

SB

187

HOUSE COMMITTEE REPORT

(7)

Date Referred to Committee: April 30, 1997

FURTHER REFERRALS:

Date of Committee Action: 5/6/97

The HEALTH, EDUCATION AND SOCIAL SERVICES Committee considered:

SB 187

SENATE BILL NO. 187

UNIVERSITY TUITION PAYMENT PROGRAM

"An Act relating to disclosure of public records identifying a participant in the advance college tuition payment program; relating to the composition and assets of the Alaska advance college tuition payment fund; relating to administration of the advance college tuition payment program; relating to advance college tuition payment contracts; and providing for an effective date."

recommends it be replaced the same title
 with the following committee substitute _____ a new title

additional referral to _____ Committee
 attached amendment(s)

ADOPTS: _____ Letter of Intent

ATTACHES NEW FISCAL NOTE(S): _____ (Dept)

APPROVES PREVIOUS: _____ (Dept/Date)

fiscal note(s) _____

fiscal note(s) _____

zero fiscal note(s) _____

zero fiscal note(s) University / 4-28-97

SIGNING WITH RECOMMENDATIONS	DP	DNP	NR	AM
<i>Paul Pagan</i>	✓			
<i>Carla Bunde</i>	✓			
<i>John Verney</i>	✓			
<i>John Hagg</i>			✓	

CHAIR'S SIGNATURE *Carla Bunde*

GARY WILKEN

SENATOR
Districts 29 & 30
West Fairbanks

Senate Standing Committees

Chairman: Health, Education,
and Social Services (HESS)
Vice Chairman: Transportation
Vice Chairman: Community and
Regional Affairs

Special Committee

Member: Administrative Regulation Review



During Session:
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SPONSOR STATEMENT

SB 187 – University Tuition Payment Program

In August 1996, Congress passed legislation that exempts qualified state prepaid tuition programs from income taxes similar to exemptions provided other non-profit activities. Senate Bill 187 makes the necessary statutory changes to conform the Advance College Tuition (ACT) payment plan with the new federal law.

The ACT plan, established in 1990 under AS 14.40.803, offers an incentive for Alaskan residents to save for college. Under this plan one-half of a participating individual's annual permanent fund dividend can be used to prepay college tuition credits at the current cost per credit. The University of Alaska guarantees that ACT credits can be used for tuition *regardless of the amount paid for the ACT credit or the cost of tuition at the time they are used*. Currently there are over 6,300 prepaid tuition contracts in place totaling approximately \$17.6 million.

On February 14, 1997, the University of Alaska Board of Regents adopted a revised ACT plan which conforms to the new federal requirements. The changes proposed in SB 187 will strengthen the Advance College Tuition exempt status with IRS. Failure to comply with the new tax law in a timely manner could result in retroactive taxation of the program back to 1991 and destroy the financial viability of this very worthwhile program. For this reason, I recommend passage of Senate Bill 187.

James F. Lynch
Associate Vice President for Finance

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Statewide System of Higher Education

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April 28, 1997

The Honorable Gary Wilken
Chair, Senate HESS Committee
Alaska State Senate
State Capitol: Mail Stop 3101
Juneau, AK 99801-1182

Dear Senator Wilken:

RE: Federal Legislation, Prepaid Tuition Programs

At the Senate Hess Committee meeting earlier today, I agreed to provide additional information on federal legislation which may alleviate the income tax burden for individuals saving for college. Enclosed is a copy of the McConnell Graham College Savings Act of 1996 (S.594).

The McConnell Graham bill provides fixes for a number of technical problems with last year's prepaid tuition legislation, but primarily it authorizes state sponsored prepaid tuition and college savings programs to include payment of "room and board" and completely exempts the student from the federal income tax on any increase in value or earnings credited to their prepaid tuition account. Under the current law, any distributions for room and board must be subject to a payout penalty. This bill does not provide for a federal tax deduction for contributions or payments by participants into the program, but it is the next best thing. Although a student's tax rate should be relatively low, the tax bill will come when they have no source of funds from which to pay the tax. If the funds are used in accordance with the law (exclusively for qualified expenses), there is no "cash distribution" from which to pay any tax due.

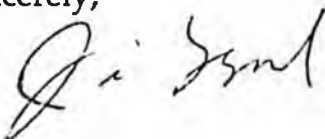
The concept of college savings programs has only recently picked up momentum. When Alaska initiated its program, there were only four other state programs. We have been actively working through the National Association of State Treasurers at obtaining national recognition for these programs and their issues. There are now approximately 20 states with active programs or are actively implementing programs, and almost every state is at some stage of evaluating the viability of a college prepaid or savings program. Today's students are leaving school with incredible amounts of debt (in many cases uncollectible) to be paid in the future. College savings programs are

University of Alaska
The Honorable Gary Wilken
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essential to turning this situation around and leverage the time value of money into payment of those costs in advance. The obstacles and disincentives to saving for college must be removed and the students encouraged to act responsibly for themselves. The primary obstacle to implantation of these programs has been the Internal Revenue Service. That problem was substantially mitigated last year. The McConnell Graham bill enclosed is another major step forward.

Senator Murkowski has signed on as a co-sponsor to the McConnell Graham bill, and I believe that Senator Stevens will be supportive. No action has occurred in the House to my knowledge. There is other federal legislation in the works. I will try to keep you informed. Communicating your support for this legislation and prepaid tuition legislation in general to the Alaska delegation will be a big help for the Alaska prepaid tuition participants. Thank you very much for your interest in the program.

Sincerely,



Jim Lynch

JFL/pe

Enclosure

cc: Senator Loren Leman



University of Alaska
Statewide System of Higher Education

THE ALASKA ADVANCE COLLEGE TUITION PAYMENT FUND

The Alaska Advance College Tuition (ACT) Payment Fund, as established in 1990 under AS 14.40.803, was created by the legislature to provide an incentive for Alaskans of all ages to continue and complete their secondary and post-secondary education. The ACT plan provides for future redemption or refund of ACT credits for payment of tuition and other qualified higher education expenses at the University of Alaska or any eligible college, university or vocational/technical institution.

The ACT fund consists of permanent fund dividend (PFD) and cash contributions under the terms of an advance college tuition payment contract. Under the PFD program, half of a participating individual's annual PFD dividend can be deposited directly into the ACT fund. Currently, there are over 6,300 pre-paid tuition contracts in place totaling approximately \$17.6 million. The Commissioner of Revenue is the custodian of the fund and the University of Alaska Board of Regents administers the program.

P.L. 104-188, signed into law on August 20, 1996, included a provision of the Internal Revenue Code (Section 529) that defined the federal tax treatment of qualified state tuition programs, thereby clarifying the tax-exempt status of the ACT fund and the tax-deferred status of a participant's earnings on any increase in value of ACT credits prior to actual use. Congress has given states with pre-paid tuition programs until August 1997 to bring their plans into conformance with the new law. The University Board of Regents has revised the ACT plan to conform with federal legislation; however, state statute changes are also necessary to better assure full compliance. Although the Internal Revenue Service will make any final determination, failure to pass conforming state legislation could result in retroactive taxation of the ACT program and its participants back to 1991 and virtually eliminate the financial viability of the program.

Senate Bill 187
Sectional Analysis
Advance College Tuition (ACT) Program

Purpose of the bill:

The bill is intended primarily to conform the state statutes related to the Advance College Tuition payment plan with federal tax legislation passed by Congress with the help of Senators Murkowski and Stevens as part of the Small Business Job Protection Act in August 1996. On February 14, 1997, the Board of Regents adopted a revised ACT Plan which was intended to conform the Plan and operation of the program to the new requirements. Congress has given prepaid tuition programs until August 1997 to bring their plans into conformance with the new law. The Internal Revenue Service (IRS) will make all determinations regarding compliance and have not yet issued any regulations or guidelines on the issues. Although the university believes that the revised ACT Plan adopted by the Board of Regents in February is adequate to comply with the new law, the proposed changes to the statute included herein will be of substantial assistance in making that argument with the IRS. Failure to comply with the new tax law in a timely manner could result in retroactive taxation of the program back to 1991 and destroy the financial viability of the program.

Section 1

AS 09.25.120(a) is amended to limit access of public records requests for personal identifying information of participants in the ACT program. The ACT records include social security numbers of purchasers and beneficiaries and personal financial information regarding amounts deposited with the Fund and the values of any participants interest in the program.

Section 2

AS 14.40.803(b)(2) is amended to eliminate unnecessary wording regarding contributions to the fund, if any.

Advance College Tuition Program

Section 3

AS 14.40.803(c) is amended to authorize payments to other eligible educational institutions, if payments to other institutions are required. Internal Revenue Service (IRS) regulations are expected to provide certain safe harbor provisions to qualified state tuition programs if payments are made directly to an eligible educational institution. An "eligible educational institution" is a defined term under the Internal Revenue Code (Code).

Section 4

AS 14.40.805(11) is amended to add the word "awards" in order to make the terminology the same as that used in AS 14.40.803(c).

Section 5

AS 14.40.809(a) is amended to clarify that ACT credits can be used for payment of "qualified higher education expenses," which are defined in the Code (basically tuition, fees, books, supplies, and potentially room and board at some future time). This change is beneficial to participants in that it allows tax deferred savings for certain expenses in addition to pure tuition. It also limits the sale of tax deferred ACT credits to purposes of funding "qualified higher education expenses" as required by federal law. In order for a prepaid tuition plan to be exempt from federal income tax, redemptions must be limited to use for "qualified higher education expenses" at an "eligible educational institution."

AS 14.40.809(a) is amended to clarify that students can utilize ACT credits for tuition and qualified expenses at other "eligible institutions." This change is beneficial to participants in that credits can be redeemed for use at institutions other than the University of Alaska. It also limits the sale of tax deferred ACT credits to use at an eligible institution as required by federal law. In order for a prepaid tuition plan to be exempt from federal income tax, redemptions must be limited to use for "qualified higher education expenses" at an "eligible educational institution."

AS 14.40.809(b)(2) is amended to indicate that the formal Plan adopted by the Board of Regents is part of the contract with the purchaser. This is intended to emphasize the fact that the terms and conditions of the ACT Plan will be deemed part of the ACT contract.

Advance College Tuition Program

AS 14.40.809(b)(4) is amended to allow the Board of Regents to enter into reciprocal agreements with other eligible educational institutions or qualified state tuition programs as considered beneficial by the Board of Regents. The Code provides for rollover provisions which are yet to be defined in IRS regulations. The university believes that it may be advantageous for participants or for qualified state programs to allow reciprocal transfers of participants between contracts, institutions, or between state programs. Although reciprocal agreements with Sheldon Jackson University and Alaska Pacific University have been authorized by statute, uncertain tax treatment of the program itself and the benefits to participants has made consideration of any such agreement unfeasible.

AS 14.40.809(b)(5) is deleted as unnecessary. This provision was added to the statutes in an effort to seek exemption of the ACT program income tax as an integral part of a tax exempt instrumentality of the state. Passage of Section 529 of the Internal Revenue Code last year eliminated the need for this provision. The commitments under the ACT Plan are, and will continue to be, a contractual obligation of the university in accordance with the terms and conditions of the ACT Plan; however, the university does not intend to make ACT participants a special or preferred class of creditors.

Section 6

AS 14.40.811(a)(1) is amended to delete the provisions related to installment contracts. This provision was included in the law prior to development of the ACT program. It was intended to apply to a situation where a purchaser would agree to payment for four years of education to be paid in installments in advance of coming to school. This provision is currently nonfunctional because the ACT program developed into a unitized program, where a purchaser receives the number of units of education that were paid for rather than making a contractual commitment to make payments in the future. Under the ACT program, there is no commitment to purchase or pay for any specified number of additional units or credits.

AS 14.40.811(a)(2),(3), and (5) are amended to clarify some of the essential information which is required for a prepaid tuition contract including name and date of birth of the purchaser and the beneficiary (prospective student), the number of credits purchased, and the commitment by the Board of Regents to provide education to the beneficiary in accordance with the terms and conditions of the Plan.

Advance College Tuition Program

AS 14.40.811(a)(7) is amended to clarify the Board of Regents will make whatever terms and condition are required by the Internal Revenue Code part of the contract with participants of the program.

Section 7

AS 14.40.817(1) is amended to clarify that "contract" as used in AS 14.40.803 - 14.40.817 means an ACT Contract.

AS 14.40.817(2) is amended to make the definition of a beneficiary under state statute the same as the definition under the Internal Revenue Code. The concept of residency for eligibility is unchanged and is retained in the formal Plan adopted by the Board of Regents.

AS 14.40. 817(4) and (8) are added to adopt the same meaning for an "eligible educational institution" and "qualified higher education expenses" as provided by the Internal Revenue Code. These definitions are critical to federal tax treatment under the Code.

AS 14.40. 817(7) is amended to clarify who is the contracting party or purchaser and to accommodate situations where payments under a contract are made by persons, such as grandparents, who are not the formally named as a purchaser or participant under a contract.



ACT Advance College Tuition

Alaska's Prepaid College Tuition Program

Save now for your child's college education.



Prepay future tuition costs at today's rate!

- The Alaska Legislature and the University of Alaska have developed the Advance College Tuition (ACT) payment plan to help Alaskan residents save for college.
- You can use one-half of your permanent fund dividend to prepay college tuition costs at the University of Alaska for yourself or your child.

Check the box on line 10 of an adult or line 12 of a child's application. One-half of the 1997 dividend will be used to purchase ACT prepaid tuition credits.

If this is the first time you are buying ACT tuition credits, call the ACT office at 1-800-478-0003 (907-474-7469 if in Fairbanks or outside Alaska) to receive a complete information packet and required forms.

What is a credit?

Just as a high school student is required to complete a specified number of course credits to receive a high school diploma, a college student is required to have a minimum number of course credits to receive a college degree.

How many credits do I need?

It generally takes a minimum of 60 course credits to acquire an associate's (2-year) degree and 120 course credits to acquire a bachelor's (4-year) degree. A student will need approximately 15 credits for each college semester. The number of course credits taken each semester determines the tuition cost for that semester. A student who purchases ACT prepaid tuition credits simply uses these credits to cover future tuition costs.

How many credits can I buy with one-half of my 1997 dividend?

In 1996, one-half of the dividend purchased approximately six ACT credits at a cost of \$77 per credit. The number of credits you can buy this year will depend on the amount of the dividend and the 1997 price of ACT credits.

Can I buy additional credits?

Yes, you may buy ACT credits directly from the ACT office at any time. You may even buy 120 credits all at one time!

When can my credits be used?

You may use your ACT credits two years after payment is received by the ACT program.

continued on next page...

Copied from the 1997 PFD Application Booklet

— continued from previous page... —

What is the guarantee offered by the University of Alaska?

The University guarantees that ACT credits can be used for tuition at any University of Alaska campus regardless of the amount paid for the ACT credit or the cost of tuition when they are used.

Can ACT credits be used at other colleges, universities, vocational or technical schools?

The student may use ACT credits to pay for tuition at almost any college, university, vocational or technical school in the nation. Payment will be made to the student to help defray their tuition costs, however the amount cannot be guaranteed. The amount of the payment will depend upon the original purchase price, tuition rates at the University of Alaska, and earnings of the ACT program.

Can I get a refund if my child doesn't go to college?

Your child may obtain a refund of the original purchase price of the ACT credits if he or she chooses not to attend college, unless you named another child or student as an alternate recipient of the credits in the ACT contract.

If I used the ACT check-off last year, do I have to check it again?

Yes. Each year you must check-off the Advance College Tuition box on the dividend application. However, you do not need to complete new contract forms unless you are buying ACT credits for a different individual than in the past.

Do I have to pay any fees?

Yes. There is a one-time, nonrefundable administrative fee for setting up an ACT contract and several transaction processing fees. Currently there is no fee for redemption or use of the ACT credits.

What about federal taxes?

The portion of your dividend paid into the ACT program is taxable to you or your child as though it had been received directly by you. Under current tax rules, the increase in value of the ACT credits from the date of purchase to the date used is taxable to the recipient when they are used or refunded. In August 1996, Congress passed legislation which exempts qualified state prepaid tuition programs from income taxes similar to exemptions provided other non-profit activities. Subject to adoption of certain plan amendments to be developed over the next year, the ACT program is expected to meet the requirements for exemption under the new law.

If I change my mind, can I get my dividend money back?

Yes, you can get your dividend money back in full if you properly notify the ACT office by February 1, 1998. After that date you can still get a refund but there is a processing fee deducted. Contact the ACT office for a withdrawal form if needed.

When you sign up for the ACT program do the following:

- Request an information packet from the ACT office, as noted on the previous page. This packet includes an ACT Plan booklet, ACT contract form, and other information about the program.
- Read the ACT Plan booklet very carefully. The information included in the permanent fund dividend application package is not a complete description of the ACT program.
- Complete and return the ACT contract form to the ACT office. Your purchase of ACT credits is not complete until the contract form is received and accepted by the University of Alaska. There are deadlines for completing these forms in order to purchase credits at the 1997 rate.

ACT • UNIVERSITY OF ALASKA • P.O. BOX 755120 • FAIRBANKS, ALASKA 99775-5120
(WITHIN ALASKA) 1-800-478-0003 • (FAIRBANKS AND OUTSIDE ALASKA) 907-474-7469

FISCAL NOTE

STATE OF ALASKA
1997 LEGISLATIVE SESSION

No. 1
Bill Version: SB 187
(S) Publish Date: 4/28/97

Revision Date:
Title: An Act relating to disclosure of public records...of the
Alaska advance college tuition payment fund.
Sponsor: Senator Wilken
Requester:

Department Affected: University of Alaska
BRU: All
Component:

COMPONENT SERIAL NO.

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY98	FY99	FY00	FY01	FY02	FY03
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL						
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REVENUE FD SOURCE						
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FUNDING: (Thousands of Dollars)

1002 FEDERAL FUNDS						
1003 OF MATCH						
1004 GENERAL FUND						
1006 GFMHTIA						
OTHER						
TOTAL FUNDING	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:						
FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: None

ANALYSIS: (Attach a separate page if necessary.)

Prepared by: Mariou Burton
Division: Statewide Budget Office
Approved by: MGB Mariou Burton, Director
Agency: Statewide Budget Office

Phone: 463-3086
Date: 4/25/97
Date: 4/25/97

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).