

A Promise to Keep:
The Alaska Public School Trust Fund

A History of the Fund - 1985-2004

A Research Paper

by

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Preface

My interest in Alaska's School Land Trust began in 1983–84 when I compiled the earliest, and perhaps only, history of it, covering the period from 1915 to 1984. Support for this effort came from a modest research grant, mostly for travel to Juneau, made by the College of Human and Rural Development at UAF, where I was a faculty member. The research paper was titled: The Alaska Public School Fund: A Permanent Fund for Education.

Prior to and for some time after my retirement from UAF in 1985 efforts were made to circulate the findings and seek support for the premise that the trust fund should be used as a permanent, or endowment fund, for public elementary and secondary education. These efforts were unsuccessful. Creating a permanent fund for education from a very small trust fund at a time when Alaska's economy was entering the late 1980's downturn was not a priority for educators or legislators.

After retiring from UAF I continued to monitor the school land trust. A small personal oversight task one might say. State reports on the trust were reviewed annually and phone and letter inquiries made to the agencies managing the land and the trust. Some typical questions:

Why isn't the fund being audited regularly? Are the required meetings of the advisory committee being held, and may I have the minutes of the last meeting? Why aren't all trust fund investment earnings distributed to the schools? What has the new 75,000 acres of school land earned and are all receipts from this land being put into the school trust fund?

My continued research and inquiries revealed the state agencies did not always follow the law and regulations governing the trust fund and the new federal land grant. At the same time, the growing trust principal drew the attention of a few state officials, who contemplated ending the deposit of receipts into the fund.

With the addition of school trust issues to *Kasayulie v. State of Alaska* in 1998, all the State's actions in this matter would be examined. Especially the first and most egregious, the redesignation of school lands to be general grant lands. Since then the Court has found the State breached the trust, and has proposed a plan of resolution.

I hope this 20-year review will be useful to those managing the new school land and the trust, to those at work resolving the current issues, and to citizens, educators, and legislators interested in the possibilities of the trust fund having a major role in financing Alaska's public schools.

E. Dean Coon
Anchorage, Alaska
January 2005

Author's Notes and Other Disclaimers

The content of this paper is drawn largely from a variety of reports available from Alaska's state agencies and legislative offices. Most financial information came from the Consolidated Annual Financial Report. When this lacked the necessary detail, agency budgets and legislative finance division reports were consulted. *Kasayulie v State of Alaska* documents were a major source of information. Other references came from my personal files, and were the result of monitoring the state's management of the school land and the school trust.

Almost all of the referenced records and reports of the Department of Revenue, the Department of Natural Resources, the Department of Administration, and the Legislative Finance Division were accessed online. The ability to obtain data in this manner was a great aid in preparation of this paper.

Every effort has been made to present accurate and up-to-date facts and data. If there have been failures to achieve this, the responsibility is mine.

CPA's and other professional accountants may discover inconsistencies in various references to money and funds. For example, in most instances this paper refers to money earned on trust fund investments as Investment Earnings, rather than Income Assets, its true name.

Some Frequently Used Acronyms:

DNR: Department of Natural Resources
CAFR: Consolidated Annual Financial Report
AS: Alaska Statutes
SLA: Session Laws of Alaska

A 7-page abstract of this paper is available from the author.

I wish to thank the Alaska PTA for its interest in the future of the Public School Trust Fund and for posting this paper on its web site.

Comments or questions? Let me know.

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Introduction

Purpose

The purpose of this paper is to examine the circumstances and events affecting the Alaska Public School Trust Fund and the School Grant Lands in the 1985–2004 period, and to present recommendations regarding the future of the Fund.

The 1916–1984 period is described in *The Alaska Public School Fund: A Permanent Fund for Education*, a paper issued in 1984 by the author. An abstract of this earlier paper follows.

Organization

The paper is organized in four sections, as follows:

The Land. Topics include the status of the land in 1978 when it was redesignated as general grant lands, uses of some of the redesignated school land, and the acquisition of additional school land from a new federal grant and through recovery of original grant land.

The Fund. Topics include general grant land receipts deposited in the Fund, the growth and size of the principal of the Fund, investment earnings, Fund management policies, and use of Fund investment earnings.

The Litigation. The school trust issues in *Kasayulie v. State of Alaska*, filed in 1997, are reviewed. The plaintiffs and their complaints are described. The opinions and rulings of the Superior Court, which found that the State breached the Trust, are presented. This section concludes with a list of unresolved issues to be addressed by the Court following an appraisal of the school lands (1978 valuation).

The Future. The Fund is presented as a legacy in peril, but a Fund that if properly protected and enhanced could serve as an endowment or permanent fund for public education. Eight recommendations for saving and strengthening the Fund are presented.

An Appendix contains the Trust Fund statutes, the author's resume, and a statutory amendment to increase the state contribution to the Trust Fund.

Abstract

The Alaska Public School Fund: A Permanent Fund for Education

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March 1984

The 40-page paper describes the development of Alaska's Public School Fund, its current status, and its potential as a major source of endowment revenue for elementary and secondary education.

Territorial Period: 1915-1958

The Public School Fund, initially called the Public School Permanent Fund, was created in accordance with an Act of Congress, March 4, 1915. It reserved sections 16 and 36 in each surveyed township for the benefit of public schools in the Territory of Alaska. Receipts from leases and minerals were to go into a permanent fund, which was to be invested, with the investment income to be expended only for the exclusive benefit of the public schools. The Fund was established in 1916, and by 1958 it had a balance of \$161,700. Investment income was being credited to the Public School Current Fund and then disbursed for support of the schools. The school land grant program, displayed in a schematic in Figure 1, was operating as stipulated by the 1915 Act.

Early Statehood Period: 1959-1978

On January 5, 1959, Alaska became a state, and the federal school lands, some 105,000 acres, became state school lands. Management of these lands was under the jurisdiction of the newly created Division of Lands in the Department of Natural Resources. The first sale of school land occurred in 1959. The Fund's investment earnings were posted to the state's General Fund. The contention was that since the investment earnings were less than the General Fund appropriation for support of schools then the intent of the law was met.

The School Permanent Fund grew more rapidly during the next 20 years, and by 1978 showed a balance of \$8.5 million. Investment income in Fiscal Year '78 exceeded \$560,000. A schematic of the Fund in the Early Statehood Period is shown in Figure 2.

During this period legislative audits revealed illegally executed land leases and that some land rental income was not credited to the Fund. Over \$2 million was credited to the Fund in settlement of two of the cases. As a result of these happenings, the State Board of Education was named trustee of the school lands and was charged with approving every land transaction.

Because of these problems, and because of public and legislative pressure to make more state land available for sale to the public and for use by state and local agencies, major changes in the management of the lands and the Fund were made by the Legislature in 1978. The school lands, some 103,000 acres (2,300 acres had been sold), were redesignated as general grant lands and put

with other general grant lands to be managed by the Department of Natural Resources. A new source of receipts designated for the Public School Fund was to be one-half of one percent of the total receipts derived from the management of all state lands. A Public School Fund Advisory Board was established; it was to approve all Fund investments.

Contemporary Period: 1979–1983

Due to the legislative changes, the state school land "disappeared" into the pool of state general grant land; there was no legal challenge. The new and larger base of land, some 105 million acres, would be the source of receipts for the Fund, now designated the Public School Fund. A schematic of the Fund as it now exists is shown in Figure 3.

With a new source of receipts beginning in FY '79, the Fund balance increased rapidly. The major reason was that receipts from state lands included state oil production royalties, as well as other related sources not available under the old scheme. As a result, Fund receipts averaged \$7 million per year and on June 30, 1983 the Fund balance exceeded \$41 million. Investments in U.S. government securities and in certificates of deposit were providing earnings in excess of \$3.5 million annually although these earnings were still being credited to the state's General Fund. The rate of return on investments in FY '83 was 11.68 percent, down from the all-time high of 13.11 percent in FY '82.

The Public School Fund Advisory Board, although stipulated by legislation in 1978, was not organized until November 1983. The Advisory Board membership consists of the Commissioner of the Department of Revenue, the Commissioner of the Department of Education, and three members of the State Board of Education.

In 1980 Congress granted Alaska an additional 75,000 acres of school land. This grant was in consideration of school lands not transferred earlier to the Territory because designated sections were withdrawn, reserved or otherwise appropriated. This land must be selected by January 4, 1994.

A Permanent Fund for Education

Through Constitutional Amendment in 1976, Alaska voters established the Alaska Permanent Fund and stipulated that 25 percent of the state's oil, gas, and mineral income be credited to it each year; additional deposits are at the option of the legislature. The purpose was to put aside current surplus revenues in an endowment fund that will help sustain basic state services in the future when mineral and oil royalties are expected to decline substantially. Numerous suggestions have been made to establish a similar endowment fund for public elementary and secondary education.

Oil, gas, and mineral income now provide about 80 percent of the state's General Fund, which is the primary source of revenue for support of public schools. State appropriated funds for school support have been increasing 20 percent per year for the past seven years and amounted to more than \$535 million in FY '83. Clearly an alternative source of revenue for public school support is needed in the future.

The Public School Fund could be an alternative source of revenue for state or local school support – a source of some magnitude if the percent of land

management receipts credited to the Fund would be increased substantially. One option would be to credit the Fund with ten percent of land management receipts (instead of one-half of one percent which is the current rate). Even though land management receipts are expected to decline in the next few years, this change would give the Fund a balance estimated at \$1.1 billion by 1991. Investment of this principal would result in revenues in excess of \$100 million in 1991. A greater return would result if deposits into the Fund were more than 10 percent and if a top rate of return on investments was obtained.

Creation of such an endowment would make the Public School Fund an Alaska Permanent Fund for Education, and would demonstrate commitment to stable school support in the future when current major state revenue sources are expected to be less than today.

Recommendations

Recommendations based on this paper include:

1. Increase the amount of land management receipts credited to the Fund
2. Manage the Fund to achieve the maximum rate of return on investments
3. Credit investment income of the Fund to a designated public school support account
4. Conduct more frequent outside audits of the Fund
5. Select and manage the 75,000 acres of school land granted additionally in 1980 in a manner that will provide maximum income to the Fund, and
6. Conduct further definitive studies to enable Alaska to capitalize on the Fund and on the new grant of school land.

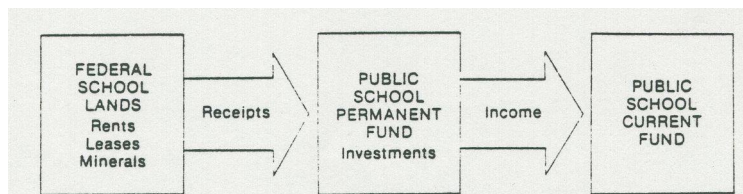


Fig. 1. Public School Permanent Fund Model: Territorial Period

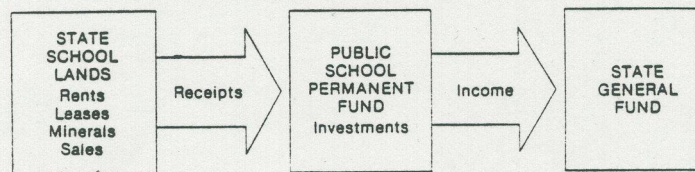


Fig. 2. Public School Permanent Fund Model: Early Statehood Period

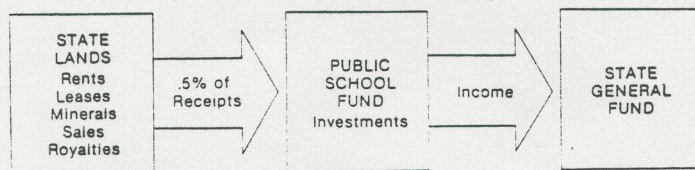


Fig. 3. Public School Fund Model: Contemporary Period

The Land

School Land Status 1959–1984

Although the content of this paper is focused on events in the 1985–2004 period, it will be instructive to take a brief look at this earlier period, and also to review the original land selection figures.

Following Statehood, Alaska selected more than 103,000 acres of federal land as authorized by Congress. On June 30, 1978, there were 101,620 acres of school grant land in Alaska; 2,320 acres had been sold.

The land consisted of part or all of eligible acreages in Sections 16 and 36 in more than 250 townships surveyed prior to Statehood. Figure 4 below shows the size and layout of townships and sections.

Figure 4
Township and Sections

6	5	4	3	2	1
7	8	9	10	11	12
18	17	16	15	14	13
19	20	21	22	23	24
30	29	28	27	26	25
31	32	33	34	35	36

Townships are 6 miles tall and 6 miles wide and are divided into 36 sections. Each section is one mile tall and one mile wide. The sections are numbered starting in the northeast corner and ending in the southwest corner. Each section contains 640 acres.

Table 1 below shows (1) the number of sections 16 and 36 at Statehood, (2) the number of those sections from which acreages could be selected, and (3) the number of acres ultimately patented. Table 1 does not show land obtained and then disposed of through sale or trade or lost for other reasons prior to 1978.

The school lands are conveyed to the State by statute, but are shown in Department of Natural Resources documents as "patented." A patent is the instrument by which the United States Government conveys, or grants, the fee-simple title to public land to another.

Table 1
Alaska School Land Grant Status
June 30, 1978

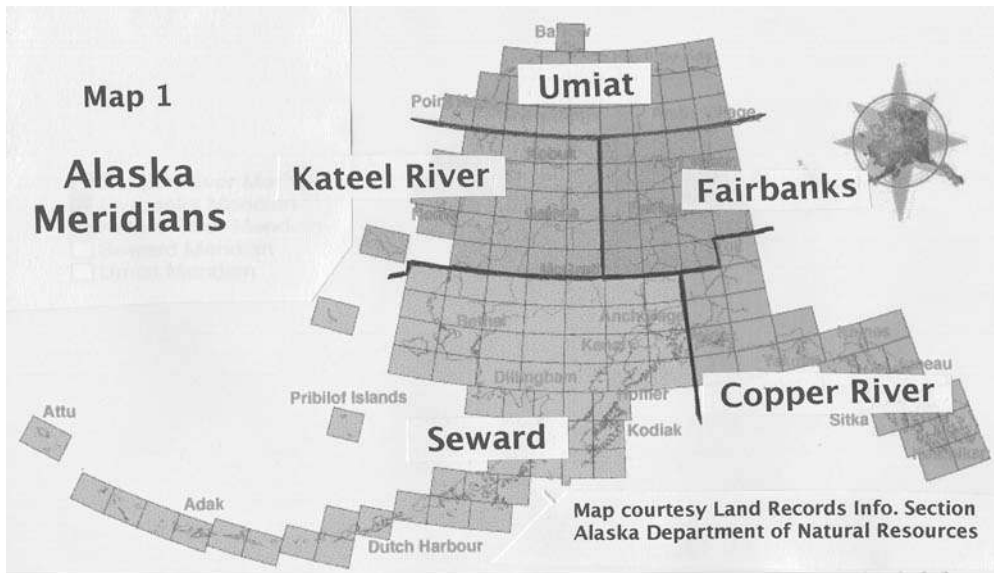
Meridian	Surveyed Sections 16 & 36	Sections Open for Selection	Acres Patented
Seward	287	105	52,714
Fairbanks	113	69	39,045
Copper River	108	22	9,861
Totals	508	196	101,620

Sources: (1) School Grant Audit, Department of Natural Resources, 11/17/98
(2) Acres of Land Involved in School Trust Appraisal Project, DNR, Jan. 12, 1999

See Map 1, Alaska Meridians, which follows, showing boundaries of Alaska's five meridians.

Sections open for selection are fewer than total sections because of federal withdrawals for a variety of reasons. For example, a substantial portion of the land in the Copper River Meridian was not available as it was in the Tongass National Forest, which was established in 1907. See Map 1 which follows for a map of meridians in Alaska.

It is interesting to contemplate a "What If?" at this point. What if Alaska had received as school land the entire acreages of sections 16 and 36, which was the intent of the 1915 Federal law? The computation: 508 sections times 640 acres per section equals 325,120 acres. More than three times as much school grant land would have been obtained!



No school land was patented in Umiat and Kateel River Meridians.

Zero Acres of School Land in July 1978

On July 1, 1978 Alaska had no school trust lands, due the legislative redesignation of the land as general grant land. Alaska did have 101,620 acres of *former school trust land* that was now part of the corpus of the State's general grant lands. The restrictions and requirements under which the school land had been managed were no longer in force. Instead, the use, sale, or transfer of this land would be the same as for all other general grant lands. Its identity as former school trust land, however, would not be lost in the land management records of the Department of Natural Resources.

Status of Redesignated School Lands

There was heightened interest in the school lands once they had been redesignated as general grant lands. The land would be managed by the Department of Natural Resources under generally the same rules and regulations as for the general grant lands. The former school land now would be sold, leased, or traded without meeting former obligations, such as crediting land receipts to the school trust fund.

The new status of the former school land achieved one of the purposes of the legislative redesignation. That purpose was to make available additional land for public and private use and ownership. The surveyed (at statehood) townships containing school sections 16 and 36 were mostly located in or near existing population centers. That in itself made much of the land desirable. (Location, location, location!)

The cities and boroughs, through the State's municipal entitlement program, could now obtain ownership of these former school lands. These lands could easily be included in regularly scheduled DNR land sales. State agencies generally could now obtain this land at no cost.

The State itself took advantage of the school land's new status by trading almost 15 percent of it for land owned by a Native corporation, Cook Inlet Region, Inc. (CIRI), and several villages in the Cook Inlet Region.

Former school land acquired by CIRI totaled 14,714 acres located in 45 sections in the Seward Meridian, according to the School Land Audit, DNR, 11/17/98 and current DNR Land Administration Records. Although most was on the Kenai Peninsula, acreages were located in other areas, including Point McKenzie, Knik-Willow, Kashwitna, and Chickaloon. During 1979 and 1980, the State transferred title in these redesignated school lands back to the Bureau of Land Management (BLM). BLM then patented the land to regional and village corporations in the Cook Inlet Region. An interesting consequence of this procedure: CIRI could be shielded from legal action should litigation seek to reclaim the school land and reconstitute the trust lands.

This was a tiny part of a much larger land exchange involving the State, CIRI, and BLM. The exchange was intended to help resolve land issues arising out of implementing the Alaska Native Claims Settlement Act (ANCSA). The nature of the exchange and its magnitude made it impossible for the author to specify the locations and amount of land the State got in return. (Persons interested in a description of this land exchange are referred to U.S. House of Representatives Report 104-643 - *Conveyances of Lands to Certain Native Villages under ANCSA*).

As indicated earlier, municipalities were now eligible to obtain former school land within their borders. One example of this was Anchorage's selection of Section 36 in Township 12N, Range 3W. This is located in Southeast Anchorage, between Bear and Rabbit Creek Valleys. Many public and private uses were considered, according to Municipality of Anchorage's *Section 36 Land Use Study*, March 1991, p. 2-3. Later the land was returned to the jurisdiction of the Parks and Recreation Department. Then in 2000, an Anchorage Daily News story headlined "Ridge park in sight," December 28, page 1, reported, in part:

The city is poised to make Section 36 into parkland. The move would culminate more than a decade's struggle between local residents, conservationists, and city government. What once was intended for high-end housing may end up as a source of recreation and wildlife habitat.

And that is what happened (early in 2003). A 640-acre park is now being developed – made possible only because of the school land grant program. Similar acquisitions can be found in other communities.

Alaska had no school trust land in 1984, but that would change. New land would be obtained in two ways. The first would be to recover land the State was eligible for in 1959 but which could not be selected due to various withdrawals by the Federal government. The second way would be from a new land grant by the Federal government.

Additional Original Grant Land Recovered

During the 1980's, audits by the Department of Natural Resources revealed that some of the 1959 school land withdrawals by the Federal government had been reversed. Audit results were reported by Carol Shobe, Chief of the Realty Services Section, Division of Land, DNR (Affidavit of Carol Shobe, *Kasayulie v. State of Alaska*, Nov. 16, 1998). Excerpts from this Affidavit follow:

This audit determined which lands had not been conveyed to the State at statehood due to pre-statehood federal withdrawals that had been subsequently removed. BLM indicated that it would convey such lands to the state . . . As a result of the audit . . . the state obtained an additional 2,850.18 acres of school trust land after the enactment of ANILCA in 1980 . . . These lands are in addition to those land conveyed under 906(b) of ANILCA.

According to the *School Land Trust Appraisal Project*, a Department of Natural Resources report issued early in 1999, the 2,850 acres of recovered lands were in seven tracts. Four were in the Seward Meridian, one was in the Fairbanks Meridian, and two were in the Copper River Meridian. Patents for this land were obtained in the period between October 8, 1985 and February 3, 1992.

A Territorial Grant for school purposes made in 1957 was also reclaimed, according to the DNR report previously cited. This 640-acre tract, Sec. 16, Township 4 South, Range 15 West, Seward Meridian, was patented December 30, 1991. (The original school lands corpus includes three other Territorial Grants also patented before Statehood.)

This reclaimed land has not been redesignated by the legislature as general grant land. It is managed by the Department of Natural Resources, and should retain its status as school land, with 100 percent of receipts from its use credited to the Public School Trust Fund.

A New School Land Grant

The Alaska National Interest Lands Conservation Act (ANILCA), P.L. 96-487, Dec. 2, 1980, 94 Stat. 2371, specified that Alaska was to receive an additional 75,000 acres of school land. The provision for the new land grant was in Section 906, which read in part:

(b) SCHOOL LANDS SETTLEMENT.-- (1) In full and final settlement of any and all claims by the State of Alaska arising under the Act of March 4, 1915 (38 Stat. 1214), as confirmed and transferred in §6(k) of the Alaska Statehood Act, the State is hereby granted seventy-five thousand acres which it shall be entitled to select until January 4, 1994, from vacant, unappropriated, and unreserved public lands. In exercising the selection rights granted herein, the State shall be deemed to have relinquished all claims to any right, title, or interest to any school lands which failed to vest under the above statutes at the time Alaska became a State (January 3, 1959), including lands unsurveyed on that date or surveyed lands which were within Federal reservations or withdrawals on that date.

(3) Lands selected and conveyed to the State under this subsection shall be subject to the provisions of subsections (1) and (k) of §6 of the Alaska Statehood Act.

Why did Alaska receive this additional school land? It is because it was unable to select and patent all the land to which it was entitled in 1959. That is, part or all of many Sections 16 and 36 could not be conveyed to the State due to pre-statehood federal withdrawals. Some reasons for the withdrawals included territorial homestead entries, inclusion in a national forest, territorial grants, federal public land orders including mining claims, and conveyances for territorial use. One report indicates that of some 181,000 acres eligible for selection as school land, only 104,000 acres was ultimately patented (School Grant Audit, Department of Natural Resources, Revised Updated, November 17, 1998).

By 1986 the Alaska Department of Natural Resources (DNR) had not yet selected any of this new school land. According to DNR the delay was necessary to clear up conflicts in conveyances on related land transfers, and because of an ongoing audit of sections 16 and 36 to determine if Alaska received all the school trust land to which it was entitled under the 1915 Act of Congress. As previously noted, lifting of pre-statehood federal withdrawals on some trust land allowed Alaska to now claim school sections it was originally denied. Such action had to be taken before selecting Sec. 906(b) lands.

The status of the new school land grant was stated in a DNR letter that year (Letter from Tom Hawkins, Director, Division of Land and Water Management, to E. Dean Coon, December 16, 1986) which stated, in part:

As you are aware, on July 1, 1978, the legislature redesignated all trust land as general grant land, which included approximately 103,000 acres of school land. However, the redesignation does not affect land approved for conveyance after July 1, 1978. Sec. 906(b) of ANILCA states that "lands selected and conveyed to the State under this subsection shall be subject to the provisions of subsection (j) and (k) of Section 6 of the Alaska Statehood Act." These particular subsections of the Statehood Act related to the confirmation of title to the State of Alaska and removed land and monetary management restrictions.

Once the Sec. 906(b) land is selected and title is obtained, this agency will manage the land as general grant land is managed. We will also insure that a trust account is established so that revenues derived from this land will be placed in the public school fund.

The Department of Natural Resources established criteria for selecting the new school land. Resource value of the land would be a major criterion, and was detailed in a DNR document (E. ANILCA School Grant, prepared by Dick Mylius, Manager, Division of Land, Resource Assessment and Development Section, n.d.). An excerpt follows:

Selections should be for land capable of earning revenue for the state. The desire was to limit the number of parcels to four or less to reduce management and survey costs. Because the grant is small, it was desired that all of the selections be conveyable, that is, the grant would not be used to topfile on lands selected by ANCSA corporations, currently withdrawn, or encumbered with federal mining claims.

Very few of the lands available for selection had high enough surface values that could be turned into revenue with certainty, so the steering committee decided to select land with subsurface values or with both surface and subsurface potential for this grant. It was determined that this acreage was too small to use to acquire land in speculative oil and gas areas. Areas with known and accessible sand and gravel were identified by DGGs (Division of Geological and Geophysical Services), but determined not to be available. As a result, the use of this grant focused on land with potential mineral deposits or a mix of mineral and surface values.

The land ultimately selected on May 21, 1993 comprised three large tracts as well as part of one section. Locations of these ANILCA 906(b) lands were identified by DNR (Letter from Jane Angvik, Director, Division

of Land, to E. Dean Coon, April 9, 1997) as follows:

Copper River Meridian: 38,647 acres Southeast of Tonsina, located in Township 3 South, Range 2 East, and T. 4 S., R. 2 E.

Fairbanks Meridian: 17,190 acres North of the Denali Highway in the Clearwater Mountain Range, located in T. 19 S., R. 5 E., and T. 19 S., R. 6 E.

Fairbanks Meridian: 19,027 acres South of Black Rapids Glacier within the Alaska Range, located in T. 18 S., R. 8 E.

Copper River Meridian: 66 acres Southeast of Gustavus Airfield. Section 16, Lot 2, T. 40 S., R. 59 E.

Acres patented: 74,930

The Mylius document, previously cited, estimates acreages in the Fairbanks Meridian have good economic prospects for mineral development, noting they contain “. . . the Zackly gold-copper skarn deposit with estimated reserves of 1.25 million tons of 2.6% copper and greater than 6 grams of gold per ton . . . with a high potential for metamorphic gold veins and moderate potential for placer gold and basalt-related copper deposits . . .”

The new land is managed by the Department of Natural Resources, along with other general grant lands of the state, and is under the same stipulations of the first school land grant. It retains its designation as “school land” and all of the income from its use, such as gravel sales, mineral leases, rent, etc., ultimately should be credited to the School Trust Fund. This land has not been redesignated general grant land by the legislature, and cannot be, per *Kasayulie v. State of Alaska*.

Here is a recap of the existing school grant lands in Alaska.

1. ANILCA Sec. 906(b) grant	74,930
2. Original grant land recovered	2,850
3. Territorial Grant recovered	<u>640</u>
Total	78,420 acres

By 1995 fewer than 85,000 acres of redesignated school land was still a part of the State's general grant land holdings. But this land, the land already sold or traded, the land recovered, and the new grant of land remain the central issue if and when these lands are appraised, a task described later in this paper.

The Fund

The Public School Trust Fund

The Alaska Public School Trust Fund has grown rapidly during the past twenty-five years. Ending balances were as follows:

June 30, 1978	\$ 7,800,000
June 30, 1983	41,079,000
June 30, 1993	126,249,000
June 30, 2003	280,505,000

A New Income Source

When the Legislature redesignated the school land in 1978 it eliminated the lands as a direct source of revenue for the fund. The new revenue source was to be a portion of the receipts derived from the management of all state land. Alaska Statutes, Section 37.14.150 reads in part:

During each fiscal year the commissioner of the Department of Revenue shall transfer to the fund . . . a sum equal to one-half of one percent of the total receipts derived from the management of state land, including amounts paid to the state as proceeds of sale or annual rent of surface rights, mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue-sharing payments or bonuses.

Specific land management receipt sources are as follows:

- | | |
|------------------------------|------------------------------|
| 1. Oil/Gas Lease Royalties | 9. Mineral Leases |
| 2. Mineral Royalties | 10. Sale of Land |
| 3. Mineral Rentals | 11. Sale of Timber |
| 4. Coal Rental/Leases | 12. Bonus-Mineral Leases |
| 5. Coal Royalties | 13. Tideland Leases |
| 6. Sale of Gravel | 14. Oil Production Royalties |
| 7. Offshore Prospecting Fees | 15. Gas Property Royalties |
| 8. Land Leases/Rentals | |

The Fund also receives its percentage of receipts from fines and forfeitures associated with any of these sources, as well as from the National Petroleum Reserve special revenue fund (AS 37.05.530)

The receipts from this new source are several times larger than amounts received from school grant lands. Table 2, Capital Gains/(Losses) and Ending Balances, which follows, shows the rapid growth of the school trust fund for the past twenty years.

Table 2
Capital Gains/(Losses) and Ending Balances
Alaska Public School Trust Fund
1985 - 2004
(in 000's)

Fiscal Year	Capital Gains/ (Losses)*	Ending Balance**
'85		79,812
'86		77,583
'87		80,835
'88		86,136
'89		89,569
'90		96,282
'91		106,047
'92		120,924
'93		126,249
'94		128,904
'95		142,219
'96		151,997
'97	58,244	211,536
'98	34,590	249,373
'99	19,300	273,000
'00	5,825	288,391
'01	(12,731)	286,086
'02	(20,454)	269,374
'03	7,285	280,505
'04	13,875	299,152

* Fiscal Year '97 was the first year assets were recorded at fair (market) value, not book (cost).

** Ending Balance: Book (cost) value through FY '96 on the last day of the fiscal year; after that market value.

Ending Balance Computation: Land Receipts PLUS Investment Earnings MINUS Distributions (and including adjustments and transfers) PLUS Capital Gains/(Losses) EQUALS Ending Balance.

Sources: *Investment Policies & Procedures*, State of Alaska, Department of Revenue, Treasury Division, Version 2.0, March 15, 2004, Sec. XII, Page C-4 (through '03); *CAFR* for '04.

The DNR land receipts credited to the principal vary greatly from year to year. This is partly due to fluctuations in the price of oil, as oil production royalties comprise a large share of the receipts. A court ruling favorable to the state resulting in a forfeiture of funds can result in an increase in receipts for that year.

Investment Income

In addition to its share of the receipts from the state's general grant lands, the Public School Trust Fund has a second source of revenue. That source is income from investments. Alaska Statutes Sec. 37.14.140, 37.14.170, and 37.14.110 state in part:

The principal of the fund . . . shall be retained in the fund for investment . . . (and) . . . the income of the fund may not be appropriated for a purpose other than for the support of public school programs

The commissioner of revenue . . . may invest the principal of the fund . . . in the same manner as specified for the investment of surplus pension funds.

The income of the fund . . . consists of the interest and dividends earned from investments of the principal of that fund . . .

Earnings from investments are temporarily credited to the Trust Fund but then are transferred to its Income Assets account. The money in Income Assets is also invested until being distributed for support of the public schools (and other related purposes).

Table 3, Land Receipts and Investment Earnings, which follows, shows the income amounts credited to the Alaska Public School Trust Fund for the past 25 years.

The amount of investment earnings has not steadily increased each year, but fluctuates. This is partly due to changes in the amounts paid in dividends by the companies in which the fund owns stock. The size of the investment earnings not only depends upon the rate of interest being earned on securities and the dividends being earned on stock, but on the management of the invested funds.

With this in mind, an examination of fund management policies is in order.

Table 3
Land Receipts and Investment Earnings
Alaska Public School Trust Fund
FY '79 – FY '04
(in 000's)

Fiscal Year	Land Receipts* Credited to Principal	Investment Earnings** (interest/dividends) of Principal
'79	1,308	695
'80	7,142	629
'81	7,470	1,752
'82	7,994	3,153
'83	9,450	-
'84	9,217	15,626***
'85	7,121	6,769
'86	6,578	8,029
'87	3,262	10,112
'88	6,470	6,358
'89	4,333	8,091
'90	5,208	8,694
'91	8,331	8,412
'92	6,637	15,998
'93	5,748	7,971
'94	3,987	7,201
'95	8,764	11,488
'96	6,150	9,101
'97	5,482	7,730
'98	4,026	8,497
'99	2,608	8,997
'00	5,921	11,895
'01	5,788	13,157
'02	4,328	11,325
'03	6,224	10,235
'04	7,136	10,275
Totals:	156,683	212,190

* Land Receipts includes one-half of one percent of rents, royalties, fines, and forfeitures from State grant lands.

** This is statutory net income and excludes unrealized and realized capital gains/(losses). These moneys are regularly transferred to an Income Assets account (FU 34012) for distribution.

*** Includes prior years' corrections: dividends were incorrectly recorded in the General Fund. (Author's note: This coincides with the upcoming capital projects distribution which began in FY '86.)

Sources: *Investment Policies and Procedures*, State of Alaska, Department of Revenue, Treasury Division, Version 2.0. Sec. XII: C-4 Released March 15, 2004, and *CAFR* for FY '04.

Fund Management Policies

Management responsibility and investment objectives for the Public School Trust Fund are in state law. Alaska Statutes 37.14.170 reads as follows:

Investments. The commissioner of revenue is the fiduciary of the trust fund and shall invest the fund to provide increasing net income over long-term periods to the fund's income beneficiaries. The commissioner may invest the money in the fund on the basis of probable total rate of return to promote the long-term generation of income. In managing the trust fund, the commissioner shall:

- (1) consider the status of the fund's capital and the income generated on a current and a probable future basis;
- (2) determine the appropriate investment objectives;
- (3) establish investment policies to achieve the objectives; and
- (4) act only in regard to the financial interests of the fund's beneficiaries.

Over the years the Department of Revenue has created increasingly detailed policies and procedures to meet this statutory responsibility. Some of the changes in policy were made in response to the increased size of the principal of the fund.

It will be instructive to examine several of the policy documents developed during the past 20 years. The first one below is particularly revealing as it includes then current institutional opinions regarding the nature and future of the fund.

The following is from *Policies and Procedures Applicable to the Treasury Division*, Department of Revenue, State of Alaska, 1990, Appendix ZB, Pages 20-24:

Public School (Endowment) Trust Fund. The Public School Trust Fund is an endowment trust fund, separately accounted and invested.

1. Nature

The principal of endowment trust funds, including all subsequent principal contributions and principal gains, is retained in perpetuity in the funds, but the earned income is used for the purposes for which the trusts were established. The total retention of principal is a firmly established requirement of fiduciary law aimed at assuring perpetual income benefits by preventing diminution of the corpus of the trust.

The perpetual nature of the Public School Trust Fund and the dedication of its income to public education programs is essentially a requirement of federal law. The Alaska Constitution provides for exceptions to a Constitutional prohibition against dedicated funds (Section 7, Article IX) when required by the federal government or for dedications existing at

the time of the Constitution's ratification. Both of these exceptions apply to the Public School Trust Fund to a degree.

Additional principal contributions to the Public School Trust Fund are made from State mineral revenues as compensation for land grant properties expropriated by the State. The total amount of compensation has not as yet been determined, but it will be a limited amount and at some future date additional contributions will cease. Income earned on the principal of the fund is set aside in income subaccounts and reinvested pending appropriation by the legislature and subsequent expenditure. In conformance with fiduciary principles, the distinction between principal and income is strictly maintained through accrual accounting with amortization of bond premiums and discounts on a constant yield-to-maturity basis in order to prevent unwarranted conversions of principal to income or income to principal. It is possible that contributions have or will have exceeded required compensation. This would result in some amount of principal being returned to the State's general fund to comply with the Constitutional prohibition against dedicated funds. It is important that a determination of the required compensation and the disposition of any excess contributions be made because investment policy is based on the assumption that the entire principal will remain as principal of the fund. The determination should be made in the near future because it has become increasingly likely that excess contributions have been made as each year passes.

2. Policy

The most important characteristic of the fund for investment policy purposes is its perpetual nature and the restriction that its principal can never be expended. As in the case of the retirement funds, this expands the universe of investment possibilities and increases the potential for achieving higher returns on the investments over the long run.

The primary objective of investment policy should be to continuously increase the principal of the fund without severely reducing the current income flow available for the purposes of the trust. It is the typical objective of other endowment funds in the nation. The larger corpus over time leads to larger income flows, which in turn permit increased support of the activities for which the endowment was established. If the corpus were not to grow after the original contributions cease, the annual dollar income flows would be limited to the prevailing range of interest rates and would not be able to assist in financing any expansion of the activities or any increasing costs of the activities.

The need for continuing growth of the principal of the fund in order to increase the available income is evident from the fact that the current income from the Public School Trust Fund constitutes only about 1 percent of the total annual appropriations for public school programs. Although the Public School Trust Fund can invest as broadly as the retirement funds, until recent years it has been too small to effectively use the equity markets at reasonable transaction costs and the Commissioner of Revenue did not have the necessary discretionary

authority. With the delegation of the authority from the Public School Fund Advisory board, required by former AS 37.14.170(a) and granted in September 1986, domestic common stock investments were initiated for the fund. In 1988, legislation was enacted making the Commissioner of Revenue the sole fiduciary for the fund and eliminating the need for delegation from the board.

Currently, the fund holds about 27 percent of its assets in common stocks and the remainder in straight corporate or federal government debt issues. The percentage held in equities will rise toward the retirement fund levels as opportunities develop in the equity markets. The corporate debt is diversified to reduce the exposure to credit risks and the debt maturities are structured to maximize interest income over interest rate cycles. Liquidity and market risks are not important elements of the policy, except to the extent necessary to preserve the ability to reallocate the investments within the funds. The fund's investment policy has been to maximize the realized return on the investments over a 10 to 20 year time span. Reduction of the perpetual life of the fund to a shorter time horizon is a practical necessity of the investment decision process.

Under the professional prudence standard of current statutes, the investment policy will shift to a predominant reliance upon equity issues. Educational endowment funds in the nation typically hold about two-thirds of their assets in equities. Equities currently are confined to domestic common stocks, through the consolidated investment pool which also includes the retirement funds' domestic common stock investments. When the fund grows larger, or when suitable pooled accounts are established by the Treasury Division, it may include real estate or international equities in its portfolio. This policy seeks to maximize the future income of the fund by increasing the principal of the trust. The greater potential exposure to residual risks is ameliorated through adequate diversification.

Ten years later, trust fund policy and procedures filled 15 pages, with sections as follows: Overview, History, Facts and Figures, Management, Investment Policy, Control and Reporting Requirements, and Treasury Funding. Significant changes or additions in this version, *Investment Policies and Procedures*, Alaska Dept. of Revenue, Treasury Div., V. 1.3 Released April 1, 2000, Section XII, Pages C-I-13, are as follows:

1. A significant change was made in accounting procedures in 1997. The fund's assets were to be recorded at market value, rather than book (cash purchase) value. Unrealized capital gains and losses thus became a component of the fund's ending balance each year.
2. In February 2000 a new payout model (of earnings) employing a rolling five-year smoothing methodology was adopted. *This is described in the next section, Use of Fund Earnings.*
3. Effective April 1, 2000 the investment policy for principal assets of the fund is: 55% Long-term Fixed Income Investment Pool and 45%

Domestic Equity Collective Funds. Performance benchmark for the Long-term Funds is the Lehman Brothers Aggregate Index. For the Domestic Funds the benchmark is the Russell 300 Index. The equity (common stock) position is intended to provide real and inflation-adjusted value to the principal in the long-term.

4. Effective April 1, 2000 the investment policy for income assets is the Short-term Fixed Income Investment Pool; performance benchmark is the Three-month U.S. Treasury Bill.

Since then adjustments made in investment policies for the principal, as stated in *Investment Policies and Procedures*, are as follows:

	Fixed Income	Equity	Effective Date
Version 2.0	59%	41%	July 1, 2003
Version 2.1	57%	43%	July 1, 2004

So how do these investment policies work? What are the rates of return on investments of principal? A partial answer is found in Table 4, Annual Rate of Return on Principal.

Table 4
Annual Rate of Return on Principal
Alaska Public School Trust Fund
FY '95-FY '04

Fiscal Year	Ending Balance	Income* Earned	Rate of Return
'95	142.2M	11.5M	8.1%
'96	152.0M	9.1M	6.0%
'97**	211.5M	7.7M	3.7%
'98	249.4M	8.5M	3.4%
'99	273.0M	9.0M	3.3%
'00	288.4M	11.9M	4.1%
'01	286.0M	13.1M	4.6%
'02	269.4M	11.3M	4.2%
'03	280.5M	10.2M	3.6%
'04	299.1M	10.3M	3.4%

* Income is comprised of interest and dividends and excludes unrealized or realized capital gains/losses.

** FY '97 is the first year assets (the principal) were recorded at fair (market) value rather than at book (cost) value.

Sources: Balance and Income figures from *Investment Policies and Procedures*, State of Alaska, Department of Revenue, Treasury Division, Version 2.0 Released March 15, 2004, Section XXI, Page C-4, and *CAFR* for '04.

Another way to check the fiscal health of the Fund is to see what changes in ending balances are attributable to capital gains and losses. Using the same ten year period as Table 4, we can examine this question as follows:

Trust Fund beginning balance, FY '95	\$128,900,000
Land Receipts credited FY '95–FY '04	<u>56,427,000</u>
Book (cost) Value Total	185,327,000
Ending Balance, Market Value, FY '04	\$299,152,000
Ending Balance, Book Value FY '04	<u>185,327,000</u>
Difference	113,825,000

The difference is attributable to \$105,916,000 in unrecognized capital gains (see Table 2) plus other increases such as corrections and transfers and restatement of prior period amounts. The gains, of course, were generated over the life of the Fund, not just the last ten years.

Use of Fund Earnings

Through 1983, the State continued to credit the Fund’s investment earnings to the State’s General Fund. The contention was that since appropriations from the General Fund were used for school support programs, the School Trust Fund’s investment earnings were being spent for school purposes, as required by law. However, no transfers to the General Fund were made in 1984 and 1985.

The 1985 Legislature then did appropriate \$19M from School Trust Fund earnings for construction and renovation of public school facilities in FY '86 (CSSB 27 [fin], Chapter 96). This amount was equal to the total of Trust Fund earnings from the inception of the fund through 1985. The State had withheld distribution of investment earnings for two years to build up the earnings account to allow this large appropriation.

This action marked the first known instance since Statehood of Fund earnings being appropriated directly for support of the public schools rather than indirectly via the General Fund.

Twelve school districts, both rural and urban, were designated to receive funds from this appropriation. Although only \$19M was appropriated, specific allocations to these districts totaled \$21M. Such over-allocation usually is not a problem due to failure of districts to complete all projects as planned. Schools in FY '86 used less than \$19M and reallocations

were required for FY '87 and FY '88 in order to disburse the entire amount.

In 1985 the Legislature also appropriated in the FY '86 budget \$109.3M for 25 other school construction projects (SCS CHSB 195 [Fin] am S, Chapter 105). This appropriation came from the State's General Fund.

For FY '87, the Legislature appropriated School Trust Fund earnings directly to the Department of Education where it was then disbursed as a part of one or more major school support programs. This practice has continued to date and today these funds are generally posted for use by the School Foundation Program.

School Trust Fund earnings also are being appropriated to three other state agencies, as follows:

1. In 1987, the Division of Treasury in the Department of Revenue began receiving an annual allocation to help defray its costs of managing the Fund.
2. In May 1998 \$432,525 was appropriated from the Trust Fund to the Department of Natural Resources to pay for the appraisal of the school trust lands (House CS for CS for SB 231 [fin] am H). A small amount of this appropriation (\$91,900) was used that year, but the balance was not promptly utilized. In 2002 the amount remaining from this appropriation was reappropriated for use through FY '04 (CS CSSB 2006 [fin] am H). In addition, this same legislation provided a new appropriation of \$305,000 from the School Trust Fund to the Department of Natural Resources. The statute reference notes that these sums are to be used ". . . for an appraisal of public school lands to determine the market value of the public school trust land where (sic) the land was redesignated as general grant land in 1978."
3. In 2001, the Department of Law began receiving monies from the Fund which it then disburses to the plaintiffs in *Kasayluie vs. State of Alaska* for their legal expenses in planning and monitoring the appraisal called for by the lawsuit.

See Table 5, Distribution of Investment Earnings, Fiscal Years '85-'04, which follows, for the specific amounts, by department.

Table 5
Distribution of Investment Earnings
Alaska Public School Trust Fund
FY '85 – FY '04
(in 000's)

Fiscal Year	Capital Projects*	Department				Totals
		Education: Foundation Program	Revenue: Treasury Division	Natural Resources: Land- **	Law: <i>Kasayulie</i> Plaintiffs	
'85 ***						
'86	16,836.0					16,836.0
'87	2,010.0	8,000.0	82.7			10,092.7
'88	154.0	7,398.0	110.2			7,662.2
'89		8,830.9	161.9			8,992.8
'90		7,015.2	142.7			7,157.9
'91		7,015.0	124.5			7,139.5
'92		7,499.0	240.3			7,739.3
'93		8,309.0	83.4			8,392.4
'94		8,452.7	80.4			8,533.1
'95		6,816.6	80.7			6,897.3
'96		5,394.7	86.2			5,480.9
'97		11,855.9	53.0			11,908.9
'98		9,221.1	74.8			9,295.9
'99		7,118.7	67.7	91.9		7,278.3
'00		7,612.3	67.7	.1		7,680.1
'01		8,415.6	57.2	15.3	43.4	8,531.5
'02		11,812.8	56.1	18.0	24.7	11,911.6
'03		12,478.5	66.2	25.0	42.8	12,612.5
'04		12,582.0	72.0	17.0	****	12,671.0
Totals	19,000.0	155,828.0	1,707.7	167.3	110.9	176,813.9

* Capital Projects' (CH 96 SLA 1985) total equals investment earnings 1916–1984.

** A DNR report shows expenditures of 65.4 for FY '02; Legislative Finance shows expenditures of 66.9 for FY '03.

*** Earnings were not distributed in FY '84 and '85.

**** \$ 46.0 was requested but not paid in FY '04.

- Sources: 1. *Consolidated Annual Financial Reports*, State of Alaska.
2. Selected Department Budget Requests (showing prior year actuals).
3. Legislative Finance Division reports, FY '87–'03.
4. Trust Fund History, 1978–98, prepared by Betty Martin, Comptroller, Treasury Division; submitted in Discovery Materials, *Kasayulie vs. State of Alaska*; and FY '99–'03 Supplement.

The availability of investment earnings for appropriation is governed by Department of Revenue policy. This policy defines distributable income, and is contained in *Revenue Sources Book, Spring 2004* (Alaska Department of Revenue Tax Division, Table 7-3, page 68) which states, in part:

Public School Trust. The annual distribution is 4.75% of a five-year moving average of the fund principal's market value so long as that amount does not exceed the interest and dividend earnings available in the earnings account. The trust has accumulated a sizable income account balance so the fund is better able to retain its ability to distribute in a sustained bear market.

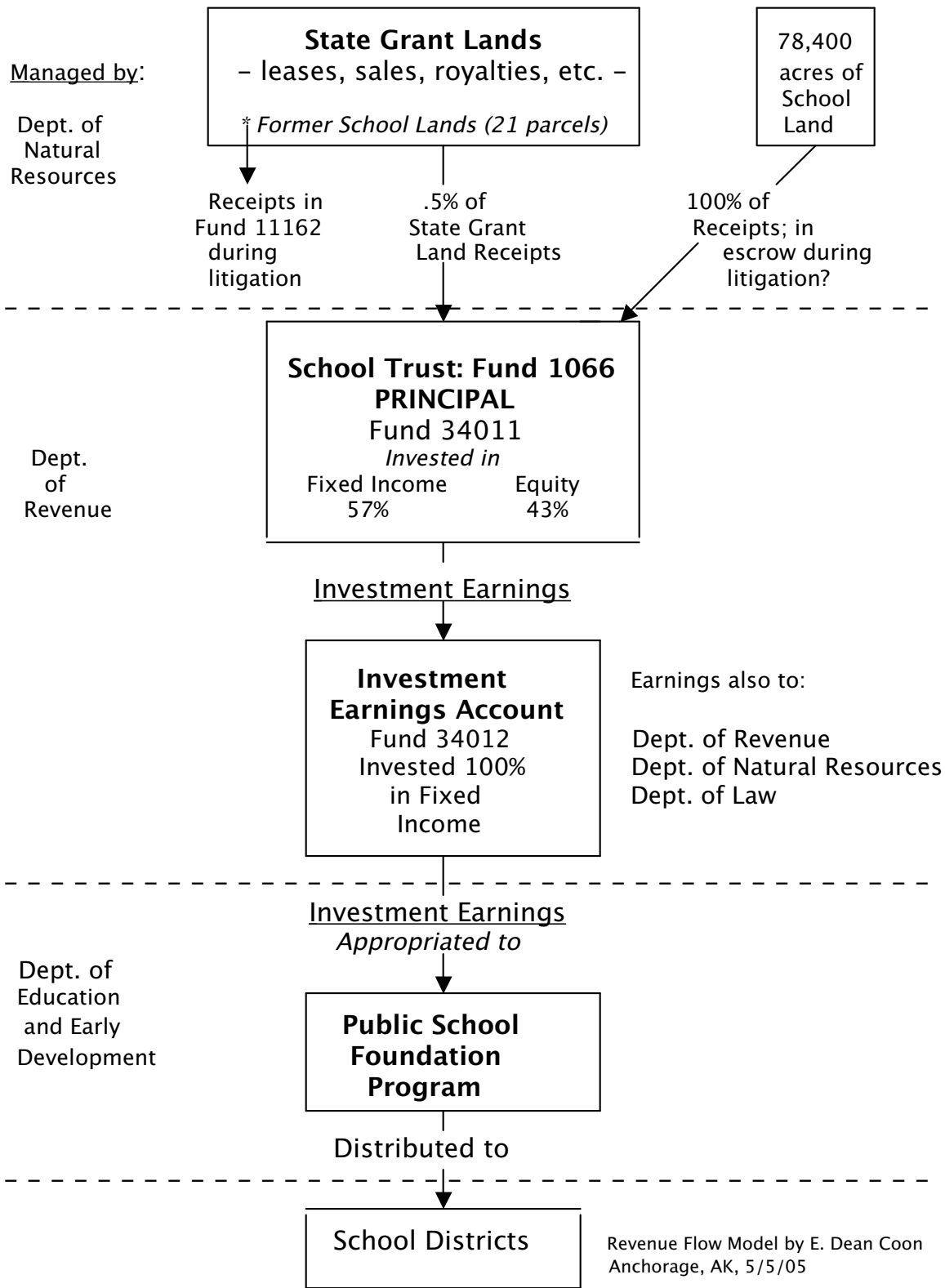
The distributable income calculated by this formula is a base amount available to be distributed. In practice, however, the amount actually distributed from the income account often exceeds the figure calculated. For example, in FY '03 the distributable income figure was \$9.5M; \$12.6M was actually distributed.

Similar policies, but with different distribution rates, are used for distributable income determination for the other five state endowment funds.

The sources of money for the Fund, the management of the Fund, and the distribution of Fund earnings to the schools have been presented. State agencies involved are the Department of Natural Resources, the Department of Revenue, and the Department of Education and Early Development. Each agency has its own statutorily assigned functions.

The agencies and their respective tasks are shown in Figure 5, Alaska School Trust Fund: Revenue Flow Model, 2004, which follows. This figure shows the trail of the Trust Fund monies from the Department of Natural Resources to the school districts.

**Figure 5
Alaska School Trust Fund: Revenue Flow Model
2004**



The Litigation

Kasayulie et al v. State of Alaska

Litigation that would ultimately affect the status of the Public School Trust fund and the former state school lands was initiated in 1997. On May 20, Case No. 3AN-97-3782 Civ, *Kasayulie et al v. State of Alaska*, was filed in the Superior Court, Third District of the State of Alaska, at Anchorage.

The 27-page Complaint for Declaratory Relief filed in this case defined the Nature of the Action as follows:

The Alaska Constitution guarantees to the citizens of the state of Alaska and the children of this state a public school system open to all children of the state. This constitutional mandate requires the state to provide adequate educational facilities. Despite the mandates of the Constitution, the school finance system adopted by statute for capital facilities and major maintenance denies some school districts the funds necessary to provide minimally adequate facilities, while other school districts have more than sufficient resources to meet capital needs. The districts and parents bringing this action allege the capital budget and appropriations established by the state for each Alaska school district creates gross disparities and inadequacies that violate the equal protection and education provisions of the Alaska Constitution, Art. VII, § 1 and Art. I, § 1.

Although this initial complaint was silent on the issue of school trust lands, an amended and expanded complaint filed within a year would include a charge that the state breached the school land trust.

The Plaintiffs

Plaintiffs in this action included three sets of parents, six school districts, and an advocacy group named Citizens for the Educational Advancement of Alaska's Children.

Parents. The three sets of parents resided in communities in Southwest Alaska. All had children in schools in the plaintiff districts. They were:

Willie and Sophie Kasayulie, Akiachak, Alaska; two of their children are enrolled in the Yupiit School District's Akiachak village schools.

Paul and Maryann Mike, Kotlik, Alaska; three of their children are enrolled in the Kotlik School in the Lower Yukon School District.

Arthur and Ruth Heckman, Pilot Station, Alaska; their four children are enrolled in the Pilot Station School in the Lower Yukon School District.

School Districts. The school districts are all classified as Regional Educational Attendance Areas, charged with providing educational services within their respective boundaries in the Unorganized Borough of Alaska. The districts:

Bering Strait School District, with 1,700 students in 15 village schools; administrative offices of its 24,240 square mile district are in Unalakleet.

Iditarod Area School District, with 420 students in 9 village schools; administrative offices of its 44,441 square mile district are in McGrath.

Kashunamut School District, with 230 students enrolled in its single school in Chevak

Lower Kuskokwin School District, with 3,500 students in 23 village schools; administrative offices of its 23,792 square mile district are in Bethel.

Lower Yukon School District, with 1,700 students in 12 village schools; administrative offices are in Mountain Village.

Yupiit School District, serving 400 students in three village schools; its administrative offices are in Akiachak.

CEAAC. Citizens for the Educational Advancement of Alaska's Children was organized during the 1995-96 school year. Its goals were (1) adequate funding for school district programs, (1) appropriate facilities for all students, and (3) increased public awareness of the state's responsibilities to meet these needs. These goals were sought through public education, legislative action, and finally through litigation.

The group's mission statement and membership, as presented on its web site <<http://www.ceaac.us/>>.html in October 2004, follow:

Mission Statement

Citizens for the Educational Advancement of Alaska's Children (CEAAC) is an organization representing people and organizations concerned for the general welfare of school children of Alaska. It has been active in advocating for the adequate funding of education, including but not limited to the funding of school

construction projects and appropriate funding increases to support public school programs.

CEAAC is not in competition or in opposition to the Association of Alaska School Boards (AASB), the Association of Alaska School Administrators (AASA), the Department of Education and Early Development (DEED) or any other group of educators. In fact, these organizations have goals for Alaskan children which are closely aligned with CEAAC goals, thus cooperation and collaboration is welcome.

CEAAC does not promote a "rural versus urban" or a "native versus non-native" approach to school program funding problems or to the school facilities problems which have been identified. CEAAC does not advocate that any public school funds be taken away from one group of children and given to another. We are looking for solutions that will be of value to children throughout Alaska, wherever they live and regardless of their race.

Current Membership

Member School Districts (the following districts are current members or have been members and/or have made significant contributions):

Alaska Gateway School District, Aleutian Region Schools, Aleutians East Borough School District, Bering Strait School District, Chugach Schools, Copper River School District, Dillingham City Schools, Hydaburg City Schools, Iditarod Area Schools, Kake City Schools, Kashunamiut School District, Kuspuk School District, and

Lower Kuskokwim School District, Lower Yukon School District, North Slope Borough Schools, Northwest Arctic Borough Schools, Pribilof School District, St. Mary's School District, Southeast Island Schools, Southwest Region Schools, Unalaska City Schools, Wrangell City Schools, Yakutat City Schools, Yukon Flats Schools, and Yupiit School District.

The Complaint was filed by attorneys Howard S. Trickey and Saul R. Friedman, of the law firm Jermain Dunnagan & Owen, on behalf of the Committee for the Educational Advancement of Alaska's Children. Cooperating on the case was the law firm of Middleton & Timme, P.C., represented by Collin Middleton. Others in both firms would be involved over time, as well as Attorney Glenn E. Cravez.

The Office of Attorney General, Department of Law, would represent the Defendant State of Alaska. Attorney General at that time was Bruce M. Botelho and Thomas H. Dahl was an Assistant Attorney General.

School Trust Issues Added to *Kasayulie*

In the year following the filing of *Kasayulie v. State of Alaska*, the plaintiffs developed new and expanded allegations against the State. While most of this new material directly concerned inadequate school facilities the breach of the school land trust was introduced. The contention was that the State's failure to manage the lands and trust properly contributed to the underfunding of school facilities.

Also introduced was an allegation of the State's failure to receive, use, and account for proceeds of sale of federal lands for support of the public schools, as required by §6(f) of the Alaska Statehood Act. It was required that five percent of the proceeds of sale of Federal land in Alaska be paid to Alaska for the support of public schools.

Author's Note: The aforementioned federal lands are not school lands and the proceeds from their sale are not credited to the school trust fund. The State's share from sale of federal lands in Alaska, while an important component of the court case, is not directly related to the discussions in this paper concerning the public school trust fund and public school land.

Second Amended Complaint Filed

The Second Amended Complaint for Declaratory Relief filed by the plaintiffs in Superior Court May 20, 1998, paragraphs 88 through 101, presented these Causes of Action: (1) Breach of School Land Trust, and (2) Accounting by the State of Alaska. Statements in these sections included the following:

The school land grants were expected to produce a fund, accumulated by the sale and use of the trust lands, with which the Territory would be required to support public schools in Alaska.

The school land grants made by the federal government were confirmed and transferred to the new State of Alaska . . . for the same purpose the grants were originally made.

The State of Alaska applied for and received title to over 100,000 acres of land from the United States under the school land grant.

In 1978, the State of Alaska breached its trust obligations under the school land grants when it purported to redesignate the school trust lands as general grant lands. At the same time, the State established a "public school trust fund," the principal of which was to consist of the balance of a 'school permanent fund' on July 1, 1978 plus sums transferred each fiscal year into the public school trust fund in an amount equal to one-half of one percent of the total receipts derived from management of State land, including

amounts paid to the State as proceeds of sale or annual rent of surface rights, mineral lease receipts, royalties, royalty sale proceeds, and federal mineral revenue-sharing payments or bonuses. The net income of the public school trust fund was not to be appropriated for a purpose other than the support of the State public school program. The principal and the capital gains or losses realized on principal were required to be perpetually retained in the public schools trust fund for investment purposes. Chapters 181 and 182, SLA 1978, AS 37.14.110–170.

The plaintiffs are intended beneficiaries of the school lands trust and the public school trust fund.

The public school trust fund does not adequately compensate plaintiffs for the State's breach of the school land trust.

The State has failed to fund public schools as required under the public school trust fund.

The practice of failing to fund facilities construction and major maintenance in plaintiff's rural school districts is the result of the State's violation of its trust obligations under the school land grants and/or the public school trust fund.

The defendant State of Alaska has never provided plaintiffs with any accounting of the funds received, the lands received or the value of the land received . . . nor of the funds expended.

Plaintiffs are entitled to an accounting by the State of Alaska of the sums received by it and expended, . . . of the lands received by it, their value, . . . and the funds placed in and the monies expended from the public school trust fund established in Chapters 181 and 182 of SLA 1978.

Plaintiffs, in the Second Amended Complaint, also presented an expanded Prayer for Relief. In it, they requested the Court to enter judgment against the defendant to include the following:

Enter a judgment declaring the practice for funding capital projects is void under the Alaska Constitution, Art. VII, §1 and Art. I, §1, and violates Title VI of the Civil Rights Act of 1964, and its (sic) a breach of the State's trust obligations to plaintiffs under Section 6(f) of the Alaska Statehood Act, the school land trust first established in 1915 and later confirmed in Section 6(k) of the Alaska Statehood Act, and the public school trust fund now codified at AS 37.14.110 et seq.

Issue an order directing the defendant, the Governor of the State of Alaska, and the Legislature of the State of Alaska to immediately

comply with the mandates and trust obligations of Art. VII, §1, and Art. I, §1 of the Alaska Constitution, Title VI of the Civil Rights Act of 1964, Sections 6(f) and 6(k) of the Alaska Statehood Act, and the public school trust fund by developing capital budget and corresponding capital appropriations for state educational facilities which meet the current capital needs of the plaintiff school districts and funds the current capital projects on a priority basis as ranked by the Department of Education.

For an accounting of all funds and lands received by the State of Alaska for the support of public schools within the State of Alaska

Soon after the school trust issue was added to the *Kasayulie* litigation, the Department of Natural Resources established new management criteria for the school lands held with other general grant lands. Pending and future actions which would dispose of school land or resources must meet criteria in DNR Department Order 143, dated December 21, 1998, which stated, in part:

1. The action approved must be for full, Fair Market Value at the highest and best use of the parcel, or
2. The action must be a result of an existing contractual obligation (i.e., land sale contract, reappraisal of an existing lease, or a land with a municipality)

This Order further required the DNR Commissioner to be notified of any pending action not meeting these criteria; the Commissioner will determine if the action may proceed. It also noted that conveyances to boroughs and municipalities do not meet the criteria. This last condition effectively prevented any new municipal entitlements of former school land during the life of the litigation.

At the same time a notice of litigation was added to all school land case files and maps in the DNR land information files. DNR also established an escrow account for the receipts from school land sales underway. Receipts from land sales initiated after December 21, 1998 would likely be credited to this escrow account but whether this is happening was not determined by the author.

The State responded vigorously to the charges made in the Second Amended Complaint. The plaintiffs submitted their answers. Memoranda, motions, requests for summary judgments, discovery requests, affidavits, depositions, etc., were generated by the parties. Judge Reese issued opinions and judgments on some aspects of the case. There were conferences and hearings. It was a busy time for the attorneys on both sides, as they sought to convince the Court of the merits of their respective positions.

In January 1999, the combined motions for summary judgment were argued before Judge Reese. Now the State and the Plaintiffs would await a response by the court.

State Found at Fault

On September 1, 1999, Judge John Reese, Superior Court, Anchorage, issued his rulings in *Kasayulie v. State of Alaska*. The banner headline in the Anchorage Daily News on September 3 told the story: Judge: "State fails rural schools," and the subhead: "Inadequate funding violates constitution, federal law, ruling says." The story, by Rosemary Shinohara, Daily News Reporter, follows:

Alaska is violating the state constitution and civil rights law by providing inadequate school buildings for students in rural Alaska, a state Superior Court judge in Anchorage has ruled. The decision, if upheld, could force a reallocation of school construction money statewide.

Judge John Reese cited a list of failings - "roofs falling in, no drinkable water, sewage backing up and enrollment up to 187 percent of capacity" --and said it adds up to failure by the state to meet the Alaska Constitution's requirement that it establish and maintain a school system.

The state Department of Education maintains a priority list for repairing and replacing schools, but the Legislature year after year appropriates little money for school construction. The list contains \$236 million in projects.

Besides ducking its basic obligations, the state is treating rural residents, who are predominately Native, differently than those who live in cities and boroughs, Reese said. It is violating a federal law which prohibits discrimination in federally funded programs, he said.

The judge, in a decision Wednesday, also said the state has not properly accounted for an education trust of land and money given to it by the federal government and must do so.

"We're really excited about the decision," said Pam Van Wechel, superintendent of the Kashunamiut Schools in Chevak, a Western Alaska village. "I'm sure the effects will be far-reaching."

Van Wechel is president of a group of parents and rural school districts that banded together to bring the lawsuit, the Citizens for the Educational Advancement of Alaska's Children. They began their fight 2 1/2 years ago.

The Chevak School is at the top of the state Department of Education priority list for replacement. It was built in 1973 by the federal government and is crowded and unsafe, say state administrators and the people who sued.

The group's attorneys, Collin Middleton and Howard Trickey, said that if the decision stands, the state will have to come up with a new funding plan that makes more money available to rural schools.

Alaska Attorney General Bruce Botelho will study the decision for several weeks and talk to lawmakers and educational leaders before deciding whether to appeal to the Alaska Supreme Court.

"The administration has been consistently concerned about the condition of rural schools and has fought extensively to see capital projects in rural Alaska, but to no avail," Botelho said.

The Department of Education's priority list is based on which schools are most crowded or unsafe, Education Commissioner Rick Cross said.

"We don't pretend the rankings are perfect, but they are good and getting better," he said. The list contains rural and urban school construction requests.

"It has been ignored, not funded and not considered" by the Legislature, Cross said.

"Well, there is just so much money," said House Speaker Brian Porter, R-Anchorage. He agreed it is up to the Legislature to appropriate adequate funds but he said he couldn't comment on the decision because he hadn't read it.

While rural districts rely solely on state grants for construction money, cities and boroughs are able to sell voter-approved construction bonds to build and repair schools. In most years, the state reimburses local governments for a share of the school bond debt even if no rural school projects are funded.

That amounts to disparate funding, Judge Reese said: "The rural areas do not have substantially equal access to facilities funding. As a result, many rural schools are continuously denied facilities funding."

Botelho said the issue of disparity, of rich vs. poor, has been the subject of education funding disputes in many states. He said he believes the Legislature will view the decision as the court's intruding on its appropriation powers.

But the court is the final arbiter on the state constitution, he said.

A related story reported that the high school in Manokotak had been condemned due to structural problems and forced to close. Three dozen students will be forced to attend classes in split shifts in the village's elementary schools. Manokotak is west of Dillingham in the Southwest Region School District.

Judge Reese's Rulings

Judge Reese's rulings were contained in an 18–page Order Regarding Motions for Partial Summary Judgment on Breach of Trust Issues. Significant content regarding the school trust and school land follow:

The court holds that the State has breached its duties as a trustee of the public school lands. The purpose of the trust was to create a permanent source of revenue for the exclusive benefit of State schools.

Redesignation of the public school lands into general grant land is not permitted.

There was no valuation of the land before the State redesignated it in 1978. That was a breach of the State's trust obligations.

There followed a discussion as to whether the state paid fair market value for the land at redesignation. The plaintiffs contended there has been no determination, or indication in the statutes, that the 1/2% paid from state lands is full compensation, that the state did not commit to contribute for any set time or for any specific amount, and that the 1/2% is illusory as it could be revoked at any time. The State contended that the 1/2% of receipts from management of state land is compensation for up to the fair market value.

The court finds that it is impossible to know if the fair market value has been paid (through the contribution of 1/2% from state land revenues to the school trust fund) without an appraisal. The lands must be appraised or otherwise valued before any acts subsequent to the redesignation will be judged.

There followed discussion regarding revenues from the ANILCA 906(b) lands. This is a 75,000–acre grant of additional federal land in lieu of school lands never received under the 1915 Act of Congress. The land was finally selected in 1992, 12 years after the grant was made. Plaintiffs contend the school trust fund should get 100 percent of revenues generated by this land through leases, gravel sales, etc. The State says it has set up a separate agency trust fund especially for the ANILCA land revenues.

The court holds that it is not clear from the record that adequate separation and accounting has occurred (with respect to the ANILCA land). An appraisal must take place before the court will be prepared to rule on this issue.

The court finds that aside from breaches of trust duties, appraisal of the res of the trust is an appropriate trust expenditure. The

fund should bear the appraisal expense ultimately. However, the State should front it as the land cannot be properly defined until the appraisal and remedies are accomplished.

There followed a discussion on the premise that State expenditures on education set off, or compensated for, the interest on the unpaid balance due the fund. Plaintiffs contend the State failed to account for or pay interest or capital gains on the unpaid balance due the schools after the 1978 redesignation. The State asserts that any money owed the fund for interest on the unpaid balance is set off by the large sums the State pay to the schools each year, and that after the appraisal the interest can easily be determined.

The court holds that an amount equal to what properly enumerated, valued, and managed trust assets would have produced could be set off.

The court holds that the State has not commingled the trust assets by depositing the funds into the general fund. The assets are deposited into the general fund late in the fiscal year for an appropriation from the legislature to the Department of Education.

There followed a discussion regarding an accounting of the trust. The plaintiffs contend they are entitled to an annual accounting. The State contends it has provided an adequate accounting of the trust activities and assets.

(The court says) Therefore, resolution of this issue, if needed, will occur at a later date.

(With regard of the use of trust funds by the Department of Revenue) The court finds that reasonable fees for the management of the fund are appropriate. This policy encourages the trustees to continue to administer the fund even after a breach.

There followed a discussion regarding the 1/2% of total receipts derived from the management of the state land. The State contends that after the State pays back the value of the land, the 1/2% would be a constitutionally prohibited dedicated fund. Plaintiffs do not agree, and say this was a grant of public school land which was to exist in perpetuity, that the State's actions do not change the nature of the trust, and if the 1/2% is compensation, it is to be the trust's permanent and primary funding scheme. Art. IX, Sec. 7 of the Alaska Constitution reads in part: "This provision shall not prohibit the continuance of any dedication for special purposes existing upon the date of ratification of this section by the people of Alaska."

The court holds that there is no violation of the dedicated funds provision. Education funding is required by the federal government for State participation in federal programs and the assets are dedicated to schools by federal law. Furthermore, the trust fund and the purposes therefore existed prior to ratification of the Alaska Constitution.

There followed a discussion about requests by both parties for instructions regarding the 1/2% contribution as compensation for the full market value of the land taken, as applied to the dedicated fund provision. Plaintiffs contend the State wants to value the land to determine if payments have exceeded the fair market value of the land taken, whereby the excess would be prohibited as contributions to a dedicated fund and could be withdrawn from the fund. The State asks the court to use the remedy used in Weiss v. State, 706 P.2d 681 [Alaska 1985], and that if there is a breach the State wants to pay full market value, instead of reconstituting the land.

The court holds that without a valuation of the trust violations, it is premature to consider remedies. Therefore the parties request for instructions is DENIED at this time.

There followed discussion of several affirmative defenses put forward by the State to counter the entire suit brought by the plaintiffs. The court's position on each is given.

The court holds that governmental immunity does not apply in this case.

The court holds that the statutes of limitation defenses do not apply to actions in equity unless there is an express statute permitting them, and there is not.

The court finds that the State is not prejudiced by plaintiffs delayed filing.

The court finds that there is no estoppel. Kasayulie did not actively present a position in 1978 or at any time up to this suit.

As is apparent from a review of this ruling, there are a number of unresolved issues that won't be addressed by the Court until the appraisal of the former school lands is completed.

Pending Issues

Major questions and issues facing the Court include:

1. What was the appraised value of the school grant land in 1978?

2. Has the State paid fair market value for the land (by virtue of the contribution of .5% of state land receipts)?

3. Did adequate separation and accounting occur with respect to the ANILCA land grant?

4. What is the amount of setoff, that is the amount equal to what properly enumerated, valued, and managed trust assets would have produced?

5. Has there been an adequate accounting of trust activities and assets? *(Note: This question is not linked directly to the completed appraisal, but is something to "occur at a later date.")*

6. What remedies will the Court consider to resolve the issues in this case?

The answers to these questions and issues await completion of the appraisal. What is the status of this important task?

Appraisal of School Lands: Redesignated and New

As noted earlier, the State should have conducted an appraisal when the school lands were redesignated as general grant lands in 1978. Then in 1999 the Superior Court ruling previously referenced ordered that there be an appraisal. Remedies in *Kasayulie vs. State of Alaska* cannot be considered without an appraisal, the Court said. *Six years later there has been no appraisal.*

The author is aware that there has been considerable dialogue between the State and the plaintiffs on this matter in the past five years. Draft versions of a Request for Proposals (RFP) to conduct the appraisal have been circulated back and forth. The Department of Natural Resources ultimately will issue the RFP and will be responsible for the appraisal.

Both DNR and the plaintiffs are receiving money from the School Trust Investment Earnings Account for their expenses associated with the appraisal and related activities. As reported earlier in Table 5, Distribution of Investment Earnings, through FY '04, DNR has spent \$161,300 and the plaintiffs \$110,900.

There has been no lack of funds to pay for the appraisal. Two legislative appropriations cited earlier, \$432,525 and \$305,000, have been made to DNR. Of these amounts, \$580,325 is unexpended. The plaintiffs' \$110,900 has come via supplemental appropriations made to the Department of Law.

Certainly this will be an unusual appraisal. Consider these few elements:

1. It will involve more than 181,000 acres of land.
2. Except for three large parcels, the land is located in tracts of 640 or fewer acres in diverse areas of the state -- Fairbanks/Interior, Anchorage/Mat-Su, Kenai Peninsula, and Southeast.
3. Much of the land has been subdivided, traded, sold or is under contract to be sold, or otherwise encumbered.
4. Resource values for timber, minerals, and oil and gas must be included.
5. It will not be possible to make site visits to each property.
6. Land valuation as of 1978 will be sought for 101,000 acres; the balance is to be valued as of the date patented to the State.

In the two years following the initial *Kasayulie* ruling on school facilities the State did little to provide more money for rural school construction. So on March 27, 2001, Judge Reese reaffirmed the original ruling by issuing a brief order that he would issue specific orders if the State failed to act. These specific orders have not been issued.

The Future

What Next?

Congress, as it had done for most other states, granted Alaska federal land to be used for the support of public education. Congress specified that receipts from the use of the school land would be put into the permanent fund, and the principal of the fund, which can never be spent, would be invested. The investment earnings would then be used for the benefit of public schools. When Alaska became a state it accepted this scheme -- school land/permanent fund/earnings to the schools -- and pledged to continue it in the same manner.

But this pledge was ignored and the scheme was destroyed in 1978 when the Alaska Legislature "redesignated" over 103,000 acres of school land and made this land a part of its general grant lands. The income stream from the school lands to the school permanent fund was eliminated. There were no school lands to generate receipts for the school permanent fund. Finally, 21 years later, Superior Court Judge John Reese said: "The state had breached its duties as a trustee of the public school lands."

At the same time the legislature redesignated the school lands, it offered a new source of receipts for the School Permanent Fund (the name was later changed to Public School Trust Fund). The fund was designated to receive 1/2 of one percent of receipts from Alaska's general grant lands. The annual receipts from this new source are considerably higher than the Fund had previously received from school land receipts.

Even though the School Trust Fund was receiving more money from this new source, the Fund was in jeopardy. The reason: The legislature had designated the new source of receipts and had set the percent to be paid into the fund; and the legislature is free to change this at any time. Even to eliminate it! This is a peril facing the Public School Trust Fund.

The current litigation, *Kasayulie vs. State of Alaska*, addresses many concerns caused by the breach of the trust. Many issues have yet to be ruled on, the major one being: "Has the amount of money put into the trust fund since 1978 exceeded the value of the school land in 1978?"

This situation raises some important questions, such as:

1. Will the court mandate that .05% receipts from general grant lands continue to be credited to the trust fund?
2. Will the court suggest a minimum rate or amount that must be put into the trust fund each year?
3. Will the court, through order or ruling, prevent the State from breaching its duties as trustee of the public school trust fund?
4. Will the court, in these ways, or some other, guarantee that the State will continue to meet its school land/school trust obligations to the public schools, as it promised at Statehood?

With a completed land appraisal, the Court should be able to resolve the unanswered questions in the first ruling as well as deal with the four questions posed above.

Since Judge John Reese has retired, will the new judge handling the case proceed in the same manner as Reese? Or will some new avenue of resolution be presented? Whichever happens, the outcome of this case may determine the future and financial well-being of the Public School Trust Fund, a fund that can provide increasingly larger amounts of money for the benefit of the public schools.

The Alaska School Trust Fund is an important source of revenue for the public schools. It will become more valuable as the principal grows, and as the investment earnings increase. Some recommendations to make this happen follow.

Recommendations

These first two recommendations are in direct response to circumstances brought about due to unsettled issues of the current litigation.

1. *Negotiate a Settlement and Cancel the Appraisal.* The settlement would include the following mutually agreeable terms (more may be needed):

1. The current value of the redesignated school land is equal to the general grant land receipts paid into the trust fund since 1978.
2. The question of the fair market value of the school land when it was redesignated in 1978 is moot.

3. It is mutually agreed that the appraisal of the school lands may be terminated.
4. The State will not seek to recover any amounts it earlier sought to deem overpayments into the school trust fund.
5. The Plaintiffs will not seek interest or capital gains earlier sought on the unpaid balance due the school fund after the 1978 redesignation.
6. It is mutually agreed that this settlement does not relieve the State of its obligation to continue financial contributions to the Trust Fund, contributions made in lieu of the receipts no longer available from the original school lands.
7. The State agrees to retain the current school land (ANILCA Sec. 906(b) land, and recovered Original and Territorial Grant) as school land, with total receipts from land leases, royalty income, etc, on this land being deposited into the Public School Trust Fund.
8. It is mutually agreed that resolution to any remaining school land and school trust issues will be sought through negotiations, with court mediation if necessary.
9. No charges for expenses attributed to *Kasayulie vs. State of Alaska* may be made by the Department of Natural Resources or the Department of Law (for the plaintiffs) after (insert date).

And if Recommendation Number 1, a negotiated settlement, is not followed, use No. 2 below.

2. Appraise School Lands as of 2004, not 1978. The long-delayed appraisal of the redesignated school lands should establish a current assessed value, not an estimate of 25 years ago. The land was illegally transferred to general grant land status without benefit of bill of sale, or any other agreement at that time that addressed just compensation for land taken.

The beneficiaries of the school grant land did not release title to another state entity. The beneficiaries could still be considered de facto "owners" of the school grant land.

Since the process to resolve the breach of the land trust is occurring now, the current value of the land should be used. Consider the receipts paid in over the years as "rent to own" payments. Or as payments on a mortgage. With interest due!

Knowing the value of the school land relative to what has been put into the Fund since 1978 should not relieve the State from continuing its contributions to the Fund. Maintaining the revenue flow is essential since the Fund's original income source was abolished through illegal action by the State. The Plaintiffs said it best as noted in Judge Reese's ruling (p. 12): " If the 1/2% payment is compensation, it is to be the Trust's permanent and primary funding scheme."

Regardless of the outcome of the appraisal, the following recommendation is the most important one. Implementing it would elevate the status of the Trust Fund, and demonstrate the State's commitment to keep and strengthen the Fund. Perhaps most importantly it would be a reaffirmation of the obligation made in 1959, an obligation to maintain the fund forever to provide financial support to elementary and secondary education.

3. Designate the Trust Fund as a Permanent Fund for Education. The Public School Trust Fund should be Alaska's Permanent Fund, or Endowment, for Education. Legislative endorsement of this must be obtained. Past efforts to start a new permanent fund for education have all failed. The most recent effort was H.B. 333, which would establish an endowment for public education. It passed the House but died in the Senate at the close of the last session.

Use of the already-existing School Trust Fund has been overlooked, as its potential was not recognized. Its status as a dedicated fund, seemingly in conflict with a constitutional prohibition against such funds, and the subject of several Attorney General opinions, is not an issue; in fact this status is a strong reason for it to be THE permanent fund for education.

Some legislative modification of the current enabling legislation would be required. The fund must be codified in a way that would insure its continued purpose and existence, including a specified and stable flow of revenue to it.

4. Put All School Land Receipts into the Trust Fund. Receipts from the new and recovered public school land must be credited to the Public School Trust Fund. These lands total 78,420 acres and consist of the ANILCA Sec. 906(b) lands, and recovered Territorial and Original Grant lands. The status of this land cannot be changed, as Judge Reese's ruling stated: "Redesignation of the public school lands into general grant land is not permitted."

5. Manage School Land for a Higher Revenue Return. The public school lands, especially the large ANILCA tracts, should be managed

aggressively in order to obtain the maximum income from leases or resource sales. Some of these lands were selected due to their mineral potential (gold) and an effort should be made to obtain productive leases.

6. Increase Trust Fund Receipts. The amount of land receipts credited to the Fund could be increased. Increasing the amount, from 1/2 to 1 percent of receipts from general grant lands would be a good start. (See Appendix C for the text of a bill to do this). With a larger principal, there would be a significant increase in investment earnings.

It should be possible to make deposits in the Fund from sources other than the receipts from state grant and new school lands. This would allow it to receive gifts and bequests, state "windfall" monies, transfers of funds from other state accounts, including the general fund, etc.

7. Increase the Rate of Investment Earnings. The annual rate of return on principal must be increased. Earning \$10.3 million on a principal of \$299.1 million in FY '04 is only a 3.4 percent rate of return. The rate of return has declined over the past ten years. The investment policies should be reviewed and modified so the fixed income/equity mix on securities would generate greater earnings.

8. Target the Use of Fund Earnings. Options for specific use of Trust Fund investment earnings should be explored. For example, why not use the earnings to pay off bonds issued by the state for school building construction? Here is the math on an example:

Bond Issue Amount:	\$200,000,000
Term:	25 years
Rate of Interest:	4 percent
Annual Payment:	\$12,802,392

There may be other recurring needs in education where an annual appropriation of \$12M to \$14M would serve a useful purpose. A need that could be met without competition from other programs dependent upon appropriations from the State's general fund.

But if the principal was doubled, more than \$25 million could be available annually for school maintenance and construction or other important programs. A deposit of \$300 million would increase the principal to \$600 million. That could result in investment earnings of more than \$25 million annually.

The following example will illustrate how \$25 million could be used to pay off a \$400 million school bond issue.

Bond Issue authorized: \$400M at 4% for 25 years. Payoff schedule:

	<u>Year One</u>	<u>Year Two</u>	<u>Year Three</u>	<u>Year Four+</u>
Issue				
Amounts	\$200M	+ \$100M	+ \$100M	
Payment	12.8M	19.2M	25.6M	Thereafter 25.6M Each Yr.

The type of bond suggested here would have zero value after 25 years. All figures are approximate.

See Figure 6, The School Permanent Fund/Bond Issue Plan, on the next page for a chart illustrating the concept of targeting investment earnings to pay for a critical state need. If the Fund is large enough, a portion of the bond issue could be used to pay a percentage of school building reimbursements for city and borough districts. Paying for school buildings through this method will relieve the State's general fund of some of that obligation.

Many of these recommendations are remarkably similar to those made by the author 20 years ago, in a paper proposing the Public School Fund (its name then) be turned into an endowment or permanent fund for public education. These initial recommendations, *which went nowhere*, are included in the introductory section of this paper,

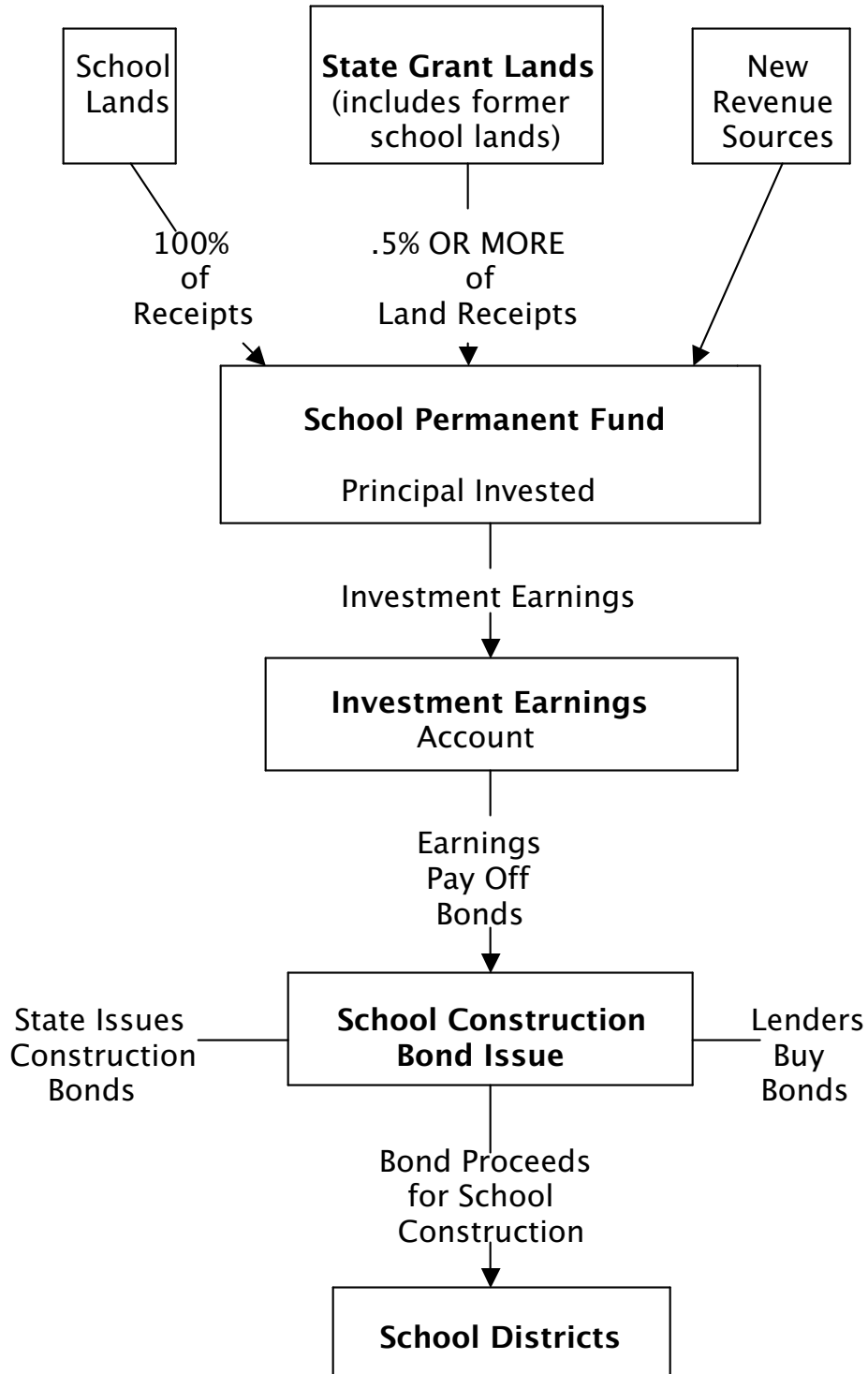
The Time for Action is Now

The situation is quite different now. *Kasayulie v. State of Alaska* has brought the Fund to the attention of many, including the education community and the legislature. The size of the Fund, \$300M and growing, guarantees it is not likely to be ignored from now on. The Court's final rulings and eventual settlement in the case will again focus attention on the Fund.

The need to protect the continued existence of the Fund should be apparent. The potential of the Fund as a stable source to meet a specific public education need must be examined, and appropriate legislation offered to stabilize and strengthen the Fund. The final recommendation to citizens, the education community, and to the legislature:

**Keep the Promise:
Save and Strengthen the Public School Trust Fund
Make It Alaska's Permanent Fund for Education**

Figure 6
The School Permanent Fund / Bond Issue Plan



Appendices

Appendix A

Alaska Public School Trust Fund Statute

Article 02. PUBLIC SCHOOL TRUST FUND

Sec. 37.14.110. Public school trust fund established.

(a) There is established as a separate endowment trust fund the public school trust fund.

(b) The principal of the fund established in (a) of this section consists of

(1) the balance of the public school permanent fund on July 1, 1978; and

(2) sums transferred under AS 37.14.150 .

(c) The commissioner of revenue shall determine the net income of the fund in accordance with investment accounting principles and in a manner that preserves the distinction between principal and income and that excludes capital gains or losses realized on principal. The principal of the fund and the capital gains or losses realized on principal shall be perpetually retained in the fund for investment purposes.

Sec. 37.14.120. Public School Fund Advisory Board created.

(a) There is created in the Department of Revenue the Public School Fund Advisory Board composed of the commissioner of education and early development, three members elected by the Board of Education and Early Development from among its membership, and the commissioner of revenue.

(b) The board created in (a) of this section shall elect a chairman from the membership of the board. Members serve without compensation but are entitled to per diem and travel expenses authorized by law for other boards.

Sec. 37.14.130. Powers and duties of board.

The board created in AS 37.14.120 has the following powers and duties:

(1) to hold regular meetings and special meetings considered necessary;

(2) to have prepared an annual accounting of the principal and income of the fund established in AS 37.14.110 ; and

(3) [Repealed, Sec. 33 ch 141 SLA 1988].

Sec. 37.14.140. Utilization of income.

The net income of the fund may not be appropriated for a purpose other than the support of the state public school program. The commissioner of revenue shall invest realized net income that has not been appropriated or that has been appropriated but not expended until the income is appropriated and expended.

Sec. 37.14.150. Contributions.

During each fiscal year the commissioner of revenue shall transfer to the fund created in AS 37.14.110 a sum equal to one-half of one per cent of the total receipts derived from the management of state land, including amounts paid to the state as proceeds of sale or annual rent of surface rights, mineral lease rentals, royalties, royalty sale proceeds, and federal mineral revenue-sharing payments or bonuses.

Sec. 37.14.160. Duties of the commissioner of revenue.

The commissioner of revenue is the treasurer of the trust fund created in AS 37.14.110 and shall

- (1) in carrying out investment duties under this section, exercise the same powers and duties established for the Alaska State Pension Investment Board in AS 14.25.180 (c);
- (2) deposit the principal and income from investments in separate principal and income accounts for the fund;
- (3) invest and maintain accounting records that distinguish between the principal and income of the fund;
- (4) provide reports to the board established under AS 37.14.120 on the condition and investment performance of the fund.

Sec. 37.14.170. Investments.

The commissioner of revenue is the fiduciary of the trust fund and shall invest the fund to provide increasing net income over long-term periods to the fund's income beneficiaries. The commissioner may invest the money in the fund on the basis of probable total rate of return to promote the long-term generation of income. In managing the trust fund, the commissioner shall

- (1) consider the status of the fund's capital and the income generated on both a current and a probable future basis;
- (2) determine the appropriate investment objectives;
- (3) establish investment policies to achieve the objectives; and
- (4) act only in regard to the financial interests of the fund's beneficiaries.

Appendix B

Resume

E. Dean Coon
11835 Spyglass Circle
Anchorage, Alaska 99515

Educational Background

1. Colorado State College of Education, B.A., 1949
2. University of Nebraska, M.A., 1951
3. University of Denver, Ed.D. 1974

Employment History

1. Sidney Nebraska Public Schools, 1949–50, high school instructor.
2. U.S. Army Medical Corps (duty station in Japan), 1951–53
3. Colorado State College, Greeley, 1953–61, editor of publications.
4. Colorado State Department of Education, 1961–73, editor/assistant commissioner/associate commissioner.
5. University of Alaska Fairbanks, 1974–85, associate professor of education & assistant director, Center for Northern Educational Research/research and teaching (school finance)/assignments varied through three UAF reorganizations/executive officer, College of Human and Rural Development.
6. Post retirement activities: UAF Summer Session Catalog editor, acting business manager of Tanana Valley Community College, supervised school administration interns in the Fairbanks Public Schools. Retained as an Expert Witness for the plaintiffs in *Kasayulie v. State of Alaska*, 1998.

Appendix C

Amendment to Increase State Contribution to Trust Fund

Senate/House Bill No. _____

IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-FOURTH LEGISLATURE – FIRST SESSION

BY (Sponsor)

Introduced: (date)
Referred: (committees)

A BILL

FOR AN ACT ENTITLED

"An Act relating to the public school trust fund; and providing for an effective date."

*Sec. 37.14.150. is amended to read:

Contributions. During each fiscal year the commissioner of revenue shall transfer to the fund created in AS 37.14.110 a sum equal to [ONE-HALF OF] one percent of the total receipts derived from management of state land, including amounts paid to the state as proceeds of sale or annual rent of surface rights, mineral lease rentals, royalties, royalty sale proceeds, and federal mineral revenue-sharing payments or bonuses.

This Act takes effect July 1, 2005.

Note: Several other statutes refer to the "one-half of one percent" and would need to be amended too.