

SB

136

STATE OF ALASKA THE LEGISLATURE

POUCHY - STATE CAPITOL
JUNEAU, ALASKA 99811
907-465-3800

LEGISLATIVE AFFAIRS AGENCY LEGISLATIVE REFERENCE LIBRARY

Copies of minutes listed below were originally included in this file. The minutes are available on the STAIRS database CMPR. In order to save space copies of minutes have not been left in the files. .

Mary Van Nimwegen

SB 136

H HESS

3/20/90

H. HESS

3/27/90

H HESS

3/28/90

H HESS

4/23/90

HOUSE COMMITTEE REPORT

(7)

Date Referred: February 9, 1990

FURTHER REFERRALS:

FINANCE

Date of Committee Action: 4/23/90

The HESS Committee considered:

CSSB 136(2d Rls)

CSSB 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 CS SB 136 the same title
- have attached amendment(s) a new title
- 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)

- fiscal impact _____ fiscal note(s) 2/7/90 / Uat, Revenue
- zero fiscal note _____ zero fiscal note(s) _____
- zero with analysis _____ zero fn/analysis _____

SIGNING DO PASS:

SIGNING:

(Check approp. column)

Do Not Pass No Rec Amend

[Signature]

[Signature]

[Signature]

[Signature]

	Do Not Pass	No Rec	Amend
<u>Cheri Davis</u>		X	

[Signature]
Chairman's Signature

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.

A handwritten signature in cursive script, appearing to read "Jonny Ellis".

Rep. Jonny Ellis, Chair
House HESS Committee

A M E N D M E N T

#1

To: H CS CS SB 136 (HESS)

by: Gruenberg

Page 2, after line 28 insert

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

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

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

Letter of intent to H-~~CS~~-~~CS~~-SB 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.

FISCAL NOTE

REQUEST:

Revision Date: _____ Agency Affected: Dept. of Revenue
 Title: Alaska education trust fund BRU: Treasury
 Sponsor: Sen. Kerttula Components: _____
 Requestor: Senate Rules

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: *Arliss Sturvilowski*
 Division: Senator Arliss Sturvilowski
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 .31% 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
07
2

2 of 2

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*



Alaska State Legislature

SENATE

Official Business

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

MEMORANDUM

TO: Representative Johnny Ellis, Chairman
House Health, Education, and
Social Services Committee

FROM: Senator Kerttula

SUBJ: Senate Bill 136:
Alaska Education Trust Fund

DATE: February 20, 1990

A handwritten signature in cursive, appearing to read "Senator Kerttula", written over the "FROM" and "SUBJ" lines of the memorandum.

I would appreciate your scheduling Senate Bill 136, establishing the Alaska Education Trust Fund, at your earliest convenience. I believe this bill has a lot of merit. Senate Bill 136 offers dual benefits. First, the bill provides a relatively easy mechanism for saving for the costs of a child's education. Second, the bill provides a mechanism for guaranteeing the cost of the child's education if the child goes to the University of Alaska.

Under Senate Bill 136, a person could either contribute 50 percent of his or her permanent fund dividend or make a cash contribution to the Alaska Education Trust Fund to provide money for college for a specified beneficiary. An authorized representative of a minor would also be allowed to contribute 50 percent of the child's dividend to provide money for college for that child. At the time of the initial contribution, the Board of Regents would contract with the contributor to guarantee what the beneficiary's tuition costs will be at the University of Alaska, no matter how much costs actually rise.

Under Senate Bill 136, the Department of Revenue would administer and invest the funds, 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 by the time he/she enrolls in college. If the student decides not to go the University of Alaska, he or she can withdraw the money and use it for the costs of education at any other college or for any purpose.

Representative Ellis
February 20, 1990
Page Two

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.

Senate Bill 136 was 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.

As I mentioned earlier, I believe this bill has a lot of merit. I appreciate your attention to my request.

JK:kh



Official Business

Alaska State Legislature

Senate

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

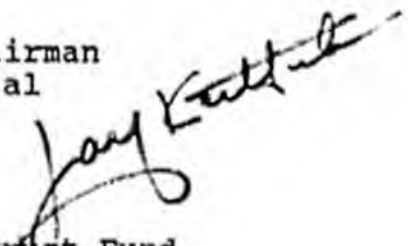
MEMORANDUM

TO: Representative Johnny Ellis, Chairman
House Health, Education and Social
Services Committee

FROM: Senator Jay Kerttula

SUBJ: Senate Bill 136 -- Educational Trust Fund
House HESS Committee Questions

DATE: February 21, 1990



I appreciate the time the House HESS Committee devoted to Senate Bill 136 during the meeting yesterday. Following are responses to the committee's concerns as they were described to me by my staff person. Please let me know if there are other concerns which I should address. As you are aware, I believe that an Educational Trust Fund has a lot of merit. I hope we can maintain the bill's momentum so that it receives the serious consideration it deserves.

1. Senator Szymanski's Amendment: I support the proposed amendment which was offered to the House HESS Committee by Senator Szymanski. As I understand the amendment, it will ensure that a trust fund under the Educational Trust would be exempt from claims under a bankruptcy proceeding. A trust fund under the amendment would not be exempt from child support claims. Senator Szymanski had offered a similar amendment on the Senate Floor, but withdrew the amendment after it was pointed out that the amendment would also exempt the trust fund from child support claims. The version of the Senator Szymanski's amendment which was submitted to House HESS takes care of that problem.

2. Requirement of a contract with the University of Alaska: I have no real objection to a parent who makes an initial contribution to the fund, having the option at that time of not entering into a contract with the University of Alaska. However, I think there are some issues associated with this option which should be discussed.

Representative Ellis
March 21, 1990
Page Two

First, Senate Bill 136 offers two major advantages as it is currently written -- guaranteeing tuition at the University of Alaska and providing a savings plan for a college education. Giving a parent the option of not entering into a contract with the University effectively eliminates one of the advantages of the bill. Some families already have a sophisticated system of investments that are earmarked for their children's education. It would be my guess that it would be these sorts of families who would have plans for their children which do not involve the University of Alaska. Therefore, I am not sure there is a reason to offer the option of not entering into a contract. I believe that most of those families who do not plan on a child attending the University of Alaska would be the same families who have investments which offer more advantages than offered by the Educational Trust Fund.

I see the second issue as having to do with what is in the child's best interest. Arguably, a parent should have a great deal to say about what his or her money is being spent for. However, Senate Bill 136 also allows a parent to contribute 50 percent of a child's permanent fund dividend into the fund. I am not sure that a parent's wishes should be controlling in the case of money which is a child's. A parent certainly does have the option of not putting their child's dividend into this fund. However, if they do so, it seems as if the child's best interest should be taken into account. Ultimately, the child is going to decide if or where he or she is going to college. It would be a shame if that child is barred from half the benefits of the Educational Trust Fund (i.e., the guaranteed tuition at the University of Alaska) because their parents did not think the University of Alaska was where the child should go to college.

I think these are issues which deserve some discussion, but I am not adamantly opposed to allowing parents the option of contracting with the University of Alaska.

3. IRS Determination: Attached is a copy of the IRS decision regarding the applicability of federal income taxes to the Michigan Education Trust Fund, per the request from Representative Gruenberg. As I understand this decision, income from the trust is excludable by both the beneficiary and the donor until either educational services are provided or until a refund is received.

Representative Elli
March 21, 1990
Page Three

4. Reference to "treasurer": Representative Gruenberg pointed to the reference to the commissioner of revenue as the "treasurer" of the fund on page 2, line 2, and asked if that designation should not be "trustee" rather than "treasurer." I believe that Representative Gruenberg is correct, although I believe that the Department of Revenue would have a fiduciary obligation regardless of which term is used.

In conclusion, I very much appreciate the consideration that the House HESS committee has given to Senate Bill 136. Please let me know if I can provide any additional information. I hope that your time constraints will permit the bill appearing on the committee agenda soon.

JK:kh

Attachment

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

Department of the Treasury

MAR 29 1966

Washington, DC 20224

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

MAR 29 1966

- 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 includable 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?

Robert A. Rowman

(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.F. 207, 209. Property rights will not become gross income subject to taxation until a gain is clearly realized. Eisner v. Macomber, 332 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 actual or constructively to be in receipt of income at the time the contract is entered into between A and the Trust.

Robert A. Bowman

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 1.61-5 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.

Robert A. Bowman

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

Robert A. Bowman

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 Z 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(b)(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.

Robert A. Rowman

Section 25.2503-6(c) 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 3, 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.

A'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



Alaska State Legislature

Senator Mike Szymanski

While in Session:
PO. Box V
Juneau, Alaska 99811
(907) 465-4978

Interim:
3111 C Street, Suite 510
Anchorage, Alaska 99503
(907) 561-7617
or
165 E. Parks Highway
Wasilla, Alaska 99687
(907) 376-6453

REC'D MAR 1 1990

February 26, 1990

JIM

TO: Representative Johnny Ellis
Chairman, House HESS Committee

FROM: *Mike Szymanski*
Senator Mike Szymanski

SUBJECT: Senate Bill 136, Education Trust Fund

When Senate Bill 136 is heard in the House HESS Committee, I would like to offer the attached amendment for inclusion. The purpose of this amendment is to protect the fund from bankruptcy proceedings except for child support claims.

Thank you for your consideration of this request.

MS:pt
cc: Senator Kerttula
enclosure

Senate District E

Mat-Su Borough • Sitka • Anchorage • Bethel/Indian • Cordova • Nikiski • Cooper Landing • Hope • Seward • Prince William Sound

A M E N D M E N T

Sen. Szymanski

OFFERED IN THE HOUSE

TO: CSSB 136 (2d Rules)

Page 5, after line 25:

Insert new bill sections to read:

"* Sec. 2. AS 09.38.015 is amended by adding a new subsection to read:

(e) Contributions to the Alaska education trust fund under the terms of an advance tuition payment contract are exempt, except for child support claims.

* Sec. 3. AS 09.38.055 is amended to read:

Sec. 09.38.055. BANKRUPTCY PROCEEDINGS. In a proceeding under 11 U.S.C. (Bankruptcy) only the exemptions under 09.38.010, 09.38.015(a) and (e), 09.38.017, 09.38.020, 09.38.025 and 09.38.030 apply.

* Sec. 4. AS 09.38.065(a) is amended to read: -

(a) Except as provided under AS 09.38.015(e), notwithstanding [NOTWITHSTANDING] other provisions of this chapter,

(1) a creditor may make a levy against exempt property of any kind to enforce a claim for

(A) child support;

(B) unpaid earnings of up to one month's compensation or the full-time equivalent of one month's compensation for personal services of an employee; or

(C) state or local taxes; and

(2) a creditor may make a levy against exempt property to

enforce a claim for

(A) the purchase price of the property or a loan made for the express purpose of enabling an individual to purchase the property and used for that purpose;

(B) labor or materials furnished to make, repair, improve, preserve, store, or transport the property; and

(C) a special assessment imposed to defray costs of a public improvement benefiting the property."

Renumber the following bill sections accordingly.

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

1 IN THE SENATE

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

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 following powers and duties under this section:

3 (1) to 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) to receive all items of cash and investments belonging
7 to the fund;

8 (3) to 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) to invest and reinvest the assets of the fund as pro-
12 vided in this section and as provided for the investment of retirement
13 funds under AS 14.25.180;

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

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

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

22 (8) to engage an independent firm of certified public
23 accountants to annually audit the financial condition of the fund's
24 investments and investment transactions;

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

27 (10) to report to the university the condition and invest-
28 ment performance of the fund.

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

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

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

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

16 (b) The Department of Revenue shall pay contributions directly
17 to the fund.

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

19 (a) The Board of Regents of the University of Alaska may contract
20 with a purchaser for the advance payment of tuition by the purchaser
21 for a qualified beneficiary of any age to attend a branch of the
22 university to which the qualified beneficiary is admitted, without
23 further tuition cost to the qualified beneficiary. A purchaser and a
24 qualified beneficiary may be the same person.

25 (b) The board shall

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

28 (2) establish standard payment plans to be used under
29 advance tuition payment contracts;

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

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

6 (1) the amount of payments required from the purchaser on
7 behalf of the qualified beneficiary;

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

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

10 (4) the name and age of the qualified beneficiary under the
11 contract and a statement that the purchaser, with the approval of the
12 board, may substitute another person for the qualified beneficiary
13 originally named in the contract;

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

16 (6) the name of the persons entitled to terminate the
17 contract, the terms and conditions under which the contract may be
18 terminated, and the amount of the refund to which the person terminat-
19 ing the contract is entitled;

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

22 (8) the number of credit hours the qualified beneficiary
23 may receive if the qualified beneficiary is not entitled to in-state
24 tuition at the time of enrollment at the university;

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

27 (10) other terms and conditions the board determines to be
28 appropriate.

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

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

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

5 (3) if the qualified beneficiary certifies to the board,
6 after the contracted date of entrance to the university or after the
7 qualified beneficiary has received a high school diploma or reached
8 the age of majority, that the qualified beneficiary has decided not to
9 attend the university;

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

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

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

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

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

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

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

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

26 (6) "university" means the University of Alaska, including
27 a community college affiliated with the university.
28
29