

Approved by the Natural Resources Interim Committee

**MINUTES
NATURAL RESOURCES INTERIM COMMITTEE
August 29th and 30th, 2011
Capitol Building – East Wing – Room EW42
700 West Jefferson Street
Boise, Idaho**

Cochairman Senator Monty Pearce called the meeting to order at 9:30 a.m.

Members present were: Cochairman Representative Dell Raybould, Senators Steve Bair, Jeff Siddoway, Lee Heider and Michelle Stennett and Representatives Bert Stevenson, Scott Bedke, Mike Moyle and Donna Pence. Ad Hoc members present included Senators Bert Brackett and Shawn Keough and Representatives Ken Andrus, John Vander Woude, Paul Shepherd and Grant Burgoyne. Senators Dean Cameron and Elliot Werk, Ad Hoc members, were absent and excused. Staff members present were Katharine Gerrity, Ray Houston and Jackie Gunn. Others present included Secretary of State Ben Ysursa; Former State Controller, J.D. Williams; Superintendent of Public Instruction, Tom Luna; Brian Patton and Cynthia Bridge Clark, Idaho Department of Water Resources; Lesa Stark and Robert Schattin, Bureau of Reclamation; Ellen Berggren, Army Corps of Engineers; Jay O’Laughlin; Dennis Colson; Laurie Boeckel; Karen Echeverria; Marty Peterson; Robert Maynard; Clive Strong, Office of the Attorney General; Kathy Opp, David Groeschl, Bob Brammer and Mike Tracy, Idaho Department of Lands; Larry Johnson; Richelle Sugiyama; Bob Boeh; Ken Wixom; Skip Oppenheimer; Dr. Peter Crabb; Brent Olmstead, Milk Producers of Idaho; John Eaton, Idaho Association of Realtors; Chris Halvorson, Investment Officer, Endowment Fund Investment Board; Tony Park, Payette Lake Cabin Owners’ Association; Robert Forrey, Rachel Gilbert, John Runft and Maurice Clements, Taxpayers Accountability Committee; Todd Hatfield, Hatfield Log Homes; Bonnie Butler, Governor’s Office; Anabel Manchester, Tracy Consulting; Larry Benton, Benton Ellis & Associates; Jack Harty; Erik Makrush, Idaho Freedom Foundation; Bill Podobnik, Priest Lake State Lessees’ Association; Lynn Tominaga, Idaho Ground Water Appropriators; Brenda Tominaga, Idaho Ground Water Appropriators/Idaho Irrigation Pumpers Association; Benjamin Davenport, Risch Pisca; Scott Phillips, Dan Goicoechea and Ashley Liggett, Office of the State Controller; Norm Semanko, Idaho Water Users Association; Kristy Sternes, Office of Raul Labrador; Al Marino, Thorton Oliver Keller; Jayson Ronk, Idaho Association of Commerce and Industry; Mark Branson, CH2MHILL; Justin Hayes, Idaho Conservation League; Jerry Deckard, Capitol West; Mike Brassey and Rich Hahn, Idaho Power Company; Jane Wittmeyer, Whittmeyer and Associates; Kent Lauer, Idaho Farm Bureau; and George Kirk.

NOTE: All copies of presentations, reference materials, and handouts are on file at the Legislative Services Office and are also available online at the Legislative Services Office website, <http://www.legislature.idaho.gov>.

Cochairman Senator Monty Pearce called for a silent roll call. **Cochairman Representative Dell Raybould** read the charge of the Natural Resources Interim Committee, as directed by House Concurrent Resolution 3. **Cochairman Pearce** introduced **Mr. Brian Patton**, Chief of Planning Division, Idaho Department of Water Resources. **Mr. Patton** recognized **Mr. Chuck Cuddy**, member of the Water Resource Board. He then provided a PowerPoint presentation entitled *“Update on Water Storage Studies and Aquifer Management Efforts.”* Topics covered in the presentation included:

- An overview of the Water Storage Studies directed by HJM8 (2008 Legislature)
 - Minidoka Enlargement Study
 - Boise River Interim Feasibility Study
 - Henrys Fork (Teton) Basin Study
 - Weiser-Galloway Project Studies

- Aquifer Planning and Management – directed by Section 42-1779, Idaho Code
 - Rathdrum Prairie Comprehensive Aquifer management Plan
 - Treasure Valley Comprehensive Aquifer management Plan
 - Eastern Snake Plain Aquifer CAMP and Management Efforts

At the conclusion of **Mr. Patton's** presentation, **Cochairman Raybould** briefly detailed aquifer water use between 1902 and 1952, describing the role excess flows from the rivers and streams played in maintaining equilibrium. He noted that the springs are now depleting the aquifers and that there is a necessity to get the aquifers recharged. Specifically, he stated that we have to find some way to accumulate water to use for artificial recharge projects, to at least compensate for the amount springs are depleting from the aquifer and to get what we need from the aquifer for our city, industry and agriculture to maintain our economy. **Cochairman Raybould** closed his comments, emphasizing how important it is to the state of Idaho that we find solutions for funding and water sources, to get the aquifer stabilized in order to preserve our economy.

Senator Heider asked if the Teton Dam can be built in a more secure manner, given its failure in 1976. He also asked **Mr. Patton** to detail Idaho Power's cloud seeding operation and to discuss whether its efforts have been beneficial. **Mr. Patton** explained that, because of the failure of the dam, the board knows more about the dam site than many other dam sites in the world. He confirmed that the dam could be rebuilt. Due, however, to environmental challenges and public perception challenges, the Bureau of Reclamation is participating in studies that are exploring other alternatives that would provide similar storage in that area and provide similar benefits. These alternatives may be more cost-effective than rebuilding the dam. The study will continue in order to bear that out. Additionally, **Mr. Patton** spoke to the cloud seeding efforts and stated that they have been beneficial, though it is a little too early to tell how much additional water has been generated. He remarked that we have to let the five year pilot project play out.

Representative Bedke asked **Mr. Patton** to discuss the obstacles the Water Resource Board faces. **Mr. Patton** stated that managed recharge is the most challenging aspect along with funding issues. **Mr. Patton** went on to detail how the CAMP itself attempted to specify the geographic distribution of where recharge should occur - fifty percent above American Falls Reservoir and fifty percent below American Falls Reservoir. He explained the role geography plays in determining which canals in the upper and lower basin are used for recharge, and he outlined how there are only two canals that can carry the recharge below the reservoir. He discussed the reasons why the canals in the upper basin are far more prepared to carry the recharge water and why at present the geographic distribution is skewed much more heavily toward the upper basin than the lower basin. **Mr. Patton** continued by noting the challenging aspects of renting from the rental pool. He stated that matching the timing with when the canals are available to carry the water has been difficult. Finally, he discussed the issue related to the Swan Falls Reaffirmation Agreement between the state and Idaho Power and the subsequent legislation limiting managed recharge to an average annual 175,000 af for natural flow above Swan Falls Dam. He continued, stating that in terms of doubling the recharge, it's an issue that has to be considered.

Senator Siddoway noted that Ashton Dam is currently under renovation. He asked if a concerted effort to increase capacity is to be made, should it be done while the dam is under renovation. **Mr. Patton** explained that the time frame for building additional storage in Teton Basin is one or two decades or longer, that the renovation has to be completed now for safety reasons and that the two efforts are not in conflict because of the time frame involved.

Cochairman Pearce, referring to the ESPA - Cumulative Change in Aquifer Storage chart, asked **Mr. Patton** to discuss his prediction for the future – whether he thought we would likely drop lower or hit a plateau and turn the storage level back up. **Mr. Patton** stated that without the actions such as managed recharge outlined in the CAMP, the current trend will continue. He stated that if we can find a way to put those actions into place and continue those actions out in the long-term, then we can stabilize the situation. He continued, stating that if we hit the CAMP targets we can stem the loss, start to turn the tide and begin to add back.

Senator Heider noted that at the last CAMP meeting he attended the members appeared ready to dissolve the committee. He asked **Mr. Patton** if there has been any emphasis on maintaining CAMP and providing the funds necessary to help the CAMP process along. **Senator Heider** also asked **Mr. Patton** why, in a wet year like this year, we haven't filled the canal systems earlier and recharged the systems over in the eastern Idaho and Northside Canal systems to try to improve the aquifer situation. **Mr. Patton** agreed that the CAMP Implementation Committee has faced challenges. He commented that the committee has not met in some time because they come back to the same funding issue discussions. He stated that a committee meeting should be called sometime this fall or winter and he identified the Water Resource Board to be the driver in moving forward with these actions.

He continued, reiterating that there is just more capacity in the upper valley than in the lower valley. Additionally, he said that many canal companies in the upper valley participated and they encouraged participation but some opted out due to maintenance issues or other things.

Representative Pence asked **Mr. Patton** to provide an update on the work done on projects other than the canals. **Mr. Patton** emphasized that they are not disregarding other opportunities, but there is the need for additional capacity in the lower basin, to get the balance back towards a fifty-fifty split. Addressing other projects, he noted the constructed site out of Shoshone that has been utilized over the last several years for managed recharge. He stated that there are also several proposals to construct additional off-channel managed recharge sites and that some of these proposals will make their way to the Water Resource Board for consideration.

Representative Stevenson responded to comments he heard earlier in the meeting that the upper valley is able to do more. He highlighted the timing challenges involved in participating in recharge. He explained that the lower valley starts about a month earlier than the irrigation season does in upper valley. He emphasized that once they start their season, they can't do managed recharge and that it's not that those canal companies are unwilling.

Representative Andrus asked that if money was the reason we aren't doing more recharge whether the users would be willing to pay. **Mr. Patton** agreed that funding has been an issue and the board has been cognizant to get the best use of the money available to achieve the best benefit through the recharge efforts. He stated that users did contribute this year. He pointed to the contribution this year by the Idaho Ground Water Appropriators (IGWA), representing all the ground water users across the Eastern Snake Plain, of \$100,000 to the Water Resource Board to help achieve managed recharge. He said this

was done on a cost-sharing basis and that they hope to see more of this type of participation in the future to maximize the recharge volumes.

Representative Moyle asked if everyone who wished to participate in recharge had a chance to participate this spring. **Mr. Patton** stated that they attempted to maximize the recharge among the participating canals and in the upper valley most that wanted to participate did so.

Representative Bedke suggested that the committee should come up with a strategy when water is there, a mechanism by which all obstacles can be removed so we don't miss our opportunities to recharge. He asked **Mr. Patton** if the board was thinking along these lines, considering various possibilities and whether it has any proposals. **Mr. Patton** stated that the board is constantly thinking along those lines and shared that this year was a great example, where the 1980 priority water rights stayed on until almost the third week in July, though he said we missed some opportunities because of that. He indicated that there are funding opportunities, highlighting the transfer of \$2.4 million dollars into the secondary aquifer management fund last year and some of that could possibly be made available for recharge. The board will have to make that decision. He said there is an opportunity to expand the cost-share participation from users. He added that, in the future when the pay stream comes back in from the Pristine Springs loan, those payments could also be transferred into the secondary aquifer management fund for future aquifer management projects.

Representative Bedke stated that he was more comfortable with the Pristine Springs loan payments going toward capital improvements rather than ongoing water-related charges. **Mr. Patton** indicated that that debate is currently going on with the Water Resource Board and the chairman shares his perspective.

Cochairman Pearce thanked **Mr. Patton**. **Senator Bair** asked that **Mr. Patton** to pass on his compliments to the Bureau of Reclamation (BOR) and the Corps of Engineers for their successful efforts in doing their best to prevent flooding. He stated that he lives in the Thomas area where fifty-some homes were threatened and he spoke highly of how the BOR learned from what happened in 2007 and prevented a big surge.

Kathy Opp, Deputy Director, Idaho Department of Lands, introduced the members of Panel 1, Trust Law 101: **Dr. Jay O'Laughlin**, Professor of Forest Resources, University of Idaho and **Dennis Colson**, Professor of Law Emeritus, University of Idaho College of Law. The panel members discussed constitutional and trust law principles applicable to management of state endowment trust assets.

Dr. O'Laughlin reviewed the report of the Policy Analysis Group – College of Natural Resources, entitled "*Idaho's Endowment Lands: A Matter of Sacred Trust*" (Tab 2, DOL Binder). **Dr. O'Laughlin** stated that the Policy Analysis Group (PAG) was created by the Idaho Legislature 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. **Dr. O'Laughlin** thanked the legislature for their continued support of the PAG. Further, he briefly reviewed the mission of the group and the make-up of the PAG Advisory Committee. And he noted a variety of PAG reports published since the group's inception.

Dr. O'Laughlin's overview of the PAG report included a review of the purpose of federal land grants to the states from the federal public domain, with specific focus then on the disposition and management of the 3.6 million acres of territorial and statehood grants to Idaho. He touched on the debates of the

Constitutional Convention of 1889, because he said it helps inform discussions regarding the trust under which these lands are held. **Dr. O’Laughlin** discussed the “sacred trust” concept, a concept unique to Idaho’s Constitution, which evolved out of the debates. He stated that key elements in effective trust management are: Clarity, accountability, enforceability, perpetuity and prudence. He continued, providing an overview of the institutions responsible for administering the endowment assets and their operations and he discussed how the trust land management concept creates distinct differences between “state lands” and federal public lands administered by agencies under statutory missions defined by the U.S. Congress.

Dr. O’Laughlin stated that the overarching issue for state policy makers has remained the same since statehood: Whether the land assets be retained and managed to produce streams of net income for the beneficiaries, or whether the lands be sold and the proceeds invested for the beneficiaries in other types of assets. He stated that, whatever the choice 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.

Dr. O’Laughlin concluded his remarks, discussing five issues of endowment land management. The final issue was how to determine the scope of the Land Board’s management authority. He stated that the Land Board must be given large discretionary power and he reviewed court cases that addressed this topic.

Professor Colson was the next speaker to address the committee, reviewing the report entitled “*Idaho Endowment Lands and the Idaho Constitution*” (Tab 4, DOL Binder). **Professor Colson** thanked the committee for the opportunity to speak to them about the constitution. He stated that constitutions set out the most fundamental principles of our legal and political life. They are about creating, empowering and limiting the various branches of state government and though they are enduring, by their very nature they have to be adapted to the exigencies and crises that we face over time. Related to the questions about endowment land management and their legislative role, he suggested that the committee review the language of the Idaho Constitution and the debates of our founders that produced that language. He discussed the details of the debates, concluding by stating that the middle-of-the-road view prevailed at the Convention. And, at the end of the debates concerning the endowment lands, the Convention adopted the following principles:

- The majority of the delegates were willing to trust the Board of Land Commissioners and the Legislature with the power to decide the future of the endowment lands, but thought it wise to impose limitations on those powers.
- The lands were to be held in trust for the beneficiaries of the endowment.
- The land was to be managed according to private trust law and free from political influence and considerations.
- The land was to be disposed of, sold or rented, at public auction.
- The lands should be managed to secure the maximum possible amount therefor. No lands were to be sold for less than \$10 per acre. No pre-emption right of settlers should be recognized. No more than 25 sections were to be sold in any one year.
- The land was to be sold in subdivisions not to exceed 160 acres to any one individual, company or corporation.

Professor Colson concluded that the majority of the delegates thought that the immediate sale of the school lands would provide the most revenue for public education in Idaho, while a minority thought that leasing would provide the most long-term revenue. He said that both sought the greatest return from the endowment in order to reduce the burden on the taxpayer. **Professor Colson** indicated that, in the end, the Convention did not decide on a policy of selling, or renting. Instead, the Convention left that decision for the generations to follow by empowering the Board of Land Commissioners and legislature to sell or rent the public lands.

Professor Colson discussed the addendum to his report, "*The Founders and the Disposal at Public Auction Issue*" Tab 4, DOL Binder). He reviewed the pertinent question: "Did Idaho's Founders intend to include the leasing of the lands held in trust in the phrase *disposal at public auction*?" He suggested that in order to answer this question, one must look to the constitutional language of Article IX as well as the debates from *The Proceedings and Debates*. **Professor Colson** stated that a close review indicates that it is clear the delegates were using "disposal" broadly to include leases as well as sales. He said that Section 8 refers to "disposal" at public auction; the language does not say "sale" at public auction. Continuing, **Professor Colson** pointed to the Article IX Committee Report that repeatedly used the "disposal" language. The Board of Land Commissioners was to have the "direction, control and disposition of the public lands." (Section 7) The Board of Land Commissioners was charged with the duty of providing for the "location, protection, sale or disposition" of the public lands. (Section 8)

Professor Colson emphasized that the delegates shared the concern that the management of these lands be transparent and disposal at public auction was one of the ways of assuring this. He added that had the delegates intended it to be just the sale of the property, he believed they would have said that and they wouldn't have used the phrase "disposal" in these various other places. **Professor Colson** closed by stating that we are wrestling with the same questions with which the delegates wrestled.

Representative Burgoyne asked **Dr. O'Laughlin** to describe what is meant by "permanent land assets." He wondered if **Dr. O'Laughlin** includes business profits, not passively but actively owning and operating, within the term "permanent land assets." **Dr. O'Laughlin** responded by stating that, if we consider land to be real estate, then assets attached to real estate are to be included. By improving bare land, by growing timber, by growing forage, by erecting buildings, he said you are still dealing with land. And, he continued, what kind of business is to be conducted on that land with its improvements is a discretionary item that the Land Board has the discretion to deal with.

Representative Burgoyne discussed the Admissions Act and its use of the term "other land." He asked **Dr. O'Laughlin** if the term meant that one may acquire the land but one may not necessarily put it into a trust. **Dr. O'Laughlin** stated that the challenge of limiting the improvements on bare land is that you won't meet the maximum long-term financial return provision in the constitution.

Representative Bedke commented that the legislature is trying to determine if the state should compete with the private sector. He asked **Professor Colson**, is it constitutional, given the powers vested in the Land Board, for the legislature to limit investment areas for the Land Board. He asked whether it would be stepping on areas carved out to the Land Board in the constitution. He continued by asking whether there would have to be a change to the constitution to get there. **Professor Colson** replied that he thinks it would be unconstitutional for the legislature to tell the Land Board it didn't have to hold the land in trust. The harder question is what the constitutional language means for the Land Board and whether the legislature is infringing on powers of the Land Board. In terms of our founders, **Professor Colson** remarked that no one worried about the Land Board competing with private interests. He stated

that he believes the founders knew full well that the board would be in competition with other profit makers and the bottom line is that it is to the taxpayer benefit to keep tax rates down.

Representative Vander Woude asked **Dr. O’Laughlin** where he draws the line between “maximum return” and “sacred trust.” **Dr. O’Laughlin** explained that the term “sacred trust” is unique to Idaho, that it is a term of art. He said that it defines a duty that the trustees have to beneficiaries. He continued, explaining that “maximizing long-term return” is the key phrase. He went on to say that the Land Board has the discretion to determine what vehicles – what prudent business investments - are used to accomplish this. **Representative Vander Woude** then asked if the Land Board could invest speculatively and **Dr. O’Laughlin** responded that the board does have the discretionary authority to invest in anything they think would benefit the designated beneficiaries. He also explained that the principles of trust management holds that if someone believes they are doing something that is too speculative, then they can seek remedy in court.

Representative Stevenson asked **Professor Colson** for clarification of the term “trust,” specifically, whether it an honorary trust or an enforceable trust. **Professor Colson** stated that it is more important that the Idaho Supreme Court has defined it as an enforceable trust. He emphasized that the term did not appear in the Admissions Act but that our founders functionally set it up as a trust in the constitution.

Referring to an earlier discussion of Article IX, Sections 7 and 8, of the Idaho Constitution relating specifically to the question of the role the legislature, **Senator Keough** asked **Dr. O’Laughlin** how the phrases “prescribed by law” and “as the legislature shall provide for the sale of land” meld with the board’s defined authority. **Dr. O’Laughlin** stated that the legislature is the appropriate body to determine the answer to that question.

Representative Bedke asked **Dr. O’Laughlin** to consider an example where you lease a cabin site valued at \$100,000 an acre and any process that conveys that property to another owner - is it a direct violation of the principles discussed earlier if the legislature stepped in to convey that property to the current lessees. **Dr. O’Laughlin** acknowledged the example, the situation where the Land Board was not realizing maximum return on some investments. He stated that they have done a study on the cottage sites and recognize that the state is not getting what some other states get. Continuing, he stated that beneficiaries are entitled to full market value from the assets that are held in trust and they aren’t getting it from the cottage sites.

Representative Bedke asked **Dr. O’Laughlin** if a constitutional change would be required in this situation. **Dr. O’Laughlin** responded, answering that he did not think a constitutional amendment would be required in the case of the disposal of the cottage site leases and immersion into some other asset type. **Cochairman Raybould** commented that the issue is establishing fair market value, and that the Land Board should focus on the local situational factors and not on the lease rates in other states to establish a price on our property, particularly if that exceeds the amount you would pay and then you don’t get anything at all on the property. To get the maximum value the landlord needs to determine the amount someone would pay to rent.

Senator Siddoway asked **Professor Colson** whether he thinks the landlord can give some consideration to ancillary benefits. **Professor Colson** answered that given the recent Supreme Court decisions, without changing the constitution, he doesn’t see a way of doing that. At present, with the “disposal at public auction” provision you don’t get into the consideration of ancillary things. **Senator Siddoway** asked for

Professor Colson to provide a definition of “disposition,” and to include every use possible. **Professor Colson** replied that our founders used the word broadly. Installment savings of land and all said installment contracts are disposals and therefore “subject to public auction.” He said that leases were also spoken of and that those are the disposals they talked about subject to the public auction requirement. And, in section 8, he stated that the word “disposal” was taken out and “rental” was put in at the convention because “disposition” was too broad. **Professor Colson** noted that John Gray, a legislator, thought the word “disposal” too broad, stating his concern that the word would be interpreted to include mortgages. **Professor Colson** stated that Mr. Gray moved to amend and remove the word “disposition” and put in the word “rental.”

Representative Stevenson asked **Professor Colson** if we are in the same position as they were at the Constitutional Convention in trying to decide what all these words mean. **Professor Colson** replied that a lot of the fundamental disagreements are still there, but noted that their debates have sharpened and clarified the meaning of some of these words, if we take their debates and employ them to determine constitutional meanings. **Senator Stennett** commented on the ambiguity involved with pinning down a future return amount in our attempt to meet the constitutional requirement to provide “maximum long-term return.”

Kathy Opp introduced the members of Panel 2 – The Trustee Perspective: **Secretary of State, Ben Ysursa**, and **Former State Controller, J.D. Williams**.

Secretary Ysursa commented that we are at an intersection crossroads of three branches of government dealing with endowments property. He discussed the impending state Supreme Court decision regarding the constitutionality of Section 58-310A, Idaho Code, and noted the timeliness of our discussion of what the extent of the legislative power is to limit the discretion of the Land Board and still be within the constitutional mandates. He explained the decision of the Idaho Supreme Court case relating to Section 58-310B, Idaho Code, where the court ruled that the Land Board does not have the ability to look at outside consequences and must maintain an undivided loyalty to the beneficiaries.

Secretary Ysursa then discussed the challenges faced with the properties at Priest Lake and Payette Lake. He said that the real evolution he has seen over his 37 years is that they wear one hat. He quoted Utah’s constitutional language regarding its Land Board’s mandate - that it must have “undivided loyalty” to the beneficiaries, balancing short-term and long-term interests so that long-term benefits are not lost in an effort to maximize short-term gains. He continued, stating that beneficiaries do not include other governmental institutions or agencies, the public at large or the welfare of the state.

Secretary Ysursa concluded, stating that we’ve been discussing the land values for a long time. He pointed to the wisdom of the early legislatures, setting five elected officials on the Land Board and by doing that, they expected reasoned and prudent decisions. As a trustee, he said that he understands the furor over some of the Land Board’s investments but appreciates that we are at an intersection – that we wish to proceed with constructive alternatives that are consistent with the principles enumerated in Article IX, Section 8 of the Idaho Constitution.

Mr. Williams thanked the legislators for their service and stated that he was appearing as a private citizen and as a grandfather. He commented that we must do what is in the best interest of the beneficiaries, and that we have some discretion in terms of that. He stated that every dollar we make from the endowments is less tax we have to collect. The changes that were initiated in the 1990s are going to make a whole lot of difference as the state goes on. He then discussed the board’s history

regarding the early steps taken to diversify the investment portfolio. He remarked upon **Governor Batt's** leadership with the endowment reform effort and noted the effort to change how we could invest, presently at a seventy percent equity - thirty percent debt ratio, to manage the land and the trust together, and to diversify the portfolio. Investments in timber have worked well and he supported investments in commercial property around the Capitol and at the same time protecting the space around the Capitol. He discussed the cottage site leases situation and introduced the subject of exchanges as a possible solution.

Mr. Williams stated that if he were advising the Land Board today he would encourage them to get on with the exchanges, that the harvest of that value should be reaped and diversify the portfolio. He said that the only way you can do that, to ensure added value in the future, is to have commercial property. He pointed to the Eagle Hills property as an example. **Mr. Williams** concluded, stating that he thinks that the Land Board is on the right track in its efforts to diversify the portfolio and that they should be supported.

Cochairman Pearce called for a break for lunch at 12:09 p.m. and the committee reconvened at 1:35 p.m.

Cochairman Raybould asked **Mr. Williams** to share his thoughts regarding the cottage site leases. **Mr. Williams** discussed the viability of exchanges, that Payette Lake is the easiest to start exchanges on. He said that more care is required with exchanges at Priest Lake, when you look to the long term development with the impact on the endowment lands because of the impact on its use for timber. When you look for exchanges regarding timber, he noted that you have to look for saw mills. He restated that he believed exchanges were a solution that should be evaluated and moved upon.

Cochairman Pearce asked **Secretary Ysursa** to comment on whether the state would have to absorb any loss in an investment if the Land Board invested in a more volatile type of investment. **Secretary Ysursa** responded that there is a payback provision that states that over a period of time the legislature must make the permanent fund whole again when the principal is diminished. He continued, explaining that investment in equities is allowed by the constitution and the people of Idaho after endowment reform. And, he stated that the investments have performed well lately with the assistance of professional managers.

Cochairman Pearce asked **Secretary Ysursa** to explain the apparent lack of funds at present for the update and care of the Idaho State Capitol. **Secretary Ysursa** stated that the Capitol fund is the only endowment fund that doesn't have an earnings reserve fund. He stated he would make that information available to the committee.

Representative Moyle asked **Secretary Ysursa** if the Endowment Board has looked at the tax shift that has occurred within in the counties when land purchased by the board is taken off the tax rolls, and whether he has that information broken down by county. **Secretary Ysursa** stated that he believed they had that information and would get a breakdown for the committee. He also stated that one has to, when evaluating this, look at the increased revenue the purchased land has provided the endowment.

Representative Vander Woude asked **Secretary Ysursa** to explain why commercial property is only returning about two percent when it doesn't have to pay property tax. Secretary Ysursa stated that the value goes down based on the market. In addition, he noted that they had to do some upgrades. He stated that the Department of Lands can provide the committee with more specific information.

Representative Vander Woude asked how two percent could be construed as a reasonable maximum return over four years when it's not paying any property tax. **Secretary Ysursa** responded that he spoke to the downturn in the market and also renovations that were paid for as realities reflected in the lower return. He gave a brief history of the earliest commercial property investment. He also explained that the key phrase is "maximum long-term return," rather than taking a short timespan snapshot of the investment. **Mr. Williams** suggested that the committee review the financial statements, focusing on income of the various assets and nets. He also identified a remodeling effort underway as one of the reasons why there was so much less going to schools, noting that the dip in return percentage is a one year aberration. In closing, **Representative Vander Woude** commented that the investment in that property seems to be going down compared to 2007.

Cochairman Pearce asked **Secretary Ysursa** to offer his opinion on the perception held by many that government typically doesn't do well in business, in other words, will the Land Board do well competing in the market place. **Secretary Ysursa** stated that having land is always a good idea. He continued, highlighting that one reason behind the establishment of the Land Bank was the need to retain acres we possess for the long term. He said that he believes that investment efforts should be a mixture, keep the Land Bank concept and the concept of retaining land ownership and also diversify, follow the prudent investor standard and don't put all your eggs in one basket. Though he doesn't see the board going into active investment competition with private enterprise, **Secretary Ysursa** stated that he recognizes the need to take advantage of business opportunities. With regard to the cottage site leases, he stated that some sites will be disposed of and some will be retained. He emphasized that the need for an orderly process is critical.

Representative Burgoyne asked **Secretary Ysursa** what is the acceptable risk and whether the Land Board has a concept of what that acceptable risk is. **Secretary Ysursa** stated that the Land Board has an asset management plan where they try to balance risk and reward, all for the benefit of the beneficiaries.

Representative Moyle asked **Secretary Ysursa** to comment on how he would gauge investment situations where the state ends up taking property off the property tax rolls. He asked whether we can compensate the counties for the loss experienced when property is taken off the tax rolls. **Secretary Ysursa** stated that he would take a look at the property tax issue.

Kathy Opp introduced members of Panel 3 – Beneficiary Representatives: **Tom Luna**, Superintendent of Public Instruction; **Laurie Boeckel**, Idaho PTA & Children's Land Alliance Supporting Schools; **Karen Echeverria**, Executive Director, Idaho School Boards Association; and **Marty Peterson**, Special Assistant to the President, University of Idaho.

Superintendent Luna discussed the wisdom of keeping the endowments in place without selling the assets and spending the money. He stated that the primary responsibility of the endowment and the Land Board is to guarantee the most advantageous benefit for the future beneficiaries. He expressed the concern of protecting the future beneficiary at the expense of the current beneficiary, adding that this concern needs to continue to be discussed. He also emphasized that there is a need to balance the interests of the current and future beneficiaries and that long-term sustainability is critical in planning for education in the future.

Ms. Boeckel stated that she was presenting to the committee advocating for Idaho's public school children. She asked that all elected officials recognize that endowment lands are not state lands but are rather held in a trust by the state. She presented a video to the committee, explaining that the video illustrates that the challenges Idaho faces in this area are not unique. **Ms. Boeckel** also noted the highlights of successes relating to endowment plans going on in other states.

Ms. Echeverria discussed the challenges inherent in managing endowment land investments. She emphasized that the trust, all facets of the trust, the land, the endowment funds, the reserve accounts is for the beneficiaries, that these lands are not owned by the state but are only managed by the state. She continued, stating that the lands are owned by the beneficiaries. **Ms. Echeverria** stated that the importance of appropriately managing these assets and stated that the Idaho School Boards Association believes that the philosophy of the board's long-term asset management plan is sound and should continue to be followed. Addressing the issue of diversification of the portfolio, **Ms. Echeverria** stated that the Association believes the managers should reposition the portfolio to maximize the benefits for the beneficiaries. She encouraged the committee to read the PAG report presented by **Dr. Jay O'Laughlin** entitled "*Idaho's Endowment Lands: A Matter of Sacred Trust.*" She added that the mechanisms that are now in place are the best ones for the long-term viability of the trust. She stated that the position of the Idaho School Boards Association is that no law should be enacted that limits the viability of the trust and its long-term benefits

Mr. Peterson explained that the University of Idaho is the beneficiary of three land endowments: the University of Idaho endowment, the Science School endowment and the Department of Agriculture endowment, encompassing slightly more than 164,000 acres. He continued, explaining that for general fund dollars going to the four four-year institutions, for every dollar of endowment earnings we receive under the formula, they lose one dollar of general fund money. He expressed the appreciation of the University for the Land Board, the Department of Lands and their staff, stating that the University believes they are making significant strides with improved administrative management practices to keep up with the times. **Mr. Peterson** described the recession faced in the 1980s and how it was faced by the state executive and legislative branch, paying special note to the contribution of the efforts of former **Governor Batt** and his budget director **Mr. Mike Brassey**, who set up the earnings reserve fund to level up the annual endowment payments.

Senator Siddoway asked **Superintendent Luna** to address his position related to selling land when schools are in need of money, whether we utilize the benefits from the trust to beef up the schools or hang on through good times and bad and keep those lands at all costs. **Superintendent Luna** stated that he did not think it is wise to sell any of the assets of the endowment and distribute the money made from the sale. He acknowledged that through proper management we do sell some assets within the endowment and use that money earned and invest in other higher return investments generating more assets for the endowment, but he emphasized that it is unwise to distribute the corpus. **Senator Siddoway** asked **Superintendent Luna** to explain in more depth the term "corpus," as it relates to the storage facility. **Superintendent Luna** identified "corpus" as timberlands, grazing land acreage, cottage site leases, and storage facilities and other properties that generate rental income. He continued, stating that regardless of initial investment, when we sell it, whatever we collect in sales is the money that stays in the corpus – it just makes that larger and if the corpus is larger, we should in turn spin-off more revenue.

Representative Bedke asked the panel to share their thoughts on how the legislature could do better in their role as manager, overseeing the Land Board.

- **Ms. Boeckel** commented that the board has paid professionals, experts reporting to the Land Board and that the board should hold these professionals accountable, as ultimately the Land Board Commissioners themselves are held accountable. The Idaho PTA & Children’s Land Alliance Supporting Schools believes that all lands should be providing revenue. Additionally, she stated that there is a need to educate the public on how endowment lands are different than public lands and to encourage them to ask more questions.
- **Superintendent Luna** stated that he believed that they are making headway now with the cottage site leases because of the proposal put forth by **Secretary of State Ysursa**. He emphasized the need for the Land Board to maximize return and to this end he encouraged the Land Board to explore trading with the federal government for lands available that they have access to in an effort to open up landlocked properties.
- **Director Echeverria** reemphasized the importance of a diversified portfolio, reiterating **Secretary Ysursa’s** advice to avoid putting too many eggs in one basket.
- **Mr. Peterson** commented that there are non-productive lands out there yet, by and large, the landlords and the Department of Lands staff has been very good for us to work with given the current constraints of the law. And, he continued, they are pleased with the work of the members of the Land Board and Department of Lands staff as they work through the challenges. He added that at this time they do not anticipate a need for help from the legislature.

Representative Bedke commented to the panel that the legislature is struggling with the underperforming assets in the portfolio. He asked them to discuss principles they should steer by when reinvesting and he asked them if the state should compete with the private sector in real estate.

Superintendent Luna emphasized the need for a level playing field when planning to provide for the future. He also expressed his concern for the current beneficiary, that they are paying the price when the endowment purchases property that was previously on the tax rolls, that money will not be collected by local school districts for local schools for bond debt service or supplemental levies. **Ms. Boeckel** stated that there should be an undivided loyalty to the beneficiaries and no other factors should be considered. **Ms. Echeverria** stated that all kinds of institutions don’t pay property taxes and that the suggestion that an unfair advantage is enjoyed by the state does not take into consideration the many restrictions the board presently faces in buying and selling land.

Cochairman Raybould discussed the offset involved with this situation, and suggested that perhaps the legislature should look at how to level that portion of what goes in the tax roll and what comes off the tax roll and explore compensation solutions. **Representative Burgoyne** cautioned the beneficiaries, noting that where there is lessened red tape in asset reinvestment, there may be a loss of the level of transparency that the government provides. He emphasized that what appears to be a short-term advantage could have a very significant long-term cost.

Kathy Opp introduced Panel 4 – Idaho Endowment Reform: Robert M. Maynard, Chief Investment Officer, PERSI; and Clive Strong, Division Chief, Natural Resources Division, Office of the Attorney General.

Mr. Maynard referred to his PowerPoint presentation entitled “*Idaho Endowment Reform*” (Tab 10, DOL Binder). He stated that the purpose of reform was to put in place a mechanism by which policy makers could discuss the questions and look at the major issues that are being discussed today, how to treat current generations versus how to treat future generations and how to best invest the assets. He chronicled the history of the structure of the Land Board and the Endowment Board and in-depth detailed challenges addressed via endowment land reform and their proposed solutions:

Problems addressed via reform:

- No central organization, but rather two entirely separate departments
- No policy control over distributions or cash flow
- Underperforming assets
 - Endowment fund
 - Cropland, grazing land, cottage sites
- Lack of diversification, exposure to volatility
- Short-term orientation

Proposed solutions:

- Centralize overall trust management
 - Land Board policy and strategy oversight
 - Endowment Board report to Land Board
- Allow expansion investment flexibility
 - Expand endowment beyond fixed income
- Expand management flexibility
 - Create earnings reserve as “shock absorber”
 - Use timber sale money to smooth distributions
 - Create Land Bank for land management

Mr. Maynard continued, discussing the creation of two tactical implementing agencies, the land trust (current Land Department) for the tactical policy with regard to timber, cropland grazing land, cottage sites and minerals and the financial trust (Current Endowment Board) for the tactical policy regarding the earnings reserve, endowment and Land Bank. **Mr. Maynard** stated that this shifted the way the moneys were handled - instead of separate areas with separate iron clad policies, all income would be placed in the earnings reserve and it would be the mechanism for facilitating focus on policy calls. Additionally, the Land Bank would operate under the financial trust, structured to allow the appropriate people to address the appropriate policies. He stated that prior to reform you could not address them.

Referring to a report prepared by **Mr. Strong** along with **Mr. Maynard**, “*Overview of Land Board Endowment Reform*” (Tab 11, DOL Binder), **Mr. Strong** discussed the creation of the 1996 Governor’s committee addressing endowment reform and moving forward to the present. He discussed the charge of the Governor’s committee, to establish a framework, in a transparent way, to take into account balance opportunities with the risk related to the projected return on assets. He stated the importance of focusing on the portfolio as a whole. He recounted that in 1998, when a legislative committee headed by **Senator Danielson** and **Representative Deal** considered what kind of constitutional amendment would be necessary to accommodate reform, they looked to make several changes to Article IX, Section 10, to provide flexibility to diversify. He continued, stating that they looked to Section 4 for the ability to establish an earnings reserve fund governed by the prudent investor rule. In this manner, a maximum long-term return could be determined. **Mr. Strong** also stated that a proposal was to create the Land Bank for the purpose of repositioning the assets. There was, at that time, litigation over grazing lands so the desire was to create a way to provide more flexibility. Referring to his report, **Mr. Strong** chronicled the recommendations of the ad hoc evaluation committee under **Governor Kempthorne** in 2001, the 2005 Endowment Fund Reform Review Task Force, and the 2009 report and recommendations for the State Board of Land Commissioners.

Representative Vander Woude asked **Mr. Strong** if he would be willing to accept changes the legislature believes are necessary. **Mr. Strong** clarified that he was presenting at the meeting as the attorney for the Land Board. He stated that it is his job is to advise and determine risk. He continued, stating that this is a shared responsibility and that they all have roles that need to be taken into account. He added that everyone should be open to suggestions, keeping in mind the responsibilities of the constitutional requirements and everyone should be willing to discuss any suggested changes that would enhance or facilitate the purpose of the trust.

Senator Siddoway asked **Mr. Strong** for the rationale the Attorney General had in bringing suit. **Mr. Strong** responded that the Attorney General wears several hats in his official capacity. **Mr. Strong** stated that the Attorney General sits on the Land Board in his defined capacity but also he must fulfill his role as chief legal officer. He said that as the Attorney General he has a responsibility to try to protect the public trust and when the Attorney General believes the board as a whole has acted outside that trust, then he has an ethical obligation to address it. **Senator Siddoway** asked **Mr. Strong** whether he believed the Attorney General also had an ethical obligation to support the decisions of the board. **Mr. Strong** replied that as a member of the board he consulted with the Idaho State Bar and it was determined that there was a need to appoint outside counsel to represent the board.

Cochairman Pearce asked **Mr. Strong** whether the Attorney General should come off the Land Board and **Mr. Strong** stated that would be a policy decision. In response to a follow-up question by **Cochairman Pearce**, **Mr. Strong** stated that the Land Board needs an open process that is accountable to the beneficiaries. He stated that the board needs people that have the capability to analyze the legal transactions and ensure stability of the program itself.

Representative Burgoyne asked **Mr. Maynard** if the Land Board had yet addressed the question of what constitutes acceptable risk, from an endowment policy perspective (safest investment versus long-term return). **Mr. Maynard** stated that what is required is a broad range of investments across a wide diversity of potential returns. How much risk and over what time are you thinking about return are questions answered by a broad set of policy makers rather than a computer. **Representative Burgoyne** followed-up stating that he believed the question comes down to how much risk the board is willing to take. He asked **Mr. Maynard** if the Land Board has any quantification that reflects what the board regards as acceptable risk. **Mr. Maynard** replied that the Land Board and the Endowment Fund Investment Board take a lot of time looking at these issues and **Mr. Larry Johnson** and **Ms. Richelle Sugiyama** can add their input during their panel presentation tomorrow. **Mr. Maynard** then stated that **Senator Burgoyne's** question about acceptable risk is difficult to answer because of the multifaceted definition of the word "risk." He concluded by saying that you can't answer the question without first addressing what the goals are.

Mr. Strong agreed with **Mr. Maynard** on the question related to defining or quantifying acceptable risk. Additionally, he stated that the Land Board has spending rules that try to address these issues and that today we are looking at the whole, which in the long term will provide a better rate of return and overall balance.

Representative Vander Woude asked **Mr. Strong** to explain why the stated goals are for diversification of investments yet there is talk of divestment from all residential lots. **Mr. Strong** stated that with split ownership there is an economic advantage to try to move the cost to the other side of the equation. In this situation, the board is looking to divest that asset and invest the money in something with a better

overall rate of return. He stated that on diversification into commercial property, the question is what type and how much. He added that this is a valid policy question to evaluate.

Cochairman Pearce asked **Representative Burgoyne** if he agreed to move his presentation regarding House Bill 188 to Tuesday morning at 8 a.m. **Representative Burgoyne** agreed. The meeting continued with public testimony:

Mr. John Eaton, Idaho Association of Realtors, addressed the committee. He stated that he does not support the board's decision to increase their activities to invest in a number of commercial properties. It is his view that it is an improper role not only that the government competes with the private sector, but also because they will be creating market places and affecting market places more than just the competition between two businesses. He explained that the board's diversification isn't diversifying by trading one stock for another, but by diversifying going from one business type to another. He emphasized that there is a difference between the public and the private sector. He would support the legislature addressing this concern.

Mr. Robert Forrey, former Idaho state legislator and a member of the Tax Accountability Committee addressed the committee and submitted written public testimony for review. **Mr. Forrey** responded to a statement presented earlier, "(i)f we sell the land we'll have nothing left." He stated that this is not true, that the money from the sale goes into the permanent endowment fund and it grows. Regarding the concern for security of the endowment fund for future generations, he stated that the Land Board has injected itself into the competitive free market, it has taken a business license, and that this type of activity was never intended. **Mr. Forrey** read from the opinions of the Idaho Supreme Court regarding investments related to endowment lands. **Mr. Forrey** then read from the Sections 57-117 and 57-715, Idaho Code, which define education endowment funds. He stated that the Land Board is speculating in its commercial efforts and quoted from an Attorney General opinion and court rulings when he stated that land endowment investments must enjoy a guarantee of full repayment, an unconditional promise to repay and security must be guaranteed. He concluded by emphasizing that speculative investments in commercial businesses do not have a guarantee on long-term financial return. He added that the interim committee is in a good position to present legislation to stop the Land Board action and he encourages the legislature to take action so that the issue does not have to be settled in our courts.

Ms. Rachel Gilbert, resident of Boise, former Idaho state legislator, real estate investor and member of the Tax Accountability Committee addressed the committee. **Ms. Gilbert** stated that the state is in competition with free enterprise when they get involved in commercial properties and though the state calls it diversification, she calls it competition with free enterprise. She stated that this constitutes a dangerous shift toward socialism and it guts the property tax base. Additionally, she stated that the state owns 52 parcels of land in Ada County and 15 parcels within the city of Boise. She provided data on vacancy rates in the city of Boise and she reiterated her concern that the state is involved in commercial properties and asserted that the legislature needs to get a handle on this state land grab. **Ms. Gilbert** stated that she is baffled by the statement that the endowment fund is the Land Board's private fund and is not subject to the legislature. She concluded, stating that she believes that Article IX authorizes the legislature with the responsibility to control the Land Board pursuant to state law and she asks them to do so.

Mr. Maurice Clements, resident of Nampa, Idaho, a former state legislator, a member of the Tax Accountability Committee and also representing himself was the next individual to address the committee. Regarding House Bill 188, **Mr. Clements** stated that he hopes the legislature favorably

considers it, though he doesn't believe it goes far enough. He stated that the Endowment Fund is supposed to be non-speculative and he thinks the Land Board is moving away from the that position right now. In closing, he asked that the committee consider the possibility of disposing of the Endowment Fund, allowing the private sector to step in where it would pay associated property and income taxes.

Mr. George Kirk, resident of Hailey, Idaho and in professional real estate investment, addressed the committee and submitted public testimony for review. He commented on the controversy and the board's ownership of self-storage as well as involvement in the retail sector. He asked the committee to remember we are talking about endowment lands, to continue to differentiate between endowment lands and state lands. He identified the controversy related to the appropriateness of the Department owning some modicum of traditional real estate investment and he thinks that it is highly appropriate and imperative. He said that the structure of the Land Board requires that they seek a balanced investment portfolio. In closing, he stated that given the returns, the yields, and the risk, the board should invest in traditional real estate investments. He continued, stating that he saw nothing nefarious with the state doing its due diligence, developing a proposal in order to evaluate what the costs are and ascertain the risk and reward associated with a tenant's use of a particular piece of property.

Representative Vander Woude asked **Mr. Kirk** what is the expected return for commercial real estate. **Mr. Kirk** stated that that differs from individual to individual, though a yield of less than five percent is not tolerable by anyone and a yield approaching ten percent is preferable to everyone. It all depends on the market place you are in.

Senator Siddoway asked **Mr. Kirk** if he thought it was a flawed rationale to assume people naturally go with the least expensive alternative, as we evaluate the competition of the state enterprise that does not pay property tax versus the private enterprise that pays property tax. **Mr. Kirk** stated that it was a flawed rationale. He stated that if the state is a more able competitor than everyone else in the market place then perhaps that theory has some validity. He went on to say that markets are made on the demand side and needs to be understood in that context. **Senator Siddoway** responded, saying that the state has an unfair advantage in some instances. **Mr. Kirk** stated that there are other significant institutional investors in the market place, PERSI for instance. He said that he finds the notion that the endowment beneficiary is more competitive than the others to be a stretch.

Representative Burgoyne discussed an example related to a life insurance agency's choices when they purchase land on which a storage facility business operates. He asked **Mr. Kirk** in this instance does the agency own the business operation end. **Mr. Kirk** responded that he did not have the answer to that question. He concurred with **Representative Burgoyne** when the Representative stated that the agency's expertise was in land ownership, the improvements and in leasing. He stated that in terms of traditional real estate ownership, self storage is right on the edge. **Representative Burgoyne** followed-up, asking **Mr. Kirk** if, when he was on the 2009 Endowment Lands Transaction Advisory Committee, his position was that the Endowment Committee members should get in the business of operating for-profit businesses. **Mr. Kirk** stated that the charge of the members of ELTAC was to conduct an impartial review of the Admission Act to identify any impediments to conducting real estate transactions in the 21st century so the make-up of the portfolio was out of their purview.

Mr. Todd Hatfield, resident of McCall, Idaho and representing himself addressed the committee and submitted public testimony for review. He stated that he wished to make some comments regarding the Idaho and United States Constitution. He stated that **Mr. Maynard's** 1998 paper downplayed the

continued timber revenues and he pointed to **Representative Burgoyne's** question of what is an acceptable level of risk. **Mr. Hatfield** responded to this question stating that he believes that the board sees no minimum risk. In concluding, he stated that he agreed with the founders, that we should keep with traditional investments and how they are managed.

Mr. John Runft, taxpayer, member of the Tax Accountability Committee and a lawyer in Boise addressed the committee. **Mr. Runft** stated that the issue is identifying where the legislative authority ends and the constitutional authority begins. He suggested that the Supreme Court discusses this issue in various court opinions and he states that the legislature may need to get direction from the Idaho Supreme Court to help identify the power of the legislature in this area as well as where the constitutional power of the Land Board begins.

Cochairman Pearce adjourned the committee at 4:35 p.m.

The Committee reconvened at 8:00 a.m. on Tuesday, August 30, with **Cochairman Dell Raybould** chairing the meeting. All Committee members were present with the exception of Senators Cameron and Werk who were absent and excused.

The first matter taken up by the Committee was a discussion of HB 188 as proposed during the 2011 legislative session. **Representative Grant Burgoyne** addressed the Committee regarding Section 58-104, Idaho Code, which is reflected in Section 1 of HB 188. **Representative Burgoyne** noted that in terms of the power of the state land commissioners to exercise the general direction, control and disposition of the public lands of the state, the proposed amendment would add an exception to provide that except in those instances where the land is used by a public entity for a public purpose, all nonagricultural improvements on the land shall be leased to private persons, and all business operations located on or using the land shall be sold to private persons.

Representative Burgoyne also provided the committee with a copy of an Attorney General's opinion regarding HB 188. The Attorney General indicated that he saw a constitutional problem with Section 1 of HB 188. However, the Attorney General also left open the door for the legislature to regulate in this area. The Attorney General, in its opinion, stated that "(a)ny legislative prohibition on Board operation of businesses on endowment lands would have to be carefully drafted to exclude any operations that fall under the umbrella of "land business.""

Representative Burgoyne noted that Section 2 of HB 188, relates to Section 58-133, Idaho Code, regarding the land bank fund. The proposed amendment would provide that the land bank fund was created for the purpose of temporarily holding and allocating proceeds from land sales to the respective permanent endowment funds involved in such sales. The proposed amendment would also provide that proceeds from the sale of lands which are a part of one or more endowment land grants shall forthwith be allocated to and deposited in the permanent endowment fund of each respective endowment along with any earnings on said proceeds. **Representative Burgoyne** directed the committee to Section 5(a)(2)(A)(ii) of the Idaho Admission Bill reflecting language similar to the current statute.

Representative Burgoyne then went on to the proposed amendment of Section (3) of the Section 58-133, Idaho Code, which would take away the land board's ability to hold proceeds for a period of time not to exceed five years. The Attorney General essentially said that Section 2 of HB 188 would be constitutional but opined that it would be a good idea to include some statement of purpose or finding to make it clear that prohibition on use of land bank funds to purchase land for the benefit of endowed

institutions is taken solely to protect the interests of the trust beneficiaries and is not intended, in whole or part, to protect or benefit other persons.

Representative Burgoyne then distributed an exhibit used at the committee hearing on HB 188 by former Representative Robert Forrey. That exhibit reflects a certificate of assumed business name of “Affordable Self-Storage” by the State Board of Land Commissioners as trustee for the Idaho Endowments. **Representative Burgoyne** noted that there is a distinction that the Idaho Constitution, the Admissions Bill and the statutes make it clear that the State Land Board can buy land and they can use the proceeds to buy land but it doesn’t say they can buy a corporation or limited liability company or partnership. He said that he believes that is an important distinction that has become blurred. He said that HB 188 provides that when the State Land Board buys land and improvements thereon, they don’t operate the business being operated on that land. **Representative Burgoyne** said that his concern is that if we continue on the path we’re on we will end up doing more harm to the endowment than good. He noted that he is concerned with politicizing the economy and the fact that the character of the endowment would change substantially. He continued that the endowment would be more exposed to the ups and downs of the economy. In addition, he noted what it would do to government itself. He said that if there is a potential three billion dollars on the table from the endowment lands, even good people would find themselves tempted. He said that this issue is coming up now because we are under financial pressure. He said that quick gains today may prove to be no gains at all and perhaps losses in the long run. He added that the endowments cannot be managed for today only.

Cochairman Representative Raybould asked whether the Committee had any questions. **Senator Shawn Keough** asked whether there are any definitions for “non-agricultural improvements” and “business operations.” **Representative Burgoyne** deferred to **Mr. John Runft** who responded that in other places in the Code, “agricultural” is defined and that the word “improvement” has a legal meaning although some definitions could be added to bolster the proposed legislation. **Senator Keough** noted that in some definitions, “agricultural” includes timber and in others it does not. “Business operations” is also troublesome so as we move forward she would like clarification in the form of definitions.

Senator Jeff Siddoway commented that the Department of Lands has historically been involved in some way or another with business in the state and would also like clarification as to what the terms mean. He said that throughout history, the Department has owned buildings and equipment. He also had a question as to the proposed changes to the five-year period of time in which the Department is allowed to hold proceeds from the sale of land. **Representative Burgoyne** responded that he is not here to question the investment decisions of the board in general but in one area only – that being the ownership and operation of a for-profit business. He added that in terms of the land bank fund, from his perspective that he questions whether the land bank fund is being used properly when used to purchase and operate non-agricultural businesses. **Senator Siddoway** asked whether the bill would allow the board to take furniture out of a building it purchases and act to sell those items and then act as a realtor to seek someone to rent the building – whether all of those activities would be alright. **Representative Burgoyne** responded that would be correct.

Cochairman Senator Monty Pearce inquired about the history of the land bank fund. **Mr. Clive Strong** responded that it was created in 1998 as part of the endowment reform.

Representative Scott Bedke asked how **Representative Burgoyne** squares the presentation by **Mr. Dennis Colson** regarding the fact that the framers of the Idaho Constitution had no problem having competition with a for-profit business owned by the endowment. **Representative Burgoyne** responded

that **Professor Colson** related a number of different thoughts that ran the gamut. He continued that from his perspective, the debates that were held at the time the constitution was written really don't matter unless the constitution or statutes are unclear. He added that the world has changed a great deal and what may have been acceptable then would not be now.

Cochairman Representative Raybould stated that he assumed **Representative Burgoyne** and **Representative Vander Woude** would put together some revisions to the proposed legislation.

Panel 5 – Land Assets Owned in Trust was the next panel to address the Committee. According to the Department, the purpose of the panel is to provide a more detailed review of endowment land assets, their contribution to overall portfolio performance and the risks and opportunities associated with each asset type. Of the original 3.6 million acres of land granted to Idaho upon statehood, approximately 2.5 million acres remain. The Department manages the land assets for a variety of uses, including renewable timber harvest, farming, grazing, communication site leases, mining, residential leases and other commercial activities. The estimated value of trust lands is over \$2 billion dollars. The majority of revenue generated goes to support K-12 public education. The panel was comprised of **Ms. Kathy Opp**, Deputy Director, Idaho Department of Lands, **Mr. David Groeschl**, Division Administrator – Forestry & Fire, Idaho Department of Lands, and **Mr. Bob Brammer**, Division Administrator – Lands, Minerals & Range, Idaho Department of Lands.

Ms. Kathy Opp was the first member to address the Committee. **Ms. Opp** indicated that the trust assets consist of land assets and financial assets, specifically the permanent fund and the earnings reserve. She said that there are 2.4 million acres of land, comprising 4.6% of the land base in Idaho.

Ms. Opp indicated that there is approximately \$1.2 billion in the financial asset allocation. The Endowment Financial Investment Board recommends the mix of financial investments and use professional fund managers to do so. According to **Ms. Opp**, land asset allocation is valued at approximately \$2.3 billion, with thirty-eight percent in agriculture and rangeland, forty-eight percent in timberland, thirteen percent in residential real estate and two percent in commercial real estate. **Ms. Opp** stated that whole trust management, with a diversification of assets, minimizes risk. Whole trust management was a key concept in endowment reform.

Ms. Opp indicated that the purpose of endowment management is to maximize financial returns over time, to maintain or improve revenue generating capacity of land, and to provide a stable and perpetual distribution of income to the trust beneficiaries. **Ms. Opp** also addressed the prudent investor standard of care as provided by Chapter 5, Title 68, Idaho Code.

Ms. Opp stated that an asset management plan is important to ensure assets can be managed, preserved and protected for long-term goals and strategy, to define over-arching beliefs and philosophy about a set of collective investments, and includes elements of financial analysis, asset selection and divestiture, asset allocation/diversification, plan implementation and ongoing monitoring of the investments and assets.

Ms. Opp then addressed the endowment beneficiaries. There are nine endowments with 14 legal beneficiaries, the largest of which is public schools. **Ms. Opp** noted that from 1995 to 2010, approximately \$548 million was the cumulative public school distribution with approximately \$254 million being the cumulative distribution to other institutions. From 2001 to 2011, the average timber

revenue available for beneficiary distribution was \$43 million and the average for other revenue available for beneficiary distribution was \$4.7 million.

Mr. David Groeschl was the next Panel 5 participant to present to the committee regarding forest management on state trust lands. **Mr. Groeschl** noted that seventy-five percent of the forest land in Idaho is owned by the federal government. Fifteen percent is privately owned and five percent are state trust lands. The other five percent include fish and game, parks and recreation and the department of transportation. **Mr. Groeschl** indicated that harvest and employment relating to timber has declined by fifty percent since 1990.

Mr. Groeschl noted that about eighty-five percent of the total land asset revenue comes from the forest management program. He stated that the ten-year average annual net revenue is approximately \$43 million and that for every dollar we spend we generate about \$3.56.

Mr. Groeschl then discussed the trust land harvest volume and value from 1951 through 2010. We harvested 11.2 Bbf, generated \$1.3 billion in gross revenue, generating eighty-two percent of total revenue in the last twenty years.

In terms of continuing to maximize returns and maintain or improve the revenue-generating capacity of endowment timberlands into the future, **Mr. Groeschl** informed the committee about the forest asset management planning process. **Mr. Groeschl** indicated that the following elements were addressed: business-market changes and risks, technological/operational changes, biological changes and risks, ownership and management changes, climate change and forest functions. He went on to state that current and future challenges and risks include economic times and market volatility, forest industry infrastructure, staffing, forest ownership changes and conversion, biological risks, social and political support and legal challenges.

Mr. Bob Brammer presented the Committee with information relating to the net income performance for all other types of assets. The other assets do not show the volatility of the timber revenue. There are seven asset classes including rangeland which is the largest with approximately 1.4 million acres and which is typically used for grazing. He noted that commercial asset class includes about 15,000 acres that includes not only office but also industrial, communication sites, commercial outfitter and guide leases, and wind energy leases. The residential asset class consists of the cottage sites at Priest Lake and Payette Lake and cover about 700 acres. The agriculture asset class has about 15,000 acres that are actively farmed. The conservation asset class includes 22,000 acres, lands involved in the CRP and lands leased to fish and game for wildlife habitat. The recreation asset class and minerals asset class – with no lands classified as such now. These typically fall under one of the other classes as the primary use.

Mr. Brammer went through each rate of return for the various classes. He stated that the rangeland class is break-even at best. The commercial assets reflect 1.23 percent return and during the last few years they have been conducting maintenance on such assets which is reflected in the rate of return. They expect that in the future these will have greater returns. The residential asset class barely meets the target. The agriculture class is less than targeted. **Mr. Brammer** indicated that when we look at opportunities to move the returns to a higher level, they envision over the next twenty years to move from \$5 million currently to \$52 million, primarily through commercial properties which he indicated has the highest earning potential of any of the asset types they have.

Mr. Brammer also updated the Committee on oil and gas in Idaho. The Department is involved in some endowment trust land leasing relating to oil and gas, with the leases being auctioned. In addition, the Department is involved in the Oil & Gas Conservation Commission. The commission is made up of the top five elected officials in this state.

Representative Mike Moyle asked for further explanation about several of the asset class returns. **Mr. Brammer** explained why some of net revenues are less than one would expect. He stated that some represent a very small number of acres or have certain irrigation issues where they don't own the water rights. **Representative Moyle** also asked about mineral rights on certain lands near Emmett. **Mr. Brammer** indicated that they have had a number of questions relating to Scottish Bank and those leases are related to Bridge Energy. He said he doesn't think it is tied only to state lands. **Representative Moyle** asked if **Mr. Brammer** thinks legislation is needed. **Mr. Brammer** responded that he is not aware of it at this time. He added that some of the surface rights issues are being addressed through the Department's rules.

Representative Bedke asked **Ms. Opp** about additional details relating to the represented rates of return. **Ms. Opp** addressed the returns of the various assets and responded that the discount rate that used was six to seven percent. **Representative Bedke** also asked how they are valuing timberland. **Ms. Opp** said that it really depends on the conditions. **Ms. Opp** went on to say that they were generally seeing about \$1,500 an acre. **Mr. Groeschl** added that the value of timberlands varies quite a bit from around \$850 to \$1,800 per acre based on location, productivity, species composition, etc., **Mr. Groeschl** responded to another question by **Representative Bedke** that the \$3.50 rate of return is a statewide average and that it varies from market to market.

Representative Bedke then asked how variability is any different in the commercial world. **Mr. Groeschl** responded that he wanted to make it clear that the Department is not opposed to acquiring good timberland in core market areas. The issue becomes one of availability and the willingness of the private sector to give those up. The other issue, he stated, is one of the percentage of ownership. It becomes a matter of dilution. **Mr. Groeschl** said that on the commercial side the percentage of ownership is far less.

Representative Bedke commented on the changes contemplated in HB 188 or its revised form, and asked whether that affects the vision of the Department. **Ms. Opp** responded that to the extent they are talking about commercial buildings, they see that as a valuable component to diversification and, with respect to the storage facility, it is the highest earning asset in the portfolio

Representative Moyle asked what the storage facility paid in taxes and what their rate of return would be if they had to match that. **Ms. Opp** responded that she thought it was \$24,000 to \$30,000. That would drop the return into the six to seven percent range.

Senator Michelle Stennett asked once the wells are up and running whether the state would be taking that over. **Mr. Brammer** responded that a contractor with Bridge Energy would be conducting the fracking and that the state has no intention of taking over the operation of the wells. That would be through their lessee, Bridge Energy. **Mr. Brammer** went on to explain the increase in permit fee would be to cover their administrative costs to process the application, coordinate with water resources, etc., **Senator Stennett** also questioned the need for environmental oversight. **Mr. Brammer** responded that the Department would have oversight of those issues on any well, whether endowment or private.

Representative Ken Andrus asked about some news mentioning the state taking over land owned by the federal government. **Ms. Opp** responded that a group of county commissioners had reorganized a task force regarding a pilot project associated with the management of certain federal lands for the benefit of rural schools.

Representative John Vander Woude asked about the transition to commercial property projecting revenue increases from \$5 million to \$52 million. He wanted to know how much the state would have to put into that property. **Mr. Brammer** responded that they used the projection of about half the value of the cottage sites which is approximately \$100 million.

The next panel to address the Committee was Panel 6 for the purpose of addressing the management of financial assets in trust. The Department's executive summary for Panel 6 provides that all proceeds from land management activities are passed to the Endowment Fund Investment Board. The nine members of the Board currently manage financial assets of the nine land grant endowment funds totaling approximately \$1.2 billion. Over the past five years, the endowment fund's returns have been in the top 25% of public funds in the nation. The purpose of the panel is to gain a better understanding of the principles of managing financial assets with prudent and professional management practices used by large institutional investors. Speakers on the panel included Mr. Larry Johnson, Manager of Investments, Idaho Endowment Fund Investment Board, and Richelle Sugiyama – Expert financial advisor for the Public Employee Retirement System of Idaho.

Ms. Richelle Sugiyama was the first panel presenter to address the committee. **Ms. Sugiyama** stated that investment principles include investment to meet liabilities and diversification to reduce risk. She indicated that key considerations in investing to meet liabilities are the level of return, need for real or nominal returns and the time horizon. In addition, there must be a determination of equity or fixed income preferences.

Ms. Sugiyama noted that key investment concepts include expected return which is what an investor expects to make from a particular investment and risk, which is the possibility that the expected return will not be earned (measured as the difference between the actual return and the expected return). She indicated that one key concept is that assets with higher long-term returns have greater risks.

Ms. Sugiyama went on to state that about 2/3rds of annual returns are within one standard deviation of the expected return, 95% are within two standard deviations and 99.5% are within three standard deviations.

In addressing the issue of risk, **Ms. Sugiyama** stated that holding only a few "safe" assets is more dangerous than owning many assets, including some exposure to "risky" assets and that one should avoid extreme results.

In summarizing her presentation, **Ms. Sugiyama** noted that there are three factors in investment theory: Expected returns, the variance (risk) in those returns, and the co-movement (correlation) of the returns. She indicated that the primary principle is diversification and that the main purpose is to put together a mix of different assets in a manner that reduces the risk and is for a given necessary level of return.

Ms. Sugiyama then addressed portfolio considerations and implementation. She indicated that some considerations are the governance structure, resources and investment policy. Implementation considerations are whether you want a simple vs. complex model, internal vs. external management and

active vs. passive management. Finally, **Ms. Sugiyama** addressed asset allocation of public funds, the range as well as the average.

Mr. Larry Johnson was the next panel presenter to address the committee relating to an overview of the Idaho Endowment Fund. He stated that trust assets overseen by the board include the Endowment Fund, the State Insurance Fund, the Judges' Retirement Fund and the Parks and Receptions Endowments. He noted that the mission of the Endowment Fund Investment Board is to provide professional investment management services to their stakeholders consistent with their constitutional and statutory mandates.

Mr. Johnson noted that the board is made up of nine members, appointed by the Governor and confirmed by the Senate. There are two legislators on the board, one professional educator and six members of the public familiar with financial matters. The board meets at least quarterly and has a full-time staff of four.

Mr. Johnson stated that the basic guidelines for fund management are in the Land Board's Asset Management Plan. As perpetual funds, per our state constitution and statutes, the endowment funds have a long-term investment horizon. He added that market risk is mitigated by investing in diversified portfolios. **Mr. Johnson** noted that the asset mix of the fund takes into account the entire endowment portfolio, in other words, the fact that the revenues of the endowment lands, net of Department expenses, will be contributed to the endowment funds. **Mr. Johnson** stated that the five elements of fund diversification include the risk of return, region, investment style, size and active vs. passive security and industry selection.

In terms of objectives for determining distributions, **Mr. Johnson** stated that they look to avoid reductions in total endowment distributions, maintain adequate earnings reserves to protect distributions from temporary income shortfalls and grow distributions and permanent corpus faster than inflation and population growth. Current distributions are 4-5% of each endowment fund. Rates are based on expected sustainable income from the fund and from the land, expected rate of inflation, expected growth in population and adequacy of the earnings reserve.

In concluding his presentation, **Mr. Johnson** stated that in support of each endowment's goal of providing perpetual distributions to its beneficiaries, the board manages a diversified portfolio of securities to obtain a reasonable long-term rate of return. He added that today's distributions must be balanced with the need to retain funds for future beneficiaries. He stated that the amount of distributions is driven by both the expected level and the expected volatility of both fund returns and land revenues and efforts to improve fund and land returns and reduce their volatility will result in higher distributions.

Senator Siddoway asked about the proposed changes represented in HB 188, as discussed during the meeting, particularly the proposed elimination of the ability for the commissioners to hold proceeds in the land bank fund for a period not to exceed five years. **Senator Siddoway** asked how long, on average, proceeds are held. **Mr. Johnson** responded that it depends on whether there is an attractive investment available. He added that the land bank has only been in existence since 2000 and, on average, it has take almost five years to reinvest proceeds.

Senator Steve Bair asked if a piece of property is sold and the money goes into the land bank fund and stays there five years, under HB 188 it would have to move into the endowment fund. In the event that

happened, he asked whether that money could ever be taken out of the fund and used to purchase land if that was a good investment at the time. **Mr. Clive Strong** later responded to this question. Please see page 27 of the minutes.

Panel 7, representing the customers of the endowment, were the next to present to the Committee. The Department, in its executive summary for Panel 7, noted that the panel was representative of the many industries and businesses that directly and indirectly benefit from the management of endowment trust lands. The Department notes that these include the timber industry, loggers, ranchers, farmers, miners, property management companies, truckers, equipment dealers, parts dealers, mechanics, consultants and many others. Panel members included Mr. Bob Boeh, Idaho Forest Group, Mr. Ken Wixom, a grazing lessee, Mr. Skip Oppenheimer, Oppenheimer Development, and Dr. Peter Crabb, Professor of Finance & Economics, Northwest Nazarene University – School of Business.

Mr. Bob Boeh, Idaho Forest Group, was the first panel 7 presenter to address the Committee. **Mr. Boeh** provided the Committee with information relating to the Idaho Forest Group. He noted that they are the largest lumber producer in Idaho. The group has four mills located in north Idaho, all of which are state of art facilities. Idaho Forest Group ships products worldwide and has 550 direct employees.

Mr. Boeh stated that the Idaho Department of Lands timber sale program provides approximately twenty-five percent of log capacity needs for existing infrastructure in Idaho. The program is sustainable and renewable, reliable and stable. He indicated that the program seeks involvement on changes from customers and has been consistently customer-oriented. **Mr. Boeh** went on to state that quality timber crates a high quality product. He also noted the importance of specie diversity which allows them to meet market demands and customer needs. **Mr. Boeh** stated that stumpage on three year contracts allows for the building of a portfolio of volume under contract and the market pricing through competitive bidding provides eighty percent of endowment revenues.

Mr. Boeh indicated that the Department’s timber sale program is generally the cornerstone of the Idaho Forest Group mills annual log sourcing plan from twenty to forty percent of their mill needs. He said that it averages one in three logs used. In terms of stumpage, **Mr. Boeh** told the Committee that they can control the timing of deliveries and log lengths. He added that they also have specie to meet their customers’ needs and provides capital gains vs. ordinary income tax treatment. The contractual structure of up to three years gives the Idaho Forest Group flexibility. **Mr. Boeh** stated that the group has had a thirty-seven percent success rate on bids during the last four years. He added that they are very supportive of the state’s active management of school trust for sustainable forestry and rate the program a triple A, giving it a strong vote of confidence.

Mr. Ken Wixom, a grazing lessee, was the next Panel 7 member to address the committee. **Mr. Wixom** told the committee that he is a wool grower and a member of eastern Idaho grazers association. He said that the range industry in eastern Idaho grazing involves about 85,000 acres, 50,000 is state land, 27-28,000 is private land and the rest is Bureau of Land Management land. He added that they run approximately 6,000 head of cattle on that lease and 10,000 head of sheep. There are 52 families in their association.

Mr. Wixom continued to explain the association’s operation in eastern Idaho. He reminded the committee that they pay sales tax, property tax, taxes on equipment, etc., and that is all a byproduct of the leasing of state lands. He stated that they know two percent isn’t much for a return on the investment but the profitability is both in income and what it costs to run a business. He added that there is also recreational use on the land.

Mr. Skip Oppenheimer was the next member of Panel 7 to address the committee. **Mr. Oppenheimer** informed the committee that through a competitive bid, Oppenheimer Development Corporation was selected by the Department to perform property management and maintenance services in February, 2011. He said that the Department has approximately 112,000 square feet of office and retail space for lease in downtown Boise which represents approximately 2% of the downtown market and .5% of the Ada County market.

Mr. Oppenheimer noted that the Department's current vacancy rate is 22%. He said that downtown Boise currently has a 9% vacancy rate. **Mr. Oppenheimer** added that the Department's average asking rate is \$17.50/sf with the average asking rates for comparable space at \$15.50/sf. According to **Mr. Oppenheimer**, operating expenses are not passed through directly to tenants but rather included in base rent charges with annual operating cost adjustments made based upon increase/decrease of operating expenses of prior years to current year and also that as long as the Department continues with full service leases at market rents, there is no competitive advantage over the private sector.

Dr. Peter Crabb, Professor of Finance & Economics, Northwest Nazarene University – School of Business, was the final Panel 7 presenter to address the committee. **Dr. Crabb** noted that he prepared "*The Economic Activity of Idaho's Endowment Trust Lands*" in July, 2011, for the Idaho State Board of Land Commissioners (Tab 28, DOL Binder). He noted that the document represents current economic activity but not an impact summary. The results of his study are summarized in Table 2 as found on page 17 of the report. The results, according to **Dr. Crabb**, show that the direct, in-state expenditures by the Department's programs average \$14,410,762 annually and contribute \$26,716,911 in economic activity, supporting 218 jobs across the state. He went on to note that the estimated in-state expenditures by the beneficiaries of the endowment trust lands average \$34,216,181 annually and contribute \$56,119,437 in economic activity, supporting 915 jobs across the state. Expenditures from recreational activity on endowment trust lands are estimated at \$32,390,370 annually and contribute \$50,071,567 in economic activity, supporting 821 jobs across the state. **Dr. Crabb** noted that, in total, it is estimated that Idaho's endowment trust lands contribute \$132,907,915 in annual economic activity supporting 1,954 jobs across the state. **Dr. Crabb** proceeded through various other conclusions made during the study which are available for review in his PowerPoint presentation.

Representative Bert Stevenson asked **Mr. Oppenheimer** how many state properties are occupied by state agencies. **Mr. Oppenheimer** didn't have that information readily available and will get that information for the committee members.

Senator Stennett commented on the 22% vacancy rate. She asked **Mr. Oppenheimer** what his advice would be in terms of getting more involved in the commercial sector. **Mr. Oppenheimer** responded that the market in commercial real estate, like all real estate at the present time, is depressed. He said that vacancy rates have actually been higher than what they have seen in downtown Boise. He added that the potential to see returns go up is positive because new construction is limited and that there seems like there is an upside for existing properties relative to how the market is today.

Representative Moyle asked **Mr. Oppenheimer** whether the vacancy rate has climbed substantially. **Mr. Oppenheimer** noted that they took over the contract for management just a few months ago. He said that the philosophy of their company is that a part of reducing vacancy rates is to make sure the tenants are satisfied and that they take care of any issues the tenants might have. **Representative Moyle** also

asked how the state paid for the maintenance service. **Mr. Oppenheimer** responded that it is 4.5% of occupancy.

Representative Bedke noted to **Mr. Wixom** that rangeland grazing leases are “break even” at best. He added that cottage site owners say that they are ready to step up and buy the ground their cabins are on. **Representative Bedke** asked whether the families in Mr. Wixom’s association are ready to step up and purchase the grazing rights off of the allotment. **Mr. Wixom** responded that they have talked a bit about that and if the land went up for sale they would have to competitively bid against it against mega bidders from out-of-state. He said that he thinks that as ranchers, they are a bit better off renting from the state than buying, but they could possibly find the money if they had to.

The committee then took public testimony. **Mr. Al Marino**, Thorton Oliver Keller, was the first to testify. He said that his company manages 4.5 million square feet of commercial space. **Mr. Marino** added that he was also a member of the Endowment Land Transaction Advisory Committee (ELTAC). He said that from his perspective, money to schools is a good trade-off for any lost tax revenues. He added that, from his perspective, they haven’t seen or heard from other private owners about competitive problems with the state.

Mr. Marino told the Committee that his company also has a group that specializes in self-storage. He said that he thinks the state produces more net revenue from such an asset than others. It is not a single tenant asset, you don’t have to spend much to re-tenant and he thinks it is a good type of asset to own. **Mr. Marino** also stated that he believes owning commercial properties is a good way to diversify.

Senator Siddoway asked about Mr. Marino’s involvement on ELTAC. He asked Mr. Marino’s opinion about how long he would hold a non-performing asset. He added that he was primarily speaking of rangeland and that some Land Board members have said they aren’t willing to dispose of those lands. **Mr. Marino** said that he thinks that would have to be weighed on what the opportunities are – that any type of balancing of portfolio would be weighing what other opportunities are present.

In response to a question from **Representative Vander Woude**, **Mr. Marino** indicated that there were guarantees that values would go up but that they would hope diversification would be the most prudent strategy.

Representative Moyle asked how Mr. Marino’s company is paid for storage unit management and whether they manage those themselves or subcontract that out. **Mr. Marino** responded that they receive a percentage of overall rents collected and that they manage in-house.

Mr. John Runft provided the next public testimony. **Mr. Runft** provided various comments relating to HB 188. He discussed the difference between the province of the legislature vs. the province of the Land Board. He believes that the Land Board’s province is policy and the legislature’s province is procedure. He said HB 188 was drafted with that in mind. He referred again to the Attorney General’s opinion presented to the committee by **Representative Grant Burgoyne**. **Mr. Runft** then made some suggestions relating to the title of the bill.

Mr. Runft also addressed the issue of diversification and the prudent investment standard. He commented that it appears the investments in the permanent endowment fund are invested with a great deal of diversity and, given that, why would the Department have to do the same thing. He stated that there is already diversity present. He added that the term “prudent investment standard” has been

used again and again, and it is a sound investment standard, but it is a commercial standard. **Mr. Runft** stated that the trust is permanent, referred to as eternal, sacred, etc., He believes the prudent investment standard is needed, but may not be quite sufficient. He also said he believes there is a significant difference between leasing and managing an asset.

The final speaker offering public testimony was **Mr. Jack Harty**. **Mr. Harty** was providing testimony as a citizen but told the committee that he was also a member of the Endowment Land Transaction Advisory Committee (ELTAC). **Mr. Harty** stated that ELTAC was asked to review the Idaho Constitution, statutes and the Land Board practices and restrictions and asked to make recommendations from a business point of view about best practices. ELTAC determined that if there is a decision to dispose of any assets, the best practice would be to look at private industry and see how they have disposed of assets. The methodology of the private sector is to use techniques in addition to public auction – although he noted that we are in stressed economic times now. He went on to say that in times that are not stressed, the public sector uses all sorts of methods in disposing of property. **Mr. Harty** summarized that their first recommendation was to use modern techniques if a decision to dispose of assets is made and secondly, to allow larger increments of land to be sold when appropriate.

The final speaker to address the committee was **Mr. Clive Strong, Division Chief, Natural Resources Division, Office of the Attorney General**. **Mr. Strong** gave the committee an update regarding litigation involving cottage sites and provided the committee with a two-page summary of the litigation. He began by clarifying several questions, the first being related to the origin of the land bank. He clarified that in 1998 the first constitutional amendment relating to the land bank was passed. That was found unconstitutional. In 2000, the final constitutional amendment was enacted and we have had a land bank since that time. In regard to further clarification relating to the land bank, once money goes out of the land bank into the permanent fund, it stays there.

In regard to the cottage site leases, **Mr. Strong** said he looks at the litigation as valuable in terms of getting some clarification about the disposal of public lands at auction, particularly whether the provisions are applicable to leases or not. **Judge McLaughlin** found the relevant statute constitutional and they are now settling the record and expect to argue the case early next year.

Mr. Strong stated that the other case that is also proceeding through the courts is referred to as *Babcock I*. He told the committee that the issues in that case involve the questions of whether the leases provide an automatic contractual right to renew and, if renewal does not occur, whether there is a contractual obligation to purchase all improvements on the various cottage sites. In that case the district court held in favor of the Land Board and said the administrative procedures act had to be followed. **Mr. Strong** noted that the court entered final judgment and an appeal by the lessees is anticipated. They expect a similar timeline. **Mr. Strong** indicated that there are four other cases pending relating to cottage site rental rates. He said it is not clear in terms of a time line. They are presently stayed. The lessees and the Land Board will likely request consolidation of the four cases.

Representative Vander Woude asked Mr. Strong whether he anticipated any proposed legislation for the next legislative session relating to cottage site leases. **Mr. Strong** responded that he did not.

Senator Keough asked whether there was any work being done regarding exchanges. She indicated that she knows the Department is working on this but some other entities are also working on exchanges as well and she wondered if there were any barriers for them to do so. **Mr. Strong** responded that there

were not and that people could come forward to the Department with proposals for exchanges and they would be evaluated along with any other exchanges proposed by the Department.

Senator Pearce asked what is being done regarding 2011 cottage site leases. **Mr. Strong** responded that they should have the litigation resolved by the time the two-year leases are up.

A motion was made by Cochairman Senator Pearce to adjourn the meeting and seconded by Representative Stevenson. The meeting was adjourned by **Cochairman Dell Raybould** at 12:15 p.m.