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HOUSE COMMITTEE REPORT

CORRECTED

11)
Date Referred: April 24, 1990

FURTHER REFERRALS:

Date of Committee Action: 5/3/90

The FINANCE Committee considered:

CSSB 136(2d rls)

CS SB NO. 136 (2d Rules)

EDUCATION TRUST FUND

"An Act establishing the Alaska education trust fund and authorizing advance tuition payment contracts; and providing for an effective date."

RECOMMENDATIONS:

- be replaced with HCS CSSB 136 (FIN) the same title
- a new title
- have attached amendment(s)
- do pass
- do not pass
- no recommendation
- individual recommendations
- additional referral to the _____ Committee

ADOPTS: _____ letter of intent

ATTACHES NEW FISCAL NOTE(S):
(Dept)

APPROVES PREVIOUS:

(Date/Dept)

- 3 fiscal impact 2 Rev, HFC
- zero fiscal note _____
- zero with analysis _____

- fiscal note(s) _____
- zero fiscal note(s) _____
- zero fn/analysis _____

SIGNING DO PASS:

SIGNING:

(Check approp. column)

Do Not Pass No Rec Amend

Ronald J. Larson Larson

Clay Swackhammer Swackhammer

Fay Brown Brown

Thompson KOPONEN

Signature	Do Not Pass	No Rec	Amend
<u>Phillips</u> Phillips		<input checked="" type="checkbox"/>	
<u>Barnes</u> BARNES		<input checked="" type="checkbox"/>	

Chairman's Signature
Ronald J. Larson LARSON

FISCAL NOTE **R/O HFC 5-3-90**

REQUEST

Revision Date: May 3, 1990
Title: An Act establishing the Alaska education trust fund
Sponsor: KERTTULA, Kelly, et al
Requestor: House Finance

Agency Affected: Revenue
BRU: Permanent Fund Dividend Division
Components: Permanent Fund Dividend Division

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
OPERATING						
PERSONAL SERVICES	24.1	11.9	11.9	11.9	11.9	11.9
TRAVEL	-0-	-0-	-0-	-0-	-0-	-0-
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	0.2	0.2	0.2	0.2	0.2	0.2
EQUIPMENT	-0-	-0-	-0-	-0-	-0-	-0-
LANDS & STRUCTURES	-0-	-0-	-0-	-0-	-0-	-0-
GRANTS, CLAIMS	-0-	-0-	-0-	-0-	-0-	-0-
MISCELLANEOUS	-0-	-0-	-0-	-0-	-0-	-0-
TOTAL OPERATING	29.3	17.1	17.1	17.1	17.1	17.1
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND	29.3	17.1	17.1	17.1	17.1	17.1
FEDERAL FUNDS	-0-	-0-	-0-	-0-	-0-	-0-
OTHER	-0-	-0-	-0-	-0-	-0-	-0-
TOTAL	29.3	17.1	17.1	17.1	17.1	17.1

POSITIONS:

FULL-TIME	-0-	-0-	-0-	-0-	-0-	-0-
PART-TIME	3	2	2	2	2	2
TEMPORARY	-0-	-0-	-0-	-0-	-0-	-0-

ANALYSIS: See Attached.

Prepared By: Ervin Jones
Division: Permanent Fund Dividend Division

Phone: 465-2323
Date: May 3, 1990

Approved by Commissioner: [Signature]
Agency: Revenue

Date: 5/4/90

Distribution (by preparer):
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

Department of Revenue
Permanent Fund Dividend Division
Fiscal Note Analysis
HCS CS SB 136 (FIN)
May 3, 1990

Assumptions:

1. The bill will take effect for the 1991 permanent fund dividend year and application or later. The 1990 dividend application has already been printed and distributed.
2. There are other bills which if signed into law, would result in some form of "check-off" on the 1991 dividend application. The Department of Revenue has no insight as to which, and how many, of these bills will become law. This fiscal note is prepared on the assumption that the subject bill is the only bill of this nature which will become law. The passage of multiple bills with varying formulas will inevitably have a compounding effect. Whereas there may be savings in some areas, there will be increased costs in others.
- 3) Funding for the administrative costs of the Permanent Fund Dividend program in providing the mechanism for contributions from the General Fund as appropriated by the legislature.
- 4) The incremental cost of computer resources will result in a chargeback by the Department of Administration.
- 5) Whereas the cost of programming changes will be a one-time cost, the cost of document review, data capture and the data processing chargeback will be continuing.
- 6) Contributions will only be honored to the extent of available funds. Garnishments and assignments will take precedence in the order established by statute.
- 7) The Permanent Fund Dividend will electronically transfer contributions to the trust fund account, but will have no involvement in the management or accounting duties associated with the trust account. Such duties, including liaison with the Board of Regents, will be by the Treasury Division, Department of Revenue.

Department of Revenue
Permanent Fund Dividend Division
Fiscal Note Analysis
HCS CS SB 136 (FIN)
May 3, 1990

Program Summary:

The provision of a new contribution decision on the dividend application will cause additional administrative cost in several areas:

- a) The computer system will need to be changed to account for the change in the program, to establish new accounting controls and to provide for the transfer of funds to the trust account.
- b) Each of approximately 525,000 PFD applications will need to be visually reviewed and coded as to decision on the contribution decision. Each application will be data captured with additional attention and keystrokes expended on each positive decision.

1. Positions

	<u>FY 91</u>	<u>FY 92</u>
1 PPT Analyst/Programmer V, R21 @ \$6,110.86/Mo including salary and benefits for 2 months	= \$12.2	

PCN 04-1125 would be funded for an additional two months, in accordance with Attachment A. Ongoing maintenance of new programs would be accomplished by existing staff.

1 PPT Document Processor I, R7 @ \$2,340.37/Mo, including salary and benefits for 3 months	=	\$7.0	\$7.0
--	---	-------	-------

This position would assist in the manual review and coding of 525,000 applications for the new contribution decision. This position represents the equivalent of the additional time and effort.

Department of Revenue
 Permanent Fund Dividend Division
 Fiscal Note Analysis
 HCS CS SB 136 (FIN)
 May 3, 1990

	<u>FY 91</u>	<u>FY 92</u>
1 PPT Data Processing Clerk I, R8, @ \$2,446.08/Mo, including salary and benefits for 2 months =	\$4.9	\$4.9

This position would assist in the data capture of the additional contribution decision. The position represents the equivalent value of the additional time and effort.

TOTAL Personal Services	\$24.1	\$11.9
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2. Other Expenditures:

a) Travel:	\$0.0	\$0.0
b) Contractual:		
Data Processing Chargeback	\$5.0	\$5.0
c) Supplies:	\$0.2	\$0.2
d) Equipment: Use existing equipment	<u>\$0.0</u>	<u>\$0.0</u>
TOTAL COST	<u>\$29.3</u>	<u>\$17.1</u>

Suggested Amendments:

1. Consider removing the check-off provision.

Attachments: Attachment A: "Summary of DP Needs"

Department of Revenue
Permanent Fund Dividend Division
Fiscal Note Analysis
HCS CS SB 136 (FIN)
Summary of Data Processing Requirements
May 3, 1990

<u>Wang data entry processing</u>	75.0 hours
Includes: Data entry	
Batch lists	
Corrections	
Wang to IBM transfer	
<u>IBM Update jobs</u>	30.0 hours
Includes: Edits	
Batch listings	
Log sheets	
<u>DMS Online programs for lookup and changes</u>	37.5 hours
<u>Nightly Update of Changes</u>	22.5 hours
<u>Warrant Jobs</u>	90.0 hours
Includes: Printing warrants with different amounts. Include check stub messages. Modify warrant registers as needed for balancing. Create new program(s) for transferring accumulated decisions to trust account and to account for the reserve necessary due to returned and cancelled PFD warrants.	
<u>Miscellaneous</u>	45.0 hours
Includes: Setting up test files on IBM Systems testing Administrative functions, i.e. paper work required by Admin. DP to add files and programs to tables.	
TOTAL HOURS	300.0 hours

2/0 HFC 5-3-90

STATE OF ALASKA
1990 LEGISLATIVE SESSION

Bill Version: HCS SB 136 (FIN)
Publish Date: _____

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: Alaska education trust fund
Sponsor: House HESS
Requestor: House Finance

Agency Affected: Department of Revenue
BRU: Treasury
Components: _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
OPERATING						
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	46.0	87.0	131.0	179.0	235.0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LANDS & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	0	46.0	87.0	131.0	179.0	235.0
CAPITAL	0	0	0	0	0	0
REVENUE	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER	0	46.0	87.0	131.0	179.0	235.0
TOTAL	0	46.0	87.0	131.0	179.0	235.0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS: attach a separate page for analysis. FY 90 fiscal effect is zero.

Prepared By: Milt Barker MB
Division: Treasury

Phone: 465-2350
Date: May 3, 1990

Approved by Commissioner: Milton B. Barker for
Agency: Department of Revenue

Date: 5-3-90

Distribution (by preparer):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

Alaska Education Trust Fund
Investment Management Expenses

	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	(\$000)						
Age	<u>Earnings</u>	<u>Ending Balance</u>	<u>Securities Safekeeping Fees</u>	<u>Common Stock Management Fees</u>	<u>Performance Measurement Fees</u>	<u>Audit</u>	<u>Total Fees</u>
0	0	0	0	0	0	0	0
5	1	26	1	23	12	10	46
1	3	53	2	63	12	10	87
3	5	82	4	105	12	10	131
3	8	116	5	152	12	10	179
3	11	155	7	206	12	10	235

anent Fund, December 1989

dividend receipts; initial participation in a similar Florida program was

fer to trust fund occurs on average on November 15; also assumes no payouts

location to common stocks

R/O HFC 5-3-90

STATE OF ALASKA
1990 LEGISLATIVE SESSION

BILL VERSION: HCS GSSB 136 (FIN)
PUBLISH DATE: _____

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: Alaska Education Trust Fund

Agency Affected: University of Alaska
BRU: Statewide Programs & Services

Sponsor: Senator Kerttula
Requestor: _____

Components: _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
PERSONAL SERVICES		62.4	62.4	62.4	62.4	62.4
TRAVEL						
CONTRACTUAL	5.0					
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	5.0	62.4	62.4	62.4	62.4	62.4

CAPITAL						
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REVENUE						
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FUNDING: (Thousands of Dollars)

GENERAL FUND	5.0	62.4	62.4	62.4	62.4	62.4
FEDERAL FUNDS						
OTHER						
TOTAL	5.0	62.4	62.4	62.4	62.4	62.4

POSITIONS:

FULL-TIME	0	1	1	1	1	1
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

Prepared by: House Finance Committee Phone: 465-3727
Division: Co-Chairman Ron Larson *Ronald Larson* Date: _____

Approved by Commissioner: Co-Chairman Lyman Hoffman *Lyman Hoffman* Date: _____
Agency: _____

Distribution (by preparer):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

12 G-11  E GENT 5/5 6-0557R Pulce

Original sponsor(s): SEN. KERTTULA, Kelly, Sturgulewski, Eliason, Faiks, Rodey, Binkley, Duncan, Frank, Fischer, Jones, Pearce, Coghill, Zharoff, Szymanski

1 IN THE SENATE

BY THE FINANCE COMMITTEE

2 HOUSE CS FOR CS FOR SENATE BILL NO. 136 (Finance)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 SIXTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act establishing the Alaska education trust fund
7 and authorizing advance tuition payment contracts."

8 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9 * Section 1. AS 14.40 is amended by adding new sections to read:

10 ARTICLE 6. ALASKA EDUCATION TRUST FUND.

11 Sec. 14.40.803. ALASKA EDUCATION TRUST FUND ESTABLISHED. (a)

12 The Alaska education trust fund is established as an endowment trust
13 fund separate from the general fund. The fund may be divided into
14 separate accounts for accounting purposes.

15 (b) The fund consists of

16 (1) permanent fund dividend and cash contributions made
17 under AS 14.40.807 under the terms of an advance tuition payment
18 contract;

19 (2) gifts, bequests, and contributions of cash or other
20 assets from a person; and

21 (3) income and earnings of the fund.

22 (c) Assets of the fund shall be expended in the following order
23 of priority:

24 (1) to make payments to the university on behalf of quali-
25 fied beneficiaries;

26 (2) to make refunds upon termination of an advance tuition
27 payment contract;

28 (3) to pay the costs of administration of the fund.

29 Sec. 14.40.805. POWERS AND DUTIES OF THE COMMISSIONER OF

1 REVENUE. The commissioner of revenue is the trustee of the fund and
2 has the powers and duties under this section to

3 (1) act as official trustee of the cash and investments
4 belonging to the fund and to secure adequate and safe custodial facil-
5 ities;

6 (2) receive all items of cash and investments belonging to
7 the fund;

8 (3) collect the principal and income from investments
9 acquired by the trustee and deposit the amounts in separate principal
10 and income accounts for the fund;

11 (4) invest and reinvest the assets of the fund as provided
12 in this section and as provided for the investment of retirement funds
13 under AS 14.25.180;

14 (5) exercise the powers of a trustee with respect to the
15 assets of the fund;

16 (6) do all acts, whether or not expressly authorized, that
17 the commissioner of revenue considers necessary or proper in adminis-
18 tering, as a trustee, the assets of the fund;

19 (7) maintain accounting records of the fund in accordance
20 with investment accounting principles and with distinction between the
21 principal and income accounts of the fund;

22 (8) engage an independent firm of certified public accoun-
23 tants to annually audit the financial condition of the fund's invest-
24 ments and investment transactions;

25 (9) enter into and enforce contracts or agreements con-
26 sidered necessary for the investment purposes of the fund;

27 (10) report to the university the condition and investment
28 performance of the fund;

29 (11) make payments to the university on behalf of qualified

1 beneficiaries;

2 (12) make refunds upon termination of an advance tuition
3 payment contract; and

4 (13) pay the costs of administration of the fund.

5 Sec. 14.40.807. CONTRIBUTION TO THE ALASKA EDUCATION TRUST FUND.

6 (a) Contributions to the fund under the terms of an advance payment
7 contract may be made by direct cash payments or by contributions from
8 the permanent fund dividend. The Department of Revenue shall

9 (1) prepare the permanent fund dividend application to
10 allow an applicant, or a parent, legal guardian, or other authorized
11 representative of an applicant who is an unemancipated minor to con-
12 tribute 50 percent of a dividend to the fund under the terms of an
13 advance tuition payment contract; and

14 (2) include with each application for a permanent fund
15 dividend an explanation of the trust fund, including the right of a
16 purchaser to receive a refund upon termination of an advance tuition
17 payment contract, and a statement that the tax liability of the fund
18 has not yet been determined; after the Internal Revenue Service deter-
19 mines the tax liability of the fund, a statement summarizing the tax
20 determination shall be included with each application for a permanent
21 fund dividend.

22 (b) The Department of Revenue shall pay contributions directly
23 to the fund.

24 Sec. 14.40.809. POWERS AND DUTIES OF THE UNIVERSITY OF ALASKA.

25 (a) The Board of Regents of the University of Alaska may contract
26 with a purchaser for the advance payment of tuition by the purchaser
27 for a qualified beneficiary of any age to attend a branch of the
28 university to which the qualified beneficiary is admitted, without
29 further tuition cost to the qualified beneficiary. A purchaser and a

1 qualified beneficiary may be the same person.

2 (b) The board shall

3 (1) make appropriate arrangements as necessary to fulfill
4 the board's obligations under an advance tuition payment contract;

5 (2) establish standard payment plans to be used under
6 advance tuition payment contracts;

7 (3) establish the circumstances under which an advance
8 tuition payment contract may be terminated and the amount of the
9 refund the person entitled to terminate the contract may receive.

10 Sec. 14.40.811. ADVANCE TUITION PAYMENT CONTRACTS. (a) An
11 advance tuition payment contract must include

12 (1) the amount of payments required from the purchaser on
13 behalf of the qualified beneficiary;

14 (2) the terms and conditions for making the payments;

15 (3) provisions for late payment charges and for default;

16 (4) the name and age of the qualified beneficiary under the
17 contract and a statement that the purchaser, with the approval of the
18 board, may substitute another person for the qualified beneficiary
19 originally named in the contract;

20 (5) the number of credit hours to be provided to the quali-
21 fied beneficiary under the contract;

22 (6) the name of the persons entitled to terminate the
23 contract, the terms and conditions under which the contract may be
24 terminated, and the amount of the refund to which the person terminat-
25 ing the contract is entitled;

26 (7) the assumption of a contractual obligation by the board
27 to provide for credit hours of higher education at the university;

28 (8) the number of credit hours the qualified beneficiary
29 may receive if the qualified beneficiary is not entitled to in-state

1 tuition at the time of enrollment at the university;

2 (9) the period of time during which the qualified benefi-
3 ciary may receive the benefits of the contract; and

4 (10) other terms and conditions the board determines to be
5 appropriate.

6 (b) An advance tuition payment contract may be terminated

7 (1) if the qualified beneficiary dies or becomes so dis-
8 abled that the beneficiary cannot complete an education;

9 (2) if the qualified beneficiary is not admitted to a
10 branch of the university after making a proper application;

11 (3) if the qualified beneficiary certifies to the board,
12 after the contracted date of entrance to the university or after the
13 qualified beneficiary has received a high school diploma or reached
14 the age of majority, that the qualified beneficiary has decided not to
15 attend the university;

16 (4) if the board determines that the number of purchasers
17 is insufficient to maintain the fund on an actuarially sound basis; or

18 (5) under other circumstances determined by the board and
19 set out in the advance tuition payment contract.

20 Sec. 14.40.817. DEFINITIONS. In AS 14.40.803 - 14.40.817,

21 (1) "advance tuition payment contract" means a contract
22 entered into by the board and a purchaser to provide for the higher
23 education of a qualified beneficiary;

24 (2) "board" means the Board of Regents of the university;

25 (3) "fund" means the Alaska education trust fund estab-
26 lished under AS 14.40.803;

27 (4) "purchaser" means a person who makes or is obligated to
28 make advance tuition payments under an advance tuition payment con-
29 tract;

1 (5) "qualified beneficiary" means a resident who has rights
2 under an advance tuition payment contract;

3 (6) "university" means the University of Alaska, including
4 a community college affiliated with the university.
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Attachment 2

5/2/90 am

<SB 136>

Amendment II

By Rieger

Page 4, Line 9:

DISCUSS

IN

SUBCOMMITTEE

Delete "An"

Insert "Subject to AS 14.40.012, an"

Page 5, Line 19, insert a new section to read:

"Sec. 14.40.012. ~~AMENDMENT~~ CHANGES TO ACHIEVE

TAX PREFERRED STATUS. ~~AMENDMENT~~

A term of an advance tuition payment contract

may ~~not~~ differ from the requirements of 14.40.011(a)(4),

14.40.011(a)(6), 14.40.011(b)(1), 14.40.011(b)(2), and

14.40.011(b)(3) if the variation is necessary in order

to achieve tax deferred or tax exempt status for

the Alaska education trust fund."

HEALTH, EDUCATION AND SOCIAL SERVICES COMMITTEE

ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES .

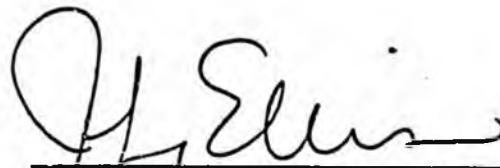


P.O. BOX V, JUNEAU 99811
(907) 465-3759

April 23, 1990

Letter of Intent to
HCSCSSB 136 (HESS)

It is the intent of the Legislature that the Department of Revenue request that the Internal Revenue Service determine if the income earned by the Alaska education trust fund established in section 1 of this Act is taxable income and to whom that income would be taxable under federal law.



Rep. Johnny Ellis, Chair
House HESS Committee



Official Business

Alaska State Legislature

SENATE

P.O. Box V
State Capitol
Juneau, Alaska 99811

MEMORANDUM

TO: Representative Ron Larson, Co-Chairman
House Finance Committee
Representative Lyman Hoffman, Co-Chairman
House Finance Committee

FROM: Senator Kerttula

SUBJ: Senate Bill 136 -- Educational Trust Fund

DATE: April 23, 1990

thanks - very much!

Day

I would appreciate your scheduling Senate Bill 136, relating to the Educational Trust Fund, at your earliest convenience.

As the cost of a college education steadily rises, parents have become increasingly concerned about their ability to provide a college education for their children. Because of this concern, many states have been looking at ways to provide parents and students with alternatives for financing college tuition.

Senate Bill 136 offers one such option. The legislation establishes a "guaranteed tuition plan" which assures future tuition payments to a University of Alaska campus upon an investment in a newly created Alaska Education Trust Fund. The bill provides for either a cash contribution or a set contribution of 50 percent of a permanent fund dividend, and allows an authorized representative of a minor to contribute 50 percent of his or her dividend.

The state would then invest the money, intending that, at a minimum, the tuition fund investments would have a rate of return that would equal the expected tuition cost for a child

Representative Larson
Representative Hoffman
April 23, 1990

by the time he/she enrolls in college. A contract would be made between the state and the purchaser that would guarantee tuition for a given number of credit hours at the University of Alaska, no matter how much the costs rise.

Senate Bill 136 has been modeled after a similar program which was adopted and implemented by the State of Michigan. When Michigan adopted its plan in 1986, 44,000 people applied during a two-month period. In Florida, approximately 40,000 people applied for a similar program.

While the option always exists for parents to place their money in other types of savings and investments, the guaranteed tuition plan offers low-cost tuition and assurances for the future.

Internal Revenue Service
Index Nos.: 0061-0000
0115-0000
2503-0000

Department of the Treasury

MAR 29 1988

Washington, DC 20224

Robert A. Bowman, Treasurer
State of Michigan,
Department of Treasury
Treasury Building
P.O. Box 15128
Lansing, MI 48901

MAR 29 1988

- A = the purchaser of a tuition contract
- B = the individual designated to receive the educational benefits described in a tuition contract
- C = the individual designated to received the refund benefits described in a tuition contract
- State X = Michigan
- Trust = the Michigan Education Trust

Dear Mr. Bowman:

This is in reply to a ruling request, submitted on behalf of State X, on the federal tax consequences of a college tuition prepayment program.

FACTS

State X has enacted legislation providing for a state-created corporation (Trust) to implement and administer a college tuition prepayment program. The program provides a choice of two plans for the payment of tuition. The substance of these two plans is described below.

Plan 1

Under the plan, A, an individual, makes a current payment to Trust, and in return, Trust contracts to arrange for four years of educational services at a State X public educational institution, or at a private educational institution within State X, for an irrevocably designated beneficiary, B, when B matriculates. The contract provides, however, that upon the occurrence of certain specified events a cash refund of the up-front payment, less an administrative fee, will be made to C, a person irrevocably designated by A at the time the contract is executed. B and C are related to A and the natural objects of A's affection. It is

Robert A. Bowman

represented that under the law of State X a parent is not under a legal obligation to provide a college education.

A cash refund only will be made if (1) B dies, (2) B is denied admission to a State X public educational institution, (3) B certifies that he or she has reached the age of 18 and will not attend a college or university, or (4) the tuition prepayment program administered by Trust is determined to be actuarially unsound. Refunds generally will be paid in four equal, annual installments. No refund will be provided if a beneficiary has completed more than one half the credit hours required by a State X educational institution for a bachelor's degree.

Trust is operated autonomously by a board of directors, and the board's decisions, including those involving investment discretion, may not be overridden by any state agency. The board consists of the Treasurer of State X and eight other persons appointed by the Governor of State X and approved by its legislature. The State X enabling legislation provides that funds collected by Trust are not subject to the claims of the creditors of State X and are not considered the money or common cash of State X. State X may not loan, transfer, or use Trust's funds for any purpose. Trust's funds may only be used for the tuition payment or refund purposes expressly provided in the enabling legislation. Income earned and property held by Trust are exempt from taxation under the laws of State X.

Plan 2

The facts are the same as in Plan 1, except that the plan provides for a cash refund that may be substantially in excess of A's up-front payment. The amount of the excess will be determined by an index tied to the increase in tuition costs of various State X institutions of higher education. The beneficiary may also attend an out-of-state educational institution for which State X will make a payment based on the same index as the refund computation.

ISSUES

(1) Is the excess of the fair market value of the educational services (or the cash refund) when received under the contract over the payment for the contract includible in the gross income of the beneficiary, B (or the refund designee, C), under section 61 of the Internal Revenue Code?

(2) Is the income of Trust, earned during the administration of the program, excludable from gross income as income earned by an integral part of State X or as income derived from the exercise of an essential governmental function that accrues to a state under section 115 of the Code?

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(3) Has A made a completed gift of the up-front payment for federal gift tax purposes at the time the tuition contract is purchased? If the purchase of the contract results in a completed gift, is the transfer excluded from the application of the gift tax under section 2503(e)(2)(A) of the Code as an amount paid as tuition to a qualifying educational organization? If the purchase results in a completed gift and is not excluded from gift tax liability under section 2503(e)(2)(A), does the transfer nevertheless qualify as a gift of a present interest in property eligible for the \$10,000 annual exclusion provided in section 2503(b)?

LAW, RATIONALE AND CONCLUSIONS (Plan 1 and Plan 2)

ISSUE 1

Section 61 of the Code provides that gross income means all income from whatever source derived. Section 1.61-1 of the Income Tax Regulations, in part, provides that gross income includes income realized in any form, whether in money, property, or services. Gross income can be realized in the form of the receipt of educational services. See Fulton v. Commissioner, T.C.M. 1983-17.

Gross income is defined to encompass all "accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." Commissioner v. Glenshaw Glass Co., 348 U.S. 426, 431 (1955), 1955-1 C.B. 207, 209. Property rights will not become gross income subject to taxation until a gain is clearly realized. Eisner v. Macomber, 252 U.S. 189 (1920), 3 C.B. 25.

Section 102 of the Code provides that gross income does not include the value of property acquired by gift. A transfer of property is excludable from income by the recipient as a gift if the property is transferred out of a detached and disinterested generosity. Commissioner v. Duberstein, 363 U.S. 278 (1960), 1960-2 C.B. 428.

When A executes the contract with Trust and designates B and C, both B and C realize an accession to wealth. Because the contract rights (property) are transferred out of a detached and disinterested generosity, however, the transfer constitutes a gift for income tax purposes and is thus excludable from B's and C's gross income. See section 102 and Duberstein. Neither A nor B nor C will be considered actually or constructively to be in receipt of income at the time the contract is entered into between A and the Trust.

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Although the receipt of property by B and C is excludable from their gross income under section 102, that section has no application to income (including gain) realized from such property subsequent to its receipt. See section 1.102-1(a) of the regulations. Thus, to the extent that the fair market value of the educational services received by B, or any cash refund received by C, under the contract exceeds B's or C's basis in the property received by gift from A, either B or C will realize a further accession to wealth and thus gross income. Neither A nor B nor C, however, will be considered actually or constructively to be in receipt of income at any time between the date on which the contract is purchased by A and the date on which either B receives educational services or C receives a cash refund. A will not be considered actually or constructively to be in receipt of income when either B receives educational services or C receives a cash refund. Accordingly, A will not realize income as a result of his or her involvement in the program as the purchaser of a contract. (If A designates himself or herself as the beneficiary of the educational services or the cash refund, then the income tax consequences to A will be the same as the consequences to B or C).

To determine the amount of gross income realized by either B or C, the basis in the property must be determined.

Section 1012 of the Code provides that generally the basis of property shall be the cost of such property.

Section 1015(a) of the Code provides that generally the basis of property acquired by gift is the same as it would be in the hands of the donor (a substituted basis).

B's basis in the property is the substituted basis of A, which is A's cost of (payment for) that contract. Because the State X tuition prepayment program is generally designed to provide for educational services over a four-year period, B's basis must be recovered annually over the four-year period during which B receives educational services. See section 1.61-6 of the regulations. Thus, when Trust provides educational services for B at the beginning of a school year, B must recognize income to the extent that the fair market value of the educational services to be received for that school year exceeds one quarter of B's basis.

If a refund is received by C, C will realize gross income to the extent that the amount refunded exceeds the allocable portion of C's basis. C's basis in the property is the substituted basis of A. Thus, assuming a one-year tuition installment is refunded to C, then one quarter of C's substituted basis is subtracted from such refund to determine the amount of the refund includible in C's gross income.

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ISSUE 2

Income earned by an integral part of a state or a political subdivision of a state is generally not taxable in the absence of specific statutory authority for taxing such income. See Rev. Rul. 87-2, 1987-2 I.R.B. 4, holding that a trust account fund created, supervised, and controlled by a state Supreme Court is an integral part of a state and is therefore not subject to federal income tax.

Trust was created as a corporation to operate independently from State X under an appointed board of directors. Decisions by Trust's board of directors, including those involving investment discretion, may not be overridden by any state agency. Trust's funds are not derived from State X or one of its political subdivisions, and by statute are not subject to the claims of State X creditors and are not considered state money or common cash of the state. State X may not loan, transfer, or use Trust's funds for any purpose. Trust's funds may only be used by Trust for the tuition payment or refund purposes expressly provided in the enabling legislation. These factors indicate that Trust is not an integral part of State X or one of its political subdivisions. Therefore, Trust's income, unless otherwise excluded by statute, is subject to federal income tax.

Section 115(1) of the Code provides, in part, that gross income does not include income derived from the exercise of any essential governmental function that accrues to a state or any political subdivision of a state.

To qualify under section 115, it must be established that the income does not serve private interests such as designated individuals, shareholders of organizations, or persons controlled, directly or indirectly by such private interests. Thus, even if the income serves a public interest, the requirements of section 115 are not satisfied if the income also serves a private interest that is not incidental to the public interest. The basic principle underlying section 115 is that property (including any income thereon) must be devoted to purposes which are considered beneficial to the community in general, rather than particular individuals.

Trust provides B with a direct economic benefit in the form of education the value of which is expected to be substantially in excess of the up-front payment. Moreover, this benefit is available only to those persons such as B who are beneficiaries of a contract. Thus, the requirements of section 115 are not satisfied and the income of Trust, earned during administration of

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the program, is not excludable from its gross income. However, payments made under the contract entered into between A and Trust, and any contributions that State X might make to Trust, are excludable from the gross income of Trust.

ISSUE 3

Section 2501(a)(1) of the Code imposes a tax on the transfer of property by gift.

Section 2511(a) of the Code provides that the federal gift tax shall apply whether a transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 25.2511-1(h)(3) of the Gift Tax Regulations provides the following example regarding the indirect transfer of property.

The payment of money or the transfer of property to [X] in consideration of [X's] promise to render a service to [Y] is a gift to [Y], or to both [X] and [Y], depending on whether the service to be rendered to [Y] is or is not an adequate and full consideration in money or money's worth for that which is received by [X].

Section 25.2511-2(b) of the regulations provides that a gift becomes complete, and thus subject to the gift tax, at such time as the donor has so parted with dominion and control as to leave the donor no power to change the disposition of the transfer.

A transfers money to Trust in consideration for Trust's promise to provide, at some future time, educational services on behalf of B or a cash refund to C. Because the designations of B and C are irrevocable, A parts with dominion and control over the money transferred to Trust. Thus, there is a completed gift for federal gift tax purposes at the time the contract is purchased. See section 25.2511-2(b) of the regulations.

Section 2503(e)(2)(A) of the Code excludes from the application of the gift tax any amounts paid on behalf of an individual as tuition to an educational organization described in section 170(b)(1)(A)(ii) for the education or training of such individual. An educational organization described in section 170(b)(1)(A)(ii) is an organization which normally maintains a regular faculty and curriculum and normally has a regular enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. Section 25.2503-6(b)(2) of the regulations.

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Section 25.2503-6(b)(2) of the regulations further provides that to qualify for the gift tax exclusion under section 2503(e)(2)(A), the payment must be made directly to an educational organization. The determination of whether a transfer constitutes a payment of tuition made directly to an educational organization is made when the gift becomes complete for gift tax purposes.

Section 25.2503-6(c), Example 2, of the regulations considers a situation where a donor makes a completed gift of property to a trust, the terms of which require the funds to be used for tuition expenses incurred by the donor's grandchildren. The example concludes that the completed gift is not a direct transfer to an educational organization and therefore does not qualify for the section 2503(e)(2)(A) exclusion.

Although the payment made by A to Trust is a completed gift, Trust is not an educational organization within the meaning of section 2503(e)(2)(A) of the Code. Thus, the payment by A to Trust is not excluded from the application of the gift tax under section 2503(e)(2)(A).

Section 2503(b) of the Code excludes from the application of the gift tax the first \$10,000 of gifts of present interests in property made to any person during the calendar year. An interest constitutes a present interest in the transferred property only if the beneficiary is entitled to an unrestricted right to the immediate use, possession, or enjoyment of the property under the terms of the transfer. See section 25.2503-3(b) of the regulations.

B's or C's use or enjoyment of the payment made to Trust by A will be delayed until such time as Trust provides educational services for B, or until such time as a refund is made to C. Therefore, A's payment does not constitute a gift of a present interest in property, and is not eligible for the \$10,000 annual exclusion under section 2503(b) of the Code.

The above conclusions are based solely on the facts and the representation set forth above. Also, except as specifically ruled upon above, no opinion is expressed regarding the federal tax consequences of the transaction described above under any other provisions of the Code.

Robert A. Bowman

In accordance with the power of attorney on file in this office, we are sending a copy of this ruling to your authorized representative.

Sincerely,

Mario E. Lombardo

Mario E. Lombardo
Director, Individual Tax Division

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: Alaska Education Trust Fund
Sponsor: Kerttula and Kelly
Requestor: Senate Rules

Agency Affected: University of Alaska
BRU: Statewide Programs and Services
Components: _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
PERSONAL SERVICES	62.4	62.4	62.4	62.4	62.4	62.4
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	62.4	62.4	62.4	62.4	62.4	62.4

CAPITAL						
---------	--	--	--	--	--	--

REVENUE						
---------	--	--	--	--	--	--

FUNDING: (Thousands of Dollars)

GENERAL FUND	62.4	62.4	62.4	62.4	62.4	62.4
FEDERAL FUNDS						
OTHER						
TOTAL	62.4	62.4	62.4	62.4	62.4	62.4

POSITIONS:

FULL-TIME	1	1	1	1	1	1
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

Personal services include one professional position at range 79.

Prepared by: *Arliiss Sturgulewski* Phone: 465-3818
Division: Senator Arliiss Sturgulewski Date: Feb. 1, 1990
Chair, Senate Rules Committee

Approved by Commissioner: _____ Date: _____
Agency: _____

Distribution (by preparer):
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

) Changes in CSSB 136 (2nd Rules)
have no fiscal impact.
This fiscal note is
appropriate. *MEL*

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: Alaska education trust fund

Agency Affected: Dept. of Revenue
BRU: Treasury

Sponsor: Sen. Kerttula
Requestor: Senate Rules

Components: _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	45.0	84.0	127.0	174.0	235.0	299.0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	45.0	84.0	127.0	174.0	235.0	299.0

CAPITAL						
---------	--	--	--	--	--	--

REVENUE						
---------	--	--	--	--	--	--

FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER	45.0	84.0	127.0	174.0	235.0	299.0
TOTAL	45.0	84.0	127.0	174.0	235.0	299.0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

) Changes in CSSB 136 (2d Rules)
have no fiscal impact.
This fiscal note is
appropriate. *MSK*

Prepared by: *Arless Sturgulewski*
Division: Senator Arless Sturgulewski
Chair, Senate Rules Committee

Phone: 465-3818
Date: Feb. 1, 1990

Approved by Commissioner: _____ Date: _____
Agency: _____

Distribution (by preparer):
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

**Alaska Education Trust Fund
Investment Management Expenses**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	(\$ Millions)						(\$000)				
Fiscal Year	Beginning Balance	Permanent Fund Dividends	Contributions	Average Balance	Earnings	Ending Balance	Securities Safekeeping Fees	Common Stock Management Fees	Performance Measurement Fees	Audit	Total Fees
FY90	0	460	23	14	1	24	1	22	12	10	45
FY91	24	477	24	39	3	51	2	60	12	10	84
FY92	51	471	24	66	5	80	3	102	12	10	127
FY93	80	466	23	95	8	111	5	147	12	10	174

Notes:

1. Column 6, prior year
2. From "Revenue Sources," Fall 1988, Department of Revenue
3. 5% of Column 2, assuming 5% participation by dividend recipients; initial participation in a similar Florida program was .37% of the population
4. Column 1 + (7.5/12)(Column 3) assuming transfer to trust fund occurs on average on November 15; also assumes no payouts during first four years of the program
5. 8% x Column 4
6. Column 1 + column 3 + Column 5
7. Column 4 x 5.25%/1000 per contract
8. Column 4 x .31% per contract x 50% asset allocation to common stocks
9. Per contract
10. Treasury Division estimate
11. Columns 7 + 8 + 9.

2 of 2

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FISCAL NOTE

REQUEST

Revision Date: April 25, 1990
Title: An Act establishing the Alaska
education trust fund
Sponsor: KERTTULA, Kelly, et al
Requestor: House Finance

Agency Affected: Revenue
BRU: Permanent Fund Dividend Division
Components: Permanent Fund Dividend
Division

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
OPERATING						
PERSONAL SERVICES	24.1	11.9	11.9	11.9	11.9	11.9
TRAVEL	-0-	-0-	-0-	-0-	-0-	-0-
CONTRACTUAL	15.9	15.9	15.9	15.9	15.9	15.9
SUPPLIES	0.2	0.2	0.2	0.2	0.2	0.2
EQUIPMENT	-0-	-0-	-0-	-0-	-0-	-0-
LANDS & STRUCTURES	-0-	-0-	-0-	-0-	-0-	-0-
GRANTS, CLAIMS	-0-	-0-	-0-	-0-	-0-	-0-
MISCELLANEOUS	-0-	-0-	-0-	-0-	-0-	-0-
TOTAL OPERATING	40.2	28.0	28.0	28.0	28.0	28.0
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND	-0-	-0-	-0-	-0-	-0-	-0-
FEDERAL FUNDS	-0-	-0-	-0-	-0-	-0-	-0-
OTHER (PFD)	40.2	28.0	28.0	28.0	28.0	28.0
TOTAL	40.2	28.0	28.0	28.0	28.0	28.0

POSITIONS:

FULL-TIME	-0-	-0-	-0-	-0-	-0-	-0-
PART-TIME	3	2	2	2	2	2
TEMPORARY	-0-	-0-	-0-	-0-	-0-	-0-

ANALYSIS: See Attached.

Prepared By: Ervin Jones
Division: Permanent Fund Dividend Division

Phone: 465-2323
Date: April 25, 1990

Approved by Commissioner: _____
Agency: Revenue

Date: April 25, 1990

Distribution (by preparer):
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

FISCAL NOTE

REQUEST

Revision Date: February 5, 1990
Title: An Act establishing the Alaska education trust fund
Sponsor: Kerttula and Kelly, Sturgulewski
Requestor: _____

Agency Affected: Revenue
BRU: Permanent Fund Dividend Division
Components: Permanent Fund Dividend Division

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
OPERATING						
PERSONAL SERVICES	24.1	11.9	11.9	11.9	11.9	11.9
TRAVEL	-0-	-0-	-0-	-0-	-0-	-0-
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	0.2	0.2	0.2	0.2	0.2	0.2
EQUIPMENT	-0-	-0-	-0-	-0-	-0-	-0-
LANDS & STRUCTURES	-0-	-0-	-0-	-0-	-0-	-0-
GRANTS, CLAIMS	-0-	-0-	-0-	-0-	-0-	-0-
MISCELLANEOUS	-0-	-0-	-0-	-0-	-0-	-0-
TOTAL OPERATING	29.3	17.1	17.1	17.1	17.1	17.1
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND	-0-	-0-	-0-	-0-	-0-	-0-
FEDERAL FUNDS	-0-	-0-	-0-	-0-	-0-	-0-
OTHER	29.3	17.1	17.1	17.1	17.1	17.1
TOTAL	29.3	17.1	17.1	17.1	17.1	17.1

POSITIONS:

FULL-TIME	-0-	-0-	-0-	-0-	-0-	-0-
PART-TIME	3	2	2	2	2	2
TEMPORARY	-0-	-0-	-0-	-0-	-0-	-0-

ANALYSIS: See Attached.

Prepared By: Ervin Jones
Division: Permanent Fund Dividend Division

Phone: 465-2323
Date: February 5, 1990

Approved by Commissioner: [Signature]
Agency: Revenue

Date: Feb. 5, 1990

Distribution (by preparer):
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)