



Idaho's Endowment Lands: A Matter of Sacred Trust

Second Edition

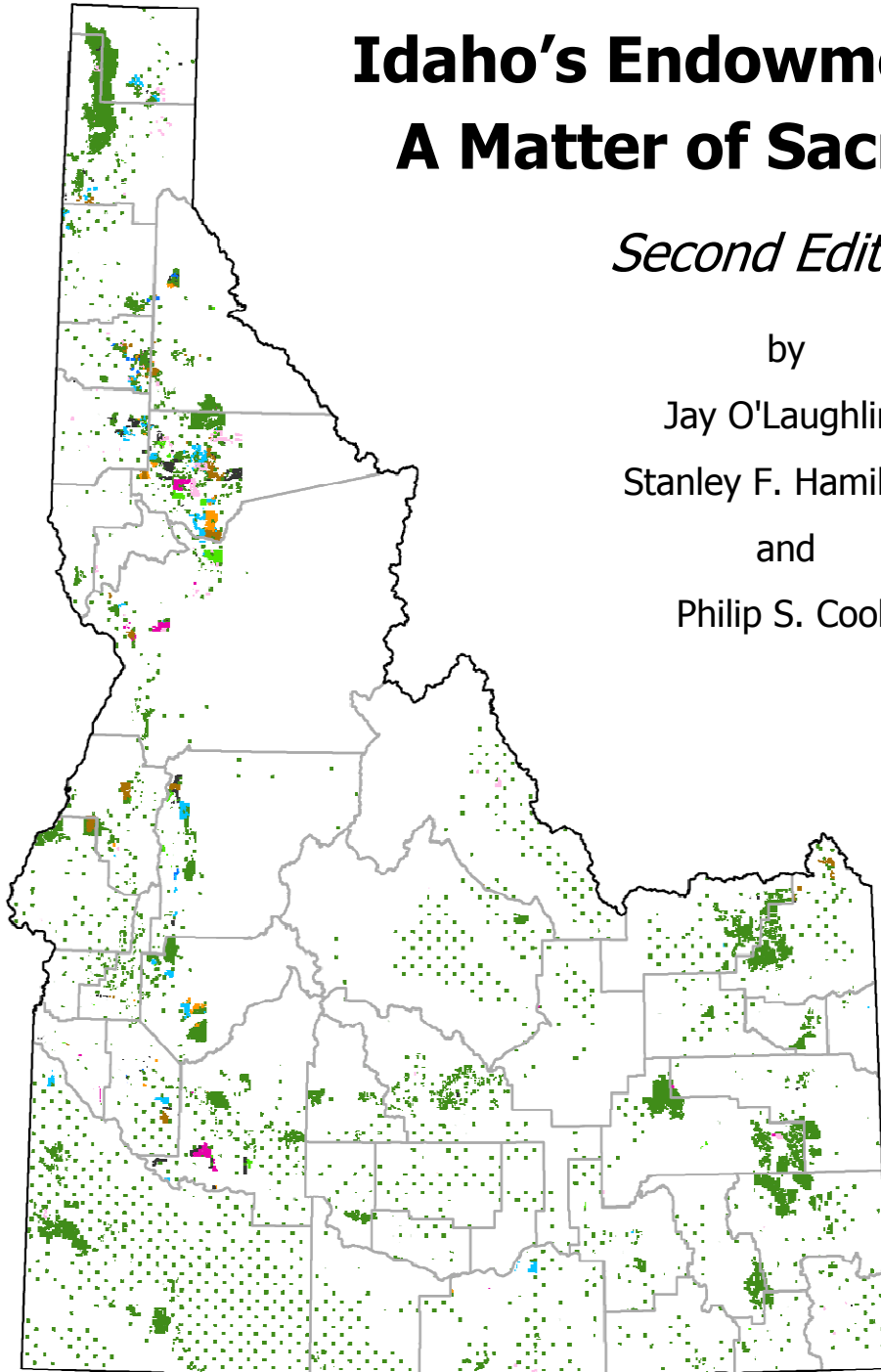
by

Jay O'Laughlin,

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and







Philip S. Cook



Endowment Institution

- Public Schools
- Agricultural College
- Charitable Institution
- Normal School
- Penitentiary
- Capitol Permanent F
- School of Science
- State Hospital South
- University of Idaho

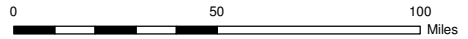
GOVERNMENTAL AGENCY LAND OWNERSHIP & SURFACE MANAGEMENT

- | | | | |
|---|---------------------------|---|-------------------------|
|  | State Endowment Land |  | US Forest Service |
|  | Misc. State Lands |  | Other Federal Ownership |
|  | Bureau of Land Management |  | Tribal Lands |

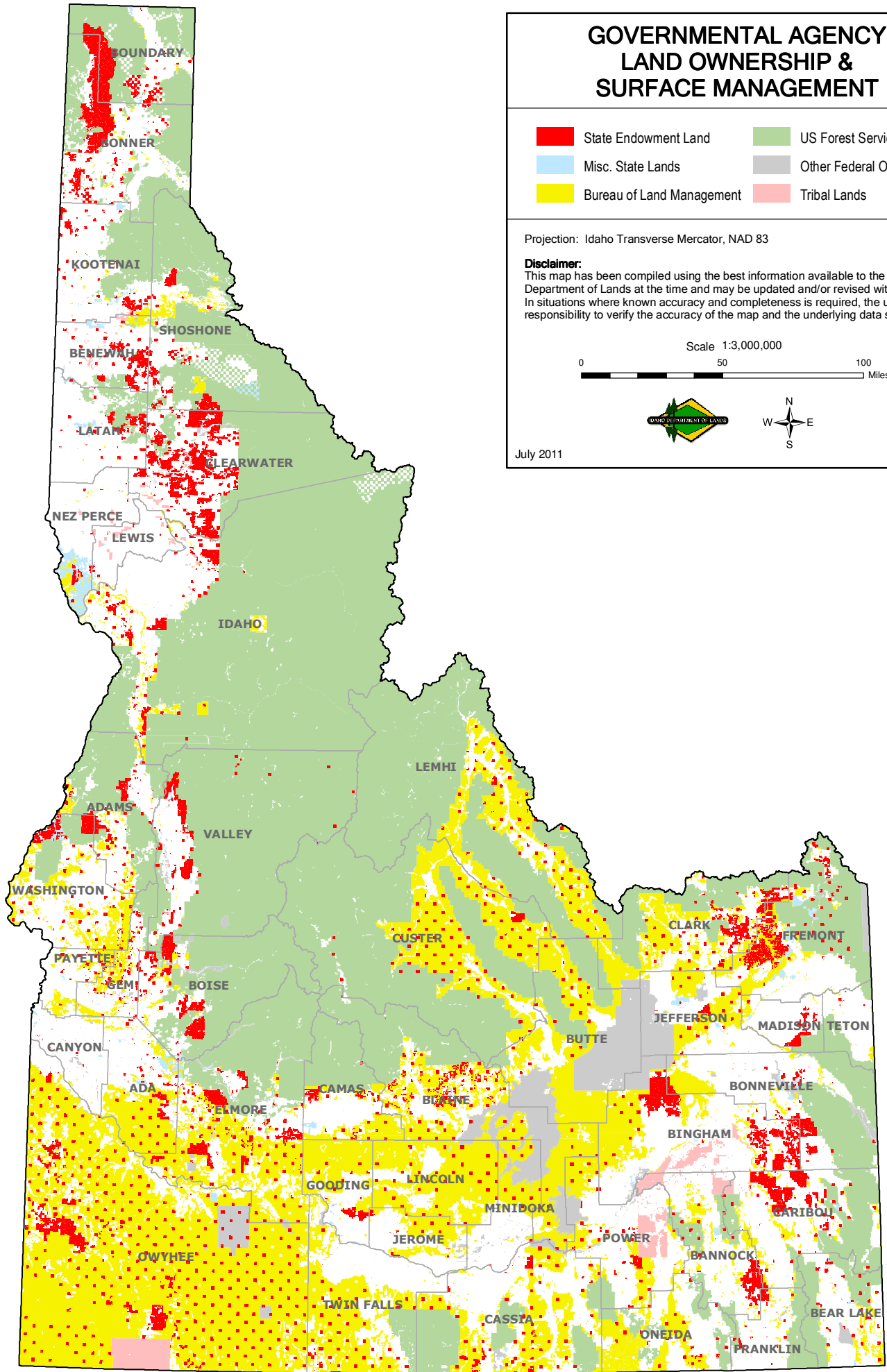
Projection: Idaho Transverse Mercator, NAD 83

Disclaimer:
This map has been compiled using the best information available to the Idaho Department of Lands at the time and may be updated and/or revised without notice. In situations where known accuracy and completeness is required, the user has the responsibility to verify the accuracy of the map and the underlying data sources.

Scale 1:3,000,000



July 2011



Idaho's Endowment Lands: A Matter of Sacred Trust

Second Edition

by

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and

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**Report No. 1, Second Edition
Policy Analysis Group
College of Natural Resources
University of Idaho**

August 2011

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About the Policy Analysis Group (PAG)

Role and Mission. The Idaho Legislature created the Policy Analysis Group (or “PAG”) in 1989 as a way for the University of Idaho to provide timely, scientific and objective data and analysis, and analytical and information services, on resource and land use questions of general interest to the people of Idaho (see Idaho Code § 38-714). The PAG is a unit of the College of Natural Resources Experiment Station, administered by Kurt Pregitzer, Director, and Dean, College of Natural Resources.

PAG Reports. This is the second edition of the Policy Analysis Group’s first report, originally published in 1990.* The PAG is required by law to report the findings of all its work, whether tentative or conclusive, and make them freely available. PAG reports are primarily policy education documents, as one would expect from a state university program funded by legislative appropriation. In addition, the PAG publishes series of **Issue Briefs** and **Fact Sheets**; listings can be found on the PAG website at <http://www.cnr.uidaho.edu/pag>

Advisory Committee. The PAG’s enabling legislation created a standing Advisory Committee (members are listed on page *iii*) and assigned it specific functions. The committee’s main charge is to review current issues and suggest topics for analysis. Based on those suggestions, the dean of the College of Natural Resources works closely with the PAG director to design analysis projects. The Advisory Committee has a responsibility to suggest the appropriate focus of the analysis. This is done iteratively, until an outline for the project is mutually agreed upon by the committee and the PAG. The outline is usually organized as a series of focus questions, and the PAG’s analytical tasks are to develop replies to the questions. The PAG uses the resources of the University of Idaho and other public and private organizations as needed. When the PAG becomes active on a project, the Advisory Committee receives periodic oral progress reports. This process defines the scope of PAG report content and provides freedom for the PAG to conduct unbiased analysis.

Technical Review. Peer review of PAG work is absolutely essential for ensuring not only technical accuracy but also impartiality and fairness. Reviewers are selected for each project by the dean and PAG director, sometimes upon recommendation of the Advisory Committee, to ensure that a wide range of expertise is reflected in the design and execution of PAG reports.

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* Listing of PAG reports and Advisory Committee members appears on page *iii*.

Advisory Committee

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Policy Analysis Group (PAG) Reports*

1. Idaho's endowment lands: A matter of sacred trust (March 1990, second edition July 2011)
2. BLM riparian policy in Idaho: Analysis of public comment on a proposed policy statement (June 1990).
3. Idaho Department of Fish and Game's land acquisition and land management program (October 1990).
4. Wolf recovery in central Idaho: Alternative strategies and impacts (February 1991).
5. State agency roles in Idaho water quality policy (February 1991, with separate Executive Summary).
6. Silver Valley resource analysis for pulp and paper mill feasibility (October 1991).
7. A national park in Idaho? Proposals and possibilities (June 1992).
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10. Idaho roadless areas and wilderness proposals (July 1993).
11. Forest health conditions in Idaho (December 1993, with separate Executive Summary).
12. Grizzly bear recovery in Idaho (November 1994).
13. Endangered Species Act at the crossroads: New directions from Idaho case studies (October 1995, with separate Executive Summary).
14. Idaho water quality policy for nonpoint source pollution: A manual for decision-makers (December 1996, with separate Executive Summary).
15. Guidelines for managing cattle grazing in riparian areas to protect water quality: Review of research and best management practices policy (December 1997).
16. History and analysis of federally administered land in Idaho (June 1998).
17. Public opinion of water pollution control funding sources in Idaho (December 1998).
18. Toward sustainable forest management: Part I – certification programs (December 1999).
19. Toward sustainable forest management: Part II – the role and effects of timber harvesting in Idaho (December 2000).
20. Taxing forest property: Analysis of alternative methods and impacts in Idaho (November 2001).
21. Endowment fund reform and Idaho's state lands: Evaluating financial performance of forest and rangeland assets (December 2001).
22. Forest resource-based economic development in Idaho: Analysis of concepts, resource management policies, and community effects (May 2003).
23. Comparison of two forest certification systems and Idaho legal requirements (December 2003).
24. Forest fire smoke management policy: Can prescribed fire reduce subsequent wildland fire emissions? (November 2004).
25. Delisting endangered species: Process analysis and Idaho case studies (October 2005).
26. Idaho's forest products business sector: Contributions, challenges, and opportunities (August 2006).
27. Off-highway vehicle and snowmobile management in Idaho (October 2008).
28. Analysis of procedures for residential real estate (cottage site) leases on Idaho's endowment lands (Oct. 2008).
29. Public land exchanges: Benefits, challenges, and potential for Idaho (December 2009).
30. Bighorn sheep and domestic sheep: Current situation in Idaho (January 2010).
31. Accounting for greenhouse gas emissions from wood bioenergy (September 2010).

*The PAG also publishes series of **Issue Briefs** and **Fact Sheets** (see www.cnr.uidaho.edu/pag).

ACKNOWLEDGMENTS

The first edition of this report was published in 1990. Technical review was provided at the time by Idaho Department of Lands staff, including especially Director Stanley F. Hamilton and Steven J. Schuster, Deputy Attorney General assigned to the department, and five University of Idaho faculty members, including two who are still active: Professor Dale Gobel, College of Law; and Professor Charles C. Harris, Jr., Department of Conservation Social Sciences.

This second edition updates the earlier report and reflects changes in policy since then, especially those put into place following amendments to the Constitution of the State of Idaho in 2000. These amendments—often referred to as “endowment reform”—reorganized the management of the financial assets in the endowment trust’s Permanent Fund and created an Earnings Reserve Fund. Linkages between the land assets and financial assets of the trust were strengthened as a result of this reorganization, and are reflected in the *State Trust Lands Asset Management Plan* approved by the State Board of Land Commissioners in 2007.

We acknowledge with gratitude the following individuals for providing technical review:

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TABLE OF CONTENTS

| | |
|--|----|
| About the Policy Analysis Group (PAG) | ii |
| Acknowledgments | iv |
| Table of Contents | v |
| List of Tables, Figures, Maps and Boxes | vi |
| Introduction | 1 |
| Purpose of Federal Land Grants | 2 |
| Territorial and Statehood Grants to Idaho | 3 |
| The Constitutional Convention | 4 |
| The “Sacred Trust” | 6 |
| Trust Asset Management Concepts, Component Parts, and Principles | 8 |
| Trust Terms—Mission Statement | 8 |
| Trust Property and Trust “Corpus”—The Endowment Assets | 10 |
| Idaho State Board of Land Commissioners—The Trustee | 12 |
| Asset Management Philosophy of the Land Board | 15 |
| Idaho Department of Lands (IDL) —The Land Manager | 16 |
| Endowment Fund Investment Board (EFIB)—The Funds Manager | 16 |
| Permanent Fund | 17 |
| Land Bank Fund | 17 |
| Earnings Reserve Fund | 17 |
| Fund Management | 17 |
| Distributions to Beneficiaries | 18 |
| Performance Reporting | 19 |
| Endowment Fund Reorganization in 2000 | 20 |
| Idaho Department of Lands’ Programs and Budget | 16 |
| The Endowment Trust Funds | 17 |
| Differences between “State Lands” and Federal Public Lands | 21 |
| Frequently Asked Questions | 23 |
| Who owns the endowment lands? | 23 |
| Who gets to use the land? | 23 |
| How much do they pay for that use? | 24 |
| Who gets the proceeds? | 25 |
| What is the scope of the Land Board’s management authority? | 25 |
| Applicable Case Law | 26 |
| United States Supreme Court | 26 |
| Sister States’ Supreme Courts | 28 |
| Conclusions | 30 |
| References Cited | 31 |
| Appendix A. Asset Classification | 34 |

LIST OF TABLES

Table 1. Federal land grants to Idaho by beneficiary institution, 1890 2
Table 2. Idaho endowment land ownership by beneficiary institution, 1890-2010 3
Table 3. Idaho endowment trust land acreage and fund value by beneficiary institution,
June 30, 2010 15
Table 4. Endowment trust land net income by program, FY-2001 to FY-2010 15
Appendix Table A-1. Endowment trust land asset classifications 15

LIST OF FIGURES

Figure 1. Idaho endowment trust assets estimated value, June 30, 2009 11*
Figure 2. Idaho endowment trust asset organization structure 12*
Figure 3. Distributions from Earnings Reserve Funds to the beneficiary institutions 20

LIST OF MAPS

Map 1. Idaho endowment lands by endowment institution front cover
Map 2. Idaho land ownership by governmental agencies inside front cover

LIST OF BOXES

Box 1. Constitutive authority for the Land Board 13
Box 2. Idaho endowment trust land management mission 16

* Figures 1 and 2 also appear in color on inside back cover.

INTRODUCTION

In 1969, the commissioner of the Idaho Department of Public Lands—a predecessor of today's Idaho Department of Lands—described in a published letter to Idaho's governor a troublesome problem the agency faced in managing the state's endowment lands:

Evidence strongly suggests a lack of public knowledge and understanding of the term “state lands.” These lands are, at times, referred to as, “public lands,” “grant lands,” “school lands,” “endowment lands,” etc. Irregardless of the term used to describe them, there appears to be a general misconception as to how they were acquired, their purpose and dedication, and their disposition.¹

By providing the people of Idaho with a guide to understanding the land grant endowment trusts administered by the Idaho State Board of Land Commissioners (Land Board) this report, like its first edition in 1990, attempts to overcome that problem. The body of assets (or “corpus”) in the endowment trusts consists of three principal assets: 2.5 million acres of land managed by the Idaho Department of Lands (IDL),² a Permanent Fund consisting of financial assets that “shall forever remain inviolate and intact,”³ and an Earnings Reserve Fund from which distributions are made to beneficiary institutions. The financial trust funds are administered by the Endowment Fund Investment Board (EFIB).⁴

Prior to Idaho statehood in 1890 the federal government granted land to the Idaho Territory for the explicit purpose of providing financial support for the state's public schools. The school land grant was confirmed at statehood, at which time other specifically designated public institutions also received land grants.⁵ The financial assets in the endowment trusts today were derived from the sale and leasing of the 3.6 million acres of original land grants. Proceeds from land sales, leases, and sales of severable assets (e.g., timber and minerals) become financial assets in the trust funds. The Land Board plays a key role as it fulfills its constitutional assignment to oversee endowment trust operations on behalf of the endowment trust's beneficiary institutions to ensure they receive “maximum long term financial return” from the trust assets.⁶

We begin this report by reviewing the **Purpose of Federal Land Grants** to the states from the federal public domain, and then focus specifically on the disposition and management of the 3.6 million acres of **Territorial and Statehood Grants to Idaho**. We include debate during **The Constitutional Convention** regarding these lands because it is germane today and helps to inform discussions regarding the trust under which these lands are held. **The “Sacred Trust”** concept that evolved out of the debate recognizes that whether Idaho sells these lands or retains them, the state has a fiduciary obligation to use the lands exclusively to provide a flow of funds to the public schools and other institutions that were designated as the sole beneficiaries of the land grants. In the **Trust Asset Management Concepts**,

¹ Idaho Department of Public Lands, *Idaho Land Grants: Acquisition, Dedication, Disposition*, Preface, letter from Commissioner Gordon C. Trombley to Governor Don Samuelson, Boise, Idaho (1969).

² Idaho Code § 58-101.

³ *Idaho Constitution*, Article IX, Section 3.

⁴ Idaho Code § 57-718.

⁵ *Idaho Admission Act*, 26 Stat. 215, ch. 656, §§ 4-14 (1890).

⁶ *Idaho Constitution*, Article IX, Section 8.

Component Parts, and Principles section we provide an overview of the institutions responsible for administering the endowment assets and their operations. We also discuss how the trust land management concept creates distinct **Differences between “State Lands” and Federal Public Lands** administered by agencies such as the U.S. Forest Service, Bureau of Land Management, or the National Park Service under statutory missions defined by the U.S. Congress. Next, this report provides answers to a set of **Frequently Asked Questions**, including who owns the endowment lands, who gets to use them, how much do they pay, and who gets the proceeds? In addition, what is the scope of the Land Board's investment authority? Some of these questions have been before the courts in other jurisdictions, so we review the **Applicable Case Law** from federal and state courts

The **Conclusion** of the report is that the overarching issue for state policymakers has remained the same since statehood: Should the land assets be retained and managed to produce streams of net income for the beneficiaries, or should the lands be sold and the proceeds invested for the beneficiaries in other types of assets? Whatever the reply is, two things are clear from case law: 1) the endowment lands were granted to Idaho for the sole purpose of supporting the public schools and other designated beneficiary institutions, and 2) the beneficiaries are entitled to receive the full value from the use and/or disposal of these lands.

For the reader's convenience, at the end of this report we provide a list of **References Cited** for books, articles, statutes, case law and other works appearing in footnotes.

PURPOSE OF FEDERAL LAND GRANTS

At one time or another the federal government held title to approximately 80% of the land in the United States.⁷ Today federal ownership of lands within the United States is about 29%.⁸ Title to the remainder of America's land once held by the federal government was granted or sold to private entities and state institutions for a variety of purposes.⁹ Most of these grants of land were provided as incentives to encourage or support the settlement of the American frontier.

In total, the largest divestiture of federal land was made when states were admitted to the Union. The grants were an attempt to promote equity and harmony among the new states and the old. The grants to the states were part of a political compromise under which newly admitted states agreed not to contest or tax the federal land holdings within their borders in exchange for grant lands.¹⁰ Grants to the states have totaled 337 million acres,¹¹ almost 15% of the nation's land. One type of grant to the states (totaling 77.6 million acres,¹² almost 3.5% of the nation's land) was for the specific purpose of supporting public education in the common schools.

⁷ U.S. Department of the Interior, Bureau of Land Management, *Public Land Statistics* (2000, Tables 1-1 and 1-3).

⁸ U.S. General Services Administration, *Federal Real Property Profile* (2004, p. 18).

⁹ U.S. Department of the Interior, Bureau of Land Management, *Public Land Statistics* (2007, p. 7).

¹⁰ Gates, Paul W., *History of Public Land Law Development*, Public Land Law Review Commission (1968, p. 317); Fairfax, Sally K., and Yale, Carolyn E., *Federal Lands*, Island Press (1987, p. 16).

¹¹ *Public Land Statistics* (2007, *supra* note 9).

¹² *Id.*

The concept of federal land grants to the states for the purpose of maintaining public schools may be traced back to Thomas Jefferson's strong belief that an educated populace is the foundation of democracy.¹³ These ideals were put into operation with the Northwest Ordinance of 1784, designed to admit territories as states on equal footing with the original thirteen colonies. The General Land Ordinance of 1785 provided for rectangular surveying of the public lands into townships to aid in dividing the land.¹⁴ President Theodore Roosevelt described the school land grants as having been "the basis for the whole system of public education" in the western states.¹⁵

Beginning in 1785 with the passing of the General Land Ordinance, each state was to be given 1/36 of the land in the territory as school lands—specifically section 16 in each thirty-six square mile township. These school land grants did not actually begin until 1803 with the admission of the state of Ohio.¹⁶ With the admission of California in 1850, grants of 1/18 of the land (sections 16 and 36) were made to the new western states in appreciation of their vastness. Idaho was granted these two sections per township at statehood in 1890 for its common schools.¹⁷

Today the states must continue to abide by the original purpose of the grant lands—to benefit the common or public schools within the state and the other specifically designated beneficiaries of the land grants. The land was given only for specific purposes defined in federal statutory laws and state constitutions. As summarized in the **Applicable Case Law** section of this report, these concepts have withstood many legal challenges.

TERRITORIAL AND STATEHOOD GRANTS TO IDAHO

The first land grant in Idaho was made under the Territorial Act of 1863,¹⁸ granting sections 16 and 36 of each township for the support of public schools, a total of almost 3 million acres¹⁹ (**Table 1**). The Territorial Act of 1883 granted 46,080 acres for the support of the State University, which in 1889 became the University of Idaho. Upon admission as a state on July 3, 1890, the federal government reconfirmed these grants,²⁰ and provided an additional 50,000 acres for the University of Idaho, plus lands for the support of seven additional institutions.²¹

¹³ Bassett, Kedric A., *Utah's School Trust Lands*, 9 J. Energy Law & Policy 195 (1989).

¹⁴ *Id.*

¹⁵ Roosevelt, Theodore, *The Winning of the West*, Current Literature Publishing Co. (1905, v. 5, p. 29).

¹⁶ Souder, Jon A., and Fairfax, Sally K., *State Trust Lands: History, Management and Sustainable Use*. University of Kansas Press (1996).

¹⁷ Later, Utah (1896) and New Mexico and Arizona (1912) received four sections per township. According to Bassett (1989, *supra* note 13), this was due to the arid, and presumably less valuable, land in those territories.

¹⁸ Idaho State Board of Land Commissioners, *State Trust Lands Asset Management Plan* (2007).

¹⁹ Public school acreage was determined by assuming 1/18 of the total area of the state (53,688,320 acres) as published in the June 30, 1931, annual report of the General Land Office.

²⁰ *Idaho Admission Act*, 26 Stat. 215, ch. 656, § 4 (1890).

²¹ *Id.* §§ 6, 8-11.

Table 1. Federal land grants to Idaho by beneficiary institution, *Idaho Admission Act* (1890).

| Beneficiary Institution | Acres Granted |
|------------------------------------|---------------|
| Public Schools | 2,982,683 |
| Public Buildings | 32,000 |
| State University located at Moscow | 96,080 |
| Agricultural College | 90,000 |
| Charitable Institutions | 150,000 |
| Insane Asylum located at Blackfoot | 50,000 |
| Normal Schools | 100,000 |
| Penitentiary located at Boise City | 50,000 |
| School of Science | 100,000 |
| Total | 3,650,763 |

Because many of the sections of land granted for the support of the public schools were already in private ownership prior to statehood, the *Idaho Admission Act* authorized the state to select replacement lands from the public domain. These were called “lieu lands” then and now. Many of the granted lands were within the Forest Reserves created in 1891 (now part of the National Forest System), so the state was authorized to select lieu lands from the public domain in other locations. Initially, Idaho chose to concentrate on selecting high-valued agricultural and grazing lands with the intention of selling them. Timberlands were selected with the intention of removing the timber and then selling the land as agricultural or grazing lands.²²

THE CONSTITUTIONAL CONVENTION

In 1889, the framers of the Idaho Constitution faced a dilemma. Statehood required a formal constitution that, among other things, had to address the disposition of the federal land grants. How should Idaho go about using the land endowment given to the state to support its public schools and other institutions? Lively discussion at the Constitutional Convention focused on this matter.²³

Some argued that the state should sell the land, invest the principal, and use the interest to support the schools and institutions:

Now if this land could be sold at what would be a fair price, if it could be converted into money, we would get something from it, and further than that, it would pass into the hands of those who would have to pay taxes, for which we get no taxation now.²⁴

²² Idaho State Planning Board, *A Preliminary Report on Management of State-Owned Lands in Idaho*. Technical Advisory Committee on Land Management, Idaho State Planning Board (1940). Cited in *State Trust Lands Asset Management Plan* (2007, *supra* note 18).

²³ *Idaho Constitutional Convention Proceedings*, discussion of Article IX, Section 8, “Location and disposition of public lands” (1889, Vol. I, pp. 637-670, 703-712, 729-765).

²⁴ *Id.*, p. 732 (Mr. Gray).

Others argued that the state should hold the land forever, and obtain benefits by leasing the agricultural, grazing, and mineral lands, and by selling timber from time to time. Debate also focused on the difficulty of determining the value of the grant lands:

[T]hese school lands should remain to perpetuate the school fund, preserving a nucleus around which we may collect something for not only ourselves who live now, but for those who shall come after us.²⁵

[T]his territory seems so wide, and there is so much vacant and unoccupied land lying all around us, that we despise the possessions which Uncle Sam in his liberality has given us to hold in trust for our children. I say that neither I nor you have any definite idea of what this land is worth today which lies under the sun of Idaho or what it is going to be worth in the future.²⁶

The dilemma faced by the framers of the *Constitution of the State of Idaho* was resolved through compromise—up to a specified amount of land could be sold annually at a price exceeding an established minimum, and the remainder would be retained and managed by the state, with leases and sales of severable assets such as minerals and timber allowed.²⁷ In order to protect the trust assets, however, the Constitution required that lands be disposed of at public auction.²⁸ The amount of land that could be sold annually and the selling price have changed several times throughout Idaho's history. A provision for the exchange of land was ultimately added, but not until almost a century later.²⁹

To protect the value of the trust for future generations, the *Idaho Admissions Act* required that proceeds from the sale of the school lands be deposited into a permanent endowment fund.³⁰ The *Constitution of the State of Idaho* requires that the Permanent Fund “shall forever remain inviolate and intact.”³¹

Idaho began selling land immediately, and today approximately two-thirds of the original 3.6 million acres of land grants remain. Between 1900 and 1940 more than 700,000 acres were sold (**Table 2**), including almost 450,000 acres sold between 1911 and 1920. When the opportunity is appropriate, the state will engage in land trades.³² Over the past 60 years some acreage has been added to the trusts through land sale contract forfeitures, loan foreclosures, and land exchanges, but more acreage was sold from the endowment trusts than was added to them.

The method of granting to the public schools sections 16 and 36 in each township resulted in scattered and disjointed parcels (**Map 1**, see outside front cover), as endowment lands were intermingled with private and federal ownership so as to create a “checkerboard” pattern,

²⁵ *Id.*, p. 709 (Mr. Vineyard).

²⁶ *Id.*, p. 706 (Mr. Parker).

²⁷ *Idaho Constitution*, Article IX, Section 8; *Idaho Admission Act*, 26 Stat. 215, ch. 656, § 5 (1890).

²⁸ *Idaho Constitution*, Article IX, Section 8.

²⁹ To provide legal authority for land exchanges, Section 5(b) was added to the *Idaho Admission Act* in 1974, and Article IX, Section 8 of the *Constitution of the State of Idaho* was amended in 1982.

³⁰ *Idaho Admission Act*, 26 Stat. 215, ch. 656, § 5 (1890).

³¹ *Idaho Constitution*, Article IX, Section 3.

³² See Cook, Philip S., and O’Laughlin, Jay, *Public Land Exchanges: Benefits, Challenges, and Potential for Idaho*. University of Idaho (2009).

particularly in southwestern Idaho (**Map 2**, see inside front cover). Some large trust land ownership blocks have been created through “lieu land” selections and land exchanges with other land owners (see **Map 1**). Larger blocked-up holdings can facilitate management efficiency and potentially result in more returns, depending on the type of land asset and opportunities to create multiple revenue streams, and the potential for lands to shift into higher and better, and thus more valuable, land uses in the future.

Table 2. Idaho endowment land ownership by beneficiary institution, 1890-2010 (acres).

| Beneficiary Institution | 1890 | 1940 | 2010 |
|-------------------------------|------------------|------------------|------------------|
| Public Schools | 2,982,683 | 2,543,962 | 2,080,249 |
| Agricultural College (U of I) | 90,000 | 42,836 | 33,526 |
| Charitable Institutions* | 150,000 | 86,085 | 77,211 |
| Normal School† | 100,000 | 53,389 | 60,046 |
| Penitentiary | 50,000 | 34,051 | 29,067 |
| School of Science (U of I) | 100,000 | 74,714 | 75,875 |
| State Hospital South‡ | 50,000 | 30,315 | 31,414 |
| University of Idaho | 96,080 | 51,316 | 54,646 |
| Public Building (Capitol) | 32,000 | 14,719 | 7,222 |
| Total | 3,650,763 | 2,931,387 | 2,449,255 |

* Idaho State University, Industrial Training School, State Hospital North, Idaho Veterans Homes, and the School for the Deaf and Blind.

† Idaho State University Department of Education and Lewis-Clark State College.

‡ Grant was to the “Insane Asylum” and later renamed State Hospital South.

THE “SACRED TRUST”

During the deliberations at the Idaho Constitutional Convention, the term “sacred” was used to refer to the school trust fund:

[N]o fund is more sacred than the school fund, and perhaps there is no other fund so sacred; it should be guarded in every manner possible, and by having this provision in here, the children will always be made sure there will be that much money to their credit, and we will have that much at stake in our schools. But if there is no provision for making this fund good in every way, it may be squandered, and the first thing we know our school fund will be so small that we can only maintain the schools by local taxation. I think the legislature can provide for making good any losses which may occur. They will probably be more careful in making investments if it is known that the state has to make good.³³ [Emphasis added.]

³³ *Idaho Constitutional Convention Proceedings* (1889, Vol. I, p. 647, Mr. McConnell); quoted in *Moon v. Investment Board*, 96 Idaho 140, 143 (1974).

“Sacred trust” has become a convenient phrase used to describe the obligations on the part of the state.³⁴ These duties stem from the *Idaho Admission Act*,³⁵ and the *Constitution of the State of Idaho*,³⁶ even though the term “sacred trust” is not used in either law. “Sacred trust” continues to be used to describe the obligation on the part of the State of Idaho with respect to school grant lands and the proceeds from school lands that are held in the “sacred trust fund.”³⁷ Indeed, “the Fund is a trust of the most sacred and highest order.”³⁸ Furthermore,

[A]dministration of endowment lands and monies derived from them has been termed a sacred trust by the high courts. . . . Endowment lands have truly become a sacred trust to be managed and perpetuated for the benefit of Idaho's youth and institutions.³⁹

Although the term “sacred trust” may be unique to Idaho, the underlying concept is not. Numerous federal cases concerning disposition and management of school land grants have helped to define the “sacred trust” obligation.⁴⁰ For example, in *Andrus v. Utah*,⁴¹ the United States Supreme Court in 1980 characterized the school land grants as a “solemn agreement” between the U.S. Congress and the state. According to one interpretation of the case, “The school land grant and its acceptance by the state constitutes a solemn compact between the United States and the state for the benefit of the state's public school system.”⁴² In a 1968 case in eastern Washington,⁴³ the federal district court stated:

There have been intimations that school land trusts are merely honorary, that there is a “sacred obligation imposed on (the state's) public faith,” but no legal obligation. These intimations have been dispelled by [the U.S. Supreme Court in] *Lassen v. Arizona*. . . . This trust is real, not illusory.⁴⁴

Regardless of the phrase used to describe it, the trust agreement—as statutorily defined in state admission acts and constitutions and reaffirmed by subsequent case law decisions—obliges the state to limit its actions concerning the endowment trust lands and to treat the proceeds from those grant lands with extraordinary care. As the Idaho Supreme Court has repeatedly stated, the Land Board “must find authority in the constitution and statute for its acts.”⁴⁵

³⁴ See *State v. Peterson*, 61 Idaho 50, 53, 57, 97 P.2d 603 (1939).

³⁵ *Idaho Admission Act*, 26 Stat. 215, ch. 656, §§ 4, 6, 8, 9, 10 and 11 (1890).

³⁶ *Idaho Constitution*, Article IX “Education and School Lands.”

³⁷ *United States v. Fenton*, 27 F.Supp. 816 (D. Idaho 1939).

³⁸ *State ex rel. Moon v. State Bd. of Examiners*, 104 Idaho 640, 642 (1983).

³⁹ Idaho Dept. of Public Lands and Idaho Dept. of Education, *Endowment Lands of Idaho* (Boise, Idaho, ca. 1969, unpagged).

⁴⁰ For in-depth discussion of states' trust obligations see O'Day, Sean E., *School Trust Lands: The Land Manager's Dilemma Between Educational Funding and Environmental Conservation, a Hobson's Choice*, 8 N.Y.U. Envtl. L.J. (1999, p. 163).

⁴¹ *Andrus v. Utah*, 446 U.S. 500 (1980), *reh'g denied*, 448 U.S. 907 (1981).

⁴² Bassett (1989, *supra* note 13, p. 206).

⁴³ *United States v. 111.2 Acres of Land in Ferry County Washington*, 293 F.Supp. 1042 (E.D.Wash. 1968), *aff'd*, 435 F.2d 561 (9th Cir. 1970), citing *Lassen v. Arizona ex rel. Arizona Highway Dept.*, 385 U.S. 458 (1967).

⁴⁴ *Id.* at 1049; *Lassen v. Arizona* is discussed in **Applicable Case Law** section.

⁴⁵ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP I), 128 Idaho 761,765, 918

TRUST ASSET MANAGEMENT CONCEPTS, COMPONENT PARTS, AND PRINCIPLES

A trust is a legal entity involving a fiduciary relationship in which the trustee holds and manages property for the benefit of a specific beneficiary. The major fiduciary obligation of the trustee is to act with undivided loyalty to the beneficiary, with strict honesty and candor.⁴⁶ The trust is a system to produce revenues for the beneficiaries consisting of three parts: management, the trust properties or assets (often called the “corpus”), and the revenues produced by managing the trust corpus, which includes the land base and permanent funds.⁴⁷

Three elements must be present in any trust. First, there must be an expression of intent. No trust is created unless the trust settlor (i.e., the person[s] establishing the trust) expresses an intention to impose duties upon the trustees that are enforceable in the courts. Second, there must be a beneficiary. If the beneficiary cannot be ascertained, no trust is created. Finally, there must be a property interest that exists or is ascertainable and is to be held for the benefit of the beneficiary.⁴⁸ Discussion of the settlor’s intention and the trust property is provided in the next two sections of this report. The beneficiaries of the endowment assets were identified earlier (see **Map 1** and especially **Table 2**). Chief among the beneficiary institutions is the public schools, with 85% of the endowment lands in the trust for the public schools.

The legalese pertaining to the elements of a trust can be translated into a few principles that serve as general guides for managing land under the trust concept: clarity, accountability, enforceability, perpetuity, and prudence.⁴⁹ Clarity is established in the trust terms in a mission statement (see **Trust Terms—Mission Statement** section following). Accountability is the requisite reporting of financial transactions by the manager and trustees to the beneficiaries. As in all trusts, enforceability is ultimately attained through judicial proceedings following a challenge by beneficiaries, or those with standing to represent the beneficiaries.⁵⁰ The principle of providing benefits in perpetuity is analogous with sustainable resource management.⁵¹ Under trust law managers and trustees must offer evidence that they have acted prudently to meet the mandate expressed in this statement of intention.

TRUST TERMS—MISSION STATEMENT

The terms of the trust are established by the settlor as an expression of intent when the trust is created. In this case, the United States of America is the settlor and terms were established in the *Idaho Admissions Act*. The terms express the settlor’s intention to impose duties upon the trustees that are enforceable in the courts. The clarity of the trust terms as expressed in a mission statement is a key characteristic of trust principles, and can be devised to answer

P.2d 1206, 1210 (1996) citing *Balderston v. Brady*, 17 Idaho 567, 107 P. 243 (1910).

⁴⁶ Souder and Fairfax, *State Trust Lands* (1996, *supra* note 16).

⁴⁷ *Id.*, p. 37.

⁴⁸ *Id.*, p. 3.

⁴⁹ Fairfax, Sally K. *Lessons for the Forest Service from State Trust Land Management Experience*. Discussion Paper 99-16, Resources for the Future, Washington, D.C. (1999).

⁵⁰ Souder and Fairfax, *State Trust Lands* (1996, *supra* note 16, *passim*).

⁵¹ Souder and Fairfax, in *State Trust Lands* (1996, *supra* note 16, pp. 276-282), argue that the trust land management model is appropriate for sustainable resource management.

the questions who, what, where, why, when, and how. The mission statement establishes a firm foundation for decision making on the part of the trustees and the trust managers, and also makes them accountable to the beneficiaries.⁵²

The mission statement for Idaho's endowment lands as expressed in the *Constitution of the State of Idaho* is quite specific. The mission statement requires the Idaho State Board of Land Commissioners (Land Board) as trustee to manage the endowment lands

“. . . in such manner as will secure the maximum long term financial return to the institution to which granted . . .”⁵³

Under this constitutional mandate, endowment lands are “held in trust”⁵⁴ and managed to produce financial returns (i.e., revenues minus expenses, or net income) for the specified beneficiaries in such a manner that will maintain its usefulness and productivity for current and future beneficiaries. In *Idaho Watersheds Project II* the Idaho Supreme Court stated:

Article IX, § 8 [of the *Constitution*] provides that the objective of sales and leases of state endowment lands is to “secure the maximum long term financial return to the institution to which granted or to the state if not specifically granted.” This is in keeping with the *Idaho Admission [Act]* admitting Idaho into the union,⁵⁵ which indicates that monies received from the sale or lease of school endowment lands “shall be reserved for school purposes only.”⁵⁶

This duty applies to the Legislature as well as the State Board of Land Commissioners:

Article IX, § 8 [of the *Constitution*] requires the Legislature to “provide by law that the general grants of land made by congress to the state shall be judiciously located and carefully preserved and held in trust, subject to disposal at public auction for the use and benefit of the respective object for which said grants of land were made”.⁵⁷ [Emphasis added.]

As is clear from the quotations above, both the Land Board and the Legislature not only have constitutive authority to use the land to produce financial returns for the public institutions designated as beneficiaries, they have an affirmative duty to do so.⁵⁸

⁵² Souder and Fairfax, *State Trust Lands* (1996, *supra* note 16).

⁵³ *Idaho Constitution*, Article IX, Section 8.

⁵⁴ *Id.*

⁵⁵ *Idaho Admission Act*, 26 Stat. 215, ch. 656, § 5(a).

⁵⁶ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP II), 133 Idaho 64, 67, 982 P.2d 367, 370 (1999).

⁵⁷ *Id.*

⁵⁸ For discussion of “maximum long-term financial return” as a “target” rather than “a substantive requirement to do anything measurable by any objective calculation” see Ryberg, Erik, *Comedy of Errors or Confederacy of Dunces? The Idaho Constitution, State Politics, and the Idaho Watersheds Project Litigation*, 40 Idaho Law Review (2003, p. 187); for discussion of flexibility in endowment lands management see Fairfax, Sally K., et al., *The School Trust Lands: A Fresh Look at Conventional Wisdom*, 22 Environmental Law (1992, p. 797); also Souder and Fairfax, *State Trust Lands* (1996, *supra* note 16, pp. 159-167).

TRUST PROPERTY AND TRUST "CORPUS"—THE ENDOWMENT ASSETS

The body of assets that comprise Idaho's endowment trust corpus consists of three main parts: the land asset consisting of 2.5 million acres of properties in the endowment trust managed by the Idaho Department of Lands (IDL), and the Permanent Fund and the Earnings Reserve Fund managed by the Endowment Fund Investment Board (EFIB). The operations of each are explained in later sections: **Idaho Department of Lands (IDL)—The Land Manager** and **Endowment Fund Investment Board (EFIB)—The Funds Manager**.

A trust has been created for each of the nine beneficiary institutions. At almost 2.1 million acres, the public school land assets represent 85% of the total endowment trust land acreage (see **Map 1**, front cover of this report). The other beneficiary institutions received smaller grants of land that were selected from public domain lands (see **Table 2** above). **Table 3** identifies the current status of all endowment assets by beneficiary institution.

Table 3. Idaho endowment trust land acreage and fund value by beneficiary institution, June 30, 2010.

| Beneficiary Institution | Acres Owned | Permanent Fund | Earnings Reserve |
|-------------------------------|-------------------|----------------------|----------------------|
| Public Schools | 2,080,249 | \$583,075,344 | \$91,121,257 |
| Agricultural College (U of I) | 33,526 | 16,157,761 | 3,790,486 |
| Charitable Institutions* | 77,211 | 54,309,545 | 12,157,408 |
| Normal School† | 60,046 | 49,368,782 | 13,631,327 |
| Penitentiary | 29,067 | 19,948,737 | 4,845,589 |
| School of Science (U of I) | 75,875 | 54,679,953 | 15,289,531 |
| State Hospital South | 31,414 | 36,907,750 | 11,372,165 |
| University of Idaho | 54,646 | 44,095,165 | 13,106,533 |
| Capitol | 7,222 | 16,992,507 | § |
| Total | 2,449,256‡ | \$875,535,344 | \$165,314,276 |

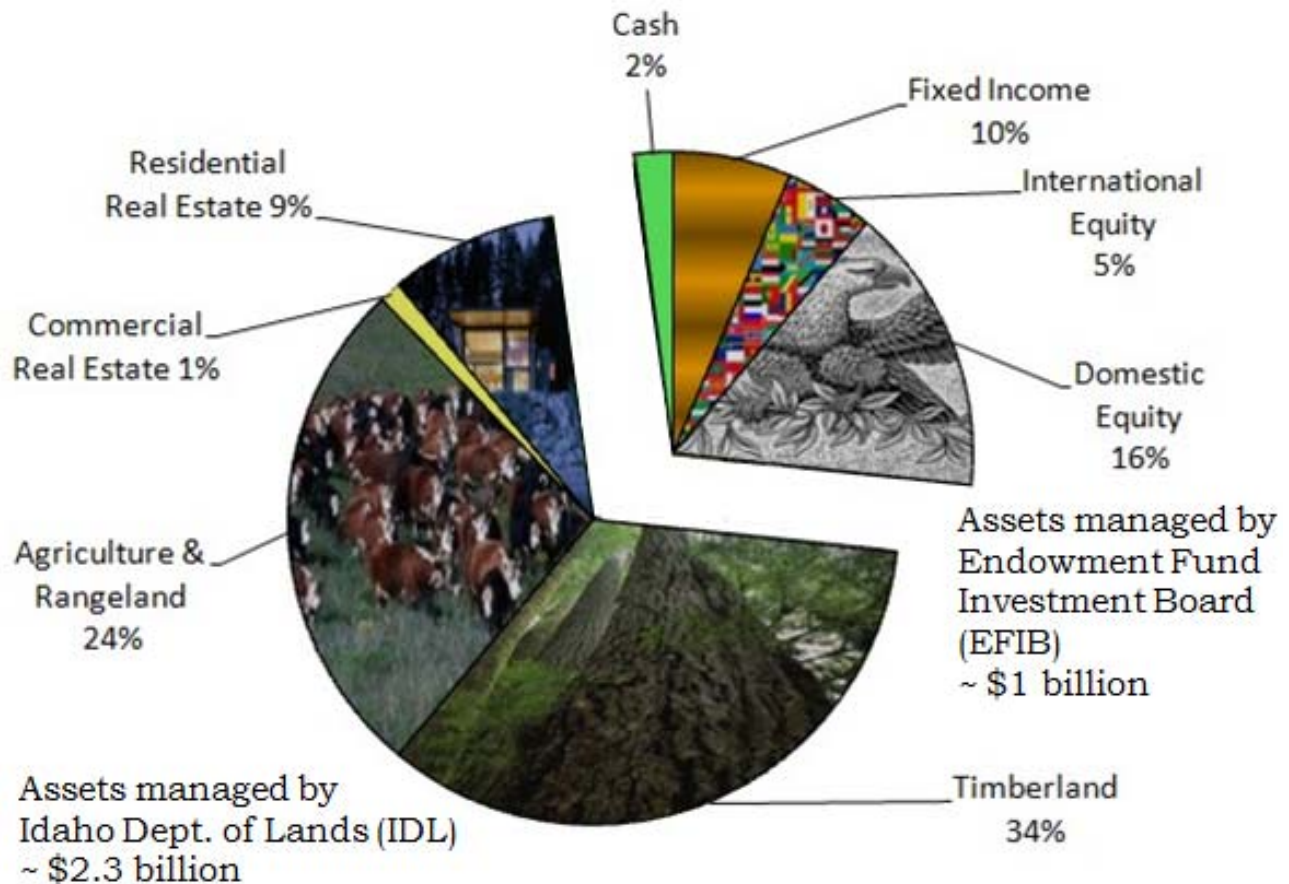
* Idaho State University, Industrial Training School, State Hospital North, Idaho Veterans Homes, and the School for the Deaf and Blind.

† Idaho State University Department of Education and Lewis-Clark State College.

‡ Estimated value of the real estate assets is \$2.3 billion.

§ Capitol trust does not have an Earnings Reserve Fund.

Each of the nine trusts in **Table 3** owns a mixture of investments similar to the aggregate holdings of all trusts in **Figure 1** (next page and inside back cover in color). The land asset represents 2/3 the value of the trusts from which more than 70% of the gross annual trust revenue is generated by land management activities. The current fair market value of all trust assets for all beneficiary institutions is estimated to exceed \$3 billion dollars.

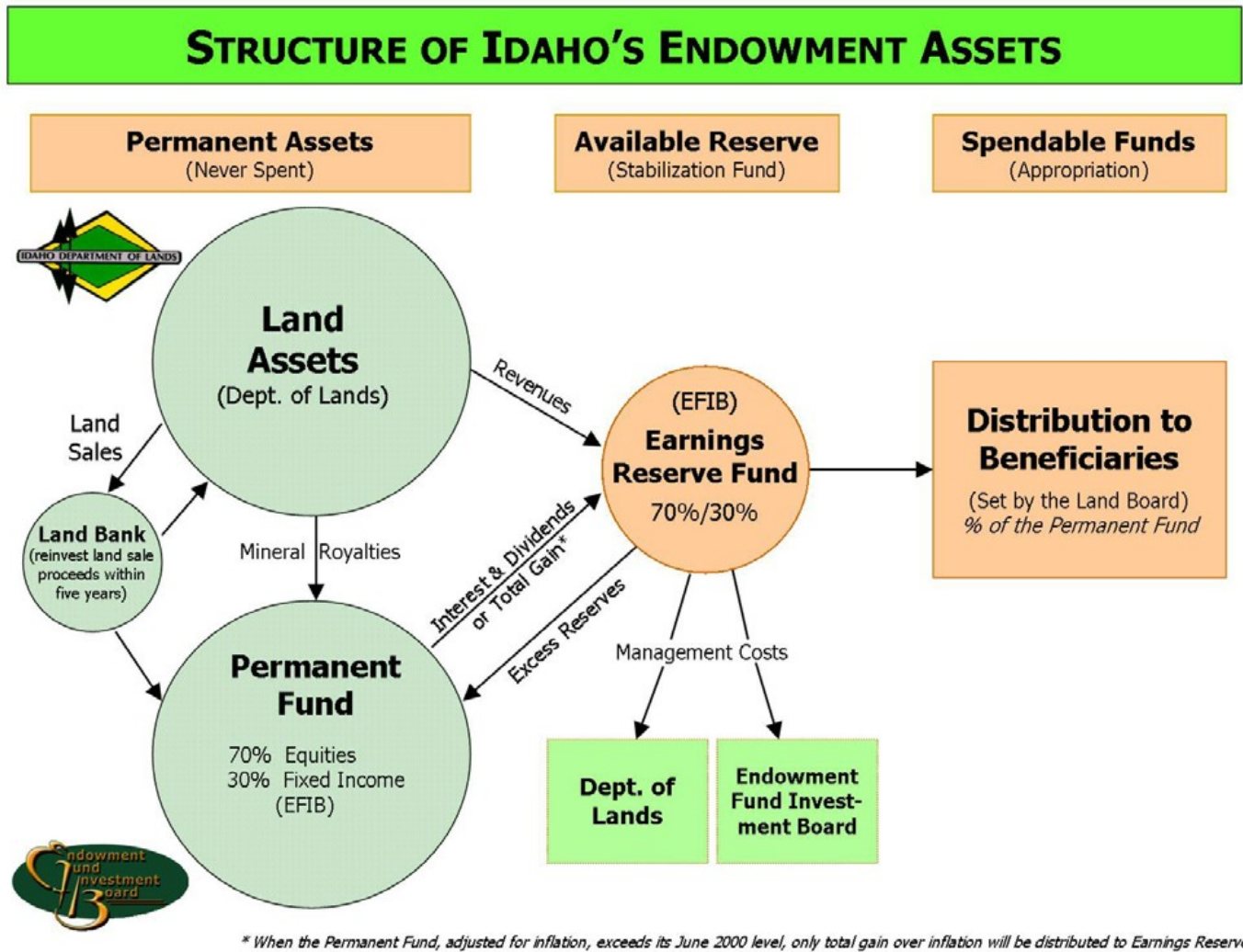
Figure 1. Idaho Endowment Trust Assets Estimated Value, June 30, 2009.

Source: Idaho Department of Lands, Director's Office.

Each of the nine endowment (with the exception of the Capitol Permanent Fund) has two types of assets: permanent assets, which can never be distributed, and a reserve or buffer fund from which distributions can be made. The permanent assets consist of endowment land properties and a Permanent Fund. **Figure 2** (next page, and inside back cover in color) illustrates the flow of money between land management operations and the two financial asset trust funds, explained in brief as follows. Renewable revenues from the land (e.g., timber harvest and rental or lease income) and income from the financial investments of the Permanent Fund flow into the Earnings Reserve Fund. Payments of asset management expenses and beneficiary distributions are made from the Earnings Reserve Fund. If the Earnings Reserve Fund balance should fall to zero, then distributions must stop because the principal of the Permanent Funds can never be distributed.⁵⁹ A more thorough explanation is provided in a later section titled **Endowment Fund Investment Board (EFIB)—The Funds Manager**.

⁵⁹ Idaho State Board of Land Commissioners, *State Trust Lands Asset Management Plan* (2007).

Figure 2. Idaho Endowment Trust Asset Organization Structure.



Source: Endowment Fund Investment Board, *Financial Statements for the Fiscal Year Ended June 30, 2010*.

IDAHO STATE BOARD OF LAND COMMISSIONERS—THE TRUSTEE

The Idaho State Board of Land Commissioners (Land Board) serves as the trustee for the endowment lands and consists of five elected officials (see **Box 1**).⁶⁰ The director of the Idaho Department of Lands is secretary to the Land Board. Drawing from its constitutive authority (see **Box 1**), the Land Board is the trustee for Idaho's endowment assets. The Land Board sets policy, oversees the land management programs, and authorizes disposals of the land base such as sales and leases. The Land Board "must find authority in the constitution and statute for its acts."⁶¹

⁶⁰ *Idaho Constitution*, Article IX, section 7.

⁶¹ *Balderston v. Brady*, 17 Idaho at 585, 107 P. at 499 (1910), cited in *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP I), 128 Idaho 761, 818 P2d. 1206 (1996).

Box 1. Constitutive Authority for the Land Board

State Board of Land Commissioners. “The governor, superintendent of public instruction, secretary of state, attorney general and state controller shall constitute the state board of land commissioners, who shall have the direction, control and disposition of the public lands of the state, under such regulations as may be prescribed by law.” *Constitution of the State of Idaho*, Article IX, Section 7; this board is commonly referred to as the Land Board.

“The land board is not a court of equity; it is an executive board charged with duties that must be executed in conformity with law.” *Balderston v. Brady*, 17 Idaho 567, 107 P. 493 (1910).

“The state board of land commissioners are trustees or business managers for the state in handling state lands. The board may act only as prescribed by law.” *Pike v. State Board of Land Commissioners*, 19 Idaho 268, 113 P. 447 (1911).

“The board is a constitutional agency charged with the administration of a public trust and vested with certain discretionary power, in the exercise of which it acts quasi-judicially.” *Barber Lumber Co. v. Gifford*, 25 Idaho 654, 139 P. 557 (1914).

When managing and administering the endowment lands, the state, as represented by the Land Board, must as a matter of basic trust law comply with the same fiduciary obligations as apply to private trustees. The Land Board is therefore constrained to look strictly at the interests of the endowment beneficiaries rather than the general public interest.⁶²

Considering the interests of other organizations, causes, or public interests—no matter how worthy they may be—would be a breach of the Land Board’s fiduciary duty to serve the interests of the beneficiaries.⁶³

The management concept that guides the Land Board is to generate the “maximum long term financial return”⁶⁴ for the nine beneficiaries of the trusts (see **Table 3**) for whom the board acts as trustee. The “maximum long term financial return” mandate can be unpopular with segments of the Idaho populace. Some people feel that state lands should be managed for the benefit of the general public by providing for public uses that do not provide revenue, such as free recreation; or for the benefit of individuals or groups other than the beneficiaries prescribed in law, such as grazing permittees or cabin site lessees; or at something less than maximum financial return in order to serve other public purposes, such as educational experiences that would reduce revenues and financial returns.⁶⁵

⁶² See *Moon v. State Bd. of Land Comm’rs*, 111 Idaho 389, 393, 724 P.2d 125 (1986); also *County of Skamania v. State*, 102 Wn.2d 127, 685 P.2d 576 (1984). For discussion of challenges that arise with elected officials serving as trustees, see Culp, Peter W., et al., *State Trust Lands in the West: Fiduciary Duty in a Changing Landscape*, Lincoln Institute of Land Policy (2006).

⁶³ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP II), 133 Idaho 64, 982 P.2d 367 (1999) held that the Legislature is also precluded from directing the Land Board to consider interests other than the endowment beneficiaries.

⁶⁴ *Idaho Constitution*, Article IX, Section 8.

⁶⁵ Regarding plaintiff’s lack of standing, see *Selkirk-Priest Basin Assoc., Inc. v. Idaho*, 127 Idaho 239,

Idaho courts have affirmed three key points concerning the Land Board. First, the Land Board is a trustee or business manager acting on behalf of the state. In *Pike v. State Board of Land Commissioners*,⁶⁶ the court in 1911 said

In the first place, the constitution (Article IX, Section 8) vests the control, management and disposition of state lands in the state board of land commissioners. They are, as it were, the trustees or business managers for the state in handling these lands, and on matters of policy, expediency and the business interest of the state, they are the sole and exclusive judges so long as they do not run counter to the provisions of the constitution or statute.⁶⁷

Second, the Land Board may exert certain discretionary authority in carrying out its trust obligations.⁶⁸ In *Barber Lumber Co. v. Gifford*,⁶⁹ a case heard by the Idaho Supreme Court in 1914, the Land Board accepted the Barber Lumber Company's bid of \$100,000 for the sale of timber from endowment lands when another bidder, Mr. Snow, had offered \$101,000. The court determined that in a sale of timber, under the circumstances in this case, the state is "financially interested in making the sale of such timber as advantageous to the state as possible."⁷⁰

Although Barber Lumber Co. was not the high bidder, the Land Board felt that the state would be financially advantaged because Barber Lumber Co. intended to build roads and a railway to access the timber, and Mr. Snow did not. The court ruled that the board had properly exercised its authority by rejecting Mr. Snow's higher bid in this case, and stated that "in consideration of other vast benefits that would occur to the state and its endowment funds which, in the opinion of the board, would be far in excess of the value of \$1,000 offered by Mr. Snow over the Barber Lumber Co."⁷¹

Furthermore, the court affirmed that "the land business of the state placed in the hands of the state board of land commissioners ought to be conducted on business principles so as to subserve the best interests of the people of the state,"⁷² and "it is clear that the state board has acted in this matter only as a man of good business sense and judgment would act in regard to his own affairs."⁷³

899 P.2d 949 (1995).

⁶⁶ *Pike v. State Board of Land Commissioners*, 19 Idaho 268, 113 Pac. 447 (1911).

⁶⁷ *Id.*

⁶⁸ For a discussion of the limits of the Land Board's discretion, particularly in the awarding of grazing leases, see Ryberg (2003, *supra* note 58); see also *Lazy Y Ranch, Ltd. v. Behrens*, 546 F.3d 580 (9th Circuit 2008).

⁶⁹ *Barber Lumber Co. v. Gifford*, 25 Idaho 654, 139 Pac. 557 (1914).

⁷⁰ *Id.* at 670.

⁷¹ *Id.* at 663.

⁷² *Id.* at 669.

⁷³ *Id.* at 668.

Third, the Board only has authority to act as provided by the constitution and duly enacted statutes. As the Idaho Supreme Court held when it struck down Idaho Code § 58-310B in *Idaho Watersheds Project II*, the Legislature has no authority to direct the Land Board to ignore its fiduciary duty to the beneficiaries:

We acknowledge that “[t]he Board is granted broad discretion in determining what constitutes the maximum long term financial return for the schools.” . . . [Idaho Code] Section 58-310B removes much of the Board’s broad discretion, however, by impermissibly directing the Board to focus on the schools, the state, and Idaho livestock industry in assessing lease applications, all to the detriment of other potential bidders like IWP [Idaho Watersheds Project], which might provide “maximum long term financial return” to the schools, but not the state and the Idaho livestock industry.⁷⁴

Asset Management Philosophy of the Land Board

Creation of an asset management plan is an important step for any private or public institutional investment manager. Asset management plans are used to ensure assets can be managed, preserved and protected for long-term goals and strategy and to define overarching beliefs and philosophy about a set of collective investments. Such plans also include elements of financial analysis, asset selection (and divestiture), asset allocation (diversification), plan implementation and ongoing monitoring of the investments/assets.

In 2007, the Land Board adopted a *State Trust Lands Asset Management Plan*. One of the key features of the plan is the classification of assets (see **Appendix A**). To fulfill its fiduciary duties to each individual endowment trust, the Land Board will:

- Manage the endowed land and financial assets as a whole trust on a total return basis.
- Seek to optimize risk and return from both the endowments’ land and financial assets through diversification of holdings.
- Ensure that significant land holdings will be maintained in perpetuity, since they provide material diversification and inflation protection to an endowment’s portfolio.
- Seek to reposition parcels to reduce risk, lower management costs and increase prospects for immediate and sustainable income, recognizing that much endowment land remains in the original scattered parcels obtained from the federal government.
- Provide for the appropriate and reasonable management expenses of each endowment from its own income.
- Accommodate public use of endowment lands, to the extent feasible, provided such use does not impair financial returns.⁷⁵

⁷⁴ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP II), 133 Idaho at 67-68, 982 P.2d at 370-71 (1999).

⁷⁵ Idaho State Board of Land Commissioners, *State Trust Lands Asset Management Plan* (2007).

IDAHO DEPARTMENT OF LANDS—THE LAND MANAGER

Idaho has 2.5 million acres of endowment trust lands, from which an average of \$47 million per year in net income is generated for the trust beneficiary institutions. The Idaho Department of Lands (IDL) manages these lands under a mission consistent with the *Constitution of the State of Idaho* (see **Box 2**). This mission is of great interest to many Idahoans.

Box 2. Idaho Endowment Trust Land Management Mission

To professionally and prudently manage Idaho's endowment assets to maximize long-term financial returns to public schools and other trust beneficiaries.

Idaho Dept. of Lands Website <http://www.idl.idaho.gov/overview.htm>

The IDL is the administrative arm of the Land Board and carries out the functions of the Land Board as assigned by the *Constitution of the State of Idaho*.⁷⁶ While the IDL also is engaged in many other natural resource-related and regulatory activities, endowment trust management is a primary activity. The IDL's managers and support staff administer the endowment land trust under the management directives specified by the Land Board and the Idaho Legislature.

The IDL is organized into three administrative divisions—Support Services; Forestry and Fire; and Lands, Minerals and Range). Endowment-related and regulatory services are provided by 14 field offices. The 14 offices are divided into North and South Operations. Details on program delivery and other organizational information are available on the IDL website at www.idl.idaho.gov.

ENDOWMENT FUND INVESTMENT BOARD (EFIB)—THE FUNDS MANAGER

The Endowment Fund Investment Board (EFIB) controls, manages, and invests the financial assets of Idaho's endowment trust in accordance with Idaho law and policies established by the Land Board.⁷⁷ Members of the EFIB are appointed by the Governor to four-year terms,⁷⁸ and include one Idaho citizen with a minimum of 10 years experience in the field of public education administration, one member of the Idaho Senate, one member of the Idaho House of Representatives, and six Idaho citizens at large who are knowledgeable and experienced in financial matters and the management of investment assets.⁷⁹

The EFIB manages the investing of both the endowment's **Permanent Fund** and the **Earnings Reserve Fund**.⁸⁰ Details regarding the two financial trust funds are provided in the respective subsections below. The interaction of the land assets and these two financial funds is illustrated in **Figure 2** (above and inside back cover in color).

⁷⁶ *Idaho Constitution*, Article IX, Section 7.

⁷⁷ Idaho Code § 57-715.

⁷⁸ Idaho Code § 57-719.

⁷⁹ Idaho Code § 57-718.

⁸⁰ Idaho Code § 57-720.

Permanent Fund. Each of the nine endowment trust funds (see **Table 3** above) by law has its own individual permanent fund and monies for each beneficiary institution must be accounted for separately. However, each of these funds is managed together by the EFIB as an asset pool called the **Permanent Fund**. This investment pool consists of proceeds from the sale of state lands (see the **Land Bank Fund** subsection below), mineral royalties, and any transfers by the Land Board from the Earnings Reserve Fund. The *Constitution of the State of Idaho* requires that the Permanent Fund “shall forever remain inviolate and intact.”⁸¹

Land Bank Fund. This fund is used to capture proceeds from the sale of endowment lands for reinvestment in permanent, income generating land assets.⁸² Each trust (except the Capitol endowment) has its own individual land bank fund. The sources of monies in this fund are finite, and are derived solely from the sale of lands owned by the beneficiary and interim investment earnings on the account balance. Land bank funds are under the control of the IDL but are invested by EFIB to earn interim revenue. After a period of five years, if monies have not been reinvested or committed to a reinvestment transaction, the monies are deposited to the Permanent Fund of the appropriate beneficiary institution.

Earnings Reserve Fund. Each of the endowment trusts (except the Capitol trust) has its own individual Earnings Reserve Fund. As with the Permanent Funds, each must be accounted for separately, but is managed as a pool by the EFIB. The Earnings Reserve Fund is the repository of all earnings from the investment of the Permanent Fund, earnings from the investment of the Earnings Reserve Fund itself, and renewable sources of land revenues, such as timber sale contract proceeds and interest, and revenues from grazing, farming, commercial real estate and residential cottage site leases. Payments of management expenses and beneficiary distributions are made from the Earnings Reserve Fund.⁸³

Fund Management. As per the state Constitution and statutes, the endowment funds are perpetual, which in practical terms means trust fund managers have a long-term investment horizon. All of the portfolios managed by the EFIB are subject to the variability of the financial markets and to the threat of eroding purchasing power due to inflation. The EFIB mitigates some of the market risk by investing in diversified portfolios of assets so that the expected variation in the whole portfolio is less than the sum of the variations of each part. The asset mix of the fund takes into account the entire endowment portfolio—i.e., the fact that the revenues the endowment lands and financial instruments, net of management expenses, will be contributed to the endowment funds.

The EFIB contracts with or employs investment managers to manage the funds.⁸⁴ The EFIB sets policies governing the types of investments allowable for Idaho's endowment funds,⁸⁵ specifying responsibilities and containing guidelines for asset mix as well as allowed and prohibited investments. Currently, investment policy for the endowment funds targets a mix

⁸¹ *Idaho Constitution*, Article IX, Section 3.

⁸² *Idaho Constitution*, Article IX, Section 4; Idaho Code § 58-133.

⁸³ Transactions in the Capitol endowment trust are handled differently because it does not have an Earnings Reserve Fund. For the Capitol trust, all revenues, expenditures, and distributions are accounted for within its Permanent Fund (see Idaho Code § 67-1610).

⁸⁴ Idaho Code § 57-721.

⁸⁵ Idaho Code § 57-720.

of 70% equities and 30% fixed income investments; these assets are expected to earn 4.0% annually after inflation and investment expenses.⁸⁶

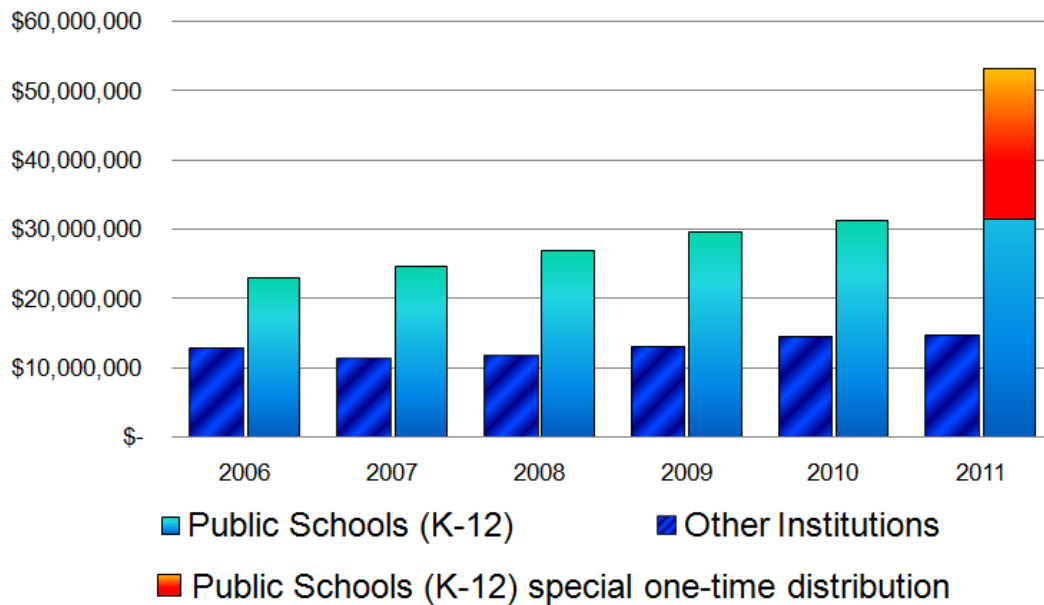
Distributions to Beneficiaries. The ultimate purpose of Idaho's endowment trusts is to provide a perpetual stream of income to the beneficiaries. As stated in the *State Trust Land Asset Management Plan*, when determining distributions, the Land Board, with assistance from the EFIB, considers the following for each endowment trust:

- Actual and expected return on the fund and income from the land.
- Expected volatility of fund and land income.
- The adequacy of distributable reserves to compensate for volatility of income.
- The beneficiary's ability to tolerate declines in distributions.
- Need for inflation and purchasing power protection for future beneficiaries.
- Legal restrictions on spending principal.⁸⁷

To guide the determination of future distributions for beneficiaries, the EFIB and the Land Board established priorities to avoid reductions in total endowment distributions and to maintain adequate Earnings Reserves to protect distributions from temporary income shortfalls (see **Figure 3**).

Figure 3. Distributions from Earnings Reserve Funds to the beneficiary institutions, 2006-2011, with cumulative distribution total, 1995-2011.

Cumulative distribution to public schools, 1995-2011 ~ \$601 million
Cumulative distribution to other institutions, 1995-2011 ~ \$268 million



Source: Idaho Department of Lands, Director's Office.

⁸⁶ Idaho Endowment Fund Investment Board, *Financial Statements for Fiscal Year Ended June 30, 2010*, p. 15.

⁸⁷ Idaho State Board of Land Commissioners, *State Trust Lands Asset Management Plan* (2007).

The trustee must also consider the need for intergenerational equity, thus the distribution policy is designed to grow distributions and permanent corpus faster than inflation and population growth. While the trustee determines sustainable distributions from each endowment trust fund—with the exception of the University of Idaho—such amounts must also be approved by legislative appropriation to be available in beneficiary operating funds.

PERFORMANCE REPORTING

Over the past ten years the management of endowment land assets has provided net income of \$47 million per year⁸⁸ for the endowment trust funds. Is this adequate to meet the “maximum long term financial return” mandate? This is not an easy question to answer. At the University of Idaho we have published general reports on how to approach this question for several types of land assets. One study focused on the financial performance of forests and rangeland assets,⁸⁹ another on the determination of lease rates for endowment residential real estate, commonly referred to as “cottage sites.”⁹⁰ The selection of financial benchmark criteria poses difficulties, beginning with the appraisal of real estate assets in order to calculate the return on assets (ROA) criterion.

For the past several years, the Western States Land Commissioners Association (WSLCA) has worked to develop a uniform asset reporting model. A pilot project that includes Idaho is examining traditional cash basis governmental reporting of net income by activity, along with more traditional investor performance calculations like return on asset (ROA). The use of ROA is desirable because it transcends public and private sector boundaries. The calculation also normalizes the variability of cash receipts within the same asset class. For example, forage values differ across landscapes such that certain regions command higher lease rates. Transition values aside, the higher earnings capacity of the land generally translates to a higher asset value per acre, but the return on asset should be similar to peer assets meeting the definition of the Rangeland classification.

Most recently the WSLCA has partnered with a key beneficiary group for public schools, the Children's Land Alliance Supporting Schools (CLASS), to produce individual state reports to capture an overview of assets, management and performance across the West. The various land asset classes, when consistently applied, enable states to more directly compare their financial performance to other states with similar mandates, as opposed to, or in conjunction with, comparisons made with the private sector. In addition to being able to more directly compare performance, the agreed upon asset classes provide the framework for how assets could be appraised (valued), while also providing a range of expected returns based on asset value. Thorough discussion of performance reporting, ROA and trust lands in the West can be found on the WSLCA website <http://www.wslca.org/> and Idaho specifics in the *Idaho State Trust Lands Asset Management Plan* <http://www.idl.idaho.gov/am/am.html>.

⁸⁸ Idaho Department of Lands Annual Reports (2001-2010).

⁸⁹ O'Laughlin, Jay, and Cook, Philip S., *Endowment Fund Reform and Idaho's State Lands: Evaluating Financial Performance of Forest and Rangeland Assets*. University of Idaho (2001).

⁹⁰ Cook, Philip S., and O'Laughlin, Jay, *Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands*. University of Idaho (2008).

ENDOWMENT FUND REORGANIZATION IN 2000

The current structure of the endowment trust funds was modified by the 1998 Idaho Legislature (S.L. 1998, Ch. 256). Before the Legislature's actions could take effect the U.S. Congress had to amend the *Idaho Admission Act* and the citizens of Idaho had to approve amendments to the *Constitution of the State of Idaho*. The U.S. Congress approved the *Idaho Admission Act* amendment in October 1998 (P.L. 105-296), and Idaho voters approved the constitutional amendments in the November 1998 general election. These changes took effect on July 1, 2000.

The post-2000 structure allows the Land Board to manage the endowment trust in a similar manner as private trustees manage a private trust. The new system is more flexible than the earlier version, and the trustees gained additional duties and responsibilities.

The changes in 2000 clearly establish the Land Board as the trustee for all parts of the endowment trust, and vested power in the Land Board over how the assets of the trust are managed and distributed to the beneficiaries. The change was essential to bring about a focused and unified approach to whole trust management. While the Land Board has always been recognized as trustee of the endowment lands and has acted as policy maker for endowment land management matters, prior to July 2000, the Land Board had no involvement in the management of the financial investments. The professional fund managers and board members of the EFIB now serve in an advisory capacity under the Land Board and regularly report fund activities and performance to the Land Board.

One of the constitutional amendments in 2000 provided that monies in the Permanent Endowment trust funds could be invested in "other investments in which a trustee is authorized to invest pursuant to state law." This change allowed investment in common stocks. Before July 2000, Permanent Fund assets were invested only in debt instruments such as bonds and mortgages held on the sale of state endowment lands. Why? When the *Constitution of the State of Idaho* was crafted more than a century ago, most stable companies were privately held and liquid equity markets were speculative. The trust terms reflected the belief that investment in land and fixed income instruments was the most prudent method of preserving wealth over the long term.

Times change. In 1996 a committee assembled by Governor Dirk Kempthorne to consider reform of endowment fund investments stated, "What were formerly the best means of preserving principal and providing a steady stream of income have, in fact, become the worst."⁹¹

Investment strategy has always been a balancing of risk and return. Common stock equity investments are characterized by greater volatility in annual returns than fixed income investments. The Earnings Reserve Fund was created as a method to counterbalance earnings volatility so that beneficiary institutions could expect a consistent level of earnings over time.

⁹¹ Governor's Committee on Endowment Fund Investment Reform, Report and Recommendations. Douglas Dorn, chair, Boise, Idaho (1996, p. 22). http://openlibrary.org/books/OL430087M/Report_and_recommendations_of_the_Governor%27s_Committee_on_Endowment_Fund_Investment_Reform

The changes made in 2000 also included the creation of a Land Bank Fund for each trust. Proceeds from the sale of endowment trust lands may be deposited into a Land Bank Fund to reinvest in other permanent land assets to generate earnings for the endowment. Reinvestment must occur within five years of sale,⁹² or the proceeds are deposited in each beneficiary's permanent endowment fund.⁹³

The changes in 2000 created a self-funded trust whereby the expenses of managing endowment land and financial assets are appropriated from the Earnings Reserve Fund (i.e., out of trust revenues). The state no longer appropriates monies for management of the endowment trust assets, as was the case before July 2000. The change highlights the need for whole trust management, asset planning, distribution policy and performance reporting, all guided by policies that were created to ensure the trust receives a competitive return on investments, and that the constitutional mandate to provide "maximum long term financial return" is not compromised by interest group agendas and politics.

DIFFERENCES BETWEEN "STATE LANDS" AND FEDERAL PUBLIC LANDS

The problem described in the opening quotation in the **Introduction** still exists—most people do not understand the purpose for and administration of the endowment trust lands and the financial returns the state obtains from managing them. This problem also exists in other states. Lengthy and occasionally heated discussions in the legislatures and courts have consistently supported the nature of trust land management and the responsibility managers of these assets have for generating financial returns for the trust beneficiaries.

The basic problem stems from perceptions of either what "public land" is or what it ought to be. The misconception is that state lands are managed under the same concept as federal lands. Perhaps in recognition of this confusion, in 1974 the agency responsible for the management and administration of Idaho's endowment lands dropped the adjective "public" from its name, and became the Idaho Department of Lands.

Determining who gets the benefits from public lands, however defined, is a significant issue in Idaho, where almost two-thirds of the state (63%) is federal land, and, in addition, almost 5% of the land is managed by the state.⁹⁴ If all the parcels of Idaho's endowment lands (now totaling 2.5 million acres) were aggregated together, the area covered would be slightly smaller than the state of Connecticut, or slightly larger than Delaware and Rhode Island combined. Determining who gets what from the majority of Idaho's lands administered by government agencies (see **Map 2**, inside front cover) is a matter of policy. Federal policy concerning land management objectives is quite general; state policy is quite specific.

Federal lands are managed under a variety of policies that promote the attainment of multiple benefits for the public.⁹⁵ For example, the Multiple-Use Sustained-Yield Act of

⁹² Idaho Code § 58-133. Note: The Capitol endowment does not have statutory authority to participate in the land bank. Idaho Att. Gen. Op. 01-4 (December 18, 2001).

⁹³ Idaho Code §§ 33-902, 33-2913, 66-1103, 33-3301, 20-102, 33-2911, 66-1101, 33-2909, 67-1610.

⁹⁴ O'Laughlin, Jay, Hundrup, Wyatt R., and Cook, Philip S., *History and Analysis of Federally Administered Lands in Idaho*, University of Idaho (1998, Appendix Table A, p. 10).

⁹⁵ For National Forest System lands administered by the U.S. Department of Agriculture, Forest Service, see 16 U.S.C. § 528 *et seq.*; for lands administered by U.S. Department of the Interior,

1960⁹⁶ provides the guiding principles for management of National Forest System lands, and it says: “Multiple use’ means the management of all the various renewable surface resources of the national forests so that they are utilized in the combination that will best meet the needs of the American people; . . . with consideration being given to the relative values of the various resources, and not necessarily the combination of uses that will give the greatest dollar return or the greatest unit output.”⁹⁷ [Emphasis added.] Although the attainment of multiple benefits is a feature of federal policy, those benefits are not to be measured solely in financial terms, or decision criteria based on efficiency.

In sharp contrast, Idaho’s endowment lands are to be managed “. . . in such manner as will secure the maximum long term financial return to the institution to which granted . . .”⁹⁸ While management activities on state endowment trust lands may provide benefits to the general public, such use must be purely incidental to the overall trust objective. As the Idaho Supreme Court held in *Idaho Watersheds Project II*, “Article IX, § 8 [of the *Constitution*] requires that the State consider only the ‘maximum long term financial return’” to the specific institution designated by law as the trust beneficiary.⁹⁹

Idaho’s endowment lands and federal public lands have different management objectives and policies. The differences stem from the historic purposes of federal land grants to the states for educational and other specific purposes that support public institutions in the states, and the retention of federal lands and creation of federal land management systems by the U.S. Congress for a variety of purposes. These include two agencies operating under multiple-use objectives that are responsible for more than 60 percent of the land in Idaho—the National Forest System administered by the U.S. Forest Service (39%) and the federal “public lands” administered by the Bureau of Land Management (21%).¹⁰⁰

In the conclusion of their *State Trust Lands* book, Souder and Fairfax stated that “Trust land management is our nation’s most ancient and durable resource policy.”¹⁰¹ More than 135 million acres of land grants to the states are managed under this model and provide billions of dollars for education and other public purposes. A decade ago two parcels of federal land were set up as trusts—Valles Caldera Trust in New Mexico and Presidio Trust in California. Other proposals were offered to pilot test the trust land management model on federal lands.¹⁰² In testimony to his congressional colleagues, Rep. Greg Walden of Oregon recently expressed dismay at the status quo on National Forest System lands in his state. Citing the

Bureau of Land Management, see 43 U.S.C. §1701 *et seq.*

⁹⁶ 74 Stat. 215, 16 U.S.C. 528 *et seq.*

⁹⁷ 16 U.S.C. § 531(a) (2008).

⁹⁸ *Idaho Constitution*, Article IX, Section 8.

⁹⁹ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP II), 133 Idaho at 67, 982 P.2d at 370 (1999).

¹⁰⁰ See O’Laughlin et al., *History and Analysis of Federally Administered Lands in Idaho* (1998, *supra* note 94, especially Chapter 2).

¹⁰¹ Souder and Fairfax, *State Trust Lands* (1996, *supra* note 16, p. 300).

¹⁰² See Fairfax (1999, *supra* note 26); O’Laughlin, Jay, *Trust Concepts Applied to the Federal Public Lands: A New Approach for Sustaining Human Communities and Biological Diversity* (2000); O’Laughlin, Jay, *Community-Based Land Management and Charter Forests* (2002); Idaho Department of Lands, “About the Federal Lands Task Force” website (1996-2004) <http://www.idl.idaho.gov/LandBoard/fltf.htm>

success of trust land management in the State of Washington, he proposed testing the trust land management model on national forests.¹⁰³

FREQUENTLY ASKED QUESTIONS

When we wrote the first edition of this report in 1990, the principal questions associated with the endowment trust lands were: Who gets to use the land? How much do they pay for that use? Who gets the proceeds? Who decides the answers to these questions? These are enduring questions that were considered during the Constitutional Convention in 1889. In addition we consider two more questions. One of them closes this FAQ section—What is the scope of the Land Board's management authority? We begin the FAQs with the other—the fundamental question of endowment trust land ownership.

Who owns the endowment lands?

The State of Idaho does not own the endowment trust lands—the beneficiaries are the actual owners of the lands. The State as trustee holds legal title solely for the purpose of administering the trust for the benefit of the designated beneficiary institutions. The various endowment trusts are the same as any private trust established to provide care for a child, conserve the assets of an estate, or provide funds to a favorite charity. As in a private trust, the maker (settlor) of the trust establishes a trust corpus (land, cash, stocks, etc.), a beneficiary, trust terms (directions), and names a trustee. In the case of the Idaho endowment trusts, the settlor is the United States of America and the corpus of each of nine trusts is the land granted at statehood. The trustee is the Idaho State Board of Land Commissioners (Land Board), comprised of five elected officials: the Governor, Secretary of State, Attorney General, State Auditor, and the Superintendent of Public Instruction. As trustee, the Land Board has a fiduciary duty to carry out the intent of the trust settlor—the United States. The Land Board cannot change the trust terms and must operate within the confines of those instructions. As the Idaho Supreme Court stated, “The board must find authority in the constitution and statutes for its actions.”¹⁰⁴ To do otherwise is to violate the trust responsibility and risk the loss of the trust corpus.

Who gets to use the land?

Questions concerning the use of the endowment lands are decided by the Idaho State Board of Land Commissioners, acting as the trustee for the designated beneficiaries. The Land Board has a clearly defined responsibility to obtain the maximum financial returns (i.e., highest possible net income) for the specific beneficiaries over a long term and that influences what is done with the land. As mentioned in the **Trust Asset Management Concepts, Component Parts, and Principles** section above, managers seek to provide a variety of activities on the land in order to promote diverse sources of revenue streams for the trust beneficiaries.

¹⁰³ See Walden, Greg, Testimony to House Natural Resources Committee, Washington, DC (July 14, 2011). <http://naturalresources.house.gov/UploadedFiles/WaldenTestimony07.14.11.pdf>

¹⁰⁴ *Idaho Watersheds Project v. State Board of Land Commissioners* (IWP I), 128 Idaho 761, 766, 918 P.2d 1206, 1211 (1996).

How much do they pay for that use?

The Idaho Supreme Court has made it clear that the Land Board is required to obtain the maximum long term financial return for the endowment beneficiaries. Determining whether the Board is achieving this objective has been elusive. In *Idaho Watersheds Project I*, the Idaho Supreme Court addressed whether the Board was fulfilling its duty when it awarded a lease to the existing lessee who refused to place a bid in a competitive auction for a grazing lease. The court stated:

The rationale behind the requirement of conducting an “auction” is to solicit competing bids, with the lease being granted to the bid that would, in the discretion of the Board, “secure the maximum long term financial return” to Idaho’s schools. . . . The Board does not have the discretion to grant a lease to an applicant who does not place a bid at an auction, based upon Idaho’s constitutional and statutory mandate that the Board conduct an auction.¹⁰⁵

Thus, the Court found that the public auction requirement in the constitution is the mechanism for determining the maximum long term financial return in situations where there are competing applicants. However, not all leases are contested so there remains the question of how to determine whether the Board is fulfilling its duty to maximize the return. Current litigation regarding the cottage site leasing program may offer some insight into this question. In 1990, the Idaho Legislature sought to exempt cottage site leases from the public auction requirement and directed the Board to charge market rent. This legislative directive is being challenged in several actions pending in State district court.¹⁰⁶

Appropriate payment for using granted lands has been a point of debate in other states. In a search for persuasive authority to guide the management direction of school trust lands in Utah, Bassett in 1989 stated the principal issue as “whether maximum economic return from the [school trust] lands is the only allowable management scheme . . .” and concluded that the law forcefully argues against any other approach. Furthermore, stated Bassett, California’s multiple-use approach, Arizona’s attempts to take into account non-economic values, and Wyoming’s stance that school trust lands should benefit the public generally are all potentially at odds with congressional intent as expressed in statutory law.¹⁰⁷

¹⁰⁵ *Id.* at 1211.

¹⁰⁶ *Wasden v. State Board of Land Commissioners*, CV 1023751 filed in the Fourth Judicial District Court on December 2, 2010, and *Babcock v. State Board of Land Commissioners (Babcock I)*, CV 2010-436C filed in the Fourth Judicial District on October 22, 2010. There are four additional lawsuits challenging the rental rate established by the Land Board in which Babcock is the lead plaintiff.

¹⁰⁷ Bassett (1989, *supra* note 13). Other commentators have disagreed with Bassett and emphasized that each state’s obligations for grant land management must be analyzed with due consideration of the specific content of its admission act (i.e., its original agreement with the federal government) and constitution. See, for example, Souder and Fairfax, *School Trust Lands* (*supra* note 16) and Bowlin, Tacy, *Rethinking the ABCs of Utah’s School Trust Lands*, 1994 Utah L. Rev. 923 (1994). See also sources cited *supra* at note 58.

Who gets the proceeds?

The proceeds from the sale, management, and leasing of the endowment trust lands are intended to benefit the specific beneficiaries of the original land grants, not the general public. The concept of specific beneficiaries, rather than the general public, is fundamental to determining permissible uses of the endowment lands and the amount and disposition of proceeds from that use. Case law strongly reinforces the “sacred trust” obligation to specific beneficiaries and indicates that anything less than maximum financial return is unacceptable.

What is the scope of the Land Board's management authority?

The Idaho State Board of Land Commissioners (Land Board) manages the endowment trust assets under a constitutional responsibility “to provide maximum long term financial return” for the beneficiary institutions.¹⁰⁸ This is accomplished by activities that resemble a variety of business enterprises, including a timber real estate investment trust or REIT, a commercial property leasing company, a commercial recreation business, and a financial investment fund. Trust businesses have always competed with the private sector.¹⁰⁹ [Emphasis in original source.] The question is whether these and other endowment fund business enterprises are consistent with the Land Board's constitutive authority in the *Idaho Admissions Act*, the *Constitution of the State of Idaho*, and case law (see **Box 1** above), as well as the general principles of trust management (see **Trust Asset Management Concepts, Component Parts, and Principles** section above).

The underlying issue is determining the appropriate business enterprises from which to maximize net income from the endowment assets. The nurturing of timber and forage products as improvements on bare land is an historically accepted enterprise, even though these activities put the endowment trust directly in competition with private business operations that sell the same product. In the same fashion, utilization of improved real estate to maximize financial return for the endowment trust should not be rejected simply because of competition with the private sector.

The crux of the issue is the degree of improvement considered appropriate. Under the principal established in *Barber Lumber Co. v. Gifford*,¹¹⁰ the Land Board, as “the instrumentality created to administer” the endowment trusts, must be given “a large discretionary power over the subject of the trust.” This should include discretion over the degree of improvement to the real estate utilized by the trust to maximize the return to the beneficiaries.

As discussed in the **Idaho State Board of Land Commissioners—The Trustee** section of this report, note that the issue addressed by the court in *Barber Lumber* was whether the Land Board had the discretion to include the value of improvements that a bidder would make to the land—i.e., building a railroad line that accessed the land as well as other state

¹⁰⁸ *Idaho Constitution*, Article IX, Section 8.

¹⁰⁹ Idaho Department of Lands Report to the House Resources & Conservation Committee following the Committee's “Discussion of Endowment Commercial Leasing Policy” held on Thursday, March 17, 2011. On file with Idaho Department of Lands, Director's Office.

¹¹⁰ *Barber Lumber Co. v. Gifford*, 25 Idaho 654, 139 Pac. 557 (1914).

endowment lands in the area—as part of the overall benefit to the trust, thus justifying acceptance of a lower bid for the sale of the timber located on the land.

Furthermore, in *Barber Lumber* the court affirmed that “the land business of the state placed in the hands of the state board of land commissioners ought to be conducted on business principles so as to subserve the best interests of the people of the state,”¹¹¹ and “it is clear that the state board has acted in this matter only as a man of good business sense and judgment would act in regard to his own affairs.”¹¹²

In *Moon v. State Board of Land Commissioners*, the court found that the Land Board must as a matter of basic trust law comply with the same fiduciary obligations as apply to private trustees. The Land Board is therefore constrained to look strictly at the interests of the endowment beneficiaries rather than the general public interest.¹¹³

This constraint on the Land Board was reinforced in *Idaho Watersheds Project II*. The Idaho Supreme Court found it would be a breach of the Board’s fiduciary duty to serve the interests of the beneficiaries to consider the interests of other organizations, causes, or public interests, no matter how worthy they may be. In addition, the IWP II court held that the Legislature is also precluded from directing the Land Board to consider interests other than the endowment beneficiaries.¹¹⁴

For the Land Board to invest in the same opportunities available to a private trustee is consistent with the Land Board’s constitutive authority, case law, and trust principles. Such opportunities would include the purchase of land with improvements on it, including buildings, as well as bare land upon which improvements would be made. Modifications attempting to limit investment opportunities for the endowment trusts need to consider the Land Board’s constitutive authority as well as trust principles.

APPLICABLE CASE LAW

Case law decisions reinforce the basic idea that land grants made in support of the public schools and other beneficiary institutions are a “sacred trust” or “solemn compact.”¹¹⁵ Courts have determined that anything precluding the beneficiaries from receiving the full value of benefits from the endowment lands violates both the original trust under which the federal government granted the lands and the agreement whereby the states were given title to the grant lands upon admission to the Union.

United States Supreme Court

Two cases that helped define land grant trust obligations follow.

¹¹¹ *Id.* at 669.

¹¹² *Id.* at 668.

¹¹³ See *Moon v. State Bd. of Land Comm’rs*, 111 Idaho 389, 393, 724 P.2d 125 (1986); also *County of Skamania v. State*, 102 Wn.2d 127, 685 P.2d 576 (1984).

¹¹⁴ *Idaho Watersheds Project v. State Board of Land Commissioners and Idaho Dept. of Lands (IWP II)*, 133 Idaho 64, 982 P.2d 367 (1999).

¹¹⁵ See discussion *supra* in **The “Sacred Trust”** section.

- In *Ervien v. United States*,¹¹⁶ the Court held, in 1919, that New Mexico could not spend three percent of its land grant trust income to advertise the resources and advantages of the state. Such action might be “a wise administration of the property,”¹¹⁷ but because schools would not benefit directly, such action was considered a breach of trust of the state’s enabling act whereby the school lands were granted.¹¹⁸
- In *Lassen v. Arizona ex rel. Arizona Highway Dept.*,¹¹⁹ the Court, in 1967, held that Arizona must directly compensate the land grant trust fund for the “full benefit” of school land the state obtained from trust resources for a highway right-of-way.¹²⁰ Even though an activity may ultimately benefit the trust, the trust must nevertheless be fully compensated.¹²¹

These two Supreme Court rulings—*Ervien*, benefits must accrue only to designated beneficiaries,¹²² and *Lassen*, such benefits must be at full fair market value¹²³—have been interpreted by Bassett with the following comments:

Given the language and attitude found in the relevant case law, including rulings of the United States Supreme Court, any derived benefit from the school trust lands must be used in support of schools and may not be used to support or subsidize other public purposes. Any arrangement not ensuring full fair market value for the use and/or sale of the school trust lands violates the trust obligation mandated by Congress.¹²⁴ [Emphasis added.]

It is clear from the Supreme Court rulings concerning trust lands that school trust resources are to be closely tied to the best method, economic or otherwise, of supporting public schools. No other public purpose constitutes a valid expenditure of trust resources.¹²⁵ [Emphasis added.]

The United States Supreme Court has held that the interests of the school trust beneficiaries are exclusive—they are not to be balanced against other interests.¹²⁶ [Emphasis added.]

¹¹⁶ *Ervien v. United States*, 251 U.S. 41 (1919).

¹¹⁷ *Id.* at 48.

¹¹⁸ *Id.* at 47.

¹¹⁹ *Lassen v. Arizona ex rel. Arizona Highway Dept.*, 385 U.S. 458 (1967). Souder and Fairfax, *School Trust Lands* (1996, *supra* note 16, p. 34) cite *Lassen* as “the starting point for a series of modern cases that rely on trust principles to answer ancient issues about the granted lands.” Before *Lassen*, courts were much less uniform in their interpretations of trustees’ duties regarding grant lands management. Also see further discussion in Fairfax et al., *supra* note 58; O’Day, *supra* note 40; and Mortimer, Michael J., *Condemnation Without Compensation: How Environmental Eminent Domain Diminishes the Value of Montana’s School Trust Lands* 8 Dickinson Journal of Environmental Law and Policy (2003, p. 243).

¹²⁰ *Id.* at 463-69.

¹²¹ *Id.* at 458.

¹²² *Ervien* 251 U.S. 41.

¹²³ *Lassen* 385 U.S. 458. See O’Day *supra* note 40, for further discussion of *Ervien* and *Lassen*.

¹²⁴ Bassett (1989, *supra* note 13, p. 202).

¹²⁵ *Id.* at 211.

¹²⁶ *Id.* at 205.

Another interpretation by Handy is quite similar and more succinct:

Neither the Congress nor the states may devalue the monetary trust assets to benefit others. Similarly, the trust lands and their management proceeds may not be devalued to serve other public purposes.¹²⁷ [Emphasis added.]

Sister States' supreme courts

Supreme courts in other state have solidified support for the two key points— benefits from land grant trusts must accrue only to designated beneficiaries, and such benefits must be at full fair market value—as illustrated by the following eight case summaries.

- In *Ebke v. Board of Educational Lands & Funds*,¹²⁸ the Nebraska Supreme Court in 1951 held that the state, as trustee of the endowment lands, has a duty to seek the most advantageous terms possible in managing the lands.¹²⁹
- In *County of Skamania v. State*,¹³⁰ the Supreme Court of the State of Washington in 1984 struck down a law designed to provide economic relief to purchasers of timber from endowment lands by allowing them to default on their contractual obligation or to modify or extend their contracts without penalty. The court determined that because the proposed law did not require fair market value of the contract be returned to the state, under the state's trust obligation the state's fiduciary obligation was breached.¹³¹ The state's fiduciary duty of undivided loyalty prevents it from using state trust lands to accomplish public purposes other than those which benefit the trust beneficiaries.¹³²
- In *State v. University of Alaska*,¹³³ the Alaska Supreme Court in 1981 ruled that the endowment lands belonging to the university could not be added to a state park without compensating the trust fund at the fair market value of the land, or an equal value of exchanged land for the trust lands taken.¹³⁴
- In *Kanaly v. State*,¹³⁵ the South Dakota Supreme Court found in 1985 that a state statute converting a unit of the state university into a prison was unconstitutional, because the trust compact required fair market value of the land be paid to the beneficiaries.¹³⁶ The court stated that the trust's beneficiaries "do not include the general public, other than government institutions, nor the general welfare of this state."¹³⁷

¹²⁷ Handy, Nicholas, *Legal Limitations on Federal or State Efforts to Impose Log Export Restrictions on the Federal Land Grant Trusts*, mimeo, 5 p., Washington Department of Natural Resources, Olympia, Washington (1989).

¹²⁸ *Ebke*, 154 Neb. 244, 47 N.W.2d. 520 (1951).

¹²⁹ Bassett, *supra* at 199.

¹³⁰ *Skamania*, 685 P.2d 576.

¹³¹ Bassett, *supra* at 201.

¹³² *Skamania*, 685 P.2d 576.

¹³³ *State v. University of Alaska*, 624 P.2d 807 (Alaska 1981).

¹³⁴ Bassett, *supra* at 201.

¹³⁵ *Kanaly*, 368 N.W.2d 819 (So.Dak. 1985).

¹³⁶ Bassett *supra* at 202.

¹³⁷ *Kanaly*, 368 N.W.2d at 824.

- In *Kerrigan v. Miller*,¹³⁸ an interpretation of a state statute by the Wyoming Supreme Court in 1938 stated: “The board shall lease all state lands in such manner and to such parties as shall insure to the greatest benefit and secure the greatest revenue to the state.”¹³⁹ The court concluded that the terms “greatest benefit” and “greatest revenue” as used by the state legislature were not equivalent, the former probably referring to the general benefit of the citizens of the state.¹⁴⁰ Subsequent rulings in Wyoming took the stance that trust obligations and management were for the general benefit of the entire state.¹⁴¹ Bassett’s comment in 1989 is that “the Wyoming scheme raises serious doubts as to whether this approach to management of school trust lands comports with the holdings of the United States Supreme Court and other courts that have looked at the issue.”¹⁴²

Two decisions by the Arizona Supreme Court are also relevant.

- In *Deer Valley Unified School District v. Superior Court*,¹⁴³ the Supreme Court held that the state constitution prevented action by a particular school district attempting to acquire a parcel of school trust land through condemnation, because that would not allow for any additional profit that the trust might gain from competitive bidding at advertised public auction.
- In *Kadish v. Arizona State Land Department*,¹⁴⁴ the Supreme Court held that flat rate (or fixed royalty) leases for minerals extracted from school trust fund lands were unconstitutional, in that such leases provide less than the true value to the trust beneficiaries.

Two common threads weave their way through these cases and are highlighted in a 1982 landmark case out of Oklahoma.

- In *Oklahoma Education Association, Inc. v. Nigh*,¹⁴⁵ the Oklahoma Supreme Court reaffirmed two key points concerning endowment lands: (1) school trust lands must be managed for the exclusive benefit of the public schools, and (2) school trust lands must be managed to obtain full value.¹⁴⁶
- The *Nigh* case, perhaps more than any other, crystallizes the endowment land concept. Furthermore, it explicitly defines the manner in which rents, leases and loans from the Oklahoma trust fund are to be administered. The court determined that low-rental leases of trust lands and low-interest mortgage loans of trust funds represented unconstitutional subsidies to farming and ranching. The implications of this decision for other Oklahoma permittees and lessees should be evident.

¹³⁸ *Kerrigan v. Miller*, 52 Wyo. 441, 84 P.2d 724 (1938).

¹³⁹ *Id.*, at 452, P.2d at 727.

¹⁴⁰ Bassett, *supra* at 204.

¹⁴¹ *Mayor v. Board of Land Commissioners*, 64 Wyo. 409, 192 P.2d 403 (1948); *Frolander v. Isley*, 72 Wyo. 342, 264 P.2d 790 (1953).

¹⁴² Bassett *supra* at 205.

¹⁴³ *Deer Valley*, 760 P.2d 537 (Ariz. 1988).

¹⁴⁴ *Kadish*, 747 P.2d 1183 (Ariz. 1987).

¹⁴⁵ *Nigh*, 642 P.2d 230 (Okla. 1982).

¹⁴⁶ Bassett, *supra* at 198.

CONCLUSIONS

At statehood, like the other western states, Idaho received 3.6 million acres of land from the public domain to support public schools and other designated public institution beneficiaries. Some of these lands were sold, and the proceeds placed in a permanent fund overseen by the Idaho State Board of Land Commissioners, with earnings from the fund distributed to the beneficiaries. Today, 2.5 million acres remain in the endowment trust. Net income from the sale of products (timber and minerals) sold from the endowment lands, as well as rental income from grazing and real estate leases, are also deposited in the endowment fund. In 2007 the value of the financial assets of the endowment fund surpassed one billion dollars. In addition, the endowment land assets, with an estimated value exceeding \$2 billion, continue to provide, on average, \$47 million per year in net income for the beneficiary institutions.

The concept of using endowment lands to produce financial returns for designated beneficiaries does not sit well with everyone, in part because it involves timber harvesting and livestock grazing, which are hot-button issues in the western states. The lawsuits summarized herein attest to that. Nonetheless, the constitutional directive is clear.

The problems Idaho encounters in the management of endowment lands are shared by many other states in the Union. Although decisions by the U.S. Supreme Court that interpret provisions of other states' constitutions may not be controlling in Idaho, the broad principles in those cases regarding federal grant statutes apply to Idaho's endowment lands. Additionally, while legal decisions in other states are not binding on Idaho, they often are deemed persuasive authority because of the similarity of the enabling or admission acts to Idaho's constitution and admission act. Thus, federal statutes provide a logical starting point for analysis, followed by comparison of state constitutional provisions, then case law interpreting the enabling act and state constitution. For example, the *Nigh* decision in Oklahoma¹⁴⁷ is relevant to Idaho only to the extent that the enabling acts and constitutions of the two states are similar in their grant land provisions. Such interpretations of law are why we have judicial systems and professionals trained to read the law.

The law concerning the solemn compact or "sacred trust" taken on by the states when they accepted grants of federal land is understandable and clear on two points. First, the benefits from those grants were specifically designated only to certain beneficiaries. Second, the ultimate criterion for land sales and exchanges as well as lease and permit payments is that the designated beneficiary for whom the land is held in trust by the state receive the full fair market value from any land sale or lease.

¹⁴⁷ *Nigh*, 642 P.2d 230 (Okla. 1982).

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APPENDIX A. ASSET CLASSIFICATION

The material in this appendix is excerpted with only minor editing changes from the *State Trust Lands Asset Management Plan* approved by the Idaho State Board of Land Commissioners in 2007 and available from the Idaho Department of Lands (IDL) Website.

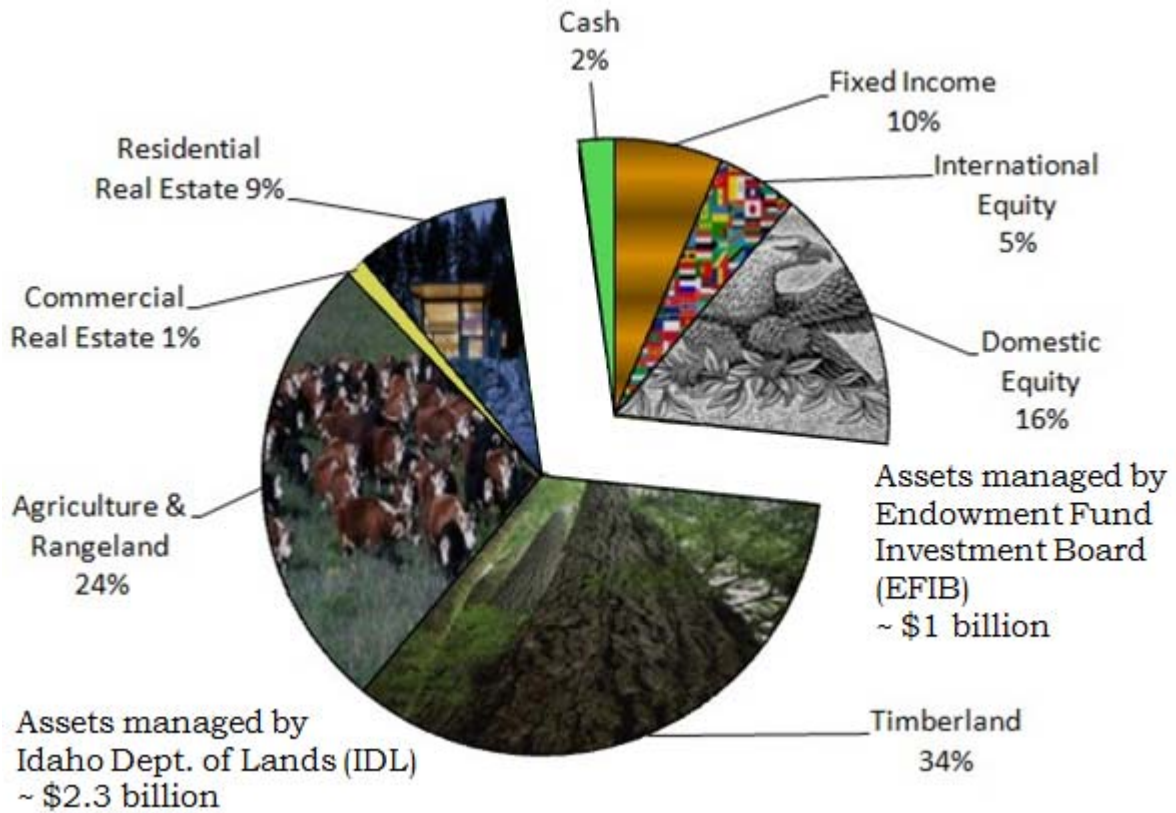
Land assets are classified according to their “primary” use as shown in **Table A-1** below. Other uses are allowed when they do not adversely impact the “primary” use and the intended financial return. This is unlike federal lands or other public lands that are managed for multiple uses or for the benefit of the general public regardless of whether these uses provide a positive financial return (see **Differences between “State Lands” and Federal Public Lands** section in this report). Land asset classifications can be modified to meet changing markets or to capitalize on emerging alternative opportunities.

| Table A-1. Endowment trust land asset classifications | |
|--|---|
| Asset Classification | Asset Description |
| Forest Land | Lands capable of regenerating and growing successive crops of commercial forest products on a sustainable basis |
| Agriculture Land | Lands used for growing cultivated plants or agricultural produce (grains, vegetables, and/or fruits). |
| Rangeland | Lands supporting natural vegetation suitable for grazing by domestic livestock & wildlife |
| Commercial Real Estate | Lands normally recognized as “commercial” in local zoning regulations, including retail and light industrial businesses, public facilities, energy resources (wind, hydro, wave), communication sites, ski resorts, etc. |
| Residential Real Estate | Sales or Leases of cottage/cabin/home sites |
| Minerals | Includes the sale of sand and gravel, oil and gas, coal, and other minerals including precious metals, decorative rock, phosphates, etc. |
| Conservation | Conservation lands are generally lands for which certain real property rights have been removed or otherwise restricted temporarily or permanently to maintain temporary or permanent rights for open space, preservation of habitat, natural areas, parks, or other such purposes. |
| Recreation (non-commercial) | Includes easements, leases, or licenses for dispersed recreational use (hunting, fishing, trapping, camping, hiking, trails) |

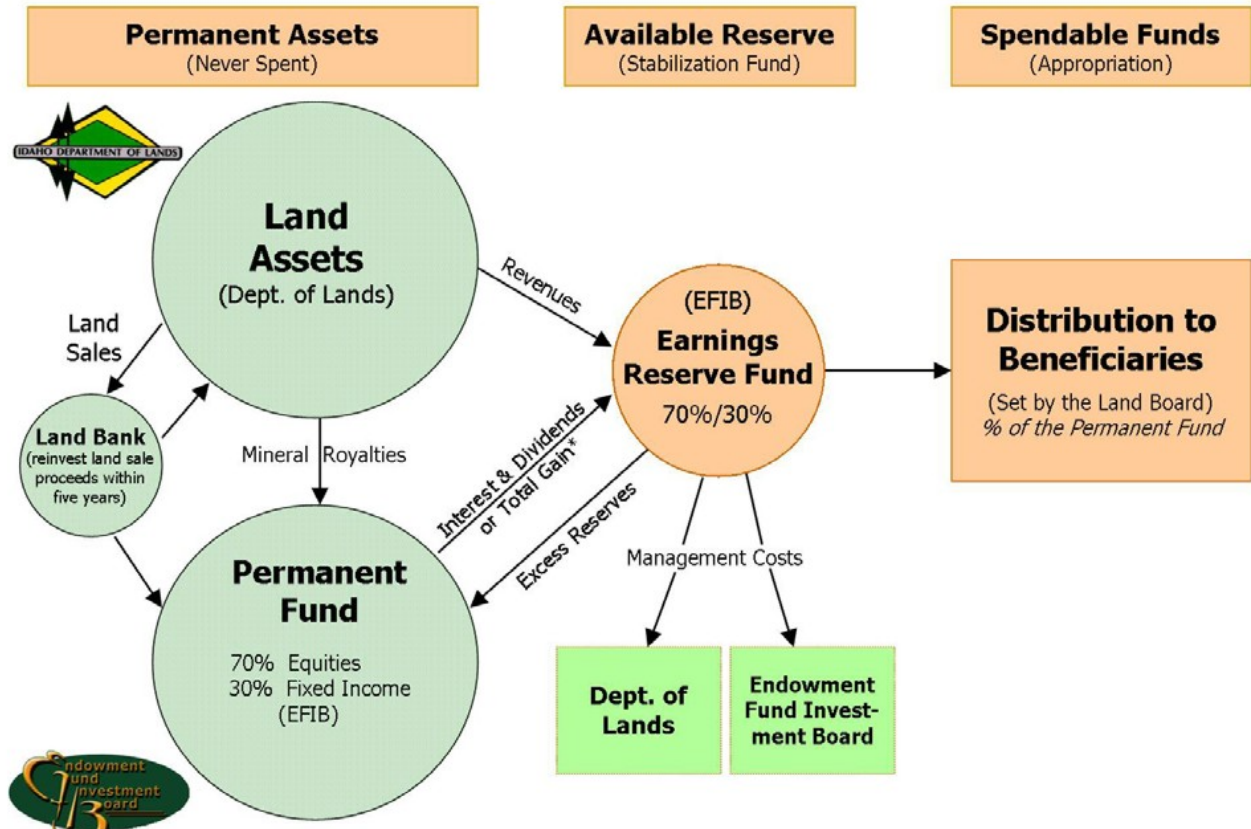
Categorizing investments into asset classifications allows land managers to customize plans and strategies so they can optimize returns based on specific asset characteristics. An ability to monitor performance by benchmarking against similar private industry (National Council of Real Estate Investment) and other trust land managers is another reason to group lands by classification. Finally, asset classifications allow land managers to make informed decisions regarding portfolio risk resulting from lack of diversification, liquidity, environmental laws and other societal pressures.

In managing the land assets, the IDL seeks to layer a variety of activities or uses as a means to diversify revenues to the trust. Activities are managed through a variety of contractual instruments designed to protect the long-term revenue generating capacity of trust assets and contract rates must reflect competitive market pricing. Typically activities include natural resource management such as the harvest and regeneration of crops, like timber and farm produce, providing grazing forage, as well as, leasing commercial and residential properties.

Idaho Endowment Trust Assets Estimated Value, June 2009



STRUCTURE OF IDAHO'S ENDOWMENT ASSETS



* When the Permanent Fund, adjusted for inflation, exceeds its June 2000 level, only total gain over inflation will be distributed to Earnings Reserve.

University *of* Idaho

College *of* Natural Resources