

ALASKA LEGISLATURE COMMITTEE FILES 1985-1986 86/2

3868 SCRA SB 244 (FILE 1) 794

RESOLUTION OF THE BOARD OF TRUSTEES
OF THE ALASKA PERMANENT FUND CORPORATION
REPEALING RESOLUTION 83-9 DEFINING "NET INCOME"
AND ADOPTING A REPLACEMENT DEFINITION

RESOLUTION 83-11

WHEREAS, the Trustees adopted Resolution 83-9 on July 22, 1983 defining "net income" for purposes of income averaging; and

WHEREAS, the resolution was further reviewed at a meeting on August 29, 1983 attended by representatives of the Department of Law, Department of Revenue, Permanent Fund Staff, and accountants Price Waterhouse (Memorandum of September 6, 1983 is attached hereto); and

WHEREAS, aforementioned representatives now believe that Resolution 83-9 improperly interprets AS 37.13.140 and AS 37.13.145 taken in full context; and

WHEREAS, generally accepted accounting principles would, more properly, treat the undistributed income account as corporate retained earnings available for distribution;

NOW THEREFORE, BE IT RESOLVED that the Trustees repeal their approval of Resolution 83-9 dated July 22, 1983; and

BE IT FURTHER RESOLVED that the Trustees determine that earnings on undistributed income are earnings of the Corporation; and

BE IT FURTHER RESOLVED that the Trustees direct the Executive Director to account for "net income" and utilize same for the calculation of "net income available for distribution" in such a manner as to include both earnings on the corpus of the Fund and earnings on the undistributed income account.

PASSED AND APPROVED by the Board of Trustees of the Alaska Permanent Fund Corporation, this 27th day of September, 1983.

Steve Cowper, Chairman
Board of Trustees
Alaska Permanent Fund Corporation

ATTEST:

David A. Rose, Executive Director

RESOLUTION OF THE BOARD OF TRUSTEES
OF THE ALASKA PERMANENT FUND CORPORATION
DEFINING "NET INCOME" FOR PURPOSES OF INCOME AVERAGING

RESOLUTION 83-9

WHEREAS, AS 37.13.140 specifies in part:

"Sec. 37.13.140. Income. Net income of the corporation must be computed annually as of the last day of the fiscal year in accordance with generally accepted accounting principles, excluding any unrealized gains or losses. Income available for distribution equals the average net income of the corporation for the last five fiscal years, including the fiscal year just ended, ..."; and

WHEREAS, the Statute does not specifically include or exclude earnings on the Undistributed Income Account from the term "net income"; and

WHEREAS, the Trustees wish to clarify the terminology as it has a bearing on calculations of income available for distribution; and

WHEREAS, earnings on the Undistributed Income Account are calculated separately and are restricted in that they cannot be utilized for inflation proofing; and

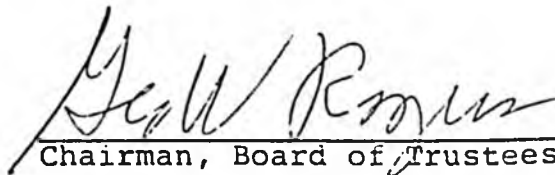
WHEREAS, these earnings are in investment and custody status with the Corporation and not subject to its use;

NOW THEREFORE, BE IT RESOLVED that the Trustees determine that the term "net income" as used in AS 37.13.140 pertains to the net income earned from the investment of those funds belonging to the Alaska Permanent Fund which it considers its corpus and over which it has total ownership, control and use; and

BE IT FURTHER RESOLVED that the Trustees determine that the net income of other funds such as the Undistributed Income Account which are invested on a commingled basis, shall be separately computed and applied to its respective parent account or fund as appropriate; and

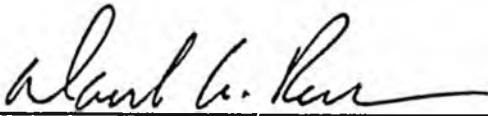
BE IT FURTHER RESOLVED that the Trustees direct the Executive Director to account for "net income" and utilize same in computations required by AS 37.13.140 in such a manner as to exclude earnings on the Undistributed Income Account from "net income" and thus also exclude these earnings from computations involving "income available for distribution."

PASSED AND APPROVED by the Board of Trustees of the Alaska Permanent Fund Corporation, this 22nd day of July, 1983.



Chairman, Board of Trustees
Alaska Permanent Fund Corporation

ATTEST:



David A. Rose, Executive Director



Alaska Permanent Fund Corporation
Pouch 4-1000 Juneau, Alaska 99802
TEL 907/465-2047 TLX 099-46-323

MEMORANDUM

DATE: September 6, 1983

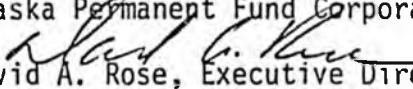
TO: Laura Davis, Assistant Attorney General
Department of Law

Milton B. Barker, Deputy Commissioner
Treasury, Department of Revenue

Vincent Wright, Chief of Research
Department of Revenue

Bill Smart
Price Waterhouse, Anchorage

Peter A. Bushre, Comptroller
Alaska Permanent Fund Corporation

FROM: 
David A. Rose, Executive Director
Alaska Permanent Fund Corporation

SUBJECT: Distributions of Permanent Fund Income

This memorandum will confirm the decisions made at our meeting on Monday, August 29, 1983. The meeting was called to resolve certain questions surrounding interpretations of AS 37.13.140, AS 37.13.145 and Section 15 of Chapter 81, SLA 1982. Specifically, the questions discussed and the decisions agreed upon by everyone present were as follows:

1. Does Sec. 15 of Ch. 81, SLA 82 include a partial distribution of FY 83 earnings? Section 15(a) provides that all of the income earned (including accrued income) prior to July 1, 1982 that was not distributable under prior law is to be transferred to the undistributed income account. The provision includes the portion of FY

81 and FY 82 earnings retained by the Fund (the undistributed portion of current income not distributable on an averaging basis) and accrued income at the end of FY 82. The section further provides that this amount is to be reduced by an amount equal to one-half of FY 83 distributable income, i.e., an amount equal to one-half of FY 83 distributable income is not retained by the Fund in the undistributed income account.

Section 15(b) provides that this amount is to be transferred to the general fund. The history of section 15 is that the legislature wanted a distribution of FY 83 earnings at least equal to the FY 82 accrual basis liability. The amount credited to the undistributed income account would be reduced by the amount of that distribution.

Conclusion: Ch. 81, SLA 82 includes a distribution of FY 83 earnings equal to one-half of distributable income for that year.

2. Is distributable income a cash basis or accrual basis calculation under Sec. 15 of Ch. 81, SLA 82? Section 15(b) provides that distributable income is to be calculated by the formula in AS 37.13.140 before it was amended by Ch. 81, SLA 82. Under prior law, AS 37.13.140 specified that the income of the Corporation was the interest received each fiscal year. Distributable income is a moving average of the income received each fiscal year.

Conclusion: Distributable income is a cash basis calculation under Ch. 81, SLA 82.

3. Is distributable income a cash basis or accrual basis calculation under AS 43.23.045(b)? Subsection (b) provides for the transfer of an amount to the dividend fund from Permanent Fund earnings (or undistributed income if current year earnings are not adequate) equal to one-half of the amount available for distribution. The amount available for distribution is determined by AS 37.13.140 which provides that it is an average of the net income of the Corporation for the last five fiscal years. Net income is defined by that section as being in accordance with generally accepted accounting principles, which is accrual basis income.

Conclusion: Distributable income is an accrual basis calculation

under AS 43.23.045(b).

4. Is net income for the years prior to adoption of Ch. 81, SLA 82, which is used in the calculation of distributable income for FY 83, calculated under current law for years prior to FY 83 or the law in effect when it was earned? AS 37.13.140 before the adoption of Ch. 81, SLA 82 specified that income was the interest received by the Corporation; after the adoption of Ch. 81, SLA 82 it was in accordance with generally accepted accounting principles. Under current law, AS 37.13.140 defines income available for distribution as an average of the net income of the Corporation for the last five fiscal years, and specifies that net income is to be computed in accordance with generally accepted accounting principles. The law makes specific reference to an accrual basis income for each of the five years in the average. Reference to an August 11, 1982 memorandum drafted by Thomas K. Williams which explains the intent of the Trustees revealed that income as calculated under the amendments of Ch. 81, SLA 82 was to be used in each year of the average.

Conclusion: Net income for the years prior to adoption of Ch. 81, SLA 82 used in the calculation of distributable income for FY 83 is determined by current law.

5. Is the liability to the Dividend Fund determined by AS 37.13.140 or by appropriation? The income distributable to the Dividend Fund for FY 83 under AS 37.13.140 is more than the appropriation for FY 83. Reference was made to an opinion of the Attorney General (file: 366-484-83) dated March 10, 1983, which held, in essence, that all or a portion of Permanent Fund earnings can be retained in the Fund by operation of law, but an appropriation is necessary for distributions to any fund other than the general fund.

Conclusion: The liability to the Dividend Fund is the amount of the appropriation.

6. Are earnings on undistributed income included in the calculation of income available for distribution? AS 37.13.145 makes specific reference to the definition of income in AS 37.13.140 as the income

Re: Distributions of Permanent Fund Income
September 6, 1983
Page 4

available for inflation-proofing, excluding the income attributed to the investment of undistributed income. AS 37.13.140 defines income available for distribution as the average net income of the Corporation for the last five fiscal years. The undistributed income account is identified by AS 37.13.145 as an account within the Permanent Fund, and its income is to be treated as an addition to that account.

Generally accepted accounting principles would treat the undistributed income account as corporate retained earnings available for distribution. A dividend or other distribution could be declared at any time by appropriation, but until it is, they are corporate earnings retained for reinvestment.

Conclusion: Earnings on undistributed income are included in the calculation of income available for distribution.

DAR/aef

Sec. 37.13.140. Income. Net income of the corporation must be computed annually as of the last day of the fiscal year in accordance with generally accepted accounting principles, excluding any unrealized gains or losses. Income available for distribution equals the average net income of the corporation for the last five fiscal years, including the fiscal year just ended, but may not exceed net income of the corporation for the fiscal year just ended plus the balance in the undistributed income account described in AS 37.13.145. (§ 5 ch 18 SLA 1980; am § 8 ch 81 SLA 1982)

Effect of amendments. — The 1982 amendment, effective July 1, 1982, rewrote this section.

§ 37.13.145

ALASKA STATUTES SUPPLEMENT

§ 37.13.170

Sec. 37.13.145. Disposition of income. At the end of each fiscal year, an amount sufficient to offset the effect of inflation on principal of the Alaska permanent fund during that year, as measured by a nationally recognized index, shall be transferred from net income as defined in AS 37.13.140, excluding income on the undistributed income account in the Alaska permanent fund, to the principal of the Alaska permanent fund for reinvestment. The balance of the net income as defined in AS 37.13.140 shall be transferred to the undistributed income account in the Alaska permanent fund. Money in the undistributed income account shall be invested in investments authorized under AS 37.13.120. Income from the investment of the undistributed income account shall be treated as an addition to that account. (§ 9 ch 81 SLA 1982)

Effective dates. — Section 16, ch. 81, SLA 1982, makes this section effective July 1, 1982.

Editor's notes. — Section 15, ch. 81, SLA 1982, provides: "TRANSITION. (a) All income earned by the Alaska permanent fund before the effective date of this Act [July 1, 1982] that is not income available for disbursement shall be transferred to the undistributed income account established in AS 37.13.145 added by sec. 9 of this Act. However, the amount transferred

under this section shall be reduced by an amount equal to one-half of the income available for disbursement for fiscal year 1983.

"(b) The amount equal to the reduction in income under (a) of this section shall be transferred to the general fund.

"(c) The amount of income available for disbursement shall be determined as set out in AS 37.13.140 before amendment by this Act."

ALASKA PERMANENT FUND Corporation

Statement of Changes in Fund Balance

For the Years Ended June 30, 1982 and 1981

	Total	Appropriations, Royalties and Other State Receipts	Undistributed Income
Balance, July 1, 1980	\$ 483,208,000	\$ 483,208,000	
Appropriations from State of Alaska General Fund	900,000,000	900,000,000	
Royalties and other state receipts	385,128,000	385,128,000	
Investment income	149,867,000		\$149,867,000
Transfer of net investment gains to principal		219,000	(219,000)
Distributable income due to State General and Segregated Funds	(90,904,000)		(90,904,000)
Balance, June 30, 1981	1,827,299,000	1,768,555,000	58,744,000
Appropriation from State of Alaska General Fund	800,000,000	800,000,000	
Royalties and other state receipts	400,522,000	400,522,000	
Investment income	368,426,000		368,426,000
Distributable income due to State General and Segregated Funds	(183,411,000)		(183,411,000)
Balance, June 30, 1982	\$3,212,836,000	\$2,969,077,000	\$243,759,000

See accompanying notes to financial statements

Note 5 — Amount Due to the State General and Segregated Funds:

The amount due to the State General and Segregated Funds is determined on the basis of the current year's distributable income as provided by statute adjusted for actual cash distributions and prior year's accrued amount due to the Funds. Summarized below is the activity for the fiscal years ended June 30, 1982 and 1981.

Balance, July 1, 1980		\$ 19,669,000
Add: 1981 accrual of distributable income		90,904,000
Less: Cash transfers made —		
Amounts transferred applicable to 1980	(19,669,000)	
Amounts transferred applicable to 1981	(43,565,000)	(63,234,000)
Balance, June 30, 1981		47,339,000
Add: 1982 accrual of distributable income		183,411,000
Less: Cash transfers made —		
Amounts transferred applicable to 1981	(47,339,000)	
Amounts transferred applicable to 1982	(94,592,000)	(141,931,000)
Balance, June 30, 1982		\$ 88,819,000

Note 6 — Administrative Expenses (Unaudited):

Administrative and other expenses are paid by the State of Alaska General Fund and are not included in the accompanying statements. The related budget and actual expenses for 1982 and budgeted expenses for 1983 for operations of the Permanent Fund Corporation are as follows (unaudited):

	<u>1982</u>		<u>1983</u>
<u>Budget</u>		<u>Actual</u>	<u>Budget</u>
\$450,500		\$391,200	\$3,070,500

Alaska Permanent Fund Corporation

Statement of Changes in Fund Equity
For The Years Ended June 30, 1983 and 1982

	<u>Total</u>	<u>Contributed Equity</u>	<u>Undistributed Income</u>
Balance, June 30, 1981	\$1,827,299,000	\$1,768,555,000	\$ 58,744,000
Appropriations from the State	800,000,000	800,000,000	
Dedicated state revenues	400,522,000	400,522,000	
Investment income	368,426,000		368,426,000
Distributions of income	<u>(183,411,000)</u>		<u>(183,411,000)</u>
Balance, June 30, 1982	3,212,836,000	2,969,077,000	243,759,000
Appropriations from the State	400,000,000	400,000,000	
Dedicated state revenues	420,957,000	420,957,000	
Net income from operations	471,125,000		471,125,000
Distributions of income	<u>(129,882,000)</u>		<u>(129,882,000)</u>
Provision for inflation		<u>231,192,000</u>	<u>(231,192,000)</u>
Balance, June 30, 1983	<u>\$4,375,036,000</u>	<u>\$4,021,226,000</u>	<u>\$353,810,000</u>

See accompanying notes to financial statements

Income Distributable to the State of Alaska

	<u>Total</u>	<u>Dividend Fund</u>	<u>General Fund</u>
Balance, June 30, 1981	\$ 12,339,000	\$ 23,670,000	\$ 23,669,000
Add: 1982 accrual of distributable income	<u>183,411,000</u>	<u>91,706,000</u>	<u>91,705,000</u>
	<u>230,750,000</u>	<u>115,376,000</u>	<u>115,374,000</u>
Less: Cash transfers - Applicable to 1981 accruals	<u>(47,339,000)</u>	<u>(23,670,000)</u>	<u>(23,669,000)</u>
Applicable to 1982 accruals	<u>(94,592,000)</u>	<u>(47,296,000)</u>	<u>(47,296,000)</u>
	<u>(141,931,000)</u>	<u>(70,966,000)</u>	<u>(70,965,000)</u>
Balance, June 30, 1982	<u>88,819,000</u>	44,410,000	44,409,000
Add: 1983 accrual of distributable income	<u>217,410,000</u>	<u>107,875,000</u>	<u>109,535,000</u>
	<u>306,229,000</u>	<u>152,285,000</u>	<u>153,944,000</u>
Less: Cash transfers applicable to 1982	<u>(1,291,000)</u>	(646,000)	(645,000)
Transition rule adjust- ment	<u>(87,528,000)</u>	<u>(43,764,000)</u>	<u>(43,764,000)</u>
	<u>(88,819,000)</u>	<u>(44,410,000)</u>	<u>(44,409,000)</u>
Balance, June 30, 1983	<u>\$217,410,000</u>	<u>\$107,875,000</u>	<u>\$109,535,000</u>

	<u>Total</u>	<u>Dividend Fund</u>	<u>General Fund</u>
<u>1983 Provision Charged To:</u>			
Earnings on undistributed income	<u>\$ 31,104,000</u>	\$ 31,104,000	
Balance of undistributed income	<u>98,778,000</u>	<u>3,007,000</u>	<u>\$ 65,771,000</u>
Sub-total	<u>129,882,000</u>	<u>64,111,000</u>	<u>65,771,000</u>
Transition rule adjustment	<u>(87,528,000)</u>	<u>43,764,000</u>	<u>43,764,000</u>
Income distributable to the State	<u>\$217,410,000</u>	<u>\$107,875,000</u>	<u>\$109,535,000</u>

Alaska Permanent Fund Corporation

Statement of Changes in Fund Equity For The Years Ended June 30, 1984 and 1983

	Total	Contributed Equity	Reserve for Inflation and Dividends	Unrealized Loss On Common Stock	Undistributed Income
Balance, June 30, 1982	\$3,212,836,000	\$2,969,077,000			\$243,759,000
Appropriations from the State	400,000,000	400,000,000			
Dedicated state revenues	420,957,000	420,957,000			
Net income from operations	471,125,000				471,125,000
Provision for 1983 dividends	(64,111,000)				(64,111,000)
Provision for distributions to the state general fund	(65,771,000)				(65,771,000)
Provision for 1983 inflation		231,192,000			(231,192,000)
Balance, June 30, 1983	4,375,036,000	4,021,226,000			353,810,000
Appropriations from the State	300,000,000	300,000,000			
Dedicated state revenues	366,183,000	366,183,000			
Net income from operations	529,457,000				529,457,000
Provision for 1983 dividend supplement	(11,869,000)				(11,869,000)
Provision for 1984 dividends	(163,116,000)				(163,116,000)
Provision for 1984 inflation		150,935,000			(150,935,000)
Allowance for unrealized loss on common stock	(20,871,000)			\$(20,871,000)	
Provision for future inflation and dividends			\$557,347,000		(557,347,000)
Balance, June 30, 1984	<u>\$5,374,820,000</u>	<u>\$4,838,344,000</u>	<u>\$557,347,000</u>	<u>\$(20,871,000)</u>	<u>\$</u>

See accompanying notes to financial statements

Income Distributable to the State of Alaska

	<u>Total</u>	<u>Dividend Fund</u>	<u>General Fund</u>
Balance due, June 30, 1982	\$ 44,410,000	\$ 44,410,000	\$ 44,409,000
Add: 1983 appropriation and transition rule liability	<u>217,410,000</u>	<u>107,875,000</u>	<u>109,535,000</u>
	206,229,000	<u>152,285,000</u>	<u>153,944,000</u>
Less: Cash transfers— Applicable to 1982 Transition rule adjustment	(1,224,000)	(646,000)	(645,000)
	(27,528,000)	<u>(43,764,000)</u>	<u>(43,764,000)</u>
	287,819,000	<u>44,410,000</u>	<u>(44,409,000)</u>
Balance due, June 30, 1983	217,410,000	<u>107,875,000</u>	<u>109,535,000</u>
Add: 1983 supplemental appropriation	<u>11,869,000</u>	11,869,000	
1984 appropriations	163,116,000	<u>163,116,000</u>	
	374,985,000	<u>174,985,000</u>	
Less: Cash transfers— Applicable to 1983	(200,979,000)	(119,744,000)	(109,535,000)
Applicable to 1984	(7,986,000)	(7,986,000)	
	(208,965,000)	<u>(127,730,000)</u>	<u>(109,535,000)</u>
Balance due, June 30, 1984	\$155,130,000	<u>\$155,130,000</u>	<u>\$</u>

Note 8 - Contributed Equity:

The principal balances of the Alaska Permanent Fund at June 30, 1984 and 1983 are as follows:

	<u>June 30,</u>	
	<u>1984</u>	<u>1983</u>
Dedicated state revenues	\$2,056,217,000	\$1,690,034,000
Appropriations from the State	2,400,000,000	2,100,000,000
Cumulative provision for inflation	<u>382,127,000</u>	<u>231,192,000</u>
	<u>\$4,838,344,000</u>	<u>\$4,021,226,000</u>

In 1980, the State Legislature appropriated \$900,000,000 from general fund revenues to the Permanent Fund. This appropriation has been paid in full. In 1981, the Legislature appropriated an additional \$1,800,000,000 from general fund revenues to the Permanent Fund. This appropriation bill directs the Commissioner of Revenue to make monthly deposits of general fund operating surplus until the balance is reached. As of June 30, 1984, \$1,500,000,000 (June 30, 1983, \$1,200,000,000) of this appropriation had been deposited in the Permanent Fund.

ALASKA PERMANENT FUND CORPORATION
STATEMENT OF CHANGES IN FUND EQUITY
FOR THE YEARS ENDED JUNE 30, 1985 AND 1984

	<u>Total</u>	<u>Contributed Equity</u>	<u>Reserve for Inflation and Dividends</u>	<u>Unrealized Loss on Common Stock</u>	<u>Undistributed Income</u>
Balance, June 30, 1983	\$4,375,036,000	\$4,021,226,000			\$ 353,810,000
Appropriations from the State	300,000,000	300,000,000			
Dedicated State revenues	366,183,000	366,183,000			
Net income from operations	529,457,000				529,457,000
Provision for 1983 dividend supplement	(11,869,000)				(11,869,000)
Provision for 1984 dividends	(163,116,000)				(163,116,000)
Provision for 1984 inflation		150,935,000			(150,935,000)
Allowance for unrealized loss on common stock	(20,871,000)			\$(20,871,000)	
Provision for future inflation and dividends			\$557,347,000		(557,347,000)
Balance, June 30, 1984	3,744,820,000	4,838,344,000	557,347,000	(20,871,000)	
Appropriations from the State	300,000,000	300,000,000			
Dedicated State revenues	368,027,000	368,027,000			
Net income from operations	657,761,000				657,761,000
Citizen contributions	1,000	1,000			
Provision for 1985 dividends	(217,274,000)				(217,274,000)
Provision for 1985 inflation		234,570,000			(234,570,000)
Recovery of unrealized loss on common stock	20,871,000			20,871,000	
Provision for future inflation and dividends			205,917,000		(205,917,000)
Balance, June 30, 1985	<u>\$6,504,206,000</u>	<u>\$5,740,942,000</u>	<u>\$763,264,000</u>	<u>\$</u>	<u>\$</u>

See accompanying notes to financial statements

Income Distributable to the State of Alaska 10

	Total	Dividend Fund	General Fund
Balance due, June 30, 1983	\$ 217,410,000	\$ 107,875,000	\$ 109,535,000
Add: 1983 supplemental appropriation	11,869,000	11,869,000	
1984 appropriations	163,116,000	163,116,000	
	174,985,000	174,985,000	
	Total	Dividend Fund	General Fund
Less: Cash transfers - Applicable to 1983	(229,279,000)	(119,744,000)	(109,535,000)
Applicable to 1984	(7,986,000)	(7,986,000)	
	(237,265,000)	(127,730,000)	(109,535,000)
Balance due, June 30, 1984	155,130,000	155,130,000	
Add: 1985 appropriation	217,274,000	217,274,000	
Less: Cash transfers - Applicable to 1984	(155,130,000)	(155,130,000)	
Balance due, June 30, 1985	\$ 217,274,000	\$ 217,274,000	\$ _____

7. CONTRIBUTED EQUITY:

The principal balances of the Alaska Permanent Fund at June 30, 1985 and 1984 are as follows:



Official Business

Alaska State Legislature

Senate

Committee on Community and Regional Affairs

Senator Edna DeVries, Chairman

Members:
Senator Ferguson, Vice Chairman
Senator Coghill
Senator Sturgulewski
Senator V. Fischer

Pouch V
Juneau, Alaska 99811

137 E. Arctic
Palmer, Alaska 99645

MEMORANDUM

Copy

October 4, 1985

TO: Senator Ferguson, Vice Chair
Senator Sturgulewski
Senator V. Fischer
Senator Coghill

FROM: Committee Staff

SUBJECT: COMMITTEE HEARING MINUTES -- held consecutively in Anchorage,
Wasilla and Soldotna, Alaska on September 24, 25 & 26, 1985

SB 244 An Act relating to the undistributed income account in the
Alaska Permanent Fund for certain municipal aid programs,
establishing a two-year funding cycle; and providing for an
effective date.

Attached for your file are copies of the subject committee minutes.

Atchs 3

BILL SHEFFIELD, GOVERNOR

DEPT. OF COMMUNITY & REGIONAL AFFAIRS

OFFICE OF THE COMMISSIONER

POUCH B
JUNEAU, ALASKA 99811
PHONE: (907) 465-4700

949 E. 35TH AVENUE, SUITE 400
ANCHORAGE, ALASKA 99508
PHONE: (907) 563-1073

September 24, 1985

TESTIMONY FOR SB 244

"An Act relating to the use of funds from the undistributed income account in the Alaska permanent fund for certain municipal aid programs, establishing a two-year funding cycle; and providing for an effective date."

On behalf of Commissioner Notti I would like to thank the Senate Community and Regional Affairs Committee for the invitation to come before it today. The Department has been asked to present background information that we hope will assist you in evaluating Senator Coghill's proposal to "forward fund" the two major programs of State aid to municipalities and communities. I have been assigned the duty of acting as a technical resource for the committee and will be on hand for all of the hearings scheduled for Southcentral Alaska.

In order to put Senator Coghill's bill in perspective, I would like to give the committee a briefing on the history and background of the State Revenue Sharing and Municipal Assistance programs.

These programs, which are presently funded at over \$140 million, have a significant impact on virtually every city, borough, village, and community in the State. Most municipalities and villages rely on these program funds to provide vital local services and curb the need for increased local taxation. While the programs have generally been accepted as a reasonable way for the State to share its substantial revenues with its political subdivisions and villages, interest remains in seeking ways to improve the programs so that they may be more useful to local governments. The Governor's Task Force on State Shared Revenue has for the past nineteen months grappled with these programs in some detail in an attempt to offer sound recommendations to the Governor or ways to make the programs more responsive to local needs. The Task Force is working under a timetable which calls for offering proposed legislation to the Governor in early December.

The State Revenue Sharing (SRS) program is the oldest of the programs under discussion as it was enacted in 1969 and started operation in FY 70. The stated objectives of the program were to: help ease the fiscal problems facing local governments; stabilize or reduce local property tax rates; stimulate local governments to provide adequate levels of services; and improve resource allocation by sharing funds with local governments which, by virtue of being closer to the people, are superior at providing public goods and services in accord with taxpayer preferences.

*Present to
Muni
League
19
Nov*

SRS began with a \$2 million appropriation and shared funding solely with municipalities. Allocations were based on population and seven categories of service the municipality could provide plus aid for roads on the basis of mileage and health facilities and hospitals based on facilities or patient beds. The program rewarded municipalities that provided a wider range of services for the greatest number of people.

If the amount appropriated by the Legislature to fund the program was insufficient, all municipal entitlements were prorated by whatever amount was necessary to bring appropriations and entitlements into balance. Each year there was pressure brought to bear on the Legislature to fully fund the program. Increases in population, incorporation of new municipalities, increased road mileage, additional health facilities, and the assumption of new services by municipalities put a constant upward pressure on the need for increased funding to fully fund the demand created by new residents and new services.

The categorical State Revenue Sharing program remained in effect for ten years. However, after about five years of operation, the formula for allocating funding came under increasing scrutiny and attack. The criticism focused on three main, somewhat related, perceived shortcomings in the

allocation formula. First, the allocation of revenue was not "needs based" and did not take into account the relative wealth of a municipality. A city or borough that had a large tax base could provide a wide range of services and, therefore, receive a larger share of SRS, even though local tax effort might be relatively low. Conversely, a poorer local government with a low tax base could not afford to provide many services (and in rural Alaska the relatively higher costs of many services may have made them prohibitive), even with relatively higher taxes, yet the SRS formula penalized them by not providing them with adequate aid to expand service delivery. In effect, the rich got richer and the poor got poorer.

Second, the categories tied to SRS dictated implicitly what services were important and would be reimbursed by the State. While the categories covered basic life, health, and safety services, many people felt the local governments were best equipped to decide what services were important to their residents and that a block grant approach would be fairer and more useful for local governments.

Third, small local governments, which had some of the same basic overhead costs as larger cities, received inadequate levels of funding and were, therefore, unable to carry out the intent of the program to provide essential local service.

As a result of these shortcomings, work began during the mid-1970's to improve the State Revenue Sharing program in such a way as to distribute funds more fairly to those municipalities which needed the aid most. Interest was focused on replacing the categorical per capita approach with a formula that would equalize the tax resources of municipalities. In other words, the formula would benefit those local governments that were helping themselves as much as they could through local revenue sources while the formula provided relatively less to those municipalities that enjoy a broader tax base requiring less taxation. This formula would focus a greater share of State aid to those cities and boroughs that demonstrated through their tax structure a greater need.

After several years of discussion, the Eleventh Legislature, in 1980, passed HB 192 to drastically change the emphasis and intent of the State Revenue Sharing program. To aid in the transition to the new formula, a five year hold harmless provision was provided and the appropriation to the program was substantially increased. The legislative intent of the program was now to: improve the revenue raising and distribution system for the benefit of residents of home rule and general law municipalities by providing for more equitable allocation of financial resources among municipalities to improve their fiscal capacities and to insure that no municipality suffers impoverishment of necessary public services, relative to other municipalities, because of the chance location of taxable wealth in the state.

The new program was divided into three parts, each in a different chapter of Title 29. The seven per capita categories were replaced with the municipal tax equalization formula (Chapter 88) which allocated funding based on population and relative local tax effort. Initially \$34.9 million was allocated to this account and by FY 86 this appropriation had increased to \$38 million. The formula apportions the account's appropriation based on the prorated share of the municipality's population times a millage rate equivalent. The millage rate equivalent measures the local revenue raising effort of the municipality by dividing local tax and fee collections by one mill of the municipalities full and true property value. In effect, all eligible locally generated revenues are converted to a millage rate for purposes of comparability. It is this millage rate equivalent and the municipality's population which determine what portion of Chapter 88 funds will be allocated to each local government.

Chapter 89 contained the miscellaneous services account and allocated funding for various services and entities. Municipalities were eligible to receive \$2,500 per mile of road, \$1,500 per mile of ice road, \$2,000 per bed or \$8,000 per facility, whichever was greater, for health facilities, and \$250,000 per hospital, all adjusted to reflect cost of living differentials in various regions of the State. Unincorporated communities for the first time were eligible to receive \$25,000

under this chapter and volunteer fire departments serving residents of the unorganized borough were eligible to receive \$10 per capita. If funding was inadequate to fully fund all of the demand under this chapter, the entitlements were prorated. In FY 85 the proration factor was approximately 94%.

Chapter 90 reimbursed municipalities or nonprofit hospitals for up to 25% of total project construction costs. This reimbursement was usually made at a rate of 5% of the construction cost for five years. Two years ago this chapter was repealed and presently the Department is paying off the last two hospitals who began participation in the program before repeal. These hospitals, should be paid off within a couple of years and this portion of the program will then be put to rest.

The application process for the program remains relatively simple and straightforward and gives participants from mid-July until December 1 of each year to apply. The statutes for the program require approved budgets and audits or, in the case of second class cities, certified financial statements as part of the application process. Upon receipt of applications and budgets in the Fall, a prepayment of up to 50% of the preceding year's entitlement is issued. Final entitlement checks cannot be mailed until all applications have been processed and appeals resolved. Theoretically, this process should be

completed by April, unfortunately unforeseen problems or events can often delay this timetable. The Department has attempted to respond to these problems by releasing a substantial portion of the final amount through issuance of provisional final payments.

The Municipal Assistance program has been existence since FY 80. The program was begun as a replacement for the former Gross Business License Tax which was repealed in 1979. The stated intent for Municipal Assistance was for "local governments which levy property taxes to reduce those levies in reasonable proportion to the amount of state aid received by a local government." The program has been administered for these last five years, along with other Shared Tax programs, by the Department of Revenue. Only incorporated municipalities are eligible to participate in the program.

There are two parts to Municipal Assistance. First, each municipality receives a "base" amount of funding equal to the amount it received during the last year of the Gross business receipts Tax program. This amount totals about \$10.6 million statewide. Second, excess funding over the base amount is allocated to municipalities on a per capita basis. A borough's per capita allocation is based only on the population which resides outside of incorporated cities within the borough. In FY 85, the excess amount totaled about \$70.7 million based on a total appropriation of \$81.3 million.

The statute provides guidance to the legislature on the level of appropriation for the program. Initially, the appropriation was set at 10 percent of the prior years receipts from the Corporate Oil and Gas Tax. However, when the separate oil and gas tax was repealed in 1982 the law was changed and now states that "the legislature may appropriate to the municipal assistance fund during each fiscal year an amount equal to or greater than 30 percent of the income tax revenue received by the state under AS 43.20.011(e) for the previous year."

A resolution requesting funding must be submitted to fulfill application requirements. Population figures used to calculate allocations are supplied by our Department from the State Revenue Sharing program. Those municipalities that operate on a calendar fiscal year receive payments on February 1 with all other municipalities receiving their funding on June 1 of each year.

Grant funds under this program are unrestricted and can be spent for any public purpose. The Title 29 revision passed last year will transfer the administration of the Municipal Assistance program from the Department of Revenue to our Department as of the effective date of January 1, 1986. This transfer of responsibility has already taken place to some degree since we must prepare to make our first payments under the program only one month after the statutory transfer.

Testimony for SB 24⁶
September 24, 1985
Page 10

I hope this has proved to be a concise and useful summary of the programs. If you have any technical questions about how the programs function I will be happy to respond to them.

STATE OF ALASKA
THE LEGISLATURE

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JUNEAU, ALASKA 99811
907-465-3800

May, 1988

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

Mary Van Nimwegen

S CRA 1-23-86 3:35 pm

3-26-85 3:39 pm

(In FBKS) 10-22-85 9:30 AM

(In North Pole) 10-22-85 2:10 pm

(In Anch.) 9-24-85 2:00 pm

(Wasilla) 9-25-85 2:00 pm

(Soldotna) 9-26-85 2:00 pm

MEMORANDUM

Linger
18-221

TO: Frances A. Ulmer, Director
Div. of Policy Development & Planning

DATE: April 11, 1979

FILE NO: J-66-614-79

TELEPHONE NO:

FROM: AVRUM M. GROSS
ATTORNEY GENERAL

SUBJECT: Use of Permanent
Fund income as debt
guarantee, HB 414

By:
Rodger W. Pegues
Assistant Attorney General



You have asked us to review HB 414, and to advise whether the legislature may provide for the use of the income from the Permanent Fund to guarantee bonds, notes, and other indebtedness issued to finance public power projects.

While HB 414 will require substantive amendment, the income from the permanent fund probably can be used for this purpose.

The constitutional amendment establishing the permanent fund provides in pertinent part that "[a]ll income from the permanent fund shall be deposited in the general fund unless otherwise provided by law." Alaska Const., art. IX, § 15. */ The concluding clause: "unless otherwise provided by law" was intended to give the legislature maximum flexibility in using the fund. 1976 H. Jour. 684-685. It may be that the record of proceedings before the several committees which considered the amendment and of proceedings on the floor of the legislature would show its purpose in more detail. Its purpose is not discussed in the ballot summary or voter's pamphlet. Both simply advised the electorate that the income would go into the general fund and be available for appropriation unless otherwise provided by law. The title of the joint resolution by which the legislature proposed the amendment makes no reference to the disposition of the Permanent Fund's income. Disposing of it so as to establish still another dedicated fund probably encompasses a whole new and different subject from establishing the

*/ The clause, "unless otherwise provided by law" was added to the proposed constitutional amendment by a House Judiciary Committee Substitute. Compare SSHJR 39, 1/15/76, with CSSS HJR 39, 3/24/76. It was dropped by SCS CSSS HJR 39, 4/7/76 (which would have authorized additional dedications), and restored by SCS CSSS HJR 39 (Res), 5/21/76. It remained in SCS CSSS HJR 39 (Res) am S, 5/21/76, the final version.

Frances A. Ulmer
April 11, 1979
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Alaska Permanent Fund. As a general rule, separate subjects must be treated separately in adopting constitutional amendments, and each must be summarized for the voters. Our conclusion is, therefore, that the clause does not exempt the fund's income from the prohibition against dedicated funds.

We turn to the question of whether the clause permits the legislature to provide for the Permanent Fund's income to be pledged as a guarantee for financing public power projects. While we doubt that the clause exempts the fund's income from the prohibition against dedications for a special purpose, we believe that neither repaying debts nor guaranteeing their repayment comes within the constitution's prohibition against dedicated funds and that, therefore, the income can be used as a security to repay or guarantee the repayment of a debt for a given capital improvement. */

The next question is whether an appropriation is required to make payments on the debt as may become necessary.

The relevant provisions of the constitution provide as follows:

No money shall be withdrawn from the treasury except in accordance with appropriations made by law.

Alaska Const., art. IX, § 13. **/

It appears that an appropriation would be necessary either to make the guaranty at the outset or subsequently to make payments. A guaranty is a promise that payment will be made in accordance with its terms. ~~Aside from those cases where~~

*/ This conclusion is based on a reading of the Minutes of the Constitutional Convention and the files of the Convention's Committee on Finance and Taxation. The wording, "proceeds of any tax or license," in article IX, section 7, of the constitution was intended to allow exemptions for pension fund payments, bond proceeds, sinking fund receipts, and the like. 1975 Op. Atty. Gen. No. 9, 6-9.

**/ A related provision, article II, § 13, requires appropriations to be made in bills that are confined to appropriations.

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April 11, 1979
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the promise is unconditional. However, any promise to pay made by the state is necessarily conditioned on the appropriation of the monies to be paid. Id. In order to meet this constitutionally imposed condition, an appropriation is necessary. It can be made at the outset as a conditional appropriation, e.g., "\$x million is appropriated annually to pay the guaranty on the condition that it becomes due." It can be made, as is done for general obligation bonds, as the payments become due, i.e., in the case of a guaranty, an annual, conditional appropriation.

While there is authority that no money can be paid from the treasury even on a judgment, United States v. Commonwealth, 288 S.W.2d 664 (Ky. 1956), the better view is that the provisions of a state constitution requiring an appropriation to be made by law must give way under the combined effect of the federal constitution's contracts and supremacy clauses. */ Cf., Virginia v. West Virginia, 246 U.S. 565 (1918). A guaranty is a contract and cannot be impaired. The legislature's refusal to honor it would constitute its impairment. A court would render judgment for the debtor and levy on the fund's income to enforce the judgment. Therefore, no appropriation would be required in order to enforce payment. Nevertheless, to avoid the necessity for obtaining a judgment, an appropriation should be made.

It appears that the concluding clause of the 1976 amendment authorizes the legislature to make an appropriation from the income on a continuing basis for the purpose of paying or guaranteeing payment of a debt for a public power project, i.e., provide in a single Act for a given sum of monies to be expended annually from the income of the fund. Thus, a conditional appropriation could be made at the time the guaranty is made, and no further appropriations would be required. With respect to a guaranty, our best guess is that a continuing appropriation would probably be upheld. The guaranty would probably include a promise not to repeal the appropriation so long as the guaranteed debt remains outstanding. Any repeal would then be invalidated by a court.

*/ U.S. Const., art. VI, cl. 2; Amend. V, XIV, § 1.

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April 11, 1979
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The next question is whether the guaranty must be made by law and approved by the voters. Because the guaranty would be a contract for a conditional debt which could result in the state's being, in effect, in debt to the creditor, it appears that the approval of the electorate would be required to make the guaranty. Article IX, section 7, of the Alaska Constitution prohibits contracting debt unless it is for a capital improvement and is ratified by the electorate. The court places a great premium on this ratification. Thomas v. Rosen, 522 P.2d 1120 (Alaska 1974). The constitutional exceptions from the requirement of ratification do not expressly apply to a guaranty. Alaska Const., art. IX, § 11. Our best guess is that the requirement, therefore, applies to guaranties and that any proposed guaranty would have to be presented to the voters as a ballot proposition. It would almost certainly, therefore, require as well that, as with a bond issue, the guaranty be authorized by law in the first instance and then submitted to the voters. Enactment of a law is what the language of the 1976 amendment requires on its face.

We do not believe that a one-time-only ratification by the voters of an Act generally authorizing the Permanent Fund's managers to guarantee debts for public power projects would satisfy the constitutional requirement for contracting debt. However, it might aid the court in deciding that those requirements do not apply to a guaranty which is based solely on the Permanent Fund's income. There is a line of cases which hold that debt restrictions similar to those contained in article IX, section 8, of the Alaska Constitution apply solely to debts which the state's full faith and credit is pledged to pay. The likelihood that the rationale of these cases would be applied by the Alaska Supreme Court to a guaranty based solely on the income from the Permanent Fund could possibly be increased by the voter's having ratified the concept. Nothing prevents the legislature from making the statutory authorization for guaranties contingent on voter approval. Accordingly, while we do not believe it will be valid, a general authorization for the Permanent Fund managers to make guaranties could be enacted and then tested in court.

Finally, the constitution provides that the "public credit [cannot] be used except for a public purpose." Alaska Const., art. IX, § 6. We believe that only the most

Frances A. Ulmer
April 11, 1979
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irrational of power projects would be barred under this provision. E.g., Wright v. City of Palmer, 468 P.2d 326 (Alaska 1970). We assume that the projects would be public works. Whether the income from the Permanent Fund could be used to guarantee financing for private works is an entirely different question which involves entirely different issues.

RWP/pjg

cc: Jerry Reinwand
Office of the Governor

Ron Lind
Div of Budget & Management

Keith Specking
Office of the Governor

bcc: Tom Singer
Div of Policy Development
& Planning

STATE OF ALASKA

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

0 1
JAY S. HAMMOND, GOVERNOR

Per

POUCH K - STATE CAPITOL
JUNEAU 99511

January 3, 1976

M E M O R A N D U M

TO: The Honorable Jay S. Hammond
Governor

FROM: Avrum M. Gross *by LAW*
Attorney General

RE: Proposed joint resolution calling for a
constitutional amendment establishing a
permanent fund.

Attached is the proposed joint resolution calling for a constitutional amendment to establish a permanent fund to which mineral leasing revenues would be dedicated.

In contrast to HJR 39 which you introduced last year, the attached resolution would establish a constitutional permanent fund into which 10 percent of all mineral leasing revenue and mineral production taxes would automatically be dedicated without further legislative action. Last year's resolution would simply have given the legislature the authority to establish a permanent fund by law which could be changed or repealed by subsequent legislatures.

The revenues that would be dedicated include mineral leasing rentals, royalties and bonuses. Questions do arise, however, as to some special circumstances. For example, what is to occur when the state takes its royalty in kind? Should 10 percent of the proceeds from the sale of royalties taken in kind be dedicated to the fund? I have assumed that this would be the case and have included language in the draft transmittal letter to clarify our intent in this respect.

Also, what is to occur if the state changes its leasing policy from the traditional bonus bidding with a 1/8 or 1/6 royalty to a royalty bidding arrangement with a nominal cash bonus with the state instead receiving a larger royalty share such as 50 percent? Again I have assumed that you have intended that a full 10% of this larger royalty

The Honorable Jay S. Hammond
Governor

January 3, 1976

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share would be dedicated to the fund, and I have included language in the transmittal letter to state your position on this.

Also, what is to occur with respect to the revenue sharing which the state receives from federal mineral leasing? If this revenue is to be included, we should add some appropriate language in the resolution and in the transmittal letter to accomplish it.

Other revenue that would be dedicated to the fund would include mineral production taxes. I have assumed that this would only include the state's oil and gas properties production tax ("severance tax"), the oil and gas conservation tax (conservation tax), and the mining license tax regardless what form they may take in the future. Taxes that have not been included are the oil and gas exploration, production and pipeline property tax (20-mil property tax) and the oil and gas reserves ad valorem tax (reserve tax). If it is intended that these taxes should also be dedicated then the resolution and draft transmittal letter should be changed accordingly.

A question can be raised as to what amount of tax should be dedicated. For example, what is to occur with respect to any production taxes which the state must transmit to the Native Fund? Should 10 percent of taxes which the state receives and then transmits to the Native Fund be dedicated? I have assumed not and have so stated in the draft transmittal letter.

Also, what is to occur with respect to the production taxes which the state does not receive in cash but in effect receives through the application of accumulated "reserve tax" credits? For example, a taxpayer having a production tax liability of \$100,000 may credit his accumulated reserve tax against the production tax up to \$50,000 and only pay the remaining amount. Again, I have assumed that the production tax paid by the reserve tax credit would not be dedicated. If it is intended that more than just the net amount of cash tax revenue received by the state should be dedicated, then some additional changes should be made to the transmittal letter.

The resolution specifies that the fund will be used for investment only, with the legislature specifying the types of investment. A question has arisen whether the

The Honorable Jay S. Hammond
Governor

January 3, 1975

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fund should be used to purchase obligations financing capital expenditures. For example, may the fund be used to purchase bonds issued to finance relocation of the capital? I have assumed this was not intended and have so stated in the transmittal letter.

If you wish to acknowledge, or go to the extent of withdrawing, the currently pending HJR 39, you may wish to add a comment on it in the transmittal letter to the legislature.

AMG:md:JRM