

LEGAL SERVICES

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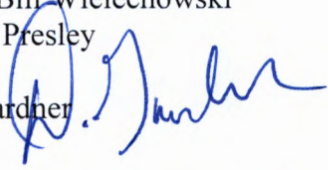
State Capitol
Juneau, Alaska 99801-1182
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MEMORANDUM

January 26, 2016

SUBJECT: HB 256 and appropriations relating to the CBR
(Work Order No. 29-LS1357)

TO: Senator Bill Wielechowski
Attn: TJ Presley

THRU: Doug Gardner 
Director

FROM: Megan A. Wallace 
Legislative Counsel

You have asked for a legal analysis of the governor's proposal pertaining to the budget reserve fund (art. IX, sec. 17, Constitution of the State of Alaska). You have stated that based on the governor's budget, which proposes to transfer money between the constitutional budget reserve fund, the statutory budget reserve fund (AS 37.05.540(a)), and the earnings reserve account (AS 37.13.145), the governor believes the earnings reserve account to be exempted from the constitutional sweep in future years and that a supermajority vote to access the constitutional budget reserve fund will not be required under art. IX, sec. 17(d), Constitution of the State of Alaska.¹

HB 256

The governor's operating budget, introduced as HB 256, appropriates money not traditionally transferred to the earnings reserve account, including "all mineral lease bonuses, rentals, royalties, royalty sale proceeds, net profit shares under AS 38.05.180(f) and (g), and federal mineral revenue sharing payments."² In addition, HB 256 proposes a "reverse sweep" from the constitutional budget reserve fund and transfer of the unexpended and unobligated balance of the constitutional budget reserve fund to the statutory budget reserve fund.³ Both of the appropriations from the constitutional budget reserve fund are made under art. IX, sec. 17(c), Constitution of the State of Alaska,

¹ The Department of Law also issued an opinion on January 25, 2016, outlining the administration's position on this issue.

² HB 256, sec. 8(a), page 48, lines 19 - 22. *See also* sec. 8(b), page 48, lines 23 - 27.

³ HB 256, secs. 27(a) and (b), page 69, lines 15 - 23.

requiring a three-fourths supermajority vote.⁴ HB 256 also proposes to transfer \$3,000,000,000 from the statutory budget reserve fund to the earnings reserve account.⁵ If the unrestricted state revenue is insufficient to cover general fund appropriations for 2017, HB 256 proposes that the amount necessary to cover the deficit be transferred from the statutory budget reserve fund to the general fund.⁶ Appropriations from the statutory budget reserve fund require only a majority vote. If HB 256 becomes law, no money will remain in the constitutional budget reserve fund.

Appropriations to the Earnings Reserve Account

The appropriation of non-income money to the earnings reserve account in HB 256 poses a novel issue not yet resolved by the Alaska Supreme Court. By co-mingling money from the constitutional budget reserve fund that came from sources other than the permanent fund, as well as money from royalties, with income from the permanent fund in the earnings reserve account, the governor risks two constitutional restrictions: the restrictions on the use of the permanent fund in art. IX, sec. 15, Constitution of the State of Alaska, as well as the sweep in art. IX, sec. 17(d), Constitution of the State of Alaska. The attorney general has in the past concluded that once money is deposited in the permanent fund, the money may only be used for income producing investments and the legislature may not, even if the deposits exceeded the constitutional requirement and were made with the intent that they be retrievable, transfer the money out of the permanent fund.⁷

⁴ HB 256, sec. 27(c), page 69, lines 24 - 25.

⁵ HB 256, sec. 28(a), page 69, lines 26 - 28.

⁶ HB 256, sec. 28(b), page 69, line 29 through page 70, line 2.

⁷ "It could be possible, one might argue, for the legislature to make appropriations to the fund by law and specify [sic] 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.

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 provision of section 15 that it is void. Either there is a permanent fund or there is not." August 31, 1977, Inf. Op. Att'y Gen., File No. J-66-106-78.

As you know, the earnings reserve account is part of the permanent fund⁸ and is currently used to pay dividends, not to fund operating expenses of the state. If the legislature were to begin using the earnings reserve account like any other account in the general fund, by depositing money from sources other than the permanent fund earnings, and by appropriating money from the account for general operating expenses, a court may find that the earnings reserve account should no longer be characterized as an account in the permanent fund, but as an account in the general fund, which is not otherwise described in statute. If that is the case, the non-income appropriations to the earnings reserve account may be vulnerable.

The Constitutional Sweep

Based on the governor's proposal, another issue becomes whether money appropriated to the earnings reserve account, other than income from the permanent fund, is subject to the sweep provision of the constitutional budget reserve fund under art. IX, sec. 17(d), Constitution of the State of Alaska. The Supreme Court has considered the application of the sweep provision and concluded that the use of the phrase "available for appropriation" in that subsection has the same meaning as the phrase has in the other subsections of art. IX, sec. 17, except that the sweep applies only to money "available for appropriation" that is also "in the general fund," and, therefore excludes funds that are outside of the general fund. The Court specifically found the earnings reserve account to be "subject to appropriation" but outside of the general fund and protected from the sweep.⁹

In *Hickel v. Cowper*, the Supreme Court, noted:

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 sec. 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.^[10]

Nowhere in the constitution or in statute is "general fund" defined. The Court, in *Hickel*, decided that the constitutionally created permanent fund, together with its earnings reserve account, is outside the general fund. Presumably, the constitutionally created budget reserve fund would also be considered to be outside the general fund. In any case,

⁸ "The earnings reserve account is established as a separate account in the fund." AS 37.13.145.

⁹ See *Hickel v. Cowper*, 874 P.2d 922, n. 32 (Alaska 1994).

¹⁰ *Hickel*, 874 P.2d at n. 32.

under the literal holding of the case, money in the earnings reserve account in the permanent fund is not subject to the sweep into the constitutional budget reserve fund.

However, caution is warranted. The Court did not specifically consider, in *Hickel*, the status of general fund money placed into the earnings reserve account. If faced with the question of whether an amount appropriated to the earnings reserve account, distinct from permanent fund income, is also protected from the sweep, the Court might narrow its holding in *Hickel*. In short, the Court could decide that its holding applies to the earnings reserve account that consists only of permanent fund earnings and does not include other appropriated money, as that account is described by the Court itself in *Hickel*:

This fund is established as a separate account within the permanent fund under the authority of the last sentence of Article IX, sec. 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.*^[11]

Because *Hickel* did not anticipate general fund money passing through the earnings reserve fund, it is possible that, if confronted with the issue, the court would find that only the portion of the earnings reserve account that consists of income from the permanent fund is protected from the sweep. Otherwise, of course, the legislature could simply, by statute, place much or all of the state general fund revenue into that account as a device to evade the constitutional sweep provision, a prospect the court may not find acceptable.

In order to prevent the sweep from including amounts appropriated to the earnings reserve account, either appropriated amounts are already protected from the sweep under the reasoning of the *Hickel* case, which seems unlikely to me, or those amounts can only be protected from the sweep through an amendment to the state constitution. If the amounts are already protected from the sweep under the reasoning of the *Hickel* case, money appropriated to the earnings reserve account under the proposal in HB 256 could not be swept back into the constitutional budget reserve fund. If, however, the amounts appropriated to the earnings reserve account in HB 256 are deemed "sweepable," then some -- or all -- of the funds in the earnings reserve account may be deemed subject to the constitutional sweep, and a supermajority vote would be required to do a reverse sweep or otherwise appropriate the funds out of the constitutional budget reserve fund under art. IX, sec. 17(c), Constitution of the State of Alaska.

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¹¹ *Hickel*, 874 P.2d at 934. (Emphasis added.)