



THE STATE
of **ALASKA**
GOVERNOR BILL WALKER

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February 6, 2018

The Honorable Neal Foster and the Honorable Paul Seaton
Alaska State Representatives
Co-chairs, House Finance Committee
State Capitol Rooms 410 and 505
Juneau, AK 99801

Re: Clarifications regarding HB 213

Dear Co-Chairs Foster and Seaton:

With respect to HB 213, we believe the House Finance Committee may benefit from a few clarifications regarding the history of the Public School Trust and related litigation as the committee considers this bill.

Restrictions on Expending Trust Principal; Impact on the POMV Approach.

From a legal perspective, we believe the state has considerable flexibility to modernize the public school trust fund by implementing a percent of market value (POMV) approach in HB 213. Section 1 of HB 213 would make amendments that would continue to require the "principal of the fund" to be "perpetually retained in the fund for investment purposes." Perpetually retaining the principal of the fund is contrary to a pure POMV approach, which eliminates distinctions between income and principal. However, some suggest concern with the pure POMV approach because if significant capital losses occur, some portion of the principal could be expended.

One question is whether amending HB 213 to implement a pure POMV approach is prohibited because the pure POMV approach potentially may result in the expenditure of principal?

As a starting point in the analysis, the POMV approach proposed in HB 213 would only authorize the legislature to appropriate up to the 4.75% POMV amount.¹ If the appropriation of the maximum amount would result in the expenditure of principal, the legislature could elect to appropriate less for reasons based upon policy, consideration of trust principles, or legal obligations. Further, ongoing legislative oversight over the public school trust fund should help ensure that actual problems do not arise. The POMV approach could be modified to meet future investment circumstances. The potential possibility that principal might be expended can be avoided without explicitly stating that the principal shall be perpetually retained.

Regarding federal law restrictions, the state obtained public school trust land under two distinct federal grants. One grant applies to the majority of public school trust land, the second applies to one section (640 acres). Each federal grant imposes different rules to the management of the specific land.

Rules Applicable to the Majority of Public School Trust Land. Congress in Section 6(k) of the Alaska Statehood Act repealed the detailed mechanisms that had applied to the Territory of Alaska for preserving principal and expending only income from the trust fund. Instead, only general trust law principles apply to how the state expends public school trust monies.

During territorial times, the Act of March 4, 1915² (the “1915 Act”) reserved sections 16 and 36 in surveyed townships. The 1915 Act gave the Territory of Alaska authority to lease or manage the land. Income derived from the land was required to be deposited into a permanent fund. Income from the permanent fund was available to be expended to support public schools. These specific restrictions on preserving trust principal and expending only income from the trust fund were repealed by section 6(k) of the Alaska Statehood Act.

In addition to repealing the 1915 Act, section 6(k) of the Alaska Statehood Act granted to the state lands which had been reserved by the 1915 Act. Congress granted those lands for the purposes for which the lands had been reserved; meaning lands were granted for the support of public schools. The Alaska Supreme Court held that the grant

¹ HB 213, sec. 3 (adding new AS 37.14.165).

² 48 U.S.C. § 353 (repealed 1959). A copy of the 1915 Act is attached.

of public school lands and its acceptance by the state created a trust.³ The Court has also held that general trust law principles apply to federally created trusts.⁴

In summary, for the majority of the public school trust land, no federal law restrictions expressly prohibit the expenditure of principal. Instead, general trust law principles apply, and do not prohibit modernizing the public school trust fund with a POMV approach.

Rules Applicable to Territorial Grant 1. The exception to the flexibility described above is Territorial Grant 1, by which Congress granted 640 acres to the Territory of Alaska in 1957.⁵ In the grant, Congress gave the Territory ownership and the right to manage or dispose of the land. Proceeds or income from the lands or minerals above the costs of disposal were to be deposited into territorial permanent funds to be invested, and the income expended exclusively for the use and benefit of public schools. Congress confirmed and transferred Territorial Grant 1 to the state under Section 6(k) of the Alaska Statehood Act. The State thereby obtained Territorial Grant 1 with the obligation to retain principal and only expend income from the territorial public school fund.

While Territorial Grant 1 was only one section of the public school trust (640 acres out of 175,000 acres), its location in Anchorage makes it more valuable than other trust lands. Territorial Grant 1 is located in the Merrill Field, Northway Mall, Penland Park area east of downtown Anchorage. A land valuation described below estimated Territorial Grant 1 held approximately 31% of the total value of public school trust lands.⁶

Thus, the state obtained Territorial Grant 1 with the restriction that income and proceeds from the land be permanently retained. While these federal restrictions apply to only one section, that section was estimated to hold about 31% of the total trust land value. The federal restrictions may attach to that portion of the public school trust fund.

³ *Wessells v. State Dept. of Highways*, 562 P.2d 1042, 1051 n. 34 (Alaska 1977).

⁴ *State v. University of Alaska*, 624 P.2d 807, 813 (Alaska 1981) (University Trust); *State v. Weiss*, 706 P.2d 681, 683, n. 3 (Alaska 1985) (Mental Health Trust).

⁵ A copy of Territorial Grant 1 is attached.

⁶ See page 5 of the attached Executive Summary of the land valuation; TG-1 is valued at \$74,125,000.

Land Valuation:

The settlement of the *Kasayulie v. State* litigation authorized the state to complete a valuation of former public school trust lands jointly initiated with *Kasayulie* plaintiffs during the litigation. The state completed that valuation, estimating a total value of \$241,787,500. A copy of the executive summary of the valuation is attached. Most of the land is valued as of July 1, 1978; the date the land trust was transformed into a monetary trust. This effort was completed as contemplated by the settlement of *Kasayulie v. State*.

Dedicated Fund Clause.⁷

The dedicated fund clause of the Alaska Constitution provides that "[t]he proceeds of any state tax or license shall not be dedicated to any special purpose" with only specific exceptions. The exceptions include the Alaska permanent fund, when the dedication is required for state participation in federal programs, and dedicated funds that pre-date the ratification of the constitution (April 24, 1956).

We understand there may be some confusion regarding whether the dedicated fund clause requires the allocation of land revenues into the public school trust fund under AS 37.14.150 must cease as soon as total allocations equal the 1978 value of school trust land. A 1985 AG Opinion concluded that the 1978 redesignation of public school trust lands was not a breach of trust, and that the dedication of state land revenues to the trust under AS 37.14.150 "is permissible until the amount deposited in the public school fund equals the fair market value of the lands."⁸ The Superior Court in *Kasayulie v. State* disagreed with each of those conclusions. In particular, the Court found the dedicated fund clause was not violated by the allocation of land revenue under AS 37.14.150 after allocations equaled the 1978 value of public school trust land.⁹

Later Alaska Supreme Court decisions likewise cast doubt on the conclusion that the AS 37.14.150 became unconstitutional as soon as allocations equaled the 1978 land value. Courts begin their analysis presuming statutes to be constitutional. The party

⁷ Alaska Const., Art. IX, § 8.

⁸ A copy of the 1985 AG Opinion is attached. The comment regarding the dedicated fund clause is at page 3.

⁹ A copy of the Court's September 1, 1999 decision is attached. The finding regarding the dedicated fund clause is at pages 12-13.

challenging the statute has the burden of persuasion and doubts are resolved in finding the statute constitutional.¹⁰ The court in *Meyers v. Alaska Housing Finance Corporation*¹¹ analyzed the dedicated fund clause in the context of the treatment of future revenues the state would obtain from the settlement of tobacco litigation. The transaction in *Meyers*, involved a sale of these future state revenues. The state “sold” future tobacco settlement payments to secure bonds issued to raise money for current public needs, including to support construction of public schools. Future state revenues were sold to provide current funds for public needs. The court held the dedicated fund clause allows the state to sell future revenues, at least in some circumstances.¹²

Similarly, the transformation of the public school trust from a land to a monetary trust in 1978 could be characterized in a manner that AS 37.14.150 does not violate the dedicated fund clause. The legislature in 1978 enabled the state to obtain all public school trust lands in exchange for the public school trust obtaining a right to a portion of future state land revenues to be allocated under AS 37.14.150. While the state legislature may take and use school trust land for other public purposes, taking trust land creates a federal trust obligation to compensate the trust for the full market value of the lands.¹³ The state could have paid the required full market value compensation in a lump-sum in 1978. Instead, compensation for public school trust land is being paid over time through the allocations made by AS 37.14.150. A court could reasonably determine that compensation paid through AS 37.14.150 must continue after the allocations equal the 1978 land value to compensate the public school trust for the time it has taken for the state to pay the full market value of the land.

Therefore, the legislature should not rely on the prior AG Opinion. The presumption is AS 37.14.150 remains constitutional. And, although the Superior Court’s opinion in *Kasayulie v. State* is not binding, the conclusion finds support from subsequent

¹⁰ *Alaskans for a Common Language, Inc. v. Kritz*, 170 P.3d 183, 192 (Alaska 2007).

¹¹ 68 P.3d 386 (Alaska 2003).

¹² *Id.* at 394.

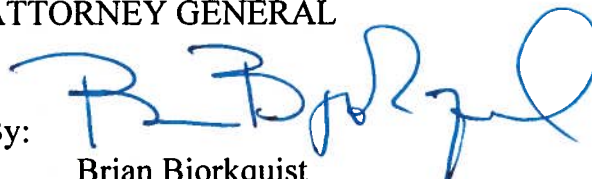
¹³ *State v. University of Alaska*, 624 P.2d at 815-16.

Alaska Supreme Court decisions. A court may reasonably find that AS 37.14.150 does not violate the dedicated fund clause.

Sincerely,

JAHNA LINDEMUTH
ATTORNEY GENERAL

By:



Brian Bjorkquist
Assistant Attorney General

BDB/aec

cc: Rep. Justin Parish
Jahna Lindemuth, Attorney General
Mike Barnhill, Deputy Commissioner, Dept. of Revenue

Encl: 1915 Act
Territorial Grant 1
Executive Summary, Land Valuation
1985 AG Opinion
September 1, 1999 Decision in *Kasayulie v. State*