otherwise, of all informal conference appeals involving mineral lease bonuses, rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments or bonuses, or involving taxes imposed on mineral income, production, or property, shall be deposited into the Budget Reserve Fund established by Art. IX, Sec. 17 of the Alaska Constitution, along with an amount of money equal to the income which would have been earned on these funds if the funds had been properly placed in the Constitutional Budget Reserve Fund.[1]
[1] The evidence presented by the parties up to the date of this final order suggests that the relevant monies received by the State after July 1, 1990, totals an amount of not less than $951,518.827.86, which total represents at least $924,051,580.19 in principal, plus at least $27,467,247.67 in income which would have been earned.
[3.] The defendants are hereby ordered to restore and fully fund the constitutional Budget Reserve Fund, by not later than the end of the regular session of the Eighteenth Alaska Legislature, consistent with the terms of this order and with Article IX, Section 17 of the Alaska Constitution. Action by the State of Alaska consistent with the constitution and laws of the State which properly obligate these funds is not precluded by this order. (e.g., a ¾ths vote of each house of the legislature to authorize appropriation of part or all of the funds).

5 The order stated:
The parties shall submit supplemental briefs, on a schedule to be established by the clerk, on the following questions:
(a) Whether the notice and demand for payment provided in AS 43.05.245-also referred to as the assessment-triggers the beginning of an "administrative proceeding" within the meaning of article IX, section 17 of the Alaska Constitution; and, if so,
(b) Whether any ruling so concluding should be given prospective effect only.

6 To be distinguished are rulemaking administrative proceedings which are clearly not included within the meaning of the term used in article IX, section 17.

7 In construing the meaning of a statute or constitutional provision, it is necessary to view the words in the context in which they are used. *Homer Elec. Ass'n v. Towsley,* 841 P.2d 1042, 1044 (Alaska 1992).

8 The record is replete with references, in both the legislative history of Senate Resolve No. 129 and the voter pamphlet explaining the proposed constitutional amendment which became section 17, to the need to remove "windfalls" from the normal appropriations power of the legislature. *See* House Finance Fiscal Policy Subcommittee Report No. 3, at 15 (Jan. 10, 1990); House Finance Committee Hearing (May 1, 1990), transcript at 37; Voter pamphlet, statements for and against amendment. "Windfall" is not the most precise of terms. The most relevant definition in *Webster's Third New Int'l Dictionary* 2619-20 (1969), is "an unexpected or sudden gain or advantage."

9 Article IX, section 17 is a response to a perceived impending fiscal crisis resulting from a growing gap between State spending levels and general fund revenues. *See* House Finance Fiscal Policy Subcommittee Report No. 3 (Jan. 10, 1990). To combat this "gap" and the crisis thought to accompany it, the amendment seeks to hold down current spending levels, by preventing the legislature from appropriating certain "windfall" receipts *and* creating a savings fund to help offset future revenue declines. *Id.; see also* Statement in support of Amendment in voter pamphlet.

10 We undertake this "essential attribute" analysis rather than rely on the labels given certain procedures by the legislature or the agencies themselves because it is a necessary step in interpreting the constitution as the people ratified it. Recognizing that the people understood the term "administrative proceeding" to reach the adjudicatory functions of administrative agencies is only a first step. It is not an end in itself. We must also determine what the people would have understood such adjudications to contain. Labels alone cannot answer this question.
Similarly, our use of the term "adjudicatory" and its derivatives to describe the type of proceedings referred to by "administrative proceeding" in section 17 is not meant to graft "adjudicatory" into the Alaska Constitution. It is merely an useful means of distinguishing the type of administrative actions encompassed by the constitutional language from other types of actions which are not included. We might also refer to this type of administrative action as "dispute resolution procedures." For this reason, we do not consider narrow, context-specific definitions of adjudications, like

those described by the Administrative Procedures Act, AS 44.62.330-.630, (APA) to be controlling. Although we look to the APA for help in determining the essential attributes of adjudicatory procedures, the APA also provides procedural protections which serve other functions and are not essential to the concept of adjudication, or individualized decision-making.

11 "Dispute" is defined as "a conflict or controversy; a conflict of claims or rights; an assertion of a right, claim, or demand on one side, met by contrary claims or allegations on the other. The subject of litigation; the matter for which a suit is brought and upon which issue is joined, and in relation to which jurors are called and witnesses examined." *Black's Law Dictionary* 472 (6th ed. 1990).

12 This pamphlet is an authoritative source of the voters' common understanding of section 17. *See, e.g., State v. Lewis,* 559 P.2d at 637-38 (relying on widely distributed report explaining constitutional provisions to Alaska voters as the most "cogent expression of the intent ... of those voting for ratification of the Constitution").

13 The ballot measure refers to money received from "mineral revenue lawsuits or administrative actions." The neutral description of the amendment prepared by the Legislative Affairs Agency uses the term "administrative proceeding." The statement in support of the amendment also refers to "[r]evenues from mineral or oil and gas legal settlements and administrative proceedings."

14 *See, e.g.,* AS 10.13.870 (providing for appeal from "administrative proceedings"; implying that proceeding itself adjudicated rights); AS 14.480.190 (providing for imposition of civil fine in "administrative proceeding"); AS 25.35.120 (referring to parties to an administrative proceeding); AS 34.08.320 (granting association of owners in common interest community the power to "institute, defend, or intervene in litigation or administrative proceedings"). We decline to undertake an extensive analysis of each of the several statutory references to "administrative proceedings" because the use of the term in the statutes is never so specific as to impose a peculiar meaning.

15 We emphasis that a dispute may exist for our purposes even where the non-initiating party immediately agrees with the initiating party's assertions and where the non-initiating party would have been disposed to agree prior to initiation of the proceeding. It is the placing of an issue in controversy, under circumstances that require a response and eventual resolution of the issue, and not the exact means by which a resolution is reached, that indicate the presence of a dispute.

16 The primary function of each of these documents is to provide specific written notice to the other party that rights or obligations between the parties are being contested and that particular relief is being sought. For example, under the APA both an accusation and a statement of issues must be in writing, specify the statute or regulation at issue, include reference to any particular conduct which would justify denial of the right at issue, and be served on the opposing party. AS 44.62.360, .370. Similarly, a civil complaint must contain a statement of the claim showing entitlement to relief and a demand for judgment, and be served on the opposing party. Alaska Rules of Civil Procedure 4, 8. We note that each of these documents also serves to set in motion mechanisms for the resolution of the dispute. We address this function as the third essential attribute of an administrative proceeding.

17 *See Wickersham v. State, Commercial Fisheries Entry Comm'n,* 680 P.2d 1135, 1144 (Alaska 1984) ("An elementary and fundamental requirement of due process in any proceeding which is to be accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action.") (quoting *Mullane v. Central Hanover Bank and Trust Co.,* 339 U.S. 306, 314, 70 S.Ct. 652, 657, 94 L.Ed. 865 (1950)); *see also Kerr v. Kerr,* 779 P.2d 341, 342 (Alaska 1989) ("Notice reasonably calculated to afford the parties an opportunity to present objections to a proceeding, and affording them a reasonable time to do so, is a fundamental requirement of due process.").

18 Our conclusion that minimal due process must be afforded in order for an administrative action to be an administrative proceeding under section 17 does not require either a formal hearing or a right of immediate judicial appeal. Both of these additional conditions relate to whether and to what extent the administrative decision will be subject to judicial review, assuming that the private party is not satisfied with the decision. Our concern, however, is not with the means by which further objections may be pursued, but rather with whether, if no objection is made, the decision will be treated as final.

19 *See, e.g., Black's Law Dictionary,* at 42 ("Adjudicatory hearing" is a "proceeding before an administrative agency in which the rights and duties of particular persons are adjudicated after notice and opportunity to be heard.").

20 In another context, we have stated: " 'Proceedings' has been generally described as 'all the steps or measures adopted in the prosecution or defense of an action.' ... the phrase 'other action or further action or proceeding' as used

in AS 34.20.100 means a form of litigation or some type of in-court proceeding." *Hull v. Alaska Fed. Sav. & Loan Ass'n,* 658 P.2d 122, 125 (Alaska 1983) (quoting *Statter v. United States,* 66 F.2d 819, 822 (9th Cir.1933)). This definition was dependent on the context in which the word was used in the statute and therefore is not directly relevant here, especially given that an *administrative* proceeding will never be an in-court proceeding. Nevertheless, this definition does illustrate the use of the word "proceeding" to signify the series of steps involved in reaching a result.

21 *See also Black's Law Dictionary* at 42 ("Adjudicatory action: Administrative actions are 'adjudicatory' in character when they culminate in a final determination affecting personal or property rights.").

22 The same document need not serve both functions. An adjudication does not begin, however, until both functions have been served. Notice without the initiation of the proceeding is only notice of intent to initiate, requiring further notice. Similarly, until the second party is notified of the initiation of the proceeding, the proceeding cannot be effective as an adjudication. Furthermore, the notice document could not vary from the initiating document without a risk of misinforming the receiving party of the nature of the proceedings. As a practical matter the same document will serve both functions.

23 We do not address the question whether, in a contractual setting involving rentals or royalties, dispute resolution mechanisms prescribed by contract may substitute for such mechanisms prescribed by statute or regulation within the terms of this definition.

24 The taxation statutes of Alaska *require* a taxpayer to file a return if taxes are due. *See, e.g.,* AS 43.20.030(a), 43.55.020-.030. There is no provision which allows a taxpayer to request without penalty that DOR complete its return. If the taxpayer fails to file a return, DOR is authorized to complete a return on the taxpayer's behalf. AS 43.05.245. The taxpayer will, however, be responsible for all penalties associated with failing to file a timely return. Therefore, if an individual or entity fails to file a return, an implied assertion that no taxes are due is made.

25 This is true even if the taxpayer immediately concedes the correctness of the assessment and the error of its own return. At the moment that the assessment is issued, the State and the taxpayer have contrary assertions outstanding concerning the amount of tax owed. Subsequent agreement cannot erase this moment of disagreement. An administrative proceeding requires no greater dispute.

26 In effect a taxpayer's failure to respond to an assessment is similar to a failure to appeal a judgment or a failure to participate in a civil action or an adjudication under the APA. In all of these cases, the party's failure to act has legal consequences. *See* Appellate Rule 204; Civil Rule 55; AS 44.62.530.

27 Because the assessment marks the beginning of an administrative proceeding and because mechanisms which follow from the assessment are part of the proceeding, it is unnecessary to separately discuss application of our essential attribute analysis to the informal conference process.

28 We note that at the time the House Finance Committee amended the legislative resolve that was to become section 17 to include the term "administrative proceeding," the amendment was described as reaching "back taxes that are still under consideration in the Department of Revenue." House Financing Committee Hearing (May 1, 1990), transcript at 38 (comments of budget officer Mary Halloran). We recognize that "back taxes" could conceivably include all taxes received after an original due date, including all amounts received during the course of an audit. This phrase, however, does not control over the language of the constitution itself, which explicitly requires that money for the budget reserve be received as a result of an administrative proceeding.

29 In *Commercial Fisheries Entry Comm'n v. Byayuk,* 684 P.2d 114, 117 (Alaska 1984), the court restated this element as requiring consideration of the effect retroactive application would have on the administration of justice. However this element is stated, it requires an analysis of whether retroactive application will cause more harm than good. *See Johnstone,* 669 P.2d at 545 (stating this element as "whether a holding of retroactivity would cause substantial inequitable results, injustice or harm") (quoting *Warwick v. State ex rel. Chance,* 548 P.2d 384, 395 (Alaska 1976)).

30 We have previously noted that this factor "is generally designed to protect persons who innocently rely on judicial or legislative law rather than agencies which rely on their own regulation." *Byayuk,* 684 P.2d at 119.

31 Members of the legislature had insisted that informal conference settlement proceeds be separately tracked within the general fund. This accounting system was in use at the time these funds were appropriated.

32 This factor carries more weight with respect to monies received after a notice of assessment had been issued but prior to a taxpayer appeal. The possibility that the constitutional language reached such monies was not fully comprehended

until well into the current litigation.

33 The Alaska Permanent Fund was established under article IX, section 15 of the Alaska Constitution.

34 We also reject Gov. Cowper's argument that the accounting ordered by the superior court should include the income actually earned on funds which should have been deposited in the budget reserve but were not. Article IX, section 17 establishes the correct measure of income owed to the fund on monies incorrectly withheld from the fund: "Money in the budget reserve fund shall be invested so as to yield competitive market rates to the fund." § 17(a). The State proposed calculating the interest due on the amount in controversy based on the actual return received by the fund for the relative time periods. The superior court ordered the State to provide Gov. Cowper and the Senate Majority with these computations. Unless the plaintiffs can show reason why this is not an accurate means of calculating the interest owed, no further information is necessary. Our ruling on this point should not be read as suggesting that the income actually earned is not public information available to any member of the public even in the absence of litigation. Such information is, however, not relevant to the remedy in this case.

End of Document

10. **June 18, 2003, Op. Att'y Gen., File No. 663-03-0153** [addresses questions concerning the accounting for principal and income of the permanent fund]
11. **June 16, 2009, Op. Att'y Gen., File No. JU2009-200-509** [addresses questions concerning the accounting for principal and income of the permanent fund]

874 P.2d 922
Supreme Court of Alaska.

Walter J. HICKEL, Governor of the State of Alaska, Darrel J. Rexwinkel, Commissioner of the Department of Revenue for the State of Alaska, and the State of Alaska, Petitioners and Cross-Respondents,
v.
Steve COWPER, Respondent and Cross-Petitioner.

Nos. S-6294, S-6304.
|
May 27, 1994.

Action was brought challenging as unconstitutional statute defining terms contained within section of the Alaska Constitution establishing budget reserve fund. The Superior Court, Third Judicial District, John Reese, J., declared statute unconstitutional, and the state petitioned for emergency review. Petitioner cross-petitioned on same issue. After granting petitions, the Supreme Court, Matthews, J., held that statute was unconstitutional because it did not provide accurate definition of constitutional terms.

Affirmed.

Attorneys and Law Firms

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Douglas Pope, Thomas A. Ballantine, Wagstaff, Pope & Katcher, Anchorage, for respondent and cross-petitioner.

Before MOORE, C.J., RABINOWITZ, MATTHEWS and COMPTON, JJ., and BRYNER, J. Pro Tem. [*]

MATTHEWS, Justice.

OPINION

In *Hickel v. Halford,* 872 P.2d 171 (1994) (*Halford*), we addressed the meaning of the term "administrative proceeding" as used in article IX, section 17 of the Alaska Constitution. [1] This is one of the terms which describes state revenues which must be deposited into the budget reserve fund. We are now required to interpret several other key terms of section 17, including "amount available for appropriation" and "amount appropriated for the previous fiscal year." § 17(b). These terms govern the legislature's ability to withdraw from the budget reserve fund by a simple majority vote.

This case arises out of a legislative attempt to define these terms. While final decision in *Halford* was pending, the Alaska Legislature passed and Governor Hickel signed Senate Committee Substitute for Committee Substitute for House Bill 58 (FIN) (the Act). Chapter 5, SLA 1994. Section 1 of the Act amends AS 37.10 by adding new sections AS 37.10.410 and .420. Alaska Statute 37.10.410 defines what money is received as a result of the termination of an administrative proceeding under article IX, section 17(a) of the Alaska Constitution. Alaska Statute 37.10.420 defines several other key phrases and concepts used in section 17, including "amount available for appropriation," "amount appropriated for the previous fiscal year," and "amount of appropriations made in the previous calendar year for the previous fiscal year." Alaska Statute 37.10.420 also establishes the means by which appropriations from the budget reserve fund are ***924** repaid. [2] Section 2 of the Act states that the provisions of section 1 "are declaratory of existing law and represent the intent of the legislature when the Sixteenth Alaska State Legislature passed [the resolution proposing the constitutional amendment creating section 17]." Ch. 5 SLA 1994.

Following passage of the Act, the current respondent and cross-petitioner, former Governor Steve Cowper, applied to this court for a limited remand in the pending *Halford* case so that he could challenge the constitutionality of the Act. [3] Petitioners and cross-respondents, Governor Walter J. Hickel, Commissioner of Revenue Darrel J. Rexwinkel, and the State of Alaska (hereafter referred to as the State), applied to this court for original jurisdiction to consider the constitutionality of the Act. We granted a limited remand to the superior court so that Gov. Cowper could move to amend his complaint in order to challenge the constitutionality of the Act. [4]

On remand, the consolidated cases were severed and Gov. Cowper was allowed to amend his complaint to allege that the Act was unconstitutional. He then moved for partial summary judgment on this question. The State also moved for a partial summary judgment declaring the Act constitutional.

The superior court granted expedited consideration of the summary judgment motions. Following briefing and oral argument, the court declared the Act unconstitutional on April 8, 1994.[5] In a written decision the superior court held that AS 37.10.420 is unconstitutional because it unduly limits the funds counted as available for appropriation. The court explained that "[i]f a simple majority vote can withdraw the funds ... it is ***925** available for appropriation ... [unless] it belongs to someone else ... or would not be there without the purpose and permission of the source." The superior court also ruled that AS 37.10.420(b), which provides for repayment of funds appropriated out of the budget reserve, unconstitutionally limits the source of these funds. The superior court did not attempt to identify which funds were and were not available for appropriation under section 17(b).

The State petitioned this court for emergency review of the superior court's decision with respect to AS 37.10.420. Gov. Cowper cross-petitioned on the same issue. We granted both petitions. After expedited briefing, we heard oral argument on April 22, 1994.

I. *STANDARD OF REVIEW*

The State argues that this court should defer to the legislature's interpretation of section 17. The State bases this argument on a "strong presumption" in favor of legislative interpretations, *State ex rel. Udall v. Colonial Penn Ins. Co.*, 112 N.M. 123, 812 P.2d 777, 783 (1991), and the presumption that statutes are constitutional, *Bonjour v. Bonjour*, 592 P.2d 1233, 1237 (Alaska 1979). Further, the disputed terms in section 17(b) involve appropriations, and the power to appropriate is wholly legislative, Alaska Const. art. IX, § 13. The State misconstrues the applicable standard of review.

The cases cited by the State do not support the proposition that courts should defer to legislative interpretations of ambiguous constitutional provisions. On the contrary, in each of the cases cited by the State, the court clearly is engaged in interpreting the constitutional provision.[6] Nor does the legislature's role in making appropriations somehow alter or increase its authority to define constitutional terms merely because the terms contain the word "appropriation." This court retains the same power to interpret constitutional terms regardless of the subject matter of the term.[7]

***926** **[1]** This court's task, therefore, is identical to that faced whenever a statutory enactment is claimed to run afoul of a constitutional provision. "Questions concerning the constitutionality of a statute are questions of law and are reviewed *de novo*." *Sun v. State*, 830 P.2d 772, 775 n. 4 (Alaska 1992). We must first determine what the constitution actually means. The proper interpretation of a constitutional provision is a question of law to which this court applies its independent judgment. *Arco Alaska, Inc. v. State*, 824 P.2d 708, 710 (Alaska 1992). We then examine the statute to see whether it conflicts with the constitutional requirement. "[S]tatutes should be construed if reasonably possible to avoid the conclusion that they are unconstitutional." *Sonneman v. Hickel*, 836 P.2d 936, 940 (Alaska 1992).

The appropriate approach to interpreting language in the Alaska Constitution is well established. "Constitutional provisions should be given a reasonable and practical interpretation in accordance with common sense. The court should look to the plain meaning and purpose of the provision and the intent of the framers." *Arco Alaska*, 824 P.2d at 710; *see also Kochutin v. State*, 739 P.2d 170, 171 (Alaska 1987). Because of our concern for interpreting the constitution as the people ratified it, we generally are reluctant to construe abstrusely any constitutional term that has a plain ordinary meaning. Rather, absent some signs that the term at issue has acquired a peculiar meaning by statutory definition or judicial construction, we defer to the meaning the people themselves probably placed on the provision. Normally, such deference to the intent of the people requires "[a]dherence to the common understanding of words."

Citizens Coalition for Tort Reform, Inc. v. McAlpine, 810 P.2d 162, 169 (Alaska 1991) (citations omitted) (quoting *Division of Elections v. Johnstone*, 669 P.2d 537, 539 (Alaska 1983)).

II. *DISCUSSION*

A. "Amount Available for Appropriation"

[2] The primary issue in this case is the meaning of the term "amount available for appropriation" as used in article IX, section 17(b) of the Alaska Constitution.[8] The State asserts, in accordance with the definition set forth in AS 37.10.420(a)(1), that the "amount available for appropriation" consists only of 1) unrestricted revenue accruing to the general fund during the fiscal year; 2) general fund program receipts as defined in AS 37.05.146;[9] 3) the unreserved, undesignated ***927** general fund balance carried forward from the preceding fiscal year; and 4) the balance in the statutory budget reserve fund, AS 37.05.540. In addition

to the program receipts excluded under AS 37.05.146, this definition excludes the funds listed in AS 37.05.146, several other funds which have been established by the legislature, [10] and the surplus assets of public corporations. [11] Gov. Cowper argues that the "amount available for appropriation" includes the total amount accessible by the legislature, including all of the funds and assets referred to above. Under this argument, funds are available for appropriation so long as a simple majority can make the funds available.

We reject both interpretations. The text of section 17 cannot support the State's narrow interpretation. However, Gov. Cowper's position would require a complete restructuring of the established financial system of the state government. We are unwilling to add "missing terms" to the Constitution or to interpret existing constitutional language more broadly than intended by the framers or the voters. Instead, we consider it appropriate, as well as consistent with both the language of the amendment and the intent of the framers, to focus on the legal status of the various funds implicated in relationship to the legislative power of appropriation. The "amount available for appropriation" must include all funds over which the legislature has retained the power to appropriate and which are not available to pay expenditures without further legislative appropriation. It must also include all amounts which the legislature actually appropriates for the fiscal year, whether or not they could have been considered available prior to the appropriation.

Our analysis of a constitutional provision begins with, and remains grounded in, the words of the provision itself. We are not vested with the authority to add missing terms or hypothesize differently worded provisions ***928** in order to reach a particular result. [12] Our task is to identify the meaning that the people probably placed on the term. *Halford,* 872 P.2d at 176. The dictionary definitions of the controlling words "amount" and "available" provide a helpful starting point. *Webster's Third New International Dictionary* defines "amount" as "a: the total number or quantity ...; b: the sum of individuals ...; c: the quantity at hand or under consideration." *Id.* at 72. Relevant definitions of "available" are "3: such as may be availed of: capable of use for the accomplishment of a purpose: immediately utilizable ...; 4: that is accessible or may be obtained ...: at disposal esp. for sale or utilization." *Id.* at 150.

From similar dictionary definitions, Gov. Cowper paraphrases "amount available for appropriation" as meaning "the total funds accessible by the legislature for appropriation." He further interprets this paraphrase as meaning that all funds which the legislature can make available to itself by a majority vote, whatever their current use or designation, are "available for appropriation." [13] At the outer limits, this construction would require that all net assets held by the State, however liquid, be considered available in determining whether the amount available was less than the amount appropriated for the previous year. [14] Such an expansive reading of the constitutional language would render section 17(b) superfluous for all practical purposes. [15] It would also involve the adoption of a radically different approach to government financing. Neither result is consistent with the purpose of the amendment, the intent of the framers, or extrinsic indications of the voters' probable understanding of section 17's terms.

Section 17(b) allows a simple legislative majority to use the constitutional budget reserve fund in order to make up the difference between the "amount available for appropriation" for a given fiscal year and the "amount appropriated for the previous fiscal year." If net state assets are included in the total amount available, then they would have to be actually expended before the budget reserve fund could be reached by a simple majority to keep spending at a constant level. Even if we consider only net assets which exist in a cash form-such as the balances contained in ***929** any one of the State's several revolving loan funds [16] -the existing state programs dependent on these funds would have to be curtailed if these funds were expended on another purpose. These funds are maintained, however, because in the judgment of the legislature they serve worthwhile purposes. Therefore, one of the uses the legislature presumably would want to make of the newly available money would be to reestablish these funds. Yet, to the extent that any of these funds were started and funded before the previous year, there would not be an equivalent appropriation in the previous year to balance out the appropriation required in the present year. Gov. Cowper's interpretation of section 17(b)'s majority access formula would, in effect, require reductions in the level of government service until no liquid funds remained before a simple majority could reach the budget reserve.

One of the purposes of the budget reserve amendment, however, was to provide a "stabilizing mechanism" in the budgetary process. [17] The formula in section 17(b), which compares funds currently available to the amount appropriated for the previous fiscal year, and allows simple majority appropriation from the budget reserve fund to the

extent necessary "to provide for total appropriations equal to the amount of appropriations made in the previous calendar year for the previous fiscal year," Alaska Const. art. IX, § 17(b), reflects this purpose and clearly anticipates use of the budget reserve fund to maintain "equal" appropriation levels from year to year. Gov. Cowper's interpretation is inconsistent with this purpose because it would only allow simple majority access to the budget reserve fund if all state programs involving cash funds were eliminated or if state spending were reduced by the total amount retained in such funds.

Similarly, both the legislative history of section 17 and extrinsic evidence of the voter's understanding of the amendment's provisions indicate that elimination of state services and/or liquidation of state assets was not considered a necessary prerequisite to simple majority access to the budget reserve. Both Representative Rieger and Representative Brown stated in committee that if revenues declined, a simple majority could appropriate from the fund to make up the difference.[18] Statements in the voter pamphlet indicated similar conditions to appropriation. The statement in support of the amendment in the voter pamphlet states:

The Legislature will be able to spend money from the Budget Reserve only if:
• revenues are less than the amount appropriated the previous year, in which case money could be appropriated from the Budget Reserve in an amount not to exceed the shortfall[.]

. . . . .
At the very least, this ballot measure will establish a savings account that can help minimize the effects of a "boom" one year, and a "bust" the next.

The statement in opposition expresses a similar understanding:

> Under paragraph (b) of the proposed constitutional change, a simple majority in the legislature could "borrow" funds from the reserve, to make up any shortfall in revenues, up to the amount appropriated in the previous year.

(Emphasis eliminated.)

These statements demonstrate that Gov. Cowper's expansive reading of "amount available ***930** for appropriation" is not consistent with the purpose of the amendment or the probable understanding of the drafters and voters.

On the surface, these statements may appear to support the State's interpretation of "amount available for appropriation" as including only revenues received by the State within the fiscal year.[19] This interpretation is, however, plainly inconsistent with the language of section 17(b). If the drafters of the amendment had intended that a decline in revenues alone would trigger access, it would have been easy to formulate a test which compared current revenues to prior revenues. The formula in section 17(b), however, compares the "amount available for appropriation" to the amount previously appropriated. In order to accept the various secondary indications of the people's possible understanding as dispositive, it would be necessary to read "amount available for appropriations" as meaning only current revenue. Yet it is clear that in the normal functioning of state government, other funds are routinely available including, at a minimum, the general fund balance carried forward. Nor is an understanding that the reserve fund could be reached by a simple majority when revenues decline necessarily inconsistent with requiring some standing funds to be considered available for appropriation. The State concedes that the statutory budget reserve and the general fund balance would have to be considered available. *See* 37.10.420(a)(1)(C)-(D). Eliminating even these funds from the calculation would allow majority access to the budget reserve whenever there was even the slightest decline from year to year in revenues, even if in the prior year a huge sum was left unappropriated or placed in the statutory budget reserve. The language of section 17 and the purposes behind the establishment of the fund do not support such easy access.

The flaw in Gov. Cowper's analysis of the text of section 17(b) is in his assumption that "available" can only mean "accessible by any means." The dictionary definitions of the word indicate narrower meanings which are more consistent with the purpose and intent of the provision and with the probable understanding of the voters. As quoted above, one of the definitions of "available" is "immediately utilizable," indicating that the ease with which funds may be accessible is a factor in determining their availability. This is in accord with a common sense understanding of section 17. As demonstrated above, the purpose and common understanding of the language in section 17(b) allows the budget reserve to be used by a simple majority as necessary to maintain

state appropriations at a constant level. Although all funds might be available by some means, counting funds already validly appropriated to a specific purpose as still "available" would disrupt existing state programs and would constitute an inflexible constitutional intrusion on the legislature's authority to evaluate the wisdom of particular appropriations. Although such a constitutional intrusion is conceivable, we are unwilling to read it into a provision with quite a different purpose.

It is far more reasonable to interpret "amount available for appropriation" in light of the relative consequences of and circumstances attendant in making appropriations from different sources. In this light, monies which already have been validly committed by the legislature to some purpose should not ***931** be counted as available.[20] In addition, illiquid assets owned by the state are not available so long as they remain illiquid. Given the "stabilizing" purpose of the amendment, it would make little sense to interpret section 17 as requiring the costly and time-consuming process of liquefying state assets before allowing majority access to the constitutional budget reserve fund. *See supra* note 14. The "amount available for appropriation" would include, however, all monies from which the legislature can make an appropriation and which require a legislative appropriation before they can be expended, as well as any amount which would not otherwise be counted as "available" but from which the legislature does in fact appropriate. This interpretation is consistent with the stabilizing purpose of section 17 and with the extrinsic evidence of the voter's understanding of the amendment. Most importantly, it is consistent with the text of section 17(b), as it is based on a reasonable and practical interpretation of the words of that section, in accordance with common sense.[21]

This definition necessarily includes all amounts which are in fact appropriated for a fiscal year, including "trust receipts."[22] There is nothing in the text or history of section 17 which would justify classifying money actually appropriated as *unavailable* for appropriation.[23]

The State argues that "[s]ound policy" requires that these trust receipts be excluded because they "are not available for discretionary appropriation by the legislature." Even if we were to agree that policy considerations favored a system which compared only amounts available for discretionary appropriation to the previous year's appropriations from such amounts, we could not impose that policy choice on a differently worded constitutional provision.

Moreover, it is not clear that excluding these receipts would constitute a better policy. The appropriations made from these receipts represent a significant portion of state spending. The purposes to which these funds are restricted include many core state government functions, including education, ***932** health, social services, public safety, and transportation. *See* State of Alaska, Dep't of Revenue, *Revenue Sources Book* (Fall 1993) at 54 (listing historical grants-in-aid by category). Because these funds are an integral part of the State's annual spending, changes in the amounts received would certainly affect other budget decisions. Policy considerations therefore appear to favor including trust receipts in the amount available, so that, for example, declines in federal funding might result in increased access to the budget reserve fund. The budget reserve amendment does anticipate that all budget decisions be made in relation to one another. We need not choose between these alternative policies, however. Regardless of which policy argument is in fact more compelling, the text of section 17(b) clearly requires that all funds which are in fact appropriated be counted as "available for appropriation."

The key question in applying our interpretation of the term "amount available for appropriation" to particular funds[24] is what constitutes a valid appropriation such that the funds involved are no longer available. "Appropriation" is defined as

something that has been appropriated; *specif.:* a sum of money set aside or allotted by official or formal action for a specific use (as from public revenue by a legislative body that stipulates the amount, manner, and purpose of items of expenditure).

Webster's Third New Int'l Dictionary 106 (1969). *Black's Law Dictionary* defines "appropriation" as

[t]he act of appropriating or setting apart; prescribing the destination of a thing; designating the use or application of a fund

....

In governmental accounting, an expenditure authorized for a specified amount, purpose, and time.

....

Public law. The act by which the legislative department of government designates a particular fund, or sets apart a specified portion of the public revenue or of the money in the public treasury, to be applied to some general object of governmental expenditure, or to some individual purchase or expense. Authority given by legislature to proper officers to apply distinctly specified sum from designated fund out of treasury in given year for specified object or demand against the state.

Black's Law Dictionary 101-02 (6th ed. 1990); *see generally McAlpine v. University of Alaska*, 762 P.2d 81, 87-88 (Alaska 1988) (discussing definitions of "appropriation").

In *Thomas v. Rosen* we cited with approval the following definition of appropriation by the Wisconsin Supreme Court:

> An appropriation is the setting aside from the public revenue of a certain sum of money for a specified object, in such manner ***933** that the executive officers of the government are authorized to use that money, and no more, for that object, and no other.

569 P.2d 793, 796 (Alaska 1977) (quoting *State ex rel. Finnegan v. Dammann*, 220 Wis. 143, 264 N.W. 622, 624 (1936)). Finally, in *City of Fairbanks v. Fairbanks Convention and Visitors Bureau*, in determining that a local initiative did not make an appropriation, we asked "whether the initiative would set aside a certain specified amount of money or property for a specific purpose or object in such a manner that is executable, mandatory, and reasonably definite with no further legislative action." 818 P.2d 1153, 1157 (Alaska 1991).

Under these definitions, it is clear that one of the fundamental characteristics of an appropriation, in the public law context, is that it authorizes governmental expenditure without further legislative action. Therefore, funds established by the legislature which may be used to pay state expenditures without further legislative action are not available for appropriation, to the extent that expenditures are authorized. This is true regardless of whether the fund is nominally established within the general fund or within a state agency. For example, the oil and hazardous substance release response fund is a restricted fund within the general fund. AS 46.08.010. The commissioner of environmental conservation is authorized to
use money from the fund to

(1) investigate and evaluate the release or threatened release of oil or a hazardous substance, and contain, clean up, and take other necessary action, such as monitoring and assessing, to address a release or threatened release of oil or a hazardous substance that poses an imminent and substantial threat to the public health or welfare, or to the environment.

AS 46.08.040(a). The entire balance of the fund could potentially be used by the commissioner of environmental conservation under this provision without any further authorization by the legislature.[25] In addition, AS 46.08.040(b) authorizes the governor to use money from the fund to respond to an oil or hazardous substance discharge emergency during the effective period of such an emergency declared under AS 26.23.020(c). Because the legislature has made the entire balance of this fund available for expenditure, the amounts deposited into the fund are validly appropriated and therefore no longer available for appropriation.

On the other hand, funds which require further legislative appropriation before expenditures can be made against them are available for appropriation. Thus, the Railbelt energy fund, AS 37.05.520, the Alaska marine highway system vessel replacement fund, AS 37.05.550, and the educational facilities maintenance and construction fund, AS 37.05.560, remain "available for appropriation," within the meaning of section 17(b). Each of these funds has the same general structure. Each is established as a "restricted" fund within the general fund, and each consists of money "appropriated" to it by the legislature. AS 37.05.520, .550(a), .560(a). These initial appropriations, however, are not sufficient to support any expenditure. Further legislative appropriations are necessary. *See* AS 37.05.520 ("The legislature may appropriate money from the fund for programs, projects, and other expenditures to assist in meeting Railbelt energy needs, including projects for retrofitting state-owned buildings for and facilities for energy conservation."); AS 37.05.550(a) ("The legislature may appropriate money from the fund for refurbishment of existing state ferry vessels, or replacement of retired or outmoded state ferry vessels."); AS 37.05.560(b) ("Money in the fund may be appropriated (1) to finance the design, construction, and maintenance of public school facilities; and (2) for maintenance ***934** of University of Alaska facilities.").[26] Because the initial "appropriations" to

these funds cannot support any expenditure, the money in these funds remains "available for appropriation" until further appropriations are made. [27]

A similar analysis applies to the permanent fund earnings reserve account (earnings reserve account), AS 37.13.145. This fund is established as a separate account within the permanent fund under the authority of the last sentence of Article IX, § 15 of the Alaska Constitution: "All income from the permanent fund shall be deposited in the general fund unless otherwise provided by law." AS 37.13.145(a) provides otherwise: "The earnings reserve account is established as a separate account in the fund. Income from the fund shall be deposited by the corporation into the account as soon as it is received." Therefore, money in the earnings reserve account never passes through the general fund, and is never appropriated as such by the legislature.

A percentage of the money in the reserve account is automatically transferred to the dividend fund at the end of each fiscal year. AS 37.13.145(b). After that transfer has been made, an additional amount is transferred from the earnings reserve account to the principal of the permanent fund in order to "offset the effect of inflation on principal of the fund." AS 37.13.145(c). No regular provision is made for amounts in the earnings reserve account in excess of that necessary to fund dividends and inflation proof the permanent fund principal. Absent an appropriation, this excess accumulates from year to year. The unencumbered balance of this account was $1.087 billion as of February 28, 1994.

The balance remaining in the earnings reserve account each year after the dividend and inflation-proofing transfers have been made is liquid, has never been appropriated by the legislature, and is not subject to expenditure without further legislative action. There are no statutory or constitutional prohibitions against direct appropriations from this account. [28] The earnings reserve account is therefore available for appropriation. [29]

***935** **[3]** Alaska Statute 37.10.420 fails to include several funds-including trust receipts, "restricted" accounts within the general fund which require further legislative appropriation before they can be expended, and the permanent fund earnings reserve account-in the "amount available for appropriation" which are in fact available within the meaning of article IX, section 17 of the Alaska Constitution. It therefore does not provide an accurate definition of the constitutional term. Therefore, although we differ from the superior court in our analysis of the "amount available for appropriation," we affirm the superior court's decision declaring AS 37.10.420(a)(1) unconstitutional.

In summary, the "amount available for appropriation" within the meaning of article IX, section 17 of the Alaska Constitution includes all monies over which the legislature has retained the power to appropriate and which require further appropriation before expenditure. In addition, all amounts actually appropriated, whether or not they would have been considered available prior to appropriation, are available within the meaning of section 17. Illiquid assets, such as land and unexploited natural resources, are not available so long as they remain illiquid. For these reasons, trust receipts are available for appropriation, as are funds like the Railbelt energy fund and the educational facilities maintenance and construction fund, which are not available for expenditure without additional appropriations. In contrast, the oil and hazardous substance release response fund is not counted as available because the entire balance of the fund may be expended at any time without further legislative action. The availability of funds not specifically discussed in this opinion must be determined in accordance with this opinion. Finally, the permanent fund earnings reserve account must be counted as available for appropriation, because appropriations may be made from it and it is not subject to expenditure without legislative action.

B. "Amount appropriated for the previous fiscal year"

[4] The meaning of the term "amount appropriated for the previous fiscal year" in article IX, section 17(b) of the Alaska Constitution follows logically from the definitions of the word "appropriation" listed above. The "amount appropriated for the previous fiscal year" means all amounts set aside for the previous fiscal year by the legislature "for a specific purpose or object in such a manner that is executable, mandatory, and reasonably definite with no further legislative action." *Fairbanks Convention and Visitors Bureau*, 818 P.2d at 1157. In short, the "amount appropriated" includes every dollar appropriated by the legislature, whatever its source. [30] Because our definition of the amount available for appropriation includes all amounts actually appropriated, it is unnecessary to exclude artificially any amount actually appropriated from the "amount appropriated" in order to achieve symmetry in the comparison. The State correctly argues that this symmetry is necessary in order to insure that the comparison required by section 17(b) fairly measures the need for access to the budget reserve fund. Contrary to the

State's argument, however, symmetry can be obtained without abandoning the plain meaning of the words used in the constitution. Because AS 37.10.420(a)(2) does not include all actual appropriations made for the previous fiscal year in the "amount appropriated for the previous fiscal year," it does not accurately reflect the meaning of the constitutional term. We therefore affirm the superior court's decision declaring AS 37.10.420(a)(2) unconstitutional.

C. "Amount of appropriations made in the previous calendar year for the previous fiscal year"

[5] Alaska Statute 37.10.420(a)(3) defines the "amount of appropriations made in the previous calendar year for the previous fiscal ***936** year" in terms of the unconstitutionally limited number of appropriation sources identified in subsection (a)(2) of the statute, which itself relies primarily on the sources identified in subsection (a)(1). It cannot be severed from these subsections and therefore is also unconstitutional, as the superior court properly held.

This term is meant to prevent the legislature from increasing prior year appropriations in order to increase access to the budget reserve in the present year.[31] Other than its unduly narrow interpretation of what counts as an appropriation, the definition of the term in AS 37.10.420(a)(3) appears to be consistent with this purpose. The "amount of appropriations made in the previous calendar year for the previous fiscal year" means the amount of all appropriations made in the calendar year in which the previous fiscal year began.

D. Constitutionality of AS 37.10.420(b)

[6] Alaska Statute 37.10.420(b) designates the means by which appropriations from the budget reserve fund are paid back to the fund. Article IX, § 17(d) provides:

> If an appropriation is made from the budget reserve fund, until the amount appropriated is repaid, the amount of money in the general fund available for appropriation at the end of each succeeding fiscal year shall be deposited in the budget reserve fund. The legislature shall implement this subsection by law.

Pursuant to the authority granted it by § 17(d), the legislature enacted AS 37.10.420(b), which provides:

> If the amount appropriated from the budget reserve fund has not been repaid under art. IX, sec. 17(d), Constitution of the State of Alaska, the Department of Administration shall transfer to the budget reserve fund the amount of money compromising the unreserved, undesignated general fund balance to be carried forward as of June 30 of the fiscal year, or as much as necessary to complete the repayment. The transfer shall be made on or before December 16 of the following fiscal year.

This definition excludes restricted funds within the general fund from the calculation of the amount available to pay back appropriations from the budget reserve fund. As discussed above, some of these funds remain "available for appropriation" within the meaning of section 17.[32] Although the constitution gives the legislature authority to implement subsection (d), the legislature's authority must be exercised within the constraints of subsection (d)'s own requirements. Because AS 37.10.420 fails to consider all amounts which are "available for appropriation" within the meaning of section 17 in determining the State's repayment obligation, it is unconstitutional. The superior court's decision declaring AS 37.10.420(b) unconstitutional is therefore affirmed.

III. *CONCLUSION*

The decision of the superior court is AFFIRMED, for the reasons stated in this opinion.

All Citations

874 P.2d 922

Footnotes

* Sitting by assignment made pursuant to article IV, section 16 of the Alaska Constitution.

1 Article IX, section 17 provides as follows:

Budget Reserve Fund. (a) There is established as a separate fund in the State treasury the budget reserve fund. Except for money deposited into the permanent fund under Section 15 of this article, all money received by the State after July 1, 1990, as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation in a State or federal court involving mineral lease bonuses, rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments or bonuses, or involving taxes imposed on mineral income, production, or property, shall be deposited in the budget reserve fund. Money in the budget reserve fund shall be invested so as to yield competitive market rates to the fund. Income of the fund shall be retained in the fund. Section 7 of this article does not apply to deposits made to the fund under this subsection. Money may be appropriated from the fund only as authorized under (b) or (c) of this section.
(b) If the amount available for appropriation for a fiscal year is less than the amount appropriated for the previous fiscal year, an appropriation may be made from the budget reserve fund. However, the amount appropriated from the fund under this subsection may not exceed the amount necessary, when added to other funds available for appropriation, to provide for total appropriations equal to the amount of appropriations made in the previous calendar year for the previous fiscal year.
(c) An appropriation from the budget reserve fund may be made for any public purpose upon affirmative vote of three-fourths of the members of each house of the legislature.
(d) If an appropriation is made from the budget reserve fund, until the amount appropriated is repaid, the amount of money in the general fund available for appropriation at the end of each succeeding fiscal year shall be deposited in the budget reserve fund. The legislature shall implement this subsection by law.

2 AS 37.10.420 provides:
(a) For purposes of applying art. IX, sec. 17(b), Constitution of the State of Alaska,
(1) "the amount available for appropriation" or "funds available for appropriation" means
(A) the unrestricted revenue accruing to the general fund during the fiscal year;
(B) general fund program receipts as defined in AS 37.05.146;
(C) the unreserved, undesignated general fund balance carried forward from the preceding fiscal year that is not subject to the repayment obligation imposed by art. IX, sec. 17(d), Constitution of the State of Alaska; and
(D) the balance in the statutory budget reserve fund established in AS 37.05.540;
(2) "the amount appropriated for the previous fiscal year" means the amount appropriated from the
(A) constitutional budget reserve fund under the authority granted in art. IX, sec. 17, Constitution of the State of Alaska; and
(B) same revenue sources used to calculate the money available for appropriation for the current fiscal year; and
(3) "the amount of appropriations made in the previous calendar year for the previous fiscal year" means appropriations made from sources identified in (2) of this subsection for a fiscal year that were enacted during the calendar year that ends on December 31 of that same fiscal year.
(b) If the amount appropriated from the budget reserve fund has not been repaid under art. IX, sec. 17(d), Constitution of the State of Alaska, the Department of Administration shall transfer to the budget reserve fund the amount of money comprising the unreserved, undesignated general fund balance to be carried forward as of June 30 of the fiscal year, or as much of it as is necessary to complete the repayment. The transfer shall be made on or before December 16 of the following fiscal year.
(c) In this section, "unrestricted revenue accruing to the general fund" or "unreserved, undesignated general fund balance carried forward" is money not restricted by law to a specific use that accrues to the general fund according to accepted principles of governmental or fund accounting adopted for the state accounting system established under AS 37.05.150 in effect on July 1, 1990.
(d) An appropriation under art. IX, sec. 17(b), Constitution of the State of Alaska, requires an affirmative vote of the majority of the members of each house of the legislature. An appropriation under art. IX, sec. 17(c) requires an affirmative vote of three-fourths of the members of each house of the legislature.

3 See *Halford,* 872 P.2d at 174-76, for a full statement of the earlier proceedings in this case.

4 This court does not possess original jurisdiction over the case. AS 22.05.010. In addition, no Alaska court could normally adjudicate an action by the State seeking to have a statute declared constitutional, in the absence of the willing participation of a truly adverse party. *See Greater Anchorage Area Borough v. City of Anchorage,* 504 P.2d 1027, 1036 (Alaska 1972) ("Parties seeking a judicial determination of a hypothetical, advisory or moot question will be denied relief.").

5 The superior court found AS 37.10.410 unconstitutional based on an inconsistency between the statute and this court's interpretation of the term "administrative proceeding" in *Halford.* The State does not challenge this portion of the court's decision in this petition.

6 *See Heckendorn v. City of San Marino,* 42 Cal.3d 481, 229 Cal.Rptr. 324, 327, 723 P.2d 64, 67 (1986) ("We must determine what the term 'ad valorem tax' means in Article XIII A."); *Amador Valley Joint Union High Sch. Dist. v. State Bd. of Equalization,* 22 Cal.3d 208, 149 Cal.Rptr. 239, 257, 583 P.2d 1281, 1300 (1978) (en banc) (discussing rules of construction used by courts in interpreting constitutional provisions); *State ex rel. Udall v. Colonial Penn Ins. Co.,* 112 N.M. 123, 812 P.2d 777, 782-83 (1991) ("We interpret our constitution to carry out its spirit."); *Coronado Oil Co. v. Grieves,* 603 P.2d 406, 411 (Wyo.1979) ("Though the legislature's interpretation of the constitution is not binding on the supreme court, we would be loath to interpret the constitution otherwise. We must give weight to legislative interpretation, though not conclusive.") (citations omitted).

7 The legislature's interpretation of the constitutional terms at issue in this case may be considered more persuasive than otherwise because of its greater familiarity with appropriations. Deference in such circumstances is at most, however, a single tool for use by this court in interpreting the constitution. If the legislature adopted AS 37.10.420 contemporaneously with its approval of the Legislative Resolve No. 129 (eventual Article IX, section 17), that would be considered a significant indication of the actual meaning of section 17. A statement by the Eighteenth Legislature of the intent of the Sixteenth Legislature would not bear great weight even if the subject was the meaning of a statute; the applicable degree of deference is lessened by the fact that at issue is the meaning of a constitutional amendment for which the legislature is not the ultimate adopting authority. Our discussion of the weight to be afforded a subsequent legislative statement of the meaning of an earlier statute in *Hillman v. Nationwide Mut. Fire Ins. Co.,* 758 P.2d 1248, 1252-53 (Alaska 1988), is relevant here.

While the legislature is fully empowered to declare present law by legislation, it is not institutionally competent to issue opinions as to what a statute passed by an earlier legislature meant. If the legislature were in some form to declare its opinion as to the meaning of prior law, that declaration would be entitled to the same respect that a court would afford to, for example, an opinion of a learned commentator; that is, the court would examine the reasoning offered in support of the opinion and either reject or accept it based on the merit of the reasons given.... It is possible to argue that the legislature has knowledge superior to a disinterested commentator because there may be some legislators in the current legislature who were also members of the legislature which passed the prior law and thus have special insight into the intent of the legislature. However, the force of this is dispelled when one considers that it is not permissible to allow a legislator to testify on the question of his unexpressed legislative intent or on the unexpressed legislative intent of others. *Id.* (citing *Kenai Peninsula Borough Sch. Dist. v. Kenai Peninsula Educ. Ass'n,* 572 P.2d 416 (Alaska 1977)).

8 As preliminary matters, Gov. Cowper argues that the statutes are invalid irrespective of their substantive content because (1) they violate the separation of powers doctrine; (2) they constitute an impermissible attempt by the legislature to influence an ongoing judicial controversy; (3) they intrude on the judicial realm of constitutional interpretation; and (4) the statute violates article IX, section 7's prohibition against dedicated funds. The "influencing" claim pertains entirely to AS 37.10.410 and therefore is not relevant to the present petitions which deal exclusively with AS 37.10.420. The "intrusion on the judicial realm" argument is without merit.

Gov. Cowper's argument that the Act establishes a dedicated fund is also without merit. Although the Act defines certain funds as not available for appropriation under section 17(b), it does not prohibit the executive branch from requesting that these funds be reassigned to different purposes or the legislative branch from allocating these funds differently. *Sonneman v. Hickel,* 836 P.2d 936, 940 (Alaska 1992). In addition, because the Act does not dedicate any state revenue to any particular fund, it cannot implicate the prohibitions of section 7. Therefore, these funds are not made dedicated funds by virtue of the Act.

9 AS 37.05.146 provides:

In AS 37.05.142-37.05.146 and AS 37.07.080, "program receipts" means fees, charges, income earned on assets, and other state money received by a state agency in connection with the performance of its functions; all program receipts except the following are general fund program receipts:

(1) federal receipts;

(2) University of Alaska receipts (AS 14.40.491);

(3) individual, foundation, or corporation gifts, grants, or bequests that by their terms are restricted to a specific purpose;

(4) receipts of the following funds:

(A) highway working capital fund (AS 44.68.210);

(B) correctional industries fund (AS 33.32.020);

(C) loan funds;

(D) international airport revenue fund (AS 37.15.430);

(E) funds managed by the Alaska Housing Finance Corporation (AS 18.56.020), the Alaska Railroad Corporation (AS 42.40.010), the Municipal Bond Bank Authority (AS 44.85.020), the Alaska Aerospace Development Corporation (AS 14.40.821), or the Alaska Industrial Development and Export Authority (AS 44.88.020);
(F) fish and game fund (AS 16.05.100);
(G) school fund (AS 43.50.140);
(H) training and building fund (AS 23.20.130);
(I) retirement funds (AS 14.25, AS 22.25, AS 26.05.222, AS 39.35, and former AS 39.37);
(J) permanent fund (art. IX, sec. 15, Alaska Constitution);
(K) public school fund (AS 37.14.110);
(L) second injury fund (AS 23.30.040);
(M) fishermen's fund (AS 23.35.060);
(N) FICA administration fund (AS 39.30.050);
(O) receipts of the employee benefits program established under AS 39.30.150-39.30.180;
(P) receipts of the deferred compensation program established under AS 39.45;
(Q) clean air protection fund (AS 46.14.260);
(R) receipts of the group insurance programs established under AS 39.30.090.
(5) receipts of or from the trust established by AS 37.14.400-37.14.450, except reimbursements described in AS 37.14.410.

10 These additional funds include the Railbelt energy fund, AS 37.05.520, the Alaska marine highway system vessel replacement fund, AS 37.05.550, the educational facilities maintenance and construction fund, AS 37.05.560, the oil and hazardous substance release response fund, AS 46.08.010, the power cost equalization and rural electric capitalization fund, AS 42.45.100, the power project fund, AS 42.45.010, the Alaska science and technology endowment, AS 37.17.020, and the permanent fund earnings reserve account, AS 37.13.145.

11 In 1985, the Department of Law issued an informal opinion, written by Assistant Attorney General James L. Baldwin, which concluded that "unrestricted money in the [Alaska Housing Finance Corporation] revolving fund is probably *available for appropriation.*" 1985 Informal Op. Att'y Gen. 307 at 309 (emphasis added). The Opinion recommended that the statute governing the Alaska Housing Finance Corporation (AHFC) be amended to specifically authorize interim transfers of unrestricted surplus assets of AHFC to the general fund and to provide that the board of directors annually determine the amount of surplus available for transfer. *Id.* at 310-11.

The statutes governing the AHFC and the Alaska Industrial Development and Export Authority (AIDEA) now require each organization to annually determine whether it has assets in excess of the amount required to fulfill its purposes. *See* AS 18.56.089(b)(1); AS 44.88.205(b)(1). Each organization must present this determination to the legislature by January 10 of each year. AS 18.56.089(b)(2); AS 44.88.205(b)(2); *See* Ch. 12 SLA 1991.

12 On this basis alone, we must reject the State's plea to convert the term "amount available for appropriation," as used in section 17(b), to either "amount available for appropriation from the [unrestricted] general fund" or "revenues available for appropriation." If the definition of "amount available for appropriation" in AS 37.10.420 is to withstand constitutional scrutiny, it must be because it is in conformity with the text of section 17(b), and not because section 17(b) is missing words which would make it conform to AS 37.10.420.

13 The State argues that the "common understanding" of the phrase "available for appropriation" is more limited. It states that the term should have the same meaning in the Constitution that it has in the budget process, meaning only "revenue sources customarily considered by the legislature." The State asserts that only unrestricted revenues are so considered. To be distinguished are "restricted revenues," the use of which is restricted in some way, usually by the source of the funds, predominantly the federal government.

The State never asserts or shows evidence, however, that the term "available for appropriation" is actually used in any particular way in the budget process. Rather, it argues that the term "should be interpreted with reference to revenue sources customarily considered by the legislature when it considers the state budget." It is also not clear that the legislative definition of "amount available for appropriation" includes all monies "customarily considered by the legislature." Although it probably does include all *revenues* customarily considered, it may not include all amounts so considered.

14 Gov. Cowper does limit his argument to cash funds, presumably because of the relative ease with which cash funds can be converted to different purposes, as compared to illiquid assets. This is a reasonable limitation. Although we have held, in a different context, that property other than money may be "appropriated," *see McAlpine v. University of Alaska,* 762 P.2d 81, 87-89 (Alaska 1988), it does not follow that it is necessarily "available for appropriation" within the meaning of section 17(b).

There does not appear to be any significant difference, however, in the type of legislative action necessary to reach cash funds and less liquid state assets. Gov. Cowper's interpretation therefore recognizes that "available," as used in section 17(b), requires more than mere accessibility.

15 Under this interpretation, if state assets are in excess of annual appropriations, even a total lack of revenue would not allow a simple majority to withdraw from the budget reserve fund.

16 *See, e.g.,* AS 03.10.040 (agricultural revolving loan fund); AS 14.43.090 (scholarship revolving loan fund); AS 14.43.630 (teacher scholarship revolving loan fund); AS 16.10.340 (commercial fishing revolving loan fund); AS 42.45.010 (power project fund); AS 42.45.250 (bulk fuel revolving loan fund); AS 44.29.210 (alcoholism and drug abuse revolving loan fund); AS 44.88.400 (small business economic development revolving loan fund); 45.95.060 (small business revolving loan fund); AS 45.98.010 (historical district revolving loan fund).

17 *See, e.g.,* Testimony of budget officer Mary Halloran, House Finance Comm. TR. 37, May 1, 1990.

18 *See* Statement of Rep. Rieger, H. Finance Comm., HFC tape 90-97, tr. at 31 (May 3, 1990) ("[I]f oil prices went to $9, it would take a simple majority to use the Budget Reserve Fund to bring you back to what you had last year."); Statement of Rep. Brown, *Id.* at 30 ("[T]o get back to last year's spending level, a simple majority could appropriate from the budget reserve.").

19 The State asserts that this reading is further supported by newspaper descriptions of the amendment prior to the 1990 general election. Some of the statements in these articles do support the State's position:

If State revenues decline, money could be taken out to fill the gap. For example, let's say our state earned $2.5 billion in fiscal year 1995. For some reason, such as a drop in production or a drop in price, we earned just $1.5 billion in fiscal year 1996. The legislature could tap into the Budget Reserve Fund to make up the gap.

"Vote Yes on Ballot Measure No. 1," *Fairbanks Daily News-Miner,* Nov. 2, 1990, at 4; *see also* John Enders, "Cowper pushes for economic stability in form of state budget reserve fund," *Juneau Empire,* Oct. 25, 1990, at 3; John Enders, "Budget Reserve-Account Would Cushion State Revenue," *Anchorage Daily News,* Oct. 28, 1990, at M16; John Enders, "Ballot measure would set up budget reserve," *Fairbanks Daily News-Miner,* Oct. 22, 1990, at 6 ("[I]f state revenues fell from one year to the next the Legislature could tap the reserve to make up the difference."). These articles cannot, however, control over contrary wording in the constitution.

20 To do otherwise would be to continue to count sums of money as "available for appropriation" after they have been appropriated, so long as they have not been paid out or converted from cash to some other type of asset. Instead, we recognize that any given sum of money can only be appropriated once during a given time period. Of course, if an appropriation lapses or if the legislature does in fact reappropriate money from an excluded fund to another purpose, it is no longer necessary to exclude that money from the "amount available for appropriation" in order to protect the legislature's authority to make such decisions.

21 This interpretation is related to the State's argument that AS 37.10.420 properly excludes "restricted funds" because those funds, at least in part, have already been appropriated. We reject, however, the State's conception of relevant fund restrictions and the State's definition of when an amount has been validly appropriated. Therefore, our definition of the "amount available for appropriation" includes several funds excluded by the statutory definition.

22 "Trust receipts" include all funds, whatever the source, which the State can only use for a specific stated purpose under applicable law. The largest "trust receipt" category is federal funding, which may only be appropriated by the State for the purposes prescribed by the federal government. Private entities may also grant the State money to use for specific purposes. State appropriations from trust accounts, such as the Public Employees Retirement Fund, for purposes relating to the trust, such as fund administration, are also properly characterized as trust receipts. Although the amount of the appropriation is apparently set by the legislature, it must be made in accordance with trust principles. Therefore, the amount which the legislature appropriates in accordance with trust principles is the amount available to the legislature for such appropriation. Finally, amounts appropriated by the legislature out of other funds within executive agencies for purposes of administering these funds, under explicit statutory authority, may also be treated as a type of trust receipt. *See, e.g.,* AS 03.10.040(b) (agricultural revolving loan fund); AS 16.10.340 (commercial fishing revolving loan fund); AS 45.95.060(*o*) (small business revolving loan fund). Although these funds are not trust funds, the statutes do limit legislative authority to appropriate from them.

23 Money appropriated from the AHFC and the AIDEA therefore must be counted as available for appropriation. However, money which either organization determines to be in excess of the amount required to fulfill its purposes, see AS 18.56.089(b)(1); AS 44.88.205(b)(1), should not be counted unless actually appropriated to another purpose or transferred to the general fund. The statutes do not automatically transfer these funds out of the respective organizations.

24 In this regard, the State argues that the question of whether funds outside the unrestricted general fund are "available for appropriation" is "not justiciable in a court of law." To the extent the State argues that this court cannot decide the meaning of the term "available for appropriation" or the legal status of different funds under this definition, its position is without merit. The meaning of the constitution and its application to particular facts are questions squarely within the jurisdiction and inherent power of the judiciary. "[T]he judicial branch of government has the constitutionally mandated duty to ensure compliance with the provisions of the Alaska Constitution, including compliance by the legislature." *Malone v. Meekins,* 650 P.2d 351, 356 (Alaska 1982). The State's error is in assuming that the "power of appropriation necessarily includes the power to determine what amounts are available to finance appropriations enacted." *Compare Abood v. Gorsuch,* 703 P.2d 1158, 1161-62 (Alaska 1985) ("What quorum is necessary for the confirmation votes is a question of Alaska constitutional law. It is therefore a question to which the nonjusticiability doctrine does not apply."). Although the court cannot say what particular funds should be used for appropriations, or set the amount of appropriations, it can and must determine the status of particular funds when such a determination is necessary for constitutional interpretation or enforcement.

The State is correct, however, insofar as it asserts that decisions to appropriate certain funds and withdraw other appropriations are political questions. All this means, however, is that the court cannot second guess the wisdom of individual appropriation or non-appropriation decisions. This limitation supports a definition of "available for appropriation" which does not require amounts validly appropriated to specific purposes to be counted. As these amounts have already been appropriated, counting them as available is functionally equivalent to questioning the wisdom of the original appropriation.

25 AS 46.08.040 lists eight other purposes for which the commissioner of environmental conservation may use money from the fund. *See* AS 46.08.040(a)(2)-(7) and (d)(1)-(2). Except as provided for in AS 46.08.040(d)(1), however, expenditures for these purposes are limited to amounts available from appropriations made specifically for the purposes listed. AS 46.08.040(c). AS 46.08.040(d)(1) provides that the commissioner of environmental conservation shall, upon request of the Alaska Legislative Council, "use money from the fund to reimburse the Alaska Legislative Council for expenditures that it makes for the operation of the Citizens' Oversight Council on Oil and Other Hazardous Substances."

26 The lists of specific purposes in each statute for which these second appropriations "may" be made are not sufficient to make the assignment of money to these funds "appropriations." Further appropriations are necessary before expenditures can be made. In addition, we have previously recognized that statutory statements that the legislature "may" appropriate money from funds within the general fund for specific purposes "impose no legal restraint on the appropriations power of the legislature." *Sonneman v. Hickel,* 836 P.2d 936, 939-40 (Alaska 1992).

27 In a hybrid situation, where expenditures can be made from part but not all of a fund, the fund is not available for appropriations to the extent that it is subject to expenditure without further legislative approval. We express no opinion on the possible status of funds which technically are subject to full expenditure, but which are funded well beyond any reasonably expectable need, as there is no evidence in the record before us that any such fund exists.

We also make no attempt to name and classify as "available" or "unavailable" every fund within the treasury of the State of Alaska. We leave it, in the first instance, to executive and legislative branch officials more familiar with all of the funds involved to apply the general definition we adopt today.

28 In a May 1990 memorandum describing the budget reserve amendment, budget officer Mary Halloran states that the amount available for appropriation includes "all revenue sources, such as permanent fund earnings, federal funds and other restricted funds."

In addition, the language of section 17, and specifically the difference in language between sections 17(b) and (d), suggests that at least some funds outside the general fund may be available for appropriation. *Compare* § 17(b) ("the amount available for appropriation for a fiscal year") with § 17(d) ("the amount of money in the general fund available for appropriation").

29 In oral argument before the superior court, the State argued that the earnings reserve account should not be considered available because, under current projections of the Alaska Permanent Fund Corporation, the entire balance will be used for dividend payments and inflation proofing by the year 2010. This argument rests on reasoning similar to that which prompted us to conclude that the oil and hazardous substance release response fund was not available for appropriation: the entire account may be expended without further legislative action. Unlike the release response fund, which may be needed for expenditure at any time, the earnings reserve account balance will not be used for many years to come. In the meantime, there are no restrictions on its use. Something more than a possibility of future use is necessary before a fund is considered no longer available for appropriation.

30 This amount would include appropriations made from the constitutional budget reserve fund. It would not include "appropriations" made to funds from which additional appropriations are necessary before expenditures can be made. If the legislature both appropriates money into a fund which is not available for appropriation and removes money from the same fund to appropriate to a different purpose in the same year, the amounts should be offset so that the same amount of money is not counted twice in determining the total amount appropriated.

31 *See* Halloran memorandum, at 5 ("The phrase 'in the previous calendar year' was inserted by the House Finance Committee specifically to preclude stratagems whereby a supplemental appropriation to the current fiscal year ... could be made in order to increase the allowable size of a Budget Reserve Fund appropriation for the fiscal year being budgeted.")

32 We see no reason to give "available for appropriation" a different meaning in subsection (d) than we did in subsection (b). We recognize, however, that the payback provision in section 17(d) is limited to only those funds which are "available for appropriation" *and* "in the general fund." Thus, available amounts outside the general fund, such as the earnings reserve account, need not be deposited in the budget reserve. This additional limitation has no effect on funds which exist within the general fund.

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1995 Alaska Op. Atty. Gen. (Inf.) 111 (Alaska A.G.), 1995 WL 867852

Office of the Attorney General

State of Alaska
File Nos. 663-95-0475; 663-95-0474
May 18, 1995

Subject: Application of the definition of "administrative proceeding" in the budget reserve fund provision of the Alaska Constitution to settlements of tax appeals involving unaudited years and royalty settlements prior to litigation

***1** The Honorable Wilson Condon
Commissioner
Dep't of Revenue

The Honorable John Shively
Commissioner
Dep't of Natural Resources

We have been asked two questions concerning allocation of certain mineral revenues between the general fund and the constitutional budget reserve fund. Both questions concern whether the state received these revenues as a result of the termination of an administrative proceeding. The administrative proceeding determination is important because revenue received in settlement of an administrative proceeding must be deposited in the budget reserve fund; revenue received in settlement of a dispute before an administrative proceeding begins is deposited in the general fund. [1]

The Department of Revenue (DOR) asks about settlement of tax disputes. The Alaska Supreme Court has held that an administrative proceeding begins when DOR issues an assessment. In some cases, however, tax disputes are settled issue-by-issue. Sometimes the parties reach agreement on issues in tax years for which no assessment has been issued. DOR asks whether money received for settlement of issues in years for which no assessment has been issued should be deposited in the budget reserve fund.

We conclude that the entire amount of a lump-sum settlement agreed to during an administrative proceeding is the result of the termination of the administrative proceeding, regardless of whether some of the money is received in settlement of unassessed years. Thus, the entire amount of a lump-sum settlement should be deposited in the budget reserve fund. Money subsequently received, however, in payment for issues in unassessed years for which liability was not fixed by the settlement of the administrative proceeding, would not be received as a result of the termination of the administrative proceeding and should be deposited in the general fund.

The Department of Natural Resources (DNR) asks about settlement of royalty disputes. Royalty disputes are creatures of contract, and, unlike tax disputes, no statute mandates use of a statutory dispute resolution procedure. Accordingly, DNR asks whether a settlement of a royalty dispute before litigation ensues can be the result of an administrative proceeding.

We conclude that royalty settlements occurring before litigation can be the result of an administrative proceeding, and thus subject to deposit in the budget reserve fund. An administrative proceeding does not begin, however, until one of the parties notifies the other that it is invoking a binding administrative dispute resolution procedure. Any settlement occurring before such notice would not be the result of an administrative proceeding.

INTRODUCTION

***2** **Article IX**, **section 17** of the Alaska Constitution was established by an amendment to the Constitution adopted by the voters in 1990. [2] **Section 17** provides that all revenue received after July 1, 1990, as a result of the termination of administrative or judicial proceedings concerning mineral revenues must be deposited in a budget reserve fund. It allows the legislature to spend the money in the fund in two circumstances. First, if the amount available for appropriation in one year was less than the amount appropriated in the previous year (without counting supplemental appropriations), the legislature could make up the difference with an appropriation from the fund by a simple majority vote. Alaska Const. art. **IX § 17**(b). Second, the legislature could appropriate for any purpose by a 3/4 majority vote. Id at **§ 17**(c)

Shortly after adoption of the amendment, state officials questioned the definition of "administrative proceeding" as used in **Section 17**. In particular, state officials were uncertain whether DOR "informal conferences," which taxpayers could request in lieu of formal hearings to settle tax disputes, amounted to administrative proceedings for purposes of the budget reserve fund provision of the Constitution. Both DOR and the Office of Management and Budget requested a legal opinion on this question from the attorney general.

In a formal opinion issued in April 1992, Attorney General Charles E. Cole advised that an informal conference did not rise to the level of formality necessary for an official administrative proceeding. Under this opinion, settlements received from informal conferences should not be deposited in the budget reserve fund, but should instead be deposited in the general fund. 1992 Op. Att'y Gen. No. 1 (April 24) (April 1992 opinion).

The April 1992 opinion immediately sparked controversy. In response, the Hickel administration entered into an agreement with the legislature to create a special subaccount within the general fund, called the "administrative settlements account." All money received in settlement of DOR informal conferences would be deposited into the administrative settlements account.

In February 1993, the state and British Petroleum reached agreement on disputes over taxes due for several tax years under the Alaska Net Income Tax, AS 43.20. BP agreed to pay the state 630 million dollars on June 30, 1993, to settle tax years 1982-86 completely, and to settle certain issues for years 1987-1990. The BP settlement was the result of the termination of an informal conference. Consequently, most, but not all, of the BP settlement was deposited in the administrative settlement account. The remainder of the BP settlement was deposited in the general fund because it was received to settle certain issues for years under audit for which no assessment had been issued.

During the 1993 legislative session, the legislature appropriated virtually all of the money in the administrative settlement account, and the administration closed out the account. In June 1993, however, the Senate Majority filed a lawsuit against the administration. The lawsuit asked the court to reverse the April 1992 opinion and find that settlements received in informal conferences were the result of administrative proceedings and, therefore, should have been deposited in the budget reserve fund. In July, former Governor Steve Cowper filed a similar lawsuit, and the two actions were consolidated.

***3** Following cross-motions for summary judgment, the superior court held that informal conferences were administrative proceedings, and granted summary judgment for the plaintiffs. The court ordered the state to transfer the mineral revenue received in informal conferences since July 1, 1990, with interest, from the general fund to the budget reserve fund. The state immediately appealed to the supreme court and asked for expedited consideration. The supreme court issued an interim order affirming the superior court, but requested further briefing and argument on the question of whether the notice of appeal or the assessment begins the administrative proceeding.

During the second round of briefing and argument, the state and the plaintiffs asked the court to rule on two related issues: (i) whether the settlement of tax issues in dispute in unassessed years constituted settlement as a result of administrative proceedings; and (ii) whether settlement of royalty disputes by officials at DNR before initiation of a lawsuit constituted settlement as a result of administrative proceedings.

The parties agreed that settlements of royalty disputes sometimes occurred before litigation, but few facts were placed in the record concerning these settlements. Instead, the question was put before the court as a matter of law. The state argued that royalty payments were creatures of contract and thus, settlement of royalty disputes, in the absence of an administration adjudication, were the result of consensual contract negotiations. The Senate Majority and former Governor Cowper argued that because these settlements occurred in an administrative agency they were necessarily the result of administrative proceedings.

In contrast, the question concerning tax settlements of unassessed years was very fact specific. This question was called the "BP question," because the BP settlement raised the issue. The record before the supreme court showed that in February 1993, the state negotiated an agreement with BP settling certain disputes under the Alaska Net Income Tax, AS 43.20. BP agreed to pay the state 630 million dollars on June 30, 1993.

Most of the BP settlement was received to settle BP's income tax liability for tax years 1982-86. The Department of Revenue had completed the audit of BP's returns for these tax years, and had issued an assessment for underpayment of tax. BP filed a notice of appeal and requested an informal conference to resolve the dispute.

At issue in the informal conference were, among other disputes, four "big" issues that both the taxpayer and the state knew would also arise in the next audit cycle, 1987-90. At the time of the negotiation, state auditors were conducting an audit of BP for 1987-90, but no assessment had been issued. In the informal conference, the negotiators agreed that if they could reach resolution of the "big four" issues for 1982-86, they should also reach agreement on the issues for 1987-1990, and avoid having to negotiate those issues again in the next audit/appeal cycle. The parties did in fact reach agreement on those four issues. The closing agreement negotiated between the parties specified that the lump-sum settlement of $630 million constituted a final determination of BP's income tax liability for tax years 1982-86 and of its liability for the "big four" issues for 1987-90. [3]

***4** The BP settlement was deposited in the general fund, pursuant to the April 1992 opinion. In interpreting the agreement establishing the administrative settlement subaccount, department officials concluded that not all of the BP settlement was received as a result of an informal conference. In their view, there was no informal conference for tax years 1987-90 because no request for appeal had been filed for those years. Accordingly, the Department segregated the amount received from BP that it calculated was attributable to the issues settled in the unassessed years, 1987-90. Only that amount received for the closed years, 1982-86, was deposited in the administrative settlements account. The remaining amount was commingled in the general fund.

In arguing the BP issue before the supreme court, the state suggested that when a settlement extends forward into future years, money received in settlement for the future years was the result of an application of an agreed methodology, and not the result of the administrative proceeding. Accordingly, we argued, the BP settlement was properly allocated between assessed and unassessed years. During oral argument, one supreme court justice, Judge Bryner, sitting pro tem, took issue with the state's approach. Although he agreed that independent payments received in the future might not be subject to deposit in the budget reserve fund, Judge Bryner suggested that the state's approach ignored the word "result" in **Article IX**, **Section 17** of the Alaska Constitution. He expressed the view that the issue was not whether an appeal existed for unassessed years but whether the settlement for those years was the result of the proceeding, and that this inquiry would depend on the facts of each case.

The supreme court issued a published decision on April 4, 1994. The court rejected the state's argument that an administrative appeal begins with the notice of appeal, and held that an administrative proceeding begins with the assessment. Moreover, the court declined to discuss the "BP issue" or the royalty issues. Hickel v. Halford, 872 P.2d 171, 183 (Alaska 1994).

In explaining its decision, the supreme court identified the three essential attributes of an "administrative proceeding":
1. A dispute must exist.

2. A document reflecting the fact of the dispute which serves a function similar to that of a complaint in a civil action, or an accusation or statement of issues under the Administrative Procedure Act, AS 44.62.360, 370, must be served by one party on the other party.

3. The document must set in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved.

Id. at 175. The court emphasized that the crucial element of an administrative proceeding was the ability to bind a party against the party's will. Id. at 181. Thus, service of a document that, if not challenged, would result in a legal obligation, begins the administrative proceeding. Id.

***5** Under this decision, whether the taxpayer requests an informal conference or proceeds to a formal hearing is of no consequence. The administrative proceeding begins when the department issues the assessment. Accordingly, the court affirmed that all settlements from informal conferences should be transferred from the general fund to the constitutional budget reserve, with interest. The transfer was made and the legislature reappropriated from the budget reserve to the general fund, retroactive to the beginning of the fiscal year, money necessary to fund that year's appropriations. Whether “administrative proceeding” includes tax years that were settled but not assessed or royalty settlements occurring before litigation remained unanswered by the courts. Thus, these questions are addressed by this opinion.

DISCUSSION

I. Lump-sum payments that are agreed to at the termination of an administrative proceeding to fix a taxpayer's tax liability for a year or issue should be deposited in the budget reserve fund.

Commissioner Condon has asked whether money received in an administrative proceeding to settle tax disputes for years that have not been assessed must be deposited in the constitutional budget reserve fund, or whether a lump-sum settlement can be allocated between the general fund and the budget reserve fund, depending upon whether the money was received for assessed or unassessed years. In our view, **article IX**, **section 17**, requires that all of a lump-sum settlement received as a result of the termination of an administrative proceeding must be deposited in the budget reserve fund.

The Constitution requires that
all money received by the state after July 1, 1990, as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation in a State or federal court involving mineral lease bonuses, rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments of bonuses, or involving taxes imposed on mineral income, production, or property, shall be deposited in the budget reserve fund.

Alaska Const. art. **IX § 17**.

The BP settlement involved taxes imposed on mineral income. The settlement was a lump-sum settlement that was received at the termination of an administrative proceeding. Unless circumstances prove otherwise, a normal inference would be that all money received at the end of an informal conference was a result of the termination of the administrative proceeding, and thus subject to deposit in the budget reserve. Here, the facts and the law support the conclusion that an allocation of the settlement between the general fund and the budget reserve is not warranted.

Two arguments can be advanced in favor of allocating a settlement between assessed and unassessed years. First, it could be argued that the definition of “administrative proceeding” in Hickel v. Halford compels an allocation. Under this argument, because Hickel v. Halford held that an administrative proceeding begins with the filing of an assessment, it arguably stands for the proposition that an assessment is required for all funds under consideration at an administrative proceeding. Thus, because no assessment was filed for the portion of the settlement that concerned unassessed years, those years would not be part of the administrative proceeding.

***6** We do not think a court would agree with this interpretation of Hickel v. Halford. Hickel v. Halford merely held that an assessment begins an administrative proceeding. 872 P.2d at 181. The court did not hold that the administrative proceeding was limited to those issues raised in the assessment. Indeed, by recognizing that the BP question remained unresolved, the court implicitly acknowledged that the question of the scope of the proceeding was different from the question of the initiation of the proceeding. Id. at 186. In short, nothing in Hickel v. Halford dictates that the BP settlement should be allocated between the general fund and the budget reserve fund.

The second possible argument in favor of an allocation was raised by the state in oral argument. We argued that settlement of issues for years not covered by the request for appeal could be viewed as equivalent to applying a methodology after a judgment. Under this argument, the portion of the BP settlement that applied to unassessed years was not the result of the termination of an administrative proceeding, but was the result of applying an interpretation of law to future factual situations.

In other contexts, this argument would be persuasive. For example, in the settlement of the ANS royalty litigation, the parties resolved the issue of valuation of royalty oil, and agreed to a formula for future valuation. Only the payments received for the settlement of the years at issue in the ANS litigation, however, were deposited in the budget reserve fund. Future royalty payments calculated under the settlement formula will be deposited in the general fund unless those payments themselves become the subject of an administrative proceeding or litigation.

In the BP case, however, this argument is not persuasive. We expect the courts will follow Judge Bryner's reasoning that the facts of each case should be examined to determine if a payment was a result of the proceeding or was independent of the proceeding. The BP settlement was a lump-sum settlement received at the termination of the proceeding. No formula or method was derived in that settlement that will be applied to future tax years. Instead, the parties determined BP's final liability for both the assessed years and for certain issues from unassessed years, and one closing agreement governed the entire settlement. Money received in settlement of the unassessed issues was commingled with money received in settlement for other issues in the proceeding. Under these facts, the BP settlement is distinguishable from the ANS settlement.

Moreover, Hickel v. Halford held that the hallmark of an administrative proceeding is finality. 872 P.2d at 181-82. Here, BP's liability for the settled issues is final. The money received from BP for these issues is not subject to further appeal. In contrast, application of a settlement or judgment to future liability could be the subject of an appeal, even though the methodology or point of law decided in the settlement or judgment would not be at issue. It follows that all money received in the lump-sum settlement from BP was received as a result of termination of an administrative proceeding, and should be deposited in the budget reserve fund.

***7** Thus, we advise that the money received in the 1993 BP settlement that had been allocated to the general fund should be transferred to the budget reserve fund, with the interest it would have earned had it been in the budget reserve fund. Any other lump-sum settlements agreed to as a result of the termination of an administrative proceeding that fixed liability for unassessed years should also be deposited in the budget reserve fund. Revenues received for unassessed years that were affected by a settlement of an administrative proceeding, but for which the tax liability had not been finally determined at the proceeding, however, are not subject to deposit in the budget reserve fund.

II. Contractual disputes concerning royalty payments are administrative proceedings if one party properly notifies the other that a binding proceeding has begun.

Commissioner Shively has requested advice on when settlements of disputes concerning mineral revenues under oil and gas leases and royalty sale contracts are settlements of “administrative proceedings” subject to deposit in the budget reserve fund. In royalty disputes, unlike tax disputes, the rights of the parties are usually governed by contract. Two types of contracts are at issue. First, DNR administers contracts for sale of royalty oil to third parties. Many of these contracts contain dispute resolution clauses that require a purchaser to seek adjudication of a dispute before the commissioner of DNR. Second, DNR administers

oil and gas leases, which require an oil and gas producer to pay the state a royalty consisting of a percentage of the oil produced on the lease. These leases have typically not contained dispute resolution clauses.

A. A binding resolution of a contract dispute by DNR under the dispute resolution clause of a royalty sale contract begins an administrative proceeding.

State oil and gas leases require that a lessee pay to the state a royalty consisting of a portion of the oil and gas produced under the lease. The state may take its royalty oil "in kind"--as oil--or "in value"--as money. Typically, when the state takes the oil in kind, it does so after it has negotiated a contract to sell the oil to an in-state refiner. Disputes occasionally arise under these sales contracts, many of which contain a dispute resolution clause such as the following:
INTERPRETATION OF TERMS AND CONDITIONS. In the event that there is a disagreement about the meaning or application of a word, term, or condition in this Agreement, Purchaser will present the arguments supporting its view in writing to the Commissioner for her consideration. The Commissioner will subsequently, within a reasonable time, issue a finding on the meaning or application of the disputed word, term, or condition, setting forth the basis for her conclusions. Purchaser agrees to accept findings by the Commissioner under this **Article** as long as there is substantial evidence supporting the Commissioner's findings.

***8** Whether a settlement of a dispute concerning the amount due on a royalty sales contract is an administrative proceeding for purposes of the budget reserve fund depends on whether the dispute resolution process meets the criteria described in Hickel v. Halford. The first criterion requires the existence of a dispute. 872 P.2d at 175.

In Hickel v. Halford, the court discussed when a dispute between an administrative agency--DOR--and a taxpayer over the interpretation and application of tax statutes would amount to an "administrative proceeding." In royalty cases, the dispute would concern the state as a party to a contract, not as a sovereign implementing statutes. The Alaska Supreme Court has determined, however, that disputes arising under contracts can give rise to administrative proceedings. Fairbanks North Star Borough v. State, 826 P.2d 760, 763 (Alaska 1992) (determinations by DNR made pursuant to a contractual dispute resolution clause are administrative determinations which must be appealed under administrative appeal processes rather than be subject to original action). Indeed, one superior court case interpreting a royalty sales contract found that the contractual dispute resolution process was subject to an appeal in superior court and must comply with due process. See Tesoro Alaska Petroleum Co. v. State, Case No. 3AN-86-15298 (Alaska Superior Ct., April 6, 1988). Accordingly, we conclude that a dispute over a contract term satisfies the first prong of the Hickel v. Halford test.

The second and third criteria for initiating an administrative proceeding require a "document," similar to an accusation or a complaint, that "set[s] in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved." Hickel v. Halford, 872 P.2d at 175. Hickel v. Halford established that the notice of assessment sent to a taxpayer following an audit begins an administrative proceeding for the purposes of resolution of a tax dispute. Id. at 181. The court acknowledged that an assessment would not necessarily lead to a hearing or other formal proceeding, but emphasized that the assessment would fix the taxpayer's tax liability if not challenged. Id.

DNR regulations provide for an appeal process that is "available to a person adversely affected by a decision of the department." 11 AAC 02.010(a). A document that initiates this process would "set in motion mechanisms prescribed by statute or regulation under which the dispute will ultimately be resolved." Hickel v. Halford, 872 P.2d at 176. Under North Star Borough and Tesoro, a decision reached under the administrative process would be binding and would have to be appealed to superior court by the rules governing appeals from administrative decisions. [4] Accordingly, the dispute resolution procedures invoked to resolve disputes under royalty sales contracts constitute "administrative proceedings" for purposes of the budget reserve fund. [5]

***9** For purposes of the budget reserve fund the question is, when does that proceeding begin? Unlike DOR statutes which require DOR to issue an assessment within three years if it wishes to challenge a tax return, DNR regulations and statutes do

not require DNR to pursue administrative remedies if it wishes to challenge a purchaser's contractual payment. Nor do the royalty sales contracts provide for a specific document that begins an administrative proceeding. DNR's administrative appeal procedure, however, is "available to a person adversely affected by a decision of the department." 11 AAC 02.010(a). Thus, the document that begins the administrative proceeding is the "decision" specified by the regulation.

Under the regulations, "decision" means "a written determination by the department specifying the details of the action taken." 11 AAC 02.080(3). This decision can include a decision of the director of a division, which may be appealed to the commissioner, or even the decision of an employee, which may be appealed to the division director. A royalty sales dispute often arises following an audit of a purchaser's payments. Usually, an employee or the director of the division of oil and gas would write a demand letter to the purchaser. As explained below, if the demand letter provides notice that it is a final decision, and that the purchaser must appeal the decision to a higher authority or lose all legal recourse, then it begins the administrative proceeding.

Hickel v. Halford stated that the document that triggers an administrative proceeding must bind the recipient against its will unless the recipient appeals the decision. Notice is a crucial element in a binding decision. "Adjudicatory proceedings begin with the issuance by one party to the other of a document which serves both as the initiation of the dispute resolution process and as notice that the process has been initiated." Id. at 180-81.

Notice of the right to appeal a decision must be included in the decision. "Unless the document which the first party serves on the opposing party creates a legal obligation on the opposing party to either respond or accept a determination made in the party's absence, then the opposing party is free to ignore the document." Id. at 181. In Manning v. Alaska Railroad Corp., the court held that "[f]or Appellate Rule 602(a)(2) to apply, an agency must clearly indicate that its decision is a final order and that the claimant has thirty days to appeal." 853 P.2d 1120, 1124 (Alaska 1993).

Thus, not all communications from DNR officials to a purchaser would necessarily begin an administrative proceeding. For example, DNR could send a notice of deficiency and demand for payment without initiating an administrative proceeding, if DNR does not inform the purchaser that it was initiating a proceeding and that the purchaser had thirty days to respond:
An adjudication does not begin, however, until both functions have been served. Notice without the initiation of the proceedings is only notice of intent to initiate, requiring further notice. Similarly, until the second party is notified of the initiation of the proceeding, the proceeding cannot be effective as an adjudication.

***10** Hickel v. Halford, 872 P.2d 181 n.22. [6]

The same criteria apply when a purchaser purports to invoke the dispute resolution clause contained in many of the royalty sales contracts. If the purchaser has the right to invoke the clause and provides sufficient notice that it is invoking the clause, DNR would be obligated to respond within a reasonable time. This legal obligation to respond means that an administrative proceeding has begun. Id. at 181.

In sum, any money received in settlement of a dispute arising under a royalty sale contract after either party clearly invokes administrative dispute resolution procedures in a manner that binds the other party, must be deposited in the budget reserve fund. This is true even if the money is received as a result of amicable settlement negotiations prior to the convening of a hearing.

As we understand the facts, this opinion will not require transfer of any money from the general fund to the budget reserve fund. Most of the royalty sales disputes settled since July 1, 1990, were being litigated in court and the money was deposited in the budget reserve fund. In one dispute settled before litigation began, DNR sent a demand letter to the purchaser, but did not notify the purchaser of its right to appeal or purport to invoke the dispute resolution clause. Accordingly, in that case, no administrative proceeding was begun and the money received in settlement was properly deposited in the general fund.

B. Royalty disputes arising under leases have traditionally been resolved by litigation rather than administrative proceedings.

The state has a long history of royalty disputes with North Slope producers. These disputes have generally resulted in litigation. The leases with oil and gas producers do not contain a dispute resolution clause. In seeking a resolution of disputes that arise under the leases, the state has traditionally acted as a private contracting party, usually suing the producers for breach of contract rather than pursuing an administrative remedy.

Disputes have arisen under oil and gas leases that have been resolved prior to litigation. In the usual case, settlement discussions are precipitated by a demand letter from DNR to the lessee. To our knowledge, however, DNR has never purported to issue a "binding" decision to a lessee regarding a deficiency, or informed a lessee that it must appeal the decision through the administrative process. Accordingly, we conclude that all settlements of lease disputes that have occurred prior to litigation were properly deposited in the general fund.

Whether, in the absence of a dispute resolution clause in the lease, DNR could require a lessee to appeal a notice of deficiency under 11 AAC 02.010--02.080, remains an open question. Although we believe that DNR could invoke these procedures, this question probably will not be resolved until it is heard in court. For purposes of the budget reserve fund, an administrative proceeding will have begun when DNR issues a final decision under a lease that informs the lessee that it either must pay the amount due or appeal the decision through the administrative process. [7]

CONCLUSION

***11** Lump-sum tax settlements received at the termination of a tax appeal must be deposited in the budget reserve fund, regardless of whether some of the money received was to settle unassessed years. Money received for tax years for which no assessment has been issued, and for which liability has not been fixed at the termination of the administrative proceeding, however, should be deposited in the general fund.

Royalty settlements occurring before litigation are the result of an administrative proceeding, and thus subject to deposit in the budget reserve fund, if one of the parties notifies the other that it is properly invoking administrative dispute resolution procedures. Any money received in a settlement occurring before such notice would not be the result of an administrative proceeding, and should be deposited in the general fund.

Stephen C. Slotnick
Assistant Attorney General

Footnotes

1 A percentage of some settlements is subject to deposit in the permanent fund or the school fund. This memorandum concerns only that portion of the settlements subject to deposit in either the budget reserve fund or the general fund.

2 The sparse legislative history of **Section 17** is described in 1992 Op. Att'y Gen. No. 1 (April 24).

3 Other issues for 1987-90 remained live and state auditors continued working on the audit for these tax years.

4 A tax assessment that has not been appealed grants the state special collection rights that other administrative decisions do not enjoy. See AS 43.05.270. Hickel v. Halford made clear, however, that a document begins an administrative proceeding if that document subjects a party who fails to respond to an order of judgment by default. 872 P.2d at 182 n.26.

5 These procedures may be modified to some extent by contract. Nevertheless, any dispute resolution procedure followed by DNR must conform to the requirements of due process, Tesoro, Case No. 3AN-86-15298, and, once properly invoked, would constitute an administrative proceeding.

6 In a decision that predated the adoption of DNR's regulations governing appeals, Judge Shortell held that DNR must provide an opportunity for the royalty purchaser to present its case in an appeal under the royalty sales contract. Tesoro, Case No. 3AN-86-15298, at 4. In Tesoro, the purchaser had written to the Commissioner, presenting pages of argument and information about the dispute, requesting that the Commissioner issue an interpretive decision on the question. The Commissioner issued a decision, and Tesoro

appealed to superior court, arguing, among other things, that it was not given sufficient opportunity to present its case. Although the only process specified in the contract provided that the Commissioner would issue a decision after the purchaser presented its views in writing, the court held that due process principles applied and that Tesoro's right to argue its position fully was impaired. Yet, even in this case, the problem was defective notice--had DNR notified Tesoro that the dispute resolution clause had been invoked, Tesoro could have voiced its arguments more fully.

7 Settlements under mineral leases other than oil and gas leases may also be subject to deposit in the budget reserve fund. We have not researched these leases, but the principles of this opinion apply when determining whether mineral revenue was received as a result of the termination of an administrative proceeding.

1995 Alaska Op. Atty. Gen. (Inf.) 111 (Alaska A.G.), 1995 WL 867852

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1977 WL 21975 (Alaska A.G.)

Office of the Attorney General

State of Alaska
August 31, 1977

Re: Permanent fund, irretrievability of money appropriated to; our file J-66-106-78

***1** Hon. Clark Gruening
Chairman
House Special Committee on the **Permanent Fund**
528 West Fifth, Suite 270
Anchorage, Alaska 99501

Dear Representative Gruening:
You have asked whether money appropriated to the **permanent fund** in excess of the amount required by the constitution is irretrievable.

Section 15 of article IX of the Alaska Constitution, as added by the 1976 amendment to the constitution, reads as follows (emphasis added):
At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a **permanent fund**, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for **permanent fund** investments. All income from the **permanent fund** shall be deposited in the general **fund** unless otherwise provided by law.

Your question really is whether the limiting language of section 15 applies not only to the mandatory 25 percent of mineral revenues placed in the **permanent fund** but also to any additional money placed in the **fund**.

We believe that the answer is yes.

The language of the amendment providing for the **permanent fund** is clear enough. There is to be a **permanent fund**. At least 25 percent of the enumerated mineral revenues are to be placed in it. The use of the words “[a]t least” clearly contemplates that additional monies may well be placed in the **fund**. Once there, they form the **fund's** principal. That principal “shall be used only” for income-producing investments. Hence, on its face, what becomes a part of the principal may no longer be withdrawn for another purpose. Only the income from investments of the principal is available.

It is a universal principle that the legislature's law-making power is plenary except as limited by the state or federal constitutions. In order to hold that the legislature may not appropriate additional monies to the **permanent fund** and also provide for their subsequent withdrawal, the courts must find an express or implied prohibition against its doing so. Facially, the constitution's restriction on the use of the **fund's** principal seems to constitute such an implied restriction, i.e., the principal may be invested but nothing else, including a withdrawal, may be done with it.

It could be possible, one might argue, for the legislature to make appropriations to the **fund** by law and specify that they are made on the condition that they are intended to be retrievable and are null and void ab initio if ruled not to be. The problem is that the courts would likely rule that the condition itself is so inconsistent with the provisions of section 15 that it is absolutely void, i.e., that the legislature is prohibited from withdrawing from the principal both directly and indirectly.

***2** Or the legislature could appropriate to the **fund** and specify that the monies appropriated are not to be considered a part of the **fund's** "principal" in the sense of the constitution, i.e., as monies available solely for investment, but rather are to be considered as a temporary addition to the **fund** which is to be used for investment but which shall be accounted for separately and may be withdrawn. Again, the problem is that the courts would likely rule that such legislation is so inconsistent with the provisions of section 15 that it is void. Either there is a **permanent fund** or there is not.

We are dealing here with a peculiar—perhaps unique—quasi-trust. Unlike most trusts, the principal may not be reached whatever, either now or in the future. No one has a future right to the principal. Instead, the principal is to be invested in perpetuity to produce income. Only the income from investments may be reached. Absent still another constitutional amendment, we see no way around this result. A **permanent fund** was intended, and a **permanent fund** appears to have been achieved.

Accordingly, we doubt very much that any money appropriated to the **permanent fund** may subsequently—without a constitutional amendment—be withdrawn.

Sincerely yours,

Avrum M. Gross
Attorney General
Rodger W. Pegues
Assistant Attorney General

1977 WL 21975 (Alaska A.G.)

End of Document

1977 WL 21820 (Alaska A.G.)

Office of the Attorney General

State of Alaska
File No. J-66-107-78
September 16, 1977

Re: Permanent fund, accounting for inflation

***1** Hon. Clark Gruening
Chairman
House Special Committee on the **Permanent Fund**
528 West Fifth, Suite 270
Anchorage, Alaska 99501

Dear Representative Gruening:
You have asked whether there is any legal requirement that the statutory guidelines for administering the **permanent fund** take inflation into consideration.

We believe that the answer is no.

The answer to your question requires an inquiry into the legal nature of the **permanent fund** and, there being no law on the precise subject, involves some speculation.

First, we believe that, despite the absence of an actual transfer of legal and equitable interests to a trustee and beneficiary respectively, the Alaska Supreme Court will treat the **permanent fund** as a trust or quasi-trust, and as a general rule, apply trust concepts in determining its administrators' duties. We make this assumption (1) because of the tendency of the court, exemplified by such cases as Moore v. State, 553 P.2d 8 (Alaska 1976), to impose trust-like duties upon the State's management of its patrimony, and (2) because the constitutional amendment which created the **permanent fund** is extremely similar to the classic spendthrift trust both in its roots or causes and in its establishment, i.e., the owner of the State's capital, the people, dissatisfied with the state government's spending of the royalty bonus from the Prudhoe Bay leases, has resolved to remove a portion of that capital from the spending power of the government and to place it in trust, with only the income from its investment available to the government for expenditure.

Because the people established the trust, we believe that the state government will be deemed to be the trustee, not the trustor. This means that, despite the power vested in it by the constitutional amendment to designate by law the kinds of investments to be made, the legislature—as the appropriating arm of the government—will not be deemed to be the trustor or settlor, and that therefore, its power to designate eligible investments is not plenary but rather is limited by the express terms of the amendment on the one hand and by implied trust concepts on the other. In other words, the legislature may designate only income-producing investments and may not designate imprudent, income-producing investments or provide for imprudent administration of the **fund** principal. To the extent, if any, that it did, the managers of the **fund** would nevertheless remain under a duty to make only prudent income-producing investments and to provide a prudent administration.

Finally, we believe that the Alaska Supreme Court will rule that—absent exceptional circumstances involving the very existence of the State or its citizens—the preservation of the **fund** principal is of primary import, i.e., that investment policies cannot endanger the principal. This belief rests on what we perceive to be the essential character of this trust or quasi-trust, i.e., a conservative, cautionary nest egg. [a1]

***2** Of course, the Alaska Supreme Court could rule that no trust or quasi-trust exists and the law of trusts does not, therefore, govern the **fund's** administration. That would remove the administration of the **fund** from the operation of the prudent-man rule. There would then be no duty to limit investments to those which are prudent. That would pretty much give the legislature the power to authorize the expenditure of the **fund's** principal on any income-producing investment even though it would not be a prudent, i.e., an investment which a trustee could not properly make. This result would allow the **fund** principal to be frittered away and thereby frustrate the basic purpose of the constitutional amendment. Principally for that reason, we believe the Alaska Supreme Court will impose trust concepts to avoid that result and to give the amendment its full effect.

There can be no question that a trustee must take into consideration the trend of prices and the cost of living, the prospect of inflation or deflation. RESTATEMENT (SECOND) OF TRUSTS 2d § 227, Comment e (1959). To do otherwise would hardly be the conduct of a man of prudence. Accordingly, the **fund** managers will have to take inflation (or deflation) into account in making and changing investments, if—as we believe—the **fund** constitutes a trust.

It does not follow, however, that the legislature has a duty to provide specific guidelines on the matter. If the court rules that there is a trust, the prudent-man rule applies. If it rules otherwise, the rule does not apply. Unless the legislature itself resolves the question by making the **fund** a trust, the matter is entirely up to the court. Whichever way it rules, the court would not, and could not, order the legislature to adopt any particular guidelines. It would merely order the **fund** managers to follow the prudent-man rule.

Nor does the legislature have any duty to increase the amount of the **fund** principal because of inflation. The constitutional amendment, which sets forth the principal terms of the trust, makes it mandatory to deposit 25 percent of the designated mineral revenues in the **fund**. That is the trust property which must be administered, we believe, under the prudent-man rule. While the legislature qua legislature clearly has the power to increase that amount, nothing in trust law places a duty on it to do so. It could also provide for all or a portion of the income from the principal to be deposited in the **fund**, i.e., added to the principal. But under the terms of the trust, i.e., the constitutional amendment, it has no duty to do so.

We hope that this answers your question. We remind you that we are making an educated guess as to the trust or quasi-trust nature of the **permanent fund**. We believe it is a trust or quasi-trust and that trust law applies. We are constrained to add that we could be wrong. The legislature may wish to treat the **fund** as a trust. That would resolve the issue. It should feel free, however, to experiment and treat it otherwise insofar as it determines the public interest warrants doing so, and let the court resolve the issue.

Sincerely yours,

***3** Avrum M. Gross.
Attorney General
By: Rodger W. Pegues
Assistant Attorney General

Footnotes

a1 While the **permanent fund** is essentially a conservative device, the constitutional amendment was not overly conservative. It did not apply to taxes on minerals at all and it still leaves 75 percent of other mineral revenues available for expenditure.

1977 WL 21820 (Alaska A.G.)

End of Document

1983 WL 42491 (Alaska A.G.)

Office of the Attorney General

State of Alaska
File No. 366-484-83
March 10, 1983

Appropriation of income from and deposits to the Alaska permanent fund

***1** Honorable Don Bennett
Alaska State Legislature
Pouch, V
Juneau, AK 99811

Dear Senator Bennett:
This responds to your letter of March 3, 1983. My views in response to your specific questions are:
1. The **permanent fund** dividend **fund** established under AS 43.23.045 would arguably involve an unconstitutional dedication of state revenue if money were transferred to that **fund** from income of the **permanent fund** without an appropriation. However, this view is not free from doubt since an argument can be made, based on the language of article IX, section 15 establishing the **permanent fund**, that an appropriation for that purpose is not required. Although I understand that in past years money has been transferred to the dividend **fund** pursuant to AS 43.23.045 without an appropriation, I have advised that this practice be discontinued in the future. Senate Bill 149 which was introduced this session at the Governor's request, would appropriate additional money from the **permanent fund** dividend **fund** to pay 1982 dividends under AS 43.23. I would also advise that, if the dividend program is not repealed, AS 43.23.045 be amended to clarify this appropriation requirement in order to avoid any confusion on this point.

2. I believe that the reinvestment of income of the **permanent fund** as principal may be authorized by statute without an appropriation. The reasons for this view are explained below.

3. Yes, it is permissible for the legislature to increase by statute the percentage of certain mineral revenues which are constitutionally dedicated to the **permanent fund**.

The reasons for my responses to your questions follow in reverse order.

The constitutional amendment authorizing the creation of a **permanent fund** dedicates 'at least twenty-five percent' of certain mineral revenues to that **fund**. Alaska Const. art. IX, § 15. This language clearly anticipates that the percentage of revenues so dedicated may be increased. The legislature has increased that amount to 50 percent of revenues from certain sources. AS 37.13.010. I see no question as to the constitutionality of this statute.

With regard to the use of income produced by the **fund**, the constitution provides that it 'shall be deposited in the general **fund** unless otherwise provided by law.' Alaska Const. art. IX, § 15. When this language was adopted by the legislature for submission to the voters, it was accompanied by a 'joint chairman's report on CSSS HJR 39' (1976 H. Jour. at 684-685), which stated that the purpose of this language is 'to give future legislatures the maximum flexibility in using the **Fund's** earnings —ranging from adding to **Fund** principal to paying out a dividend to resident Alaskans.' On its face, the requirement that the income be deposited in the general **fund** 'unless otherwise provided by law' appears to authorize statutory dedication for any public purpose. This office has advised in the past and I concur that this reading of article IX, section 15 would create a tremendous exception to the constitutional dedicated **fund** prohibition, art. IX, § 7, which was not explained to the voters in

the ballot materials, election pamphlet, or publicity surrounding the amendment. See 1980 Op. Att'y Gen. No. 3 (March 19) at 7-9 (copy attached).

***2** For this reason, I favor a narrower interpretation of the last sentence of article IX, section 15. One possible reading would be that the legislature intended that the income could be used without appropriation either for reinvestment or for distributing dividends to Alaskans, as explicitly mentioned in the joint chairman's report, and the attached Attorney General opinion. However, it is difficult to discern from the language of article IX, section 15 why the income could be dedicated for these but not for other important public purposes. Another possible interpretation is that an appropriation is required for any use of the income, including reinvestment as principal of the **permanent fund**. However, this interpretation would render the phrase 'unless otherwise provided by law' meaningless, since the income would then be treated as automatically becoming part of the general **fund** despite any attempted dedication by law. Article IX, section 15 clearly contemplates that the legislature may by law provide for some use of the **fund** other than deposit in the general **fund**.

The interpretation of article IX, section 15 which I find to be most reasonable and compatible with the constitutional prohibition against dedications is that the legislature may provide by law for the income to remain in the **permanent fund** (either through reinvestment as principal or retention in an undistributed income account) without appropriation, but may not transfer income to another **fund** or authorize it to be spent without an appropriation. This view is consistent with the legislation enacted last session providing for reinvestment of an amount sufficient to offset inflation, and retention of the balance in an undistributed income account where it remains available for appropriation. AS 37.13.145, a amended by ch. 81, SLA 1982. Legislation which will soon be introduced at the Governor's request will propose amendments to AS 37.13 which are consistent with this view.

I share your concern that our state government avoid the problems associated with statutory dedications of revenue. I also appreciate that the legal and constitutional provisions regarding governmental finance and their past and present administrative interpretations are sufficiently complex to require careful study and thorough discussion by all involved. A copy of a recent lengthy opinion regarding the meaning and application of the dedicated **fund** prohibition is attached for your information. 1982 Op. Att'y Gen. No. 13 (Nov. 30). Please let me know if I can be of further assistance.
Very truly yours,

Norman C. Gorsuch
Attorney General

1983 WL 42491 (Alaska A.G.)

End of Document

1984 WL 60991 (Alaska A.G.)

Office of the Attorney General

State of Alaska
File No. 366-405-84
February 6, 1984

Appropriation of permanent fund income to finance the 'hold harmless' provisions of the permanent fund dividend program

***1** Jay Hogan
Associate Director
Office of Management & Budget
Division of Budget Review

You have requested our review of a proposed appropriation set out in HB 511 (an appropriation to implement the executive budget). The provision in question authorizes the expenditure of **permanent fund** income to replace public assistance payments to individuals lost because of the receipt of **permanent fund** dividends. AS 43.23.075.

Article IX, section 15 of the Alaska Constitution provides: 'All income from the **permanent fund** shall be deposited in the general **fund** unless otherwise provided by law.' The constitution has been implemented by the provisions of AS 37.13.145 and AS 43.23.045. Under those statutes, a certain part of the income is allocated to the **permanent fund** dividend **fund**. AS 43.23.045(b). Another part of the income is allocated to offset the devaluation of money caused by inflation. AS 37.13.145. The remainder of the income is retained in the undistributed income account and is available for appropriation by the legislature for any valid public purpose.

The 'hold harmless' benefits are paid through an existing general relief program administered by the Department of Health and Social Services under AS 47.25.120-47.25.300. It appears that all of the elements are present to make this an effective appropriation. The following elements are essential:
1. a **funding** source must be identified;

2. H&SS must have the power under AS 47.25 to provide the hold harmless benefit; and

3. nothing in law prevents the unallocated part of the **permanent fund** income from being appropriated by the legislature.

In conclusion, we believe that nothing prevents the financing of the hold harmless benefits with an appropriation of **permanent fund** income retained in the undistributed income account. We recommend that AS 37.13.145 be amended to clearly provide that the undistributed income is available for appropriation. If the source of **funding** for the hold harmless benefit is the dividend **fund**, AS 43.23.055(1) should be amended to authorize the payment of administrative expenses from the dividend **fund**.

Norman C. Gorsuch
Attorney General
James L. Baldwin
Assistant Attorney General
Governmental Affairs-Juneau

1984 WL 60991 (Alaska A.G.)

End of Document

1987 WL 121054 (Alaska A.G.)

Office of the Attorney General

State of Alaska
File No. 663-87-0356
February 12, 1987

Irretrievability of money appropriated to permanent fund

***1** Honorable Rick Halford
Senate Majority Leader
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Dear Senator Halford:
You have requested our advice on whether the "extra appropriation" made from the general **fund** to the **permanent fund**, which was considered a loan and subsequently forgiven by the legislature, can be withdrawn from the **permanent fund** principal. Briefly, the answer is no and we hereby reaffirm the opinion issued on this topic in 1977. See 1977 Inf.Op.Att'y Gen. (Aug. 31; 663-78-0106).

When the legislature exercised its plenary power by transferring money from the general **fund** to the **permanent fund**, it considered the appropriation to be a loan. Then, when the legislature forgave the loan, the appropriation to the **permanent fund** became a gift. Once a gift is added to the principal of the **fund**, it is subject to the provisions of article IX, section 15 of the Alaska Constitution. A gift to the principal of the **fund** cannot be given subject to conditions. See 1983 Inf.Op.Att'y Gen. (Nov. 14; 663-84-0260). It should also be noted that the subject loan was forgiven unconditionally by the legislature. For example, see: sec. 20, ch. 101, SLA 1982.

Finally, as stated in the 1977 opinion, we believe that appropriations (or gifts in the form of forgiven loans) to the **fund** which are made on the condition that they are retrievable would be ruled null and void ab initio by the courts under article IX, section 15, of the Alaska Constitution.

We hope this opinion addresses your concerns.
Sincerely yours,

Grace Berg Schaible
Attorney General
Marjorie L. Odland
Assistant Attorney General

1987 WL 121054 (Alaska A.G.)

2003 WL 25875053 (Alaska A.G.)

Office of the Attorney General

State of Alaska
AG File No. 663-03-0153
June 18, 2003

Re: Questions Concerning the Accounting for Principal and Income of the Alaska Permanent Fund

***1** Eric Wohlforth
Chair
Board of Trustees
Alaska Permanent Fund Corporation
P.O. Box 110410
Juneau, Alaska 99811-0410

Dear Mr. Wohlforth:
This letter responds to a request from the Alaska Permanent Fund Corporation (the corporation) for an opinion interpreting the provisions of article IX, section 15, of the Alaska Constitution and implementing statutes. Particularly, the APFC trustees ask if their current policies correctly determine net income available for appropriation and the limitations, if any, properly placed upon the expenditure of income from the earnings reserve account.

Introduction

At the end of each fiscal year, AS 37.13.145(b) directs the corporation to transfer to the dividend fund established under AS 43.23.045 an amount that is equal to 50 percent of the "income available for distribution" under AS 37.13.140. In addition, AS 37.13.145(c) directs the corporation to transfer to the principal of the Alaska permanent fund an amount "sufficient to offset the effect of inflation" on the principal ("inflation-proofing"). These transfers are to be made from the permanent fund's earnings reserve account established by AS 37.13.145(a). Separate appropriations authorizing those transfers for the current fiscal year (ending June 30, 2003) were approved by the legislature in the FY 2003 operating budget (sec. 10, ch. 94, SLA 2002).

Although the necessary appropriations for the transfer of money to pay permanent fund dividends and inflation-proofing in 2003 are enacted, possible declines in the financial markets can cause some uncertainty whether there will be a balance available for expenditure from the earnings reserve account to cover the amounts appropriated. The question arises for two related reasons. First, there is an apparent inconsistency between the provisions of AS 37.13.140 and AS 37.13.145, both adopted in the 1980's, and the accounting requirements of GASB 31, [1] which became effective in 1998, regarding how to determine the size of the earnings reserve account from which money may be transferred. Second, although the constitutional provision that created the permanent fund [2] has always been viewed as providing "protection" for the principal, the nature and extent of that protection are unclear. Accordingly, the corporation requested an opinion from this office to assist in determining how much is available for expenditure from the earnings reserve account to finance the 2003 appropriations for dividends and inflation-proofing. [3]

Questions presented:

Is the corporation's current policy that only realized income of the permanent fund is available for expenditure under AS 37.13.145 correct? If not, how should the amount available for expenditure from the permanent fund under AS 37.13.145 be determined?

***2** Short answer: We believe that the corporation's policy that only realized earnings are available for expenditure is correct.

Is the corporation's current practice that both realized and unrealized income of the **permanent fund** should be taken into account in determining the amount that is available for appropriation correct? If not, how should the amount available for appropriation from the **permanent fund** be determined?

Short Answer: We believe that it would not be correct to compute the amount available for distribution by using unrealized gains and losses to determine income. Existing law clearly provides that only realized gains and losses are allocated to income and are thus available for distribution. Under the relevant constitutional provision, what is not principal is income; therefore any gain or loss not expressly allocated to income must be allocated to principal.

Do the constitution and statutes require that income of the **fund** may not be appropriated when doing so would bring the total value of the **permanent fund** including all unrealized gains and losses below the sum of the amounts deposited or appropriated to principal? If not, are there any other limitations with respect to the use of principal that are applicable in determining the amount that is available for expenditure or appropriation from the **permanent fund**?

Short Answer: We believe that principal is the total value of all deposits and appropriations adjusted for unrealized gains and losses that should properly be allocated to principal. There is no doubt that the principal of the **permanent fund** cannot be deposited in the general **fund** and must only be used for income producing investments. However, if unrealized gains and losses are allocated to principal, by definition there is no invasion or misuse of principal if only statutory income, realized gains, is deposited in the earnings reserve **fund** and available for appropriation.

Before we explain how we arrived at the answers set out above, it is necessary to consider the history of the **permanent fund** amendment and the actions of the legislature and the corporation to implement the amendment.

Legislative History Relevant to the Questions Presented.

1. Prior to Adoption of the Amendment.

The legislature passed the **permanent fund** amendment in the form of HJR 39 which was ratified by the voters at the 1976 general election. The effective date of the amendment was February 21, 1977.[4] The amendment was introduced by Governor Hammond.[5] The legislative history of consideration of the resolution is primarily devoted to the amount and kind of revenue to be dedicated to the **permanent fund**. The governor first proposed a 10 percent dedication of mineral revenues but later supported an increase to at least 25 percent.

In a joint report of the House Judiciary and Finance Committees, the chairmen explained that the principal would be used only for income-producing investments that the legislature could change from time to time to meet the needs of the state. They explained that the effective date of the amendment was delayed somewhat to permit the legislature to provide by law for an investment structure for the **fund**. Finally, they explained that it was their intent to give future legislatures the maximum flexibility in using **permanent fund** earnings, ranging from adding to principal to paying out a dividend to residents.[6]

***3** In supporting materials provided at the time of consideration by standing legislative committees, it appeared that the governor intended that the **permanent fund** could be used to invest in economic development projects with a long term net economic benefit.[7] This same view was repeated after adoption of the resolution when various proponents took their case to the voters.[8] Although the voters were told that it was up to the legislature to shape the **permanent fund**, it was explained that the "income producing" requirement gave the state broad latitude and that local bonds could be purchased as a means of financing instate development.[9] The Revenue Commissioner reported

I hear public support for the **fund** from three sectors, ... from those who favor a savings account approach, those who want it used to provide assistance in community development and those who want it to provide economic diversity in the state. ... [A] major goal [is] the strengthening of the state's economic base by investing in renewable resources and by policies which would reduce seasonality of employment. [10]

The voters were told that "the income from the **fund** will be available for general appropriation by the legislature but the principal of the **fund** may not be touched." [11] The **permanent fund** was described as "a lasting savings account." [12]
The object is to prevent future legislatures from doing what previous legislatures did with the $900 million bonanza received by the state from the sale of Prudhoe Bay leases in 1969. That gigantic sum ran through the legislators' fingers like water, to the alarm of many who had pleaded at the time that the $900 million be invested, the principal preserved and the state spend only that money derived from interest. [13]

There is fairly strong evidence that the voters were aware that the legislature would have a role in providing the details for administration of the **permanent fund**. Whether the **fund** was to be a savings account or a development bank was not resolved by the legislature until four years after adoption of the amendment.

2. Post Adoption

A. Legal Opinions

After the amendment took effect, the attorney general was asked to interpret its meaning for various purposes. Set out below are opinions discussing aspects of the **permanent fund** that are relevant to our consideration of the corporation's accounting practices.

In August of 1977, the attorney general answered whether money appropriated to **permanent fund** principal in excess of the amount required by the constitution is irretrievable. The attorney general confirmed that once money was deposited in principal by any means, it could not be removed without further amendment of the constitution. [14] The attorney general advised that the constitution's restriction on the use of **fund** principal is an implied restriction against the withdrawal of appropriated principal. [15]
The attorney general speculated that the legislature probably could not condition appropriations to principal on the ability to withdraw at a future date or to specify that such amounts would not be considered principal. The attorney general observed that the **permanent fund** was a "peculiar — perhaps unique — quasi-trust."

***4** In September of 1977, the attorney general again interpreted the amendment to determine whether the legislature was required to enact legislation which takes inflation into consideration in the management and investment of **fund** principal. [16]
In this opinion, the attorney general restated the conclusion that the **permanent fund** was a trust or quasi-trust. This was based on a prediction that "the Alaska Supreme Court will follow a previously exhibited tendency to impose trust-like duties on the state's management of its patrimony" and the amendment "is extremely similar to the classic spendthrift trust both in its roots and causes and in its establishment ...."

The attorney general also concluded that the legislature acts as a trustee which must prudently exercise any duty in relation to administration of the **permanent fund**. In this regard, the legislature was advised that its power was not plenary but limited by the constitution and implied trust concepts. This office advised that there was no legal requirement that inflation be taken into account in statutes enacted to implement the **permanent fund**. The legislature was advised that the foregoing interpretation cannot be considered settled until the supreme court rules on the matter. However, the legislature was advised that it could resolve the question of status by making or treating the **permanent fund** as a trust.

In 1999, the attorney general contracted for an opinion from outside counsel on behalf of the board of trustees to advise on the possible transfer of **permanent fund** principal to the Constitutional Budget Reserve **Fund** (CBR). Morrison & Foerster Opinion, March 3, 1999. The advice was sought to assist the state in determining whether a proposed transfer of a portion of the **permanent fund's** assets to the CBR would involve an expenditure of principal. Similar to earlier legal opinions on the subject, Morrison & Foerster concluded that the **permanent fund** is not a true public or private trust **fund**. However, after rejecting the notion that the **fund** is a trust, the opinion resorts to trust law to support conclusions concerning the possibility of spending principal as a consequence of the transfer of principal to the CBR. Counsel observed that the board of trustees had a fiduciary obligation imposed by statute to preserve principal and to manage **fund** assets as prudent investors.

Morrison & Foerster accepted without comment the corporation's assumptions regarding principal. Under the corporation's longstanding practice, “principal” is reported as a notational number that changes only with further contributions to the **fund** - it does not fluctuate with changes in the market value of the investments purchased with principal. [17] Counsel interpreted AS 37.13.140 as inconsistent with the principal and income allocation rules usually applicable to trusts. They determined that, after the adoption of GASB 31, an invasion of principal would occur if the amount paid out exceeded the balance of the earnings reserve account which, under GASB 31, would include both realized and unrealized gains and losses. It would not occur where, after a distribution, the balance of that **fund** turned negative. The critical difference, according to that opinion, is between an action of the trustees and the natural fluctuation of the investment markets. The opinion suggests that unrealized losses could not force an invasion of principal. Morrison & Foerster Op. at p. 16, n.7.

***5** At the time of the opinion, the **permanent fund** was enjoying the benefits of a sustained period of capital appreciation which was accounted for in the earnings reserve. This fact permitted Morrison & Foerster to conclude that, because the **fund's** GASB 31 earnings reserve account was then substantially in excess of that amount, a $4 billion transfer of assets was possible to accomplish without “invading principal.”

B. Principal and Income Accounting Practices

Next we consider the past principal and income accounting practices applied to the **permanent fund** and the sources from which those practices were derived. These practices show that differing interpretations of principal and income prevailed under previous versions of the **fund's** enabling statutes.

For the period 1977 - 1980, the **permanent fund** was under the interim management of the Department of Revenue while legislation was pending to create the corporation. The **fund** was invested primarily in debt instruments with a fixed rate of return. Ch. 6, SLA 1977. In 1980, legislation was enacted providing for the management of the **permanent fund** by a public corporation within the Department of Revenue, managed by a board of trustees. Ch. 18, SLA 1980. This legislation modified the rate of dedication to the **permanent fund** from 25% to 50% of revenue received by the state from mineral leases issued after December 1, 1979, or, in the case of bonuses, after February 15, 1980. The 1980 legislation only authorized the corporation to invest in certain fixed return instruments. [18] Under this statute, income was defined to be the interest earned on investments and any realized gains or losses were to be allocated to principal. [19]

In 1982, legislation was enacted making four amendments bearing on the corporation's accounting practices: (1) the authorized list of investments was expanded to include equities; (2) the concept of “net income” was established which included gain or appreciation in value determined by generally accepted accounting principles, excluding unrealized gains or losses; (3) a portion of each year's **permanent fund** income was targeted for reinvestment back into the **fund** to offset inflation; and (4) a valid **permanent fund** dividend program was established. Ch. 81, SLA 1982; ch. 102, SLA 1982. [20]

During the interim management period of 1977 - 1980, and after creation of the corporation until 1982, the accounting practices applied to the **permanent fund** distinguished between income and appreciation in the value of investments. For the first two accounting cycles of the corporation (1980 - 1982), income of the **fund** was defined as “the interest received in a year.” Sec. 5,

ch. 18, SLA 1980. For the entire period 1977 - 1982 during which the **fund** was limited to fixed income investments, appreciation in value ("gain") was credited to principal, interest was credited to income. [21] However, if losses exceeded gains, interest was to be transferred to principal in an effort to cover some of the loss. Former AS 37.13.130 (repealed 1982); former 15 AAC 137.060 (repealed 7/12/92).

***6** In 1982 after the **fund** was authorized to invest in equities, income was defined to include realized gain representing appreciation in value. Under then-applicable generally accepted accounting principles ("GAAP"), only realized gains (and losses) of the **fund** were recorded as income in the earnings reserve account established under AS 37.13.145. This former GAAP approach was consistent with the statutory requirement of AS 37.13.140 (in effect since 1982) for determining **fund** "net income" (from which the amount of the annual dividend transfer is then computed), which specifically excluded unrealized gains and losses from the determination. [22]

This consistency in treatment ended with the implementation of GASB 31 in 1997. Under GASB 31, the corporation is required to record as revenue in its financial statements the **permanent fund's** readily marketable investments at current fair value. The corporation has interpreted this change in GAAP as requiring all unrealized market appreciation and depreciation (unrealized gains and losses) to be included in determining income for accounting purposes, potentially resulting in large differences between GAAP net income and "net income" under AS 37.13.140. As a result, the corporation now has two different ways to report income. The first method is to report realized income, as called for by the definition of "net income" under AS 37.13.140, to determine how much is available for distribution. The other method is to apply the GAAP definition and include both realized and unrealized gains and losses to determine net income for financial reporting purposes. Depending on the situation, the corporation applies both approaches in its financial statements. The inherent conflict between these two approaches is at the heart of the request for this opinion.

In late 2001, the audit committee of the corporation considered an issue paper prepared by APFC staff which discussed the policy for determining the amount available for expenditure to pay the dividend and inflation-proofing transfers provided for under AS 37.13.145. The issue paper did not resolve the matter, but recommended the trustees seek a legal opinion from the Department of Law. While the subject was briefly discussed by the trustees, they did not pursue an opinion from the Department of Law at that time. In the absence of an attorney general's opinion, the corporation has applied a conservative "invasion test" under which realized income may not be spent if doing so causes the total value of the **permanent fund** and the earnings reserve account to fall below the historic dollar amount ("notational principal") contributed to principal from all sources. Although this limitation is not specifically addressed in the statutes, it was presumably applied in order to "protect" past contributions to principal from diminishment and has been subsumed in the corporation's accounting practices.

***7** Notwithstanding this conservative "invasion test," there have been instances in the past when distributed earnings were more than offset by unrealized losses. These distributions to the state general **fund** occurred in fiscal years 1978 and 1979 and would have amounted to an expenditure of principal under the corporation's "invasion test." This is apparently why, beginning in 2001, the corporation and corporate counsel recommended obtaining a legal review of corporate accounting policy by this office.

For fiscal year 2002, there was enough realized income accumulated in the earnings reserve account and in excess of "notational principal" to fully pay the 2002 dividend and inflation-proofing distributions without having to apply the limitation regarding invasion of principal. However, given the current investment allocation of the **fund**, a sustained downward trend in financial markets could result in the total market value of the **permanent fund** at the end of a fiscal year totaling less than the sum of the amount attributed to "notational principal," plus the amount of realized income in the earnings reserve account. If total market value of the **permanent fund** is less than the sum of those two figures, then current corporation accounting practices would limit the amount available for expenditure under AS 37.13.145 to the amount (if any) by which the total market value of the **permanent fund** on the last day of that fiscal year, including the earnings reserve, exceeds "notational principal" (the sum of all dedications and appropriations to the principal of the **fund** over time).

Discussion

At the outset we observe that the **permanent fund** has not yet experienced market conditions that required the trustees to apply an "invasion test" to limit appropriations from the earnings reserve. It appears, though, that the possibility of this happening caused the trustees to request this opinion. Notwithstanding the apparent lack of immediacy, this opinion is as appropriate and necessary now as it was in 2001 when staff and counsel first recommended it. It is important that the public and the trustees understand the correct application of the law and that the corporation's financial statements properly inform the public. It now appears that the financial condition of the **fund** and earnings reserve, barring some unforeseen and extraordinary financial event at the end of the fiscal year, will again not test the application of the concepts discussed here. Clearer opinions no doubt result when the law is not looked at through the fog of a looming crisis.

While the **permanent fund** is not a trust, we resort in part to trust principles to answer the corporation's questions, the central issue of which turns on construction of AS 37.13.140, defining income for purposes of the **permanent fund** corporation. The terms of every trust are governed by the governing document, statutes, court decision, and general trust principles. In the case of the **permanent fund**, the governing document is the Alaska Constitution and valid implementing statutes. In arriving at the correct interpretation of sec. 140, we will attempt insofar as possible to harmonize the provisions of that statute with trust principles. [23] However, if there is a conflict, existing law must prevail. An added complication is that the provisions of AS 37.13.140 can be read to be ambiguous regarding the treatment of unrealized gains and losses on assets of the **permanent fund**. We must determine whether unrealized gain or loss is an element of principal or income. This allocation is important for determining how much is available for distribution in a given year.

***8** All who have considered the legal character of the **permanent fund** agree that it is not a trust. It is a constitutionally dedicated **fund**, the principal of which must be invested in income producing assets. However, each analysis inevitably turned to trust principles to support the advice given. Early in the life of the **fund**, this office advised the legislature that it was not obligated to protect the **fund** from inflation, but that it could undertake that responsibility and make clear that the **fund** will be operated according to trust concepts. We also advised that the legislature is a trustee when it provides for the administration of the **permanent fund**. This means that the legislature may be limited in its lawmaking power when it provides meaning to terms and concepts applicable to the **permanent fund**.

It appears that the legislature intended to act consistent with the advice of this office when it first enacted statutes to implement the **permanent fund** amendment. In a free conference committee report, the chairmen declared the **permanent fund** is "... designed to be a trust which focuses on the safety of principal first and the maximization of earnings second." [24] The corporation has also done its part to interpret both the constitution and the statutes. The corporation made specific the legislature's direction through various resolutions and policies. The corporation's powers to interpret and make specific the constitution are important. However, because we are interpreting the constitution and enabling statutes, it is not likely that a court will accord deference to interpretations by either the legislature or the corporation. [25]

The constitution uses the terms "principal" and "income" in establishing the **permanent fund**. As a limited exception to the general constitutional prohibition on dedicated **funds**, the constitutional amendment creating the **permanent fund** is explicit in that only principal must remain dedicated for investment and that income should be made available for appropriation from the general **fund**. This requirement by implication prevents appropriation of principal but does not further define principal or income. It clearly does not require that principal be preserved in the manner contemplated by the "invasion test" or in any way subjugate the availability of "income" for expenditure to the dedication of "principal" to income producing investments.

Consistent with the constitutional dedication of **fund** principal to one purpose, income producing investment, the legislature has declared a general purpose to provide safety for principal and legislative committees have, in a non-binding way, expressed intent that principal must be preserved. Relying in part on this expression of intent, the corporation interpreted the constitution and enabling statutes to require that principal be recorded at the dollar amount historically deposited by dedication and

appropriation without any diminishment for gain or loss on investments. However, in doing so it appears that the corporation failed to consider the potential effect on the constitutional requirement that income be made available for appropriation.

***9** The pre-adoption history of the **permanent fund** amendment provides no evidence that a particular definition of income would be preferred over another. As explained above, the amendment was promoted by some as a savings account that would serve as a form of development bank to help diversify an economy that was too dependent on non-renewable resource revenues. There was also a clearly stated purpose to dedicate oil revenue and prevent expenditure of the dedicated amounts. The amendment expressly provided that income is to be deposited in the general **fund** or other legislatively authorized purpose. After the amendment was adopted, the legislature abandoned the development bank approach in favor of an investment **fund** managed by a public corporation authorized to make conservative fixed income investments. [26]

At the time the **permanent fund** amendment was adopted in 1976, trust law traditionally allocated gain and loss on equity securities to principal rather than income.
The proceeds of the sale of trust property are ordinarily to be treated as trust principal, even though they include profit in excess of cost price or inventory value. Losses on such sales fall on trust principal. The rule should govern sales of corporate stock where there is a gain in value due to undistributed earnings.

Bogert on Trusts, sec. 120 (6th ed. 1987). As recently as 1984, the legislature chose to adopt traditional allocation rules for common trusts. [27]

There has been a movement among the trustees of endowment trusts to change traditional allocation rules to permit investment in equity securities. This approach would authorize a trustee to consider capital gain as part of the total return, enabling distributions to beneficiaries without being restricted by whether the returns are accounting income or value appreciation. A uniform act was proposed in 1972 to permit trustees to allocate both realized and unrealized capital appreciation to income for distribution purposes. [28] The uniform act is the law in 46 states and the District of Columbia. The UMIFA contains an impairment rule very similar to the "invasion test" contemplated by the corporation. Realized and unrealized gains are offset to determine if the historic dollar amount of contributions to principal will be impaired by a planned distribution. Sec. 2 UMIFA. However, the uniform act is not the law in Alaska. Aside from the difference between the **permanent fund** and an endowment trust, the uniform act differs from existing law by permitting distributions based on unrealized appreciation. State law charts a different course for the **permanent fund** by not allowing such a distribution. For that reason, it is not appropriate to apply the impairment rule of the uniform act. When the legislature expanded authority for investments to include equity securities, it added a definition of income. AS 37.13.140 provides in pertinent part:

> ***10** Net income of the **fund** shall be computed annually as of the last day of the fiscal year in accordance with generally accepted accounting principles, excluding any unrealized gains or losses.

(Emphasis added.) This hybrid definition of income is intended to "to allow the maximum use of disposable income." AS 37.13.020(3). By making clear that "gain" is to be an element of income, the definition of income was expanded to include capital appreciation, but it plainly prevented any distribution of unrealized gain. Section 140 does not explain the accounting treatment for unrealized gains and losses other than to provide that this form of appreciation or loss is to be excluded from the determination of income.

The limitation of income to that which is realized appears to be consistent with the text of both the constitution and statute. The constitution provides the income "shall be deposited in the general **fund**." Alaska Const., art. IX, sec. 15. The statute provides: "[I]ncome from the [**permanent**] **fund** shall be deposited by the corporation into the [earnings reserve] account as soon as it is received." AS 37.13.145(a). When interpreting these words, a court will attempt to discover the plain meaning and purpose of the provision.

Because of our concern for interpreting the constitution as the people ratified it, we generally are reluctant to construe abstrusely any constitutional term that has a plain ordinary meaning. Rather, absent some signs that the term at issue has acquired a peculiar meaning by statutory definition or judicial construction, we defer to the meaning the people themselves probably placed on the provision. Normally, such deference to the intent of the people requires "[a]dherence to the common understanding of words." [29]

The words "deposit" and "received" convey a meaning that income is to be in hand, or realized. [30] By applying these common meanings there is no conflict between sections 140, 145, and the **permanent fund** amendment.

Section 140 defines income with reference to generally accepted accounting standards. Before 1997, these standards did not include unrealized gain or loss in the determination of income. These unrealized values were permitted to be reported in notes at the foot of an agency's financial statements. After 1997, accounting principles changed to require the depiction of investment income as the net increase or decrease in fair value. Fair value is what a willing buyer would pay for the security in an arm's length transaction and necessarily includes unrealized gain or loss on the valuation date of a security held in the corporation's portfolio. Para. 22, GASB 31. This change reflected a concern that the disclosure of fair value in the notes may not have allowed financial statement users to be sufficiently aware of the potential effect of investment gains and losses. Appendix A to GASB 31. Even though GASB 31 requires fair value reporting, the National Council on Governmental Accounting recognized that state law requiring other methods for the computation of income governs when there is a conflict. [31] The restrictive definition of income set out in AS 37.13.140 embodies a policy instituted by the legislature to allow distributions to be made from the appreciated value of investments in equity securities. However, the legislature permitted appreciation to be considered income only if it is realized. Unrealized capital appreciation is not expressly allocated to either principal or income by section 140. As recounted in our discussion of the accounting practices set out above, realized appreciation was allocated to the principal of the **permanent fund** until the corporation was authorized to invest in equity securities. It is unclear whether unrealized appreciation was allocated at all, but we presume it would have been allocated to principal as well. We find no evidence that the legislature intended to alter the traditional allocation rules as to unrealized gain or loss. Therefore, we decline to attribute a legislative intent to allocate unrealized appreciation to income for any purpose, including the use of unrealized losses to determine whether there has been an invasion of principal. We believe that this policy is not authorized and could possibly upset the balance in the accounting for principal and income. The better interpretation is to give a consistent meaning to the exclusion of unrealized appreciation or loss in section 140 and account for such gains and losses as an element of principal where it has traditionally been allocated.

***11** In our opinion, authority to invest in equity securities does not imply that unrealized gain or loss becomes an element of income for any purpose. The legislature can establish allocation rules for common trusts under its plenary law-making powers. *See Bogert on Trusts and Trustees*, sec. 816 (2nd ed. rev.) (but the best criterion for making [allocation] decisions is the practical treatment of the topic by the courts or the legislature.) We believe that the legislature established such a criterion when it enacted section 140.

Under article IX, section 15 of the Alaska Constitution and the relevant implementing statutes, there is no basis for expanding the concept of principal by creating a notational number that serves as a limitation on the deposit of income for distribution purposes. Once dedicated or appropriated, the principal in the **permanent fund** is used only for income producing investments the value of which rise and fall in corporation financial statements as unrealized gains and losses dictate. Only through a constitutional amendment, like that currently proposed by the corporation trustees establishing a payout limit of 5 percent of the total **fund** value, can the rate of dedication be increased and the deposit of income available for distribution be limited. Absent such an amendment, the full amount of income, made up of the realized gains and losses, is available for expenditure. It is up to the legislature, as it has done in the past, to appropriate excess **permanent fund** income to principal. [32] A corporate practice cannot operate to prevent the legislature from exercising discretion over the disposition of income.

Finally, we anticipate some will claim that our reading of the constitution and statutes serves to permit a silent invasion of principal when the **permanent fund** is carrying a large unrealized loss on its books. Realized income does not lose its character as income even if it were offset by unrealized capital losses. There simply is no basis in the history of the amendment or the enabling statutes for a liberal interpretation that would expand the scope of the dedicated **fund** by foreclosing expenditure of traditional accounting or statutorily defined income. To do so would do violence to the plain meaning of the constitution and section 140 which require that income be determined by realized gains and losses and be available for expenditure.

The constitutionally required dedication of principal is more than satisfied by the prudent investing practices of the corporation in statutorily approved investments and the generous inflation-proofing and contributions to principal appropriated by the legislature. We decline to read into either the constitution or the statutes a broader exception to the general prohibition on dedicated **funds** than can be justified by the plain meaning of article IX, section 15 of the Alaska Constitution and relevant implementing statutory provisions and the history leading to the adoption or enactment of these provisions.

Sincerely,

***12** Gregg D. Renkes
Attorney General

Footnotes

1 "GASB 31" is shorthand for Statement No. 31 of the Governmental Accounting Standards Board, Accounting and Financial Reporting for Certain Investments and for External Investment Pools.

2 Section 15, article IX of the Alaska Constitution provides:
Section 15. Alaska **Permanent Fund**. At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a **permanent fund**, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for **permanent fund** investments. All income from the **permanent fund** shall be deposited in the general **fund** unless otherwise provided by law.

3 Since it is clear under both AS 37.13.145 and the appropriations for **permanent** funddividends and inflation-proofing that **funding** of the PFD appropriation has priority and must be fully paid before any amount is transferred for inflation-proofing, you did not request our advice on whether or how those two transfers should be prioritized or allocated.

4 The ballot summary read as follows:
This proposal would amend Article IX, Section 7 (Dedicated **Funds**) and add a new section to Article IX, Section 15 (Alaska **Permanent Fund**) of the Alaska Constitution. It would establish a constitutional **permanent fund** into which at least 25 percent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payment and bonuses received by the State would be paid. The principal of the **fund** would be used only for income producing investments permitted by law. The income from the **fund** would be deposited in the State's General **Fund** and be available for appropriation for the State unless law provided otherwise. 1976 Ballot Proposition No. 2.

5 The resolution was introduced in January, 1976 as a sponsor substitute for the initial version of HJR 39, introduced by the governor the previous June, which had only proposed amending the dedicated **funds** provision of article IX, section 7 of the Alaska Constitution to permit the dedication of the proceeds of mineral lease bonuses. The sponsor substitute proposed adding a new section 15 to article IX to create a **permanent fund** by dedicating 10 percent of nonrenewable resource revenue. The resolution substituted by the governor also expressly provided that the legislature could make additional contributions to the **fund**. 1976 House J. at 39-40.

6 Joint Chairmen's Report on CS SSHJR 39, 1976 House J. at 684.

7 1976 House and Senate J. Supp. (fiscal note comments dated January 12, 1976).

8 Anchorage Daily News editorial, October 26, 1976 ("a percentage of the **fund** would go for direct use by Alaskans - for loans to businessmen, fishermen and builders.") The **permanent fund** was described as a "tool whereby Alaska can take some of today's mineral wealth and prepare for the future by investing in the development of human and material resources that will remain productive for many generations ...." *Quoting* Revenue Commissioner Sterling Gallagher.

9 Anchorage Times, October 24, 1976 ("Lawmakers Would Shape **Permanent Fund**").

10 Anchorage Times, October 14, 1976 ("Panel Mulls **Permanent Fund**").

11 Anchorage Times, October 27, 1976 ("Governor's Point of View").

12 Anchorage Daily News, October 24, 1976 (editorial, "Its **Permanent**").

13 Anchorage Times, October 24, 1976 (editorial, "No Easy Choice").

14 1977 Inf. Op. Att'y Gen. (Aug. 31; 663-78-0106).

15 *See also* 1986 Inf. Op. Att'y Gen. (Mar. 6; no file number); 1987 Inf. Op. Att'y Gen. (Feb. 12; 663-87-0356).

16 1977 Inf. Op. Att'y Gen. (Sept. 16; 663-78-0107).

17 These contributions have included one-time legislative appropriations to the **permanent fund** of both income and general **fund** revenues and the annual inflation-proofing amounts, as well as the natural resource revenues dedicated under the constitutional provision.

18 The corporation was given authority to place **funds** in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments, and federally guaranteed loans. The **fund** was directed to give preference to Alaska investments as long as they met the standards of quality set out in law. Specifically, deposits could be made in Alaska banks, mutual savings banks, savings and loan associations, and credit unions. Residential real estate (owner occupied single family dwellings, duplexes, and condominiums) could also be purchased if the mortgage was privately insured by a company doing business in Alaska.

19 This legislation was accompanied by a free conference committee report in which the joint committee chairmen explained "[t]he **fund** is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second." 1980 Senate J. at 671. It was intended that the **fund** would be held to a more restrictive list of investments than other fiduciary trusts.

20 The authorized list of investments has since been expanded at least four more times by the legislature: in 1989 to include investments in non-U.S. securities; in 1992 to include A-rated corporate bonds; in 1994 to expand permissible real estate investments; and in 1999 to make a variety of adjustments to the authorized list, to authorize up to 5% of the **fund** to be invested in other prudent investments not specifically included in the list, and to increase the allocation limit placed on equity investments.

21 According to annual financial statements of the **permanent fund**, realized gain was credited to principal for fiscal years 1980 and 1981. When the **permanent fund** was under Department of Revenue management, income was deposited in the general **fund**. After the corporation was created, statutes called for income to be deposited in an undistributed income account.

22 There were actually some minor differences in determining "net income" between the methods called for by GAAP pre-GASB 31 and by AS 37.13.140, but those differences did not affect the underlying requirement of each that only *realized* gains and losses be taken into account. The drafters of sec. 140 were aware of the potential that GAAP and state law might some day be inconsistent. In his transmittal letter, Governor Hammond made clear his intent that the statutory method for computing income should prevail over generally accepted accounting principles. Letter from Gov. Jay Hammond, regarding Sponsor Substitute for Senate Bill 684, 1982 Senate J. at 494, 496 (March 9, 1982).

23 We have located no case law in Alaska applying trust principles relevant to the questions presented.

24 1980 Senate J. at 671 (Senate and House J. Supp. No. 7).

25 In *Hickel v. Cowper*, 874 P.2d 922 (Alaska 1995), the Alaska Supreme Court declared that matters of constitutional construction are reviewed *de novo*. The court will determine what the constitution actually means and will approach this task as a question of law which requires the exercise of independent judgment. 874 P.2d at 926.

26 *See* discussion of legislative history set out in 1994 Inf. Op. Att'y Gen. (Sept. 23; 663-94- 0207).

27 1984 House and Senate J. Supp. No. 21; *see also* AS 13.18.020(b) and 13.38.050.

28 Uniform Management of Institutional **Funds** Act, 7A U.L.A. 316 (West Supp. 1997) (UFIMA).

29 *Citizens Coalition for Tort Reform, Inc. v.McAlpine*, 810 P.2d 162, 169 (Alaska 1991) (citations omitted).

30 "Deposit" means to "place, cache, or entrust", while "receive" means to "take possession or delivery." Webster's Third International Dictionary.

31 "Conflicts between legal provisions and GAAP do not require maintaining two accounting systems. Rather, the accounting system may be maintained on a legal-compliance basis, but should include sufficient additional records to permit GAAP based reporting." Para. 13, National Council on Governmental Accounting Statement No. 1 (Governmental Accounting and Financial Reporting Principles, issued March 1979).

32 As of June 30, 2002 the **permanent fund** recorded net assets totaling $23.5 billion. Of that total, $21.8 billion was principal. Since 1982, $7.5 billion of **permanent fund** income has been added to principal for inflation-proofing, through June 30, 2002. In addition to the constitutionally and statutorily mandated dedicated revenues, the legislature has made special appropriations to the **permanent fund** totaling $6.9 billion. The amount and sources of these appropriations are set out below:

Permanent Fund

Special Appropriations

(amounts in millions)

Year	Amount	Source
FY 81-85	$2,700	Surplus Oil Revenues
FY87	1,264	Earnings Reserve Account
FY96	1,842	Earnings Reserve Account
FY97	803	Earnings Reserve Account
FY00	250	Earnings Reserve Account

In FY 03 the legislature appropriated and additional amount to principal which could not be determined as of the date of this opinion.

2003 WL 25875053 (Alaska A.G.)

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2009 WL 1719849 (Alaska A.G.)

Office of the Attorney General

State of Alaska
A.G. File no: JU2009-200-509
June 16, 2009

Re: Review of 2003 Attorney General Opinion

***1** Steve Frank
Chair
Board of Trustees
Alaska **Permanent Fund** Corporation
P.O. Box 110410
Juneau, Alaska 99811-0410

Dear Mr. Frank:
In 2003, the Board of Trustees of the **permanent fund** requested Law to answer the following three sets of questions relating to accounting for principal and income of the Alaska **permanent fund**:
1. Is the corporation's policy that only the realized income of the **permanent fund** is available for expenditure from the **permanent fund** under AS 37.13.145 correct? If not, how should this amount be determined?

2. Is the corporation's practice that both realized and unrealized income of the **permanent fund** should be taken into account in determining the amount that is available for appropriation, *i.e.*, distribution under AS 37.13.140, correct? If not, how should the amount available for distribution from the **permanent fund** be determined? Should unrealized income of the **Fund** be excluded in determining the amount that is available for distribution?

3. Do the constitution and statutes require that income of the **fund** not be appropriated when doing so would bring the total value of the **permanent fund** including all unrealized gains and losses below the sum of the amounts deposited or appropriated to principal? If not, are there any other limitations with respect to the use of principal that are applicable in determining the amount that is available for expenditure or appropriation from the **permanent fund**?

You have asked us to review the responses we provided to these three questions. 2003 Op. Att'y Gen. (June 18) ("2003 Opinion"). Additionally you have asked for an opinion as to whether **permanent fund** dividends may be paid in 2009. Finally, you have asked for an opinion as to the appropriate accounting treatment of unrealized gains and losses on the investments of the earnings reserve account.

Here are the short answers to your five questions.

1. Only realized earnings are to be deposited in the earnings reserve account. The earnings reserve account should, however, retain the unrealized gains and losses attributable to the investments of the earnings reserve account. The entire balance of the earnings reserve account is subject to appropriation, and thus available for expenditure.

2. For purposes of computing the amount "available for distribution" under AS 37.13.140, the unrealized gains and losses of the **fund** should be excluded. The amount available for distribution under AS 37.13.140 is different than the amount constitutionally available for appropriation — which is the entire balance of the earnings reserve account.

3. Nothing in law prohibits an appropriation from the earnings reserve account, even if doing so would reduce the total value of the **permanent fund** to less than the amounts deposited or appropriated to the principal.

4. Nothing in law prohibits the payment of **permanent fund** dividends this year. A valid appropriation for 2009 **permanent fund** dividends has been enacted into law, **funds** are currently available for this appropriation in the earnings reserve account, and therefore these dividends can be paid.

***2** 5. The earnings reserve account is a government investment account established by AS 37.13.145(a) which will naturally have unrealized gains and losses on its investments. While AS 37.13.145 does not expressly address how to account for the unrealized gains and losses on the investments of the earnings reserve account, AS 37.13.170 requires the Corporation to include in its annual report "an appraisal at market value" of the investments of the **fund**. We think AS 37.13.170 reasonably contemplates that the Corporation should report on the market value of the investments of the principal as well as the market value of the investments of the earnings reserve account. Thus, the unrealized gains and losses attributable to the earnings reserve account should be accounted for in the earnings reserve account.

The questions you have asked are prompted by two developments.

First, as discussed in our 2003 Opinion, in 1997 the Governmental Accounting Standards Board adopted a new standard for reporting income. This new accounting standard, GASB Statement No. 31 ("GASB 31"), required that investment income include changes in the fair value of investments of government entities. GASB 31 defines fair value to mean "the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale." For publicly traded securities, fair value is the same as market value. Thus, GASB 31 raised the question as to whether the net income of the **permanent fund** calculated under AS 37.13.140 should include the unrealized gains and losses that accrue on investments. We observed in our 2003 Opinion that this accounting change had been anticipated when the legislature repealed and reenacted AS 37.13.140 in 1982, and that the legislature intended to exclude unrealized gains and losses from the calculation of statutory net income. 2003 Opinion at 14 n.22, 23-26.

Second, because of unrealized investment losses incurred during FY 2009, the fair value of the principal of the **permanent fund** has been "underwater," in other words, the fair value has declined below the original dollar value of the amounts deposited to or appropriated to principal. As a consequence, some observers have suggested that 2009 **permanent fund** dividends should not be paid.

As discussed more fully in this opinion, neither accounting changes nor investment losses can change a fundamental fact about the **permanent fund**: the earnings reserve account is subject to the constitutional prohibition against dedicated **funds**. Therefore, if there are **funds** in the earnings reserve account, and those **funds** have been appropriately deposited in that account, they can be appropriated for any public purpose, including the payment of **permanent fund** dividends. Accordingly, we re-affirm our conclusions from the 2003 Opinion.

Because the answers to these questions turn in large part upon the extent to which the constitutional prohibition against dedicated **funds** applies to the **permanent fund**, we begin with a background discussion of that prohibition. Next, we show how the legislature may always appropriate **funds** from the earnings reserve account by analyzing the following issues: (a) how the constitutional prohibition against dedicated **funds** applies to the **permanent fund**; (b) whether the framers and voters expressed an intent to not permit the expenditure of income when the value of the **permanent fund** is underwater; and (c) whether the modern law of endowments permits the expenditure of income when the value of an endowment **fund** is underwater. Finally, we consider the issue of the appropriate accounting treatment of the unrealized gains and losses on the investments of the earnings reserve account.

I. Background: The Constitutional Prohibition Against The Dedication Of Funds

***3** Generally speaking, a dedication of **funds** occurs when the legislature sets aside the proceeds of a certain state revenue source for a special purpose. 1975 Op. Att'y Gen. No. 9 at 24 (May 2); 1982 Op. Att'y Gen. No. 13 at 8 (Nov. 30). [1] The framers of the Alaska Constitution referred to this concept as "earmarking" and considered it a serious problem. *See, e.g.*, 6 Proceedings of the Alaska Constitutional Convention ("P.A.C.C") 111 (Commentary on the Article on Finance and Taxation); 3 P.A.C.C. 2364, 2368. Accordingly, the framers decided to prohibit this practice, with certain exceptions. The Alaska Constitution provides:

> The proceeds of any state tax or license shall not be dedicated to any special purpose, except as provided in Section 15 of this article [2] or when required by the federal government for state participation in federal programs. This provision shall not prohibit the continuance of any dedication for special purposes existing upon the date of ratification of this section by the people of Alaska.

Alaska Const, art. IX, § 7. Alaska is one of two states that prohibits the dedication of revenue for a particular purpose. [3]

The Alaska Supreme Court has frequently observed that the framers of the Alaska Constitution adopted this prohibition for two reasons: (1) to ensure the legislature has flexibility in exercising its power of appropriation, and (2) to ensure that the legislature does not abdicate its responsibility for budgeting. *State v. Alex*, 646 P.2d 203, 209 (Alaska 1982); *Fairbanks v. Convention & Visitors Bureau*, 818 P.2d 1153, 1158 (Alaska 1991); *Sonneman v. Hickel*, 836 P.2d 936, 938-39 (Alaska 1992); *Southeast Alaska Conservation Council v. State*, 202 P.3d 1162, 1169 (Alaska 2009) ("*SEACC*"). The prohibition protects each legislature's power of appropriation from encroachment by a prior legislature. *See, e.g.*, *Sonneman*, 836 P.2d at 940 ("The constitutional clause prohibiting dedicated **funds** seeks to preserve an annual appropriation model which assumes that ... the legislature remain[s] free to appropriate all **funds** for any purpose on an annual basis.").

Because of the framers' intent, the Alaska Supreme Court has held that "the prohibition is meant to apply broadly." *SEACC*, 202 P.3d at 1170. The Court has interpreted the language "proceeds of state tax or license" broadly so as to include not only taxes and licenses, but almost all public revenues including salmon royalty assessments (*Alex*), [4] litigation settlement revenue (*Myers*), [5] and the proceeds of sales of state lands (*SEACC*). [6] The Court, however, has not been offended by accounting structures, such as a general **fund** subaccount, that are merely intended to track the revenues and expenses of a particular state agency, so long as there is no restriction on the legislature's ability to appropriate money attributed to the subaccount for any public purpose, and no restriction on the executive branch's ability to request an appropriation from the subaccount. *Sonneman*, 836 P.2d at 939-40. [7]

***4** Finally, the Court has recently suggested, without directly so holding, that there is "sufficient doubt as to the constitutionality" of a statutory dedication of income generated by the investments of assets in a state account. *SEACC*, 202 P.3d at 1175. In casting doubt, the Court relied upon an opinion from this office in which we opined that investment income from state accounts is probably subject to the prohibition against dedicated **funds**, and that such investment income should be annually appropriated to the state account that generated the income. 1982 Op. Att'y Gen. No. 13 at 18 (Nov. 30). [8]

II. Analysis: The Legislature May Always Appropriate Funds from the Earnings Reserve Account

In this section, we show why the legislature may always appropriate **funds** from earnings reserve account. To show this, we analyze three issues: (a) how the constitutional prohibition against dedicated **funds** applies to the **permanent fund**; (b) whether the framers and voters expressed an intent to not permit the expenditure of income when the value of the **permanent fund** is underwater; and (c) whether the modern law of endowments permits the expenditure of income when the value of an endowment **fund** is underwater.

As noted above, the answers to your questions turn in large part upon the extent to which the constitutional prohibition against dedicated **funds** applies to the **permanent fund**. In particular, as discussed below, the corpus of the earnings reserve account is subject to the prohibition, and therefore always subject to appropriation.

A. **How the Constitutional Prohibition Against Dedicated Funds Applies to the Permanent Fund**

Created by amendment to the Alaska Constitution in 1976, the **permanent fund** is a state **fund** into which certain mineral proceeds are placed for purposes of investment. Alaska Const, art. IX, § 15.[9] Like many trust or endowment **funds**, the accounting framework of the **permanent fund** is a variation on the "principal and income" model.

The accounting framework of the **permanent fund** has a number of unique elements, some of which are established by constitution (the mineral revenue earmark, restricted principal, and alternative income use authorization), and others by statute (earnings reserve account, **permanent fund** income dedication, **permanent fund** dividend transfer, and inflation-proofing transfer). We analyze here how the constitutional prohibition against dedicated **funds** applies to the accounting elements of the **permanent fund**.

1. The Constitutional Framework of the Permanent Fund

Article IX, § 15 of the Alaska Constitution establishes three elements of the accounting framework of the **permanent fund**: the mineral revenue earmark, the restricted principal, and the alternative income use authorization. The first two of these elements must be established in the Alaska Constitution, otherwise they would be void, and in the case of the alternative income use authorization—probably void if used to dedicate income, under the constitutional prohibition against dedicated **funds**.[10]

i. Mineral Revenue Earmark

***5** The first accounting element of the **permanent fund** is the mineral revenue earmark. "At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a **permanent fund** ...." Alaska Const, art. IX, § 15. As seen above, revenue earmarks are impermissible under the constitutional prohibition against dedicated **funds**. *Alex*, 646 P.2d at 207-210. Thus, establishing the mineral revenue earmark in the Alaska Constitution is necessary in order to ensure its validity.

ii. Restricted Principal

The next accounting element of the **permanent fund** is the restricted principal. The proceeds from the mineral revenue earmark are placed in the **permanent fund**, "the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for **permanent fund** investments." Alaska Const, art. IX, § 15. Because the principal may only be used for income-producing investments, it is not subject to legislative appropriation.[11] As discussed above, placing **funds** in a separate state account is permissible, but only if the legislature retains its power of appropriation. *Sonneman*, 836 P.2d at 939-40. Thus, to restrict an account from appropriation, as this clause does, the restriction must be set forth in the constitution.

iii. Alternative Income Use Authorization

The final accounting element in the constitution is the authorization for an alternative use of **permanent fund** income: "All income from the **permanent fund** shall be deposited in the general **fund** *unless otherwise provided by law*." Alaska Const, art. IX, § 15 (emphasis added). As noted above, the Alaska Supreme Court has expressed doubts as to whether the prohibition against dedicated **funds** would permit the retention of income in a statutory **fund**. *SEACC*, 202 P.3d at 1175. Accordingly, to the extent that this language is intended to authorize a statutory dedication of **permanent fund** income, its placement in the constitution is probably required in order for the dedication to survive scrutiny under the prohibition against dedicated **funds**.

Review of the legislative history of HJR 39 reveals that the framers of the **permanent fund** intended the language "unless otherwise provided by law" to maximize the legislature's flexibility with respect to use of the **fund's** income, including the pledging of **permanent fund** income. In January 1976, Governor Hammond introduced a sponsor substitute for HJR 39. SSHJR 39, 9th Legislature (1976). This version of the resolution simply provided that "[a]ll income from the **permanent fund** shall be deposited in the general **fund**." *Id.* At the first hearing on HJR 39, the House Finance Committee discussed whether this language should be changed to permit a pledge of **permanent fund** income:
House Finance Chair Malone:

***6** What about the question of pledge or dedication of **fund** income for securities of the state? Would that be allowable under the language of the resolution as drawn?

Revenue Commissioner Gallagher:

The dedication of income?

Malone: Not the way it's drawn right now. It wouldn't be I guess.

Gallagher: As you have seen the Morgan report, they feel it would be, could be, a great enhancement to be able to dedicate that income to whatever purpose the legislature so feels. And I also, personally, feel it would be a great enhancement. It's one of the things I've gotta talk to the governor about. I would hope also a week or so to get back to you on that one.
Representative Cowper: You mean like a dedication of debt service?

Gallagher: To debt service or whatever purpose the legislature sees fit.

Hearing on HJR 39 Before the House Finance Comm., 9th Legislature (Feb. 21, 1976). [12] Later in the hearing, Jim Rhodes, staff to Chair Malone, reported as follows:
Rhodes: Mr. Chair, I discussed this matter with representatives of White Weld in New York who felt that if the phrase "unless otherwise directed by the legislature" appeared in the constitution that would be a sufficient legal peg so that income from the **permanent fund** could be pledged in the bond covenants for the security of state agencies or general obligation bonds or, they said, it could also permit the legislature to make a dividend payment to citizens of Alaska from the income of the **fund** .... and also if you put "unless otherwise directed" it would permit the **fund** to go into joint ventures with private corporations and pledge income from the **fund** as partial security of that debt. So it would give you maximum flexibility, they felt, by just adding the phrase "unless otherwise directed by the legislature" or words to that effect.

Hearing on HJR 39 Before the House Finance Comm., 9th Legislature (Feb. 21, 1976) (tape in State Archives Box 18461). At the next committee of referral, the House Judiciary Committee amended the last sentence of the joint resolution to read: "All income from the **permanent fund** shall be deposited in the general **fund** unless otherwise provided by law." CS SSHJR 39 (JUD). The joint report of the chairs of House Finance and House Judiciary stated, "[t]he purpose of the language in the last sentence of the resolution is to give future legislatures the maximum flexibility in using the **Fund's** earnings — ranging from adding to **Fund** principal to paying out a dividend to resident Alaskans" 1976 House J. 685 (Mar. 24). [13] The legislative thus suggests that the legislature intended the language "unless otherwise provided by law" to allow **permanent fund** income to be used in a variety of ways, including a pledge to pay debt service.

This office has been reluctant to endorse statutory dedications of **permanent fund** income for purposes outside of the **permanent fund** (*i.e.*, the principal or earnings reserve account). 1983 Inf. Op. Att'y Gen. (366-484-83; Mar. 10) (transfers of

funds to the permanent fund dividend fund should be made by appropriation). We have based our reluctance on the view that the voters were not advised in 1976 that the "unless otherwise provided by law" language could be used to create a "tremendous exception" to the prohibition against dedicated funds. *Id.* at 2. In any event, to the extent that this alternative income use language is intended to authorize a statutory dedication of permanent fund income, its placement in the constitution is probably required in order for the dedication to survive scrutiny under the prohibition against dedicated funds.

2. The Statutory Framework of the Permanent Fund

***7** The legislature has fleshed out the constitutional framework of the permanent fund by adding a number of statutory elements: the earnings reserve account, permanent fund income dedication, permanent fund dividend transfer, and inflation-proofing transfer. The extent to which the constitutional prohibition against dedicated funds applies to these elements varies.

i. The Earnings Reserve Account

The earnings reserve account is established by AS 37.13.145(a) as a separate account in the permanent fund. Income from the permanent fund must be deposited into the earnings reserve account "as soon as it is received." AS 37.13.145(a).

Nothing in law restricts the earnings reserve account from appropriation. In *Hickel v. Cowper*, 874 P.2d 922 (Alaska 1994), the Alaska Supreme Court held: "There are no statutory or constitutional prohibitions against direct appropriations from [the earnings reserve] account. The earnings reserve account is therefore available for appropriation." *Id.* at 934. Thus, the prohibition against dedicated funds applies to the balance in the earnings reserve account. Under *Hickel* and *Sonneman*, all funds in the earnings reserve account are subject to appropriation by the legislature. This office has held this view for at least 25 years. *See* 1984 Inf. Op. Art'y Gen. (366-405-84; Feb. 6) ("nothing in law prevents the unallocated part of the permanent fund income from being appropriated by the legislature").

ii. The Permanent Fund Income Dedication

By statute, "[i]ncome from the fund shall be deposited" into the earnings reserve account "as soon as it is received." AS 37.13.145(a). The income deposited into the earnings reserve account comes from two sources: (1) investments of the principal, and (2) investments of the earnings reserve account.

Since the balance in the earnings reserve account is subject to appropriation, the automatic deposit of income to the earnings reserve account is arguably not a dedication, since such income remains subject to the appropriation power of the legislature. *See* 1982 Op. Att'y Gen. No. 13 at 20 (Nov. 30). But we remain mindful that the objective of the prohibition against dedicated funds is to maintain legislative budgeting flexibility and control. As a practical matter, any deposit of funds into the earnings reserve account arguably decreases the legislature's flexibility and control over such funds because of the public and political pressure to use such funds only for permanent fund dividends or inflation-proofing. Accordingly, a court may conclude that in this context the deposit of investment income into the earnings reserve account is for all practical purposes a dedication.

The dedication, however, is authorized by the Alaska Constitution: "[a]ll income from the permanent fund shall be deposited in the general fund unless otherwise provided by law." Alaska Const, art. IX, § 15; Alaska Const, art. IX, § 7 (allowing dedications "as provided in section 15"). Alaska Statute 37.13.145(a) implements this provision by requiring permanent fund investment income to be automatically deposited in the earnings reserve account.

***8** The AS 37.13.145(a) dedication of income from investments of the permanent fund's principal and earnings reserve account to the earnings reserve account has been in place since 1982. [14] In our opinion, the doubts recently expressed by the Alaska Supreme Court in *SEACC* regarding the statutory dedication of income from an investment fund are addressed by the constitutional language permitting the legislature to otherwise provide for the income from the permanent fund. We understand

that in reliance on this language, such income has always been automatically deposited to the earnings reserve account without an appropriation. We have approved of this practice since 1983. *See* 1983 Inf. Op. Att'y Gen. 3 (366-484-83; Mar. 10).

iii. The Permanent Fund Dividend Transfer

By statute, certain **funds** in the earnings reserve account are to be transferred to the **permanent fund** dividend **fund** at the end of each fiscal year. AS 37.13.145(b). The amount of the transfer is 50 percent of "*income available for distribution* under AS 37.13.140." *Id.* "Income available for distribution" is defined in AS 37.13.140 as "21 percent of the *net income of the **fund*** for the last five fiscal years, including the fiscal year just ended, but may not exceed *net income of the **fund*** for the fiscal year just ended plus the balance in the earnings reserve account described in AS 37.13.145." "Net income of the **fund**" includes "income of the earnings reserve account" and "shall be computed annually as of the last day of the fiscal year in accordance with generally accepted accounting principles, excluding any unrealized gains or losses." AS 37.13.140.

While the Alaska Supreme Court has apparently assumed that the **permanent fund** dividend transfer is made automatically without an appropriation, [15] this is incorrect. These **funds** have been annually appropriated from the earnings reserve account to the **permanent fund** dividend **fund** since our opinion in 1983 advising that such transfers should be made by appropriation. 1983 Inf. Op. Att'y Gen. (366-484-83; Mar. 10). We expressed the view that the best way to harmonize the "unless otherwise provided by law" language in article IX, section 15 with the constitutional prohibition against dedicated **funds** "is that the legislature may provide by law for the income to remain in the **permanent fund** (either through reinvestment as principal or retention in an undistributed income account) without appropriation, but may not transfer income to another **fund** or authorize it to be spent without an appropriation." *Id.* at 3.

iv. The Inflation-Proofing Transfer

Finally, AS 37.13.145(c) provides for a transfer of **funds** from the earnings reserve account to principal in the amount necessary to offset the effect of inflation on principal. While our 1983 opinion would permit such an automatic transfer pursuant to this statute, the practice since fiscal year 1991 has been to appropriate amounts for inflation-proofing from the earnings reserve account to principal. *See* sec. 13, ch. 209, SLA 1990.

* * * *

***9** In sum, the **permanent fund** is only partly exempt from the application of the prohibition against dedicated **funds**. In particular, the corpus of the earnings reserve account is not exempt. Thus, any **funds** in the earnings reserve account are fully subject to appropriation by the legislature.

We next consider the issue of what, if anything, the framers and the voters intended with respect to spending from earnings of the **permanent fund** when the value of the **permanent fund** is underwater.

B. The Framers and Voters Did Not Express an Intent to Limit Spending When the Value of the Permanent Fund Is Underwater

The legislature has found that "the [**permanent**] **fund** should be used as a savings device managed to allow the maximum use of disposable income from the **fund** for purposes designated by law." AS 37.13.020(3). For most of the history of the **permanent fund**, there has not been a conflict between these goals of saving and spending. As a consequence of positive investment returns, the **permanent fund** has been able to preserve the "purchasing power" [16] of the deposits of the earmarked mineral revenues and the additional appropriations, and still have money left over to **fund** a healthy **permanent fund** dividend program.

For much of FY 2009, however, the fair value of the **permanent fund** principal has been underwater. Thus, the expressed goals of savings and spending are in seeming conflict. We characterize this as a "seeming conflict" because as set forth above,

the amounts in the earnings reserve account are constitutionally subject to appropriation regardless of whether the fair value balance of the principal is underwater. Unless otherwise required by the Alaska Constitution, legislative goals or statutes must give way to the constitutional prohibition against dedicated **funds**.

Accordingly, we must examine whether there is any constitutional requirement that the principal retain income and stop further deposits into the earnings reserve account until such time as the fair value of the principal is restored to a level above original dollar value. There is no such requirement in the plain text of the Alaska Constitution. As discussed above, the text of article IX, § 15 is limited to establishing the revenue earmark, the restricted principal and the alternative income use authorization. The text of the constitution sets out no limitations or restrictions on the expenditure of income, nor does it require retention of income when the value of principal is underwater.

Thus, we turn to intent.

The framers' intent for the **permanent fund** is sometimes invoked in the ongoing public discussion regarding the extent to which the Alaska Constitution prohibits the payment of **permanent fund** dividends when the fair value of the **fund** is underwater. The intent of the framers is considered by the courts in determining the meaning of the Alaska Constitution. *Hickel*, 874 P.2d at 926. Additionally, the Court will consider the extrinsic evidence of the voter's understanding of a constitutional amendment's provisions. *Id.* at 929. [17] Accordingly, we review the framers' intent as well as the extrinsic evidence of the voter's understanding regarding the **permanent fund** amendment to the Alaska Constitution. [18]

***10** As set forth below, following review of the entire record of HJR 39, as well as the public record from 1976, we find no evidence that the framers or the voters expressed an intent for article IX, § 15 of the Alaska Constitution to require retention of income as principal when the fair value of principal is underwater. We start with the framers' intent.

1. Framers' Intent

From January to May 1976, the legislature debated Governor Hammond's proposal for a constitutional **permanent fund** and made a number of significant changes. During the course of these deliberations, a representative from the Hammond Administration (Department of Revenue Commissioner Sterling Gallagher), and the primary legislative proponents of HJR 39 (Representative Hugh Mai one and Representative Clark Gruening) described the intent and vision of the **permanent fund** proposal.

During the hearings, Representative Malone and Representative Gruening articulated a three-part vision for the **permanent fund**. The first objective was to save a portion of the state's non-renewable mineral income for the future. The second objective was to preserve the legislature's flexibility with respect to how the principal of the **permanent fund** was to be invested, and how the income was to be used. The third objective was to use the **permanent fund** to diversify the Alaska economy.

The first objective—savings—was accomplished simply by restricting the use of principal to income-producing investments. As discussed above, this meant that the principal could not be appropriated. Representative Gruening testified: “none of that principal could be used under the ... governor's concept for operating expenses.” Hearing on HJR 39 Before the House Judiciary Comm., 9th Legislature (Mar. 15, 1976) (tape in State Archives Box 18287).

The second objective—flexibility—was accomplished by not specifying the types of investments (beyond “income-producing”) or how the income was to be used. The flexibility objective was reiterated multiple times. [19]

The third objective—diversification of Alaska's economy—was repeatedly emphasized by Representatives Malone and Gruening both during the legislative hearings and in their comments in the media. *See* Appendix A (collected statements). Representative Malone in particular envisioned that the **fund** would be used to make business loans to all Alaskans. *Id.* [20] Of

course, this particular objective was necessarily subsidiary to the flexibility objective and depended on the manner in which future legislatures would chart the course of the **permanent fund**.

* * * *

Representative Malone summarized the framers' three-part vision in his statement to the House Judiciary Committee:
I'd like to make a couple of general statements .... We're talking about preserving a percentage or portion of income or wealth that is not renewable. That's the main item in the legislation—is that this sort of income we're talking about here and these benefits the state derives, the mineral sources are not, in so far as we know, renewable and that's one thing that makes this **permanent fund** different from a lot of other **permanent funds** that exist in other places. That's one thing.

***11** The other thing that makes this sort of **permanent fund** different from **permanent funds** that exist in other laws and maybe other constitutions, state constitutions, is that the income from the **fund** as well as the principal of the **fund** is not limited to specific uses—to certain uses ... it's not limited at all in the constitutional amendment. The income would go to the state's general **fund** or as otherwise provided by law which could also be changed whatever the provision is there or might be adopted by law. So we're not talking about a **permanent fund** like some places have set up, you set up a **fund**, taking the income from a specific source and then turning around and using it for a specific purpose that locks the state into something that maybe is completely inflexible. The income could be used wherever the legislature thought it needed to be used or where the governor though it needed to be used or if it goes someplace else. Same thing on the investments. Really the idea of putting in "which shall be established by law" [with respect to income-producing investments] is to provide for public debate and participation in what the investment program is going to be.

I think that the idea is to as much as possible, so far as the Alaska economy can provide good and reasonable investments within the state, that's where we would want to invest the money at least finally if not initially, and that that's something that's sort of the case where you can have your cake and eat it too. You can put the money out in sound investment programs, some of which could be loan programs that benefit the people of the state in the form of capital and the same time derive an income from. And when those loans are returned new loans will be made. So it's the situation where the wealth stays basically in the state, stays at work in the state, and continues to provide both direct and indirect benefits to the people.

It's not like other **permanent funds** that people might be used to compare this one with limited to the very narrow area ... this is something very broad.

Hearing on HJR 39 Before the House Judiciary Comm., 9 Legislature (Mar. 15, 1976) (tape in State Archives Box 18287).

In sum, the legislative record demonstrates an express intention to (1) preserve principal for the future, (2) preserve legislative flexibility for how the **fund** is to be invested and the income spent, and (3) subject to future legislative authorization, preserve the option for investing the **fund** for the purposes of in-state economic development. But there is nothing in the legislative record that expresses an intent that expenditure of income must be restricted, or income retained, when the value of the principal is underwater.

2. Voters' Intent

Following the passage of HJR 39 by the legislature on May 31, 1976, the discussion regarding the **permanent fund** shifted to the public. In our 2003 Opinion we identified a number of statements made during the public discussion of HJR 39 prior to the vote of the people in November 1976. 2003 Opinion at 6-8.

***12** Review of the public materials from the June — November 1976 time period demonstrates that the three-part vision articulated by the framers (savings, flexibility and economic development) was effectively communicated to the voters prior to the November election. *See* Appendix B.

As noted above, in older cases the Alaska Supreme Court has expressed concerns about the difficulties inherent in discerning voter intent. *Starr v. Haglund*, 374 P.2d at 319, 321. In the case of the **permanent fund**, however, discerning voter intent is made easier by the fact that a number of surveys were conducted immediately following the 1976 election. These surveys reflect that the voters understood and agreed with the vision articulated by the framers.

In early 1977, Governor Hammond commissioned a statewide policy issue survey. Some of the questions pertained to the use of the **permanent fund**. The survey found that "[w]ith the exception of a few percent who would either save the money outright [5%], or reduce present taxation with it [5.3%], the public is thinking about ways of investing the money wisely in Alaska, and almost always the idea sounds a lot like most of the capital improvement concepts emerging from the government itself." Rowan Group, Citizen Feedback No. 2—A Survey of Alaskan Citizens on the Major Policy Questions of the Day 11 (July 1977). The survey also found that 72 percent of the participants agreed with the following statement: "The **permanent fund** should be managed to assist Alaska directly through low-interest loans for such things as community development, fisheries enhancement, and so on." *Id.* at 12. The survey found no consensus on the use of **permanent fund** earnings, and concluded that "*[t]he public has not yet made up its mind about what the **permanent fund** is*; only that it should exist. The purposes of the **fund**, the purposes of the earnings, and the relationship of the size of the **fund** to the size of the operating budget, are unsettled points." *Id.* at 15 (emphasis in original).

The Alaska Public Forum conducted statewide policy issue surveys in 1977 and 1978. These surveys also included questions about the **permanent fund**. The results were similar to the Rowan Group survey. In 1977, the survey showed that 36 percent of participants wanted to use the **permanent fund** for loans for renewable resources, and 26 percent wanted to "save it." The Alaska Public Forum, Year End Report 10 (1977). In 1978, the survey showed that 79 percent wanted to use the **permanent fund** to promote renewable resource industries. The Alaska Public Forum, Year End Report 36 (1978). "The support for these industries was so strong that 68 percent of Forum respondents this year were willing to sacrifice a substantial return on **Permanent Fund** investments in order to promote renewable resource industries, which are considered a risky investment." *Id.* at 37.

3. Summary

***13** There is no question that the record from 1976 demonstrates that the intention of the framers and the voters was to save a portion of mineral revenue for the future. Moreover, the framers repeatedly expressed their desire that the **permanent fund** would be invested in diversifying the Alaska economy. But of the three-part vision set forth above, the dominant objective appears to be preservation of legislative flexibility. Under the flexibility objective, the framers and the voters expressed the intent that the legislature would decide how to invest the principal of the **permanent fund** and how to use the income. [21]

The record from 1976 reflects a considerable spectrum of views as to how the **permanent fund** would be invested and how the income would be spent. One proposal was to pledge **permanent fund** income to secure state bonds. Hearing on HJR 39 Before the House Finance Comm., 9th Legislature (Feb. 21, 1976) (tape in State Archives Box 18460). Such a pledge would be required to be paid from income even if the value of the principal were to decline. Another proposal was to invest the principal in huge infrastructure assets the value of which depreciate over time — such as hydroelectric dams. Yet at the same time, the framers envisioned that the income from such investments would continue to be available for expenditure by the legislature. Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (tape in State Archives Box 18290). In yet another proposal, the **permanent fund** would be invested in potentially risky in-state economic development investments —but there is no suggestion that the income from the **permanent fund** could not be spent if such investments were to lose value. Debate on HJR 39 on the House Floor, 9th Legislature (Mar. 25, 1976) (tape in State Archives Box 18385).

It is difficult to overstate the framers' radical vision for the **permanent fund**, particularly when it was conveyed to the public on the front page of the Anchorage Daily News: "People always talk about return on the dollar. The priorities always get based on the value of money. Well, I don't think that should be the main concern for this investment program. ... I don't think the managers—and that's what the legislature will be—should just look at return in dollars; we have to talk about the quality of life in Alaska." Howard Weaver, ***Permanent Fund*** *is Biggest Project*, Anchorage Daily News, June 2, 1976, at 1. Given the nature of framers' vision, the notion that income should be retained when the value of principal is underwater is a concept that was arguably foreign to the framers.

Taking into consideration the plain text of the Alaska Constitution, the tenor of the framers' testimony and comments to the media, the three-part vision for the **permanent fund** that was presented to and understood by the voters, the answer to the question whether the framers and the voters expressed an intent for the Alaska Constitution to require the retention of income in the principal of the **permanent fund** is underwater is evident. They did not. [22] Nothing in the record from 1976 would compel, or even suggest, that such an intent exists. [23]

***14** This result is consistent with the modern law of endowments as articulated by the Uniform Law Commission. We examine that law next.

C. The Law of Endowments Permits the Expenditure of Income from an Underwater Fund in Certain Situations

In this section we analyze whether the law of endowments would permit spending from an underwater **fund**. Such spending is permitted in certain situations. [24]

The origin of modern endowment law has been traced to *St. Joseph's Hosp. v. Bennett*, 22 N.E.2d 305 (N.Y. 1939), where the New York Court of Appeals defined an endowment to mean "the bestowment of money as a **permanent fund**, the income of which is to be used in the administration of a proposed work." *Id.* at 306. In 1969, the Ford Foundation commissioned a study on the developing law of endowments. The result was the seminal work by William Cary and Craig Bright, *The Law and the Lore of Endowment* ***Funds*** (1969). [25] This work in turn prompted the Uniform Law Commission in 1972 to draft the Uniform Management of Institutional **Funds** Act ("UMIFA"). [26] In 2006, the Uniform Law Commission recommended replacement of UMIFA with the Uniform Prudent Management of Institutional **Funds** Act (UPMIFA).

Alaska has not adopted either UMIFA or UPMIFA. [27] To the extent that UMIFA and UPMIFA embody the common law of endowments, or at least a principled understanding of what the law should be, we think courts in Alaska would at least consider modern endowment law in resolving legal issues related to the **permanent fund**. [28]

Cary and Bright discussed whether spending of income was permitted from an underwater endowment **fund**:

> Assume that the college realizes a net loss of $60,000 from the sale of securities, and that the balance in its reserve for gains and losses from the sale of securities is only $30,000. Must it retain $30,000 of income from dividends and interest to make up the deficit? We believe not, even if the market value of the endowment falls below the book value as adjusted for inflation. There is no authority under existing law and practice for the imposition of such a requirement, and we submit that it would be unwise and undesirable to include such a requirement ....

Cary & Bright, The Law and the Lore of Endowment **Funds** at 45. Imposing a requirement to make up a deficit could impair the flexibility of endowments. But Cary and Bright also thought a primary goal of endowments should be preservation of purchasing power. *Id.* at 46-47.

The Uniform Law Commission partially adopted the Cary and Bright view when it drafted UMIFA in 1972. The Uniform Law Commission distinguished, however, between appreciation (*i. e.*, realized and unrealized capital gains) and income (interest, dividends and rents). At that point in time, the law was in flux as to whether capital appreciation should be credited to principal, as opposed to income. The Uniform Law Commission adopted a hybrid approach. Under UMIFA, income as defined can always be spent, regardless of the value of principal. Appreciation, however, could only be spent when the fair value of the endowment exceeded the historic dollar value (*i.e.*, original dollar value), unless otherwise specified by the rules governing the endowment. *UMIFA*, § 2, 7 A U.L.A. 19-20 (2006).

***15** UMIFA commentators have repeatedly recognized an endowment's power to spend income, as defined by UMIFA, when the endowment is underwater. For instance, in the view of the New York Department of Law:
[T]he assets [of an endowment **fund**] must be invested, and the income — traditionally, interest, dividends, rents and royalties — is available for expenditure, even if the value of the principal drops below historic dollar value, whether because of specific investment losses or general decline in market values. [29]

Under New York law, however, appreciation cannot be appropriated when **fund** value is below historic dollar value, unless such appreciation was appropriated prior to the decline in value:
If the board properly appropriates net appreciation, the corporation may expend such appreciation even if at the time of expenditure endowment **fund** value drops below historic dollar value. However, like appropriation, such expenditure must be prudent under [New York UMIFA].

New York Dep't, Advice for Not-for-Profit Corporations on the Appropriation of Endowment **Fund** Appreciation (undated).

One commentator, however, has observed that appreciation can be spent from an underwater endowment **fund** if the donor has permitted it:

> [A] charity may *always* spend the **fund's** income — that is interest, dividends, and other classic forms of income such as rents and royalties — if three conditions are met: (a) if the gift instrument does not prohibit spending income when the **fund** is underwater, (b) if the **fund** is underwater due to asset depreciation rather than appropriations that dipped into historic dollar value, and (c) if the expenditure of the income meets the standard of prudence .... Capital gains in an underwater endowment **fund** are not considered income for this purpose, unless, again, the donor has stipulated otherwise.

John Sayre, *United States: Underwater Endowments: Understanding Your Options*, Patterson Belknap Webb & Tyler Client Advice Publication (Mar. 29, 2009) (emphasis in original).

In 2006, the Uniform Law Commission recommended that UMIFA be replaced with the Uniform Prudent Management of Institutional **Funds** Act (UPMIFA). The reason for the revision was the Commission's recognition that the prudence standards that governed the investment of institutional **funds** had evolved to govern all aspects of **fund** management, including expenditure of **fund** income. *UPMIFA*, Prefatory Note, 7A Pt. Ill U.L.A. 4 (2008).

One of the most significant changes advanced by UPMIFA was the elimination of the rule prohibiting expenditure of appreciation when **fund** value is less than historic dollar value. The Commission was concerned about the impact of this historic dollar value rule on investment strategy:

> A **fund** that [drops below historic dollar value] is commonly called an "underwater" **fund**. Conflicting advice regarding whether an organization could spend from an underwater **fund** has led to difficulties for those managing charities. If a charity concluded that it could continue to spend trust accounting income until a **fund** regained its historic dollar value, the charity might invest for income rather than on a total-return basis. Thus, the historic value dollar rule can cause inappropriate distortions in investment policy and can ultimately lead to a decline in a **fund's** real value. If, instead, a charity with an underwater **fund** continues to invest for growth, the charity may be unable to spend anything from an underwater endowment **fund** for several years. The inability of a charity to spend anything from an endowment is likely to be contrary to donor intent, which is to provide current benefits to the charity.

***16** *Id.* at 5. Thus, the Commission adopted a rule of prudent expenditure: "[s]ubject to the intent of a donor expressed in the gift instrument, an institution may appropriate for expenditure or accumulate so much of an endowment **fund** as the institution determines is prudent for the uses, benefits, purposes, and duration for which the endowment **fund** is established." *UPMIFA*, § 4, 7 A Pt. Ill U.L.A. 16-17 (2008). The rule then provides a number of factors to consider in determining whether a particular expenditure is prudent, including consideration of the duration and preservation of the endowment. One commentator observed that "UPMIFA emphasizes the long-term nature of the **fund**, and the need to maintain not only the original dollar value of the **fund**, but the purchasing power of the **fund** .... but without a bright-line determination of what maintaining the purchasing power means." Gary, *Charities, Endowments, and Donor*, 41 Ga. L. Rev. 1277 at 1310.

In sum, under modern endowment law there is no absolute bar to spending income from an underwater endowment **fund**. Under UMIFA, **fund** income (not including capital gains) can always be spent from an underwater **fund**. Under UPMIFA, the distinction between principal and income is abandoned and **funds** can be spent if it is prudent to do so. [30]

Neither UMIFA nor UPMIFA are the law in Alaska. But they provide a useful body of law to which courts can turn for guidance in the **permanent fund** context. In this case, they are useful because they demonstrate that in certain situations spending may continue from an endowment **fund** even when the value of the **fund** is underwater.

III. Accounting for the Unrealized Gains and Losses of the Investments of the Earnings Reserve Account

The final issue we have been asked to consider is the appropriate accounting treatment of unrealized gains and losses on the investments of the earnings reserve account. Prior to the adoption of GASB 31, the Corporation generally recorded the value of the **permanent fund** investments at cost and the market values were reported in the footnotes. *See, e.g.*, Alaska **Permanent Fund**, 1993 Annual Report at 29-37. After the adoption of GASB 31, the Corporation recorded all of the unrealized gains and losses of the **permanent fund** in the earnings reserve account. *See, e.g.*, Alaska **Permanent Fund**, 2000 Annual Report at 26. Following our 2003 Opinion, the Corporation recorded all of the unrealized gains and losses in the principal. *See, e.g.*, Alaska **Permanent Fund**, 2008 Annual Report at 23. Our 2003 Opinion did not specifically address the issue of accounting for the unrealized gains and losses on the investments of the earnings reserve account.

We think that the appropriate treatment of the unrealized gains and losses on the investments of the earnings reserve is to account for them in the earnings reserve account. The earnings reserve account is an account that is established in law. AS 37.13.145(a). This statute requires that **fund** income [31] be deposited to this account, and that such **funds** be invested. *Id.* Any state investment account will have unrealized gains and losses on its investments. Accordingly, we think the Corporation should state the value of the earnings reserve account with an entry adjusting that value to reflect the unrealized gains and losses of the investments of the earnings reserve account. This is consistent with AS 37.13.170, which requires "an appraisal at market value" of the **permanent fund's** investments. [32]

***17** By their very nature, unrealized gains and losses represent economic value that is attributable to the investments from which they are generated. For example, if the earnings reserve account is invested in 100 shares of Company X, and those shares appreciate in value from $100 to $200, that increase in value belongs to the earnings reserve account. Moreover, we think the legislature has the right to appropriate that value as it sees fit, including appropriating it to principal. Conversely, if those shares decrease in value from $100 to $50, an appropriation by the legislature of the balance of the earnings reserve account, unadjusted for unrealized loss attributable to the earnings reserve account, would arguably result in an impermissible appropriation of principal.

The legislative history indicates that the legislature intended for the earnings reserve account to retain the earnings produced by the investments of the earnings reserve account. This was explicitly stated in the law from 1982 to 1992: "[i]ncome from the investment of the earnings reserve account shall be treated as an addition to that account." *See* Sec. 2, ch. 28, SLA 1986; sec. 9; ch 81, SLA 1982 (former AS 37.13.145). This language was repealed in 1992, but the legislative history for the 1992 changes reflects an intention to conform the statute to the accounting practices in place since 1982. [33] The Alaska **Permanent Fund** Corporation historically retained the earnings reserve account income in the earnings reserve account:

How the Alaska Permanent Fund Works

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Alaska **Permanent Fund** Corporation, 1987 Annual Report at 10. Accordingly, we believe that the unrealized gains and losses attributable to the investments of the earnings reserve account should be booked in the earnings reserve account. [34]

IV. Conclusion

In summary, our answers to your questions are as follows.

A. First Question

Question. Is the corporation's policy that only the realized income of the **permanent fund** is available for expenditure from the **permanent fund** under AS 37.13.145 correct? If not, how should this amount be determined?

Answer. Under AS 37.13.140 only realized net income from the investments of the principal is considered income for purposes of depositing **funds** into the earnings reserve account in AS 37.13.145. As discussed above, income consists of interest, dividends, royalties, rents, and net realized capital gain.

Once deposited, such income must be re-invested. AS 37.13.145(a). In our view, the entire balance of the earnings reserve account, including the unrealized gains on the investments of the earnings reserve account, is subject to appropriation. If the legislature were to appropriate the entire balance of this account, the unrealized gains or losses would be recognized in the process of appropriation.

B. Second Question

Question. Is the corporation's practice that both realized and unrealized income of the **permanent fund** should be taken into account in determining the amount that is available for appropriation, i.e., distribution under AS 37.13.140, correct? If not, how should the amount available for distribution from the **permanent fund** be determined? Should unrealized income of the **Fund** be excluded in determining the amount that is available for distribution?

***18** Answer. Only the balance of the earnings reserve account is available for appropriation. The balance of the earnings reserve account consists of the realized net income from the investment of principal, as well as all income, including unrealized gains and losses, from the investment of the earnings reserve account.

C. Third Question

Question. Do the constitution and statutes require that income of the **fund** not be appropriated when doing so would bring the total value of the **permanent fund** including all unrealized gains and losses below the sum of the amounts deposited or appropriated to principal? If not, are there any other limitations with respect to the use of principal that are applicable in determining the amount that is available for expenditure or appropriation from the **permanent fund**?

Answer. The entire balance of the earnings reserve account may be appropriated by the legislature, even if the fair value balance of the principal is underwater, that is, below original dollar value. This result is required because the balance of the earnings reserve account is subject to the prohibition against dedicated **funds**, and therefore not restricted from appropriation. As discussed above, this result is not contrary to the expressed intent of the framers and voters. This result is also permitted by UMIFA, if the donor instrument permits it, and by UPMIFA, if the expenditure is prudent.

Under Alaska law, no amount of **permanent fund** principal may be appropriated. But the fair value of the principal is not a fixed notional number — it may increase and decrease.

D. Fourth Question

Question. May **permanent fund** dividends be paid in 2009?

Answer. **Permanent fund** dividends for 2009 were appropriated in the 2009 operating budget. *See* sec. 9(a), ch. 27, SLA 2008. There is currently a balance in the earnings reserve account that is sufficient to pay dividends. The Alaska **Permanent Fund** Corporation is authorized by law to make the transfer, and the **Permanent Fund** Dividend Division is authorized by law to issue the dividend checks.

E. Fifth Question

Question. What is the appropriate accounting treatment of unrealized gains and losses in the earnings reserve account?

Answer. Because the earnings reserve account is a state investment account established in law, the unrealized gains and losses on the investments of the earnings reserve account should be accounted for in the earnings reserve account. Accounting for the unrealized gains and losses of the investments of the earnings reserve account in the earnings reserve account will ensure that the legislature has accurate information as to the full amount of **funds** that are available for appropriation from the earnings reserve account.

* * *

In conclusion, spending from the earnings reserve account when the principal is underwater is a question that is firmly committed to the legislature's exercise of its appropriation power.

We also note that as both statutory net income and the balance of the earnings reserve account decrease, the dividend calculation for future dividends is trending downward. As it does so, the amount of money transferred to pay **permanent fund** dividends will likewise trend downward. We anticipate that even though 2009 dividends will be paid, the dividends for future years may be small in comparison to recent dividends. Thus, the design of the existing statutes will limit expenditures from the **permanent fund**, perhaps significantly so, as a consequence of the decline in the market.

Sincerely,

***19** Richard A. Svobodny
Acting Attorney General
By: Michael A. Barnhill
Senior Assistant Attorney General

APPENDIX A

Framers' Statements Regarding Use of the Permanent Fund for Economic Development

I. Excerpts from Legislative Deliberations on HJR 39,1976

***20** "I think the idea is to as much as possible so far as the Alaska economy can provide good and reasonable investments within the state that's where we would want to invest the money at least finally if not initially and that that's something that's sort of the case where you can have your cake and eat it too. You can put the money out in sound investment programs some of which could be loan programs that benefit the people of the state in the form of capital and the same time derive an income from it and when those loans are returned new loans will be made. So it's the situation where the wealth stays basically in the state; stays at work in the state and continues to provide both direct and indirect benefits to the people." Hearing on HJR 39 Before the House Judiciary Comm., 9th Legislature (Mar. 15, 1976) (Representative Malone statement) (tape in State Archives Box 18287).

"The very purpose for which we're asking that this become part of our constitution that is to start building a reserve **fund** to build a more viable economic base for the state." Debate on HJR 39 on House Floor, 9th Legislature (Mar. 25, 1976) (Representative Gruening statement) (tape in State Archives Box 18385).

"A **permanent fund** at the 25 percent level would result in an accrual of capital investment available for investment within Alaska in homes and in businesses for the good of the people in the state of approximately $2.8 billion by 1985. It's an alternative approach to using state money rather than filtering it through the state bureaucracy. It's an approach that provides direct tangible benefits to the people of the state." Debate on HJR 39 on House Floor, 9th Legislature (Mar. 25, 1976) (Representative Malone statement) (tape in State Archives Box 18385).

"Sometimes you can do as much or more good for people by making some capital available to them as individuals, groups and corporate organizations, both public and private, as you can by having the state perform those types of services .... The purposes of this **fund** are much broader than any narrow dedication of taxes. It's a **fund** that would be available for the diversification of the economy of the state and be available to the citizens of the state as individuals and groups. It would lend some economic stability, I believe, once the **fund** is established." Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (Representative Malone statement) (tape in State Archives Box 18290).

"[Unless there is a significant attitude change by a future legislature], we're pretty well assured that the [implementing] legislation will be written and the laws enacted to provide for maximum possible investment within the state." Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (Representative Malone statement) (tape in State Archives Box 18290).

"The [Hammond] administration has that same commitment." Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (Commissioner Sterling Gallagher statement referring to Representative Malone's statement regarding maximum possible investment within the state) (tape in State Archives Box 18290).

***21** "I think this is the primary purpose of the **permanent fund** and that is to retain capital in Alaska .... I think the **permanent fund** can provide for more capital leverage for the state. ... I think the **permanent fund** of course can provide I think greater control or greater development by Alaska capital in the areas than say even outside capital would not develop in. An example

of course and this would be taken up after the constitutional amendment is, either, if it is approved, the Susitna dam project is one, the hatchery projects are another example." Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (Representative Gruening statement) (tape in State Archives Box 18290).

II. Comments in the Media Regarding HJR 39,1976

"This concept makes portions of the oil revenue available to citizens on a more direct level. By establishing the program, we will be able to allow Alaskans a direct hand in managing part of the money." Howard Weaver, ***Permanent Fund*** *is Biggest Project*, Anchorage Daily News, June 2, 1976, at 1 (quoting Representative Malone).

"People always talk about return on the dollar. The priorities always get based on the value of money. Well, I don't think that should be the main concern for this investment program. ... I don't think the managers—and that's what the legislature will be—should just look at return in dollars; we have to talk about the quality of life in Alaska .... This legislature now has given people a chance to let the average Alaskan get a piece of all this (oil) action. That's more important than government programs, or return on the dollar or any of that. It can give the people a chance to start a business, or live in a decent home .... Think about hydroelectric projects. Some of them, the big ones, are open to question, sure. But when you get down to providing an eternal supply of electric power to some small community, maybe you've done something with no terrific return on the dollar, but you've sure improved the quality of people's lives. And you let them manage it; it's a loan, an investment. It's not just another government project .... The wealth that those resources represent belongs to the people of this state, and that shouldn't be exported .... The main concerns of this **fund** ought to be diversifying the economy of Alaska, of developing the resources first of all for the people of Alaska. Agriculture, timber, fish, businesses—we've got to put the emphasis on things owned and operated for the people of the state. The resources in the state ought to be used in the state, or at least for the state. We have to have first call on the use. If the resource leaves the state, the value shouldn't." Howard Weaver, ***Permanent Fund*** *is Biggest Project*, Anchorage Daily News, June 2, 1976, at 1 (quoting Representative Malone).

APPENDIX B

Public Statements Regarding the Objectives of the Permanent Fund

I. Savings

22** "The **permanent fund** indeed would be a trust, held inviolate for prescribed uses. It also would have much to offer the state's heritage for it would preserve for future Alaskans some of the benefits of oil wealth." *Editorial, A Future* ***Fund, Anchorage Daily News, April 20, 1976, at 4.

"It also would give the state an important alternative: instead of spending oil revenues automatically for more bureaucracy, the state would be allowed to open a sound 'savings account."' *Editorial, 2 Plans, 1* ***Fund***, Anchorage Daily News, April 21, 1976, at 6.

The **permanent fund** "will be a kind of savings account where we will be able to sock some of this revenue away and preclude long-fingered politicians from picking the public pocket." *Alaska's Portrait in Oil: "A Crazy Quilt Economy*, U.S. News & World Report, Aug. 2, 1976, at 33 (quoting Gov. Hammond).

"The idea of a 'savings account' type arrangement has been advocated by many." ***Permanent Fund***, Alaska Department of Revenue Journal, Oct. 1976, at 7.

"Politicians could spend the interest, but never the principal." ***Permanent Fund*** *Raises Use Issue*, Anchorage Daily News, Oct. 22, 1976, at 2.

The **permanent** **fund** will be a "lasting savings account from some of the oil revenues." *Editorial, It's **Permanent***, Anchorage Daily News, Oct. 24, 1976, at 4.

"The object is to prevent future legislatures from doing what previous legislatures did with the $900 million bonanza received by the state from the sale of Prudhoe Bay leases in 1969. That gigantic sum ran through the legislators' fingers like water, to the alarm of many who had pleaded at the time that the $900 million be invested, the principal preserved and the state spend only that money derived from interest." *Editorial, No Easy Choice*, Anchorage Times, Oct. 24, 1976, at A-4.

"[Those promoting the **permanent** **fund**, including Gov. Jay Hammond] also view it as a savings account, to keep some of the state's income from oil and gas out of the general **fund** so it can't be spent." Susan Andrews, *Lawmakers Would Shape **Permanent** **Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

"The income from the **Permanent** **Fund** will be available for general appropriation by the legislature, but the principal of the **fund** may not be touched. It could only be removed from the **fund** by another constitutional amendment." Gov. Jay Hammond, *The Governor's Point of View*, Anchorage Times, Oct. 27, 1976, at 6.

"The principal of the **fund** would be used only for income-producing investments permitted by law." Legislative Affairs Agency, *Summary of Proposition*, 1976 Official Election Pamphlet, at 56.

"Just as a wise and prudent family sets aside money in a savings account for the future, so should Alaska's state government set aside a rainy day **fund** to benefit this and future generations of Alaskans." Alaska State Chamber of Commerce, *Statement in Favor of Proposition No. 2*, 1976 Official Election Pamphlet, at 57.

II. Flexible Use

23** "Exactly how the **permanent** **fund** is set up would be the job of future legislatures. Our elected representatives, by law, would prescribe how the money is to be invested. That may demand a different application of the **fund** from one year to the next, but flexibility to meet changing demands is guaranteed by current legislation. Likewise, future legislators would be able to decide what to do with the considerable earnings of the **fund**." *Editorial, 2 Plans, 1 **Fund, Anchorage Daily News, April 21, 1976, at 6.

"[T]he legislature would supervise [the **permanent** **fund**] as a 'board of directors' and designate investments for which it could be used." *Demos Hear Gruening, Sassara*, Anchorage Daily News, July 16, 1976, at 6 (quoting Representative Gruening).

"Nobody knows exactly how the **fund** will be used; that decision will be made by legislative action in the future. Although the **fund** is protected against certain kinds of usage, its precise organization and management have been left flexible by designers .... [t]he flexibility of allowing future legislatures to decide on precise uses will prevent the 'locked up' circumstance .... There have been many proposals for possible **fund** uses. They range from paying direct dividends to Alaskans to using the money to underwrite such vast projects as hydroelectric dams." ***Permanent** **Fund** Raises Use Issue*, Anchorage Daily News, Oct. 22, 1976, at 2.

"[Representative] Malone said the **fund** could go for all three of those uses [economic development, savings, and community development]. The legislature would decide what per cent of the **fund** would go to each use." Susan Andrews, *Lawmakers Would Shape **Permanent** **Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

"Consultants have told the state's Investment Advisory Committee that the "income-producing requirement" [for investments of the principal] of the **fund** gives the state broad latitude." Susan Andrews, *Lawmakers Would Shape **Permanent** **Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

"There are a number of possibilities for uses of the earnings — and the legislature will decide those uses." Susan Andrews, *Lawmakers Would Shape **Permanent** **Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

III. Economic Development

"It would allow Alaskans to directly share from the oil revenues because the **permanent** **fund** would offer loans to businessmen, builders and fishermen. This would pump money to Alaskans who, in turn, would pump it back into the state's economic mainstream. The state would be investing in itself." *Editorial, A Future **Fund***, Anchorage Daily News, April 20, 1976, at 4.

"A percentage of the **permanent** **fund** would go for direct use by Alaskans-loans to businessmen, fishermen and builders." *Editorial, 2 Plans, 1 **Fund***, Anchorage Daily News, April 21, 1976, at 6.

"What sort of enterprises? The **fund** could help put a viable state agricultural industry on its feet. It could provide loans to Alaskans who want to build their own homes, but can't obtain conventional financing. It could also be utilized in revitalizing the state's depleted fishing industry by helping individual fishermen finance and construct new boats. And it could simultaneously encourage the development of aquaculture corporations to rebuild the fish stocks." *Editorial, The **Permanent** **Fund***, Fairbanks Daily News-Miner, April 26, 1976, at A-4.

***24** "We'll be plowing it [the **permanent** **fund**] into the economy, all right, but using it for investment purposes—not to balloon the economy .... [t]he most critical goal is to strengthen our renewable resource industries—such as fishing and timber —for the day when nonrenewable resources run out." *Alaska's Portrait in Oil: "A Crazy Quilt Economy*, U.S. News & World Report, Aug. 2, 1976, at 33 (quoting Gov. Hammond).

Economist Bob Richards of Alaska Pacific Bank "presented a paper addressing the possible investment options for the proposed **fund** .... Richards indicated that bolstering Alaska's traditional industries of fishing and forest products along with creating a more broadly based economy 'would most effectively satisfy the intent of the Alaska voters ...'" *Experts Discuss **Permanent** **Fund***, Anchorage Daily News, Aug. 30, 1976, at 2.

"The concept of 'controlled economic diversification' is being broached by many as one that merits the attention of the populace. If the State can 'wisely' funnel money into good investments within its borders, then several goals may be achievable .... The **funds** could thus immensely aid Alaska's citizenry." ***Permanent** **Fund***, Alaska Department of Revenue Journal, Oct. 1976, at 6.

"This **fund** can become a tool whereby Alaska can take some of today's mineral wealth and prepare for the future by investing in the development of human and material resources that will remain productive for many generations." ***Permanent** **Fund** Raises Use Issue*, Anchorage Daily News, Oct. 22, 1976, at 2 (quoting Revenue Commissioner Sterling Gallagher).

"This is a chance to let average Alaskans have a stake in managing some of the oil wealth. It's more than a bank account; it's a way to change some basic patterns." ***Permanent** **Fund** Raises Use Issue*, Anchorage Daily News, Oct. 22, 1976, at 2 (quoting Representative Malone).

A portion of the **permanent** **fund** "would go for direct use by Alaskans — for loans to businessmen, fishermen and builders." *Editorial, It's **Permanent***, Anchorage Daily News, Oct. 24, 1976, at 4.

"Those promoting the **permanent** **fund**, including Gov. Jay Hammond, see it as a way of providing development capital to diversify the state's economy, strengthen renewable resources such as fisheries, timber and tourism, and make possible large projects such as dams, which couldn't otherwise be financed." Susan Andrews, *Lawmakers Would Shape **Permanent** **Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

"Others see the **fund** as a source of loans for community development, such as home mortgages, small business loans, for power development, ports, utilities, roads ...." Susan Andrews, *Lawmakers Would Shape* ***Permanent Fund***, Anchorage Times, Oct. 24, 1976, at A-3.

"The **Permanent Fund** won't be simply a giant bank savings account/—it will be a pool of cash available for business investments either in Alaska or outside the state. If these investments are approved wisely by the state, we'll not only have continued earnings from our one-time oil resources but we'll also have a new spur to the economy of our state through loan programs which could extend from the largest businessman to the smallest homeowner." *Editorial, Some Serious Propositions*, Fairbanks Daily News-Miner, Oct. 29, 1976, at A-4.

***25** "Projects invested in with sources from the '**Permanent Fund**' could help broaden Alaska's narrow based economy and bring more stability to our State." Alaska State Chamber of Commerce, *Statement in Favor of Proposition No. 2*, 1976 Official Election Pamphlet, at 57.

"Because of the constitutional requirement that the **permanent fund** be used only for income-producing projects, it is likely the **fund** will be designed to provide loans to Alaskan individuals or businesses." Paul Nussbaum, *The Issues in* 77, Anchorage Daily News, Nov. 11, 1976, at 1.

Footnotes

1 We have also opined that a dedication additionally requires that the legislature relinquish any further control over the **funds**. 1982 Op. Att'y Gen. No. 13 at 20 (Nov. 30).

2 Article IX, section 15 of the Alaska Constitution pertains to the **permanent fund**.

3 Georgia is the only other state with a constitutional prohibition against dedicated **funds**. *Myers v. Alaska Hous. Fin. Corp.*, 68 P.3d 386, 389 (Alaska 2003).

4 *Alex*, 646P.2d at 210.

5 *Myers*, 68 P.3d at 390-91.

6 *SEACC*, 202 P.3d at 1167-70.

7 We note that the Court in *SEACC* observed that "the reach of the dedicated **funds** clause might be extended to statutes that, while not directly violating the clause by dedicating revenues, in some other way undercut the policies underlying the clause." *SEACC*, 202 P.3d at 1170. We do not know what kinds of statutes the Court has in mind, but we are aware of the extensive practice of **fund** and account designations that give certain recipients a "'talking point,' that is, a possible advantage over other agencies, when seeking the **funds** from the legislature." *Id.* at 1174.

8 This office has recognized certain implied exceptions to the broad interpretation of "proceeds of state tax or license," including pension contributions, bond proceeds, sinking **fund** receipts, and revolving **fund** receipts because the Alaska Constitutional Convention clearly intended to exempt these types of revenues from the scope of the prohibition against dedicated **funds**. 1982 Op. Att'y Gen. No. 13 at 10-11 (Nov. 30). We continue to believe that the Court would recognize these implied exceptions.

9 The legislature has also made a number of special appropriations to principal from the general **fund** or earnings reserve account over the history of the **permanent fund**.

10 The constitutional framework of the **permanent fund** was graphically depicted prior to the vote of the people in 1976 as follows:

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Anchorage Times, October 24, 1976, A-3. This depiction, however, does not show the alternative income use authorization.

11 The legislative history of HJR 39, the constitutional resolution establishing the **permanent fund**, establishes that the framers intended this language to restrict the principal from appropriation. The principal "could not be used to **fund** the general operating expenditures or capital improvements of the State." Letter from Gov. Hammond to Speaker Bradner (Jan. 15, 1976), *reprinted in* 1976 House J. 39-40.

12 Tape in State Archives Box 18460. Because the condition of the tapes referred to in this opinion have significantly deteriorated, the State Archives has made digitized copies of them. The disks are identified by archive box number and date.

13 Staff Jim Rhodes later described this element of the **permanent fund**: "Perhaps the most important break with the past may have been the language dispersing the earnings of the **fund** to the general **fund** 'unless otherwise provided by law.' This opened numerous

possibilities, including the pledging of earnings as security for state and local debt (or debt of the **fund** itself), increased municipal revenue sharing, and cash payments to specified Alaskan residents (the seed of the Alaska, Inc. proposals).” Jim Rhodes, A Short History of the Alaska **Permanent Fund** at 4-5, Folder S-l, State Archives Box 7862 (unpublished manuscript, circa 1977-1980).

14 This account was known as the undistributed income account from 1982 to 1986, when it was re-named the earnings reserve account. *See* sec. 9, ch. 81, SLA 1982; sec. 2, ch. 28, SLA 1986.

15 *Hickel*, 874 P.2d at 934.

16 By preserving purchasing power, we mean that the real value of the deposit is preserved over time. In an inflationary economic environment, the real value of a monetary unit (such as a dollar) will decline over time, while the nominal or face value stays the same. Thus, to maintain real value or purchasing power, the deposit needs to be invested in assets that will appreciate in value in order to keep up with inflation. For example, in order to preserve the purchasing power of a deposit of $1 in 1977, the fair value of the investments of that deposit would need to be worth approximately $3.51 in 2008.

17 In the initiative context, the Court will attempt to discern the intent of the voters by looking at “published arguments” relating to the initiative. “To the extent possible, we attempt to place ourselves in the position of the voters at the time the initiative was placed on the ballot, and we try to interpret the initiative using the tools available to the citizens of this state at that time.” *Alaskans for a Common Language, Inc. v. Kritz*, 170 P.3d 183, 193 (Alaska 2007).

18 While the Court frequently refers to the minutes of the constitutional convention when addressing issues of constitutional construction, its older cases recognized the pitfalls of undue reliance on minutes as evidence of framers' intent: “This court has previously held that opinions of individual members of the convention generally are not considered to be a safe guide in ascertaining the purpose of a majority of the convention when adopting a particular provision. But reports of committees and statements of chairmen of such committees stand on a more solid footing, and may be resorted to in determining the intent of the enacting body.” *Starr v. Haglund*, 374 P.2d 316, 319 (Alaska 1962) (citing *Matthews v. Quinton*, 362 P.2d 932, 944 (Alaska 1961)). The *Starr* Court also observed that it would be “purely a matter of conjecture” to determine the understanding of the voters. *Id.* at 321. We review the record with these cautionary but older statements in mind.

19 *See* Hearing on HJR 39 Before the House Finance Comm., 9th Legislature (Feb. 21, 1976) (adding “unless otherwise directed by the legislature” with respect to the deposit of income to the general **fund** will give “maximum flexibility” to the use of income) (tape in State Archives Box 18461); Hearing on HJR 39 Before the House Judiciary Comm., 9th Legislature (Mar. 15, 1976) (Representative Gruening statement that the **permanent fund** concept was “much more flexible” than the tobacco tax dedication) (tape in State Archives Box 18287); Joint Chairman's Report on CS SSHJR 39 (maximum flexibility” for the use of income); Debate on HJR 39 on the House Floor (Mar. 25, 1976) (Representatives Malone and Gruening statements regarding need to preserve flexibility of the **fund**) (tape in State Archives Box 18385); Hearing on HJR 39 Before the Senate Resources Comm., 9th Legislature (May 15, 1976) (Representative Malone statement that the investments will be decided by future legislatures) (tape in State Archives Box 18290).

20 During the House floor debate on HJR 39, Representative Urion attempted to amend the resolution to require that the principal be invested in guaranteed rate of return investments. Representatives Malone and Gruening opposed the amendment on the grounds that it would limit the ability to use the **permanent fund** to diversify the economy of the State. 1976 House J. 698-99; Debate on HJR 39 on the House Floor (Mar. 25, 1976) (tape in State Archives Box 18385).

21 An early historian of the **permanent fund** put it this way: “The reason for much confusion was that the legislature had created the **permanent fund** before it had come to any consensus about what the **fund** was. After the success of the constitutional amendment, there was a general understanding of what the **permanent fund** was not; that is, that it was not the general **fund**.” Mike Doogan, **Permanent Fund** History, ch. 7, p. 2, unpublished manuscript (1982) (Alaska State Archives, Box 7862, Folder S-2).

22 We note that under modern endowment law, discussed below, the mere use of the words “principal” and “income” in connection with the creation of an endowment **fund**, unless expressly stated otherwise, are interpreted only to intend the creation of an “endowment **fund** of **permanent** duration.” *Uniform Prudent Management of Investment **Funds** Act*, § 4, 7 A Pt. III U.L.A. 17 (2008).

23 We note that in 1980, four years after the creation of the **permanent fund**, a statutory framework for administering the **permanent fund** was enacted. Ch. 18, SLA 1980. By this time, the concept of protecting **permanent fund** principal had more fully evolved in the minds of legislators and the public. The legislative history characterizes the principal as an “inviolate trust” (1980 H. Journal 461-62) and explicit provisions were made to protect principal: no investment in equities (AS 37.13.120(g)) and any capital losses were to be recouped from income (AS 37.13.130). Capital gains were credited to principal. *Id.* (These particular protections, however, were abandoned in 1982 in favor of inflation-proofing in order to facilitate the **permanent fund** dividend program. *See* sees. 5 (amending AS 37.13.120(g) to permit investment in equities), 8 (net income is computed to include capital gains), 9 (inflation-proofing) and 13 (repealing AS 37.13.130), ch. 81, SLA 1982).

In 1979, one of the framers described the evolution of thinking regarding the **permanent fund**:

I recall writing an article in which I enumerated various worthy things the **Permanent Fund** could do. Principal among these was the opportunity to use **Permanent Fund** money to diversify the economy and to replace absentee ownership of certain industries, particularly renewable resource industries, with Alaskan ownership. Now that I'm older and wiser, or at least older, I see the **Permanent Fund** cannot reasonably be expected to accomplish all our goals at once. One reason for a modification in my view is that the **fund** didn't turn out to be as big a pot of gold as anticipated. Another fact was the realization that many of the "development banking" investments would be at risk levels generally incompatible with the concept of a savings trust.

Hearing Before House Special **Permanent Fund** Comm., 11th Legislature, (Mar. 30, 1979) (written testimony of Clark Gruening at 10-11).

24 In past opinions, we have questioned whether the **permanent fund** is subject to trust law. Our view has generally been that the **permanent fund** is not a true "trust" but that courts might apply trust principles. *See* 1977 Inf. Op. Att'y Gen. at 2 (J-66-106-78; Aug. 31); 1977 Inf. Op. Att'y Gen. at 1-5 (J-66-106-78; Sept. 16); 2003 Op. Att'y Gen. at 9-10, 18-19 (June 18). In addition to applying trust principles, we think the courts may also at least consider the law of endowments.

25 The Ford Foundation also commissioned a blue ribbon panel to review this work. The blue ribbon panel was comprised of many leading lawyers of the day including Lewis F. Powell, Jr., Eli Whitney Debevoise, and Alan Stroock. William Cary and Craig Bright, The Law and the Lore of Endowment **Funds** at vii (1969). For a discussion of Cary & Bright, see Susan N. Gary, *Charities, Endowments, and Donor Intent: The Uniform Prudent Management of Institutional **Funds** Act*, 41 Ga. L. Rev. 1277, 1284-88 (Summer 2007).

26 *UMIFA*, Prefatory Note, 7A U.L.A. 3 (2006).

27 A bill for the adoption of UPMIFA was introduced this year. S. B. 13 4, 26th Legislature (2009).

28 For instance, the Alaska Supreme Court routinely considers the American Law Institute's Restatements of the law of various subjects.

29 New York Dep't of Law, Advice for Not-for-Profit Corporations on the Appropriation of Endowment **Fund** Appreciation (undated); *see also*, Pietrina Scaraglino, Restricted Gifts, Practicing Law Inst. No. 8571 at 144 (2006) ("Importantly, income on an endowment can always be expended [under New York law], regardless of whether a **fund** falls below its historic dollar value. Of course, consistent with the applicable gift instrument, a nonprofit board may determine that it is prudent not to expend income when a **fund** is below its historic dollar value; however, there is no statutory prohibition against the appropriation and expenditure of income").

30 A subjective prudent spending rule in the **permanent fund** context could be difficult to administer. To the extent that the legislature or the people wish to consider a UPMIFA-like law to govern the **permanent fund**, it may be worth considering an objective spending limitation, such as a maximum expenditure ceiling, rather than a subjective rule of prudency.

31 The "income" to be deposited in the earnings reserve account is the net income of the **permanent fund**, computed according to generally accepted accounting principles, excluding any unrealized gains or losses. AS 37.13.140. Thus, the definition of income includes traditional components of income, such as interest, dividends, royalties and rents, and also includes net realized appreciation, that is, net realized capital gains and losses.

32 It follows that the Corporation should state the value of principal at original dollar value (as it currently does) with an entry adjusting that value to reflect the unrealized gains and losses of the investments of the principal. Thus, only the unrealized gains and losses attributable to principal should be accounted for in the principal. The term "principal" simply means the amount deposited to principal. Because investment value changes over time, there are two ways to describe principal: original dollar value and current fair value.

33 The legislative history states that the purpose of rewriting this statute was to "clarify original legislative intent and Corporation practice regarding the annual disposition of **Fund** income." Memo from David Rose to Sen. Pat Pourchot at 2 (Feb. 1, 1991), S.B. 39 Bill File, 17th Legislature (1991)

34 The APFC may wish to consider the use of unitized pooling, where a common pooling account holds and invests the assets of multiple participating government accounts and each government account owns units in the common pooling account. Unitized pooling is commonly used by endowments. Unrealized gains and losses are accurately tracked because the unit values reflect the net asset values of the investments of the underlying unitized pooling account.

2009 WL 1719849 (Alaska A.G.)

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