SENATE FINANCE COMMITTEE
Amendment Number: 7
Bill Number: SJR 29
Sponsor: Donley Date: 2/10/00
Logged In By: Mindy

1-LS1162\D.6
Chenoweth
2/10/00

AMENDMENT

OFFERED IN THE SENATE

TO: CSSJR 29(JUD)

Page 1, line 2, following "**legislators,**":

Insert "**, to the location of special legislative sessions,**"

Page 2, following line 6:

Insert a new section to read:

"* **Sec. 3.** Article II, sec. 9, Constitution of the State of Alaska, is amended to read:

Section 9. Special Sessions. Special sessions may be called by the governor or by vote of two-thirds of the legislators. The vote may be conducted by the legislative council or as prescribed by law. At special sessions called by the governor, legislation shall be limited to subjects designated in his proclamation calling the session, to subjects presented by him, and the reconsideration of bills vetoed by him after adjournment of the last regular session. Special sessions are **held at a location determined by the legislature and are** limited to thirty days."

Renumber the following resolution section accordingly.

SENATE FINANCE COMMITTEE

2000 COMMITTEE ACTION

Bill Number	SJR 29
Amendment	#7
Motion	adopt
Motion by	D
Objection	
Objection by	W ?
Removed	
Second Objection by	
Committee Member	***Vote***
Senator Al Adams	N
Senator Gary Wilken	N
Senator Pete Kelly	Y
Senator Lyda Green	Y
Senator Randy Phillips	Y
Senator Dave Donley	Y
Senator Loren Leman	Y
Co-Chair Sean Parnell	N
Co-Chair John Torgerson	Y
Tally	
Yea	0 6
Nay	0 3
Absent	0
MOTION	Pass

SENATE FINANCE COMMITTEE

2000 COMMITTEE ACTION

Bill Number	SJR 29 as amended
Amendment	SJR
Motion	☆ Move from Committee
Motion by	P
Objection	
Objection by	
Removed	
Second Objection by	
Committee Member	***Vote***
Senator Randy Phillips	
Senator Dave Donley	
Senator Loren Leman	
Senator Al Adams	
Senator Gary Wilken	
Senator Pete Kelly	
Senator Lyda Green	
Co-Chair Sean Parnell	
Co-Chair John Torgerson	
Tally	
Yea	**0**
Nay	**0**
Absent	**0**
MOTION	

FISCAL NOTE

DRAFT

STATE OF ALASKA
2000 LEGISLATIVE SESSION

NO. SJR 29
BILL VERSION:
PUBLISH DATE:

Revision Date:
Title: "Proposing amendments to the Constitution of the State of Alaska relating to terms..."
Sponsor: Senator Parnell
Requestor: Senator Parnell

Department Affected: Legislative Affairs Agency
BRU: Legislative Council
Legislative Operating Budget
Component: All

COMPONENT SERIAL NO:

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 01	FY 02	FY 03	FY 04	FY 05	FY 06
PERSONAL SERVICES	-513.0	-513.0	-513.0	-513.0	-513.0	-513.0
TRAVEL	-255.0	-255.0	-255.0	-255.0	-255.0	-255.0
CONTRACTUAL	-24.0	-24.0	-24.0	-24.0	-24.0	-24.0
SUPPLIES	-18.0	-18.0	-18.0	-18.0	-18.0	-18.0
EQUIPMENT	0.0	0.0	0.0	0.0	0.0	0.0
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-810.0	-810.0	-810.0	-810.0	-810.0	-810.0
CAPITAL	0	0	0	0	0.0	0
REVENUE FUND SOURCE	0	0	0	0	0.0	0

DRAFT

FUNDING: (Thousands of Dollars)

GENERAL FUND	-810.00	-810.00	-810.00	-810.00	-810.00	-810.00
FEDERAL FUNDS						
OTHER FUND SOURCE						
TOTAL	-810.00	-810.00	-810.00	-810.00	-810.00	-810.00

POSITIONS:

FULL-TIME	0	0	0	0	0.0	0
PART-TIME	0	0	0	0	0.0	0
TEMPORARY	0	0	0	0	0.0	0

Estimate of current year impact: 0

ANALYSIS: (Attach a separate page if necessary)

would amend the Constitution of the State of Alaska by limiting the regular session to 90 days. The Legislature would realize a cost savings of approximately $27.0 per day for each day of a shorter session. 120 days minus 90 days equals 30 days. 30 x 27.0 equals a cost savings of $810.0.

Prepared By: Karla Schofield, Deputy Director Karla Schofield Phone: 465-3852
Division: Administrative Services Date: 2/1/00

Approved By: Pamela A. Varni, Executive Director Pamela A. Varni
Agency: Legislative Affairs Agency Date: 2/1/00

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

The Legislature traditionally charges expenses occurring during session to session expense accounts and expenses occurring during the interim to interim expense accounts. For example: Most legislative staff payroll costs are charged to operating expense accounts during the interim. Staff salaries for most legislative staffers are charged to session during the session. The legislative payroll is higher during a legislative session. If the regular session were shortened to 90 days, the session payroll would decrease and the interim payroll would increase. There would be a decrease in the total amount of the payroll due to the higher cost of personal services during a session. The majority of the personal services costs would be a tranfer of costs between allocations.

The costs below are for items not needed if the legislature shortened the number of days of a session.

		Per Day	times 30 days	Total
Personal Services		17.1	30	513.0
Travel				
Session per diem	9.5			
less increase $65 interim	-1.0			
per diem	8.5	8.5	30	255.0
Contractual		0.8	30	24.0
Telephones, chaplin fees, copier Maintenance				
Supplies		0.6	30	18.0
Lounge supplies				
Printshop paper supplies				
		27.0		810.0

Current number of session days	120
Proposed number of session days	90
Diffference	30

Alaska State Legislature

SENATE DISTRICT I

Bayshore
Campbell
Dimond
Independence Park
Klatt
Old Seward
Southport
Taku
Abbott Loop
Bear Valley
Bird Creek/Indian
Girdwood
Glen Alps
Hillside
Huffman/O'Malley
Portage
Rabbit Creek

716 W. FOURTH AVE., SUITE 530
ANCHORAGE, AK 99501-2133
(907) 269-0250 *Fax:* (907) 269-0249

While in Session:
STATE CAPITOL
JUNEAU, AK 99801-1182
(907) 465-2995 (800) 365-2995

SENATOR SEAN PARNELL
Senate Finance Committee Co-Chair

Sponsor Statement
Senate Joint Resolution 29

Senate Joint Resolution 29 would place a constitutional amendment on the 2000 general election ballot to limit the Alaska State Legislature to regular annual sessions of no more than 75 days, which would begin on the fourth Monday in February.

The Alaska Constitution originally imposed no session limits, and while pre-oil sessions averaged about 70 days, by the 1980s sessions stretched from January into June or even July. In 1984, Alaska voters amended the Constitution to impose a 120-day limit, and legislators found they could transact the people's business in the time allowed. It is likely that legislators could likewise adapt to a 75-day session that would save money, foster a citizen legislature and focus attention on legislative priorities.

- **SAVE MONEY:** Shortening sessions would help lower the cost of state government. Fiscal notes show savings of $1.21 million, including legislative per diem, session staff, contractual services, and operations and maintenance.

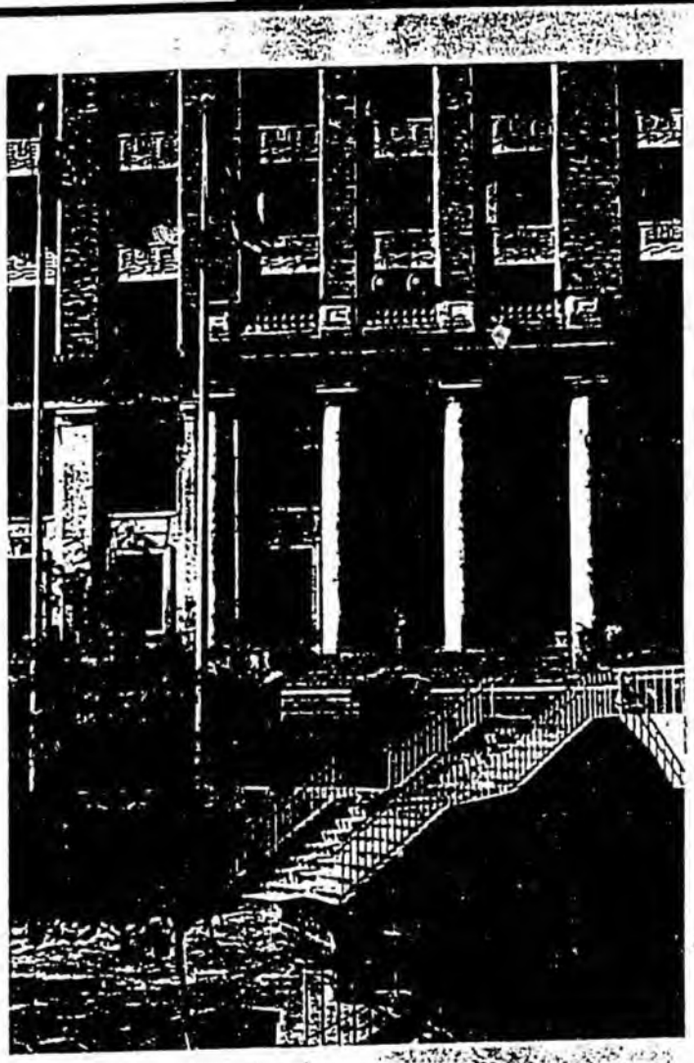
- **FOSTER CITIZEN LEGISLATURE:** Many Alaskans choose not to seek legislative office because it can mean putting their families and careers on hold – or moving them along to Juneau – for at least 120 days each year. Reducing session by 45 days would lessen that impediment significantly, making legislative service more attractive to more Alaskans.

- **FOCUS ATTENTION:** A shorter session would focus the Legislature's attention on its primary constitutional duty – to pass a budget – and bring its work schedule more in line with the spring revenue forecast. And with more time in their home districts to hear constituents' concerns face-to-face, legislators would be better prepared to use the remainder of the session on the issues of greatest concern to their constituents.

Some would argue that shortening the session would simply shift workload and expenses to the interim, but this is not likely given historical trends. Legislative Council and other standing committees already meet during interim, but at a fraction of the cost of full sessions. Unless the Legislature increased interim staff budgets or committee powers, interim expenses would continue to be much lower than regular session costs.

Alaskans in 1984 saw the benefit of reducing legislative sessions from no limit to 120 days. Alaskans in 2000 deserve the chance to continue this process. Passing SJR 29 will give voters their say on a measure that would save the state money, speed action on legislative priorities and allow more Alaskans to serve their state.

I urge you to pass SJR 29 on to a vote of the people.



Alaska's Constitution

A CITIZEN'S GUIDE

Third Edition

Alaska Legislative Research Agency • Gordon S. Harrison

Section 8. Regular Sessions

> **The legislature shall convene in regular session each year on the fourth Monday in January, but the month and day may be changed by law. The legislature shall adjourn from regular session no later than one hundred twenty consecutive calendar days from the date it convenes except that a regular session may be extended once for up to ten consecutive calendar days. An extension of the regular session requires the affirmative vote of at least two-thirds of the membership of each house of the legislature. The legislature shall adopt as part of the uniform rules of procedure deadlines for scheduling session work not inconsistent with provisions controlling the length of the session.**

The first sentence of this section provides for annual sessions of the legislature. The majority of states ha[illegible]nnual sessions, and in those where the constitution provides for biennial sessions (a session every two years), a special session during the "off" year is common. The ability to meet annually, in order to keep abreast of current developments and administrative activity, is generally considered necessary for a legislature to be an effective policy-making body and to avoid being dominated by the executive branch.

The legislature has changed the beginning of the regular session to the second Monday in January at 10:00 a.m., except following a gubernatorial election year, when it is the third Monday in January at 10:00 a.m. (AS 24.25.090). The later date following a gubernatorial election gives a new governor an extra week to prepare for the opening of the session.

The second sentence establishes a limit of 120 days after convening for each regular session (with one ten-day extension if agreed to by two-thirds of each house). This limit was imposed by a constitutional amendment ratified by the voters in 1984. Until that time, the constitution did not limit the length of sessions. The framers of the constitution adopted the progressive view that the legislature should not be rushed in its deliberations, as the business of modern state government is too complex to be transacted in hurried,

in frequent sessions. (About two-thirds of state constitutions impose some limit on the length of sessions.) Delegates feared that constraints on the length (and frequency) of sessions might result in ill-conceived or imprudent measures as well as a legislative disadvantage *vis-a-vis* the executive.

Over the years, sessions lasted progressively longer. Initially, they ran about 70 days; by the early 1980s, sessions over twice that length were common. Alaskans both inside and outside the legislature grew increasingly skeptical that all of this time was spent wisely and productively. In 1978, the legislature (stopping short of adopting an amendment) asked Alaskans to cast an advisory vote on limiting the length of regular sessions to 120 days. The proposition asked voters whether a constitutional amendment to that effect should be placed before them in the 1980 election. The voters responded strongly in the affirmative. Three years later the legislature acted to put an amendment before the electorate in the 1984 general election that would limit the session to 120 days. It was ratified by a large majority (150,999 to 46,099).

In May 1986, at the end of the 120th day of the second regular session of the fourteenth legislature, legislative leaders stopped the clock in order to complete business before the adjournment deadline. A suit was filed challenging the legality of the 29 laws passed after midnight. The Alaska Supreme Court rejected the challenge, holding that the day the legislature convenes should not be counted against the 120-day limit, so the legislature has, in effect, a total of 121 days in which to transact business (*Alaska Christian Bible Institute v. State*, 772 P.2d 1079, 1989).

The call for deadlines for scheduling session work, found in the last sentence of this section, is an effort to mitigate the perennial problem of the "logjam" of legislation at the end of the session (most of the bills that pass the legislature are enacted in the closing days of the session, often in long, wearisome meetings which are not conducive to the studious deliberation of each item).

At the end of the second regular session of the seventeenth legislature (1991 - 1992), both houses adjourned before work was completed on several appropriation bills. In this case it was too late to extend the regular session according to the provision in this section, so the legislature called a special session to finish its business.

Section 11. Interim Committees

There shall be a legislative council, and the legislature may establish other interim committees. The council and other interim committees may meet between legislative sessions. They may perform duties and employ personnel as provided by the legislature. Their members may receive an allowance for expenses while performing their duties.

This section authorizes the legislature to carry on business with the help of staff between sessions. These powers were considered essential for the legislature to become an efficient and effective body, fully the equipoise of a strong governor. At the time of the constitutional convention, the concept of the legislative council was becoming popular nationwide as a means of strengthening the legislative branch by giving it organizational continuity between sessions, leadership in the area of policy making, and professional research and bill-drafting services. The Alaska territorial legislature had created a legislative council in 1953, and the delegates considered it such a successful innovation that they did not want to leave to chance its continuation under statehood. (The general import of the council at that time is revealed in the fact that the *Model State Constitution* devoted four separate sections to it in the otherwise terse legislative article.)

Today the Alaska legislative council oversees the work of the Legislative Affairs Agency, which performs day-to-day administrative functions for the legislature such as accounting, property management, data processing, public information, teleconferencing, printing, bill drafting and maintaining a reference library. The council does not play a role in policy development as it did in the early years. It is composed of fourteen legislators, seven from each house, including the president of the senate and the speaker of the house. The council is now one of four permanent interim committees of the legislature. The others

are the legislative budget and audit committee (which oversees the legislative auditor and the legislative finance division), the administrative regulation review committee, and the ethics committee.

The second sentence of this section allows interim committees to meet between sessions. Does this suggest that special committees and the regular standing committees (finance, state affairs, judiciary, and others) must confine their activity to the session? The legislature has not read this section to restrict the activities of standing or special committees, which routinely work between sessions.

A major political controversy over budgetary matters developed during the 1970s between the legislative and executive branches, the solution to which was sought in amendments to this section. The controversy concerned the ability of the legislative budget and audit committee to jointly review and approve with the governor budget revisions when the legislature was not in session. This had been a common practice in Alaska and elsewhere until questions about its constitutionality were raised around the country. State courts elsewhere ruled that it violated the separation of powers doctrine and constituted an improper delegation of legislative power. In 1977, the Alaska legislature amended the executive budget act to authorize the legislative budget and audit committee to review and authorize budget revisions jointly with the governor between sessions (ch 74 SLA 1977). The governor vetoed the bill as being "clearly unconstitutional." The legislature overrode the veto and shortly thereafter took the administration to court over the matter (*Kelly v. Hammond*, Civil Action No 77-4, Juneau Superior Court). The lower court sided with the governor, who then prevailed on the legislature to put the matter before the voters as a constitutional amendment, and the suit was dismissed.

Voters defeated the proposed amendment at the general election in 1978. A second attempt was made in 1980, when the voters rejected essentially the same amendment by an even wider margin. Consequently, the entire legislature must act on all appropriations and any subsequent modifications of them.

ALASKA STATE LEGISLATURE
SESSION LENGTH AND PERCENTAGE OF DAYS WITH FLOOR SESSIONS, 1981-1996

		HOUSE				SENATE			
LEGISLATURE	YEAR	SPEAKER	SESSION LENGTH(1)	NOT IN SESSION(2)	PERCENTAGE OF DAYS IN SESSION	PRESIDENT	SESSION LENGTH(1)	NOT IN SESSION(2)	PERCENTAGE OF DAYS IN SESSION
Twelfth	1981(4) 1982	J. Duncan J. Duncan	165 143	45 54	68%	J. Kerttula J. Kerttula	164 144	46 38	73%
Thirteenth	1983 1984	J. Hayes J. Hayes	161 152	62 53	64%	J. Kerttula J. Kerttula	162 152	45 46	71%
Fourteenth (First legislature under 120-day session limit)	1985(4) 1986	B. Grussendorf B. Grussendorf	119 120	50 52	57%	D. Bennett D. Bennett	119 120	33 33	73%
Fifteenth	1987(4) 1988	B. Grussendorf B. Grussendorf	122 121	54 49	58%	J. Faiks J. Faiks	121 121	33 36	72%
Sixteenth	1989 1990(4)	S. Cotten S. Cotten	121 122(3)	50 46	61%	T. Kelly T. Kelly	121 121	32 33	74%
Seventeenth	1991 1992(4)	B. Grussendorf B. Grussendorf	122(3) 122(3)	54 53	57%	R. Eliason R. Eliason	121 121	55 56	55%
Eighteenth	1993 1994(4)	R. Barnes R. Barnes	121 121	54 51	57%	P. Halford R. Halford	121 121	44 54	60%
Nineteenth	1995 1996(4)	G. Phillips G. Phillips	121 121	47 54	58%	D. Pearce D. Pearce	121 121	41 52	62%

Notes:
(1)Session lengths as published in "Summary of Alaska Legislation," Legislative Affairs Agency, Alaska State Legislature.
(2)Information obtained from Alaska State Legislature's printed House and Senate Journals, and Legislative Affairs Agency Folioviews Database.
(3)House adjourned after midnight on the 121st day.
(4)Legislature went into special session.

Prepared by Legislative Research Services, June 1996 (96.069).

NATIONAL CONFERENCE of STATE LEGISLATURES

The Forum for America's Ideas

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LEGISLATIVE SESSIONS

Annual v. Biennial.

In the early 1960s, only 19 state legislatures met annually. The remaining 31 held biennial regular sessions. All but three (Kentucky, Mississippi and Virginia) held their biennial session in the odd-numbered year. Ten of the 19 states with annual sessions limited the "off-year" to consideration of budgetary and fiscal matters.

By the mid-1970s, the number of states meeting annually grew tremendously--up from 19 to 41. However, several of these states used a "flexible" session format in which the total days of session time was divided between two years; these states included Minnesota, North Carolina, Tennessee and Vermont.

Today, 43 state legislatures meet annually. The remaining seven states--Arkansas, Kentucky, Montana, Nevada, North Dakota, Oregon and Texas--hold session every other year. Six of the biennial legislatures hold their regular sessions in the odd year; the seventh--Kentucky--holds its regular session in the even year. Six states have limited scope sessions--that is, where one year of the biennium is limited to consideration of specific types of legislation. The states with limited scope sessions are Connecticut, Louisiana, Maine, New Mexico, North Carolina and Wyoming.

Washington and New Hampshire were the last states to switch from biennial to annual sessions, doing so in 1981 and 1985, respectively. A November 1998 constitutional amendment to move Kentucky to annual sessions was defeated.

Session Length.

In the early 1960s, 17 states did not place restrictions on the length of their legislative sessions. In another 10 states, the limits were indirect, being set by; restrictions on legislator compensation, per diem or travel reimbursements. Several states increased their session length. These were Colorado (from 120 to 160); Georgia (from 80 to 85); Kansas (from 90 to 120); Minnesota (from 90 to 120); and South Dakota (from 60 to 75).

Throughout the 1970s, 1980s and early 1990s, session limitations were becoming more defined. Fewer states had unrestricted sessions, and the number of states with indirect session limits had fallen.

Currently, only 11 states do not place a limit on the length of regular session. The remaining 39 set limits through a variety of ways. Constitutional provisions establish the limits in 29 states. Indirect limits on legislator compensation, per diem or mileage reimbursement are in effect in 4 states. Statutory provisions set the restrictions in 3, and another 3 use chamber rules.

The recent trend is to shorten session lengths. For example, Colorado's session was cut to 120 days in 1988. In 1992, Louisiana changed its constitution to shorten and limit the scope of its even-year session. The most recent limit was imposed in Nevada; the November 1998 constitutional amendment restricts session to 120 days.

Session Length Limits

State	1962-63	1972-73	1982-83	Dec 1998
Alabama	36 L	36 L	30 L in 105 C	30 L in 105 C
Alaska	None	None	None	120 C
Arizona	63 C (indirect)	None	Sat of week in which 100th C falls (chamber rule)	Sat of week in which 100th C falls (chamber rule)
Arkansas	60 C	60 C	60 C	60 C
California	Odd-120 C Even-30 C	None	None	Odd-Sept 12 Even-Aug 31
Colorado	160 C within biennium (indirect)	None	Odd-None Even-140 C	120 C
Connecticut	Wed after 1st Mon in June	Odd-Wed after 1st Mon in June Even-Wed after 1st Mon in May	Odd-Wed after 1st Mon in June Even-Wed after 1st Mon in May	Odd-Wed after 1st Mon in June Even- Wed after 1st Mon in May
Delaware	Odd-90 L Even-30 L	June 30	June 30	June 30
Florida	60 C	60 C	60 C	60 C
Georgia	Odd-45 C Even-40 C	Odd-45 L Even-40 L	40 L	40 L
Hawaii	Odd-60 C Even-30 C	60 L	60 L	60 L
Idaho	60 C (indirect)	60 C (indirect)	None	None
Illinois	None (by custom-July 1)	None	None	None
Indiana	61 C	Odd-61 L or April 30 Even-30 L or March 15	Odd-61 L or April 30 Even-30 L or March 15	Odd-Apr 29 Even-Mar 14 (by statute)
Iowa	None	None	(indirect)	Odd-110 C Even-100 C (indirect)
Kansas	Odd-90 L Even-30 C (indirect)	Odd-90 C Even-60 C (indirect)	Odd-None Even-90 C	Odd-None Even-90 C
Kentucky	60 L	60 L	60 L	60 L or Apr 15
Louisiana	Odd-30 C Even-60 C	Odd-30 C Even 60 C	60 L in 85 C	Odd-60 L in 85 C Even-30 L in 45 C
Maine	None	None	Odd-100 L Even-50 L	Odd-3rd Wed in June Even-3rd Wed in Apr (by statute)
Maryland	Odd-90 C Even-30 C	90 C	90 C	90 C
Massachusetts	None	None	None	Formal sessions: Odd-3rd Wed in November Even-July 31 Informal sessions: None (by chamber rule)
Michigan	None	None	None	None

State	1962-63	1972-73	1982-83	1998
Minnesota	120 L	120 L	120 L total within biennium or 1st Mon after 3rd Sat in May each year	120 L total within biennium or 1st Mon after 3rd Sat in May each year
Mississippi	None	90 C except year after gub elect, then 125 C	90 C except year after gub elect, then 125 C	90 C except year after gub elect, then 125 C
Missouri	July 15	Odd-June 30 Even-May 15	Odd-June 30 Even-May 15	May 30
Montana	60 C	60 L	90 L	90 L
Nebraska	None	Odd-90 L Even-60 L	Odd-90 L Even-60 L	Odd-90 L Even-60 L
Nevada	60 C (indirect)	60 C (indirect)	60 C (indirect)	120 C
New Hampshire	July 1 (indirect)	90 days or July 1 (indirect)	90 L or July 1 (indirect)	45 L or July 1 (indirect)
New Jersey	None	None	None	None
New Mexico	60 C	Odd-60 C Even-30 C	Odd-60 C Even 30 C	Odd-60 C Even-30 C
New York	None	None	None	None
North Carolina	120 C (indirect)	None	None	None
North Dakota	60 L	60 L	80 L	80 L
Ohio	None	None	None	None
Oklahoma	None	90 L	90 L	Last Fri in May
Oregon	None	None	None	None
Pennsylvania	None	None	None	None
Rhode Island	60 L (indirect)	60 L (indirect)	60 L (indirect)	60 L (indirect)
South Carolina	None	None	1st Thurs in June (by statute)	1st Thurs in June (by statute)
South Dakota	Odd-45 L Even-30 L	Odd-45 L Even-30 L	Odd-40 L Even-35 L	Odd-40 L Even-35 L
Tennessee	75 C (indirect)	90 L	90 L (indirect)	90 L (indirect)
Texas	140 C	140 C	140 C	140 C
Utah	60 C	Odd-60 C Even-20 C	Odd-60 C Even-20 C	45 C
Vermont	None	None	(indirect)	None
Virginia	60 C (indirect)	Odd-30 C Even-60 C	Odd-30 C Even-60 C	Odd-30 C Even-60 C
Washington	60 C	60 C	Odd-105 C Even-60 C	Odd-105 C Even-60 C
West Virginia	Odd-60 C Even 30 C	60 C	60 C	60 C
Wisconsin	None	None	None	None
Wyoming	40 C	Odd-40 L Even 20 L	Odd-40 L Even-20 L	Odd-40 L Even-20 L

Key:

C = calendar day
L = legislative day

Solid highlight = biennial

STRIPED HIGHLIGHT = "FLEXIBLE" SESSION FORMAT

Table 3.2
LEGISLATIVE SESSIONS: LEGAL PROVISIONS

State or other jurisdiction	Regular sessions: Year	Regular sessions: Legislature convenes: Month	Regular sessions: Legislature convenes: Day	Regular sessions: Limitation on length of session (a)	Special sessions: Legislature may call	Special sessions: Legislature may determine subject	Special sessions: Limitation on length of session
Alabama	Annual	Jan. Apr. Feb.	2nd Tues. (b) 3rd Tues. (c, d) 1st Tues. (e)	30 L in 105 C	No	Yes (f)	12 L in 30
Alaska	Annual	Jan. Jan.	2nd Mon. 3rd Mon. (g)	120 C (h)	By 2/3 vote of members	Yes (i)	30 C
Arizona	Annual	Jan.	2nd Mon.	(j)	By petition, 2/3 members, each house	Yes (i)	None
Arkansas	Biennial-odd year	Jan.	2nd Mon.	60 C (h)	No	Yes (f,k)	(k)
California	(l)	Jan.	1st Mon. (d)	None	No	No	None
Colorado	Annual	Jan.	2nd Wed.	120 C	By request, 2/3 members, each house	Yes (i)	None
Connecticut	Annual (m)	Jan. Feb.	Wed. after 1st Mon. (n) Wed. after 1st Mon. (o)	(p)	Yes (q)	(q)	None (r)
Delaware	Annual	Jan.	2nd Tues.	June 30	Joint call, presiding officers, both houses	Yes	None
Florida	Annual	Mar.	Tues. after 1st Mon. (d)	60 C (h)	Joint call, presiding officers, both houses	Yes (f)	20 C (h)
Georgia	Annual	Jan.	2nd Mon.	40 L	By petition, 3/5 members, each house	Yes (i)	(s)
Hawaii	Annual	Jan.	3rd Wed.	60 L (h)	By petition, 2/3 members, each house	Yes	30 L (h)
Idaho	Annual	Jan.	Mon. on or nearest 9th day	None	No	No	20 C
Illinois	Annual	Jan.	2nd Wed.	None	Joint call, presiding officers, both houses	Yes (i)	None
Indiana	Annual	Jan.	2nd Mon. (d, t)	odd-61 L or Apr. 30; even-30 L or Mar. 15	No	No	30 L or 40
Iowa	Annual	Jan.	2nd Mon.	(u)	No	No	None
Kansas	Annual	Jan.	2nd Mon.	odd-None; even-90 C (h)	Petition to governor of 2/3 members, each house	Yes	None
Kentucky	Biennial-even year	Jan.	Tues after 1st Mon. (d)	60 L (v)	No	No	None
Louisiana	Annual	Mar. Apr.	last Mon. (d, n) last Mon. (m, o)	odd-60 L in 85 C; even-30 L in 45 C	By petition, majority, each house	Yes (i)	30 C
Maine	(Lm)	Dec. Jan.	1st Wed. (b) Wed. after 1st Tues. (o)	3rd Wed. of June (h) 3rd Wed. of April (h)	Joint call, presiding officers, with consent of of majority of members of each political party, each house	Yes (i)	None
Maryland	Annual	Jan.	2nd Wed.	90 C (g)	By petition, majority, each house	Yes	30 C
Massachusetts	Annual	Jan.	1st Wed.	(w)	By petition (x)	Yes	None
Michigan	Annual	Jan.	2nd Wed. (d)	None	No	No	None
Minnesota	(y)	Jan.	Tues. after 1st Mon. (n)	120 L or 1st Mon. after 3rd Sat. in May (y)	No	Yes	None
Mississippi	Annual	Jan.	Tues. after 1st Mon.	125 C (h, z); 90C (h, z)	No	No	None
Missouri	Annual	Jan.	Wed. after 1st Mon.	May 30	By petition, 3/4 members, each house	Yes	30 C (aa)
Montana	Biennial-odd year	Jan.	1st Mon.	90 L	By petition, majority, each house	Yes	None
Nebraska	Annual	Jan.	Wed. after 1st Mon.	odd-90 L (h); even-60 L (h)	By petition, 2/3 members	Yes	None
Nevada	Biennial-odd year	Jan.	3rd Mon.	60 C (u)	No	No	20 C (u)
New Hampshire	Annual	Jan.	Wed. after 1st Tues. (d)	45 L	By 2/3 vote of members, each house	Yes	15 L (u)
New Jersey	Annual	Jan.	2nd Tues.	None	By petition, majority, each house	Yes	None
New Mexico	Annual (m)	Jan.	3rd Tues.	odd-60 C; even-30 C	By petition, 3/5 members, each house	Yes (i)	30 C
New York	Annual	Jan.	Wed. after 1st Mon.	None	By petition, 2/3 members, each house	Yes (i)	None
North Carolina	(y)	Jan.	3rd Wed. after 2nd Mon. (n)	None	By petition, 3/5 members, each house	Yes	None
North Dakota	Biennial-odd year	Jan.	Tues. after Jan. 3, but not later than Jan. 11 (d)	80 L (bb)	No	Yes	None
Ohio	Annual	Jan.	1st Mon.	None	Joint call, presiding officers, both houses	Yes	None
Oklahoma	Annual	Feb.	1st Mon. (cc)	160 C	By vote, 2/3 members, each house	Yes (i)	None
Oregon	Biennial-odd year	Jan.	2nd Mon. after 1st Tues.	None	By petition, majority, each house	Yes	None
Pennsylvania	Annual	Jan.	1st Tues.	None	By petition, majority each house	No	None
Rhode Island	Annual	Jan.	1st. Tues.	60 L (u)	No	No	None
South Carolina	Annual	Jan.	2nd Tues. (d)	1st Thurs. in June (h)	No	Yes	None
South Dakota	Annual	Jan.	2nd Tues.	odd-40 L; even-35 L	No	No	None
Tennessee	Annual	Jan.	(dd)	90 L (u)	By petition, 2/3 members, each house	Yes	30 L (u)
Texas	Biennial-odd year	Jan.	2nd Tues.	140 C	No	No	30 C
Utah	Annual	Jan.	3rd. Mon.	45 C	No	No	30 C (ee)
Vermont	(y)	Jan.	Wed. after 1st Mon. (n)	None	No	Yes	None
Virginia	Annual	Jan.	2nd Wed.	odd-30 C (h); even-60 C (h)	By petition, 2/3 members, each house	Yes	None
Washington	Annual	Jan.	2nd Mon.	odd-105 C; even-60 C	By vote, 2/3 members, each house	Yes	30 C
West Virginia	Annual	Feb. Jan.	2nd Wed. (c, d) 2nd Wed. (c)	60 C (h)	By petition, 3/5 members, each house	Yes (ff)	None
Wisconsin	Annual (gg)	Jan.	1st Mon. (n)	None	No	No	None

See footnotes at end of table.

LEGISLATIVE SESSIONS: LEGAL PROVISIONS — Continued

State or other jurisdiction	Regular sessions: Year	Legislature convenes: Month	Legislature convenes: Day	Limitation on length of session (a)	Special sessions: Legislature may call	Special sessions: Legislature may determine subject	Special sessions: Limitation length o session
Wyoming	Annual (m)	Jan. Feb.	2nd Tues. (n) 3rd Mon. (o)	odd-40 L; even-20 L	No	Yes	None
Dist. of Columbia	(hh)	Jan.	2nd day	None			
American Samoa	Annual	Jan. July	2nd Mon. 2nd Mon.	45 L 45 L	No	No	None
Guam	Annual	Jan.	2nd Mon. (ii)	None	No	No	None
No. Mariana Islands	Annual	(jj)	(d, jj)	90 L (jj)	Upon request of presiding officers, both houses	Yes (l)	10 C
Puerto Rico	Annual	Jan.	2nd Mon.	None	No	No	20 C
U.S. Virgin Islands	Annual	Jan.	2nd Mon.	None	No	No	None

Sources: State constitutions and statutes.

Note: Some legislatures will also reconvene after normal session to consider bills vetoed by governor. Connecticut–if governor vetoes any bill, secretary of state must reconvene General Assembly on second Monday after the last day on which governor is either authorized to transmit or has transmitted every bill with his objections, whichever occurs first; General Assembly must adjourn *sine die* not later than three days after its reconvening. Hawaii–legislature may reconvene on 45th day after adjournment *sine die*, in special session, without call. Louisiana–legislature meets in a maximum five-day veto session on the 40th day after final adjournment. Missouri–if governor returns any bill on or after the fifth day before the last day on which legislature may consider bills (in even-numbered years), legislature automatically reconvenes on first Wednesday following the second Monday in September for a maximum 10 C sessions. New Jersey–legislature meets in special session (without call or petition) to act on bills returned by governor on 45th day after *sine die* adjournment of the regular session; if the second year expires before 15th day, the day preceding the end of the legislative year. Utah–if 2/3 of the members of each house convening to consider vetoed bills, a maximum five-day session is set by the presiding officers. Virginia reconvenes on sixth Wednesday after adjournment for a maximum three-day session (may be extended to seven days upon vote of majority of members elected to each house). Washington–upon petition of 2/3 of the members of each house, legislature meets 45 days after adjournment for a maximum five-day session.

Key:

C — Calendar day

L — Legislative day (in some states called a session day or workday; definition may vary slightly, however, generally refers to any day on which either house of legislature is in session).

(a) Applies to each year unless otherwise indicated.

(b) General election year (quadrennial election year).

(c) Year after quadrennial election.

(d) Legal provision for organizational session prior to stated convening date. Alabama–in the year after quadrennial election, second Tuesday in January for 10 C. California–in the even-numbered general election year, first Monday in December for an organizational session, recess until the first Monday in January of the odd-numbered year. Florida–in general election year, 14th day after election. Indiana–third Tuesday after first Monday in November. Kentucky–in odd-numbered year, Tuesday after first Monday–in January for 10 L. Louisiana–in year after general election, second Monday in January, not to exceed 3 L. Michigan–held in odd-numbered year. New Hampshire–in even-numbered year, first Wednesday in December. North Dakota–in December. South Carolina–in even-numbered year, Tuesday after certification of election of its members for a maximum three-day session. West Virginia–in year after general election, on second Wednesday in January. No. Mariana Islands–in year after general election, second Monday in January.

(e) Other years.

(f) By 2/3 vote each house.

(g) Following a gubernatorial election year.

(h) Session may be extended by vote of members in both houses. Alaska–2/3 vote for 10-day exte Arkansas–2/3 vote. Florida–3/5 vote. Hawaii–petition of 2/3 membership for maximum 15-day exte Kansas–2/3 vote. Maine–2/3 vote for maximum 10 L. Maryland– 3/5 vote for maximum 30 C. Missis 2/3 vote for 30 C extension, no limit on number of extensions. Nebraska–4/5 vote. South Carolina–2/3 Virginia–2/3 vote for 30 C extension. West Virginia–2/3 vote (or if budget bill has not been acted upon days before session ends, governor issues proclamation extending session). Puerto Rico–Joint resolutio

(i) Only if legislature convenes itself. Special sessions called by the legislature are unlimited in sc Arizona, Georgia, Maine, and New Mexico.

(j) No constitutional or statutory provision; however, legislative rules require that regular sessions a no later than Saturday of the week during which the 100th day of the session falls.

(k) After governor's business has been disposed of, members may remain in session up to 15 C by a 2/ of both houses.

(l) Regular sessions begin after general election, in December of even-numbered year. In California, le ture meets in December for an organizational session, recesses until the first Monday in January of the numbered year and continues in session until Nov. 30 of next even-numbered year. In Maine, session begins in December of general election year runs into the following year (odd-numbered); second s begins in next even-numbered year.

(m) Second session limited to consideration of specific types of legislation. Connecticut–individual le tors may only introduce bills of a fiscal nature, emergency legislation and bills raised by committees. L ana–fiscal matters. Maine–budgetary matters; legislation in the governor's call; emergency legislation; le tion referred to committees for study. New Mexico–budgets, appropriations and revenue bills; bills pursuant to governor's message; vetoed bills. Wyoming–budget bills.

(n) Odd-numbered years.

(o) Even-numbered years.

(p) Odd-numbered years–not later than Wednesday after first Monday in June; even-numbered-yea later than Wednesday after first Monday in May.

(q) Constitution provides for regular session convening dates and allows that sessions may also be held "such other times as the General Assembly shall judge necessary." Call by majority of legislators is impli

(r) Upon completion of business.

(s) Limited to 40 L unless extended by 3/5 vote and approved by the governor, except in cases of imp ment proceedings.

LEGISLATIVE SESSIONS: LEGAL PROVISIONS — Continued

(t) Legislators may reconvene at any time after organizational meeting; however, second Monday in January is the final date by which regular session must be in process.

(u) Indirect limitation; usually restrictions on legislator's pay, per diem, or daily allowance.

(v) May not extend beyond April 15.

(w) Legislative rules say formal business must be concluded by Nov. 15th of the 1st session in the biennium, or by July 31st of the 2nd session for the biennium.

(x) Joint rules provide for the submission of a written statement requesting special session by a specified number of members of each chamber.

(y) Legal provision for session in odd-numbered year; however, legislature may divide, and in practice has divided, to meet in even-numbered years as well.

(z) 90 C sessions every year, except the first year of a gubernatorial administration during which the legislative session runs for 125 C.

(aa) 30 C if called by legislature; 60 C if called by governor.

(bb) No legislative day is shorter than a natural day.

(cc) Odd number years will include a regular session commencing on the first Tuesday after the first Monday in January and recessing not later than the first Monday in February of that year. Limited constitutional d can be performed.

(dd) Commencement of regular session depends on concluding date of organizational session. Legisla meets, in odd-numbered year, on second Tuesday in January for a maximum 15 C organizational session, returns on the Tuesday following the conclusion of the organizational session.

(ee) Except in cases of impeachment.

(ff) According to a 1955 attorney general's opinion, when the legislature has petitioned to the governor called into session, it may then act on any matter.

(gg) The legislature, by joint resolution, establishes the session schedule of activity for the remainder o biennium at the beginning of the odd-numbered year.

(hh) Each Council period begins on January 2 of each odd-numbered year and ends on January 1 o following odd-numbered year.

(ii) Legislature meets on the first Monday of each month following its initial session in January.

(jj) 60 L before April 1 and 30 L after July 31.

Table 3.19
BILL AND RESOLUTION INTRODUCTIONS AND ENACTMENTS: 1996 AND 1997 REGULAR SESSIONS

State or other jurisdiction	Duration of session**	Introductions		Enactments		Measures vetoed by governor	Length of session
		Bills	Resolutions	Bills	Resolutions		
Alabama	Feb. 6-May 20, 1996	1,793	760	437	367	20 (a)	30L
	Feb. 4-May 19, 1997	1,832	741	387	385	47 (a)	30L
Alaska	Jan. 4-May 19, 1996	342	77	146	39	20 (a)	122C
	Jan. 13-May 11, 1997	495	132	113	51	10 (a)	119C
Arizona*	Jan. 10-April 17, 1994	1,160	60	380	17	0	98C
	Jan. 9-April 13, 1995	957	70	300	23	8	95C
Arkansas	No regular session in 1996						
	Jan. 13-May 2, 1997 (b)	2,041	149	1,362	N.A.	9 (a)	96C
California	Jan. 3-Sept. 1, 1996	2,367	146	1,174	83	114	127L
	Dec. 2, 1996-Sept. 13, 1997	3,024	233	951	136	197	139L
Colorado	Jan. 10-May 8, 1996	615	94	344	84	19	120C
	Jan. 8-May 7, 1997	598	113	338	101	27	120C
Connecticut*	Feb. 9-May 4, 1994	1,296	161	263	144	4 (a)	85C
	Jan. 4-June 7, 1995	3,226	256	387	149	2	155C
Delaware	Jan. 16-June 30, 1996	538	181	309	16	3	49L
	Jan. 14-June 30, 1997	628	187	220	14	5	51L
Florida*	Feb. 8-April 15, 1994	2,447	210	380	0	15	60C
	Mar. 7-May 11, 1995	2,605	152	473	0	28	60C
Georgia	Jan. 8-Mar. 18, 1996	975	1,017	458	881	16	40L
	Jan. 13-Mar. 28, 1997	1,515	1,176	511	975	15	40L
Hawaii	Jan. 17-April 29, 1996	3,064	1,209	315	235	27	60L
	Jan. 15-May 1, 1997	4,287	961	383	211	14	61L
Idaho	Jan. 8-Mar. 15, 1996	774	63	433	22	8	68C
	Jan. 6-Mar. 19, 1997	695	57	404	38	5	73C
Illinois	Jan. 10-May 25, 1996	3,038	259	275	90	13 (a)	(c)
	Jan. 8-May 17, 1997	3,484	293	537	245	88 (a)	(c)
Indiana*	Nov. 16, 1993-Mar. 4, 1994	888	24	179	2	0	30L
	Nov. 22, 1994-April 29, 1995	1,504	50	34	6	11 (a)	61L
Iowa	Jan. 8-May 1, 1996	981	10	220	1	13	115C
	Jan. 13-April 29, 1997	1,290	32	217	2	13	107C
Kansas	Jan. 8-May 23, 1996	876	47	272	15	3 (d)	69L
	Jan. 13-May 27, 1997	970	41	192	10	2	68L
Kentucky	Jan. 2-April 15, 1996	1,333	323	357	239	1	60L
	No regular session in 1997						
Louisiana	April 29-June 12, 1996	313	306	45	254	0	30L
	Mar. 31-June 23, 1997	4,087	636	1,487	488	19	60L
Maine*	Jan. 5-April 14, 1994	615	11	340	0	12 (a)	29L
	Dec. 7-June 30, 1995	1,586	33	607	2	1	70L
Maryland	1996 N.A.	2,259	30	692	7	104	90C
	Jan. 8-April 7, 1997	2,385	45	759	8	132	90C
Massachusetts*	Jan. 8, 1992-Jan. 5, 1993	7,353	0	414	0	39 (a)	(c)
	Jan. 6, 1993-Jan. 4, 1994	7,667	0	498	0	53 (a)	(c)
Michigan*	Jan. 12-Dec. 29, 1994	1,103	20	451	2	10	352 (c)
	Jan. 11-Dec. 28, 1995	2,299	43	291	2	4	352 (c)
Minnesota	Jan. 16-April 3, 1996	2,398	0	187	1	19	47L
	Jan. 7-May 19, 1997	4,258	0	235	4	15	63L
Mississippi*	Jan. 7-May 16, 1992	2,693	535	676	221	0	125C
	Jan. 5-April 2, 1993	4,346	3[illegible]	406	155	17	90C
Missouri*	Jan. 5-May 13, 1994	1,256	[illegible]	180	3	6	129C
	Jan. 4-May 12, 1995	1,242	[illegible]	170	4	5	129C
Montana	No regular session in 1996						
	Jan. 6-April 23, 1997	1,013	75	552	56	7 (a)	87L
Nebraska	Jan. 3-April 18, 1996	503	26	182	2	5	60L
	Jan. 8-June 12, 1997	891	53	307	8	5 (a)	90L
Nevada	No regular session in 1996						
	Jan. 20-July 7, 1997	1,167	202	691	158	3	169C

See footnotes at end of table.

INTRODUCTIONS AND ENACTMENTS: REGULAR SESSIONS — Continued

State or other jurisdiction	Duration of session*	Introductions		Enactments		Measures vetoed by governor	Length of session
		Bills	Resolutions	Bills	Resolutions		
New Hampshire	Jan. 3-June 13, 1996	887	57	302	6	2	23L
	Jan. 8-June 25, 1997	1,007	49	w351	8	4	25L
New Jersey	Jan. 11, 1996-Jan. 9, 1997	4,352	467	168	8	10	(c)
	Jan. 9, 1997-Jan. 8, 1998	1,462	186	259	6	18 (a)	N.A.
New Mexico	Jan. 16-Feb. 15, 1996	1,586	43	146	12	57	30C
	Jan. 21-Mar. 22, 1997	2,617	35	370	6	102	60C
New York*	Jan. 8-July 30, 1992	17,667	3,731	846	3,731	51 (d)	151L
	Jan. 6-July 7, 1993	14,596	3,607	720	3,607	93 (d)	152L
North Carolina	May 13-June 21, 1996	781	32	211	14	0	27L
	Jan. 29-Aug. 28, 1997	2,334	60	528	33	0	123L
North Dakota	No regular session in 1996						
	Jan. 6-April 11, 1997	881	116	554	90	11 (a,d)	66L
Ohio (f)	(g)	379	41	168	23	1	(c)
	(h)	856	77	112	26	1	(c)
Oklahoma	Feb. 6-May 31, 1996	1,638	244	363	145	35	69L
	Jan. 7-May 30, 1997	1,963	242	421	151	24	71L
Oregon	No regular session in 1996						
	Jan. 13-July 5, 1997	3,091	191	871	38	43	174C
Pennsylvania (l)	Jan. 3, 1995-Nov. 26, 1996	4,764	640	377	464	1	(c)
Rhode Island*	Jan. 4-July 17, 1994	3,565	(j)	959	490	38	85L
	Jan. 3-Nov. 17, 1995	3,708	(j)	445	522	24	77L
South Carolina	Jan. 9-June 27, 1996	1,342	N.A.	314	N.A.	21 (a)	(c)
	Jan. 14-June 17, 1997	1,389	775	257	553	19 (a)	64L
South Dakota	Jan. 9-Mar. 11, 1996	651	9	306	2	11 (a)	35L
	Jan. 14-Mar. 26, 1997	557	13	300	3	13 (a)	40L
Tennessee	Jan. 9-April 26, 1996	1,387	830	625	670	3	(c)
	Jan. 14-May 31, 1997	2,044	987	661	N.A.	0	(c)
Texas	No regular session in 1996						
	Jan. 14-June 2, 1997	5,561	166	1,487	15	36	140C
Utah	Jan. 15-Feb. 28, 1996	797	69	348	33	5	45C
	Jan. 20-Mar. 5, 1997	668	63	394	41	6	45C
Vermont	Jan. 3-May 3, 1996	409	128	138	97	1	122C
	Jan. 8-June 13, 1997	738	136	74	120	0	157C
Virginia	Jan. 10-Mar. 11, 1996	2,193	599	1,066	487	16	60C
	Jan. 8-Feb. 22, 1997	1,920	663	933	536	15	N.A.
Washington	Jan. 8-Mar. 7, 1996	1,540	36	325	11	49 (a,d)	60C
	Jan. 13-April 27, 1997	2,408	88	456	12	126 (d)	105C
West Virginia*	Jan.-Mar. 1994	1,293	402	333	206	7	60C
	Jan.-Mar. 1995	1,431	197	303	31	4	60C
Wisconsin	Jan. 3, 1995-Jan. 6, 1996	1,779	201	467	98	8	735C
	Jan. 6, 1997-Jan. 4, 1999 (i)	936 (k)	121 (k)	27 (k)	38 (k)	1 (k)	307C
Wyoming	Feb. 19-Mar. 15, 1996	282	14	126	3	3	20L
	Jan. 14-Mar. 1, 1997	463	20	202	3	1	34L
Puerto Rico	Jan. 8-June 30, 1996	524	1,468	238	602	4	65L
	Jan. 13-June 30, 1997	2,205	1,651	212	678	4	101C
	Aug. 18-Nov. 18, 1997						
U.S. Virgin Islands	Jan. 9-Dec. 19, 1995	169	30	67	23	26	20L
	Jan. 13 -Nov. 18,1997	178	9	60	6	7 (a)	14C

INTRODUCTIONS AND ENACTMENTS: REGULAR SESSIONS — Continued

Source: The Council of State Governments; legislative survey, 1997 except where noted by * where data are from *The Book of the States, 1996-97.*

** Actual adjournment dates are listed regardless of constitutional or statutory limitations. For more information on provisions, see Table 3.2, "Legislative Sessions: Legal Provisions."

Key:

C - Calendar day.

L - Legislative day (in some states, called a session or workday; definition may vary slightly; however, it general refers to any day on which either chamber of the legislature is in session.)

N.A. - Not available.

(a) Number of vetoes overridden: Alabama: 1996-1, 1997-1; Alaska: 1996-1, 1997-6; Arkansas: 1997-8; Connecticut: 1994-2; Illinois: 1996-1, 1997-1; Indiana: 1995-3; Kansas: 1994 - 7 bills and 2 line items: Louisiana: 1; Maine: 1994-1; Massachusetts: 1992-7, 1993- 6; Montana: 1997-3; Nebraska: 1997-1; New Jersey: 1997-1; North Dakota: 1997-2; South Carolina: 1996-11, 1997-8; South Dakota: 1996-2, 1997-1; Washington: 1996-1; U.S. Virgin Islands: 1997-3.

(b) Recessed for two weeks.

(c) Length of session: Illinois: 1996 Senate 47L and House 70L, 1997 Senate 50L and House 63L; Massachusetts: 1992 Senate 37L and House 144L, 1993 Senate 49L and House 150L; New Jersey: 1996 Senate 36L and House 41L; Ohio: 1996 Senate 121L and House 92L, 1997 Senate 126L and House 107L; Pennsylvania: Senate 136L and House 152L; South Carolina: 1996 Senate 67L and House 66L, Tennessee: 1996 Senate 43L and 40L, 1997 Senate 52L and House 51L.

(d) Line item or partial vetoes. Kansas 1996: 17 appropriations - line items. New York - includes line item vetoes in appropriation bills. North Dakota - 2 line item vetoes. Washington - 1996: includes 27 measures partially vetoed; 1997: includes 34 measures partially vetoed.

(e) In addition, an organizational session was held on January 13, 1992.

(f) Preliminary information.

(g) Senate: Jan. 3, 1996-Dec. 31, 1996; House: Jan. 3, 1996-Dec. 27, 1996.

(h) Senate: Jan. 6, 1997-Dec. 11, 1997; House: Jan. 6, 1997-Dec. 10, 1997.

(i) Continuous 1995-1996 session.

(j) Bills and resolutions are not counted separately.

(k) Data as of Nov. 8, 1997.

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Where to cut?

ANCHURAGE TIMES
10/15/99

ONE OF THE questions on the table now, in the wake of last month's election, is simply this: Where does the Legislature make some of the cuts necessary to help reduce the cost of government?

The answer is equally simple: It should start right in the Legislature's own backyard by cutting the enormous fat that has crept into the legislative process.

Basically, there is far too much lawmaking going on, for far too many weeks every year, by far too many people, doing far too little to justify the cost.

The first thing to be done is make big — make that very big — reductions in the number of legislative employees, including staff aides, deputies, secretaries and clerks, part-time and full-time, who have turned the Legislature's operation into a mini-Congress.

The next thing to be done is to cut the length of the annual legislative sessions. Meeting for one-third of the year, every year, year in and year out, to serve a population of 600,000 is ludicrous.

The Alaska Constitution is framed to provide this state with a strong executive branch. The governor is in charge. Unfortunately, in the last decade or two, those who serve and have served in the legislative branch have developed delusions that they are mini-governors, micro-managing state government operations.

There is no reason that legislative sessions could not be cut back routinely to two months every year — or, at the very outside, three months — instead of dragging out for four months. The savings would be enormous.

As proof that this easily could be done, consider this: In any given year, hardly any real lawmaking business happens in the first three or four or five weeks, anyway. That time is spent jousting for positions, political posturing, and other non-productive fun and games in which legislators love to engage, all at public expense.

Further, the Legislature could decide — if statesmanship were a real part of the operations in Juneau — to divide its duties, restricting one session to an intensive budget-setting process to cover a two-year period, in a session lasting no more than 30 or 40 days, and then devote the next session to general lawmaking.

It can be done, and done easily, if there were a will to do so. States many times bigger than Alaska, with populations much greater than ours, have biennial legislative sessions or limit one of their annual sessions to budget-making only.

There is too much time wasted in Juneau. There is too much money wasted in Juneau.

Cut government? That was one of the powerful messages heard in the recent election.

The job should begin within the Legislature itself.

Shorter session, better government

Among the more pertinent pieces of legislation filed this session is a proposed amendment to the state Constitution that would limit the 120-day session to 90 days. If passed, House Joint Resolution No. 1 would require a vote of the people.

It's a worthy concept that keeps surfacing, especially with legislators who live elsewhere, and we think it merits discussion.

Here's why: Every year, Christmas and New Year holidays are very nearly ruined for people preparing to return to Juneau for the session. First, they must wind down their duties and close up their offices before Christmas. Then, they must pack up their belongings and hit the road around the New Year to make it to Juneau in time to settle in for the session. New legislators must be in Juneau by about Jan. 4 so they can take part in orientations. Some legislators and staff members must catch a ferry. Many of them arrive in the capital exhausted, having had their family time over the holidays completely disrupted.

This has spawned an annual sense of dread among many involved in the Legislature, a dread that isn't easily dissolved by the friendliness of Juneau. As one staff member put it, they feel as though they are gerbils on a treadmill: "We get here (Juneau) with a bad attitude."

Rep. Norm Rokeberg and Rep. Jerry Sanders are putting their efforts behind the resolution, the very one that died of neglect last session. Rokeberg argues the Legislature could start later, perhaps in February or early March. So much of what the Legislature does must wait until the March budget forecast from the Department of Revenue, so why not wait to get started until some of the real nuts-and-bolts work can be done?

Years ago, the people of Alaska became frustrated with the Legislature when sessions-without-limits dragged on until June or July. Thus, the 120-day limit was passed by voters. We think an even shorter session would be just as responsive, more cost-effective for the people of Alaska, and possibly even more productive. Other states do it.

Although Juneau would feel an economic impact, the perceived need to move the capital to Anchorage or elsewhere would become far less important.

The idea of a shorter session is also in line with the concept of a citizen-statesman government, one that has legislators spending more time in their districts, working in their own professions and being available to listen to their constituents. And that's a capital idea that would benefit the state as a whole.

JUNEAU EMPIRE
1/26/97

SJR

33

SFIN

FILE

SJR 33

was referred to the Senate Finance Committee

Hearing(s) were held

The bill did not move from Committee

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ALASKA STATE LEGISLATURE

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SENATOR JERRY MACKIE

SENATE MAJORITY LEADER

SPONSOR STATEMENT

SJR 33

Constitutional Amendment on the Permanent Fund

I introduced SJR 33 to find an acceptable long-term solution to the state's revenue deficit problem and bring fiscal security and stability to future state government operations and responsibilities.

SJR 33 is a proposed constitutional amendment that will accomplish three things. It will give every eligible Alaskan a 25 thousand dollar one time payment from the Permanent Fund and end all future dividends. Secondly, earnings from the 12 billion dollars remaining in the fund will be available for the original, primary purpose of the Permanent Fund. That purpose was to provide a revenue source for necessary and essential public services when facing the effects of declining oil revenues. Finally, the proposal requires approval by a majority vote of the people.

There certainly are other ways to stem the current deficit spending spiral. The voter rejection of last year's long-term plan, however, shows that any new proposal must not only provide a real budget solution, but it must also be acceptable to the electorate.

Moreover, the vote last September seems to have deadened any further administrative or legislative efforts to address the long-term aspects of our budget

situation. This is a situation that inevitably will worsen with inattention. Not only are drastic spending cuts and taxes a looming presence, but also the dividend program itself is in jeopardy.

The constitutional amendment proposed by SJR 33 is a long-term solution to our revenue problems. I believe it would be approved in the coming general election.

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

MEMORANDUM

DATE: January 18, 2000

TO: Senator Mackie

FROM: Jim Kelly
Director of Communications

SUBJECT: **APFC Financial Projection**

You have asked the Alaska Permanent Fund Corporation (APFC) to do a financial projection using certain assumptions which you provided.

You asked us to draw down all Fund income and as much principal as necessary in order to pay each Alaskan a $25,000 dividend in 2001. You have also asked us to assume that all Fund income in subsequent years would be used first to inflation-proof Fund principal, and the balance then would be transferred to the General Fund. You asked us to assume that the Fund earned a rate of return of 8%, 10% and 12%. Based on these assumptions, the table below indicates the amount of income in millions of dollars that would be transferred to the General Fund each year beginning in 2002:

Year	8%	10%	12%
2002	588	884	1,200
2003	615	923	1,252
2004	642	962	1,304
2005	671	1,004	1,360
2006	699	1,046	1,416
2007	729	1,090	1,474
2008	759	1,132	1,530
2009	788	1,176	1,580
2010	817	1,219	1,646
TOTALS:	6,308	9,436	12,762

You have also asked our estimate of per capita dividends for the projection period, based on the status quo. These numbers appear in the following table:

2000	1,888.77
2001	1,900.53
2002	1,877.56
2003	1,772.58
2004	1,695.11
2005	1,768.48
2006	1,828.57
2007	1,894.01
2008	1,962.86
2009	2,034.48
2010	2,108.06
TOTAL:	20,731.00

Senator, I should point out that the rates of return you have asked us to assume – 8%, 10% and 12% – are in excess of what the APFC expects to earn given current Fund asset allocation and capital market assumptions. In addition, these projections represent only our best estimate of the median case; actual performance will vary with market volatility.

PLEASE NOTE THAT THE CORPORATION NEITHER SUPPORTS NOR OPPOSES ANY PROPOSED CHANGES TO THE CURRENT USE OF FUND EARNINGS, EXCEPT AS THEY MAY RELATE TO THE PROPER EXERCISE OF THE TRUSTEES' FIDUCIARY RESPONSIBILITIES AS REQUIRED UNDER THE PRUDENT INVESTOR RULE.

c: APFC Acting Executive Director
APFC Director of Finance

MACKIE PLAN IMPACTS ON STATE PROGRAMS

By Sen. Mackie

1. STUDENT LOANS:

There are 10,100 defaulted loans totaling $80.9 million

8,600 are for less than $10,000.

It is estimated that garnishment of the 25K will close 9000 accounts and return $67 million to the student loan program.

This will support the loan requirements 11,000 students.

2. CHILD SUPPORT DEBTS:

Currently, 11,000 pfd's are garnished in part or in whole for child support debts.

It is estimated that the garnishment of the 25K will collect $103 million of approximately $570 million owed.

This will eliminate 7,500 cases that are less than $25,000 and make a considerable impact on the remaining 3,500 that are greater than $25,000.

3. PRISIONER PFDs:

Garnished PFDs for 3500 prisioners yields $87.5 million.

These funds are currently allocated to
Domestic Violence and Sexual Abuse Programs
Violent Crimes Compensation
Department of Corrections Prisoner Rehab Programs

4. LOW INCOME HOUSING:

Current tenants of low income housing would not be affected by the Mackie Plan as federal income requirements allow for exempting a one time pay out.

It would affect, however, new people trying to get into low income housing. Then, the $25k counts in the income determination and could disqualify many Alaskans for the year 2001.

For families wishing to purchase a home with the $25K pay out, the First Time Homebuyer program of AHFC is well suited to offering low interest rates for low and moderate income families.

5. EDUCATION AND CHILD CARE:

The Mackie Plan does not affect the following low income programs:

Day Care Assistance
USDA Child and Adult Care Food Program
School Meals Eligibility
Head Start

6. HEALTH AND WELFARE:

Generally, the Mackie Plan should greatly assist people to permanently get off welfare. Since welfare benefits are limited to five years duration, the payout may be the key ingredient to attaining a secure economic future.

Alaska Temporary Assistance Program for low income families with dependent children: The Mackie Plan would not affect the program and its hold-harmless costs in FY 01. Because dividends terminate, the program will lose a $6 million funding source in future years.

Adult Public Assistance (APA) and Supplemental Security Income (SSI) for needy aged, blind and disabled persons: The $25K would count as income in determining eligibility for benefits. If the asset is not reduced to the income eligibility level, the current hold-harmless program continues to pay the SSI equivalent for up to 4 months.

Food Stamps: Income requirements for this program is similar to the SSI program above. As such, hold-harmless payments are expected to increase for the extent of the four month period.

Medicaid: The Mackie Plan would not affect the Family Medicaid and Denali Kidcare programs.

7. ALASKANS UNDER THE AGE OF 18 (DOL July, 1999 est.):

193,543 individuals

$25k pay out = $ 4.841 billion

Tony Knowles, Governor

Alaska Department of Community and Economic Development

Division of Banking, Securities, and Corporations
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March 2, 2000

The Honorable Pete Kott
Chair, Judiciary Committee
Alaska House of Representatives
State Capitol Room 118
Juneau, AK 99801-1182

Dear Chairman Kott:

RE: Banking, Securities & Corporations

I was able to view some recent testimony before your committee during which Representative Green asked Representative Davis and Senator Mackie who would protect Alaska investors from scam artists and who could provide some investor education for Alaskans. That Representative Davis and Senator Mackie did not immediately reply those services are provided by the division of banking, securities and corporations, tells me that I have not adequately reached out to members of the legislature to let you know what this division does for the investing public.

Our mission is to protect Alaska investors. We do this by registering or noticing securities and people who effect transactions and offer investment advice to Alaskans. We issue orders against people who violate the Alaska Securities Act, AS 45.55. So far in FY 00, we have issued 8 orders involving 15 respondents, and have levied fines of $108,750. In addition, $133,000 has been returned to Alaska investors due to our direct involvement. We have made filing complaints easier by providing forms on our web site.

We always encourage Alaska investors to check with us before they invest to verify that the security they are buying or the person with whom they are dealing is properly registered. While that does not guarantee it is a good investment, and also does not guarantee the person is honest, in our experience, the worst offenders do not register with appropriate jurisdictions. We can often provide information to investors on the disciplinary history of broker-dealers, agents, investment advisers and their representatives.

While we have never received specific funding for investor education, we do offer investor education services. On our web site, at http://www.dced.state.ak.us/bsc/bsc.htm, we provide an investor education module that provides new information each month on mutual funds and on general investment topics. It also provides archives of past articles. That is a service we provide directly through an investor education service provider. We also provide links to other sites that

contain investor education information on timely subjects such as on-line trading. Finally, we publish on the site various investor alerts to warn people of questionable people or companies that we or other securities regulators may be investigating, and we publish information on the orders we issue.

Through our participation in the North American Securities Administrators Association, we have provided free teaching guides to Alaska teachers to include a financial literacy module in the high school curriculum. This is called the Financial Literacy 2001 program. Depending on funding, we try to make ourselves available to meet with interested parties to discuss securities regulation.

I hope this letter makes it clear why it was apparent to me that I have not provided legislators with sufficient information on the great history of service this division has provided Alaska investors. Depending on resources, we have plans to increase the information available to the public and to improve access via the Internet. We are here to help your constituents with any problems they may have that are covered by the Alaska Securities Act. I would be happy to answer any questions you or members of your committee may have. Thank you.

Yours truly,

Franklin T. Elder
Director

cc: The Honorable Joe Green
The Honorable Eric Croft
The Honorable Gary Davis
The Honorable Jerry Mackie
Mr. Patrick Pourchot, Legislative Director
Ms. Sally Saddler, DCED

Mackie Plan Assumptions

- Alaska voters must approve the plan
- $25,000 payout to all PFD eligible Alaskans
- Dividend program ends after one-time payout
- Remaining principal of Permanent Fund is constitutionally protected
- Permanent Fund is first inflation proofed
- Remaining earnings would go to General Fund

Amount of income in millions of dollars that would be transferred to the General Fund each year beginning in 2002.

Year	8%	10%	12%
2002	588	884	1,200
2003	615	923	1,252
2004	642	962	1,304
2005	671	1,004	1,360
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2007	729	1,090	1,474
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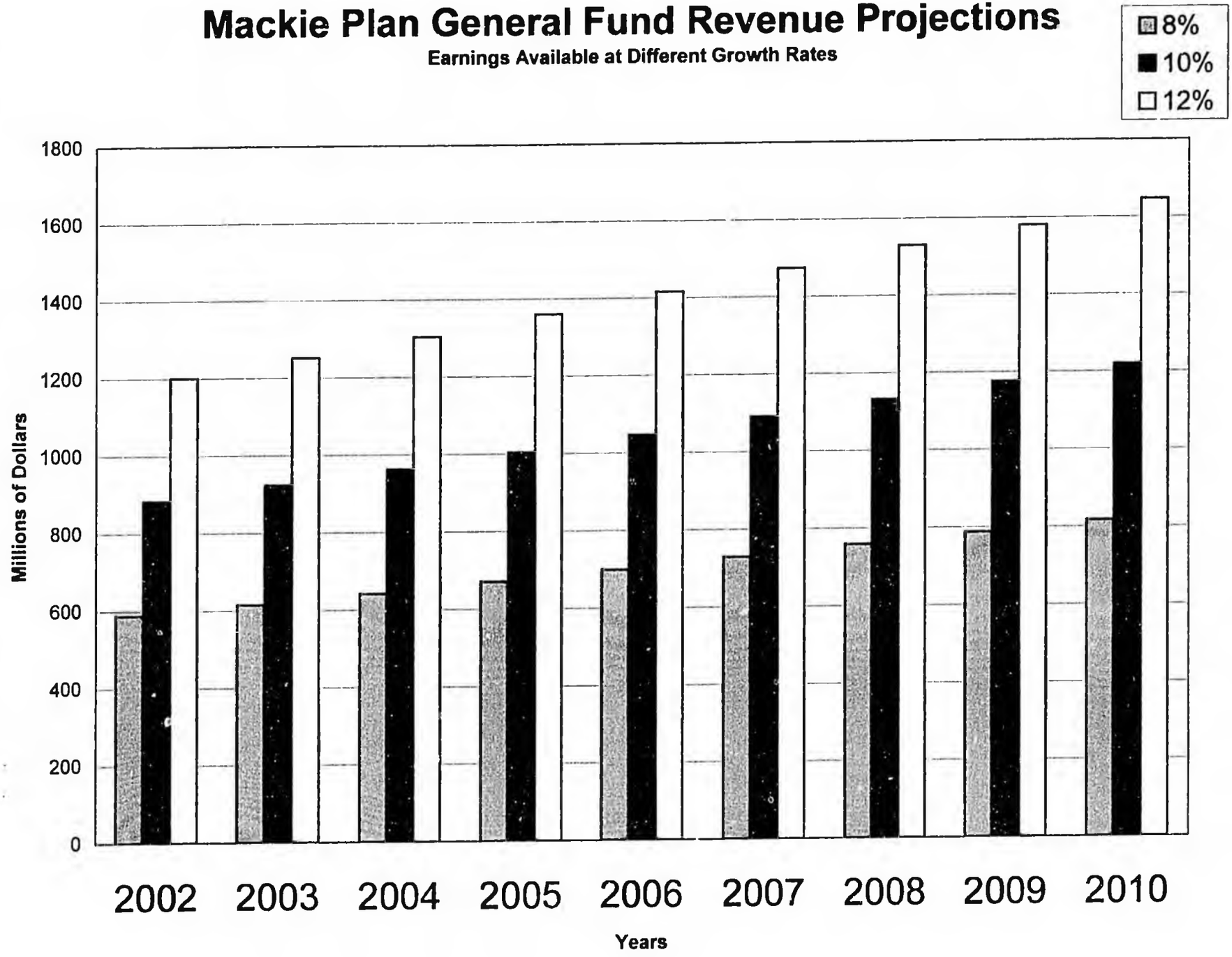
2009	788	1,176	1,580
2010	817	1,219	1,646
Totals:	**6,308**	**9,436**	**12,762**

Mackie Plan General Fund Revenue Projections

Earnings Available at Different Growth Rates



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By Overnight Delivery

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Assistant Attorney General
Alaska Department of Law
Civil Division
P.O. Box 110300
Juneau, AK 99811-0300

RECEIVED
APR 21 1998
SIMPSON, THACHER & BARTLETT,
SORENSEN & LORENSEN

Re: Alaska Permanent fund Corporation

Dear Jim:

You have requested an update of the Report ("Report ") that we provided to the Alaska Permanent Fund Corporation ("APFC") approximately 10 years ago, regarding the question whether the Fund and APFC are subject to federal taxation. I have reviewed the cases and rulings that have been issued since 1988, as well as the statutory amendments made to Title 37, chapter 13 of the Alaska Statutes, Attorney General opinions, and the recent annual reports. This letter summarizes and discusses the legal developments relating to the central legal arguments addressed in our previous report. We assume for purposes of this letter that the factual description of the Alaska Permanent Fund ("Fund") and the APFC contained in the Report are still applicable, apart from the legislative amendments which substituted references to the fund for references to the APFC, and other changes discussed below at page 32.

I. Executive Summary

As before, we believe that there are three primary arguments supporting the position that the income of the Fund and the APFC are not subject to federal taxation.

First, it might be argued that the constitutional doctrine of implied immunity of state instrumentalities from federal taxation applies. As we concluded before, this doctrine has been so narrowly construed that it offers only questionable protection. The few legal developments under this doctrine have only reinforced our previous conclusion.

Second, we relied on a history of IRS rulings, albeit without judicial authority, to argue that income earned by a State or an integral part of a State is not specifically subjected to State taxation. Since 1988, there has been quite a lot of ruling activity related to the integral part doctrine, as well as publication of the first judicial decisions to address it. We believe that these additional authorities strengthen the position that the Fund and the APFC are an integral part of the state and thus not subject to state taxation.

Third, we argued that, in the alternative, the income is excluded under section 115 of the Internal Revenue Code ("Code").[1] Section 115 excludes from gross income any income that is derived from the conduct of an essential governmental function and accrues to a State or political subdivision. At the time of the Report, there were a number of older authorities in this area, but there were no recent authorities. Since 1988, this has been an unusually active area for IRS rulings. Recent case law also has addressed this statute, and the IRS has published one ruling of precedential value. Although we believe that these developments continue to support also the position we took with respect to the Fund and the APFC, they do indicate that the IRS's analysis increasingly turns on the issue of private benefit.

In short, we believe that the legal developments in this area in the last 10 years reinforce the conclusions reached in our earlier Report.[2]

Finally, we note that a number of the recommendations we made to strengthen the Fund and the APFC's position were subsequently adopted. We felt at the time that the practical changes and proposed statutory amendments would substantially reinforce the State's legal position that the Fund and the APFC are integral parts of the State and that income earned on Fund assets is earned directly by the State. We believe that the factual analysis in the subsequent cases and rulings underscore the wisdom of such actions.

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[1] All references to the Internal Revenue Code or the Code are to the Internal Revenue Code of 1986 as amended, 26 U.S.C. §1 *et seq*

[2] We have reason to believe that the IRS is currently considering several additional private rulings under the integral part doctrine and section 115, which may further elaborate on the factors that are essential to exemption under the integral part doctrine or exclusion from income under section 115. We understand that they have been controversial, in that they were previously submitted and rejected and have been resubmitted to the IRS. We do not have enough information at this time to determine if the rulings will add any meaningful discussion or elaboration to the prior rulings.

II. Constitutional Immunity

The 1988 Report concluded that the constitutional doctrine of implied intergovernmental tax immunity had been so narrowly interpreted over the years that it was unlikely to provide a reliable basis for arguing that any income received by a state was immune from federal taxation should Congress choose to impose such taxation. At one time, the constitutional doctrine of intergovernmental tax immunity held that, as a matter of constitutional relationship between the federal government and the states, the federal government may not tax the sovereign states. This doctrine has been so eroded over the years that it is difficult to determine what its remaining scope might be.

During our previous consideration of this issue, the Supreme Court decided *South Carolina v. Baker*, 485 U.S. 505 (1988), which held (among other rulings) that the doctrine of intergovernmental immunity did not bar a nondiscriminatory federal tax on interest earned by holders of state government-issued bonds ("[T]he States have never enjoyed immunity from all federal taxes considered to be 'on' a State."). Although that case did not deal with a federal attempt to tax a state or state instrumentality, but rather a state attempt to dealt with a tax on bondholders, the Court offered a sweeping analysis of the doctrine of intergovernmental tax immunity, a discussion which might be characterized as dicta. Although the Court never addressed the question of the "extent to which, if any, States are currently immune from direct federal taxation," 485 U.S. at 523 n. 14, the decision includes the often-quoted caveats that "at least some state activities have always been subject to direct federal taxation", 485 U.S. at 523 n.14, and "at least some nondiscriminatory federal taxes can be collected directly from the States even though a parallel state tax could not be collected directly from the Federal Government." 485 U.S. at 523.[3]

We concluded that *South Carolina*, read in conjunction with the Court's expansive reading of the commerce clause in *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528 (1985), suggested that the Court recognized few restraints on the federal commerce or taxing powers over state activities. Nevertheless, we believed that the Court was likely to conclude that there was a limited set of core powers of sovereignty that would remain immune from the federal taxing power, such as state tax revenues, but that there was less comfort that the Court would not approve a

[3] The Court defined "directly" with respect to a state tax on the federal government as "'when the levy falls on the United States itself, or on an agency or instrumentality so closely connected to the government that the two cannot realistically be viewed as separate entities ...'" and indicated that the same definition applied to a federal tax on a state. 485 U.S. at 523.

nondiscriminatory tax on other state income, such as investment income. Report at 69-76.

The *South Carolina* case, of course, had just been decided at the time of our prior Report, and the impact of the decision and dicta therein had not yet been determined. Since then, there have been approximately half a dozen federal cases regarding the intergovernmental tax immunity doctrine, and none have given us a reason to alter this conclusion.

> Specifically, in a case concerning federal taxation of investment income of the state-created Michigan Educational Trust ("MET"), a federal district court rejected the intergovernmental tax immunity claim on the grounds that the MET was not so closely connected to the state that the two could be realistically be viewed as separate entities. *Michigan v. United States*, 802 F. Supp. 120, 126 (W.D. Mich. 1992). On appeal, the state dropped its intergovernmental immunities claim. The 6th Circuit eventually ruled that the Michigan Educational Trust was indeed an "integral part" of the state, and thus exempt from federal taxation. *Michigan v. United States*, 40 F. 3d 817 (6th Cir. 1994). The Court noted, however, that "it was an appropriate move" for the state to drop its intergovernmental immunities challenge because that doctrine had "been severely eroded with the passage of time, and several years ago the Supreme Court suggested that it is now an open question whether there is 'any' extent 'to which States are currently immune from direct non-discriminatory federal taxation.'" *Michigan v. United States*, 40 F.3d at 823 (quoting *South Carolina v. Baker*, 485 U.S. 505, 518 n.11 (1988)).
>
> The 6th Circuit concluded that "*we are confident that today's Supreme Court would say that Congress is free to impose a non-discriminatory tax on the investment income at issue here if it wants to.*"

40 F.3d at 823 (emphasis added). Since the Court had already concluded that the MET was an integral part of the state, this statement with respect to the intergovernmental immunities doctrine is disturbing, since it indicates that even a generally favorable Court would not conclude that a state's investment income is exempt from federal taxation.

Since then, no other case has addressed the question of the potential permissible constitutional scope of federal taxation of the states.[4]

---

[4] Several cases have discussed the doctrine in the context of discriminatory indirect state taxation of persons or entities arguably associated with the federal government. These include: discriminatory state taxation of federal retirees, *see, e.g.*, *Harper v. Virginia*, 509 U.S. 86 (1992); *Davis v. Michigan*, 489 U.S. 803 (1989); nondiscriminatory state taxation of oil and

III. Federal Taxation Does Not Reach Income Earned by an Integral Part of a State

We previously contended that the strongest argument was that the Fund and the APFC were an "integral part" of the state, and thus wholly outside the federal tax code. That is, the IRS has consistently taken the position that the federal income tax law does not impose income tax on income earned directly by a State or an entity that is an "integral part" of a State absent a specific statutory provision.

This is a separate argument from the constitutional doctrine of intergovernmental immunities, which is premised on the constitutional relationship between the federal government and the states.

In contrast, the "integral part" argument assumes that, if Congress so chose, it might be empowered to tax the states directly, but that careful review of the income tax laws reveals that Congress has not attempted to do so. At its most developed, the "integral part" theory argues that any congressional imposition of tax must be clear and unequivocal. The Internal Revenue Code expressly taxes corporations, but does not expressly tax states or political subdivisions, and there is no evidence that Congress ever intended the code to apply to states. The IRS had developed this theory in several precedential published rulings as well as numerous nonprecedential administrative interpretations and internal memoranda. *See* Report, at 27-39.[5]

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gas production on Indian reservations by non-Indian lessees, *Cotton Petroleum Corp. v. New Mexico*, 490 U.S. 163 (2988) (describing the intergovernmental immunities doctrine as "'thoroughly repudiated' by modern case law"); and whether state use taxes on bankruptcy sale proceeds unduly burden the processes of the federal bankruptcy court, *California v. Sierra Summit, Inc.*, 490 U.S. 844 (1989).

[5] See the Report, at footnotes 26 and 30, for a discussion of the varying forms of IRS interpretations and rulings, and their precedential weight. In this letter, we have included discussion of many Private Letter Rulings (PLR) which are written advice provided to taxpayers who submit written requests for rulings on specific legal issues based upon a specific set of facts. Under section 6110(j)(3), such private letter rulings are directed only at the taxpayer that requested the ruling and may not be used or cited as precedent. Since the IRS has substantially reduced its output of published guidance and no longer produces even general counsel memoranda (discussed at footnote 30 of the report), private rulings are a valuable window into the developing position of the IRS, particularly in areas such as this which are rarely the subject of published guidance and even more rarely litigated. Although nonprecedential, private letter rulings also can provide a basis for seeking a similar interpretation by the IRS with respect to similar fact patterns.

At the time of the Report, there was no judicial authority to support the "integral part" theory. In our Report, we discussed the then-recent IRS private ruling issued to the Michigan Educational Trust ("MET"), which was the nation's first government-sponsored prepaid college tuition plan. In that ruling, the IRS determined that the fund was not an integral part of the state, and thus its income was not exempt from taxation. PLR 8825027. (March 29, 1988). Since our Report, the State of Michigan challenged the IRS in tax refund litigation. The trial and appellate decisions in *Michigan v. United States* are the only judicial decisions ever to consider the integral part theory. 802 F. Supp. 120 (W.D. Mich. 1992), *rev'd*, 40 F.3d 817 (6th Cir. 1994).

Since 1988, the IRS has been invited to rule on the "integral part" theory several times, due in large part to the interest on the part of the states in prepaid college tuition investment programs, disaster insurance funds, and self-insurance programs for local governments. The IRS has issued another precedential Revenue Ruling as well as numerous private rulings. These rulings, however, have further developed the theory in unexpected ways. The IRS has been inexplicably inconsistent in its approach, narrowly applying the theory in some cases (prepaid state tuition plans) yet expansively applying it in others (state disaster insurance programs).

A. Michigan Educational Trust

The Michigan Education Trust case is interesting because of the many structural parallels with APFC in terms of its creation and control by the State. Its facts diverge, however, in terms of the source and destination of the funds. It further highlights the IRS's concern with private benefit, although this typically is raised in the context of section 115 rather than the "integral part" doctrine.

The Michigan Education Trust was established as a public corporation. Its corporate purpose — higher education —was declared by the legislature to be a public purpose and an essential function of state government. It was "allocated by law" to the state treasury department, but acted independently of the department. It had an independent board appointed by the governor and confirmed by the senate; the board included the state treasurer. The board exercised its powers as authorized by the statute, including investing, paying out funds, determining the eligibility of participants, and contracting on behalf of the state. A separate state administrative board was made up of officers of the state, including the governor. The administrative board had to approve the form contracts used.

The state attorney general had advised the trust's board that it was an "agency" of the state. The employees of MET were subject to rules governing state employees, *e.g.*, civil service and state laws governing liability of public officers, and the MET was

subject to laws governing the conduct of state agencies, *e.g.*, open records law, open meetings laws, and FOIA. The attorney general provided legal counsel.

An important factor was the source of funds — the entire assets of the MET consisted of actuarially-determined amounts paid by parents under pre-paid tuition contracts. MET was to invest the funds and guaranteed the college tuition of beneficiaries at some time in the future. The act expressly provided that the funds were to be used solely for the purposes of the trust and could not be used by the state for any other purposes. The assets of MET were not considered state money or state revenues, and were not subject to payment of full faith and credit obligations of the state (although the appellate court later determined that the reason for this may have been to give the trust broader investment powers than it otherwise would have). Another important factor was the destination of funds, which were to be paid out to beneficiaries. Moreover, upon dissolution, the assets would not go to the state but would be distributed pro rata to the investors, although state could claim any actuarially determined excess. The state was not legally obligated to make up any shortfall in funding, although it was authorized to do so.

The MET funds were segregated from state funds, although they could be pooled with state funds for investment purposes. Apparently, state treasury department employees actually handled the investments. The bank trust accounts were in the name of the state treasurer, with the state as agent for the trust. MET made an annual accounting to the state governor and legislature. Annual audits were conducted by the state auditor general. Fund payments were paid out through state warrants. Trust income was exempted from state taxes.

During our work on the 1988 Report, the IRS issued a private letter ruling rejecting the exempt status of the MET. PLR 8825027 (March 29, 1988). The IRS discussed the "integral part" theory only briefly, concluding that MET was not an integral part of the state. The key factors mentioned in the IRS ruling were that it was created as a corporation to operate independently from the state; the trustees' decisions could not be overridden by any state agency; the funds were not derived from the state, were not subject to the claims of the state's creditors, and were not considered state funds; the state could not loan, transfer, or use MET funds for any purpose; and the MET funds could be used only for the tuition payment or refunds to investors.

Michigan then filed returns and sued for a refund of the taxes paid. In the District Court, the parties stipulated the facts and filed cross motions for summary judgement. The District Court denied the refund claim, determining as a matter of law that the MET was subject to federal taxation. *Michigan v. United States*, 802 F. Supp. 120 (W.D. Mich. 1992). Michigan raised, and the court addressed, several possible

bases for exemption —constitutional doctrine of intergovernmental immunities and the 10th Amendment, the integral part of the state doctrine, section 115, and section 501(which expressly exempts charities and certain other similar entities).

The District Court implicitly accepted the "integral part" theory as a matter of law that states are *de facto* exempt from federal internal revenue laws. MET was a corporation, however, and thus was subject to federal taxation unless it was an integral part of the state entitled to the state's immunity. The Court concluded that MET was not an integral part of the state because, although the state put up some seed money, the actual funds came from investors and could not be used by the state to pay state creditors or for any other purposes. Also, MET's obligations were not backed by the full faith and credit of the state.[6] The Court concluded that these facts demonstrated that MET was an entity distinct from the state and not entitled to immunity as an integral part of the state.

Michigan appealed to the 6th Circuit, which reversed, holding that the MET was exempt from federal taxation, as an instrumentality or political subdivision, and as an integral part of the state. *Michigan v. United States*, 40 F. 3d 817 (6th Cir. 1994), *rev'g* 802 F. Supp. 120 (W. D. Mich. 1992). The 6th Circuit initially addressed the question whether Congress had imposed taxation on a government corporation such as MET. The Court observed that the Internal Revenue Code plainly imposes tax on corporations. Literally read, that section would tax all governmental corporations include municipalities organized as bodies corporate, public universities, and federal instrumentalities that are organized in corporate form (citing a list of federally owned corporations that are presumed to be exempt from taxation). The IRS conceded the legal premise that the Code did not impose taxation on a state, a political subdivision, or an "integral part of a state." 40 F.3d at 823.

The Court further cited a long line of Supreme Court authorities requiring Congress to express its intent unequivocally when it intends to alter the usual constitutional balance between the States and the federal government. The Court concluded that Congress knew how to make the kind of "plain statement" necessary to impose a tax on a state instrumentality but had not done so here.

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[6] The Court's opinion regarding the constitutional arguments and section 115 are discussed at pages 3-4 and 25-32, respectively. The court also rejected exemption under section 501 because MET's direct benefits impermissibly inured only to parents who purchased contracts, thus violating the private benefit and private inurement restrictions on section 501 charitable organizations. As we suggested in our prior Report, a similar concern would likely be raised with respect to the Fund, APFC, and the dividend program if exemption were sought under section 501.

Unfortunately, the 6th Circuit's decision is so over-inclusive in its argument and use of analogous legal tests that it is somewhat muddled, and to some extent confuses, rather than clarifies, the appropriate legal standard under the "integral part" theory. The 6th Circuit seemed to feel that it had to conclude that the MET was not only an instrumentality but also a political subdivision in order to conclude that it was an integral part of the state. The Court determined that the statutory description of the MET as a "public body corporate and politic" rendered it a state instrumentality. 40 F.3d at 818. The Court relied on an Advisory Opinion of the Supreme Court of Michigan that the grant of corporate powers to a state agency rendered it a "quasi-corporation" but that the agency nevertheless "remains an instrumentality of the State." *Id.* (quoting Advisory Opinion re Constitutionality of PA 1966, 380 Mich. 554, 575, 158 N.W. 2d 416, 425 (1968)).

The Court then reviewed the case law regarding whether an entity is a political subdivision or part of a state for tax purposes, concluding that the standard was whether the entity had been created by state authorities, acting within their constitutional powers, and had been delegated the right to exercise a part of the state's sovereign power for the purposes of carrying out state functions. The treasury regulations defined "political subdivision" as a division of the state which either is a municipal corporation or has been delegated the right to exercise part of the sovereign powers of the state. The Court concluded that the contractual obligations of the MET were no less than those of other entities determined by the courts to be political subdivisions, and that the contracting powers delegated to the MET empowered it to exercise essential governmental functions on behalf of the state. *Id.* at 825.[7]

Citing prior authorities[8], the Court focused less on the creation and powers of the entity rather than its purposes, finding that the "real criterion" was whether the activities

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[7] Not surprisingly, this aspect of the Court's decision has been criticized as confused and inconsistent with the authorities relating to political subdivisions, primarily on the grounds that MET was not granted sovereign powers.

[8] *Commissioner v. Shamberg's Estate*, 144 F.2d 998 (2d Cir. 1944), *cert. denied*, 323 U.S. 792 (1945) (port authority is political subdivision even though it had no power to impose taxes or pledge the credit of the state and was not subject to debt-limiting provisions of state constitution). Critics question how MET can be a political subdivision without sovereign powers. The political subdivision argument is not likely to be strong outside the 6th Circuit, due primarily to the lack of sovereign powers. The case law is quite old that a political subdivision must have sovereign powers, defined as the power to tax, the power of eminent domain, and the power to regulate (the police power). The case cited, *Shamberg's Estate*, is the leading "political subdivision" case. It dealt with a port authority that had eminent domain and police powers, but not the power to tax -- it was held to be a political subdivision. Other political

of the subdivision were for a public purpose. Responding to the District Court's rather summary dismissal of higher education as a governmental function, the 6th Circuit determined that education was a governmental purpose and public function, particularly given the history of Michigan as a land grant state and the emphasis in the state constitution of education as an essential government function. The Court noted that the act creating the trust included extensive legislative findings that it was an essential function of the state to support education, to encourage attendance to state institutions, and to provide educational assistance to students. The Court found that education was at least as much a state purpose as the bridges and tunnels that were the functions of the entities held to be exempt political subdivisions in the prior case law. The Court thus concluded that MET was a public agency authorized to exercise contracting powers on behalf of the state for a purpose declared by the legislature to be a public purpose.

The Court then added that MET would qualify as a political subdivision since it was a "public body corporate and politic", and thus was "in a broad sense" a municipal corporation. *Id.* at 825-26.[9]

For further support, the Court also borrowed a six-factor test used by the IRS and the courts for determining whether an entity is an agency or instrumentality for purposes of federal law governing governmental benefits plans. Those factors are (1) whether it is used for a governmental purpose and performs a governmental function; (2) whether it performs its function on behalf of a state or political subdivision; (3) whether there are private interests involved or whether the state or political subdivision has the powers and interests of an owner; (4) whether control and supervision is vested in public authorities; (5) whether express statutory authority is required for the instrumentality and whether such authority exists; and (6) the degree of financial autonomy and the source of operating expenses. 40 F.3d at 826-27 (citing *Rose v. Long Island Railroad Pension Plan*, 828 F.2d 910 (2d Cir. 1987), *cert. denied*, 485 U.S. 936 (1988), and Rev. Rul. 57-128, 1957-1 C.B. 311). The Court concluded that MET satisfied the first five factors (the sixth was not presently satisfied but the court

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subdivision cases discussed by the 6th Circuit include *Commissioner v. White's Estate*, 144 F.2d 792 (2d Cir. 1944) (bridge authority was political subdivision with power to issue exempt bonds); *Philadelphia National Bank v. United States*, 666 F.2d 834 (3rd Cir. 1981)(Temple University was not a political subdivision eligible to issue tax-exempt debt); *Rose v. Long Island Railroad Pension Plan*, 828 F.2d 910 (2d Cir. 1987), *cert denied*, 485 U.S. 936 (1988)(metropolitan transit authority (MTA) was political subdivision and pension plan was part of MTA).

[9] The Court did not cite any authority for this conclusion, which not surprisingly, also has been criticized by commentators and the IRS.

speculated that it could not be ruled out for the future), and concluded that, on balance, the presence of five factors led to the conclusion that it was a state instrumentality.[10]

The Court also distinguished *United States v. Maryland Savings-Share Insurance Corporation*, 308 F.Supp. 761 (D. Md.), *rev'd on other grounds*, 400 U.S. 4 (1970) ("*MSSIC*"), which was discussed in our Report at pages 85-90. In *MSSIC*, the Supreme Court upheld the lower court's conclusion that a nonprofit insurance corporation charted to insure savings and loan accounts was not exempt from federal taxation as an instrumentality. The 6th Circuit pointed out that that *MSSIC* was a private corporation, organized by and for savings and loan members, with a Board largely comprised of elected directors. 40 F.3d at 827-828. In contrast, the MET was a public instrumentality, had a board appointed by the governor, and was delegated authority to contract on behalf of the state.

The court also rejected both of the government's arguments that the trust could not be an integral part of the state because its corporate form made it functionally independent and because the source and earmarking of funds made it fiscally independent. The Court determined that it was "immaterial' that the state chose to use a public corporation rather than to assign the functions to a traditional department. 40 F.3d at 828. The Court cited the example of the U.S. Postal Service as a corporate entity that did not become taxable by virtue of its corporate form. 40 F.3d at 828-29. Similarly, the Court rejected the argument that the source or earmarking of funds was determinative, again citing the example of the U.S. Postal Service, the TVA, and ports authority as examples of governmental instrumentalities that obtain funding from private sources and are earmarked for the performance of public functions that the agencies were created to perform. The Court was also critical of the government's focus

[10] Critics argue that this six-factor test of "instrumentality" is irrelevant for two reasons. First, it was developed in a different context involving different law, legislative history and intent, and different requirements (ERISA and governmental plans). This argument was made by the IRS in criticizing the *MET* case in subsequent rulings. *See, e.g.*, PLR 9809013 (Nov. 7, 1997); PLR 9706006(Nov. 8, 1996); PLR 9627016(April 5, 1996); PLR 9622019 (Feb. 28, 1996). The IRS's challenge is a bit disingenuous, however, since it was the IRS itself that issued a series of G.C.M.s and rulings relying on this six-factor test for purpose of section 115. *See, e.g.*, G.C.M. 34704 (Dec. 2, 1972); G.C.M. 34502 (May 2, 1971); PLR 8820030 (Feb. 16, 1988); PLR 8740015 (July 2, 1987); PLR 8650017 (Sept. 10, 1986). Second, critics argue that "instrumentality" is not synonymous with "political subdivision" or "integral part of a state", and that instrumentalities are not even certain of exemption under section 115. *See, e.g*, Letter to Editor from Prof. Ellen P. April, 66 Tax Notes 121 (Jan. 2, 1995) (citing *Maryland Savings-Share Insurance Corp. v. United States*, 400 U.S. 4, 7 n.2 (1970) ("*MSSIC*") and Rev. Rul. 77-261, 1977-2 C.B. 34).

on the form, rather than the substance of the entity, analogizing the trust to government student loan programs and state pension funds. *Id.* at 829.

Not surprisingly, the IRS has chosen to reject the 6th Circuit's decision, criticizing it in public appearances and statements, and taking the position that it is not authoritative anywhere outside the 6th Circuit. In rulings since *MET*, the IRS has repeatedly rejected the analysis of the Court as "internally inconsistent", arguing that its "reliance on the [six] factors listed in Rev. Rul. 67-128 ... to reach its conclusion is misplaced." *See, e.g.*, PLR 9809013 (Nov. 7, 1997); PLR 9706006(Nov. 8, 1996); PLR 9627016(April 5, 1996); PLR 9622019 (Feb. 28, 1996). Moreover, the IRS declared that it would no longer entertain state requests for rulings relating to the exemption of state prepaid tuition programs under the "integral part" theory or section 115, thus shutting the door on states that might want to adopt a variation on the Michigan plan that might be more acceptable to the IRS. Rev. Proc. 96-34, 96-1 C.B. 721.

Lacking access to guidance, the states began to lobby for Congressional grant of exemption to such programs. Finally, in 1996, the Small Business Job Protection Act added new section 529 to the Code, which expressly provides tax-exempt status for state tuition programs that meet the requirements of the statute. P.L. 104-188, §1806. Even after this statement of Congressional approval, the IRS continues to refuse to issue rulings under the "integral part" theory or section 115 to states relating to prepaid tuition programs, thus in effect taking the position that only plans organized pursuant to the statute may be exempt. Rev. Proc. 98-3, 1998-1 I.R.B. 100 (Jan. 5, 1998).

B. Disaster Insurance Programs

The IRS has issued a number of widely publicized "integral part" rulings to states in recent years that shed additional light on the IRS's concerns in this area, particularly regarding which characteristics of an entity qualify it as an integral part of the state. In contrast to the MET IRS ruling, the extent to which a proposed state entity's activities appear to be private rather than public in nature (*e.g.*, private funds, investors, beneficiaries) continues to be a significant consideration, yet apparently is not determinative once certain other indicia of state creation and control and financial commitment are satisfied.

The most significant rulings in recent years involve a series of proposed state disaster insurance programs, which typically create some sort of entity or fund which individuals or insurers would pay into or purchase insurance from, which entity would then pay claims or reimburse insurers in the event of a certain natural disaster.

1. Florida Hurricane Catastrophe Fund

In 1995, Florida successful obtained a private ruling which held that the Hurricane Catastrophe Fund ("CAT Fund"), a trust fund created by state law, would be considered an integral part of the state. PLR 9507037 (Nov. 4, 1994). It is described as a "trust fund under state law", *i.e.*, a separate legal entity, but it does not appear from the ruling or the state statute that it was structured as an actual trust but rather as a state fund. Participating insurers were to pay premiums into the fund, and would be reimbursed for a percentage of losses resulting from certain events. The state also imposed an assessment on a broader class of insurers, including many nonparticipants, with the revenues to be earmarked for the fund.

It appears that the state was not liable if the fund proved to be insufficient, although if that occurred, local governments could issue revenue bonds for the benefit of the fund, and the bonds would be backed by the fund's future revenues. It appears that monies in the fund were not subject to the state's creditors. The ruling does not indicate whether the fund was treated as a state account for accounting purposes, or whether there was any duty to provide financial reports or to be audited by the state. The state legislature also could appropriate funds from the fund for grants to local governments and nonprofits for preparedness programs. All assets of the fund would revert to the state upon termination of the fund. It was governed by the State Board of Administration, a three-member board comprised entirely of state officials. Operations of the fund were conducted by fund employees and contract advisors. It appears that the board was not created for the purposes of governing the fund, but rather was a pre-existing body that had been created under the state constitution to administer certain special purpose tax revenues, and also could be delegated other powers under state law.

The ruling cryptically states that "[t]he method of accounting for moneys related to certain operations does not by itself determine whether the operation is an integral part of the state or an entity separate from the state." Nothing in the ruling discusses the method of accounting for funds. It is known that the fund was very controversial and was initially rejected by the IRS. This comment may be an observation that the fund was actually a state fund, rather than an independent fund, and that that distinction alone did not resolve the issue of integral part. Certainly, past IRS rulings have found that the existence of a separate legal entity or independent entity was a determinative factor in finding that an entity was not an integral part of the state.

The ruling does rely on the state's exercise of its taxing power and "significant contribution" of monies to the fund, the state's power to appropriate monies from the fund for certain specified purposes, and the state's receipt of the assets upon dissolution as significant factors in concluding that the state has a "financial interest" in the fund. Another factor cited by the ruling was that the monies could only be used for purposes

authorized by state law, and no other purposes. The ruling also noted that the state exercised direct control over the fund through the board which consisted of state officials.

Curiously, there was no discussion of the issue which animated the debate over the MET ruling — the significant private benefit. Here the very purpose of the fund, as there, was to pay out virtually all of the income and assets to private parties, but that issue was not even discussed. Apart from the MET ruling, it would appear from a general review of IRS rulings that the private benefit analysis is limited to section 115 and plays little or no part in determining whether an entity is an integral part of a state. That may well be the wrong interpretation of the IRS's position, however. Contemporaneous public statements by Florida state officials during the ruling negotiations indicate that the IRS's chief concern was indeed the MET -type private benefit issue. The Florida CAT Fund was perceived by the IRS not as a state fund but rather as plan to help private insurers. Negotiations with the IRS dragged on for over a year — the IRS apparently demanded that the state have a significant investment of its own funds at risk in the fund before it would rule that it was an integral part of the state.

Subsequently, Florida apparently did not enact the plan in the form it was presented to the IRS, and the IRS threatened to withdraw the exemption ruling unless the state committed "significant" state funds to the fund. Several amendments to the plan were made, including additional annual appropriations from the general revenue fund and another state trust fund for the first two years, a broader base of nonparticipants who would be taxed to fund the program, and additional powers on the part of the state to appropriate monies from the fund. The IRS accepted these changes and issued a favorable supplemental ruling. PLR 9522039 (March 6, 1995).

2. Hawaii Hurricane Relief Fund

In the wake of Hurricane Iniki, Hawaii also developed a state sponsored disaster relief fund, which the IRS held was an integral part of the state. PLR 9627016 (April 5, 1996). Significantly, the fund was established as a public corporation. The fund was placed under the State Department of Commerce and Consumer Affairs for administrative purposes. The board was made up of the commissioner of insurance, *ex officio*, and six members chosen by legislative leadership and the governor. Departmental employees were assigned to the fund, and continued to be considered state and departmental employees.

The fund issued hurricane policies for properties covered by private property insurance, and the private insurance companies served as servicing agents for the fund hurricane policy as well as the property insurance. The fund's policy revenues were

kept in a trust fund outside the state treasury. The fund revenues came principally from annual premiums for the policies. The fund was authorized to levy annual assessments on insurers in the state. The law also created a special mortgage recording fee to be earmarked for the fund. If the fund was insufficient to pay claims, the law also provided for increased assessments on insurers, or additional special assessments, or surcharges on hurricane policy premiums. Additionally, the law authorized creation of a bond fund within the state treasury, and authorized the commerce department to issue state debt obligations which would not be backed by the full faith and credit of the state, as well as other further revenue bonds which would be backed by the full faith and credit of the state under certain limited circumstances. The bond fund would make loans to the trust fund to support its operations. Upon dissolution of the fund, any remaining monies after settlement of any claims, would revert to the state general fund.

The ruling concluded that the state exercised significant control over the fund. All board member would be state officials or nominated by state officials and confirmed by the state senate. The initial plan of operations was subject to legislative review. It would be administered by a state department and was required to report annually to the state insurance commissioner. Employees were considered employees of a state department. The state had made a substantial financial commitment to the fund through assessing the mortgage recording fee, levying an annual assessment on insurers, providing for potential surcharges on premiums, pledging full faith and credit for certain debt obligations, and receiving the assets of the fund upon dissolution. Based on the elements of state control and financial commitment, the IRS concluded that it was an integral part of the state.

3. California Earthquake Authority

The IRS revisited the issue with the California Earthquake Authority ("CEA"), issuing, revoking, and reissuing rulings as the state amended its proposed program to satisfy the IRS. Initially, after about six months of negotiations, the IRS issued a private ruling determining that the CEA was an integral part of the state. PLR 9622019 (Feb. 28, 1996). As described in the ruling, the CEA was established by a statute which created both an agency and the fund to provide earthquake coverage. Private insurers were required to offer coverage in one of two ways — either directly, or by participating in the fund and issuing a fund policy to be administered and serviced by the private insurer. Premium rates for fund policies were subject to approval by the state and subject to public rate-making procedures.

The fund was governed by a board consisting of three voting members, all state officials, and two nonvoting members, both legislators. The board members could designate a state employee to serve in their place. The board also had an advisory panel,

representing the insurance industry and general public, to be appointed by the board members. Meetings of the board and advisory panel were subject to state open meetings requirements. The fund was administered under the direction of the state insurance commissioner. The initial plan of operations had to be approved by the commissioner and legislature. Subsequent amendments had to be approved by the commissioner. Senior executives would be employed under contract. The fund's employees were subject to state civil service requirements, and subject to state laws governing post-government employment.

The state annually would contribute the equivalent of the state premium tax collections on the fund policies to the fund as part of the fund's capital. The state also contributed the remaining balance in a defunct previous earthquake trust fund. Participating private insurers would pay an initial assessment to the fund based upon market share. The primary source of revenue, however, would be premiums for fund policies sold. The fund would purchase reinsurance. The statue authorized that a certain percentage of investment income could be used for earthquake mitigation programs. If the fund were unable to cover claims, the fund could ask the state treasurer to issue debt obligations to be repaid through a policy surcharge, but the state would have no liability for those obligations. The statute expressly provided that the state would not be responsible for any of the liabilities of the fund. In the event of the fund's termination, all assets would be transferred to the state.

The ruling distinguished *MSSIC* on the grounds that : (1) only three of eleven MSSIC directors were selected by state officials; (2) the state made no financial contribution to MSSIC; and (3) the state had no present interest in the income of MSSIC. The ruling also mentions that MSSIC was a corporation, but does not discuss the significance of that fact. The ruling also mentions that under the MSSIC charter, the full faith and credit of the state was not pledged for MSSIC's obligations. Similarly, the California statute expressly declined to give the state's backing to the obligations or liabilities of the CEA.

The ruling also distinguished *MET* in a discussion, repeated in other rulings, that makes it clear that the IRS does not agree or acquiesce to that decision. The *MET* decision was distinguished as "internally inconsistent" because it found that the MET was both a political subdivision and an integral part of the state. The California ruling further rejected the decision's discussion of the factors listed in Rev. Rul. 57-128 as irrelevant because they apply only to entities that are separate from a state, and are not used to determine if it is a separate entity or an integral part of a state. This seems to misstate the Revenue Ruling, which admittedly is not an "integral part" or section 115 ruling, but in another context does spell out a list of factors to be considered in determining whether a entity is an instrumentality of a state or not.

Other factors cited in the ruling were the significant government interest set forth by the state in providing assistance to its citizens and economy in the event of natural disasters of the magnitude of an earthquake. The state also had argued that this plan represented an exercise of the state's power to regulate an industry, and that the fund was as valid an exercise of state power as the regulatory alternatives.

Two months later, the IRS revoked the ruling letter for further review of the issue. Letter dated April 30, 1996, LEXIS, FEDTAX, TNT, 96 TNT 102-54. It appears that this revocation may have been prompted by the state legislature's consideration of further legislation that threatened to significantly revise the CEA.

The state then conducted an unusual high pressure campaign, seeking assistance from the White House and imposing pressure through its congressional delegation. Legislation was introduced in Congress to grant an express federal tax exemption to the CEA.

Then in June, 1996, the IRS reinstated the ruling granting exemption as an integral part of the state without discussion. PLR 9641010(June 25, 1996) (reinstating PLR 9622019). The ruling noted that the state legislature was considering legislation affecting the fund, and warned that the IRS was not giving any opinion as to the continuing exempt status of the fund if the legislation were to be enacted.[11]

After the California legislature further amended the statutory scheme, the state again sought a reaffirmation of the IRS's ruling. Subsequently, the IRS again issued a ruling to California, concluding that after numerous statutory changes, the CEA was an integral part of the state. PLR 9706006(Nov. 8, 1996).

In general, the legislative amendments did not really address the issues of either state control or financial interest, which apparently were the chief concerns of the IRS. The chief purpose of the amendments appears to have been to forbid the CEA from declaring bankruptcy, to strengthen the capitalization of the fund, and to create additional "tiers" of remedy in the event that the assets of the fund proved inadequate to satisfy claims, including various additional surcharges on participating insurers. The

[11] Published accounts of the California Earthquake Authority tax negotiations, discussed below, and private discussions with Florida, Hawaii, and California state officials and IRS officials reveal that the IRS was very concerned about the overwhelmingly private benefit characteristics of these funds. The IRS required amendments, if necessary, to strengthen state control, to impose requirements that assets revert to the state upon dissolution (although given the nature of these funds, the possibility of remaining assets is so remote as to be meaningless), and most important, to require a significant state financial commitment.

amendments also seemed to make it harder for participants to avoid sharing the burden of fund obligations by dropping out. The only amendments that seemed relevant enough to warrant mention in the IRS's discussion in the final ruling were: (1) the legislature "provided for" additional surcharges on policies, and probably more important, the state appropriated some monies to assist in the start-up of the fund, and loaned additional monies at a legal rate of interest; and (2) the board members and officers were made subject to the financial disclosure requirements for state officials. Otherwise, the ruling is almost verbatim identical to the earlier ruling (PLR 9622019).

The California ruling is somewhat surprising in that the state assumed no liability for the fund, unlike the Florida hurricane catastrophe fund. The California insurance commissioner publicly stated that lawmakers demanded that the state's general fund be immune from liability, and described the structure of the program as one of "building firewalls between the CEA and the General fund."

C. Other Integral Part Rulings

There have been a few other integral part rulings worth noting. Unfortunately, several rulings have made broad and disturbing statements that a corporation created by a state is not an integral part of a state because it is a corporation and is not within a branch of government. For example, in PLR 9549030 (Sept. 11, 1995), the IRS ruled that a corporation created by a county to manage a commercial district was not an integral part of the State or a political subdivision of the State "because it was created as an entity separate and distinct from the district and is not within the Executive or Legislative branches of County". [12]

Similarly, another ruling concerned a state-created public corporation which was organized to establish a university. PLR 8935012 (May 30, 1989). The governing board was appointed and confirmed by the state. It received state appropriations for capital outlays and operational expenses. Apparently the state itself argued that the corporation was an entity separate and apart from the state. The IRS concurred and concluded that it was not an integral part of the state, without further discussion. [13]

Similarly, the IRS has determined that a regional development authority was not an integral part of the state, apparently because it was formed as a separate corporation,

[12] The ruling did conclude that the corporation's income was excluded from taxation under section 115, and thus was required to file a federal corporate tax return.

[13] The ruling did conclude that section 115 applied to exclude the corporation's income from federal taxation.

had its own officers and employees, and was not under the control of any state agency or any one political subdivision. PLR 9009063 (Dec. 8, 1989).[14]

One distinction between these rulings and other favorable rulings is that these involve public corporations, while other favorable rulings involve trusts or other entities of more nebulous legal status. It is difficult, however, to determine the significance of corporate status, especially when the IRS does not elaborate on the issue, or when the IRS eventually finds the entity to be exempt under another provision. For example, while the IRS considered corporate status to be a negative factor for MET, it apparently was not the determinative factor in concluding that it was not an integral part of the state.

Certainly, there are other rulings that conclude that a corporation can be an integral part of the state. For example, the Hawaii hurricane fund was organized as a public corporation, yet the IRS did not raise that as an issue. It would appear generally that while corporate status is a significant factor for the IRS, it may be neutralized by sufficient evidence of state control and, in the words of the IRS, "domination." *See, e.g.*, G.C.M. 39601 (Jan. 30, 1987) (lawyer trust fund); G.C.M. 38921 (Nov. 26. 1982) (housing authority).[15] Yet is extremely difficult to predict when separate organizational structure will be determinative or what level of government control renders a separately organized entity an integral part of the state.

Also, if a corporation cannot by definition qualify as an integral part of the state due to its separate legal existence, then the same rational should apply to a trust. Yet there are several rulings that conclude that trusts can be integral parts of a state. *See* Rev. Rul. 87-2, 1987-2 I.R.B. 4 (1987).

In one recent ruling, the IRS held that a trust was an integral part of the state regardless of the fact that was created as a separate and distinct entity apart from the political subdivision. The IRS reviewed a trust set up by a municipality to pay retiree medical benefits. PLR 9809013 (Nov. 7, 1997). Although the municipality asked for a ruling under section 115, the IRS concluded that section 115 did not apply because the

[14] *See also* PLR 8934052 (May 21, 1989) (arts commission is "corporate and politic," therefore not integral part).

[15] *See also* PLR 8920056 (Feb. 22, 1989) (An unincorporated city economic development board was not an integral part because the board could hire its own staff who were not considered city employees. The board was created under state statute and funded by taxes, board members were appointed by the city, the city budgeted expenses, the board submitted financial reports to city, city audited the board).

trust was an integral part of the state. The trust was created by statute to hold and invest amounts contributed by the municipality to fund retiree medical benefits for former public safety officers. The trust was administered by a board, and six of the eight trustees were appointed by program participants (and at the time were active municipal employees although that was not a requirement), and only two were appointed by the municipality. However, the legislative body of the municipality confirmed all appointments. Day-to-day administration was performed by a municipal employee, who was paid by the municipality and participated in the employee benefit system. The municipality provided facilities, equipment, and legal services to the trust. The municipality could amend or terminate the trust at any time, and in the event the trust were terminated, all assets would revert to the municipality. The IRS stated:

If an enterprise is deemed to be an integral part of a state or political subdivision of a state, that enterprise will not be treated as a separate entity for federal tax purposes, regardless of the fact that the enterprise was created as a separate entity.

PLR 9809013.

The IRS determined that it must consider all the facts and circumstances, particularly the state's degree of control over the enterprise and the state's financial commitment to the enterprise. Key factors were that the municipality had made a substantial financial commitment by providing all of the start up money as well as portion of the annual costs. Other important factors included the significant influence exerted by the municipality, its power to amend or terminate the trust at any time, the control over day-to-day operations by a city employee, approval of the board by the city legislative body, and the requirement that the board act only as authorized by the statute. *Id.*

Yet in PLR 9217032 (Jan. 27, 1992), the IRS determined that a mine reclamation trust fund created under state law was not an integral part of the state because it was separately organized as a trust under state law, the trustees had total discretion over the funds, and the trust could accept funds from nongovernmental sources. It is difficult to square this ruling with the later disaster fund rulings, except that it was clearly a separately organized legal entity.

Whether the governing board is appointed by the state or independently elected was a deciding factor in PLR 8944031 (Aug. 7, 1989). That ruling held that a soil and water commission was an integral part of the state, but the soil and water districts were not an integral part because the governing bodies consisted of four independently elected members and only one government appointee.

Yet another group of rulings echo the MET ruling in considering the source and/or destination of the assets and income of the entity. In 1994, the IRS held that a trust fund created by a state court to collect private contributions to pay for judges' portraits was an integral part of the state. PLR 9439008 (June 30, 1994). The funds were from private sources and there was no financial commitment on the part of the government. A key factor in the ruling, however, were that the court created the trust and controlled it through its ability to select and discharge the state employees who controlled the funds and the trust. Moreover, reflecting the IRS's interest (sometimes) in the destination of funds, the ruling was expressly made contingent on trust documents being amended to provide that any funds remaining after the purposes were met would be delivered to the government's general fund. The ruling concluded that the trust was an integral part of the state, since it was created by the court, controlled by the court officers, and upon termination, any remaining funds would go the state general fund.

In another ruling, the IRS considered a "lifeline" fund, created by the state to subsidize the utility rates of the poor, and concluded that it was an integral part of the state. The fund was created by statute, although it is unclear from the ruling what its legal status was. The funds came from a state-ordered surcharge on utility bills, and were invested until paid out to needy individuals. It was administered by a committee appointed by a state commission. No state officials served on the governing committee. The fund's budget was subject to state review, and annual reports were submitted to the legislature. If terminated, assets would be distributed as ordered by a state public utilities commission, but could not revert to private interests. The IRS concluded that the fund was an integral part of the state due to the state's control over the creation, operation, funding, and supervision of the fund. PLR 8931042 (May 8, 1989). The fact that the assets and income were paid out entirely to private individuals did not seem to merit discussion.

Another recent ruling addressed funds created by state officials from the proceeds of litigation judgments or settlements. The state created two funds to hold settlement payments received as a result of litigation by the attorney general. PLR 9733003 ((May 9, 1997). A fund was created in the state treasury to hold litigation judgments or settlements, and was controlled by the treasury department. Distributions from the fund were made pursuant to court order. All income from investment of the fund was deposited in the fund. Fees were paid to the treasurer for investment and administrative services. The fund consisted of two litigation settlements, funds A and B. Settlement A was from state litigation against a trade school. The state court's order required the Attorney General to create a fund, fund A, to receive payments from the defendants for civil penalties, attorneys fees, and restitution to students of the school. In other words, the proceeds in the fund were to be paid as restitution to the individual claimants. The second fund, fund B, consisted of settlement proceeds of antitrust cases

in federal court brought by the state as *parens patriae* for its residents. The plaintiff class members who were to receive the settlement proceeds in fund B were the state and municipalities.

The state argued that the funds were an integral part of the state.[16] In discussing the "integral part" issue, the IRS noted that the state was involved in the administration of the funds, and state employees, acting in their governmental capacities conducted the funds' business. In both cases, a court controlled distributions and the state remained answerable to the court regarding its administration of the funds.

For fund A, the state controlled disbursement because of the jurisdiction of the state court. The state was not responsible for shortfalls in either fund and did not contribute state funds to either fund. The state did not have the authority to access the assets or income of the funds for the benefit of the state. The state's only financial interest was as a potential claimant. Regarding fund A, the IRS determined that the fund benefited private parties and lacked public benefit, and was not an integral part of the state.

Regarding fund B, the IRS determined that the state lacked the requisite level of control since disposition of the assets and income had to be determined by a federal court. The IRS concluded that the Fund was not an integral part of the state, but rather was a form of receivership imposed on the state by the court.

The litigation settlement ruling is instructive in that it focuses on two concerns of the IRS. The focus on creation and control by the state has long been an element of the "integral part" theory. The focus on "private benefit" however, is a recent development. At times, private benefit appears to be the determining factor, as in this ruling and the MET rulings. Yet just as often, programs such as the disaster insurance programs, that unquestionably have an almost exclusive private benefit are held to be "integral parts" of the state. *See also* PLR 8925010 (March 21, 1989) (city development district is integral part of city even though money reverts to private property owners upon dissolution).

Corporate status does not explain the distinction, since the Hawaii hurricane fund, for example, was a corporation. Curiously, this new destination of income analysis is borrowed from the section 115 analysis, discussed below, and the private benefit focus, which we see in both "integral part" and section 115 rulings, appears to be borrowed from section 501 charitable organization law, which forbids any nonincidental

[16] The state also argued that the income of the funds would be excluded from income under section 115. See discussion below at page 25-32.

private benefit. It is unclear why the IRS has adopted this analysis, but it is equally clear that not only is it now a key element under section 115, there is a not insignificant likelihood that the IRS may well import it into an "integral part of the state" determination as well.

D. Summary Regarding Integral Part Theory

Overall, we believe that these developments have helped to further elucidate the courts' and the IRS's rationale under the integral part theory in ways that generally are favorable to the fund and the APFC. The *MET* decision is particularly generous, as are the disaster fund rulings.

Ten years after the Report, the fact that APFC is structured as a corporation continues to give some cause for concern. Commentators have argued that the use of a separate entity, such as a corporation or a trust, must preclude integral part status, and must be analyzed under section 115. This does not seem to be the IRS position, however. Although the rulings of the last 10 years continue to be inconsistent on this point, it appears that, given sufficient indicia of control and financial commitment by the state, a corporation or trust is not automatically precluded from being an integral part of the state.

In this case, the assets and income are not those of the corporation, but rather belong to the State. As a matter of statute, APFC is simply the manager of the Fund assets. This has been reinforced through the 1992 amendment of section 37.13.030 which now plainly clarifies that the assets are managed and invested by APFC, rather than "allocated to" APFC. Similarly, the annual report clearly reports income and assets as those of the Fund, and not the corporation.

Certainly, it would appear that - apart from the corporate structure issue - state creation, control and domination, and declaration of state purpose are essential factors. Similarly, the MET and disaster fund rulings seem to teach that some not significant part of the assets must come from the state, and that it must have some financial risk in the enterprise. The IRS's MET ruling reflects the IRS's evolving but erratic interest in the destination of funds as well although this did not appear to concern the 6th Circuit.

A comparison of MET with the Alaska Permanent Fund and APFC is both instructive and reassuring. The key characteristic of the MET and similar prepaid tuition programs, which gives pause to the IRS and, we suspect to any court, is the source and destination of the program funds at issue. The MET may have had all the appearances of being a part of the state, but it was still wholly a private activity conducted by private investors for the benefit of private beneficiaries. The state

contributed only minimal start-up administrative funds, all of the funds were entirely private funds, the MET's assets were not considered to be state assets, the income was not state income, and upon dissolution, the assets reverted to the investors rather than the state. The IRS-state negotiations over the disaster fund rulings, and subsequent rulings in other areas, discussed below, reveal that the source and destination of the assets and income, as well as private benefit, are becoming significant concerns of the IRS with respect to the integral part doctrine, as well as section 115.

In contrast, the assets and income of the Alaska Permanent Fund are unquestionably those of the state, and not the corporation or any private person. While the legislature has chosen to appropriate certain state funds to the dividend program, the recipients do not have an entitlement to the income of the Fund. If the corporation were dissolved, the assets would remain those of the State, and would not accrue to any individuals. This argument, of course, is premised on the legislature's ultimate control over any allocation, appropriation, or payment to private persons. If at any time, the legislature or government loses that power of appropriation, or private persons are granted an entitlement to the assets or income in the Fund, this argument is considerably weakened.

What plainly bothers the IRS about prepaid tuition programs, although it seemed to be unable to discuss it openly in the MET ruling, is the appropriateness of "lending" the state's tax-exempt status to private investors so they can earn a greater return on their investment than they might otherwise. IRS officials have frequently raised this objection in public discussions of prepaid tuition programs. Apart from tax-exempt bonds, the tax code is full of provisions designed to prevent taxable persons from benefiting from a charitable organization's exemption (*e.g.*, UBIT). The IRS views such programs as opening the door to abuse.

On the other hand, the *MET* decision and disaster fund rulings indicate that private benefit does not, in all cases, undermine the integral part argument. It would appear from both *MET* and the disaster fund rulings that sufficient indicia of state control and public purpose can support integral part status, despite the existence of significant private benefit. Obviously, however, it is an open question whether dividend payments to individuals outside the context of a higher education purpose (or governmental pensions, or health insurance claims, or other "approved" governmental or public purpose) will suffice to satisfy the public purpose criterion.

Unfortunately, since the IRS continues to reject the holding and rationale of the 6th Circuit's *MET* decision, it is clear that it could not be relied on as a basis for obtaining a ruling. Similarly, it likely would provide cold comfort in an administrative proceeding, such as an audit or appeal. We suspect that other courts may well be

skeptical of its reliance on the political subdivision cases in particular, or its apparent finding that "instrumentality" status is sufficient for exemption under the "integral part" theory.

Although it is difficult to reconcile the IRS's continuing hostility to prepaid tuition plans, which the IRS labels as private investment schemes that seek improperly benefit from the state's exemption, with its generous position on disaster insurance programs, a key distinguishing factor is the element of the state's financial commitment to the enterprise. The IRS insisted that the disaster programs include a significant level of state financial commitment as a source of funds, such as through contributions of funds, earmarking of certain tax or fee revenues, or allowing certain debt obligations to be backed by the state's full faith and credit. In the case of the Fund, it is an essential distinction that the assets clearly are those of the State.

IV. Section 115 Exclusion From Income

The previous Report concluded that the Fund might alternatively claim exclusion of income under section 115, although that position was not entirely free from doubt.[17] Section 115 requires: (1) that the income of an instrumentality be derived from an essential governmental function, and (2) that the income accrue to the State. We noted that the few judicial authorities did not clearly support this argument, yet the IRS appeared to be more liberal than the courts in applying section 115 in the ruling context, particularly with respect to finding "accrual" of income by the State. Since 1988, section 115 has been discussed on only one reported case, *Michigan v. United States*, 802 F.Supp. at 120, described above, which was reversed by the appellate court without discussion of section 115. The IRS has issued one precedential ruling and approximately 170 nonprecedential rulings in this area.

A. Michigan Educational Trust

In *Michigan v. United States*, the state made the alternative argument that the MET's income was excluded from gross income under section 115. In the private ruling, the IRS did not discuss the essential governmental function prong of the statutory test, concluding rather that the accrual requirement was not met because the income served private interests that were more than incidental to the public interest. PLR 8825027 (March 29, 1988). The MET provided direct economic benefits only to

[17] Section 115 and "integral part" theory are not merely alternative arguments. The distinction has important consequences — if the income were excludible under section 115, APFC would be required to file tax returns.

provide participants who were the beneficiaries of a contract. The IRS stated "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." PLR 8825027.

The District Court also did not discuss the "essential governmental function" requirement, although its discussion of the "integral part" claim and 501(c) exemption claim certainly suggest that the Court found that element wanting. *Michigan*, 802 F. Supp. at 123-125. Instead, it held that section 115 did not apply because MET did not satisfy the accrual requirement. 802 F. Supp. at 124. The opinion reaffirmed earlier cases which require an actual or bookkeeping transfer of income to the state, or require that the state have a vested right or enforceable claim to the income. *Id.* In contrast, the MET statute expressly provided that the state had no claim to either MET's assets or income. The possibility of excess assets passing to the state upon dissolution was too remote to constitute "accrual". *Id.* at 124.

The 6th Circuit, having ruled that the MET was an integral part of the state, found it unnecessary to reach the section 115 issue. *MET*, 40 F. 3d at 829. In its discussion of the "integral part" theory, the Court effectively made the case that financing higher education was an essential governmental function, distinguishing *Philadelphia National Bank v. United States*, 666 F. 2d 834 (3d Cir. 1981), *cert. denied*, 457 U.S. 1105 (1982) (which suggested that higher education was not an essential governmental function). We suspect that even the 6th Circuit, had it addressed the section 115 claim, also would have found the accrual element wanting. Under *MSSIC*, potential escheat to the state is not accrual, and the lack of a state financial obligation or risk of state funds is fatal. 308 F. Supp. at 765-766.

B. Rev. Rul. 90-74: Pooled Insurance Funds

The IRS has only issued one authoritative ruling under section 115 since 1988, Rev. Rul. 90-74, 1990-2 C.B. 34, although this ruling has prompted many dozens of private rulings under section 115 addressing pooled risk-sharing or self-insurance funds formed by political subdivisions. These follow Rev. Rul. 90-74, which held that the income of an organization formed, operated, and funded by political subdivisions to pool their casualty risks or other risks concerning public liability, workers compensation, or employee health benefits, is excluded from income under section 115. The key test is whether private interests participate in the organization or benefit more than incidentally from the organization. However, the fact that the purpose of the entity is to insure and reimburse payment of claims to individuals has been held to be an incidental private benefit. PLR 9741002 (June 26, 1997); PLR 9740005 (June 26, 1997); PLR 9646026 (Aug. 20, 1996).

Rev. Rul. 90-74 illustrates the typical ruling. The political subdivisions agree to create a pooled self-insurance entity, which could be a corporation. *See, e.g.*, PLR 9646026 (Aug. 20, 1996); PLR 9101005 (Sept. 1, 1990).[18] In some cases, the pooling entity was created or authorized by state statute. This did not appear to be a necessary factor, although it supported the finding of essential government function. Each participating body authorized participation in the entity. The board was elected by the member political subdivisions, and controlled the entity. Typically, the state treasurer managed the fund, although this was not the case in all the rulings. Each member contributed funds from general revenues based on actuarial risk determinations. The entity received investment income. The entity reimbursed members for casualty losses. In the event of dissolution, assets would be distributed to member political subdivisions. The rulings held that the investment of funds was a necessary incident of the power of governmental entities to raise revenue and meet expenses. The rulings also concluded that insuring political subdivisions against risk arising from governmental activities also was a governmental obligation. The rulings determined that risk pooling (rather than purchasing commercial insurance) fulfilled the obligations of the political subdivisions to protect their financial integrity. A universal requirement was that no private interests participated in or benefited from the operation of the entities. The IRS concluded that the entities performed an essential governmental function. Regarding the accrual requirement, the rulings observed that, since income was used to reimburse losses incurred by the participating political subdivisions or to reduce their annual fees, and did not benefit private interests, and since assets would be distributed to members upon dissolution, the income accrued to a political subdivision. Any private benefit to employees (*i.e.*, payment of claims) from insuring against these risks was incidental to the public benefit.

C. Section 115 Rulings

Since 1988, the IRS has issued over 170 private rulings under section 115, triple the number during the previous decade. These rulings generally look to *Maryland Savings Share Insurance Corp. v. United States*, 308 F. Supp. 761 (D. Md.), *rev'd on other grounds*, 490 U.S. 4 (1970) ("*MSSIC*") and Rev. Rul. 77-261, 1977-2 C.B. 45 for guidance.

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[18] Apparently, even if these self-insurance entities are not organized as separate corporations, they are treated as such by the IRS (absent exclusion under section 115) because unincorporated entities primarily involved in insurance activities are taxable as corporations. Rev. Rul. 83-132, 1983-2 C.B. 270.

The key "essential governmental function" factors most often cited in the rulings include state control and domination, the importance of the activity to the state as evidenced by legislation declarations, and the extent of the state's own investment in the enterprise, which indicates whether the state viewed the function as sufficiently essential "to lay its money on the line." The rulings look at the state's investment in the enterprise, whether the state bears the operating costs, and whether the state has committed to meet the liabilities of the enterprise. The key accrual factors seem to be whether income is paid to or credited to the account of the state; whether, upon dissolution, the enterprise's assets will be transferred to the state; and the extent of private benefit.

1. State Investment Funds

In recent years, the IRS has considered investment pools established on behalf of political subdivisions, and has reaffirmed its position in Rev. Rul. 77-261, 1977-2 C.B. 45, that investment of public funds can be an essential governmental function. In PLR 9541030 (Oct. 13, 1995), the IRS ruled that the income of an unincorporated investment pool established by several political subdivisions was exempt from federal taxation under section 115. The purpose was to permit investment of idle funds. The investment objective was maximum current income consistent with the primary objectives of preservation of capital and maintenance of liquidity. The fund members were political subdivisions and their integral parts. A nonprofit corporation was organized solely to govern the fund. The board of the corporation managed and administered the fund; board members were elected by the member political subdivisions. The state treasurer served as president of the corporation and was a board member. The net assets or earnings did not inure to and were not distributed for the benefit of any private persons. Members could withdraw their funds with interest at any time. If the fund dissolved, the net assets would be distributed to the fund member political subdivisions. The IRS relied on Rev. Rul. 77-261, concluding that the fund performed an essential governmental function. The income was used solely to provide benefits to members, which were political subdivisions, and in the event of dissolution, all assets were to be distributed to members. Consequently, the IRS concluded that the income accrued to political subdivisions within the meaning of section 115. However, since the exemption from income was under section 115, the IRS ruled that the fund was required to file a tax return. The ruling did not address the tax status of the nonprofit corporation.

Similarly, in PLR 9435031 (Sept. 2, 1994), the IRS considered a pooled investment fund created for state school districts to invest surplus funds. Because the school districts had the power to tax, it was held that they were political subdivisions. The fund was a public corporation authorized by state statute. It was governed by a board. All but one board member were elected by the participating school districts, and

were school district employees. The board held legal title to cash and other property contributed by the members. The board could enter into contracts for administrative and custodial services. The investment goals were safety, liquidity, and return on investment. The income could not accrue to a private party. Upon dissolution, assets would be distributed to the members.

The IRS concluded that "[t]he investment of positive cash balances by a state or political subdivision thereof in order to receive some yield on the funds until they are needed to meet expenses is a necessary incident of the power of the state or political subdivision to collect taxes and other revenues for use in meeting governmental expenses." Therefore the fund performed an essential government function. Since no part of it accrued to any private party, members could redeem their interest at any time except during emergency situations, and the dissolution clause provided that the assets returned to members. The IRS held that the income accrued to a state or political subdivision. The fund was a wholly-owned instrumentality of the political subdivisions, and its income was excluded under section 115.

This approval of governmental investment activities as essential governmental functions has been criticized by some commentators who favor restricting state exemption from federal taxation. It also potentially creates some tensions with the IRS position on programs like the prepaid tuition programs, where the IRS takes the position that it is not an essential governmental function for the government to lend its own exempt status to the investment activity of individual investors. The IRS faces this difficulty particularly in reviewing programs in which the state indirectly conducts investment activity on behalf of individual beneficiaries.

2. Litigation Settlement Funds

As discussed above, several rulings address funds created by state officials from the proceeds of litigation judgments or settlements. In one case, a state created two funds to hold settlement payments received as a result of litigation by the attorney general. PLR 9733003 ((May 9, 1997). Settlement A was from state litigation against a trade school; the proceeds in fund A were paid as restitution to the individual claimants who were former students of the school. The second fund, fund B, consisted of settlement proceeds of antitrust cases in federal court brought by the state as *parens patriae* for its residents. The plaintiff class members who were to receive the settlement proceeds in fund B were the state and municipalities.

The IRS seemed to conclude without discussion that the funds were an essential governmental function. Applying the accrual test, however, the IRS determined that only the income of fund B was excluded from gross income under section 115, since

that income eventually accrued to the state and municipalities, while private parties received more than an incidental private benefit from fund A.

3. Other Section 115 Rulings

Other rulings under section 115 continue to illustrate that the IRS is, inexplicably, more liberal than the courts in finding both essential governmental function and accrual.

For example, a decedent bequeathed property to a city in trust to be used exclusively to establish and support a library. The IRS recognized libraries as ordinary municipal functions, and concluded that section 115 was met without any analysis of the accrual requirement. PLR 9115016 (Jan. 10, 1991). Although there was no private benefit, there also was not accrual to the city, at least not as it has historically been understood. The city had no control over the library, its assets or income, and under the terms of the bequest, the assets and income could not be used by the city for any other purpose. Thus, the apparent lack of control did not seem to affect the determination of either essential governmental function or accrual.

A mine reclamation fund ruling provides another unusual ruling relating to accrual. PLR 9126027 (March 29, 1991). As part of a mine reclamation program, a state created an insurance program to pay private property owners for land subsidence due to mining. The program was funded by a federal grant. Homeowners paid a fee to participate. Upon termination, the remaining funds reverted to the federal government, not to the state. The ruling determined that such a program was an essential governmental function. It concludes that the accrual requirement was satisfied because all of the income "used to perform the public purpose," which was payments to private landholders. Curiously, there is no discussion of the fact that the entire purpose of the program was a substantial private benefit limited to participants in the program. This would appear to be inconsistent with the IRS's ruling with respect to the Michigan Educational Trust, although it is consistent with the IRS rulings under the "integral part" theory relating to disaster insurance programs.[19]

[19] This ruling also is inconsistent with GCM 39006 (June 28, 1983), which reviewed a similar mine subsidence fund which was established by statute but run by insurers. The IRS ruled that the state had no long-term commitment (other than a start-up loan) and received no financial benefit. The beneficiaries were private landowners. The IRS denied exclusion under section 115. PLR 9126027 does not mention GCM 39006, which suggests that the accrual test requires a direct financial benefit to the state.

D. Summary of Section 115

It is clear from the rulings that the IRS adopts a very broad view that an "essential governmental function" is whatever the state legislative says it is. Most rulings quote Rev. Rul. 77-261, which stated the premise that "it may be assumed that Congress did not desire it any way to restrict a state's participation in enterprises that might be useful in carrying out those projects desirable from the standpoint of the state government which, on a broad consideration of the question, may be the function of the sovereign to conduct." *See, e.g.*, PLR 9669634 (Dec. 1, 1995).

For purposes of the accrual test, the IRS has long looked to the destination of the funds and more particularly, looks for benefits to private individuals, which apparently is fatal under section 115 (although apparently not under the "integral part" theory, under the *MET* decision and disaster fund rulings). Certainly in the MET ruling, the IRS made its decision based on a private benefit analysis without any actual discussion of accrual. This seems to reflect a trend toward emphasizing a concern with benefits to private individuals over the historical understanding of the accrual test (which required that the income must accrue in a technical sense). *See* Rev. Rul. 90-74. To some extent the IRS appears to use the private beneficiary test as a separate requirement from the accrual test, rather than a part of it, *see, e.g.*, PLR 8825027 (MET). On the other hand, there are numerous rulings in which the IRS has granted section 115 exclusion to governmental pension plans, which exclusively pay benefits to individuals. *See, e.g.*, G.C.M. 34704 (Dec. 2, 1971); PLR 8825027 (July 2, 1988). The IRS has not explained how it distinguishes pension plans from prepaid tuition plans in terms of the applicable criteria. One possible explanation is that the rulings also appear to reflect a trend toward examining whether the activity benefits the government financially by relieving it of some present or future financial obligation, which can have the effect of permitting private benefit which is considered "incidental" to the public benefit, resulting in an even more generous application of section 115.

Although there is no authority for this argument, it may be possible to argue under section 115 that any income that does not benefit private parties (*i.e.*, is not transferred to the dividend fund) should be excluded under section 115. We find no rulings addressing whether income can be allocated in this fashion, although the *MET* ruling determined that the payments by the state and investors into the fund were excludible, presumably as some form of "capital" contribution. Section 115 does not purport to characterize all of the income of an entity as taxable or excluded from gross income. Rather it provides that "gross income does not include" income of a certain character. Arguable, income that in fact accrues to the state should be excludible, even if the income that ultimately benefits private persons might not be.

V. Other Developments

We understand that there have been several factual developments which we believe enhance the Fund's position. These include legislative clarification of the Permanent Fund provisions and other statutory provisions, state court decisions, Attorney General opinions, and perhaps subtle changes in the way the APFC presents itself publicly and in publications such as its annual report. There may well be other developments that we have failed to note here that also serve to enhance the Fund's position in asserting these legal arguments.

For example, AS section 37.13.030, which formerly stated that the Fund's assets were "allocated to" the APFC, was amended in 1992 to state that the Fund's assets were to be managed "by" APFC, thus clarifying that the statute creating the APFC effected no change of ownership. *See also* AS 37.13.020, .140, .150, .160, .170, .180, .190 for similar changes in reference from APFC to the Fund. In particular, the statute no longer refers to the "net income of the corporation" but rather to the "net income of the Fund." AS 37.13.140.

We note that there have been, over the years, positive albeit subtle changes in the language used by APFC to describe its functions and role *vis a vis* the Fund and the State. The Annual Report plainly indicates that the assets and income are those of the Fund, and that APFC is a state instrumentality which is the investment manager and not the owner. We understand that APFC's accounting procedures record the assets and earnings as those of the Fund, and the earnings reserve account is reported on a public fund model rather than a corporate model.

The Alaska Supreme Court confirmed that the earnings reserve account is subject to legislative appropriation and cannot be spent absent a legislative appropriation. *Hickel v. Cowper*, 874 P.2d 922, 934-935 (Alaska 1994).

Since 1988, several Attorney General opinions have reinforced earlier opinions with respect to the Fund and APFC's relationship to the State and the applicability of certain state laws. For example, the Attorney General determined that all operating funds of the APFC are public funds subject to the constitutional requirement that they be used only for a public purpose, and could not be expended in a manner inconsistent with the government-approved budget. The opinion further concluded that the APFC was subject to the State's Open Meetings Act and the Ethics Act, both of which apply only to governmental agencies. OAG File No. 663-93-0397 (July 6, 1993). Similarly, the AAG determined that the APFC is subject to state contracting and procurement requirements applicable to state agencies. OAG File No. 663-93-0250 (Jan. 26, 1993).

VI. Conclusion and Recommendations

We continue to recommend that the State take the position that the Fund and APFC are integral parts of the state, and thus not subject to federal taxation, relying on the authorities cited in our prior Report and the *MET* decision. We recommend that section 115 be presented as an alternative basis for exclusion of income from federal taxation, relying on the authorities cited previously and Rev. Rul. 90-74.

The many rulings issued by the IRS, while not authoritative, are nevertheless instructive. It is clear that many of the factors discussed in rulings relating to legislative purposes, governmental function, and state control are present in the Fund and APFC. *See* Report at 45-64, 104, 122-25. The recent rulings reinforce the importance of these indicia of state creation, control and domination. While we would reiterate our preference that the Fund be managed by an agency rather than a corporation, the statutory amendments and other changes in the APFC's mode of doing business have done much to relieve this concern. The several rulings granting integral part status to corporations also indicate that although this may be an important threshold consideration for the IRS, it does not appear to be determinative given sufficient evidence of state control and financial commitment.

We continue to be concerned about the potential perception of the dividend fund program as an improper private benefit, particularly in light of the wide-ranging discussion about the future of the Fund and the dividend program. While private benefit has always been an element of the accrual test under section 115, it increasingly appears to be an important criterion of independent significance. The rulings suggest that private benefit is simply impermissible under section 115, other than that incidental to the public purpose (*e.g.*, payment of state employee insurance claims under a pooled insurance program). It is unclear to what extent the income of the Fund, although it clearly accrues to the State, might be considered to ultimately benefit private beneficiaries.

The developments of the last ten years also have revealed the surprising extent to which this concern with private benefit seems to be influencing the IRS' interpretation of the "integral part" theory. Since that theory has been developed in only one case, *MET*, which the IRS rejects, the IRS presently is to a great extent in a position to interpret "integral part of a state" as it chooses, constrained only by its own prior (and reversible) rulings. On the other hand, the disaster fund rulings seem clearly to suggest that private benefit is not a bar to an entity being characterized as an integral part of the state. In cases where there is significant private benefit, the IRS appears to be willing to overlook it if there is not only sufficient evidence of public purpose and state control, but also a significant state financial commitment such that the assets of the state are at risk in the enterprise. Although this focus on the state's financial commitment does not

appear to be greatly emphasized in the rulings, it was clearly the guiding principle in the IRS's negotiations with the states regarding those rulings. And certainly that element is satisfied with respect to the Fund.

The private benefit arguably represented by the dividend program continues to fall into a gray area in terms of public purpose. At one end of the spectrum are the approved disaster insurance programs> The IRS found a sufficient governmental purpose to help its citizens protect themselves against natural disasters in the wake of significant disasters with profound economic consequences for the state. The IRS may have been particularly persuaded by the suggestion that, absent such programs, the financial consequences would be borne more directly by the state. At the other end of the spectrum are the prepaid tuition programs, which the IRS characterized as private investment schemes wrapped in the state's cloak of tax exemption. It may be difficult to argue that the dividend program is more like the former than the latter.

We believe that as long as the income from the Fund clearly accrues to the State and no individual has a vested interest in the income or assets of the Fund, the income and assets are those of the State alone, and thus not subject to federal taxation. How the State chooses to appropriate or spend its revenues should have no impact on this determination, except perhaps to further reinforce the argument that the investment activity is an integral part of the State and essential governmental function. And as long as the dividend program is implemented as a matter of legislative grace, we believe that it will be difficult for the IRS to argue that, having earned the income (investment being an appropriate public purpose and essential governmental function), it is not entirely within the discretion of the State to appropriate it as it sees fit, whether through legislative allocation or annual budget appropriations.

Conversely, to the extent that the Fund, or some portion of it, becomes irreversibly dedicated to the benefit of private beneficiaries, or to the extent that the dividend program becomes an entitlement that is beyond the reach of the government, then it becomes more like the prepaid tuition programs and is subject to potential challenge by the IRS as a private, rather than public, investment activity.

Sincerely,

Linda Arnsbarger

Linda Arnsbarger

Enclosures

dc-111890

Alaska State Legislature

Please enter into the record my testimony to the Senate Finance committee name

committee on SJR 33 / PFD bill/subject, dated 3/22/00.

PLEASE SEE TESTIMONY ATTACHED

Signed: Kathleen Ballenger
Testifier

Representing (Optional)

PO Box 126 Kodiak, AK 99615-0126
Address

907-486-3384
Phone No.

Good morning from Kodiak. My name is Kathleen Ballen, Jr. and I have called this wonderful island my home for 32+ years.

Several weeks ago I addressed the House Judiciary Committee on HJR 47 and felt it was incumbent on me to also plead my case to your committee. Please show me as a strong supporter of Senate Joint Resolution 33.

I believe passionately that this senate bill should be given very serious consideration and not merely scoffed at as a whimsy of Senator Jerry Mackie. Personally I think the dialogue that this bill has generated has been overwhelming and for that Senator Mackie and Representative Davis can certainly be proud.

I am in support of this bill mainly so we can get ourselves out of the economic quagmire we are in. It is ludicrous that the State of Alaska is sitting on billions of dollars and we are having problems balancing the budget and trying to decide which programs to keep and which to cut. I have difficulty listening to the hassle over funding for the local communities, the schools, roads, public safety and on and on. I am pleading with you to pass this bill out of committee to allow the entire Senate to debate the pros and cons of the bill and to get more input from the electorate. I cannot

honestly see how anyone can argue against a plan that would wipe out the current deficit and allow us to start again from ground zero. There certainly aren't many states that have that capability. We truly are in a very unique situation and to me this bill makes perfect sense.

We can do a lot of finger pointing to what's gone on in the past. It's apparent that we overspent during our flush times and are now having problems cutting out programs that all of us have gotten used to. It seems that this would be a wonderful way to say – okay here is the money you need for all the programs the State feels are vital and important and then safeguard the balance of the funds for future needs -- not just wants. We would then be able to put the onus back on you -- our legislators - to run a fiscally prudent ship. Responsibility would also be put on us - the voters – to be certain that we do a better job at election time making sure our legislators are doing what we asked of them. Everyone wants to blame everyone else and this to me would be a perfect way to level the playing field for all.

The comments I have heard against the passage of this bill and the one-time pay-out of $25,000 per resident are mighty lame at best. They run from "I would take the money if I didn't have to pay

income taxes on it" to "people will take the money and leave" to "we would be short changing the future generations." These are all pretty inconsequential as far as I'm concerned. Unless you have a better accountant than I do, I have been paying income taxes on the PFD's all along. And of course the idea of wanting the state to pay your income taxes coincides with the new TV show "Greed." When is enough enough? For those who say some would take the money and leave I say fine – if that's all they wanted from our great State – good riddance. And the argument about not having the PFD for future generations is mighty hopeful at best. Who can say how long it will be before the PFD is used for something or another.

I think the State should realize that they cannot and should not be concerned with what is or is not done with the $25,000 if it should pass. Some of us will do wise things – some will not – but that is not the responsibility of the state nor should it be.

Many will be able to do great things with the money – I just cannot help but think that some will be able perhaps for the only time in their lives to "grab the ring". I will love being here to see it and to feel the fervor in them.

I urge you to pass this bill out of committee to get it one step closer to allowing all of us to have a say. I sincerely believe that even those who say they are against the $25,000 distribution and ultimate elimination of the Fund might in fact vote differently behind the closed curtain. Please let us have a say in this very important issue.

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