

**ALASKA STATE LEGISLATURE  
HOUSE EDUCATION STANDING COMMITTEE**

March 13, 2015

8:05 a.m.

**MEMBERS PRESENT**

Representative Wes Keller, Chair  
Representative Paul Seaton  
Representative Harriet Drummond  
Representative Jonathan Kreiss-Tomkins

**MEMBERS ABSENT**

Representative Lora Reinbold, Vice Chair  
Representative Jim Colver  
Representative Liz Vazquez

**OTHER LEGISLATORS PRESENT**

Representative Daniel Ortiz  
Representative Sam Kito III

**COMMITTEE CALENDAR**

BRIEFING ON THE KETCHIKAN GATEWAY BOROUGH LAWSUIT

**PREVIOUS COMMITTEE ACTION**

No previous action to record

**WITNESS REGISTER**

REBECCA HATTON, Assistant Attorney General  
Labor and State Affairs Section  
Department of Law  
Juneau, Alaska

**POSITION STATEMENT:** Presented a briefing regarding the Ketchikan Gateway Borough v. State of Alaska lawsuit.

KATE VOGEL, Assistant Attorney General  
Appellate Section  
Department of Law  
Anchorage, Alaska

**POSITION STATEMENT:** During the presentation offered comments and responded to questions.

## **ACTION NARRATIVE**

8:05:51 AM

**CHAIR WES KELLER** called the House Education Standing Committee meeting to order at 8:05 a.m. Representatives Drummond, Kreiss-Tomkins, Seaton, and Keller were present at the call to order. Also present were Representatives Kito and Ortiz.

### **Briefing on the Ketchikan School Lawsuit**

8:06:06 AM

CHAIR KELLER announced that the only order of business would be a briefing from the Department of Law regarding the Ketchikan Gateway Borough Lawsuit.

8:07:23 AM

REBECCA HATTON, Assistant Attorney General, Labor and State Affairs Section, Department of Law, advised the Ketchikan Gateway Borough filed suit against the State of Alaska in January 2014, regarding the Required Local Contribution (RLC), which is an element of Alaska's public school funding formula under the Alaska State Constitution. In February and March 2014, both parties to the case asked Superior Court Judge William Carey to grant summary judgment in their favor. She explained that summary judgment is granted when there are no issues of material fact to be resolved. While there was disagreement regarding the law, there were no contested facts as it was purely a question of law. The lawsuit was resolved in January 2014 as Judge Carey ruled on the cross-motions for summary judgment and issued final judgment on the matter in January 2015. She stated that Judge Carey's decision found in favor of the Ketchikan Gateway Borough as to one their constitutional claims, and in favor of the state as to several other constitutional claims, but ultimately the effect of the claim was to hold the RLC in violation of the Alaska State Constitution. She explained that in January the state requested Judge Carey to stay his ruling as the state had filed an appeal with the Alaska Supreme Court. In late February 2015, Judge Carey denied the state's request for a stay and when the state informed the Alaska Supreme Court regarding that development and requested the Alaska Supreme Court stay Judge Carey's ruling until the court had an opportunity to hear and decide the case, the Alaska Supreme Court granted that motion [March] 11, 2015.

8:10:49 AM

MS. HATTON continued and began to describe described the constitutional claims within the lawsuit. Again, she remarked, the challenge was to the RLC which requires municipalities to contribute toward the operation of its local school district at the equivalent of a 2.65 mill rate and statewide municipalities pay on average approximately 16 percent of the basic need costs of education in their local school districts. She explained that in FY2014 the Ketchikan Gateway Borough's RLC payment was approximately \$4.2 million, out of a total \$22.5 million in basic need for Ketchikan. The lawsuit claimed that the required contribution violated three separate constitutional provisions: Article XI, Section 7 the dedicated funds prohibition; Article IX, Section 13 the appropriation clause; and, Article II, Section 15 the governor's veto clause. She quoted Article XI, Section 7, as follows:

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 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.

8:12:37 AM

MS. HATTON continued that the purpose underlying the state's funds prohibition was to prevent ear marking as the intention was to prevent a situation where a new tax is created and the proceeds of that tax is dedicated or promised to a specific purpose or outcome. She conveyed that the intent of the framers was to maximize the legislature's ability to spend money where in its estimation it was needed at any given point in time. In order to determine whether or not the dedicated funds prohibition has been violated the Alaska court use a two-part test: whether the funds at issue are the proceeds of a state tax or license; and, whether there was a dedication to a special purpose. She related that the state made many arguments on this constitutional claim as the state's position was that the RLC is not a specific tax and is not state revenue. Judge Carey did not decide in favor of this claim and held the RLC does violate the dedicated funds prohibition. The other two constitutional claims, she said, the appropriations clause and governor's veto clause are interrelated as the appropriations clause concerns

the legislature's authority to appropriate funds whereas the governor's veto clause has to do with the governor's authority to either strike or reduce line items from an appropriation bill. Again, she explained, the state's claim, also relevant to the dedicated funds issue that the RLC is not state revenue, the state believed was fatal to the other two constitutional claims. The state argued that the legislative authority to appropriate funds is limited to funds that come within the state treasury, and that the governor's authority to strike or reduce appropriations is limited to appropriations that have been authorized by the legislature. She pointed out that the state's briefing argued that the RLC, which is collected by, deposited by, and appropriated by the borough's treasury as opposed to the state, therefore, the required local contributions did not violate either the governor's line item veto or the appropriations clause. As to these two points, Judge Carey sided with the state dismissing both of the constitutional claims.

[8:15:13 AM](#)

MS. HATTON continued that the Ketchikan Gateway Borough made a claim in assumpsit, which is a common law action for the recovery of damages with the intentionality to basically correct situations where a party has been unjustly enriched. Essentially, she remarked, Ketchikan Gateway Borough was asking for a refund. She stated that prior to the litigation and during the pendency of the litigation the Ketchikan Gateway Borough made its RLC in FY13 and FY14, but did so with letters advising they were doing so but under protest and would like its money back should their claim be granted. Judge Carey denied this claim and said that the state had not been unjustly enriched largely because the RLC never becomes state revenue and never comes within the power of the state treasury. Basically, she advised, Judge Carey's order found that the RLC was unconstitutional as violating the dedicated funds prohibition, and not in violation of either the appropriation's clause or the governor's veto clause and finally, Ketchikan Gateway Borough's request for repayment of prior RLC payments was denied. As a result of the stay issued by the Supreme Court, the state at this point can continue to enforce the public school funding formula as it was written in statute. She thanked the committee for their time as it is important for the legislature to understand the issues raised. She related that the state is very confident in its legal arguments but it is certainly possible the Alaska Supreme Court could come to Judge Carey's conclusion and were that situation to come to pass, it would be

an issue requiring considerable attention from the legislature in the future.

[8:17:36 AM](#)

REPRESENTATIVE SEATON pointed out that the January 11 date should have been March 11.

MS. HATTON agreed.

[8:17:52 AM](#)

CHAIR KELLER asked for information, at a later date, as to the real impact to the general fund should the state lose the issue.

[8:18:22 AM](#)

REPRESENTATIVE SEATON questioned that if the judge decided that it was a tax, and it was dedicated to a special purpose, therefore, it didn't violate the appropriations or veto clause. He asked whether the state is arguing it wasn't a tax required by the state, or it wasn't a state tax.

MS. HATTON responded that essentially the state argued it was dispositive, that the money didn't come within the power of the state treasury. Although, Judge Carey thought differently and through the distinction he drew was able to come to his conclusions.

[8:19:24 AM](#)

KATE VOGEL, Assistant Attorney General, Appellate Section, Department of Law, added that Judge Carey's decision did not find it to be significant that the money was locally raised money and locally allocated. She explained that was a distinction the state drew and anticipates will continue to draw on appeal from previous dedicated funds cases. Judge Carey did not agree and distinguished between the application of the dedicated funds clause and not the application of the appropriation or the governor's veto clause.

[8:20:33 AM](#)

REPRESENTATIVE KITO referred to the decision by Judge Carey that appears to identify the tax or a license can be local, and asked whether there is a requirement that the funding the local government's pay come from a tax or license. Theoretically, he

questioned, whether there could be a municipality that has an endowment and uses those earnings to pay this local contribution and it wouldn't be a tax on the citizens of the local government.

[8:21:19 AM](#)

MS. VOGEL answered yes, the state made that argument as the statute gives an amount that the RLC is and states that amount as being the equivalent of a mill rate. Nothing in the statutes dictate how a local community should raise that money and it doesn't have to be a tax. Judge Carey did not accept that argument but it was certainly a part of the state's position, she maintained.

REPRESENTATIVE KITO commented that with regard to the impact to the general fund and opined the amount of local contribution currently is approximately \$220 million which represents the total amount all municipalities contribute to education.

[8:22:43 AM](#)

REPRESENTATIVE KREISS-TOMKINS surmised that if the Supreme Court granted a stay presumably it will take up the case and rule.

MS. HATTON agreed, and advised that both sides have launched appeals and in fact has a scheduling conference this afternoon to determine due dates with the Supreme Court. She expects the Supreme Court, based on the short order it issued in granting the stay, intends to deal with the case in an expedited fashion.

REPRESENTATIVE KREISS-TOMKINS asked her opinion as to the timeline for the Supreme Court.

MS. HATTON replied that she would not speculate and will keep the committee apprised, but the Supreme Court is within its authority to take any length of time it deems sufficient.

[8:24:14 AM](#)

CHAIR KELLER questioned that should the Supreme Court agree, will the local school district be short that money. Or, is there a clear implication that it goes back to the general fund.

MS. HATTON responded that she will not speculate what the Supreme Court might rule, but would draw the committee's attention to the fact that although the Ketchikan Gateway

Borough did not clearly challenge the RLC under the education clause, they did include arguments that the state had somehow abdicated its responsibility to fully fund education. Judge Carey clearly decided that the state does not have an obligation to fully fund education, she explained.

CHAIR KELLER asked her comments as to the implications regarding impact aid.

MS. HATTON offered that is an area of concern as Alaska is deemed to have an equalized funding formula for purposes of federal impact aid. As such, she put forward, it is allowed to take into account 90 percent of the impact aid payments made to districts, which amounts to an approximate offset of state education funding of \$69-70 million annually. She said it would be speculation to say if any revised formula would be passed by the legislature in the future, as it is an open question whether or not it would be considered equalized by the Federal Division of Impact Aid.

CHAIR KELLER pointed out that those questions highlight what the legislature is up against.

[8:26:32 AM](#)

REPRESENTATIVE KITO asked whether a decision in this case impact other payments the legislature might require from a municipality, such as a first contribution or a match for a capital project.

MS. VOGEL answered yes, a dedicated funds decision from the Supreme Court in this arena, particularly if it adopted an analysis similar to that of Superior Court, could have further reaching implications for other matching grant programs or other times when the state mandates a local entity put in some money in exchange for access to state funds. That is something the state would argue would be an extension of the way the dedicated funds clause has been interpreted in the past. She opined that how much of an impact the decision has would depend on what the Supreme Court decides and words its decision. Certainly, she pointed out, the dedicated fund provision has implications beyond the education arena so the state's position has been one of trying to highlight to the court all of the implications of ruling that this is a dedicated fund.

[8:28:26 AM](#)

REPRESENTATIVE SEATON questioned whether the discussion is regarding the 70/30 reimbursement rate for debt incurred be implicated in this.

MS. HATTON responded that it was an area of concern, not specifically 70/30 grants, but other joint municipal state participation type programs currently in statute which was a significant part of the state's argument in the lower court. She said that it was an area of concern for the state and that that sort of joint participation program could be endangered by an expansive interpretation of the dedicated funds provision encompassing the RLC, and it remains to be seen how the Supreme Court will decide or word a ruling.

REPRESENTATIVE SEATON inquired whether the PERS participation is one of the issues the state is arguing would be an expansion.

MS. HATTON replied that it was not a particular area highlighted in the state's briefing to the lower court, and as to the briefing to the Supreme Court they "haven't done it yet."

[8:45:10 AM](#)

REPRESENTATIVE ORTIZ requested a summary of the three parts of the constitution that the Ketchikan Gateway Borough based its lawsuit upon and how they relate to the case.

MS. HATTON responded that the first constitutional claim was the dedicated funds provision and constraint against ear marking of identifying a particular source of income to the state and tying it to a particular outgoing source or project. Its connection to this case was that the Ketchikan Gateway Borough argued that the reprisal for contribution violates that constitution provision. The appropriations clause and the governor's veto power had to do with the legislature's ability to approve appropriations, and the governor's ability to use his line item veto power. She explained that the Ketchikan Gateway Borough contends this was a dedicated fund thereby implicating the other two clauses because if the conclusion was that it was a state tax, the fact that the money moved directly from municipalities to local school district. She remarked that the Ketchikan Gateway Borough's argument was that it somehow violated both of those constitutional provisions by unconstitutionally skirting the respective power of the legislature and governor.

REPRESENTATIVE ORTIZ surmised that Judge Carey ruled against Ketchikan Gateway Borough on those last two point.

MS. HATTAN answered correct.

[8:32:03 AM](#)

REPRESENTATIVE SEATON referred to the appeal and asked whether all three issues are being appealed or just the dedicated funds portion.

MS. HATTAN responded that it is everything. Initially the state appealed the point on which they lost, the dedicated funds prohibition and then Ketchikan Gateway Borough cross-appealed the other two constitutional claims as well as its assumpsit claim.

[8:32:41 AM](#)

REPRESENTATIVE DRUMMOND asked whether the state considered what other states do in terms of education funding. For example, Alaska's school districts are dependent school district as they rely upon local governments and the state to provide funding. She pointed out that many states have independent school districts that require a local tax contribution from its citizens and go to the citizens for its tax portion and capitol funds. She opined that she can see this turning Alaska into a different sort of structure in terms of how its school district function. In the event the state loses, she offered, and school districts have to find another source of revenue, it could turn them into independent school districts looking to their local governments for taxes directly and going to the local ballot.

CHAIR KELLER said he would like to know whether that was part of the court's consideration.

[8:34:43 AM](#)

MS. HATTAN advised that the state's focus was quite limited in the sense that its goal was defending the legality of Alaska's system as it currently exists.

The legislature has, within the confines of what the education clause requires, essentially plenary power to decide what education is going to look like in the State of Alaska. She explained that the Department of Law considered it task because there were and continue to be good legal defenses of Alaska's current system. Their goal was to legally defend the current system which puts the legislature in a better position to come

at this issue from a policy perspective and decide what is best for the state.

[8:35:37 AM](#)

MS. VOGEL added that one other consideration on that issue is before statehood school districts had independent taxing authority and they initially paid for their schooling and requested refunds from the territory, but currently the constitution does not give school districts taxing authority. She said the state and municipalities have taxing authority, for example, the school districts in unorganized Alaska do not have taxing authority. In terms of how it works now, the tools Alaska has at its disposal for funding schools is state aide, aide raised from municipalities through RLC and how it chose to access that money, and federal aid are the main sources. She offered that the Department of Law is aware of how much state aid Alaska schools receives and presented evidence to the court regarding how Alaska follows with respect to other states. She agrees with Ms. Hatton that the focus in the litigation is the legality of the RLC in light of the dedicated funds provision.

[8:37:22 AM](#)

REPRESENTATIVE DRUMMOND surmised that "let's figure this out first before we worry about what is going on down the road." She noted it sounds like it would take a constitutional amendment to change the funding source for schools.

MS. VOGEL responded that it is not specifically being litigated yet so no need to go there, and did not want to speculate for need for a constitutional amendment to change things one way or another.

[8:38:06 AM](#)

REPRESENTATIVE SEATON said that the state requires all municipality boroughs to use 100 percent fair market assessed valuations. In the event there is a dedicated funds problem couldn't the state impose a 3.65 mill tax on all assessed valuations in the state and give it to the general fund. Then, he remarked, as the legislature appropriates money it can fund education as it sees fit, and oil and gas properties are separately assessed so it is in a different category. He questioned whether that is the logical response if it is a dedicated funds problem.

MS. HATTAN answered that it would certainly be a solution available to the legislature, but she wouldn't speculate on the parameters of what the Supreme Court might rule in the future. In the state's briefing to the lower court emphasized the benefit to local school districts in the sense that the money isn't deposited into the general fund and is allocated directly from municipalities to its local school districts and all of the money goes directly to that purpose. Therefore, they felt there was significant benefits to individual school district to have the RLC implemented the way it is written now, she stated.

REPRESENTATIVE SEATON clarified he was asking whether there is anything prohibiting the state from having a property tax at whatever millage rate it decides based upon 100 percent fair market valuation which is what is required of all assessments.

MS. HATTAN replied that nothing she is aware of and deferred to Ms. Vogel.

[8:40:11 AM](#)

MS. VOGEL agreed that it would be a possible solution and she is not aware of any constitutional problems. Certainly, she pointed out, the manner it was described the idea of a state imposed tax being deposited in the general fund and not pledged to schools would seem to be permissible under the dedicated funds clause no matter what the court decides about the status quo and the current way the state does it.

CHAIR KELLER said it is a discussion the committee may or may not get into in the future.

[8:41:01 AM](#)

REPRESENTATIVE ORTIZ inquired as to whether Ketchikan Gateway Borough argued it was unequitable treatment and integrate that into different Articles in the Alaska State Constitution between how students in borough areas are funded by the state versus students in non-borough areas.

MS. HATTAN answered it did not.

[8:42:25 AM](#)

REPRESENTATIVE SEATON commented that the current system is better as the prior system caused a problem between equities and different parts of the state. He opined Alaska does not have a

problem other than the will to determine there will be a property tax at whatever mill rate across the state. He said that it is basically what the state does by requiring a local contribution at the 3.65 level, and it does not appear the legislature is in a box. He explained it would mean a change in the system as it would go to the general fund and the appropriation and veto clauses would be available. Although, he remarked, he is worried about the lawsuit and redoing the system, it appears there are mechanisms without totally turning over the way in which districts are organized and taxed. He pointed out that a fairly simple solution is that the state could either keep it the same level or go back to the previous formula if there are funding problems for local school districts.

CHAIR KELLER pointed out that it may be an anticipated discussion in the future.

[8:45:03 AM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Education Standing Committee meeting was adjourned at 8:45 a.m.