LAWRENCE G. WASDEN
ATTORNEY GENERAL

STEVEN L. OLSEN, ISB NO. 3586
Chief of Civil Litigation Division

MELISSA MOODY, ISB No. 6027
Deputy Attorneys General
954 W. Jefferson, 2nd Floor
P.O. Box 83720
Boise, ID 83720-0010
Telephone: (208) 334-2400
Fax: (208) 854-8073

Attorneys for the State of Idaho

FILED
MAR 24 2010
Supreme Court Court of Appeals
Entered on ATS by

IN THE SUPREME COURT OF THE STATE OF IDAHO

HON. LAWRENCE G. WASDEN, the Attorney General of Idaho, *ex rel.* the STATE OF IDAHO, Petitioner, vs. IDAHO STATE BOARD OF LAND COMMISSIONERS, and GEORGE BACON, in his official capacity as Director of the Idaho Department of Lands Respondent.	**Supreme Court No.** 37528 **VERIFIED PETITION FOR ISSUANCE OF A WRIT OF PROHIBITION**

Petitioner the Hon. Lawrence G. Wasden, the Attorney General of Idaho, petitions this Court pursuant to Idaho Constitution, Article V, § 9, Idaho Appellate Rule 13(g), Idaho Code §§ 7-401 *et seq.*, and applicable substantive law, to issue a Writ of Prohibition (a) against the

COPY

Idaho State Board of Land Commissioners ("Board") and the Director of the Idaho Department of Lands (b) to prevent the following actions (c) contrary to or in excess of his/its authority under Idaho law:

(a) That George Bacon, the Director of the Idaho Department of Lands, and the Board,

(b) be prohibited and enjoined from signing and implementing so-called "cottage leases" for rental of state endowment lands held in trust for the public schools, normal schools and the Idaho State Hospital,

(c) unless and until they are leased under terms meeting the requirements of Idaho Constitution, Article IX, § 8.

In support of this Petition for the Issuance of a Writ of Prohibition, Petitioner, the Attorney General of Idaho, alleges as follows:

I. Jurisdiction

1.

This Court has jurisdiction to consider this Petition and to grant relief pursuant to Idaho Constitution Article V, § 9, Idaho Appellate Rule 13(g), Idaho Code §§ 7-401 *et seq.*, and applicable substantive law.

II. Description of the Parties and Their Roles in State Government

2.

Petitioner is the Attorney General of the State of Idaho. The Attorney General of Idaho is a constitutional office established by Idaho Constitution, Article IV, § 1. The Attorney General

is required by Idaho Code § 58-120 to represent the State of Idaho "in all suits, actions, contests or controversies relating to or involving state lands." The Attorney General has authority under the common law and under Idaho Code § 67-1401(5), to "supervise ... persons holding property subject to any public or charitable trust and to enforce whenever necessary any noncompliance or departure from the general purpose of such trust" and to "institute, in the name of the state, any proceeding necessary to enforce compliance with the terms of the trust or any departure therefrom."

3.

The Attorney General is a member of the State Board of Land Commissioners. The other members of the Board are the Governor of Idaho, the Superintendent of Public Instruction, the Secretary of State, and the State Controller. Idaho Constitution, Article IX, § 7; Idaho Code § 53-101.

4.

Under Article IX, § 8 of the Idaho Constitution, the Board is the trustee of public schools, normal schools and state hospital lands in the vicinity of Priest Lake and Payette Lake. The Constitution requires the Board to manage the state endowment lands in a manner that "will secure the maximum long term financial return to the institution to which granted or to the state if not specifically granted." Idaho Constitution, Art. IX, § 8. *See also* Idaho Code § 58-119(3) (referring to lands held in trust); § 58-133 (same); § 58-136 (same); and § 58-156(3) (declaring that "the endowment lands are held in trust by the state board of land commissioners and are managed to generate the maximum long-term financial returns to the public school endowment").

5.

The Idaho Department of Lands ("IDL") is the executive agency established to administer state endowment lands. Idaho Code § 58-101; § 58-119. George Bacon is the Director of the Idaho Department of Lands. Among other things, Mr. Bacon's duties and responsibilities include countersigning leases issued by the president of the State Board of Land Commissioners for rental of state endowment lands held for the benefit of public schools, state normal schools and the state hospital. Idaho Code § 58-121.

6.

Other real parties in interest include persons desiring to renew "cottage leases" during the upcoming calendar year, public schoolchildren, college students and patients of the state hospital, who are the beneficiaries of the three trusts involved.

III. The Board's Action on March 16, 2010 Means that the Trusts' Beneficiaries Will Not Receive the Money to which They Are Entitled Under Idaho's Constitution and Idaho Code § 58-310A

7.

On March 16, 2010, the Board voted 3-2 to implement a 4% annual rental rate, based on average property values of the previous decade, with a 5 year phase-in, and a premium rent of the greater of 10% of the gross income or 50% of the net income received by lessees when conveying leaseholds to assignees. The Board's action means that the trusts' beneficiaries will not receive the money they would receive if the Board were getting market rent for the leases, as constitutionally and statutorily required.

Board member Ysursa acknowledged that the 4% would not meet market value: "the suggested four percent of a rolling ten-year average of the five year phase-in is not talking current market value. It's talking less than four percent current market value." Exh. 36 at 23-24.

Expert economists Terry Anderson and Reed Watson agreed. They concluded that using a ten year average land value to calculate rent would "make it virtually impossible for the Land board to charge lessees 'market rent' as required by the Idaho Code" because "the state will always be earning rents based on past rather than current land values and therefore, especially during times of appreciation, will continually be below market rents." Exh. 31 at 3. Economists Anderson and Watson also expressed concern about policies that phase in rent increases or cap rent increases. They concluded phasing in target rents over a five year period "guarantees that the state is not securing market rents for the five year adjustment period [and] guarantees that the actual return will be less than the prudent market return." Id. at 4.

At the March 16, 2010 Board meeting, four of the five Board members acknowledged that the subcommittee's recommendation would not achieve a market rental rate. Exh. 42 at 28, 31-32, 35.[1]

IV. Premium Rent Occurs When Rental Rates Are Not at Market Value: an Explanation of Premium Rent

8.

In 1981, the Board, in addition to requiring rental payments, invented the concept of "premium rent." Premium rent is not rent at all; rather, it refers to the requirement that lessees pay 10% of the leasehold value upon assignment or transfer of the lease to someone outside the

[1] Transcript, Agenda Item 8, Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (March 16, 2010)

lessee's immediate family. Exh. 1.[2] Leasehold value is determined by subtracting the value of the improvements and the personal property from the total sale price. IDAPA 20.03.13.25. Premium rent was imposed as a compromise to avoid the "very large increases" in annual rent that would have been necessary to reflect fair market values. Exh. 1. Premium rent was adopted so that when lessees assigned leaseholds for value, "the State could share in the profit." Exh. 2.[3] In essence, upon assignment of a cottage site lease, premium rent offsets a portion of the rent the State would have collected during the remaining term of the original lease, if the contract rental rate had been set at the market rate.

In 1987 the Board adopted a rule extending premium rents "through December 31, 1992 or until contract rents have been increased to full market rents, whichever comes first." IDAPA 20.03.13.27. Although the premium rent rule expired in 1992, the Board, in recognition of the fact that annual rents remained well below fair market value, has continued to impose the premium rent requirement as a matter of policy and contract. Exh. 18.[4]

The continued imposition of premium rent has proven problematic. Board members, IDL staff, and outside consultants all agree that its continued existence is an admission that contract rents are below market rents.

Board members initially conceived premium rent as a temporary measure that would have utility only as long as rents remained below market values. In 1998 Board member J.D. Williams stated that "when market value is reached the Land Board should look at removing it." Exh. 16 at 8.[5] Appraisers John McFadden and Bradford Knipe, hired by the Board in 1998 to examine rental rates both agreed that the large amounts of money being paid to acquire

---

[2] Land Bd. Meeting Minutes (Aug. 4, 1981)

[3] Land Bd. Meeting Minutes (Oct. 13, 1981)

[4] Land Bd. Agenda Memorandum, Cottage Site Rental Policy Recommendations, (June 11, 1991).

[5] Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).

leaseholds confirmed that contract rents were well below market rents. Exh. 26 at 22; ex 27 at 151.[6]

In 2008, Board member Ysursa informed the lessees that "if we really are at market rent, we shouldn't be seeing that leasehold value," and stated premium rent "was put in . . . to justify 2.5, which was low from every other study that was done. And that's why it was put in." Exh. 33 at 61-62.[7] A 2008 analysis by the Policy Analysis Group of the University of Idaho College of Natural Resources affirmed that leasehold value accrues "where contract rent is lower than market rent." Exh. 25, Attachment 1 at 11.[8]

In 2010, Board member Ysursa reiterated that premium rent is a "kind of the stop gap measure because over the years [we had a] lease rate that . . . was lower than any of these studies, be it Duffield, be it Knipe, be it McFadden, be it others." Exh. 36 at 57.[9] Board member Ysursa stated: "If we were at market rent, we wouldn't need premium rent." Exh. 41at 56.[10]

V. The History of Lessees Benefitting at the Expense of the Beneficiaries: an Overview of the Cottage Sites' Leasing Program

9.

The Board leases 355 recreational home sites on Priest Lake and 167 recreational home sites on Payette Lake. Exh. 25, Attachment 1 at 1.[11] The recreational home sites have traditionally been referred to as "cottage sites." The 355 cottage sites at Priest Lake are located

---

[6] John T. McFadden, Appraisal Report, Bradford T. Knipe, Complete Appraisal,

[7] Transcript, Land Bd. Cottage Site Subcommittee Meeting (April 22, 2008).

[8] Cook and O'Laughlin.

[9] Transcript, Land Bd. Meeting (Feb. 16, 2010).

[10] Transcript, Land Bd. Cottage Site Subcommittee Meeting (March 1, 2010).

[11] Philip S. Cook and Jay O'Laughlin, Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands at 1 (October 2008), attached to Idaho State Bd. of Land Comm'rs, Agenda Memorandum, Recommendation of the Cottage Site Subcommittee (Feb. 16, 2010).

on public school lands. Of the 167 cottage sites at Payette Lake, two are located on public school lands, 56 on normal school lands and 109 on state hospital lands.

The majority of the cottage sites were first leased in the mid 1940s and early 1950s, though some date back to as early as 1924. Exh. 20 at 1.[12] Each cottage site lot is owned in fee simple by the State of Idaho as trustee for public schools, normal schools (Idaho State University, Department of Education, and Lewis-Clark State College), and the state hospital. The improvements on the cottage site lots are owned by the lessees.

10.

Rents for Priest Lake lots in 1945 were as low as $10 per year. Exh. 25, Attachment 1 at 4.[13] From 1945 through 1988, rents remained relatively flat, with only sporadic increases. Id.

11.

In 1986, IDL estimated that the state was receiving a return on assets value of 0.67% for all cottage site leases. Exh. 3.[14] In response, the Board adopted a rental rate based on a percentage of the value of the cottage site after subtracting the value of all lessee-owned improvements. The initial rental rate was 2.5%, to be implemented in 1989 using a two-year rolling average of fair market value. Id. The rental schedule was modified in 1988 by adopting a phase-in schedule that limited annual rent increases to no more than 25%. Exh. 4.[15]

12.

Until 1990, expiring cottage site leases were "subject to disposal at public auction" pursuant to the provisions of Idaho Constitution Article IX, § 8 and the provisions of Idaho Code § 58-310, providing procedures for conflict auctions. The Board, however, discouraged public

---

[12] Land Bd. Agenda Memorandum, Cottage Site Rental at Priest and Payette Lakes (April 8, 1997).
[13] Cook and O'Laughlin.
[14] Land Bd. Meeting Minutes (June 25, 1986).
[15] Land Bd. Meeting Minutes (May 17, 1988).

auctions by posting notices of availability only on the local court house bulletin board, instead of advertising them as they did on other expiring leases. Exh. 28b.[16] As a result, prior to 1990, few applications for conflict auctions were received and none had proceeded to auction. Exh. 28a at 2.[17]

By 1990, demand for cottage site leases had increased significantly, so that people were willing to pay "substantial amounts of money to buy their leasehold" from existing lessees. Exh. 28b.[18] The large increases in leasehold values accrued because contract rent was below market rent. Two pending applications for conflict auction prompted the Board to delay the applications and seek legislative action to protect the lessees.

13.

In written testimony submitted to the Legislature in 1990, cottage site lessees complained that conflict auctions were unfair because "[o]ne hundred percent of the money from a conflict bid goes to the State," Exh. 28b.[19] Lessees argued that they would lose the "substantial amounts of money" they had paid to predecessor lessees for the right to assume the lease. Id.

Legislators questioned whether eliminating the public auction requirements conflicted with the duty to obtain maximum long-term returns. Exh. 28c at 5. Senator Vance stated: "the constitution requires that the State manage the land to experience maximum gain [but] it is hereby declared that we aren't going to do it anymore. That's what they're saying. It's the craziest thing I've ever witnessed. I can't believe it." Id. at 7.

---

[16] Senate Resources and Environment Committee Minutes of February 16, 1990.

[17] Senate Resources and Environment Committee Minutes of February 9, 1990.

[18] Senate Resources and Environment Committee Minutes of February 16, 1990. The quoted material is from the attached written statement of Payette Lakes Cabin and Pilgrims Cove Association titled "Questions and Answers Concerning Lease Lot Issues".

[19] Senate Resources and Environment Committee Minutes of February 16, 1990. The quoted material is from the attached written statement of Payette Lakes Cabin and Pilgrims Cove Association titled "Legislative Fact Sheet in Support of SB 1516."

Ultimately, the Idaho Legislature, concerned that "the conflict application and auction procedure have caused considerable consternation and dismay to the existing lessees at the prospect of losing a long-time lease," Idaho Code § 58-310A(1)(e), abolished the use of public auctions as a means of establishing market rents and established a general requirement that the Board "ensure that each lot generates market rent throughout the duration of the lease." Idaho Code § 58-310A(3).

Nonetheless, during the legislative debates, Legislators expressed dismay over the large leasehold values being retained by lessees upon assignment or sale of the leases. For example, Senator Reed stated: "I do have a problem in thinking if any profits are going to accrue from the exchange of those leases that profits should perhaps go to the state. Now how do you respond to that sort of glitch where it is possible for the lessees to make some money off of their leases." Id. at 11.[20]

Senator Donesley stated: "you've described the benefit of enjoying the property and then selling it for a profit after the enjoyment of the property. Somewhere in there is a slice of the state given that it is state property being enjoyed, it's appreciating and the profit from the sale which is going into private pocket and now we're having a bill to protect that kind of a situation." Id. at 22.

Senator Calabretta asked: "[s]o, roughly, a million dollars are transacted on state properties by the assignment of the lease and we get out of that ninety thousand, or a hundred thousand dollars in any given year?" Id. at 23.

---

[20] Transcript of Senate Resources and Environment Committee Meeting February 16, 1990.

Senator Reed concluded by stating: "I think an awful lot of the questions that have come up today really relate to another policy which deals with the whole aspect of transfer. So I think we don't just need to deal with hot potatoes, perhaps, although there's nothing cool about the issue of transfer, but I think we really should put this on the legislative agenda and address that in the future . . . should they be able to have assignments, and big money and all this kind of stuff without passing along to the state their fair rate?" Id. at 25-26.

The legislative history suggests that in passing Idaho Code § 58-310A, the expectation was that the issue of large leasehold values being pocketed by lessees upon transfer of leaseholds would be resolved by requiring market rent throughout the duration of the lease. IDL Director Stan Hamilton testified "As rents go up, the leasehold values do come down. And there is a relationship there than can be determined." Ex. 28c at 24. He further testified that if the legislation passed the Board might consider increasing the premium rent up to 50 or 60 percent. Id. at 23.

15.

The passage of Idaho Code § 58-310A prompted the Board to take action in 1991 to reexamine its rental policies to comply with the new statutory requirement to obtain market rent. To determine market rent, the Board had the Real Estate Consulting Group perform an initial appraisal on 13 lots at Payette Lake and 16 lots at Priest Lake. Exh. 18.[22] The Real Estate Consulting Group recommended a variable rate of return tied to lot values, with rates of 4.5% to 5.5%; however, a subcommittee of Board members rejected that recommendation and proposed continuing the then-present Board policy of phasing in a 2.5% rental rate. Id.

---

[22] Land Bd. Cottage Site Subcommittee Memorandum (June 11, 1991).

Board member Jerry Evans observed that the professionals hired by the Board had concluded that "a more reasonable rate of return would be between 4-1/2% and 5-1/2%," and he expressed concern that the "subcommittee recommendation chooses to ignore this professional advice." Exh. 6. at 2.[23] He cautioned that "the phase-in schedule must be abandoned because the law is in effect now and it says market rent throughout the duration of the lease." Exh. 5 at 4.[24]

Instead of abolishing the phase-in schedule, however, which at that time limited annual increases to no more than 25%, the Board modified it to further restrict annual rent increases to 5.3%. Exh. 7 at 4.[25] The Board's action ignored information presented by IDL staff demonstrating that a phase-in rate of 5.3% annually would not achieve the target of 2.5% of land value "because land values—and target rentals—are rising faster than 5.3% annually." Exh. 19 at 3.[26]

16.

In 1997, the Board again reviewed the cottage site lease rates. Following adoption of the phase-in schedule with a 5.3% annual rent increase cap, leasehold values escalated. Exh. 8 at 4.[27] In "some cases local property taxes actually exceed[ed] the rent the Department receive[d] for the property." Id. Because of the disparity between the rapid rise in market value and the cap on rent increases, the actual rate of return was 1%. Exh. 20. at 13.[28] IDL staff recommended

---

23 Land Bd. Meeting Minutes (June 11, 1991).
24 Land Bd. Meeting Minutes (July 10, 1990).
25 Land Bd. Meeting Minutes (June 9, 1992).
26 Land Bd. Agenda Memorandum, Cottage Site Rental Rates (June 9, 1992).
27 Land Bd. Meeting Minutes (June 4, 1997).
28 Land Bd. Agenda Memorandum, Cottage Site Rental at Priest and Payette Lakes (April 8, 1997).

that rents be raised over a five year period to achieve a return of 5% of property value. Id. at 18-19.

In 1997, the Board, after hearing from a number of lessees, once again rejected staff recommendations to raise the rent and instead affirmed the 2.5% rental rate "with the understanding that it can be reopened based on incoming information." Exh. 8 at 12.[29] The Board then commissioned two appraisal reports, one for Priest Lake, and one for Payette Lake, and asked the appraisers to determine market rents. John McFadden, in his report for Priest Lake, recommended a rental rate of 3.5% of fee simple value, but also noted that there was a "relatively wide range of indications for the rate of return." Exh. 26 at 24-25.[30] McFadden derived the 3.5% rate of return by analyzing leasehold sales. Exh. 16.[31] McFadden recommended close monitoring of leasehold values as an indicator of market rent, with the notation that once "the market level is reached for rents, true leasehold values should be zero and that market for cabins should remain active." Exh. 26 at 25[32].

The appraisal report for the Payette Lake cottage sites, prepared by Bradford T. Knipe, concluded that under then-existing Board policies, a 4% rate of return was justified, though he believed a 6% rate of return would be fair if accompanied by certain conditions to provide certainty to lessees. Exh. 27 at 156, 163.[33] Knipe also emphasized the role of leasehold values in assessing market rent, stating that when "lessees are paying anything more than the

---

[29] Land Bd. Meeting Minutes (June 4, 1997).

[30] John T. McFadden, Appraisal Report: Project Report with Comparable Sales for Priest Lake Cottage Site Appraisals 24-25 (1998).

[31] Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).

[32] John T. McFadden, Appraisal Report: Project Report with Comparable Sales for Priest Lake Cottage Site Appraisals (1998).

[33] Bradford T. Knipe, Complete Appraisal, Self Contained Report and Market Analysis of 14 Payette Lake Cabin Sites, (1998).

depreciated/contributory value of the former tenant's building and site improvements, the market is acknowledging rents are below market rental return levels." Id. at 151.

17.

In 1998, a subcommittee of Board members, appointed to make a recommendation on the cottage site leases, met to consider the recommendations of the Knipe and McFadden reports. McFadden reiterated his conclusion that the persistent sale of leasehold interests, which were then routinely selling for $100,000, was clear evidence that contract rents were below market rents. Exh. 16 at 6.[34] IDL director Stanley Hamilton pointed out that the presence of "substantial leasehold values . . . indicates a very clear issue that we are not at market rent." Id. at 8.

The cottage site subcommittee report acknowledged that the recommended rental rate of 3.5% for Priest Lake cottage sites "with an annual escalator of eight percent" was "strongly supported by the past 21 year trend study." Exh. 21.[35] Likewise, they acknowledged that the appraisal of the Payette Lake cottage sites indicated a market rent of 4 percent. Id. They concluded that such rates were equitable "if the only aspect of the current rental policy subject to change is the rate of return." Id. But, they nonetheless adopted a rental rate of 2.5% because such a rate "recognizes and takes into consideration the lessees sweat equity and site improvements." Id. The lessees argued that the Board needed to "give credit for improvements—not to the house, but to the lot." Exh. 16 at 5.[36]

---

[34] Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).
[35] Land Bd. Cottage Site Subcommittee Report (Dec. 15, 1998).
[36] Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).

18.

The annual rental rate has remained ostensibly at 2.5% since 1998, but real returns have at times fallen below 2.5% due to freezes on valuation of cottage sites in the face of rapidly rising land values.

19.

In the last several years, leasehold values and premium rents have escalated to the point where in many cases the value of leaseholds far outweighs the value of improvements. For example, in 2008, a Payette Lake cottage site leasehold sold for $863,280, while the lessee's improvements sold for $36,720. Exh. 22 at Attachment 4.[37] Ninety percent of the proceeds from sales of leaseholds go to the lessees. Since 2003, "cottage site owners have realized in excess of $25 million for the use of State endowment land," while the endowments have received only $2.7 million in premium rent from leasehold assignments. Exh. 25 at 3.[38] As one lessee who paid $750,000 for a leasehold wrote to Board members, "the past policies of the Land Board allowed the previous leaseholder to make very substantial profits at the expense of the State and to myself." Exh. 39.[39]

20.

In four of the last seven years, the amount of money received by lessees for the conveyance of leaseholds exceeded the total rent received by the Board on behalf of endowment beneficiaries. Exh. 38.[40] For example, in 2006, nine lessees received $6,482,709 for the

---

[37] Land Bd. Agenda Memorandum, 2009 Rent Changes for the Payette Lake and Priest Lake Cottage Sites (June 19, 2008).

[38] Land Bd. Agenda Memorandum, Recommendation of the Cottage Site Subcommittee (Feb. 16, 2010).

[39] Letter, Karl Klokke to Land Board members (Feb. 24, 2010).

[40] Spreadsheet Comparing Annual Rents to Leasehold Sales, 2001-2009, provided by Idaho Department of Lands in response to request from Attorney General Lawrence Wasden (March 1, 2010).

conveyance of leaseholds. That same year, the total amount of annual and premium rent received by the Board for all 522 cottage sites was $4,022,676. Id.

21.

In 2007 land values in Valley County increased dramatically. The assessed value of waterfront lots increased an average of 47%, while the assessed value of second tier lots increased 88%. Exh. 21.[41] In response, the Board initially entertained a motion to limit the 2008 rent increase at Payette Lake to 25%. Exh. 12[42] Ultimately, the Board approved a substitute motion to freeze the 2008 rent for the Payette Lake cottage sites at the 2007 rate. Id. The rents collected at Priest Lake, however, increased 15% for 2008, based on an evaluation of market data from the prior five years. Exh. 23 at 1.[43]

VI. The 2007 Appointment of a Two-Person Subcommittee Did Not Resolve the Issues Surrounding the Cottage Site Leases

22.

In 2007, the Board appointed two Board members – Secretary of State Ben Ysursa and Superindentent of Public Instruction Tom Luna - to form a subcommittee to recommend a rental formula to be applied to the cottage sites during the lease term that starts January 1, 2011. Exh. 11. at 6.[44] Over the next several years, the subcommittee held a series of meetings with lessees to hear their concerns and to evaluate alternative methods of calculating rents.

The members of the subcommittee expressed the desire to work on a "collaborative basis" with the lessees to establish a mutually-agreeable rent. Exh. 33 at 46.[45] Board member

---

41 Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Report (Dec. 15, 1998).

42 Land Bd. Meeting Minutes (Dec. 4, 2007).

43 Land Bd. Agenda Memorandum, 2009 Cottage Site Rental Rates at 1 (Dec. 16, 2008).

44 Land Bd. Meeting Minutes (June 12, 2007).

45 Transcript, Land Bd. Cottage Site Subcommittee Meeting (April 22, 2008).

Luna described the subcommittee's mission as an opportunity "to meet our obligation on the Land Board to bring some stability . . . to these cottage site leases, and, you know, for those who own the leases." Id. at 5. Board member Ysursa stated he was "very sympathetic to the plight of the cottage site owners as far as predictability and stability as far as these rapid escalation of rents." Exh. 34 at 28.[46]

23.

On June 19, 2008, the Board met to determine 2009 rents. IDL staff recommended that rents at Payette Lake be increased to reflect current assessed value, which, due to the 2007 rental freeze, would have resulted in a 47% rent increase for waterfront lots and an 88% rent increase for second tier lots. Exh. 22.[47] IDL staff recommended a 23% increase for Priest Lake cottage sites, as recommended by a consultant after reviewing the past five years of market data. Id. The Board rejected the recommendations and voted to limit the rent increases at Payette Lake and Priest Lake to 15%, effective January 1, 2009. Exh. 13.[48] On December 16, 2008, however, the Board rescinded all rent increases for 2009, and froze rents at 2008 levels for both Payette Lake and Priest Lake. Exh. 14.[49] IDL staff calculated that the rent freezes would result in a 2009 revenue loss of $1,776,560 for the Payette Lake cottage sites and $583,691 for the Priest Lake cottage sites. Exh. 23 at 2.[50]

---

46 Transcript, Land Bd. Cottage Site Subcommittee Meeting (May 18, 2009).

47 Land Bd. Agenda Memorandum, 2009 Rent Increases for the Payette Lake and Priest Lake Cottage Sites (June 19, 2008).

48 Land Bd. Meeting Minutes (June 19, 2008).

49 Land Bd. Meeting Minutes (Dec. 16, 2008).

50 Land Bd. Agenda Memorandum, 2009 Cottage Site Rental Rates (Dec. 16, 2008).

24.

On June 16, 2009, the Board met to determine rents for 2010. Market data indicated that assessed values for Payette Lake cottage sites decreased by 5% in 2009. Exh. 24 at 1.[51] IDL staff noted, however, that without the rent freezes in 2008 and 2009, rents would be 39% higher for waterfront lots and 78% higher for second tier lots. Id. At Priest Lake, the market data for the previous five years indicated that rents should be increased by 26%. Id. at 2.

IDL staff, however, recommended that rents not be increased for 2010. Id. The Board agreed and again froze rents. Id. at 3. As a result, the effective rent rates for 2010 were 2.03% for Priest Lake, 1.7% for Payette Lake waterfront lots, and 1.33% for Payette Lake second tier lots. Id. at Attachment 1. Total revenue was $2,027,222 less than would have been received at the contract rate of 2.5% of current assessed value. Id.

25.

On February 16, 2010, the Board met to determine rents for 2011. The subcommittee's report to the Board recommended "a target annual lease rent ("target rent") will be calculated at 4.0% of the average appraised value of each lot over the most recent 10 years (the sum of the 10 prior years appraised or indexed values for each lot divided by 10). Actual rent will increase or decrease annually from the prior year's rent at a constant percentage rate to reach the target rent in year five. Every five years from the effective date of the lease, the actual rent will be recalculated using this same methodology and appraised values of the lot for the most recent 10 years. Lot values shall be appraised by the applicable county assessor or determined by an Idaho Certified Appraiser, at the discretion of the Department. At the end of the (sic) each five year

[51] Land Bd. Agenda Memorandum, 2010 Rent Changes for Payette Lake and Priest Lake Cottage Sites (June 16, 2009).

period under the lease, the target rent will be calculated at 4.0% of the average value for the duration of the lease." Exh. 25 at 3.

The subcommittee's rationale for its recommendations was that "severely impairing or eroding longstanding business relationships with our lessees is not in the best interest of our trust beneficiaries" and the fact that fluctuations in rent "cause[] concern for cabin site lessees." Id. at 3. The subcommittee report expressed the concern that "raising rents too high would result in these lands going unleased, to the detriment of beneficiaries." Id. In presenting the subcommittee report to the Board, however, subcommittee member Ysursa described the process as "balancing our constitutional mandate in article 9, section 8, prudent investor standards, whatever you want to say, with the long-term relationship we have with the lessees." Exh. 36 at 3.[52]

26.

An analysis of the subcommittee's recommendation prepared by IDL Director George Bacon concluded that while the target rate would be 4%, the effective rental rate (actual rent returns compared to current land value) would vary between 2.37% and 2.43% if land appreciated at 4.8% annually. Exh. 29 at Appendix 3.[53] If land were to appreciate at an annual rate of 10.30%, the effective rental rate would stabilize at around 1.54%. Id. at Appendix 3. Director Bacon concluded: "I do not believe the Subcommittee's recommendation insures that each leased lot generates market rent throughout the duration of the lease, but neither does the current system." Id. at 2. 36.

Director Bacon also examined recent leasehold sales, which indicated that the contract rate of 2.5% of current assessed or appraised value that was in effect in recent years was below

---

52 Transcript, Land Bd. Meeting (Feb. 16, 2010).

53 Letter, IDL Director George Bacon to Lawrence Wasden, Feb. 12, 2010.

market value. In 2008 and 2009, two "down" years in the real estate market, 21 leaseholds sold for $6,392,039, an average of over $300,000 per leasehold. Id. at Attachment 1.[54] Director Bacon stated: "[b]ased on the numerous studies previously commissioned and conducted by real estate experts, it appears as long as there is leasehold value, the rent charged is not at market." Id. at 2.

27.

In 2010, Board member Lawrence Wasden commissioned economists Terry L. Anderson and Reed Watson to independently examine the issue of market rent generally and to determine whether the subcommittee recommendation would achieve market rent and fulfill the Board's duty to maximize the long term financial return for endowment beneficiaries. Idaho Const., art. IX, § 8. The economists concluded that the subcommittee recommendation would not fulfill the Board's duty to maximize the long term financial return for the endowment beneficiaries.

Economists Anderson and Watson found particularly troubling the subcommittee's proposal to "smooth" rent increases by using both a ten year rolling average to establish lot values and a five year phase-in to reach the rent based on such ten-year average value, since it "guarantees that the state is not securing market rent for the five year adjustment period." Exh. 31 at 4. In response to questioning from Board member Ysursa, Mr. Anderson emphasized that the combination of rolling average and phased-in target rent would "hamstring the Board in meeting its fiduciary responsibility" to obtain market rent. Exh. 36 at 88.[55]

During the February 16, 2010 meeting, Board member Ysursa asked Mr. Anderson his opinion regarding the subcommittee's rationale for combining rent smoothing with a phase in:

---

[54] An additional 27 leaseholds were transferred to family members or family trusts. Such "love and affection" transfers are not subject to the leasehold reporting requirement and do not pay premium rent for the assignment of the lease.

[55] Transcript, Land Bd. Meeting (Feb. 16, 2010).

> If we, as the current Board members voted for freezes along the way, were we complicit in these current scenarios . . . the State helped create the imbroglio that we're in, and what I'm suggesting, and the Subcommittee is suggesting, we didn't. We need to get out of it and have some measure of fundamental fairness involved when we do come out of this. To immediately put a four hundred percent increase on the lessees is in my opinion unconscionable . . . .

Id. at 84. Mr. Anderson responded that trying to phase in a new rental structure "with this rolling appraised value, and phasing it in with some target rent, not target rate, target rent, is not a good way to appease your conscience." Id. at 85.

Lessees had much the same view of the proposed "smoothing" methodology. Attorney Terry Copple, representing the Payette Lakes Cabin Owners Association, later wrote that "averaging that total with the value of the Leased Premises for the previous ten years does not give one current market rent; it simply produces an arbitrary number and does so under the assumption that current market rent is somehow achieved by deferring to the economic conditions of the previous decade." Exh. 40 at 2.

Economists Anderson and Watson also concluded that the proposal to gradually increase premium rent until it reaches 50% of leasehold value "validates that the board has not been charging market rents, that below market rents have contributed to leasehold values, and that the state has been missing out on revenues that a prudent investor would have captured." Exh. 31 at 4.

28.

In examining the history of Board actions regarding cottage sites, economists Anderson and Watson concluded that a phenomena known as "rent seeking" had thwarted past proposals to obtain market rent. Id. at 12-13. They explained that "rent seeking" occurs when a small, politically influential group uses political pressure to receive the benefits of a public lands rental

policy while the costs are diffused over a larger group. With the benefits "concentrated, the small group can afford to exert political pressure for a policy which benefits it; with the costs diffused, however, it is not worth it for anyone in the large group to organize political opposition." Id. at 13.

29.

At the February 16, 2010 Board meeting subcommittee member Ysursa moved to adopt the recommendation of the subcommittee. Board member Wasden, mindful of his two prior votes to freeze rents, reminded the other Board members that the question before them was "how to fulfill the Board's fiduciary duty to the trust beneficiaries to achieve the maximum long-term financial return from the cottage site lessees." Id. at 116. While Board member Wasden recognized the lessees' desire to preserve their family ties to the state cottage sites, he maintained that "nothing in the Idaho Constitution provides that the Board should seek, in the administration of this trust, to preserve family traditions." Id. at 117. Board member Wasden asserted that "the Constitution expressly requires the Land Board to exercise a duty of undivided loyalty to the endowment beneficiaries," so that "the Board in its trust capacity cannot take into account matters other than the maximum long-term financial return to the trust beneficiaries." Id. Board member Wasden indicated he would "vote in opposition to the Subcommittee's proposal" because it fell "short of meeting this Board's constitutional duty to achieve the maximum long term financial return to the endowment beneficiaries." Id. at 118.

Board member Ysursa challenged Wasden to propose his own lease terms and conditions: "What are you in favor of what we ought to do?..." Id. at 120. In response, Board member Wasden pointed to the expert report he had commissioned from economists Terry Anderson and Reed Watson. Id. at 121. Economists Anderson and Watson had examined all previous work commissioned by the Board to determine market rent, including comparables showing market

rates of 3.5% to 6%, and had concluded that "the more economically sound approach" was to use a method developed by John Duffield to estimate market rents using leasehold values. Exh. 30 at 5-6.[56] The Duffield model can be used to "calculate an implicit market rental rate of return" because "positive leasehold values reflect the buyer's valuation of below market rental rates." Id. When applied to the cottage site sales the Duffield model suggested an implicit rate of return of 6% of appraised market value.

Board member Wasden concurred with Anderson and Watson's analysis and stated his belief that a market rent "would require six percent tied to T-bills, assessed value, ten-year leases." Exh. 36 at 121.[57]

30.

At the February 16, 2010 meeting, Board member Ysursa withdrew his motion to approve the subcommittee's recommendation, and without apparent consensus on the issues of market rent and premium rent, the Board voted to defer decision on those issues and have the cottage site subcommittee report back in one month with a recommendation for final action. Id. at 131-32. The Board did vote unanimously to limit the lease term to ten years, and to order IDL staff to report back to the Board by January 2011, with a plan for unifying ownership of cottage sites. Id. at 127-29.

31.

At the March 9, 2010 Board staff briefing, IDL staff made a final review of the issue of market rent and circulated draft recommendations to the Board staff members. IDL staff recommended that the Board "establish a rental structure that achieves market rates between four

---

[56] Terry L. Anderson and Reed Watson, Report to Idaho Attorney General Regarding Cottage Site Leases (2010).
[57] Transcript, Agenda Item 7. Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (Feb. 16, 2010).

and six percent of land value, with the ability for the Board to change the rate from year to year." Exh. 43.[58] Annual recommendations to amend rental rates would be made by IDL staff based on monitoring of leasehold values during lease assignments. Id. IDL staff recommended eliminating premium rent once rental rates reflected market rates. Id.

32.

The subcommittee's final recommendation was presented to the Board on March 16, 2010. Exh. 37.[59] Despite an earlier concession from subcommittee member Ysursa that the 4% rental rate, when combined with the subcommittee's recommended "smoothing effect" resulted in rents "quite a ways away from market rent," Exh. 36, at 111-112, the subcommittee did not alter its previous recommendation for annual rent. Indeed, the only change made by the subcommittee was to succumb to pressure from lessees to reduce the premium rent. The subcommittee agreed to discard its recommendation that the Land Board phase in a requirement for lessees to pay 50% of gross leasehold value upon transfer of the leasehold interest. Id. Instead, the subcommittee recommended that lessees be required to pay either 10% of gross leasehold value or 50% of net leasehold value,[60] whichever was greater for each individual sale. Id.

33.

At the March 16, 2010 Board meeting, four of the five Board members acknowledged that the subcommittee's recommendation would not achieve a market rental rate. Subcommittee chairman Ysursa explained:

---

[58] Idaho Department of Lands Cottage Site Considerations & Recommendation (draft circulated to Land Board staff on March 9, 2010).

[59] Addendum to Cottage Site Subcommittee Report (March 16, 2010).

[60] Net leasehold value is calculated by determining gross leasehold value then deducting the amount the lessee originally paid (if any) to acquire the leasehold.

> And I use the term four, and I've been – and I've stated this many a time, at the end of a five-year period, this, frankly, gets them to a little bit over what they agreed to ten years ago on two point five of current. I find it incredulous at times that the lessees are outraged that I would suggest this type of rate when it, in fact, is very close to the two point five percent of current that they agreed to ten years ago. Why aren't we at current? We, as a Board, all – everyone on this Board has voted for a freeze at least two times; some of us three times. We are complicit in the problem that we're at – that we're not even at the two point five. And we need to be reasonable and fair in the way we extricate ourselves, and I believe that immediately going to a huge increase goes against all sense of fairness to both sides.
>
> . . . .
>
> Do we acknowledge that we're not at market rent by using the term premium rent? Yes. We've done that since 1981.

Exh. 42 at 28.[61] Board member Donna Jones stated:

> I do disagree with your rental rate recommendation. Just – I don't think that will bring us to a true market rent, as you said. And by continuing to collect the premium rent, we're openly acknowledging that our rental rate is too low. That was – that would be my comments.

Id. at 31. Board member Lawrence Wasden stated:

> Governor, I think my – my voice has been heard on this. About a month ago at our previous Land Board meeting I reiterated my concerns. We have an obligation to obtain the maximum long-term return. Those are words that mean a lot to all of us. I – I cast no aspersions regarding that. We have an obligation to act as a prudent investor. We have an obligation to have undivided loyalty to the beneficiaries, and we are statutorily required to get market rent for the duration of the lease. I do not believe we will be fulfilling that responsibility with regard to this motion. I will be voting no.

Id. at 31-32. Board member Thomas Luna stated:

> We're never going to see true market rent, or true market value, as long as there's this comingling of government and private sector. . . . The other point, Governor, is we're never going to maximize earnings for these properties, or this asset, until

[61] Transcript, Agenda Item 8, Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (March 16, 2010).

we sell them. . . . [W]e've never realized our full return to benefit the beneficiary . . . . Id. at 35.

34.

Despite the discussion on March 16, 2010, acknowledging that the subcommittee's recommendation would not achieve market rate, the Board voted 3-2 to implement the subcommittee's recommendation.

The new rents are scheduled to go into effect on January 1, 2011. The rental schedule adopted by the Board on March 16, 2010, will be included in new leases being finalized for the lease term starting January 1, 2011. Such leases are scheduled to go into effect on January 1, 2011. Under the terms of Idaho Code § 58-307, all cottage site lessees must reapply to renew their leases by April 30, 2010. New leases for the 2011-2020 lease term may be finalized and signed anytime thereafter.

35.

In the absence of writ of prohibition enjoining the signing and implementation of the cottage site leases, the endowment beneficiaries will be deprived of rental income that they are constitutionally and statutorily entitled to receive. In addition, if the cottage site leases are implemented the lessees will continue to pocket the lion's share of the leasehold value, value that should accrue to the endowment beneficiaries.

Wherefore, the Attorney General respectfully requests that this Court issue a writ of prohibition prohibiting the Board and the Director of the Department of Lands from signing and implementing the cottage site leases unless and until they are leased under terms meeting the requirements of Idaho Constitution Article IX, § 8.

DATED this 24th day of March 2010.

STATE OF IDAHO
OFFICE OF THE ATTORNEY GENERAL

By _____
STEVEN L. OLSEN
Deputy Attorney General

By _____
MELISSA MOODY
Deputy Attorney General

EXHIBIT LIST

1. Land Bd. Meeting Minutes (August 4, 1981).
2. Land Bd. Meeting Minutes (Oct. 13, 1981).
3. Land Bd. Meeting Minutes (June 25, 1986).
4. Land Bd. Meeting Minutes (May 17, 1988).
5. Land Bd. Meeting Minutes (July 10, 1990).
6. Land Bd. Meeting Minutes (June 11, 1991).
7. Land Bd. Meeting Minutes (June 9, 1992).
8. Land Bd. Meeting Minutes (June 4, 1997).
9. Land Bd. Meeting Minutes (Oct. 21, 1997).
10. Land Bd. Meeting Minutes (Dec. 15, 1998).
11. Land Bd. Meeting Minutes (June 12, 2007).
12. Land Bd. Meeting Minutes (Dec. 4, 2007).
13. Land Bd. Meeting Minutes (June 19, 2008).
14. Land Bd. Meeting Minutes (Dec. 16, 2008).
15. Land Bd. Meeting Minutes (June 16, 2009).
16. Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).
17. Transcript, Land Bd. Cottage Site Subcommittee Meeting (June 3, 1991).
18. Land Bd. Agenda Memorandum, Cottage Site Rental Policy Recommendations (June 11, 1991).

19. Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Recommendation for Rental Rates (June 9, 1992).

20. Land Bd. Agenda Memorandum, Cottage Site Rental at Priest and Payette Lakes (April 8, 1997).

21. Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Report (Dec. 15, 1998).

22. Land Bd. Agenda Memorandum, 2009 Rent Changes for the Payette Lake and Priest Lake Cottage Sites (June 19, 2008).

23. Land Bd. Agenda Memorandum, 2009 Cottage Site Rental Rates (Dec. 16, 2008).

24. Land Bd. Agenda Memorandum, 2010 Rent Changes for Payette Lake and Priest Lake Cottage Sites (June 16, 2009).

25. Land Bd. Agenda Memorandum, Recommendation of the Cottage Site Subcommittee (Feb. 16, 2010), with Attachment 1: Philip S. Cook and Jay O'Laughlin, Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands (October 2008).

26. John T. McFadden, Appraisal Report: Project Report with Comparable Sales for Priest Lake Cottage Site Appraisals (1998).

27. Bradford T. Knipe, Complete Appraisal, Self Contained Report and Market Analysis of 14 Payette Lake Cabin Sites (1998).

28a. Senate Resources and Environment Committee Minutes of February 9, 1990.

28b. Senate Resources and Environment Committee Minutes of February 16, 1990 (with attached written statement of Payette Lakes Cabin and Pilgrims Cove Association titled "Questions and Answers Concerning Lease Lot Issues").

28c. Transcript of Senate Resources and Environment Committee Meeting February 16, 1990 (prepared by Attorney General's Office from tape on file with Legislative Services Office).

29. Letter, IDL Director George Bacon to Lawrence Wasden, Feb. 12, 2010.

30. Terry L. Anderson and Reed Watson, Report to Idaho Attorney General Regarding Cottage Site Leases (2010).

31. Terry L. Anderson and Reed Watson, Analysis of Subcommittee Recommendation to the Idaho Board of Land Commissioners (2010).

32. Deliberately left blank.

33. Transcript, Land Bd. Cottage Site Subcommittee Meeting (April 22, 2008).

34. Transcript, Land Bd. Cottage Site Subcommittee Meeting (May 18, 2009).

35. Transcript, Agenda Item 10, Cottage Site 2010 Rent Changes and Update on Cottage Site Subcommittee, Land Bd. Meeting (June 16, 2009).

36. Transcript, Agenda Item 7. Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (Feb. 16, 2010).

37. Addendum to Cottage Site Subcommittee Report (March 16, 2010)

38. Spreadsheet Comparing Annual Rents to Leasehold Sales, 2001-2009, provided by Idaho Department of Lands in response to request from Attorney General Lawrence Wasden (March 11, 2010).

39. Letter, Karl Klokke to Land Board members (Feb. 24, 2010).

40. Letter, Terry Copple to Land Board members (March 12, 2010).

41. Transcript, Land Bd. Cottage Site Subcommittee Meeting (March 1, 2010).

42. Transcript, Agenda Item 8, Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (March 16, 2010).

43. Idaho Department of Lands Cottage Site Considerations & Recommendation (circulated to Land Board Staff on March 9, 2010)

44. Letter from Attorney General Lawrence Wasden to Governor C.L. "Butch" Otter (Feb. 12, 2010).

LAWRENCE G. WASDEN
ATTORNEY GENERAL

STEVEN L. OLSEN, ISB NO. 3586
CHIEF OF CIVIL LITIGATION DIVISION

MELISSA MOODY, ISB No. 6027
Deputy Attorneys General
954 W. Jefferson, 2nd Floor
P.O. Box 83720
Boise, ID 83720-0010
Telephone: (208) 334-2400
Fax: (208) 854-8073

Attorneys for State of Idaho

FILED - COPY
MAR 24 200
Supreme Court ____ Court of Appeals ____
Entered on ATS by ____

IN THE SUPREME COURT OF THE STATE OF IDAHO

HON. LAWRENCE G. WASDEN, the Attorney General of Idaho, *ex. rel.* the STATE OF IDAHO Petitioner, vs. IDAHO BOARD OF LAND COMMISSIONERS, and GEORGE BACON, in his official capacity as Director of the Idaho Department of Lands	**Supreme Court No.** 37528 **BRIEF IN SUPPORT OF PETITION FOR ISSUANCE OF A WRIT OF PROHIBITION**

I.

INTRODUCTION

The Idaho Board of Land Commissioners ("Board") ignored its constitutional and statutory duty to provide for Idaho's public schoolchildren, college students, and patients of the

state hospital when, on March 16, 2010, the Board, in a 3/2 vote, implemented cottage site lease-terms that were acknowledged by a majority of its members to be below market rent. *Petition*, Exh. 42, p. 27, Ls. 808-09 (remarks of Ben Ysursa); Exh. 42, p. 35, Ls. 992-95 (remarks of Thomas Luna); Exh. 42, pp. 31-32, Ls. 887-894 (remarks of Lawrence Wasden); Exh. 42, p. 31, Ls. 876-881 (remarks of Donna Jones).

The cottage sites at issue in this case are located at Priest and Payette Lakes. The 355 cottage sites at Priest Lake are located on Public School Endowment Lands. Of the 167 cottage sites at Payette Lake, two are located on Public School Endowment Lands, 56 on Normal School Endowment Lands and 109 on State Hospital Endowment Lands.

The lease terms approved by the Board – 4% annual rental rate, with a 5 year phase-in, use of a 10 year average lot value to calculate rent and a premium rent of the greater of 10% of the gross income or 50% of the net income received by lessees when conveying leaseholds to assignees – fail the constitutional imperative to "secure the maximum long term financial return to the trust beneficiary," as well as the Board's statutory duty to "insure that each leased lot generates market rent throughout the duration of the lease." Idaho Constitution, art. IX, § 8; Idaho Code § 58-310A(3).

Because the Board acted beyond the scope of its authority by adopting cottage site lease terms that are contrary to the requirements of Idaho's Constitution, and Idaho law, and to its duty of undivided loyalty to the trust's beneficiaries, the Attorney General[1] asks this Court to grant the

---

[1] The Attorney General brings this lawsuit not as a member of the Land Board, but as a representative of the sovereign, rooted in the common law power of *parens patriae*, and pursuant to his statutory duty to regulate charitable trusts under Idaho Code § 67-1401. *See also Dolan v. Johnson*, 95 Idaho 385, 509 P.2d 1306 (1973) (The Attorney General has supervisory power over charitable trusts to insure that such trusts are executed according to the settlor's intent.)

writ of prohibition and enjoin the Board and the director of the Idaho Department of Lands from executing cottage site leases until the Board adopts cottage site lease terms that fulfill its fiduciary duty under Article IX, § 8 of the Idaho Constitution.

II.

RELEVANT LAW

Idaho Code § 7-401 provides:

> The writ of prohibition is the counter part of the writ of mandate. It arrests the proceedings of any tribunal, corporation, board or person, when such proceedings are without or in excess of the jurisdiction of such tribunal, corporation, board or person.

Idaho Appellate Rule 13(g) provides that the Supreme Court:

> may also, in its discretion, enter an order staying a proposed act, a pending action or proceeding, or the enforcement of any judgment, order or decree, including but not limited to an injunction, writ of mandamus or prohibition, at any time during the pendency of an original application or petition for any extraordinary writ, or during the pendency of any appeal or a motion for certification of appeal. . .

Before this Court will issue a writ of prohibition, two contingencies must be shown: (1) the tribunal, corporation, board or person is proceeding without or in excess of the jurisdiction of such tribunal, corporation, board, or person, and (2) that there is not a plain, speedy, and adequate remedy in the ordinary course of law. *Henry v. Ysursa*, 2008 WL 4330547 (2008). As set forth below, both of these contingencies are present in this case.

III.

THE BOARD ACTED IN EXCESS OF ITS JURISDICTION IN FIXING UNCONSTITUTIONAL LEASE TERMS

The Board must comply with the Idaho Constitution, which requires the Board to act "in such manner as will secure the maximum long term financial return to the institution to which

granted..." Idaho Const. art. IX, § 8. In fixing lease terms that fail to secure the maximum long term financial return, the Board acted contrary to its constitutional mandate.

The Board must also comply with Idaho Code § 58-310A(3), which requires the Board to "insure that each leased lot generates market rent throughout the duration of the lease."[2] In fixing lease terms that include premium rent, the Board openly violated its statutory duty to obtain market rent throughout the duration of the lease.

A. The Board Knew that it Was Acting Contrary to the Constitution and Idaho Law and its Duty to the Trusts' Beneficiaries

The Board was warned that the lease terms it passed - 4% annual rental rate, based on average property values of the previous decade, phased in over 5 years, with a premium rent of the greater of 10% of the gross income or 50% of the net income received by lessees when conveying leaseholds to assignees - would fail to meet the Board's constitutional obligation to maximize long term returns and its statutory duty to secure market rent. The Board had reviewed the report of two independent economists, who questioned the Board's policies of phasing in rental rate increases over time, and imposing annual caps on rent increases. *Report to Idaho Attorney General Regarding Cottage Site Leases (2010), Petition*, Exh. 30, p. 4. Economist Terry Anderson told the Board at its February 16, 2010 meeting that:

---

[2] The Attorney General presumes the constitutionality of Idaho Code § 58-310A for the purpose of this Petition, notwithstanding Attorney General Opinion 09-01 (2009), which concludes that Idaho Code § 58-310A is an unconstitutional infringement on the Board's constitutional duty to employ public auctions for leases of endowment lands. If Idaho Code § 58-310A were to be declared unconstitutional, the arguments contained in this brief would not be substantially affected because as long as the cottage sites are being rented, the Board's independent constitutional duty to maximize long-term financial returns for endowment beneficiaries encompasses, at the very least, the duty to secure fair market value for the rentals of endowment lands.

> Unfortunately, the phase-in over ten years – using a ten-year average – fails to capture the current value of the asset and therefore is not prudent. Furthermore, to try and phase in a target rent over a five-year period means, again, you're missing a period of time when you're not capturing the rents.
>
> And to suggest that the Board should be charging a ten percent premium rent or a fifty percent premium rent is to say guilty of not being a prudent investor.

February 16, 2010 Board Meeting Transcript, *Petition*, Exh. 36, p. 80, Ls. 2296-2301.

George Bacon, the Director of the Idaho Department of Lands, also advised the Board that the cottage site subcommittee recommendation would not achieve market rent: "I do not believe the Subcommittee's recommendation insures that each leased lot generates market rent throughout the duration of the lease, but neither does the current system." *February 12, 2010 Letter to Attorney General Lawrence Wasden*, *Petition*, Exh. 29.

The Board was aware that, since premium rent arises only when substantial leasehold values accrue to the lessees, in setting any premium rent whatsoever, the Board was continuing a violation of its constitutional and statutory duty to secure rents at market rate. *Cf.* I.C. § 58-310A; IDAPA 20.03.13.10.06 (Leasehold value "accrues to a leasehold estate when the contract rent is below market rent.") Director Bacon advised the Board that "[b]ased on the numerous studies previously commissioned and conducted by the real estate experts, it appears as long as there is leasehold value, the rent charged is not at market. Even in today's 'down' market, transactions are occurring with leasehold value on some properties..." *February 12, 2010 Letter to Attorney General Wasden*, *Petition*, Exh. 29. At the March 16, 2010 meeting, before voting to approve a rental rate below market value, Board member Ysursa even admitted: "Do we acknowledge that we're not at market rent by using the term premium rent? Yes. We've done that since 1981." *March 16, 2010 Board Meeting Transcript*, *Petition*, Exh. 42, p. 29, Ls. 808-809.

The Board had information that detailed, in economic terms, why the cottage site owners have been historically successful in obtaining below market rents. The economists explained:

> Given that it is not easy to separate the contributions of the [land value and the improvements on the land] to the total value, opportunistic behavior is likely. The lessee may act opportunistically by putting political pressure on the Idaho Land Board to enact policies that favor lessees at the expense of the endowment beneficiaries. This is known as "rent seeking" because it uses politics to give the private owners a larger share of the land rents (Krueger 1974). Rent seeking is particularly prevalent when a small well organized group receives the benefit from a policy while the costs are diffused over a larger group. With the benefits concentrated, the small group can afford to exert political pressure for a policy which benefits it; with the costs diffused, however, it is not worth it for anyone in the large group to organize political opposition. In the case of cottage site leasing, the lessees are the former while the trust recipients are the latter.

Report to Idaho Attorney General Regarding Cottage Site Leases (2010), Petition, Exh. 30, at pp. 12-13. The report went on to explain that "[s]everal Land Board policies reflect this rent-seeking dynamic," including: (1) below market rents, (2) extended periods of flat or declining rents despite significant land appreciation, and (3) giving 90% premium rent upon transfer of the lease to the lessee, with only 10% going to the trust's beneficiaries. *Id.*, p. 13.

Because the Board was on notice that this type of "post-contractual opportunism" was taking place with respect to the cottage site leases, the Board should have redoubled its efforts to comply with its fiduciary duty as set forth in Idaho's Constitution. Indeed, economist Terry Anderson recommended that the Board not adopt the rolling average of appraised value, but that it establish a contract rental rate of 6% (with 4% being "at the very bottom end of anything that you should consider to be a prudent rate of return") and eliminate leasehold value entirely. *February 16, 2010 Board Meeting Transcript*, *Petition*, Exh. 36, p.91, Ls.2605-2604; p.92, L. 2635. Instead, the Board succumbed to the very political pressure it had been warned about – adopting lease terms that act as a windfall to cottage site lessees, to the detriment of Idaho's

public schoolchildren, college students and patients of the state hospital. The Board's actions on March 16, 2010 were consistent with its history of acting to benefit cottage site lessees, at the expense of those whom the Board is constitutionally obligated to protect.

The fact that the Board has accommodated the lessees' interests is apparent not only in the Board's actions, but it is also revealed in the way subcommittee member Secretary of State Ben Ysursa has characterized the relationship between the Board and the lessees: as a "partnership with the state and the lessees," with the Board as the senior partner (*April 22, 2008 Board Meeting Transcript*, *Petition*, Exh. 33, p. 46); and later, with the Board acting as a "gift horse" whom the lessees look in the proverbial mouth. *June 16, 2009 Board Meeting Transcript*, *Petition*, Exh. 35, p. 17. Secretary of State Ysursa summarized the relationship most succinctly as follows: "I think we have bent over pretty good for the lessees." *May 18, 2009 Board Meeting Transcript*, *Petition*, Exh. 34, p. 85.

Implicitly acknowledging the reality of post-contractual opportunism, and the effects of a Board that has been historically unwilling to stand up to the lessees' political pressure, subcommittee member Tom Luna expressed hopelessness at the situation ever improving. He stated: "... I don't think you're ever going to be able to create a situation where it's a truly market-driven system because you have this weird relationship between government and private." *May 18, 2009 Board Meeting Transcript*, *Petition*, Exh. 34, p. 40. The "weird relationship" between the government and the private is nothing more than post-contractual opportunism, and the Board has an obligation to the beneficiaries of the trusts to recognize and resist this political pressure. The Board's failure to do so is an abdication of its constitutional and statutory duties.

B. The Board's Actions Were Consistent with Its History of Benefiting the Cottage Site Lessees to the Detriment of Idaho's Public Schoolchildren, College Students and Patients of the State Hospital

In 1986, at a time when the state was receiving a rate of return on its cottage site leases of approximately 0.67%, the Board adopted a rent of 2.5% to be implemented in 1989. Even before this modest rental increase could be implemented, however, the Board further eroded the returns to the trust beneficiaries by adopting a phase-in schedule that limited annual rent increases to no more than 25%. *Petition, paragraph 11, Exhs. 3 and 4.*

In 1992, the Board again acted to reduce perceived impacts on lessees by further limiting annual rent increases to 5.3%, despite the fact that this phase in rate would not achieve the target of 2.5% of land value "because land values – and target rentals – [were] rising faster than 5.3% annually." *Petition, paragraph 15, Exh. 7.* To keep the cottage site rental rates down, and to assuage the cottage site lessees, the Board chose to ignore the data that showed its rental cap was a dereliction of its constitutional duty.

By 1997, as predicted, the capped annual rent increases were unable to keep up with increases in property value. Because of the disparity between the rapid rise in market value and the cap on rent increases (still at 5.3%), the actual rate of return was a mere 1%. *Petition, paragraph 16, Exh. 20.* Nevertheless, in 1997, the Board rejected Department of Land staff recommendations to raise the rent to 5% and affirmed the nominal rate of 2.5% with the understanding that it could be "reopened based on incoming information." *Id., Exh. 8 at 12.*

When the new information came in, however, in the form of two appraisal reports commissioned by the Board itself, this information was also disregarded in favor of the cottage site lessees' interests. The first report commissioned by the Board recommended a 3.5% rental rate with a close monitoring of leasehold values; the second report recommended a rate of return between 4%-6%, depending on various factors. *Id.* The Board's subcommittee report

acknowledged that the recommended rental rate of 3.5% for Priest Lake cottage sites with an annual escalator of eight percent was "strongly supported by the past 21 year trend study." *Petition, paragraph 17.* Still, the Board voted to maintain the rental rate of 2.5%. *Id.*

The 2.5% annual contract rental rate, set in place in 1986, remains in effect today despite overwhelming evidence that such a low rental rate violates the Board's obligation to its trust beneficiaries. *Petition, paragraph 18.* As low as this rental rate is, the actual rate of return has often been even lower, due to freezes on cottage site valuations in the face of rising land values. *Id.*

In 2008, with the assessed value of various lots increasing, the Board rescinded all rent increases for 2009 and froze rents at 2008 levels for both Payette Lake and Priest Lake. *Petition, paragraph 23.* As in the past, the Board succumbed to political pressure from the lessees and took action that benefited the cottage site lessees to the detriment of the trust beneficiaries. The Idaho Department of Lands' staff estimated that the rent freezes would result in a 2009 revenue loss of $1,776,560 for the Payette Lake cottage sites and $583,691 for the Priest Lake cottage sites. *Id.*

In 2009, the Board froze rents at the following effective rates: 2.03% for Priest Lake, 1.7% for Payette Lake waterfront lots, and 1.33% for Payette second tier lots. *Petition, paragraph 24.* The total revenue for the trusts' beneficiaries was $2,027,222 less than would have been received at the contract rate of 2.5% of the current assessed value. *Id.*

The Board has not only permitted the cottage site lessees to exploit effective rental rates far below market value, the Board has allowed the cottage site lessees to pocket the lion's share (90%) of the proceeds from leasehold sales – proceeds that should be benefitting Idaho's schoolchildren, college students, and patients of the state hospital. *Petition, paragraph 19.* In 2006, for example, the nine lessees who conveyed leaseholds received $6,448,709 after paying

premium rent. That same year, endowment beneficiaries received only $4,022,676 from annual and premium rents on all 522 cottage site leases combined. *Petition, paragraph 20.* Since 2003, cottage site lessees have realized in excess of $25 million from the assignment of their state endowment leases while the endowments have received only $2.7 million in premium rent from leasehold assignments. *Petition, paragraph 19.*

In sum, the Board's pattern of consistent deference to lessees has created a situation where rents are so far below market value that any effort to comply with the constitutional requirement to obtain the maximum long term financial return and the statutory mandate to obtain market value will require significant rental increases. The Board's fiduciary duties to the public school children, college students and patients of the state hospital demand nothing less. Yet the Board refuses to pay more than lip service to its fiduciary obligations to the designated beneficiaries, and in fact cites its past failure to obtain market rent as a justification for its present failure to comply with its constitutional and statutory duties.

Ben Ysursa, chairman of the cottage site subcommittee, assisted in preparing the most recent cottage site rental recommendation. He described past rent freezes that had resulted in rents far below market value and explained:

> If we were in a vacuum and didn't have the – another one of my great quotes I suppose, but the millstone of history around our neck that we helped create, we'd be saying go to market rent right now. I know there's – we agree to disagree on what market rent is obviously, but you know where we are. I agree. If we were at market rent, we wouldn't need premium rent.

Petition, Exh. 41, pp. 55-56, Ls. 1529-1533. The Board's complicity in allowing rents to remain far below market for so many years cannot justify the current dereliction of its constitutional and statutory duties, which set a minimum and inviolable floor of obtaining market rent for cottage site leases throughout the duration of the lease. Indeed, the record demonstrates that each time

market data was presented to the Board showing that the contract rate was significantly below the market rate, the Board justified its failure to implement a market rate of return by pointing out the increased cost to current lessees, a consideration outside the Board's jurisdictional authority and constitutional duty. Under the Board's rationale there will never be a time when it can implement a market rate of return because its continuing failure to meet its fiduciary duty necessarily means that the disparity between the contract rental rate and the market rental rate will continue to grow and will require the imposition of an even greater rental rate increase on the lessees.

Given the Board's support for legislatively removing recreational cottage sites from the statutory public auction requirement in exchange for the lessees' commitment to pay market rent, the Board's failure to achieve market rent is even more inexplicable. To date, the promise of Idaho Code § 58-310A remains unfulfilled.

C. A Writ of Prohibition Should Lie Where the Board Acted Beyond Its Constitutional Authority, in Violation of Its Constitutional Mandate, and Directly Contrary to Idaho Code § 58-310A

The Board has consistently refused to uphold its constitutional duty to the trusts' beneficiaries, as evidenced by the pattern of below-market rents, frozen rents, positive leasehold generation and willful disregard of information that runs contrary to the interests of the cottage site lessees. The Board's failure to address the cottage site lessees' post-contractual opportunism in any meaningful way, i.e. to do anything other than accommodate the cottage site lessees' demands, is an abdication of the Board's duty to maximize long term financial returns as required by Idaho's Constitution, as well as a violation of Idaho Code § 58-310A.

This Court has not hesitated to issue a writ of prohibition when it was clear that the targeted party was acting contrary to the law. As early as 1910, this Court issued a writ of

prohibition against the State Land Board when the Board was acting outside the law in attempting to "give away" school trust lands; this Court held that the "State Land Board has no power to relinquish or surrender the right or title of the state of Idaho to any of its school lands." *Balderston v. Brady*, 17 Idaho 567, 573, 107 P. 493, 499 (1910). In that same case, this Court also addressed the contention that a writ of prohibition will not lie against the Governor or against a board of which the Governor is a member. This Court squarely rejected that contention, writing:

> It is doubtful if any one would seriously contend that the process of the courts will not run against an individual or individuals, holding an executive office or offices, or comprising an executive board, simply because they occupied such official position and were assuming to act as officials, although their action was beyond the scope of their authority, and wholly unauthorized by law. We do not hold such a position tenable, and have never so held.

Id., at 569, 107 P. at 495. This Court distinguished the authorities that held that a writ of prohibition would not lie against the Governor to restrain him from performing an executive act, explaining:

> The State Board of Land Commissioners is a constitutional body. It is composed of four members, each of whom has a vote on all matters coming before the board. This board is as distinct and separate from all other offices as is the office of Governor or judge of this court. It is created by the same instrument which created the office of Governor and the judicial department of the state. The individuals who compose the board and discharge its duties happen to be state officers, and it so happens that the Governor of the state by reason of being Governor is chairman of the board. When acting and voting at a meeting of the State Board of Land Commissioners, and discharging the particular and special duties devolving upon the board, he is not acting as the chief executive, but on the contrary is acting as one of four members of a board in the discharge of certain ministerial and quasi judicial duties imposed on such board by the Constitution and statutes. The writ, if issued, would run against the board, and not against the Governor.

Id., at 569-570, 107 P. at 495-496.

In 1933, this Court issued a writ of prohibition to prevent the state treasurer from investing monies from "a sacred trust fund created for the express purpose of maintaining the public educational institutions of the state" in a manner contrary to law. *Parsons v. Diefendorf, State Commissioner of Public Investments*, 53 Idaho 219, 221, 23 P.2d 236, 238 (1933). Similarly, in *Moon v. Investment Board*, 98 Idaho 200, 560 P.2d 871 (1977), this Court made permanent a writ of prohibition preventing the Investment Board Expense Fund from defraying its administrative expenses with earnings from the investment of public school funds.

In 1999, this Court granted a writ of prohibition against the State Land Board of Commissioners, barring the implementation of a procedurally flawed constitutional amendment. *Idaho Watersheds Project v. State Board of Land Commissioners*, 133 Idaho 55, 982 P.2d 358 (1999). In so doing, this Court acknowledged its own "jurisdiction to review a petition for extraordinary relief where the petition alleges sufficient facts concerning a possible constitutional violation of an urgent nature." *Id.* at 57, 982 P.2d at 360. This Court reiterated that standard a year later in *Van Valkenburgh v. Citizens for Term Limits*, 135 Idaho 121, 15 P.3d 1129 (2000), when it granted a writ of prohibition prohibiting the Secretary of State from carrying out statutory requirements pertaining to the placement of ballot legends on the ballot.

Other courts have employed writs of prohibition in similar circumstances to prohibit trustees of public endowment lands from leasing such lands at below-market rates. In *Oklahoma Education Ass'n v. Nigh*, 624 P.2d 230 (Okla. 1982), the Oklahoma Supreme Court assumed original jurisdiction to determine whether the commissioners of the Oklahoma Land Office should be prohibited from applying certain statutes capping rents of school endowment lands. One statute capped rents of farming and ranching lands at 3% of fair market value, and another statute limited rents to between 2% and 4% of fair market value. *Id.* at 235. An accompanying statute provided for renewal of leases "without requiring the current lessee to exceed or match

other bids." *Id.* The court agreed with the petitioners' assertion that the below-market rents, combined with the elimination of conflict auctions, "inure only to the benefit of farmers and ranchers [and] serve only one purpose, that of subsidizing farming and ranching operations," id. at 236, and issued writs of mandamus and prohibition. *Id.* at 232.

IV.

NO PLAIN, SPEEDY, AND ADEQUATE REMEDY EXISTS IN THE ORDINARY COURSE OF LAW

No plain, speedy and adequate remedy at law exists to cure the Board's action in setting lease terms that violate the Board's constitutional mandate and Idaho Code § 58-310A. Under the terms of Idaho Code § 58-307(8), lessees must apply to renew their leases by April 30, 2010. Any time thereafter the Board may enter into new leases that would go into effect when the current leases expire on December 31, 2010. Given the impending execution and implementation of new leases, there is simply not enough time to seek a remedy in district court.

It is imperative that a final decision be obtained and implemented by the Board prior to the new lease term to prevent further harm to endowment beneficiaries. Even if the Attorney General were able to obtain a favorable decision in district court before the end of the year, the outcome would be an injunction staying the implementation of the new leases while an appeal is sought by the lessees. Such an injunction would do little to make the beneficiaries whole, however, since it would likely leave in place not only the present lease terms, but the effects of recent Board actions that froze effective rental rates. Such freezes have reduced cottage site lease income by over $2 million per year. *Petition, Paragraphs 23-24.* Thus, any injunction pending a final appeal before this Court would result in the beneficiaries losing millions of dollars of income.

Prolonged proceedings before the district court would also harm lessees, for they would be forced to decide whether to sign new ten-year leases while litigation is pending that may require substantial alteration of the lease terms. Informed decisions are virtually impossible under such uncertain circumstances. Expedited proceedings before this Court would remove such uncertainty and allow lessees who are currently paying rental rates well below market value to make an informed decision as to whether they will, depending on the outcome of this petition, enter into new leases that meet constitutional and statutory mandates to obtain market rent.

If a district court could provide a plain, speedy and adequate remedy, the Attorney General would certainly seek a remedy in that forum; however, with respect to the Board's unconstitutional actions on the cottage site lease terms, the Attorney General has no alternative but to seek this extraordinary writ. Time is of the essence for all parties involved. A prompt resolution of this matter will provide an opportunity for the Board to take such action as this Court determines is necessary for the Board to fulfill its fiduciary duty to the endowment beneficiaries.

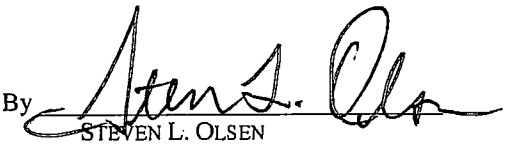
V.

CONCLUSION

The Board's actions on March 16, 2010 directly violated its constitutional and statutory obligations to the beneficiaries of the three trusts. Because the Board acted contrary to the Idaho Constitution and Idaho Code § 58-310A in setting lease terms that cannot secure the maximum long term financial return to the trusts' beneficiaries, the Board was without authority or jurisdiction to approve the lease terms, and the Attorney General prays this Court to grant the writ of prohibition and enjoin the implementation of the illegal lease terms.

DATED this 24th day of March 2010.

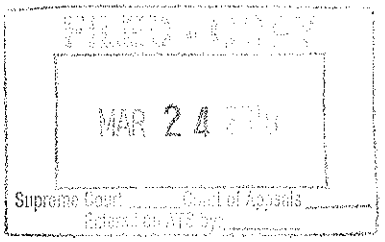
STATE OF IDAHO
OFFICE OF THE ATTORNEY GENERAL

By 
STEVEN L. OLSEN
Deputy Attorney General

By:
MELISSA MOODY
Deputy Attorney General

LAWRENCE G. WASDEN
ATTORNEY GENERAL

STEVEN L. OLSEN, ISB NO. 3586
MELISSA MOODY, ISB No. 6027
Deputy Attorneys General
954 W. Jefferson, 2nd Floor
P.O. Box 83720
Boise, ID 83720-0010
Telephone: (208) 334-2400
Fax: (208) 854-8073



Attorneys for State of Idaho

IN THE SUPREME COURT OF THE STATE OF IDAHO

HON. LAWRENCE G. WASDEN, the Attorney General of Idaho, ex. rel. the STATE OF IDAHO Petitioner, vs. IDAHO BOARD OF LAND COMMISSIONERS, and GEORGE BACON, in his official capacity as Director of the Idaho Department of Lands	)	**Case No.:** 37528 **AFFIDAVIT OF STEVEN W. STRACK IN SUPPORT OF BRIEF IN SUPPORT OF PETITION FOR PROHIBITION**

STATE OF IDAHO)
)
County of Ada)

I, Steven W. Strack, being first duly sworn, depose and say:

1. I am a Deputy Attorney General and I have worked in this capacity since 1988.

COPY

2. Among other duties I oversee the provision of legal services to the Idaho Department of Lands, and am familiar with the records retained by the Idaho Board of Land Commissioners ("Land Board") and the Idaho Department of Lands. .

3. To assist the Attorney General in making an informed determination of rental rates for cottage site leases, the Attorney General requested that I gather from records of the Department all available documents relating to past and present Board actions relating to cottage site leases.

4. In addition, while preparing Attorney General Opinion 09-01, I had occasion to research the legislative history of Idaho Code § 58-310A. In doing so, I examined the records of the Legislative Services Office, and obtained a tape of the hearing held by the Senate Resources and Environment Committee on February 16, 1990, and had my assistant prepare a transcript of that hearing. That transcript is attached to this Affidavit as Exhibit 28c.

5. Upon determining to file the present writ of petition, the Attorney General requested that I prepare for filing with this Court the records I had gathered from the records of the Idaho Department of Lands, the documents provided to Land Board members at recent Land Board meetings, the transcripts of recent Land Board meetings and cottage site subcommittee meetings circulated to Land Board members and staff, and the legislative history of Idaho Code § 58-310A.

6. To the best of my knowledge and belief, the attached exhibits are true and accurate copies of the original documents in the records of the Idaho Department of Lands and the Legislative Services Office.

7. The following exhibits are attached to this Affidavit:

1. Land Bd. Meeting Minutes (August 4, 1981).

2. Land Bd. Meeting Minutes (Oct. 13, 1981).

3. Land Bd. Meeting Minutes (June 25, 1986).

4. Land Bd. Meeting Minutes (May 17, 1988).

5. Land Bd. Meeting Minutes (July 10, 1990).

6. Land Bd. Meeting Minutes (June 11, 1991).

7. Land Bd. Meeting Minutes (June 9, 1992).

8. Land Bd. Meeting Minutes (June 4, 1997).

9. Land Bd. Meeting Minutes (Oct. 21, 1997).

10. Land Bd. Meeting Minutes (Dec. 15, 1998).

11. Land Bd. Meeting Minutes (June 12, 2007).

12. Land Bd. Meeting Minutes (Dec. 4, 2007).

13. Land Bd. Meeting Minutes (June 19, 2008).

14. Land Bd. Meeting Minutes (Dec. 16, 2008).

15. Land Bd. Meeting Minutes (June 16, 2009).

16. Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998).

17. Transcript, Land Bd. Cottage Site Subcommittee Meeting (June 3, 1991).

18. Land Bd. Agenda Memorandum, Cottage Site Rental Policy Recommendations (June 11, 1991).

19. Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Recommendation for Rental Rates (June 9, 1992).

20. Land Bd. Agenda Memorandum, Cottage Site Rental at Priest and Payette Lakes (April 8, 1997).

21. Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Report (Dec. 15, 1998).

22. Land Bd. Agenda Memorandum, 2009 Rent Changes for the Payette Lake and Priest Lake Cottage Sites (June 19, 2008).

23. Land Bd. Agenda Memorandum, 2009 Cottage Site Rental Rates (Dec. 16, 2008).

24. Land Bd. Agenda Memorandum, 2010 Rent Changes for Payette Lake and Priest Lake Cottage Sites (June 16, 2009).

25. Land Bd. Agenda Memorandum, Recommendation of the Cottage Site Subcommittee (Feb. 16, 2010), with Attachment 1: Philip S. Cook and Jay O'Laughlin, Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands (October 2008).

26. John T. McFadden, Appraisal Report: Project Report with Comparable Sales for Priest Lake Cottage Site Appraisals (1998).

27. Bradford T. Knipe, Complete Appraisal, Self Contained Report and Market Analysis of 14 Payette Lake Cabin Sites (1998).

28a. Senate Resources and Environment Committee Minutes of February 9, 1990.

28b. Senate Resources and Environment Committee Minutes of February 16, 1990 (with attached written statement of Payette Lakes Cabin and Pilgrims Cove Association titled "Questions and Answers Concerning Lease Lot Issues").

28c. Transcript of Senate Resources and Environment Committee Meeting February 16, 1990 (prepared by Attorney General's Office from tape on file with Legislative Services Office).

29. Letter, IDL Director George Bacon to Lawrence Wasden, Feb. 12, 2010.

30. Terry L. Anderson and Reed Watson, Report to Idaho Attorney General Regarding Cottage Site Leases (2010).

31. Terry L. Anderson and Reed Watson, Analysis of Subcommittee Recommendation to the Idaho Board of Land Commissioners (2010).

32. Deliberately left blank.

33. Transcript, Land Bd. Cottage Site Subcommittee Meeting (April 22, 2008).

34. Transcript, Land Bd. Cottage Site Subcommittee Meeting (May 18, 2009).

35. Transcript, Agenda Item 10, Cottage Site 2010 Rent Changes and Update on Cottage Site Subcommittee, Land Bd. Meeting (June 16, 2009).

36. Transcript, Agenda Item 7. Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (Feb. 16, 2010).

37. Addendum to Cottage Site Subcommittee Report (March 16, 2010)

38. Spreadsheet Comparing Annual Rents to Leasehold Sales, 2001-2009, provided by Idaho Department of Lands in response to request from Attorney General Lawrence Wasden (March 11, 2010).

39. Letter, Karl Klokke to Land Board members (Feb. 24, 2010).

40. Letter, Terry Copple to Land Board members ((March 12, 2010).

41. Transcript, Land Bd. Cottage Site Subcommittee Meeting (March 1, 2010).

42. Transcript, Agenda Item 8, Recommendation of the Cottage Site Subcommittee, Land Bd. Meeting (March 16, 2010).

43. Idaho Department of Lands Cottage Site Considerations & Recommendation (circulated to Land Board Staff on March 9, 2010).

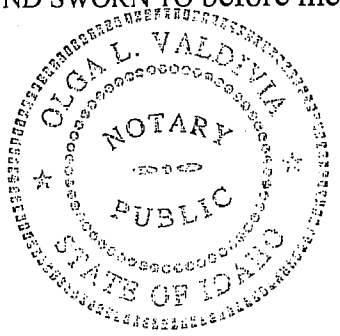
44. Letter from Attorney General Lawrence Wasden to Governor C.L. "Butch" Otter (Feb. 12, 2010).

This concludes my affidavit.

DATED this 24th day of March, 2010.

By _____
STEVEN W. STRACK
Deputy Attorney General

SUBSCRIBED AND SWORN TO before me this 24th day of March 2010.



_____
Notary Public for Idaho
My Commission Expires 2/8/2012

Exhibit 1

Land Bd. Meeting Minutes

(August 4, 1981)

SPECIAL ACTION
STATE BOARD OF LAND COMMISSIONERS
July 23, 1981

On this date special action was taken by the Board to consider the following:

Dredge Mining Permit Application No. 107 - Aileen Mayes: Application was submitted on July 1, 1981 for ten acres located in the N 1/2 Section 26, and the SE 1/4 Section 23, Township 22 North, Range 6 East, B.M., Valley County, in the Calumet #1 unpatented mining claim. The surface is administered by the U.S. Forest Service.

Application was approved with stipulations as stated. Members approving this application were:

Honorable Pete T. Cenarrusa, Secretary of State
Honorable David H. Leroy, Attorney General
Honorable Joe R. Williams, State Auditor

STATE BOARD OF LAND COMMISSIONERS

By John V. Evans President
and Governor of the State of Idaho

COUNTERSIGNED:

Secretary of State

Director, Department of Lands

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
AUGUST 4, 1981

The regular meeting of the State Board of Land Commissioners was held Tuesday, August 4, 1981, at 1:30 p.m. in the West Conference Room of the Hall of Mirrors. Governor John V. Evans presided. Those members present were:

Honorable John V. Evans, President, and Governor of the State of Idaho
Honorable David H. Leroy, Attorney General
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Joe R. Williams, State Auditor

Gordon Trombley, Secretary to the Board

Absent and Excused:

Honorable Jerry L. Evans, Superintendent of Public Instruction

Cottage Site Lease Rates

Jack Gillette, Assistant Director, Department of Lands, was asked to report. He said that a number of years ago the Land Board adopted a systematic formula for adjusting cottage site lease rates. This was based on a five-year review, taking the leasehold value or value of the sale or assignment, less the improvement value, dividing by 3 and multiplying by 7-1/2%. Division by 3 is dividing by a third of the year when the sites are generally not usable, and the 7-1/2% was about the average percentage the endowments were earning at that time. Mr. Gillette said when this formula was applied to the rates to be established in 1982, it came out to very large increases. Therefore, the Department looked at some alternatives, particularly since many of the people who have cottage sites are of modest means. A different approach is being suggested. The formula would take the average increase, and when the cottage site sells, the State acquire 10% of that value. The State would recoup in the long run. The Department is recommending that the Board adopt the alternative of using the average leasehold increase over the 1976 base and 10% of the leasehold value as premium rental be adopted for 1982 rents and that an annual leasehold value and rate review by the Department be required.

Governor Evans opened the discussion asking for further clarification on this proposal and how many sites are sold each year and how much would the State benefit in a year. Mr. Gillette said the estimate is that about 10% of the sites are sold each year and the estimate of the amount is about $480,000, which would offset the reduction in rates. Mr. Leroy asked what is the difference between a Class 1 site and a Class 2 site. Mr. Gillette explained that Class 1 is on the waterfront and Class 2 is in back without direct access.

JULY 23, 1981
AUG. 4, 1981

Mr. Eugene Heil of the Pilgrim Cove Owners Association came forward and asked questions of Mr. Gillette. He asked if the 10% increase applies to the value of the land itself or the entire leasehold. Mr. Gillette explained that the 10% fee would only apply if the property were sold and the State would get 10% of the leasehold value after the improvements were subtracted.

Governor Evans suggested postponing this issue until the Department can bring back more information on leasehold values. Mr. Leroy agreed it might be useful to postpone this matter for 30 days and get additional input from the leaseholders associations, perhaps include some who would like to have acquired leases in the past, but have not been able to because of the scarcity. He would also like to see some leasehold value projections; a simplified, large diagram illustrating the various computations used to arrive at these numbers. He also suggested exploring the possibility of breaking down Class 1 into a group of subclasses; and asked that the Department return with some maps of the various areas that are being considered, illustrating how they differ, and perhaps spotlight a few subject properties with photographs of the area, etc. Mr. Williams made a motion to postpone the issue to next month. Mr. Cenarrusa seconded. The motion passed unanimously.

Airport Commission

Mr. Trombley explained this is an issue that was before the Board at the May meeting and concerns a minerals policy relating to the mineral rights, mainly sand and gravel, at the Boise City Airport. The policy concerns leasing activity, safety and use of the surface near the airport. The City has had an opportunity to respond to the recommendations made by the Department and they have approved everything but Recommendation #2. This recommendation deals with the City's right to issue leases or permits for a reasonable sum, not to be unreasonably withheld to anyone who might lease the State's mineral rights.

Mr. Ferd Koch, Chairman of the Airport Commission; Mr. Don Duvall, Manager and Mr. Mike Moore, City Attorney, appeared to state their views. Mr. Koch said that they feel Recommendation #2 has to do with some sort of approval or right of the City to approve the lessor, and they would also like to be able to issue a permit to the company for a reasonable fee to hold the City harmless in the event of an accident. Mr. Moore said the principle concern is that the statute now on the books provides for bond and does not clearly run in favor of the surface owner. Therefore, they are requesting the authority to require a bond to protect the City.

Mr. Leroy stated that the State is more than willing to work with the City to be sure there be no safety difficulty; that the special and peculiar requirements for the safety and operation of the airport is a main consideration, but would not want to give exclusive or veto control to the surface owner. He feels the language offered here would essentially take the control of this project from the State and place it in the City's hands. He said the Land Board wants to work any way it can with the Airport Commission and the City, but would still prefer to have the Land Board generally control the project with as much input and attention to the safety needs as necessary.

Governor Evans made the suggestion that the Boise City Attorney and the Attorney General work together on protective language that would provide both entities satisfaction. There being no objections from any of the members present, the Governor so ordered to delay action until there is a report from the Attorney General and the Airport Commission.

Hydrodevelopment - Priest Lake

Mr. Jim Martin, Forest Lands Manager for the Pack River Co., thanked the Board for allowing them to come before the Board to make this presentation. Mr. Martin introduced the others with him today: Richard Chastick and Bill Nixon who are partners and legal counsel for Packer Management Co.; Dan Larson, Manager of Power Associates Co.; and Bill Delp, President and majority owner of both Home State Consulting Investment, Inc., and Independent Power Developers. They are here to present a proposal for another use in the multiple use concept of managing state forests. This proposal is for permanent, or long-term easements on some endowment lands in the Priest Lake State forest for non-consumptive use of hydro-electric power generation, using small or mini-high head water power generators. He said that Mr. Bill Delp would make the presentation today.

Mr. Delp said that what had prompted investigation of remote sites such as Priest Lake was that in 1979 the Federal Energy Regulatory Commission passed a law called PURPA (Public Utilities Regulatory Policy Act) which essentially excluded private developers on a small scale basis from being qualified as a utility. This was prompted to get off fossil fuel systems as much as possible; to create alternatives and was aimed at private investor utilities. Preliminary permits have been filed for the Priest Lake proposed project and Area Supervisors have looked at the hydroelectric site in Clarksfork, particularly Mr. Gill who is responsible for the Priest Lake area, to evaluate the impact on the land use and the environment. They also have worked with Mr. William Goodnight of Department of Fish & Game. Fish & Game gave a very favorable response to the proposed development. Mr. Gill supplied a letter of permission to do specific surveying work required to establish an easement on which to base a fee for land use. The land areas involved for these projects would be fairly narrow easements for lines and an underground turbine house. Mr. Delp said they are prepared at this point to move forward and establish that this is a credible use for state lands, develop a fee structure for these easements in order to forge ahead on these projects this fall and be able to bring meaningful amounts of power on the lines by next spring.

Mr. Delp said there are twelve proposed sites and they would produce somewhere in the area of a megawatt each and would offset the utility's need to upgrade their powerline from the Sandpoint side. In answer to questions from the Board, he said

In answer to Mr. Leroy's question about difficulties of options 2 and 3, Mr. Korte said his suggestion in attempting to amend the Comprehensive Plan would be to go for the one-dwelling per five acre amendment process, if a municipal sewer system could not be obtained. This would involve a rezoning application but he believes that procedure should be investigated.

Mr. Korte said that on the issue of the potential expansion of the golf course, the ordinance today allows a golf course as a conditional use in that zone. There could be a situation where that golf course could be expanded after public hearings and approval by the Ada County Zoning Commission. In doing that, the issue of being able to locate houses and dwelling units adjacent to it, could be addressed at that time without a Comprehensive Plan change, so basically it could only be a golf course, and not a residential development.

Jerry Evans suggested asking the staff to analyze options 2 and 3 and then come back with a recommendation as to the better of the choices, and to eventually move toward the sale of this property; if possible, getting a change in the Comprehensive Plan that would allow for a higher appraisal. Mr. Evans therefore made a motion that the Board ask staff to analyze alternatives 2 and 3 and bring back recommendations to the next Board meeting. Mr. Williams seconded. The motion passed unanimously.

Cottage Site Lease Rate Increases

Mr. Trombley said there are some Department recommendations before the Board and there are a number of people present who have requested the opportunity to testify before the Board. Governor Evans first asked for a presentation by the Department and then to hear from the people concerned. Jack Gillette presented the issue. He said that two meetings ago, the Department presented a proposal to amend the cottage site lease rates. Five years ago a Board decision was to reappraise the cottage lease rates every five years based on a formula that recorded leasehold value transactions. Applying that formula now produces extremely high rental rates. Therefore, the Department submitted an alternative formula, calling for reducing the formula rate, but also applying a 10% assignment fee to be returned to the State when the property is sold. The idea is that those people who have had leases would not be severely penalized, and if they did sell, the State could share the profit. Mr. Scribner reviewed the formula for the Board and answered questions. He said that leasehold value is based on the total sale price less the value of the improvements which are determined by using two factions, the assessor's value and the Department's estimate of construction costs in the area.

Governor Evans invited the representatives from the Priest Lake Association to come forward to testify. Mr. Carroll Martell, President of the Association, and Mr. Ken Coffman, Vice-President of the Association, introduced themselves to the Board. Mr. Martell said there are approximately 360 lease lots at Priest Lake of which approximately 260 are dues paying members of the Association. Mr. Martell believes that the determination of lease rates for cottage sites was not fully addressed when recent procedures were established. At Priest Lake the State is not in a position to provide water and sewer systems, and access is minimal. He said that with the anticipated increase in lease fees, they will be paying more in fees and taxes for the privilege of seasonal use of cottage sites than for living in developed residential areas. The Priest Lake Association feels the proposed alternative method as proposed in the July memo to the Land Board would percentagewise be a very substantial increase which would work a hardship for those who have to sell for conditions beyond their control. The Association's primary interest is to keep the lease fee as reasonable as possible so that people with ordinary income, such as retirees, can continue to afford cottage sites. If this percentage-of-leasehold value at time of sale formula is adopted, they ask that arrangements take into consideration the tenure of the occupant. The quick, turnover speculator should be discouraged. The Association is also opposed to an annual review and request maintaining the five-year review period. Mr. Ken Coffman reported that during the last three years, lessees have been working on the problem of polution of Priest Lake, and the solution is going to be very costly to the lessees. Mr. Coffman also expressed concern with some subleasing situations that have arisen.

Mr. Scott Nelson, President, Pilgrim Cove Association, said they recognize the State's obligation to maximize its income, but should not adopt any plan which encourages speculation. He outlined a plan the Association proposes which comes near what the Land Department proposed in Alternative 2 but there would be no surcharge or premium rental.

Charles Blanton, Payette Lakes Leasehold Association, said a significant factor has been overlooked and that is that thirty years ago the State enticed and encouraged people to lease those lots, and the lease charged was, in fact, in lieu of taxes. This has gone totally beyond this concept. By their own efforts, the lessees have made decent sites out of the land. They are now trapped and the leaseholder never knows from one minute to the next what he is going to be subjected to. Mr. Blanton went on to say that their association has tried to encourage the Board to make at least available to those who want to buy, and by any reasonable basis fixing the land values, to let the leaseholders who wanted to buy, to purchase the property. Their recommendation is that the lease payments be coordinated with the taxes; there should be a direct coordination between what is charged for leases and what is charged for taxes.

Other persons present who asked to be heard by the Board:

Adelaide McLeod, lessee of lakefront property at Pilgrim Cove and a real estate broker, stated that in doing a market analysis, she disagrees with the Department figures. She said that tax evaluations from Valley County do not reflect correct value. The properties have not been evaluated properly, and she thinks this is what is causing the problem.

Dr. Forney stated that he is astounded by some of the unrealistic fees. He feels the State should be out of the leasing business; the lessees would be better off owning the property. His suggestion is that the State sell, although he realizes it would have to be done by open bidding.

Mr. Wayne Peterson said he has leased his property since 1945, and he also owns some property on Davis Beach. He has had to install his own sewer, water and pumping system, and put in a piling wall. His new fee, including taxes, will be over $900 which he feels is too high when he had to do all this work. Mr. Leroy asked Mr. Peterson if he feels the lease rate formula should be a flat rate or a graduated rate. Mr. Peterson said he thinks rates should be variable.

Harvey Hoff, member of the Pilgrim Cove Association, suggested the Land Board consider looking at a revision of the one-year cancellation revision, since lesses can't borrow money on their leases.

Kathy Daley said that there are only so many lots, which are become more attractive all the time, and the lessees through no fault of their own, are becoming a captive group.

Jack Flaherty said he has a lease lot at Pilgrim Cove and suggested the State sell if there could be some way to favor the current lessees rather than sell by public auction.

Mr. Leroy asked the Association representatives two questions: 1) what would the Association's position be on the single rate for Class 1 and 2 as opposed to a variable rate adjusted parcel-by-parcel; and 2) its position on a five-year averaging approach versus an annual adjustment. The answer from the representatives was that they would think the Class 1, Class 2 structure is adequate; and they would be in favor of the five-year adjustment.

Cynthia Dalrymple, a lot lessee, voiced several complaints concerning speculators and subleasing and/or pooling issues. Governor Evans asked if there is any prohibition against frequent transferring of property. Mr. Trombley said that assignment of leases require Department approval, and if there were very many changes, it would be looked into. However, some of these transfers may not be on paper and Department agents may not be aware of it. Land Board policy is that only one name can be be recognized on a lease. Mr. Riddoch explained that it would be very difficult to draw or construct a clause which would discourage rapid turnover while at the same time opening the door for legitimate turnover. Governor Evans asked that Mr. Trombley make the Area Supervisor aware of what is going on and perhaps circulate a letter to the lessees cautioning them against these kinds of abuses.

There being no further persons wishing to testify, Mr. Leroy offered a five-point motion: 1) the State Land Board adopt the formula Option B as the basis for rentals and cottage site leasing for the next five years providing for rental rate of $730, $422, and $608, repectively, on Payette Lakes Class 1 and 2, and Priest Lake; 2) that the Board reaffirm the Class 1, Class 2 flat rate structure for Payette and Priest Lakes; 3) that the Board recompute new rental rates in 1986 based upon the five-year average as provided in Option B of the formula; 4) that the Board adopt a 10% tariff on lease transfer arrangements effective January 1, 1981; and 5) offset that tariff by an additional benefit to the leaseholders of changing the one-year cancellation notice to a two-year cancellation notice. The motion was seconded by Jerry Evans. Mr. Trombley asked for clarification that the two-year proviso means for Department disposition and not for cancellation due to violation of lease. The answer was affirmative.

Jerry Evans said that although he supports the motion, he feels there is a need to find some way to tie into the market value increase from a broader rather than a very narrow sales sample. Before another five years down the road, there should be some way to make these adjustments on an objective, formula basis, so that all could know in advance and understand. Mr. Cenarrusa stated he thinks the 10% tariff has some problems, but is confident that if it isn't right, the Board will change it. Governor Evans agreed that there are some problems and said that the Land Department staff will come forward with a recommended policy the Land Board can adopt in relation to this, examining carefully all aspects of the 10% factor, and adopting rules and regulations to apply to it. The motion passed unanimously.

The Walker Center - Carl Bergstrom

Mr. Bergstrom told the Board that the Center is currently facing a financial crisis for three reasons: state cutbacks in spending; a continued low census; and a lack of acute hospital status. The result is that they are $75,000 behind this fiscal year, and it is unlikely that St. Benedicts will subsidize. The Center still plans to go forward with the Gooding County Hospital transaction, but in the interim, are seeking some immediate relief in rent payments.

Jerry Evans said the Land Board has attempted to be as reasonable and supportive as possible, and have made several allowances. The State may be at the point that instead of facing an empty building later on, face it now. Mr. Bergstrom stated that the State has benefitted from their maintaining the building in good repair. Governor Evans suggested having Mr. Trombley analyze the situation and come back with a recommendation, letting the Walker Center continue to operate until then. Mr. Leroy said he would not be interested in further adjustments of that lease nor in having the Department staff work at that magnitude. There have been many adjustments to that lease. He would prefer to move toward mothballing the building and indicate to them that the State has bottomed out on what it can do on lease terms. Mr. Trombley inquired that if the Board should move in the direction of mothballing, would there be a grace period to allow these people an orderly transition out of there. Mr. Evans said they could stay until they are delinquent in their payments. Mr. Trombley stated that the Center has been unable to meet their commitments and are delinquent now. Governor Evans said he would think it would now be up to the Walker Center and

Exhibit 2

Land Bd. Meeting Minutes

(Oct. 13, 1981)

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
October 13, 1981

The regular meeting of the State Board of Land Commissioners was held Tuesday, October 13, 1981, at 9:00 a.m. in the Conference Room of the Hall of Mirrors. Governor Evans presided. Those members present were:

Honorable John V. Evans, President, and Governor of the State of Idaho
Honorable David H. Leroy, Attorney General
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Joe R.Williams, State Auditor
Honorable Jerry L. Evans, Superintendent of Public Instruction

Gordon Trombley, Secretary to the Board

Airport Committee Matter

Mr. Trombley said this matter needs to be deleted from the agenda since the City Council and the Attorney General's office are still working on legal language relating to the agreement.

Martin Clemets - Visitor

Mr. Trombley said this matter also needs to be deleted from today's agenda as Mr. Clemets could not be here today due to conflicts in his schedule.

Hansberger Land Exchange

Mr. Trombley said this issue has been before the Board previously, and a Land Board subcommittee examined the property and may have a report relating to it. Governor Evans asked if the Chairman of the subcommittee would report. Mr. Cenarrusa reported the subcommittee did make a trip to look at the land involved and have made no decision. The recommendation was for the Board to hear testimony on the matter and this was done. It is therefore submitted to the Board without recommendation.

Attorney General Leroy stated that when the Board last heard testimony a number of legal issues were raised and the Attorney General's office has examined those. Mr. Don Olowinski has a report on those issues of concern. Mr. Olowinski reported that the questions raised during testimony were: 1) Senator Risch, speaking on behalf of the King's, raised the possibility that the State in fact did not own the lands in question, but had in fact, by platting the area in question divested itself of title to those lands; 2) regardless of ownership, an exchange could subject the State to liability for inverse condemnation of Mr. Risch's clients' property. The Attorney General's office researched those questions and concluded that ownership still remains in the State. That conclusion was buttressed by a decision of Judge Smith recently in a suit that raised a similar issue. In addition, it was concluded that the State would not be subject to liability for inverse condemnation, however, the State recognizes that if litigation ensues, there could be a risk. Mr. Hansberger indicated that he would be willing to indemnify the State and hold harmless the State for any losses that would result from an approval of the exchange. There is a document from Mr. Hansberger so stating. Mr. Olowinski said it would be only prudent that when there can be no risk to the State, he would advise the Board to accept that indemnification offer from Mr. Hansberger if the Board chooses to go ahead with the exchange. Legally, there is nothing to prevent the Board from proceding with the exchange.

Mr. Williams said this has been before the Board several times and it has heard from all the interested parties, therefore he is of the opinion that 50 feet of property is better for the State than 30 feet and made a motion that the Board accept Mr. Hansberger's offer, with legalities to be worked out with the Attorney General's office. Mr. Cenarrusa seconded. The motion passed unanimously.

Hydroelectric Generating Plant Applications - Priest Lake

Mr. Trombley said this is a matter relating to an application from the Homestate Development Co. who is seeking easements from the State in order to develop some hydroelectric sites at Priest Lake. Some of the Board members have had the opportunity to view these sites to some degree. There is a delegation here from the applicants who may wish to give further testimony. The visitors introduced themselves: Jim Martin, representative of Power Associates Co., as a consultant; Dan Larson, President and Manager of Homestate Investments Co. Mr. Martin said that he had sent a letter in August outlining their proposal for rates to be returned to the State in regard to the easements for right-of-ways for pipelines, powerlines and power generating sites. Mr. Delp said that they have received concurrence with the various licensing agencies. The installed capacity would be about 2 megawatts with an average output of about 1 megawatt, and their proposal is based on installed capacity. They are asking the Board's consideration to allow a formula which would let them identify the risks and remain flexible in developing watershed for power production to offset fossil fuel consumption.

Governor Evans asked what the procedure would be in relation to public hearings on this matter. Mr. Trombley said this was discussed at a previous meeting and there has been extensive advertising in the local papers relating to these applications. Mr. Martin said there have been no formal hearings, but there has been no adverse comments from newspaper advertising. Mr. Riddoch reported that the Department has filed a protest which is meant only to preserve the Board's rights. The basis for this was that these are school endowment lands subject to strict constitutional guidelines and the Board had not completed its administrative review or made any kind of a decision. Governor Evans asked if all the State agencies involved have been directly contacted to make sure we receive their recommendations.

Herb Pollard, State Fisheries Manager, Idaho Fish & Game Department, spoke to the Board and said that Fish & Game has agreed to the proposal. Governor Evans requested a letter from Fish & Game with their comments. Mr. Trombley said the applicants had requested permission to appear before the Board and answer any interim questions that may have developed and to discuss the question of easement fees. This is not an ironclad recommendation for the granting of an easement now, but is only to develop some policy that would lead to easement considerations for any and all such types of development. Mr. Trombley explained that Department staff has reviewed the information on the fee proposals and in keeping with the Board's instructions, have incorporated a proposal for revenue in with the policy statement. The applicants have not been involved in any discussion of the 4% of gross figure proposal. Jerry Evans asked Mr. Martin if he would make some comment with respect to the 4% proposal, whether that is a reasonable or an unreasonable figure. Mr. Martin said that it is a higher rate than what they had proposed. He said their fee had been suggested upon installed capacity rather than on generated revenue. The 4% gross is about twice as high as some figures that they have negotiated with some private ownerships. Mr. Larson said the 4% rates suggested, using the acreage projected, might net the State around $21,000. The earlier rate they suggested was about one quarter of that. They used timberland easements as a comparable and came up with what they feel is a fair figure. Mr. Delp said he feels that for the first few years, 2% of gross would be more appropriate with an accelleration after a good learning curve has been established on the site. Jack Gillette reported to the Board that most other easements are in the vicinity of 4% of gross. Governor Evans said the Board should look to maximizing return and the State should derive a suitable return. If 4% is a reasonable figure that the Department had established earlier, then in this case, it could be applied uniformly. If any substantial hardship developed in relation to that before the contract is finalized, these applicants could come back for another review. For now, Governor Evans said he feels comfortable accepting the Department recommendation initially in this preliminary policy formulation program.

Mr. Trombley said that with the aid of legal counsel, a specific form can be developed to be used to accomplish the purpose of satisfying these applications. Mr. Delp said what they want is to set some parameters that can be negotiated and possibly giving them a period of years to gain a confidence level on the watershed prior to escalating the percentage of gross revenue.

Governor Evans asked for a motion to approve the development of policy dealing with hydroelectric generation. Mr. Leroy moved the approval of this policy on a tentative basis with an eye toward the Department using it as a framework for negotiations, and perhaps there will be a number of changes. He also offered in his motion two amendments: 1) Page 1, provision #5, in discussing easements in perpetuity with the normal 5-year non-use termination clause, it may be if certain of these projects have an anticipated lesser use for life than perpetuity, and we may want to talk about easements for some lesser scope of time, so would insert after the word perpetuity, the phrase "or period of years" to contemplate either of those events; and 2), would make the motion adding on page 2 in paragraph 12, providing that the State application be similar in form and content to mining permits including a proposed operating plan providing for site inspections by various State agencies with any of the conditions of operation written into either the easement of the lease and proposing as well a reclamation policy or reclamation program after the termination of any operating improvement. Jerry Evans seconded. The motion passed unanimously.

Indian Lakes Golf Course Site Proposal - Mr. Sheldon Gerber

Mr. Trombley said this matter is back before the Board in keeping with the Board's previous actions to seek additional information from the local Planning and Zoning Association pertaining to the question of the sale of that property.

Sheldon Gerber, Secretary to the Ada County Planning Commission, and Mr. Chris Korte, Ada County Zoning Administrator, appeared before the Board to make a presentation concerning this property. In August they received a letter from Mr. Trombley asking if they could identify what higher density developments could be permitted on the property so that a higher income could be generated for the school endowment fund. Presently the property is zoned D-1, Rural Area Zone, which allows one dwelling per 80 acres, plus a one-acre lot split for each 40-acre parcel. So there are three dwelling units that can be permitted on the 80 acres. There are four options he briefly outlined: 1) The land as now zoned, D-1, allows conditional use permits if a public hearing is held by the Zoning Commission and they grant the use. Some of the uses allowed within the D-1 zoned by conditional use permit are riding stables, schools, golf courses, drive-in theaters, gravel pits and any one of those uses could possibly yield a higher value for the land than the three dwelling units on 80 acres; 2) Amend the Comprehensive Plan to designate the area as rural residential which would allow a density of one dwelling on five acres. Mr. Gerber pointed out there are some unusual circumstances in this particular area such as ground water pollution problems and lack of public services. The process of applying for an amendment could take from six months to one year to complete; 3) Amend the Comprehensive Plan applying with the Owyhee Sewer District who has a grandfather right and can develop up to four dwelling units per acre. However, the way the Plan is written, there are some difficulties such as possible ground water pollution, etc. He said the Southwest Community is in close proximity to Boise and may be a logical place for urban expansion in the future, however, the central sewers which were in the planning stages were dropped because of public hearings in the Southwest Community. There may be a reversal of that when septic tanks need to be replaced. Replacement could be as costly as an extensive sewer system.

In summary, Mr. Gerber said that at the present time the Urban Service Planning areas in Ada County allow for growth of about 400,000 to 450,000 people over the next 30 years.

In answer to Mr. Leroy's question about difficulties of options 2 and 3, Mr. Korte said his suggestion in attempting to amend the Comprehensive Plan would be to go for the one-dwelling per five acre amendment process, if a municipal sewer system could not be obtained. This would involve a rezoning application but he believes that procedure should be investigated.

Mr. Korte said that on the issue of the potential expansion of the golf course, the ordinance today allows a golf course as a conditional use in that zone. There could be a situation where that golf course could be expanded after public hearings and approval by the Ada County Zoning Commission. In doing that, the issue of being able to locate houses and dwelling units adjacent to it, could be addressed at that time without a Comprehensive Plan change, so basically it could only be a golf course, and not a residential development.

Jerry Evans suggested asking the staff to analyze options 2 and 3 and then come back with a recommendation as to the better of the choices, and to eventually move toward the sale of this property; if possible, getting a change in the Comprehensive Plan that would allow for a higher appraisal. Mr. Evans therefore made a motion that the Board ask staff to analyze alternatives 2 and 3 and bring back recommendations to the next Board meeting. Mr. Williams seconded. The motion passed unanimously.

Cottage Site Lease Rate Increases

Mr. Trombley said there are some Department recommendations before the Board and there are a number of people present who have requested the opportunity to testify before the Board. Governor Evans first asked for a presentation by the Department and then to hear from the people concerned. Jack Gillette presented the issue. He said that two meetings ago, the Department presented a proposal to amend the cottage site lease rates. Five years ago a Board decision was to reappraise the cottage lease rates every five years based on a formula that recorded leasehold value transactions. Applying that formula now produces extremely high rental rates. Therefore, the Department submitted an alternative formula, calling for reducing the formula rate, but also applying a 10% assignment fee to be returned to the State when the property is sold. The idea is that those people who have had leases would not be severely penalized, and if they did sell, the State could share the profit. Mr. Scribner reviewed the formula for the Board and answered questions. He said that leasehold value is based on the total sale price less the value of the improvements which are determined by using two factions, the assessor's value and the Department's estimate of construction costs in the area.

Governor Evans invited the representatives from the Priest Lake Association to come forward to testify. Mr. Carroll Martell, President of the Association, and Mr. Ken Coffman, Vice-President of the Association, introduced themselves to the Board. Mr. Martell said there are approximately 360 lease lots at Priest Lake of which approximately 260 are dues paying members of the Association. Mr. Martell believes that the determination of lease rates for cottage sites was not fully addressed when recent procedures were established. At Priest Lake the State is not in a position to provide water and sewer systems, and access is minimal. He said that with the anticipated increase in lease fees, they will be paying more in fees and taxes for the privilege of seasonal use of cottage sites than for living in developed residential areas. The Priest Lake Association feels the proposed alternative method as proposed in the July memo to the Land Board would percentagewise be a very substantial increase which would work a hardship for those who have to sell for conditions beyond their control. The Association's primary interest is to keep the lease fee as reasonable as possible so that people with ordinary income, such as retirees, can continue to afford cottage sites. If this percentage-of-leasehold value at time of sale formula is adopted, they ask that arrangements take into consideration the tenure of the occupant. The quick, turnover speculator should be discouraged. The Association is also opposed to an annual review and request maintaining the five-year review period. Mr. Ken Coffman reported that during the last three years, lessees have been working on the problem of polution of Priest Lake, and the solution is going to be very costly to the lessees. Mr. Coffman also expressed concern with some subleasing situations that have arisen.

Mr. Scott Nelson, President, Pilgrim Cove Association, said they recognize the State's obligation to maximize its income, but should not adopt any plan which encourages speculation. He outlined a plan the Association proposes which comes near what the Land Department proposed in Alternative 2 but there would be no surcharge or premium rental.

Charles Blanton, Payette Lakes Leasehold Association, said a significant factor has been overlooked and that is that thirty years ago the State enticed and encouraged people to lease those lots, and the lease charged was, in fact, in lieu of taxes. This has gone totally beyond this concept. By their own efforts, the lessees have made decent sites out of the land. They are now trapped and the leaseholder never knows from one minute to the next what he is going to be subjected to. Mr. Blanton went on to say that their association has tried to encourage the Board to make at least available to those who want to buy, and by any reasonable basis fixing the land values, to let the leaseholders who wanted to buy, to purchase the property. Their recommendation is that the lease payments be coordinated with the taxes; there should be a direct coordination between what is charged for leases and what is charged for taxes.

Other persons present who asked to be heard by the Board:

Adelaide McLeod, lessee of lakefront property at Pilgrim Cove and a real estate broker, stated that in doing a market analysis, she disagrees with the Department figures. She said that tax evaluations from Valley County do not reflect correct value. The properties have not been evaluated properly, and she thinks this is what is causing the problem.

Dr. Forney stated that he is astounded by some of the unrealistic fees. He feels the State should be out of the leasing business; the lessees would be better off owning the property. His suggestion is that the State sell, although he realizes it would have to be done by open bidding.

Mr. Wayne Peterson said he has leased his property since 1945, and he also owns some property on Davis Beach. He has had to install his own sewer, water and pumping system, and put in a piling wall. His new fee, including taxes, will be over $900 which he feels is too high when he had to do all this work. Mr. Leroy asked Mr. Peterson if he feels the lease rate formula should be a flat rate or a graduated rate. Mr. Peterson said he thinks rates should be variable.

Harvey Hoff, member of the Pilgrim Cove Association, suggested the Land Board consider looking at a revision of the one-year cancellation revision, since lesses can't borrow money on their leases.

Kathy Daley said that there are only so many lots, which are become more attractive all the time, and the lessees through no fault of their own, are becoming a captive group.

Jack Flaherty said he has a lease lot at Pilgrim Cove and suggested the State sell if there could be some way to favor the current lessees rather than sell by public auction.

Mr. Leroy asked the Association representatives two questions: 1) what would the Association's position be on the single rate for Class 1 and 2 as opposed to a variable rate adjusted parcel-by-parcel; and 2) its position on a five-year averaging approach versus an annual adjustment. The answer from the representatives was that they would think the Class 1, Class 2 structure is adequate; and they would be in favor of the five-year adjustment.

Cynthia Dalrymple, a lot lessee, voiced several complaints concerning speculators and subleasing and/or pooling issues. Governor Evans asked if there is any prohibition against frequent transferring of property. Mr. Trombley said that assignment of leases require Department approval, and if there were very many changes, it would be looked into. However, some of these transfers may not be on paper and Department agents may not be aware of it. Land Board policy is that only one name can be be recognized on a lease. Mr. Riddoch explained that it would be very difficult to draw or construct a clause which would discourage rapid turnover while at the same time opening the door for legitimate turnover. Governor Evans asked that Mr. Trombley make the Area Supervisor aware of what is going on and perhaps circulate a letter to the lessees cautioning them against these kinds of abuses.

There being no further persons wishing to testify, Mr. Leroy offered a five-point motion: 1) the State Land Board adopt the formula Option B as the basis for rentals and cottage site leasing for the next five years providing for rental rate of $730, $422, and $608, repectively, on Payette Lakes Class 1 and 2, and Priest Lake; 2) that the Board reaffirm the Class 1, Class 2 flat rate structure for Payette and Priest Lakes; 3) that the Board recompute new rental rates in 1986 based upon the five-year average as provided in Option B of the formula; 4) that the Board adopt a 10% tariff on lease transfer arrangements effective January 1, 1981; and 5) offset that tariff by an additional benefit to the leaseholders of changing the one-year cancellation notice to a two-year cancellation notice. The motion was seconded by Jerry Evans. Mr. Trombley asked for clarification that the two-year proviso means for Department disposition and not for cancellation due to violation of lease. The answer was affirmative.

Jerry Evans said that although he supports the motion, he feels there is a need to find some way to tie into the market value increase from a broader rather than a very narrow sales sample. Before another five years down the road, there should be some way to make these adjustments on an objective, formula basis, so that all could know in advance and understand. Mr. Cenarrusa stated he thinks the 10% tariff has some problems, but is confident that if it isn't right, the Board will change it. Governor Evans agreed that there are some problems and said that the Land Department staff will come forward with a recommended policy the Land Board can adopt in relation to this, examining carefully all aspects of the 10% factor, and adopting rules and regulations to apply to it. The motion passed unanimously.

The Walker Center - Carl Bergstrom

Mr. Bergstrom told the Board that the Center is currently facing a financial crisis for three reasons: state cutbacks in spending; a continued low census; and a lack of acute hospital status. The result is that they are $75,000 behind this fiscal year, and it is unlikely that St. Benedicts will subsidize. The Center still plans to go forward with the Gooding County Hospital transaction, but in the interim, are seeking some immediate relief in rent payments.

Jerry Evans said the Land Board has attempted to be as reasonable and supportive as possible, and have made several allowances. The State may be at the point that instead of facing an empty building later on, face it now. Mr. Bergstrom stated that the State has benefitted from their maintaining the building in good repair. Governor Evans suggested having Mr. Trombley analyze the situation and come back with a recommendation, letting the Walker Center continue to operate until then. Mr. Leroy said he would not be interested in further adjustments of that lease nor in having the Department staff work at that magnitude. There have been many adjustments to that lease. He would prefer to move toward mothballing the building and indicate to them that the State has bottomed out on what it can do on lease terms. Mr. Trombley inquired that if the Board should move in the direction of mothballing, would there be a grace period to allow these people an orderly transition out of there. Mr. Evans said they could stay until they are delinquent in their payments. Mr. Trombley stated that the Center has been unable to meet their commitments and are delinquent now. Governor Evans said he would think it would now be up to the Walker Center and

St. Benedict's to determine what their next position is. He said apparently there is no motion to accept the Center's proposal to suspend the lease payments. Mr. Bergstrom said he appreciated the time and stated that they do intend to pay what they are committed to pay and will take the Board's sentiments back to St. Benedicts and his advisory board.

Jay Somsen - Trespass

Mr. Jay Somsen told the Board that he lives at Grays Lake and owns a sawmill there. He was accompanied by Earl Somsen, his brother. Mr. Somsen said that they had taken some of the State's timber without realizing what they had taken. The location of the trespass was in sections 33 and 34, T3S, 42E. This was dead, infested timber that Gentile Valley Cattle Co. was trying to salvage. At the time of the cutting, Gentile Valley believed that all of the timber that existed in that portion was on their own land. The Somsen's were told by Dewayne Denton that all the timber on the hillside, the south side of the old existing fenceline, east and west, was their property and that property existing on the north side was state property. They went on what the man told them since he was believed to be the landowner. Mr. Somsen said their whole business is now on the brink of disaster with this trespass hanging over them. If this trespass is assessed at a figure of $16,483.54, they will stand a chance to lose all they have and more. He said the timber was bought in good faith, thinking Gentile Valley would surely know where the boundaries were. They have dealt with them for over twenty years and have never had a problem until now. Governor Evans inquired whether Gentile Valley has paid the Somsen's back, and if they have paid the State. Mr. Somsen replied that they have offered to pay back the money paid for the timber. The Somsens presented a proposal for the Board's consideration: $30 a thousand at 73.76 thousand board feet which would be $2,212.80. This is the amount that would have been paid Gentile Valley for that timber. Governor Evans asked why there is such a great differential in the two amounts, $16,000 versus $2,000. Jack Gillette explained the volume is the same, but the difference is in the price per thousand. The Land Department ran an appraisal assuming the timber would have sold, and the appraisal came out to $105.80 per thousand. Earl Somsen said the big difference stems from the quality; it was dead and defective timber damaged by the timber beetle. The Forest Service makes a large allowance for this. That quality of timber could easily be secured from the Forest Service or private individuals at that time for $15.00 per thousand. Since there was some green, mature timber taken with it, they came up with a ratio which came out to $30 a thousand. Jack Gillete said the Department doesn't go by whether the timber is dead or green, but by the merchantability. Mr. Gillette also thought the appraisal was high, and did have it double checked by the Eastern Area office. They stood by this appraisal.

Mr. Trombley explained that the staff is unanimous in feeling that the Somsens did not knowingly or willingly commit this trespass, and the reason for charging double stumpage is due to the existing policy concerning that they did not report it. Jerry Evans said he is bothered by the fact that Gentile Valley sold the State's timber, received money for it, yet the Somsens are the one that are held on the hook, and wonders if the State has the wrong people here. Mr. Somsen said there were no boundaries up there, no markers, rocks or anything whatsoever for the BLM or the State. Had they found a survey post of any type, then they would have had an idea they were on the wrong property. Governor Evans said the president of Gentile Valley Cattle Co. should be here today talking in terms of why they contracted with the Somsens to cut state timberland. It is their responsibility as landowners and they are as guilty as anyone. Mr. Williams said he believes the State has a very poor case against these brothers and does not believe this is their fault and would not like to see them assessed for $16,000.

Governor Evans suggested appointing a subcommittee of Jerry Evans and Joe Williams to get together with the staff and to come back with a recommendation on how this matter should be settled. Mr. Cenarrusa said he does not feel the State should deal punitively with the Somsen's, and it does not appear that the State has really lost anything, in fact, it may have been enhanced by the cutting down of that dead and diseased timber. He would like to see a fair and equitable settlement with the Somsen's.

Governor Evans asked Mr. Evans and Mr. Williams if they would accept the subcommittee assignment, and pointed out that they should have discussions with staff in eastern Idaho, and not apply penalties, but rather go on the value of the timber. Mr. Evans and Mr. Williams accepted the assignment. Mr. Leroy also requested the Department to provide more adequate diagrams than those presented here today.

Memorandum Agreement Between Idaho Department of Water Resources and Idaho Oil & Gas Commission

Governor Evans said that Mr. Ken Dunn from Department of Water Resources is here today to speak to this matter. Mr. Dunn said this agreement is for the purpose of ensuring there is no duplication between the efforts of Water Resources and the Oil & Gas Commission. Both have some jurisdiction over injection of waste material into underground areas, aquifers, with the Oil & Gas Commission regulating production of the resources. Because of this duplication, they feel it appropriate for the two agencies to generally agree on how they are going to handle those instances where both agencies are involved. Mr. Dunn said they don't think it takes away any authority or responsibility but only verifies that one permit will be required and the process is being simplified. Mr. Leroy recommended two changes in the draft: Page 3, provision 1, a: strike the words "determination of", and b: change to read "will make the second review of oil and gas." He finds the draft acceptable with these changes and would recommend the Board's adoption. Mr. Williams seconded. Mr. Douglas Bean asked

for and received permission to speak to the Board. He said this is absolutely new to him and he has not had a chance to review it. He asked that a comment period or a delay be allowed until the next Board meeting. Governor Evans said this has been under review by the agencies for some time. Mr. Leroy suggested that the Board indicate its tentative approval of this construction and give it a return date of no longer than thirty days for comments. With no objections, Governor Evans delayed action on this matter to the next meeting to give the industry the opportunity to review. Mr. Leroy suggested circulating the draft for comments to those involved in the oil and gas industry.

Surplus Land Sale - Kendrick

Mr. Trombley said this deals with surplus Department of Lands property in Kendrick. The property has been vacated and is no longer needed by the Department. The City of Kendrick originally deeded this property to the State for $1.00 to use as Forest Protection District headquarters. There were two deeds involved, one with a reversion clause and one without. The one without the reversion clause has an old abandoned building on it which is appraised at $12,500. The City of Kendrick will get the one parcel by reason of reversion; the other they would like to acquire for city purposes but can only pay $2500. This is $10,000 less than the appraisal. The Code allows the State to transfer a negotiated sale to a tax-supported unit of government for fair and valuable consideration but the question is what fair and valuable consideration is. Mr. Trombley pointed out there should be other considerations such as the City of Kendrick welcomed the State while there, gifted the property, etc. The question is whether to offer the property at public auction for the appraised value or whether to try to negotiate a sale with the City starting with the $2500 offer and relating it to the $12,000 appraisal.

Mr. Leroy said it would be feasible to negotiate with them for a $2400 reduction in the appraised value and still follow the Code. Governor Evans said he feels this compromise is fair. Mr. Williams made a motion to offer the parcel to the City of Kendrick for $10,100.00 which is the appraised cost of the building only. Mr. Leroy seconded the motion. The motion passed unanimously.

Proposed Land Sales

1. Parcel No. 149-80. 442.50 acres in Jefferson County. A lone parcel of state land located approximately 4 miles southeast of Homer or 28 miles northwest of Idaho Falls. Proposed to be sold in two units for the total appraised price of $43,900.00.

2. Parcel No. 192-82. 160 acres in Bannock County. This is a lone parcel of state land located approximately 7 miles west of the village of Virginia and approximately 1/2 mile east of Hawkins Reservoir. Recommendation is that this parcel be sold as one unit for the appraised price of $23,800.00.

3. Parcel No. 193-82. 280 acres in Bannock County. This is a lone parcel of state land located approximately 4-1/2 miles south and west of the village of Virginia on the west side of Marsh Valley. Recommendation is that the parcel be sold as one unit for the appraised price of $34,100.00.

4. Parcel No. 194-82. 160 acres in Bear Lake County. Recommendation is that the parcel be sold in one unit at the appraised price of $37,200.00.

5. Parcel No. 212-82. 40 acres in Caribou County, located approximately 4 miles southwest of Soda Springs. Recommendation is for sale as one unit at the appraised price of $7,800.00.

6. Parcel No. 218-82. 163.29 acres in Oneida County, located approximately 4 miles northeast of Malad. Recommendation is that it be sold in one unit for the appraised price of $31,200.00.

7. Parcel No. 219-82. 160 acres in Oneida County. This is a lone parcel of State land located in the Arbon Valley 11 miles south of Pauline. Recommendation is tnat this parcel be sold as one unit for the appraised price of $50,800.00.

8. Parcel No. 220-82. 320 acres in Oneida County, located in Arbon Valley approximately 12 miles south of Pauline. Recommendation is that is be sold as one unit for the appraised price of $29,800.00.

9. Parcel No. 221-82. 80 acres in Power County, 10 miles south and 2 miles west of Rockland. Recommendation is that it be sold in one unit for the appraised price of $22,500.00.

10. Parcel No. 222-82. 80 acres of Power County, 1-1/2 miles southeast of Rockland. Recommended for sale as one unit at the appraised price of $10,800.00.

11. Parcel No. 223-82. 472.50 acres in Power County, 1 mile southeast of Rockland. Recommended to be sold in two units for the total appraised price of $107,500.00.

12. Parcel No. 224-82. 320 acres in Power County, approximately 2 miles southeast of Rockland. Recommended for sale as one unit at the appraised price of $96,000.00.

13. Parcel No. 225-82. 80 acres in Power County located 9 miles south of Rockland. Recommended for sale in one unit at the appraised price of $19,500.00.

14. Parcel No. 226-82. 480 acres in Power County, 11 miles southeast of Rockland. Recommended for sale in two units for the total appraised price of $138,500.00.

Since all Board members have had time to review these proposals before the meeting, Mr. Williams moved to approve Department recommendations for 1 through 14. Jerry Evans seconded. The motion passed unanimously.

Quitclaim Deed - Nick Bishop

Mr. Riddoch explained that the upland owners in this case have a strong claim of adverse use having farmed the accretion tract for many years. This quitclaim deed will relieve the costs and time delays involved in a quiet title action. These are the only people who have a legal claim. The State has no interest. Mr. Evans moved to approve the Department recommendation to grant the quitclaim deed. Mr. Williams seconded the motion which passed unanimously.

Land Exchange Proposals 1 and 2:

1. Thorn Creek No. 1 Exchange, Boise National Forest land in the Idaho City area, will fill the block of state ownership. Jerry Evans moved to approve this land exchange with Boise National Forest. Mr. Leroy seconded. The motion passed unanimously.

2. Smith Ridge Exchange. Mr. Leroy requested this be held for thirty days. Mr. Williams seconded. The motion passed unanimously.

Timber Sale Contract Modification - Idaho Veneer TSC #2187

Mr. Trombley said that at the time of sale, it was thought this timber could be logged on snow roads with deep snows in that vicinity. Those deep snows have not materialized. Therefore, Idaho Veneer is requesting this contract be modified deleting that portion of the contract only. The Department concurs. Mr. Evans moved to approve the Department recommendation. Mr. Williams seconded. The motion passed unanimously.

Timber Sale Principal Payment Deferments

Governor Evans said he thinks everyone has anticipated these in light of the industry having serious problems. Following are the principal payment deferment requests:

1. #2323 Calhoun Creek Poles, L.D. McFarland Co.
2. #2324 - Rainy Creek Poles, L.D. McFarland Co.
3. #2327 - Crazy-Little Pine, W-I Forest Products, Inc.
4. #2271 - Santa Divide, Pacific Crown Timber Products
5. #2326 - West Fork Big Bear Creek, Bennett Tree Farms, Inc.

Jerry Evans moved that payments be deferred as listed 1 through 5. Mr. Williams seconded. The motion passed unanimously.

Riverbed Lease and Dredge and Placer Mining Requests

Mr. Leroy asked for unanimous consent that these be delayed for thirty days. There being no objections, it was so ordered.

Mineral Lease Application 6384 - Clearwater National Forest

Tom Markland explained that the Forest Service has asked to have the State amend its standard lease agreement and waive the bond and liability insurance. Their liability insurance limits them to a tort and the court would only be able to subject them to what the law allows anyway, and they are self-bonded. Mr. Leroy said he has reviewed this request and has no problems with it. Mr. Williams moved to approve the Department recommendation, Alternative No. 1. Jerry Evans seconded. The motion passed unanimously.

Final Oil & Gas Rules

Mr. Trombley said that as the Board knows, the State is currently operating under emergency rules and there is some urgency associated with this subject. Mr. Riddoch told the Board that on the whole, there were favorable comments about the rules and about the auction. He explained the few changes that have been made are mostly minor. Mr. Leroy asked Mr. Riddoch if it then would be his opinion, for this record, that in considering final adoption of rules and regulations for oil and gas leasing, that they have been in every substantial particular reviewed, publicized, public hearings held, and those amendments made are fairly insignificant in matters of technicality that do not change the substance of what was offered to the public and received comment upon. Mr. Riddoch said yes, with just a couple of exceptions. A public hearing was not held during this last final rulemaking since it was not requested in spite of extensive publication, including international. He believes there has been more than ample opportunity for comment and discussion, and commented there has been excellent input which has been incorporated. Mr. Leroy moved the approval of the final rules and regulations for oil and gas. Mr. Williams seconded. The motion passed unanimously.

The meeting was adjourned.

STATE BOARD OF LAND COMMISSIONERS

John V. Evans, President
and Governor of the State of Idaho

COUNTERSIGNED:

Pete T. Cenarrusa
Secretary of State

OCT 13, 1981

Exhibit 3

Land Bd. Meeting Minutes

(June 25, 1986)

SPECIAL MEETING
STATE BOARD OF LAND COMMISSIONERS
June 25, 1986

A special meeting of the State Board of Land Commissioners was held Wednesday, June 25, 1986, at 7:00 p.m., in the conference room of the Hall of Mirrors. Governor John V. Evans presided. Those members present were:

Honorable John V. Evans, President, and Governor of the State of Idaho
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Jim Jones, Attorney General
Honorable Joe R. Williams, State Auditor
Honorable Jerry L. Evans, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

Governor Evans called to order a special meeting to discuss the proposal on cabin site lease rates owned by the State of Idaho on Payette and Priest Lakes. He said that after the department report, representatives for the cabin site owners on Priest Lake would testify first; Payette Lakes representatives second. Others wishing to speak would follow, and he would ask those individuals to limit their remarks to three minutes.

Director Hamilton said that Lance Nielsen of the department would review the subcommittee's proposal. Mr. Hamilton also commented that all the letters received from lessees have been forwarded to Board members. Also, some were just handed to him tonight; one from Representative Terry Sverdsten in support of fair market evaluation in rentals for cottage sites indicating that is a question the legislature may want to look at; a letter from the Idaho Education Association supporting fair rentals for cottage sites; also on a letter from the Idaho School Board Assocation and from the Idaho Association of School Administrators. These letters are to be entered into the record. The Governor, hearing no objections, so ordered.

Lance Nielson said that following the meeting last year, the department was directed to go out and gather more information on the following six items: 1) determination of market value; 2) determination of appropriate yield rates; 3) increase of the lease term; 4) inclusion of a rate shock provision to limit annual increases; 5) the sale of isolated lots; 6) phasing out premium rental.

Mr. Nielsen explained that in determining the market value, the department did a market study of comparable fee simple properties. They found from that study that an average lot on Payette Lake was worth approximately $156,000; a secondary lot was worth $18,000; and a primary lot at Priest Lake was worth $145,000. It was concluded from the study that the rental rates are definitely below full market rent and do need to be increased.

On the yield rates, the department found that a 5% real rate of return has been accepted from biblical times to the present as a reasonable rate of return. They found that higher value properties typically yield a lower yield rate than lower value properties.

They also found they needed to take the different sizes of lots into consideration. On Priest Lake a lot is approximately 150' in width; on Payette Lake, a primary lot is approximately 75' in width. An addition or subtraction of $5 per front foot either larger or smaller than that average was made. On Payette Lake, it would be a $10 addition or subtraction from the average. Because of restrictions of leasing, the department felt that a 2-1/2% yield rate would be fair for primary lots; and 5% for secondary lots.

The issue of the lease term would take legislative action.

A rate shock provision was taken into consideration on this recommendation.

The department feels the premium rental should be kept in effect; however, recommends continuing no premium rental whatsoever for love and affection assignment that occur within a family.

On the subject of the sale of lease lots, it is recommended that if there are lessees interested in purchasing their property, an exchange program could be initiated.

In summary, Mr. Nielsen said that on an average, the state is receiving a .67% yield rate on all of the cottage site leases which is an unrealistically low return, and that needs to be increased to a full market rent and it needs to be phased in over a period of years.

Representatives from the Priest Lake Lessee's Association were invited to give testimony.

Carroll Martell spoke first. Mr. Martell said that with him are Jack Philleo, President of the Association; and Kent Helmer, member of the board of directors. Mr. Martell stated that, historically, the association has supported establishing a continuing basis, or formula, to guide the analysis and periodic adjustment of annual rentals. The formula suggested at the 1985 meeting has now been set aside. Lessees only received copies of the report in the first week of June, leaving them with little time to prepare a response. He thinks that if the 500 government owned cottage site lots were in private ownership, no one knows what that value would be. Using the Valley County assessor's roles is totally illogical and illusory. The lessees are trapped in a situation where their rentals will now be increased more than 400%. They feel it is most pertinent that a recent purchase by the state of prime waterfront at Squaw Bay on Priest Lake establishes values which are approximately one-third the amount discussed in the report. This deserves a greatest consideration. Mr. Martell provided a copy of his complete testimony for the record.

Kent Helmer, Mayor of Post Falls, and member of the board of directors of the Priest Lake Lessee's Association, stated that the Board should not only be concerned with the lease rates, but what is best for Priest Lake as a whole. He questions the validity of the figures in the report. Real estate has not been selling at Priest Lake for the last several years. The front-foot value is not the only measurable value -- some lots are accessible only by water and only useable during summer months. Several weeks ago, the Land Board purchased 275 acres of beachfront property described as the best sandy beach at Priest Lake. The purchase price was $900,000. This sale should give an accurate value of the land. Broken down into lots, the value would be much less than the $150,000 figure given in the market study. He also feels there is a movement to change the character of Priest Lake from summer cottages to year-around residences. They are concerned with the pristine quality of the lake when that happens.

Jim Jones asked Mr. Helmer if he disagreed with the proposed rate of return at 2-1/2% on the land value.

Mr. Helmer said he had no problem with that figure.

Jack Philleo, President, Priest Lake Lessee's Association, said the rate of increase as proposed is not realistic -- it is a 333% increase, which is inappropriate. The method used to determine an average lot is erroneous as many variables were not considered. There are inconsistencies in the market study. He has computed that an average lot at the Squaw Bay property recently purchased by the state would be $45,000. The Priest Lake Lessee's Association recommends that there be no increase in the rentals.

Jim Jones asked Mr. Philleo if he had objections to the yield rate of 2-1/2%.

Mr. Philleo replied that doesn't seem unreasonable, if the value is reasonable.

Harvey Hoff and Monte McClure from the Pilgrim Cove Association came forward. Mr. Hoff commented that market rent is that market which can be obtained from a willing tenant with a willing landowner. Market value is that value that can be obtained from a willing buyer and a willing seller. They submit that some of the terms in the report are ambiguous and confusing. Mr. McClure said that since the 1970's, the rates on cottage sites have become unreasonable. He feels the state has reneged on promises made thirty or more years ago.

Jerry Evans commented that a number of people have suggested the market is not what it was a few years ago, but as he relates the results of the sales ratio study to the market value for assessment purposes, he has not seen a decrease but a fairly significant increase in Valley Co. Mr. Hoff said he was not aware of that, but he knows there are many more leases available today, and submits that leasehold value and assessed valuation are very hard to compare.

Charles Blanton, Payette Lakes Cabin Owners Association, said that although the report stated there was a market study done, there was no market study -- only a simple use of the Valley County assessment rolls. The report has many inept and inaccurate positions and has no value. The basic fact is that what the state is leasing is raw, undeveloped land, often with no access, water, sewer or docks, etc. He also feels the report confuses values of recreation property with commercial property. He expressed the opinion that the state should consider sale of the properties within certain guidelines.

Jim Jones asked Mr. Blanton if the state should offer lots for sale, would those that are isolated and not a part of a contiguous block, be a reasonable place to start? Mr. Blanton said he thought it would.

Mr. Hamilton asked Mr. Blanton his opinion on the proposal suggested in the report of a land exchange option. Mr. Blanton said that not accomplish anything. Mr. Hamilton said a device could be set up to deal with exchange -- other states have done it. Mr. Blanton said he would not want to deal with the state on that, he would prefer the state to put it up for bid. If the state wants more land, sell the cottage sites and buy it. Barter is not the only way to do business.

Mike McAllister was the first of the general lessees to speak, saying he didn't think it is necessary for another 25 lessees to get up and speak and just be repetitious.

Charles Hummell said his impression at the last meeting had been that there was going to be a very careful process to be taken by the Board and that the lease owners would be involved in that process. Instead, a report was presented within a month of this meeting with no conversation to his knowledge with any of the leaseholders. The state is proposing to set up the leases on the basis of commercial property and that is totally at variance with the highly restrictive language of the lease.

Adelaide McLeod said she thinks the main problem with the study was that you cannot use assessed values to talk about market. She thinks that is very important. The market is in a slump in McCall; the economy is bad. The lessees need some stability with a long-term plan that will not be upended each year -- a formula is needed.

Steve Hager stated that he thinks the study is off in an amount of great magnitude.

Jim Boyd remarked on the rate of return question. He pointed out an area of state land south of Indian Lakes golf course. He said the rate of return on that property is .04%. The rate of return on a Payette Class I lot at $949 a year is .61%. This tells him that maybe the State Land Board is picking on the cottage site leaseholders because they are a high visibility group. At first he thought the 2.5% rate of return sounded low, but is not so sure now.

Dwayne Bills said he is concerned with the three musical-chair positions on the Board, and how many times the leaseholders have to come before the Board depending upon the political make-up of the State Land Board. He would request that the Board would take some form of affirmative action that would be reasonably consistent and render a policy that could be lived with for a few years. Also, if the lots are sold, the leaseholder should have first right of refusal to be able to buy that property at the highest bid price. He also thinks the two different yield rates of 2.5% and 5% are discrimination; there should only be one return rate.

Wayne Peterson said he has a lease lot and also a deeded lot. He has been trying to sell the deeded lot for two years, but cannot sell it. It has a 52' front and is listed at $85,000. He feels the county's assessed valuations are not correct.

Jack Flaherty commented there have been two sales in the past year at Pilgrim Cove. Property that had originally been listed at $29,000 sold at $16,000 with the assessed value of $10,160. That was lot 12, block 5, at Pilgrim Cove. Lot 16 was being sold at about the same time which was listed two years ago at $75,000, and it was sold a year later for $32,500; the assessed value was $23,925. The state will be hard pressed to find any purchasers under the current conditions.

Dr. (Bill) Forney, said he read with dismay the most recent proposed extortions for leaseholds at Payette Lake. The report reeks of ridiculous misinformation and misconceptions in order to reach an unrealistic goal of pricing lessees out of the improvements and investments they have been making in improving raw lands for the State of Idaho. Currently a lease is a severe liability and he sees no possible resale of a lease. He thinks the lease rates should be frozen where they are; they are already too high. The Board should explore the sale of lots where desired.

Gene Heil commented that the state had not worked with lessees as they had been directed to last year. The report came to them as a surprise and he thinks it unfair that they had no input.

Jim Kimball stated that if the rates are raised substantially, it will force a change in the type of use of the lake from vacation to either commercial or high use by more people from out of state. He asks that protection of the environment be considered. The report was more of an attitude rather than an analysis. He thinks selling the property would be a good investment; trading should be considered.

Jim Jones asked Mr. Kimball if in the interim between now and selling if he thought the proposed rate of $1,080 would be reasonable. Mr. Kimball said he thought it would.

Doc Caldwell said he would keep his remarks short, but he does think this matter needs to be straightened out as coming before the Board every year has hurt the leasing situation for the state, and has hurt the lessees. He also mentioned he is not comfortable with going with a 5% yield rate on Class II property and 2.5% on Class I property.

Jeff Farrady stressed consideration of what it is the state is actually leasing; what is it that it has to sell. That is bare land. What is the state giving to the lessee? The lease is only for ten years, but the annual rent is subject to change every year. Other restrictions are no subleasing, no assignments without approval, landscaping restrictions, etc.

That concluded the lessee's comments. Governor Evans asked Director Hamilton why the lessees had not been involved in the study program as had been envisioned a year ago. Mr. Hamilton said it was his impression that department staff was working with lessees, not as a group, but on an individual basis. It is true the work of the subcommittee was not concluded, nor the report prepared, until just a short time ago, so there was no opportunity to put it out for public review. They worked with the testimony from last year's meeting, and the department felt it had the necessary information.

Governor Evans said that they have heard the lessees emphasizing that the estimate of values are substantially higher than what they really are, and asked Mr. Hamilton to comment on that. Mr. Hamilton said the question of value has never had an easy answer, and there is no way to do it and satisfy everybody. The department approached this from the standpoint that lease lots have a value. Without having to go to a full appraisal at this point, the department looked at the assessor's values. The assessor's values at Payette Lake are questionable, and are in court, however, the assessor's approach in determining value is probably as reasonable an approach as exists in the public sector. The real issue is trying to come up with a fair rental. The department was trying to come up with pricing mechanism -- something to tie to, to give some measure of consistency in the future. A percentage of the assessed valuation is a reasonable way to go, and the question is, what is the percentage and what is a fair rental. Lots do sell in these areas, and they do sell at high values. Department staff live in those areas and they do know what is occurring in the market. Assessed value is a reasonable way to arrive at consistency.

Governor Evans asked if this matter had to be settled tonight. Mr. Hamilton replied that what has to be settled for the coming year is if there is to be a rental increase and what that would be. That information has to be settled by June 30. The Board options tonight would be; no increase or to set an increase for next year or to adopt a longer range policy.

After a five-minute recess, Governor Evans invited Attorney General Jones to make his recommendation.

Attorney General Jones stated that his motion is as follows: That the Board within the next two years market at public auction or exchange at fair market value between five and ten percent of the lots that the department has both at Payette Lake and at Priest Lake giving preference to those people who do hold isolated lot leases; that the marketing program begin forthwith; that we use the sale prices established by those auction sales and other sales in the area to determine market value; that we utilize that market value on a two-year rolling average with the initial two years' experience to set the market value of lots and that we charge 2-1/2 percent of market value as the rental for property commencing two years from now --that would be in 1989; that during the interim -- that is, 1987 and 1988, we use the charges as proposed for 1987 -- that is, $1,080 for Class I at Priest Lake; $1,261 at Payette Lake for a Class I lot; and $530 at Payette Lake for a Class II. Those values would be charged for this coming year -- 1987 and 1988. Starting in 1989, we would start using the two-year rolling average with the 2-1/2 percent of market value return.

The motion was seconded by Jerry Evans with the comment that they have heard from witness after witness that the state must establish some kind of market value, and the only way to get that is by placing the property on the market. That will give the needed information in order to continue to market those properties, and as witness after witness sugested the state get out of the business, this would set it clearly in that direction.

Governor Evans asked for a division of the question as he agreed with the sale of 5-10% of the lots to establish a market value of the lots involved; and to utilize an appraisal system to establish that value. However, he does not agree with the portion of the motion indicating the 2-1/2% to be used against the market value, and he also doesn't agree with raising the rates to the level on the schedule at the 1987 level.

Because of objections to the Governor's request for a division of the question, Governor Evans made an alternate motion as follows: That the Board propose to the department the sale of 5-10% of the lots on both Payette Lake and Priest Lake to determine market value that could be used to establish the appropriate rental level for those properties; that the Board establish the rate for 1987 and 1988 at a rate using the 1986 rate and adding to it the cost price indices used generally at the national level.

Joe Williams seconded the alternate motion.

The motion lost 2-3; Governor Evans and Joe Williams in favor; Jim Jones, Jerry Evans and Pete Cenarrusa opposed.

After discussion on the first right of refusal issue which would take legislative action, and with approval of the seconder of the original motion, Jim Jones amended his motion by adding to that motion the condition that the Board attempt to obtain legislation and that it recommend to the legislature legislation which would allow lessees to meet the highest bid and to obtain then the property.

Jerry Evans, as the seconder of the motion, agreed to the amendment.

The motion, with the amendment, passed 3-2; Governor Evans and Joe Williams opposed.

There being no further business brought before the Board, the special meeting of June 25, 1986, was adjourned.

STATE BOARD OF LAND COMMISSIONERS

By _____, President
and Governor of the State of Idaho

COUNTERSIGNED:

_____
Secretary of State

_____
Director

Exhibit 4

Land Bd. Meeting Minutes

(May 17, 1988)

issues, and that proposal pertains to an agreement only between KEA and Hagadone Hospitality.

Jerry Evans commented that although he will support this resolution, he thinks it is much to do about very little.

Governor Andrus asked that it be made very clear in the minutes of this meeting that he is opposed to Exhibit #3. Jerry Evans asked that it also be made clear that the Land Board has made no commitment, agreement or obligation in any way on the development of a marina. Governor Andrus stated that the only actions the Board is involved with relate to a floating green and the fill property.

Jerry Evans said that he thinks some of the language in Exhibit #1, "each impacted and interested party will be given adequate notice of all proceedings," would be difficult to carry out and thinks there should be some language in there that states "reasonable notice" shall be given.

Joe Williams moved the approval of the settlement between KEA and Hagadone Hospitality and the increase in the dollar value, but not in any of the appendages and authorizing staff to enter into a stipulation to see that the lawsuit is dismissed with prejudice. This is no way is to be interpreted as obligating the Board or the department to any plans beyond what they have specifically approved in the past. Jim Jones seconded the motion. Governor Andrus again pointed out that Exhibit #3 does not pertain to the State Land Board in any way. The motion passed unanimously.

There being no further business brought before the Board, the meeting was adjourned.

STATE BOARD OF LAND COMMISSIONERS

By Cecil D. Andrus, President
and Governor of the State of Idaho

COUNTERSIGNED:

Secretary of State

Stanley F. Hamilton
Director

* * * * * * * * * * * *

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
MAY 17, 1988

The regular meeting of the State Board of Land Commissioners was held Tuesday, May 17, 1988, at 9:00 a.m. in Room 420 of the Statehouse. Governor Cecil D. Andrus presided. Those members present were:

Honorable Cecil D. Andrus, President, and Governor of the State of Idaho
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Joe R. Williams, State Auditor
Honorable Jerry L. Evans, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

Absent:

Honorable Jim Jones, Attorney General

Consent Agenda

A. Official Transaction Reports:

1. March 1988 2. April 1988

B. Supplemental Agreement Requests -- Land Sale Certificates:

1. Michael T. Ricks
2. Velma and Blair Calaway
3. Roger Seaton
4. Gregory H. Wood
5. Eastern Idaho Production Credit Association (Henry Rigby)
6. Nedrow Farms (9)

C. Proposed Sale of Surplus Property - Idaho Department of Transportation:

1. 0.17 Residential Acre - City of Twin Falls
2. Moscow Mountain Rest Area - Latah County
3. 2.15 acres - Bonner County

D. Surplus Property - Idaho Military Division - Transfer of Jurisdiction to North Idaho College

E. Surplus Property - Idaho Department of Transportation - Return of Jurisdiction

F. Easement Requests:

1. Corps of Engineers - Channel Improvement, Salmon River
2. City of Hagerman - Sewer outfall line
3. General Telephone - Cable Crossing - Bonner County
4. Klaus Groenke - Pump and water intake line - Lake Pend Oreille
5. U.S. Spring Communications Co. - Fiber optic cable - Bonner County

G. Proposed Timber Sales:

1. Lucky Lion
2. Mid Trapper
3. Pleasant Valley
4. South Blackrock Bridge OSR
5. Glover Creek
6. Finn Saddle
7. Cedar Creek OSR
8. Township Butte
9. Shattuck-Cameron Pole
10. Bishop Creek OSR
11. Lost Valley
12. Fall Creek

H. Hearing Officer Report - International Orofino Placers, Inc.

Mr. Hamilton reported a correction to Item B-6, LSC #25419-A, the amounts were to be changed from "no principal" and "1,461.80" to "$17,130" and $20,575."

Jerry Evans questioned Item D, transfer of jurisdiction of the old Coeur d'Alene National Guard Armory to North Idaho College. He recalled that this has been before the Land Board on previous occasions andat one time it had been offered for sale to the Coeur d'Alene School District for $133,000. At that point, the issue was transferring the actual value. Then a further move was made to allow it to be leased or rented for additional revenue, and now are considering transferring the property to North Idaho College for no consideration. Mr. Evans asked why this is so.

Jay Biladeau said that the National Guard had asked that the property simply be transferred to North Idaho College for no consideration.

Jerry Evans explained that the reason the property had not been put to good use by the Coeur d'Alene School District was that they could not come up with the $133,000. If it is to be made available for no consideration, then it should be proper to re-advertise to see what the most appropriate use would be for that facility.

Jay Biladeau indicated that it had not been advertised but had been offered to the other state agencies with no consideration, however, the school districts had not been included.

Jerry Evans asked that this matter be held and that the property at least be made available to the other agencies on the same basis. Governor Andrus, hearing no objections, so ordered.

Jerry Evans questioned Item F-1 which had been held back before until the easement rules on submerged lands were adopted. He asked if those rules have been adopted and whether they provide for the payment of $4,200. Jay Biladeau answered that the rules have not been adopted, and in looking at this, it appears the fee should be $250 until those rules are adopted. Mr. Evans requested this item be held. Governor Andrus, hearing no objections, so ordered that this item be held until the next regular meeting of the State Land Board.

Governor Andrus asked when the reclamation will take place on Item H, International Orofino Placers, Inc. hearing officer report and who will do the reclamation. Mr. Hamilton explained that the reclamation will take place as soon as the certificate of deposit is obtained and when the timing is appropriate for the revegetation process. The bid process will determine who will do the reclamation. Governor Andrus asked that the staff keep the board members advised and provide an update at the next regular meeting.

Jerry Evans moved to adopt the consent agenda items as amended and with the exception of Items D and F-1. Joe Williams seconded. The motion passed unanimously.

Rental Rates for Cottage Site Leases

Lance Nielsen explained that this proposal is largely an extension of previous board actions to sell 5-10% of the cottage site lots at Priest and Payette Lakes in order to establish value on which to calculate rental rates. This proposal has the same phase-in schedule and limits annual increases to no more than 25%. It sets base rents for both primary and secondary lots and uses a methodology for modifying rental rates to keep them in line with changing land values. The only new issue is the lot valuations and the corresponding 2-1/2% rental rate and the lot rents for secondary lots. Notices were sent to the officers of the lessee associations but not to each individual lessee. Attachment #3 to the recommendation outlines the procedure the department proposes following to address lot valuation concerns raised by lessees.

After the lot values are adopted, the department intends to notify the individuals lessees about their assigned lot values and rental rates.

Governor Andrus advised the audience that the board will recognize officers from the associations and Dr. Forney who had made previous arrangements to speak, but that there would not be enough time to let every person in the room speak.

Monty McClure, President of the Pilgrim Cove Homeowners Association at McCall, said that he is not arguing with the valuation of the second-tier lots but argues that the department staff has raised the minimum lease rate approximately 5% or double the actions the board took in 1986. He believes the board should abide by the 2-1/2% yield rate.

William Forney addressed the board saying that this is another crisis board meeting continuing the same regressive, exorbitant lease rates. He stated that whatever formula is used, the bottom line is that these rates are already too high. They are not comparable with values to those of deeded property and they carry many restrictions. He also pointed out that Attachment #3 needs to be addressed, specifically, in Paragraph 2 which says, "Lessee comments and concerns regarding lot values shall only be accepted from individuals presenting substantial evidence refuting the state assigned value" and "Additional appraisals will not be considered"; "Lessee comments shall be directed to their respective area offices for resolutions"; and in Paragraph 5, "Valuation concerns will be resolved by the department. Only in the most unusual of circumstances will valuation questions be forwarded to the board for review." Mr. Forney believes the Board should retain its responsibility to the lessees and serve as a board of appeals. He feels the only solution will be when the lessee can buy his property. Realizing that that decision isn't going to be considered, he asked the board to hold the line on these high lease rates for at least twelve years.

John Flaherty, Secretary-Treasurer of the Pilgrim Cove Lessee Association, said that he thinks it is very important to stablize the lease rate not only for the lessee's sake but also for when he needs to sell the property. Now that a rate has been established, a way is needed to maintain that. Mr. Flaherty believes one way to do that is to occasionally sell some of the lots. He also suggested a committee of the lessees be formed to work closer with department staff in advance of board meetings.

Jerry Evans made the following suggestions for amending Attachment #3: 1) Under Item #2 where it says "additional appraisals will not be considered" -- delete that from the procedure and allow any substantial information to be considered in making those adjustments.

Hearing no objection, Governor Andrus so ordered.

The second amendment suggested by Mr. Evans was to change Item #5 to read: "Every attempt to resolve valuation concerns will be made by the department. Those which they cannot, may be forwarded to the board for review." This allows the board to serve as that final board of appeals and does not leave it totally within the judgment and discretion of the department, yet the primary responsibility remains with the department to resolve those matters.

Hearing no objection, Governor Andrus so ordered.

Joe Williams moved to approve the department recommendation with those amendments. Jerry Evans seconded the motion. The motion passed unanimously.

Proposed Rules for Grazing and Cropland Leases - Final Adoption

Mr. Hamilton explained that these proposed rules have gone through the Administrative Procedures Act review process. Extensive discussions have been held with the Cattlemen and Wool Growers associations on these rules.

Don Hobbs briefed the board on some of the changes made during the process. He said this is a culmination of nearly two years of work and many meetings with members of the industry. Changes that have been made are explained in the attachment to the board memo. These changes were made due to comments received and most were to clarify the rules further. Recommended changes to nineteen rules were not included, and comments and reasons are addressed in a board memo attachment. In addition, due to further discussion with industry representatives, it is recommended that in Rule 28, in the last sentence, that "jointly" be changed to "equally." Department staff recommends adoption of the rules.

Stan Boyd, Idaho Wool Growers Association, addressed the board. Mr. Boyd said that he was accompanied by representatives of the cattle association and the lamb and wool industry. He thanked the department for working out these regulations with the industry, and the industry is satisfied with the result as a whole. He pointed out some minor points of concern. The first matter was addressed by Mr. Gary Glenn of te Idaho Cattle Association. On Rule 6.b., they recommend that the last three words "prohibiting such action" be stricken. Mr. Boyd then recommended on Page 21, the last page, the attachment concerning fee structure, that the minimum rental fee be adjusted since $50 is a 100% increase from the current fee. They recommend the current fee be retained. Mr. Maurice Guerry added his comments regarding the rules but voiced no objections.

Department staff commented on those recommendations from the industry. Mr. Hobbs said the recommendation on Rule 6b would not significantly affect the program. Governor Andrus recommended that those words be stricken and hearing no objections, so ordered.

Pete Cenarrusa recommended that the fee be raised 25% per year until it reaches the $50 mark. Hearing no objections, Governor Andrus so ordered.

Jerry Evans moved to approve the rules for final adoption, with those amendments mentioned above. Joe Williams seconded the motion which passed unanimously.

Land Exchange Between the BSU Foundation and Boise State University

Mr. Hamilton said this is a land exchange between the university and the BSU Foundation. Mr. Steve Schmidt, Director of Institutional Research at Boise State University, was available to answer questions. Governor Andrus recommended a language change from the "future college of technology" to "classroom facilities on the campus" until the Board of Education makes a determination whether it will or will not have a college of technology. There being no objections, Governor Andrus so ordered.

Joe Williams moved to approve the recommendation of the department. Jerry Evans seconded.

Mr. Cenarrusa voiced his concern that the legislature should have input into this issue.

Jerry Evans said he agrees with Mr. Cenarrusa on basic policy issues, but he believes responsibility has been given this board for land exchanges.

The motion passed 3-1, Mr. Cenarrusa opposed. (Jim Jones absent.)

Plantation Golf Course, Inc.--Extension of Memorandum of Agreement and Special Lease

Lance Nielsen reported that staff has met with the parties involved with this segment of the greenbelt project as directed by the board. They have looked at different alternatives and costs, along with impacts to residents, environmental impacts and public interest. The department today is seeking conceptual approval of the route which Mr. Nielsen explained using a map. This plan involves two bridges, jumping over to the south side of the river to avoid the eroded property and back.

Darcy Kull, Garden City Commissioner, addressed the Board. She said this plan was approved in concept at the Commissioners meeting held last night. They have heard no opposition to this. She recommended that the board put a time limit on the start of construction in order to have it finished by 1990.

Steve Bradbury, attorney with Eberle Berlin, representing the Firemens Fund Mortgage Company, the present owner of the property, stated the main problem is that the 1983 river course change that eroded the back yards of the homeowners in the Plantation development. Firemens Fund is willing to participate in the path as it is shown, however, the estimated cost of placing the path along the north shore as originally proposed is about $120,000. The estimated cost to follow the plan presented here has been estimated as high as $540,000. They are not willing to participate much beyond the $120,000.

Governor Andrus questioned whether the agreement had been tied into a dollar amount. Mr. Bradbury said that he did not think so, but he's not sure the successors to the developers have that obligation.

Jeff Casey, representing the Plantation homeowners, added his comments. They have approved the plan in concept and are willing to aid and assist with grants and possibly with financial contributions.

Mr. Hamilton stated that the department recommendation is that the Board approve this plan in concept only and that further negotiations between department staff and other interested parties will continue with an effort to come back in June. Joe Williams moved to approve the department recommendation. Jerry Evans seconded. The motion passed unanimously.

Proposed Amendments of Oil and Gas Leasing Rules

Mr. Hamilton said that this is a revision of a set of rules that has been in place for some time. It is the department recommendation to enter these into the rule making process.

Linda Ray reported that there are only two major changes. One is the rental rate which has been increased to $1.50 for the second through the tenth year. Additionally, they also will pay the first year's rental of $1.00 an acre. The other change is after the sale is over, tracts will be available on an over-the-counter basis for a six-month period. The rest of the changes amount to language changes. Industry comments have been included.

Joe Williams moved approval of the recommendation. Jerry Evans seconded. The motion passed unanimously 3-0 (Mr. Cenarrusa absent at time of the voting).

Declaration of Zone of Infestation

Mr. Hamilton explained that this is a request that the Board declare a zone of infestation under I.C. §38-602 to deal with gypsy moth. They have been found in Sandpoint and Coeur d'Alene. The department has been doing some ground spraying with the permission of the property owners.

Jerry Evans moved to approve the department recommendation. Joe Williams seconded. The motion passed unanimously.

FY89 Timber Sale Plan

Winston Wiggins briefed the Board on the plan. Mr. Wiggins said that this is the first plan developed that reflects the increased annual allowable harvest of 200 million board feet of sawlogs and cedar poles. There are a variety of sales which range from less than a million feet up to over 15 million with the bulk of them in the two to three million foot range. There are seven cedar pole sales of about 23,700 cedar poles.

Joe Williams moved to approve the plan; Jerry Evans seconded. The motion passed unanimously.

FY-89 Road Development Plan

Mr. Hamilton reported that about two years ago the department was instructed by the Board to bring back a road development plan each year as a part of the timber sale plan.

Walt Clark briefed the Board on the plan. The plan calls for accessing and harvesting some unroaded timber and also for improving and maintaining some existing roads to FPA standards and to keep water quality as high as possible. The plan calls for about 86 miles of new roads; about 43 miles of reconstruction; 17 miles of surfacing for a total of $1.48 million. The 200 million board feet of timber will bring in $20 to $30 million.

Joe Williams moved to approve the road development plan. Pete Cenarrusa seconded. Passed unanimously.

Installment Payment Policy

Mr. Hamilton said this question had been raised at an earlier meeting. Lance Nielson briefed the Board on the department's policy and recommendation. Mr. Nielson reported that the department for a number of years has allowed rental extensions on its cropland leases. Those have been granted on a case-by-case basis on the showing of financial hardship by the lessee. As an extension of that policy on cropland leases, occasionally a lease extension has been granted to a cottage site lessee. Of the 600 cottage site leases, four have been requested and two have been approved. They are considered only in rare circumstances upon demonstration of financial hardship.

Jerry Evans said that under those limited provisions, he does not object to the policy, as long as the state collects a late payment fee plus interest. If the practice becomes routine, then the policy will need to be looked at again.

Governor Andrus asked whether any action is necessary from the Board today. Mr. Nielson said that the case held over from the February/March official transactions for Mr. Leland Stanford will need approval. Governor Andrus, hearing no objections, so ordered.

Proposed Closure of the Snake River Bed at Shoshone Falls

Fred Kisabeth reported that this is a rather unique request to close the Snake River bed at Shoshone Falls for the sake of public safety. The department was advised of the current safety situation by the manager of the Shoshone Falls power plant, Idaho Power Co. In determining how to handle this, the department feels the best way is by recognizing the Board's authority under I.C. §58-104, Subsection 9, to control use of lands in the beds of navigable rivers. Once a board order is in place, then local governments will be pursuing promulgation of a city or county ordinance to give them some legal basis for enforcement.

Jerry Evans moved to approve the department recommendation. Joe Williams seconded. The motion passed unanimously.

Supplemental Agreement - Floodwood Cooperative Road

Mr. Hamilton explained that there has been a problem with the Floodwood road. There's been a slump with access cut off for three state timber sales. The road is managed as a cooperative function with other landowners in the Floodwood. This one serves both state and Potlatch land. Based on tributary acres, the state's share of the cost will be $17,634.

Jerry Evans moved to approve the department recommendation. Pete Cenarrusa seconded. The motion passed unanimously.

Executive Session -- Appel v. Washington Water Power

Jerry Evans made the motion to go into executive session to discuss legal issues under Idaho Code §67-2345 (f). Motion was seconded and passed.

Pat Kole updated the Board on actions taken in this case and how it may affect the state.

After discussion, with no action necessary, the board went back into regular session.

Regular Session

There being no further business brought before the Board, the meeting of May 17, 1988 was adjourned.

STATE BOARD OF LAND COMMISSIONERS

By Cecil D. Andrus, President
and Governor of the State of Idaho

COUNTERSIGNED:

Pete T. Cenarrusa
Secretary of State

Stanley F. Hamilton
Director

* * * * * * * *

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
JUNE 14, 1988

The regular meeting of the State Board of Land Commissioners was held on Tuesday, June 14, 1988, at 9:00 a.m. in the conference room at the Hall of Mirrors. Governor Cecil D. Andrus presided. Those members present were:

Honorable Cecil D. Andrus, President, and Governor of the State of Idaho
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Jim Jones, Attorney General
Honorable Jerry L. Evans, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

Absent:

Honorable Joe R. Williams, State Auditor

Consent Agenda

A. Official Transaction Reports - May 1988

B. Easement Requests:

1. General Telephone of the N.W. - Underwater Cable, Kootenai County
2. G. R. Johnson - Bulkhead on Lower Twin Lake - Kootenai County
3. Panhandle Brewing Co. - Water Intake Line - Boundary County

C. Cropland Rental Rates

D. Proposed Timber Sales:

1. California Gulch
2. Flannigan Creek
3. Grouse Creek Rerun
   a. Cost-Share Road Agreement, Murray Creek Road
4. North Trapper

E. Supplemental Agreement - Floodwood Cooperative Road

Jerry Evans moved to approve the consent agenda items. Pete Cenarrusa seconded. The motion passed unanimously.

Reconveyance of Lands at School for Deaf & Blind from State Building to Department of Education

Ann Barker, Department of Administration, represented the Idaho State Building Authority, who has initiated a request to reconvey land to the state. When this project was begun, as a matter of convenience, the entire parcel associated with the school, approximately 40 acres, was conveyed to the Building Authority. The project, which consisted of about 18 acres, is now completed. They are conveying back to the state approximately 22 acres consisting of the old gymnasium, the old boys' dorm, the old administration building, and the superintendent's house. These were clearly not involved in the building of the new school and the Building Authority has no need of these parcels.

Jim Jones moved to approve the reconveyance request. Jerry Evans seconded. The motion passed unanimously.

300.
5/17-6/14/88

Exhibit 5

Land Bd. Meeting Minutes

(July 10, 1990)

Governor Andrus inquired if the Attorney General's office is satisfied with the document. Clive Strong, Deputy Attorney General, stated that the Attorney General's office drafted this resolution at the request of the department. Mr. Strong explained that it is a very complicated transaction, and to the best of their ability, they have gone back through the record and brought together the relevant information. He said the reason this approach is recommended is a result of the Public Trust Doctrine. In the Kootenai Environmental Alliance case, the Idaho Supreme Court indicated that the alienation of public trust lands required special consideration. The purpose of the resolution is to indicate that the board has taken into consideration those factors that are set forth in the Kootenai Environmental Alliance case so that the alienation of this property is consistent with the public trust elements or standards. To the extent that they have been able to review the record, the Attorney General's office feels this accomplishes that objective.

Mr. Strong stated that he would like to bring the board's attention to some points in the resolution. First, a provision has been inserted that the lands revert back to the state if certain conditions are not satisfied. In addition, inclusions have been put in indicating that this resolution is only the alienation of the lands, and that there is a requirement for compliance with other state laws and procedures.

Jerry Evans moved to approve the resolution and quitclaim deed form; furthermore, that the quitclaim deed be issued to Hagadone Hospitality Co. upon the receipt of the $130,000 remuneration. J. D. Williams seconded.

Governor Andrus asked what conditions have not yet been complied with. Mr. Kisabeth said other than the $130,000 payment, there is the water quality monitoring associated with the floating green, but it is understood that negotiations are proceeding and no problems are expected with that. They have complied with removal of the log booming structures and they have reconstructed the seawall and taken care of potential pollutants due to the mill waste, etc. They have satisfied the requirement for making Sanders Beach available to the public; a fence was constructed to isolate their upland from the beach area. Governor Andrus said that the Sanders Beach requirement is the one that he was concerned with and asked that the department be certain.

Jerry Evans stated this his motion was made with the understanding that those conditions be satisfied.

The motion passed unanimously.

Land Sale Plan--Fiscal Year 1991

Jay Biladeau stated that at the beginning of Fiscal Year 1990, twenty-five parcels remained on the department's cumulative sales plan. These are tracts from previously authorized sales including two parcels approved on last year's plan. Seven of those twenty-five parcels were offered for sale during the past year. Four sold at the appraised value. Three did not sell. In most cases, market conditions still do not favor land sales. The department is recommending for FY-91 only two parcels, each having been a part of a larger tract of state ownership. The larger portion was exchanged to the BLM. The two parcels are both in Jefferson County, one is 160 acres and the other 80 acres. As each parcel is appraised, they will be brought back to the board for final approval.

Jerry Evans moved to approve the department recommendation for the FY-91 land sale plan. J. D. Williams seconded. The motion passed unanimously.

Cottage Sites--SB 1516--Outline of Proposal to Ensure Market Rents

Mr. Hamilton said that the board had asked the department to bring this matter back to the July meeting with a proposal for how the department could assure compliance with SB 1516.

Governor Andrus recognized some interested citizens in the audience and invited them to feel free to make comments if they wish.

Don Hobbs presented the proposal to the board. Mr. Hobbs outlined the recommended five-part plan:

1. Appraisals be contracted to determine land values and market rent for a few sites at Priest and Payette lakes.

2. The department would use the information to determine rental values for the remaining sites.

3. The department would bring to the board by May 1991 the results and recommendations for any changes to the current system.

4. The department would compile information and report on lease transfer activity.

5. The department would then prepare recommended changes to the rules covering cottage sites and these changes would include continuing the equity premium policy and increasing the percentage to the state.

Mr. Hamilton commented that the process for determining the market rent is a difficult process, but the recommendation is to ask a fee appraiser to help establish what market rental should be.

Governor Andrus asked whether SB 1516 was introduced by the Department of Lands or by private parties. Mr. Hamilton said the legislation was put together by both the department and the lessees.

Jerry Evans commented that he was disappointed that more attention was not given to the Valley County assessor's sales ratio study. He also believes that this legislation means that the phase-in schedule must be abandoned because the law is in effect now and it says market rent throughout the duration of the lease.

J. D. Williams moved to approve the recommendation. Jerry Evans seconded. The motion passed unanimously. (Pete Cenarrusa and Jim Jones absent.)

Governor Andrus requested that the two absent board members be notified in writing of this board action.

Mineral Report -- Democrat Gulch Ranch

Mr. Hamilton explained that this issue had been on the agenda in June and the Board deferred action on it to allow the staff to take an additional look at what the mineral value there might be.

Mr. Kisabeth reported that the department mineral staff did further research with most of the information being obtained from the Idaho Bureau of Mines and Geology Pamphlet No. 90. Attachment No. 1 to the board memorandum illustrates the Hailey-Bellevue mineral belt which is 72 square miles in area -- eight miles wide and nine miles long. The subject property lies in the center. The veins and lodes are widely distributed along the mineral belt but show a closer spacing on the slope southwest of the Big Wood River. The subject property is north of Croy Creek where deposits are more widely spaced. These lands have not been very productive. Department staff feels that there are probably some minerals in that state parcel, but because of lack of interest over the years, that there is little, if any, economic mineral potential. Mr. Kisabeth also reported that Exxon had the only lease of record there for exploratory purposes, and when they got the results, cancelled the lease. There is an existing geothermal lease on the property and that is the area that department staff feels has the most potential for development. Mr. Kisabeth said that with this

information, the department stands by its previous recommendation that the area be withdrawn from mineral entry with the payment of consideration of $14,640 in return. Geothermal and hydrocarbon rights would be maintained by the state.

Jerry Evans moved to approve the department's recommendation for the mineral withdrawal with the conditions listed in the memorandum: 1) an application fee for requesting withdrawal in the mount of $50 be remitted; 2) a consideration of $14,640 be paid by Dever Barker for the withdrawal from mineral entry; 3) the cost of advertising the mineral entry withdrawal be paid by Dever Barker. J. D. Williams seconded the motion which passed unanimously.

Abandoned Docks at Payette Lake – Authority

Mr. Hamilton reported that this item comes before the board in response to a letter from the sheriff in Valley County expressing concerns with dealing with abandoned docks on the lake. The county has been dealing with those docks which have been cut or broken loose during storms by hauling them off and disposing of them. Because the department administers the Lake Protection Act and requires permits for those kinds of structures, they are asking whether there is any assistance available to help them with that problem. They ask also if we could use some kind of a licensing process to identify the owners of the docks. The state does not have funds to deal with this problem without going to the legislature to either fund the state to help the counties or to assist the counties directly.

Governor Andrus stated he sees no reason for the state to take on the liability and the expense of cleaning up after those people who permit debris to float throughout the lake. Jerry Evans suggested perhaps a fee system needs to be examined with some of those fees transferring back to the counties. Governor Andrus added that he thought the counties could set up a fee system themselves and leave the state out of it.

J. D. Williams thinks a follow-up letter should go to the sheriff indicating that there are no state funds available and not knowing whether it is a proper state role, encourage them to look at any regulatory authority they would have such as zoning or fees to assist them. Hearing no objections, Governor Andrus so ordered.

Director's Salary

Governor Andrus stated that it is his opinion that the director is a state employee and should receive the same amount of increase percentagewise as other state employees. He has no objection.

J. D. Williams moved to approve the 5% raise for the director. Jerry Evans seconded. The motion passed unanimously.

Ron Duby, President, Priest Lake Lessee's Association

Mr. Duby, a member of the audience, asked permission to address the board. He asked if it would be possible to get a copy of the cottage site proposal. Governor Andrus assured him he would get a copy.

Information Items

Governor Andrus suggested that the board members familiarize themselves with the information items and noted that the timber sale report shows the state is doing well.

Mr. Hamilton advised that the gypsy moth spraying project in Coeur d'Alene and Sandpoint has been completed and the trapping will begin in August.

Mr. Hamilton pointed out the 60-day notice for violations of the Clean Water Act is Scott Reed's notice regarding the I-90 slides that have occurred in the Coeur d'Alene area.

Mr. Hamilton reported on the summary of land sale contract supplemental agreements and/or extensions, stating that 23 of them have reached the maximum number of five allowed.

Fire Season

Mr. Hamilton reported that the state is having an excellent fire season so far, but the department would like authorization to use deficiency warrants to pay excess fire expenses. The board expressed agreement and authorized Mr. Hamilton to send around a resolution for the board members' signatures.

Manchester Development at McCall

Mr. Hamilton pointed out a pictorial news story from the Star News on the proposed development. Governor Andrus stated his position is that no additional permits be given until it is known what they will do about the sewer system.

There being no further business brought before the board, the meeting was adjourned.

STATE BOARD OF LAND COMMISSIONERS

Cecil D. Andrus

President, and Governor of the State of Idaho

Countersigned:

Secretary of State

Stanley F. Hamilton

Director, and Secretary to the Board

Exhibit 6

Land Bd. Meeting Minutes

(June 11, 1991)

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
June 11, 1991

The regular meeting of the State Board of Land Commissioners was held Tuesday, June 11, 1991, at 9:00 a.m. in the conference room in the Joe R. Williams office building. Governor Cecil D. Andrus presided. Those members present were:

Honorable Cecil D. Andrus, President, and Governor of the State of Idaho
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Larry EchoHawk, Attorney General
Honorable J. D. Williams, State Auditor
Honorable Jerry Evans, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

Consent Agenda

A. Official Transactions -- April 1991

B. Proposed Timber Sales:

1. Brockman
2. Caldwell Creek Pole
3. Last Stand
4. Lava
5. Pick and Pan Creek Pulp
6. Rough House

C. Qualified Bidders List:

1. Clearwater Management Co., Inc.
2. Kenneth Walters dba Shorts Bar Logging
3. Helmich Log Products

D. Easement Requests:

1. USGS Streamflow Gauging Station--Snake River, Elmore County
2. Steve Clapier -- Pump and Waterline into Snake River, Owyhee County

E. Cropland Lease Rates

Pete Cenarrusa moved to approve the consent agenda. Jerry Evans seconded. The motion passed unanimously.

Regular Agenda

Cottage Site Rental Policy

Governor Andrus noted that this had come before the Land Board two meetings ago when he appointed a subcommittee, chaired by Superintendent Evans, with membership of State Auditor Williams and Attorney General EchoHawk.

Chairman Jerry Evans reported that the subcommittee met on three occasions and were joined by Mr. Cenarrusa at those meetings. At the first meeting they listened to the concerns of the lessees through the leadership of the associations. The second meeting was devoted to an examination of the basis upon which the appraisals were made. At the third meeting they tried to bring this all together and asked the department for a recommendation. Representatives from the associations participated in each meeting.

Mr. Evans observed that the subcommittee recommendation basically continues the existing Land Board cottage site rental policy for another fiscal year, indexes the lot values using the implicit price inflator, and maintains the minimums as they currently exist. It does provide for some increases in those specific cases where with that inflator built in, the lease rate is still less than 2-1/2%. It also suggests that this subcommittee of the board be continued for one additional year. The recommendation was adopted by a vote of 2-1. Mr. Evans commented that his was the dissenting vote.

Governor Andrus opened the subject for discussion.

J. D. Williams said that in reviewing this, a major consideration was the fact that in 1987 the Land Board did a similar review of the estimated lot appraisals and presented to the lot owners a ten-year schedule. As a result of that, he believes it is incumbent upon the board to work for another year with the lot owners to try to come up with new values and to review the impact of what the state does at these two lakes. He thinks it should be clarified that the third appraisal would be sought and it probably would be best if that appraiser was selected by department staff in conjunction with the lot owners since there is some conflict between the two appraisers now. Also, he thinks it is understood that the department will pay for that. The main concept of this recommendation is that the program created in 1987 is intact for another year and those lots that reach the target rent, as estimated in 1987, would be updated and indexed to 1991 and then there would be a 2-1/2% return to the endowment. That would be continued for another year to allow further negotiations with the lot owners.

Jerry Evans pointed out that there really were not two appraisals. There was the appraisal the department had done and paid for which was supplemented by some additional appraisal work. The other appraisal was not a full-blown appraisal, but was basically a criticism of the appraisal that had been done. Mr. Evans said that this is a very difficult issue to deal with, it is very emotional, and it is easy to understand that people who have had the use of these sites for a long time of family history get very attached to them. A year ago, realizing this was a very delicate matter, the board decided it needed some professional advice as to a good idea of what the value of these properties are and then come to a conclusion as to what a reasonable rate of return should be. The board then asked the appraiser to give them an idea as to the value of these properties and an idea of a reasonable rate of return to expect from that value. That was done and those numbers came out very high. The appraiser also suggested a reasonable rate of return would be in the neighborhood of 8%. The association people said that might be a reasonable rate of return if this were fee simple property, but it is not. The appraiser then said a more reasonable rate of return would be between 4-1/2% and 5-1/2%. Mr. Evans feels that the subcommittee recommendation chooses to ignore this professional advice and to continue the study for another year.

Mr. Hamilton asked for clarification about the recommendation regarding the second appraiser's recommendation that the lot values would be binding upon all parties. He also asked what the board wants included in the appraisal.

It was established that the new appraisal should take lot values only into consideration.

Governor Andrus invited comments from anyone in the audience who feels strongly about speaking to this issue.

Charles Hummel, 305 Mobley Drive, Boise, President of the Payette Lake Cabin Owners Association, handed out his prepared written material and commented that in regard to the prior discussion, that an appraisal is an opinion and not a scientific fact. The appraisal contracted by the department was discussed by some very competent people who they believe demonstrated the deficiencies of the contracted appraisal and the two recommendations regarding rate of return.

Mr. Hummel advised that a resolution from the two Payette Lake associations was unanimously adopted by 170 members present on June 4, the day after the subcommittee meeting. The six points addressed in the resolution are: 1) That the current program is regarded by the associations as a good faith commitment and will continue to be relied upon by the lessees; 2) That they agree that as the constitution requires, maximum long-term return is the mandate of the board; 3) That it is imperative that the lessees and the state have a stable, predictable rental program which doesn't undermine their commitment; 4) That any rental program should recognize the difference between deeded property values and the value of leases; 5) That the rental program should incorporate a rental adjustment index which protects the rights of both the state and the lessees; and 6) The lessees appreciate the reaffirmation of the 1988 rental program by the subcommittee. They welcome the opportunity to work with the board during the next twelve months to clarify the 1988 program.

Mr. Hummel added that the lessees feel there should be an exception to the recommendation in that it is not practical to agree to a binding agreement with respect to the new appraisal which the department will contract for. They also suggest that the department's notice to the lessees be drafted in the most readable and unambiguous manner possible, and it would be desirable if the actual rent for 1992 be shown for each lease rather than providing a formula for the computation to be made by the lessee.

Candace Anderson, President, Pilgrim Cove Association, McCall, commented that they would like to see the subcommittee process continue. Some issues they woul like to see addressed this next year would be the lessee ownership of cottage sites through a specified trade procedure or the opportunity to buy. Ms. Anderson handed out her written comments to the board members and stated that they would also like reconsideration of the lease conditions, including subleasing. They would like improvements and maintenance of cottage site lease land by the Department of Lands and provisions for safety and well-being of residents. They would like discussions to continue on leasehold value using it as an indicator of market rent.

Kent Helmer, Post Falls, President-Elect of the Priest Lake Lessees Association, addressed the board, and commented that they are ready and willing to work with the department and subcommittee to bring to a conclusion this continuing problem. The main problem at their lake is in regard to the sewers. The last appraisal increased the appraisals for those with sewers -- in effect penalizing those who are trying to clean up the environment.

J. D. Williams made a motion to approve the recommendation of the subcommittee with the additional understanding regarding how the arrangements would be made for the appraisal in Paragraph 3 of the recommendation and payment for the appraisal and also that all efforts be made to try to give an actual lease amount in the year 1992 (billing from the department). Larry EchoHawk seconded the motion. The motion passed 4-1; Jerry Evans opposed.

Governor Andrus, hearing no objections, ordered that the subcommittee would remain in effect for another year.

Larry EchoHawk requested that the letter from Mr. John Kerdy be entered into the record. Governor Andrus so ordered and also to include those of Mr. Hummel and Ms. Anderson.

Gooding T.B. Hospital – Mayor Gene Heller

Mayor Gene Heller petitioned to the Board to again extend for six months the option to purchase the T.B. Hospital for the city of Gooding. He offered again the token payment of $10 in cash to secure this transaction. Mayor Heller said that the necessity for this third extension was partially caused by the Gulf war which changed the money market investment approach but which did not change the need for a prison development. They are again making renewed efforts with plans to move ahead. Mayor Heller said that they appreciate the continued support of this board and Governor Andrus in their desire to change a liability to an asset.

Jerry Evans moved to approve the department recommendation for an additional six-month option to purchase for a $10 fee. Pete Cenarrusa seconded. The motion passed unanimously.

Twin Buttes Phase III Land Exchange

Mr. Hamilton reported that this is the third phase of a three-part land exchange involving the Twin Buttes area. He asked Mr. Kisabeth to brief the board.

Fred Kisabeth said that preliminary approval for this exchange was given in April 1989. He stated that the appraised values reflect that it is a balanced exchange. This exchange involves 4,810.86 acres of state land in eight parcels which Mr. Kisabeth located on the map. The state lands are valued at $482,000 and the federal lands (totaling over 7,500 acres) are valued at $483,000. Ted Frome, the major federal lessee, has not appealed this action. The department recommends approval.

Jerry Evans asked for clarification that none of these lands are involved in wilderness study. Mr. Kisabeth affirmed that is correct.

J. D. Williams moved to adopt the exchange recommendation. Larry EchoHawk seconded. The motion passed unanimously.

Repeal of Obsolete Rules

Mr. Hamilton said this is the final action on the repeal of obsolete rules under the Administrative Procedures Act. On December 11 the board authorized the department to enter into that process with five chapters of rules relating to land sales, land leases, mineral leases, slash disposal, easements and right-of-ways. These old rules were very procedural and included sections of code which are now obsolete and forms and procedures which the department no longer follows. Mr. Hamilton explained this is part of the department's effort to bring all of its rules and regulations up to the standards currently required by the APA. The department recommends approval.

Jerry Evans moved to approve the department recommendation to repeal. Larry EchoHawk seconded. The motion passed unanimously.

Mountain Home AFB Training Range

Governor Andrus explained that Dave Jett who is the staff person who handles this is unavailable as he is meeting in Washington D.C. today with the Air Force.

Governor Andrus outlined the latest proposal regarding the additional territory for Air Force training purposes. He used a map to illustrate the proposal encompassing the existing Saylor Creek Range which is about 112,000 acres in total. Two years ago, the Air Force had a proposal which would have expanded this range to a total of 1-1/2 million acres which was ill conceived and totally unacceptable to the people of the state of Idaho.

Governor Andrus mentioned that there was then the situation of a possible base closure, and in the interim, his office worked with the citizens of Mountain Home,

Elmore County, and the Air Force and looked at just what was necessary in the training area. They came up with a proposal for 147,000 acres which includes two private land holdings belonging to Mr. Nahas and Mr. Black. These people are meeting with Gary Best, the deputy assistant secretary of the Air Force at this time discussing an option to purchase their deeded property and their AUMs. These are the only two owners/lessees and they have agreed to a sale.

Governor Andrus pointed out the area that would not be utilized in the government's proposal of the training range thereby giving solitude, freedom and decreased impact upon the mountain sheep and other game animals in that area. He said the proposal does not provide for any low level supersonic activity. It provides that the AUMs that are in that area will be retired and utilized only for wildlife. The areas around the canyon lands are protected. The other significant factor is that there will be no live ordnance of any kind. There would be an electronic emitter which would be closed off so that animals (and humans) could be kept away from it.

Governor Andrus stressed that the thing that kept the Air Force base alive was the advantages of the additional training capability available. Once the environmental impact statement has become final, we will know a better configuration of the properties and there will probably be some land exchanges. Governor Andrus also pointed out an area that would become available for a state recreation area or park.

In addition, Governor Andrus received a letter last week from Mr. Nahas who owns the Deep Creek Ranch outlining a proposal which will be turned over to the department. The Air Force has offered Mr. Nahas $500 per acre for the land which would make the value of that ranch plus the $150 per AUM about $1,750,000. Mr. Nahas has proposed to trade, if the state is willing, adding another 1-1/4 million dollars to that, for our McCall (Lakeview Village) trailer park.

Jerry Evans stated that he would like the state to explore the possibility of selling those lands rather than exchanging. He does not think the state should be locked into any one proposal. Beyond that, exchange has some merit, and this proposal (Mr. Nahas') has some merit, but he would like to see all of the options on the table. Governor Andrus said he agreed with that, and the Air Force is willing to work with whatever the state decides to do.

Pete Cenarrusa and J. D. Williams expressed support of this proposal.

Governor Andrus said he should mention that some members of the Idaho Cattle Association are opposed to the retirement of those AUMs.

Information

Payette Lakes Timber Sale

Governor Andrus announced that as an informational item, Stan Hamilton has an issue to discuss regarding a timber sale in the Payette Lakes area.

Mr. Hamilton distributed copies of information relating to this. One is a letter dated June 5, 1991, from the Idaho Conservation League to the Board, which appears to be an appeal of the Box Creek timber sale at McCall and asking that the Board take a look at proposed timber sales in the McCall area. That sale was sold last Friday to Boise Cascade Corporation. Since this is not on the regular agenda today, Mr. Hamilton proposed to bring back to the next meeting the department's response to this appeal.

Governor Andrus asked that the department hold up that sale until after the next meeting.

Jerry Evans suggested spending some time regarding an orderly process to follow with regard to how timber might be appealed and the steps to be followed to bring that information to the board in an orderly manner.

Other informational items provided but not discussed were the timber sale and gypsy moth reports.

There being no further business brought before the board, the meeting was adjourned.

STATE BOARD OF LAND COMMISSIONERS

President, and Governor of the State of Idaho

COUNTERSIGNED:

Secretary of State

Stanley F. Hamilton

Director, and Secretary to the Board

Exhibit 7

Land Bd. Meeting Minutes

(June 9, 1992)

REGULAR MEETING
STATE BOARD OF LAND COMMISSIONERS
June 9, 1992

The regular meeting of the State Board of Land Commissioners was held at 9:00 a.m., Tuesday, June 9, 1992, in the conference room of the Joe R. Williams Office Building. Governor Cecil D. Andrus presided. Those members present were:

Honorable Cecil D. Andrus, President, and Governor of the State of Idaho
Honorable Pete T. Cenarrusa, Secretary of State
Honorable Larry EchoHawk, Attorney General
Honorable J. D. Williams, State Auditor
Honorable Jerry L. Evans, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

Consent Agenda

A. Official Transactions -- April 1992

B. Proposed Timber Sales:

1. Two Mouth Bear (CR-1-0245/Priest Lake Area)
2. Spring Power (CR-3-0353/St. Joe Area)
3. Upper Moose Creek Commercial (CR-4-0507/Clearwater Area)
4. West Fork Riswold Creek (CR-4-0513/Clearwater Area)
5. Benton Divide Road (CR-4-0529/Clearwater Area)
6. Whiskey Saddle (CR-4-0530/Clearwater Area)
7. North Bishop Relog (CR-4-0533/Clearwater Area)
8. Crooked Crown (CR-5-0056/Payette Lakes Area)
9. Round Valley North (CR-5-0059/Payette Lakes Area)
10. Price Valley North (CR-5-0066/Payette Lakes Area)
11. Schoolhouse (CR-6-0138/Southwest Idaho Area)

C. Deficiency Warrant Authorization -- Gypsy Moth

D. Cropland Rental Rates

E. Disposal of Surplus Property: Idaho Dept. of Transportation -- House, Bonner County

F. Land Sale Proposal: Parcel #382-92 -- 290 acres/Lemhi County

G. Qualified Bidders:

1. Duman Logging
2. Stuivenga Vessey Logging Co.

H. Easement Request: Idaho Power Co. -- overhead powerline -- Payette River, Boise County

I. Cancellation of Designation of Reforestation Lands -- James M. Hait, Valley County

Pete Cenarrusa moved to approve the consent agenda. Jerry Evans seconded. The motion carried unanimously.

Regular Agenda

Cottage Site Lease Rates

Jerry Evans, Chairman, said the subcommittee had been requested to meet with those interested in this topic to try to work out a recommendation that would be satisfactory to those who hold the leases and that would also be faithful to the board's charge and responsibility. The recommendation, which passed the subcommittee on a vote of 2-1, uses as a target the market value for assessment purposes as determined by the county assessors. However, it turns out that will not be possible in the Priest Lake area.

Mr. Hamilton explained that the Bonner County Assessor does not assess the state-owned lots for tax purposes. One alternative would be to look at the intermingled private lots for any levy information that might be used as comparables. The department will not be able to do that before this fall. There are also some other alternatives.

Mr. Hamilton commented on the subcommittee's motion and recommendation from the department's standpoint. The motion was to use the assessed values and set the target rent at 2-1/2% of county assessed lot value. Department staff needs clarification on whether or not the target rents would move as land values move. Lot values in both Priest and Payette Lakes are moving predominantly up, and the department is recommending that the rate be free to move in order to keep up with what's happening. In regard to phasing in rental increases over a ten-year period with a maximum increase of 5.3% per year, the department comment is that the Payette Lake waterfront lots would not reach the target value unless it is fixed statically at the 1992 level over that 10-year period. Continuing the premium rent policy until 2-1/2% of full market value is attained would mean that the bulk of the Priest Lake lessees would not pay premium rent in the future; they would attain target rent this year and then would maintain that for the next ten years. The department supports keeping second-tier lots at the minimum of $720 per year, or 2-1/2% of value.

Mr. Hamilton noted that missing from the subcommittee motion is a policy for a minimum of $1,200 per year on waterfront lots, and the board may want to continue that. There are approximately six or seven Payette Lake waterfront lots with rental rates that are less than the taxes that would be required if the lots were privately owned. The department suggests that those rentals be increased to at least that amount. The last item in the motion is to continue with the subcommittee to discuss cottage site land exchange procedures.

Don Hobbs added that the Tax Commission said that Valley County is currently at 70% of the assessed values and that in Bonner County, it is estimated to be about 93%.

Jerry Evans confirmed that the motion the majority of the subcommittee voted for indicated that the target would be a fixed target based on the 1991 value, and that would

remain the target during the ten-year period and that at the end of ten years, the board would go back and look at the value at that point in time and establish a new target and move up from that point on. During that ten-year period, the annual increase would be a maximum increase of 5.3%, so the question of a moving target, moving with the market, is not provided for in the recommendation.

Governor Andrus invited the chairpersons of the three cottage site lessee associations to come forward and comment on the motion.

Diane Plastino-Graves, 2024 Creekside Lane in Boise, president of the Payette Lakes Cabin Owners Association, said that they appreciate having the opportunity to work with the subcommittee and would hope that the subcommittee would be continued in the future to deal with a variety of issues. They are in support of the subcommittee's recommendation and urge that the full board approve that recommendation. There are two things that are very important to their association; the first is that they have a program that is stable that would last for ten years. Secondly, they would like to have predictability in the program which would allow people the opportunity to budget for increases and to make decisions regarding their leases. They feel that the motion gives them a program that would fix the target under the present Valley County assessment so that they could work towards that target for ten years. Mrs. Plastino-Graves said that lakefront people have had a 218% increase in rent over the last six years and second-tier people have had a 36% increase. She also commented that considering that they do not have the benefits of being deeded property owners, that using the county levy as a minimum for rent is not necessarily germane. She suggested that perhaps this be an issue the subcommittee deal with in the future.

Candy Anderson, 2055 Honeysuckle Lane, McCall, President of the Pilgrim Cove Association, representing the east arm of the lake, also expressed appreciation for having the subcommittee to work with. They feel that using Valley County as a third party for setting estimated lot values will also be a benefit because it will provide an appeal process. They agree that 2.5% is a reasonable rate of return and that it is important to find a program that does not have to constantly be negotiated. They feel it is in the lessees' best interest to be able to have these expected increases year after year but with the idea of constantly evaluating what is happening in the market. They want the assurance of having a program in place for ten years with a cap on increases that would give them some predictability and stability.

Kent Helmer, 2815 First, Post Falls, Idaho, representing the Priest Lake association, said they too are in favor of the recommendation of the subcommittee.

J. D. Williams asked Mr. Helmer his reaction to the alternative the department suggested today about using appraisals of intermingled private lots among the leased lots and using those averages. Mr. Helmer replied that they think that would be better than the RECG appraisals. J. D. Williams then asked if he would be agreeable to the state using the 1987 appraisal with a 16% inflationary factor added for this year and then entering into a process of negotiation with the department to try to get a $10,000 individual lot appraiser through the assessor's office. Mr. Helmer said they would be agreeable to that, and they would try to be a go-between between department staff and Bonner County if that would help.

Stan Hamilton remarked on comments of Jerry Evans, saying that the assessor does have a set of 1992 values currently in place which may be more appropriate to use than the 1991 values. Association representatives confirmed that they are in agreement with the same list of values (labeled 1992).

Jerry Evans said he would defer from making the motion.

J. D. Williams observed that he thinks the subcommittee has made a lot of progress and the Superintendent has facilitated that, and there has been good staff support. Their goal was to have a predictable program and to stabilize all the external factors that are driving up private lot values. Mr. Williams also commented he feels the state is getting close to the time when it should get out of the leased lot business and get more into the timber business. That's why he thinks the subcommittee should be continued in order to set up exchange procedures so that those lessees that want to find timberland or other valuable property acceptable to the state would be a position to make exchange recommendations.

Mr. Williams made the following motion:

"That we use the county assessed lot values to determine market value for rental assessment purposes at Payette Lake, and as part of that, use the most current information available. And at Priest Lake, for this year, use the 1987 appraisals with a 16% inflationary factor, and that the department and representatives of the Priest Lake Association continue to work trying first to have a county assessment procedure similar to that of Payette Lake. And if not, come up with an alternative, and try to do that by next year. Secondly, to set a target rent at 2-1/2% of the latest county assessed lot values at Payette Lake this year and whatever that is determined to be next year at Priest lake. Set a new target rent at the end of the 10-year phase-in period to keep everything in place for ten years for stability purposes. And then continue the premium rent policy, and just stop at that -- not set it to 2-1/2% of market value, but just continue the present premium rent policy during this ten-year period. And then keep the second-tier lots at the minimum of $720 per year rent or 2-1/2(%) of value, whichever is greater, and also a minimum of $1,200 per year on waterfront lots, and then last, continue the subcommittee to discuss cottage site land exchange procedures and other matters that would be pertinent to a landlord/tenant relationship on these lots." Seconded by Larry EchoHawk.

J. D. Williams added to his motion: "There should be a 5.3% cap on increases per year, as part of that motion." Amendment consented to by the second, Larry EchoHawk. Motion stood corrected.

Jerry Evans commented that he thinks the subcommittee has made some progress but that he believes the target ought to be a changing target as the market changes and as the assessor changes those, and the 5.3% cap is too restrictive, and therefore will not be able to vote for this motion.

The motion passed 4-1; Jerry Evans opposed.

Mr. Evans noted that the last time a schedule was adopted, there was some discussion concerning whether or not the state had entered into a binding contract. Some of the lessees viewed that as a contract, and he would hope that the board clearly communicates that this is not a contract matter. It clearly signals the board's intention, but this board cannot limit or keep another board from taking a subsequent action later on.

Grazing Rental Rates

J. D. Williams, chairman of the subcommittee on grazing, reported that although the subcommittee has made progress on the grazing rate formula in working on setting a base for that formula, they have found a differentiation on private lease rates in the two studies. Since that was a major factor in determining the base, the rates were frozen last year. This year the subcommittee concluded that there probably should be another study to identify the factors necessary to have a readily ascertainable base that is explainable to people. It appears that cannot be done until October now so the benefit of this may not affect this year's rates.

Perry Whittaker addressed the board and said the department was hoping to avoid another study as one was just done two years ago. He pointed out that this study will cost the state $17,500.

Dr. Neil Rimbey, University of Idaho, Southwest Idaho Research and Extension Service, 16952 S. 10th Ave., Caldwell, explained that one of the critical issues with the last go-round was the fact that they did not have access to drawing the sample and directly surveying the survey unit. Agricultural Statistics Reporting Service did that in the past. The basic proposal is to again survey the livestock producers in the state on private grazing lease arrangements and activities, prepare a report on those activities and then provide some information for the board to derive a base value. In answer to Governor Andrus, Dr. Rimbey said that between now and October is not a good time to do this. It is better to wait until after the grazing season. If he started October 1, they could probably have a report ready in early 1993.

Jerry Evans said he thinks a study needs to be done at the end of this grazing season and not now. More importantly, he thinks it needs to be clear that this is addressing setting a rental rate base and is not addressing relief from the drought conditions; there is a policy in place now for that.

Pete Cenarrusa said that the desire for continuing this study came from the industry who is also having trouble with the federal formula. The industry is having problems with Congress over the federal rates and also with comparing fees on a public range to those on a private range. In a private lease situation, you buy for one price exclusive access and complete control of a self-sufficient production unit. In contrast, the state and federal fees buy only one component of that production unit, the grass. He asked Dr. Rimbey if that factor has been considered.

Dr. Rimbey replied that in the last study they made adjustments in the published lease rate and some of those factors like prepayment of leases. He feels that, contrary to what some livestock people say, you can come up with a net value of the forage, so that you can compare public and private.

Stan Hamilton said that $17,500 may not be too much if Dr. Rimbey can actually accomplish this task. The problem with this survey is that the industry has full knowledge that this survey is going to be done for the purpose of setting a state grazing rate and those people are not going to be very willing to come forward with the high-end lease rates.

J. D. Williams made a motion that the board authorize the department to enter into the contract with Dr. Rimbey for the bid amount submitted. Pete Cenarrusa seconded. The motion passed unopposed.

IDL Administrative Site Lease at McCall

Bryce Taylor reported that this proposal combines the Department of Lands McCall Area Office, the Southern Idaho Timber Protective Association (SITPA) office, and the subregional McCall Fish and Game office into one office site. This year's legislature has funded the necessary construction money, the architectural plans are in the final process of approval, and the contract appraisal has been completed to determine the rent. The annual rent is recommended to be set at $5,250 for the first five years, and the second five years would be increased by the implicit price deflator to keep pace with time. That rental rate is based on 10% of the land value which is the current going rate for commercial property. Construction is scheduled to begin in July. The department recommendation is for approval of this proposal.

Jerry Evans moved to approve the department recommendation. Pete Cenarrusa seconded. The motion passed unanimously.

Land Exchange Proposal: DryBuck/Fall Creek -- Final Approval

Jay Biladeau presented the background information. Mr. Biladeau said that under this proposed exchange, the state will be exchanging approximately 7,726 acres containing 47 million board feet of timber and the state would be acquiring approximately 4,210 acres containing 38 million board feet of timber which would tie in well with current state ownership. Factors considered in the exchange are timber species mix, logging costs, timber site access and volume per acre. The additional timber values the state would acquire would make this a beneficial exchange for the endowment. There has been no public concern expressed with this package and no comments have been received from the Senate and House resource committees. The department recommends approval.

Jerry Evans moved to approve the exchange. Larry EchoHawk seconded. The motion passed unanimously.

Qualified Bidder -- Ellingson Lumber Co., Baker City, OR

Mr. Hamilton explained that this is on the regular agenda because this individual is from Baker, Oregon, and does intend to take any timber sales he can purchase to Oregon for processing.

J. D. Williams moved to deny the application. Larry EchoHawk seconded. Motion passed unanimously.

Deficiency Warrant Authorization -- Fire Suppression Costs

Mr. Hamilton explained that the first part of this request is for the usual annual authorization to use deficiency warrants to pay for fire suppression activities that arise throughout the year. The legislature funded about $101,000 for suppression and directed the department to request deficiency warrants after that.

The second portion of this request is for additional initial attack resources to be better able to respond to problems that might arise due to the severe drought situation. Attachment 1 lists $219,000 worth of resources that the department feels would be prudent to put on board. Since the co-chairs of JFAC have indicated some reluctance to authorize deficiency warrants up front, the department suggests instead to use from $80-100,000 available for this purpose from the department's 1277 account, fire suppression dedicated funds, and then go to JFAC in the winter to ask for replacement supplementals.

Jerry Evans moved for authorization of the deficiency warrants and for the adjustments in the budget as outlined. J. D. Williams seconded. The motion passed unanimously.

Field Trip Discussion at the Request of Jerry Evans

Mr. Evans said that the board from time to time is called upon to make difficult decisions such as adjusting AUM allotments, changes with regard to timber sales, and other things. He thinks the Land Board should have the opportunity to go out into the field to get further on-the-ground experience to handle the issues that come before the board.

After some brief discussion from the members concerning areas that would be of interest, Jerry Evans suggested that Mr. Hamilton set up a trip or two where there seems to be the most critical need. Mr. Hamilton was directed to bring back some suggestions regarding potential sites to visit, including the Payette National Forest area.

Settlement of Minneha Fire Claims

Steve Strack, Deputy Attorney General, presented a settlement proposal in the Minneha Fire claim. He said that five years ago, Ronald Ginner was cutting firewood near the Minneha Peak Range near Idaho City when a tree he was cutting fell across a powerline and started a fire that burned about 2,000 acres of state endowment lands. Mr. Ginner was sued by the state for damages in the amount of $155,000 along with claims from a private landowner and the Forest Service for a total of $1.3 million. Mr. Ginner's insurance policy has a limit of $300,000 and the insurance company is demanding that any settlement go only to that amount. In this proposed settlement the state would get $45,000; the adjacent landowner, $40,000; and the Forest Service, $215,000. The recommendation is to approve this proposed settlement.

J. D. Williams moved to approve the settlement proposal. Pete Cenarrusa seconded. The motion passed unanimously.

Information

Information items provided were: timber sale report, gypsy moth report, interest rate on department transactions.

Mr. Hamilton said he was pleased to report that the department has completed the FY-91 and FY-92 timber sale programs on schedule. Governor Andrus expressed appreciation stating he realized this has not been an easy task.

With no further business brought before the board, the meeting was adjourned.

STATE BOARD OF LAND COMMISSIONERS

Cecil D. Andrus
President, and Governor of the State of Idaho

Countersigned:

Secretary of State

Stanley F. Hamilton
Director, Idaho Department of Lands

Exhibit 8

Land Bd. Meeting Minutes

(June 4, 1997)

2. COTTAGE SITE RENTAL AT PRIEST LAKE AND PAYETTE LAKE

The Board established the new rate for cottage site rentals at 2.5% with the understanding this can be reopened based on incoming information from the lessees)

Director Hamilton brought the issue of cottage site rental at Priest Lake and Payette Lake before the Board. Bryce Taylor presented the background information prior to consideration of the issue.

Department records indicate the first leases were entered into about 1924 with the majority of the leases being issued in the 40's and 50's. The Board did sell a number of leases in the 40's. Rentals from l945 - 1988 had been essentially handled as flat-rate rental. Second tier lots were one rate and lakefront lots were one rate. These rates were periodically adjusted - quite prominently 3-5 years.

There was one cycle that ran for 14 years with no adjustments during that period. In 1988, after significant discussion in 1987, the rent for the lots has been determined as a percentage of the lot value. In 1987, several lots were sold to determine test the market under an auction process. Those lot values were then used to determine rental as a percentage return.

Governor Batt and Superintendent Fox left the meeting at 10:20 AM

Attorney General Lance said it was his understanding that at the vote that was taken in 1992, it was made very clear on the record that the arrangement that was entered into was not necessarily binding upon subsequent Land Boards. Mr. Taylor stated that this was his understanding also and it was pointed out very clearly in the minutes.

Controller Williams stated the reason this was an issue was because in 1987, there was a 10-year phase in plan in the policy that was adopted then. Jerry Evans made it clear at that time that one board couldn't bind another. This is a plan but not a binding situation.

Mr. Taylor stated that in the review of this issue, the Department believes that the current rental is below market. The leasehold values have escalated since 1992. The market data reviewed indicates that a higher rental is necessary. In some cases local property taxes actually exceed the rent the Department receives for the property.

Mr. Taylor stated that the Department researched Montana's cottage site rental program that is very similar to Idaho in several respects. It is a 15-year lease, not subject to conflict applications, and is assignable. They use a County assessed valuation, which is

reevaluated every 5 years. Their rental is 3.5% times that assessed valuation and that's established in legislation. The average rental in Montana is $420.00 per year. Their land values are much less than in Idaho.

Minnesota was also researched. They have about 500 lots. Leases are similar. It is a 10-year lease, a 33-ft. wide easement is retained along the lakeshore for public use, and either party may terminate with 90-days notice. This gives much less security than Idaho. The state is not obligated to insure access to the client to get to the lot. Their legislature has established rental at 5% of the appraised value. The land value is less, on the whole, than Idaho. Their rents run from $175 to $3,000 per year.

The U.S. Forest Service was also researched. They also have lease lots on the West Side of Priest Lake. The Federal Register establishes the Forest Service Fee at 5% times the appraised fee simple value. The appraised value is examined every 20 years and in the instance of Priest Lake was last done between 1978 and 1982. They update the values annual with the Implicit Price Deflator Index. The current rent at Priest Lake is $1,910 per year. Under a reappraisal, examining the actual values compared to what they've done in the Implicit Price Deflator Index, the Forest Service has indicated that the new rent should be approximately $8,750 per year. This clearly shows that the price indicator has not kept pace.

Mr. Taylor concluded the summarization of the cottage site rental background. Director Hamilton said that the 10% transfer fee needs to be considered by the Land Board. He said the leasehold value is basically the difference between the total transaction value less the value of any improvements held by the lessee, less any personal property. The difference is what has been determined leasehold value and in some cases can be fairly substantial. Mr. George Manos asked who did the appraisal. Mr Taylor said that was an appraisal done by a firm named RCEG.

Secretary of State Cenarrusa proceeded with the Priest Lake Lessees Association. Doug Cresswell, President of the Priest Lake Lessees Association said the association represents approximately 355 lessees at Priest Lake. Kent Helmer and Frank Nichols, members of the board, were present at the meeting. Mr. Cresswell's issues brought before the Board covered process, Land Board obligations with regard to the 10-year phase in agreement, cost comparison information and recommendations.

Mr. Cresswell stated that the official notice was received on May 28 - one week prior to the meeting. On Friday, May 30, a FedEx was received which contained a packet of information supplied by the Department of Lands for consideration. There was no time to notify the members and very little time to consult with board members. He stated that he hoped the Land Board did not make a decision at this meeting. He also stated that the lessees have not had the opportunity to meet with staff from the Department.

Mr. Cresswell stated in 1991, when a new lease agreement was negotiated, IDL and the Land Board were asked to give the lessees an agreement that was long-term enough so that the lessees could plan for the future. The 10-year agreement gave the lessees, who could not afford to keep their property, reasonable time to put their property up for sale and recover their investment. In 1988 there was another 10-year phase in agreement which was to have been good through 1997. The state reneged on that agreement. Again, we have a 10-year agreement - the 1992 agreement. We are into this 5 years and you are looking at terminating the agreement. What does that do to stability and predictability?

Mr. Cresswell stated that he feels the lessees are on a roller coaster - not knowing whether to get on or off. He stated the moral and ethical thing to do is to live up to the 10-year agreement.

Governor Batt returned at 10:50 AM.

Mr. Cresswell covered the cost comparisons, as they perceived them. They are concerned about the assessed values and their appraiser will address the board. He asked that all the information be looked at before a decision is made.

Attorney General Lance asked Mr. Cresswell how many of the 355 lessees appealed, to the Bonner County Assessors office, the evaluation. Mr. Cresswell stated he didn't know. Attorney General Lance stated that appellate process goes to the Assessors Office in the County in which the property is located - not the Land Board. Mr. Cresswell stated that what was received from Bonner County is an assessment notice of the value of the improvements, not necessarily the value of the lots. Director Hamilton stated that the valuation of the lots comes to the Idaho Department of Lands - they do belong to the Department.

Attorney General Lance left the meeting at 10:55 AM.

Controller Williams asked about adequate notices regarding the meeting. He asked Mr. Cresswell if he had known about the meeting 6 months before, what would have been done differently. Mr. Cresswell said he would have expected a meeting in North Idaho - a hearing - with the Board of Directors to discuss specifics - such as information that was used. He said he hoped the Board would extend this 5 years, study it, develop a proposal and conduct the hearings so the lessees have ample notice and a reasonable time to make decisions.

Mr. Cresswell stated he would at least hope the Land Board would at delay this for another year. Director Hamilton stated that if rental rates were to be increased for the next calendar year, a decision needs to be made and the Department needs to notify each of the lessees in writing by July 1. They have to be given 6 months written notice of any increase. The lease year runs from January 1 - December 31.

Attorney General Lance returned at 11:05 AM.

Mr. Ed Morse, Real Estate Appraiser from Coeur d'Alene addressed the Land Board. He was asked, by the association, to review the recommendation from the Department of Lands staff. He prepared a brief report that raised several issues he would like the Board to consider. He stated this material had no recommendation to look at in terms of a change in rental rates. There is a lot of data contained therein. He reviewed terminology. He said under the state law and under the lease agreement, the lessees own all improvements that are put in and that not only includes building improvements but it includes site improvements. Understanding the nuances of the legal interests is very important to understanding his concerns about the past appraisal work and the accuracy of some of the conclusions that were arrived at. The Attorney General stated that, it seems to him, the lessee, assuming that the Land Board approved these improvements, would get paid for them whether on the front end or the back end.

Superintendent Fox returned at 11:10 AM

Mr. Morse continued discussion regarding mistakes he felt were made by the Bonner County appraisal. Mr. Morse said that it appeared to him that the IDL appraisers have not looked at several issues. Mr. Morse asked that the Land Board have the Idaho Department of Lands look at the issue of valuation. He stated that there are significant questions regarding accuracy and methodology in terms of value that should be looked at in fairness to the lessees.

Governor Batt invited Mr. Charles Lempesis, Attorney for the Priest Lake Association to address the Board. Mr. Lempesis provided background and history of this issue to the Board. He discussed the process that has been employed and the status of the record upon which the Land Board is called to make a decision. He then suggested a paradigm or critical path for decision making that, for the first time in the history of the State Land Board, could thoroughly and decisively address the issue.

This is the most contentious, divisive, time-consuming, emotion ridden, political (in some respects) contradiction in terms that the Land Board is faced to deal with. He commended the Board for looking hard at the issue, recognizing they do have a sacred trust. Running the state as a business is a sound philosophy and examining this issue is certainly a fiduciary responsibility.

In 1992, the lessees felt they had a stable lease for the next 10 years. Stability is important in that marketplace, not only because it is fair but because you can de-stabilize market rates and the value of the leases and the long-term return to the state of Idaho if you do de-stabilize that marketplace. Tampering with that lease should be looked at long and hard.

Mr. Lempesis spoke about the process and the Department of Lands staff. The lessees have been talking with Mr. Taylor and others on this particular issue for at least 6-8 months. He stated that the Department - in good faith - did what they could to present a report today. You will note that it does not contain a recommendation. Issues and sub-issues are complex. Mr. Morse only highlighted a few. On the record here today, there is no basis upon which you should make a final decision. He asked that the Land Board be the first Land Board under the direction of Governor Batt to thoroughly decide this issue.

He outlined five things that, in his opinion, really need to be addressed.

1) What would the Land Board be with respect to these cottage site leases? What really is the philosophy presently?
2) In defining what rates and fees should be, what is the Land Board policy in respect to the character of these areas? Should Priest Lake be Lake Tahoe? Should Payette Lake be some other place?
3) Economic data - while all of us can use whatever facts we choose in trying to decide what is a fair value, no one has ever, in any appraisal, in any assessment, truly determined with all of the competing factors what the value of the leasehold interest is, exclusive of the fee simple interest.
4) That study should be commissioned and then involve the lessees.
5) What terms, when you arrive at that data and have credible data to deal with, you implement those increases.

Mr. Lempesis suggested that someone needs to do, in problem solving, a critical path and paradigm how to finally resolve this problem and answer these questions after fifty years. Until that is done, there will be constant revisiting of this issue.

Attorney General Lance stated that Mr. Morse clearly brought to the attention of the Land Board, the percentage of the improvements that belong to the lessee clearly enhances the value of the overall package (the interest of the Land Board). He said the Land Board needs to determine what this percentage should be. He asked Mr. Lempesis what percentage do the lessees feel their improvements make. Mr. Lempesis stated that he was not an appraiser. He stated that he would, on the behalf of his clients, submit a critical path to decision making.

Director Hamilton commented that this Land Board and past Land Board's have examined the question of improvements. The appraisal instructions that the Department has used for years, based on direction from the Board, have been to appraise the lots as vacant and unimproved. The Bonner County Assessor was instructed to work under these instructions.

Governor Batt said that this is not a new issue to the Board. It has been discussed in nearly every meeting of the Land Board. It is a valid point that this document has not been in hand long enough to do good work on it, but the issue itself has been around for a long time and

discussed in great detail. The appraisal business itself is a very complicated issue. The Land Board has to take an honest attempt at doing what the Board believes is right.

Mr. Lempesis stated that he has no doubt that the Land Board will make an honest effort to do what's fair. He said he doesn't feel that is an issue. One major issue is a false assumption that there is data that exists that properly values that market rate with the valuation of those property interests.

Controller Williams said a good question brought out was - should the Land Board be in this business? These are valuable properties. What should we be doing with them? There is the trust responsibility - we need to increase the return to the endowment. He stated that he felt the economic issues could be resolved in a period of time between now and the renewal date of January. He emphasized that the Land Board had to make a move.

Mr. George Manos addressed the Land Board. He said everyone is in a catch 22 situation, with the uncertainty that has been created on the leases - not knowing exactly where the lease payments are going to go. He stated that he was content where we are on the scale. He felt the Land Board did a good job. The appraiser raised his $200,000. He stated that he felt this was in line - even though he will pay a considerable amount down the road. The value has been created by the deeded property going up.

Governor Batt asked Mr. Daniel Glynn, Attorney for the Payette Lake Cabin Owners Association to address the board. He would like to see the creation of a sub-committee mandated by the Board and hoped it would include participation by the lessee organizations. He hopes that they will come to a recommended action that is satisfactory not only short-term but also long-term. He referenced the Association's memorandum of May 27th. He encouraged the Land Board to look at this in detail. The position of the Payette Lake Cabin Owners Association is that the Board, through its administration of this program over the last 40-50 years has set forth an administration, with regard to the lessees, which encouraged the lessees to participate in this program.

Mr. Glynn asked that the Board recognizes and preserves, in tact, the leasehold value that has been encouraged. Talk about the leasehold value, how it was created, how the lessees were induced to participate in it and what the Land Board is going to do to preserve that leasehold interest. This should go a long way in satisfying the other questions. Lessees need to have security and stability with regard to their leasehold interests. That has to be assured to the lessees. Hopefully within the next year we can sit down and achieve a mutual resolution of this matter.

Superintendent Fox stated that it was her understanding that when the previous Board made the agreement, that Jerry Evans clearly said that it was not a contract. It was a lease schedule that they put in place. Director Hamilton stated that Mr. Evans made it fairly clear in the minutes.

Superintendent Fox read from the June 9, 1992 minutes. As Mr. Evans noted that the last time a schedule was adopted, there was some discussion concerning whether or not the state had entered into a binding contract. Some of the lessees viewed that as a contract and he would hope that the Board clearly communicates that this is not a contract matter. It clearly signals the Board's intentions, but this Board cannot limit or keep another Board from taking a subsequent action later on. Mr. Glynn showed in the minutes that the motion was made, seconded and passed 4-1 with Mr. Evans abstaining. His comment was after the motion was made. There was never a statement by the Board that this was clearly not a contract matter. This was simply the statement of Mr. Evans. He stated that he felt, despite the statement, this is still a contract matter. And it must be recognized that the lessees left there thinking this was a contract.

Controller Williams stated that he was there. It was a 10-year plan. One thing that that Board was trying to accomplish was stability. No one could have predicted the increase in values that has occurred since then. He stated that Jerry Evans was chairman of the sub-committee and had sat through at least 3 official meetings with various lessees and their groups. This issue from the 1987 10-year plan was brought up. That was why he said what he did. Everyone on the Board at that time understood that we could not bind subsequent Land Boards. There is a lot of case law that says, because of the fiduciary nature of our duties, that we can do something - but it has to follow the law. If it doesn't, then it is not binding upon other Boards. Mr. Glynn stated that stability and market rents go hand in hand. That needs to be recognized. You can't pursue market rents that destroys the stability.

Governor Batt left at 1:20 PM.

Mr. Tom Smith addressed the Board. He stated that he had also been at the meeting where Jerry Evans made his comment. The letters to the lessees were unequivocal, and except for Mr. Evans, who was a dissenter to the policy, he never saw anything else to that effect. Certainly the Land Board cannot bind future Land Boards on all things, but they can certainly enter into 10-year leases in certain cases and he stated that he did not feel this Land Board would be able to terminate, without cause, a 10-year lease. He stated that this 10-year contract is a part of the fabric of the agreement. To tamper with this is to fly in the face of the Constitutional mandate to achieve the long-term maximum rate. If you continually unsettle these long-term leases, you're going to drive the values down. If the Land Board carries this to the ultimate extreme, this could turn Priest Lake and Payette Lake into another Lake Tahoe. Only the extremely rich would be able to afford that kind of lease.

Mr. Mark Prusynski, President, Pilgrim Cove Homeowners Association, addressed the Land Board. Pilgrim Cove is on the east bay of Payette Lake. What is market rent - or what is the market that the Land Board is mandated to obtain. Land is appraised on a fee simple

basis because that's the way the Land Board - maybe several Land Boards past - wrote the appraisal instructions. Last year an appraiser was hired and they went through the whole idea of what are we appraising here. Mr. Corlett presented the Board with a packet of material – talking about you ought to appraise the property, as it is, not some cloudy concept of "O.K. let's assume." Try to appraise on leasehold value or leased fee estate. This complies with the statutory mandate of this Board to determine market rent. It doesn't say market rent of fee simple property. It is what is the market for the property the state has. The state needs to consider that in looking at the market, the state is a major player. The state controls and affects the market. When the state owns the majority of the land, it's not a free market.

Governor Batt returned to the meeting at 1:55.

Sally Trott asked to address the Land Board. She spent considerable time looking at this issue in the Evergreen Land Exchange. She said she was pleased that the Board was looking at the fiduciary responsibilities to the endowment fund. Ms. Trott stated that she had no self-interest in this because she has deeded property at Payette Lake. She said their property has been re-assessed every year and their property taxes have risen. She commended the Board for looking hard at the fiduciary responsibility to the endowments. It is not only a Constitutional requirement, it is an Idaho State statute 53-310A. Governor Batt stated that it was not necessary to be a lawyer to have a legal opinion "in this court."

Governor Batt said one thing that concerns him is that the Land Board has not been diligent enough to get the maximum amount of money for the endowment. Attorney General Lance stated that a decision needs to be made in the month of June to give the Department enough lead-time to notify anyone of any proposed changes. There is no scheduled regular Land Board meeting for the month of June.

Governor Batt asked the Attorney General if the Board has the authority to make a new agreement. Attorney General Lance stated it does. Governor Batt stated that the Board should be somewhere at a relatively low rate of return, higher than we presently are and it should not be phased in. A reasonably low rate of return can be justified because this is a growth piece of property.

Superintendent Fox made a motion that the Board decides, at this point, to set a new rate for the properties. Attorney General Lance stated that a rate should be decided upon then the motion made. Superintendent Fox suggested 2.5%. Secretary of State Cenarrusa seconded the motion saying this would satisfy the 58-310A as it reads.

The Attorney General brought out that some of the value of this property is the sweat equity of the lessees. He stated that he felt the Board was close with the existing motion, keeping in mind the other issue, to be looked at later and probably separately, is the transfer fee.

Controller Williams said that he felt the 2.5% is in the area. He agreed with the Attorney General that the lessees have a point - a lot of the value that is there is the result of what the lessees have done.

The Attorney General stated that he didn't see any problem using the latest available assessed numbers. Superintendent Fox stated that this motion is a proposal, which will allow for reconsideration if warranted. Attorney General Lance was concerned that this was just a proposal due to time frames. He suggested making this the action of the Board subject to revisiting if information is provided that warrants a special meeting prior to the 1st of July.

Director Hamilton stated that there was not a single day in June all Board members could be present for a meeting. Attorney General Lance suggested that if this is made the action of the Board today, sent out notices as suggested and the people have an opportunity to change their minds by July or August or September, no one has paid any more rent by this time. Controller Williams stated that what has been proposed by the Attorney General would work.

Controller Williams brought out that maybe the values that are being used through the assessment process may be questionable and there should be a period of time for review. He suggested acting now with the understanding that it can be reopened based on incoming information. Superintendent Fox agreed with this as long as, in writing, each renter is notified with that statement. The Attorney General stated that until the Board establishes something different this is the action of the Board. Motion carried on a vote of 5-0.

Motion was made by Controller Williams and seconded by Superintendent Fox to adjourn the meeting. Motion carried on a vote of 5-0.

IDAHO STATE BOARD OF LAND COMMISSIONERS

Philip E. Batt

President, State Board of Land Commissioners and
Governor of the State of Idaho

Pete T. Cenarrusa
Secretary of State

Stanley F. Hamilton
Director, Idaho Department of Lands

Exhibit 9

Land Bd. Meeting Minutes

(Oct. 21, 1997)

STATE BOARD OF LAND COMMISSIONERS

Philip E. Batt, Governor and President of the Board
Pete T. Cenarrusa, Secretary of State
Alan G. Lance, Attorney General
J. D. Williams, State Controller
Anne C. Fox, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

MINUTES
REGULAR LAND BOARD MEETING
October 21, 1997

The regular meeting of the Idaho State Board of Land Commissioners was held on October 21, 1997, in Boise, Idaho. The Honorable Philip E. Batt presided. The following members were present:

Honorable Secretary of State Pete T. Cenarrusa
Honorable Attorney General Alan G. Lance
Honorable Controller J.D. Williams
Honorable Superintendent of Public Instruction Anne C. Fox

Secretary Stanley F. Hamilton

The meeting convened at 9:00 a.m. and adjourned at 11:30 a.m.

CONSENT AGENDA

The following Consent Agenda was approved in its entirety upon a motion by Superintendent Fox, seconded by Controller Williams and carried on a vote of 5-0.

1. This agenda item requested approval of official transactions as follows:
   A. Bureau of Range Management and Surface Leasing Official Transactions for Cropland, Grazing, Cottage Site, Miscellaneous, and Submerged Land Leases for the month of August 1997
   B. Land Sale Section, Official Transactions for the Bureau of Real Estate for August, 1997
   C. Official Transactions for the Bureau of Real Estate, Easement Section for August, 1997
   D. Bureau of Minerals Official Transactions for September 1997
   E. Timber Sale Official Transactions for the period August 23, 1997 through September 19, 1997

2. This agenda item presented applications for addition to the qualified bidders list, timber sales as follows:

   Blue Mountain Leasing Company
   P.O. Box 190
   Usk, WA 99156

   North Idaho Timber Management, Inc.
   P.O. Box 63
   Blanchard, ID 83804

3. This agenda item requested approval of a timber sale as follows:

   A. Outlet Helo CR-1-0296 1,750 MBF

4. This agenda item requested an increase in the administrative fees charged for processing disclaimer of interest requests for accretion land along navigable rivers and lakes from $200.00 to $600.00 effective November 1, 1997; however, the fee could be greater if the department incurs costs in excess of $600.00. This is for non endowment land that lies between the ordinary high water mark and the meander lines established by the original surveys by the General Land Office. The predecessor to the Bureau of Land Management.

5. This agenda item presented a request for a disclaimer of interest from Mr. Glen Richman on behalf of the Del Monto Fife Trust, doing business as Fife Enterprises, for former riverbed located in and/or adjacent to portions of Sections 19, 30 and 31, Township 21 North, Range 22 East, B.M. in Lemhi County. The recommended fee is $200.00.

6. This agenda item requested approval of the following Land Board Minutes:
   May 28, 1997 – Regular Land Board meeting
   June 4, 1997 – Special cottage site meeting
   July 8, 1997 – Regular Land Board meeting
   August 12, 1997 – Regular Land Board meeting

7. This agenda item requested Board approval of proposed revisions to the existing submerged land lease form.

8. This agenda item requested approval to submit for pending rule, revisions to IDAPA 20.03.02 Exploration and Surface Mining Operations in Idaho (Final approval by the Board)

9. This agenda item requested approval to submit for pending rule, revisions to IDAPA 20.03.04 Regulations of Beds, Waters and Airspace over Navigable Lakes in the State of Idaho (Final approval by the Board)

10. This agenda item requested approval to submit for pending rule, revisions to IDAPA 20.02.01 Rules Governing the Idaho Forest Practices Act (Final approval by the Board)

REGULAR AGENDA

11. Proposed light industrial use lease on Collins 80 (Approval of Black Cat Lease)
Presented by Alvin Carr, Leasing Specialist

Director Hamilton introduced Item #11 which is a proposed light industrial use lease on Collins 80 which is approximately 2 miles south of the Boise airport adjacent to the Pleasant Valley road. Alvin Carr presented the Land Board with background information.

The Department received an application from Black Cat Contractors of Boise to lease approximately 10 acres of the Collins 80 for a hot plant, site aggregate stockpile, and aggregate washing facility. The Department in accordance with Idaho Code §58-307, which requires the Department to follow certain procedures prior to entering into a commercial lease, reviewed this lease application. The Department met these requirements and received no adverse comments. Black Cat Contractors have notified the Department that they have applied for an obtained a conditional use permit. Light industrial use is compatible with the general area. This lease is for a 10-year term. Annual rental is $10,000 or 10% times the appraised land value, subject to an annual adjustment based on CPI Urban.

The Department is requiring that an access road be built along the southern perimeter of the parcel to facilitate heavy traffic into the southern and southeast portion. The cost associated with the construction of the road not to exceed $50,000 will be amortized during the term of the lease. The state will own the road and control the access of future development. The improvements consist of non-permanent facilities and two-gravel wash settling ponds. Upon expiration or termination of the lease, the lessee will be required to removed the improvements and complete the need of reclamation work. The Department is considering a similar lease to Monroc, Inc. which would be compatible with Black Cat Contractors lease.

The recommendation of the Department is to approve issuance of the lease to Black Cat Contractors and delegate authority to the Director for approval of new commercial leases on this property, up to 10 years in term.

Governor Batt asked what if the contractor does not remove the improvements. Mr. Carr stated that the Department is looking at a $25,000 bond that has been reviewed to make sure this amount is adequate.

Mr. Carr stated that the Department did extensive advertising of the acreage in 1994, with no interest obtained at that time. There have been some interim uses on a year to year basis since that time. Attorney General Lance stated that with a hot plant being put on the property, he has some environmental concerns. He also stated that he felt the hot plant would make it more difficult to lease the home. Governor Batt stated he had some concerns and would like the opportunity to look at the property. Controller Williams expressed that he also had some concerns. Attorney General Lance stated he would like to have the Department of Administration look at this property. This department has considerable commercial leasing expertise. Secretary of State Cenarrusa agreed.

Governor Batt said after the property has been looked at, a special meeting or conference will be held to make a decision. The recommendation was deferred by unanimous consent.

12. Request for Final Approval – State of ID, Potlatch/Clearwater Land Exchange
Presented by Perry Whittaker, Real Estate Bureau Chief

Director Hamilton stated that Item #12 was a request for final approval to complete a State of Idaho/Potlatch Corporation – Clearwater land exchange. Perry Whittaker provided the background information.

Mr. Whittaker said this is one of a series of exchanges between the State of Idaho and Potlatch Corporation to consolidate ownership in Northern Idaho. The exchange involves the acquisition of 2,693.14 acres of Potlatch property for 2,591.70 acres of State endowment property. The lands being exchanged are fairly similar in most respects.

The timber was cruised by an independent cruiser and check cruised by both Potlatch and Department personnel. Appraisals were independently done. A public hearing was held September 19, 1997 to seek public input for the exchange. No opposition to the proposed land exchange was expressed. The Department staff requested permission to complete the Clearwater land exchange with Potlatch Corporation.

Superintendent Fox stated that this was a good proposal and it does not appear that it will negatively impact the schools. Attorney General Lance stated it looks like a good exchange and facilitates the philosophy of the Land Board.

Governor Batt asked if cruisers were certified. Mr. Whittaker stated that cruisers generally run a consulting forestry business. They have forestry background. Cruisers measure the diameter of the tree, determine the species and measure the height. Check cruising takes place on the same trees for diameter, height and species. The Department knows whether a cruiser does a good job. A 10% sample is taken. Controller Williams stated, that on the Evergreen Exchange, he ran a tape for his own benefit and the measurements were accurate.

The motion was made by Attorney General Lance and seconded by Controller J.D. Williams to approve the Department's recommendation. The motion carried on a vote of 5-0.

13. Reconsideration of Submerged Lands Lease Rental Regarding Floathomes
Presented by Bryce Taylor, Range Management & Surface Leasing Bureau Chief

Director Hamilton introduced Item #13, which is a reconsideration of submerged land lease rates for floating homes. Three people have indicated they would like to address the Board. Bryce Taylor provided a brief summary of the meeting that was held in North Idaho.

Mr. Taylor said the Board approved the submerged lands leasing rules (IDAPA 20.03.17), rental and fees. Those rules went before the 1997 legislative session and in March of 1997, the legislature passed the rules. These rules became effective in July of 1997.

Land Board members and the Department began receiving and responding to letters from constituents regarding the approved rental for floathomes in April 1997. The letters received requested relief and reconsideration of the approved $1,000.00 per year rental for floathomes. Many indicated disappointment they had not had an opportunity to present their concerns to the Board.

Attorney General Lance, Superintendent Fox, Controller Williams and Department staff met with the Bayview Floating Homes Association in the Bayview Community Center on Sunday, September 21, 1997 to hear the concerns. Testimony was taken from 2:00 – 4:00 p.m. from the floathome owners. There were approximately 128 people at the meeting. After the meeting, the Board members and staff were taken on a tour of the Bayview floathome community.

Representatives of the floathome owners association presented their concerns to the Board. Floathome owners felt that a rental of $1,000 per year is to high compared to the rental charged for similar size docks. They also felt it was unfair when compared to the license fee that would be charged for a boathouse. The floathome owners' feel, from a rental standpoint, the focus should be on the displacement of surface water and that all uses should be treated similar and fair.

Mr. Denny Davis thanked the board members who came to Bayview for the floathome meeting. Mr. Lou Wilson, President of the floating homes association addressed the Board. He said he represents a constituency of ninety-four (94) floathome owners in the area. He stated that floathomes are unique and a historical treasure. Many date back to the 1920-30's. 87% of the floathome owners qualify as senior citizens. He asked that they not be confused with lavish floathomes in Seattle, Sausalito or the Portland area. The floathomes are used approximately four (4) months per year at the most. Some marinas turn off water to the floathomes and most are not well insulated or equipped for winter living. Mr. Wilson said the association asked for fairness and equity concerning this issue.

Controller Williams said the Board would like to do something for the floathome owners and felt that the problem has to do with the definition "non-navigational, commercial use."

Attorney General Lance said there are two types of floathomes – one type is outside a marina and the other is inside a marina. Mr. Taylor said there is a difference on how the Department can examine the two types of properties.

Attorney General Lance stated that, at the Bayview meeting, he picked up an undercurrent of some dissatisfaction with some of the marina owners. If a floathome owner is tied up to a marina, the prospect of moving your home to another marina is not practical. Some feel the marina owners are taking advantage of this. He said it is possibly a mistake for the Department to tie themselves closely with the marina owners in terms of computing and collecting the rent.

Gary MacDonald, a marina owner, addressed the Board. He stated that all of the complaints regarding marina owners were against one marina. This marina has had a difficult time and has had several owners. Generally speaking, the marina owners have a good relationship with their customers. He said that a $1,000 fee on the floathomes is a very arbitrary figure and is not fair.

Attorney General Lance said he would recommend, with the approval of the full Land Board, that the sub-committee meets in the next few weeks, and with the floathome owners' input, try to put together a proposal to recommend to the Board at the November meeting. Superintendent Fox recommended that the sub-committee meet to find a fair solution for the floathome owners.

Governor Batt asked when the rents take effect. Mr. Taylor stated that with the new leasing rules that became effective in July, the Department would begin sending out new leases in January. There are leases in existence that are being charged rent under the old policy. Mr. Taylor said he felt the Board had some latitude to work within.

The decision was unanimous that the sub-committee meets prior to the November Land Board meeting and report back to the full Land Board at the November meeting.

14. Report on Cottage Site Rental Reconsideration
Presented by members of the sub-committee

Director Hamilton introduced agenda item #14 that is a reconsideration of the 1998 cottage site rental. This issue was on the Land Board agenda previously and deferred to a sub-committee. Mr. Bryce Taylor provided the background information.

In the June 4th meeting, the Land Board approved a new rental for cottage sites commencing January 1, 1998. The rate is 2.5% times the 1996 county assessed value. Hundreds of letters were received asking the Land Board to reconsider this rate.

At the September meeting, a sub-committee was appointed to examine the rates. The sub-committee consisted of Controller Williams, Superintendent Fox, and Secretary of State Cenarrusa.

On October 7th, the cottage site sub-committee addressed this issue. The proposed agenda covered three items.

1. Cottage site rental for 1998
2. Cottage site valuation appeal process – Priest Lake and 14 lots at Payette Lake
3. Rule Making – Discussion

An additional item included hardship cases. Draft minutes of this sub-committee meeting were submitted at the Board meeting.

The suggested rental rate posted by the sub-committee is to charge 2.5% of the 1992 assessed value versus the 1996 or to increase the 1997 rent by 25% whichever is greater. There will be

another sub-committee meeting scheduled to cover agenda items 2 and 3 and also address any hardship cases.

Governor Batt asked for an identifiable difference between fee simple and leasehold value. Mr. Taylor said that leasehold value is the value that a leaseholder might sell it someone else for. Fee simple is the value of the property in fee if you were selling it full title vs. selling the lease. Director Hamilton said the assessor and any fee appraiser hired by the Department would assess or appraise property as its market value and in a bare land condition. The assessor also appraises the improvements and tries to place an estimated value on them as well. Director Hamilton stated that the Department does not believe that it is appropriate to use leasehold value in an effort to value these properties. In the past, the Board has settled for a lower rate of return (2.5%) which may take into account many of those other factors that are out there.

Governor Batt stated that the lessees have not objected to the 2.5%. They realize this is a low figure. It is the appraisal they are concerned with and he said he felt the lessees had a good point.

Attorney General Lance stated that there is another area that concerns him regarding these leases. It has to do with Idaho residents vs. non-residents who hold the leasehold. Residents of the state of Idaho already pay into the General Fund, certain taxes, which supports the operation of the Department of Lands and other administrative overhead. Non-residents do not make those contributions. He presented examples to the Board using resident and non-resident tuition at BSU and resident and non-resident hunting and fishing licenses. He stated that this would also pertain to floathomes as well as cottage site leases. He felt a differential in terms of premium or rental should be discussed.

Controller Williams said the sub-committee meeting was a good meeting with input from the associations and their legal counsel. The sub-committee arrived at an interim policy regarding 1998 rates. He said it will probably take a year to get the appraisals worked out.

The recommendation to the full Land Board was to go with 2.5% of the 1992 values, which is the last time there was agreement on valuations, or 25% of the 1996 valuations, whichever is greater. There will be a substantial increase in the lease rates for next year. Association members and legal counsel attending the meeting supported the recommendation.

Governor Batt asked if the sub-committee brought up the issue of vigorously pursuing land exchanges. Both Superintendent Fox and Controller Williams said that the consensus of the sub-committee was that land exchanges be pursued quickly.

Attorney Charles Lempesis urged that the Land Board follow the recommendation of the sub-committee to adopt the 1992/25% of 1997 for the forthcoming year. This will buy the time to do the arduous task of examining the other issues. Those issues as their association views it are:

1. We get to the question of how and what we are appraising,
2. Work on the appeal process, and
3. Look at the hardship issue.

As this is the first that has been discussed regarding the resident/non-resident issue, he will also be prepared to speak on this issue. This will all be for naught, unless the question of how and what we are appraising is not seriously looked at because all other issues stem from that.

Attorney Daniel Glynn said his association was guardedly optimistic at the outcome of the sub-committee meeting. He reinforced that the Land Board is only looking at the 1998 rates with further discussion on the other agenda items with the sub-committee.

Controller Williams moved, on behalf of the sub-committee, that the Board adopt the following:

1. The lease rates for cottage sites for 1998 be 2.5% of the 1992 appraised value or 25% more than the 1997 rent, whichever is higher.
2. That the sub-committee continues to meet to review items such as the appraisal process, appeal process and stabilize the process and work on the issue of what is fair market value.
3. That the board retains the 10% surcharge on transfers of leasehold interest for 1998.

Secretary of State Cenarrusa seconded the recommendation. Governor Batt stated that he would vote for this motion but he wanted it clearly understood that this is for one year only and is in no way binding on future actions of the Board. Two (2) percent of the fair market value is not out of line for these properties. He thanked the sub-committee for their work on this issue. Controller Williams clarified by saying this is an interim policy that has been brought back to the Board, primarily on appraisals. This is the big issue that needs to be resolved.

Attorney General Lance if the overhead is not being paid for by non-residents, he reserved the right to make a motion at a later time to make sure that everyone is paying his fair share of the cost of administrating the overhead. Controller Williams said the sub-committee would finalize this process at a future meeting.

The above motion was made by Controller Williams and seconded by Secretary of State Cenarrusa. The motion carried unanimously.

Superintendent Fox made a motion that land exchanges be opened up and that the focus be on commercial property for those exchanges. Governor Batt asked that the Board be made aware of any exchanges in the early stages of an exchange. Superintendent Fox stated that this would be in the Payette Lake area not to open up the Priest Lake area at this time. Controller Williams seconded the motion. The motion carried on a vote of 5-0.

INFORMATION AGENDA (Informational items only – no action required)

15. Timber sale activity report
16. Interest rate update
17. Triumph Mine update
18. 1997 Fire Season update
19. Grazing Fee for calendar year 1998
    Director Hamilton informed the Board that the grazing rate for 1998 will be $4.16 and AUM based on the formula that the Board has used for several years.
20. DoI - RS 2477 - roads

There being no further information to come before the Board, a motion was made by Superintendent Fox and seconded by Controller Williams to adjourn the meeting. The motion carried. The meeting adjourned at 11:30 AM.

IDAHO STATE BOARD OF LAND COMMISSIONERS

Philip E. Batt
President, State Board of Land Commissioners and
Governor of the State of Idaho

Pete T. Cenarrusa
Secretary of State

Stanley F. Hamilton
Director, Idaho Department of Lands

Exhibit 10

Land Bd. Meeting Minutes

(Dec. 15, 1998)

STATE BOARD OF LAND COMMISSIONERS

Philip E. Batt, Governor and President of the Board
Pete T. Cenarrusa, Secretary of State
Alan G. Lance, Attorney General
J. D. Williams, State Controller
Anne C. Fox, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

MINUTES
REGULAR LAND BOARD MEETING
December 15, 1998 9:00 AM

The regular meeting of the Idaho State Board of Land Commissioners was held on December 15, 1998, in Boise, Idaho. The Honorable Philip E. Batt presided. The following members were present:

Honorable Secretary of State Pete T. Cenarrusa
Honorable State Controller J.D. Williams
Honorable Attorney General Alan G. Lance
Honorable Superintendent of Public Instruction Anne C. Fox

Secretary to the Board Stanley F. Hamilton

CONSENT AGENDA

Director Hamilton informed the Board that on Agenda Item #4, regarding the results of 1998 lease auctions, the lessee, Mr. Grant Lloyd – grazing lease G-9048, has filed an appeal. This appeal is tentatively scheduled to be considered at the February Land Board meeting. Passage of this agenda item is with the understanding that the Grant Lloyd appeal will not be part of this agenda item.

The motion was made by State Controller Williams to approve the consent agenda with the exception of grazing lease G-9048 – agenda item #4. Attorney General Lance seconded the motion. The motion carried on a vote of 5-0.

1. The following official transactions were approved:

   Bureau of Real Estate, Easement Section for October 1998
   Bureau of Real Estate, Land Sale Section for October 1998
   Bureau of Minerals for October 1998
   Bureau of Range Management and Surface Leasing for Cropland, Grazing, Cottage Site, Miscellaneous and Submerged Land Leases for October 1998
   Timber Sales for the period October 20, 1998 through November 24, 1998

2. The following timber sale, staffed by Ron Litz, Chief, Bureau of Forest Management, was approved:

   A. Murray Creek CR-6-0148 6,260 MBF

3. The following application for addition to the qualified bidders list for timber sales, staffed by Ron Litz, Chief, Bureau of Forest Management, was approved:

   Alliance Construction, Inc.
   6700 Winding Trail Lane
   PO Box 2669
   Coeur d'Alene, ID 83816

4. The Board accepted the high bids that were submitted at the 1998 lease auctions, with the exception of lease G-9048, lessee Grant Lloyd. An appeal was filed on this grazing lease and is tentatively scheduled to be considered at the February 1999 Land Board meeting. This issue was staffed by Tracy Behrens, Range Management Specialist.

5. The addition of Nancy Umbach, Andrea Umbach-Tevlin and M.Kathleen and Karl C. Klokke to the Payette Lake Non-Lakefront Cottage Site Exchange List was approved. This issue was staffed by Perry Whittaker, Chief, Bureau of Real Estate.

6. The Disclaimer of Interest request from Thomas and Norma Jean Tapscott of Salmon for 10.82 acres of accretion land, staffed by Perry Whittaker, Chief, Bureau of Real Estate, was approved.

7. The request for Deficiency Warrant Authority for gypsy moth suppression, staffed by R. Ladd Livingston, Forest Insect and Disease Supervisor, was approved.

REGULAR AGENDA

At the request of Director Hamilton, agenda item #15 was placed at the beginning of the regular agenda.

15. Lakeview Village/Ponderosa Park Lands Exchange – Idaho Department of Lands/Idaho Parks and Recreation - Presented by Perry Whittaker, Chief, Bureau of Real Estate

Director Hamilton stated that this agenda item is a request for conceptual approval to initiate a land exchange with the Department of Parks and Recreation for the Lakeview Village parcel.

Perry Whittaker provided the background information. Nick Krema, Deputy Attorney General was present for any questions. Yvonne Ferrell, Director, Idaho Parks and Recreation was also available.

The Department requested Land Board conceptual approval to enter into a Memorandum of Understanding with Idaho Parks and Recreation. The department would then begin the process of identifying parcels of property which either Idaho Parks & Recreation or Idaho Parks & Recreation and some cottage site lessees could acquire for exchange to the Idaho Department of Lands.

Mr. Whittaker stated that the Department of Parks and Recreation is interested in obtaining title to Normal School endowment lands lying within and adjacent to Ponderosa State Park at McCall, Idaho. There are three parcels that are being considered for transfer to the Department of Parks and Recreation.

The department will begin the process of identifying potential properties for the Idaho Department of Parks and Recreation or the Idaho Building Authority to acquire for exchange to the Idaho Department of Lands subject to approval by the land board.

Mr. Whittaker stated that if the exchange takes more than one year to complete, it may be necessary for the Board to consider a rent adjustment in the Lakeview Village lease. This would free up enough cash so that the Idaho Department of Parks and Recreation can accomplish capital improvements necessary to maintain and protect the endowment asset value until the exchange can be completed.

Director Farrell said that the property known, as Ponderosa State Park has been the destination of many of the Treasure Valley people. It is totally beyond capacity and has been for several years. That is what prompted leasing the Lakeview Village property about five years ago. The five (5) percent per year increase in lease rates makes it financially unfeasible for the Department of Parks and Recreation to be able to raise enough revenue to pay the lease rate beyond the year 2000. These are lands that have long been appropriate for public recreation. She said that the Department of Parks and Recreation is comfortable with the Memorandum of Understanding that has been prepared.

State Controller Williams asked why the value was not stated in the Memorandum of Understanding. Director Farrell said it was her understanding that if the land exchange were not completed within one year, there would have to be a re-appraisal to insure that current values are addressed.

State Controller Williams stated that he thought the Board was going to enter into a contract where the value would be set and then paid for at one million dollars per year with land over the term of the installment – like an installment contract. Director Hamilton stated the Department had explored this avenue and felt that this was not appropriate under the law. That would have been looked at as a purchase. With the Building Authority coming into the picture, they have given the Department the capability to deal with this quickly. It is not anticipated that the appraisal would change significantly.

The motion was made by State Controller Williams and seconded by Attorney General Lance to accept the recommendation of the department. The motion carried on a vote of 5-0.

8. Request to approve and accept Clear List from BLM for the State's Indemnity Selection Application IDI-32323 - Presented by Perry Whittaker, Chief, Bureau of Real Estate

Perry Whittaker provided the background information. The state of Idaho did not receive all of its public school entitlement at the time of Statehood as per the Enabling Act for various reasons. The department and the BLM staff are very interested in completing the indemnity selection process. This will allow the public school endowment to receive additional revenue from these lands.

The state currently has an estimated 3,697.04 acres of "base" lands remaining. The State Board of Land Commissioners on April 8, 1997 approved this application in concept. The BLM has completed their environmental analysis, has advertised the indemnity selection for public comment and both the BLM and the Department have agreed on an acceptable package.

The federal land is productive commercial timberland that fits in well with the state owned land. The federal parcels typically lie adjacent to other state land. BLM indicated that the state could receive Clear List No. 5 before the end of 1998. This clear list should just about complete the in lieu selection in Idaho.

The department recommended that the Land Board give approval to acquire the federal lands in state indemnity selection application IDI-32323.

The motion was made by Superintendent Fox and seconded by State Controller Williams to approve the recommendation of the department. The motion carried on a vote of 5-0.

9. Cottage Site rental – Land Board Subcommittee recommendations - Presented by Alvin Carr, Commercial and Recreational Leasing Specialist and State Controller J.D. Williams, Subcommittee Chair

Alvin Carr provided the background information. The Land Board subcommittee has met on several occasions to discuss and review the Priest Lake and Payette Lake appraisal reports, the rental rate, the appeal process, hardship claims and the 10% premium rent. Those have been completed and accepted by the Department.

The following are the recommendations from the sub-committee.

A. Retain the current market rent as adopted by the Board at their regular meeting of June 4, 1997 which is 2.5% of current county assessed values. For clarification purposes, the current assessed or appraised fee simple value of the land is determined as though the land is vacant and unimproved, subject to any outstanding rights and reservations of record and may at the Department of Lands discretion be determined by a department administered appraisal or county assessed valuation. The 2.5% rate recognizes and takes into consideration the lessee's sweat equity and lessee site improvements. Therefore there would be no deduction or credit granted for lessee site improvements.

B. Write the rental rate formula into new 10-year leases. This would provide for rental rate stability, which has been a major concern with lessees. Any subsequent lease amendments or extensions for mortgage purposes will be specific to a review of

rental rate in the year 2009. Revision of the cottage site recreational lease will be dependent upon legal counsel review. The new lease would be effective January 1, 2000 and expire December 31, 2009.

C. Any phase-in of rental rate be considered by the full Land Board.

D. Adopt the Department of Lands proposed appeal process.

E. Retain the current parameters for hardship claims as adopted by the Board at their regular June 9, 1998 meeting

F. Retain the current 10% premium rent. This recommendation will become moot if market rent is achieved.

In addition to the Subcommittee recommendations, department staff recommends that the current 10% premium rent be revised to eliminate the personal property value. The leasehold value shall be determined by subtracting the value of improvements as determined by county assessed value or department administered appraisal from the total sale price.

State Controller Williams asked that the 2 ½ percent of current county assessed values be clarified to include, in Bonner County, the value as determined by the Assessor. He stated that the subcommittee was in agreement that the 2 ½ percent takes into account the various factors that have been raised by the lessees.

State Controller Williams said that the lessees asked that the lease rate formula be written into their leases for stability and it was the consensus of the subcommittee that that would be a recommendation.

As to the phase-in of the rental rates, there was some concern with the subcommittee because of the fact there was no raise in rates for 1999. The subcommittee felt that the full Land Board should make that decision.

The appeals process is if a lessee has a problem with his value as determined by the county, he could come to the Department and make a presentation to them. If he felt he did not receive the relief he sought, he could then come before the full Land Board for determination. If he still was not pleased, he could appeal through the Administrative Procedures Act to the court. This would be an appeal based on the record in the Land Board meeting.

There was discussion as to whether the surcharge issue should remain. The consensus of the subcommittee was that it should remain.

Superintendent Fox said she felt very comfortable with the recommendations being brought before the Land Board. She said that extensive studies were done.

Secretary of State Pete Cenarrusa stated that the phase-in was discussed with legal counsel for both Priest Lake and Payette Lake. There was no increase in 1999 with the consideration that the state goes for full value at 2 ½ percent in the year 2000.

State Controller Williams said that he felt the lessees would like to speak to the issue of a percentage limit of an increase so that it is not an extraordinary amount for one year. Attorney

General Lance said the subcommittee recommendation does not include a cap on fair market value increases. State Controller Williams said that was right.

Attorney Chuck Lempesis, on behalf of his association, commended the subcommittee on their efforts throughout these meeting. He said he felt, in a large part, that the lessees are in agreement with the recommendations of the subcommittee.

Attorney Lempesis said that the 2.5% of market value is fair. If there is an appeal process, that will be the appropriate way to resolve any discrepancies on appraisals. He said with respect to Controller Williams point, the lessees at Priest Lake are not assessed annually, but if the lease that is issued can speak to the issue that it is market value as determined by the assessor rather than the assessment, it would be more accurate.

Attorney Lempesis said in regard to hardship, the lessees have always appreciated the staff and Board's position to help people who are at the point of hardship.

He stated that the lessees do have a disagreement with the 10% surcharge. When the 10% surcharge was adopted, it was done with the view that there was a disparity between lease rates and what the state should be receiving under its Constitutional statutes. That was its sole purpose. It is felt that the 10% surcharge is excess, it is unfair under these circumstances and should be removed in its entirety. He asked that the Land Board consider removing it.

Attorney Lempesis said he has reviewed the appeal process. The lessees had proposed something differently but are willing to accept what is being proposed.

Attorney Lempesis asked to be on the record as not accepting the current valuations.

He stated that the lease incorporating these changes has not been prepared. He asked that any motion that is made or adopted by the Land Board include room for the lessees to have the opportunity to work with legal counsel to review the proposed lease. The lessees would like to have the opportunity to come back and visit with the Land Board on any terms they feel might be in dispute before the final lease is adopted.

State Controller Williams expressed his thanks to all the lessees and their counsel for their efforts on this issue.

Director Hamilton stated that the Department recommends that the 10% surcharge (premium rent) needs to stay. It is based on the fee that a prospective lessee pays to the existing lessee because contract rent is less than market rent. It is a standard procedure. If the rentals get to the point where they approach market rent, what the market is willing to pay, then the 10% would fade away. Department staff feels firmly that this should remain in place.

Attorney Daniel Loras Glynn represented Attorney Dick Greener at this meeting. With him were Mr. Chuck Hervey, President of the Payette Lake Homeowners Association and Richard Smith also of the Payette Lake Homeowners Association.

Attorney Glynn stated that he would echo the sentiments that were previously expressed by Attorney Lempesis from Priest Lake.

He stated that they were present to accept in principal, the recommendations of the subcommittee. The 2 ½ percent is reasonable and being written into the leases will give the security and stability that this process has been striving to obtain.

Attorney Glynn stated that he felt the appeal process also needed to be written into the lease provisions.

Attorney Glynn asked that the Land Board consider a percentage cap with respect to the rental increases. He stated that his association feels this would be a workable solution. Attorney General Lance asked how the Land Board could square their obligation to charge fair market value with a cap – acknowledging that fair market value is something higher than what it is that the lessees are required to pay. State Controller Williams asked Clive Strong, Deputy Attorney General to respond to this question.

Deputy Attorney General Clive Strong started with the Constitution, which empowers the Land Board to administer these lands for the maximum long-term return to the endowments. As a trustee, the Board has an obligation to maximize that return. There are also statutory provisions specifically with cottage site leases that say they will be rented at fair market value. That was the agreement reached, based upon the need to address the issue of being able to continue to lease these properties without going to the conflict auction. He said it was his conclusion, that as a Board, it is the obligation to insure that you are maximizing that return to the endowment and that a phase-in provision would not be consistent with the fiduciary duties.

The motion was made by State Controller Williams to approve the recommendation of the department with the modification that the appraised values at Priest Lake include values as determined by the assessor. That there be no phase-in and that the appeal processes outlined be approved and that the hardship parameters be approved and that the 10% premium rent be retained. Attorney General Lance seconded the motion. The motion carried on a vote of 5-0.

Director Hamilton stated for clarification that it includes writing it into the new leases. State Controller Williams said that the leases would be rewritten. He also added that the motion included the staff recommendation that the current 10% premium rent be reviewed to eliminate the personal property value. Attorney General Lance concurred that the motion included the staff recommendation regarding the 10% premium rent.

10. Air Force Enhanced Training Range State land lease– Owyhee County - Presented by Bob Snapp, Lands Leasing Specialist

Attorney General Lance stated that another arrangement between the department and the Air Force was being considered. He asked that Clive Strong, Deputy Attorney General and Colonel Richey inform the Board as to what is currently being considered.

Deputy Attorney General Clive Strong said that the question is how does this lease relate to the current grazing lease already out on the property. The current grazing lease will remain in place and the lessee will work under the current leasing plan. This would be a secondary lease (or overlay lease) with the Air Force.

Attorney General Lance asked if the Air Force would be a sub-lessee for a while. Deputy Attorney General Strong said the idea would be that there would be two overlaying compatible

leases – it would not be a sub-leasing situation. Attorney General Lance said one lease would be a miscellaneous lease and that information is not available to the Land Board currently.

After considerable discussion, Attorney General Lance asked for unanimous consent to defer any action on this item to the January 20, 1999 meeting. This would allow the Air Force to put in their application for a miscellaneous overlaying lease. There were no objections. The issue will be addressed at the January 20, 1999 regular Land Board meeting.

11. Float Homes – Audience with the Board - Introduced by Bryce Taylor, Bureau Chief, Range Management/Surface Leasing - Presented by Representatives of the Float Home Owners Association

Denny Davis, representative for the float home owners, briefed the Land Board on what the float home owners feel to be exorbitant rental rates imposed by Scenic Bay Marina.

Mr. Davis provided the Land Board with a list of potential grievances that the membership has against the marina. He also provided the Board with figures that reflect information regarding moorage increases. Scenic Bay Marina recently proposed rental increase to their floating homeowners of approximately 50%. He brought out to the Board that this increase is not due to no previous rent increases, or trying to achieve a market rent such as the cottage site lessees. Mr. Davis provided comparison information with other marinas in the area. Scenic Bay did send out notice to the floathome owners that they would implement the raise in rental in early February.

Mr. Davis said that this is really not a free market. Floathomes are difficult to move and would involve a considerable investment by the floathome owner. He stated that the floathomes are a captive audience and are subject to unfair rental practices.

Mr. Davis said due to these circumstances, the owners prepared and presented to the Legislature last year, a piece of legislation called the floating homes residence act. It passed unanimously by both houses and was signed by Governor Batt the bill. This is now in effect and does provide the owners a measure of protection. This legislation does not impose any sort of controls on rent.

There was a meeting between the floathome owners and Scenic Bay and these issues were laid out on the table. There was discussion, but no agreement was reached at that time.

Mr. Davis asked that the department, with direction from the Land Board, work with the float homeowners to reach a fair agreement on the rental rates imposed by Scenic Bay Marina. If lease rates are allowed to be unregulated, floathome owners could be forced out of the marina.

Controller Williams stated that he did not believe Scenic Bay had a lease at this time. Mr. Bryce Taylor stated that they have not consummated their lease at this time. When the lease was mailed to Scenic Bay last April, there were some flaws in the description of the record that Scenic Bay asked to have corrected. These were corrected and the lease was mailed back to Scenic Bay. At this time, Scenic Bay does not have a consummated lease.

State Controller Williams stated that he would like the department to develop a statement for reasonable rates that would be implemented as part of policy for float home marinas. He asked that this be presented at the January 20, 1999 meeting. There were no objections.

12. Military Lease – Portion of Gowan 40 - Presented by Bryce Taylor, Bureau Chief, Range Management/Surface Leasing

Mr. Taylor provided the background information. Idaho's Military Division has applied to lease six acres of Public Building Endowment land adjacent to their military base at Gowen Field. They would fence the property to increase security and use it for a motor pool, training area, or other military purposes.

The land is currently unleased. It has been approved by the legislature for long-term leases for commercial purposes; however, the department has not received or requested board approval for any commercial proposals for this property.

The department recommended to approve a ten-year lease to Idaho Military Division on six acres of Public Building land at $18,000/year adjusted annually by the CPI-U and appraised each five years to insure rent is keeping pace with time.

General Kane stated that the Military would like a 2-3 year lease at $5,000 per year. The Military would like to arrange to purchase the property outright. He stated that the Military is currently maintaining the property.

State Controller Williams stated that Gowen Field is a huge economic engine. This area should be part of the base. Governor Batt asked General Kane what the facilities at Gowen Field are worth. General Kane said the physical plant worth at Gowen Field, including equipment that is located there, is about 1.2 billion dollars.

State Controller Williams made a motion to allow the military to have a short-term lease of up to three years for $5,000 annually. Secretary of State Cenarrusa seconded the motion. The motion carried on a vote of 5-0.

Superintendent Fox informed the Land Board that her department has been working with the National Guard in looking at an opportunity for students from other parts of the state to come and stay in the facilities at Gowen Field. This would be for a reasonable rate and allow the students to have a site to live while they tour the Capital, see the Governor, etc. She said General Kane's office was outstanding in assisting to put this packet together.

13. Reconsideration of qualified applicant status – O.L. Dudley – expiring grazing lease #G-6597 - Presented by Tracy Behrens, Range Management Specialist

Tracy Behrens provided the background information. The department provided options for the Land Board to consider. They are as follows:

1. Reaffirm the September Board action that qualifies Mr. Dudley as an applicant for the portion of the state parcel on the north side of the Boise River and rejects his application for the land on the south side of the river.

2. Reverse the September Board action and qualify Mr. Dudley to bid for the lease on the state land on the south side of the river. This option should include granting IWP an additional opportunity to submit a management proposal for consideration by the Board before an auction is scheduled

3. Vacate the September Board action that was taken on all three of the applications that were submitted on expiring lease G-6579 and begin the lease renewal process anew.

Secretary of State Cenarrusa made a motion that the Land Board take option #3 to vacate the September Board action that was taken on all three of the applications that were submitted on expiring lease G-6579 and begin the lease renewal process anew. He included in the motion that after HB643 goes into effect, the Land Board could proceed to sell this property. State Controller Williams seconded the motion. The vote carried on a vote of 4-0 with Attorney General Lance abstaining from the vote.

14. Request for final approval to complete a land exchange between the State of Idaho and Jim Reininger - Presented by Dan Spanfelner, Real Estate Specialist

Dan Spanfelner provided the background information. Jim and Connie Reininger, in coordination with the Southwest Area Office have proposed an exchange of state of Idaho land for private land generally located between Boise and Idaho City.

The private land consists of 40 acres and is considered to be a good growing site for timber. The timber is mostly Ponderosa Pine with an estimated volume of 166 MBF. The parcel has access from a logging road.

Governor Batt asked if the state would retain the mineral rights. Mr. Spanfelner informed the Land Board that the state of Idaho would reserve minerals on the State land.

The department recommended final approval of this land exchange.

The motion was made by Superintendent Fox and seconded by Secretary of State Cenarrusa to accept the recommendation of the department. The motion carried on a vote of 5-0.

16. Director's Salary

Governor Batt stated that the Land Board agreed earlier to revisit the Director's Salary issue. The motion was made by Secretary of State Cenarrusa to adjust the Director's Salary as scheduled in the earlier meeting. State Controller Williams seconded the motion. The motion carried on a vote of 5-0.

Prior to the Information Agenda, Stephanie Balzarini, Deputy Attorney General provided the Land Board with updated information regarding the Dupont Dock case. She informed the Land Board that the City of Coeur d'Alene has filed an appeal on the District Court decision in the Dupont matter. They also moved to stay the District Court decision, which would, if granted, affect the department's ability to conduct additional administrative proceedings. She asked for

confirmation on the direction the Land Board would choose to take. She stated that her understanding from the informal discussion last month was that the Board was inclined to proceed with additional administrative proceedings. She stated that Director Hamilton would need direction from the Land Board to initiate those proceedings. Along with that, the department would need to oppose the City of Coeur d'Alene's motion to stay the District Court decision.

Attorney General Lance made the motion to follow the recommendation of counsel. Secretary of State Cenarrusa seconded the motion. The motion carried on a vote of 5-0.

INFORMATION AGENDA

Director Hamilton briefed the Land Board on the information issues. He stated that the contract work on Triumph Mine is proceeding nicely. Work will cease shortly for the winter months and start again in the spring. Everything that had been scheduled is in progress.

17. Timber sale activity report
18. Interest rate update
19. Triumph Mine cleanup update

Secretary of State Cenarrusa commended Governor Batt for his work on Land Board during his time in office. He also commended Superintendent Fox for her diligence and commitment to the Board.

Attorney General Lance and State Controller Williams echoed the Secretary of State's comments.

Governor Batt and Superintendent Fox expressed their pleasure at serving on the Land Board.

There being no further business to come before the Land Board, the meeting adjourned at 12:00 noon.

IDAHO STATE BOARD OF LAND COMMISSIONERS

President, State Board of Land Commissioners and
Governor of the State of Idaho

Pete T. Cenarrusa
Secretary of State

Stanley F. Hamilton
Director

Exhibit 11

Land Bd. Meeting Minutes

(June 12, 2007)

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

Final Minutes
Regular Land Board Meeting
June 12, 2007

The regular meeting of the Idaho State Board of Land Commissioners was held on Tuesday, June 12, 2007 in Boise, Idaho. The meeting began at 9:12 a.m. in the second floor courtroom of the Borah Post Office building. The Honorable Governor C. L. "Butch" Otter presided. The following members were present:

Honorable Secretary of State Ben Ysursa – via conference phone
Honorable Attorney General Lawrence G. Wasden
Honorable State Controller Donna M. Jones
Honorable Superintendent of Public Instruction Tom Luna

Secretary to the Board Director George Bacon

- **CONSENT**

A motion was made by Attorney General Wasden to approve the Consent Agenda in its entirety. Controller Jones seconded the motion. The motion carried on a vote of 5-0.

1. **Director's Report** – *approved*

A. Interest Rate on Department Transactions – May 2007
B. Timber Sale Official Transactions - April 24, 2007 through May 30, 2007
C. Timber Sale Activity Report – April 2007; May 2007
D. Legal Matter Summary
E. Bureau of Surface and Mineral Resources, Official Transactions – April 2007
F. Bureau of Real Estate, Official Transactions – Easement – April 2007
G. Bureau of Real Estate, Official Transactions – Land Sale – April 2007

2. **Timber Sales** – *Staffed by Roger Jansson, Operations Chief-North, and Steve Douglas, Operations Chief-South* – *approved*

NORTH OPERATIONS

A.	Midbugs Over	CR-10-0351	1,035 MBF	Bonner
B.	Horton Hunt Divide	CR-10-0362	4,200 MBF	Bonner
C.	Caribou Chop	CR-10-0371	7,300 MBF	Bonner
D.	Beaver Dam	CR-21-3013	3,300 MBF	Boundary
E.	Log Power	CR-30-0490	7,270 MBF	Shoshone
F.	Two-Bit	CR-30-0521	2,270 MBF	Shoshone
G.	Stove Creek	CR-41-0023	3,190 MBF	Latah
H.	Upper Brush Creek	CR-41-0033	4,525 MBF	Latah

SOUTH OPERATIONS

I.	Dent Garden Poles	CR-40-0796	155 MBF 169,780 LF	Clearwater
J.	Northwest Passage	CR-60-0172	7,060 MBF	Boise
K.	West Dry Buck	CR-60-0174	2,900 MBF	Boise

DISCUSSION: Director Bacon highlighted sales C and D. Both sales require helicopter yarding. The Department is requesting the Board's permission to reappraise and offer the sales again without returning to the Board should the sales not sell at the first offering. This is a tactic the Department has used in the past with perishable timber. While this timber is not perishable, the timber market is declining. The benefit of not returning to the Board is potentially another month to get the sales turned around. If the sales do not sell, and the Department finds it is because of reasons other than market conditions, the Department would likely return to the Board.

3. **Request from the Idaho Park and Recreation Board to Authorize the Grant of an Easement at the Boise IDPR Headquarters** – *Staffed by Steve Strack, Office of the Attorney General* – *approved*

RECOMMENDATION: That the Board authorize the grant of a permanent easement to United Water Idaho for the construction of a pump house at IDPR headquarters property.

BOARD ACTION: Approved.

4. **Request from the Idaho Park and Recreation Board to Authorize the Endowment Fund Investment Board to Manage Investment of an Endowment – Ritter Island Unit of Thousand Springs State Park** – *Staffed by Steve Strack, Office of the Attorney General* – *approved*

RECOMMENDATION: That the Board authorize the Endowment Fund Investment Board to manage the Ritter Island Endowment Fund under such terms as the Endowment Fund Investment Board and the Parks Board determine are appropriate.

DISCUSSION: Controller Jones noted that the Endowment Board will be able to manage this additional responsibility with its current staff.

BOARD ACTION: Approved.

5. **State Participation as a Member of:** [*Staffed by Ron Litz, Assistant Director, Forestry and Fire*] – *approved*

A. Southern Idaho Timber Protective Association
B. Clearwater-Potlatch Timber Protective Association

DEPARTMENT RECOMMENDATION: That the Board authorize the Department to continue to participate as a member of the Southern Idaho Timber Protective Association.

BOARD ACTION: Approved.

6. **Authorization for Issuance of Deficiency Warrants to Pay Fire Suppression Costs in Fiscal Year 2008** – *Staffed by Brian Shiplett, Chief, Bureau of Fire Management* – *approved*

DEPARTMENT RECOMMENDATION: That the Board authorize the Department to issue deficiency warrants necessary to pay fire suppression costs beyond the $131,300 appropriation for fiscal year 2008.

BOARD ACTION: Approved.

7. **Minutes** – *approved*

A. Regular Land Board Meeting – May 8, 2007

- **REGULAR**

8. **Endowment Fund Investment Board** – *Presented by Larry Johnson, Manager of Investments*

A. EFIB Manager's Report
B. Investment Report

DISCUSSION: Mr. Johnson reported that:

- fiscal year-to-date returns are 17% through the end of May;
- the Agricultural College Endowment Fund has moved to 100% bonds;
- an investment consultant, Callan Associates, has been selected;
- managers are performing as expected.

BOARD ACTION: A motion was made by Controller Jones to move that the report be accepted as presented. Attorney General Wasden seconded the motion. The motion carried on a vote of 5-0.

9. **Acquisition of St. Maries Compound** – *Presented by Kathy Opp, Division Administrator, Support Services* – *withdrawn*

DEPARTMENT RECOMMENDATION: That the Board approve the Department's request to encumber one hundred and twenty thousand dollars ($120,000) from the 2007 or 2008 budget, as available.

DISCUSSION: Governor Otter asked if the Department does not plan to acquire this property, will the Department look for a different place or continue to lease the current site. Director Bacon stated the Department will review different purchase options. Governor Otter asked about the difference in appraisals. Director Bacon stated the appraisals could be anywhere from $300,000 for residential development and $600,000 for commercial development. The appraisal used by the Department was completed several years ago and was inflated by the Consumer Price Index. However land values are rising rapidly in certain areas of the state. Governor Otter asked if the Department is anticipating the rent increasing to reflect the higher return on investment for the city. Director Bacon stated the city may not have the option to increase the rent during the lease term.

BOARD ACTION: By unanimous consent, this agenda item was withdrawn.

10. **IDL Executive Staff Reorganization** – *Presented by George Bacon, Director*

DEPARTMENT RECOMMENDATION: Approve the Director's request to initiate phase one of the proposed reorganizational plan, and direct the Department to take the necessary steps to achieve phase two as soon as reasonably practicable.

DISCUSSION: Attorney General Wasden asked how members of the public have received this proposal. Director Bacon stated he has discussed the proposal with a couple of customers. The timber industry most notably said they would be supportive. Director Bacon stated he does not believe the public will see any change because the public interfaces with field staff, and those changes will not be made at this time.

Governor Otter asked if the proposed Deputy Director position will be exempt status. Director Bacon stated the deputy director position will be an exempt, non-classified position serving at the will of the Director.

Attorney General Wasden noted that Director Bacon has received some very specific directives from the Board about how to go about change at the Department of Lands preparing for the future. He asked Director Bacon if this proposal is a significant part of the plan to make those changes. Director Bacon stated yes. He added that last month the Board finalized his work plan, and this was one of the items specified in the plan.

BOARD ACTION: A motion was made by Controller Jones to approve the Director's request to initiate Phase I of the proposed reorganizational plan. Attorney General Wasden seconded the motion. The motion carried on a vote of 5-0.

11. Subcommittee Report – Review of Lease Terms and Floathome Moorage Rate Structure – *Presented by Donna Jones, Subcommittee Chair*

SUBCOMMITTEE RECOMMENDATION: (1) The subcommittee recommends that the Board rescind the second paragraph of the July 6, 1999 "Maintenance and Moorage Rate Facility Policy" related to floathome moorage rates, thereby allowing the market and individual commercial operator's business situations to establish floathome moorage rates; (2) The subcommittee recommends that if the portion of the Board policy related to floathome moorage rates is rescinded, that the remaining portions of the policy stay in place under the new title of "Marina Maintenance Policy" in order to protect public trust values; (3) The subcommittee also recommends that the Board direct the Department to issue a letter to the floathome owners and commercial marina operators clarifying the Board's position on this matter and its authority relative to the Floating Homes Residency Act.

DISCUSSION: A transcript is available upon written request to Susan Terry, Idaho Department of Lands, 954 West Jefferson, Boise, Idaho 83720-0050, (208) 334-0242, sterry@idl.idaho.gov.

BOARD ACTION:

- A motion was made by Controller Jones to move the recommendations as presented at the May 8, 2007 regular meeting of the Board. Attorney General Wasden seconded the motion.
- During further discussion of the motion, Attorney General Wasden suggested that the Board consider adding a directive to the Department to include reasonableness language into the contracts to allow the Board enforcement ability. Secondly, Attorney General Wasden suggested that this matter be addressed jointly with the Legislature, recognizing the respective responsibilities and authorities of the Board and the Legislature, in the hope that a tolerable solution may be found.
- Superintendent Luna commented that if the Board is seeking further discussions, he would feel more comfortable reviewing the products of those discussions as a total package.
- Controller Jones asked Superintendent Luna if he was amending the motion. Superintendent Luna stated yes. For clarification, Governor Otter restated Superintendent Luna's amended motion that the Board adopt number one of the recommendations made at the last Board meeting with the amendment thereto that the Board review the limitations imposed by the State thereby limiting the market place and the availability of moorages. Superintendent Luna stated by his amendment he was recommending that the Board not adopt anything at this time. Superintendent Luna stated he wants to review the whole package in one series of recommendations and not one part now and then more later.
- Attorney General Wasden asked permission of the maker of the motion to withdraw his second and to make a separate motion. Controller Jones consented. Governor Otter noted the motion has been withdrawn.

- Attorney General Wasden moved to direct the Department to implement a policy of reasonable rates through inclusion of appropriate language in future marina leases and to request that the Legislature consider amendments to the Floathome Residency Act to address issues of fairness in floathome rental rates. Controller Jones seconded the motion.

- Governor Otter remarked that he would also like to have some definition indicating what needs to be considered when the term reasonableness is addressed.

- Superintendent Luna suggested an amendment to the motion to include a direction to the Department to perform an economic study of the forces in play when it pertains to the floathome and moorage relationship.

- Secretary of State Ysursa suggested including in that study the rate the State could be charging marina owners.

- Attorney General Wasden stated he has no objection to the amendment of his motion to include that the Department of Lands perform an economic analysis of the moorage rates and floathome circumstances that exist throughout the state. He asked Controller Jones if she would second the amended motion. Controller Jones seconded the amended motion.

- The amended motion carried on a vote of 5-0.

12. Cottage Site Lease Terms – *Presented by Mike Murphy, Chief, Bureau of Surface and Mineral Resources*

DEPARTMENT RECOMMENDATION: That the Board approve the draft lease document for use with the two new cottage site leases at Priest Lake set for auction in August 2007.

DISCUSSION: A transcript is available upon written request to Susan Terry, Idaho Department of Lands, 954 West Jefferson, Boise, Idaho 83720-0050, (208) 334-0242, sterry@idl.idaho.gov.

BOARD ACTION: Attorney General Wasden moved that the Board delay the determination on the cottage site lease terms for the period of one month. During that delay, Attorney General Wasden requested that the proposed lease be reviewed by the Contracts and Administrative Law Division of the Office of the Attorney General. This Division has expertise in lease terms. Secondly, Attorney General Wasden moved that the Department provide public input, primarily from the Priest Lake Lessee Association, on the proposed lease terms. Controller Jones seconded the motion. The motion carried on a vote of 5-0.

13. Request for Adoption of Formal Policy Regarding Reservation of 25-foot Wide Public Use Right-of-Way Along Navigable Rivers – *Presented by George Bacon, Director*

DEPARTMENT RECOMMENDATION: Consistent with the recommendation as presented at the March 13, 2007 Board meeting, direct the Department to reserve a 25-foot wide public use right-of-way along navigable rivers when issuing Disclaimers of Interest, while allowing the Department to propose alternatives to the Land Board due to unusual circumstances. Alternatives to the 25-foot wide public use right-of-way will be presented to the Land Board for approval.

DISCUSSION: A transcript is available upon written request to Susan Terry, Idaho Department of Lands, 954 West Jefferson, Boise, Idaho 83720-0050, (208) 334-0242, sterry@idl.idaho.gov.

BOARD ACTION: A motion was made by Attorney General Wasden to move the adoption of the suggested formal policy regarding reservation of a 25-foot wide public use right-of-way along navigable rivers. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 3-2, with Governor Otter and Superintendent Luna voting nay.

14. Wood River Land Trust Land Exchange – *Presented by Perry Whittaker, Chief, Bureau of Real Estate*

DEPARTMENT RECOMMENDATION: That the Board direct the Department to work with the WRLT to complete this exchange. Completion of the exchange requires the expenditure of $50,000 of land bank funds to equalize the exchange values.

DISCUSSION: None.

BOARD ACTION: A motion was made by Controller Jones to move the Department's recommendation. Superintendent Luna seconded the motion. The motion carried on a vote of 5-0.

- **INFORMATION**

No Land Board action is required on the Information Agenda.

15. Conflicted Grazing Leases – *Staffed by Tracy Behrens, Program Manager, Grazing/Cropland*

DISCUSSION: Attorney General Wasden suggested that the Board form a subcommittee to examine the process of grazing lease conflict auctions. He noted that while this review is part of the Board's specific assignment to Director Bacon, he believes a subcommittee review may help the Board provide guidance to the Department as well as preparing the Board to address this matter in the future.

Governor Otter agreed with Attorney General Wasden's suggestion and appointed Attorney General Wasden as the Chairman of the subcommittee. In addition, Governor Otter volunteered to serve as a member of the subcommittee. Director Bacon informed the Board that the Department has formed a Livestock Workgroup that this subcommittee could tie into. The Livestock Workgroup is made up of representatives of the grazing industries, the Wool Growers and the Cattlemen's Association, as well as the University of Idaho and the Farm Bureau.

16. 2008 Cottage Site Rent Adjustments – *Staffed by Mike Murphy, Chief, Bureau of Surface and Mineral Resources*

DISCUSSION: A transcript will be available upon written request to Susan Terry, Idaho Department of Lands, 954 West Jefferson, Boise, Idaho 83720-0050, (208) 334-0242, sterry@idl.idaho.gov.

Governor Otter noted that during public testimony a suggestion was made that the Board appoint a subcommittee to review this matter further. In light of that suggestion, Governor Otter appointed Secretary of State Ysursa to serve as the Chairman of the subcommittee with Superintendent Luna appointed to serve as a subcommittee member.

17. Fire Protection Program Overview – *Staffed by Jim Newton, Fire Business Program Manager*

At 12:35 p.m. Attorney General Wasden left the meeting. At 12:37 p.m. Governor Otter left the meeting. Controller Jones presided in Governor Otter's absence.

At 12:40 p.m., Controller Jones requested a motion to resolve into Executive Session. A motion was made by Superintendent Luna to resolve into Executive Session. Governor Otter returned to the meeting at 12:41 p.m. The motion carried by unanimous consent of those present, and the Board resolved into Executive Session.

- **EXECUTIVE SESSION**

A. To Consider Personnel Matters [Idaho Code § 67-2345(1)(b)]

B. To Acquire An Interest in Real Property which is not owned by a Public Agency [Idaho Code § 67-2345(1)(c)

C. To Consider Records that are Exempt from Disclosure [Idaho Code § 67-2345(1)(d)]

D. To Consider and Advise Its Legal Representatives in Pending Litigation or Where There is a General Public Awareness of Probable Litigation [Idaho Code § 67-2345(1)(f)]

At 12:50 p.m. a motion was made by Superintendent Luna to resolve into Regular Session. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 4-0, with Attorney General Wasden absent for this vote.

There being no further business to come before the Board, the meeting adjourned at 12:50 p.m.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ C. L. "Butch" Otter
President, State Board of Land Commissioners and
Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ George B. Bacon
George B. Bacon
Director

The above-listed final minutes were approved by the State Board of Land Commissioners at the July 10, 2007 regular Land Board meeting.

Exhibit 12

Land Bd. Meeting Minutes

(Dec. 4, 2007)

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

Final Minutes
Special Land Board Meeting
December 4, 2007

A special meeting of the Idaho State Board of Land Commissioners was held on Tuesday, December 4, 2007 in Boise, Idaho. The meeting began at 9:05 a.m. in the second floor courtroom of the Borah Post Office building. The Honorable Governor C. L. "Butch" Otter presided. The following members were present:

Honorable Secretary of State Ben Ysursa
Honorable Attorney General Lawrence Wasden
Honorable Superintendent of Public Instruction Tom Luna
Honorable State Controller Donna Jones

Secretary to the Board Director George Bacon

- **REGULAR SESSION**

1. Consideration of Payette Lake Lease Rate Amendment for 2008

BOARD ACTION: A motion was made by Secretary of State Ysursa that the Board, for one year only, limit the 2008 rates at Payette Lake to a 25% increase over the 2007 rates. Controller Jones seconded the motion.

Prior to a vote being taken, and upon further discussion, Superintendent Luna put forward a substitute motion that the Board, for one year only, and at Payette Lake only, freeze the 2008 rates at the 2007 value. Attorney General Wasden seconded the substitute motion. The substitute motion carried on a vote of 5-0.

A transcript is available upon written request to Susan Terry, Idaho Department of Lands, 300 North 6th Street, Suite 103, Boise, Idaho 83720-0050.

At 9:28 a.m. there being no further business to come before the Board, a motion was made by Controller Jones to adjourn. Attorney General Wasden seconded the motion. The motion carried on a vote of 5-0. Meeting adjourned.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ C. L. "Butch" Otter
President, State Board of Land Commissioners and
Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ George B. Bacon
George B. Bacon
Director

The above-listed final minutes were approved by the State Board of Land Commissioners at the January 17, 2008 regular Land Board meeting.

Exhibit 13

Land Bd. Meeting Minutes

(June 19, 2008)

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

State Board of Land Commissioners
Regular Meeting – June 19, 2008
Final Minutes
Meeting Held Off-site at Idaho State University, Pocatello

The June 19, 2008 regular meeting of the State Board of Land Commissioners was held on the campus of Idaho State University, Pocatello, Idaho.

The Idaho Department of Lands manages state endowment lands. When Idaho achieved statehood in 1890, over three and one-half million acres of land were granted to the state by the federal government to support public schools and other designated beneficiary institutions.

Of the endowment beneficiaries, the Normal School Fund (Idaho State University Department of Education and Lewis-Clark State College) and the Charitable Institutions Fund (Idaho State University Industrial Training School, State Hospital North, Idaho Veterans Homes and the School for the Deaf and Blind) jointly own about 137,499 acres. Our founding fathers outlined the purpose of endowment lands in Article 9, Section 8 of Idaho's Constitution. These lands are to be managed "in such manner as shall secure the maximum long-term financial return to the institution to which granted." Income is primarily generated through timber sales, livestock grazing, mining and other commercial ventures, such as communication sites, office buildings, parking lots and ski resorts.

The Idaho Constitution also established the State Board of Land Commissioners to oversee endowment land management. The Board consists of the Governor, Secretary of State, Attorney General, Superintendent of Public Instruction and the State Controller. The Land Commissioners act in the capacity of trustees on behalf of the beneficiary institutions.

On behalf of the Land Board, Governor Otter, Controller Jones and Secretary of State Ysursa presented Dr. Kent Tingey, Vice President for University Advancement, with a facsimile check in the amount of $2,020,677. The check represents the contribution of endowment land management to Idaho State University's fiscal year 2009 budget.

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

Final Minutes
Regular Land Board Meeting
June 19, 2008

The Idaho State Board of Land Commissioners meeting began at 9:00 a.m. in the Rendezvous Suite, Building 38, 921 South 8th Avenue, Pocatello, Idaho. The Honorable Governor C. L. "Butch" Otter presided. The following members were present:

Honorable Secretary of State Ben Ysursa
Honorable Attorney General Lawrence Wasden (via conference phone)
Honorable State Controller Donna Jones

Secretary to the Board George Bacon

Superintendent Luna was absent for this meeting. Attorney General Wasden joined the meeting by conference phone at 9:20 a.m.

- **CONSENT**

A motion was made by Secretary of State Ysursa to approve the Consent Agenda in its entirety. Controller Jones seconded the motion. The motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.

1. Director's Report – *approved*

A. Interest Rate on Department Transactions – June 2008
B. Timber Sale Activity Report
C. Timber Sale Official Transactions
D. Legal Matter Summary
E. Bureau of Surface and Mineral Resources, Official Transactions – April 2008
F. Bureau of Real Estate, Official Transactions, Land Sale – April 2008
G. Bureau of Real Estate, Official Transactions, Easement – April 2008
H. Fire Settlement Information

DISCUSSION: Director Bacon noted that item B includes a graph showing monthly stumpage prices. The graph shows that stumpage prices for timber are fairly strong but have dipped down to 2003-2004 levels with the current economic downturn.

Governor Otter stated he has heard that housing market prices may come back in the second quarter of 2009. He noted that lumber prices started dropping at the same time that the housing market started to fall. He asked if the Department anticipates stumpage prices to come back in the second *quarter* of 2009. Director Bacon stated yes. In his experience over the last thirty years when the economy softens, the timber industry is usually one of the first to decline and is an indicator that the general

economy will follow shortly. He feels that occurred again this time. Decreasing prices have been seen over the last couple of years. Director Bacon added, however, that when the economy rebounds, the timber industry is also one of the last to see the effects of a rebound. Governor Otter asked if Director Bacon anticipates any management changes, cut schedules or other actions being taken to try to balance the downturn. Director Bacon stated the Department is working on recommendations to be presented to the Board in April 2009.

Governor Otter expressed concern about falling farther behind on the cut and, subsequently, the maturity of the stands. He expressed interest in having the Department convince the Board that any cuts should be held off the market. He believes management practices should not be changed simply to respond to the market. Director Bacon agreed and stated the Department will update the Board in the coming months on the status of the timber harvest analysis. The Department believes that some action needs to be taken to reduce stocking regardless of what is going on with the markets. The Department will bring forward recommendations for an increased harvest to keep the forest healthy and to do the right thing on the ground.

2. **Timber Sales** – *Staffed by Roger Jansson, Operations Chief-North, and Kurt Houston, Operations Chief-South* – ***approved***

NORTH OPERATIONS				
A. Lower Trapper Poles	CR-10-0377	305	MBF	Bonner
		84, 875	LF	Bonner
B. POL Poles 2008	CR-20-0263	420	MBF	Bonner
		166,630	LF	Bonner
C. Trail Mix	CR-21-3017	4,495	MBF	Boundary
D. Mica Widespread OSR	CR-22-5010	2,600	MBF	Kootenai
E. D and D Pole	CR-30-0550	800	MBF	Benewah
		187,635	LF	Benewah
F. Lo-ol OSR	CR-30-0551	7,109	MBF	Benewah/Shoshone
SOUTH OPERATIONS				
G. Captain John Fuel Break	CR-43-4112	3,385	MBF	Nez Perce
H. Beavertail	CR-50-0128	5,540	MBF	Valley
I. Spruced-Up Hat	CR-50-0136	4,645	MBF	Idaho
J. East Fork Shorts	CR-50-0144	2,905	MBF	Idaho
K. South Williams	CR-60-0177	5,285	MBF	Elmore

DISCUSSION: Governor Otter expressed concern that all of the southern timber sales are more than a hundred miles from the closest log mill and are not doing well. He suggested projecting sale information so a potential investor might consider retrofitting one of the closed mills. He encouraged the Department to contact the timber industry to investigate this scenario. Director Bacon stated the Department will contact the timber industry. Some studies have been completed on the south Idaho timber supply and a big issue is the lack of activity on federal lands. Director Bacon stated the Department will also contact the Idaho Department of Commerce to see if there are opportunities for incentives.

3. **Authorization for Issuance of Deficiency Warrants to Pay Fire Suppression Costs in Fiscal Year 2009** – *Staffed by Brian Shiplett, Chief, Bureau of Fire Management*

DEPARTMENT RECOMMENDATION: Authorize the Department to issue deficiency warrants necessary to pay the fire suppression costs beyond the $231,800 appropriation for fiscal year 2009.

BOARD ACTION: Approved.

4. **State Participation as a Member of:** *[Staffed by Brian Shiplett, Chief, Bureau of Fire Management]*

A. Southern Idaho Timber Protective Association
B. Clearwater-Potlatch Timber Protective Association

DEPARTMENT RECOMMENDATION: That the State continue to participate as a member of the Southern Idaho Timber Protective Association.

BOARD ACTION: Approved.

5. **IDL Strategic Plan FY 2009-FY 2012** – *Staffed by Patrick Hodges, Division Administrator, Support Services*

DEPARTMENT RECOMMENDATION: Direct the Department to submit the FY 2009-FY 2012 Strategic Plan to the Division of Financial Management by the July 3, 2008 deadline.

DISCUSSION: Governor Otter stated that last year the Board expressed the importance of establishing in the public mindset the difference between endowment lands and public lands and how the Board's fiduciary responsibility on endowment lands is directed by the Idaho Constitution and not necessarily by the will of the public. He reaffirmed his desire that the Department continue with this effort.

BOARD ACTION: Approved.

6. **Minutes – *approved***

A. Regular Land Board Meeting – May 15, 2008

- **REGULAR**

7. **Endowment Fund Investment Board Manager's Report** – *Presented by Andy Potter, EFIB*

A. Monthly Report

The Endowment Fund will meet on August 11 to develop a recommendation on distributions to the beneficiaries for Fiscal Year 2010. The Land Board will be asked to set the FY2010 distributions at its August 19, 2008 regular meeting. Guidelines proposed by the EFIB are included in the endowment fund section of the asset management plan.

B. Investment Report

For fiscal year through May 31 the Fund was up 2.8% and is ahead of its benchmark for the fiscal year. All managers are performing as expected.

C. Asset Management Plan – Endowment Fund Section

For the past two years, the EFIB has been developing a comprehensive set of workable guidelines to govern the administration of all endowment assets to ensure the fulfillment of the constitutional mandate to maximize the long-term revenues for the beneficiaries. The final land management sections were approved at the December 2007 meeting. The only section that remains to be completed is one that deals with the management of the financial assets of the endowments. Attachment 1 is a proposed section on endowment fund management for the Land Board's review and comment. Included in the financial asset section is a proposed policy on distribution to beneficiaries. The EFIB will use this to make recommendations to the Land Board at the August meeting. Approval is not being requested at this time, but comments and questions are welcome. A final draft of this section will be presented to the Land Board for approval at the July 17 meeting.

No action was taken on this agenda item.

8. **Request to Clear Property Title by the Idaho Department of Fish and Game** – *Presented by Gregg Servheen, Wildlife Program Coordinator, Idaho Department of Fish and Game*

DEPARTMENT RECOMMENDATION: Allow the Idaho Department of Fish and Game to clear title of property by approving quitclaim deeds to landowners Timm Johnson and Earl Wuthrich.

DISCUSSION: None.

BOARD ACTION: A motion was made by Secretary of State Ysursa to adopt the Department's recommendation. Controller Jones seconded the motion. The motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.

9. **2009 Rent Changes for the Payette Lake and Priest Lake Cottage Sites** – *Presented by Mike Murphy, Chief, Bureau of Surface and Mineral Resources, IDL*

DEPARTMENT RECOMMENDATION: That the Board apply the rent increase to the 2009 Payette Lake cottage site rent consistent with the 2008 Valley County Assessed values. The Department also recommends that the Board apply the indexing method to the Priest Lake cottage sites as outlined in the cottage site lease for the 2009 rent at the Columbia Valuation Group recommended rate of 23%.

DISCUSSION: A verbatim transcript will be available upon written request to Susan Terry, Department of Lands, Post Office Box 83720, Boise ID 83720-0050. An electronic version of the transcript can be requested by email to sterry@idl.idaho.gov.

BOARD ACTION: A motion was made by Secretary of State Ysursa to raise the rate for cottage site rent across the board for next year at fifteen percent for waterfront and secondary lots at Payette Lake and lakefront lots at Priest Lake. Controller Jones seconded the motion for discussion purposes. Controller Jones noted that Secretary of State Ysursa indicated a need for additional time to continue reviewing this matter. She asked that Secretary of State Ysursa amend his motion to a time certain. Secretary of State Ysursa amended his motion that the Board raise the rate for cottage site rent across the board fifteen percent with the proviso that the subcommittee will report back to the Board on or before December 1, 2008, with a new methodology on price. Controller Jones seconded the amended motion. The amended motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.

At this point, the Board moved forward to Executive Session. At 10:30 a.m., a motion was made by Controller Jones to resolve into Executive Session pursuant to Idaho Code §§ 67-2345 (1)(b) and (1)(f) for the purpose of evaluating an employee and to communicate with legal counsel regarding pending litigation. The motion carried by unanimous consent.

- **EXECUTIVE SESSION**

A. To consider the evaluation, dismissal or disciplining of, or to hear complaints or charges brought against, a public officer, employee, staff member or individual agent, or public school student; [Idaho Code § 67-2345(1)(b)]

B. ~~To conduct deliberations concerning labor negotiations or to acquire an interest in real property which is not owned by a public agency; [Idaho Code § 67-2345(1)(c)]~~ - **WITHDRAWN**

C. To communicate with legal counsel for the public agency to discuss the legal ramifications of and legal options for pending litigation, or controversies not yet being litigated but imminently likely to be litigated. The mere presence of legal counsel at an executive session does not satisfy this requirement. [Idaho Code § 67-2345(1)(f)]

At 11:03 a.m., the Board resolved into Regular Session by unanimous consent. The Executive Session was conducted pursuant to Idaho Code § 67-2345 (1)(b) and (1)(f) for the purpose of evaluating an employee and to communicate with legal counsel regarding pending litigation. No action was taken by the Board during the Executive Session.

BOARD ACTION UPON RETURN TO REGULAR SESSION

At 11:05 a.m., a motion was made by Controller Jones that the salary of Director Bacon be increased to policy. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.

At 11:07 a.m., Attorney General Wasden left the meeting.

For the record, Governor Otter complimented Director Bacon for doing a tremendous job in meeting expectations and for executing strategy, including the management of the resource base and personnel and for the strategic plan for the future. Director Bacon has demonstrated creativity in his efforts to increase the maximum return from the endowment assets of the state. Secretary of State Ysursa and Controller Jones concurred with Governor Otter's remarks.

- **INFORMATION**

Background information was provided by presenters as indicated below. No Land Board action is required on the Information Agenda.

10. Minerals Program Presentation – *Presented by Eric Wilson, Program Manager, Navigable Waters/Minerals Regulatory Program and Sharon Murray, Program Manager, Minerals Leasing, Bureau of Surface and Mineral Resources, IDL*

DISCUSSION: Governor Otter asked how the Department will handle leases on solar and wind. Director Bacon stated those activities are identified in the asset management plan as revenue sources, and it appears there are numerous opportunities in the future. In coordination with the Western States Land Commissioners, the Department has developed a draft lease that is currently under review by the Attorney General's office. The lease identifies royalties, payments and production requirements. A couple of projects are being floated around the state that will involve endowment land if the projects are allowed to go forward. Generally the state will be a minor player because of the disposition of the state land. Transmission lines are also incorporated into the lease language, as are outbuildings, maintenance sheds, access roads and substations. Director Bacon added that once the Attorney General's office provides their comments and the lease is finalized, the Department will be ready to move forward, and the timing may be right.

11. Idaho Admissions Act, Section 7 and Sale of Federal Public Land – *Presented by Bob Brammer, Assistant Director, Lands, Minerals, Range*

DISCUSSION: Secretary of State Ysursa noted BLM recently sold some tracts of land around Council. He asked how and when the state receives the money from BLM. Mr. Andy Potter responded that the EFIB receives the money from the Idaho Treasurer on a yearly basis, usually in late November or early December.

Governor Otter expressed support for the APPLE bill. He stated the west would be the largest benefactor of the bill, and he believes Idaho should be allowed to select five percent of available non-encumbered lands, which can not be tribal, wilderness or set aside lands. Governor Otter's calculation shows that five percent of available Idaho lands would translate to 1.5 million acres. He suggested that the Department discuss and show support for the APPLE bill during the upcoming Western States Land Commissioners' meeting. Governor Otter will also discuss and seek support for this bill at the upcoming Western Governors' Association meeting.

12. Timber Sale Revenue Forecast – *Presented by Bob Helmer, Chief, Bureau of Forest Management*

DISCUSSION: Governor Otter noted that between the stumpage only and the stumpage plus estimated contract interest for 2009, the interest rate appears to be approximately twelve and a half percent. He asked if that is the kind of interest rate charged by the Department. Mr. Helmer stated the Department charges six percent, but the total amount of interest depends on the length of time that the purchaser holds the sale. The length of time makes a definite difference in the Department's receipts.

Upon conclusion of the Information Agenda, a Department of Lands' employee award presentation was held.

Director Bacon and Deputy Director Opp presented Bob Helmer, Chief, Bureau of Forest Management, with a special award for excellence in executive leadership. Bob was honored for his work on the Asset Management Plan Committee, chairmanship of the right-of-way committee, oversight of the development of the Forest Asset Business Plan and leadership in the Department's timber market and harvest level studies. In addition, Bob was honored for being one of the Department's lead fire investigators.

At 11:41 a.m., a motion was made by Secretary of State Ysursa to adjourn. Controller Jones seconded the motion. The motion carried on a vote of 3-0, with Attorney General Wasden and Superintendent Luna being absent for this vote. Meeting adjourned.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ C. L. "Butch" Otter
C. L. "Butch" Otter
President, State Board of Land Commissioners and
Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ George B. Bacon
George B. Bacon
Director

The above-listed final minutes were approved by the State Board of Land Commissioners at the July 17, 2008 regular Land Board meeting.

Exhibit 14

Land Bd. Meeting Minutes

(Dec. 16, 2008)

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

Final Minutes
Regular Land Board Meeting
December 16, 2008

The regular meeting of the Idaho State Board of land Commissioners was held on Tuesday, December 16, 2008, in Boise, Idaho. The meeting began at 9:42 a.m. in the second floor courtroom of the Borah Building. The Honorable Governor C. L. "Butch" Otter presided. The following members were present:

Honorable Secretary of State Ben Ysursa
Honorable Attorney General Lawrence Wasden
Honorable State Controller Donna Jones
Honorable Superintendent of Public Instruction Tom Luna

For the record, Governor Otter recognized the presence of a quorum.

- **CONSENT**

A motion was made by Attorney General Wasden to adopt the Consent Agenda in its entirety. Controller Jones seconded the motion. The motion carried on a vote of 5-0.

1. **Director's Report - *approved***

A. Interest Rate on Department Transactions – December 2008
B. Timber Sale Activity Report
C. Timber Sale Official Transactions – November 2008
D. Legal Matter Summary
E. Bureau of Surface and Mineral Resources, Official Transactions – November 2008
F. Fire Settlement Information

DISCUSSION: Governor Otter asked if the Department has been contacted regarding possible infrastructure projects that the incoming Administration might consent to pursue, such as projects having a potential value for the wood products industry. Director Bacon stated his involvement has been general. Possible infrastructure projects could include public buildings or that type of activity. Construction could spur an earlier recovery for the lumber industry; however, he has not looked at that specifically.

2. **Timber Sales** – *Staffed by Roger Jansson, Operations Chief-North, and Kurt Houston, Operations Chief-South* – ***approved***

NORTH OPERATIONS				COUNTY	AREA OFFICE
None					
SOUTH OPERATIONS					
A. John Lewis Road	CR-40-0985	1,635	MBF	Clearwater	Clearwater (Orofino)

3. **Disclaimer of Interest for the Former Bed of the Boise River, Canyon County (W & H, LLC)** – *Staffed by Kurt Houston, Operations Chief-South* – ***approved***

DEPARTMENT RECOMMENDATION: That the Board direct the Department to issue a disclaimer of interest for one parcel totaling 95.357 acres of the former bed of the Boise River and require W & H, LLC to pay a fee of $600.00 to the Department of Lands for this transaction.

BOARD ACTION: Approved.

4. **Disclaimer of Interest for the Former Bed of the South Fork Payette River, Boise County (Bassford)** – *Staffed by Kurt Houston, Operations Chief-South* – ***approved***

DEPARTMENT RECOMMENDATION: That the Board direct the Department to issue a disclaimer of interest for one parcel totaling 0.67 acre of the former bed of the South Fork Payette River and require Dennis Bassford to pay a fee of $600.00 to the Department of Lands for this transaction.

BOARD ACTION: Approved.

5. **Minutes** – ***approved***

A. Regular Land Board Meeting – November 18, 2008

- **REGULAR**

6. **Audience with the Board – Doug Wilson, Court-Appointed Receiver, Tamarack, and Scott Turlington, Principle Strategic Advisors**

Doug Wilson, Court-Appointed Receiver for Tamarack Resort, was introduced to the Board by Scott Turlington of Principle Strategic Advisors. In addition, Mr. Turlington noted the presence in the audience of Jim Spence, Vice President of Operations, Tamarack Resort, Krista Freitag, Douglas Wilson Companies, and Attorney Bob Maynard, Perkins Coie.

A transcript for this agenda item is available by written, fax or email request to Susan Terry, Idaho Department of Lands, 300 North 6th Street, Suite 103, Boise, Idaho 83720-0050, fax (208) 334-2339, or email sterry@idl.idaho.gov.

No action was taken on this agenda item.

7. **Endowment Fund Investment Board Manager's Report** – *Presented by Larry Johnson, Manager of Investments, EFIB*

A. Monthly Report

- At the end of October, reserve balances remain at three years' worth of distributions for all endowments.
- The Investment Board met on November 18 and established a three-year plan to increase the endowment fund's commitment to international equities.
- In conjunction with the Treasurer's office, the Investment Board is working on legislation to clarify the process by which school bonds are guaranteed by the state and the Public School Endowment Fund. This allows schools to issue school bonds at lower interest rates.
- The EFIB is updating its forecast of earnings reserve funds for the next two to three years. The Department of Lands has provided a revised forecast of land revenues and harvest levels.

B. Investment Report

- Fiscal year-to-date returns: -25%, which includes a 4% loss in November.
- Investment managers are performing as expected.

C. *[Action Item]* Proposed Legislation – Compensation of the Endowment Fund Investment Board

EFIB Recommendation on Item C – PROPOSED LEGISLATION: That the Board endorse the proposed legislation on Investment Board compensation for enactment by the Legislature in the upcoming session.

DISCUSSION: Governor Otter asked how this legislation would impact benefits for EFIB members. Mr. Johnson replied that he was not familiar with benefits for board members. Governor Otter explained that he is currently conducting an inventory of boards and commissioners to determine what, if any, state employee benefits those members receive. Although he appreciates the hard work performed by boards and commissions, he believes benefits, such as PERSI, life insurance and medical insurance, should be reserved for full-time state employees.

Superintendent Luna asked if this item could be held to a later date so information, as mentioned by Governor Otter, could be collected.

Secretary of State Ysursa asked about the relevance of benefits to this proposed legislation. Governor Otter responded that sometimes many of the benefits are indexed against compensation. Some boards and commissions are not only part time, but serve very limited periods of time. In some cases members are receiving benefits from the state along with compensation. Currently a statewide policy is being developed for all boards and commissions.

Superintendent Luna stated that the cost of health benefits for state employees is approximately $9,200 per year. He asked if some members of boards or commissions receive, for example, $50 a month and in addition receive the full $9,200 health insurance benefit. Governor Otter responded he is trying to determine the answer to that question.

BOARD ACTION: A motion was made by Controller Jones that the Land Board endorse the proposed legislation on Investment Board compensation for enactment by the Legislature in the upcoming session. Secretary of State Ysursa seconded the motion. Prior to a vote being taken, Controller Jones offered an amended motion that approval is subject to clarification by the Division of Financial Management by the end of the day [December 16, 2008] to confirm that no benefits are being paid or affected. Secretary of State Ysursa seconded the amended motion. The amended motion carried on a vote of 5-0.

8. Authorization to Raise the Forest Fire Protection Assessment to the Maximum Allowed by Idaho Code – *Presented by David Groeschl, Assistant Director, Forestry and Fire*

DEPARTMENT RECOMMENDATION: That the Board raise the forest protection assessment to the maximum authorized by Idaho Code § 38-111 ($0.60/acre) and grant permission to the Department to seek a legislative sponsor to carry a bill for the above-recommended statute changes. **NOTE:** If the Legislature approves these statutory changes, IDL will seek Land Board approval to increase the improved parcel surcharge.

DISCUSSION: Secretary of State Ysursa commented that industry supports this agenda item. Director Bacon stated he would work with the constituent group to find a sponsor for the bill.

BOARD ACTION: A motion was made by Attorney General Wasden to move adoption of the Department recommendation to raise the forest protection assessment to the maximum currently allowed and authorized by Idaho Code § 38-111, that is sixty cents an acre, and also grant permission to the Department to seek a legislative sponsor to carry a bill for the recommended statute changes. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 5-0.

9. 2009 Cottage Site Rental Rates – *Presented by Mike Murphy, Chief, Bureau of Surface and Mineral Resources*

DEPARTMENT RECOMMENDATION: The Department recommends that the fifteen percent (15%) rent increase for 2009 at both Payette Lake and Priest Lake be maintained as adopted by the Land Board on June 9, 2008.

*[**For Reference** – June 19, 2008 Board Action: A motion was made by Secretary of State Ysursa to raise the rate for cottage site rent across the board for next year at fifteen percent for waterfront and secondary lots at Payette Lake and lakefront lots at Priest Lake. Controller Jones seconded the motion for discussion purposes. Controller Jones noted that Secretary of State Ysursa indicated a need for additional time to continue reviewing this matter. She asked that Secretary of State Ysursa amend his motion to a time certain. Secretary of State Ysursa amended his motion that the Board raise the rate for cottage site rent across the board fifteen percent with the proviso that the subcommittee will report back to the Board on or before December 1, 2008, with a new methodology on price. Controller Jones seconded the amended motion. The amended motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.]*

BOARD ACTION [December 16, 2008]:

- A motion was made by Secretary of State Ysursa to modify the June 19, 2008 Land Board action to lower the 2009 lease rate to five percent across the board at Payette Lake and Priest Lake. In addition, the Cottage Site Subcommittee is directed to report back to the Land Board no later than June 15, 2009 with a price methodology to be used in future leases. Controller Jones seconded the motion. This motion was replaced by Superintendent Luna's substitute motion.

- A substitute motion was made by Superintendent Luna to freeze the cottage site lease rates at the current level, and that the Cottage Site Subcommittee report back to the Board no later than June 15, 2009 with a price methodology to be used in future leases. Governor Otter seconded the motion. *See below for the vote.

- Prior to a vote being taken on the substitute motion, a subsequent substitute motion was made by Controller Jones to increase the lease rate to two and a half percent. This subsequent substitute motion failed for lack of a second.

* Returning to the substitute motion by Superintendent Luna and seconded by Governor Otter, which is to freeze the cottage site lease rates at the current level and that the Cottage Site Subcommittee will report back to the Board no later than June 15, 2009 with a price methodology to be used in future leases, a vote was taken. Superintendent Luna, Governor Otter and Secretary of State Ysursa voted aye; Attorney General Wasden and Controller Jones voted nay. The substitute motion carried on a vote of 3-2. [The substitute motion superseded the original motion by Secretary of State Ysursa.]

10. Owyhee Initiative – State and BLM Proposed Land Exchange – *Presented by Kurt Houston, Operations Chief-South*

DEPARTMENT RECOMMENDATION: That the Board direct the Department to enter into an ATI with the BLM for the above-described land exchange.

DISCUSSION: Governor Otter asked about wording in the board memo indicating it is better to exchange the land. He asked why it is better to exchange the land rather than protect the water right. Operations Chief Houston stated from a management standpoint, it is more cost efficient to block up ownership. Deputy Attorney General Clive Strong stated the rationale used was even if we had the water rights, we would have difficulty gaining access to those lands across lands that would then be designated wilderness or wild and scenic. Then we would have to obtain federal authority to gain access to actually use the land. It became a logical solution to go outside of that area to avoid federal restrictions for access.

Governor Otter stated it would be a good idea even without the Owyhee Initiative to consolidate these lands. Operations Chief Houston agreed and stated that this exchange has merits on its own. The Department is taking advantage of the Initiative's current momentum.

BOARD ACTION: A motion was made by Attorney General Wasden to direct the Department to enter into an ATI with BLM for the above-described land exchange. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 5-0.

- **INFORMATION**

Background information was provided on the Information Agenda items. No Board action is required on the Information Agenda.

11. Maggie Creek Pulp Plan Update – *Presented by Kurt Houston, Operations Chief-South*

Secretary of State Ysursa left the meeting at 11:40 a.m.

Prior to beginning the next agenda item, Attorney General Wasden noted for the record that Secretary of State Ysursa is at this time en route to the hospital for surgery. Attorney General Wasden requested that the Board by motion send greetings to Secretary Ysursa along with get well wishes for a speedy recovery. Attorney General Wasden volunteered to deliver those greetings to Secretary Ysursa on behalf of the Board. Controller Jones seconded the motion. The motion carried on a vote of 4-0, with Secretary of State Ysursa being absent for this vote. (Voting aye: Otter, Wasden, Jones, Luna)

12. Forest Asset Management Plan Update – *Presented by David Groeschl, Assistant Director, Forestry and Fire*

DISCUSSION: Director Bacon informed the Board that the Department will also send letters and pamphlets to legislators. Governor Otter expressed his appreciation for the quality of the brochure.

13. Budget Holdback Update – *Presented by Patrick Hodges, Division Administrator, Support Services*

DISCUSSION: Superintendent Luna asked for the dollar figure for Project Learning Tree. Director Bacon stated total funding was $23,800. PLT suffered about a $9,200 cut in the first go around and was totally eliminated with the requirements of the second.

Governor Otter asked about the impact of the two percent reserve. Director Bacon stated to make the two percent reserve the Department had to actually cut some portions of the statutory programs, but more in the form of seasonal employees. Services will have to be cut to some level because the Department will not have the necessary workforce to help permanents, and that would be mainly in regulatory lake protection and possibly a small amount in fire.

Superintendent Luna noted funds being eliminated are general fund. He asked if there is any other fund support. Director Bacon stated it is his understanding that the Idaho Forest Products Commission's annual budget is somewhere between $140,000 and $144,000. IFPC would lose the Department's component.

At 11:50 a.m., subject to the call of the Chair, a brief recess was taken. At 11:57 a.m. the Board reconvened into Regular Session.

At 11:58 a.m. a motion was made by Attorney General Wasden to resolve into Executive Session pursuant to Idaho Code § 67-2345(1)(f) to communicate with legal counsel for the public agency to discuss the legal ramifications of and legal options for pending litigation or controversies not yet being litigated but imminently likely to be litigated. Superintendent Luna seconded the motion. The motion carried on a vote of 4-0, with Secretary of State Ysursa being absent for this vote.

- **EXECUTIVE SESSION**

A. Idaho Code 67-2345(1)(f) – To communicate with legal counsel for the public agency to discuss the legal ramifications of and legal options for pending litigation or controversies not yet being litigated but imminently likely to be litigated.

At 12:18 p.m. a motion was made by Attorney General Wasden to resolve into Regular Session. Controller Jones seconded the motion. The motion carried on a vote of 4-0, with Secretary of State Ysursa being absent for this vote. The Executive Session was held in accordance with the Idaho Open Meeting Law. No action was taken by the Board during the Executive Session.

There being no further business to come before the Board, at 12:19 p.m. a motion was made by Controller Jones to adjourn. Superintendent Luna seconded the motion. The motion carried on a vote of 4-0, with Secretary of State Ysursa being absent for this vote. Meeting adjourned.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ C. L. "Butch" Otter
C. L. "Butch" Otter
President, State Board of Land Commissioners and
Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ George B. Bacon
George B. Bacon
Director

The above-listed final minutes were approved by the State Board of Land Commissioners at the January 20, 2009 regular Land Board meeting.

Exhibit 15

Land Bd. Meeting Minutes

(June 16, 2009)

STATE BOARD OF LAND COMMISSIONERS
C. L. "Butch" Otter, Governor and President of the Board
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Superintendent of Public Instruction

George B. Bacon, Secretary to the Board

Final Minutes
Regular Land Board Meeting
June 16, 2009
Idaho First Bank, 475 East Deinhard Lane, McCall

The regular meeting of the Idaho State Board of Land Commissioners was held on Tuesday, June 16, 2009, in McCall, Idaho. The meeting began at 1:27 p.m. at Idaho First Bank, Community Room, 475 East Deinhard Lane, McCall, Idaho. The Honorable Governor C. L. "Butch" Otter presided. The following members were present:

Honorable Secretary of State Ben Ysursa
Honorable Attorney General Lawrence Wasden – *via conference phone*
Honorable State Controller Donna Jones
Honorable Superintendent of Public Instruction Tom Luna

For the record, Governor Otter recognized the presence of a quorum.

Prior to beginning the Consent Agenda, Director Bacon asked that item eleven be moved forward to before item 9. Assistant Director Groeschl will present that item and has another engagement. No objection being heard, Governor Otter so ordered.

- **CONSENT**

A motion was made by Controller Jones to approve the Consent Agenda with corrections as noted on pages 6 and 8 of the April 21, 2009 draft minutes. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 5-0.

1. Director's Report – *approved*

A. Interest Rate on Department Transactions – June 2009
B. Timber Sale Activity Report
C. Timber Sale Official Transactions – May 2009
D. Legal Matter Summary
E. Bureau of Surface and Mineral Resources Official Transactions – May 2009
F. Fire Settlement Information

DISCUSSION: Referring to item B, the Timber Sale Activity Report, Director Bacon noted timber sales sold for approximately $138 to $140 a thousand. Sales that did not sell will be reappraised and reoffered.

2. Timber Sales – *Staffed by Roger Jansson, Operations Chief-North, and Kurt Houston, Operations Chief-South* – ***approved***

NORTH OPERATIONS				COUNTY	AREA OFFICE
A. Upper Wolf Track	CR-10-0378	1,540	MBF	Boundary	Priest Lake (Coolin)
B. Hump Bump	CR-10-0379	2,100	MBF	Bonner Boundary	Priest Lake (Coolin)

C. Something Cherry	CR-30-0536	6,485	MBF	Benewah	St. Joe (St. Maries)
D. Lost Hobbit	CR-30-0553	5,480	MBF	Shoshone	St. Joe (St. Maries)
E. Bogus OSR	CR-30-0566	4,710	MBF	Shoshone	St. Joe (St. Maries)
SOUTH OPERATIONS					
F. South Dent	CR-40-0986	1,010	MBF	Clearwater	Clearwater (Orofino)
G. Silver Lewis OSR	CR-40-1036	1,865	MBF	Clearwater	Clearwater (Orofino)
H. Maggie-Harris Cutoff	CR-42-5037	5,050	MBF	Idaho	Maggie Creek (Kamiah)
I. Shotgun Pulp	CR-42-5038	4,950	MBF	Clearwater	Maggie Creek (Kamiah)
J. Dry Fir	CR-50-0148	2,290	MBF	Adams Washington	Payette Lakes (McCall)

DISCUSSION: Regarding item D, Lost Hobbit, Superintendent Luna asked which endowment would pay for the $90,000 repair to the Henderson Loop Bridge. Director Bacon stated Lost Hobbit is 100% public school endowment so the public school endowment would pay. Superintendent Luna asked if other endowments would pay a proportionate share if they also benefited from the bridge repair. Director Bacon stated the Department does calculate proportionate shares and charges each endowment accordingly.

Governor Otter asked about the window for rehab on the 338 acres of clearcut. Director Bacon stated typically the Department collects seed from trees during good cone years so that activity is ongoing. Governor Otter asked if the Department has a seed inventory. Director Bacon stated the Department does have a seed inventory and keeps adding to that inventory. However, some species, such as larch and ponderosa pine, are hard to get and could be as much as seven years between good cone crops.

When clearcuts are planned and the sale is sold, staff receive logging plans from the operators and start planning the planting of trees. Sow seed orders are placed in the fall, and the nursery will grow the trees through the next summer. Young trees will be delivered the following spring. Through this process, the Department receives a two-year old seedling in a little less than two years. Replanting will occur anywhere from one to two years after harvest.

3. **Authorization for Issuance of Deficiency Warrants to Pay Fire Suppression Costs in Fiscal Year 2009** – *Staffed by Brian Shiplett, Chief, Bureau of Fire Management* – ***approved***

DEPARTMENT RECOMMENDATION: That the Board authorize the Department to issue deficiency warrants necessary to pay fire suppression costs beyond the $154,300 appropriation for fiscal year 2010.

DISCUSSION: Governor Otter asked about the $154,300 figure. Director Bacon stated this request covers costs above $154,300. Typically deficiency warrants range from $4 million in a light year and our worst year, two years ago, was $21 million.

BOARD ACTION: Approved.

4. **State Participation as a Member of:** *[Staffed by Brian Shiplett, Chief, Bureau of Fire Management]* – ***approved***

A. Southern Idaho Timber Protective Association
B. Clearwater-Potlatch Timber Protective Association

DEPARTMENT RECOMMENDATION: That the State continue to participate as a member of the (A) Southern Idaho Timber Protective Association and (B) Clearwater-Potlatch Timber Protective Association.

BOARD ACTION: Approved.

5. **Request to Complete Conveyance of General Fund Land to Panhandle Health District –** *Staffed by Bob Brammer, Assistant Director, Lands, Minerals, Range* – ***approved***

DEPARTMENT RECOMMENDATION: That the Board direct the Department to complete the conveyance of the General Fund Land ownership in Lots 12 and 13, Block 8, Southmayd, McKinney and Wilsons Addition in the City of Sandpoint, Idaho, to the Panhandle Health District upon payment to the General Fund of $26,104.59.

DISCUSSION: None.

BOARD ACTION: Approved.

6. **Conveyance of Homedale Armory Property to Owyhee County** – *Staffed by Bob Brammer, Assistant Director, Lands, Minerals, Range* – ***approved***

DEPARTMENT RECOMMENDATION: That the Board direct the Department to revert the one-half ownership in the Homedale Armory Property, identified as Lots 10, 11 and 12 of Block 14, back to Owyhee County per Idaho Code §46-726.

DISCUSSION: None.

BOARD ACTION: Approved.

7. **Minutes – *approved as corrected**

A. Regular Land Board Meeting – April 21, 2009
page 6, agenda item 7 – change Decker to **Deckard; page 8, agenda item 8 – change 2012 to **212**.*

B. Regular Land Board Meeting – May 19, 2009 – *no corrections/changes noted.*

- **REGULAR**

8. **Endowment Fund Investment Board Manager's Report** – *Presented by Larry Johnson, Manager of Investments, EFIB*

A. Monthly Report

- Endowment reserves at the end of April were at least 2.7 times the size of approved 2010 distributions. Some endowments had over five times their 2010 distribution in reserve.
- The Endowment Fund Investment Board met on May 19 after the last Land Board meeting. The Investment Board reviewed the distribution policy found in the Land Board's Asset Management Plan Guideline and recommended no changes.
- No compliance or legal issues.
- *Upcoming Events:* The EFIB will present a recommendation on proposed FY 2011 distributions at the August 18 Land Board meeting. Based on current information, including investment losses and expected reduced land revenues, the EFIB staff will recommend to the Investment Board that the distribution be maintained at FY 2010 levels. However, the Department of Lands recently provided a revised forecast of land revenue. Based on that revised forecast it is possible the EFIB's recommendation could change before the August Land Board meeting.

B. Investment Report

- 4.6% positive return for the month of May.
- Fiscal year-to-date deficit is -18%.
- Through the end of May, the fund is even with its benchmark for the fiscal year.

- To date returns for the month of June have been flat.

DISCUSSION: Governor Otter asked for the investment reserve balance in the public school fund. Mr. Johnson stated that the public school fund, relative to its distribution, is the lowest at 2.7 times the size of approved 2010 distributions.

No action was taken on this agenda item.

9. Revision of IDAPA 20.03.14, Grazing Leases and Cropland Leases – *Presented by Bob Brammer, Assistant Director, Lands, Minerals, Range*

DEPARTMENT RECOMMENDATION: That the Board direct the Department to request gubernatorial approval of the revised rule as a Temporary Rule to the extent authorized under the Idaho Administrative Procedure Act and that the Board direct the Department to proceed with rulemaking in accordance with the Idaho Administrative Procedure Act using the revised rule as the Proposed Rule.

DISCUSSION: Governor Otter asked about the boiler-plate language for the section covering rights reserved to the Department, the old section 021. He wondered why the Department would make it part of the contractual relationship and what part is negotiated. Mr. Brammer stated the boiler plate language is incorporated into the lease, and the Department felt restating it in the rules would be redundant.

Secretary of State Ysursa commended the Grazing Subcommittee for their work. He asked if the Board plans to lengthen grazing leases from the current ten years to up to thirty-five years. Mr. Brammer stated there has been support for a twenty-year grazing lease. The twenty-year figure has been used fairly consistently throughout discussions and public meetings. The Department does see value in moving forward with legislation in the next session to extend the lease term up to twenty years for grazing leases. Secretary of State Ysursa stated he would be sure to watch for the legislation. He noted changes to the Admissions Act removed the ten year limit and left it open.

BOARD ACTION: A motion was made by Secretary of State Ysursa to move the approval of the Department's recommendation. Attorney General Wasden seconded the motion. The motion carried on a vote of 5-0.

10. Cottage Site 2010 Rent Changes and Update on Cottage Site Subcommittee – *Presented by Mike Murphy, Chief, Bureau of Surface and Mineral Resources*

DEPARTMENT RECOMMENDATION: That the Land Board retain the 2010 rental rate for all cottage sites at the existing 2009 level.

DISCUSSION: A verbatim transcript will be available upon written request.

BOARD ACTION: A motion was made by Secretary of State Ysursa that the Board approve the recommendation to freeze the rents at Payette Lake and Priest Lake. Controller Jones seconded the motion. The motion carried on a vote of 5-0.

11. Authorization to Raise the Fire Assessment Surcharge for Each Improved Lot or Parcel to the Maximum Allowed by Idaho Code – *Presented by David Groeschl, Assistant Director, Forestry and Fire*

DEPARTMENT RECOMMENDATION: That the Board authorize the Department to raise the surcharge for each improved lot or parcel from $20 to $40, which is the maximum allowed by Section 38-111, Idaho Code.

DISCUSSION: None.

BOARD ACTION: A motion was made by Secretary of State Ysursa to move the Department's recommendation. Attorney General Wasden seconded the motion. The motion carried on a vote of 5-0.

*** Governor Otter left the meeting at 2:40 p.m.*

12. Adoption of Proposed Rule, IDAPA 20.02.02, Rules of Practice and Procedure before the State Board of Land Commissioners – *Presented by Steve Schuster, Deputy Attorney General*

DEPARTMENT RECOMMENDATION: That the Board adopt the proposed rule IDAPA 20.01.01, Rules of Practice and procedure before the State Board of Land Commissioners.

DISCUSSION: None.

BOARD ACTION: A motion was made by Controller Jones to adopt temporary rule IDAPA 20.02.01, Rules of Practice and Procedure before the State Board of Land Commissioners. Superintendent Luna seconded the motion. The motion carried on a vote of 4-0, with Governor Otter being absent for this vote.

*** Governor Otter returned to the meeting at 2:43 p.m.*
*** Secretary of State Ysursa left the meeting at 2:44 p.m.*

13. IDL Annual Strategic Plan Update – *Presented by Patrick Hodges, Division Administrator, Support Services*

DEPARTMENT RECOMMENDATION: That the Board direct the Department to submit the FY 2010 – FY 2013 Strategic Plan to the Division of Financial Management by the July 1, 2009 deadline.

DISCUSSION: None.

BOARD ACTION: A motion was made by Controller Jones to approve the work product in the annual strategic plan update and to submit the 2010-2013 strategic plan to the Division of Financial Management by the July 1, 2009 deadline. Attorney General Wasden seconded the motion. The motion carried on a vote of 4-0, with Secretary of State Ysursa being absent for this vote.

*** Secretary of State Ysursa returned to the meeting at 2:50 p.m.*

- **INFORMATION**

None

At 2:50 p.m. a motion was made by Controller Jones that pursuant to Idaho Code 67-2345(1)(c) and (f) the Board resolve into Executive Session for the purpose of discussing the acquisition of an interest in real property which is not held by a public agency and to communicate with legal counsel regarding legal ramifications of, and legal options for, pending litigation or controversies not yet litigated but imminently likely to be litigated. Controller Jones requested that a roll call vote be taken and that the secretary record the vote in the minutes of the meeting. Superintendent Luna seconded the motion. Prior to a vote being taken, Attorney General Wasden asked if the motion included Idaho Code 67-2345(1)(d) or (c). Controller Jones stated (1)(c). Attorney General Wasden asked if there is a need to go into Executive Session also for (1)(d). Director Bacon stated the need for Executive Session is for items (d) and (f). With consent of her second, Controller Jones modified her motion to reflect sections (d) and (f). The motion carried on a vote of 5-0. [Aye – Otter, Ysursa, Wasden, Jones, Luna; Nay – 0; Absent – 0; Excused – 0]

*** Secretary of State Ysursa left the meeting at 2:51 p.m.*

- **EXECUTIVE SESSION**

A. Idaho Code 67-2345(1)(d) – To consider records that are exempt from disclosure as provided in chapter 3, title 9, Idaho Code.

B. Idaho Code 67-2345(1)(f) – To communicate with legal counsel for the public agency to discuss the legal ramifications of and legal options for pending litigation, or controversies not yet being litigated but imminently likely to be litigated.

*** Secretary of State Ysursa returned to the meeting at 3:01 p.m.*

At 3:01 p.m. a motion was made by Controller Jones to resolve into Regular Session. Superintendent Luna seconded the motion. The motion carried on a vote of 5-0. No action was taken by the Board during the Executive Session.

Action Taken Subsequent to Executive Session

Upon return to Regular Session a motion was made by Superintendent Luna that the Board move to disclaim interest in clay, kaolin, quartz and clay by-products in state mineral estate in property sold prior to 1986. Controller Jones seconded the motion. The motion carried on a vote of 4-0, with Governor Otter recused for this vote.

There being no further business to come before the Board, at 3:23 p.m. a motion was made by Secretary of State Ysursa to adjourn. Superintendent Luna seconded the motion. The motion carried on a vote of 5-0. Meeting adjourned.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ C. L. "Butch" Otter
C. L. "Butch" Otter
President, State Board of Land Commissioners and Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ George B. Bacon
George B. Bacon
Director

The above-listed final minutes were approved by the State Board of Land Commissioners at the July 21, 2009 regular Land Board meeting.

Exhibit 16

Land Bd. Cottage Site Subcommittee Meeting Minutes (Nov. 23, 1998)

STATE BOARD OF LAND COMMISSIONERS

Philip E. Batt, Governor and President of the Board
Pete T. Cenarrusa, Secretary of State
Alan G. Lance, Attorney General
J. D. Williams, State Controller
Anne C. Fox, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

COTTAGE SITE SUBCOMMITTEE MEETING

November 23, 1998 1:00 P.M.
East Conference Room
Joe R. Williams Building
Boise, Id

The Cottage Site Subcommittee meeting was called to order by State Controller J.D. Williams, Chairman. The following subcommittee members were present:

State Controller J.D. Williams, Chairman
Superintendent of Public Instruction Anne C. Fox
Secretary of State Pete T. Cenarrusa

Alvin Carr, Commercial and Recreational Leasing Specialist provided the background information as presented in the board memorandum.

Mr. Carr introduced the appraisers who prepared the appraisals for the Idaho Department of Lands – Mr. John McFadden who prepared the appraisals for Priest Lake and Mr. Brad Knipe who prepared the appraisals for Payette Lake.

Attorney Greener thanked the sub-committee for their patience and their work. He stated there were a number of areas where there were disagreements. Their appraiser, Ed Morse, raised a number of issues that were discussed. There needs to be some type of closure on these issues for everyone's best interests.

Mr. Greener presented a proposal to the sub-committee. A 2 ½% figure – 2 ½% of the assessed value of the land – be used. The terms of which would be written into a new 10-year lease. He asked that a 5-year phase-in be considered. These increases will be dramatic to everyone involved.

Mr. Greener asked that the appeals process be finalized. He felt there were some i's to be dotted and t's to be crossed in that process – no major issues. He also addressed the hardship cases. He stated that he felt this process was well on the way to being resolved. He asked that the 10% surcharge be removed. He stated that the lessees needed certainty in their lives.

Superintendent Fox stated that Mr. Greener didn't mention market rent. Mr. Greener said that

would be the assessed value determined by the Valley County Assessor – assessed value of the land. He said starting with that basic concept, then we can decide where to go.

Mr. Carr stated that he wanted some clarification. He asked Mr. Greener if what he said was basically the existing rental rate formula the Land Board has now, which is the current county assessed value. Mr. Greener said it is essentially that. Director Hamilton said – except drop the 10% surcharge. Mr. Greener said to write it into the lease so the lessees have the certainty and stated again that they were also asking for a phase-in. State Controller Williams said by writing this into the lease, it would be a contract term that would be binding during the term of the lease and could not be adjusted.

Controller Williams asked Mr. Knipe, the department's appraiser at Payette Lake, about the comparison between the county assessed values and his appraisals – were they pretty close. Mr. Knipe said within about 10%. He said the problem with the assessed value is that by the time you have to give notice to the lessees, you are working with a two-year old assessed value. Controller Williams said that by virtue of the timing involved there is always a lag. Bryce Taylor stated that the grazing formula does the same thing.

Controller Williams asked how much longer the lots would continue to be assessed by the Valley County Assessor. Mr. Taylor said the current sewer assessment is due to delete this year. There will always be ongoing operating expenses at the sewer district level and stated that he felt the county would continue to assess that property.

Mr. Hervey stated that there are 14 lots that are not part of the sewer district and these may have to be added in on a contractual basis. Mr. Taylor stated that there are 14 lots outside the sewer district. A couple of these lots are being considered in a land exchange. He stated that the county has been willing to assist the department in that endeavor and applied their existing data to those lots and provided the department with a value.

Mr. Cresswell said in response of the 2 ½% of the Bonner County values, the Priest Lake Association did not like the Bonner County values and felt they were too high. Their association also feels that Mr. McFadden's appraisal is too high. He stated that without Mr. Lempesis, the association's attorney being present and without being able to consult the Board of Directors, it would be difficult to make a commitment. He did state that he would take this information back to his association and respond back to the department.

He said that one thing that would be absolutely necessary would be to have an appeal process accompany the approval of this 2 ½ % provision. He stated that he certainly liked the 5-year phase-in suggestion. Hardship – he felt there was agreement that there would be some type of provision. He stated that he would certainly hope that the 10% surcharge would be eliminated.

Mr. Cresswell stated that he came prepared primarily to let the sub-committee know why they did not like Mr. McFadden's appraisal report. Mr. Morse was present to discuss those issues.

Mr. Manos stated that the Bonner County Assessor told him that the numbers at Priest Lake were factored in. He asked Mr. Carr if the department was going to put a value on the lots at Priest Lake. He said he did not feel a factored in situation is a proper approach. Mr. Carr said there might be an option to look at this most recent appraisal by Mr. McFadden in coordination with the county on county-assessed values - up-to-date 1998 values. Mr. Manos asked if the

staff would determine this figure. Controller Williams told Mr. Manos what he felt might be done. Assuming that a formula can be arrived at, we do have about a year until this will go into effect which would be a productive time to work with any lessee who feels their values are out of line.

Mr. Taylor said the department felt this would be available to the lessee through the appeal process. He said that all counties in the state of Idaho are required to assess approximately 20% of their lands each year because it has to be updated every five years. When Bonner County initially did the appraisal of the cottage site lots – under contract a few years back – they did go out and appraise the lots. It was a mass appraisal. From that point on they use the county sales ratio to update these figures. Any new program the department did with the county would rely on the county sales ratio for an annual update. This is a standard process in all counties. Nothing different was done at Priest Lake, even though it was done under contract.

Considerable discussion was held regarding the assessed values. Mr. Carr stated the coordination the department would have with the counties under contract to get the values and the appeal process would allow any discrepancies to be brought to the attention of the department. State Controller Williams stated that he felt the Land Board would want the lessee to have the opportunity to present any data to the department they wanted. Mr. Taylor stated that the lessees would have the opportunity to bring that data to the department. He stated they may be caught again between using the county values and the department's adjustment of those values, but he felt the department could work with that. State Controller Williams said there was nothing that says the department could not make adjustments.

Mr. Taylor stated that the appeal would be available to the lessees, first to the department and secondly to the Land Board. State Controller Williams stated that he felt the Land Board would expect the department to try to work the values. They are not anxious to see very many appeals. Mr. Taylor said that given the information the department has, they would be working closely with the county. He stated that while the department will not be instructing the county as to values, he felt that the county would probably listen to suggestions.

Director Hamilton stated that at the last meeting, it was pretty much agreed that the counties would be used as an outside third party. Director Hamilton said he would not have any problem in taking information to them and ask them to take a look at it. When it comes to the final value, he said he did not think the board should be adjusting them. We may let the county know that the board doesn't agree with a value, but we should be very cautious in changing values or we don't have an outside third party.

Mr. Cresswell said it was his understanding that in the appeal process, the Department of Lands is just the first step and then there were other steps that could be taken. State Controller Williams said he felt the basic steps were: If you disagree with a value as set by the county, then you go to the department staff and let them know you don't think a value is fair, and why. Then the department has to make a decision. If you agree with the decision that's it. If you don't agree then you come to the Land Board and they make the decision. Then from there, that decision can be appealed to the District Court. It will not be a de novo appeal, it will be - did the Land Board abuse its discretion.

Mr. McFadden stated that the estimates of market value were based on sales of deeded properties. The rate of return that was applied to that came from an analysis of leasehold sales on Priest Lake of state leased lots. This was a direct indication from that precise market. It was

3 1/2% and it does consider, by definition, precisely all of these characteristics of the state leases because it came from the state leases.

Mr. Cresswell asked if the group should move ahead and discuss the appraisals and their concerns about the appraisals, assuming that there is a possibility that they would be accepted or are the lessees looking at 2.5% of the county assessed value. State Controller Williams stated that the present proposal before the Board is 2.5% of the assessed valuation from the county. This has been deferred through the year 2000 at this time. Mr. Cresswell stated that he would like to move ahead if in fact it looks like Mr. McFadden's appraisals are the ones that will be used. State Controller Williams stated that it would not be Mr. McFadden's appraisals that would be used. The reason Mr. McFadden determined market value was to see the comparison with the county appraisals. In looking at the figures, they are pretty close in most cases.

Mr. Cresswell stated that in the case of Priest Lake, 9 of the 15 lots were appraised at a higher rate and 6 were appraised less. State Controller Williams said in order to have a system, the county assessments will be used.

Mr. Greener stated that he viewed the appeal process, as taking care of problems that would arise. Any difficulties that any lessee had with the rent he was being charged, those points could be brought before the Land Board if they wished to go through the appeal process - if it got that far. Mr. Greener stated that he told Mr. Lempesis, in a phone call, that he would ask for deferment of any i dotting and t crossing on the appeal process until he returned to participate. He also stated that they would like a final decision made on this at the December 15, 1998 Land Board meeting.

State Controller Williams stated that it might be beneficial to discuss the appraisals. Even though the Land Board made the decision last year that the amount would be 2 ½ percent of the most current available assessed valuation; the appraisers have come up with different recommendations. Priest Lake was 3 ½ percent, Payette Lake was 6 percent if certain conditions could be met, or 4 percent if they couldn't. That 2 1/2 percent may not be written in stone. He stated that he personally did not feel it would change very much, but he could not speak for the full Land Board. He felt everyone that wanted to address this issue should have an opportunity to speak.

Mr. Morse said that his review was quite lengthy and he felt that all the issues he raised were not necessarily addressed. He stated that there were some differences in methodology and some assumptions that produced significantly different estimates. He covered several of the areas of disagreement.

State Controller Williams stated that one of the reasons the Land Board decided to go with 2 ½ percent, they knew they were on the very low end of return on market. Looking at what the appraisers have come up with, 2 ½ percent is 29 percent less than 3 ½ percent or 38 percent less than 4 percent, which were the two recommendations. The Land Board recognizes that the state has not done a whole lot – is basically an absentee landlord. By going with this lower percentage, they have tried to be as fair as they could. He stated that this would probably compensate for not looking at some of the issues Mr. Morse presented. Secretary of State Cenarrusa stated that he felt the Land Board did factor those issues in when they made the determination of the 2 ½ percent. Superintendent Fox said the Land Board felt the 2 ½ percent seemed much fairer than the department recommendation of 5 – 6 percent. She also stated

that the Land Board needed to be careful in meeting their fiduciary responsibility to the state.

Director Hamilton commented on a previous remark that lots were not moving at Priest Lake. He stated that this is information he tracks regularly. There were three transactions at Priest Lake just this past month. There were several transactions at Payette Lake and these transactions are characteristic month after month. He stated that the transfer fees range from $100,000 – 120,000 up to over $200,000. This shows that the 2 ½ percent is on the low end of the scale. State Controller Williams stated that the numbers show twenty-four (24) transfers or assignments of leases this past year.

Jim Parkinson stated that the 2 ½ percent is a lot higher than the rents that were charged in 1979-80 and all the years past. He stated that the lessees and the state are in this together. If the state has mismanaged this property and perhaps it has, however, he feels that it is highly unfair to cure it on the backs of the lessees by asking them to step to the plate and pay three – four times the rent. The rent has already gone up over a thousand percent over the last few years. Mr. Parkinson said he had attended these meeting a lot of years and he doesn't want to be here any more. He said these decisions need to be cast in stone – put to bed. The lessees deserve this. The lessees are anxious to get this behind them.

Doug Cresswell said they were concerned about the process that was followed. They were disappointed that they did not have an opportunity – until after the appraisals were completed – to meet with Mr. McFadden and provide any type of input. His association felt the appraisals were high and that there was not enough credit given for improvements. They were also concerned about the 3.5 percent recommendation and feel that Mr. McFadden missed the market rent altogether. Mr. Cresswell stressed that his association did not feel their input was listened to.

Mr. Duane Bills stated that he wanted to go on record objecting to one aspect of the appraisals on the Payette Lake appraisals. He stated that he felt the lessees were being lulled to sleep on the proposition that the leaseholders have been given credit in the appraisals for the leasehold improvements. He said he did not agree with Mr. Knipe's appraisals. In view of the fact that there is a shortage of this type of property, we know the value will continue to climb. He said that for future appraisals he would expect to be credited for the leasehold improvements he puts in to the property.

Mr. Taylor stated that the 2 ½ percent would take care of this problem. State Controller Williams said the lessees need to talk to the department if they feel it was not assessed as bare land. Mr. Bills said he differed with Mr. Taylor. He said he sat down with the chief appraiser of Valley County twice in the last six months and they do not give credit for leasehold improvement, they simply go on comparable values – comparable sales. They do not deduct the improvements that have been made to my lot. You need to give credit for improvements – not to the house, but to the lot.

Director Hamilton said the appraisal instructions were very clear how to appraise those lots and he felt Mr. Knipe followed those appraisal instructions. He felt Mr. Knipe considered lots that were basically bare and unimproved in selecting the comparables he used. He stated that Mr. Knipe and Mr. McFadden may have used different techniques, but both were proper and arrived at the same point. Mr. Knipe stated that he would agree to meet with Mr. Bills and go over the appraisals with him.

Secretary of State Cenarrusa asked what is the equitable appraised value? He stated that he is confused as to what the real equitable assessed value is, because different factors are brought in. He stated that the 2 ½ percent that was arrived at to take care of these other factors is fair.

Superintendent Fox stated that she is comfortable with the 2 ½ percent and feels that it is fair. She said that the lessees were given a full year for discussion and had no raise in rentals. She felt the Board should go ahead and put this in place this next year. There will then be time to look at any hardship cases. She asked if Mr. McFadden would speak to Mr. Cresswell's concerns.

Mr. McFadden said there was no intent to avoid the lessees during the appraisals. Mr. Cresswell said he felt this was a department decision. Mr. Carr said the appraisal instructions were provided to the appraiser along with the list of lots and maps. The desire was to follow the appraisal instructions and keep the amount of involvement with the appraisers to a minimum to allow the appraiser to do his job. It was the responsibility of the department to provide the lessee concerns and issues to the appraiser.

Mr. McFadden stated that in doing work with the Forest Service, meetings were held after the appraisals in order to have documentation to show. Mr. McFadden said his draft report was a signed report that met all standards. He also stated that this did not mean it could not be revised. Mr. Cresswell questioned the comment that only 10 percent of the lake is deeded. He said he felt this was incorrect. Mr. Cresswell said virtually all the west side is Forest Service and the east side is State so no more than 10 pervent is deeded. Mr. McFadden said he measured the frontage on contour maps and estimated it closer to 25 percent. In terms of lot numbers, it is probably closer to 1/3 deeded and 2/3 Forest Service and State. He stated his figures are in his report.

Mr. Cresswell asked Mr. McFadden if he would agree that deeded property is at a premium. He said the associations concern is that the prices are being driven up. Mr. McFadden stated that Priest Lake properties are premium because it is a lovely place in the world and always will be. He stated that he took his values from sales of deeded lots, but he reiterated that the rate of return came from an analysis of leasehold sales on that lake with those same consistent lots. He stated that he made sure there was consistency in the prices of the sales – the fee value prices to those used in the analysis of the leaseholds. That consistent analysis is what led to the 3 ½ percent conclusion.

Director Hamilton asked Mr. McFadden about his comment that values have gone up at Priest Lake over the last 20 years. He asked him if that was incompatible with what is going on with other lakes in other places. Mr. McFadden said he did not think so. Director Hamilton stated that this is pretty standard – anywhere.

Mr. McFadden stated that leasehold interests in lots on Priest Lake today are routinely selling for $100,000. That is clear evidence that the existing rents are below market rents – by definition. The 3 ½ percent came from an analysis of 13 leasehold sales or 10 sales and 3 listings that have taken place over the last 2 ½ years. It was a factoring of those rents and those leasehold prices and their deeded values.

Mr. Manos said he has been at Priest Lake for 35 years and felt he had a pretty good idea of the value of the land per foot. He stated that he has no argument on the 2 ½ percent. He said he could not understand how Mr. McFadden could use fee simple property in such a comparison to lease property and exclude the federal lands.

Mr. McFadden stated that there is better data on the state leases and state leases are more comparable to state leases than the federal permits. The 5% federal return is locked for a period of time and his 3 ½%conclusion assumed annual increases so it must keep up with the moving market. Those with permits on federal land do not have control over the beachfront. They do not have control over the land between the lots. The public is invited to use that land unlike the state leases. Federal permits are really for building pads. The permit covers only the land under the buildings – not an entire leased lot area. The appraiser for the Forest Service viewed the limitation on the Forest Service lots as being so great that he valued all of them as 50-foot lots, knowing they were actually up to four times that because of the limitations that are imposed on those lots. They do not have exclusive use.

Ms. LaShaw asked if Mr. McFadden stated there was a public trail in front of the federal lots and the shoreline. Mr. McFadden stated there is a required public access corridor on Forest Service land. She said she was told the state owns to the high-water mark and was told they could not kick someone off if they were in this area. She also mentioned the public road that goes through their lot and ends at Mr. Mano's driveway. Mr. McFadden stated that he had no argument with that. He was only describing the way the appraiser for the Forest Service viewed those lots.

Mr. Greener asked if Superintendent Fox intended to discuss a phase in? He stated that some clarification of the position of the sub-committee regarding that aspect would be appreciated. Superintendent Fox said there were several things that would assist the Land Board if some preliminary suggestions were considered. First was the percentage of the assessed value. Second, is the assessed value yearly – how will it be appraised. Third is the phase-in and the fourth would be the surcharge issue.

Controller Williams said it was his understanding that the value would be assessed yearly, but there would be a 2-year lag using county appraisals. There would be annual adjustments. The sub-committee would consider the 2 ½ percent that is determined to be reasonable.

Secretary of State Cenarrusa stated that he suggested a phase-in at the last sub-committee meeting. He stated at that meeting that the lessees might want to increase the 1999 rate in order to minimize the impact of the 2000 rates. Mr. Cenarrusa said at that time, he was suggesting a one-year phase in. If the county values were out of line, the Land Board would have the ability to deal with that. State Controller Williams stated that he felt the phase-in had already been taken care of by postponing the rates. It should be the full amount in the year 2000. The full Land Board needs to make this decision. Secretary of State Cenarrusa stated that Mr. Greener agreed with a phase-in, however Mr. Lempesis stated that his association would not want a phase-in.

Director Hamilton stated that the department would look at where the bulk of the rates are and put together some figures for the Land Board to consider. State Controller Williams stated that there is some disparity in values of the lots. He stated that he did not know whether the Land Board would ever consider selling lots at Priest Lake due to the timber holdings there. He

stated that the overall plan for Payette Lake is to divest as soon as possible implementing the new Constitutional Amendments.

State Controller Williams addressed the surcharge issue. His feeling is when market value is reached the Land Board should look at removing it. Secretary of State Cenarrusa stated that it might be worth looking at a rental cap.

Director Hamilton stated that the surcharge is a sensitive issue. He stated that both appraisers indicated that there are substantial leasehold values when these properties transfer. This indicates a very clear issue that we are not at market rent. His suggestion was to leave it at 10 percent. If values drop remarkably, then there is a basis for removing it.

Mr. Bills said in lieu of a phase-in period, the Land Board could use a three-year average on the appraisals. Director Hamilton stated that this average would put the state five years behind. If you start two years behind and average the three that you have, you are using five-year-old data.

Doug Cresswell stated that the 10% premium rent is appropriate, but when full-assessed value is reached it should be eliminated. Jim Parkinson stated that a cap is a good idea. Director Hamilton stated that the cap is much preferable to elimination of the 10 percent surcharge. State Controller Williams said a cap might be a good idea, however, he informed the group that these caps will be high – not 5.3% again. Mr. Taylor said if we are at market rent, there is nothing to charge. Ten percent of zero is zero, it is self-defeating. It sunsets itself.

Director Hamilton said just because the Land Board says 2 ½ percent is the rent does not make it market rent. It is Board rent. Mr. Parkinson stated that these rates would not stabilize for several years.

State Controller Williams said it was suggested earlier to make new leases. He asked the department how much of an imposition it would be to create new leases. Mr. Taylor said there were 584 with 29 being looked at in a land exchange. It would take approximately 30 days to create the new leases; they are computer generated. Director Hamilton said this might be able to be accomplished with an amendment to the existing lease. Mr. Taylor said this might work better.

Ben Ysursa stated that there would be no reason for the six-month notice. Director Hamilton stated this was in code. Mr. Ysursa said this is statutory but it is a moot point. State Controller Williams said this is a housekeeping issue that ought to be taken care of this session.

Mr. Taylor said the department would probably send notices every year anyway. This system is in place.

Director Hamilton asked to do some clarification on one point. The department will establish the valuation on an annual basis. It will be 2 ½ percent of the appraised value. Then the Land Board gave the department permission to substitute assessed valuations wherever the opportunity arose – or seemed reasonable. It did allow leeway whenever the department was concerned with something they could get an appraisal if it fit with the terms of the Board policy.

The department would substitute assessed valuations, except where they were out of line and then comes the appeal process. If the department were setting the valuation, it would be appealed to the Land Board without any difficulty.

Mr. Greener, asked in fairness to Mr. Lempesis, that this wait until Mr. Lempesis returns to be a part of drafting this.

Mr. Greener stated that the appeal process has been pretty well covered and there does not appear to be any difficulty with this process. Mr. Taylor said he felt there was still some question whether the lessees had accepted that this was not going to be a de novo review. Mr. Greener said the associations were asking for de novo review to the District Court. He said he didn't understand what State Controller Williams articulated excluding an appeal to the District Court. He said he had been authorized by his clients to forego the request for a de novo appeal, but the lessees would still have the right to appeal. Director Hamilton suggested that legal counsel participate in this discussion. Mr. Greener concurred.

Mr. Taylor said that there had been a lot of discussion on this process earlier and all agreed that this would not be finalized at that time. It was felt that the appraisal process might bring forth some of the issues to be addressed in the appeal process. There were no motions at the Land Board to make this final.

Director Hamilton asked if we were looking at appealing all of these appraisals. State Controller Williams said only those who initiated an appeal.

Superintendent Fox was commended for her work on the sub-committee and her participation on the Land Board concerning cottage site issues.

The cottage site meeting was adjourned.

The sub-committee reconvened to cover an issue that was presented at the regular Land Board meeting. State Controller Williams stated that this issue was on the valuation of Dr. Forney's lot to be included in the Capitol Park Plaza land exchange.

Dr. Forney spoke to the sub-committee regarding the valuation of his lot. He stated that he did not feel the appraiser was fair. Some years ago, he obtained an additional appraisal from Idaho Land Appraisal or from Mountain States Appraisal. They were willing to do a new appraisal, but could not have it done by the December 2, deadline. Mr. Knipe's appraisal is the only one available.

Mr. Perry Whittaker said the original appraisal was done in June. Due to Dr. Forney's concerns about the sewer, the valuation was reduced to $600,000. This is the only appraisal the department has to base an exchange value on. There are 28 other participants in this exchange.

Mr. Knipe said he had been through this with Dr. Forney several times and he felt his figures were a fair number. Dr. Forney said he had been a careful steward of this land for some time. He stated that he did not feel it was fair treatment. He stated his reasons for not wanting to be in the second phase of the land exchange. He said he did not know that it was going to happen and he felt the department did not know if it was going to happen. There are no guarantees.

He said he was asked to put $600,000 in a trust hoping that something will happen. In the meantime, be a lessee.

State Controller Williams suggested to Dr. Forney that if phase II did not take place, the department would find another piece of property for him to exchange for.

Ben Ysursa said he had understood earlier Dr. Forney was in phase II. Then the department worked with Dr. Forney to get him in phase I. Mr. Ysursa stated that phase I would happen right away and suggested to Dr. Forney that he go back to phase II if he wanted to pursue discussion of values. Dr. Forney said he paid $5,000 to be part of phase I even though he still disagrees with the valuation.

Kent Nelson, Deputy Attorney General said that his directions were to get Capitol Park Plaza land exchange put together. The department is set for closing on phase I as soon as these issues are resolved. He stated that Dr. Forney has his right to disagree with the valuations, but for purposes of this transaction, we are at the "fish or cut bait stage."

Jay Biladeau said if Dr. Forney pursues going to another phase or another property and has the property re-appraised by another appraiser it is likely that that value could come out higher. State Controller Williams reiterated that if Dr. Forney wanted to wait for another appraisal, he felt that the Land Board would look for another exchange for him.

Kent Nelson said there would be significant expense on phase II that will have to be done prior to that phase closing. We cannot find ourselves in a position where we do not know whether or not we will have a participant in phase II. The transaction is currently structured so that the values for phase II would be established the day the pen goes to the paper on the exchange agreement. It would be unfortunate to put it in jeopardy at this point because we continue to have a disagreement over values.

Director Hamilton informed Dr. Forney he would be obligated to get his own MAI appraisal. The Board can only use that appraisal in comparison to the existing appraisal. Then the difference would have to be reconciled between the two appraisals. A common value would have to be reached for department purposes. The three-appraisal route is another option in reaching agreement. Dr. Forney said that he will accept the current appraisal and decided to stay with Phase I of the land exchange.

There being no further business to be brought before the subcommittee, the meeting adjourned at 4:30 p.m.

IDAHO STATE BOARD OF LAND COMMISSIONERS

President, State Board of Land Commissioners and
Governor of the State of Idaho

Pete T. Cenarrusa
Secretary of State

Stanley F. Hamilton
Director

Exhibit 17

Transcript, Land Bd. Cottage Site Subcommittee Meeting (June 3, 1991)

M O T I O N

Cottage Site Leasing Subcommittee Meeting
June 3, 1991

Jerry Evans: I have struggled with this issue for quite some time and I guess I still come back to the idea that lease rate should be related to the value of the property and appraisal is a reasonable way to get to the estimate value, understanding full well that those appraisals are not perfect. I think they are the most reasonable way that we have and I think reasonable rate of return based on that is the way to go. I was troubled with the 8 percent. I was pleased when the staff came in with a recommendation, although even with the staff's recommendation I had some difficulty because any rationale for $4^1/_2$, 5, $5^1/_2$ percent, whatever it is, it ought to be reasonably uniform. So I was hoping that we would probably come out today with a recommendation that we adopt the appraisal, go back to a smaller rate of return, something in the neighborhood of 4, $4^1/_2$ percent. That we would go with the implicit price deflator as that annual adjustment that I think we have been missing and then the other part that I had some real trouble with the staff's recommendation had to deal with not going through kind of another round of appraisal until the year of 2001. I thought that was way too far down the road, cause if this appraisal is in error, and is not as accurate as it needs to be hanging your hat on those values through 2001 without any opportunity to look again. I think you could have some real problems, so I think the three of us are each coming from a little different perspective, but today we need to pull together a conclusion and will form the basis of the recommendation of this subcommittee to the Board a week from tomorrow so I guess the question is who would like to make a motion?

J.D. Williams: See if I can read my notes. Mr. Chairman I would make this motion that we continue the present schedule for the 1992 lease year, that for those lot values that have reached the thresholds, that they be increased this year by 5.52 percent which is one-third of the annual Valley County appraisal increase for the last three years times 60 percent. Math not being my greatest strength though, it may be a little different than that, but that is how I compute is 5.52 percent whatever the figure would be. That we solicit a third appraisal opinion on the values, that appraiser to be selected by the appraiser hired by the State and by an appraiser designated by the lessees by a mutual agreement and the parties agreed to the, that the values arrived by the appraiser either by himself if he can't get an agreement of the three or by the three if they can agree to be the values that will be used as the base for future leases, that we continue the subcommittee for the coming year to settle the lease, the base values, settle along with the index formula will be and any other issues that will need to be resolved between the State and our tenants.

Jerry Evans: I'm glad I made notes because I would never have been able to repeat the motion. Is there a second?

Larry EchoHawk: I second the motion.

Jerry Evans: There is a motion and a second. Anything more you want to say? Stan are you clear in terms of what our motion says?

Stan Hamilton: I think we can get it off the tape, but there are a couple of questions just for clarification I think we need to consider. Talked about soliciting a third appraiser. I think what I hear there is only one appraisal on the table unless you consider the 1987 appraisal on as well. There is only one appraisal on the table so you can probably get there from where you are by simply saying that their appraiser and the State appraiser of RECG will select another appraiser who will simply take a look at what is there and his termination will be final. It is not really a consideration of two separate appraisals, there is only one on the table.

J.D. Williams: One was just somewhat of a criticism of the first appraisal.

Stan Hamilton: Yes

Jerry Evans: Are you clear?

Stan Hamilton: I have no problem if that is your understanding. We can do that and there is no problem with doing that, but there is only one appraisal on the table so I need to make sure that that was clear. I think the number two recommendation was that the valuation, that the rental for next year, o.k. next year the rental would be simply what it says here in the table, was that what your recommendation was?

Jerry Evans: Unless any of those reach -

Stan Hamilton: Those that have reached target rental and there are a couple, yours are a few, a number of them have reached it last year. Normally what we would have done was take either an index from 1987 and indexed it each year so that the lot value for 1992 would be five years up the road on the index. What you are suggesting, however, is that you simply take the 1987 values and increase it by 5.25 percent and then take 60 percent of it.

J. D. Williams: Well let me ask a question.

Jerry Evans: Go ahead.

J. D. Williams: You said 1987 values, you mean that is what this

schedule is to do is to arrive at the 1987 value or the value of 1990.

Stan Hamilton: What the whole thing was based on was originally the proposal 1988, if you will, proposal was to take the 1987 appraisal and establish those values for the lots, then set out this phase in schedule and say when a lot hits target rental, in other words $2^1/_2$ percent of the 87 values, that we would index. What the intention was there was to take an index and we never did get to the index because when we were about to do that when this issue came up last year, so we laid it aside for a year. Normally what we would do is take an index, whether it would be the County sales ratio index or the implicit price deflator index or any other index we agreed on. Starting in 1987 we would then index it for 88, index it for 89, index it for 90, index it for 91 and index it for 92, so we would be dealing with a new lot value and it would be 88, 89, 90, 91 and 92 would be roughly 20 percent. It would be five years of 4 percent a year roughly is what it would work out to, something in that neighborhood. That is a little different than what you have purposed and what the Land Board proposal was at that time was that we would then simply take that value and the rental would be $2^1/_2$ of whatever that lot value was at the time as adjusted by the index so that would give - Well take a $100,000 lot, it would be probably $120,000 lot now or $115,000 or somewhere in there. I don't know what it would be and that was what the proposal was, that was the original board proposal in 1987 or 88. Actually it was proposed in 86, it was affirmed in 87 and it was affirmed again in 88 that would be the policy. Maybe what your proposal is continue the Board policy for another year, the existing board policy for another year.

J. D. Williams: I don't have any problem with that inflation index. In my mind, I was thinking that when they got to the target rent, that was also target market value for the year. In reality it is an 87 market value.

Stan Hamilton: Right, and you have to index it out.

J. D. Williams: O.K. Well, the last three years the County has gone up 27 percent I would say implicit price. You said there is various -

Stan Hamilton: It has been running about four and a quarter percent. Charles, about four and a quarter, four and a third percent, something like that?

Jerry Evans: We use the implicit price deflator. That seems to be one thing that we have agreed upon.

Stan Hamilton: We would have taken it from the 87 value and run it off.

Charles Hummel: I would like to add one clarification. I think what Stan's been concerned about is that his recommendation was saying use the implicit price deflator as a multiple against the estimated current estimate of lot values, then apply the whatever agreed upon percentages then that would equal the rent. Numerically it is the same whether you would do that or if all the other values the same, as if you apply the percentage increase and implicit price deflator to the rent itself, the current rent itself would actually numerically work out to be the same rental amount.

Stan Hamilton: That is exactly right. The reason that we wanted to tie to the lot value is that the Board has established the concept of lot values and rent being $2^1/_2$ percent of that. We felt that that is the only thing in this process that we can actually get out and take a look at and that is what is the value of these lots, right or wrong, and that is the only thing we have so by moving that out then we had a measure of where it was and it was something that if you wanted to come in and take an appraisal you could actually see how you were performing. That was what this current appraisal would have done. We would have taken a look at that and where are we and its our mid course correction, we would have adjusted it based on actual appraisal periodically in order to get things back on track because the indexes, they are not representative of what is going on in real estate markets. They are kind of general state of an economic health as you all know and all especially residential recreational property is just all over the board.

Jerry Evans: Stan if we end up at the same place and with the recommendations that we continue to work with the subcommittee for next year, aren't we the same place either way? Don't you get the same place with calculate lease rates?

Stan Hamilton: Yes. Whether he used the lease rate or whether he used the lot value doesn't make any difference.

Jerry Evans: So for this next year with the understanding that this subcommittee will continue, we'd be at the same place.

Stan Hamilton: It makes a difference. If you took the index - if you took the rental as it was, no you can't do it that way. You can't deal with rental, you have to deal with a lot value and because lot values are going up and the rental is going up as well and eventually the rental is going to hit that $2^1/_2$ percent of where the lot value is and that was always a moving target to begin with because of the index. We never new exactly when that was and Candy indicates that she has been there for a couple of years, well if that had been indexed when she hit that then there would have been another jump if we had followed that indexing. We knew there was no need to use the index for about two years

after we started, maybe three because we were not going to get to target in three years.

Jerry Evans: I know that airplane out there is not going to wait for Mr. EchoHawk, so we need to get - Are you clear?

J. D. Williams: Yes, I think I am, so we would amend the motion to use the implicit price inflator for the last four years.

Stan Hamilton: I think at this point if you simply use adopt the Board or readopt the Board's existing policy for another year.

J. D. Williams: Because that was the policy?

Stan Hamilton: That was the policy, that would get it for another year. You don't need anything else. Just adopt the Board's policy for another year and then go on to get your other appraiser.

J. D. Williams: Well, except we have to have the index. We have to see what the index says so we better say the implicit price.

Don Hobbs: I am trying to figure out what the proposal would because I'm going to have to figure all these out when it is all done.

Jerry Evans: It is going to be easy Don.

Don Hobbs: Are you looking at a minimum increase or stay with the current policy with minimum for this next year or 8 percent increase for each one, is that what you are trying to achieve?

Jerry Evans: Only for those, it would be like it is on the schedule except if you have met the target, then you go back and use the implicit price inflator and see what the rate on that one is.

Don Hobbs: What I was thinking of is, though, if you have someone, say within one percent of meeting the target, and you go with four percent with someone else, then the person who is almost the target, because you are going to have some leases that are all variation with distances form target, and so that is why I was asking what you are shooting for is minimum or what your are trying to accomplish.

J. D. Williams: That would be a little difference but I think to make it as easy as we can this year, lets try to keep it in force -(changed tape)-

Stan Hamilton: I don't know whether on the sheets you have there its what I have circled here and these two. One is the actual GNP and the other is the total for the personal consumption

expenditures. To be honest about it, I don't care, either one is acceptable to me. The total gross national product - one may be just as easy to use and as long as we agree.

Jerry Evans: I understood there was an agreement on this point before we came. Which one did you have in mind? We talked about the implicit price.

Stan Hamilton: We were talking about one of these two, I know that and that doesn't matter to me.

Jerry Evans: Which one is it?

Candy Anderson: Mr. Chairman, we were talking about the implicit price deflator, but I have a very big question at this point and I'm sorry we are running out of time, but there is a point that I don't understand here.

Jerry Evans: We are going to have to vote on a motion here pretty soon. Is there an agreement Stan in terms of which one of these? J. D. would you specify which implicit price would be.

Stan Hamilton: Just a GNP here, this first one is fine with me. I have no problem with that.

J. D. Williams: That's fine. First column.

Jerry Evans: We have a motion and second. Is there further discussion?

Larry EchoHawk: Mr. Chairman I agree with the amendment and my understanding is that we are sticking with the policy that was in existence since the 1988 schedule was adopted.

Jerry Evans: Basically, it sticks with the same policy. The only thing it does it fills in that void.

Stan Hamilton: Mr. Chairman, if I could, I think maybe you ought to hear what Candy has to say.

Candy Anderson: Because you know exactly what it is don't you?

Stan Hamilton: I think I might.

Candy Anderson: O.K. We have to go back to the wording in this schedule right here and it says, "rent shall be phased in according to the table below and shall be indexed to keep pace with changing land values after the formula rent of $2^1/_2$ percent of lot value is reached." To me that indicates once I have reached that then my rents will be indexed. In other words, it will be increased a certain amount so that I am on a steady increasing rent schedule. I believe Stan is saying something

that is not right down here.

Stan Hamilton: What I am saying is not right down there. What I am saying is exactly what the Board approved and adopted and I guess I have a real strong problem with whether it is me or any other staff or department putting words in the Board's mouth. This is the Board's policy. This is what was laid out here and I guess that is where I come back down to. I understand all the other issues that you are talking about there, but this is what the Board said and I guess I think we ought to stick with that and if that's what they want to do.

Jerry Evans: And the motion is to stick with that.

J. D. Williams: With the change on the index so that much is done.

Jerry Evans: Candy, we'll discuss this more before we get to the full Board meeting.

Candy Anderson: This is a very important point right here because from what I understand, Stan says that you will go back and take - set my value - that was put at a certain amount - you will take every year this increase and apply the total increase to that. Is that true.

Jerry Evans: We will increase the value by that factor and then calculate $2^1/_2$ percent of that.

Larry EchoHawk: Mr. Chairman, I need to vote or I'm going to miss the airplane and to me this is probably a question of going back and reconstructing what happened and we can probably deal with this at the full Board meeting. It comes up as a question of interpretation.

Jerry Evans: I agree and we will come back and do that.

Candy Anderson: Thank you very much.

Jerry Evans: I will call for the motion. All those in favor say I.

Those oppose no and I would like to be recorded as voted no, so Stan if you have access to some, but by a vote of 2 to 1 this will be the recommendation that will go to the Board at it's June meeting which will be a week from tomorrow and I would like to continue this discussion particularly with you to make sure there is an absolute clear understanding, because this is our recommendation of the Board and if we need to make some adjustment in that to stay with the present policy we'll do so.

Larry EchoHawk: May I be excused.

Jerry Evans: Yes, thank you very much. Run for the airplane.

Now it almost seems wrong to talk about the motion after the fact. It has been passed. Stan, do you have the details so that you can put together this recommendation of the Board and distribute it to all the folks who are present today and anyone else who has an interest in it because more than anything else we want clear understanding so that we don't want any of this business, I thought it was this and someone else said "oh no, I understood it to be something different."

Stan Hamilton: I can do that. It is going to be a tight race again because the Board does meet next Tuesday. I can distribute, I think, and get it out to everybody, but I think I understand what the motion was. We will confirm it on the tape as well. In fact what I will try to do is get ahold of the maker of the motion since I've tinkered with it.

Jerry Evans: If there is anyone present who did not sign this who would like to make sure you get a copy of this, would you sign because this will also give us the list of folks who would like to have the recommendation. So Stan I would like to see it kind of reduced to writing as quick as possible out to everyone who is here and others who may be interested so we can have an opportunity before the Board meeting a week from tomorrow.

Stan Hamilton: What I think I will do is basically drive off of what is right here only when it gets to the recommendation I'll strip out of the materials that relate to the appraisal and simply deal with your motion so it's very brief and very straight forward.

J. D. Williams: O.K.

Jerry Evans: Well with that let me thank all of you for your patience and trying to rush something. We have not had the opportunity to get together very often. I think the discussions have been very helpful and I want to thank all of you. We will have this on the agenda a week from tomorrow and at the full Board meeting level there will also be some opportunity for discussion before the Board acts I'm sure. So with that, I thank you all and will see you at least a week from tomorrow.

Exhibit 18

Land Bd. Agenda Memorandum,

Cottage Site Rental Policy

Recommendations,

(June 11, 1991)

STATE BOARD OF LAND COMMISSIONERS
June 11, 1991

SUBJECT

Cottage site rental policy recommendations

AUTHORITY

Idaho Constitution, Article 9, Section 8
Idaho Code 58-304, 58-305, 58-310A

BACKGROUND

On February 12, 1991, the State Board of Land Commissioners established a committee to evaluate the appraisal report of the Real Estate Consulting Group, Inc. (RECG) relating to the appraised value of selected cottage sites at Priest Lake and Payette Lake. The committee was also charged with reviewing existing board policy relating to establishment of annual rentals.

The committee, consisting of Mr. Evans, Chairman, and Messrs. EchoHawk and Williams, met three times with representatives of the lessee associations, department staff, and principals of RECG. Mr. Cenarrusa joined the committee during its deliberations.

The following is the report and recommendation of the committee to the full board.

The board's existing policy is as follows:

1. Use the estimated lot valuations, approved May 17, 1988, for the purpose of setting rental rates;

2. Establish $100 per month or $1,200 per year as the minimum acceptable rental rate for any waterfront lot and $60 per month or $720 per year as the secondary lot rent;

3. Phase in rental rates, in accordance with the 1988 rental rate phase-in schedule shown below, until every lessee is paying a rate no less than 2.5 percent of the estimated value of the lot they occupy.

Calendar Year	Priest Lake Class I	Payette Lake Class I	Payette Lake Class II
1988	1370	1261	530
1989	1660	1573	574
1990	1950	1885	620
1991	2240	2197	665
1992	2530	2509	710
1993	2820	2821	720
1994	3110	3133	720
1995	3400	3445	720
1996	3625	3757	720
1997	3915	3900	720

4. Index lot values/rental rates periodically by the respective county sales ratio index to keep those values current with changing land values;

5. Revise estimated lot values from time to time through selected lot appraisals and application of those "comparables" to all lots;

6. Continue the ten percent premium rental as long as contract rent is below market rent. Note: This contradicts the sunsetting of premium rental in the leasing rules.

DISCUSSION

An appraisal of cottage site fee simple title base land values was contracted in October 1990 and delivered in May 1991. The effective date of the appraisal is October 1990.

Sixteen (16) lakefront lots on Priest Lake and thirteen (13) cottage site lots on Payette Lake were appraised. The thirteen (13) Payette Lake lots included five (5) with lake frontage, one (1) with indirect frontage (fronts on a common beach area) and seven (7) secondary sites.

The RECG appraisers were of the opinion that land values have increased significantly at both Priest Lake and Payette Lake since the 1987 appraisal.

The October 1990 RECG appraisal stated that front-foot values at Priest Lake ranged from a low of $325 to a high of $1,000 per front foot. This represents a considerable increase from the values found during the 1987 appraisal which indicated a range of $250 to $650 per front foot.

The October 1990 RECG appraisal stated that Payette Lake lakefront lots have a general value of $2,600 to $2,900 per front foot as compared to $1,000 to $1,200 per front foot in 1987; indirect lakefront lots at $1,000 to $1,200 per front foot in October 1990 as compared to $35,000 to $40,000 per lot in 1987; and second-tier lots at $28,000 to $35,000 per lot in October 1990 as compared to $15,000 to $18,000 per lot in 1987.

In May 1991, the department asked the Real Estate Consulting Group, Inc. (RECG) to further evaluate the residential ground lease market to see what actual rates of return or rental factors were being achieved by landowners.

RECG reported back that there seemed to be a relationship between lot values and rates of return. They recommended the following:

Lot Value Range	Rental
0 - $50,000	5.5% of lot values
$50,001 - $100,000	5.0% of lot values
$100,001 - up	4.5% of lot values

RECOMMENDATION

The cottage site committee makes the following recommendation to the State Board of Land Commissioners on the motion of Mr. Williams and the second by Mr. EchoHawk. Mr. Evans voted nay.

1. Continue the existing Land Board cottage site rental policy for the CY-1992 rental year.

a. Index the estimated lot valuations, approved May 17, 1988, for the purpose of setting rental rates (See Item 2. below).

b. Maintain $1,200 per year as the minimum acceptable rental for waterfront lots and $720 per year as the secondary lot rent;

c. Phase in rental rates in accordance with the rental rate phase-in schedule shown below until every lessee is paying a rate no less than 2.5 percent of the estimated value of the lot they occupy.

Calendar Year	Priest Lake Class I	Payette Lake Class I	Payette Lake Class II
1988	1370	1261	530
1989	1660	1573	574
1990	1950	1885	620
1991	2240	2197	665
1992	2530	2509	710
1993	2820	2821	720
1994	3110	3133	720
1995	3400	3445	720
1996	3625	3757	720
1997	3915	3900	720

d. Continue the ten percent premium rental through rental year CY-1992.

2. Estimate new lot values for the CY-1992 rental year using the Implicit Price Deflator Index produced by the U.S. Department of Commerce, Bureau of Economic Analysis. Such adjustment shall be done prior to June 1 for the calendar year to follow. Example: To calculate the CY-1992 lot values, the estimated lot valuations for the CY-1987 rental year would be multiplied by the 1990 IPD Index value and divided by the 1986 IPD Index value, e.g., a lot valued at $100,000 by the 1987 appraisal would be valued at ($100,000) (131.5 ÷ 113.8) = $115,554 for rental purposes in CY-1992. The rental for such a lot at Priest Lake would be the lesser of $2,530 (phase-in) or $2,889 (2.5%). The rental for a similar lot at Payette Lake would be the lesser of $2,509 (phase-in) or $2,889 (2.5%).

The implicit price deflator is the price index for gross national product. The index is the ratio of GNP in current prices to GNP in constant prices. It is a weighted average of the price indexes used to deflate the components of GNP, the implicit weights used being expenditures in the current period. All expenditures are valued in prices of the base year -- now 1958 -- to obtain the constant dollar GNP.

Because it is so comprehensive, the implicit price index is generally regarded as the best single measure of broad price movements in the economy as a whole.

The Gross National Product -- Implicit Price Deflator Index for the period 1980-1990 is shown below along with U.S. Department of Commerce estimates for index values for CY-1991 and 1992.

1980	85.2	1986	113.8
1981	94.0	1987	117.4
1982	100.0	1988	121.3
1983	103.9	1989	126.3
1984	107.7	1990	131.5
1985	110.9	1991	136.2*
		1992	140.5*

*Estimated

3. The board should seek another opinion as to the fee simple base land value of the lots appraised by RECG. The board would retain an MAI appraiser(s) selected jointly by RECG and the lessee association's consulting appraiser with the selected appraiser's recommendation as to lot values to be binding on all parties and to be used by department staff to estimate all lot values for setting future rentals.

4. The board should continue the committee for one more year through June 1992 to consider other cottage site issues and to resolve the basic lot valuation and market rental issues.

BOARD ACTION Adopted recommendation of the subcommittee with the additional understanding regarding how the arrangements would be made for the appraisal in paragraph 3 (LOT values only) and for payment of the appraisal (dept.) (also, dept. to help select appraiser) (finding not binding on lessees) and also that dept. try to give actual lease amounts (in notice to the lessees).

JUN 1 1 1991

SFH/cl
6/6/91

Exhibit 19

Land Bd. Agenda Memorandum,

Land Board Cottage Site Subcommittee

Recommendation for Rental Rates,

(June 9, 1992)

STATE BOARD OF LAND COMMISSIONERS
June 9, 1992

SUBJECT

Land board cottage site subcommittee recommendation for rental rates.

BACKGROUND

Superintendent Jerry Evans, chairman, State Auditor, J.D. Williams, and Attorney General, Larry EchoHawk, were appointed to a subcommittee to study cottage site rentals at the February 12, 1992, land board meeting. This subcommittee has met on three occasions with the department and cottage site lessee associations to hear recommendations regarding future rental.

The subcommittee last met on May 18, 1992. After review and discussion of the issues, Auditor J.D. Williams made a motion to:

1) Use county assessed lot values to determine market value for rental assessment purposes at Payette Lake and Priest Lake;

2) Set target rent at 2.5% of county assessed lot value;

3) Phase in rental increases over a ten-year period with a maximum increase of 5.3% per year;

4) Set a new target rent at the end of the ten-year phase-in period;

5) Continue the premium rent policy. ~~until 2.5% of full market value is attained;~~

6) Keep second-tier lots at the minimum $720 per year rent or 2.5% of value, whichever is greater; and,
$1200/yr waterfront

7) Continue this subcommittee to discuss cottage site land exchange procedures.

Attorney General Larry EchoHawk seconded the motion and the motion passed with a 2 to 1 vote. Superintendent Jerry Evans opposed the motion because he felt not having any adjustment in target rent for ten years will place the rent even further behind the market at the end of ten years than it is today.

DISCUSSION

There are several aspects of the motion that require further discussion.

Part (1) of the motion was to "Use the county assessed lot values to determine market value for residential assessment purposes at Payette Lake and Priest Lake".

This is a relatively easy process in Valley County, because the county has assessed all but 20 of the state lots for the special benefits payment associated with the sewer district. The 20 lots not assessed are outside the sewer district boundary. Department staff has assigned each lot a value based on the county formula.

The process is more difficult in Bonner County. Early indications were that the Bonner County Assessor could establish state lot values rather easily. However, in a recent discussion with the assessor, he has indicated that the state would have to fund his office $100,000 to accomplish the job. He feels he would have to hire two or three more appraisers to deal with the 352 lots. Staff believes that $100,000 is an unreasonable amount of money for this job, and funds are not available in the department budget.

As an alternative, staff can establish values for the state lots through a comparable lot analysis using county values on intermingled private lots. The process would be similar to what staff did to establish private fee simple values, but staff would apply county values rather than appraised values. It would require 8-12 weeks to accomplish this task due to existing heavy summer workloads. The six-month notice could not be accomplished with this approach.

For 1993 rental calculations, the Board could make a percentage adjustment or use the RECG values. Another option is to use '87 appraised values and add the county adjustments for the five year period. The '87 values plus IPD could also be used.

Part (2) of the motion was to "Set target rent at 2.5% of county assessed lot value". The department recommends the Board continue to set "target rent" at not less than 2.5% of lot values. Such target rents should move with changes in land values.

Part (3) of the motion states "Phase in rental increases over a ten-year period with a maximum increase of 5.3% per year".

The advantages of this phase-in schedule to the lessees are predictability and small increases. The disadvantages to the State are that actual rentals for waterfront lots probably cannot reach target rentals in ten years because land values -- and target rentals -- are rising faster than 5.3% annually.

The existing phase-in schedule is as follows:

Calendar Year	Priest Class I	% Change	Payette Class I	% Change	Payette Class II
1988	1370		1261		530
1989	1660	21.2	1573	24.7	574
1990	1950	17.5	1885	19.8	620
1991	2240	14.9	2197	16.6	665
1992	2530	12.9	2509	14.2	710
1993	2820	11.5	2821	12.4	720
1994	3110	10.3	3133	11.1	720
1995	3400	9.3	3445	10.0	720
1996	3625	6.6	3757	9.0	720
1997	3915	8.0	3900	3.8	720

It would appear that a higher phase-in percentage rate of at least 10 percent annually would be necessary to reach target. Such a rate is not inconsistent with the current phase-in schedule for 1993 and 1994, and is necessary if the Board is ever to achieve target rent.

Part (4) of the motion states "Set a new target rent at the end of the ten-year phase-in period. This part of the

motion needs clarification because Part (2) of the motion states "Set target rent at 2.5% of county assessed lot values". Historically, the Board has set target rent as a moving figure tied to lot values. If lot value increased or decreased, target rental followed. The Board needs to clarify whether target rent is 2.5% of lot value and free to move as land values change, or that target rent is 2.5% of 1992 Assessor's lot values locked in for ten years.

The department recommends that Part (4) of the motion be deleted. The Board should not freeze its target rental at 2.5% of 1992 Assessor's lot values for the next ten years.

Part (5) of the motion is to "Continue the premium rent policy until 2.5% of full market value is attained". The department agrees that the premium rent policy should continue in place -- it is due to "sunset" on December 31, 1992. Cottage site lessees -- particularly Payette Lake waterfront lessees -- are taking $50,000 - $120,000+ out of state-owned lots when lot leases are sold and assigned. These large "leaseholds" are attributable in large part to low annual rentals. The State should continue to recoup some of the lost rental dollars when the opportunity occurs.

The department recommends that the premium rental policy continue until the Board specifically decides that it is no longer necessary or appropriate.

Part (6) of the motion is to "keep second-tier lots at the minimum $720 per year or 2.5% of value, whichever is greater". The department supports this part of the recommendation to make the second tier consistent with the waterfront parcels.

Part (7) of the motion is to "Continue this subcommittee to discuss cottage site land exchange procedures". The department supports this part of the recommendation. The recommendation does not specify when the Board will again review the cottage site rent policy, although there is an implication in Parts (3) and (4) that the period is ten years. The Board should clearly state when it will next review the rent policy. The Board has authority to amend its policy at any time, but a maximum time frame for rental review should be clearly stated. Because of the rapidly increasing land values, a new appraisal of market rental values should be completed within ten years.

If rental increases are limited to 5.3%, some Payette Lake waterfront lot lessees will apparently pay a 1993 rent less than they would have to pay in taxes if they owned the property providing the county makes planned adjustments to the assessed values. The department recommends that the Board require a rent payment of not less than the amount of the tax that would be levied against the lot if it were privately owned.

BOARD ACTION

Following motion by J. D. Williams was approved 4-1 (Jerry Evans opposed):

"That we use the county assessed lot values to determine market value for rental assessment purposes at Payette Lake, and as part of that, use the most current information available. And at Priest Lake, for this year, we use the 1987 appraisals with a 16% inflationary factor, and that the department and representatives of the Priest Lake Association continue to work trying first to have a county assessment procedure similar to that of Payette Lake. And if not, come up with an alternative, and try to do that by next year. SEcondly, to set up a target rent of 2-1/2% of the latest county assessed lot values at Payette Lake, and whatever that is determined to be next year at Priest Lake. Set a new target rent at the end of the 10-year phase-in period to keep everything in place for 10 years for stability purposes. And then continue the premium rent policy and just stop at that -- not set it to 2-1/2% of market value, but just continue the present premium rent policy during this 10-year period. And then keep the second-tier lots at the minimum of $720 per year rent or 2-1/2% of value, whichever is greater, and also a minimum of $1,200 per year on waterfront lots, and then last, continue the subcommittee to discuss cottage site land excahnge procedures and other matters that would be pertinent to a landlord/tenant relationship on these lots." Amendment added: "There should be a 5.3% cap on increases per year, as part of that motion."

ATTACHMENTS

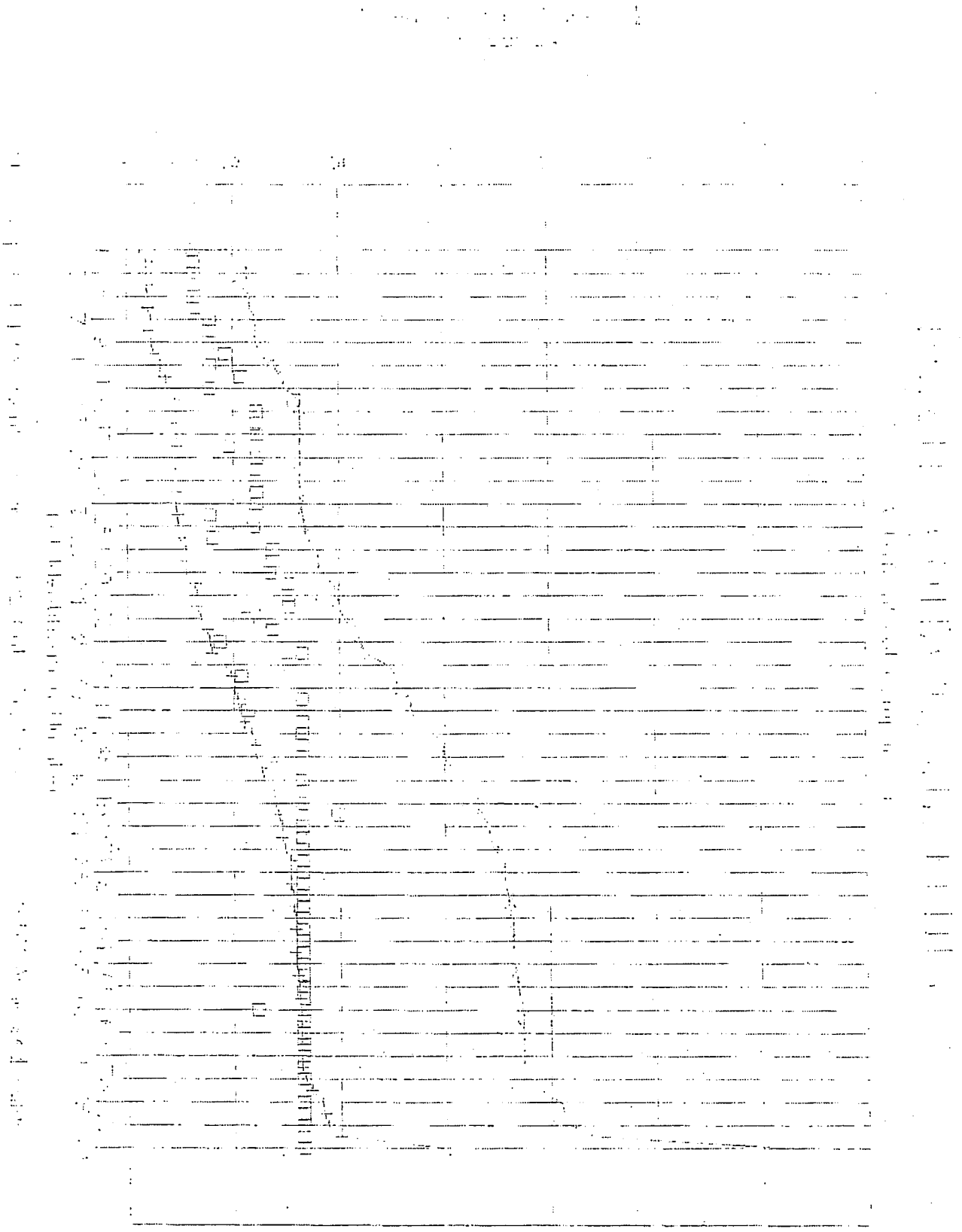
1. Table
2. Graph

JUN 9 1992

DH:drd
June 2, 1992

LEASE NO.	LESSEE	1987 APPRAISAL	ASSESSOR'S 1992 VALUES	2.5% RENT	1992 RENT	1993 RENT	5.3% LIMIT	CNTY LEVY 1992	LOT ID NUMBER
R-5048	Onweiler	55,000	80,535	2,013	1,547	1,629	1,629	1,117	1
R-5057	Sawyer	55,000	85,250	2,131	1,547	1,629	1,629	1,182	2
R-5056	Hamill	55,000	85,250	2,131	1,547	1,629	1,629	1,182	3
R-5055	Cheney	55,000	85,250	2,131	1,547	1,629	1,629	1,182	4
R-5020	Reiber	55,000	86,288	2,157	1,547	1,629	1,629	1,197	5
R-5021	Bridenbaugh	55,000	86,288	2,157	1,547	1,629	1,629	1,197	6
R-5003	Farber	60,000	88,500	2,213	1,688	1,777	1,777	1,227	7
R-5005	Hummel	60,000	88,500	2,213	1,688	1,777	1,777	1,227	8
R-5004	Pence	60,000	88,500	2,213	1,688	1,777	1,777	1,227	9
R-5032	Sweet	65,000	89,988	2,250	1,828	1,925	1,925	1,248	10
R-5062	Dalrymple	60,000	95,034	2,376	1,688	1,777	1,777	1,318	11
R-5066	Whitesel	70,000	98,614	2,465	1,969	2,073	2,073	1,368	12
R-5058	Goul	60,000	99,120	2,478	1,688	1,777	1,777	1,375	13
R-5033	Kloss	87,000	105,168	2,629	2,447	2,577	2,577	1,458	14
R-5029	Garber	75,000	105,168	2,629	2,109	2,221	2,221	1,458	15
R-5044	Kurdy	75,000	105,168	2,629	2,109	2,221	2,221	1,458	16
R-5035	Mott	75,000	105,168	2,629	2,109	2,221	2,221	1,458	17
R-5081	Tenneyson	66,000	105,168	2,629	1,856	1,955	1,955	1,458	18
R-5024	Baranco	75,000	105,168	2,629	2,109	2,221	2,221	1,458	19
R-5030	Davidson	75,000	105,168	2,629	2,109	2,221	2,221	1,458	20
R-5014	McCarroll	75,000	105,168	2,629	2,109	2,221	2,221	1,458	21
R-5060	Taylor	75,000	105,168	2,629	2,109	2,221	2,221	1,458	22
R-5053	Atchley	75,000	105,168	2,629	2,109	2,221	2,221	1,458	23
R-5047	Dean	60,000	106,200	2,655	1,688	1,777	1,777	1,473	24
R-5028	Jones	74,000	107,046	2,676	2,081	2,192	2,192	1,485	25
R-5080	Wutherich	61,000	107,166	2,679	1,716	1,807	1,807	1,486	26
R-5031	Hopffgarten	80,000	111,898	2,797	2,250	2,369	2,369	1,552	27
R-5046	Maggard	80,000	111,898	2,797	2,250	2,369	2,369	1,552	28
R-5039	Anderson	79,000	111,898	2,797	2,222	2,340	2,340	1,552	29
R-5041	Brooks	85,000	117,771	2,944	2,391	2,517	2,517	1,633	30
R-5015	Clark	85,000	119,410	2,985	2,391	2,517	2,517	1,656	31
R-5040	Edson	85,000	119,410	2,985	2,391	2,517	2,517	1,656	32
R-5022	Hetland	72,000	121,694	3,042	2,025	2,132	2,132	1,688	33
R-5027	Zimmerman	80,000	126,139	3,153	2,250	2,369	2,369	1,749	34
R-5078	Brandt	63,000	127,588	3,190	1,772	1,866	1,866	1,769	35
R-5008	Corbeil	90,000	129,113	3,228	2,509	2,642	2,642	1,791	36
R-5043	McAllister	85,000	138,346	3,459	2,391	2,517	2,517	1,919	37
R-5052	O'Reilly	70,000	141,540	3,539	1,969	2,073	2,073	1,963	38
R-5079	Coughlin	70,000	141,540	3,539	1,969	2,073	2,073	1,963	39
R-5038	Vycital	108,000	146,945	3,674	2,509	2,642	2,642	2,038	40
R-5026	Clark	72,000	147,606	3,690	2,025	2,132	2,132	2,047	41
R-5050	Peterson Trust	93,000	151,650	3,791	2,509	2,642	2,642	2,103	42
R-5049	First Security	100,000	156,140	3,904	2,509	2,642	2,642	2,165	43
R-5019	Copsey	100,000	159,140	3,979	2,509	2,642	2,642	2,207	44
R-5018	Turner	110,000	159,140	3,979	2,509	2,642	2,642	2,207	45
R-5082	Babcock	81,000	163,236	4,081	2,278	2,399	2,399	2,264	46
R-5068	Curtis	120,000	164,610	4,115	2,509	2,642	2,642	2,283	47

ATTACHMENT 1



ATTACHMENT 2

Exhibit 20

Land Bd. Agenda Memorandum,

Cottage Site Rental at Priest and Payette

Lakes (April 8, 1997)

DRAFT

STATE BOARD OF LAND COMMISSIONERS
Regular Agenda
April 8, 1997

SUBJECT

Cottage Site Rental at Priest Lake and Payette Lake

BACKGROUND

RENTAL

Records indicate that a few leases were issued as early as 1924 with the majority of leases issued in the mid 1940's and early 1950's. The Board also sold several lots in the mid 1940's. Attachment 2 provides a look back to rental in 1945.

From 1945 to 1988, rentals were a flat rate with sporadic adjustments. One period was fourteen years (1947-1961) between adjustments while other periods were from three to five years.

Since 1988, rental has been determined as a percentage of land value so that rental for each lot reflects the attributes of the individual lot. To set forth the change in rental determination that was adopted in 1988, the Board first directed the department to sell at auction up to 10% of the existing cottage site lots in 1987. The lots to be sold were to be representative of lakefront, non-lakefront, and different locales on the lakes. All lots to be sold were appraised to determine fee simple value which then established the minimum bid.

The intent of the sale was to establish lot values that would be used to determine rental from the formula of 2.5% times land value. Ultimately, twenty-two (22) lots were sold at Payette Lake in August 1987.

There were no lots sold at Priest Lake. The sale program at Priest Lake was withdrawn due to pending litigation filed by the lessees. Lot values at Priest Lake were determined through a department staff appraisal.

Subsequent to that sale, and with grudging consent from the lessees, the Board adopted a rental policy of 2.5% times the 1987 lot value, to be phased-in over a period of ten years. The phase-in increased rental by equal dollar amounts each year until the target rent was reached. Attachment 3 presents the phase-in schedule.

S.B. 1516 was passed by Idaho's Centennial legislature. The lessees introduced this bill to remove cottage site leases from conflict lease application because two leases had been applied for by a conflictor. Since cottage sites were removed from conflict, the legislature included a section in the code that states: "the Board shall ensure that each lot generates market value throughout the duration of the lease." On April 10, 1990, the Board directed the department to prepare a plan that would ensure that the intent of the bill could be met. The department reported back to the Board July 10, 1990 with a five-part plan (Attachment 4). The plan required an appraisal of cottage site land value and an appraisal of market rent. Based on these appraisals, the department would make recommendations

to the Board regarding cottage site rental derived as a percentage times land value.

The department reported the results of the contract appraisals on February 12, 1991. After discussion of the report, the Board appointed a subcommittee to evaluate the appraisal report and to review existing board policy regarding cottage site rentals.

The board subcommittee report and recommendation was made at the June 11, 1991 board meeting (Attachment 5). The committee recommendation continued the existing 1987-88 rental policy, increased 1987-88 lot values by the Implicit Price Deflator Index, directed another appraisal, and continued the subcommittee through one more year.

After monthly meetings between department staff and the lessee associations, the department recommended to the Board that direction for a new appraisal be rescinded since the lessees and the department concluded it would not provide significant new information. The recommendation was approved October 22, 1991 (Attachment 6).

The board subcommittee recommendation for rental rates was discussed at the June 9, 1992 meeting (Attachment 7). The existing cottage site rental policy was approved at this meeting. Specifically, the existing rental policy is:

- Use the 1992 county-assessed lot value to determine market value for rental assessment purposes;

- Set target rent at 2.5% of the 1992 county assessed lot value;
- Phase in rental increases over a ten-year period with a maximum increase of 5.3% per year;
- Set a new target rent at the end of the ten-year phase-in period;
- Continue the 10% premium rent policy; and
- Keep second tier lots at the minimum $720 per year rent or 2.5% of value, whichever is greater, and minimum $1,200 per year for waterfront.

LEASEHOLD VALUE

Leasehold value results from the economic principle that a buyer will pay a premium to a current leaseholder to assume a lease when the lease rent (contract rent) is less than market rent. Leasehold value may also result as a matter of demand; if no fee simple property is available, a buyer would likely pay a small premium to acquire an existing lease.

Leasehold values have escalated from an average $9,175 in 1974-75 to a high of $284,567 in 1994 for lakefront leases at Payette Lake.

Leasehold value for non-lakefront leases at Payette Lake has increased from an average value of $5,480 in 1974-75 to a high of $59,000 in 1996.

Lakefront leases at Priest Lake had an average leasehold value of $7,710 in 1974-75 and have increased to a high of $96,004 in 1995.

Recognizing that low contract rent was resulting in significant leasehold value, the Board, with grudging consent from the lessees, adopted an equity sharing "premium rental" policy in October 1981. The policy had an effective date of January 1981. This policy was formally adopted into department rules in 1987 (IDAPA 20.03.13.027). The rules had a sunset clause of December 1992 for equity sharing premium rental. The Board again adopted equity sharing premium rental as policy in May 1992 with no expiration date.

The rate of premium rental is 10% of the leasehold value. Leasehold value is determined by subtracting the value of improvements and personal property sold from the total sale price. The amount remaining after these subtractions is the amount paid for the leasehold.

Family transactions have not normally paid premium rental in the past. Family transactions are generally from a family member(s) to a family trust or from an estate to family members. These transactions have not typically been treated as sales because, usually, no money is paid. Thus, there is no basis from which to determine leasehold value. It is important to note that if a family transaction does have an exchange of money, the premium rental does apply.

DISCUSSION

LEASE RENTAL

It is apparent that current cottage site lease rental is below market rent. The basis of this reasoning is (1) leasehold values have continued to escalate significantly since implementation of the 1992 rental policy, (2) available market data indicates a higher rate of return, and (3) in some cases, rental is lower than local county taxes on similar private land.

(1) Leasehold Value. Staff has researched leasehold sales to determine the trend. Cottage site leasehold sales from 6/1/92 to 6/1/96 show an average annual appreciation of 29.39% at Priest Lake, 14.34% for Payette Lake lakefront and 9.62% for Payette Lake non-lakefront. This appreciation has occurred while cottage site rental was increasing at only 5.3% per year.

The leasehold appreciation trend is more clearly shown on the following chart:

	Payette Lake Class I Average Leasehold		Payette Lake Class II Average Leasehold		Priest Lake Class I Average Leasehold	
	Sales	Average	Sales	Average	Sales	Average
FY 92	3	$ 121,435	5	$16,508	20	$ 26,364
FY 93	2	147,268	3	18,735	15	28,844
FY 94	0	no sales	1	39,476	4	49,776
FY 95	3	213,727	3	27,287	10	73,375
FY 96	2	161,322	9	29,805	5	76,347
FY 97 (to present)	1	299,068	4	42,949	2	102,120

Further evidence of this trend can be seen from Lots 39 and 40 in the Payette Lakes Cottage Sites Subdivision. These lots are side by side and both have 100 feet of lake frontage.

Lot 39 has sold five times since 1966. The full history of this lot is shown in Attachment #8. In summary, Lot 39 leasehold sold in 1985 for $80,540, resold in 1991 for $159,870, and resold again in 1994 for $284,565. Lot 40 leasehold was purchased in 1977 for $20,000. It resold in 1996 for $299,068.

Second tier lots are also exhibiting strong leasehold appreciation. Lot 107, Payette Lakes Cottage Sites Subdivision, is a non-lakefront lot of approximately ⅓ acre. The leasehold sold in 1984 for $16,375, resold in 1988 for $12,785, resold in 1991 for $11,821 and resold in 1996 for $56,195.

Lot 161 was leased at auction in 1994 for a premium bid of $41,000. It was resold in 1996 for $59,000. This is a bare lot and very clearly demonstrates leasehold value since no improvements were included. It is also important to note that the endowment received the $41,000 bid in 1994. This lot is mentioned here only to demonstrate the leasehold value appreciation trend.

(2) Rate of Return/Market Data. The 1987/1988 rental formula established rental as 2.5% times the 1987 appraised fee simple value. Similarly, the 1992 formula used 2.5%

times the 1992 county assessed value. This rate of return was determined after significant discussion between the Board, the lessees, and department staff. The 1992 assessed value times 2.5% is equal to a 1% rate of return on 1996 county-assessed value.

The majority of the market evidence gathered by the department supports a 3% to 5% rate of return for cottage site land rental with most of the market data pointing to 5%. The 2.5% figure is supported only through an earlier appraisal which reveals that Newport Beach City, California has an actual rate of return of 1.8% - 2.5%. Their stated rate of return is 5% but they allow a 50% times land value site improvement credit to the lessees; thus, the actual rate of return is 1.8% - 2.5% (1991 appraisal). However, in addition to the rental, the home on the lease must be removed or it reverts to the City at the end of the lease term (50 years). Waterfront lot rental averaged $24,756/lot and interior lot rental averaged $8,880/lot in 1992.

A. Montana Program. The Montana Department of State Lands (DSL) administers 618 cottage site leases on endowment land. Major lease provisions include:

- The lease is for fifteen years
- The lease is <u>not</u> subject to conflict at renewal if the lessee wishes to renew
- The lease is assignable
- Rental is 3.5% times assessed value established by legislation
- Assessed value is reevaluated every five years

The Montana State Legislature established a rate of 5% times assessed value in 1988 but reduced it in 1993 due to legislation establishing the 3.5% level after pressure from the lessees. The average yearly rent is $420.00. Montana's cottage site study has relevant information for Idaho. It very closely parallels Idaho's program. The Montana study (1993) is included as Attachment #9.

B. Minnesota Program. The State of Minnesota Department of Natural Resources (DNR) presently administers 582 lakeshore cabin site leases on state-owned land. In 1984, prior to an active sale program, they administered 1,784 lakeshore leases on 90 lakes in 11 northern counties. The major provisions of the present lakeshore leases include:

- The leases run for 10 years
- A 33-foot wide easement along the lakeshore is reserved for public travel
- Either party may terminate the lease on 90 days notice
- The state is not obligated to ensure access to the lot

Minnesota's lakeshore cabin site leasing program has been through an extensive review process since the 1970's. The Minnesota legislature has established the rental at 5% of the appraised value. The appraised value is synonymous with estimated market value and appraised values are adjusted at five year intervals. Lease fee increases are phased-in with three equal annual increments. Minnesota's

annual rents range from $175 to $3,000.

C. Federal Program. The Federal Register requires that the federal residential lease rate is 5% times the appraised fee simple value. The appraised value is determined each 20 years, and was last done in 1982. Rent is adjusted each year after the initial appraisal using the Implicit Price Deflator Index (IPD). A recent newspaper article (Attachment #11) displays current U.S. Forest Service rent at Priest Lake ($1,910/year) and the proposed new rent ($8,750/year).

D. Department 1991 Rental Rate Appraisal. The department contracted an appraisal to determine fee simple lot values in May 1991 at Priest and Payette Lakes. A second portion of that contract was to appraise the market rent for state owned cottage sites at these lakes. Based on the market data gathered by the appraisers, the suggested market rate at Payette Lake for non-lakefront lots is 5.5% times land value and 5% times land value for non-lakefront lakeview lots. The suggested market rate for lakefront lots at Payette Lake is 4.5% times land value. For Priest Lake, the appraisal suggests a rate of 5.5% for any lot valued at less that $50,000, a rate of 5.0% for lots valued between $50,000 and $100,000 and a rate of 4.5% for all lots valued over $100,000. This appraisal report on market value rental is Attachment #10.

(3) Private Property Tax Comparison. During February 1995, staff researched

private property taxes at Payette Lake to see how rental compared to county taxes. The 1995 rental plus the special benefits payment for sewer installation was often less than taxes would be on the same property. An example is lease #R-5070 for which the 1995 rental of $2,929 plus special benefits payment (0.1555763%) of $524.60 totaling $3,453 is less than the 1995 Valley County taxes (1.2307817%) of $4,145 would be. The levy amount will change year to year depending upon the total assessed values and the county needs. The higher county-wide total assessed values have typically resulted in lower levy amounts. In Valley County the residential property levy has changed from 0.013868 in 1991 to .008529909 in 1997. In Bonner County the change has been from 0.012 in 1991 to .007978302 in 1997.

ANTICIPATED RENTAL PHASE-IN SCHEDULE

Attachment #14 is a spreadsheet that shows the 1992 and 1996 assessed land value and the current 1997 lot rental based on the current formula. This spreadsheet also demonstrates the department's proposed phase-in schedule and assumes a 5% annual land appreciation. All lots at Priest and Payette Lakes are shown.

GOVERNOR'S COMMITTEE ON ENDOWMENT FUND INVESTMENT REFORM

The Governor's Committee believes that the endowment should expect an overall rate of return of 10% for each asset in the land trust, or around 6%-6.5% real rate of return after adjustment for inflation. The cash yield can be lower for assets that may rise in value faster than the rate of inflation, to the extent that the appreciation is greater than inflation

(page 62, Report and Recommendations of the Governor's Committee on Endowment Fund Investment Reform, Attachment 12).

To analyze the Committee perspective, staff found that county assessed values for cottage sites have appreciated from a value of $61,368,000 in 1992 to $115,485,000 in 1996 or a gain of 88%, a simple average of 22% per year. Over the longer term, lakefront lot values at Payette Lake have appreciated from $900 per front foot in 1977 to $4,500 per front foot in 1996, a simple average of 21% per year.

Inflation from 1992 to 1996 was a cumulative total of 11.42% (Consumer Price Index). Reducing appreciation of 88% over the same term by 11.42% leaves a real gain of 76.58% or a simple average of 19.14% per year. Adding the appreciated gain and the current rental rate of return of 1% reveals a return of 20.14% per year from 1992 to 1996 (appreciation minus inflation plus rental).

This analysis is for a very short term. It is not expected that land value would appreciate at this rate over the long term. In fact, appraisals done in the summer of 1996 indicate a slight downward shift in land value at Payette Lake. The expected long term appreciation rate is 5%-7% per year. If the expected long term gain is 5%-7%, then rental should be 3%-5% to achieve the committee's recommendation of a 10% return before inflation.

The above analysis does indicate that the current 1% rate of return plus appreciation has met or exceeded the committee's recommendation in the short term. The Board's fiduciary goal to maximize returns over the long term would not be met with the current formula.

It is important to note that this analysis is investment driven rather than market based.

LESSEE ALTERNATIVES

Lessees at Payette Lake who find continued leasing is no longer tenable should be offered the opportunity to acquire their lot in fee simple title either through a land exchange or through land sale at auction.

The department does not favor fee simple sale or land exchange at Priest Lake. The Public School Endowment ownership at Priest Lake comprises a large block, approximately 184,000 acres, that is a dedicated state forest with a sustainable annual harvest of 16 million board feet. The Board has never sold or exchanged cottage site lots at Priest Lake so the state's ownership is not fractured and intermingled with other private homesites. The department believes it is in the state's best interest to maintain the current ownership at Priest Lake to avoid future management issues.

The Priest Lake Land Use Plan, approved by the Board on March 10, 1992, does not indicate a disposal of cottage sites. Rather, the plan indicates there are additional lands

suitable for future cottage site development and commercial recreation development.

Based on the Governor's Committee on Endowment Reform Report recommendation to diversify the state's portfolio, land exchange would be the preferred alternative in the short term for disposal of lots at Payette Lake. These high value, rapid appreciation type properties should normally be exchanged for developed commercial property to ensure maintenance of good cash flows and continued rapid appreciation. The process for cottage site land exchange for Payette Lake was adopted by the Board on April 8, 1996.

The Committee has recommended that a 'land bank' process be established for repurchase of property from land sale receipts. If this recommendation is followed and legislation is successful, then sale at auction provides equal opportunity to diversify and would perhaps be a preferred alternative since it would provide the opportunity for competitive bidding. Lessees also have the option to sell their lease and invest in property elsewhere.

The following chart indicates the values associated with leasing versus acquisition:

Location	Number of Lots	*Average Lot Value	**Annual Lease Rate at 5%	***Annual Cost to Purchase at 8% for 30 yrs, including taxes
Priest Lake	8	$ 77,932	3,897	$ 7,544
Priest Lake	110	160,133	8,007	15,500
Priest Lake	195	241,648	12,082	23,393
Priest Lake	42	339,248	16,962	32,842
	355			
Payette Lake	158	48,963	2,448	$ 4,767
Payette Lake	4	163,522	8,176	15,920
Payette Lake	26	251,564	12,578	24,492
Payette Lake	50	421,295	21,065	41,017
	238			

* Average lot values based on 1996 county assessed values and broken into $100,000 increments.

** Annual lease rate of 5% based on market data

*** Purchase at 8% for a 30 year loan based on U.S. Bank current rate as of 3/10/97. Taxes based on information from applicable county assessor offices (1997 property levy):

Bonner County: .007978302

Valley County: .008529909

Based on 1996 county assessed values, cottage site leases remain a bargain when compared to the cost to purchase.

LESSEE LEGAL COUNSEL

The department received a notice from Mr. Richard A. Greener of Cosho, Humphrey, Greener and Welsh, P.A., on September 9, 1996 stating that he had been retained by the Payette Lakes Cabin Homeowners Association and the Pilgrim Cove Association to represent their concerns regarding the state's future plans with the cottage site lease program at Payette Lake. The notice also requested, per the Idaho Open Records Law, all records pertaining to the cottage site lease program. The records were reviewed by Mr. Daniel Glynn of the same firm in October 1996.

Mr. Greener wrote to the department again on November 1, 1996 advising that a failure to recognize every aspect of his clients interests in the real property and the leasehold estate would place his clients in a position where they have no alternative but to seek relief in the courts. Mr. Greener believes his clients have viable claims based on theories of breach of contract, estoppel, waiver, and condemnation.

Department legal counsel wrote Mr. Greener on January 22, 1997 asking him to clarify some of the matters raised in his letter November 1, 1996. Specifically, counsel asked Mr. Greener:

1. Can you clarify what specific Land Board policy you contend cottage site lessees have relied upon for fifty years?

2. Can you identify what real property interest individual lessees have in the leasehold itself (not the property improvements, such as houses and buildings, or off-site improvements such as sewer lines)?

3. You contend that if the state does not recognize every aspect of your clients' property interest, your clients will have viable legal claims based upon breach of contract, estoppel, waiver or condemnation. Can you please clarify more precisely the basis for these claims? For example, what actions of the state involve an alleged breach of what contract? How is the state estopped due to the claimed leasehold property interest?

Mr. Greener has not responded to counsel's questions or clarified the matters raised in his letter of November 1, 1996. Attachment #13 is a compilation of the letters between the department and Mr. Greener and his staff.

SUMMARY

Based on the market data, leasehold value information, and the comparison of property taxes to rent, it is apparent that the current rental is too low. The market data indicates 5% of property value for determination of rental. The rental phase-in schedule will necessitate a two-year time lag on assessed land value. The 10% premium rent policy should continue as is.

RECOMMENDATION

1. Idaho Code §58-310A(3) states: "In the absence of the conflict application and auction procedure in the single family recreational cottage site and homesite lease and lease renewal process, the Board shall ensure that each leased lot generates market rent throughout the duration of the lease." In compliance with I.C. §58-310A(3), to achieve market rent the department recommends that cottage site rent be determined within the range of three (3) to five (5) percent times county assessed value. Since the majority of the market data indicates the higher end of the range, the department recommends a rental rate of 5% times current county assessed value.

2. Recognizing that there will be a significant increase in rental, the department recommends a rental phase-in schedule, as opposed to a one-time increase, according to the following schedule:

1997	Rent is already established
1998	1.5% x 1996 land value*
1999	2.0% x 1997 land value
2000	2.5% x 1998 land value
2001	3.0% x 1999 land value
2002	3.5% x 2000 land value
2003	4.0% x 2001 land value

2004	4.5% x 2002 land value
2005	5.0% x 2003 land value
Thereafter	5.0% x current assessed value

*Idaho Code §58-304 (Attachment 1) requires that the Board shall notify lessees of any increase in the applicable rental rate six (6) months in advance of the date rent is due and payable. For 1998 rental, the lessees must be notified by June 1997 if there is an increase. The 1997 assessed land value will not be known until early 1998. Subsequently, rental for 1998 must be determined as a percentage of 1996 land value. There will necessarily be a two-year time lag on assessed land value in every instance.

3. Continue the 10% premium rent policy.

BOARD ACTION

ATTACHMENTS

1. Idaho Code, §58-304
2. Rent History
3. June 16, 1988 Rental Phase-In Schedule Letter
4. July 10, 1990 Land Board Memorandum-Market Rent
5. June 11, 1991 Land Board Memorandum-Rental Policy
6. October 22, 1991 Land Board Memorandum-Appraisal
7. June 9, 1992 Land Board Memorandum-Subcommittee
8. Payette Lake Lease R-5064 Assignment History
9. Montana Analysis of Cabin Lease Rates
10. 1991 Knipe/McKevitt Market Rent Analysis

11. February 10, 1997 Spokesman-Review article
12. Page 62, Governor's Committee on Endowment Fund Investment Reform Report
13. Letters to and from Mr. Richard H. Greener
14. Spreadsheet on Projected Rents

BT:dw:lf

Exhibit 21

Land Bd. Agenda Memorandum, Land Board Cottage Site Subcommittee Report (Dec. 15, 1998)

STATE BOARD OF LAND COMMISSIONERS
December 15, 1998
Regular Agenda

SUBJECT

Land Board Cottage Site Subcommittee report

BACKGROUND

APPRAISAL

The Priest Lake and Payette Lake appraisal reports were complex multi-parcel appraisals requiring significant work. The appraisal reports were prepared in conformity with the requirements of the Uniform Standards of Professional Appraisal Practice (USPAP), in conformity with the appraisal instructions, and adequately documented with market evidence supporting the conclusion of value, as defined and as presented. The appraisals have been completed and accepted by the department.

RENTAL

The Priest Lake appraisal provided a conclusion of market rent at 3.5% of the unimproved market value with an annual escalator of eight percent strongly supported by the past 21 year trend study.

The Payette Lake appraisal suggests that a market rent at 4% of the fee simple value is equitable if the only aspect of the current rental policy subject to change is the rate of return.

The current market rent as adopted by the Board at their regular meeting of June 4, 1997 is 2.5% of current county assessed values. The 2.5% rate recognizes and takes into consideration the lessees sweat equity and site improvements. The county assessed value is recognized as lagging behind current market conditions due to the need of the counties to gather and extrapolate market data and the department's requirement to provide a six month notice of any rental change.

The 1999 interim rental rate is the same as the 1998 interim rental rate that was based on the greater of 2.5% of the 1992 assessed land value or 1997 rent plus 25%. At the June 9, 1998 meeting the Board voted to hold the 1999 rental rate at the 1998 interim rate to allow the appraisal process to be completed and the new rate to go into full effect for the year 2000.

APPEALS PROCESS

The last review by the subcommittee of the appeal process was at its meeting of May 6,

1998. It was felt at that time that it would be premature to finalize an appraisal appeal process without the completion of the appraisals.

At the May 6, 1998 subcommittee meeting the lessees were seeking an appeal process that would provide that the ultimate review by the district court would be on a de novo basis.

The department had proposed that appeals of appraised value must be filed with the department. After review by a department panel, if still aggrieved a request for reconsideration must be made with the Board. An interim step to Board reconsideration may include a review by a Board subcommittee.

Any party to the administrative appeal proceeding who is aggrieved can seek judicial review under the Idaho Administrative Procedures Act (IDAPA) and Idaho Code §§ 67-5720 to 62-5279.

HARDSHIP CLAIMS

The Board at their regular June 9, 1998 meeting accepted in general principle the parameters for hardship claims with adoption contingent upon the development of a specific format in concurrence with legal counsel. Essentially, any lessee forced to sell due to escalating rental could ask for deferment of any increase in rental for a period of up to three years. Payment of deferred rent would be due upon sale of the leasehold or at the expiration of the deferment. The deferred rent would be subject to interest at the Board rate and a lien would be taken on the improvements to protect the state's interest.

10% PREMIUM RENT

Currently, upon sale of a lease, the Board requires that 10% of the leasehold value be paid to the endowment as premium rental. Leasehold value is determined by subtracting the value of improvements and personal property sold from the total sale price.

The lessee has the option to determine the value of improvements by using the county assessed valuation of improvements or paying for a department administered appraisal of improvement value. The personal property value is an itemized list of the personal property and values prepared by the lessee.

The Board has in the past agreed to review the 10% premium rent policy as a part of any review of rental policy.

DISCUSSION

The Board's cottage site subcommittee met with lessee representatives, their legal counsel, other interested lessees and the department on November 23, 1998. The discussion included a review of the Priest Lake and Payette Lake appraisal reports, rental rate, appeal process, hardship claims, and 10 % premium.

Payette Lake lessee representatives and legal counsel proposed the following:

1. Use 2.5% of county assessed value of the land for rental purposes.

2. Write the rental rate formula into new lease.

3. Consider a 5 year phase-in of rental.

4. Adopt the department's proposed appeal process that allows an appeal first to the department, then to the Land Board and ultimately to judicial review. The judicial review would be based on the Board's record.

5. Use the already agreed to parameters for hardship claims.

6. Do away with the 10% premium rent.

Priest Lake lessee representative and consulting appraiser discussed the Payette Lake proposal and the review of the Priest Lake appraisal report. Priest Lake would need to give further consideration to the proposed rental rate formula and appeal process, but concurred with the proposed 5 year phase-in of rental, proposed elimination of the 10% premium rent and use of the adopted parameters for hardship claims. They felt disappointed in the appraisal process in that there was a lack of lessee participation and the appraisal report did not address all their concerns. They disagreed with the appraised fee simple value and the market rent as determined by the appraisal.

The subcommittee and the lessees agreed that the current rental rate formula percentage of 2.5% is acceptable. The 2.5% rate recognized and takes into consideration the lessees sweat equity and lessee improvements.

Department staff believes that the only way to know for sure if the lease rental rate is at market rent is to monitor the lease assignment leasehold value. If leasehold values remain substantially high with full implementation of the 2.5 percent figure market rent has not been achieved. If, on the other hand, leasehold value is reduced to nearly zero, market rent is being paid.

Leasehold value results from the economic principle that a buyer will pay a premium to a current leaseholder to assume a lease when the lease rent is less than market rent. When market rent is reached leasehold values should be nearly zero and the market for cabins should remain active. This principle is reiterated in the Priest Lake appraisal.

The proposed phase-in period of five years was discussed with consideration given to the increase in rental rates, the requirement of Idaho Code § 58-310A that states, "the board shall ensure that each leased lot generates market rent throughout the duration of the lease", and the Board's adopted 1999 interim rental rate. Some of the scenarios discussed included a full fee in year 2000 or a percentage cap with full fee by year 2002. A vast

majority of the leases would reach full rental in year 2002 with less than a 70% per year increase, however, a 70% per year increase will be necessary for all leases to reach market rent by the year 2002.

The subcommittee discussed the proposal to write the rental rate into the lease by means of issuing new 10 year leases or amending the existing leases. Issuance of new 10 year leases appears to be the preferred alternative. Allowance for mortgage agreements during the term of a lease will require that the year 2009 be specifically identified for review of the rental rate by the Board. Revision of the leases will require legal counsel review and assistance to bring the lease form up to current standards.

The department proposed appeal process will allow county assessed valuations to be appealable to the department. The department will obtain county assessed values on an annual basis to maintain current values for determination of the lease rental rates.

The lessees are interested in eliminating the 10% premium rent. They indicated that the Board has agreed to its demise at such time as market rent has been obtained. If market rent is being paid there is little or no leasehold value so the 10% premium rental will be eliminated. No action would be necessary to accomplish this portion except to insure market rent is achieved.

Department staff believes that the deduction of personal property value from the lease sale price to determine leasehold value is questionable. Personal property is typically not recognized or considered by lending institutions or mortgage companies. The acceptance of lessee provided values affecting the premium payment seems contrary to the Utah case wherein the Utah Supreme Court determined that the state must administer appraisal contracts of state land values to avoid undue influence by a purchaser/lessee. Legal counsel has advised that it is likely that an Idaho court would rule similarly. The deletion of personal property from the 10% premium calculations will eliminate potential lessee influence on value and an administrative concern.

RECOMMENDATIONS FROM THE SUBCOMMITTEE

1. Retain the current market rent as adopted by the Board at their regular meeting of June 4, 1997 which is 2.5% of current county assessed values. For clarification purposes, the current assessed or appraised fee simple value of the land is determined as though the land is vacant and unimproved, subject to any outstanding rights and reservations of record and may at the Department of Lands discretion be determined by a department administered appraisal or county assessed valuation. The 2.5% rate recognizes and takes into consideration the lessee's sweat equity and lessee site improvements. Therefore there would be no deduction or credit granted for lessee site improvements.

2. Write the rental rate formula into new 10 year leases. This would provide for rental rate stability which has been a major concern with lessees. Any subsequent lease

amendments or extensions for mortgage purposes will be specific to a review of rental rate in the year 2009. Revision of the cottage site recreational lease will be dependent upon legal counsel review. The new lease would be effective January 1, 2000 and expire December 31, 2009.

3. Any phase-in of rental rate be considered by the full Land Board.

4. Adopt the Department of Lands proposed appeal process (Attachment #5).

5. Retain the current parameters for hardship claims as adopted by the Board at their regular June 9, 1998 meeting (Attachment 6).

6. Retain the current 10% premium rent. This recommendation will become moot if market rent is achieved.

In addition to the Subcommittee recommendations staff recommends that the current 10% premium rent be revised to eliminate the personal property value. The leasehold value shall be determined by subtracting the value of improvements as determined by county assessed value or department administered appraisal from the total sale price.

APPROVED DEC 1 5 1998

BOARD ACTION

The motion was made by State Controller Williams to approve the recommendation of the department with the modification that the appraised values at Priest Lake include values as determined by the assessor. That there be no phase-in and that the appeal processes outlined be approved and that the hardship parameters be approved and that the 10% premium rent be retained. Attorney General Lance seconded the motion. The motion carried on a vote of 5-0. Director Hamilton stated for clarification that it includes writing it into the new leases. State Controller Williams said that the leases would be rewritten. He also added that the motion included the staff recommendation that the current 10% premium rent be reviewed to eliminate the personal property value. Attorney General Lance concurred that the motion included the staff recommendation regarding the 10% premium rent.

ATTACHMENTS

1. November 23, 1998 Land Board Subcommittee Memorandum with attachments
2. Lease Assignments
3. Rental Rates 1998-2002
4. Assessed land values
5. Department appraisal appeal process
6. Hardship claim parameters

AC:dw
c:\data\wpwin\12-15lbm.mem

Exhibit 22

Land Bd. Agenda Memorandum,

2009 Rent Changes for the Payette Lake

and Priest Lake Cottage Sites

(June 19, 2008)

STATE BOARD OF LAND COMMISSIONERS
June 19, 2008
Regular Agenda Item

SUBJECT

2009 rent changes for the Payette Lake and Priest Lake cottage sites

BACKGROUND

In accordance with the Payette Lake and Priest Lake cottage site leases, the Department is required to provide a 180-day written notice of pending rent increases to all lessees. Notices of the rent changes will be mailed to the lessees the week of June 23 to meet the July 1 deadline. Actual invoices will be mailed in November with first half rent due January 1, 2009 and second half rent due June 1, 2009.

During June of last year, the Department mailed the 180-day notice of pending rent increases to all lessees for the 2008 rent. The Board, however, took action at a December 4, 2007 special meeting freezing the 2008 rent for the Payette Lake cottage sites (at the 2007 rate) for one year only. The Board took this action based on pending increases that averaged 48% for waterfront lots and 87% for non-waterfront lots. The largest increase for a waterfront lot was 49% and the largest increase for a non-waterfront lot was 144%.

The Land Board has received letters from the Payette Lake lessee association (April 25, 2008 letter from Jim Young, Payette Lake Cabin Owners Association - Attachment 1) and the Priest Lake cottage site lessee association (May 23, 2008 letter from Charles B. Lempesis - Attachment 2) requesting a freeze of the 2009 rent.

DISCUSSION

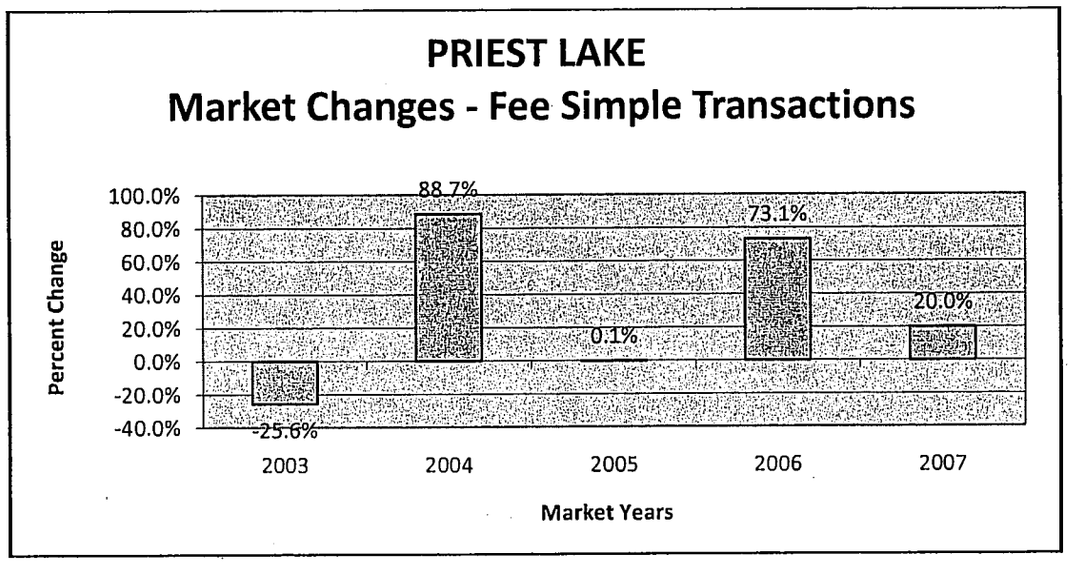
PAYETTE COTTAGE SITES

In accordance with the cottage site lease, the rent for the Payette Lake cottage sites is 2.5% of the assessed land value as determined by the Valley County Assessor's office. The Department receives the data annually from Valley County and applies the rental formula for the forthcoming rental year. The 2008 assessment data that applies to the 2009 rent was provided by Valley County on June 2, 2008. The data indicates that with the exception of one lot, all of the 2008 Payette Lake cottage site assessed values remain the same as the 2007 final assessed values. The value for Lease R-5013, the one exception, was reduced by $111,120 from the 2007 assessed value of $2,222,470. Recent Payette Lake cottage site assessed values and rental rates data is included in Attachment 3. Assignment data from 2007 and 2008 is included as Attachment 4. Revenue data considering frozen rent scenarios is included as Attachment 5. Rent data based on the Department's recommendation is included as Attachment 6.

PRIEST LAKE COTTAGE SITES

In accordance with the cottage site lease, the rent for the Priest Lake cottage sites is 2.5% of the appraised land value as determined by the Department appraisal contractor. Appraisals of individual cottage sites are completed every five years with an indexing process applied in "non-appraisal" years. 2009 is a "non-appraisal" year for all of the Priest Lake cottage sites. The Department contracted with Columbia Valuation Group (CVG) to complete an evaluation of the market data from the past five years in order to develop an indexing rate for the 2009 cottage site rent. This indexing process is defined in the cottage site leases. A copy of the CVG report is included as Attachment 7.

The following chart reflects the market data collected by CVG for fee simple, land-only transactions in the Priest Lake market area. The overall percentage change during this five-year timeframe is 192.3%. Applying a compounded average, CVG recommended a 23% indexing increase for the 2009 Priest Lake rent. The cottage site lease stipulates that indexing increases greater than 5% are appealable.



The following indexing increases have been applied at Priest Lake:

2006 -	5% (applied to only 60 lots, remainder appraised)
2007 -	12%
2008 -	15%
2009 (proposed)	23%

The Priest Lake indexing process has successfully buffered the market spikes found objectionable by the Payette Lake cottage site market and should not be abandoned within the current lease term.

Assignment data from 2007 and 2008 is included as Attachment 4. Revenue data considering frozen rent scenarios is included as Attachment 5. Rent data based on the Department's recommendation is included as Attachment 6.

RECOMMENDATION

The Department recommends the Board apply the rent increase to the 2009 Payette Lake cottage site rent consistent with the 2008 Valley County assessed values. The Department also recommends that the Board apply the indexing method to the Priest Lake cottage sites, as outlined in the cottage site lease, for the 2009 rent at the CVG recommended rate of 23%.

BOARD ACTION

A motion was made by Secretary of State Ysursa to raise the rate for cottage site rent across the board for next year at fifteen percent for waterfront and secondary lots at Payette Lake and lakefront lots at Priest Lake. Controller Jones seconded the motion for discussion purposes. Controller Jones noted that Secretary of State Ysursa indicated a need for additional time to continue reviewing this matter. She asked that Secretary of State Ysursa amend his motion to a time certain. Secretary of State Ysursa amended his motion that the Board raise the rate for cottage site rent across the board fifteen percent with the proviso that the subcommittee will report back to the Board on or before December 1, 2008, with a new methodology on price. Controller Jones seconded the amended motion. The amended motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.

ATTACHMENTS

1. April 25, 2008 letter from Jim Young, Payette Lake Cabin Owners Association
2. May 23, 2008 letter from Charles B. Lempesis
3. Payette Lake Cottage Site Assessed Value and Rent History
4. Assignment data for Priest and Payette Lake – 2007 and 2008
5. Revenue data considering frozen rent scenarios
6. Rent data based on Department recommendation
7. CVG Report

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

Payette Lake Cabin Owners Association
711 East Broadway
Meridian, Idaho 83642

April 25, 2008

Ben Ysursa, Secretary of State
Office of Secretary of State
PO Box 83720
Boise ID 83720-0080

Superintendent Tom Luna
Superintendent of Public Instruction
Idaho State Board of Education
PO Box 83720
Boise, ID 83720-0037

RE: Payette Lake Cottage Leases – 2009 Rent – Request for Extension of Rent Freeze.

Dear Secretary Ysursa and Superintendent Luna,

Thank you for allowing us to participate in the Subcommittee meeting held April 22, 2008. During the meeting it was noted that the current cottage site lease requires a six month notice to lessee for any increases in rent. As such, this would require notice by June 30, 2008 for any change in rent starting January 1, 2009. Secretary Ysursa requested we give our view with regard to potential increases in rent for 2009.

The members of the Payette Lake Cabin Owners Association request an extension of the current rent freeze until such time as the new lease currently being negotiated is in place. All of the facts, circumstances, reasons and conditions which led to the Land Board's decision to freeze rents at the Special Meeting held in December, 2007 remain and the overall conditions affecting the general Valley County real estate market have worsened and deteriorated . Indisputably, Valley County is in the midst of a painful economic slump with little real estate activity, plummeting real estate prices and very little, if any, new positive economic activity. More specifically, the market for State leased property around Payette Lake continues to be non-existent.

At the December 2007 Special Meeting, the Land Board members unanimously acknowledged that the cottage site lease program is broken and needs fixing. Land Board members correctly expressed their legitimate concern that a broken cottage site lease program jeopardized both current and future income streams for the State Endowment. Further, several of the Land Board members acknowledged that neither the State nor the lessees contemplated the conditions that lead to the unprecedented rent escalation experienced in recent years at Payette Lake and none would have agreed had those conditions been known.

There seems to be general consensus that the rent charged to lessees should reflect market rent. Lessees expect and are willing to pay a fair market rent. Presently, however, there is no general agreement about how to arrive at a fair market rent. Lessees contend, as demonstrated by the non-existent cottage site lease market at Payette Lake that the current cottage site lease rent is well above market. Given the universally depressed market conditions in Valley County, it is unthinkable to posit that true market rents have increased or will increase during 2008.

As Secretary Ysursa correctly stated: "we need to fix what is broken." Thankfully, the Subcommittee members, the Idaho Department of Land and the lessees are meaningfully engaged in a collaborative process to "make that fix" by crafting a lease that will stabilize the cottage site leasing program for the current and long term. We have every expectation that we can arrive at a new lease which will fairly determine market rent and the other lease terms.

An increase in rents at this time is not supported by the current market conditions and, as such, would undermine the current "fix and repair efforts" as it would exacerbate the conditions that broke the leasing program in the first place. We respectfully urge you to extend the freeze until such time as the new lease is in place.

Again, we appreciate the time and effort you have dedicated to this important issue. We look forward to continuing our work with you to arrive at a fair solution for all parties.

Very truly yours,

Jim B. Young, President

Cc: Governor Butch Otter
Attorney General Lawrence Wasden
Controller Donna Jones
Director George Bacon, Idaho Department of Land

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

Charles B. Lempesis, Chtd
attorney at law

May 23, 2008

DEPT. OF LANDS
08 MAY 27 AM 9:09
BOISE, IDAHO

Honorable Ben Ysursa, Secretary of State
700 West Jefferson Street
P. O. Box 83720
Boise, ID 83720-0080

Honorable Tom Luna, Superintendent of Schools
650 West State Street
P. O. Box 83720
Boise, ID 83720-0027

RE: **Priest Lake State Lessees Association/2009 Rent - Request for Moratorium on Increases**

Dear Secretary Ysursa and Superintendent Luna:

First of all, let me express the sincere appreciation of the Priest Lake State Lessees Association for the courtesy, cooperation and candor displayed by the two of you and your able staff at the Cottage Site Subcommittee Meeting of April 22, 2008. All of us left that meeting with a genuine belief that we can work together to find a fair and long lasting solution to the calculation and collection of fair market rents.

We also appreciate your recognition that we "need to fix what is broken". We are encouraged that we have tasked each of our appraisers to work together to search for and make recommendations for a process that better reflects an accurate assessment of "market rent". I note that they have already agreed on the parameters of their mission.

The Priest Lake State Lessees Association is aware that in December 2007, the Land Board determined that it was appropriate to freeze rents for the Payette Lake Lessees pending resolution of the concerns we are now addressing. At that time, this rent freeze was not applied to Priest Lake, and the Priest Lake State Lessees Association did not object.

At this time, we believe the rent freeze should be applied to Priest Lake cottage site leases as well, given the rapid decline in real estate values in North Idaho, and the

201 West Seventh Avenue *Post Falls, Idaho 83854*
Telephone 208 777-8815 *Facsimile 208 773-1044*

---

general deterioration of economic conditions in the state and national housing market. It is apparent that the "indexing" used to determine rent increases for Priest Lake has, in light of these deteriorating economic conditions, become skewed and manifestly unfair as it is based in large part on prior years that reflect the peak of market conditions and high prices.

We would respectfully ask that any rent increases for Priest Lake cottage site leases for 2009 be deferred or abated. Any loss of revenue to the state, if any, will be significantly outweighed by the opportunity to find a solution that creates long term stable rents that accurately reflect market rent in accordance with appropriate appraisal standards and practices.

Once again, we want to thank you for the courtesy of our meeting, and thank you in advance for your consideration of this important request. We look forward to working with you throughout the year in a cooperative and forthright manner to achieve a mutually acceptable resolution that is long overdue.

Very Truly Yours,

CBL/cyb

CHARLES B. LEMPESIS
Attorney for Priest Lake State Lessees Association

CBL/cyb

cc: Honorable Butch Otter, Governor
Honorable Lawrence Wasden, Attorney General
Honorable Donna Jones, Controller
Director George Bacon, Idaho Department of Lands

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5003	$1,263,140	$1,879,400	$1,879,400	$31,579	$31,579	$46,985	$15,407	49%
5004	$1,254,450	$1,858,800	$1,858,800	$31,361	$31,361	$46,470	$15,109	48%
5005	$1,119,680	$1,665,940	$1,665,940	$27,992	$27,992	$41,649	$13,657	49%
5006	$1,318,760	$1,962,140	$1,962,140	$32,969	$32,969	$49,054	$16,085	49%
5007	$621,840	$925,220	$925,220	$15,546	$15,546	$23,131	$7,585	49%
5009	$1,340,840	$1,995,000	$1,995,000	$33,521	$33,521	$49,875	$16,354	49%
5010	$1,148,590	$1,708,970	$1,708,970	$28,715	$28,715	$42,724	$14,010	49%
5011	$1,382,330	$2,056,720	$2,056,720	$34,558	$34,558	$51,418	$16,860	49%
5012	$1,380,210	$2,053,570	$2,053,570	$34,505	$34,505	$51,339	$16,834	49%
5013	$1,493,730	$2,222,470	$2,111,120	$37,343	$37,343	$52,778	$15,435	41%
5014	$633,430	$937,030	$937,030	$15,836	$15,836	$23,426	$7,590	48%
5015	$959,390	$1,423,220	$1,423,220	$23,985	$23,985	$35,581	$11,596	48%
5016	$1,263,970	$1,880,620	$1,880,620	$31,599	$31,599	$47,016	$15,416	49%
5018	$1,213,810	$1,806,000	$1,806,000	$30,345	$30,345	$45,150	$14,805	49%
5019	$992,860	$1,477,250	$1,477,250	$24,822	$24,822	$36,931	$12,110	49%
5020	$386,550	$575,140	$575,140	$9,664	$9,664	$14,379	$4,715	49%
5023	$1,228,710	$1,828,170	$1,828,170	$30,718	$30,718	$45,704	$14,987	49%
5024	$795,320	$1,118,690	$1,118,690	$19,883	$19,883	$27,967	$8,084	41%
5025	$1,140,080	$1,696,300	$1,696,300	$28,502	$28,502	$42,408	$13,906	49%
5027	$764,140	$1,126,380	$1,126,380	$19,104	$19,104	$28,160	$9,056	47%
5028	$619,920	$909,670	$909,670	$15,498	$15,498	$22,742	$7,244	47%
5029	$815,120	$1,210,250	$1,210,250	$20,378	$20,378	$30,256	$9,878	48%
5031	$879,930	$1,174,790	$1,174,790	$21,998	$21,998	$29,370	$7,372	34%
5032	$608,790	$899,790	$899,790	$15,220	$15,220	$22,495	$7,275	48%
5034	$1,469,890	$2,187,010	$2,187,010	$36,747	$36,747	$54,675	$17,928	49%
5035	$827,860	$1,231,750	$1,231,750	$20,697	$20,697	$30,794	$10,097	49%
5036	$1,379,150	$2,052,000	$2,052,000	$34,479	$34,479	$51,300	$16,821	49%
5037	$1,277,040	$1,900,070	$1,900,070	$31,926	$31,926	$47,502	$15,576	49%
5039	$860,830	$1,275,270	$1,275,270	$21,521	$21,521	$31,882	$10,361	48%
5040	$961,900	$1,430,660	$1,430,660	$24,048	$24,048	$35,767	$11,719	49%
5041	$765,600	$1,082,160	$1,082,160	$19,140	$19,140	$27,054	$7,914	41%
5042	$1,251,450	$1,862,000	$1,862,000	$31,286	$31,286	$46,550	$15,264	49%

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5043	$1,076,360	$1,601,480	$1,601,480	$26,909	$26,909	$40,037	$13,128	49%
5044	$792,330	$1,013,200	$1,013,200	$19,808	$19,808	$25,330	$5,522	28%
5045	$1,406,450	$2,092,620	$2,092,620	$35,161	$35,161	$52,316	$17,154	49%
5046	$876,310	$1,300,110	$1,300,110	$21,908	$21,908	$32,503	$10,595	48%
5049	$1,203,190	$1,790,200	$1,790,200	$30,080	$30,080	$44,755	$14,675	49%
5050	$524,900	$782,101	$782,101	$13,122	$13,122	$19,553	$6,430	49%
5051	$507,889	$756,755	$756,755	$12,697	$12,697	$18,919	$6,222	49%
5052	$838,370	$1,247,400	$1,247,400	$20,959	$20,959	$31,185	$10,226	49%
5055	$362,423	$540,010	$540,010	$9,061	$9,061	$13,500	$4,440	49%
5056	$565,690	$842,878	$842,878	$14,142	$14,142	$21,072	$6,930	49%
5057	$463,302	$690,320	$690,320	$11,583	$11,583	$17,258	$5,675	49%
5058	$696,460	$914,340	$914,340	$17,412	$17,412	$22,859	$5,447	31%
5059	$1,358,420	$2,021,150	$2,021,150	$33,961	$33,961	$50,529	$16,568	49%
5060	$804,750	$1,190,750	$1,190,750	$20,119	$20,119	$29,769	$9,650	48%
5062	$612,150	$910,800	$910,800	$15,304	$15,304	$22,770	$7,466	49%
5063	$1,236,380	$1,839,580	$1,839,580	$30,910	$30,910	$45,990	$15,080	49%
5064	$1,264,220	$1,881,000	$1,881,000	$31,606	$31,606	$47,025	$15,420	49%
5067	$1,137,640	$1,692,670	$1,692,670	$28,441	$28,441	$42,317	$13,876	49%
5069	$1,379,680	$2,052,800	$2,052,800	$34,492	$34,492	$51,320	$16,828	49%
5070	$1,289,120	$1,918,040	$1,918,040	$32,228	$32,228	$47,951	$15,723	49%
5071	$892,310	$1,327,650	$1,327,650	$22,308	$22,308	$33,191	$10,884	49%
5072	$1,251,450	$1,862,000	$1,862,000	$31,286	$31,286	$46,550	$15,264	49%
5073	$1,251,450	$1,862,000	$1,862,000	$31,286	$31,286	$46,550	$15,264	49%
5074	$1,172,510	$1,377,000	$1,377,000	$29,313	$29,313	$34,425	$5,112	17%
5075	$1,267,010	$1,696,630	$1,696,630	$31,675	$31,675	$42,416	$10,741	34%
5080	$656,360	$976,590	$976,590	$16,409	$16,409	$24,415	$8,006	49%
5082	$872,520	$1,298,200	$1,298,200	$21,813	$21,813	$32,455	$10,642	49%
5083	$1,264,220	$1,881,000	$1,881,000	$31,606	$31,606	$47,025	$15,420	49%
5201	$67,130	$123,519	$123,519	$1,678	$1,678	$3,088	$1,410	84%
5203	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5205	$79,410	$143,130	$143,130	$1,985	$1,985	$3,578	$1,593	80%
5208	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5209	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5210	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5211	$81,720	$123,510	$123,510	$2,043	$2,043	$3,088	$1,045	51%
5213	$56,220	$116,590	$116,590	$1,406	$1,406	$2,915	$1,509	107%
5215	$59,850	$134,270	$134,270	$1,496	$1,496	$3,357	$1,861	124%
5216	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5218	$57,590	$117,380	$117,380	$1,440	$1,440	$2,935	$1,495	104%
5220	$64,390	$118,620	$118,620	$1,610	$1,610	$2,966	$1,356	84%
5221	$71,140	$118,190	$118,190	$1,779	$1,779	$2,955	$1,176	66%
5222	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5224	$71,380	$132,100	$132,100	$1,785	$1,785	$3,303	$1,518	85%
5225	$65,330	$119,000	$119,000	$1,633	$1,633	$2,975	$1,342	82%
5226	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5227	$81,240	$122,780	$122,780	$2,031	$2,031	$3,070	$1,039	51%
5228	$76,780	$121,770	$121,770	$1,920	$1,920	$3,044	$1,125	59%
5229	$76,490	$141,460	$141,460	$1,912	$1,912	$3,537	$1,624	85%
5230	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5231	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5232	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5233	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5234	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5235	$90,670	$144,250	$144,250	$2,267	$2,267	$3,606	$1,340	59%
5236	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5239	$71,380	$139,050	$139,050	$1,785	$1,785	$3,476	$1,692	95%
5240	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5241	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5242	$119,770	$158,480	$158,480	$2,994	$2,994	$3,962	$968	32%
5243	$74,680	$139,880	$139,880	$1,867	$1,867	$3,497	$1,630	87%
5244	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5245	$65,510	$119,330	$119,330	$1,638	$1,638	$2,983	$1,346	82%
5247	$99,280	$131,440	$131,440	$2,482	$2,482	$3,286	$804	32%
5248	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5249	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5251	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5252	$62,630	$133,520	$133,520	$1,566	$1,566	$3,338	$1,772	113%
5254	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5255	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%
5256	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%
5257	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5259	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5260	$89,250	$124,200	$124,200	$2,231	$2,231	$3,105	$874	39%
5261	$75,760	$122,070	$122,070	$1,894	$1,894	$3,052	$1,158	61%
5262	$59,190	$116,250	$116,250	$1,480	$1,480	$2,906	$1,427	96%
5263	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%
5264	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5265	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5266	$65,480	$136,240	$136,240	$1,637	$1,637	$3,406	$1,769	108%
5267	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5269	$55,430	$114,940	$114,940	$1,386	$1,386	$2,874	$1,488	107%
5270	$65,480	$136,420	$136,420	$1,637	$1,637	$3,411	$1,774	108%
5271	$67,310	$119,650	$119,650	$1,683	$1,683	$2,991	$1,309	78%
5272	$74,380	$121,700	$121,700	$1,860	$1,860	$3,043	$1,183	64%
5273	$76,950	$122,030	$122,030	$1,924	$1,924	$3,051	$1,127	59%
5274	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5275	$62,630	$133,520	$133,520	$1,566	$1,566	$3,338	$1,772	113%
5276	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%
5278	$64,610	$134,690	$134,690	$1,615	$1,615	$3,367	$1,752	108%
5279	$57,720	$134,440	$134,440	$1,443	$1,443	$3,361	$1,918	133%
5280	$83,130	$144,080	$144,080	$2,078	$2,078	$3,602	$1,524	73%
5282	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5283	$63,110	$136,190	$136,190	$1,578	$1,578	$3,405	$1,827	116%
5284	$63,770	$135,320	$135,320	$1,594	$1,594	$3,383	$1,789	112%
5285	$65,320	$134,240	$134,240	$1,633	$1,633	$3,356	$1,723	106%
5286	$49,830	$116,500	$116,500	$1,246	$1,246	$2,913	$1,667	134%

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5287	$42,020	$120,060	$120,060	$1,051	$1,051	$3,002	$1,951	186%
5288	$69,930	$136,300	$136,300	$1,748	$1,748	$3,408	$1,659	95%
5290	$62,630	$133,520	$133,520	$1,566	$1,566	$3,338	$1,772	113%
5291	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5294	$65,480	$136,240	$136,240	$1,637	$1,637	$3,406	$1,769	108%
5298	$54,570	$132,890	$132,890	$1,364	$1,364	$3,322	$1,958	144%
5299	$72,420	$137,420	$137,420	$1,811	$1,811	$3,436	$1,625	90%
5300	$68,200	$121,220	$121,220	$1,705	$1,705	$3,031	$1,326	78%
5304	$62,170	$136,400	$136,400	$1,554	$1,554	$3,410	$1,856	119%
5306	$56,780	$134,870	$134,870	$1,420	$1,420	$3,372	$1,952	138%
5307	$55,260	$137,920	$137,920	$1,382	$1,382	$3,448	$2,067	150%
5309	$64,660	$137,010	$137,010	$1,617	$1,617	$3,425	$1,809	112%
5310	$62,040	$116,130	$116,130	$1,551	$1,551	$2,903	$1,352	87%
5313	$75,490	$139,650	$139,650	$1,887	$1,887	$3,491	$1,604	85%
5314	$95,560	$161,280	$161,280	$2,389	$2,389	$4,032	$1,643	69%
5315	$65,050	$136,730	$136,730	$1,626	$1,626	$3,418	$1,792	110%
5316	$106,321	$195,630	$195,630	$2,658	$2,658	$4,891	$2,233	84%
5319	$78,030	$143,130	$143,130	$1,951	$1,951	$3,578	$1,628	83%
5322	$99,150	$144,250	$144,250	$2,479	$2,479	$3,606	$1,128	45%
5323	$66,260	$120,890	$120,890	$1,657	$1,657	$3,022	$1,366	82%
5327	$62,880	$135,610	$135,610	$1,572	$1,572	$3,390	$1,818	116%
5328	$43,003	$79,125	$79,125	$1,075	$1,075	$1,978	$903	84%
5329	$91,040	$143,840	$143,840	$2,276	$2,276	$3,596	$1,320	58%
5331	$73,040	$156,850	$156,850	$1,826	$1,826	$3,921	$2,095	115%
5336	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5338	$56,530	$120,650	$120,650	$1,413	$1,413	$3,016	$1,603	113%
5340	$67,590	$135,880	$135,880	$1,690	$1,690	$3,397	$1,707	101%
5341	$62,630	$137,250	$137,250	$1,566	$1,566	$3,431	$1,866	119%
5343	$62,170	$136,500	$136,500	$1,554	$1,554	$3,413	$1,858	120%
5346	$55,430	$114,940	$114,940	$1,386	$1,386	$2,874	$1,488	107%
5348	$64,610	$94,280	$94,280	$1,615	$1,615	$2,357	$742	46%
5349	$67,130	$119,330	$119,330	$1,678	$1,678	$2,983	$1,305	78%

Payette Lake Cottage Site Assessed Value and Rent History

Lease #	2006 Assessed Value (for 2007 rent)	2007 Assessed Value (for 2008 rent)	2008 Assessed Values (for 2009 rent)	2007 Rent	2008 Rent	2009 Rent	Rent Increase from 2008 to 2009	% Increase from 2008 to 2009
5350	$59,770	$129,940	$129,940	$1,494	$1,494	$3,249	$1,754	117%
5351	$63,140	$118,190	$118,190	$1,579	$1,579	$2,955	$1,376	87%
5353	$61,990	$133,620	$133,620	$1,550	$1,550	$3,341	$1,791	116%
5355	$54,570	$132,890	$132,890	$1,364	$1,364	$3,322	$1,958	144%
5357	$99,280	$131,490	$131,490	$2,482	$2,482	$3,287	$805	32%
5901	$627,970	$934,340	$934,340	$15,699	$15,699	$23,359	$7,659	49%
5903	$806,120	$1,199,400	$1,199,400	$20,153	$20,153	$29,985	$9,832	49%
5904	$689,330	$1,025,640	$1,025,640	$17,233	$17,233	$25,641	$8,408	49%

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

2008 Cottage Site Assignment Data

Priest Lake

Lease	Waterfront	2007 Value (for 2008 Rent)	2008 Rent	Sale Price	Improvements	Leasehold Value	Premium Rent	Year	Assignment
R1123	yes	$302,680	$7,567	$600,000	$430,000	$170,000	$17,000	Jan-08	Sale
R1196	yes	$359,352	$8,984	NA	NA	NA	NA	Jan-08	Family
R1202	yes	$358,064	$8,952	$565,000	$172,766	$392,234	$39,223	Jan-08	Sale
R1301	yes	$267,904	$6,698	$575,000	$381,041	$193,959	$19,396	Jan-08	Sale
R1021	yes	$226,688	$5,667	NA	NA	NA	NA	Feb-08	Trust
R1252	yes	$310,408	$7,760	NA	NA	NA	NA	Apr-08	Trust
R1166	yes	$231,260	$5,782	NA	NA	NA	NA	May-08	Trust

Payette Lake

Lease	Waterfront	2007 Value (for 2008 Rent)	2008 Rent	Sale Price	Improvements	Leasehold Value	Premium Rent	Year	Assignment
R5269	no	$55,430	$1,386	NA	NA	NA	NA	Jan-08	Family
R5287	no	$42,020	$1,051	NA	NA	NA	NA	Jan-08	Family
R5285	no	$65,320	$1,633	$125,000	$46,190	$78,810	$7,881	Jan-08	Sale
R5023	yes	$1,228,710	$30,718	NA	NA	NA	NA	Feb-08	Family
R5213	no	$56,220	$1,406	$175,000	$51,950	$123,050	$12,305	Mar-08	Sale

ATTACHMENT

2007 Cottage Site Assignment Data

Priest Lake

Lease	Waterfront	2006 Value (for 2007 Rent)	2007 Rent	Sale Price	Improvements	Leasehold Value	Premium Rent	Year	Assignment
R1219	yes	$134,400	$3,360	$325,000	$190,600	$134,400	$13,440	Jan-07	Sale
R1157	yes	$292,320	$7,308	$495,500	$106,274	$389,226	$38,923	Sep-07	Sale
R1183	yes	$238,728	$5,968	NA	NA	NA	NA	Jul-07	Trust
R1260	yes	$250,880	$6,272	$375,000	$102,897	$272,103	$27,210	Mar-07	Sale
R1350	yes	$203,840	$5,096	NA	NA	NA	NA	Mar-07	Family
R1005	yes	$228,420	$5,712	$490,000	$111,330	$378,670	$37,867	Oct-07	Sale
R1065	yes	$237,552	$5,939	$538,000	$159,940	$378,060	$37,806	Oct-07	Sale
R1254	yes	$202,720	$5,068	$450,000	$120,958	$329,042	$32,904	Oct-07	Sale
R1070	yes	$231,840	$5,796	$495,000	$141,538	$353,462	$35,346	Nov-07	Sale
R1089	yes	$235,200	$5,880	$430,000	$87,346	$342,654	$34,265	Nov-07	Sale
R1093	yes	$273,280	$6,832	$395,000	$65,396	$329,604	$32,960	Nov-07	Sale
R1117	yes	$239,904	$5,998	N/A	NA	N/A	N/A	Nov-07	Family
R1176	yes	$292,320	$7,308	$695,000	$376,311	$318,689	$31,869	Nov-07	Sale
R1280	yes	$250,880	$6,272	N/A	NA	N/A	N/A	Dec-07	Family

Payette Lake

Lease	Waterfront	2006 Value (for 2007 Rent)	2007 Rent	Sale Price	Improvements	Leasehold Value	Premium Rent	Year	Assignment
R5254	no	$63,140	$1,579	$210,000	$35,070	$174,930	$17,493	Feb-07	Sale
R5023	yes	$1,228,710	$30,718	$900,000	$36,720	$863,280	$86,328	Jul-07	Sale
R5045	yes	$1,406,450	$35,161	NA	NA	NA	NA	Aug-07	Trust
R5059	yes	$1,358,420	$33,961	NA	NA	NA	NA	Feb-07	Family
R5254	no	$63,140	$1,579	NA	NA	NA	NA	Apr-07	Family
R5263	no	$67,130	$1,678	$320,000	$159,400	$160,600	$16,060	Apr-07	Sale
R5273	no	$76,950	$1,924	NA	NA	NA	NA	Apr-07	Trust
R5327	no	$62,880	$1,572	NA	NA	NA	NA	Apr-07	Family
R5222	no	$63,140	$1,579	$168,630	$105,490	$63,140	$6,314	Oct-07	Sale

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

PAYETTE LAKE COTTAGE SITE REVENUE

	A 2008 with full increase 2009 with full increase	B 2008 frozen 2009 frozen	C 2008 frozen 2009 with full increase
2008 Rent	$2,631,494	$1,741,723	$1,741,723
2009 Rent	$2,628,710	$1,741,723	$2,628,710
TOTAL REVENUE	$5,260,204	$3,483,446	$4,370,433
Departure from Assessed Values		$1,776,757	$889,771

PRIEST LAKE COTTAGE SITE REVENUE

	E 2008 Rent 2009 (increased by 23%)	F 2008 Rent 2009 frozen
2008 Rent	$2,537,791	$2,537,791
2009 Rent	$3,121,484	$2,537,791
TOTAL REVENUE	$5,659,275	$5,075,583
Departure from Indexed Values		$583,692

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

RENT DATA BASED ON DEPARTMENT RECOMMENDATION

	2008 Average Rent	2009 Average Rent	2009 Rent Increase Lowest	2009 Rent Increase Highest	2009 Rent Increase Average
Priest Lake	$7,169	$8,818	$874	$2,978	$1,649
Payette Lake					
Waterfront Lots	$24,828	$36,436	$4,440	$17,928	$11,608
Non-waterfront Lots	$1,691	$3,173	$742	$2,233	$1,482

2009 RENT CHANGES FOR THE PAYETTE LAKE AND PRIEST LAKE COTTAGE SITES

COLUMBIA VALUATION GROUP, INC.
Real Estate Appraisers and Consultants

1602 East Sherman Avenue, Suite 100
Coeur d'Alene, ID 83814-5300
(208) 667-7940
Fax: (208) 666-1474

Stanley D. Moe, MAI
moecvg@verizon.net

May 01, 2008

Idaho Department of Lands
Attn: Craig Thompson
954 West Jefferson Street
Boise, ID 83720-0060

Re: Indexing Values for leased sites on Priest Lake, Bonner County, Idaho
Index rate for the period January through December 2007

Dear Mr. Thompson:

At your request we have completed our study of price changes for lakefront lots on Priest Lake over the past six years. The purpose of our study was to determine, from market data, the average rate of increase over the past five years, which rate will be used as an Index for adjusting lease rates in 2008. Using 2002 as the base year we calculated annual increases (or decreases if indicated by the data) as well as the overall value change through 2007.

For 2006 we researched and catalogued two sales. Our report last year showed only one sale that could be verified. It is a difficult and time consuming process because not all sales are reported in the Multiple Listing Service, or simply because Idaho is a non-disclosure state and the parties refused to discuss prices or terms. Due to privacy laws, information sources like title and escrow companies are not accessible. For 2007 we documented two sales, one of which is the resale of one of the 2006 sales. Our current assignment was to determine the average rate of change in value over the past five years for fee owned waterfront lots on Priest Lake.

There are currently four vacant lots on the market at Priest Lake, all located in Huckleberry at Priest Lake, South Shores Addition. We have attached a list that shows the asking prices are $5,500/ff. These properties were listed for sale at the time the two 2007 sales were closed at prices of $6,092/ff and $6,800/ff. The asking prices have risen at a compounded rate of 18.38% over the past five years. As a general rule, current asking prices set an upper limit for range of current market value, based on the principle of substitution, so one could surmise that the listed sites are somewhat inferior to the sites that sold. The four listings are along a very

steep section of shoreline where private driveway and foundation costs are higher than typical. The inferior topography, in our opinion, accounts for the lower asking price per front foot.

Market conditions change over time with inflation, national and local economic conditions, in or out-migration from an area, employment opportunities, etc. Ideally, sufficient recent sales data is available so that adjustments for value changes over time are not needed. When this is not the case, sales and resales or the use of "matched pairs" can be used to develop an indication of price trends. We documented two sales and resales of the same lot. Lot 23, Sandy Shores sold 5/12/2006 for $4,232/ff and then sold again October 15, 2007 for $6,800/ff, a 42.51% annual increase. Lot 15 South Shores sold March 15, 2003 for $1,879/ff and again on March 15, 2005 for $2,525/ff, a 16.91% annual increase.

Appreciation rarely occurs at an even or constant rate over several years. More typically, prices will increase rapidly during a one or two year period then level off for a time. Prices will sometimes decline for a period of time, as when interest rates skyrocketed in late 1979 and 1980, then recover as economic conditions return to a stabilized pattern. Negative changes in personal financial situations are usually first reflected in the recreational property market. Luxury items such as recreational property and "toys" are the first things to be liquidated. Conversely, positive changes are slow to reflect in the recreational property market. Our research indicates that most people invest in recreational properties with "discretionary funds." Some buy as investments with no intention of building or living in them full-time, but simply to cash in on value increases over time. As a result, market fluctuations tend to be more pronounced for this class of real estate, much like the stock market.

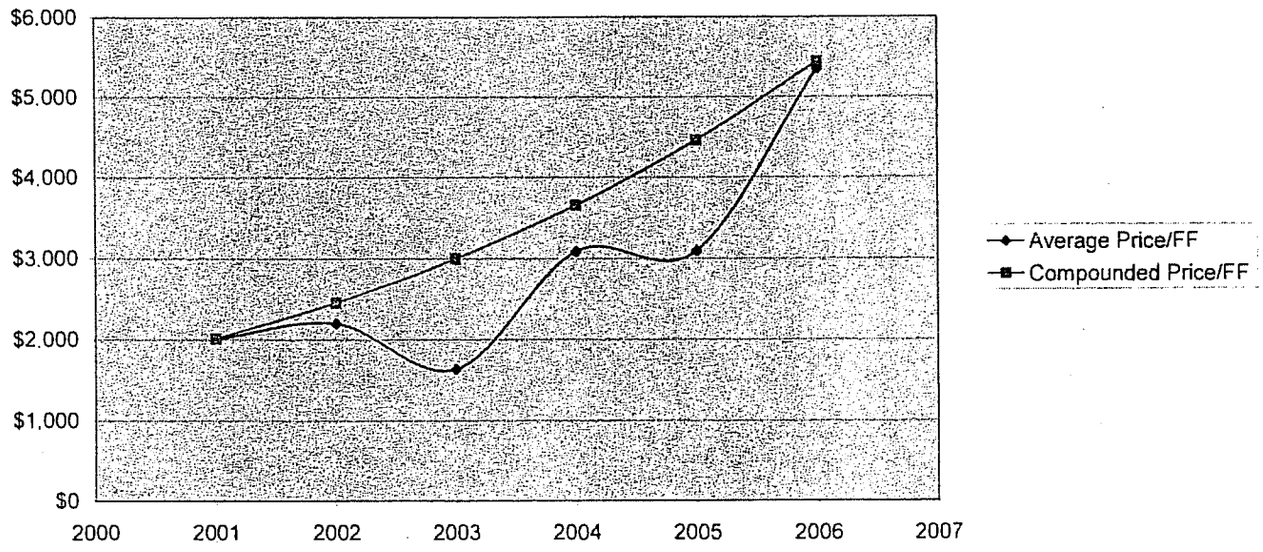
CONCLUSIONS

Tracking market changes for real estate is not an exact science because of the many variables that impact pricing and negotiations. At Priest Lake, as in many seasonal resort locations, real estate transactions generally coincide with the high resort season. During the winter, when most properties are inaccessible and visitors are scarce, the real estate market is almost dormant. Rather than a steady, month by month progression in value changes, prices generally change on a seasonal cycle. The active season at Priest Lake is between the end of April or first of May through August, and sometimes into September.

Sales of vacant lots have been few in number. One reason is the lack of available inventory (and undeveloped land to create new lots). Over the past five year period the average number of sales is just over three sales per year (16 sales in five years) with only two sales each year in 2006 and 2007. Prices for improved properties and undeveloped waterfront building sites have risen rapidly over the past five years, from $2,197/ff in 2002 to $6,423/ff in 2007. This change over five years represents an average of 38.5% per year and a compounded annual rate of 23.93%.

2001 - 2006 TIME FRAME

Average Sale Price/FF		% change	5 yr increase	Annual Compounded	Value using compounded rate of	22%
2001	$2,011				$2,011	
2002	$2,197	9%			$2,453	
2003	$1,636	-26%			$2,993	
2004	$3,086	89%			$3,652	
2005	$3,091	0%			$4,455	
2006	$5,351	73%	166%	21.62%	$5,435	



Because of the limited inventory of vacant waterfront building sites when compared to the number of improved sites, a 24% rate of appreciation over the past five years is not surprising. Any time demand exceeds supply for a commodity, prices tend to rise. This rate does seem high when compared with the core inflation rate for goods and services over the past 12 months of less than 3%, but core inflation rates have little association with real estate values. Core inflation excludes energy costs, food, and prescription drugs which are all increasing at record rates. With the current price trend for petroleum products related commodities such as RV's, boats, and remote recreational properties that require significant travel may very well decrease in cost in the near future.

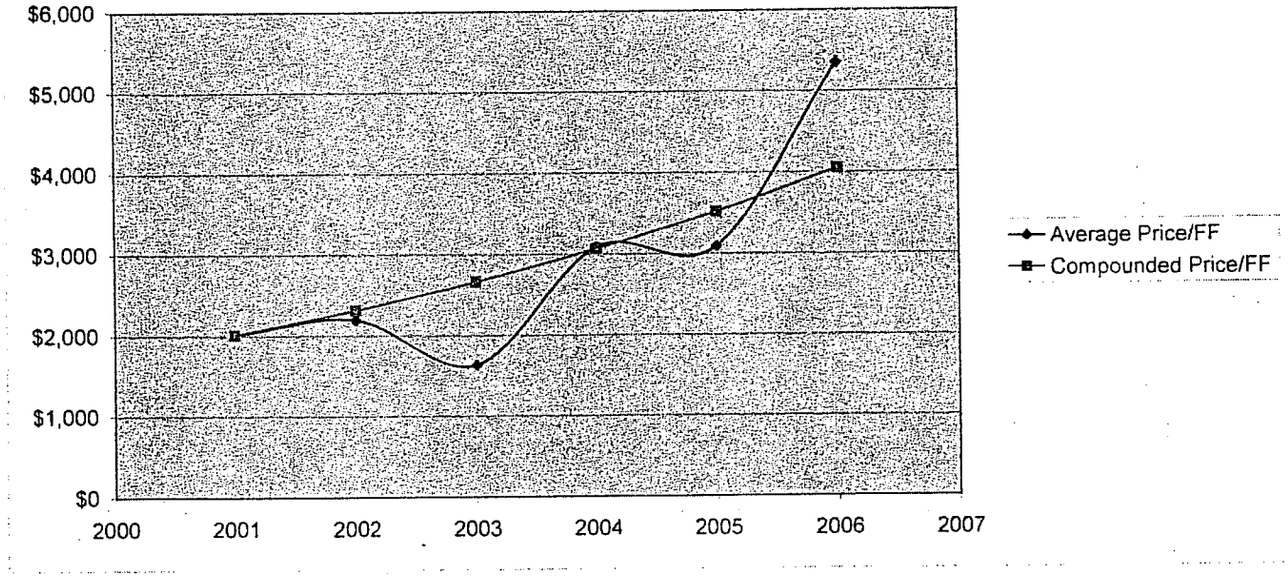
Estimating the five-year floating average of price increases is a challenge when there have only been two sales each year over the past two years. When estimating the index for last year we had only one confirmed sale for 2006. We subsequently found one more sale in 2006 and two sales in 2007 of vacant lots. Being reluctant to rely on only one sale in 2006, we adjusted our conclusion of value increases for 2006 to a lower figure based on current listings. With three additional sales it is now apparent that the one sale in 2006 at over $6,000/ff was not an aberration, as we suspected when doing the indexing study. From all indications lakefront prices have continued to increase, though at a slower rate. In 2005-2006 land values along Lake Coeur d'Alene and the Spokane River increased between 50% and 75%. From what sales data is available for vacant lots it appears the upward trend has continued through 2007.

We have prepared three graphs to illustrate price changes used to form our conclusion for indexing lease rates in 2008. The first graph, shown on the facing page, illustrates the annual fluctuation in sale prices each year. The line titled "Average Price/FF" represents the simple average of prices paid each year. While this line indicates declines in 2003 and 2005, the overall trend was continuing to increase. Had we used only this data last year the average or compounded rate of increase would have been 22%. Because we were uncertain that the single sale in 2006 represented a change in the market, we used a 2006 price of just over $4,000 /FF based on current listings. The resulting compounded rate of increase, which we are calling the average rate of increase over five years for indexing, was only 15% (see graph on following facing page).

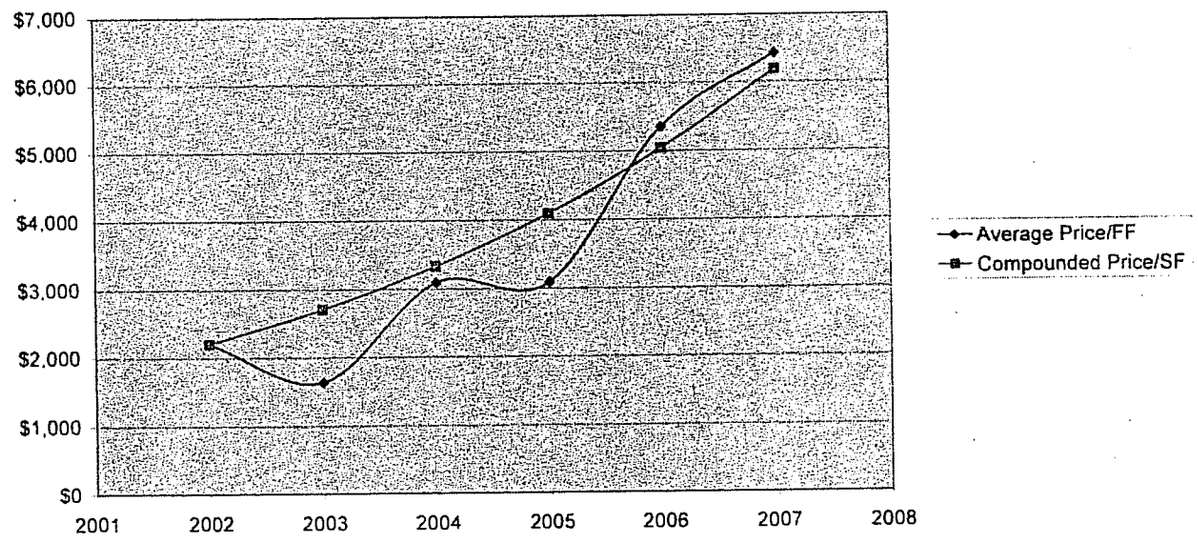
In calculating the index for 2008, based on value changes from 2002 to 2007, we have considered two options for the starting point in year 2002. One option is the average sale price found from sales data, which was $2,197/FF. The other option was the value indicated for 2002 using our annual compounding factor of 15% multiplied times the 2001 average sales price. This would be $2,313/FF. The result is essentially the same indicating a compounded rate of 23.93% using $2,197/FF as the base value (see graph on following page), or 22.66% using $2,313 as the base. Considering this data we conclude that an indexing factor for 2008 should be **23%**. This is based on the compounded rate of increase in value over five years, as specified in our scope of appraisal. While prices did not increase by 23% last year, the average is influenced by exceptionally high increases in previous years.

2001 - 2006 TIME FRAME

Average Sale Price/FF		% change	5 yr increase	Annual Compounded	Value using compounded rate of	15%
2001	$2,011				$2,011	
2002	$2,197	9%			$2,313	
2003	$1,636	-26%			$2,660	
2004	$3,086	89%			$3,058	
2005	$3,091	0%			$3,517	
2006	$5,351	73%	166%	21.62%	$4,045	



2002 - 2007 TIME FRAME Average Sale Price/FF		% change	5 yr increase	Annual Compounded	Value using compounded rate of	23%
2002	$2,197				$2,197	
2003	$1,636	-26%			$2,702	
2004	$3,086	89%			$3,324	
2005	$3,091	0%			$4,088	
2006	$5,351	73%			$5,029	
2007	$6,423	20%	192%	23.93%	$6,185	



Thank you for the opportunity to be of service. If you have any questions pertaining to the attached report, or if we can be of further assistance, please let me know.

Respectfully submitted,

Stanley D. Moe, MAI
Idaho Certified General Appraiser 72

Attachment 1:

Fee simple sales, land only
Two-page spreadsheet with sales listed by date sold
16 sales indicate an increase of 192.3% over five years
Average is 38.5% per year or 23.93% compounded

Attachment 2:

Current listings of building sites on Priest Lake showing an 18.38% (compounded) annual increase over the past five year

Attachment 3:

Sales and Resales of same property showing annual rates of increase of 16.91% and 42.51%

Attachment 4:

Sixteen (16) sales with line chart showing market trend over the five year period between 2003 and 2007. The compounded rate of increase using the highest sale from 2003 and 2007 indicates 22.16% per year

Attachment 5:

Calculations showing increases in lease rates (hypothetical) over the past three years

Certification
Qualifications of Stanley D. Moe, MAI

CVG 1278-08 **Attachment 1**

FEE SIMPLE SALES, LAND ONLY **PRIEST LAKE, BONNER COUNTY, IDAHO**

RP 004210000080A	8	Sherwood Bay Road	$135,000	80	7/15/2002		$135,000	$1,688	
RP 054040000030A	Lot 3	South Shores Circle	$230,000	125	9/15/2002		$230,000	$1,840	
RP 056530000100A	Lot 10	Huckleberry Bay Subdivision	$291,000	150	9/15/2002		$291,000	$1,940	
RP 004200010030A	1646	Sherwood Beach	$265,000	60	10/15/2002		$265,000	$4,417	
RP 054040000340A	Lot 34	South Shores Circle	$280,000	145	10/15/2002		$280,000	$1,931	
RP 054040000420A	Lot 42	South Shores Circle	$245,000	130	10/15/2002		$245,000	$1,885	
RP 00463001007BA	B-1 L-7-8	Thompsons Lots	$290,000	100	12/15/2002		$290,000	$2,900	
		Sales:	**7**			**Range:**	**From:**	**$1,688**	
		2002					**To:**	**$4,417**	***Base***
						Average:		**$2,197**	***Year***
RP 054040000020A	Lot 2	South Shores Circle	$150,000	135	1/15/2003		$150,000	$1,111	
RP 054040000150A	Lot 15	South Shores Circle	$310,000	165	3/15/2003		$310,000	$1,879	
RP 004190000060A	Lot 6	Sherwood Beach ADD #3	$150,000	60	4/15/2003		$150,000	$2,500	
RP 008080000110A	Lot 11	Sandy Shores	$215,000	99	6/15/2003		$215,000	$2,172	
RP 008080000320A	Lot 32	Sandy Shores	$165,000	99	9/15/2003		$165,000	$1,667	
RP 05207000001AA	Lots 1,2,3	Lamb Creek Estates	$250,000	200	10/15/2003		$250,000	$1,250	
									Change
		Sales:	**6**			**Range:**	**From:**	**$1,111**	-34.2%
		2003					**To:**	**$2,500**	-43.4%
						Average:		**$1,636**	**-25.6%**
RP 054040000050A	Lot 5	South Shores Circle	$285,000	125	4/15/2004		$285,000	$2,280	
RP 054040000230A	Lot 23	South Shores Circle	$610,000	165	6/15/2004		$610,000	$3,697	
									Change
		Sales:	**2**			**Range:**	**From:**	**$2,280**	105.2%
		2004					**To:**	**$3,697**	47.9%
						Average:		**$3,086**	**88.7%**
RP 054040000120A	Lot 12	South Shores Circle	$428,000	145	2/15/2005		$428,000	$2,952	
RP 054040000150A	Lot 15	South Shores Circle	$415,000	165	3/15/2005		$415,000	$2,515	
RP 054040000100A	Lot 10	South Shores Circle	$560,000	160	5/15/2005		$560,000	$3,500	
RP 003880000020A	Lot 2	Sandpiper Shores	$405,000	115	9/15/2005		$405,000	$3,522	

									Change
		Sales:	4			Range:	From:	$2,515	10.3%
		2005					To:	$3,522	-4.7%
						Average:		$3,091	0.1%
RP 008080000230A	Lot 23	Sandy Shores	$529,000	125	5/12/2006		$529,000	$4,232	
RP 00170000003BA	Lot 3	Hagman's Beach	$675,000	100	5/26/2006		$675,000	$6,750	
									Change
		Sales:	2			Range:	From:	$4,232	68.3%
		2006					To:	$6,750	91.7%
						Average:		$5,351	73.1%
RP 056530000120A	Lot 12	Huckleberry Bay Subdivision	$865,000	142	9/6/2007		$865,000	$6,092	
RP 008080000230A	Lot 23	Sandy Shores	$850,000	125	10/15/2007		$850,000	$6,800	
									Change
Lot 23, Sandy Shores is a sale and resale with no construction		Sales:	2			Range:	From:	$6,092	43.9%
		2007					To:	$6,800	0.7%
						Average:		$6,423	20.0%

CHANGE OVER THE PAST FIVE YEARS:		
2002 through 2007	Difference:	192.3%
	Average per year:	38.5%
	Compounded Rate:	23.93%

CURRENT LISTINGS Attachment 2 CVG 1278-08

Huckleberry at Priest Lake - South Shores Addition

Lot	Front Feet	SF	Asking Price May, 1997	$ per FF	Asking Price Sept., 2003	$ per FF	Six Year Increase	Average over first 6 years	Asking Price EOY, 2005	$ per FF	2 Year Increase	Annual	Asking Price EOY, 2007	$ per FF	2 Year Increase	Annual	9.5 Year Increase	Average over last 9.5 Years
4	145	25,700	$275,500	$1,900	$311,750	$2,150	13.16%	2.19%	$580,000	$4,000	86%	43%	$797,500	$5,500	38%	19%	189%	19.94%
7	145	34,412	$304,500	$2,100	$348,000	$2,400	14.29%	2.38%	$580,000	$4,000	67%	33%	$797,500	$5,500	38%	19%	162%	17.04%
8	160	38,333	$352,000	$2,200	$384,000	$2,400	9.09%	1.52%	$672,000	$4,200	75%	38%	$880,000	$5,500	31%	15%	150%	15.79%
9	155	37,462	$341,000	$2,200	$387,500	$2,500	13.64%	2.27%	$651,000	$4,200	68%	34%	$852,500	$5,500	31%	15%	150%	15.79%
	605 ff	135,907 sf		Total	$1,431,250					4 sites available		Total	$3,327,500		18.38%	Compounded, 2003-2007		

CVG 1278-08 Attachment 3

SALES AND RESALES, SAME PROPERTY PRIEST LAKE, BONNER COUNTY, IDAHO

Parcel Number	Lot	Subdivision	Sale Price	FF	Sale Date	$ / FF	Annual Rate
RP 008080000230A	Lot 23	Sandy Shores	$529,000	125	5/12/2006	$4,232	42.51%
RP 008080000230A	Lot 23	Sandy Shores	$850,000	125	10/15/2007	$6,800	
RP 054040000150A	Lot 15	South Shores Circle	$310,000	165	3/15/2003	$1,879	16.91%
RP 054040000150A	Lot 15	South Shores Circle	$415,000	165	3/15/2005	$2,515	

CVG 1278-08 PRIEST LAKE, BONNER COUNTY, IDAHO

Attachment 4

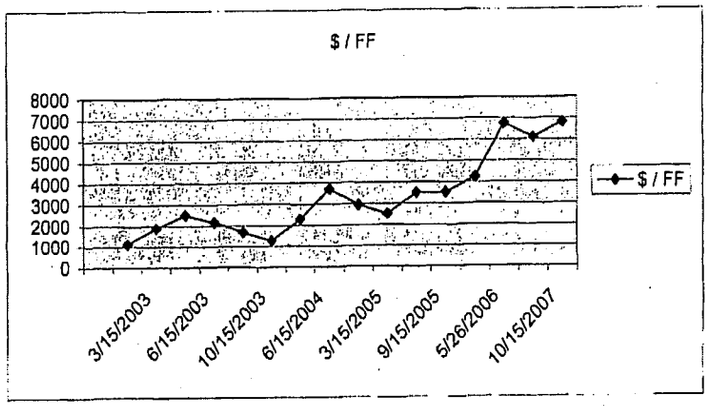
FEE SIMPLE SALES, LAND ONLY

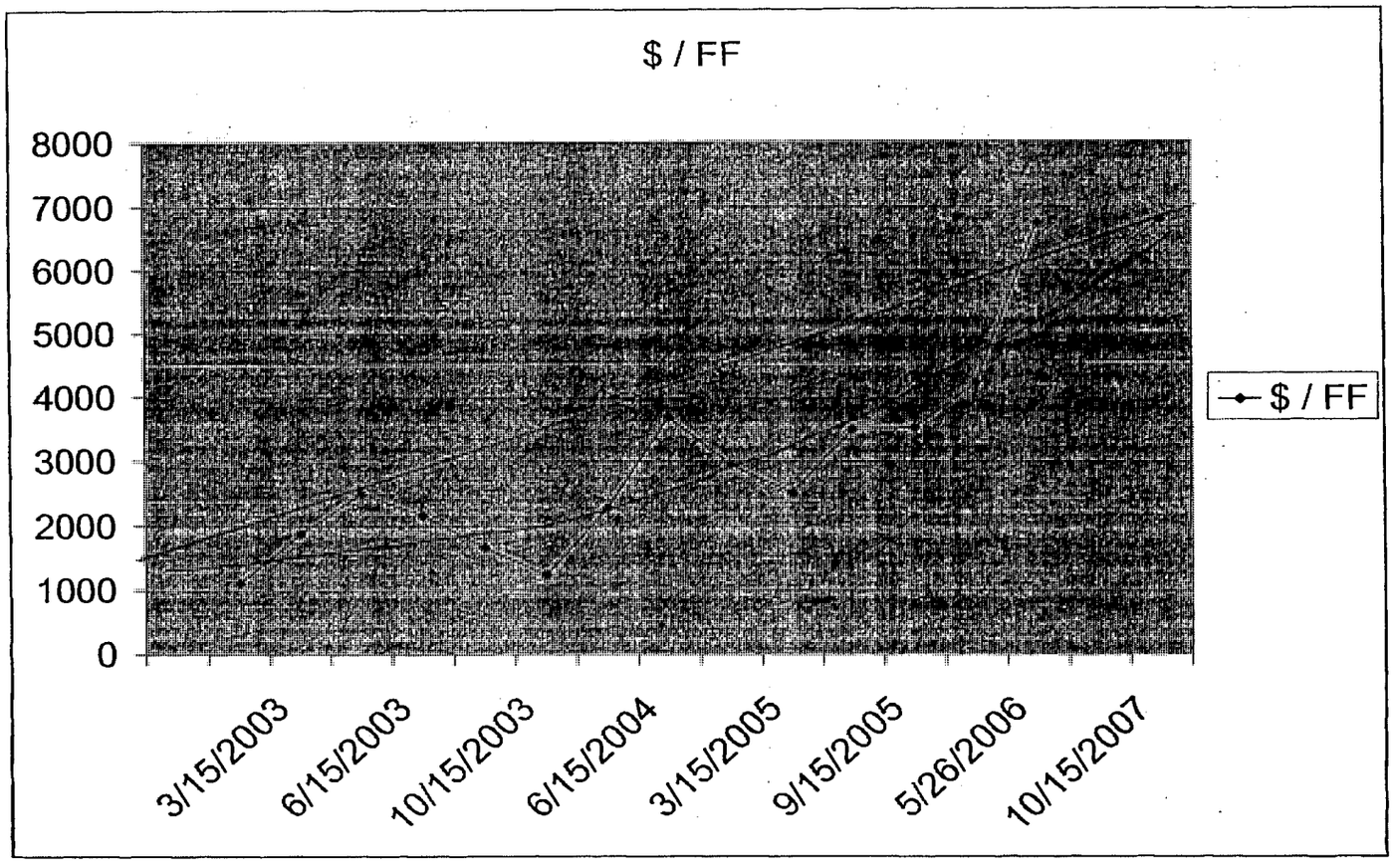
Parcel Number	Lot	Subdivision	Sale Price	FF	Sale Date	$ / FF
RP 054040000020A	Lot 2	South Shores Circle	$150,000	135	1/15/2003	$1,111
RP 054040000150A	Lot 15	South Shores Circle	$310,000	165	3/15/2003	$1,879
RP 004190000060A	Lot 6	Sherwood Beach ADD #3	$150,000	60	4/15/2003	$2,500
RP 008080000110A	Lot 11	Sandy Shores	$215,000	99	6/15/2003	$2,172
RP 008080000320A	Lot 32	Sandy Shores	$165,000	99	9/15/2003	$1,667
RP 05207000001AA	Lots 1,2,3	Lamb Creek Estates	$250,000	200	10/15/2003	$1,250
RP 054040000050A	Lot 5	South Shores Circle	$285,000	125	4/15/2004	$2,280
RP 054040000230A	Lot 23	South Shores Circle	$610,000	165	6/15/2004	$3,697
RP 054040000120A	Lot 12	South Shores Circle	$428,000	145	2/15/2005	$2,952
RP 054040000150A	Lot 15	South Shores Circle	$415,000	165	3/15/2005	$2,515
RP 054040000100A	Lot 10	South Shores Circle	$560,000	160	5/15/2005	$3,500
RP 003880000020A	Lot 2	Sandpiper Shores	$405,000	115	9/15/2005	$3,522
RP 008080000230A	Lot 23	Sandy Shores	$529,000	125	5/12/2006	$4,232
RP 00170000003BA	Lot 3	Hagman's Beach	$675,000	100	5/26/2006	$6,750
RP 056530000120A	Lot 12	Huckleberry Bay Subdivision	$865,000	142	9/6/2007	$6,092
RP 008080000230A	Lot 23	Sandy Shores	$850,000	125	10/15/2007	$6,800

Sales over the past five years: 16

Compounded Rate **22.16%**

(Using highest sale from 2003 and highest sale from 2007)




$ / FF
8000
7000
6000
5000
4000
3000
2000
1000
0
3/15/2003
6/15/2003
10/15/2003
6/15/2004
3/15/2005
9/15/2005
5/26/2006
10/15/2007
$ / FF

Attachment 5		Year Appraised	EXAMPLE (Appraised values vary)
		2004	$250,000 (Representative Lot)
Rate:	2.5%		
2004 Lease Fee:		$6,250 (at 2.5% of appraisal)	
2005 Index	12%	$7,000	
2006 Index	15%	$8,050	
2007 Index	23%	$9,902	58.42% overall
			19.47% per year
			16.58% compounded

APPRAISER CERTIFICATION

I certify that, to the best of my knowledge and belief:

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions and are my personal, impartial and unbiased professional analyses, opinions, and conclusions.
- The reported analyses, opinions and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics and the Standards of Professional Appraisal Practice of the Appraisal Institute, which include the Uniform Standards of Professional Appraisal Practice.
- I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest or bias with respect to parties involved.
- I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
- My compensation for completing this assignment is not contingent upon the reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value estimate, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this appraisal.
- My analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the Uniform Standards of Professional Appraisal Practice promulgated by the Appraisal Institute.
- Stanley D. Moe made a personal inspection of the property that is the subject of this report and supervised the research and report writing functions.
- Laune Clem, an employee of Columbia Valuation Group, Inc. provided significant professional assistance to the person signing this report in the form of research and report preparation. The final conclusions as to value are my own.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- This appraisal assignment was not based on a requested minimum valuation, a specific valuation, or approval of a loan. The appraiser is competent and qualified to perform this appraisal assignment.
- As of the date of this report, Stanley D. Moe has voluntarily completed the requirements of the continuing education program of the Appraisal Institute.

Stanley D. Moe, MAI, Idaho Certified General Appraiser #072

Date: May 01, 2008

QUALIFICATIONS OF STANLEY D. MOE, MAI, RM

Work Experience:

San Francisco Bay Area Rapid Transit District Right-of-Way Agent in Property Management - 1967.
California Division of Highways, Right-of-Way Agent in Property Management, Acquisition and Appraisal of Highway Rights-of-Way - 1967 to 1971.
Washington State Highway Department, Staff Appraiser - 1971 and 1972.
Eaton & Associates, Inc., Longview Washington, Real Estate Appraising and Counseling - 1972 through April 1976.
Mountain States Appraisal & Consulting, Inc., Boise, Idaho, Co-owner and President - 1976 through 1990. Firm engages in real estate appraisal and counseling.
Eaton & Associates, Inc. – Appraiser and Manager, 1991
Hoagland & Associates, Inc. – Appraiser and Manager, late 1991 through March, 1992

Current Business Connections:

Sole owner of Columbia Valuation Group, Inc., an Idaho Corporation, providing professional real estate appraisal and consulting services.

Professional Societies and Positions:

Appraisal Institute - Professional Designations, MAI and RM
State of Idaho Real Estate Brokers License
American Institute of Real Estate Appraisers
- Southern Idaho Chapter No. 55 -President, 1980
- Inland Northwest Chapter - President, 1997

Idaho Real Estate Appraiser Board (Current)

Certification:

State of Idaho, Certified Appraiser No. ICA-72, expires 10/31/2008.
State of Montana, Certified General Appraiser, 618RAG, expires 03/31/2008.
State of Washington, General Classification No. 1100678, expires 10/31/2009.
State of Idaho, Real Estate Broker, License No. DB00005532, expires 10/31/2008

Special Education:

San Jose State College, San Jose, California, Bachelor of Science Business and Industrial Management with Real Estate Emphasis.
Real Estate Classes Taken (1965-66):
- Principles of Real Estate - San Jose State College.
- Real Estate Law - San Jose State College.
- Principles of Real Estate Appraising - San Jose State College.
- Real Estate Appraisal Problems - San Jose State College.
- Real Estate Practices - Delta Community College, Stockton, California.

QUALIFICATIONS OF STANLEY D. MOE, MAI, RM

American Institute of Real Estate Appraisers Courses :

Real Estate Appraisal IA (Basic Principles)
Real Estate Appraisal IB (Capitalization Theory & Techniques)
Real Estate Appraisal II (Urban Properties)
Real Estate Appraisal VI (Investment Analysis)
Feasibility Seminar, Course VIII (Single Family Residential Appraisal)
Educare Seminar (Computerized Investment Analysis)
Farm Valuation

Appraisal Institute Courses:

Business Practices and Ethics – September 2006
Standards and Ethics of Professional Practice – 7 hour update – October 2006

Appraisal Institute/ Foundation Sponsored Seminars:	**Hrs.**	
Uniform Appraisal Standards for Federal Land Acquisitions	14	4/07
Online: Appraising Convenience Stores	7	11/07
Online: Appraising Small Hotel and Motels	7	11/07
Online: Condominiums, Coops and PUDs	7	11/07
Real Estate Fraud	6	9/05
Analyzing Distressed Real Estate	4	9/07
Uniform Standards of Professional Appraisal Practice	15	9/04
Condemnation Appraising: Advanced Topics & Application	16	9/03
The IDOT Proximity Damage Valuation Model	8	8/03
Corridors and Rights of Way: Valuation and Policy	14	9/02
Online Analyzing Operating Statements	7	10/01
Condemnation Appraising	15	9/01
The Law and Value: Communications	14	4/01
Corridors, Tower Sites, and Property Rights	15	4/01
Forester's Role in Timberland Valuation	6	9/99
Appraising Non-conforming Properties	6	pre 1999
Industrial Valuation	7	pre 1999
Public Interest Value vs. Market Value	7	pre 1999
The Appraisal of Local Retail Properties	7	pre 1999
Timberland Valuation	14	pre 1999

Various seminars sponsored by the American Right-of-Way Association.

Instructor - Principles of Real Estate Appraisals, Lower Columbia College, Longview, Washington.
Instructor - Basic appraisal courses required for state certification, North Idaho College.

Expert Testimony Experience:

State of Washington, Superior Court, Counties of Clark, Cowlitz and Spokane.
State of Idaho, various District Courts.
United States District Court, Boise, Idaho.

QUALIFICATIONS OF STANLEY D. MOE, MAI, RM

The Appraisal Institute conducts a program of continuing education for its designated members. MAI's and others who meet the minimum standards of this program are awarded periodic education certification. Mr. Moe is voluntarily certified.

Bureau of Occupational Licenses
Department of Self Governing Agencies

The person named has met the requirements for licensure and is entitled under the laws and rules of the State of Idaho to operate as a(n)

CERTIFIED GENERAL APPRAISER

STANLEY D MOE
1602 E. SHERMAN AVE. #100
COEUR D ALENE ID 83814 5300

Tana Cory Chief, B.O.L.	CGA-72 Number	10/31/2008 Expires

Exhibit 23

Land Bd. Agenda Memorandum,

2009 Cottage Site Rental Rates

(Dec. 16, 2008).

STATE BOARD OF LAND COMMISSIONERS
December 16, 2008
Regular Agenda Item

SUBJECT

2009 Cottage Site Rental Rates

BACKGROUND

Based on the existing cottage site lease, the rent for the Payette Lake cottage sites is 2.5% of the assessed land value as determined by the Valley County Assessor's office. The Department receives the data annually from Valley County and applies the rental formula to the forthcoming rental year.

The rent for the Priest Lake cottage sites is 2.5% of the appraised land value as determined by the Department appraisal contractor. Appraisals of individual cottage sites are completed every five years with an indexing process applied in "non-appraisal" years.

The following reflects the recent history related to the cottage site rental rates at Priest Lake and Payette Lake:

- **2008 Rent – Payette Lake –** The final 2007 Valley County assessed values (used to calculate the 2008 rent) for the Payette Lake cottage sites resulted in an average increase of 47% for waterfront lots and an average increase of 88% for second tier lots.

  Based on the magnitude of the increases the Land Board took action during the December 4, 2007 meeting to freeze the 2008 Payette Lake cottage site rent at the 2007 rent levels.

- **2009 Rent – Payette Lake –** The 2008 Valley County assessed values (used to calculate the 2009 rent) for the Payette Lake cottage sites resulted in no increase for second tier and waterfront lots.

  On June 19, 2008 the Land Board voted to apply a 15% rent increase to the Payette Lake cottage sites recognizing that the increases in rent from 2007 to 2008 had not been applied.

- **2008 Rent – Priest Lake –** 2008 was a "non-appraisal" year for all of the Priest Lake cottage sites. The Department contracted with Columbia Valuation Group (CVG) to complete an evaluation of the market data from the past five years in order to develop an indexing rate for the 2008 cottage site rent. CVG recommended a 15% increase.

  The 15% increase was implemented by the Land Board.

- **2009 Rent – Priest Lake –** 2009 is a "non-appraisal" year for all of the Priest Lake cottage sites. The Department contracted with Columbia Valuation Group (CVG) to complete an evaluation of the market data from the past five years in order to develop an indexing rate for the 2009 cottage site rent. CVG recommended a 23% increase.

  On June 19, 2008 the Land Board voted to apply a 15% rent increase to the Priest Lake cottage sites.

DISCUSSION

The Department has reviewed the following letters requesting a freeze of the 2009 cottage site rental rates from the Priest:

- October 24, 2008 from Charles Lempesis, Priest Lake lessee association attorney to the Land Board subcommittee (see Attachment 1);
- November 12, 2008 from David Leroy, Payette Lake lessee association attorney to the Land Board (see Attachment 2);
- November 17, 2008 from Bud Belles, President of the Priest Lake lessee association to the Land Board subcommittee (see Attachment 3);
- December 3, 2008 from Bud Belles, President of the Priest Lake lessee association to the Land Board (see Attachment 4);

Subsequent to this review the Department took the following actions:

- First, the Department reviewed the financial impact of the following three scenarios: 1) full application of the lease; 2) freeze for the 2008 rent and a 15% increase for 2009 rent; and 3) freeze for both 2008 and 2009 rent.

  The Department determined that the 2009 cash-on-cash return for Payette Lake cottage sites would be 1.7% for waterfront lots for Scenario #1 compared to 2.0% for Scenario #2 and 1.3% for second tier lots for Scenario #1 compared to 1.5% for Scenario #2. The cash-on-cash return for the Priest Lake cottage sites would be 2.0% for Scenario #1 compared to 2.3% for Scenario #2. The cash-on-cash return for Scenario #3 would be 2.5% for both lakes (see Attachment 5). The cash-on-cash return is the revenue divided by the assessed value.

  The Department also calculated the cottage site revenues for 2008 and 2009 using these same three scenarios (see Attachment 6). The result of a full freeze for the 2008 and 2009 rent would be a loss in revenue from the assessed values of $1,776, 560 for Payette Lake and $583,691 for Priest Lake.

- Second, the Department attempted to obtain national, regional and local market data for residential homes during the past two years to assess whether the real estate markets in the Payette Lake and Priest Lake areas have declined enough during the this timeframe to support a further reduction in the 2009 cottage site rent from the 15% increase adopted by the Land Board.

  Because Idaho is a non-disclosure state, sales data for residential transactions is difficult to obtain. The Department, however, did identify relevant data from the Office of Federal Housing Enterprise Oversight (OFHEO) and the Idaho Business Review (Attachments 7 and 8). OFHEO is used by the Idaho Tax Commission to set homeowner exemptions for Idaho homeowners.

  According to OFHEO data, the percent change in house prices from June 2007 to June 2008 for Idaho was +1.2% with a recent quarterly change of -0.7%. The Mountain Region change during this same timeframe was -4.9%. The Mountain Region includes Idaho, Montana, Wyoming, Nevada, Utah, Colorado, Arizona and New Mexico.

The percent change for the Pacific Region (Washington, Oregon, and California) was -16.4%. According to the OFHEO data, percent changes of -34.5% (Merced, CA), -32.7% (Stockton, CA) and -28.5% (Modesto, CA) were the sharpest declines.

Data in an Idaho Business Review report, dated November 26, 2008, stated that Ada County median existing home prices from June 2008 to October 2008 have dropped 17.3% according to National Association of Realtors data and have dropped 7.6% according to Intermountain Multiple Listing Service data.

The Department has reviewed no data which separately or collectively indicates that the markets have declined to the point where the average 47% increase in waterfront land values or the average 88% increase in second tier land values in the 2008 rent have been erased. Nationally, the worst case scenarios for property value declines during this same timeframe occurred in California, not Idaho, and appear to include declines of approximately 30%. From a market standpoint the application of a 15% increase appears to be a justifiable and fair adjustment.

Lastly, the Department contacted Valley County to obtain information related to current market trends. The Valley County Assessor's office reported one sale of waterfront property and a moderate level of land sales elsewhere in the Valley County during 2008. Valley County would not provide any specific land value information related to these sales. Absent significant waterfront sales data, the Department would expect that the 2009 Valley County assessed values for the cottage sites would likely fall close to the regional and local data noted above. Even if the 2009 Valley County waterfront assessments were reduced by 15% to 20%, the 15% increase adopted by the Land Board for the 2009 rent would remain a fair adjustment. None of the data reviewed by the Department suggests anything near a 20% reduction has occurred. The Department has not been able to obtain similar information from Bonner County.

RECOMMENDATIONS

The Department recommends that the 15% rent increase for 2009 at both Payette Lake and Priest Lake be maintained as adopted by the Land Board on June 9, 2008.

BOARD ACTION

FOR REFERENCE – June 19, 2008 Board Action: *A motion was made by Secretary of State Ysursa to raise the rate for cottage site rent across the board for next year at fifteen percent for waterfront and secondary lots at Payette Lake and lakefront lots at Priest Lake. Controller Jones seconded the motion for discussion purposes. Controller Jones noted that Secretary of State Ysursa indicated a need for additional time to continue reviewing this matter. She asked that Secretary of State Ysursa amend his motion to a time certain. Secretary of State Ysursa amended his motion that the Board raise the rate for cottage site rent across the board fifteen percent with the proviso that the subcommittee will report back to the Board on or before December 1, 2008, with a new methodology on price. Controller Jones seconded the amended motion. The amended motion carried on a vote of 4-0, with Superintendent Luna being absent for this vote.*

DECEMBER 16, 2008:

- A motion was made by Secretary of State Ysursa to modify the June 19, 2008 Land Board action to lower the 2009 lease rate to five percent across the board at Payette Lake and Priest Lake. In addition, the Cottage Site Subcommittee is directed to report back to the

Land Board no later than June 15, 2009 with a price methodology to be used in future leases. Controller Jones seconded the motion. This motion was replaced by Superintendent Luna's substitute motion.

- A substitute motion was made by Superintendent Luna to freeze the cottage site lease rates at the current level, and that the Cottage Site Subcommittee report back to the Board no later than June 15, 2009 with a price methodology to be used in future leases. Governor Otter seconded the motion. *See below for the vote.

- Prior to a vote being taken on the substitute motion, a subsequent substitute motion was made by Controller Jones to increase the lease rate to two and a half percent. This subsequent substitute motion failed for lack of a second.

* Returning to the substitute motion by Superintendent Luna and seconded by Governor Otter, which is to freeze the cottage site lease rates at the current level and that the Cottage Site Subcommittee will report back to the Board no later than June 15, 2009 with a price methodology to be used in future leases, a vote was taken. Superintendent Luna, Governor Otter and Secretary of State Ysursa voted aye; Attorney General Wasden and Controller Jones voted nay. The substitute motion carried on a vote of 3-2. [The substitute motion superseded the original motion by Secretary of State Ysursa.]

ATTACHMENTS

1. October 24, 2008 letter from Charles Lempesis
2. November 12, 2008 letter from David Leroy
3. November 17, 2008 letter from Bud Belles
4. December 3, 2008 letter from Bud Belles
5. Payette and Priest – Cash on Cash Return
6. Payette and Priest – Cottage Site Revenue
7. OFHEO data
8. Idaho Business Review Article – November 26, 2008.

Ex. 24

Land Bd. Agenda Memorandum,

2010 Rent Changes for Payette Lake and

Priest Lake Cottage Sites (June 16, 2009).

STATE BOARD OF LAND COMMISSIONERS
June 16, 2009
Regular Agenda Item

SUBJECT

2010 Rent Changes for the Payette Lake and Priest Lake Cottage Sites

BACKGROUND

In accordance with the Payette Lake and Priest Lake cottage site leases, the Department is required to provide a 180-day written notice of pending rent increases to all lessees. Notices are typically mailed to the lessees during the last week of June to meet the July 1 deadline. Actual invoices are mailed in November with first half rent due January 1st and second half rent due June 1st.

DISCUSSION

PAYETTE LAKES COTTAGE SITES
In accordance with the cottage site lease, the rent for the Payette Lake cottage sites is 2.5% of the assessed land value as determined by the Valley County Assessor's office. The Department receives data annually from Valley County and applies the rent formula for the forthcoming rental year. The 2009 assessment data that applies to the 2010 rent was provided by Valley County on June 2, 2009. The Valley County data indicates that values for the Payette Lake cottage sites (both waterfront and secondary lots) have decreased 5% from their 2008 assessed values.

However, this decrease does not lower projected rental rates. Current rental rates were frozen by action of the State Board of Land Commissioners in both 2008 and 2009. Due to dramatic land value increases, the 2007 and 2008 assessed values were not used to establish the 2008 and 2009 rents. The 5% decrease reported by Valley County for the 2009 assessed values does not offset the value increases reported in the 2007 and 2008 assessed values. Had no rent freezes been instituted, current rents would be approximately 39% higher for waterfront lots and approximately 78% higher for second tier lots. A table containing comparisons of the rental revenue and comparisons of the cash-on-cash (gross) return is included as Attachment 1.

PRIEST LAKE COTTAGE SITES
In accordance with the cottage site lease, the rent for the Priest Lake cottage sites is 2.5% of the appraised land value as determined by the Department appraisal contractor. Appraisals of individual cottage sites are completed every five years with an indexing process applied in "non-appraisal" years. 2010 is an appraisal year for 60 of the 354 cottage sites at Priest Lake, with the remaining 294 cottage being indexed.

A table indicating the values identified in the 60 appraisals conducted by Columbia Valuation Group is included as Attachment 2. The appraised values of the 60 lots were on average 7.2% higher than if the indexing methodology had been applied. A table containing comparisons of the rental revenue and comparisons of the cash-on-cash (gross) return is included as Attachment 1.

Based on the information provided by Columbia Valuation Group (the Department's contracted appraiser), the indexing percentage for the 294 cottage sites is +26%. This percentage is based on market data from the past five years and includes a market decline during 2008 of -20%. A copy of the Columbian Valuation Group indexing report is included as Attachment 3. The Columbian Valuation Group recommended indexing percentage was +15% based on the past six years of market data, the Department made the adjustment to five years (to be consistent with the cottage site lease) which changed the indexing percentage to +26%.

The 2009 rent for the Priest Lake cottage sites was frozen by the Land Board on December 16, 2008 based on significant land value increases. Columbia Valuation Group had completed an indexing process for the 2009 rent which indicated a 23% increase was warranted. The Land Board's action eliminated this increase.

LAND BOARD SUBCOMMITTEE

A Land Board Cottage Site Subcommittee (Subcommittee) was formed on June 12, 2007 to review alternative rent methodologies for the Priest Lake and Payette Lake cottage site leases set to expire on December 31, 2010. A chronology of the cottage site program and related Land Board actions is included as Attachment 4.

Since its formation, the Subcommittee has met formally with cottage lessee representatives and Department staff on several occasions (most recently on April 22, 2009) to discuss and research the following:

- Current valuation methodologies;
- Valuations methodologies proposed by the lessee representatives, including seasonal rental rates;
- Appropriateness of using land values to determine rental rates;
- Buffering land value/market spikes;
- Deferred market valuation approaches;
- Premium rent;
- Subleasing;
- Lessee insurance requirements;
- General lease provisions; and
- Current market conditions.

Based on this work, the Department anticipates that the Subcommittee will be making a recommendation to the Land Board during the July 21, 2009 meeting regarding a new rent methodology for forthcoming cottage leases. The methodology likely to be recommended will include the calculation of annual rent by multiplying a fixed percentage (likely between 3.0% and 5%) by the average county assessed land value from the past 10 years. This calculation would identify a target rental rate for five years in the future. Rental rates for years one, two, three, and four in the future would then be identified by taking the existing rental rate and calculating annual adjustments that evenly stair-step to the targeted rental rate for year five. The process would then be repeated after each five year period.

The percentage which the Subcommittee ultimately recommends be applied to the average county assessed value from the previous 10-year period will have a direct affect on the percentage of premium rent the Subcommittee recommends (likely between 0% and 50%).

RECOMMENDATION

Based on:

- the Land Board's past actions to freeze the 2008 and 2009 rent for the Payette Lake cottage sites;
- the Land Board's past action to freeze the 2009 rent for the Priest Lake cottage sites; and
- the significant rent increases that would result with the implementation of the 2009 Valley County (Payette Lake) assessed values and Columbia Valuation Group's appraisals and indexing (Priest Lake);

The Department recommends the Land Board leave the 2010 rental rate for all cottage sites at their existing 2009 level.

BOARD ACTION

A motion was made by Secretary of State Ysursa that the Board approve the recommendation to freeze the rents at Payette Lake and Priest Lake. Controller Jones seconded the motion. The motion carried on a vote of 5-0.

ATTACHMENTS

1. Rental Revenue and Cash-On-Cash Tables
2. Columbia Valuation Group – 60 appraisals
3. Columbian Valuation Group – Indexing Report
4. Cottage Site Program Chronology

GROSS REVENUE - Contract Rate vs. Frozen Rate

	Revenue at Contract Rate	Revenue at Frozen Rate	Difference
Priest Lake	$3,822,701	$2,537,791	$1,284,910
Payette Lake - Waterfront	$2,155,897	$1,552,582	$603,315
Payette Lake - 2nd Tier	$316,555	$177,558	$138,997
TOTAL	**$6,295,153**	**$4,267,931**	**$2,027,222**

CASH-ON-CASH - Contract Rent vs. Frozen Rent

	Contract Rate	Frozen Rate	Difference
Priest Lake	2.50%	2.03%	0.47%
Payette Lake - Waterfront	2.50%	1.70%	0.80%
Payette Lake - 2nd Tier	2.50%	1.33%	1.17%

Appraisal Data - 60 Priest Lake Cottage Site Lots

Lease Number	Frontage (feet)	2004 Appraised Value	$ / FF	2009 Appraised Value	$ / FF	% Change from 2004
R-1027	115	$115,000	$1,000	$217,600	$1,892	89.22%
R-1233	79	$120,000	$1,519	$237,600	$3,008	98.00%
R-1044	108	$184,000	$1,704	$372,000	$3,444	102.17%
R-1083	144	$223,000	$1,549	$433,600	$3,011	94.44%
R-1095	157	$231,000	$1,471	$443,800	$2,827	92.12%
R-1107	177	$230,000	$1,299	$478,000	$2,701	107.83%
R-1339	177	$230,000	$1,299	$478,000	$2,701	107.83%
R-1153	222	$383,000	$1,725	$777,200	$3,501	102.92%
R-1049	165	$227,000	$1,376	$489,700	$2,968	115.73%
R-1075	163	$226,000	$1,387	$472,200	$2,897	108.94%
R-1060	157	$222,000	$1,414	$457,600	$2,915	106.13%
R-1041	129	$190,000	$1,473	$400,600	$3,105	110.84%
R-1059	159	$208,000	$1,308	$444,500	$2,796	113.70%
R-1115	152	$204,000	$1,342	$437,200	$2,876	114.31%
R-1183	150	$203,000	$1,353	$434,800	$2,899	114.19%
R-1086	114	$181,000	$1,588	$365,400	$3,205	101.88%
R-1142	175	$213,000	$1,217	$432,700	$2,473	103.15%
R-1170	169	$142,000	$840	$283,400	$1,677	99.58%
R-1146	150	$188,000	$1,253	$320,800	$2,139	70.64%
R-1185	151	$189,000	$1,252	$323,000	$2,139	70.90%
R-1163	149	$187,000	$1,255	$321,400	$2,157	71.87%
R-1080	150	$203,000	$1,353	$320,800	$2,139	58.03%
R-1102	150	$203,000	$1,353	$320,800	$2,139	58.03%
R-1085	153	$205,000	$1,340	$322,500	$2,108	57.32%
R-1117	153	$204,000	$1,333	$322,500	$2,108	58.09%
R-1051	159	$207,000	$1,302	$323,200	$2,033	56.14%
R-1065	147	$202,000	$1,374	$320,100	$2,178	58.47%
R-1076	150	$203,000	$1,353	$320,800	$2,139	58.03%
R-1256	154	$190,000	$1,234	$322,800	$2,096	69.89%
R-1001	155	$191,000	$1,232	$322,000	$2,077	68.59%
R-1124	155	$191,000	$1,230	$322,000	$2,074	68.59%
R-1164	151	$220,000	$1,457	$321,200	$2,127	46.00%
R-1129	149	$218,000	$1,463	$322,000	$2,161	47.71%
R-1212	149	$203,000	$1,362	$322,000	$2,161	58.62%
R-1139	150	$216,000	$1,440	$320,800	$2,139	48.52%
R-1182	133	$219,000	$1,647	$333,200	$2,505	52.15%
R-1201	129	$228,000	$1,767	$373,400	$2,895	63.77%
R-1014	128	$228,000	$1,781	$373,000	$2,914	63.60%
R-1018	110	$211,000	$1,918	$344,500	$3,132	63.27%
R-1002	98	$193,000	$1,969	$286,500	$2,923	48.45%
R-1071	142	$241,000	$1,697	$387,700	$2,730	60.87%
R-1025	164	$259,000	$1,579	$405,700	$2,474	56.64%
R-1348	164	$259,000	$1,579	$405,700	$2,474	56.64%
R-1052	136	$236,000	$1,735	$398,400	$2,929	68.81%
R-1235	153	$221,000	$1,444	$417,100	$2,726	88.73%
R-1118	155	$238,000	$1,535	$417,900	$2,696	75.59%
R-1334	154	$253,000	$1,643	$431,000	$2,799	70.36%
R-1068	156	$255,000	$1,635	$450,900	$2,890	76.82%
R-1050	151	$250,000	$1,656	$443,900	$2,940	77.56%
R-1032	136	$258,000	$1,897	$424,900	$3,124	64.69%
R-1179	116	$238,000	$2,052	$409,400	$3,529	72.02%
R-1128	136	$256,000	$1,882	$446,600	$3,284	74.45%
R-1166	82	$183,000	$2,232	$328,800	$4,010	79.67%
R-1209	85	$188,000	$2,212	$336,800	$3,962	79.15%
R-1166	75	$171,000	$2,280	$310,100	$4,135	81.35%
R-1154	149	$248,000	$1,664	$446,400	$2,996	80.00%

COLUMBIA VALUATION GROUP, INC.
Real Estate Appraisers and Consultants

1602 East Sherman Avenue, Suite 100
Coeur d'Alene, ID 83814-5300
(208) 667-7940
Fax: (208) 666-1474

Stanley D. Moe, MAI
moecvg@verizon.net

June 08, 2009

Idaho Department of Lands
Attn: Craig Thompson
954 West Jefferson Street
Boise, ID 83720-0060

Re: Indexing Values for leased sites on Priest Lake, Bonner County, Idaho
Index rate for the period January through December 2008

Dear Mr. Thompson:

At your request we have completed our study of price changes for lakefront lots on Priest Lake over the past six years. The purpose of our study was to determine, from market data, the average rate of increase over the past five years, which rate will be used as an Index for adjusting lease rates in 2009. Using 2003 as the base year we calculated annual increases (or decreases if indicated by the data) as well as the overall value change through 2008.

Our current assignment was to determine the average rate of change in value over the past five years for fee owned waterfront lots on Priest Lake.

There are currently three vacant lots on the market at Priest Lake not including any sites remaining in Huckleberry at Priest Lake, South Shores Addition that are not listed in the Multiple Listing Service. We have attached a list that shows current asking prices range from $4,587/ff to $7,022/ff. The last reported prices for South Shores were around $5,500/ff. As a general rule, current asking prices set an upper limit for range of current market value, based on the principle of substitution.

Market conditions change over time with inflation, national and local economic conditions, in or out-migration from an area, employment opportunities, etc. Ideally, sufficient recent sales data is available so that adjustments for value changes over time are not needed. We found no sales of vacant waterfront building sites on Priest Lake during 2008. Because of the lack of sales on Priest Lake the only option for tracking waterfront price changes was to reference

ATTACHMENT 3

other major lakes in north Idaho. On Pend Oreille Lake for 2007 and 2008, the difference in average selling price for the 12 sales completed in 2007 and the eight sales completed in 2008 was -21% ($3,807/ff to $3,008/ff). The difference between list price and final sale price ranged as high as -28.9% and averaged -5.6%.

We did the same for Lake Coeur d'Alene where prices are generally higher and the number of properties occupied year around is significantly higher. The difference in average selling price for the nine sales completed in 2007 and the seven sales completed in 2008 was -11.4% ($4,618/ff to $4,090/ff). The difference between list price and final sale price ranged as high as -46.5% and averaged -12%.

Real estate prices rarely change at an even or constant rate over several years. More typically, prices will increase rapidly during a one or two year period then level off for a time. Prices will sometimes decline for a period of time, as when interest rates skyrocketed in late 1979 and 1980, then recover as economic conditions return to a stabilized pattern. Negative changes in personal financial situations are usually first reflected in the recreational property market. Luxury items such as recreational property and "toys" are the first things to be liquidated. Conversely, positive changes are slow to reflect in the recreational property market. Our research indicates that most people invest in recreational properties with "discretionary funds." Some buy as investments with no intention of building or living in them full-time, but simply to cash in on value increases over time. As a result, market fluctuations tend to be more pronounced for this class of real estate, much like the stock market.

The current economy is in a state of turmoil and uncertainty. The pace of residential sales of all types has slowed considerably in the north Idaho panhandle (four counties) over the past 24 months from the "overheated" markets of 2004 and 2005. The number of home sales peaked in 2004-2005 at just over 4,000 units per year. Since then sales have fallen off to about 3,000 in 2006, 2,500 in 2007 and around 2,000 in 2008. Year to date sales for 2009 show 268 sales through the first three months. The average price has continued to decrease.

While Bonner County and Priest Lake have been somewhat insulated from the current national financial crisis, it is affected in indirect ways that are quite serious.

- People who can afford multiple homes have become conservative with their cash expenditures and have adopted a "wait and see" posture, resulting in reduced market demand
- Retirees have seen losses in their retirement funds and many have postponed their retirements plans
- Those who want to sell and move here are often stymied when their properties in hard-hit markets won't sell or sell for significantly less than their expectations
- Unemployment in Bonner County has risen from 3.4% to just over 8% over the past 12 months, indicating that while somewhat insulated, it has clearly been impacted.

Marketing time is directly related to pricing; however, we have yet to find examples in the local market of any developer lowering prices to a "whatever it takes" level to clear their inventory. One developer reduced prices in his subdivision on Lake Coeur d'Alene by 35% in order to generate cash. The price reduction was offered for 120 days and no sales were generated.

The number of recreation and second home properties listed for sale is significant, and those willing to lower prices will most probably generate the sales. We are experiencing a "buyers market" with numerous choices, competitive pricing and the occasional "steal" when an owner is forced to liquidate. At this point there is no evidence on which to base a prediction of market recovery. Faint signs of recovery are being seen in the housing market, due in large part to investors buying at bargain-basement prices.

CONCLUSIONS

Tracking market changes for real estate is not an exact science because of the many variables that impact pricing and negotiations. At Priest Lake, as in many seasonal resort locations, real estate transactions generally coincide with the high resort season. During the winter, when most properties are inaccessible and visitors are scarce, the real estate market is almost dormant. Rather than a steady, month by month progression in value changes, prices generally change on a seasonal cycle. The active season at Priest Lake is between the end of April or first of May through August, and sometimes into September.

Sales of vacant lots were non-existent in 2008 at Priest and were few in number on other lakes. One reason is the lack of available inventory (and undeveloped land to create new lots). Prices for undeveloped waterfront building sites on Priest Lake rose rapidly between 2002 and 2007, averaging from $2,197/ff in 2002 to $6,423/ff in 2007. This change over five years represents an average of 38.5% per year and a compounded annual rate of 23.93%.

Because of the limited inventory of vacant waterfront building sites when compared to the number of improved sites, a 24% annual rate of appreciation over that time period is not surprising. Any time demand exceeds supply for a commodity, prices tend to rise. Most of the increase, however, took place between 2004 and 2006. This rate does seem high when compared with the core inflation rate for goods and services over the past 12 months of less than 3%, but core inflation rates have little association with real estate values. Core inflation excludes energy costs, food, and prescription drugs which are all increasing at record rates. With the current price trend for petroleum products related commodities such as RV's, boats, and remote recreational properties that require significant travel may very well decrease in cost in the near future.

Estimating the five-year floating average of price increases is problematic when there is no sales data in the fifth year. Relying on sale data from Lake Pend Oreille, also in Bonner County, we conclude that for 2008 sale prices dropped an average of -20%. A similar drop in prices was found on Coeur d'Alene Lake, although spread over two years rather than one.

We have prepared a graph to illustrate price changes used to form our conclusion for indexing lease rates in 2009. The graph shown on the following page, illustrates the annual fluctuation in sale prices each year. The line titled "Average Price/FF" represents the simple average of prices paid each year. While this line indicates declines in 2003 and 2005, the overall trend was continuing to increase.

In calculating the index for 2009, based on value changes from 2003 to 2008, we determined the five year increase is 103% overall with a compounded rate of 15.21%. Considering this data we conclude that an indexing factor for 2009 should be **15%**. This is based on the compounded rate of increase in value over five years, as specified in our scope of appraisal. While prices did not increase by 15% last year, and the market indicates a -20% decrease, the five year average is influenced by exceptionally high increases in previous years.

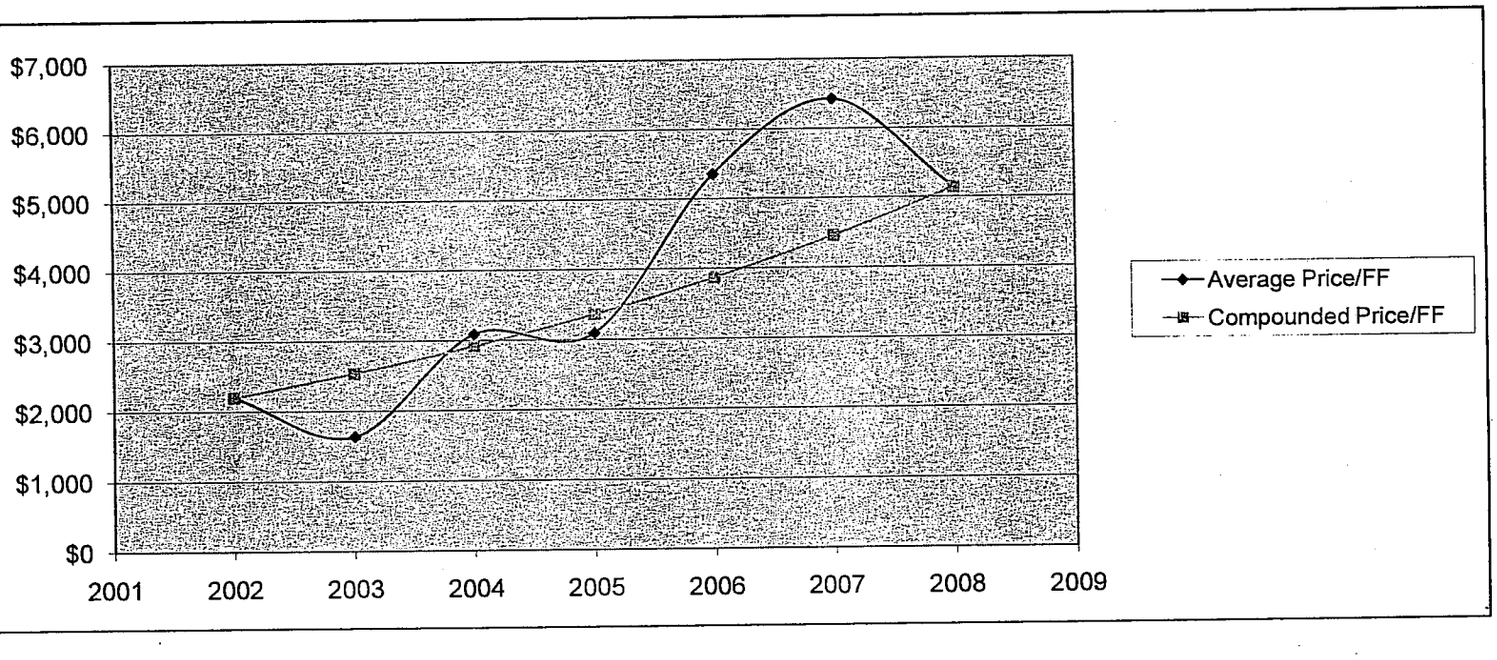
Thank you for the opportunity to be of service. If you have any questions pertaining to the attached report, or if we can be of further assistance, please let me know.

Respectfully submitted,

Stanley D. Moe, MAI
Idaho Certified General Appraiser 72

Attachment 1: Chart
Attachment 2: Lake Pend Oreille Market Data
Attachment 3: Lake Coeur d'Alene Market Data
Attachment 4: Current Listings on Priest Lake
Appraiser's Certification
Qualifications of Stanley D. Moe, MAI
Copy of Idaho License

03 - 2008 TIME FRAME erage Sale Price/FF		% change	6 yr increase	Annual Compounded	Value using compounded rate of 5 yr. increase	15.21% 103%
2002	$2,197				$2,197	
2003	$1,636	-26%			$2,531	
2004	$3,086	89%			$2,916	
2005	$3,091	0%			$3,360	
2006	$5,351	73%			$3,871	
2007	$6,423	20%			$4,459	
2008	$5,138	-20%	134%	15.21%	$5,138	



Cottage Site Chronology

February 14, 2006	Board authorizes Department to auction Lots 37A and 37B at Priest Lake.
September 12, 2006	Board cancels auction pending resolution of lease terms.
May 8, 2007	Department presents Residential Site Survey to Board. Board authorizes Department to auction Lots 37A and 37B at Priest Lake.
June 12, 2007	Board approves a cottage site lease document for Lots 37A and 37B which includes a 5% rental rate and the opportunity to dovetail with the remaining leases in 2011.
June 12, 2007	Board establishes cottage site subcommittee consisting of Secretary of State Ysursa and Superintendent Luna.
October 21, 2007	Auction assembled and no bidders register. Auction canceled.
November 7, 2007	Cottage Site Subcommittee holds a 5 hour public hearing with extensive public testimony.
December 4, 2007	Board freezes the Payette Lake cottage site rental rates for one year. Priest Lake rates increase by 15%.
April 22, 2008	Cottage Site Subcommittee meeting with Payette Lake and Priest Lake representatives.
June 19, 2008	Land Board proposes 15% increase for both Payette and Priest Lakes for 2009 rents with a provision to revisit methodology in December.
October 18, 2008	University of Idaho policy analysis group releases Report No. 28 pertaining to cottage site leases.
December 16, 2008	Land Board freezes rent at both lakes for 2009 at 2008 rates with Cottage Site Subcommittee reporting to its full board at the June 2009 meeting.
March 19, 2009	Cottage Site Subcommittee meeting with Payette Lake and Priest Lake representatives with discussion centered around possible new methodologies.
April 15, 2009	Appraisers submit regression curve methodology.
April 22, 2009	Cottage Site Subcommittee meets with Payette Lake and Priest lake representatives to discuss appraiser methodology and Subcommittee's methodology using a ten year average.

Exhibit 25

Land Bd. Agenda Memorandum, Recommendation of the Cottage Site Subcommittee, with Attachment 1, Philip S. Cook and Jay O'Laughlin, *Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands* (October 2008).

State Board of Land Commissioners
February 16, 2010
Regular Agenda

SUBJECT

Recommendation of the Cottage Site Subcommittee

RECOMMENDATION

Refer to the Cottage Site Subcommittee Report to the Idaho State Board of Land Commissioners, February 16, 2010 *(next page)*.

BOARD ACTION

ATTACHMENTS

1. University of Idaho, Policy Analysis Group, Report No. 28, *Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands by Philip S. Cook and Jay O'Laughlin, October 2008*;

2. Cabin Site Scenarios – 2010 through 2015

COTTAGE SITE SUBCOMMITTEE REPORT

TO

THE IDAHO STATE BOARD OF LAND COMMISSIONERS

February 16, 2010

COTTAGE SITE SUBCOMMITTEE REPORT
February 16, 2010

INTRODUCTION

The Idaho Department of Lands (Department) currently has 354 cottage site lots on Priest Lake and 167 lots on Payette Lakes. Most of these cottage site lots are lake-front or lake-view properties. Land values and demand for these cottage sites have substantially increased since the 1970s, particularly since 1980.

Over the last two decades, the Department has recommended adjusting the lease terms and increasing the lease rates on these lots. These recommendations, however, have not been supported by cottage site lessees or adopted by previous Idaho State Board of Land Commissioners (Land Board).

All cottage site leases currently held by the Department and cabin owners around Payette and Priest Lakes expire December 31, 2010. Pursuant to Idaho Statute §58-307(8), applications to lease or renew an existing lease must be filed with the Department by April 30, 2010.

In order to identify any new lease terms the Land Board established a Cottage Site Subcommittee (Subcommittee), consisting of Ben Ysursa, Secretary of State, and Tom Luna, Superintendent of Public Instruction. The Subcommittee held meetings attended by legal counsel representing the Priest and Payette Lake cottage site lessees, presidents of the respective associations and individual cottage site lessees, along with Department legal counsel and staff.

The Subcommittee reviewed several studies previously conducted on the topic by various experts and also commissioned the report published by Phillip S. Cook and Jay O'Laughlin of the Policy Analysis Group in the College of Natural Resources at the University of Idaho: *Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands* (2008) (PAG Report). They also studied several leasing methodologies and rental structures presented by various Subcommittee members, individual leaseholders and/or presidents of the respective associations.

SUMMARY

Establishing land values and cottage site rental rates present several challenges. Appraisers continue to find it difficult to find comparable transactions because of the limited number of sales of fee simple properties in this unique market. Also, land values and associated rental rates can fluctuate widely, impacting both the revenue stream to the trust beneficiaries and causing concern for cabin site lessees.

Applying a rate to a land value that is adjusted annually has caused drastic swings in annual rental fees. Using an 10 year average of the land value in calculating the rent would smooth out the impact of those rapid swings, and provide greater stability than is currently the case.

Numerous measures, such as mortgage rates, appraiser opinions, federal and state leasing programs, and other indicators, have been examined and used in several different studies over the last twenty years in calculating rent. These indicators range from 3.5% to 18%. In an attempt to determine a rate that would provide market rent, the Department, in October 2006, offered two residential cabin sites for lease at Priest Lake. The lease contract rate was 5% of the appraised value ($450,000) which translated to a first year's rent of $22,500. One person registered for the auction, but no one bid for either lot.

RECOMMENDATIONS

The Subcommittee is well aware of the constitutional mandate of Article IX, Section 8, and the duty of undivided loyalty to the beneficiaries of the endowment trust. However we also recognize that severely impairing or eroding longstanding business relationships with our lessees is not in the best interest of our trust beneficiaries. We are also aware that raising rents too high would result in these lands going unleased, to the detriment of the beneficiaries. Therefore your Subcommittee is proposing the following:

A target annual lease rent ("target rent") will be calculated at 4.0% of the average appraised value of each lot over the most recent 10 years (the sum of the 10 prior years appraised or indexed values for each lot divided by 10). Actual rent will increase or decrease annually from the prior year's rent at a constant percentage rate to reach the target rent in year five. Every five years from the effective date of the lease, the actual rent will be recalculated using this same methodology and appraised values of the lot for the most recent 10 years. Lot values shall be appraised by the applicable county assessor or determined by an Idaho Certified Appraiser, at the discretion of the Department. At the end of the each five year period under the lease, the target rent will be calculated at 4.0% of the average value for the duration of the lease.

The 4% used in the formula falls within the range of rates mentioned above and will still generate interest in the market. It provides a reasonable rate of return and generates an 9% per year increase over the first five years to the beneficiaries.

Premium rent is the proportion of leasehold value (sales price less the value of tenant improvements) that is paid to the State when the cottage site lease is transferred from one party to another. Premium rent is currently set at 10% of the leasehold value. Since 2003, cottage site owners have realized in excess of $25 million for the use of State endowment land while the endowment received only $2.7 million.

To correct this inequity the Subcommittee recommends that the premium rent rate be increased gradually to 50% of the leasehold value upon transfer of the lease. The Subcommittee believes that a 50% premium rent rate will have the effect of maximizing the return to the beneficiaries, and that any higher rate would be counterproductive, and act as a disincentive for selling leaseholders to be active in seeking the maximum sale price.

Lease language will include a leasehold/premium rent calculation that will be phased in as follows:

Year	Distribution of Leasehold Value	
2011	10% to the State	90% to the lessee
2012	20% to the State	80% to the lessee
2013	30% to the State	70% to the lessee
2014	40% to the State	60% to the lessee
2015 and thereafter	50% to the State	50% to the lessee

The rental rate described above, coupled with the premium rent formula, meets the Land Board's fiduciary responsibility and provides sound business practices to protect the market for cottage site leases.

The term of the lease is to be for 35 years, as was contemplated when the Land Board unanimously approved a motion to seek legislation allowing that length of lease. However, the proposed lease will also contain language which is in the current lease, that would allow the Board to cancel the lease and sell or exchange the property upon proper notice.

The Subcommittee believes that the long term solution to the never ending cottage site imbroglio is to dispose of the lots in a reasonable, market savvy manner. The proceeds could then be invested in other assets which could better enhance the endowments. In that vein we recommend that the department conduct the necessary analysis and recommend to the Land Board by January 2011, specific long term land development plans of state endowment land on or adjacent to cottage sites. These plans shall deal with the sale or exchange options where practicable and in the best interests of the trusts, keeping in mind the unique circumstances including public and private ownership at each lake.

COTTAGE SITE SUBCOMMITTEE REPORT
February 16, 2010

ATTACHMENTS

1) University of Idaho, Policy Analysis Group: Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands
2) Cabin Site Scenarios – 2010 thru 2015

Policy Analysis Group — College of Natural Resources

Report No. 28 October 2008

Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands

by

Philip S. Cook

and

Jay O'Laughlin

Policy Analysis Group — College of Natural Resources
Jay O'Laughlin, Director

College of Natural Resources Experiment Station

The College of Natural Resources Policy Analysis Group (PAG) was established by the Idaho Legislature in 1989 to provide objective analysis of the impacts of natural resource proposals (see Idaho Code § 38-714). The PAG is administered by William J. McLaughlin, Dean, College of Natural Resources.

Advisory Committee

Jane Wittmeyer, Vice Pres., Idaho Affairs
Intermountain Forest Association
Boise, Idaho

Kent Henderson
Idaho Wildlife Federation
Lewiston, Idaho

Jack Lavin
Idaho Recreation / Tourism Initiative
Boise, Idaho

John Robison, Public Lands Director
Idaho Conservation League
Boise, Idaho

Kent Lauer, Director of Public Affairs
Idaho Farm Bureau Federation
Boise, Idaho

Cecilia Seesholtz, Supervisor
Boise National Forest
Boise, Idaho

Cal Groen, Director
Idaho Dept. of Fish and Game
Boise, Idaho

Margaret Soulen Hinson
Idaho Rangeland Resources Committee
Boise, Idaho

George Bacon, Director
Idaho Dept. of Lands
Boise, Idaho

Policy Analysis Group Reports

No. 1. Idaho's endowment lands: A matter of sacred trust. *J. O'Laughlin* (March 1990).

No. 2. BLM riparian policy in Idaho: Analysis of public comment on a proposed policy statement. *K.L. Johnson, C. Mosley, J.C. Mosley, and J. O'Laughlin* (June 1990).

No. 3. Idaho Department of Fish and Game's land acquisition and land management program. *C. Wise and J. O'Laughlin* (October 1990).

No. 4. Wolf recovery in central Idaho: Alternative strategies and impacts. *C. Wise, J.J. Yeo, D. Goble, J.M. Peek, and J. O'Laughlin* (February 1991).

No. 5. State agency roles in Idaho water quality policy. *A.C. Turner and J. O'Laughlin* (February 1991, with separate Executive Summary).

No. 6. Silver Valley resource analysis for pulp and paper mill feasibility. *J.G. MacCracken and J. O'Laughlin*, editors (October 1991).

No. 7. A national park in Idaho? Proposals and possibilities. *J.G. MacCracken and J.O'Laughlin* (June 1992).

No. 8. Design of forest riparian buffer strips for the protection of water quality: Analysis of scientific literature. *G.H. Belt, J. O'Laughlin, and T. Merrill* (June 1992).

No. 9. Analysis of methods for determining minimum instream flows for recreation. *T. Merrill and J. O'Laughlin* (March 1993).

No. 10. Idaho roadless areas and wilderness proposals. *J.G. MacCracken, J. O'Laughlin, and T. Merrill* (July 1993).

No. 11. Forest health conditions in Idaho. *J. O'Laughlin, J.G. MacCracken, D.L. Adams, S.C. Bunting, K.A. Blatner, and C.E. Keegan, III* (December 1993, with separate Executive Summary).

No. 12. Grizzly bear recovery in Idaho. *J.G. MacCracken, D. Goble, and J. O'Laughlin* (November 1994).

No. 13. Endangered Species Act at the crossroads: New directions from Idaho case studies. *J.O'Laughlin and P.S. Cook* (October 1995, with separate Executive Summary).

No. 14. Idaho water quality policy for nonpoint source pollution: A manual for decision-makers. *J. O'Laughlin* (December 1996, with separate Executive Summary).

No. 15. Guidelines for managing cattle grazing in riparian areas to protect water quality: Review of research and best management practices policy. *J.C. Mosley, P.S. Cook, A.J. Griffis, and J. O'Laughlin* (December 1997).

No. 16. History and analysis of federally administered land in Idaho. *J. O'Laughlin, W.R. Hundrup, and P.S. Cook* (June 1998).

No. 17. Public opinion of water pollution control funding sources in Idaho. *J. O'Laughlin and K. McGuire* (December 1998).

No. 18. Toward sustainable forest management: Part I – certification programs. *P.S. Cook and J. O'Laughlin* (December 1999).

No. 19. Toward sustainable forest management: Part II – the role and effects of timber harvesting in Idaho. *P.S. Cook and J.O'Laughlin* (December 2000).

No. 20. Taxing forest property: Analysis of alternative methods and impacts in Idaho. *P.S. Cook and J. O'Laughlin* (November 2001).

No. 21 Endowment fund reform and Idaho's state lands: Evaluating financial performance of forest and rangeland assets. *J. O'Laughlin and P.S. Cook* (December 2001).

No. 22. Forest resource-based economic development in Idaho: Analysis of concepts, resource management policies, and community effects. *C. Harris, P.S. Cook, and J. O'Laughlin* (May 2003).

No. 23. Comparison of two forest certification systems and Idaho legal requirements. *P.S. Cook and J. O'Laughlin* (December 2003).

No. 24. Forest fire smoke management policy: Can prescribed fire reduce subsequent wildland fire emissions? *P.S. Cook and J. O'Laughlin* (November 2004).

No. 25. Delisting endangered species: Process analysis and Idaho case studies. *M. McClure, P.S. Cook, and J. O'Laughlin* (October 2005).

Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands

by

Philip S. Cook[1]
and
Jay O'Laughlin[2]

Report No. 28
Policy Analysis Group
College of Natural Resources
University of Idaho

October 2008

---

[1] Philip S. Cook is a Research Associate with the College of Natural Resources Policy Analysis Group, University of Idaho, Moscow.

[2] Jay O'Laughlin is Director of the College of Natural Resources Policy Analysis Group, and Professor in the Department of Forest Resources, University of Idaho, Moscow.

About the Policy Analysis Group (PAG)

Role and Mission. The Idaho Legislature created the Policy Analysis Group (or "PAG") in 1989 as a way for the University of Idaho to provide timely, scientific and objective data and analysis, and analytical and information services, on resource and land use questions of general interest to the people of Idaho. The PAG is a unit of the College of Natural Resources Experiment Station, administered by William J. McLaughlin, Director, and Dean, College of Natural Resources.

PAG Reports. This is the twenty-eighth report of the Policy Analysis Group (see inside cover). The PAG is required by law to report the findings of all its work, whether tentative or conclusive, and make them freely available. PAG reports are primarily policy education documents, as one would expect from a state university program funded by legislative appropriation. The PAG identifies and analyzes scientific and institutional problems associated with natural resource policy issues. In keeping with the PAG's mandate, several alternative policy options are developed and their potential benefits and detrimental effects are analyzed. As an operational policy the PAG does not recommend an alternative.

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

Technical Review. Peer review of PAG work is absolutely essential for ensuring not only technical accuracy but also impartiality and fairness. A technical advisory committee and technical reviewers are selected separately for each project by the dean and PAG director, sometimes upon recommendation of the Advisory Committee, to ensure that a wide range of expertise is reflected in the design and execution of PAG reports, and that no point of view is favored. Report review criteria used by the National Research Council of the National Academy of Sciences are the guidelines furnished to PAG reviewers.

Additional Information. If you would like additional information, please contact Jay O'Laughlin, PAG Director, at any of the following addresses:

Policy Analysis Group
College of Natural Resources
University of Idaho
Moscow, ID 83844-1134

voice: 208-885-5776
FAX: 208-885-6226
E-mail: pag@uidaho.edu
World Wide Web: http://www.cnr.uidaho.edu/pag

ACKNOWLEDGMENTS

The following individuals provided comments on a review draft of this report.

Sharon W. Kiefer
Assistant Director—Policy
Idaho Department of Fish and Game
Boise, ID

Kathy Opp
Deputy Director
Idaho Department of Lands
Boise, ID

Jim Young
President
Payette Lake Cabin Owners Association
Meridian, ID

The authors also would like to acknowledge Jane Wright, Strategic Business Analyst for the Idaho Department of Lands, for her contributions of current cottage site program information.

TABLE OF CONTENTS

About the PAG . . . . . *ii*
Acknowledgments . . . . . *iii*
Table of contents . . . . . *iv*
List of tables . . . . . *v*
List of figures . . . . . *v*

Executive summary 1

1.0. Introduction 4

2.0. How were cottage site lease payments set historically? 4
2.1. Current lease 6
2.2. Recent developments 6
2.3. Premium rent 7
2.4. Lease term 7

3.0. What guidance on long-term residential real estate leasing is in published literature? 7
3.1. Property rights and leasing 8
3.2. Appraisal 9
3.3. Appraisal of leases 10
3.4. Market rent, contract rent, and leasehold value 11
3.5. Land leases 12
3.6. Appraisal of land leases 12
3.7. Rental rate and rate of return 13
3.8. Investment risk 14
3.9. Rental adjustments and reevaluations 15
3.10. Guidance from the literature 15

4.0. How do other states set lease payments for residential real estate such as cottage sites? 16
4.1. Alaska 16
4.2. California 16
4.3. Montana 16
4.4. Oregon 16
4.5. Utah 17
4.6. Wyoming 17
4.7. National forests 17

5.0. What alternative methods are available to set lease payments for endowment land cottage sites for a 35-year period that are consistent with the "market rent" mandate? 18
5.1. Appraisal 18
5.2. Other programs 18
5.3. Alternative investments 19
5.4. Benchmarks 20
5.5. Leasehold value at lease assignment 20
5.6. Auction 20
5.7. Summary 21

6.0. Conclusion 22
6.1. Exploring divestment 23
6.2. Trust responsibility 25

References 26

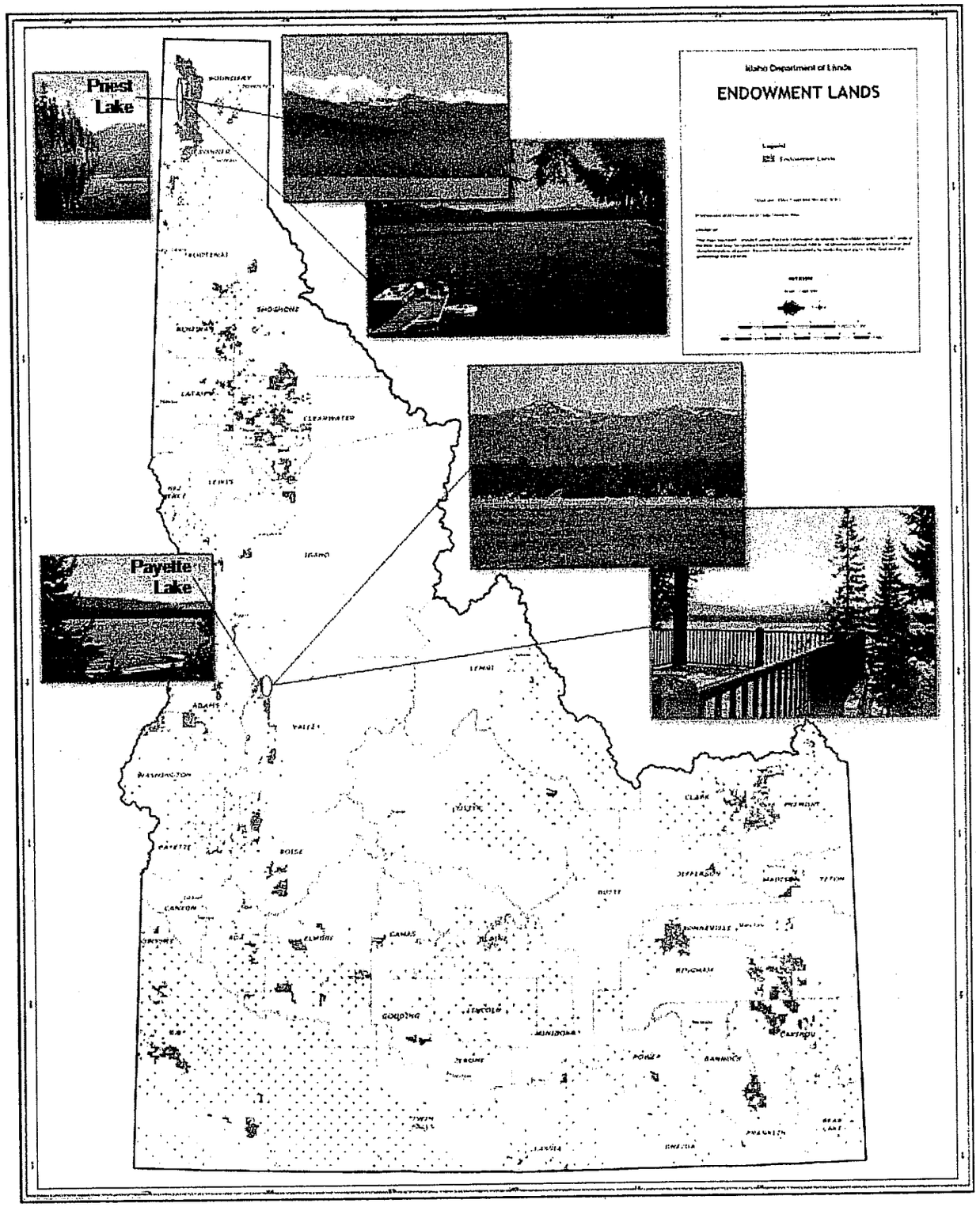
Personal communication 29

LIST OF TABLES

Table 2-1. Cottage site lease assignments per year, 2003-2007 8
Table 3-1. State of Idaho Cottage Site Program revenues, FY 2003 - FY 2007 14
Table 5-1. Rates of return (RoR) on residential real estate implied by various market measures 22

LIST OF FIGURES

Figure 1-1. Management objectives for residential real estate. 5
Figure 3-1. The bundle of rights in property. 9
Figure 5-1. Historic rates for 30-year mortgages, 30-year U.S. Treasury bonds, and AAA corporate bonds. 19
Figure 5-2. NCREIF Property Index. 21
Figure 6-1. Rate of return continuum. 24


Priest Lake
Payette Lake
Idaho Department of Lands
ENDOWMENT LANDS

Executive Summary

Idaho's endowment trust assets include 354 cottage site lots on Priest Lake and 168 cottage site lots on Payette Lake. The state leases the lots, and lessees are authorized to construct and own single-family residences on the sites. The cottage sites are to be managed, like all endowment trust assets, to provide "maximum long term financial return" to the trust beneficiaries, primarily public schools. The State Board of Land Commissioners (Land Board) is the trustee for endowment trust assets and is mandated to "insure that each leased lot generates market rent throughout the duration of the lease." Maximizing financial return to endowment land assets by obtaining market rent for cottage site leases raises several issues, addressed through replies to the following focus questions.

How were cottage site lease payments set historically? Most cottage site lots were leased for the first time during the mid 1940s and early 1950s. Rents were low and remained relatively flat from 1945 to 1988.

After selling 22 lots at Payette Lake in 1987 to determine fee simple market values, the Land Board began using a rental rate of 2.5% of fee simple market value in 1988. As of 2008, the rental rate remains 2.5% of current fee simple value of the vacant or unimproved land. At Priest Lake, the leased property is revalued every five years, and rent is adjusted annually by indexing based on market data. At Payette Lake, rent is adjusted annually based on assessed values determined by Valley County.

In 2008, the Idaho Legislature amended Idaho Code to allow the Idaho Department of Lands (IDL) to increase the lease term for all cottage sites on state endowment lands from 10 years to 35 years. The rationale for lengthening the lease term was that it would more generally coincide with a traditional 30-year mortgage term, and therefore the desirability of state cottage site leases could potentially increase due to the availability of residential financing.

What guidance on long-term residential real estate leasing is in published literature? The Land Board's fiduciary responsibility to the trust beneficiaries and the goal of generating market rent from each cottage site leads to several pertinent areas of inquiry in the research literature, including: property rights and leasing real property, appraisal, appraisal of leases, market rent and contract rent, land leases, appraisal of land leases, rates of return, and rent adjustments and reevaluations. However, because of the unique nature of the state's cottage site leasing program, guidance from the research literature is limited. Land leases for single-family residential use properties are rare in the United States, thus research has not been a priority.

The research literature leads one to question whether "market rent," as the term is conventionally used, can be established for cottage site leases because so many characteristics of the "market" are unusual. For example, markets typically are defined by many buyers and sellers, or, in the case of a market for leases, many lessors and lessees. The state is the only lessor of cottage site land leases on Payette Lake. On Priest Lake only the state and federal governments lease land for residential use. In 1998, no private land leases were found at either location. Also, markets typically are defined by transactions that take place throughout a time period. In the case of state cottage site leases, all leases currently expire at the same time. In addition, current cottage site lessees have preferential renewal rights at the end of a term (i.e., no conflict bidding is allowed).

The lack of a competitive, open market for single-family residential land leases on either Payette Lake or Priest Lake forces appraisers to make unusual adjustments to standard appraisal methods for determining opinions of value. Unusual situations and markets make appraisals more subjective, more variable, and therefore less reliable for estimating market values, market capitalization rates, and market rents.

The research literature does not provide much guidance on either an appropriate rate of return or lease rate for cottage sites but does suggest that establishing an appropriate land-

lease rate involves a higher than normal degree of subjectivity.

How do other states set lease payments for residential real estate such as cottage sites? Few other states lease their trust lands for residential use or single-family cottage sites. Most of the states that do so set target lease rates at least double Idaho's 2.5% of assessed or appraised market value. For example, California leases recreational cabin sites at an annual rental rate based on 9% of the appraised value of the leased lands. Montana's lease rate is 5% of appraised market value. Utah uses the appraised value of the land times the prime interest rate, which is currently 5%, as a base for determining the lease rate. Wyoming leases state trust lands for recreational purposes, including cabin sites, at a minimum rental rate of not less than 5.5% of the appraised land value.

The National Forest System is federal land, not state land, but nevertheless instructive. The U.S. Forest Service permits recreational residence sites on national forest lands under its special uses permit system. The base fee for a recreation residence special use permit is 5% of the market value of the recreation residence lot as determined by appraisal.

What alternative methods are available to set lease payments for endowment land cottage sites for a 35-year period that are consistent with the "market rent" mandate? Among the methods for setting lease payments are: using individual or multi-parcel appraisals to determine market rent, basing rent on what other state leasing programs are doing, setting rent comparable to rates of return on alternative investments, using benchmark rates of return from other institutional investors, using leasehold values, and auctioning the leases.

Appraisals can be used to estimate market rent in two ways. If a rental market exists, then a market rent can be determined by examining rental contracts from comparable properties. Adjustments have to be made for improvements, lease contract terms and conditions, and other property characteristics to arrive at a comparable rent for state land leases. If other similar leased properties do not exist in the market area, then determining market rent is more complex and involves appraising the current fair market value of the land that is being leased and then applying an appropriate annual rate of return to determine contract rent.

The current contract rental rate for cottage sites of 2.5% is below rental rates used by residential land leasing programs in other states. Determining the appropriate rate of return to use for setting contract rent based on rates of return reported for other investments is difficult because they include asset appreciation in addition to a cash return or dividend yield. The 2.5% contract rental rate is below the rates of return reported for other real estate investments. However, between 2003 and 2007, revenues to the cottage site program increased from $2.7 million to $4.4 million (63%, or 13% compounded annually), due to appreciation in the appraised value of cottage sites.

Adjusting contract rent to keep current with changes in land value is also challenging. The application of an index of overall price changes in the economy, such as the Consumer Price Index, does not accurately reflect price changes in the real estate markets at Priest and Payette Lakes. A local real estate price index would more closely reflect land value changes in these two areas, but such an index does not exist and would need to be developed.

Conclusion. Creating a cottage site leasing program that meets the Land Board's fiduciary responsibility to the beneficiaries as well as the market rent mandate is challenging. Identifying market rent is complicated because of the unusual characteristics of the cottage site lease "market." Appraisals to determine market rent for cottage sites are complex and stretch to the limit many of the assumptions on which standard real property appraisal methods are based. The choice of an appropriate rate of return or market rent, without having one indicated by the market, is subjective, and various elements and characteristics of the cottage site leasing program create arguments

for lower, or higher, rental rates. Accounting for and balancing all the factors involved in choosing an appropriate rate of return for the State of Idaho is a difficult political decision, and the market provides little direction. In addition, changing the program involves issues of fairness to current leaseholders.

Given the complexities of meeting the market rent mandate, one must ask the question, would the Land Board and IDL better meet their fiduciary responsibilities to the beneficiaries by divesting the cottage site properties (i.e., selling or exchanging the land) and investing the proceeds in other lands or financial instruments? In 2001, an ad hoc committee formed by the Governor to recommend efficiency/effectiveness changes to the Land Board did not reach a conclusion or recommendation about whether all cottage sites should be sold or whether all proceeds from the sales of cottage sites should be reinvested in commercial real estate. However, the committee felt that investments in additional timbered properties and in other financial instruments should be considered. The committee felt that the majority, if not all, of the proceeds from the sale of cottage sites should be used to obtain office and industrial properties in communities around the state. The asset management plan adopted by the Land Board in 2007, however, clearly states an intention to retain the cottage site leasing program.

State trust land management is different than private trust management because state trust land managers may be answerable to beneficiaries, user groups, and voters in a manner that would be inappropriate, or at least unusual, in the context of a private trust. Many state trust land decisions involve social and political considerations that are unrelated to the land manager's fiduciary duties as a trustee. The decisions of the Land Board and IDL regarding cottage site leasing require balancing fiduciary responsibility to the beneficiaries with political considerations and stakeholder concerns. There is unlikely to be a simple "correct" answer to efficiency and fairness issues. Policy decisions that guide state trust land managers have been, and likely will continue to be, a balancing of financial, environmental, and social concerns.

1.0. Introduction

The State Board of Land Commissioners (Land Board) is the trustee for almost 2.5 million acres of "endowment lands" granted to Idaho at statehood for the purpose of supporting public schools and other public institutions (see PAG #1, O'Laughlin 1990). These lands are managed as trusts, with a constitutional mandate to provide "maximum long term financial return" to nine beneficiary institutions. Public schools receive approximately 95% of the returns. Endowment land assets include 1.1 million acres of timberlands and 1.8 million acres leased for grazing (IDL 2007). The Land Board functions as the trustee and the trust assets are managed by the Idaho Department of Lands (IDL).

Endowment land assets also include 522 cottage site lots that are leased for single-family residential use. The state leases the land (site), and lessees are authorized to construct and own the improvements on the sites. These lots are located on the shores of Priest Lake (354 sites) and Payette Lake (168 sites) (IDL 2007). State statute requires that the Land Board "insure that each leased lot generates market rent throughout the duration of the lease" (Idaho Code 58-310A). In FY 2007, IDL's cottage site leasing program brought in revenues of $4.4 million, with net income to the beneficiaries of $4.3 million (IDL 2007).

In 2001 we published a report titled *Endowment Fund Reform and Idaho's State Lands: Evaluating Financial Performance of Forest and Rangeland Assets* (PAG #21, O'Laughlin and Cook 2001). In January 2008 Secretary of State Ben Ysursa, a member of the Land Board, requested that the PAG produce a similar report on cottage site leases, focusing on the challenges identified in the Land Board's asset management plan (AMP) that was adopted in December 2007 (see Figure 1-1; Land Board 2007a). The AMP categorizes these assets as residential real estate cabin leases; the more commonly used term for these lots is cottage sites. All current leases expire on December 31, 2010, and the Land Board is carefully considering new approaches to cottage site leases.

Four focus questions addressing cottage site lease issues provide the outline for this report:

- How were cottage site lease payments set historically?
- What guidance on long-term residential real estate leasing is in published literature?
- How do other states set lease payments for residential real estate such as cottage sites?
- What alternative methods are available to set lease payments for endowment land cottage sites for a 35-year period that are consistent with the "market rent" mandate?

These questions were suggested by the PAG's Advisory Committee to define the appropriate scope of inquiry reported herein. Due to limited resources, the PAG's research methods are primarily review and synthesis of existing information, especially in published peer-reviewed literature and relevant reports by public agencies and non-governmental organizations. Replies to the four focus question follow.

2.0. How were cottage site lease payments set historically?

Idaho began leasing cottage sites as early as 1924, but most lots were not leased for the first time until the mid 1940s and early 1950s (Land Board 1997). Rents were low, for example $10 per year for Priest Lake lots in 1945 (Russell 2007a). Rents remained relatively flat from 1945 to 1988, with only sporadic adjustments. For example, no rent increase occurred from 1947 to 1961 (Land Board 1997, Knipe & Knipe 1998). In 1986, the IDL estimated that the state was receiving a return on asset value of 0.67% for all cottage site leases (Land Board 1986).

In 1986, in recognition that trust beneficiaries were not receiving a market return, the Land Board decided to sell at auction up to 10% of the cottage sites with the purpose of establishing fee simple market values (Land Board 1986). Appraisals were conducted to set minimum bid prices. In August 1987, 22 lots were sold at Payette Lake (Land Board 1997, Knipe & Knipe 1998). No lots at Priest Lake were sold due to pending litigation by the lessees (Land Board 1997). In 1988, the

Management Objectives for Residential Real Estate

Idaho has been leasing residential sites since 1932. These properties consist of cabins and single family homes where the lessee is authorized to construct and own the improvements. Currently, the endowments lease over 540 sites, with the majority located on Priest and Payette Lakes.

Management Objectives

- Develop and manage long term residential leases that appropriately compensate the endowments.
- Identify additional high value residential sites.

Challenges

- Increasing real estate values associated with lake side or lake view property results in escalating annual rent and produces pressure to maintain an artificially low return on asset.
- Statutory limitation on residential lease to a duration of ten-years may impede achieving market rent.*

Opportunities

- There is a potential for over 200 additional residential sites on Priest and Payette Lakes, and numerous other potential sites on other lakes and endowment lands.

Figure 1-1. Management objectives for residential real estate.

* The 2008 Idaho Legislature amended the maximum term of residential leases on endowment lands from 10 to 35 years (Session Law 103).

Source: Idaho State Board of Land Commissioners (Land Board 2007a).

Land Board began using a rental rate of 2.5% of market value, with the market values established by the 1987 fee simple auction sales (Land Board 1997, Knipe & Knipe 1998).

In 1990, the Idaho Legislature enacted Idaho Code 58-310A, which states that the Land Board "shall ensure that each lot generates market rent throughout the duration of the lease," and eliminated auctioning of a lease at the expiration of a term (i.e., conflict bidding) (Land Board 1997, Knipe & Knipe 1998). In April 1990, the Land Board began implementation of the new statute by having 13 benchmark lots appraised. This appraisal initially concluded that market rents should be based on an 8% annual return, but in light of additional market data, the range was moderated to 4.5% to 5.5% of market value (Knipe & Knipe 1998). In October 1991, after numerous hearings with representatives of the cottage site associations, the Land Board decided to continue with the 2.5% rental rate established in 1988. In June 1992, the base year for the leases was shifted to 1992, a 10-year phase-in plan was adopted to soften the impact on lessees, and a 5.3% cap on annual rent increases was established (Land Board 1997, Knipe & Knipe 1998).

By 1997, the Land Board had renewed concerns about the 2.5% rental rate being below market return levels. The IDL's estimates of leasehold value changes from 1992 to 1997 (see Section 3.1) were continuing to escalate significantly: at Payette Lake the average annual rate of increase was 14.3% for lakefront lots and 9.6% for lots without lakefront footage. Market data in 1997 suggested that virtually all other types of investments were generating more than 2.5% annual return. Actual rents paid for cottage sites were well below the 2.5%

target rate because payments were based on 1992 assessed values and property values had appreciated significantly by 1997 (Knipe & Knipe 1998).

In 1998, the Land Board directed that multi-parcel appraisals be conducted at both Priest Lake and Payette Lake (Land Board 1998a, 1998b). The Priest Lake appraisal of 15 lots concluded that market rent was 3.5% of fee simple land value, and the Payette Lake appraisal of 14 lots concluded that market rent was 6% of fee simple land value (Land Board 1998c, 1998d; Knipe & Knipe 1998).

Lessees at Payette and Priest Lakes were unhappy with the appraisals for a variety of reasons including: adjustments made for the value of improvements and limitations of the leases, generally inadequate market rent analysis and a perception that appraisals were too high, and lessees were not given an opportunity for comment during the appraisal process (Land Board 1998c, 1998d). Lessees were also concerned about discrepancies between appraised and county-assessed values. For 11 of the 15 appraised lots at Priest Lake, the appraised value of the lot was higher than county-assessed value; for four lots it was lower (Land Board 1998c). At Payette Lake, appraised values were generally within 20% of county-assessed values, and in aggregate, the assessed value was about 88% of appraised market value (Knipe & Knipe 1998). One of the reasons such discrepancies can occur is because data used in county assessments tends to be older than that used by private appraisers (Knipe & Knipe 1998).

After discussions with lessees and their representatives, the Land Board voted to maintain the rental rate at 2.5% of current county-assessed land value (Land Board 1998e). As a result, rental rates reflected what was effectively a two-year delay because of the time between value assessment by the county and the setting of rental rates. For example, 1999 lease rates were based on 2.5% of 1997 county-assessed values, which were the most recent assessed values as of July 1, 1998. The state also must give lessees six month notice of rent changes, which further delays the time between value assessment and rent payments based on that assessment (Knipe & Knipe 1998).

2.1. Current lease. In 2000, the Land Board directed IDL to develop a new lease for all cottage sites (Land Board 2000). The new lease was adopted by the Land Board in February 2001 (Land Board 2001a, 2001b). The rental rate remained at 2.5% of current fee simple value of the vacant or unimproved land (Land Board 2001a, 2001b; IDL 2001). Today it remains at 2.5% of fee simple value.

The revaluations and readjustments are computed differently at Payette and Priest Lakes. At Priest Lake the lots are revalued every five years, and rents are adjusted annually using an index based on market data. At Payette Lake, rent is adjusted annually based on lot values established by the Valley County assessor (IDL 2001).

At Priest Lake, the land value base was the 1999 Bonner County value of lease lots minus 20%. The land value was to be adjusted annually based on an index determined by market data collected by the IDL until the readjustment period between 2003 and 2006. The annual adjustment could not exceed 5% during the first period. At the time of the land value readjustment, the annual index was to be revised based on the previous five year history of market data increases in lot value. The state or the lessee could request a readjustment of land value and the index any time during the years 2003-2006, but no later than 2006. Readjustment of lot values was based on valuation of current market value of the lots. Lot value readjustments are to be done every five years from the date of the first readjustment and updated annually by indexing based on market data, after the first readjustment (IDL 2001).

2.2. Recent developments. In February 2006, the Land Board authorized IDL to proceed with an auction of two new lot leases at Priest Lake, with subsequent analysis of the results of these auctions providing IDL and the Land Board with a plan for leasing additional cottage sites at Priest Lake (Land Board 2006a). In September 2006, the Land Board directed

IDL to review and recommend rental rate structures for new cottage sites, and to defer the auctions of new cottage sites, including the two on Priest Lake, until a rent structure for them was approved by the Land Board (Land Board 2006b).

Again in May 2007, the Land Board authorized IDL to initiate lease auctions during late summer of 2007 for the previously identified two lots on Priest Lake. The Land Board also authorized IDL to initiate informational meetings with cottage site lessees and their respective lessee associations regarding potential terms and rates for renewing cottage site leases and for any new cottage sites which the Board may choose to lease in the future. Lease rate structures and lease terms and conditions for the new sites were to be based on these recommendations with final Land Board approval prior to auction (Land Board 2007b).

In July 2007, the Land Board approved the auction of two cottage site leases at Priest Lake using a rental rate of 5% of appraised fee simple land value (Land Board 2007c). Lease bids started at 5% of appraised value, or $22,000 (Russell 2007c). The auction occurred in October 2007 and failed to attract a single bid (Russell 2007b). In November 2007, the Land Board directed IDL to postpone further cottage site auctions (Land Board 2007d).

In December 2007, the Land Board froze 2008 rates for cottage site leases at Payette Lake at 2007 values (Land Board 2007e).

2.3. Premium rent. In 1981, the Land Board recognized that low lease rent was resulting in significant leasehold value. With the consent of the lessees, the Land Board adopted an equity sharing "premium rental" policy (Land Board 1997). The policy was formally adopted into department administrative rules in 1987, with a sunset clause of December 1992. In May 1992, the Board adopted the policy again but without a sunset clause (Land Board 1997).

The premium rental policy applies if a lessee assigns the lease to another party (i.e., "sells" the lease). The current lessee then must pay the state 10% of the leasehold value established through the transaction as one-time premium rent. Leasehold value is determined by subtracting the value of approved lessee-owned improvements from the total sale price (IDL 2001). The lessee has the option to determine the value of improvements either by using the county assessed valuation of the improvements or by paying for the state to make an appraisal of improvement value (IDL 2001). Table 2-1 shows the number of lease assignments with and without premium rent at Priest and Payette Lakes between 2003 and 2007.

2.4. Lease term. Historically, the statutory maximum length for a cottage site lease was 10 years. In 2008, the Idaho Legislature amended Idaho Code to allow IDL to increase the lease term for all cottage sites on state endowment lands from 10 years to 35 years (Idaho Code 58-307(3)). The rationale for lengthening the lease term was that it would more generally coincide with a traditional 30-year mortgage term for residential real estate. The Land Board and the Legislature anticipated that this would heighten interest in state cottage site leases by prospective lessees and increase the availability of financing for residences on the cottage sites (Idaho Legislature 2008). For example, Freddie Mac (Federal Home Loan Mortgage Corporation) requires that leases terminate no earlier than five years after the mortgage term (Freddie Mac 2006).

3.0. What guidance on long-term residential real estate leasing is in published literature?

Compared to the body of real estate literature as a whole, guidance is sparse on long-term leases for residential real estate. The guidance related to cottage site leasing on state endowment lands is even more sparse because cottage site leases are land leases, or ground leases. The state leases the land, wheras improvements are owned by the lessee. Land or ground leases for single-family residential use are rare in the United States. Most single-family residences are either owned in fee simple by the resident, or are rented for short-term periods.

The goals of the Land Board and IDL are for the cottage site leasing program to a) meet the

Table 2-1. Cottage site lease assignments per year, 2003-2007.

	2003	2004	2005	2006	2007
Priest Lake					
without premium rent	11	7	9	0	0
with premium rent	14	9	9	4	6
Total	25	16	18	4	6
Payette Lake					
without premium rent	4	4	5	1	1
with premium rent	7	4	9	5	3
Total	11	8	14	6	4

Data source: IDL 2008c.

"maximum long-term financial return" constitutional obligation to the trust beneficiaries, and b) ensure that each cottage site lot "generates market rent throughout the duration of the lease" as required by statute. Several pertinent areas of inquiry in the research literature result from these goals, including: property rights and leasing, appraisal, appraisal of leases, market rent and contract rent, land leases, appraisal of land leases, rates of return, and rent adjustments and reevaluations. Although these topics may appear disjointed, each addresses a part of the challenge of creating a cottage site leasing program that meets the two goals. Each of these topics is addressed in a subsection below, with a concluding "guidance" section.

3.1. Property rights and leasing. The property rights, and therefore property values, of the state and cottage site land lessees are different than those of residents at Payette and Priest Lakes who own their properties in fee simple. A cottage site lease creates a partial private interest in the land asset property. The state has the *leased fee* interest, whereas the lessee has a private *leasehold* interest. Explanation of this key point follows.

One popular theory envisions property rights as a bundle of sticks (Figure 3-1; Barlowe 1986). Each stick represents a separate right or interest inherent in ownership. The bundle of private rights includes: the right to use and occupy the property, the right to sell an interest, the right to lease an interest, the right to mortgage an interest, the right to give an interest away, and the right to do none or all of these things. These individual rights can be separated from the bundle by sale, lease, mortgage, donation, or another means of transfer (Appraisal Institute 2001, 2007).

Ownership of the bundle of sticks (private rights) is known as the fee simple interest, or fee simple estate. Owning the fee simple estate means exclusive ownership unencumbered by any other interest or estate, subject only to the limitations imposed by governmental powers of taxation, eminent domain, police power, and escheat (Barlowe 1986, Appraisal Institute 2002).

When the fee simple estate is separated into bundles of one or more sticks (or a portion of individual sticks), a partial estate, or partial interest, in a specific property is created. When an owner enters into a lease with a tenant, two less-than-complete estates are created: a *leased fee* estate and a *leasehold* estate (Appraisal Institute 2001).

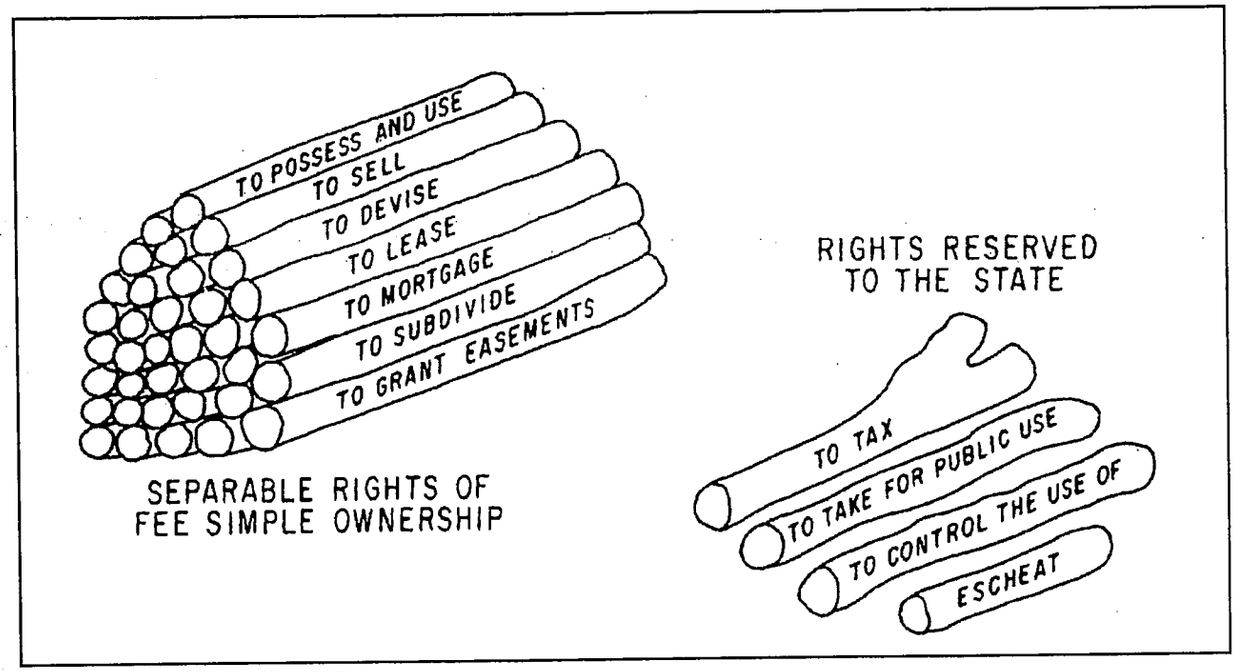


Figure 3-1. The bundle of rights in property.

Source: Barlowe 1986.

A *leased fee* estate is an ownership interest held by a landlord, with the right of use and occupancy conveyed by lease to others. The rights of the lessor (the *leased fee* owner) and the *leased fee* itself are specified by contract terms contained within the lease. The lessor is compensated for the rights transfer by some form of rent. Typically, the lessor has the right of repossession at the termination of the lease, default provisions, and the rights to sell, mortgage, or bequeath the property during the lease period (Appraisal Institute 2001, 2007).

A *leasehold* estate is the right to use and occupy real estate for a stated term under certain conditions as conveyed by the lease. Under a lease, the tenant usually acquires the rights to possess the property for the lease period, to sublease the property, and to improve the property under restrictions specified in the lease. In return the tenant must pay rent, surrender possession of the property at the termination of the lease, and abide by the lease provisions established with the lessor (Appraisal Institute 2007).

In the case of Idaho's cottage sites, numerous lease conditions affect the property rights distribution between the lessee and lessor. For example, the state restricts the use of the site to residential uses only, and lessees may not rent the property to others for more than 14 days per calendar year. No subleasing, assignment, or mortgaging is allowed without the consent of the state. Lessees must obtain consent from the state for improvement construction, landscaping, and fencing. The state also retains the right to use the land, or grant the public or others the right to use the land, to the extent that such use is not incompatible with the lessee's use (IDL 2001).

3.2. Appraisal. Appraisal is the act or process of developing an opinion of value, or the opinion of value itself (Appraisal Institute 2002). Most of the time appraisals are used to estimate the market value of fee simple ownership in a property. Market value is the value of specific ownership rights to an identified parcel of real estate as of the

effective date of the appraisal (Appraisal Institute 2002).

Appraisers determine market value by studying what people have done in the past to predict what they will do again in the future under similar circumstances. This is usually sound logic, except when unique situations make predicting a buyer's future behavior difficult (Rattermann 2007). Appraisers use one or more of three basic methods or approaches to develop an opinion of value: sales comparison, income capitalization, or cost replacement (Appraisal Institute 2001).

The sales comparison approach is a set of procedures in which a value indication is derived by comparing the property being appraised to similar properties that have been sold recently, then applying appropriate units of comparison and making adjustments to the sale prices of the comparable properties based on elements of comparison (Appraisal Institute 2002). In some markets there are so few market transactions, or the comparable properties are so dissimilar, that making comparisons is difficult, and the sales comparison approach is less reliable (NCREIF 1991, Rattermann 2007).

Elements of comparison include: property rights conveyed, financing terms, conditions of sale, market conditions, location, physical characteristics (access, visibility, topography, shape, and size), zoning, and available utilities (NCREIF 1991). The property rights of state endowment trust land leaseholders are different than the rights of fee simple owners, making sales comparisons especially problematic (see Section 3.1). For waterfront properties, such as some cottage sites on Payette and Priest Lakes, more specialized elements of comparison may come into play. Several studies have shown that while lake frontage (linear feet of shoreline) is a primary determinant of value for lakeside residential property, other site variables also are important in determining the value (Boykin 2001, Colwell and Dehring 2005). In addition, the quality and types of views have effects on residential property values (Benson et al. 1998).

The income capitalization approach is a set of procedures through which an appraiser derives a value indication for an income-producing property by converting its anticipated benefits into property value (Appraisal Institute 2002). A key element of this approach is the selection of an appropriate capitalization or discount rate (Appraisal Institute 2001).

The cost approach is a set of procedures through which a value indication is derived for the fee simple interest in a property by estimating the current cost to construct a reproduction of, or replacement for, the existing structure. The estimate includes an entrepreneurial incentive, a depreciation deduction from the total cost, and an addition for the estimated land value. Adjustments may then be made to the estimated fee simple value of the subject property to reflect the value of the property interest being appraised (Appraisal Institute 2001).

Income capitalization and cost approaches to market value are not direct studies of behavior, but reconstructions of scenarios that buyers might logically be expected to follow. If the market follows the logic of these approaches, they are excellent valuation tools; if not, they are of little practical value (Rattermann 2007).

3.3. Appraisal of leases. When partial interests are to be valued, appraisal assignments tend to become complex (Harrison 1996). Adjustments to market value for *leased fee* and *leasehold* interests are difficult to derive, and the results are less reliable indications of value (NCREIF 1991, Ratterman 2007, see Section 3.1). Lease characteristics that affect value include duration (term), amount and frequency of rental payments, escalations or adjustments to the amount of rent, renewal options, reversion of improvements, and subordination to mortgage financing (NCREIF 1991, Rodgers 1989).

The *leased fee* interest usually will not have the same market value as the fee simple interest because the tenant holds only some of the rights to the property through the lease (Appraisal Institute 2000). Also, the value of the *leased fee* interest plus the value of the

leasehold interest might not equal the value of the fee simple estate (Harrison 1996, Appraisal Institute 2001). It is possible that both the lessee and the lessor are disadvantaged because of terms of the lease (Appraisal Institute 2001).

Leases present challenges for appraisers. The sales comparison approach can be used to value the *leased fee* interest, but the approach is only meaningful when the sales being used as comparables are similar *leased fee* interests. If not, adjustments for the real property rights conveyed must be considered (Appraisal Institute 2001). The best methodology to apply when appraising the *leased fee* interest is the income capitalization approach because it allows the appraiser to perform a careful analysis of the rent compensation associated with the owner's interest, but if contract rent differs from market rent (see Section 3.4), adjustments for income potential are warranted (Keating 1998).

The sales comparison approach to valuing the *leasehold* interest is only meaningful in those relatively rare situations in which there are sales of similar *leasehold* interests that the appraiser can analyze. *Leasehold* interests are typically valued using the income capitalization approach. The income to the *leasehold* interest is the difference between market rent and contract rent (Harrison 1996). The cost approach is rarely, if ever, applicable to the valuation of a *leasehold* interest (Appraisal Institute 2001).

3.4. Market rent, contract rent, and leasehold value. Market rent is the most probable rent that a property should bring in a competitive and open market reflecting all conditions and restrictions of the specified lease agreement including term, rental adjustments and reevaluation, permitted uses, use restrictions, and expense obligations (Appraisal Institute 2002, Vernor 1988). Contract rent is the actual rental income specified in a lease (Appraisal Institute 2002). In simpler terms, market rent is the prevailing rental price for comparable properties in the marketplace, while contract rent is the compensation defined in the lease (Keating 1998). Contract rent may be equal to market rent, or it could be either more or less than market rent.

When contract rent equals market rent, the *leased fee* estate is nearly equivalent in value to the fee simple estate because if the property were to become vacant, the lessor could likely find another tenant who would pay approximately the same rent (Keating 1998). If contract rent exceeds market rent, the value of the *leased fee* estate exceeds the value of the fee simple estate. If the property were to become vacant, the lessor may not be able to find another tenant willing to pay the same rent. Instead a lower market rental rate would most likely be obtained (Keating 1998). If contract rent is less than market rent, the *leased fee* estate has a lower value than the fee simple estate. If the property were vacant, the lessor may be able to find a tenant willing to pay the prevailing market rent (Keating 1998).

When contract rent equals market rent, the *leasehold* estate basically has no value, except for the value of tenant-owned improvements. However, the potential for a positive *leasehold* value could arise, depending on the duration of the lease term (Keating 1998). If contract rent is lower than market rent, the *leasehold* interest could have positive value beyond the value of tenant-owned improvements. The value is positive if the lease agreement permits subletting or assignment and a significant lease period remains. Even if the lease does not allow subletting or assignment, it may be valuable to the tenant for its use value and opportunity cost savings over market rent levels. If the lease agreement can be cancelled or has a very short remaining term, however, it is unlikely that the *leasehold* position is marketable or has much value (Keating 1998).

If contract rent exceeds market rent, the *leasehold* estate has negative value, not considering any potential positive value resulting from tenant-owned improvements. The value is negative because the tenant is paying more than the typical market rent (Keating 1998). Negative or positive *leasehold* interests will cease if contract rent equals market rent any time during the lease or when the lease expires (Appraisal Institute 2001).

3.5. Land leases. With a land lease, also referred to as a ground lease, a landowner leases land to a tenant, but the improvements (i.e., buildings) on the land are owned by the tenant. Cottage site leases are land leases. In general, the motivation for a lessor to enter into a land lease is to retain ownership of the property while at the same time generating income (Carneghi 1994). The State of Idaho appears to follow this motivation with cottage site leases.

The motivations of a lessee are somewhat more complex because a ground lease is almost always more complicated than a fee simple ownership transaction. For example, leasehold financing is more difficult to obtain than fee financing due to a greater risk. The motivations of a lessee may include the ability to control and use property that would not otherwise be available (i.e., the property is not for sale) or to avoid the upfront capital cost of purchasing property (Carneghi 1994). The motivations of cottage site lessees likely could include either of these rationales, but for Payette and Priest Lakes the lessees' motivations are not actually known.

In general, land lease transactions are infrequent compared to outright purchase and ownership. Land leases are relatively more frequent where property is limited, and for this reason landlords have relatively greater control in the negotiating process (Carneghi 1994). Market demand is an important factor in an initial land lease transaction. Only in markets with strong demand are lessees willing to enter into land leases (Carneghi 1994). The state's recent experience when its two new Priest Lake cottage sites received no bids (see Section 2.2) may suggest weak demand for new land leases, at least under the terms and conditions offered by the state. Another aspect of market demand is the availability of substitute sites. Land leases are most commonly found where there is a shortage of alternative development sites (Carneghi 1994). Lakefront property is a relatively scarce resource.

Most land leases express the contract rent as a percentage of the fee simple market value of the land. This is the way cottage site rental rates are expressed on Payette and Priest Lakes. The problem in determining whether the contract rent equals market rent is that while sufficient data typically exist to establish market value of the fee interest in land, sufficient actual transaction data seldom exist to establish market rent. This is because land leases are generally infrequent compared to outright sales of property (Carneghi 1994). The market rent analysis in the 1998 appraisal of cottage sites at Payette Lake exemplifies this problem (see Knipe & Knipe 1998).

Most land leases in the United States are for commercial property. Land leases for single-family residential use, such as cottage sites, are much less common (Appraisal Institute 2007). A few other western states have programs where state land is leased for single-family residential use (see Section 4.0), but leases of private land for single-family residential use are more rare. Hawaii and some areas of Maryland have concentrations of land leasing for single-family residential housing (Neil 2006). Both of these situations are artifacts of historical land development: Hawaii because in times past a very few families owned most of the land in the state, and Maryland from the legacy of the English feudal land system adopted during the colonial period. Both states have undergone major land reforms, including encouraging conversion to fee simple ownership (Carneghi 1994, La Croix et al. 1995, Maryland's Peoples Law Library 2008, Maryland Department of Housing and Community Development 2008).

Land leasing is more common in the United States for manufactured or mobile home developments. Residential land leasing is also more common overseas, for example in the United Kingdom and Hong Kong (Hong 1998, Dixon et al. 2000). The rarity of land leasing for single-family residential use in the United States appears to limit the amount of research literature available to provide guidance for cottage site leasing.

3.6. Appraisal of land leases. To reach an opinion of value for leased land, an appraiser uses the same methods applicable to other forms of property ownership. Sales comparison and income capitalization methods

are discussed below. The cost approach is generally inapplicable because the appraiser is interested in land value, not replacement costs of the improvements.

Sales comparison is usually the most reliable way to estimate leased land value (Appraisal Institute 2001). However, if information on sales of comparable sites subject to land leases is unavailable, the appraiser can investigate sales of comparable plots of land that are not leased. Analysis of these transactions may yield an estimate of the rate of return an investor expects from comparable sites—i.e., a market-derived capitalization rate that can be applied to determine the land rent for the subject property (Appraisal Institute 2001). However, adjustments to the comparable properties' values must be made to reflect differences in the property rights conveyed and the specific terms and conditions of the land leases (Carneghi 1994, Janssen 2003, Appraisal Institute 2007). Residential properties on leased land can sell for significant discounts as compared to similar fee simple properties (Capozza and Sick 1991).

Ground rent capitalization, a form of the income capitalization approach, also can be used to appraise either the *leased fee* interest or the *leasehold* interest of property subject to land leases, but it is not generally applicable to single-family residential properties (Appraisal Institute 2001, Appraisal Institute 2007). To apply ground rent capitalization, an appraiser must derive a capitalization rate from the market that reflects the relationship between land sales and land rents. However, if sales are available to support such a derivation, these sales can often be used to value the land directly using the sales comparison method (Appraisal Institute 2007). On lands with improvements, the appraiser must be able to separate the value of the improvements from the value of the leased land. A land residual or allocation method is used most often (Appraisal Institute 2001; NCREIF 1991; Bioeconomics, Inc. 1993). The allocation method is based on typical ratios of land value to improvement value for specific categories of real estate in specific locations. Allocation is useful when transactional data on comparable sites in the immediate area are not available. The typical land value can be inferred by the price range of improved properties in the immediate area if an appropriate allocation ratio can be established in the community for a specific property type (Appraisal Institute 2001).

3.7. Rental rate and rate of return. The rental price for land leases usually is set as a percentage of fee simple market value. The percentage or rental rate usually reflects the lessor's expected rate of return on the real estate investment. Rates of return on investments generally reflect the risks associated with the investment (Appraisal Institute 2001).

Rates of return also are used to capitalize or discount benefits or costs in the income capitalization approach to appraisal. Comparable properties in the income capitalization approach should have the same degree of risk as the subject property because risk is a consideration in the selection of the capitalization rate (Appraisal Institute 2001).

No studies were found identifying common rates of return for residential land leases. One study suggests that a commercial land lease is often much like a bank certificate of deposit or a corporate bond, but real estate risks may be somewhat higher so that a land lease rate would be higher than a corporate bond with the same maturity schedule (Carneghi 1994). Another study suggests that equity real estate investment trusts (REITs) may provide an appropriate target for rate of return for leased properties (Hendershott 1996). Current rates of return for 10- to 35-year real estate investments are in the 10 to 13% range, which includes both capital appreciation and dividend yield (NAREIT 2008). Dividend yields over the last five years have averaged 5% (NAREIT 2008).

Total rates of return for other real estate investments are not directly comparable to the cottage site contract lease rate of 2.5% of land value. The 2.5% expresses only the proportion of cash rent as a function of the underlying cottage site asset value. In addition, the cottage site asset is appreciating, and that

change in asset value is part of a total rate of return. Cottage site program revenues are indicative of asset value appreciation. Revenues increased from $2.7 million in FY 2003 to $4.4 million in FY 2007, an increase of 63% overall or 13% compounded annually (Table 3-1).

3.8. Investment risk. Various types of risk apply to real estate investment (Appraisal Institute 2001). Market risk is the risk that revenue will be affected by changes in the market—i.e., shifts in demand and/or supply—and is influenced by factors such as the type and location of property. Financial risk is related to the use of debt to finance an investment—e.g., default, prepayment, contractual financing terms that cannot respond to interest rate changes—and is influenced by the amount and type of debt. Capital market risk is the risk that market value will be affected by changes in capital markets—e.g., mortgage yield rates, equity yield rates, or overall yield rates—and is influenced by changes in levels of interest rates, changes in availability of both mortgage and equity capital, and the rate of return for alternative investment opportunities (Appraisal Institute 2001).

Other types of risk include the following: Inflation, or purchasing power, risk is influenced by lease provisions that provide inflation protection. Liquidity or marketability risk is the difficulty of converting a real estate investment into cash at market value in a reasonable time. Environmental risk is the risk that the market value of a property will be affected by its physical environment, including perceived health hazards, costs associated with dealing with potential environmental problems, and acts of nature such as earthquakes and weather conditions. Legislative risk is the risk that legal factors will affect the market value of a property and is influenced by tax law changes, environmental regulations, change in land use regulations (zoning), and ability to navigate permitting processes. Management risk is the risk that management cannot ensure that the property meets defined goals and is influenced by the competency of management (Appraisal Institute 2001).

Each of these types of risk can influence a property separately or in various combinations. The terms of a land lease and the relative risks to the lessor and the lessee influence the

Table 3-1. State of Idaho Cottage Site Program revenues, FY 2003 - FY 2007.

	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Payette Lake—waterfront rent	$636,948	$765,069	$776,681	$1,133,897	$1,498,288
Payette Lake—non-waterfront rent	$162,576	$152,898	$149,546	$177,465	$226,662
Payette Lake—premium rent	$24,081	$214,835	$219,302	$565,275	$257,228
Priest Lake—waterfront rent	$1,796,113	$1,810,449	$1,805,310	$1,985,197	$2,192,857
Priest Lake—premium rent	$102,341	$185,658	$155,934	$155,026	$259,123
Other revenue	$5,576	$4,188	$2,877	$5,816	$10,091
TOTAL	$2,727,635	$3,133,097	$3,109,650	$4,022,676	$4,444,249

Data source: IDL 2008b.

appropriate rate of return and thus the land-lease rental rate (Carneghi 1994). For example, generally, there is more risk in obligating money for a longer term than a shorter term, and longer term investments generally provide a higher rate of return to compensate for this commitment (Carneghi 1994, Jones and Roach 1989). Also, generally, there is less investment risk associated with below-market rental rates than with a rate at or above market level, so the rate of return is lower (Keating 1998).

Subordination also can significantly influence a land lease rate (Carneghi 1994). A subordination clause means the lessor subordinates his or her interest to that of a lender. The existence of a subordination clause makes it considerably easier for a lessee to finance improvements on the land-lease parcel. This is because in the event of a default the lender's interest takes priority over that of the landowner, so the lender will view the property as substantially less risky than an unsub-ordinated land lease. Given that increased yield is based on increased risk, an unsubordinated land lease (with lower risk to the landlord) would carry a lower land-lease rate than a subordinated land lease, all other factors being equal (Carneghi 1994).

3.9. Rental adjustments and reevaluations. There are two basic ways that lessors attempt to keep contract rents current with market rents (Carneghi 1994, Rodgers 1989, Jones and Roach 1989). The most common is to adjust rent according to some standard price index such as the Consumer Price Index (CPI). The adjustment is usually made annually, or it can be periodic, for example every five years. The adjustment can be applied to the base lease rate as simple interest or cumulatively compounded. The adjustment can have a cap or a floor or be unlimited. The adjustment may be some fraction of the index change (Carneghi 1994).

Adjustments using the CPI are controversial. For example, in the 1998 appraisal of lots at Payette Lake, the appraiser suggested that CPI is not an appropriate index because it reflects the national general inflation rate, rather than the increase in local real estate values (Knipe & Knipe 1998). On the other hand, cottage site lessees claim that it is normal and customary to have an adjustment tied to CPI and not exceeding 3% per year (Payette Lake Cabin Owners Association and Priest Lake State Lessee Association 2008).

The other common adjustment in leasing is to reappraise the property periodically to bring the contract rent back to the market rent level. The reappraisal can be done as often as the parties wish, but typically because of the expense it is done every 10 or 20 years. Variations on this adjustment include reappraising the land value, but leaving the land lease rate fixed; reappraising the land value and moving the land lease rate to market; reappraising one or the other but not allowing rent to be less than the most recent amount paid; and having the reappraisal clause only at the option of the lessor or the lessee (Carneghi 1994).

3.10. Guidance from the literature. Because of the unique nature of the state's cottage site leasing program, guidance from the research literature is limited. Land leases for single-family residential use properties are uncommon in the United States, thus research has not been a priority for lessors, lessees, or real estate researchers. Also, in general, research on leases has lagged far behind research on loans or mortgages (Hendershott 1996).

The research literature leads one to question whether "market rent," as the term is conventionally used, can be established for cottage site leases because so many characteristics of the "market" are unusual. For example, markets typically are defined by many buyers and sellers (Appraisal Institute 2002), or in the case of a market for leases, many lessors and lessees. In the case of cottage site land leases on Payette Lake there is only one lessor—the State of Idaho—and on Priest Lake only the state and federal governments lease land for residential use. During the 1998 appraisals of cottage sites on Payette and Priest Lakes, appraisers were unable to locate any private land leases for residential properties on either lake (Land Board 1998c). Also, markets

typically are defined by transactions that take place throughout a time period. In the case of cottage site leases, all leases currently expire at the same time. In addition, current cottage site lessees have preferential renewal rights at the end of a term (i.e., no conflict bidding).

The lack of a competitive, open market for single-family residential land leases on Payette and Priest Lakes forces appraisers to make unusual adjustments to standard methods of arriving at opinions of value. For example, the comparable properties used to establish market lease rates in the 1998 appraisal of cottage leases at Payette Lake included properties in South Carolina, Oregon, Arizona, Washington, California, Minnesota, and Alabama (Knipe & Knipe 1998). One could question whether properties in these states are valid bases of comparison for properties in Idaho. Unusual situations and markets make appraisals more subjective, more variable, and less reliable for estimating market values, market capitalization rates, and market rents.

Does the literature suggest an appropriate lease rate for cottage sites? No, the research literature does not provide much guidance but suggests that establishing an appropriate land-lease rate involves a higher than normal degree of subjectivity (Carneghi 1994). One study of land lessors of commercial properties found the most common opinion was that *leased fee* interests are inherently similar in investment appeal to long-term debt instruments such as mortgages or bonds (Rodgers 1989). The second most common general opinion in the study was that 10% was an appropriate rate of return for land leases, but the rationale was not identifiable (Rodgers 1989).

4.0. How do other states set lease payments for residential real estate such as cottage sites?

Few other states lease trust land or other real estate for residential use or single-family cottage sites. Most of the states that do set a target lease rate at least double that of Idaho's 2.5% of assessed or appraised market value. Details follow.

4.1. Alaska. The state of Alaska leases remote recreational cabin sites, but the bases for comparison to Idaho are limited. The intent of the Alaska leasing program is to facilitate transfer of remote, unsurveyed lands into private hands. The initial lease period is three years with a lease payment of $100 per year. During that time the Alaska Department of Natural Resources surveys and appraises the property and enters into a purchase contract with the lessee. If the lessee does not wish to purchase the parcel during the three-year lease period, he/she can renew the lease for a single five-year term with lease payments of $1,000 per year (Alaska Department of Natural Resources 2008).

4.2. California. California does not allow long-term residential use of its school trust lands, but does lease other state lands for recreational cabin sites. The California State Lands Commission leases recreational cabin sites under its non-incoming producing (for the lessee) general permit system. In general, the annual rental rate is based on 9% of the appraised value of the leased lands with a minimum rental of $50, although the commission has some discretion in determining the rent. The lease period for a general permit for recreational use is 10 years (Title 2, California Code of Regulations § 2000 et seq.).

4.3. Montana. The Trust Land Management Division of the Montana Department of Natural Resources and Conservation manages Montana's residential leasing program on state trust lands. For residential leases Montana has a target lease rate of 5% of appraised market value, with a reappraisal every five years. The term of the lease is variable from 10 to 25 years (Montana Department of Natural Resources and Conservation 2008).

4.4. Oregon. The Oregon Department of State Lands has only four cabin site leases, all on Lake Owyhee in the southeastern part of the state. Oregon's asset management plan calls for the renegotiation of leases to market rates and periodic review to ensure market rates are attained. The plan also calls for the investigation of the potential for additional cabin site development. The revenues from

cabin site leases have been diminishing from $2,040 in 2000 to $406 in 2005 (Oregon Department of State Lands 2006).

4.5. Utah. Utah leases state trust land for residential purposes and recreational cabin sites. The Division of Forestry, Fire and State Lands must receive at least fair market value for the leases. According to Utah Administrative Code, lease rates are determined by multiplying the fair market value of the subject property by the current division-determined interest rate (Utah Administrative Code R652-30). In practice, Utah uses the appraised value of the land times the prime interest rate as a base for determining the lease rate. The division has some latitude for adjustment of the lease rate based on location of the land and other factors (Higgins, personal communication). In June 2008, the prime interest rate was 5.00% (Federal Reserve 2008).

Utah adjusts base rental rates based on changes in market value, changes in established indices, or other methods which may be appropriate and in the best interest of the beneficiaries. Indices may include information from any or all of the following sources: changes in assessed value for the most current year, the applicable component of the Consumer Price Index for All Urban Consumers (CPI-U), the applicable Implicit Price Deflators for the Gross National Product, data from market analyses of comparable leases, or public comment. The determination of which method to use may be based upon an analysis of the cost effectiveness of performing the review (Utah Administrative Code R652-30).

4.6. Wyoming. The Wyoming Board of Land Commissioners is authorized to lease state trust lands for recreational purposes, including cabin sites (Wyoming Statutes 36-5-115). Wyoming currently leases 24 cabin sites, and most of the leases are for 25 years, although leases may be up to 75 years in length (Van Hatten, personal communication). The annual rental rate is the amount bid by the applicant, if accepted by the Board, but is not to be less than fair market value for the same or similar use of the land and any improvements owned by the state after an economic analysis is made. In cases where annual rent cannot be established based on fair market value for the same or similar use of the land, the minimum rental rate is not to be less than $250.00 or 5.5% of the appraised land value and any improvements owned by the state (Wyoming Board of Land Commissioners 2007).

4.7. National forests. The National Forest System is federal land, not state land, but nevertheless instructive. The U.S. Forest Service permits recreational residence sites on national forest lands under its special uses permit system, and there are currently 121 such permits on national forest lands on Priest Lake (Butler, personal communication). The recreational residence special use permit program has undergone numerous changes in the last decade in response to the Cabin User Fee Fairness Act of 2000 (CUFFA, P.L.106-291). The purpose of the recreational residence program as described in CUFFA—"to preserve the opportunity for individual and family oriented recreation"—is different than the revenue-generating mission of state endowment trust lands. Unlike a state cottage site, a recreation residence on national forest land cannot serve as a permanent residence. The features of the federal leasing program are as follows.

The base fee for a recreation residence special use permit is equal to 5% of the market value of the recreation residence lot as determined by appraisal. The base fee is recalculated at least once every 10 years. The U.S. Forest Service allows a 3-year phase in of the new base fee if it increased more than 100% from the previous base fee. The term of a permit is normally 20 years (USDA Forest Service 2006).

Recreation residence fees are adjusted annually using a price index. During the transition period for implementing CUFFA the index is the Implicit Price Deflator, Gross Domestic Product (IPD-GDP). After the transition period, the index used will be changes in agricultural land prices in the appropriate state or county, as reported in the Index of Agricultural Land Prices published by the U.S. Department of Agriculture. However,

the U.S. Forest Service may select and use another index if it determines that a different index better reflects change in the value of a lot over time (P.L. 106-291). The annual adjustment to the base fee can be no more than 5% in any single year. When the annual adjustment would be more than 5%, the amount of the adjustment in excess of 5% is applied to the annual fee payment for the next year in which the change in the index factor is less than 5% (USDA Forest Service 2006).

5.0. What alternative methods are available to set lease payments for endowment land cottage sites for a 35-year period that are consistent with the "market rent" mandate?

The following reply summarizes relevant methods for setting lease payments identified previously by examining the literature (Section 3.0) and other leasing programs (Section 4.0). The challenges of meeting the "market rent" mandate are addressed further in the Conclusions (Section 6.0).

5.1. Appraisal. Theoretically, appraisal is an accurate and efficient way to estimate market rent, and therefore set contract rent, or the lease payment. If a lease market exists, appraisal of market rent is a matter of collecting information on similar properties and their leases to estimate contract rent that represents market rent. Many leases express contract rent as a percentage of appraised or assessed fee simple market value, and therefore the contract rental rate is known directly. Other leases may express rent as a periodic lump sum of cash, which then requires an appraisal of fee simple market value in order to determine the contract rental rate.

The lack of a residential land lease market at Payette and Priest Lakes complicates appraisal for determining cottage site lease payments or rates. Appraisal of fee simple bare land value is fairly uncomplicated, although it is becoming more complicated because of the lack of comparable sales of unimproved lots on Payette and Priest Lakes (Land Board 2008). Appraisal complications arise primarily because few residential properties at Payette and Priest Lakes are leased under similar conditions as state leases. For example, the limited number of private leases at Payette and Priest Lakes are for improved properties (i.e., residence and land) with shorter terms (e.g., weekly, monthly, or seasonal) (Land Board 2008). Differences in property characteristics and lease conditions require appraisers to make adjustments to value estimates, making them less accurate and more subjective and thus open to question. Additionally, appraisers must look for comparables in lease markets in other geographic areas that may not accurately represent the local lease market.

The assignment an appraiser undertakes also determines the results. One of the criticisms that lessees at Payette and Priest Lakes have voiced about the state's method for setting cottage site rents is that the appraisal assignment has always been to appraise fee simple fair market value and then assign a lease rate, not appraise market rent directly by looking at other rent contracts on the lakes (Land Board 2008). It is unclear whether there are enough rental contracts to create a sufficient data set of comparable properties. This uncertainty could be readily addressed.

Despite the challenges of estimating the fair market value of or rent for cottage site leases, appraisal is one of the tools available. Appraisal options include individual appraisal of each cottage site or a multi-property appraisal whereby several representative properties are appraised and then the values are extrapolated and aggregated to all properties. The 1998 multi-property appraisals at Priest and Payette Lakes, for example, indicated a fair market lease rate of 3.5% and 6% of fee simple market value, respectively (Land Board 1998c). The current lease rate is 2.5% of fee simple market value.

5.2. Other programs. Another option for setting lease rates is to adopt rates based on what other residential land leasing programs are doing. In Section 4.0, we examined residential and recreational leasing programs in other states and on National Forest System lands. Among programs with financial objectives similar to Idaho's, contract lease

rates ranged from 5.0% to 9.0% of fee simple market value with most in the 5.0% to 5.5% range. The appropriateness of adopting a contract lease rate based on comparison with other states is open to question, but is consistent with the comparison approach of real property appraisal.

5.3. Alternative investments. Generally, investors seek similar rates of return on investments with similar risks. Target rates of return for land leases for commercial properties have been compared to mortgages, government and corporate bonds, and REITs, but unusual conditions may affect comparability. For example, target rates of return normally reflect the cost of capital to the landowner, such as mortgage costs (Keating 1998), but in the case of cottage sites, the state already owns the land outright, having received it as a federal land grant at statehood.

Historic average rates for 30-year fixed-rate mortgages, 30-year government bonds, and AAA corporate bonds have all followed the same pattern over the last 30 years, with high rates in the early 1980s and historically low rates since 2000 (Figure 5-1). The June 2008 rates for each were 6.32%, 4.69%, and 5.68%, respectively.

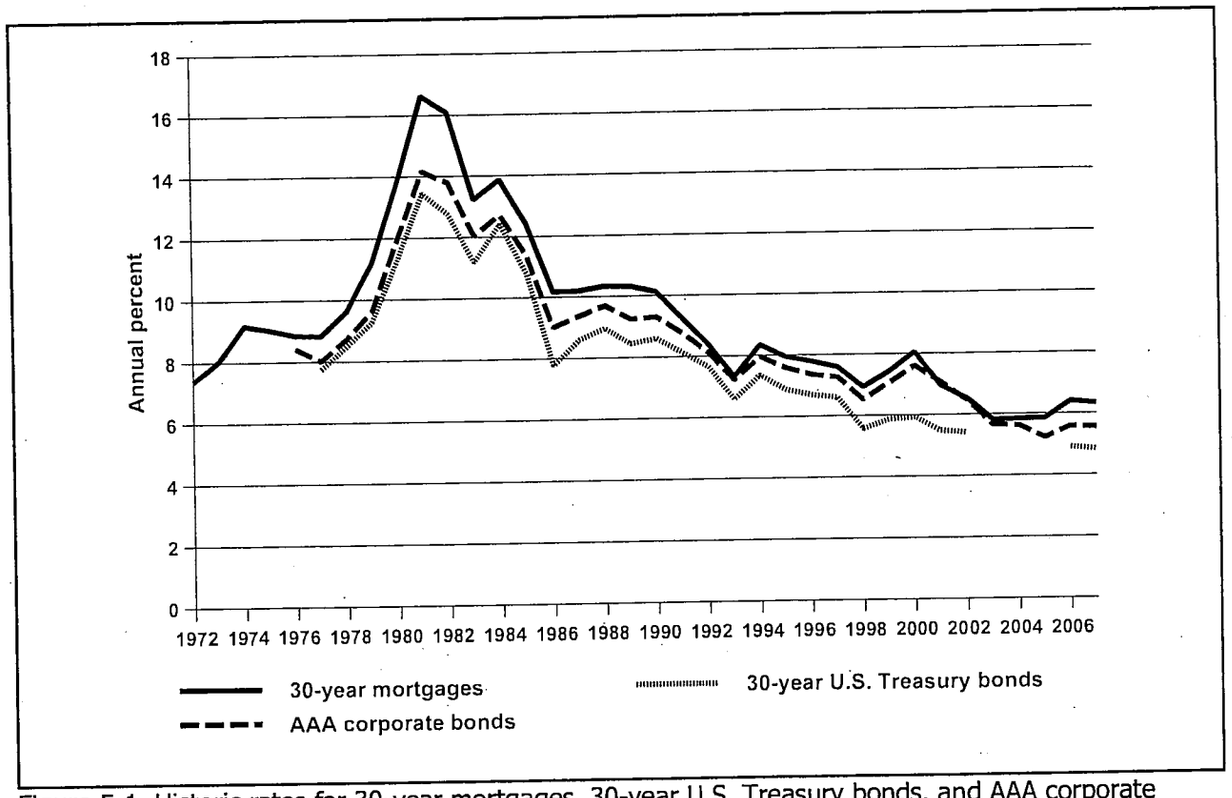


Figure 5-1. Historic rates for 30-year mortgages, 30-year U.S. Treasury bonds, and AAA corporate bonds.[1]

Note: 30-year U.S. Treasury bonds were discontinued in February 2002 and reissued in February 2006.

[1]Rates reported are: [1] 30-year mortgages—contract rate on 30-year, fixed rate conventional home mortgages; [2] 30-year U.S. Treasury bonds—market yield on U.S. Treasury securities at 30-year constant maturity, quoted on investment basis; [3] AAA corporate bonds—Moody's yield on seasoned corporate bonds–all industries AAA.

Apparently, IDL has considered using the average 30-year fixed-rate mortgage rate because it is defined as a "transaction rate" in the draft 2008-2018 cottage site lease (IDL 2008a). However, the rate is not mentioned elsewhere in the lease, and the 2008 draft lease prepared by IDL has not been adopted.

The National Association of Real Estate Invest Trusts (NAREIT) compiles an Equity REIT Index. The index indicates 5-, 10-, and 35-year return rates of 18.34%, 10.69%, and 13.27%, respectively (NAREIT 2008).

The rates of return reported on alternative investments often include asset appreciation in addition to the cash return. For example, the 5-year return on the NAREIT Equity REIT Index of 18% includes capital appreciation and a dividend yield that averaged 5% (NAREIT 2008). As we pointed out earlier (Section 3.10), the contract lease rate of 2.5% of land value used for cottage sites is the cash return, which is similar to a dividend yield. Total cottage site program revenues have been increasing at a compound interest rate of 13% annually between FY 2003 and FY 2007 (Table 3-1), due to appreciation of the cottage site asset.

5.4. Benchmarks. Another option is to set a lease rate based on a benchmark rate of return derived from other institutional investors such as pension funds or other endowments. For example, the California Public Employees' Retirement System (CalPERS) uses 8% as the minimum target rate of return on its single-family housing investment program (CalPERS 2005).

The National Council for Real Estate Investment Fiduciaries (NCREIF) also provides benchmarks for real property investments that may be useful (Agland Investment Services, Inc. 2000). The NCREIF was established to serve institutional real estate investors as a non-partisan collector, processor, validator and disseminator of real estate performance information (NCREIF 2008). The NCREIF Property Index (NPI) includes both national and regional indices (Figure 5-2). The national NPI for 2007 was 15.85%, while the western regional NPI was 18.29% (NCREIF 2008).

The Governor's Citizens Ad Hoc Committee on Lands/Endowment (2001) recommended that the Land Board use the NCREIF indices for appropriate land categories as a benchmark for endowment land investments. (See further recommendations of this committee in Section 6.1.) Unfortunately, the NCREIF does not have an index specific to single-family residential use land leasing, probably because such leases in the U.S. are uncommon.

5.5. Leasehold value at lease assignment. Another approach to estimating market rental rates is to use *leasehold* values, which are the sale prices in the assignment (transfer) of state leases from one party to another, as a basis for computing market rent (Bioeconomics, Inc. 1993; see Section 3.4). This approach assumes the *leasehold* value plus the present value of the future annual contract rent equals the fee simple market value of the property and that a purchaser is ambivalent between taking over a given state lease or paying market value for a comparable privately owned site (Bioeconomics Inc. 1993).

Bioeconomics, Inc. (1993) used a lease assignment approach to compute market rents for cabin site leases in Montana, but other appraisers (e.g., Knipe & Knipe 1998) question some assumptions used in this approach. For example, one has to either assume a market capitalization rate or assume that the market capitalization and market rental rates are equal (Bioeconomics, Inc. 1993). A more important complication is that if the "market rent" mandate is met (i.e., contract rent equals market rent), *leasehold* value is zero.

Another potential complication is negative *leasehold* values. Some current leaseholders at Payette Lake argue that contract rents are already greatly above market rents because no one wants to purchase a *leasehold*. Therefore, *leasehold* value is zero because the State of Idaho bases its market rent on market values for fee simple properties (Payette Lake Cabin Owners Association 2008).

5.6. Auction. The most accurate way to set contract rent equal to market rent at the initiation of the lease term would be to auction each lease at the end of its current term. An

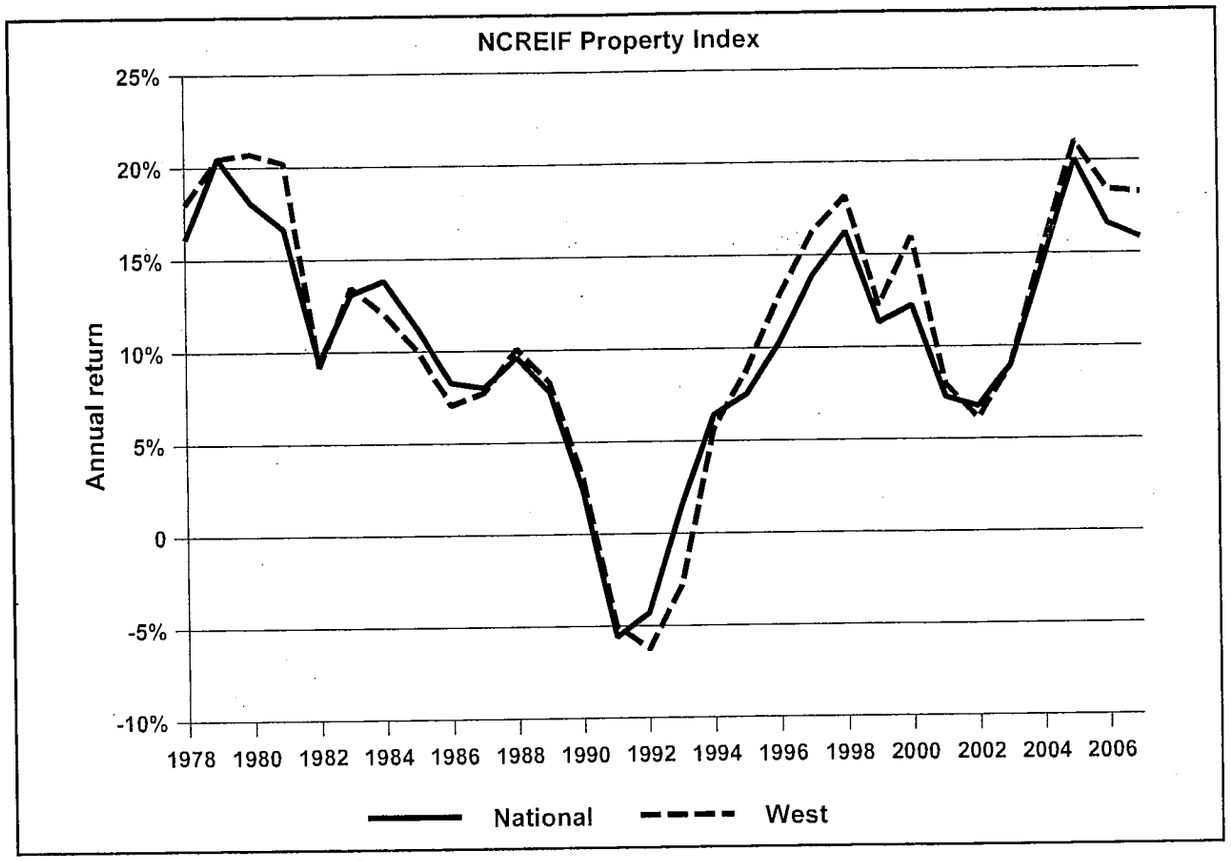


Figure 5-2. NCREIF Property Index.

Data source: NCREIF 2008.

accurate way of ensuring that contract rent continues to equal market rent would be to stagger lease auctions each year over the next lease term so that an annual metric of changes in lease values is created. Lease payments could then be increased or decreased according to this metric.

Although this alternative would be most likely to meet the market rent mandate, it involves the most financial risk to the State of Idaho. Under current statute and lease arrangements, if the Land Board cancels a lease, the state is responsible for paying the current lessee for the value of improvements. The state thus assumes the financial risk for all the improvements on cancelled leases.

Legislative change would have to occur for auctions to happen. Auctions are not consistent with the current statute that removed cottage site leases from the conflict bidding process and created the market rent mandate (Idaho Code 58-310A).

5.7. Summary. The setting of lease rental payments for cottage sites can be accomplished via several methods. Appraisals are one method and can be used to estimate market rent in two ways. If a rental market exists, then market rent can be determined by examining rental contracts from comparable properties. Adjustments have to be made for improvements, differences in lease contract terms and conditions, and other property characteristics to arrive at a comparable rent for state land leases. If other similar leased properties do not exist in the market area, then determining market rent is more complicated and is

determined by appraising the current fair market value of the land that is being leased and then applying an appropriate annual rate of return to ascertain the contract rent.

Determining the appropriate rate of return to use in setting contract rent is difficult because rates of return reported for other investments include asset appreciation as well as a cash return or dividend yield. While the current contract rental rate for cottage sites of 2.5% is below rental rates used by other residential land leasing programs and is below the rates of return reported for other real estate investments (Table 5-1), program revenues have increased at 13% compounded annually between 2003-2007, which reflects appreciation of the cottage site asset and is a part of a total rate of return for the asset.

Adjusting contract rent to keep current with changes in land value is also challenging. The application of an index of overall price changes in the economy, such as the Consumer Price Index (CPI), does not accurately reflect price changes in the real estate markets at Priest and Payette Lakes. A local real estate price index would more closely reflect land value changes in those areas, but whether such an index could be developed is open to question.

6.0. Conclusion

Creating a cottage site leasing program that meets not only the Land Board's fiduciary responsibility to the beneficiaries of the state endowment trust but also the market rent mandate is challenging. Changes to the existing program also involve issues of fairness to current leaseholders. How can the State of

Table 5-1. Rates of return (RoR) on residential real estate implied by various market measures.

Market measure	RoR%	Source
Idaho appraiser's opinion		
Priest Lake	3.5%*	Land Board (1998c)
Payette Lake	6.0%*	Knipe & Knipe (1998)
Residential leases, MT, UT & WY	5.0-5.5%**	this report, Sections 4.3 to 4.6
Recreational residence leases, nat'l forests	5.0%**	this report, Section 4.7
Recreational cabin leases, California	9.0%**	this report, Section 4.2
Residential lease program, CALPERS	8.0%	this report, Section 5.4
30-year mortgages	6.3%	this report, Section 5.3
30-year government bonds	4.7%	this report, Section 5.3
AAA corporate bonds	5.7%	this report, Section 5.3
10-year REIT	10.7%	this report, Section 5.3
35-year REIT	13.3%	this report, Section 5.3
National Property Index (NPI)	15.8%	this report, section 5.4
Western region NPI	18.3%	this report, Section 5.4

*Estimated market rental rate
**Contract rental rate. Does not include asset appreciation.

Idaho balance these challenges? No rental system has yet been devised that has the advantage of appearing equitable to both the lessor and lessee throughout its term (Barlowe 1986). The lessor and the lessee have different interests each wishes to protect. In this case, the lessor must meet goals prescribed in law, which essentially are maximizing financial return to land assets by obtaining market rent for cottage site leases.

Previous sections have outlined the complications in identifying market rent because of the unusual characteristics of the cottage site lease "market." The 1998 appraisal report for Payette Lake cottage sites summarizes the situation:

> "In the case of recreational lots in McCall, Idaho, outside of the State Dept. of Land's program, we are aware of no ground leases, and individual lots vary greatly in view, location, amenities, size, frontage, and other attributes. Expanding the search for data regionally or nationally, parallel situations are extremely rare" (Knipe & Knipe 1998).

As appraiser Ed Morris told the Land Board Cottage Site Subcommittee in April 2008, "It's a really, really complex appraisal situation" (Land Board 2008). Conducting an appraisal to determine market rent for a cottage site is indeed complicated and appears to stretch to the limit many of the assumptions on which standard appraisal methods are based.

The choice of an appropriate market rental payment, without having one indicated by the market, is subjective and based on varying perspectives (Knipe & Knipe 1998). Various elements and characteristics of the cottage site leasing program create arguments for lower, or higher, rental rates (Figure 6-1). For example, the lessee improvement buyout provision creates less risk for the lessee, so to compensate, a higher rate of return for the lessor may be warranted. On the other hand, the current rent escalation formula creates increased risk for the lessee, similar to an adjustable rate mortgage (Hendershott 1996), and thus a lower rental rate may be warranted. How the State of Idaho should account for and balance all the factors involved in choosing an appropriate rental payment is a difficult political decision, and the market provides little direction.

The law that includes the market rent mandate is also inconsistent. Idaho Code 58-310A states that the Land Board "shall ensure that each lot generates market rent throughout the duration of the lease." It also states "maximum long-term financial returns to the institutions to which granted are best obtained through *stable* leases at market rent" (Idaho Code 58-310A(1)(h), emphasis added). A given level of market rent exists only for a moment in time and will change with market conditions. Market rent is therefore inherently *unstable*.

6.1. Exploring divestment. Given the complications in meeting the market rent mandate, one must ask the question, would the Land Board and IDL better meet their fiduciary responsibilities to trust beneficiaries by divesting the cottage site properties (i.e., selling or exchanging the land) and investing the proceeds in other lands or financial instruments? We do not have a good answer, but we are not the first to ask this question. In 2001, Governor Kempthorne formed an ad hoc committee to recommend efficiency/ effectiveness changes to the Land Board regarding endowment trust assets and management practices (Governor's Citizens Ad Hoc Committee on Lands/Endowment 2001). The committee asked the same question about cottage site leases. Their reply follows.

The Ad Hoc Committee fully recognized that cottage site leasing is an emotional issue. The committee recognized that it easily can be shown that while the market value of the cottage sites has appreciated and will probably continue to increase, the cash return to the endowments is significantly below the returns provided by other investments (Governor's Citizens Ad Hoc Committee on Lands/ Endowment 2001). However, a 2.5% cash return on asset value is above the cash returns of 1.1% on rangeland assets (see PAG #21, O'Laughlin and Cook 2001, Table 1, p.5).

The Ad Hoc Committee commented that opponents to selling cottage sites argue that

Rate of Return Continuum

|----------->

0%	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%

<Public relations motives	>	Profit maximization motive>
<No lessee improvement buyout protection	>	Lessee improvement buyout protection>
<Lessee pays taxes on land	>	Lessee pays no taxes on land>
<Lower cost of capital to lessor	>	Higher cost of capital to lessor>
<Shorter lease term	>	Longer lease term>
<High rent increase risk to lessees	<	Low rent increase risk to lessees>
< Relatively high fee values	<	Relatively low fee values>

Figure 6-1. Rate of return continuum.

Source: Knipe & Knipe 1998.

Idahoans will be denied access to Payette Lake and Priest Lake in favor of wealthy people from out of state. However, the committee noted that under the current system Idahoans in general are denied access to the lakes from these cottage sites now, as they are improved properties used by individuals and families. They are held under long term agreements that are controlled by what the Ad Hoc Committee called "an elite group of generally wealthy people, many of which are from Idaho, and many of which are already from out of state" (Governor's Citizens Ad Hoc Committee on Lands/Endowment 2001).

The Ad Hoc Committee also noted that selling the cottage sites and buying commercial real estate could provide higher, safe returns to the endowments while still keeping the investment in good quality Idaho real estate. The sale and reinvestment of proceeds also may offer additional benefits because, once sold to private entities, the land is taxable, thus increasing a county's tax base (Sunderman et al. 2004). The committee also recognized the important role real estate plays in a diversified portfolio of assets in order to minimize risk and maximize long-term asset appreciation (Agland Investment Services, Inc. 2000; Governor's Citizens Ad Hoc Committee on Lands/ Endowment 2001; Sunderman et al. 2004).

The Ad Hoc Committee did not reach a conclusion or recommendation about whether all cottage sites should be sold or whether all proceeds from the sales of cottage sites should be reinvested in commercial real estate. However, the committee felt that investments in additional timbered properties and in other financial instruments should be considered. The committee felt that the majority if not all of the proceeds from the sale of cottage sites—what the committee called "good Idaho real estate"—should be used to obtain office and industrial properties in communities around the state—which are also "good Idaho real estate" (Governor's Citizens Ad Hoc Committee on Lands/Endowment 2001).

In December 2007, the Land Board adopted its Asset Management Plan that lays out management objectives for the cottage site leasing program (Figure 1-1). It appears that despite the difficulties of administering the residential real estate leasing program, the Land Board intends that cottage sites will remain a part of the endowment portfolio for the foreseeable future.

6.2. Trust responsibility. Low cash returns on leased properties and pressures from lessees to keep contract rents low are not unique to Idaho (Agland Investment Services, Inc. 2000; Sunderman and Spahr 2006). This occurs in part because state land trust managers face pressures not seen by private trust managers (Culp et al. 2006).

State trust land management is different than private trust management because often many entities perceive themselves either as trust beneficiaries—school boards, school administrators, teachers' unions, and other school advocates—or trust stakeholders—lessees, development interests, conservationists, or the public (Culp et al. 2006). Trust managers may be answerable to beneficiaries, user groups, and voters in a manner that would be inappropriate, or at least unusual, in the context of a private trust. As a result, there is not a clean separation among the roles of the state as a trustee and public agency, as well as a lawmaking and rule-making body. Many trust decisions thus involve political considerations that are unrelated to the land manager's duties as a trustee (Culp et al. 2006).

Trust management decisions, including those related to cottage site leasing, are not made in a vacuum. On the contrary, decisions are politically responsive to diverse stakeholders and concerns including those of the state legislature, the constituencies that use and benefit from trust lands and their natural resources and influence legislative and executive officials, the beneficiaries who receive the financial returns from trust decisions, and the general public whose agenda may or may not align with the strictly fiduciary concerns of the trust (Culp et al. 2006). There is unavoidable tension between obtaining financial returns for trust beneficiaries and addressing the concerns of specific stakeholders and the broader public (Culp et al. 2006). The decisions of the Land Board and IDL regarding cottage site leasing require balancing fiduciary responsibility to the beneficiaries with political considerations and stakeholder concerns.

We conclude with the same statement we made with regard to the forests and rangelands in the endowment asset portfolio. Policy decisions that guide trust land managers have been, and likely will continue to be, a balancing of financial, environmental, and social concerns (PAG #21, O'Laughlin and Cook 2001).

References

Agland Investment Services, Inc. 2000. Trust performance measurement: a report to the Western States Land Commissioners Association. <http://www.wslca.org/meetings/trust performance report-final report.pdf> [7 May 2008].

Alaska Department of Natural Resources. 2008. Leasing your site. <http://www.dnr.state.ak.us/mlw/landsale/remrec/2008/brochure/b_leasingursite.pdf> [2 May 2008].

Appraisal Institute. 2000. *The Appraisal of Rural Property. 2nd ed.* Appraisal Institute: Chicago, IL. 525pp.

_____. 2001. *The Appraisal of Real Estate. 12th ed.* Appraisal Institute: Chicago, IL. 759pp.

_____. 2002. *The Dictionary of Real Estate Appraisal. 4th ed.* Appraisal Institute: Chicago, IL. 448pp.

_____. 2007. *Appraising Residential Properties. 4th ed.* Appraisal Institute: Chicago, IL. 500pp.

Barlowe, R. 1986. *Land Resource Economics: the Economics of Real Estate. 4th ed.* Prentice-Hall: Englewood Cliffs, NJ. 559pp.

Benson, E.D., J.L. Hansen, A.L. Schwartz, Jr., and G.T. Smersh. 1998. Pricing residential amenities: the value of a view. *Journal of Real Estate Finance and Economics* 16:55-73.

Bioeconomics, Inc. 1993. Final report: economic analysis of the values of surface uses of state lands. Report for Montana Department of State Lands, Helena. In authors' files.

Boykin, J.H. 2001. *Land Valuation: Adjustment Procedures and Assignments.* Appraisal Institute: Chicago, IL. 288pp.

CalPERS (California Public Employees' Retirement System). 2005. Statement of investment policy for single-family housing program. <http://www.calpers.ca.gov/eip-docs/investments/policies/inv-asset-classes/real-estate/sgl-fam-housing-prg.pdf> [13 May 2008].

Capozza, D.R., and G.A. Sick. 1991. Valuing long-term leases: the option to redevelop. *Journal of Real Estate Finance and Economics* 4:209-223.

Carneghi, C. 1994. Determining ground-lease rental rates. *Appraisal Journal* 62:256-263.

Colwell, P.F., and C.A. Dehring. 2005. The pricing of lake lots. *Journal of Real Estate Finance and Economics* 30:367-283.

Culp, P.W., A. Laurenzi, and C.C. Tuell. 2006. State trust lands in the West: fiduciary duty in a changing landscape. <http://www.trustland.org/publications/stl_fiduciary_duty.pdf> [25 June 2008].

Dixon, T., G. Pottinger, A. Marston, and N. Crosby. 2000. Relative values: residential leasehold reform in England and Wales valuation for lease extension and enfranchisement. <http://www.cem.ac.uk/research/files/detr1.pdf> [25 June 2008].

Federal Reserve. 2008. H.15. Selected interest rates. <http://www.federalreserve.gov/releases/h15/Current/> [1 July 2008].

Freddie Mac (Federal Home Loan Mortgage Corporation). 2006. Single-family loans: resources for lenders. <http://www.freddiemac.com/singlefamily> [20 May 2008].

Governor's Citizens Ad Hoc Committee on Lands/Endowment. 2001. Report and recommendations of the Governor's Citizens Ad Hoc Committee on Lands/Endowment. <http://www.idl.idaho.gov/LandBoard/CitizenComm/CitizensReportPrelim.pdf> [7 May 2008].

Harrison, F.E. 1996. *Appraising the Tough Ones.* Appraisal Institute: Chicago, IL. 298pp.

Hendershott, P.H. 1996. Uses of equilibrium models in real estate research. Dice Center For Research in Financial Economics, Working Paper Series 96-12. <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=15173> [25 June 2008].

Hong, Y. 1998. Transaction costs of allocating increased land value under public leasehold systems: Hong Kong. *Urban Studies* 35:1577-1595.

Janssen, C.T.L. 2003. Estimating the effects of land leases on prices of inner-city apartment buildings. *Urban Studies* 40:2049-2066.

Jones, R.N., and S.D. Roach. 1989. Valuation of long-term leases. *Appraisal Journal* 57:451-459.

Keating, D.M. 1998. *Appraising Partial Interests.* Appraisal Institute: Chicago, IL. 77pp.

Knipe & Knipe. 1998. Complete appraisal, self-contained report and market rent analysis of 14 Payette Lake cabin sites. Report done for Idaho Department of Lands, Boise. In authors' files.

Idaho Legislature. 2008. House Bill No. 406. <http://www3.state.id.us/oasis/H0406.html> [31 July 2008].

IDL (Idaho Department of Lands). 2001. Cottage/Residence Site Lease. Idaho Department of Lands, Boise. In authors' files.

_____. 2007. Annual report, FY 2007. <http://www.idl.idaho.gov/news/annual_reports/ar_2007.pdf> [2 July 2008].

_____. 2008a. Cottage/residential site lease. <http://www.idl.idaho.gov/bureau/smr/cottage_sites/lease2007/oct1/app_to_lease-july2005.pdf> [1 July 2008].

_____. 2008b. Cottage program revenues, IDL financial systems, fiscal year data, FY 2003-FY 2007. Idaho Department of Lands, Boise. Data in authors' files.

_____. 2008c. Cottage site assignment data, 2003-2007. Idaho Department of Lands, Boise. Data in authors' files.

Land Board (Idaho State Board of Land Commissioners). 1986. Minutes of June 25 special meeting. Idaho Department of Lands, Boise. In authors' files.

_____. 1997. Briefing memorandum for June 4 meeting. Idaho Department of Lands, Boise. In authors' files.

_____. 1998a. Minutes of February 10 regular meeting. <http://www.idl.idaho.gov/LandBoard/1998MinutesPDF/021098--final minutes.pdf> [2 July 2008].

_____. 1998b. Minutes of May 12 regular meeting. <http://www.idl.idaho.gov/LandBoard/1998MinutesPDF/051298--final minutes.pdf> [2 July 2008].

_____. 1998c. Minutes of Cottage Site Subcommittee October 1 meeting. <http://www.idl.idaho.gov/LandBoard/1998MinutesPDF/100198--final minutes Cottage Site SUBCOMMITTEE.pdf> [2 July 2008].

_____. 1998d. Minutes of Cottage Site Subcommittee November 23 meeting. <http://www.idl.idaho.gov/LandBoard/1998MinutesPDF/112398--final minutes Cottage Site SUBCOMMITTEE.pdf> [2 July 2008].

_____. 1998e. Memorandum regarding Land Board Cottage Site Subcommittee report for December15 meeting. Idaho Department of Lands, Boise. In authors' files.

_____. 2000. Memorandum regarding proposed new cottage site lease for December 12 meeting. Idaho Department of Lands, Boise. In authors' files.

_____. 2001a. Memorandum regarding State Board of Land Commissioners Sub-Committee report on proposed cottage site lease for February 13 meeting. Idaho Department of Lands, Boise. In authors' files.

_____. 2001b. Minutes of February 13 regular meeting. <http://www.idl.idaho.gov/LandBoard/2001MinutesPDF/021301FinalMinutes.pdf> [2 July 2008].

_____. 2006a. Minutes of February 14 regular meeting. <http://www.idl.idaho.gov/LandBoard/2006MinutesPDF/feb14_06finmin.pdf> [2 July 2008].

_____. 2006b. Minutes of September 12 regular meeting. <http://www.idl.idaho.gov/LandBoard/2006MinutesPDF/sep12_06finmin.pdf> [2 July 2008].

_____. 2007a. State Trust Lands Asset Management Plan <http://www.idl.idaho.gov/am/amfiles/final_AMP_Aprvd_ Dec2007.pdf> [7 May 2008].

_____. 2007b. Minutes from May 8 regular meeting. <http://www.idl.idaho.gov/LandBoard/2007MinutesPDF/may8_07finmin.pdf> [2 July 2008].

_____. 2007c. Minutes of July 10 regular meeting. <http://www.idl.idaho.gov/LandBoard/2007MinutesPDF/jul10_07finmin.pdf> [7 May 2008].

_____. 2007d. Minutes of November 15 regular meeting. <http://www.idl.idaho.gov/LandBoard/ 2007MinutesPDF/nov15_07finmin.pdf> [7 May 2008].

_____. 2007e. Minutes of December 4 special meeting. <http://www.idl.idaho.gov/LandBoard/2007MinutesPDF/dec4_07finmin.pdf> [7 May 2008].

_____. 2008. Transcript of April 22 Cottage Site Subcommittee meeting. In authors' files.

La Croix, S.J., J. Mak, and L.A. Rose. 1995. The political economy of urban land reform in Hawaii. *Urban Studies* 32:999-1015.

Maryland Department of Housing and Community Development. 2008. Ground rent redemption loan program. <http://www.dhcd.state.md.us/Website/programs/GRRLP/Documents/FAQNew.pdf> [27 May 2008].

Maryland's People Law Library. 2008. Understanding ground rent in Maryland. <http://www.peoples-law.org/housing/ltenant/legal info/ground rent leases.htm> [8 May 2008].

Montana Department of Natural Resources and Conservation. 2008. Trust land residential lots available for lease. <http://dnrc.mt.gov/cabinsite/default.asp> [26 June 2008].

NAREIT (National Association of Real Estate Investment Trusts). 2008. Chart book, April. <http://www.nareit.com/library/performance/CB0804.pdf> [16 July 2008].

NCREIF (National Council of Real Estate Investment Fiduciaries). 1991. Land valuation: guidelines for the determination of value for undeveloped land parcels. <http://www.ncreif.com/committees/pdf/Land_Valuation.pdf> [14 May 2008].

_____. 2008. Welcome to NCREIF. <http://www.ncreif.com> [18 July 2008].

Neil, B.A. 2006. Ground rents from Maryland to Hawaii: leasehold interests in residential real estate. *Real Estate Issues* 31(2):55-59.

O'Laughlin, J. 1990. Idaho's endowment lands: a matter of sacred trust. PAG Report No. 1. <http://www.cnrhome.uidaho.edu/default.aspx?pid=69432> [10 July 2008].

_____, and P.S. Cook. 2001. Endowment fund reform and Idaho's state lands: evaluating financial performance of forest and rangeland assets. PAG Report No. 21. <http://www.cnrhome.uidaho.edu/default.aspx?pid=69354> [20 June 2008].

Oregon Department of State Lands. 2006. Asset management plan. <http://www.oregon.gov/DSL/DO/docs/amp2006final.pdf> [2 May 2008].

Payette Lake Cabin Owners Association. 2008. Letters from lease holders. <https://www.idahostateleases.com/Letters_from_Lease_Holders.html> [1 July 2008].

_____ and Priest Lake State Lessee Association. 2008. Discussion regarding new lease, April 10. In authors' files.

Rattermann, M.R. 2007. *Valuation by Comparison: Residential Analysis and Logic.* Appraisal Institute: Chicago, IL. 115pp.

Rodgers, T. 1989. Valuation of a leased fee interest. *Appraisal Journal* 57:36-50.

Russell, B.Z. 2007a. State cottage site rents to be re-examined. "Eye on Boise" blog, posted September 13. <http://www.spokesmanreview.com/blogs/boise/archive.asp?mon=Sep2006> [2 July 2008].

_____. 2007b. Priest Lake site auction flops; state may revisit new lease rate. *Spokesman Review,* October 29. <http://www.spokesmanreview.com/tools/story_pf.asp?ID=217091> [2 July 2008].

_____. 2007c. No more state cabin site auctions - for now. "Eye on Boise" blog, posted November 16. <http://www.spokesmanreview.com/blogs/Boise/archive.asp?mon=Nov2007> [2 July 2008].

Sunderman, M.A., and R.W. Spahr. 2006. Management policy and estimated returns on school trust lands. *Journal of Real Estate Finance and Economics* 33:345-362.

_____, R.W. Spahr, and S. Runyan. 2004. A relationship of trust: are state "school trust lands" being prudently managed for the beneficiary? *Journal of Real Estate Research* 26:345-370.

USDA Forest Service. 2006. Forest Service Handbook, 2709.11 – Special Uses Handbook, Chapter 30 – Fee Determination. <http://www.fs.fed.us/im/directives/fsh/2709.11/2709.11_30.doc> [30 June 2008].

Vernor, J.D. 1988. Comparative lease analysis using a discounted cash flow approach. *Appraisal Journal* 56:391-398.

Wyoming Board of Land Commissioners. 2007. Rules and Regulations. <http://soswy.state.wy.us/RULES/6566.pdf> [6 May 2008].

Personal communication

Butler, Debbie. Recreation Special Uses Permit Administrator with U.S. Forest Service, Priest Lake Ranger District. 4 August 2008.

Higgins, Curt. Surface Management Specialist with Utah School and Institutional Trust Lands Administration. 25 June 2008.

Van Hatten, Jamie. Lands Management Supervisor with Wyoming Office of State Lands and Investments. 4 August 2008.

CABIN SITE SCENARIOS
2010 thru 2015

thod	RATE * 10 YEAR AVERAGE with 5 year phase in
e	4.0%
	Same % increase annually

ue Increase(Decrease)

	VALUE	10 Year Average
endar Year	2010	2002-2011
st Lake	152,995,367	98,391,109
ette Lake Waterfront	86,235,870	57,561,691
ette Lake 2nd Tier	12,662,202	8,666,265
TOTAL	251,893,440	164,619,065

RENT	2010 FROZEN	2011	2012	2013	2014	2015
st Lake	2,537,791	2,769,981	3,023,733	3,301,077	3,604,236	3,935,644
ette Lake Waterfront	1,552,582	1,679,621	1,817,205	1,966,220	2,127,626	2,302,468
ette Lake 2nd Tier	177,558	202,826	231,778	264,962	303,010	346,651
TOTAL	4,267,932	4,652,429	5,072,716	5,532,259	6,034,872	6,584,763

RENT % Increase(Decrease)	2010	2011	2012	2013	2014	2015
st Lake	0.0%	9.1%	9.2%	9.2%	9.2%	9.2%
ette Lake Waterfront	0.0%	8.2%	8.2%	8.2%	8.2%	8.2%
ette Lake 2nd Tier	0.0%	14.2%	14.3%	14.3%	14.4%	14.4%

Exhibit 26

John T. McFadden,

Appraisal Report: Project Report with Comparable Sales for Priest Lake Cottage Site Appraisals (1998).

APPRAISAL REPORT

PROJECT REPORT

WITH

COMPARABLE SALES

FOR

PRIEST LAKE COTTAGE SITE APPRAISALS

John T. McFaddin, MAI

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:36 P.01

PROJECT REPORT

for

APPRAISALS OF 15 COTTAGE SITES ON PRIEST LAKE

as of

June and July, 1998

prepared for

IDAHO DEPARTMENT OF LANDS
BOISE IDAHO

prepared by

John T. McFaddin, MAI
420 W. Dean Avenue
Spokane, WA 99201

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:36 P.02

John T. McFaddin, MAI
REAL ESTATE APPRAISALS • APPRAISAL REVIEWS
AGRICULTURAL • COMMERCIAL • INDUSTRIAL

420 W. DEAN AVENUE
SPOKANE, WA 99201-2223
TELEPHONE (509) 326-1855
FAX (509) 326-1986

August 12, 1998

Idaho Department of Lands
954 W. Jefferson Street
PO Box 83720
Boise, Idaho 83720-0050

Subject: Priest Lake Cottage Site Appraisals
Contract Req. #50-98

This project report is one of two reports completed in compliance with the contract referenced above. The project report contains 113 pages. It describes Priest Lake and its market for waterfront properties and presents the background and basis for the appraisals of 15 individual lots. The report contains 42 comparable sales and listings, analysis of the market data and general value conclusions. Analysis is presented for both market value and market rent. The individual value conclusions are summarized on page 1.

A separate report contains the 15 individual appraisals. Each property is described in that report and the market data from the project report is applied directly to each subject property. Both reports are needed to understand the analysis and conclusions.

Please feel free to call if you have any questions. This was a very interesting appraisal assignment. Thank you for the opportunity to be of service.

Respectfully submitted,

John T McFaddin

John T. McFaddin, MAI
Certified General Appraiser,
Idaho No. CGA-98

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:36 P.03

CONTENTS

Summary of Conclusions 1
Assumptions and Limiting Conditions 2
The Appraisal Problem 4
Rights Appraised 4
- Improvements 5
- Issues 5

Location Map 7
Area Data 8
Other Background Data 8
Utilities
- Electricity 9
- Telephone 10
- Water 10
- Sewer 10

Zoning and Land Use Regulations 11
Highest and Best Use 11
Assessed Values and Taxes 11
Scope of the Appraisals 11
Analysis of Deeded (fee) Comparables 13
- Time 14
- Size 14
- Water Depth 14
- Utilities 15
- Beach 16
- Access 17
- Other Improvements 17
- General Value Conclusions 17

Analysis of Leasehold Comparables 20
- Market Rent 21

Persons Contacted 26
Sales and Listings Considered and not Used 27
Comparable Sales Map 28
Comparable Sales 30
Appraiser Qualifications 113

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:36 P.04

SUMMARY OF CONCLUSIONS

No.	Location	Front Feet	$ / FF	Improved Market Value	Lessee Imps.	Unimproved Market Value	Market Rent
6	Outlet	330	$ 575	$190,000	$13,700	$176,300	$6,170
C	Sherwood Beach	87	2,075	180,525	14,700	166,000	5,810
4	Soldier Creek	150	1,850	277,500	11,700	265,800	9,300
24	Hess Point	195	1,750	341,250	13,700	327,550	11,465
50	Rocky Point	158	1,750	276,500	17,200	259,300	9,075
69	Cavanaugh Bay	143	2,000	286,000	15,200	270,800	9,480
94	Hunt Creek	157	1,800	282,600	15,700	266,900	9,340
137A	Eightmile	107	2,250	240,750	16,700	224,050	7,840
170	Horton Creek	153	1,750	267,750	17,200	250,550	8,770
200	Indian Creek Bay	148	2,100	310,800	15,200	295,600	10,350
214T	Pinto Point	100	2,000	200,000	16,200	183,800	6,435
251	Cape Horn	151	1,800	271,800	21,200	250,600	8,770
265F	Bear Creek	100	1,800	180,000	18,700	161,300	5,645
275	Huckleberry Bay	161	1,950	313,950	10,700	303,250	10,614
295	North End	114	1,400	160,000	9,700	150,300	5,260

ASSUMPTIONS AND LIMITING CONDITIONS

The properties are appraised as though under reasonable ownership and management.

It is assumed there are no violations of zoning codes, environmental laws or building codes existing in the properties.

Legal and engineering matters are not covered by the appraisals. It is assumed that title to the properties is good and marketable and that there are no liens, encumbrances or easements except as noted. It is also assumed there are no unapparent conditions of the properties which would make them more or less valuable than other comparable properties.

It is assumed the legal descriptions and land areas are essentially correct. Maps and sketches are based on apparent boundary locations.

Information, estimates and opinions obtained from others and used in the appraisals were obtained from sources considered to be reliable. No responsibility for their accuracy is assumed by the appraiser.

This report is to be used in its entirety. Extractions will render the appraisals invalid.

This report is confidential between appraiser and client. Disclosure of the contents of the report is governed by the Uniform Standards of Professional Appraisal Practice and by the Standards of Professional Appraisal Practice and the Code of Professional Ethics of the Appraisal Institute.

Value, if any, of mineral rights is included in this estimate of value. There is no known market evidence indicating that properties of this type have any measurable increment of value for the mineral rights. There is no known indication of mineral values on these properties and such a possibility would be speculative.

These appraisals are based on the assumption the properties are not affected by hazardous substances or environmental conditions. No such condition was apparent during the inspections and investigation. However, the appraiser is not qualified to test for hazardous substances. No responsibility is assumed for any such conditions on the properties or in such proximity as would cause a loss in value.

Possession of this report, or a copy thereof, does not carry with it the right of publication.

Neither all nor any part of the contents of this report shall be disseminated to the public through advertising, public relations, news, sales or other media without the prior written consent of the appraiser.

Testimony or attendance in court is not required by reason of this appraisal.

ID ATTNYGEN NAIRL RES. Fax:208-334-2690 JUL 11 2001 9:57 P.06

It is assumed all of the subject lots have legal access rights unless it is specifically noted that access is by boat only. Although some of the lots do not front on public roads, access is by roads, lanes and individual driveways which reportedly cross other state land. The appraisals assume the rights of access are included with the lots and are perpetual.

Many lots are served by community-type sewage disposal systems. The lines, lagoons, drainfields and other improvements may occupy state land beyond the limits of the leased sites. It is assumed the right to use this land is assured perpetually without additional cost. These improvements are not included in the appraisals but it is assumed the lessees have the right to place them on state land.

Some lots are served by community-type water systems. The wells, tanks, lines and other improvements for these systems may occupy state land beyond the limits of the leased sites. It is assumed the right to use this land is assured perpetually without additional cost. These improvements are not included in the appraisals but it is assumed the lessees have the right to place them on state land.

The subject lots, although generally surveyed, are not in plats recorded in Bonner County. Their legal status as being adequate to support actual transactions is the subject of some controversy. Market value is estimated in this appraisal, not for the purpose of sales of the properties, but as a step in estimating market rent. Actual sales of the lots are not intended. Therefore, it is an assumption that the subject lots are as marketable as if they were officially platted and that no discount is appropriate for the costs and uncertainty associated with platting.

THE APPRAISAL PROBLEM

The purpose of the appraisals is to estimate market value and market rent for each of 15 recreational cottage lots on Priest Lake.

Market value is defined as the most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated;
2. Both parties are well informed or well advised, and acting in what they consider their own best interests;
3. A reasonable time is allowed for exposure in the open market;
4. Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and
5. The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

Market rent is defined as the rental income that a property would most probably command in the open market.

The 15 lots have been selected as being representative of various locations and various lot characteristics. They are intended to be a representative sample of the 355 lots on Priest Lake which are managed by the Idaho Department of Lands. The appraisals are to serve as a guide in establishing future rent rates for all of the state lots on the lake.

RIGHTS APPRAISED

The estimates of market value will assume the lots are sold in fee simple interest. They will be appraised as though vacant and available for development to their highest and best use. Limitations imposed by state leases will be disregarded. It is assumed access easements will be provided across other state land as necessary to provide the present level of vehicular access.

It was pointed out by an appraiser/attorney representing the lessees that the subject lots are not contained in recorded plats and that this could negatively affect property rights, market value or the marketability of the lots. The appraisals of market value are intended to help provide a basis for estimating market rent. It is not intended that the lots are actually to be sold. The lots have served to support building permits for many years. Leasehold interests, including cabins, are routinely transferred from one owner to another. It is not sensible that the market value estimates be reduced artificially to reflect a possible title problem when the reason for the appraisals is to set rent, and titles will not be transferred. Therefore, it is assumed that the subject lots are as marketable as if they were officially platted and that no discount is appropriate for the costs or uncertainty associated with platting.

JU HUNTGEN MHIKL KES. FAX:208-334-2690 JUL 11 2001 9:57 P.08

The estimates of market rent will consider the limitations imposed by the state leases. Most of the lease provisions are typical of lease terms in general or of restrictions otherwise imposed in the market place. The limitation of one dwelling per site is consistent with county zoning and does not impose any additional limitation. The same is true of building setbacks. A limitation on landscaping and the removal of vegetation provides for aesthetic protection which benefits all. It is not unlike deed restrictions which apply in the newest developments on the lake, Huckleberry Bay at Priest Lake. Building setbacks are established (more severe than zoning) and the removal of vegetation is severely limited (80 percent must be left) in the Huckleberry Bay developments. Boathouses are prohibited. Lots cannot be divided. A design committee must approve building plans at Huckleberry Bay. The limitations in the state leases are typical of the market in general and do not represent unusual restrictions on use or value.

The state leases do limit ownership to individual families (no partnerships, corporations) and do not allow mortgages.

IMPROVEMENTS

The appraisals of both market value and market rent will view the lots as unimproved. Improvements provided by present or past lessees will be excluded. These excluded improvements comprise not only buildings and docks, but also utilities, driveways and site work provided by the tenants. Every improvement constructed by or paid by the lessee or lessee's predecessors is treated as owned by the lessee and excluded from valuation.

ISSUES

News articles, public meetings and appraiser contacts with individual lessees raised a number of issues. Some were described as being appraisal issues. One of these pertained to affordability. It often was stated that lessees will not be able to afford rent increases. This is not an appraisal issue. The appraisals will consider affordability only from the standpoint of the overall market; not from the standpoint of lessees, individually or collectively.

Another issue was comparability. Some stated that leased lots cannot be compared with deeded lots. Others stated they cannot be compared with specific locations on the lake. The estimates of market value assume, by definition, the lots will be sold. They must be compared with sales of fee-owned lots. Differences in physical characteristics and in property rights will be considered in the analysis. Full consideration will be given to sales of both fee and leasehold interests in the overall analyses of market value and market rent. Sales of permits on Forest Service land have been considered but not relied upon. These permits do not convey exclusive use of the sites and are not considered very comparable. Adequate data exists to reach supported conclusions without sales of permits.

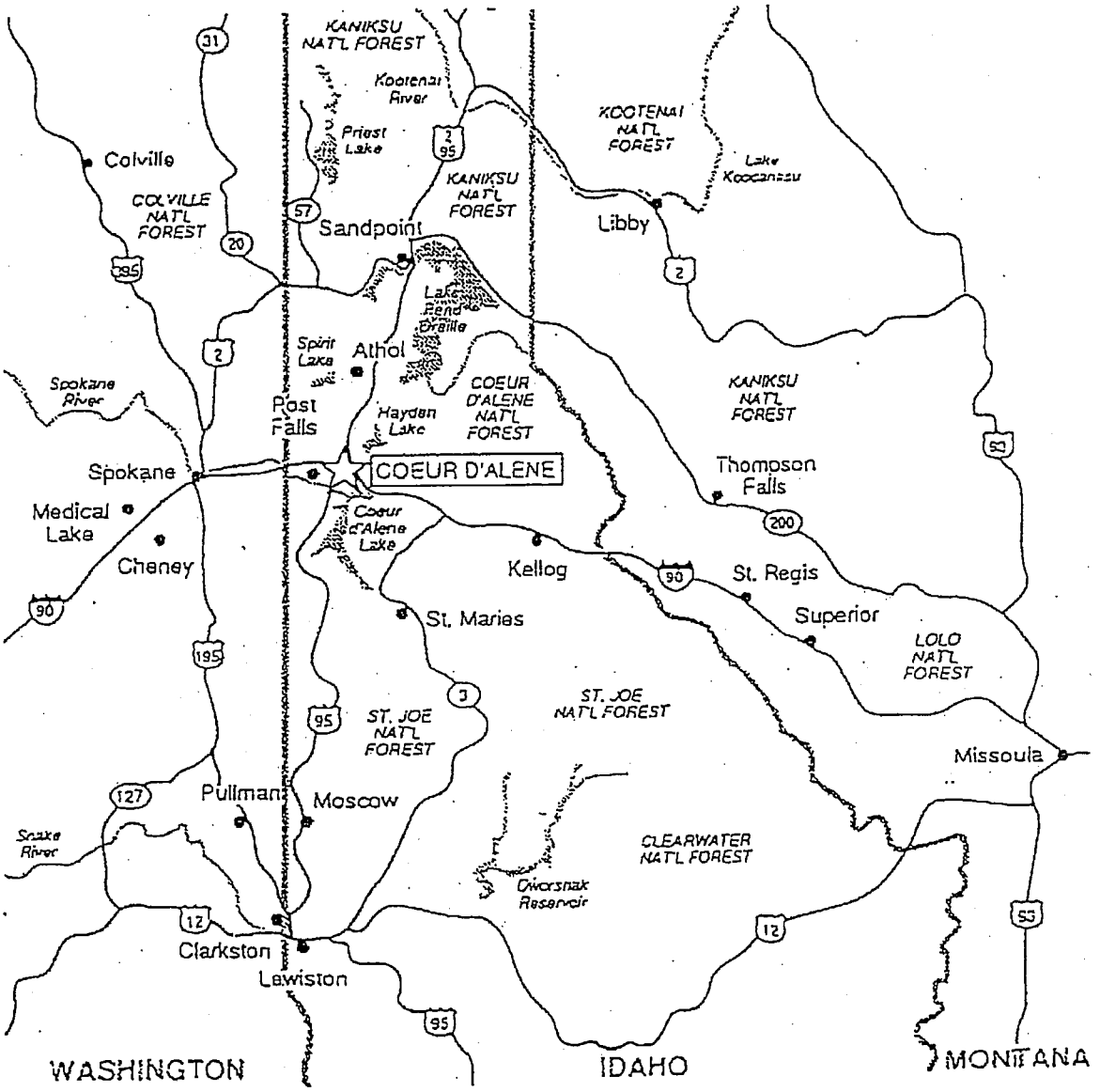
Another common concern was the possibility that the value of improvements made by lessees (utilities, lot and beach clearing, access) will be included in the appraisals. As noted elsewhere, these improvements are not included in the valuations.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:38 P.09

Some have expressed the opinion it is necessary to separate values into leased fee and leasehold interests and make allocations for all lessee improvements. This will not be done. The lots to be appraised function as recreation residence sites. The ultimate purpose is to estimate market rent for this function. Tenant improvements will be entirely excluded from the valuation analysis. Although there may be some legal reasons or technical appraisal reasons for a detailed breakdown of the property interests if the value estimates were to serve as a basis for sales of the leased fee interests, there is no reason for this kind of complication in the present situation.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:58 P.10

LOCATION MAP



ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:38 P.11

AREA DATA

Priest Lake is a pristine natural lake in the northern panhandle of Idaho, 60 miles north of Coeur d'Alene. It is in Bonner County, with the county seat of Sandpoint being 20 airline miles to the southeast. The lake is served by Highway 57 and is a 25-mile drive north from Priest River.

Priest Lake is 19 miles long (north/south) and up to almost five miles wide. A two-mile-long thoroughfare at the north end connects to Upper Priest Lake which is another 3+ miles long. The thoroughfare allows boat access to the upper lake, which is not served by roads. The main lake has about 56 miles of shoreline, not counting the seven islands. Islands add perhaps another nine miles of frontage.

The lake is in a timbered area of varied topography. Pool elevation is 2,438 feet. Elevations increase to 3,000 to 4,000 feet within two miles of the shore on the west side. On the east side the mountains are steeper, climbing to 5,500 feet within two miles of the lake. Elevations reach 7,200 feet along the scenic Selkirk Crest, six to eight miles to the east.

Most of the shoreline is in public ownership, with U.S. Forest Service land on the west side and State of Idaho land on the east side. Both of these public owners have developed cabin sites for lease to individuals and nearly all of them (nearly 500) are improved with cabins. The layout of the lots and the limitations applied to their improvement has served to minimize their impact on the environment. The cabins tend to be farther apart than on privately-owned lots and many of the cabins sit back in the trees. It is estimated that about 25 percent of the shoreline is privately owned. About 45 percent of the frontage is not developed with any cabins. Assessor's records indicate there are 676 deeded lots on the lake, of which 509 are improved with houses or cabins. The total number of deeded, leased and permit lots is 1,169 according to these records.

Marinas, restaurants and other public services exist at ten locations, all on the southern two-thirds of the main lake. Most of these are on the west side. Eight state and federal campgrounds provide more than 300 sites on the main lake. They are located on both sides, with the Forest Service campgrounds on the west and Idaho campgrounds on the east. About 76 boat-access sites are also provided on Forest Service land on the two largest islands, on the upper lake and at isolated locations near the north end of Priest lake.

OTHER BACKGROUND DATA

The Idaho Department of Lands has leased cottage sites on Priest Lake for many years. The families of some tenants reportedly have occupied their sites for more than 70 years. Historically, the rents were relatively low, but have increased as the value of lake property increased. This situation is not unique to the east side of Priest Lake. The Land Board is also responsible for 240 sites on Payette Lake near McCall. The U.S. Forest Service has 140 cabin sites on permits on the west side of Priest Lake. The Idaho Parks and Recreation Department has 170 leased residence and recreation sites in Heyburn State Park at the south end of Coeur d'Alene Lake. All of these locations have been involved in some controversy over the years as the managing government agencies and the individual lessees and permittees have disagreed over the

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:38 P.12

proper rent levels. The agencies have contracted for appraisals and have discussed the proper rates of return. The Land Board agreed to a 2½ percent rate in 1992. This represented a significant increase over actual rent. The Park Board decided preliminarily in 1997 to charge 4½ percent of market value. The Forest Service has used a figure of 5 percent but failed to keep up with increasing values. Last year the General Accounting Office criticized the Forest Service for not charging market rent. Discussions of lease and permit rates over the years have become political and emotional. Rent increases have tended to lag well behind the upward trends in the market.

The Land Board recognized that below-market rents were resulting in significant leasehold values. It adopted a policy in 1981 of charging a premium rental when leasehold interests were sold. The amount is ten percent of leasehold value, sale price less the value of tenant improvements and personal property. Leasehold prices on Priest Lake averaged about $96,000 in 1995.

A study of a similar situation in Montana pointed out that lessees benefit doubly. They benefit over the years from rent levels that are below the market. Then they benefit again when they sell the leasehold interest. The price paid for the leasehold reflects the perception of buyers that rents will remain low in the future.

The state Land Board is required to manage the lots for the maximum long-term benefit of the school endowment fund. The Board is to insure that market rent be charged. This appraisal is to research the market, analyze the data and reach conclusions of market value and market rent for each of the sample 15 lots. These conclusions can then be used as benchmarks by the department in establishing uniform rents for all lots.

The estimates of market value will be based on assumed sales of fee simple title. These value conclusions will reflect the full potential of the sites, exclusive of tenant improvements. The estimates of market rent will consider the specific terms of the state leases.

UTILITIES

ELECTRICITY

Electricity is provided around the lake by Northern Lights, Inc. from Sandpoint. The cost of extending power lines to individual cabins is set each year based on past experience. Cabin owners are charged for new line extensions. The present charge is $6.75 per foot for the first 300 feet and $3.75 per foot for additional length. This charge applies to distribution lines and the individual service lines, whether overhead or underground. For a lot with 150 feet of frontage along a proposed power line and a meter location 100 feet from the line, the current cost of providing the electric service would be 250 feet at $6.75 per foot or $1,688. Charges in previous years have varied but have trended upward. The cost 20 to 30 years ago was near $0.50 per foot and the power company waived charges for the first $1,700. Therefore, cabins developed with electricity before 1975 generally paid nothing. A line would be extended a distance of 3400 feet (0.64 mile) at no cost to the lot owner or lessee. All of the subject lots are presently served with electricity. Electricity is available to all of the comparables.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul.11 2001 9:39 P.13

TELEPHONE

Telephone service is from GTE. Telephone service is available to all subject parcels and comparables. Generally, phone lines are installed by the phone company at no charge to the owners. Exceptions apply when the distance is great and only one house is served. One lessee in Outlet Bay told me the phone company installed the lines to cabins there but the lessees paid for the trenching. Currently, the telephone company absorbs the first $3,000 in construction charges and the customer pays all additional charges. Twenty years ago the arrangement was different. The first 660 feet of a line extension was free and the customer paid for additional distance. The charges that applied to any individual lot would depend on the number of connections made at the time. If a line was extended past other cabins to serve only one, a charge would be likely. If all cabins connected at the same time, a charge would be very unlikely. Generally, the costs for connections in the intensive development of the subject lots will be fully absorbed by GTE.

WATER

Domestic water systems vary greatly around the lake. Many of the cabins draw water from the lake, with individual pumps and pressure systems. This practice has become less common in recent years as water quality problems such as Giardia and the awareness of the importance of water quality has increased. The Health District now recommends the use of filters and chlorinating systems when lake systems are used. Some owners pipe water down to their cabins from streams and springs. Some have their own wells. Two or three neighbors sometimes share in the development and maintenance of these small systems. Others on the lake have joined together to establish community water systems. The Cougar Creek Water Association on Cavanaugh Bay was developed by owners and lessees with a well on private property. This small community system serves a population of 250 people and has 70 connections.

SEWER

Individual sewage disposal also varies around the lake. Many cabins still have individual septic tanks with drainfields. However, the trend has been to establish community systems. The community systems include small systems with common drainfields on secondary sites and larger ones with lagoons. Sewer districts exist at Outlet Bay, Kalispell Bay, Coolin, Pinto Point, and Huckleberry Bay. Estimates from the state Division of Environmental Quality place current costs for these kinds of systems in the range of $5,000 to $7,000 per unit, depending on the complexity and size of the system. The Coolin sewer district has 450 to 500 connections which extend from Coolin to Cougar Creek on the east side of Cavanaugh Bay. Individual cabins have tanks and pumps. Pressure mains go to a lagoon on a hill near the center of Section 34. The present day cost to connect is typically about $5,000. This includes tank, pump, valves, pipes and hook-up. The maintenance fee is $20 per month.

Health District approval is needed for individual septic tank systems. Standards address soil, slope and distance from the lake. These systems must now be at least 300 feet from the lake. This standard essentially eliminates the use of on-site systems for most lots. To overcome this problem on state lots it has been common for the state to allow individual and community septic tanks and drainfields to be placed beyond the lots on other state land. It is assumed this practice will continue.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:39 P.14

ZONING AND LAND USE REGULATIONS

Bonner County zoning around the lake is predominately "Rural District" on cabin sites. The minimum lot size is five acres. Most lots on the lake were created before this standard applied. As legal, non conforming lots, the residential uses may be continued but the lots may not be reduced in size and may not be used for more than one residential unit. Other smaller lots on the lake were created in recent years as part of planned unit developments or other arrangements where smaller lots were permitted when common open space was provided in the development.

Minimum setbacks are 40 feet from the lake, 25 feet for both front and rear yards and five feet for side yards.

HIGHEST AND BEST USE

As with any property, the Subject lots will be appraised for their highest and best use which is defined as the most profitable, likely use to which a property may be put or that use which maximizes value. There are four criteria which highest and best use must meet. They are legal permissibility, physical possibility, financial feasibility and maximum profitability. Each lot was intended for a single residence. Zoning will limit use to single residences on each lot. A strong demand exists for this use and any other use would be speculative. The highest and best use for each subject property is the present use, as a seasonal, recreation-oriented residence site.

ASSESSED VALUES AND TAXES

Properties are assessed for taxes by the Bonner County Assessor's office. Priest Lake is divided into three geographic areas for the assessment of fee-owned properties. One appraiser is assigned to each area. A fourth appraiser is responsible for buildings on leased sites. Three independent ratio studies were recently completed to test the reliability of the assessed values. It was concluded from these studies that the current level of assessed values for land is very accurate and assessed values for buildings are perhaps five percent below market levels. According to the Assessor's office, annual taxes are essentially one percent of market value except when they are reduced by a homeowners exemption.

State lease lots and USFS permit lots are not assessed or taxed. There is no county leasehold tax that applies to these lots either.

SCOPE OF THE APPRAISALS

The search for market data included research at county offices, contacts with Realtors and other appraisers, examination of information from the local Multiple Listing Service and contacts with

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:40 P.15

individual owners, buyers and sellers. The market data includes comparable sales of vacant and improved lakefront lots, current listings of lots and rent arrangements. Both deeded (fee) and lease lots were included in the analysis. Essentially all of the developed frontage on Priest Lake was viewed both by boat and car to identify and view the sales and listings. More than 100 listings and sales were investigated. Some were discarded because the improvements were too great to provide reliable residual value indications for the sites. Sales prior to 1996 were eventually discarded because we had adequate data from the past 2½ years. The sales extend from the south end of the lake almost to the north end. Although they involve properties on both sides of the lake, most are on the east side, where subject properties are located.

JD HILINYGEN NHIKL KES. FAX:208-534-2690 JUL 11 2001 9:40 P.16

reliable. Sale 19, with a leasehold price of $68,197 or $404 per front foot, was a steep, rocky lot with the building site far above the lake level. Sale 6, at $80,000 and $520 involved a moderately steep lot and essentially undeveloped beach. Sale 63, at $105,500 and $699 per front foot was for a nearly level site in a protected location, with essentially undeveloped beach.

Two other leasehold sales occurred on July 22, 1993 when the state auctioned the leasehold interests in vacant Lots 279 and 280 on the north side of Huckleberry Bay. These leasehold interests sold for $87,000 and $76,000, respectively. Eleven individuals were bidding on the two lots. On a front-foot basis, Lot 279 sold for $557 and Lot 28 sold for $505. These are close to the mean prices for the recent sales. At the time of the auction, these lots were advertised as having minimum annual rents of $4,490 (Lot 279) and $4,326 (Lot 280). The buyers also paid $2,000 each for advertising. The lots had developed gravel road access and access to the Huckleberry Bay sewer system, but no water.

MARKET RENT

Part of the appraisal problem is to estimate market rent for each subject lot. One method of estimating market rent is to apply a rate of return to market value. It is not uncommon in investment-type real estate for the relationship between net income (or rent) and market value to be near ten percent. Historically, the rate has never been much below six percent. Rates vary primarily with risk. As the risk increases, so does the required rate of return. Related to risk, rates of return vary with expected value appreciation. Expectations for value appreciation tend to reduce the annual rate of return because additional return is expected in the form of increased value. Recreation properties are not typically viewed as investments because income is not the motive of the typical owner. However, some of the same factors will still apply in our analysis. The rate of return will tend to be lower than for many investment properties because of the expectation for appreciation. Values have trended upward strongly for prime lakefront properties and there is every reason to expect this trend will continue.

An active market does not exist where recreation properties are bought and sold as investments. Vacant recreation properties are seldom leased, especially on a long-term basis. Therefore, few comparables are available for use in estimating market rent. Additionally, the Northwest is unique in the country because there is so much public land available for recreation uses. Also, Priest Lake is unique in the Inland Northwest because of its pristine nature and large size. Market rent can better be estimated by using the data available directly from Priest Lake than by looking for "comparables" in other areas.

Nevertheless, other nearby areas were explored for rent-to-value relationships from properties with similar investment and use characteristics. Seasonal cabin sites are leased on Camp Bay on Lake Pend Orielle. Mrs. Green and her family started leasing lakefront sites for summer cabin use there in 1954. The lake frontage is part of the original family homestead. She has 17 lots. Fourteen of these have 50 feet of frontage each. They are 100 to 200 feet deep and have a graveled road between the cabins and the docks. Two lots have 100 feet of poorer quality lake frontage and one has 450 feet. The owner pays real estate taxes on the land, so the rent basis to the cabin owners is similar to the state-owned lots on Priest Lake. No water or sewer facilities are provided; each tenant develops his own. The beach is rocky. Telephone and electric services

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:55 P.17

are available. Some lessees have occupied their lots for more than 40 years. In 1972, lot rents at Camp Bay typically were about $350 per year and were considered by the owner to return 7 percent of value. Prior to 1994, the 50-foot lots had been rented for $1,200 to $1,400 per year. In 1994 one lot was appraised by a Sandpoint appraiser and the owner used the appraisal as the basis for setting new rents. The appraisal concluded a value of $55,000 after making deductions for the lack of water and sewer service. The appraiser suggested rent of $2,200 (4 percent of $55,000) and the rent was actually increased only to $2,000. or about 3.6 percent. This value is significantly lower than the present market values for the subject lots. Please see photo of Camp Bay on the facing page.

The U.S. Forest Service leases recreation sites at various locations, including Priest Lake. Their stated policy is to obtain a return of 5 percent. Since values used in the calculation will tend to lag the market, this stated rate will often be higher than the rate actually charged permittees.

A 1993 study of 618 recreation sites in Montana (state land) stated that leases are based on a 3.5 percent annual return. Market value there was increasing at an estimated 8 percent per year and rents were adjusted every five years. This caused a significant lag. The study looked at leasehold prices and concluded the lease rates should be 6 to 6.5 percent of market value.

An earlier study of more than 1,500 state-owned lots in Minnesota identified the same tendency. Rents started at a rate of 5 percent but rents were not adjusted to keep up with increasing market values. A critical review of this program by the University of Minnesota concluded "The ten year gap in the appraisal of lots has resulted in subsidies to lessees and an income loss to the state." Annual indexing of rents was found to be imperative.

Rental rates for state lots on Priest Lake have not kept up with increases in value for properties on the lake. This is clearly reflected in the prices paid for leasehold interests. When the actual contract rent for lots is equal to market rent, the values (prices) of leasehold interests will be zero. When leasehold values are positive, actual rents are below market rents, by definition. After deductions are made for leasehold improvements such as utilities, access and beach improvements, the current market clearly shows positive leasehold values. One way to estimate market rents or market rates of return is to adjust actual rents upward in proportion to the ratio of leasehold price to market value. In theory, this will bring rents to the level where leasehold value will be zero. A very important strength of this type of analysis is that the data is obtained directly from the actual Priest Lake market for state-leased lots.

Two recent leasehold sales on the lake involved minor lessee improvements, so they are most reliable for this kind of analysis. Sale 6 occurred in June, 1998. Lot No. 177, with 154 feet of frontage, was marketed by a Realtor and sold for $80,000. The dock was in very poor condition and will involve some additional disposal cost. The cabin was of poor quality and condition and had numerous fallen trees on the roof at the time of sale. The buyer intended only interim use of the cabin and planned to replace it within two years. At the time of sale, there was some risk that the cabin would be damaged as trees were removed. Windfall was extensive on the lot, so cleanup costs were significant. A cost of $1,500 would be a reasonable estimate for cleanup and dock disposal costs. The beach was essentially undeveloped. It is believed that any interim use of the cabin will be offset by cleanup and disposal costs, so the property was effectively vacant

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:56 P.18

and undeveloped. The value of this lot will be near $1,750 per front foot or $270,000. The lot rent is now $3,343 per year. The leasehold price was $80,000, so the difference between fee value and leasehold price was $190,000, or 70.4 percent of market value. This indicates a rate of return of $3,343 / $190,000 = 1.8 percent. If the rent were adjusted upward to $4,751 ($3,343 / 0.704), the return would be $4,751 / $270,000 or 1.76 percent.

Sale 63 was the November, 1997 purchase of Lot 131, with 151 feet of lake frontage just east of Eightmile Island. Realtors were involved on both sides of the transaction. A cabin was present, but was removed by the purchasers, who are building a new cabin. A surface water system was present, but was replaced with a well by the buyers. The dock was poor. A new three-car garage, a new septic system and a boat lift were the only improvements contributing to value. The beach was essentially undeveloped. Allowing reasonable values for the limited improvements and adding a small amount to cover the demolition of the cabin, the net price for the leasehold interest was $105,500. Land rent was $2,959. A reasonable market value for this lot would be about $290,000. Applying the same relationships from the previous comparable, this transaction suggests market rent of $2,959 / 0.64 = $4,651. This suggests a rate of return of about 1.6 percent.

Similar calculations were made for each of the 16 sales and listings of leasehold interests. The indicated rates ranged from one percent to three percent and averaged 2.12 percent

Another view is to consider the opportunity cost of the amount paid for a leasehold interest. The $90,692 average leasehold price from the comparables can indicate an annual opportunity cost. At a typical contract interest rate of 8 percent applied to the leasehold is $7,255 per year. When this is added to the average rent of $3,386 per year on a $255,000 average lot, the total cost is $10,641, or 4.23 percent of the lot value. This type of analysis was also completed for each of the 16 comparable sales and listings involving leasehold interests. The resulting rates ranged from 2.3 percent to 5.2 percent and averaged 4.23 percent. Both calculations are shown in the following chart.

1	2	3	4	5	6	7	8	9	10	11	12	13
Sale No.	Front Feet	Market Value	Leasehold Price	Difference (3) - (4)	Percent (5) / (3)	Contract Rent	Rate (%) (7) / (5)	Mkt. Rent (7) / (6)	Rate (%) (9) / (3)	(4) x 8%	Mkt. Rent (11) + (7)	Rate (%) (12) / (3)
2	150	$310,000	$58,800	$251,200	81.03	$2,388	0.95	$2,948	0.95	$4,704	$7,093	2.29
3	253	350,000	100,000	250,000	71.43	6,641	2.66	9,297	2.66	8 000	14,641	4.18
4	152	275,000	103,500	171,500	62.36	4,056	2.37	6,504	2.37	8,280	12,336	4.49
5	163	290,000	105,000	185,000	63.79	4,094	2.21	5,418	2.21	8,400	12,494	4.31
6	154	270,000	80,000	190,000	70.37	3,343	1.76	4,751	1.76	6,400	8,743	3.61
7	150	260,000	112,750	147,250	56.63	3,298	2.24	5,823	2.24	9,020	12,316	4.74
11	139	265,000	78,700	186,300	70.30	3,031	1.63	4,311	1.63	6,296	9,327	3.52
19	169	160,000	68,197	91,803	57.38	2,746	2.99	4 786	2.99	5,456	8,202	5.13
30	100	210,000	81,530	128,470	61.18	2,750	2.14	4,495	2 14	6,522	9 272	4.42
51	107	215,000	98,500	116,500	54.18	2,540	2.18	4,688	2.18	7,880	10,420	4.85
52	330	200,000	60,000	140,000	70.00	3 094	2.21	4 420	2.21	4,800	7,894	3.95
61	101	200,000	64,175	135,825	67 91	2,139	1.57	3,150	1.57	5,134	7,273	3.64
62	87	180,500	84,925	95,575	52.95	2 228	2.33	4,206	2.33	6,794	9,022	5 00
63	151	290,000	105,500	184,500	63.62	2,959	1.60	4,651	1.60	8,440	11,399	3 93
66	149	300,000	135,000	165,000	55.00	4,875	2.95	8,864	2.95	10,800	15 675	5.23
77	169	300,000	114,500	185,500	61.83	3,990	2.15	6,453	2.15	9,160	13,150	4.38
AVERAGES		$254,719	$90,692	$164,026	64	$3,366	2.12	$5,360	2.12	$7,255	$10,641	4.23

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:56 P.19

Indications of the rate of return vary greatly, from 1.5 percent to more than six percent. The analysis of actual leasehold sales on Priest Lake indicate two percent and four percent. The Lake Pend Oreille comparables indicate 3.6 percent. The studies in Montana and Minnesota indicate it is essential that rents be adjusted annually to track with changes in market value. Our analysis of current data on Priest Lake ratifies this finding.

In a market that is appreciating in value at 8 percent per year (Montana study), a target rent of five percent is reduced to 3.4 percent of market value in five years and 2.3 percent in ten years.

Priest Lake has a high potential and expectation for value appreciation. This is caused by the high quality, high demand and scarcity of the lots. The average price from the 20 sales of fee lots in this study was about $2,350 per front foot. A similar study conducted in 1977 showed an average price of $424 per front foot from nine sales of lake-front lots. This reflects an 8.5 percent average annual compound rate of increase over the 21-year period. A 100-foot lot on Warren Beach sold in 1977 for $600 per front foot. This was one of the highest prices on the lake at that time. Today a nearby lot is listed (Comparable 10) for $3,000 per front foot. This reflects an eight percent rate of appreciation. Three lots just north of Coolin sold in 1975, 1976 and 1977 for $400, $458 and $467 per front foot. Sales 32 and 16 are in the same area and sold in 1996 at front-foot prices of $2,400 and $2,500 and an adjacent lot is now listed at $3,000 per front foot. These comparisons suggest appreciation rates of near 9 percent per year. Two lots with rocky beaches in the Diamond Park area sold in 1976 and 1977 at $240 and $347 per front foot. Comparable 22 in Diamond Park, with better beach, sold in 1996 for $1,843 per front foot. Again, an annual appreciation rate of near nine percent is indicated.

During the same 21-year period, the consumer price index increased at an average annual rate of about five percent. Priest Lake lots have produced an average annual earnings rate from appreciation alone that is about four percentage points higher than non appreciating investments (in terms of purchasing power).

The two main benefits of an investment in a lake lot are use and appreciation in value. Clearly, appreciation has been very important on Priest Lake over the past twenty years. This is a benefit to the owner of a deeded lot but not to a lessee. A significant difference between the use (rent) return and the overall (use and appreciation) return is not unreasonable.

The comparables on Camp Bay on Lake Pend Oreille indicate a rate of return of 3.6 percent. Comparison with Forest Service policy indicates the rate will be less than 5 percent. The calculations from actual leasehold sales with known land rents and estimated fee values suggests a rate of 2.1 percent would reduce leasehold values to zero. Another comparison from the same comparables, using an opportunity cost on the leasehold price, suggests a rate of 4.2 percent would be appropriate. It is concluded the market rate of return is in the range of 3 to 4 percent. A concluded rate of 3.5 percent will be applied to subject value conclusions. When value appreciation is added, a total rate of return near 12 percent can be expected, based on past trends.

It is emphasized that some form of annual indexing is essential. If rents are to remain at a stable level for a period of even five years, the initial rent will need to be increased substantially for the 3.5 percent rate to be maintained.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:57 P.20

The absence of an active rental market for lots on Priest Lake causes a relatively wide range in indications for the rate of return. This situation will warrant close monitoring as rents are adjusted. Rent increases should cause leasehold prices to decline. When the market level is reached for rents, true leasehold values should be zero and the market for cabins should remain active.

ID ATTNYGEN NATRL RES. Fax:208-334-2690 Jul 11 2001 9:57 P.21

Exhibit 27

Bradford T. Knipe,

Complete Appraisal, Self Contained Report and Market Analysis of 14 Payette Lake Cabin Sites (1998).

DEPT. OF LANDS
98 AUG 31 PM 3:27
BOISE, IDAHO

©1993-1998, All Rights Reserved.
Do Not Copy or Distribute without Express Permission from
KNIPE & KNIPE, INC.

Complete Appraisal, Self-Contained Report and Market Rent Analysis of

14 PAYETTE LAKE CABIN SITES

Requisition No. 100-98
McCall, Valley County, Idaho
K&K File ID 98.886

Client:

Mr. Bryce Taylor, Chief
Mr. Alvin Carr, Leasing Specialist
Bureau of Range Management & Surface Leasing
State of Idaho
Department of Lands
954 W. Jefferson
Boise, Idaho 83720

Client's Log Nos:
Requisition 100-98

Date of Report:
August 26, 1998

Date of "As Is" Value:
August 18, 1998

Appraiser:
Bradford T. Knipe, MAI, CCIM
Idaho Certified General Appraiser No. 117
Montana Certified General Appraiser No. 494

KNIPE & KNIPE
INCORPORATED

Commercial
Real Estate Services

LOCATED IN RIVER RUN CENTER
600 E. Riverpark Lane • Suite 210
Boise, Idaho 83706

MAILING ADDRESS
P.O. Box 1696 • Boise, Idaho 83701

TELEPHONE / FACSIMILE
208-342-2500 / 208-342-2220

INTERNET
http://www.knipe.com

APPRAISAL SPECIALIZATION
Office • Retail • Industrial
Special-Purpose
Subdivisions • Bare Land
Appraisal Review
Business Valuation
Eminent Domain
& Litigation Valuation

RELATED SERVICES
Brokerage
Consulting
Development Services
Expert Witness Testimony
Feasibility Studies
Market Analyses
Right-of-Way Acquisition
& Publication of Market Trends

TREY KNIPE, MAI
BRADFORD KNIPE, MAI, CCIM

JOHN R. DILLMAN, MAI
WALETA M. NOVAK
JAMES W. THOMASON
PATRICK THOMASON

JOSEPH O. SWENSON, CPA
Of Counsel, Business Valuations

DONALD S. REED, ARA (RET.)
Of Counsel, Agricultural Properties

CERTIFIED GENERAL APPRAISERS
Idaho, Oregon, Montana & Nevada

INDIVIDUAL MEMBERS
Appraisal Institute
Commercial Investment R. E. Institute
Southwestern Idaho Regional MLS
Ada County Association of Realtors®
National Association of Realtors®
International Right-of-Way Association
BOMA of Idaho's Treasure Valley
Urban Land Institute

DEPT. OF LANDS
98 AUG 31 PM 3:27
BOISE, IDAHO

August 26, 1998

Mr. Alvin Carr, Leasing Specialist
Mr. Bryce Taylor, Bureau Chief
Bureau of Range Management & Surface Leasing
State of Idaho Department of Lands
954 W. Jefferson Street
Boise, Idaho 83720

Dear Gentlemen:

In accordance with your request, I have conducted market investigations, gathered pertinent data, and performed analyses necessary for an appraisal of the following property, under the following valuation scenarios and assumptions:

IDENTIFICATION OR PROPERTY, FILE REFERENCES, AND CONTACTS		Phone Numbers
IDENTIFICATION:		
Name of Property, Occupant or Project:	14 State Lease Cottage Sites	
Location:	Fronting on or Located Near Payette Lake, McCall, Valley County, Idaho	
Property Type:	Lakefront (7) and Lake Access (7) Recreational Residential Lots	
Status:	12 Improved with homes / cabins 2 Unimproved	
REFERENCE NOS:		
Client's Log #: K&K, INC. File ID:	Requisition 100-98 98.886	
CONTACTS:		
Owner/Client:	Idaho Department of Lands	
Borrower Contact:	NA	NA
Client Contact:	Alvin Carr	208/334-0229

KNIPE & KNIPE
INCORPORATED

Commercial
Real Estate Services

LOCATED IN RIVER RUN CENTER
600 E. Riverpark Lane • Suite 210
Boise, Idaho 83706

MAILING ADDRESS
P.O. Box 1696 • Boise, Idaho 83701

TELEPHONE / FACSIMILE
208-342-2500 / 208-342-2220

INTERNET
http://www.knipe.com

APPRAISAL SPECIALIZATION
Office • Retail • Industrial
Special-Purpose
Subdivisions & Acreage
Appraisal Review
Eminent Domain / Right-of-Way
& Litigation Valuation

RELATED SERVICES
Brokerage
Consulting
Business Valuation
Expert Witness Testimony
Feasibility Studies
Market Supply & Demand Analysis
Portfolio Review
& Publication of Market Trends

TREY KNIPE, MAI
BRADFORD KNIPE, MAI, CCIM

JOHN R. DILLMAN, MAI
WALETA M. NOVAK
JAMES W. THOMASON
JOSEPH O. SWENSON, CPA

DONALD S. REED, ARA (ret.)
Of Counsel, Agricultural Properties

Certified General Appraisers
Idaho, Oregon, Montana & Nevada

SOUTHWEST IDAHO REGIONAL MLS
NATIONAL ASSOCIATION OF REALTORS®
BOMA OF TREASURE VALLEY

VALUATION TYPES, EFFECTIVE DATES AND PREMISES		Effective Dates/ Comments
VALUE TYPE(S):	Market value	
SCENARIO(S)/DATE(S):	As is	August 18, 1998
INTEREST(S) APPRAISED:	Fee simple estate	
APPRAISAL TYPE: REPORT TYPE:	Complete appraisal Self-contained report	

PHYSICAL SUMMARY		
SITE SIZE (SF/AC):	9,080 SF to 33,663 SF	
SITE ZONING:	City of McCall A City of McCall R-5	(Low-Density Residential) (Rural Residential)
	As Is	As Proposed
BUILDINGS GROSS (GBA) BUILDINGS RENTABLE (RA)	NA—Not Appraised NA—Not Appraised	NA NA
	As Is	As Proposed
LAND-TO-BLDG. RATIO:	NA	NA
OTHER ATTRIBUTES:	Existing	Proposed
Year(S) Built/Age:	Not applicable	Not applicable
Occupancy:	Not applicable	Not applicable
Construction:	Not applicable	Not applicable
Quality &Condition:	Not applicable	Not applicable
Parking:	Not applicable	Not applicable

Synopsis of the Appraisal & Consulting Problem

The subject's valuation required some special assumptions and scope limitations; some of the more important assumptions are discussed in this synopsis, as well as issues critical to an understanding of the value conclusions.

Estates / Interests Valued

The client requested a valuation of the fee simple estate only. The currently marketable estate is the leased fee, due to a lease of each of the 14 cottage sites to their respective leaseholders. However, the intended use of this appraisal is to establish the fee simple benchmark of the lots as vacant, for comparison to current assessed values, and for purposes of re-indexing contract rent to prevailing rates of market return. The standard procedure for rent determination is as a percentage of fee simple value, and as such, leased fee and leasehold values are irrelevant.

Valuation Strategy

Essentially, the 14 subject parcels are appraised as bare ground, because the existing improvements are leasehold improvements (improvements constructed and/or owned by the tenants). The client has specifically asked that I ignore all improvements.

The preferred methodology for the valuation of vacant land is the sales comparison approach, and there were sufficient recent sales in the local marketplace to develop this approach. As such, it is the sole approach utilized in my valuation of the fee simple estate for each of the 14 subject lots.

For 9 of the 14 subject parcels, directly paralleling comparables were available for valuation; for these, the analysis and bracketing of market value potential if vacant was relatively straightforward and objective. These include subject Parcels 4, 5, 6, 8, 9, 10, 11, 12 and 14.

For subject Parcels 1, 2, 3, 7 and 13, however, sales of properties having similar attributes were lacking, and the bracketing analysis was therefore inherently more subjective. Obviously, an appraiser has to work with the information available to him and to the market at large, and I have done my best to minimize the subjectivity and narrow the range of uncertainty in my conclusions.

Market Value vs. Use Value

The requested value is market value assuming the highest and best use of each parcel is a single residential homesite. The implication is a legally developable single homesite. The reality is for two parcels, a single legal homesite is not the highest and best use. For those two parcels, I have estimated a use value—a value of the two parcels if the use as a single homesite granted in the lease were the highest and best use of these parcels. The parcels so affected are Parcels 1 and 2. As such, two values are set forth for these parcels—market value and use value—and it is assumed that the client would desire the rent estimate for these two parcels to be predicated on this use value.

Parcel Size

Parcel size relies on a plats provided by the client, and/or those contained in prior appraisals of these parcels by Trey Knipe, MAI, in 1991.

Market Rent Analysis

Based on the consideration of direct market evidence of rates of return from rent comparables, interviews of market participants, mathematical models for the extraction of implicit land

capitalization rates from leasehold sales, and comparison of the current Idaho Department of Lands (IDL) and other cabin site leases, a conclusion of market return is made at 6% of fee simple land value.

A comprehensive market rent analysis constitutes the last 50 + pages of this appraisal and consulting report.

The report culminates with some implementation strategies that the IDL and the State Board of Land Commissioners (Land Board) might consider to facilitate a move toward market rates.

Scope Limitations

A limited appraisal is one where the appraiser invokes the Departure Provision of the Uniform Standards of Professional Appraisal Practice. The most common departure is the exclusion of one or more of the three typical approaches to value—cost, sales comparison or income capitalization—in situations where the market would typically employ all three approaches in arriving at a price / value conclusion.

Because I am only valuing the land as vacant, neither the cost or income capitalization approaches are applicable to the fee simple valuation. Buyers and sellers of this type of property would not employ the cost or income approaches as a valid indicator of market value, and therefore, the scope of this analysis was not limited due to this exclusion.

Technically, the scope of this report was limited with respect to analysis and valuation of the existing building improvements, which the client has directed me to disregard. However, the scope was not limited with respect to that which I have been directed to appraise—the underlying ground—and therefore it is accurate to characterize this as a complete appraisal.

Special Assumptions & Limiting Conditions

1. The values estimated in this report assume all 14 subject parcels to have average / typical winter access. Specifically, this means that the subdivisions of which the subject lots are a part are assumed to have year-round accessibility, whether the cost of such is at city, county, lessee or lessee association expense. As is typical of alpine cabin site leases in Idaho and elsewhere, access to individual lots is not guaranteed by lessors, and both provision and maintenance of such access are typically the lessee's responsibility.

2. The values estimated in this report assume all 14 subject parcels have the availability of sewer and potable water (that is, if not present on the site today, potable water could be easily obtained). However, as is discussed in the valuation section, I cannot demonstrate from available sale data that the type of water source, or the lack of water altogether, results in a measurable impact on market value. This is assumed to be due in part to the fact that a well, or pump to draw water out of the lake, is a relatively inconsequential cost as compared to the value of the lot; and the fact that for improved properties, such improvements may range from relatively new to several decades old. Determining the type of water to each lot, who installed it, the age and remaining life of such equipment / improvements, and whether or not such has any demonstrable contributory value, is outside of my expertise and the scope of my report.

3. It is specifically assumed that all non-lakefront lots—Parcels 2, 3, 4, 7, 10, 13 and 14—have legal access rights to Payette Lake through the subdivisions of which they are a part or were re-subdivided from (e.g., Payette Lakes Cottage Sites, Cedar Knoll Acres, Pilgrim Cove, etc.).

4. The lakefront boundary of subject Parcels 5 and 9 were not indicated on any available plats. For purposes of calculation of the lake frontage and the parcel size, I have assumed a straight-line

rather than curvilinear lakefront boundary connecting the north and south property boundaries for these parcels.

5. The lots are appraised as though all above-ground building and site improvements did not exist, but all roads, above and underground utilities and easements did exist (in other words, the lots are valued as is, with the exception that above-grade leasehold building and site improvements are assumed to have been removed). It is not relevant which party (lessor, current lessee or a past lessee) constructed the roads, installed the well, brought in the sewer (sewer lines below to the sewer district anyway), etc. The relevant question is what the lots could sell for, as is, today. It is my understanding that when the client exchanges (sells) lots, they do so at appraised value, less some discount for sewer connection fees, as generally, such fees were paid by lessees rather than the lessor. Any and all such determination of applicable fees or discounts for below-grade utilities, if any, is up to the client, and is beyond the scope of my analysis. All my value conclusions assume sewer to be connected on site, or readily available to, each subject parcel.

6. Though addressed in the Standard Assumptions and Limiting Conditions in the Addenda, it is worthy of mention that it is not the client's policy to provide appraisers title policies or ALTA surveys for the subject lots. I have no practical ability to determine the location of underground utilities, encroachments, or other similar adverse title conditions which may impact marketability or market value. Unless specifically noted otherwise, all parcels are assumed to possess typical, non-detrimental utility easements, and to have no encroachments.

7. The client's appraisal instructions direct me to assume that the highest and best use of each subject parcel as vacant is a single home site. The implication is that each is a legal homesite. The reality is that the actual highest and best use differs from this assumption for two of the subject parcels.

   Subject Parcel 1 does not have sufficient depth to allow development were it a vacant parcel available for sale and theoretical development today. To appraise this parcel to its actual highest and best use requires a valuation via assemblage, as this is the only scenario in which it could become a part of a legally developable parcel. To appraise this parcel as a single (legal) homesite would be to overstate my opinion of this parcel's as vacant sale potential, and would require a special assumption of legality. Subject Parcel 2 has an actual highest and best use indicative of a split into two legal homesites—one with creek frontage, and another with a "peek-a-boo" (very limited) lake view. To appraise this parcel as a single homesite would be to understate its sale potential as vacant (the restriction to one homesite is a restriction of the lease, not the parcel, which would be obviated in the event of a sale).

   As such, two values are provided in this analysis—the fee simple market value reflective of what the parcels should sell for if offered on the open market without leases or lease restrictions—and the use value assuming a legal, single building lot. The use values are only utilized for calculation of market rent potential, and again, are only applicable to these two parcels. In the itemized summaries of physical attributes, values, rents, etc., both figures are shown, and rents are based on the Use Value column, which is identical to the Market Value column, save for these two parcels.

8. My market rent analysis is an economic analysis geared toward the charter of the Land Board set forth in the Idaho Constitution—to maximize financial returns on endowment lands for the public school and state hospital trust beneficiaries. It is acknowledged that a lower conclusion could be justified if non-economic factors, or secondary economic considerations potentially competitive to primary function of the Land Board and the Idaho Department of Lands, were weighed in the decision. By the same token, with some alteration of the standard IDL cottage site lease, to impose some contractual index and limits on annual rent increase, a significantly higher minimum economic return could be justified. My analysis assumes the overriding factor to be the state's responsibility to maximize revenue for the benefit of the state's endowment lands.

Value Conclusions

To fully understand the following value conclusions, please pay particular attention to the following sections of the report:

- Special Assumptions & Limiting Conditions
- Market Analysis
- Highest & Best Use Analysis
- Property Valuation
- Market Rent Analysis

The values set forth on the table facing are subject to the standard (generic), specific and extraordinary assumptions and limiting conditions as set forth in this report. Only the aggregate figure is shown in the table below. The reader is reminded that market rents are calculated as a percentage of use value rather than market value. Please see the Synopsis in the Letter of Transmittal for details.

SUMMARY OF VALUE CONCLUSIONS – 14 PAYETTE LAKE COTTAGE SITES, MCCALL, IDAHO			
FEE SIMPLE ESTATE	EFFECTIVE DATE		
As Is Market Value, Land Only	August 18, 1998		$2,999,000
As Is Use Value, Land Only	August 18, 1998		$3,054,000
As Is Market Rent, Land Only (6% of UV)	August 18, 1998		$183,240
ESTIMATED MARKETING TIME	EFFECTIVE DATE		CONCLUSION
If Priced at Value Conclusions & Professionally & Aggressively Marketed	August 18, 1998		Sale Within 6 to 12 Months for non-lakefront lots, 12 to 18 Months for lakefront lots

This appraisal has been prepared in conformity with the current requirements of the Appraisal Foundation as set forth in the Uniform Standards of Professional Appraisal Practice (USPAP), the Code of Professional Ethics of the Appraisal Institute, and with the requirements of the federal bank regulating agencies. If I may be of further assistance to you on this or other matters, please contact me at your convenience. Thank you for providing me this opportunity to be of service.

Respectfully submitted,

KNIPE & KNIPE, INC.

Bradford F. Knipe, MAI, CCIM, President
State of Idaho Certified General Appraiser 117

Underlying Assumptions, Contingencies & Scope Limitations

Overview

In the course of the normal appraisal process, situations arise wherein we must make standard (generic) and specific and/or extraordinary assumptions with regard to information not readily available to us. All Standard, Specific and/or Extraordinary Assumptions & Limiting Conditions which may appear in the report are believed to be compatible with generally accepted appraisal principles, Uniform Standards of Professional Appraisal Practice (USPAP), and Appraisal Institute requirements. All are to be considered a part of the report, and the reader is advised that acceptance of the report constitutes acceptance of all Assumptions and Limiting Conditions.

Standard Underlying Assumptions & Limiting Conditions

Standard Assumptions and Limiting Conditions include such issues as construction components of existing construction; adaptability of soils to development; existence of typical easements, etc. Additionally, since Idaho is a non-disclosure state, details of comparable property sales or leases are presumed to be accurately portrayed by the parties to the respective agreements; in lieu of cooperation by the parties (or in some cases, where parties have no recollection of such details), assumptions and/or reasonable approximations are sometimes necessitated. Such generic assumptions are provided for in the Standard (Generic) Underlying Assumptions and Limiting Conditions contained in the Addenda. The reader is encouraged to read this section of the report.

Special / Extraordinary Underlying Assumptions & Limiting Conditions

More Specific Assumptions & Limiting Conditions are sometimes required depending upon the individual nature of the appraisal problem, and are clearly disclosed in the following the Generic Limiting Conditions, and/or in the discussions within the report to which they pertain. These assumptions are of matters which we have no knowledge, expertise, or timely ability to clarify.

Standard Rule 2-1c of the Uniform Standards of Professional Appraisal Practice require, as applicable to the appraisal problem, clear and accurate disclosure of, and an indication of any impact on value of, a third classification of assumption: "extraordinary assumptions and limiting conditions" that directly affect the outcome of appraisal. In the event any specific and/or extraordinary assumptions and limiting conditions are deemed relevant to the subject and its valuation, they will be set forth immediately following, and/or in the discussions within the report to which they pertain.

Special Assumptions & Limiting Conditions

1. The values estimated in this report assume all 14 subject parcels to have average / typical winter access. Specifically, this means that the subdivisions of which the subject lots are a part are assumed to have year-round accessibility, whether the cost of such is at city, county, lessee or lessee association expense. As is typical of alpine cabin site leases in Idaho and elsewhere, access to individual lots is not guaranteed by lessors, and both provision and maintenance of such access are typically the lessee's responsibility.

2. The values estimated in this report assume all 14 subject parcels have the availability of sewer and potable water (that is, if not present on the site today, potable water could be easily obtained). However, as is discussed in the valuation section, I cannot demonstrate from available sale data that the type of water source, or the lack of water altogether, results in a measurable impact on market value. This is assumed to be due in part to the fact that a well, or pump to draw water out of the lake, is a relatively inconsequential cost as compared to the value of the lot; and the fact that

for improved properties, such improvements may range from relatively new to several decades old. Determining the type of water to each lot, who installed it, the age and remaining life of such equipment / improvements, and whether or not such has any demonstrable contributory value, is outside of my expertise and the scope of my report.

3. It is specifically assumed that all non-lakefront lots—Parcels 2, 3, 4, 7, 10, 13 and 14—have legal access rights to Payette Lake through the subdivisions of which they are a part or were re-subdivided from (e.g., Payette Lakes Cottage Sites, Cedar Knoll Acres, Pilgrim Cove, etc.).

4. The lakefront boundary of subject Parcels 5 and 9 were not indicated on any available plats. For purposes of calculation of the lake frontage and the parcel size, I have assumed a straight-line rather than curvilinear lakefront boundary connecting the north and south property boundaries for these parcels.

5. The lots are appraised as though all above-ground building and site improvements did not exist, but all roads, above and underground utilities and easements did exist (in other words, the lots are valued as is, with the exception that above-grade leasehold building and site improvements are assumed to have been removed). It is not relevant which party (lessor, current lessee or a past lessee) constructed the roads, installed the well, brought in the sewer (sewer lines below to the sewer district anyway), etc. The relevant question is what the lots could sell for, as is, today. It is my understanding that when the client exchanges (sells) lots, they do so at appraised value, less some discount for sewer connection fees, as generally, such fees were paid by lessees rather than the lessor. Any and all such determination of applicable fees or discounts for below-grade utilities, if any, is up to the client, and is beyond the scope of my analysis. All my value conclusions assume sewer to be connected on site, or readily available to, each subject parcel.

6. Though addressed in the Standard Assumptions and Limiting Conditions in the Addenda, it is worthy of mention that it is not the client's policy to provide appraisers title policies or ALTA surveys for the subject lots. I have no practical ability to determine the location of underground utilities, encroachments, or other similar adverse title conditions which may impact marketability or market value. Unless specifically noted otherwise, all parcels are assumed to possess typical, non-detrimental utility easements, and to have no encroachments.

7. The client's appraisal instructions direct me to assume that the highest and best use of each subject parcel as vacant is a single home site. The implication is that each is a legal homesite. The reality is that the actual highest and best use differs from this assumption for two of the subject parcels.

   Subject Parcel 1 does not have sufficient depth to allow development were it a vacant parcel available for sale and theoretical development today. To appraise this parcel to its actual highest and best use requires a valuation via assemblage, as this is the only scenario in which it could become a part of a legally developable parcel. To appraise this parcel as a single (legal) homesite would be to overstate my opinion of this parcel's as vacant sale potential, and would require a special assumption of legality. Subject Parcel 2 has an actual highest and best use indicative of a split into two legal homesites—one with creek frontage, and another with a "peek-a-boo" (very limited) lake view. To appraise this parcel as a single homesite would be to understate its sale potential as vacant (the restriction to one homesite is a restriction of the lease, not the parcel, which would be obviated in the event of a sale).

   As such, two values are provided in this analysis—the fee simple market value reflective of what the parcels should sell for if offered on the open market without leases or lease restrictions—and the use value assuming a legal, single building lot. The use values are only utilized for calculation of market rent potential, and again, are only applicable to these two parcels. In the itemized

summaries of physical attributes, values, rents, etc., both figures are shown, and rents are based on the Use Value column, which is identical to the Market Value column, save for these two parcels.

8. My market rent analysis is an economic analysis geared toward the charter of the Land Board set forth in the Idaho Constitution—to maximize financial returns on endowment lands for the public school and state hospital trust beneficiaries. It is acknowledged that a lower conclusion could be justified if non-economic factors, or secondary economic considerations potentially competitive to primary function of the Land Board and the Idaho Department of Lands, were weighed in the decision. By the same token, with some alteration of the standard IDL cottage site lease, to impose some contractual index and limits on annual rent increase, a significantly higher minimum economic return could be justified. My analysis assumes the overriding factor to be the state's responsibility to maximize revenue for the benefit of the state's endowment lands.

Recommendations

1. The client should contemplate obtaining a legal split of Parcel 2 into two salable / leasable lots. The market value is approximately $25,000 greater as two lots, with negligible costs of effecting such split.

2. The client is directed to the Strategies for Implementation of Rent Increases appearing at the conclusion of the Market Rent Analysis.

Contingencies

None.

Limitations of Scope

Technically, the scope of this report was limited with respect to the exclusion of an analysis and valuation of the existing building improvements, which the client has directed me to disregard. However, the scope was not limited with respect to that which I have been directed to appraise—the underlying ground—and therefore it is accurate to characterize this as a complete appraisal.

Certificate of Appraiser

I certify that, to the best of my knowledge and belief:

1. All representations of factual information contained in this appraisal report are true and correct.

2. The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions and are my personal, unbiased professional analyses, opinions, and conclusions.

3. I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest or bias with respect to the parties involved.

4. My compensation is not contingent upon the reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value estimate, the attainment of a stipulated result, or the occurrence of a subsequent event. The appraisal assignment was not based on a requested minimum valuation, a specific valuation, or the approval of a loan.

5. My analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics of the Appraisal Institute, and the Uniform Standards of Professional Appraisal Practice.

6. The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.

7. I have made a personal inspection of the properties that are the subject of this report.

8. No one provided significant professional assistance or contribution to the signatory to this report.

9. I have the necessary level of knowledge and experience to credibly estimate the value of the subject property, or have taken reasonable steps to achieve such competency and to provide a professional appraisal of the subject property, in accordance with the Uniform Standards of Professional Appraisal Practice.

10. I am an MAI Designated Member of the Appraisal Institute (No. 10992), and have met the continuing education requirements of that organization.

    I am a CCIM Designated Member of the Commercial Investment Real Estate Institute (No. 7213), and have met the continuing education requirements of that organization.

    I am an Idaho State Certified General Appraiser (No. CGA-000117), and a Montana State Certified General Appraiser (No. 494). I have met the continuing education requirements for real estate appraisers practicing in these states.

KNIPE & KNIPE, INC.

Bradford T. Knipe, MAI, CCIM, President
Idaho Certified General Appraiser No. 117

8/31/98
Date Signed

Table of Contents

COVER

LETTER OF TRANSMITTAL

UNDERLYING ASSUMPTIONS, CONTINGENCIES & SCOPE LIMITATIONS i
- Overview i
- Standard Underlying Assumptions & Limiting Conditions i
- Special / Extraordinary Underlying Assumptions & Limiting Conditions i
- Recommendations iii
- Contingencies iii
- Limitations of Scope iii

CERTIFICATE OF APPRAISER iv

TABLE OF CONTENTS v

PART I: INTRODUCTION & EXECUTIVE SUMMARY ix

SCOPE OF THE APPRAISAL & CONSULTING ASSIGNMENT x
- The Appraisal Process x
- Type of Appraisal and Type of Appraisal Report x
- Steps of the Appraisal Process xi

SUMMARY OF IMPORTANT FACTS & CONCLUSIONS xii

PROPERTY HISTORY AND OVERVIEW xiv
- History of the Subject Property xiv
- Sales within the 3-year USPAP-Required Reporting Period xiv
- Lease Summary xiv
- Agreements to Sell xiv
- Conclusions xv

PROJECT STRENGTHS & WEAKNESSES xvi
- Project Strengths xvi
- Project Weaknesses / Potential Detriments xvi

PART II: DEFINITION OF THE APPRAISAL PROBLEM 1

DEFINITIONS 2
- Purpose of the Appraisal 2
- Intended Use of the Appraisal 2
- Intended Users 2
- Definition of Market Value 2
- Definition of Property Rights Appraised 3
- Effective Dates 3
- Identification of the Property 3
- Other Definitions 4

COUNTY, CITY & NEIGHBORHOOD INFLUENCES 6
- Overview 6
- History 6
- Physical and Environmental Characteristics 7
- Social and Economic Characteristics 9
- Utilities & Infrastructure 13
- Real Estate Highlights 14
- Conclusions 20

ZONING & ADMINISTRATIVE REQUIREMENTS 21
District Classifications 21
Discussion of the A District 21
Definition and Purposes 21
Allowable Uses 21
Conditional Uses 21
Discussion of the R-5 District 22
Definition and Purposes 22
Allowable Uses 22
Conditional Uses 23
Developmental Restrictions for McCall Residential Districts 24
Non-Conforming Lots, Structures & Uses 24
Non-Conforming Lots of Record 24
Non-Conforming Structures 24
Conclusions 26

REAL ESTATE TAXES AND ASSESSMENTS 27
Assessment Summary 27
Property Tax History 27

PROPERTY IDENTIFICATION, ZONING, TAXES, DESCRIPTIONS 28
Overview of Parcel Data Sheets 29
Ownership & Identification 29
Zoning 29
Likelihood of a Zoning Change 29
Taxes & Assessments 29
Site Description 29
Physical Characteristics 30
Utilities and Easements 30
Off-Site Influences 30
Building & Site Improvements 31
Parcel 1 32
Parcel 2 33
Parcel 3 34
Parcel 4 35
Parcel 5 36
Parcel 6 37
Parcel 7 38
Parcel 8 39
Parcel 9 40
Parcel 10 41
Parcel 11 42
Parcel 12 43
Parcel 13 44
Parcel 14 45

PART III: PROPERTY VALUATION 46

THE VALUATION PROCESS 47

MCCALL RESIDENTIAL MARKET ANALYSIS 48
Non-Waterfront Subdivision Trends 48
Supply & Demand 48
Residential Trends 50
Lakefront Homesites 51
Government Influences on Lakefront Property 53

Home Values 54
Summary 55

HIGHEST AND BEST USE 57
Highest and Best Use Definition 57
Highest and Best Use of the Site As Vacant 57
Highest & Best Use As Is 59
Most Probable Buyer 60
Most Probable Scenario of Sale 60
Highest & Best Use Conclusions and Valuation Strategy 61

COST APPROACH 62

SALES COMPARISON APPROACH 63
Overview of the Comparables 64
Lakefront Single Family Lots 65
Effective Purchase Price 65
Units of Comparison 66
Discussion of the Sales 66
Adjustments to Land Sales 66
Price Per Square Foot Conclusions 74
Price Per Front Foot Conclusions 78
Sales Comparison Reconciliation for Typical Lakefront Lots 82
Lakefront Lots with Special Valuation Issues 84
Valuation of Parcel 1 84
Conclusions for the Special Lakefront Parcel 87
Valuation of Non-Lakefront Lots 88
Effective Purchase Price 88
Units of Comparison 89
Discussion of the Sales 89
Adjustments to Land Sales 89
Price Per Square Foot Conclusions 92
Price Per Front Foot Conclusions 96
Sales Comparison Reconciliation for Typical Non-Lakefront Lots 98

INCOME CAPITALIZATION APPROACH 100

RECONCILIATION & FINAL FEE SIMPLE VALUE ESTIMATES 101

REASONABLE EXPOSURE TIME & ESTIMATED MARKETING PERIOD 102
Historical Exposure Time 102
Subject's Estimated Marketing Period 102

SUMMARY OF VALUE CONCLUSIONS 103

PART IV: MARKET RENT ANALYSIS 104

MARKET RENT ANALYSIS 105
Conceptual Overview 105
Brief History of Idaho Department of Lands Leasing Program 105
Historical Overview of IDL Program 105
Current IDL Leasing Practices 107
Rent Analysis 109
Land Capitalization Rate versus Fixed Rate 110
Influences on Value versus Influences on Rate of Return 111
Private Sector vs. Public Rates of Return 111
Lease Provision Considerations 112
Discussion of the Comparables 118

Other Rate of Return Indicators....139
Calculation of Implicit Rates of Return....147
Cap Rates Relative to Value....151
Arguments in Favor of a Lower Rate of Return as Value Increases....151
Arguments Against a Lower Rate of Return as Value Increases....151
Market Rate of Return Conclusions....154
Summary of Rate of Return Indicators....154
Relevant Bracketing Factors....154

PART V: STRATEGIES FOR IMPLEMENTATION OF RENT INCREASES....158

STRATEGIES FOR IMPLEMENTATION OF RENT INCREASES....159

ADDENDA....A

UNDERLYING ASSUMPTIONS & LIMITING CONDITIONS

CLIENT'S LETTER OF ENGAGEMENT & CONTRACT

IDAHO DEPARTMENT OF LANDS BUREAU OF REAL ESTATE MISSION STATEMENT

IDAHO DEPARTMENT OF LANDS SAMPLE LEASE & ATTACHMENT A

IDAHO DEPARTMENT OF LANDS IMPROVEMENT SPECIFICATIONS

1999 PROJECTED MCCALL COTTAGE SITE RENTS–ITEMIZED

QUALIFICATIONS OF BRADFORD T. KNIPE, MAI, CCIM

Part IV: Market Rent Analysis

Market Rent Analysis

Conceptual Overview

Up to this point in the report, the focus has been on gaining a perspective on residential land market activity in McCall, Idaho, the influence of Payette lake on real estate and lifestyles, and the valuation of the 14 benchmark cottage sites that Idaho Department of Lands will attempt to use to extrapolate to their remaining 200+ lots.

As the reader will note, though it has certainly not always been the case, assessed value and appraised value for these lots are reasonably in line; individually, our conclusions varied by up to about 50 percent, but most were within 20-25 percent of the assessed value, one direction or the other. Interestingly, in the aggregate, assessed values are 93+ percent of appraised values.

Recently, we completed another appraisal for Idaho Department of Lands involving 15 Payette Lake cottage sites, and the results were similar: Individually, our appraised values diverged from assessed values by over 120 percent, but generally were within 20 percent one way or the other. In the aggregate, the assessed value was about 88 percent of total market value.

As such, the margin for error in establishing benchmark lot values from these two appraisals, reflecting a total of 28 distinct lots, is minimal, particularly for rental purposes, since the rent is but a fraction of market value.

The critical question is what that fraction or percentage should be. The balance of this report attempts to address in a reasoned manner that politically sensitive question.

From the outset, readers of this report should realize that there are two general classes of information which can be considered in formulating a rental policy: Economic considerations, and non-economic considerations. Our focus is on the economic factors, utilizing direct examples of actual rates of return other lessors are reporting, opinions of market participants, and extracted (implicit) rates of return from economic models. As will be shown, the economic considerations lead us to a conclusion that 6 percent of fee simple market value per lot would be the minimum fair market return to all parties concerned.

We fully acknowledge that non-economic factors will be reflected in the Land Board's ultimate rent policy decision for 2000 and beyond (the 1999 policy is already in place), and toward that end, we offer some suggested strategies which may ultimately assist the Board in implementing whatever level of increase—if any—they elect to pursue. However, it must be emphasized that non-economic factors—such as the sociological benefits of providing low-cost recreational lots to some citizens—is well outside the scope of our analysis; while some such factors are mentioned where relevant to an economic discussion, they have been given no weighting in our ultimate conclusion.

Brief History of Idaho Department of Lands Leasing Program

Historical Overview of IDL Program

The State of Idaho leasing program began in 1924, but most of the lots were actually leased for the first time in the 1940s and 1950s. Rents were reportedly nominal, and were held relatively flat for the period 1945 to 1988, with only sporadic adjustments (for example, there was no rent increase whatsoever for the period 1947 to 1961).

©1993-1998, Knipe & Knipe, Inc. • File ID 98.886• Page 105

In recognition of the fact that the state was not achieving a market return, the state decided to auction up to 10 percent of the cottage sites in 1987. The purpose was to establish benchmark fee simple values, and appraisals done by L.D. Knapp set minimum bid prices. In August of that year, 22 lots were sold.

In acknowledgment of speculative activity as a result of substantial leaseholds, and the disparity between contract and market rents, the state adopted a rental rate as a percentage of market value in 1988. The rate selected was 2.5 percent, and the values were established by the prior year's sales.

In 1990, the Idaho Legislature, concerned with the leasing situation and the public resistance to rents as a percentage of value, embraced SB 1516, and enacted it as Idaho Code 58-310, which stated that the Land Board "shall ensure that each lot generates market rent throughout the duration of the lease", and eliminated the auctioning of a lease to the highest bidder at the expiration of a term ("conflict bid").

In April of 1990, the Land Board adopted a policy to ensure that this statute was being complied with. This included the appraisal of 13 benchmark lots, by Trey Knipe, MAI, then of Real Estate Consulting Group. He and his partner, Tom McKevitt, MAI, initially concluded that market rents should be based on an 8 percent annual return, but in light of additional market data, moderated that to a range of 4.5 to 5.5 percent of market value.

Homeowners' associations formed by the lessees initially fought both the appraised values and the recommended lease rates. Arguments put forth by their representatives ranged from well reasoned to relatively absurd claims that were counter to generally accepted economic and appraisal standards (e.g., "lease rates cannot be based on fee simple values", "one cannot apply a rate of return to property that is not, and will never be, offered for sale", etc.).

After numerous hearings with representatives of the cottage site associations, in June of 1991, the Land Board decided to continue with the 2.5 percent rate of return established in 1988. The base year for the leases, however, was moved up to 1992, and a 10-year phase-in plan was adopted to soften the impact on lessees, as well as a 5.3 percent cap on annual rent increases.

According to one Land Board Memorandum we reviewed, it was noted that average leasehold prices escalated significantly over a 20-year period:

Average Leasehold Prices	1975	1994
Lakefront	$9,175	$284,567
Non-Lakefront	$5,480	$59,000

This suggested change is impressive, but it is not in and of itself a particularly meaningful indicator. A more meaningful comparison would be the use of the average price per square foot for non-lakefront lots, and the average price per front foot for the lakefront lots, thereby accounting for the units of comparison most often used by the marketplace. With only a few sales each year, average lot size and average lake frontage per lakefront lot can vary, and have a significant influence on the prices paid for leaseholds.

Nevertheless, on the face of such evidence, and other factors, by 1997 the State Land Board had renewed concern that the 2.5 percent rate of return may be below market return levels for this property type:

a) Leasehold values were continuing to escalate significantly—by Idaho Dept. of Lands' estimates, about 14.34 percent per year for lakefront lots, and 9.62 percent per year for non-lakefront lots since 1992;

b) Market data suggested virtually all types of investment -including money market and savings accounts—were generating better than a 2.5 percent rate of return; and

c) In some cases, the actual rents being achieved were well below even the 2.5 percent target rate, such that lessees were paying less in rent than they would have paid in taxes if they owned the lots outright. It was estimated that 2.5 percent of the 1992 assessed value, which prevails as a benchmark rate, equated to only about 1 percent of the 1996 assessed value, because of significant escalations in assessed value through the middle 1990s in an effort to catch up substantial market value increases in the early 1990s.

Interestingly, following an almost parallel timeline, in 1998 Montana tried to go from flat fees of $25 to $50 per year, to 5 percent of market value. In the face of similar lessee opposition, the State Legislature capped rents at 3.5 percent, and their program has been the subject of debate and various studies ever since. In April of this year, a Montana First Judicial District Court judge found 10 of 14 statutes unconstitutional as applied to state school trust lands, and ruled that "the [State Land] Department's practice of charging a rental rate of 3.5 percent of the appraised value violates its duty as trustee of the school trust." The same ruling noted that at trial, the defendants [State of Montana Board of Land Commissioners and Department Natural Resources and Conservation] presented no rebuttal to the plaintiff's [Montanans for the Responsible Use of the School Trust] contention that prevailing market rates of return were 8 to 12 percent. [Cause No. ADV 97-134, Decision, Order and Permanent Injunction, filed April 3, 1998]

The reference by the judge was to an economic study entitled "Task 2: Cabin Site Lease Rates", by John Duffield of Bioeconomics, Inc.; interestingly, Mr. Duffield simply cited in his report that a private fee appraiser had conducted several appraisals concluding to this range of rates, but Duffield himself simply showed a minimum implicit market return rate of 6.5 percent as calculated from the sale prices of 2-week auction offerings of leaseholds in Montana. He noted that with more typical exposure to the open market, leasehold prices, and thus implicit rates of return, would likely be higher, possibly supporting the 8 to 12 percent market returns contended by fee appraisers. (Duffield's study is discussed later in our report.)

Current IDL Leasing Practices

The current nominal rate of return on State of Idaho Department of Lands cottage site leases is 2.5 percent. This rate is multiplied times assessed value, with what is effectively a 2-year delay. For example, the 1999 lease rates are to be based on 2.5 percent of the 1997 assessed value, as that was the most recent figure available as of July 1, 1998 (the state must give lessees 6 months notice of rent changes).

Leases are assignable. When one lessee sells his leasehold interest to another, the state takes a fee equal to 10 percent of the residual leasehold value (sale price less leasehold improvement value less personal property value, if any). Leaseholds have been substantial, generally running 50 to 75 percent of fee simple value, and in several cases, leasehold prices paid appear to have actually exceeded fee simple value. When contract rents are at market rent levels, and when substitutable options exist in the marketplace, buyers of leasehold estates do not pay anything for leaseholds. That is to say, when a lessee has a lease that is at market levels, he can assign his lease interest to another party, but not at a premium.

The higher the percentage of fee value new lessees are willing to pay to take over someone else's lease, the further below market the rents are indicated to be. This will be discussed in more detail later in this rental survey.

Suffice it to say that the current program is operating from a 1992-1998 policy which adopted 2.5 percent as the target rate of return, but which established minimum rents for lower value lots, such that the least expensive lots may have had lessees paying 4 to 5 percent of market value; and because of a lag between assessed values and market, as well as a phase-in plan adopted in 1992, and alternative rent payment options offered lessees by the Land Board, lessees of more expensive lots may currently only be paying 1 to 2 percent of current market value.

The 232 lots currently administered by the Idaho Department of Lands are summarized as follows:

Lot Class	Count	1999 Rent	Average Rent	1997 Assessed Value	Average Assessed Value
Lakefront Lots	76	$296,778	$3,905	$24,261,777	$379,090
Lots on Commons	3	$8,252	$2,751	$953,153	$317,718
Non-Lakefront	153	$138,600	$906	$8,324,676	$55,130
Totals	232	$443,629	$1,912	$33,539,606	$153,851

The average and total assessed values exclude 12 lakefront lots, and 2 non-lakefront lots, which are in the McCall city limits or are otherwise outside the rural Payette Lakes Sewer District; for these lots, no assessed value is calculated. (An assessed value was calculated at the request of IDL in 1996, and that year, for all 232 lots, total assessed value was $35,551,890, with a lakefront average of $351,808 (indicating a 7.75% increase to 1997), a non-lakefront average of $51,079 (indicating a 7.93% increase to 1997), and $333,139 for lakefront lots separated by commons (indicating a 4.62 decrease for 1997—the decline accounted for by a successful tax appeal on one of the three lots).

The 1999 rent figure indicated is based on the prevailing Land Board interim rent policy, which is apparently for 1999 the greater of 2.5 percent of 1992 Assessed Value, or a 25 percent increase over what the tenants were paying for 1997. On 1998 (current) Assessed Value, which has been held constant in most cases with 1997 levels, the projected 1999 rent would equate to only about 1.32 percent of theoretical market value. Based on our this analysis and other recent appraisals we have done for the Idaho Department of Lands, assessed values seem to be on average, about 7 to 12 percent below market value; with that, and the fact that the aggregate assessed value figure of $33.5 million excludes 12 lakefront and 2 non-lakefront lots, one can approximate the percentage of market value the projected 1999 rents may represent. Using the average assessed values for these property types ($379,090 each for twelve lakefront lots, and $55,130 each for two non-lakefront lots), the total assessed 1997 (and presumably 1998) value would be approximately $38.2 million, and using only a 7% differential (division by 93%), market value would be suggested at roughly $41 million. At this level, the reality of the project Payette Lake Cottage Site rents for 1999 is likely a return to the State Endowment fund closer to only 1.1% of market value!

Rent Analysis

In the course of researching actual comparables and opinions of real estate market participants involved in the leasing of recreation-oriented land, numerous individuals were contacted by telephone, fax, or e-mail. A sampling includes:

- Leon Mason, USDA Dept. of the Interior, Utah
- Ralph & Jeanne Green, Private Lessor, Lake Pend Oreille
- Jim Gross, State Land Department, Arizona
- John McFaddin, MAI, Fee Appraiser, Washington State
- Henri LeMoyne, SRPA, Fee Appraiser, Idaho
- John Frome, MAI, Fee Appraiser, Wyoming
- Darrell Hoffman, MAI, Fee Appraiser, Wyoming
- David Groth, MAI, Fee Appraiser, Oregon
- Mike Barrie, SR/WA, Idaho Power Company, Leasing Specialist
- Jim Clawson, Leasing Agent, Pacific Gas & Electric Co.
- Ed Lehman, Leasing Agent, Pacific Gas & Electric Co.
- Steve Gray, Real Estate Specialist, Boise Cascade Corp.
- Dave van de Graaf, Timberline Mgt. Div., Boise Cascade Corp.
- Tom Montzka, Real Estate Specialist, Boise Cascade Corp.
- Ted Lyons, Real Estate Dept., Tacoma Public Utilities
- Jim Hebner, Recreational Lease Program, Boise Cascade, Minnesota
- Barry Thompson, MAI, Fee Appraiser, Washington State
- Paul Tittman, Chief Appraiser, U.S. Forest Service, Washington D.C.
- Steve Bottemiller, Real Estate Dept., Bonneville Power Admin.
- John Frederickson, MAI, Fee Appraiser, Washington State
- Bob Bancroft, MAI, Fee Appraiser, Oregon
- Andy Lilly, SRA, Fee Appraiser, Oregon
- Umatilla County Assessor's Office, Oregon
- Jim Eaton, MAI, Assistant Chief Appraiser, U.S. Dept. of Justice
- Maggie Love, MAI, Fee Appraiser, Colorado
- Bob Mautz, Esq., Tollgate Co., Lessors, Langdon Lake, Oregon
- Bob Gloodt, Manager—Appraisals, Union Pacific Railroad
- John Pilcher, Burlington Northern Railroad Real Estate Dept. (ret.)
- Jim Atkinson, Leasing Manager, Minnesota Power Co.
- John Paulson, Leasing Division, Minnesota Power Co.
- Randy Rucker, Montana State University, Dept. of Ag. Economics & Economics
- Christopher Klyza, Assoc. Prof. of Political Science and Env. Studies, Middlebury College, VT
- Stell Benefield, Alabama Power
- Ray Flaherty, Catellis Real Estate, Seattle, WA
- David Brooks, MAI, Fee Appraiser, Maryland
- Carl Barnett, Pacific Power & Light
- Carl Stillman, MAI, Fee Appraiser, Oregon
- Bob Dietrich, CCIM, MAI, Fee Appraiser, California

Numerous other appraisers, utility companies, brokers, timber companies, and government agencies were contacted, but requests for information were not answered, or were not answered in time for consideration in this publication.

In the course of this search for market data on rates of return for recreational land, we were able to develop 10 distinct comparables which bracket a broad range of situations and motivations influencing the rate of return these lessors achieve. Before discussion of the comparables, it is

worthwhile to discuss the theory behind a rate of return, and the types of factors that need be considered in bracketing a rate of return for the subject lots.

Land Capitalization Rate versus Fixed Rate

Fixed Rent Per Month or Per Year

One way to estimate market rent is to consider a commodity on the basis of what rent (per month or per year) competing properties are renting for in the local marketplace. This would be the preferred way to arrive at market rent if the type of property being analyzed:

a) Is fairly standard in characteristics (generic, with many substitutable options in the marketplace); and

b) Is a type of property typically rented in the marketplace by a variety of market participants.

For example, if one were considering the rent for office space, one would find that most offices are more or less similar, and may rent for $12 to $14 per square foot per year in a given market.

In the case of recreational lots in McCall, Idaho, outside of the State Dept. of Land's program, we are aware of no ground leases, and individual lots vary greatly in view, location, amenities, size, frontage, and other attributes. Expanding the search for data regionally or nationally, parallel situations are extremely rare. The most analogous situations are other government programs, and lot values vary considerably. For example, for a $30,000 lot on a reservoir in Washington State, rent may be $2,250 per year. Obviously, this would not provide a meaningful comparable for a $500,000 lot in McCall, Idaho.

Rate of Return (Land Capitalization Rate)

Valuation theory assumes that all commodities which have market value have the potential to achieve income based on some percentage of that value. For example, if a leased retail building has a value of $600,000 and rents for $55,000 in net income annually, it has an overall capitalization ("cap") rate of $55,000/$600,000 = 9.17 percent. This capitalization rate is also known as the overall rate of return.

Land has a rate of return as well. Again referring to typical appraisal theory, land may have one rate of return, and improvements to the land a higher rate of return. The reasoning behind this is that land has permanence, and warrants a return on its investment (a ground rent). Improvements lack permanence, and thus someone constructing them needs not only to achieve a return on the investment, but also a recapture of the costs of the wasting asset. As an example, it is typical in commercial leases in Boise for the land component to command a net annual return (land cap rate) of 9 to 10 percent of market value, and the building improvements to command a net annual return (building cap rate) of 11 to 14 percent. The weighted average of these two components makes up the overall cap rate (overall rate of return). So, if a developer were to build a commercial building for a retail tenant as a build-to-suit undertaking, with the land valued at $150,000, and the cost of the improvements at $650,000, the required overall net rent per year might be calculated as follows:

Land	$150,000 x 10.0%	=	$15,000
Improvements	$650,000 x 12.5%	=	$81,250
Annual Rent		=	$96,250
Overall Return	$96,250/$800,000	=	12.03%

Using the hypothetical Washington lot example, the previously discussed rent of $2,250 per year on a $30,000 lot has no direct applicability for an Idaho lot valued at $500,000. However, the rate of return on that lot, $2,250/$30,000 = 7.5 percent, would provide a meaningful indicator of the subject's rent potential, assuming all rights and restrictions associated with that rate are similar to the rights and restrictions influencing the subject lots. Such influences will be discussed later in this report.

Influences on Value versus Influences on Rate of Return

It is our professional opinion that land valuations should reflect the qualitative differences among the lots—for example, size, encumbering easements, parcel shape, lake-frontage (quantity and quality), lake views, etc. In other words, physical and external factors which have bearing not only on lots in the leasing program, but on lots in the market in general, should be reflected in the fee simple valuation of those lots, not the capitalization rate. Once land value has been estimated, the land cap rate then applied should be the same for all leased lots, regardless of individual lot attributes.

The best way to correlate to a rate is to try to tabulate private sector cap rates, determine whose perspective you are viewing them from (we will view them from the perspective of the lessee—what is the effective percentage of fee value they pay per year, adjusted for property taxes on land if applicable), and then compare relative rights and restrictions imposed by the leases (year-round versus partial year use, who maintains access, how long the lease term is, whether or not cabins can be remodeled/rebuilt and what level of bureaucracy is involved, etc.). These are factors which would impose limitations on the leased lots only—not factors of the market also influencing non-leased lots in the same market area. Such factors should be considered in adjusting downward the cap rate conclusion from that which might otherwise be indicated for a lease situation with minimal restrictions. In other words, if one determines a typical private sector net ground lease between individuals might be 10% per year, one involving governmental or large corporate inertia in securing approvals for leases, shorter lease terms, greater restrictions on use, or other factors might argue for a 5 to 8 percent rate of return.

In summary, the factors inherent to the land should be reflected in the land valuation (location, desirability, etc.), and the factors inherent in the lease (use restrictions, risk, uncertainty, etc.) ought to be reflected in the cap rate conclusion. Under no circumstance, however, should one discount a property's fee value for poor access, to use an example, then make a similar discount to the cap rate for that poor access. Even more blatant an error is penalizing the fee simple value conclusion of the lot for issues stemming from the lease—the fee value and the restrictions of the lease are entirely separate matters, and as much as possible must remain so to maintain the integrity of the analysis.

Private Sector vs. Public Rates of Return

The relevant land cap rate is one supported by private sector land leases. Land cap rates utilized by municipal, state or federal government agencies may be discussed and may in fact bracket the full range of returns in the private sector, but the correlation should give considerably greater weight to private sector leasing agreements, illustrative of an open and competitive market situation.

Indeed, government or large utility company rates may have been based on (have their roots in) a similar market analysis such as that we are undertaking, but they then get run through the filter of the political process, and may become tainted as a result (political motivations often result in the agency taking less than a market return, in order not to invoke public outcry in an election year, or risk a withdrawal of support from constituents on other matters deemed more critical to the public interest). The best data is that which is as removed from political (non-economic) influences as possible.

©1993-1998, Knipe & Knipe, Inc.

Lease Provision Considerations

All leases convey certain elements of the bundle of rights, including rights of use and enjoyment for a period of time, and all impose some limitations on the scope of those rights, such as the right to use year round, mortgage the property, alter its natural state, etc.

Here, we discuss some of the more important factors:

Scenarios, Rates & Terms

Type of Lessor

The more independent the lessor, the greater the chances that the lessor will be able to set lease rates of return based on market factors (rates of return on alternate investments embodying similar risk), than on policy factors. Therefore, as noted, we place more weight on private sector entities than public, and more on public utilities than on governmental agencies.

Lessor Motivations

In any market, some market participants are more savvy and experienced than others, and even among experienced market participants, motivations can vary widely. For example, some of the market participants are operating under the profit motive—that is, the motive to maximize returns—while others offer lots for the sake of public relations—that is, putting forth before the public the image of an agency or company that cares about the environment or providing recreational opportunities. The two are not necessarily at odds, but some lessors will tell you that they are achieving what the market will bear, and some will tell you that if profit were their primary motivation, they could achieve rates significantly higher than they are. This needs to be considered, just as in an analysis of market rent for an apartment building, a lessor who admittedly is leasing below market is probably not the best source of market comparables for other projects analyzed for market potential.

To understand the fundamental goal or charter of the department issuing the leases, it is worthwhile to quote from the Internet web page of the Idaho Department of Lands:

In order to effectively manage the endowment lands and funds, Article IX of the Idaho Constitution established the State Board of Land Commissioners, consisting of Idaho's Governor, Secretary of State, Attorney General, and Superintendent of Public Instruction. The state auditor was added to the board by constitutional amendment in 1910. The land commissioners, acting in the capacity of trustees on behalf of the beneficiary schools and other institutions, were given the responsibility, under Article IX, Section 8, of the Constitution (as amended), to manage the endowment lands "... in such manner as will secure the maximum long term financial return to the institution to which granted..."

In addition to this charge to the commissioners, the Constitution also established a permanent endowment fund, the principal of which " ... shall forever remain inviolate and intact ... ," and the interest from which must be used for the maintenance of the public beneficiaries of the state. This mandate resulted in the creation of the permanent "Endowment Fund," in which is found the principal assets of the trust lands and proceeds from land sales and certain royalties, and the "Income Fund," from which regular distributions of interest accrued to the perma[n]ent fund and land-lease earnings are distributed to the trust beneficiaries on a regular basis to help fund their operations.

To allow the Board of Land Commissioners to more efficiently carry out its constitutional functions, the Idaho legislature created the Department of Lands in 1905. At the helm of the department, and directly accountable to the Board, stood its director, aided by two assistant directors responsible for the day-to-day operations of the department's two major statutory divisions: Lands, Minerals & Grazing and Forestry & Fire.

The original purpose of the Idaho Department of Lands – to assist the Board of Land Commissioners in carrying out its constitutional duties – remains the same today. The department's mission statement echoes that of the board: "We manage endowment trust lands for the beneficiaries and protect natural resources for the people of Idaho."

The charter of the State of Idaho Department of Lands, per the Mission Statement of its Bureau of Real Estate, is "...to increase the financial return to the endowment funds...". This does not use the words "maximize," but the term "increase" nonetheless implies an obligation to be concerned with income generation rather than a public relations focus, and this is consistent with the Department's role as the enforcing arm of the Land Board. (The complete mission statement is contained in the Addenda.)

As such, it is fair and accurate to conclude that a primary purpose (motivation) of the State Department of Lands is to maximize economic return on state-owned lands to generate funds for Idaho's public schools, state hospitals, and other public purposes. This is as opposed to just achieving some return that allows the agency to attain economic break-even, while serving more of a custodial or public relations function, though certainly those are important secondary considerations.

Property Taxes

As discussed, to make a determination of an appropriate land capitalization rate, one must choose a perspective, and compare all rate comparables on a similar basis. We will contemplate the effective rent to the lessee. Thus, one must equate whether or not the lessee has any tax obligations.

For the subject lots, the lessees pay taxes on their leasehold improvements, but for virtually all the subject lots, there are no property taxes per se on the land. Rather, there is a nominal fee lessees are responsible for in order to retire the debt for the Payette Lakes Sewer District (this rate is about 0.08 percent—that is to say, less than 0.1 percent, of assessed value). For all intents and purposes, there is no material tax liability to lessees.

As will be seen, in most of the comparables we examined, lessees do pay property taxes on leasehold improvements, but the picture is mixed for taxes on land.

Rights of Use vs. Restrictions

While it is virtually impossible to assess all the nuances of the individual leasing situations surveyed, there are several attributes which can be contemplated globally:

Use

The subject leases are limited to 3 structures, including a single-family dwelling no higher than 35 feet and no smaller than 400 square feet, and two 1-story utility buildings (such as a boathouses or sheds). Boathouses cannot exceed 288 square feet, and other utility buildings are not to exceed 624 square feet. Mobile homes on permanent foundations are acceptable. All structures must meet state and local building codes.

The subject leases initially were limited to seasonal recreational use, but over the years, the Dept. of Lands stopped enforcing the seasonal use aspect. Access (snow removal) and lack of "winterization" of many of the leasehold improvements is why many of the lots see only seasonal use today.

Among the comparables, virtually all are for a single recreational residential use, and most allow year-round occupancy.

Lease Term

The subject's leases are on a 10-year term. However, in an effort to make it as easy as possible within this constraint for a tenant to get financing for leasehold improvements, the State of Idaho Dept. of Lands will reset the lease to a new 10-year term upon the request of the tenant. Thus, the IDL leases are effectively a rolling 10-year lease.

The cap rate comparables we found had terms ranging from a rolling 30-to-180-day out clause for the lessor, to 25 years. No obvious correlation was found between term and rate, as for example one comparable with 25-year terms showed leases at 2.5 percent of value, and another with 20-year terms showed leases at 7.5 percent of value. The primary difference between these two comparables, both leased by power companies, was lessor motivations—one being profit, and the

other being public relations. That with the 2.5 percent rate of return noted that if they were operating under a profit motive, they would require a 5.0 to 7.5 percent return, which is consistent with the rate achieved by the other lessor that is operating with the stated motivation of profit maximization.

Lease Rate Changes

The subject leases may increase or decrease annually with 180-days notice from the lessor. No method for determining changes in the lease rate are set forth in the lease, nor are any limits on how much the rate can change in any year or over the 10-year term of the lease.

Virtually all of the rate comparables had some kind of annual indexing, with CPI escalations most typical, and periodic revaluation of the underlying fee value by the lessor, by a fee appraiser, or the local assessor.

Utilities Available

All of the subject lots have sewer available. This utility was provided by the sewer district, not the lessor, and thus arguably this is a factor which should only be accounted for in the land valuation, not the rate of return. Most of the state's leased lots have a private water supply (well or lake source), or as in the case of the Pilgrim Cove lots, a shared water system within the subdivision. All water sources are owned and maintained by the lessees, and presumably some are decades old.

Most of the comparables have septic and water systems owned and maintained by the lessees. In none of the comparables did we find lessors indicating that they supplied or guaranteed any utilities, other than electricity in the case of leases from power companies.

Year-Round Accessibility

The State of Idaho lease does not specifically guarantee any access, though it is implicit that legal access is available to the larger projects containing state lots (e.g., Payette Lakes Cottage Sites, Pilgrim Cove, etc.). However, the lessor provides little if any road maintenance, no snow removal, and access to individual lots is generally the responsibility of the lessee. If lessees, either individually or as a group, desire to access their lots in the winter, they have to plow the roads should direct and immediate vehicular access be desired to their front doors. The Idaho lease has a blanket reservation for access of the lessor, and to provide access for other lessees to their lots across a lessee's individual lot.

It is more difficult to state definitively the access status of the comparables analyzed. For example, some are in climates where snow is less of an issue than it is in McCall. Some projects have the same situation as the cottage sites, while others guarantee year-round access. Still others guarantee access only to certain lots within their projects, with no report

of a different rate of return being achieved for lots having seasonal versus year round access.

Lessee's Right to Expand or Rebuild Improvements

For the State of Idaho lots, all renovations, expansions, rebuilds, or tree removal requires the permission of the lessor, and the securing of any necessary permits or reviews from local government agencies. However, Mr. Bryce Taylor reports that he is unaware of any requests for renovation/rebuild being denied, except in the case of a specific lot in the Peninsula which is targeted for exchange with the Idaho Department of Parks and Recreation.

For the comparables, similar situations apply. Only one of the comparables allows lessees to make changes to the improvements with no lessor oversight or approval requirements. Some of the comparables required lessor approval, and others went so far as to require lessor approval not only of design, but of materials. Some had requirements of local governmental authorities, and others did not. The lowest comparable found, Minnesota Power at 2.5 percent, reportedly has two levels of governmental approvals required, which the lessor reported as imposing an additional bureaucratic level which is reflected in the rate. (It should also be noted that the effective rental rate to tenants for this lessor is well above the 2.5 percent nominal rate—estimated by the lessor at 5.5 to 6 percent—inclusive of taxes on the land paid by the lessees.)

Renewal

The subject leases are structured such that current lessees have a first right of refusal to renew their leases at expiration. At least at one point in the IDL program's history, an open bid situation was tried, but the results were hostile, and the practice was abandoned. In 1990, the Idaho Legislature made illegal the practice of conflict bidding—forcing an existing tenant to compete for renewal in an auction situation.

All of the comparables have a similar first right of refusal situation.

Lessor's Termination Rights

The State of Idaho can terminate a lease at will for purposes of sale of the lot. If they do so, however, they are obligated to buy all "approved" leasehold improvements at their market value. Mr. Bryce Taylor reports that in 70+ years of the program, this right has never been exercised.

Some of the comparables indicated a right of the lessor to terminate the leases unilaterally. Most did not address this topic.

Lessee's Right to Terminate	No lessee right to terminate was noted in the State of Idaho leases. Most of the sources of competing rates did not indicate such a right in their leases, but two did—again, the two utility companies bracketing the full range of 2.5 percent (5.5 to 6 percent effective) to 7.5 percent of market value. Both had short-term notice requirements (e.g., 60 days).
Normal Expiration with Renewal Rights to Improvements	At the end of a lease, the State of Idaho lease allows tenants to remove their improvements and restore the property to as close as possible to its natural condition, or to abandon the improvements which would then become the property of the state. Most of the comparables have a provision requiring the lessees to remove improvements and restore condition. Virtually all leases state that if such improvements are not removed, they become the property of the lessor. In reality, however, most get sold as the lease is assigned from one tenant to another.
Purchase of Improvements For Non-Renewal	If an Idaho lessee desires to renew a lease at its expiration, but is denied the opportunity to renew, the terms of the standard lease indicate that the lessee is entitled to purchase of the leasehold improvements by the state. This is an unusual protection afforded by the Idaho lease not noted in any of the comparable leases.
Landscape	The subject leases allow significant changes to landscape with lessor and local government approvals. Most of the leases rate comparables have a similar clause. One, however, having one of the higher cap rates found, allows only a 10-foot landscaped envelope around the building improvements, with the balance of the lot required to be maintained in a natural state.
Ability to Mortgage	None of the lessors would allow the lessees to subordinate the lessor's interest to a mortgage, but subject to the lessor's interest in the land, virtually all comparables allowed lessees to secure mortgage financing against their leasehold improvements. The limiting factor here is the term of the lease—if of too short a duration, lenders do not provide mortgage financing, and lessees are forced to rely on seller financing, or cash-only purchases.
Other Rights & Reservations	See individual comp discussion and table.

Discussion of the Comparables

In the course of our investigations of how other recreational lot leasing programs are administered, we compiled 10 land capitalization rate (rate of return) comparables. Some sources were willing to provide very detailed information on their programs, including actual or sample lease documents, while others were only willing to provide an overview of the program. The data was sufficient to bracket a range of 3.6 to 10 percent of market value of the land in fee simple title. The following discussion, and other information subsequently considered, can be utilized to bracket a narrowed range most applicable for the Payette Lake lots.

On individual summary tables, presented facing the discussion of each comparable, the reader will note that we indicate three different rates of return: The Nominal Rate, The Effective Rate to Lessee, and the Target Rate. The nominal rate is the rate named in the lease or openly promoted in the lease. As used in our discussions, the effective rate is that nominal rate plus any taxes on the land borne by the lessees—for consistency, all effective rates are compared on the basis of what the lessees pay, which may or may not correspond with what the lessor receives, depending on who pays the property taxes on land, if applicable. The target rate is either a rate or range of rates the lessor reports to be working toward, or rates he cites as being more indicative of free market rates than the policy or legislatively-restricted rates the lessor may be charging.

For example, in Idaho, the nominal rate of return for IDL leased lots is 2.5 percent of value. In many cases, the actual rate may be well below that. (Per Land Board policy adopted in the early 1990s, all leases were to be moved to 2.5 percent of market value over a 6 to 10-year phase-in. Unfortunately, such a phase-in only really works when values hold constant through the phase in period, which is rarely the case. The problem is compounded by the fact that by law, IDL has to notify lessees of proposed rent increases 6 months before they occur. Thus, if IDL wanted to charge rents of 2.5 percent for January 1, 1999, they would have had to notify tenants by July 1, 1998, at which time the 1998 assessed values were in the process of being determined. The only available assessed value was that for 1997. Thus, when the 1999 rent of 2.5 percent was to be adopted, it would have had to have been based on the 1997 assessed value, a valuation 18 months old in actuality, and two years old in name. Thus, there is always a lag in a changing market, which may make real 1999 rents of 2.5 percent on 1997 assessed values only 1.9 percent of 1999 market values.) Since we have no way to assess such a situation globally, for either the McCall lots or the comparables, our analysis begins with reported nominal returns.

Continuing the example, most leasing situations shown by the comparables have the lessor responsible for taxes on the land, and the lessees responsible for taxes on leasehold improvements. For approximately 20 of the State Dept. of Lands' lots—those in and around the Peninsula (adjacent Ponderosa State Park)—they are located within the McCall city limits, and no land assessments are calculated / no land taxes are applicable. For the remaining 215± lots, no taxes are applicable, but a sewer bond fee is charged for all lots located outside the McCall corporate limits, and thus in the Payette Lakes Sewer District. This fee is presently 0.000843955 times assessed value, or 0.08 percent (that is, less than 1/10 percent). As such, the effective nominal cost of leasing to the lessees is the 2.5 percent nominal rent, plus the 0.08 percent sewer bond fee, which can be rounded to an effective rate of 2.6 percent.

The target rate is applicable to those lessors who admit that, due to legislative, administrative agency, or corporate policy constraints, they are not able to seek maximum economic return on their land holdings, but who have made a conscious policy decision to keep abreast of prevailing market rates of return, and to perhaps even move toward them gradually. The target return, therefore, is where the lessor expects to be, or has come to believe the market would allow him to be, if income maximization was his company's/ agency's dominant policy goal.

Land Capitalization Rate (Rate of Return) Comparables

ID	Subject Leases
Lessor	Idaho Dept. of Lands
Type	State Cottage Sites
Contact	Bryce Taylor/Alvin Carr
Phone	208-334-0229
Fax	NA
Faxed Draft/Confirmed	NA
Property Type	Lakefront & Non-Lakefront Cabin Sites
Property Locations	McCall, Idaho
	77 Lakefront Lots, 115 Lake Access Lots, Total 232 Lots
Nominal Land Capitalization Rate	2.50%
Effective Cap Rate to Lessee	2.60%
Target Rate	2.60%
Escalations	Annual per Assessed Value (2 years prior)—by policy, not lease
Property Taxes on Land	Not Applicable—sewer bond fee only—0.8%
Property Taxes on Leasehold Impvts.	Lessee pays
Rights & Restrictions	
Use	Residential Purposes Only
Lease Term	10 years
Utilities Available	Electricity, telephone and sewer (lessees generally responsible for own water supply)
Access Year Round	Not Guaranteed, but generally
Use Year Round	Allowed
Lessees Can Expand Improvements	Yes, with lessor permission and compliance with county building dept., zoning requirements
Lessees Can Rebuild?	Yes, with lessor permission and compliance with county building dept., zoning requirements
Lessees Can Sell Leasehold?	Yes, with 10% of leasehold residual payable to lessor
Renewal	Current lessees (some in place for decades) have first right of refusal
Landscape	Subject to lessor approval
Able to Mortgage	Yes
Lessee's Right to Terminate	No
Rights to Leasehold Improvements	Lessee may remove if lessee restores lot at end of lease
Reservations	None noted
Water Levels	Fluctuates 5± feet.
Other	Lessor's annual rent increases not tied to assessed value or any other index per leases. Lessor will purchase leasehold improvements if they deny a compliant renewal application.
Comments	Leases nominally at 2.5% of market value, but in reality, the 2.5% figure is based on the assessed value for 2 years prior in the best of circumstances, and often is the lesser of 2.5% of the 1996 assessed value, or a 25% increase over the prior year's rent, which was based on 1992 assessed value. Substantial leasehold values are indicated, suggesting a rental program significantly below market rates of return.
Supplemental Comments	Minimum rents established for two lot classes are $720 for non-lakefront, $1,200 for waterfront lots. The minimum rent is now irrelevant, but in prior years resulted in lessees paying 4-5% for the lowest valued non-waterfront lots, while those with expensive lots might have been under 2% of market value.
	Cap Rate Comp 1

©1993-1998, All Rights Reserved.

The reader should note that we gleaned this information from direct contact with leasing specialists in most cases (contact names, phone and fax numbers are provided), and for most such contacts, we faxed back our tabulation of the information compiled from our interviews for their final verification of our interpretation and accuracy of the data reported.

The relevant clauses of the IDL lease are summarized on the page facing. Each of the comparable capitalization rate indicators is briefly discussed in narrative format, to supplement the facing tabulations. The comparables are presented in order of increasing effective economic return:

Land Capitalization Rate (Rate of Return

ID	Cap Rate Comp 1
Lessor	The Green Family
Type	Private Sector Cottage Sites
Contact	Jeanne & Ralph Green
Phone	208-263-5716
Fax	NA
Faxed Draft/Confirmed	No
Property Type	Lakefront Cabin Sites
Property Locations	Lake Pend Oreille
	18 Lots
Nominal Land Capitalization Rate	NA
Effective Cap Rate to Lessee	3.60%
Target Rate	3.60%
Escalations	Have CPI, but haven't enforced
Property Taxes on Land	Lessor pays
Property Taxes on Leasehold Impvts.	Lessee pays
Rights & Restrictions	
Use	Residential Purposes Only
Lease Term	5 years
Utilities Available	Electricity & telephone only (lessees have outhouses, septic, take water from lake)
Access Year Round	Yes
Use Year Round	Yes
Lessees Can Expand Improvements	Yes
Lessees Can Rebuild?	Yes
Lessees Can Sell Leasehold?	Yes
Renewal	Current lessees (some in place 40 years) have first right of refusal
Landscape	No limitations
Able to Mortgage	Yes
Lessee's Right to Terminate	No
Rights to Leasehold Improvements	Lessee may remove if restore lot at end of lease
Reservations	None noted
Water Levels	Fluctuates 5 to 10 feet.
Other	Lessor reports that these are not desirable shoreline properties--not sandy beaches. Also notes that leases have no architectural control, and county has no building permit requirement, so some improvements are literally shacks.
Comments	Lease on total dollars (all going to $2,000/YR upon renewal). Jack Young, SRA, appraised lots in 1993 for an average of $55,000, and advised on a rate of return of 4% ($2,200); because of limitations, lessors settled on 3.6%, and it has taken this long for leases to begin to expire to move rates up to the levels an appraiser suggested 5 years ago. Rates flat for 5 years, then theoretically adjus (CPI not enforced). Were renting at $1,400/YR in 1991, $1,400 to $1,800 in years between then and now. Lessors noted that the use as cabin sites is not allowed by zoning--is grandfathered, but the lots could not be sold individually unless rezoned.
Supplemental Comments	Lessors report that they have a very lax lease, and don't have provisions which ensure architectural control, homogenous uses. As a result, they feel that their program has gotten out of hand, and warrants a look at other leases for more tight language. They note that lots available to buy in their market are few, and feel that they could be getting a lot more rent were they aggressive.
	Cap Rate Comp 1

Land Cap Rate Comparable 1

This is a husband and wife team who have had family-owned land on lake Pend Oreille for many decades. They have a total of 18 cabin sites, and Mr. Green of the lessor party described the lots as lower appeal, non-sandy shoreline properties improved with low-cost improvements ($50,000 was cited as the upper end), many having no indoor plumbing. Reportedly, a residential appraiser out of Sandpoint, Jack Young, SRA, counseled the lessors that prevailing rates of return by states and the U.S. Forest Service ranged from 2.5 to 5 percent, and recommended they strive for 4 percent, which at that time (1993-1994) would have been about $2,200. When this opinion was rendered, all the leases had recently been renewed. Only recently, as leases came up for renewal, have the lessors had an opportunity to escalate rents. They have picked a round number of $2,000 per year, which equates to 3.62 percent on the prior appraised values, which the lessors don't feel to have changed much (assessed values are reportedly just under $1,200 per front foot).

This is the lowest nominal rate of return indicator known to us outside of government and public utility companies (Idaho Dept. of Lands, Montana State Lands Dept., and Minnesota Power range 2.5 to 3.5 percent presently).

The Pend Oreille leases are not particularly restrictive—the lessor reported a very hands-off management policy. The main considerations in comparing this rate of return with the potential in McCall are:

- Non-professional lessors, counseled based on public-policy-constrained rent comparables rather than policies of income-maximizing entities (even they acknowledge that they could raise rents considerably given the demand in evidence, but they have relationships with some families who have leased there for decades and that are of very limited financial means—effectively, they indicated that they are not overly concerned with the profit motive);

- Low management / overhead burden;

- Lessors who have owned the property free and clear for decades—presumably a very low basis;

- Relatively low cost, low appeal and low homogeneity of the improvements in the project, which affects not only underlying fee values (reportedly the Assessor values lots across the bay at $2,000 per front foot), but also lessee's perceptions of the project as a direct result of the lax leasing standards.

Therefore, this comparable is judged to be a poor indicator of the free-market return potential of the subject lots.

The lessee pays no taxes on land, so the nominal rate and the effective rate are one and the same.

Effective Rate:	3.6 percent
Comparability:	Inferior

Land Capitalization Rate (Rate of Return

ID	Cap Rate Comp 2
Lessor	Alabama Power
Type	Utility Corporation
Contact	Stell Benefield
Phone	205-755-4420
Fax	334-241-4386
Faxed Draft/Confirmed	Yes / Yes
Property Type	Reservoir Sites
Property Locations	5 different Alabama Reservoirs
	300± Lots
Nominal Land Capitalization Rate	4.00%
Effective Cap Rate to Lessee	4- 15+%
Target Rate	7.00%
Escalations	Annual CPI
Property Taxes on Land	Lessor pays
Property Taxes on Leasehold Impvts.	Lessee pays
Rights & Restrictions	
Use	Residential Use Only
Lease Term	5 years with effectively three 5-year renewal options
Utilities Available	Electricity, telephone (lessees have septic, water)
Access Year Round	Yes
Use Year Round	Yes
Lessees Can Expand Improvements	Yes, with Lessor approval and subject to local ordinances
Lessees Can Rebuild?	Yes, with Lessor approval and subject to local ordinances
Lessees Can Sell Leasehold?	Yes
Renewal	Current lessees have first right--no conflict bid.
Landscape	No restrictions noted
Able to Mortgage	No restrictions noted
Lessee's Right to Terminate	Anytime with 90-days' notice
Rights to Leasehold Improvements	If Lessor exercises 90-day termination, Lessor must buy leasehold impvts. If Lessee terminates or lease expires, Lessor has 30-days to buy or produce a buyer, and if not bought, Lessee has 90-days to remove and restore site.
Reservations	None
Water Levels	On half their reservoirs, water is drawn down seasonally; Lessor says Lessees find this desirable, as it gives them an opportunity to work on docks, shoreline improvements, and that leasehold prices are highest on those reservoirs, perhaps because river system is cleaner because of the period draw-downs.
Other	With all the options, they are able to market as 40-year leases. Leases set at 4% of market value, then index thereafter on CPI. Thus, substantial divergence from 4% is possible over time.
Comments	Lessor rep. says they had 3,000± lots in late 1970s, when they determined that they were not getting a fair market return. Made policy decision to move to market, and gave a purchase option to lessees, and actually sold about 2700 of them. Also made a hardship policy, whereby if lessee was elderly and this lease was their primary home, could freeze rent at current level for lifetime or until leasehold sold. Lessor reports that while annual rent only 4%, their yield is considerably enhanced by one-time buy-in, which is done by auction. Min. $1,000, highest $25,000, typical $5,000 to $15,000.
Supplemental Comments	When began selling in 1984, lots went as low as $7,500. Highest sale last year was $85,000. Values exceed $100,000. Half to full acre lots typically. Since 1990, 18 to 22 percent appreciation seen. Lessor says their desired return is 7% to 8%, but being a public utility, they can't be as aggressive as a private sector developer would be. Feels the valid comparision for a state is the state's cost of borrowing funds, plus a management fee to equate leasing cabin sites with alternative forms of revenue generation. Notes that their rates are tested against the 13.5% max rate of return allowed by PUC on book value (for properties recently acquired).
	Cap Rate Comp 2

©1993-1998, All Rights Reserved.

Land Cap Rate Comparable 2

Alabama Power has been leasing reservoir-fronting recreational lots for decades, and maintains one of the largest programs in the nation. In the 1970s, they determined that they were not keeping up with market rates of return, and thus made a policy decision to sell off as many lots as they could. They ended up selling about 90 percent of the lots they had (about 2,700 of 3,000) over the next few years.

The lessor now administers leases on about 300+ lots, on a 4 percent per year nominal rate of return, 20-year terms. They report, however, that their effective yield is considerably higher by virtue of the auctioning of new leases, and those former leases not renewed. For rights to lease, Alabama power auctions the leases at a minimum of $1,000, with typical auctions bringing $5,000 to $15,000 per lot (as high as $25,000). For example, assuming a $40,000 lot, and a $10,000 auction price, the nominal return of 4 percent has the equivalent cost to the lessee / yield to the lessor of 15.17 percent (it is akin to a lender loaning $40,000 for 5 years at 4 percent, but charging the borrower $10,000 in up-front loan origination fees for the privilege; the APR is about 15.2 percent). Obviously, the longer the tenant holds the lease, the lower the return—a 20-year hold rather than 5 drops the effective return to 7.50 percent; and this is only a scenario achieved on the new leases that go to auction—not on most leases—but it is a practice that helps the lessor bring up the overall return from the leasing program.

The lessor reports that their desired or target return (minimum) is 7 percent per year, but that being a public utility, they can't be as overtly aggressive as a private sector lessor/developer could be. The auction process allows them to achieve similar market returns on some of their leases, in a way not subject to organized lessee opposition.

As noted, the leases are on 5-year terms, with (3) 5-year renewals. Present company policy allows a right to start the lease all over, for a total of (8) 5-year periods (but only 3 renewals are granted in the lease). As such, the lessor reports that they are able to market their lots as on "40-year leases", which also has a downward influence on the rate of return (leases that are too short to mortgage or provide any assurance to a lessee would have a downward influence on what a tenant would be willing to pay, and one that is very long is considered more secure and safe to the lessor, which also has a lowering effective on rates, when compared to those of intermediate duration, say 10 to 15 years).

In comparing this comparable with IDL's Payette Lake lots, the following factors are noteworthy:

- Similar restrictions to IDL leases;
- 90-day lessee out-clause
- 90-day lessor out-clause
- If lessor exercises FERC out-clause, lessor has to buy leasehold improvements (this is in contrast to a similar FERC out-clause in the Pacific Power & Light lease, which says the lessor does not have such an obligation at terminate);
- Hardship policy—if the lessee can demonstrate that the leasing program poses an economic hardship, the lease rate can be frozen until the death of the lessee (effectively, a life estate) or until the leasehold interest is sold.
- Lessee can maintain a CPI-indexed rate for up to 40 years—creating substantial leasehold potential.
- Lessors do not believe they are achieving, nor does policy allow them to achieve, a market rate.

The nominal rate of this comparable is an inferior indicator of potential rental income for IDL lots. Based on information provided by the lessor, we calculate that 7 to 15 percent effective rent is attainable by the lessor, and is paid by new lessees, in some circumstances. The lessor's opined private sector target rate of 7 percent is the best indicator available from this comparable of a true market rate of return.

Effective Rate:	4 percent / 7 percent
Comparability:	Inferior / Plausible target under income maximization, but not actually being achieved

Land Capitalization Rate (Rate of Return)

ID	Cap Rate Comp 3
Lessor	U.S. Forest Service
Type	Federal Government
Contact	Paul Tittman, Chief Appraiser
Phone	202-205-1360
Fax	
Faxed Draft/Confirmed	Yes / No
Property Type	Lakes, Rivers & Mountain
Property Locations	Various in U.S.
Nominal Land Capitalization Rate	5.00%
Effective Cap Rate to Lessee	5.00%
Target Rate	7-9%
Escalations	Annual GDP Price Deflator Index, Max. 10% with carry-over
Property Taxes on Land	Exempt
Property Taxes on Leasehold Impvts.	Unknown
Rights & Restrictions	
Use	Residential Purposes Only
Lease Term	20 years
Utilities Available	All up to lessee—none provided by lessor
Access Year Round	Not necessarily--depends on location
Use Year Round	Allowed but again, access not guaranteed
Lessees Can Expand Improvements	With permission of lessor
Lessees Can Rebuild?	With permission of lessor
Lessees Can Sell Leasehold?	No—can sublease with permission but no assignment; a lessee can terminate, and a new permit can be issued to new permittee
Renewal	First right of refusal
Landscape	No limitations
Able to Mortgage	Yes
Lessee's Right to Terminate	None noted
Rights to Leasehold Improvements	Lessee may remove within 180 days of expiration of lease
Reservations	None noted
Water Levels	NA
Other	If USFS determines that continued lease as a cabin site is not desired and that they are not going to renew lease, must give 10 years notice. If terminate per the Public Interest clause, very limited notice is required, but lessor must buy or relocate leasehold improvements
Comments	Tittman says they have had 4 MAI studies in the 1990s: One surveyed 66 comps showing a range from 1 to 50% land return, and concluded 7%; another reported 21 comps ranging 2-11%, and concluded 6.5 to 8%; another reported 42 comps ranging 1 to 41%, and concluded 7-10%; and the results of the 4th were not available. Tittman reports that the USFS 5% rate dates back to 1842, and a decision of the General Land Office, based on the prevailing interest rate for land.
Supplemental Comments	Says 5% is too low for the restrictions imposed, but is well-entrenched. 9-10% is typical for land without significant encumbrances. Says 6-8% probably real market rate of return for govt. leased lots. Said that coincidentally, land cap rate conclusions by appraisers in studies USFS has commissioned (See "Comments") have trended about 1% above 30-year treasury yield rates.
	Cap Rate Comp 3

©1993-1998, All Rights Reserved.

Land Cap Rate Comparable 3

For this comparable, no specific leases or locations were discussed. Rather, we interviewed Mr. Paul Tittman, Chief Appraiser for the U.S. Forest Service, head-quartered in Washington, D.C., to elicit his take on the USFS recreational leasing policy now in place.

Mr. Tittman reported that the roots of their current 5 percent rental rate were in a decision of a federal agency, the General Land Office, back in 1842 (156 years ago). At that time, 5 percent was reported to approximate the prevailing rate of interest on land contracts of sale, when scarcity of supply of prime resources was much less an issue than it is today.

Mr. Tittman reported that USFS leases are no longer in touch with market return requirements—if they ever were—which he feels to be in the range of 6 to 8 percent for recreational land. However, he notes that political pressures are imposing an artificial ceiling on recreational rents. In recent years, the federal government's General Accounting Office (GAO) came to a similar conclusion, and the topic has been debated in homeowners groups, the press, and even the courts, ever since.

As support for his contention that 5 percent is not an economic rate of return, and that 6 to 8 percent is the range the USFS should embrace, Mr. Tittman cited four independent fee appraisers (private sector consultants) who have been commissioned to study the matter for USFS in the 1990s:

Analyst	Location	Conclusion
John Widdoss, MAI	South Dakota	7%
Maggie Love, MAI	Colorado	7-10%
John Frome, MAI	Wyoming	6.5-8%
Undisclosed	California	Undisclosed

The fourth consultant reportedly has a proprietary study which Mr. Tittman is not at liberty to discuss. The name given was Healey.

We sent a fax requesting information to the three fully-identified appraisers above, and two of these—Love and Frome—responded by providing some or all of their findings, summarized later in our report.

The USFS has 15,500 to 16,000 cabin site leases in the U.S. All are reported to be based on 15-year lease terms, at 5 percent of market value, with restrictions that, according to Tittman, are very similar to those of IDL's Priest Lake leases, with which he was familiar.

The relevant points of comparison are:

- Similar lease rights and restrictions;
- Longer lease terms
- Rate of return concluded by both high-up lessor representatives and the GAO to be below market rates, but one which is maintained due to considerable institutional inertia.

Mr. Tittman concludes that for leased land with minimal restrictions (private sector commercial leases), 9 to 10 percent is the appropriate rate of return, and for government leases, with restrictions and bureaucratic procedural requirements involved, the reasonable market range is 6 to 8 percent of fee simple value.

While the 6 to 8 percent opinion of market returns does not carry the weight of actual leases at these levels, as an opinion proffered by the chief appraiser of the largest single of leased lots in the country, and one supported by several independent studies, it warrants considerable weighting nonetheless.

We should note that the USFS refers to their agreements not as leases, but as "term use permits," the intent apparently being to avoid the connotation of leasehold interests. In fact, one cannot sell his permit to another permittee. He can identify a successor, and if that successor is approved, the first permitte is excused, and the other takes on a new obligation.

Effective Rate: 5 percent / 6-8 percent
Comparability: Inferior / Soundly reasoned and suggested to be appropriate for restrictions very similar to Payette Lake, but not actually being attained

Land Cap Rate Comparable 4

Tacoma Public Utilities (Tacoma Power) issues temporary permits for lake and/or reservoir-fronting land on three Washington bodies of water. One, a situation at a Lake Cushman, is a bulk lease to a private corporation at a "rate well below market." This corporation reportedly turns around and leases these lots to third parties at an undisclosed, but reportedly very high rate of return.

Mr. Ted Lyons, who administers this utility company's direct leasing program, reports that their agreements are unique in the granting of "limited revocable permission"—agreements which may be renewed for decades, but which contractually bind no one beyond 30 to 180-day periods.

The restrictions of these temporary, renewable use permits exceed those of Payette Lake leases in several respects:

- Lessor can terminate the lease without having to purchase the lessee's improvements;
- The lessees cannot construct "permanent" improvements—cabins or any structure with a concrete foundation;
- Despite out-clauses, the lessor reports they have never cancelled a permit without cause (that is, unless the lessee did not pay the fee).

The lessor has created a "Bundle of Rights Worksheet" which he has shared with us; it is a simple conceptual model which attempts to identify and allocate the rights inherent in fee ownership vs. a leasehold interest vs. the interest granted by their temporary permits, as follows:

Right	Description	Fee Simple (base)	Leasehold Has?	LH %	Permit Has?	Permit %
Usage						
	Use & Occupancy	25%	Yes	25%	Yes	25%
	Access	5%	Yes	5%	Yes	5%
	Development Rights	20%	Yes	20%	Limited	5%
	Subtotal	50%		50%		35%
Period of Use						
	Indefinite	15%	Substantial	15%	Less than 1 Year	5%
	Reversion	10%	None	0%	None	0%
	Subtotal	25%		15%		5%
Transfer Rights						
	Convey/Assign	15%	None	0%	None	0%
	Subtotal	15%		0%		0%
Encumbrances						
	Mortgage	7.5%	Yes	7.5%	No	0%
	Sub-Lease	2.5%	Yes	2.5%	No	0%
	Subtotal	10%		10%		0%
Total Value		100%		75%		40%

One can take issue with the weighting—for example, transfer rights (convey/assign) would appear to be one and the same with sublease under Encumbrances, and there appears to be no accounting for easements or other lease restrictions under Encumbrances (other than right to develop under Usage). Also, the period of use allowance the same as fee simple in the leasehold is probably too generous. Regardless, however, the point remains that the lessor views their typical use permits as conveying 40 percent of the bundle of rights of fee simple ownership, and then applies a 10 percent return requirement to determine rent. For example, land having a $10 per square foot value in fee title would have a "restricted use value", for lack of a better term, of $4 per square foot under the permit's restrictions, and would therefore be leased based on 10 percent of $4, or 40 cents per square foot per year, with the lessee also responsible for taxes on the land.

More important for the state leases we are trying to compare this comparable to, this lessor feels that if they were granting actual leases for a period of years, and the right to develop permanent structures (cabins), their required rate of return would be 75 percent of fee value x 10 percent, or 7.5 percent of fee simple value. This is identical to the rate actually being achieved by Pacific Power and Light—another utility company in the same state (See Comparable 7). Again, property taxes on land would be borne by the lessee, so the effective rate of an hypothetical lease comparable to the

subject properties would be something greater than 7.5 percent.

Two additional points are noteworthy: First, it is interesting to note that the lessor does not view their program as generating a 4 percent minimum return—rather, he views it as generating a 10 percent minimum return on the real value of a commodity that is 40 percent of fee simple land. The results are the same, but from the lessor's perspective, Tacoma Power is achieving a 10 percent return on the worth of the land.

The second point is that while the 40 percent of fee value scenario is the norm, there are situations in which they report leases based on land they determine to have 60 percent to 80 percent the worth of unencumbered fee ground, or a 6 to 8 percent cost of leasing to tenants, plus taxes.

Effective Rate: 4-8 percent nominal for 1 to 6-month permits / 7.5 percent plus taxes effective for leases

Comparability: The 7.5 percent + effective rate is well reasoned, but there are no actual situations of the theory being put to the test of the market

Land Cap Rate Comparable 5

Minnesota Power has one of the oldest, largest and most well-known recreational leasing programs in the country. They have an Internet web page explaining the program, complete with a real estate link to actual properties offered for leasehold sale. The program has been in place since the 1920s—about the same amount of time as the Idaho program.

This public utility company makes very clear that theirs is more of a public relations program than a profit center. They note that good press from having such a program, and having lessees be their "eyes and ears" at their various storage reservoirs is at least as important from a company policy perspective as the economic return of the program. In short, this is not a division operating under the normal profit motive. After all, the lots were not created to start a leasing program—they were a by-product of a hydroelectric storage program. As we have found through our research, some utility companies have charters which embrace such programs as being good for the company's image (Minnesota Power, Alabama Power, etc.), some have adopted a policy which states that if the company is going to bear the administrative costs of having a leasing program, it is going to be a profit center (Pacific Power and Electric), and others are trying to get out of the business, in much the same way many states are trying to scale it down by selling the lots (Pacific Gas & Electric). Most power and timber companies have stayed away from the leasing of recreational lots altogether, seeing the burden as being greater than the politically moderated return (compared to other investment opportunities), despite vast land holdings which in theory could be put to higher and better uses.

This particular program in the not too distant past was based on a 5 percent of value rental rate, with the lessor paying taxes on the land. In 1992, in the face of rapidly escalating values and taxes, the program was changed to 2.5 percent of value, with the burden of taxes shifted to the lessees. There was some talk of this being an interim program, with the eventual goal to go back to 5 percent, leaving the tax burden shifted to lessees, but the current administrators report no such plan.

The program includes 1,200+ lots on 8 separate reservoirs and rivers. Reportedly, property taxes are relatively high, with effective rental rates to tenants reported at 5.5 to 6 percent (implying tax rates of 3 to 3.5 percent). The leases are on 25-year terms. Lessees create and maintain their own access, and year-round use is prohibited. Like virtually all the utility company leases on reservoirs (as opposed to state, federal or private sector leases on natural lakes), the cabin site leases are

subject to FERC (Federal Energy Regulatory Commission) licensing of the lessor's dams. That is to say, if the lessor loses its FERC license, or FERC for some reason wants the leasing program scaled back, the lessor can break the lease with 90-days' notice, without any obligation for the leaseholders' improvements. (Several utility company officials we spoke with indicated that, because of environmental pressure relating to fish habitat, and energy deregulation, non-productive dams that would have previously remained anyway are much more likely to be demolished, to cut the utility company's losses.) Such termination is unlikely, but it is an element of risk that would have at least theoretical downward pressure on rates of return.

The lessors report that, were they a private corporation operating under the profit motive rather than a public utility operating under the scrutiny of a public regulatory commission, they could easily achieve 2 to 3 times their current nominal rate of return of 2.5 percent (5 to 7.5 percent to lessor, 8 to 11 percent to lessee inclusive of taxes).

Also, like Alabama Power, Minnesota Power reports that their nominal return is misleadingly low. They reportedly auction off new leases periodically, and according to those administering the program, it is not uncommon to get 80 to 90 percent of fee simple land value. This is rather hard to believe, but it attests to the lessor's contention that the rates are well below market rates of return. For example, given a $50,000 lot with a 2.5 percent nominal rental rate, on a 25-year term, an 80 percent up-front payment to the lessor for the right to lease thereafter at anticipated below market rents would result in a yield to the lessor/cost to the lessee of 27.07 percent! (The result on a $450,000 lot, all other factors held constant, would be the same—27.07 percent; a 90 percent leasehold price rather than 80 percent would result in a yield of 54.27 percent over a 25-year term.)

Obviously, this only occurs on the granting of a new lease, but again, it clearly helps to boost the program's overall economic performance without globally raising rents and invoking the wrath of the media and homeowners' organizations.

The relevant issues are:

- A motive other than profit maximization;
- Substantial leaseholds indicative of rates well below market;
- Lessees pay taxes on land, which reportedly adds 3 percent+ to the nominal rates, so minimum effective rent to lessee is 5.5 percent.

Again, for consistency, we are concerned with comparing the typical effective rate paid by the lessees, inclusive of any taxes on land borne by the lessees, and in this case, the reported effective rate is 5.5 to 6 percent, and the lessors feel that a private sector lessor could add 2.5 to 5 percent to that rate of return (5 to 7.5 percent nominal, 8 to 11 percent effective, inclusive of taxes).

Effective Rate:	5.5-6 percent effective / 8-11 percent effective is lessor's opinion of market
Comparability:	Below market because of non-profit motive, FERC risk / Plausible but untested in the marketplace

Land Cap Rate Comparable 6

Pacific Gas & Electric (PG&E) has been in the leasing business at various California locations for years. They have less than 200 remaining lots at this time. For years, they have been trying to phase out the program because political and emotional pressures when dealing with peoples' homes makes achieving economic returns more trouble than it is worth. In an effort to make the lots more liquid, they have dropped the lease term from 5 and 10 year terms which formerly prevailed, to only 3 years. This has made it all but impossible for lessees to get any financing on their improvements. The lessor reports that to maintain the program, they have determined that they need to move toward a target return of 7 to 10 percent, but they admit that presently, they are achieving 5 to 7 percent typically. Thus, the immediate goal of the lessor is to move remaining leases to 7 percent, which they report to be a fair minimum rate of return for the restrictions and short terms now being offered.

The relevant factors for comparison are:

- 3-year terms—difficult if not impossible to finance improvements;
- Seasonal access / use in some locations, year-round in others;
- Lessees provide own utilities
- Subject to FERC licenses

Effective Rate: 5 percent-7 percent (lessor pays taxes on land, so nominal and effective rents are equal)

Comparability: More restrictive than subject leases—particularly in duration and seasonal use. Sets lower end of market range.

Land Cap Rate Comparable 7

PacifiCorp, d.b.a. Pacific Power & Light, leases approximately 96 recreational lots on 3 reservoirs in Washington and Oregon. They refer to themselves as a private sector utility company, and one that would not be in the cottage site leasing business if they were artificially restricted from maximizing their economic returns. They offer leases on 20-year terms, with the lessees providing and maintaining all sewage disposal and water systems. No access to the lots is guaranteed—lessees maintain their own roads. The leases are subject to FERC licensing, and there are strict limitations on building improvements: The lessor has the final say in the approval of building designs and materials, and man-made landscaping is restricted to a 10-foot ring around each structure (all else must remain in a natural state). Interestingly, the lessor reportedly has no obligation to purchase the leasehold improvements if they elect to terminate the lease. All lots have an easement along the waterfront for public access, and such access cannot be denied by the lessees. The only significant concession to the lessees is a 60-day right of termination.

The fee simple value of the lots was determined by appraisal, last done in the early 1990s by David Groth, Palmer, Groth & Pietka of Vancouver, WA. In advising the lessor as to rental rates, the appraiser noted that the State of Washington was leasing land to private individuals at 8 to 10 percent returns, the Washington State Dept. of Natural Resources was leasing at 9 to 10 percent; private sector developers were leasing commercial land for 10 to 12 percent; and the U.S. Forest Service and Minnesota Power were leasing at 5 percent (recall MN Power was at 5 percent prior to 1992)—the appraiser noted that the 5 percent rates reflected "factors other than purely economic considerations"—a contention which we have confirmed as being reflective of the opinions of these lessors as well.

Ultimately, the lessor determined that their target rate of return on straightforward net leases was 10 percent per year, and that in recognition of the rather strict limitations of their cottage site leases, a 25 percent discount was reasonable. Thus, the lease rates were set at 7.5 percent.

A copy of an actual PacifiCorp lease was provided us by the lessor, and it confirmed that this is the best direct indication of an arms-length lease rate of return for an entity putting maximization of economic return ahead of public policy considerations. Moreover, it directly confirms the contention of lessors at other government and utility concerns (Minnesota Power, Alabama Power, Pacific Gas & Electric, the U.S. Forest Service) that 5 percent to 11 percent rates of

return are reflective of market levels, and that their own rates of return are artificially capped by policy. The remaining lease comps add further support to this contention.

Relevant considerations include:

- Strict regulations;
- No access or year-round use guaranteed by lessor;
- Lessees own and maintain their own water systems;
- Leases subject to FERC approval;
- Tenants may cancel with 60-day notice.

The lessor pays taxes on the land, so the effective rate to the lessee is the same as the nominal rate.

Effective Rate: 7.5 percent

Comparability: Very good, subject to the influence (if any) of disparate value ranges for the lots

Land Cap Rate Comparable 8

Several studies and reports we read in the course of our research reported that some states, like Arizona, Washington and Alaska were achieving 8 to 10 percent returns on their leased recreational properties, while others, like Idaho and Montana seemed to struggle to achieve 2.5 to 3.5 percent. For no particular reason, other than that we had been provided a specific contact within its State Lands Department, we surveyed Arizona for their policy.

Mr. Jim Gross reported that Arizona does indeed have a limited cabin site lease program on various lakes and reservoirs, but that theses types of leases have proved over the years to be "troublesome" and as such, the state sells the lots when opportunities to do so present themselves. The goal is to put state endowment funds into more productive commercial investments.

The remaining recreational lots leased in Arizona are reported to be on maximum 10-year terms, based on a 9 or 10 percent annual return of appraised value, with the landlord paying any taxes, if applicable, on the land. Thus, the effective rate to the lessees is the 9 to 10 percent nominal rate. Rights and restrictions were reported to be similar to those of the Idaho Dept. of Lands.

Effective Rate: 9-10 percent

Comparability: Reportedly similar, but full scope of rights and restrictions unknown, as lessor did not respond in detail, or provide a sample lease agreement for our review

Land Cap Rate Comparable 9

As was discussed in the analysis of Comparable 7, in the early 1990s, David Groth, MAI, undertook a valuation and rent study assignment for Mr. Carl Barnett of PacifiCorp. Prior to that, in 1989, Mr. Groth did a limited appraisal for a homeowners association of cottage sites leased from a private corporation operating in north central Oregon. The lessees leased approximately 66 lakefront lots on a body of water known as Langdon Lake.

Reportedly, the fee simple values of the individual lots was estimated by two separate appraisers, and a 10 percent rate of return was then utilized as the rent basis. Some lot owners elected to go to mediation to challenge the basis, but it is our understanding that most remained at 10 percent.

In an attempt to verify the information compiled by Mr. Groth, and update it now 6 years later, we were put in contact with Mr. Bob Mautz, board member and attorney for the Tollgate Co., lessors for Langdon Lake. However, after some deliberation, we received a fax that the board had voted not to disclose information or financial aspects of their leasing program.

We thus rely on the limited information provided us by David Groth, MAI. Again, however, Mr. Groth did some appraisal work for these homeowners, so the source is judged to have first hand knowledge of the rate of return being achieved.

Relevant considerations include:

- Similar Northwest location;
- Private corporation as lessor;

Effective Rate: 10 percent
Comparability: No recent confirmation of terms, restrictions, etc.

Land Cap Rate Comparable 10

Mr. David Brooks, MAI, a South Carolina based appraiser and consultant, was found to be working on a large valuation project involving lakebed valuation, moorage/dock and lake access rights in the eastern U.S.

He was kind enough to share in draft form the data he had compiled to-date, and most was for waterway and moorage fees, not cabin site leases. However, Mr. Brooks did have similar information to our own on Minnesota Power, and this comparable for lake and reservoir cabin sites in New York administered by the New York Thruway Authority. Information on the program was limited, and our only confirmation was the appraiser who provided it.

It would appear that this entity leases 300 to 400 cabin sites on Kayuta Lake and Hinckley Reservoir in New York, at a rate equal to 10 percent per year of fee simple land value, plus $50 per year if dock rights are desired. The scope of rights and restrictions inherent in the leases, and their term of use, are unknown to us. Thus, this must again be considered an upper end indicator of the potential of the subject lots.

Effective Rate:	10 percent
Comparability:	Indeterminable

Market Effective Rental Rate Summary

Identity	Lessor Type	Effective Rates to Lessee	Rate Type	Comments
Comp 1	Private Party	3.6%	Actual	Inferior
Comp 2	Power Co.	4.0% 7.0%	Actual Opined	Inferior Plausible but untested
Comp 3	Federal Govt.	5.0% 6.0%-8.0%	Actual Opined	Inferior Plausible but untested
Comp 4	Power Co.	4.0%-8.0% 7.5%	Actual Opined	Most at lower level, inferior rights Plausible but untested
Comp 5	Power Co.	5.5%-6.0% 8.0%-11.0%	Actual Opined	Minimum threshold of market Plausible but untested
Comp 6	Power Co.	5.0%-7.0%	Actual	More restrictive leases, set minimum threshold
Comp 7	Power Co.	7.5%	Actual	Best overall indicator
Comp 8	State Govt.	9.0%-10.0%	Actual	Full scope of rights, restrictions unknown
Comp 9	Private Corp.	10.0%	Actual	Dated information; full scope of rights, restrictions unknown
Comp 10	State Govt.	10.0%	Actual	Full scope of rights, restrictions unknown

The data reflects the full spectrum, from 3.6 to 10 percent, with good trending in the middle of the range, at 5 to 7.5 percent, and this range is bracketed by actual lease situations conveying similar rights and restrictions (the U.S. Forest Service at the low end of the range, and Pacific Power and Light at the upper end of the range).

A rate conclusion could be reasonably defended anywhere in this range. A rate conclusion below this range is considered indefensible unless such rate is derived by considerations other than economics. A conclusion above this range is possible, but not enough information was available to assess how often such rates are attained, or what rights and restrictions are inherent.

For secondary support for this narrowed range—5 to 7.5 percent—other means of estimating the appropriate rate are briefly considered: Opinions of other market participants, and mathematical extraction models.

Other Rate of Return Indicators

Union Pacific Railroad

Mr. Bob Gloodt, Manager of Appraisals, Union Pacific Railroad (402-997-3600) reports that UPRR leases everything from corridors for utility lines and recreational uses to entire towns built on railroad land, for temporary use up to 20-year terms, on a 13 percent annual return. This figure is made up of a 10.5 percent annual return on the land (base rate) and a 2.5 percent allowance for taxes. Railroads apparently are not assessed property taxes, but instead are assessed transportation and other taxes and fees, which are passed on to lessees in the form of the 2.5 percent allowance. Mr. Gloodt notes that this component of their rate is controversial, as there is no direct way to determine if taxes would be applicable to particular parcels, but he also reports that they do not deviate from this return on their leases regardless.

Mr. Gloodt reports that the prevailing perception of a 10 percent land cap rate for real estate is for a situation where a single lessor has a single (or very few) parcels to lease, and then only on a triple net basis. When the lessor is a large organization, with infrastructure costs, and there are multiple properties leased, overhead comes into play, and it is no longer a net situation. Their rates build in management / overhead and taxes, totaling 2.5 percent on top of the 10.5 percent benchmark rate.

Burlington Northern Railroad

Mr. Ray Flaherty of Catellis Real Estate (206-748-9421) reports that Burlington Northern-Sante Fe Railroad has leased and permitted land throughout the northwestern U.S. and Canada, including land on various Alpine lakes leased for cabin and related recreational uses. No specifics were provided, but Mr. Flaherty, who manages real estate for BN, reports that the prevailing annual "hurdle rate" of return for such leases is 12 percent. Similar to UPRR, Mr. Flaherty noted that this includes allowances for management and taxes borne by the lessor on their operations. He reports that the leases are on a "month-to-month basis indefinitely", and that they are "full of restrictions" on use.

University of Minnesota Study

In 1984, a graduate student by the name of Christopher Klyza did a detailed study of leasing practices for cottage sites on Minnesota's numerous lakes and reservoirs. In addition to surveying numerous counties within Minnesota, Mr. Klyza polled various state agencies, the US Forest Service, Minnesota Power, and the Minnesota Chippewah Tribe, and reported the following rates of return at that time:

Category	Lessor	Rate	Basis
States			
	Minnesota	5%	Appraised Value
	Illinois	Flat Fee	NA
	Louisiana	Bid System	
	Alaska	8%	Appraised Value
	Maine	8%	Assessed Value
	Arizona	10%	Appraised Value
	New Mexico	Flat Fee	
Federal			
	USFS	5%	Appraised Value
Other			
	Minnesota Power	5%	Appraised Value
	Chippewah Tribe	7%	Not Noted

As our intent is to focus on private sector leasing policies as removed as possible from the moderating effects of the political process, we elected not to follow up with most of these agencies. We did confirm the policy of the Lands Department in Arizona at 9 to 10 percent (See Cap Rate Comparable 8), and the policy of the U.S. Forest Service at 5 percent (See Cap Rate Comparable 3).

Perhaps more important than his rate summary, Mr. Klyza, now Professor Klyza (Associate Professor of Political Science and Environmental Studies, Middlebury College, Middlebury, VT), lucidly brought to light some important issues with respect to determining a fair rate of return for a given situation. Some of the highlights of his detailed study are summarized following:

- Klyza notes the obvious statement that when prices paid for leasehold estates exceed the value of the leasehold improvements, the market is acknowledging that leases are below market (the higher the price paid for the privilege to take over the lease, the more rents diverge from a true economic return);

- He notes that where contract rents are below market rents, escalation to market will be difficult for those on low or otherwise fixed incomes, but he also stresses those assessing the situation and setting policy need to realize that recreational homes are not part of a wealth redistribution or welfare program. Quoting from Klyza's study:

"The retirees and low income lessees were not selected at random or by lottery to enjoy a summer home on state property; these individuals are enjoying a privilege not available to other low income residents in the state. These lakeshore leases do not represent a necessity such as food or shelter, but rather a luxury

item. Most individuals, not just low income individuals, cannot afford vacation homes. The low income individuals who presently hold leases have enjoyed this luxury for ten or more years and if they must now surrender this lease, so be it. This state, nor any other state, does not have a policy designed to make sure every individual or family has their own second home. A just state policy dictates that no individual within a group obtain special privileges if the other individuals within the group do not have an equal opportunity to obtain such privileges. If the state desires a number of its lakeshore leases to be held by low income persons, it should make this an explicit policy." (Page 58).

Klyza suggests that, if second homes were a constitutional right, most of us would have them, and the truth is, most of us don't have them because they are in limited supply to begin with. Limited supply drives prices up in a free market, but when prices or rents are artificially capped by political processes, they become a subsidized housing program. He goes on to note that the lower rates are at the expense of the state's taxpayers and the state's public schools, which would have had more income generated from the trust lands had those lands been leased at market rates of return.

- The Consumer Price Index (CPI) is an inappropriate index; rather, a local index is required to a) avoid subsidy when local real estate escalates well beyond the rate of general inflation (which has certainly been seen in McCall over the past decade), and b) avoid large percentage increases necessary to make up the different at renewal.

- The argument that values / lease fees should be lower because the lessees improved the lots does not hold water because:

  a) The lessee (or his predecessors) has reaped the benefits of his efforts (or those of his predecessors) by having enjoyed subsidized recreational property, possibly for decades; and

  b) If the lessee is not willing to pay a market rate of return on the property as it exists, it is very likely that due to scarcity, someone else will. Market value and market rent should not be based on individuals or historical events—rather, it should be based on present market perceptions of the future (anticipation), substitutable options and scarcity (supply and demand), and other accepted economic principals—including what another prudent buyer/lessee would pay for the infrastructure and rights in place without regard for who paid for or installed them in the first place.

Ultimately, Klyza concludes that fair market rents were in the range of 7 to 10 percent per year, but that for public policy reasons (ensuring public access to recreational opportunities,

for example), a state may desire to charge something less, but should not accept below 5 percent. He also notes that his conclusions for Minnesota's situation reflect an acknowledgment that on leases of state land in Minnesota, lessees pay taxes, which is not the case in our state or most others. By logical extension, therefore, in a situation where lessees don't pay taxes on land, the rate they bear could be higher. He ultimately concludes that perhaps more important than the rate of return is ensuring that whatever rate is targeted is consistently achieved by means of annual re-indexing of values (and rents) to market levels, so that no subsidies accrue in periods of rapidly rising values, as was seen in McCall in the late 1980s and early 1990s.

We contacted Mr. Klyza in the course of our investigations, to see if he had ever had occasion to update his study. He had not.

Montana Studies (Bioeconomics, Inc.)

In the course of our market research, we reviewed detailed studies done by Mr. John Duffield et al., Bioeconomics, Inc., of Missoula, Montana, for the Montana Department of State Lands, as follows:

- "Final Report: Economic Analysis of the Values of Surface Uses of State Lands", Task 2, Analysis of Cabin Site Lease Rates, John Duffield, January 1993;
- "Summary Report: Economic Analysis of the Values of Surface Uses of State Lands", John Duffield, Bruce Anderson, Chris Neher, February 1993;
- "Final Report: Survey of Western State Land Managers", James Boyer, John Duffield, December 1992.

In his cabin site lease rate study, Duffield notes that the State of Montana Department of State Lands at that time administered 618 cabin sites at various Western Montana lakes, at 3.5 percent annual return on market value, on 15-year leases with 5-year reappraisals, with leases fully assignable, lessees having first right of refusal for renewal.

Among his observations and conclusions were the following:

- "From the standpoint of the [state] school trust, the rental rate should be at a fair market level." [Executive Summary]
- Duffield cites Thomas Stevens, a Missoula-based appraiser, as doing several market rent appraisals and concluding that the market rate of return ranged from 8 to 12 percent, with most in the narrowed range of 10 to 12 percent annual return. He reported that Mr. Stevens recommended a 10 percent annual return for cabin site leases.

- Duffield reports that Montana tried in 1988 to go from a flat fee system of $25 to $50 per year, to 5 percent of market value, and due to lessee outcry, the Legislature quickly backed down to a 3.5 percent annual return.

- Duffield proposes a simple formula which simply indexes leasehold sales to the fee value of the land, derives a ratio of same (for example, that lessees are paying 45 percent of the fee value of the land for the right to lease that land going forward at what are expected to be favorable rental rates), and uses that ratio relative to the contract rate of return (in Idaho 2.5 percent) to calculate the implicit market rate of return. This method is worthy of elaboration at length, and such will be undertaken in a separate section of the report entitled Implicit Rates of Return.

In his "Summary Report: Economic Analysis of the Values of Surface Uses of State Lands", February 1993, Duffield opines:

- That Montana should get a 6 to 10 percent return for its cabin site leases;

- That the state should sell non-productive lands;

- That the state should consolidate its ownership into contiguous, manageable units;

- That the state should utilize sale proceeds to fund a land bank; and

- That the state should get into commercial land leasing.

Maggie Love, MAI
Market Rent Study

In August of 1991, Maggie Love, MAI, a private sector appraiser, conducted a market rent study for Mr. Dave Darmon, Chief Review Appraiser, USDA Forest Service, Lakewood Colorado. The request was for a survey of private ground leases throughout Colorado, and the estimation of a target range of return for ground leases in National Forest land. The following summary was offered:

Lease #	Start	Term	Rate as % of Land Value	Location	Comments
1	6-79	30	1%	Grand Lake	Trailer Park
2	6-91	1	1%	Dolores County	Grazing
3	6-91	1	1%	Dolores County	Grazing
4	6-77	101	3.5%	Boulder	Retail
5	10-86	5	4.5%	Crested Butte	Removable Office
6	1-91	6	6%	Crested Butte	Removable Office
7	1977	15	7%	Cortez	Taco Stand
8	1972	100	7%	Cooper Mtn.	Condos
9	1976	20	7%	Granby	Gas Stn.
10	1978	1	7%	Buena Vista	Car Wash
11	7-84	50	7%-8%	Glenwood	Wendy's FF
12	8-89	5	7%	Denver	Parking Lot
13	5-83	85	7.5%	Eagle County	Condos
14	1972	98	8%	Vail	Lodge
15	1973	99	8%	Vail	Condos
16	7-82	99	8%	Cortez	Single Fam. Res.
17	1-91	1	8%	Curry Cnty., NM	Farms
18	4-79	70	9%	North Glen	Retail
19	1985	15	9%	Durango	Greenhouse
20	1-65	55	10%	Durango	Motel
21	1968	40	10%	Aspen	8 lessees, various uses
22	1977	15	10%	Durango	Dairy Queen
23	4-77	99	10%	Avon	Condos
24	4-80	50	10%	Boulder	Retail
25	10-80	99	10%	Telluride	Retail & res. Condos
26	1-82	40	10%	Glenwood Spgs.	Restaurant
27	1-86	60	10%	Boulder	Retail
28	11-90	5	10%	Westminster	Parking Lot
29	10-84	10	12%	Denver	Retail
30	6-81	30	12%	Canyon City	Bank
31	1973	20	13%	Wheatridge	Car Wash
32	1958	100	14%	Boulder City	63 lessees, residential
33	1985	10	15%	Denver	Car Wash
34	1-95	30	17%	Commerce City	Pizza Hut
35	5-82	24	20%	Denver	Car Wash
36	1987	10	23%	Denver	Car Wash
37	1-81	15	41%	Aurora	Car Wash
Non-Specific					
38	1960s	30 min.	5%-7%		US Post Office
39	1990s	30 min.	10%		US Post Office
40	1986	20	6%	Denver	Medical Office
41	1990	20	6%	Aurora	Medical Office
42	1960s-1990s	Yr.-to-Yr.	10%-13%		UPRR
43	1991		10.8%		Chrysler

Ms. Love concluded no relationship among date of lease, type of use, or length of lease and rate. She did note a strong trend between supply and demand vs. rate. For example, grazing rates were lowest, with land in large supply and little

potential for a higher and better use. Site specific uses, like car washes and restaurants, fetched the highest returns.

For all the data, the rates ranged from 1 to 41 percent of land value. Interestingly, included within her array were 6 residential comparables representing 75 individual leases of condominiums and single family residences, bracketing a range of returns at 7 to 14 percent. Tight trending was noted from 7 to 12 percent, and most (78 percent) were in the narrowed range of 7 to 10 percent per year, which was this appraiser's conclusion and recommendation to the U.S. Forest Service.

John Frome, MAI, ARA
Market Rent Study

Similar to the ground lease study done by Maggie Love in 1991, John Frome did a study in Wyoming in 1992. He provided only a summary of his comparables, which he noted do not include any "residential type comparables":

Lease #	Start	Term	Rate as % of Land Value	Location	Comments
1	1987	1	2%	Grass Creek	Pasture
2	1973	20	4%	Thermopolis	Industrial
3	1989	1	4%	Afton	Crop
4	1989	1	4%	Crop	Pasture
5	1983	20	6%	Afton	Mini-Mart
6	1977	30	6%	Riverton	Office
7	1974	20	6%	Thermopolis	Industrial
8	1988	5	7%	Powell	Parking Lot
9	1977	100	8%	Afton	Motel
10	1979	100	8%	Afton	Café
11	1983	20	9%	Cody	Café
12	1982	30	10%	Jackson	Motel
13	1983	20	10%	Cody	Retail
14	1969	40	10%	Jackson	Post Office
15	1982	20	10%	Jackson	Mini-Mart
16	1983	16	11%	Jackson	Mini-Mart

Five other comparables not shown here were tabulated, but they were not private-sector leases (the were Bureau of Reclamation leases, at 3 to 6 percent.) The range of the private sector leases was 2 to 11 percent, with 4 to 10 percent typical, and like the Colorado study, 10 percent was the most typical rate. According to Mr. Tittman of the U.S. Forest Service, Frome's conclusion and recommendation to the Forest Service was 6.5 to 8 percent.

Boise Land Cap Rates

Solely for purposes of comparison with other metropolitan areas, we note that land cap rates in Boise and nearby Meridian, Idaho typically trend 9 to 12 percent, with 10 percent by far the most common situation. As such, the 10 percent return benchmark for commercial land leases appears to be the most common point of reference for a ground lease

whether one is talking about Denver Colorado, Boise Idaho, or Afton Wyoming.

There is no particular reason to believe that, were there a rental market for land in McCall, the rate would vary significantly from this benchmark—at least for commercial uses.

Market Effective Rental Rate Summary

Identity	Context	Effective Rates to Lessee	Rate Type	Comments
John Frome, MAI	Rent Study for USFS	6.5-8%	Probable	Opinion based on research of actual leases, but none residential
MT Bioeconomics, Inc.	Duffield Studies	6-10%	Probable	Opinion based on research and mathematical modeling
Univ. of MN	Klyza Study	7-10%	Probable	Opinion based on research (5% absolute minimum)
Maggie Love, MAI	Rent Study for USFS	7-10%	Probable	Opinion based on research of actual leases, including residential
Burlington Northern	Railroad	12%	Actual	Reportedly similar situations, but specifics unknown
Union Pacific	Railroad	13%	Actual	Very different situations—applicability uncertain

The data reflects a higher range, with individual conclusions from 6 to 13 percent, with good trending in the middle of the range, at 6 to 10 percent.

Calculation of Implicit Rates of Return

In his study of cabin site leasing practices, John Duffield, an economist with Bioeconomics, Inc. offered the following simplified formula, which we refer to as Method 1:

$$i = R_O (1-L/V)^{-1}$$

Where:

i = Market rate of return
R_O = Contract Rate of return
L = Leasehold value
V = Fee simple value

In application, i can be considered R_M, or the market rental rate, R_O can be considered R_C, or the contract rental rate, L can be considered the residual price of the leasehold, and V can be considered the fee simple assessed value of the land.

The whole point of this formula, and others proffered by Duffield, is to analyze leasehold sales: To the extent that lessees are paying anything more than the depreciated / contributory value of the former tenant's building and site improvements, the market is acknowledging rents that are below market rental return levels. When market and contract rent are at parity, Tenant B will pay Tenant A the value of Tenant A's building and site improvements, and Tenant B will take over the responsibility for the lease. No additional money should change hands.

When contract rent exceeds market rent, Tenant A may have to give up (subsidize) some or all of his investment in his improvements to entice Tenant B to take over the lease.

In the case which prevails in McCall and many of the comparables we investigated, when the contract rent is a good deal below market, Tenant B will not only pay Tenant A for the value of his leasehold improvements, but will pay a premium for the privilege to take over the lease at rates he perceives to be, and anticipates to remain below-market (i.e., if the lessee believes the lease assumption to be more favorable than leasing or buying elsewhere).

Duffield's contention is that the higher the ratio of the leasehold premium (L) to the fee simple lot value (V), the greater the implicit delta between the contract rate of return (R_C) and the fair market rate of return (R_M). This and other formulas Duffield proposes, which have been relied upon by state government agencies and Montana District Court, seek to extract (calculate) the implicit market rental rate of return. In deciding whether to put the models he offers to the test of McCall leasehold sale data, we contacted Professor Randall Rucker, Montana State University—Bozeman, Dept. of Economics / Ag. Economics; Rucker had done a study for the Canyon Ferry Recreation Association (a group of 265 cabin site lessees who were contesting rent increases in their project near Helena), and was familiar with the Duffield reports. We asked Dr. Rucker if the logic was sound. Rucker reported that he had not studied the Duffield equations with any detail, but had asked one of his higher level grad students who co-authored the Canyon Ferry study, to do so. The conclusion was that the model was essentially sound. Like any economic model, however the equations assume rational behavior of a well-informed market, and buyers of recreational property don't always conform to this expectation (they sometimes pay nearly all, or even more than, unencumbered fee simple value for restricted leasehold rights of use and enjoyment).

Duffield explains the theory behind the model is that the leasehold payment to the seller plus the present value of anticipated future rent to the state is equal to (or approximates) fee simple market

value (appraisal theory substantiates this, with the equation Leasehold + Leased Fee = Fee Simple) In Duffield's words:

> *"[S]ubstantial sales prices for lease transfers mean that the policy of below market contract rent does not make the leases more affordable for individuals who do not happen to hold a state cabin site lease and would like to. These individuals [who purchase an existing lessee's leasehold] are being charged a premium (the leasehold value) to obtain the leases. In other words, new leaseholders end up paying market value to hold state leases – but a good share of the total payment over time goes to the current [selling] leaseholder (in the form of the lease assignment sales price) rather than to the state. Similar results hold for Idaho data."* [Page 4]

Duffield notes that in most states, including Montana, the value of a leasehold is calculated as sale price less value of the leasehold improvements per assessed value. For example, if one lessee sold his interest to another for $50,000, and $30,000 of that was the theoretical value of the home and site improvements per assessed value, $20,000 would be the residual value of the positive leasehold. Duffield notes that in Idaho, a second deduction is sometimes made for personal property, such as furnishings and fixtures, but also notes that lessees may escalate the allocation to this category, possibly in an attempt to make it appear that leaseholds have less value than the actually do.

As shown on the facing spreadsheets under the column entitled Method 1 Implicit R_M, the first equation shows by year for the past 6 fiscal years the following implicit market rental rates of return in Payette Lakes leasehold sales (shown in the Method 1 Rate column of facing spreadsheets, and summarized on the next table):

Fiscal Year	No. of Sales	Indicated Average/ Median L/V Ratio	Indicated Implicit Market Rate of Return (R_M)—Mean/Median
1997-1998	12	60%/59%	62%/60%
1996-1997	6	81%/76%	129%/105%
1995-1996	11	73%/66%	91%/74%
1994-1995	7	85%/78%	115%/174%
1993-1994	1	Irrelevant—only one sale that year	
1992-1993	6	134%/119%	74%/135%

Note: The 1992 data is particularly questionable, for two reasons: First, the market was in the midst of significant price escalations, which would tend to make leasehold purchasers pay more on speculation; and second, the assessed value lagged behind the market considerably.

The flaw with this first model (equation) is that it assumes all buyers are rational and well-informed, and that any given buyer always has the opportunity to buy a fee simple property of equal desirability. As we have suggested, in real estate dealings, sometimes neither is the case. Because we cannot get inside the heads of the market participants, we have to look to the assessed value for the indication of land value, which was less likely to be keeping pace with market value in the early 1990s than it is in the past two years. Thus, the data from the last two fiscal years is considered more meaningful than it was earlier on this decade. Similarly, we have to defer to assessed value for the improvement value, unless in the course of the lease assignment one of the parties requested an appraisal. The Dept. of Lands reports that they have a residential fee appraiser on contract for when the parties in an assignment make a request for an appraisal; when an appraisal is done, the allocation shown by the Dept. of Lands is the appraised value rather than assessed value. The personal property allocation is the buyer's. Thus, the indication of leasehold value is the residual of the lease assumption payment less the value of the improvements (assessed or appraised value, as available), and less the

personal property (buyer's report). This residual leasehold is then divided into the assessed value of the land, and a ratio is derived (L/V).

When the L/V is 1.0 (100%) or greater than 1.0, the suggestion is that the buyer paid a leasehold price equal to or greater than the fee simple value of the land, which again, a rational buyer would not do unless:

a) He felt that even paying full fee simple value or more would be cheaper than owning the property and paying property taxes (recall that an IDL lessee has no taxes on land);

b) There were no comparable fee simple properties available for sale when he was in the market to buy.

Alternatively, because each lakefront property is relatively unique, and because most buyers are not well versed in the economic theory of leasehold versus fee simple ownership rights, one could argue that the contention that most buyers fit the definition of "rational." Recall that even in Alabama and Minnesota, lessors commented that their leasehold properties often sold for 80 percent to 100 percent of market value (in fact, on the Internet web page, Minnesota Power makes the rather bold statement that appraisers often see no difference between leasehold and fee simple values, which goes entirely against the logic of a fractional interest in the bundle of rights in real estate, but it illustrates the point that buyers sometimes simply don't know the difference, or don't care).

Still, anyone considering Duffield's first model can see that it is a useful tool when the market is buying leaseholds at something less than fee simple value. Intuitively, we know that the higher the price paid for the leasehold, the better the deal the buyer perceives the contractual rental rate to be, and the higher the implicit divergence between market and contract rates of return (that is to say, the higher L/V, the higher the rate of return the market would bear). Thus, the flaw in this model is that the simplified equation plots an exponential curve the closer L/V comes to 1.0, and after 1.0 (that is, at the point a buyer appears to have paid full fee value for a leasehold—or more), the equation returns a negative number, which is neither accurate, or useful for analysis.

Fortunately, Duffield offers a second formula or model which does not suffer from this deficiency. The formula we refer to as Method 2 does not result in meaningless output (negative returns) as buyers cross over the 100 percent of fee value theoretical rational barrier. However, it also introduces an additional element of subjectivity—all the variables are the same, save for one. This second model assumes that i and R_M are two different and independent variables, where R_M is still what we are trying to solve for, the implicit market rate of return, and i is some kind of discount rate. Duffield suggests a consumer interest rate, such as the rate of return on a credit card at 14+ percent. However, by its nature, the higher the discount rate assumed, the higher the market rental rate (land capitalization rate) is indicated by the formula. Since the substitutable option to leasing is to purchase (assuming there is product available to buy), we argue that the discount or interest rate should be that which sellers would typically offer to buyers on a land contract of sale, at about 7 to 9 percent per annum. For the development of Method 2, we utilize 8 percent, which we have found to be the most prevalent interest rate sellers of residential and agricultural properties have offered buyers in recent years.

With this model, the following implicit market rates of return are indicated:

Fiscal Year	No. of Sales	Indicated Average/ Median L/V Ratio	Indicated Implicit Market Rate of Return (RM) – Mean/Median
1997-1998	12	60%/59%	7.3%/7.2%
1996-1997	6	81%/76%	8.9%/8.6%
1995-1996	11	73%/66%	8.3%/7.8%
1994-1995	7	85%/78%	9.3%/8.8%
1993-1994	1	Irrelevant – only one sale that year	
1992-1993	6	134%/119%	13.2%/12.0%

Again, ignoring the questionable data prior to 1994, there appears to be good trending in the range of about 7 to 9 percent. One should probably not conclude that rates have been declining over these years, as the indications for Fiscal Years 1994 and 1996 are virtually identical. However, one should likely conclude that the most recent year's data, with the greatest number of sales, and a leveling off the assessed values, provides the most meaningful indication of the implicit market rate by virtue of comparison of what lessees have been willing to pay for leaseholds, relative to market value.

As secondary support only, this model is concluded to afford credibility to a market rate of return in the range of 7 to 9 percent, with emphasis on the lower end of the value range (7 to 7.5 percent).

Prior to reconciling the data gleaned from our research and analysis, and setting forth our conclusion of fair market rent (rate of return), the question of disparate rates of returns for different value levels warrants some discussion.

Cap Rates Relative to Value

To this point, the only substantive topic we have failed to address is the impact, if any, on cap rates of the value of the land. In their 1991 study for this same client, the appraiser's partner/brother, Trey Knipe, MAI, and his then partner, Tom McKevitt, MAI, concluded primarily on the basis of the prevailing lease rates of oceanfront property in California that a slightly lower rate was appropriate for lakefront lots than for non-lakefront lots. The actual conclusions were 4.5 percent for lakefront lots, and 5.5 percent for non-lakefront lots.

For purposes of the current analysis, oceanfront lots in California were excluded from this analysis, as was any type of lease of property other than for rural recreational use. Oceanfront land has the potential to bring into consideration new factors which are not in play in the case of lakefront land, including deterioration of improvements due to saline content of prevailing winds, shoreline erosion, storms, public access and trespass, and a liberal (regulatory-biased) California legislative climate, among others. In short, there is no direct way to be certain that the lower capitalization rates suggested in the 1991 study for lakefront land were for higher land values, or for other factors appurtenant to the leases or the properties involved.

Arguments in Favor of a Lower Rate of Return as Value Increases

1. Six percent of a $45,000 lot, or $2,700 per year, is probably manageable for a family having the income and budgeting capability to support a second home. However, 6 percent of a $500,000 lakefront lot, or $30,000 per year only for the land, is simply put, a great deal of money for a recreational situation. It is safe to say that it would constitute an annual expenditure far greater than the average household's expense on a mortgage—that is, land and improvements.

2. Higher rates of return may not be attainable. A wealthy family, trust or individual may well lease into perpetuity for a $500,000 lot when rents are below market, but when faced with paying a market rate, those financially able to do so would likely elect to buy. In the example above—a $500,000 lot at $30,000 per year, one has paid the price of a lot in 16.7 years of leasing, assuming no discount for present value of money, and no changes in the rental rate (appreciation of the lot could shorten the break-even analysis). While it may not be an option for someone leasing a $45,000 non-lakefront lot to buy rather than lease, it is reasonable to assume anyone who can pay $30,000 per year for the lease of the land for a second home can also finance the purchase or even pay cash for the lot.

3. As a rough analog, a sale commission for a typical residential property is 6 percent of the sale price. As one moves up in value, as in the case of a commercial property, the commission may drop to 2 to 5 percent for a property in the range of $1 to $10 million.

4. A tenant leasing a larger space, such as a 40,000 square foot warehouse, is likely to negotiate a better rent per square foot than one leasing a smaller space, say a 10,000 square foot warehouse. (However, expenses per square foot decline with increasing size, and larger buildings tend to cost less per square foot than smaller ones, so the developer/investor is not necessarily accepting a *lower return* for the more expensive commodity, and oftentimes will net a higher return due to economies of scale.)

Arguments Against a Lower Rate of Return as Value Increases

1. At least in commercial properties, all other factors held constant, overall rates of return accepted by investors do not tend to decline with increasing values. For example, if investors

in office buildings require a 9.5 percent overall cap rate on their purchases, they are not likely to take less for a property that costs more. Similarly, tenants in a multistory $10 million office building are not likely to pay less than tenants in a $500,000 office building, all other factors of quality, age and location being equal. If anything, scarcity of smaller investments tends make smaller investors—say for properties under $1,000,000, and particularly under $500,000—buy on lower rates of return.

2. Most wealth redistribution programs, such as the federal and state income tax system, charge higher rates to those theoretically better able to afford them. It is counter to logic to force the less financially able lessee of the $45,000 lot to pay a higher rate of return on each dollar of that real estate's value than is being charged to the more wealthy individual on the $500,000 lot. Disparate return requirements open the door to discrimination and reverse discrimination claims.

3. The studies done by John Duffield of Bioeconomics, Inc. show that Idaho and Montana leasehold purchases in the same time period (early 1990s)—despite disparate contract rental rates and widely different leasehold values—indicated similar implicit market rates of return. Even if one questions the absolute indicators of the Duffield models—for example, whether "i" in Method 2 should be 7 or 9 percent—as long as the formulas are equally applied to lakefront and non-lakefront lots, the relative differences in the indicated rates of return—if any—should be valid and reliable indications of whether the market perceives there to be inherently different return requirements. In fact, our own studies using Duffield's models showed no significant differences in the implicit market rates of lakefront versus non-lakefront leasehold sales. Using the more consistent (non-negative) indications of Method 2, the following is indicated:

Fiscal Year	No. of Lakefront Sales	Indicated Average/ Median L/V Ratio	Indicated Implicit Market Rate of Return (R_M)—Mean/Median
1997-1998	3	60%/57%	7.8%/7.1%
1996-1997	1	68%	8.0%
1995-1996	2	62%/62%	7.1%/7.4%
1994-1995	3	114%/113%	11.7%/11.6%
1993-1994	1	114%	11.7%
1992-1993	3	140%/161%	13.7%/15.4%

Fiscal Year	No. of Non-Lakefront Sales	Indicated Average/ Median L/V Ratio	Indicated Implicit Market Rate of Return (R_M)—Mean/Median
1997-1998	9	60%/60%	7.8%/7.3%
1996-1997	5	83%/82%	9.2%/9.1%
1995-1996	9	75%/78%	8.5%/8.75%
1994-1995	4	64%/65%	7.6%/7.7%
1993-1994	0		
1992-1993	3	128%/76%	12.7%/8.5%

As shown, the data for lakefront vs. non-lakefront lots is virtually identical for FY 1998, with lakefront returns *slightly lower* in FY 1996, but considerably higher for FY 1995, and *somewhat higher* in FY 1993. There is not enough data to draw a conclusion for 1997 or 1994. Overall, there is no clear pattern to indicate any differential treatment with respect to rates of return implicit in the prices leasehold buyers have been willing to pay, or in the ratios of leasehold to

fee values for the two types (value ranges) of lots. Again, in the most recent fiscal year, both L/V ratios and implicit rates are essentially identical.

4. While admittedly the values inherent in the programs were all considerably below those of Payette Lake lakefront lots, we found no precedent in any leasing program—state, federal, railroad, utility company, private sector or otherwise—for a sliding scale in rental rates based on land value.

5. Any time one imposes a sliding scale, it opens up a whole new avenue of contention for those cases unfortunate enough to fall on its boundaries. For example, if the cutoff point was land valued at $75,000 or less, the lessee with the $74,000 property could reasonably question what is inherently different about his lease, his property or his personal economic circumstance that dictates that he pay 7 percent instead of 5 percent, to use an example.

6. In most investments, more money in the investment typically means more growth potential on the rate of return. In other words, if someone told an investor that his only options were to invest $50,000 for a 7 percent return, or $500,000 for a 5 percent return, the investor would find a way to invest $50,000 ten times! While there may indeed be some merit to the argument that at some level, leasing no longer makes sense to the lessee, it does not stand the test of reason from the lessor's point of view that he should accept a lower rate of return on a more valuable, more scarce, and ultimately a very salable commodity. This comes back to the contention that, if the lessor cannot lease the commodity for an acceptable level of return, he should contemplate the sale of that commodity, and investment in something else not subject to an artificial ceiling on his return.

Ultimately, the most compelling argument for having only one rate of return is a political one: Unless the state wants to make take the position that cottage site leasing is a wealth redistribution program, and one that is justified in giving a financial break to the wealthy, it might be best to avoid disparate rates of return based on arbitrary value ranges. Moreover, there is no evidence that the McCall market acknowledges such a disparity, based on the percentages of fee value paid by buyers of lakefront lot versus non-lakefront lot leasehold interests.

Market Rate of Return Conclusions

Summary of Rate of Return Indicators

Source or Method	General Range	Narrowed Trending
Effective Market Rates of Return Being Achieved for Cabin Sites	3.6%-10.0%	5.0%-7.5%
Opinions of Market Participants*	6.0%-13.0%	6.0%-10.0%
Duffield Model Payette Lake Leasehold Implicit Rates	6.0%-13.5%	7.0%-7.5%
Montana District Court Ruling	6.0%-10.0%	6.0%-10.0%

The various sources researched and methods employed suggest a narrowed range from 5 to 10 percent to be the broad target range for lessors operating under the profit motive, and charged with maximizing economic returns.

Relevant Bracketing Factors

Rate of Return Continuum

I——————————————————————————————I

1% 2% 3% 4% 5% 6% 7% 8% 9% 10%

< Public Relations Motives	>	Profit Maximization Motives >
< No LH Improvement Buyout Protection	>	LH Improvement Buyout Protection>
< Lessee Pays Taxes on Land	>	Lessee Pays no Taxes on Land >
< Lower Cost of Capital to Lessor	>	Higher Cost of Capital to Lessor >
< Shorter Lease Term	>	Longer Lease Term >
< High Rent Increase Risk to Lessees	<	Low Rent Increase Risk to Lessees >
< Relative High Fee Values	<	Relatively Low Fee Values >

In making our ultimate conclusion, several factors should be noted and/or reiterated. The chart above gives a visual representation of some of these factors, in the form of a continuum or spectrum of possible rates of return.

Upward Influences on the Rate Conclusion:

- State's Mandate. The legislative mandate of the State Land Board is to maximize income, and as reinforced by the 1990 Legislature, the Dept. of Lands is required to ensure that all its leases generate market rates of return throughout their duration. Market implies an arms-length situation, not influenced or moderated by political processes or agendas, company policies, etc.

- State Buy-Out Clause. Obviously, if a lessor terminates a lease except for cause (non-payment, illegal uses, etc.), this would constitute a breach of contract, and the lessor may be liable for

damages, including compensation for leasehold improvements. However, the Idaho leases are unique in that they say state will pay the lessee the value of his leasehold improvements if a lessee makes application to renew his lease per the normal procedures for same, and if his request is denied. This is a guarantee that we found in no other comparable leases, including those of the U.S. Forest Service. In fact, the closest thing to this was an acknowledgement in the Alabama Power lease that if the lessor terminated the lease without cause, the lessor would be obligated to buy the improvements; and if the lease was either expired or terminated for cause, the lessor would have first right of refusal to buy the leasehold improvements, and failing to do so, the tenant could remove them and restore the site if the tenant so desired. At the opposite end of the spectrum, the Pacific Power & Light lease had a 90-day lessor termination clause with no requirement for the lessor to buy the leasehold improvements.

The protection that if the State of Idaho elected not to renew a lease, it would buy the improvements, minimizes the lessee's risk considerably. All other factors being equal, this clause of the IDL lease would motivate a lessee to pay a higher rate of return than he would otherwise, and would in theory require a lessor to get more of a return to protect against that potential expenditure should the state decide to get out of the leasing business and put the land to a higher and better use (were there demand for such).

- State's Performance. According to Bryce Taylor, Bureau Chief of IDL's Surface Leasing Program, the State of Idaho Dept. of Lands has never terminated a lease except for cause in 74 years of leasing. Again, this longevity is an attractive benefit for lessees, and all other factors held equal, would warrant a somewhat higher return.

- No Land Taxes. In the Idaho leasing program, lessees have no tax burden on the land. The sewer bond levy, at about 8/10 of one percent, is inconsequential, and results in an effective rental rate to the lessees of less than 2.6 percent per year.

- State Bond Rates. The state's trust endowment lands were set aside to provide a source of revenue to fund schools and hospitals; it is nothing more and nothing less than a financing vehicle for public infrastructure development. Discussions with Senator Hal Bunderson of the Idaho Legislature indicate that the State of Idaho can raise funds for developing state infrastructure, such as government office buildings, by the sale of low-risk, non-recourse bonds, currently yielding a return of about 5 percent. Given the management burden of the cottage site leasing program, time spent by Dept. of Lands personnel interacting with lessees and their homeowners' associations, and the political liability the leasing program constitutes to some members of the Board of Land Commissioners, it is reasonable to expect that for the Dept. of Lands leasing program to remain more favorable and more beneficial to its beneficiaries than selling off the asset (exchanging into more economically productive real estate), leasing of state lands should at least match the returns (cost of capital) of the sale of bonds, plus a premium of 1 to 2 percent for the management and risk factors associated (i.e., a return of 6 to 7 percent).

- Rolling 10-Year Lease. Except in extraordinary circumstances, IDL officials report that upon request of a lessee, a lease which is for example in Year 4 of its 10-year term will be reset to Year 1. Thus, while the term is only of moderate duration, it is in most cases, infinitely renewable upon request of the tenant. This is not a policy codified in the lease, but it is a prevailing policy factor to consider which adds to the benefits afforded the lessee.

Downward Influences on the Rate Conclusion:

- Relatively High Values. We have acknowledged that some of the Payette Lake secondary (that is, non-waterfront) lots equal or exceed the value of some of the lake and reservoir-fronting lots in the projects utilized for market rental rate comparables. Unfortunately, we have no direct data

that would guarantee that rates are independent of values, but conversely, there is no direct evidence to the contrary. The lack of certainty warrants a conservative conclusion, all other factors held equal.

- Non-Specific Rental Increase Policy. The biggest theoretical risk to tenants entering into a lease with the Idaho Dept. of Lands is that the lease is very one-sided when it comes to rental rate increases. Specifically, the lease states a fixed rate for Year 1, and Attachment A to the lease notes that the lease rate can go up or down from there, on an annual basis, with no other requirement but a 6-month notice to the lessee, and no stated option for the tenant to accept the new rent, or terminate the lease (the only termination option appears to be via default).

  As written, State of Idaho Department of Lands leases having theoretical, unlimited annual increase capability should have a downward effect on the rental rate of return. This has considerable merit, despite the fact that politics have held real increases at bay (again, some years have seen no increases at all). The point must be acknowledged that a typical buyer of a leasehold may not realize that rents can change each year of the lease without specified constraints, and thus may pay more for the leasehold estate than if he realized this potential to erode his investment. It is equally as likely, however, that unless the leasehold purchasers have spent the past few years out of the area or out of touch with the local press, they know the current 2.5 percent lease rate is a very politicized matter, and in full knowledge of this, elected to gamble that political pressures would minimize rent increases in the remaining years of the lease.

  According to one real estate attorney we interviewed, such a one-sided arrangement in a lease could very possibly be construed against the lessor as a non-binding agreement if challenged in court (the term utilized was an "illusory" contract.) In the same breath, however, the attorney noted that lessees are not (as a typical practice, if at all) challenging the Dept. of Lands on this basis for two reasons: First, it is counter to their interests because the lease rates are so low to begin with; and second, because to do so would be counter to their claims of significant leasehold investments—without a valid lease, there is no claim for a leasehold interest. This is beyond our expertise, and beyond the ability of most market participants to meaningfully assess, either. It is a legal matter which is best left to the courts and legislature to settle.

  For our purposes, however, the fact that the language of the standard IDL lease does not say how annual rent increases will be determined, and does not afford the lessee any means of predicting those increases or protecting against them (e.g., a maximum annual increase or escape clause), this lease provision provides a strong argument for a conservative conclusion within the narrowed range of market-indicated rates of rental return. In other words, were this clause of the lease abandoned, and were the means by which the lease rates were to be determined spelled out for a tenant to acknowledge in the lease and with some limits imposed, a significantly higher market rental rate could in good faith be argued. However, unlike most competing cottage site leases we reviewed—which are flat, or which have annual CPI, GDP-Price Deflator or other indexes the rates are tied to—the IDL's practice of indexing land values to assessed values is driven by IDL/Land Board policy, but it is not a part of the legal lease document, and the legal contract with the lessees does not reference prevailing Land Board policy directives as governing lease rate changes. As written, the IDL leases put all the financial risk on the lessees. This should be acknowledged in the ultimate conclusion of the appropriate rate of return on fee simple value.

In acknowledgment of these factors, the concluded minimum economic return we recommend for the State of Idaho, Dept. of Land's cottage site program, is equal to 6 percent of fee simple market value of the land, each and every year. In the absence of the unrestricted escalation clause and with more definitive market data for higher value recreational properties, the reasonable conclusion might well shift upward to 7 or even 8 percent (realize that even some governmental lessors, such as the States of Washington, Alaska and Arizona are reported to be exceeding this rate on their state lands),

but in recognition of the fact that any increase is going to be difficult for the Dept. of Lands and the Land Board to implement after so many years of subsidizing the lessees at Payette and Priest Lakes, the uncertain relationship (if any) between value and rate of return, and because of the theoretical unrestricted upside potential to rental rates, *our conclusion is intentionally conservative.*

The concluded minimum rate should be applied to lakefront and non-lakefront lots in the same manner.

This analysis represents a good-faith attempt to bracket a narrowed range of reasonableness for the rate of return the State of Idaho should target in light of the existing rights and restrictions inherent in the lease they utilize; those who rely on this report should realize that we are attempting to address a question which has no absolute answer. Should the state change substantive clauses in their standard lease—such as incorporating a quantifiable indexing program, offering lessees the option to buy, adopting a hardship clause, granting of a lessee out-clause if rates increase significantly, or elimination of the buyout protection in the event the lessor denies a renewal request—the narrowed range could shift one direction or the other, and the concluded rate of return would need to be re-evaluated.

Using our 6 percent conclusion, the rents indicated for the 14 subject lots are set forth on the table presented as a facing page. The basis of the determination is the fee simple lot value conclusion as if vacant, except as noted in the appraisal portion of this report, use value (value as a single, legal building site) is utilized for Subject Parcels 1 and 2.

Exhibit 28a

Senate Resources and Environment Committee Minutes of February 9, 1990

MINUTES

RESOURCES AND ENVIRONMENT COMMITTEE

Friday, February 9, 1990 room 433, 1:30 p.m.

ROLL CALL: All members of the committee were present except Senator Christiansen whose son, Joey Christiansen, sat in for him.

Chairman Noh called the meeting to order.

RS 23890 RE INTERIM PROTECTED RIVERS: TO PROVIDE INTERIM PROTECTED RIVER STATUS FOR THE WATERS OF DEVIL'S CORRAL AND OTHER SPRINGS AND STREAMS ARISING FROM THEIR POINT OF ORIGIN TO THEIR CONFLUENCE WITH THE SNAKE RIVER.

Senator Noh explained this bill comes to us from an extraordinarily united group of legislators representing Magic Valley Districts 22, 23, 24 and 25. Some representatives from the House are here today - Representative Peters, past mayor of Jerome, who is very familiar with this area, and Representative Barnes.
This proposal will provide two-year interim protected status for the waters of Devil's Corral from the headwaters to their confluence with the Snake River under the Idaho comprehensive river planning statute. This is a very short stretch of stream of high quality in Magic Valley It is one of only two, of all those which flow out of the Snake Plains Aquafer in the Snake River reach of the Magic Valley, which is yet undeveloped.

MOTION MOVED by Senator Peavey, SECONDED by Senator Tominaga that RS 23890 be sent out to print.

VOTE MOTION CARRIED BY VOICE VOTE.

RS 23884 STATE COTTAGE SITE LEASES - RELIEF FROM CONFLICT BIDS.

Senator Noh explained this is the result of a joint effort of the Department of Lands staff and attorneys who have been working for the cottage site owners.

Mr. Stan Hamilton, Director, Department of Lands, explained that for many years there has been a provision in the statute that provides that any time a parcel of state land is leased, when that lease comes up for expiration any person can file an application against that lease. When that happens, the Code provides that the Land Board must hold an auction limited to the lease holder and the conflictor, and then dispose of the lease to the highest bidder. This year, in late August, conflict applications were filed, both by the same party, against two lots at Payette Lake - Pauline King's and Robert and Celia Smith's.
Conflict applications are not unusual - in the grazing lease arena we have several each year, and they generally generate a considerable amount of revenue, but in the cottage sites, history is such that in

the 40-50 years we have been leasing we have received only four applications. The first in 1969, and one was for a lot that had been leased but no structure had been built on it. So, of all four of those applications, none has ever come to an auction because the applicant withdrew before that point. This time, however, the applications are still in place and the Land Board has set the auction for May 15th. There was discussion at the board meeting about coming to the legislature to determine whether any kind of relief might be possible. He pointed out that the bill provides that leases for single family recreational cottages, family cottage sites and home sites, shall not be subject to the conflict application and auction provisions generally set out in the Code, and it further provides that the Board shall reject any and all pending and future conflict applications and in the absence of conflict applications and auction procedures in this renewal process, the Board shall insure that each lot generates market rent throughout the duration of the lease. The emergency clause is to see if there is any way to deal with the two pending applications which will go to auction on May 15th. This legislation needs to be in effect at that time.

MOTION — Commenting that he is not sure whether he will support the bill when it comes up, Senator Beitelspacher MOVED, and Senator Reed SECONDED that RS 23884 be sent from committee with a recommendation to print.

VOTE — MOTION CARRIED BY VOICE VOTE.

RS 23407 — WILDLIFE DEPREDATION - TO AUTHORIZE CONTINUATION OF THE NEGOTIATING COMMITTEE.

Chairman Noh said this is the result of very fine, but very hard work, by the representatives of the wildlife and agricultural communities. Senator Carlson spoke in support of the bill saying that it extends the active working life of the negotiating committee through November 30, 1990, the thought being that other legislation is coming along which will either be approved to extend it as a relatively permanent thing, or the legislation will pass. He urged the support of the committee.

MOTION — MOVED BY Senator Tominaga, SECONDED by Senator Beitelspacher that RS 23407 be sent from committee with recommendation to print, and that it be returned to our committee

VOTE — MOTION CARRIED BY VOICE VOTE.

Exhibit 28b

Senate Resources and Environment Committee Minutes of February 16, 1990 (with attached written statements of Payette Lakes Cabin and Pilgrims Cove Association titled "Questions and Answers Concerning Lease Lot Issues" and "Legislative Fact Sheet in Support of SB 1516")

MINUTES

SENATE RESOURCES AND ENVIRONMENT COMMITTEE

Friday, February 16, 1990 Room 433, 1:30

ROLL CALL: All members of the committee were present.

Chairman Noh called the meeting to order

Chairman Noh introduced Mr. Hank Miller of Salmon, Idaho who has been reappointed to the Outfitters and Guides Board. Mr. Miller stated he is a river outfitter, has served one term on the board and is well into his second term. He is primarily a float outfitter but also does jet boat trips with steelhead fishing on the Salmon River. Has been Vice-President of the Outfitters and Guides Association, Vice-President of the Boating Section of the Outfitters and Guides, was with INEL for eight years and came to Idaho in 1962. He mentioned other involvements such as the Travel Council etc. Several questions were asked regarding a conflict for a license in a given area, and if Mr. Miller knew of cases where an application for a license has been denied when the board felt that it would create a conflict with the general public. He responded there had been. He explained there were some maximu on rivers, some of which have been imposed by the licensing board, some by the Forest Service or the BLM and said we are now reaching a saturation point for outfitters.

Chairman Noh introduced Mr. Dale Baird, Fish and Game nomination to the Outfitters and Guides Licensing Board who stated he had worked for the State Fish and Game Department for 28 years in the law enforcement bureau and the last ten years served as the chief of that bureau; is semi-retired and served for the past three years on the Outfitters and Guides Licensing Board as a representative of the Fish and Game Commission. He explained his position on the board is to represent the Fish and Game Commission in administering and seeing that the laws and regulations of the statute regarding outfitters and guides is carried out.

Chairman Noh thanked both men for being present, and said their appointments will be voted at the next meeting.

S 1516 RELATING TO LEASES OF STATE-OWNED RECREATIONAL COTTAGE SITE AND HOMESITE LANDS AND TO PROVIDE THAT THEY SHALL NOT BE SUBJECT TO THE CONFLICT APPLICATION AND AUCTION PROVISIONS AND TO PROVIDE THAT SINGLE FAMILY, RECREATIONAL COTTAGE SITE AND HOMESITE LEASES SHALL GENERATE MARKET RENT: AND DECLARING AN EMERGENCY.

Mr. Stan Hamilton, Department of Lands, was present to answer questions and provide technical guidance as needed. Mr. Hamilton explained the bill is to exempt single family recreational cottage sites and homesites from conflict applications and auction provisions; it directs the state Land Board to reject all pending and future conflict applications for cottage sites and homesites; it directs the board to insure that the endowments secure market rent for each lot during the duration of the lease; and it has an emergency clause to make it effective upon passage.

CALABRETTA: What are the annual rents? HAMILTON: Class 2 lots off the lake front are around $700. Most are around $2,000-$3,000, and heading for $3,000-$4,000. DONESLEY: From where arises the right to renew an existing lease - the contract? Is it by Statute? Is it by Rules? Or, do you just assume that the right flows from an expired lease? HAMILTON: There is nothing in the contract currently that provides for renewals specifically - it may be something they will have to look at.

Mr. JAY WEBB, Attorney of the firm Givens, Pursley, Webb and Huntley, spoke in favor of the bill. He pointed out that these are three or four month recreational lea that people in the mid 90's will pay quite dearly for, and if we do not pass legislati of this nature, this lease conflict application auction, we will be placed in a chaotic situation. REED: If any profits are going to accrue from the exchange of leases, how do you respond that the lessees are able to make money from them? WEBB: At this time the State does receive 10% on transfers, but that situation can be addressed separately. HAMILTON: When a lease is signed we appraise the improvemen on the property, take the market value of those improvements, subtract them from the sale price, and we take 10% of that as a leasehold interest. The remaining 90% goes to the seller. The 10% is a matter of board policy. REED: Did the people know from the beginning there was no guarantee if they put improvements on the land? WEBB: I really don't know, they probably didn't think about it.

CARLSON: We also have the responsibility of being fair. Fewer than 1% of the people in the state have the opportunity to enjoy these leases and probably the rest would like to also have an opportunity. But from what we are doing here, it appears to me that we are insuring that whoever had such an opportunity is going to continue ad infinitum, through all the families in history, and no one else gets an opportunit WEBB: No one has ever complained that they were divested of some opportunity. I think there are 70 leases at McCall that people can take advantage of, that haven't been rented at this time. HAMILTON: I think there may be some that have not been offered for lease, but there are none that are currently available for lease.

VANCE: If these lots are leased, and people have a multi-generational right to it what is the difference between leasing and selling? WEBB: People who lease the lands improve them - this is the way it has always been done. These renewable leases, arguably, are tantamount to a sale - no question about it. NOH: Other states have leases, and they range from 10 years up. CALABRETTA: Mr. Webb presumes availability. Mr. Hamilton, if I walked downstairs today would we start the paperwor on Priest Lake or Payette Lake? HAMILTON: No. You would have to obtain a lease from some other lessee. We do not have any vacant lots available.

Mr TOM MILLER: Attorney, spoke in favor of the bill. He said a lot of these people are not wealthy people. The problem arose when the challenger felt he could get the lease cheap, surveyed the situation, looked at what leases were coming up for renewal, and determined that the present lessee could not bid substantial amounts and could be picked off. And they probably can. My clients cannot afford to outbid the conflict applicant. The way the law is now it is a wealthy man's law. There is also no assurance the state is going to make a dime. The state has to pay the appraisal and will not be reimbursed. We have to isolate this conflict situation.

TOMINAGA: Mr. Hamilton, How are these leases advertised? HAMILTON: The lessee, of course, knows that it is coming up, and we post them on the bulletin board in the county court house. That's the only advertising done on cottage site leases. NOH: What was the time frame on the part of those who had the 40-year lease, between the time they received notice of the conflict application, and when the act might take place? MILLER: I believe they were advised in August or September that a confli had been filed against them. The leases all expire on December 31st. The Code requires that the applications be filed by September 30th, and the land board takes action on them sometime after November 1st. Under normal circumstances the auction would be held sometime in November or December and the board would take action and the new lease would be issued on January 1st. However, in these particular cases we extended it on a permit basis until after the auction is held. Regarding the premium fees on assignment, as I recall, the 1988 report indicated the department received about $90,000.

DONESLEY: The lessee has the benefit of enjoying the property, then selling it for a profit after the enjoyment of the property - somewhere in there is a slice of state property that is being enjoyed, that is appreciating, and the profit from the sale of which is going into private pockets - now we have a bill to protect that kind of situation. CALABRETTA: You realized $90,000 in one year from assignments and that represents 10% of the value of those assignments - so almost a million dollars are transacted on state properties by the assignment of the lease and we get $90,000? HAMILTON: That is correct. VANCE: In Section 3. in the absence of the conflict applications, they propose that each lease shall generate market rent for the duratio of the lease. How are they going to insure that if you preclude a real market evalua What criteria do you use. HAMILTON: The only way that can be done is by very carefu follow-up by the board and the department staff to make sure the leases are appraised that we do know what the value is, and that we do obtain a market rent for it. Without that clause it would not pass constitutional muster.

MOTION MOVED by Senator Peavey, SECONDED by Senator Crapo, that S 1516 be sent from committee with a DO-PASS RECOMMENDATION.

PEAVEY: I think the state will be better off with this system that is being proposed This is a tough, heart-rending problem - generations of memories are there. On the other hand you have the free market theory that sounds great but doesn't always work in the real world. I think this is one of those cases. DONESLEY: I think the bill is flawed because it doesn't give us a procedure once a lease has expired. I will vote to send this out, but with the understanding among my fellow committee members that if somebody doesn't bring one, I am going to bring one to say there's a right of first refusal to renew that should be written into any lease, and should be implie in any existing leases, because that is what is going to keep this from being a wide-open bidding contest the next time a lease expires. BEITELSPACHER: Why don't you go to the realtors and put it on the open market instead of on the bulletin board in the court house? HAMILTON. The board has had a long-standing policy that we would not advertise those leases, and beyond that, I can't say. If we did advertise them I'm sure we would have considerable interest from other places and it would essentially create exactly the situation we are talking about today.

VOTE MOTION PASSED BY VOICE VOTE.

Meeting adjourned at 3:30.

Senator Laird Noh, Chairman

Betty Bever, Secretary

3-7-96
Lane Slaton

Questions and Answers Concerning Lease Lot Issues
and SB 1516

1. How have current lessees procured leaseholds? A representative sample of leaseholds of the west side on Payette Lake shows that 11 of 12 lessees, or 92%, paid for their leases with their personal funds. Only 1 has their lease through inheritance from family members who originally developed the land at the request of the State. Further, lessees have provided all improvements to the lots: sewer, water, tree clearing, cabins and other structures, docks, road maintenance and snow-plowing. Lessees have made these lake resources what they are today, and stand to lose significant personal assets if conflict bids are allowed to occur on cottage site leases.

2. Are leaseholds available today for people who have not previously been lessees? Seven of our sample of 12, or 60%, are relatively new lessees, having purchased their leaseholds on the open market during the past six years. Five have purchased them within the past three years, and only 2 have owned theirs for twenty years or more. Leaseholds are readily available today for purchase; a few can be leased directly from the State.

3. How do current market values of leaseholds compare to the purchase price paid by the current lessee? Again, most lessees have paid substantial amounts of money to buy their leasehold, and the leaseholders' associations do not know of any example of resales at substantially higher levels. (In fact, lessees purchase leases for the pure enjoyment of a wonderful Idaho resource, not for speculation, and hold them for many years.) Plus, the resort area market is so unpredictable, just like any housing market in your hometown, that lessees who have sold are just as likely to have lost money than to have broken even or made any money in a lease sale. Jack Flaherty of Pilgrims Cove testified to an example of a leasehold selling in 1981 for $45,000 and reselling in 1987 for $37,000. As a realtor, he believes it would not sell for more than $37,000 in 1990.

Further, current speculation over the conflict bid provision itself works to destabilize and therefore depress the leasehold market. This has happened recently: In 1987, leaseholds were selling for comparable amounts to deeded property when the State instituted a highly accelerated program of rental rate increases, and since then leases have sold for significantly less than deeded land!

4. How does the State receive its 10% "assignment fee" of the leasehold value of any sale? It has been cited that $2.8 million of leaseholds changed hands in the last five years, and the State received 10% of this amount. What no one knows is how much those leaseholds cost the seller when he or she bought them. Those $2.8 million of leases may have cost the lessees $4 million to buy, for example, so those sales did not necessarily bring profit to the sellers! Further, should a lessee sell his property for the same or less than what he paid, he will have to pay the assignment fee from the money he used to initially buy the lease. For example, if a lessee buys a lease for $90,000 and sells it for $90,000, the State gets $9000, and the lessee gets only $81,000 after the sale. Only when he is able to sell his leasehold for 10% over his purchase price will he break even.

over

5. Is the State conforming to its constitutional requirement to get the "maximum long-term financial return" for this State land through this bill? Yes. In fact, the current law works to depress the value of these lands, reducing the return the State can receive for them. This bill will strengthen the value of leaseholds, thereby supporting the constitutional mandate.

Provided by:

The Payette Lakes Cabin
Owners Association, Inc.
Charles Hummel, President,
342-3928
Diane Plastino Graves, Vice President,
343-2452

The Pilgrims Cove Association

Wayne Barsness, President,
939-8823
Jack Flaherty, Secretary,
375-2441

Legislative Fact Sheet in Support of SB 1516

In the fall of 1989, an untried and relatively unknown law, I.C. 58-310, was used by an individual to challenge two current State leaseholders of cottage sites at Payette Lake in Valley County to a "conflict bid" auction for the right to take over their cottage site lease. This conflict bid can be filed upon the renewal of a leasehold, which occurs every ten years. This private auction, between the current lessee and the conflict bid challenger, subjects the current lessee to the loss of his State leasehold on May 15, 1990, the date set by the State Land Board.

The Board placed this auction in the spring to allow time for the Legislature to review and revise this law. It is imperative that this law be changed before May 15, 1990 and before forty-seven more leases renew in 1990, subjecting them to the same challenge. (As lease renewal dates are staggered, some of the State's 600 cottage site leases come up for renewal every year.) Senate Bill 1516 deletes the conflict bid provision for State cottage site leases. The following arguments are in support of passing SB 1516.

This practice, if allowed, creates the following unsatisfactory situations for the State of Idaho and its 600 lessees on Payette Lake and Priest Lake.

a. Allowing the present law to stand and an auction to occur will possibly cause the cottage site lease market to deteriorate, with the State and the lessees losing financial value in their leases. Should one conflict bid applicant successfully assume a lease, more auctions can be expected. Then, the following could occur:

-The inherent value of a State lease lot may decrease, causing the State to lose future increases in rental rates.

-The 10% "assignment" fee the State receives every time a lease is sold could decrease because the market value of the lease, upon which the fee is based, may decline.

-The State could see reduced interest in new land they wish to lease because of the uncertainty caused by the conflict bid statute to potential lessees.

State leases have not increased in market value in comparison to deeded property since the State raised rental rates in 1987. This may be a harbinger of the impact of the conflict bid law on leased land values if this law is not changed.

b. The specifics of the conflict bid applications placed on the Lawrence Smith and Pauline King leases show a fundamentally unjust situation. These lessees have held their leases and provided the improvements through their financial and personal efforts that make the properties what they are today. Under current law, the conflict bid applicants will receive an unfair opportunity to potentially assume a lease for a relatively small sum at the conflict bid auction and for the additional amount necessary to pay the Smiths or Kings for their improvements. The conflict applicant has selected properties that could

over

potentially be acquired for a small amount of money compared to the value of the lease. The financial return to the State from such an auction could be negligible. The lessees would lose any amount they spent to procure and maintain the leases except the value of their improvements. (See examples below.) The State nor the lessees benefit from the present law; only a conflict bid applicant is benefited by it.

Further, forty six leases are scheduled to renew in 1990, and all of them are potentials for conflict bid applications. That is why it is absolutely critical for SB 1516 to pass this year. These lessees not only may lose their leases in a conflict bid, but the majority of lessees have paid for their leases and will lose substantial amounts of money. Lessees would lose that amount of money that they paid for their lease over and above the assessed value of their improvements. For example, a lessee who paid $90,000 for his leasehold that contains $40,000 of cabin and improvements would get paid for the $40,000 of improvements if his lease was lost in a conflict bid. But, the lessee would lose the remaining $50,000 that he had originally paid for his lease! One hundred percent of the money from a conflict bid goes to the State; the lessee is only reimbursed by the winner of the bid for the amount of the improvements on the lot. If a lessee paid $115,000 for his lease that contained improvements of $30,000, he would be reimbursed $30,000 by the winning conflict bidder and would lose the remaining $85,000 of his investment forever!

c. No surrounding state allows conflict bids for cottage sites. Further, Idaho, Washington, Oregon, Nevada, and Montana lease laws refer to state leases for grazing, and oil, gas and mineral exploration only, and it can be argued that cottage sites were never intended to be subject to conflict bids.

Provided by:

The Payette Lakes Cabin Owners Association, Inc.
Charles Hummel, President, 342-3928
Diane Plastino Graves, Vice President, 343-2452

The Pilgrims Cove Association
Wayne Barsness, President, 939-8823
Jack Flaherty, Secretary, 375-2441

Exhibit 28c

Transcript of Senate Resources and Environment Committee Meeting February 16, 1990 (prepared by Attorney General's Office from tape on file with Legislative Services Office)

HEARINGS ON COTTAGE SITE LEASES
February 16, 1990

S. Noh: Ok, let's then turn to Senate Bill 1516 that has to do with the conflict bids on single-family cottage lease sites. The measure we have before us is the product of a lot of legal analysis, was put together cooperatively with representatives of the cottage lease holders association, but primarily I think, or at least in large part through the efforts of the staff of the Department of Lands, and the Idaho Land Board. Mr. Hamilton is here today, I think not to be for or against the particular piece of legislation, but to answer our questions, provide us technical guidance as we may need it. Stan, do you want to go over the bill with us, or do you want Mr. Webb to proceed with that, or what's your pleasure.

Hamilton: Mr. Chairman, if it would be your pleasure, I can run over it again.

S. Noh: Why don't you, quickly.

Hamilton: Essentially the bill has some findings for the legislature which essentially are factual statements that relate to the conflict auction procedure and to the constitution, and statutory relationships with these particular common lands and this particular use. The enabling clauses are fairly straight forward; it is declared that leases for single-family cottage sites are not subject to conflict auction procedures. Sections 58-307 and -310: "The Board shall reject any and all pending and future conflict applications." And there are two conflicts currently pending. In the absence of the conflict application and auction procedure in this arena the Board shall ensure that each lease lot generates market rent throughout the duration of the lease. Provides for an emergency clause. The reason for the emergency clause is that the Land Board has scheduled the auction on the two existing conflicts for May 15. And they did that specifically to provide the Idaho Legislature an opportunity to determine whether legislation was appropriate in this issue. Mr. Chairman.

S. Noh: Stan, and we want to welcome, too, the members who represent the areas around McCall and or Priest Lake who are here with us today. If you see we are overlooking anything or you have any particular questions we would be glad to entertain those. Senator Calibretta.

S. Calibretta: Mr. Chairman, and Mr. Hamilton, can you give me an idea what an average lease, rental rate woul be on Payette Lake or Priest Lake for these state properties.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Calibretta, they are somewhat in a state of flux. Most of them now are, the Board is aiming at a rental of 2 ½ percent of the appraised value of the properties. There are minimums on the Class 2 lots which are around seven hundred dollars a year. Most of the lots now are going through somewhere in the two thousand to three thousand dollar range headed for somewhere between three and four mostly.

S. Noh: Senator Calibretta.

S. Calibretta: Mr. Chairman, Mr. Hamilton, how often do you reappraise, upgrade that rate on the rentals?

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Calibretta, until just a couple of years ago the department or the Board had been setting the rates on an annual basis and had not been doing it necessarily on an appraisal basis. We did a very complete appraisal of all of the lots about three years ago and we're going, probably, do it again in about two more. Possibly start next year. So we'll be looking at about every four to five years to go through it. It's a fairly lengthy process; it does take some time, so it's not something we want to do every year.

S. Noh: Senator Calibretta.

S. Calibretta: Mr. Chairman, Mr. Hamilton, is it your opinion that were the land available and my neighbor decided that they were going to rent a lot that is available, not state land, that the rent or the lease that they would be able to acquire, a long-term lease, would be at the same level, at the same price, as what you are presently charging for the state lands. If they went in there today?

Hamilton: That's for a vacant lot or one with a facility on it?

S. Calibretta: It's vacant. We're talking about the land.

Hamilton: Mr. Chairman, Senator Calibretta, I guess my opinion is that the rental would be higher than what the Department charges. The rental that we are looking at is, right now is heading for 2 ½ percent of the, I guess I would call it asset value of, that's just of the vacant lot, we won't deal with the improvements or the structures at all, those are held solely by the occupant. And when the lots are sold,

or assigned, why they are compensated for that. My guess is that the rentals would be higher.

S. Noh: Senator Tominaga.

S. Tominaga: Mr. Chairman, Stan. I've got a couple of questions I need to ask you. I guess why, why did the Land Board not make any recommendations, or is this the recommendation from the Land Board?

Hamilton: Mr. Chairman, Senator Tominaga. This is not necessarily the recommendation of the Land Board. What the Board instructed the Department to do was to work with the cabin-site owners and to work with the legislature to see that this issue was reviewed. To see that if legislation was appropriate, that it would be taken care of. The Department did work with the cabin-site lessees' representatives in developing this and as Mr. Chairman did indicate, I think the Department staff did quite a bit of the drafting on it. The objective that we understood from the Board's discussion with the cabin-site owners, specifically with the two conflict lessees, were that the only way to deal with this issue would be to eliminate the conflict auction requirement. Otherwise they do come up for conflict every ten years when the lease is expired. I gave a little bit of the background, I guess, a few years ago, or a few days ago, when we had this printing hearing, and that is that we have had about 4 conflicts over the years. The first one was in 1969. None of those have ever come to final auction because the conflict applications were always withdrawn before it got to the auction stage. Mr. Chairman, if I might go back to a question that Senator Calibretta asked, there are some Class 2 Lots, secondary lots, which we feel that the rentals are very near to market rent at this point.

S. Tominaga: Mr. Chairman, as a follow-up.

S. Noh: Yes, Senator Tominaga.

S. Tominaga: Mr. Chairman, why doesn't the Land Board just sell the lots and then that way they wouldn't have any problems with conflict bids.

Hamilton: Mr. Chairman, Senator Tominaga, the Board did sell 25 lots at Payette Lake about 3 years ago. I think they actually sold about 23; a couple of them were withdrawn. There was, all of those lots were sold at public auction, there was bidding on one of them and the rest of them went for the appraised price. We did, the Board did decide or asked to start out to put up some lots at Priest Lake as well, and the home owners association up there went to court to stop the sale. So the Board never sold any lots.

S. Noh: Senator, let's see, I'm not sure who was next here, I believe Senator Donnelsly, or Senator Carlson.

S. Donnelsly: Mr. Chairman, Mr. Hamilton, what do you do when the lease has expired and it's time to let a new lease and yet there may be several persons wanting that lease. What priority is there given, if any, to the prior lessee. Under this law?

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Donnelsly, there is no consideration specifically given to the existing lessee. Anyone who wants to file a conflict application can do so by a specific date, I think it's September 30th, if they file before that date, including the existing lessee, they're considered to be simultaneous filings and then the auction is an auction between the conflict applications. It's not an open public auction; it's just between the conflict applications. There is no preferential right to take the lease or anything like that.

S. Noh: Mr. Donnelsly.

S. Donnelsly: Mr. Hamilton, are you talking about existing law? That's how it operates.

Hamilton: Yes.

S. Donnelsly: How will it operate under this without the conflict auctions mechanism in place?

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Donnelsly. If this bill were to pass, than there would be no conflict application procedure on cottage sites. So that when the lease comes up for renewal, there's only one possible. If the existing lessee wants it, it's theirs for the taking. Now they take it under the terms that the Board set, but it's theirs for the taking.

S. Noh: Senator Donnelsly:

S. Donnelsly: Mr. Hamilton, will you be writing something into the lease that says that the lessee has the right to renew? Otherwise the lease just ceases to exist and your rental investor situation with any variety of potential lessees out there. How to you extend that.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Donnelsly, I think the only way that that would be extended the lessee has to file the applications in prior to September 30th. That would still be part of the rules, they would have to file the application, there being no other applications, then it's theirs for the taking. If they choose not to renew, then it becomes unleased land and it's up for . . . uh, there's a different criteria that we follow.

S. Noh: r. Donnelsly.

S. Donnelsly: Mr. Chairman, Mr. Hamilton, from what / where arises the right to renew in an existing lease? Is it in the contract? Is it by statute, is it by rule, or are you just assuming that that right flows from an expired lease.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, actually I guess that there is nothing in the contract currently that provides for renewals. And that may be something that we have to look at specifically.

S. Noh: Senator Carlson.

S. Carlson: Thank you Mr. Chairman, Mr. Hamilton. Is there by chance a conflict here in the mission of the Land Board, which I think is to obtain the greatest financial gain from these properties by passing this kind of legislation?

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Carlson. Uh, I suppose the question exists, but I think that the key is the language in the statute, in this proposed bill, that requires that the Board obtain market rent for the properties. An auction procedure is probably the easiest and best way to maximize the revenues and rentals if you will from a particular parcel of ground. I think the thing that we need to take a look at is the fact that over the 40 or 50 years that we have cottage site leases, we've only had four applications and none of those ever went to the auction process. Which may indicate that the auction process, and I guess, found out about it, there's been some element of intimidation and so forth that has existed in some of this.

S. Noh: Senator Carlson.

Hamilton: Mr. Chairman and Mr. Hamilton, I am asking for an opinion off of the top of your head now. By continuing to lease, including this arrangement, would

you be generating more revenue as opposed to selling those properties at the appraised price and depositing the gain there from and drawing interest.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Carlson. I don't know that I can answer your question. I can tell you, repeat I guess, what I said earlier in the presentation to the committee, that I've gone back and looked at a couple of lots that did exist side-by-side. One was sold in the forties, one was kept and rented. And because the value was fairly low and the amount of money the block was sold for was fairly low, rentals did produce more for the bottom line beneficiary over these forty or fifty years or so, than did the proceeds that came from the investment of the sale proceeds. Now, there are situations where that wouldn't be true. For instance, if you sold a piece of property at a very high value and it never appreciated again, you would probably, than your seven or eight percent or nine percent return we got might very well exceed the rentals that you can get for them. The key is to get market rental, and keep the revenues coming in on a regular basis.

S. Noh: Senator Carlson.

S. Carlson: Well Mr. Chairman, some years ago, people did approach this committee, these were people who have had leased property and who had placed the improvements on that property. We're asking this committee to consider the sale of those properties to those who had put the improvements thereon at what ever the market value was, with the state being the mortgage holder and allowing that to be paid off over time. Would that have any merit?

S. Noh: Mr. Hamilton.

Hamilton: I think that's almost precisely the type of situation that occurred. As I said, that could be situations where that could be true in the long run, that it would produce the most revenue. However, I don't know that, I can't tell you that that is a given always. I just don't know.

S. Noh: Senator Reed, I think you're next if you want to be.

S. Reed: I'll pass this time.

S. Noh: All right. Senator Vance.

S. Vance: Mr. Chairman, I'd like to go through this bill, and it won't take long, but what I want to do is translate this from lawyer to farmer. I'll tell you what this

is. The legislative finding is that more than one person wants the lease. The first person wants to stay because he's been there a long time. So the State is required, currently, the State is required to auction and the lessee may be upset after such a long time, that someone else may be interested in the lease. So since the Board has never had occasion to follow the law in this matter, and since the constitution requires that the State manage the land to experience maximum gain. These are point by point, you can read it yourselves. And finally H that since we need to maximize long-term gains, it is hereby declared that we aren't going to do it anymore. That's what they're saying. It's the craziest thing I've ever witnessed. I can't believe it.

S. Noh: Mr. Hamilton, may be a key point there. Are you speaking to item F, Mr. Vance, when you say the Board has never held a conflict auction, and you're suggesting the reason they have not held a conflict auction is because the Board has not been following the law.

S. Vance: No they said they have never had occasion to follow the law in this manner. But they certainly do now because new lessees have come along.

Hamilton: That, Mr. Chairman, that is correct. The Board has had conflict applications; they have never gone through to an auction on this. If it goes through, the auction it will be the first one that we've had. And there have only been four cases.

S. Noh: Are there other questions of Mr. Hamilton before we move on to other witnesses? Senator Beitelspacher.

S. Beitelspacher: Mr. Chairman, Mr. Hamilton. First when you spoke of what the leases were, I'd like to see, before we debate on this on the floor, if it gets out of committee, a map of the lots and the prices that are being paid, so I can get a handle on the difference between a Class 2, and a Class 3, and a Class 1. So I'll know what we're talking about. And then that will be a lot better then, it would be a heck of a way to buy horses. And then what do you do with the, what are you going to do when you have conflict between, if this becomes law. And the current lessee disagrees with what the fee is that the Board puts out. We're currently in a broil for the last two years with the Girl Scouts. Because they want the State to come in and pony up X-million dollars because the Land Board was raising the fee up. Where are we going to be with these folks, and I intend to ask them that same question. Where are we going to be with the folks who are leasing that property and they come in. Are they going to have to sign up in order to guarantee that their lease is protected, and then sign on for another year and then argue with the Board

over what the fee is going to be? Can you address that, or have your folks thought that out.

S. Noh. Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Beitelspacher, I think that probably very much the existing situation will continue. Currently the Board sets the rentals, it is a process of give and take, if you will, and when the Board sets those rentals usually we have a full hearing room, and the Board hears considerable testimony. If the lessees group as a whole, or an individual lessee, were dissatisfied with the lease rate, my guess is, and this is purely a guess, my guess would be that they would pay the rental and then file a lawsuit against the board. That is a process that is currently available now. In fact, in a suit that we had at Priest Lake, that is currently ongoing, the rentals are an issue. And the lessees' association, or the group that filed the lawsuit, is contesting the magnitude of the rentals on the basis that they feel that they are too high. So we do have that situation now, and I don't see any reason why that situation would change, because of this legislation.

S. Noh: Senator Beitelspacher.

S. Beitelspacher: Ok, Mr. Chairman, let me ask one more question. Does the statute, we're not amending any statute. Why is it, that the, why is, why does the Land Board feels it needs a statute to implement this policy now? Essentially what you're doing is your following Section 8, Article 9 of the Constitution, so to implement this statute. Why can't you do it right now by rules and regulations like you are the existing method that you're using?

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Beitelspacher, this is true, this is a new section but it specifically indicates that the conflict application section or provisions of section 58-307 and the conflict auction provisions of 58-310 will not apply. So 58-310 is the one that specifically requires the Board to hold an auction, and the only reason that it gives support to reject an application or to reject the bids would be for collusion or some other significant irregularity.

S. Beitelspacher: Thank you sir, thank you. I have no further questions your Honor.

S. Noh: Senator Calibretta.

S. Calibretta: Mr. Chairman, and Mr. Hamilton, we've had somewhat different requests for authority now on cabin sites in state parks, and as I can vaguely recall the suggested language there we would be dealing with the right of the present cottage holder until point use of an estate situation. And I guess I understand this, that a lease would be a part of an estate that would transfer to either the spouse or the children and whatever the estate held. And so that has no application here at all in the present lease system. As it is it's renewable, almost automatically, historically would continue to be and even more so with this test.

S. Noh: Yes Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Calibretta. I think I'll answer your question this way. There has been for a long time the ability of a lessee, an existing lessee to assign a lease to someone else. That includes children, spouses, if one of the spouses passes away than it can go into the estate and can be held by the estate until it is subsequently transferred some place else.

S. Noh: Yes, Senator Calibretta.

S. Calibretta: Mr. Chairman, Mr. Hamilton, was there a provision that person could take financial remuneration, could make a financial gain in that transaction by assigning to someone else, that lease.

S. Noh: Mr. Hamilton

Hamilton: Mr. Chairman, Senator Calibretta, yes there is.

S. Calibretta: And has that occurred.

Hamilton: Yes, many times. Sometimes fairly substantial. In the hundred thousand dollar range.

S. Noh: Senator Tominaga.

S. Tominaga: Mr. Chairman, Stan, if, I guess, I guess I have one question in that we're just exempting out the single family. Why not just repeal the whole section, or the whole law that dealt with conflict bidding, I guess.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman, Senator Tominaga, because it applies to other kinds of leases including grazing and agricultural leases. And those provisions have worked, there have been conflict auctions in those areas that have gone to auction

over the years and they do generate revenue over and above what the current set AMU rate is.

S. Tominaga: Ok.

S. Noh: Ok, are there other questions? Ok, if not. Thank you Stan, appreciate your standing by and we call upon Jay Webb.

Jay Webb: Mr. Chairman, senators, Jay Webb from the Boise law firm of Givens, Pursley, representing many of the cabin owners and lessees of both Payette and Priest Lake. You know senators, I think I have talked to all of you about this and myself and I know you have searched for perhaps a perfect resolution of this problem. I am not sure there is one. Somebody might throw me out of the room for saying that, but I'm not sure there is. It seems just from talking to, I think all of you, generally the committee seems to be in two frames of mind. They want to protect the dignity of those leases, in many instances families many generations as we know, are putting their lives and fortunes into the improvements, that sort of thing. I think there is a general feeling that the committee wants to ensure the integrity of that situation. But on the same, on the other side of the fence, you as a committee, as you know, you are charged by the Constitution of Idaho that says by golly you better get your highest return, your fair market value from those lots. I don't think anyone is unaware in this room, that over the years perhaps that highest return that commitment to the Constitution perhaps has not been met. But the testimony is before the committee that the Department of Lands is doing a workmanlike job to meet that test. By the mid-nineties, as was brought out again today, I think the lease market values, moneys returned to the state, will essentially be met. We're on that track. So it appears to me, and I'll tell you personally, I think the state shouldn't sell lands. I know some of you feel that maybe the state should. I'm just talking for my self. It seems like endowment trust lands should be held by the state of Idaho forever. That's kind of me talking, I might get thrown out of here for that too, but I feel very strongly about that. And so it seems to me, that this situation provided by this legislation, we're moving on a market scale rate, we'll get there, certainly with the oversight of this committee, the Land Department will get there as soon as it is reasonably, marketably, possible, they will get there. And you do speak and address to these leases, which are not commercial leases, they are not grazing or sectionaire??? leases, they're arguably a three or four month recreational lease that people in the mid-nineties will pay fairly dearly for, three or four thousand dollars, and we won't have a disruptive thing. I submit to you, and I believe this, that if we do not pass legislation of this nature, this lease conflict bidding application auction thing is going to put us into a chaotic confab situation that I don't think this committee wants to see happen. Not to the

good Idaho folks. A lot of them are in this room. Thank you very much Mr. Chairman. We've labored with this Mr. Chairman, and if there was a better solution, we'd come with it, but I think if you read the legislative findings that Stan and his department has come up with, and I wish that I would have written it. Maybe I hinted a few time, but he did that drafting and I think it was excellent. And the bottom line here is that I think this will work and the state of Idaho will meet that constitutional test. Thank you very much Mr. Chairman.

S. Noh: Senator Reed.

S. Reed: Thank you Mr. Chairman. Well Jay, I really don't want to sell state lands either, and I don't think we should encourage out-of-state people to come in and engage in these conflicts ???. However, I do have a problem in thinking if any profits are going to accrue from the exchange of those leases that profits should perhaps go to the state. Now how do you respond to that sort of glitch where it is possible for the lessees to make some money off of their leases.

S. Noh: Mr. Webb.

Webb: Mr. Chairman, I think at this time there is, the state does receive at this time on the transfers, admittedly I think a minimal amount, is that not right Stan?

S. Noh: Mr. Hamilton.

Webb: But that situation should certainly be addressed separately in this situation.

S. Noh: You have a comment there Stan?.

Hamilton: Mr. Chairman, I would comment at your pleasure. What happens when a lease is signed is we appraise the improvements on the property. And that's basically all of the improvements. And we take the market value of those improvements, we subtract them out of the sales transaction price, and there's a difference. That difference we call the leasehold interest. We take, the Department, or the Board, takes ten percent of that as a leasehold interest, we call it premium rental, and we take that out of it and the remaining 90 percent goes to the seller.

S. Noh: Stan, is that ten percent a matter of statute, or rule and policy, or how is that ten percent set.

Hamilton: Mr. Chairman, that is a matter of Board policy.

S. Noh: Is that it Senator Reed?

S. Reed: Thank you.

S. Noh: Senator Calibretta I believe was next.

S. Calibretta: Mr. Chairman and Mr. Webb. Senator Reed addressed my problem in that, you identifying this clearly as having to do with single family recreational leases and not commercial. And yet there is a tangible value that the person with the lease realizes that they ???? price of sale for their improvements on that property and they can assign the lease. And so, you know it looks like one thing that there is something else is wrong and kind of the concern she gets about that. I guess I just want to clarify that, do you feel that the people you represent understood from the beginning that they had no guarantee on those leases when they decided to put the improvements on the land?

S. Noh: Webb?

Webb: Mr. Chairman, and Marti, I'll be darn if I know. I really don't know. I suppose some of these folks could address that. ???? I don't suppose they really thought about that. ??? They probably just got the lease and started improving it and away they went. But I will say again, Mr. Chairman, there are certainly means that this body can take to better sustain the monies running through the state in these kinds of transfers. But I would submit, I think I am fair in saying Marti, or Senator Calibretta, excuse me, that these kinds of transfers don't happen very often. I know the few friends that I have that have dirt up at McCall. They cherish like nothing else they own. Those things aren't transferred around, certainly not in what we think of as a real estate transfer situation. I think those properties are held and fiercely held and over the years. And that's why uh, its something that I need to sell my clients on is the matter of, they uh, they get I think understandably very emotional, it's understandable.

S. Noh: Senator Carlson.

S. Carlson: Thank you Mr. Chairman. Mr. Webb. You've enumerated a number of the concerns that a committee of this type would have with the good folks in Idaho and with the generation of ???? amongst the dollars for the leases. One thing that may have been overlooked here, we also have a responsibility of being fair. Probably fewer than one percent of the people in the state of Idaho have the opportunity to enjoy these leases. And there are probably eighty or ninety or

ninety-nine percent of the other people in the state of Idaho who would like to similarly have an opportunity. But from what we're doing here, it appears to me that we're ensuring that whoever has such an opportunity is going to continue that on infinitum to all of the families in history. And thereby no one else gets an opportunity. And I wonder if you have thought about that.

S. Noh: Webb

Webb: Mr. Chairman, Senator Carlson. I've thought about it a great deal, and well within, I'm kind of a rooky on this particular problem, I guess ????? Yes, I've thought about it quite a bit. The only thing I can say is, you know I've lived in Boise for a long time, not as long you have ??Herb??, but I have never heard of a complaint in know, from anybody, my contemporaries, associates, what have you, complaining about this situation, that they were divested of some opportunity in Priest Lake, or closer to my home, Payette Lake. I don't know that there is a problem in that area. I respect what you say, but I've never heard of anybody complaining. I know people of all walks of life in this area have taken advantage of me ?? up there. I have so many friends you know who mow loans, truck drivers, and even lawyers have cabins up there. So I don't think it's necessarily an elite group. The opportunity there, and I think there are seventy leases now that people can, I think there are seventy available lots at McCall that people can take advantage of that haven't been rented at this time. I think that's fair isn't it, Mr. Chairman?

S. Noh: Any response there?

Hamilton?? Mr. Chairman, I am a little non-pulsed at that. I think that there may be some that have not been offered by lease. But there are none that are currently available for lease and not occupied, or not being leased. There may be some in the subdivision that we haven't put up.

Webb: I may have to rehabilitate myself. I thought there were about seventy that you had not offered yet.

TAPE ENDS. FLIPPED OVER AND STARTS IN MIDDLE OF SPEECH PERSON NOT IDENTIFIED.

Mr. Vain??: If you feel you've answered that, I know you've said they might not have realized they were leasing. I have to wonder what they thought they were paying for then? Every year when the lease came up. But if that's your answer, you need not answer that first question. And the second question would be then, how do you see the difference between leased property and purchased property.

You said you didn't want the state to sell the property, but if it's leased and people have a multi-generation right to it, what is different here between leasing and selling?

S. Noh: Webb.

Webb: First of all Mr. Chairman, on the first inquiry Senator, I assume people that leased the lands, they improved them relying on the principal, I suppose, if they really thought about it, in talks to the Land Department, their attorney or something. I suppose there was some day-to-day and this is the way its always been done, and hopefully that's the way it will always be done. And I suppose they knew if they really searched into it that if they did transfer their lease, that sort of thing, that they would to some extent be reimbursed for their improvements. And your second inquiry, which I guess is basically, why not sell, what's the difference between selling and leasing, that was just me talking, Senator. I feel very strongly, personally, and not all of these lessees feel this way, I know that. I really want to see the State of Idaho hang onto its trust and endowment lands, forever. I take great pride in this state doing that. And I think they can make them available to more people that way. That's just the way I feel. But I'm quick to say I know that some of the lessees at these lake sites would very much like to purchase the leases.

S. Noh: Mr. Vain.

Vain: Mr. Webb, it doesn't quite get to my question. I know you feel that way about not selling land, but if you lease land for ever, then how do you see the difference here? Why not sell it. If you're saying that you don't have to buy it, you can just lease it because you, your next generation still has it. So don't worry about it. I don't see the state has then relinquished the land as far as that goes.

S. Noh: Mr. Webb.

Webb: Well its, these, these renewable leases arguably they are tantamount to a sale, I must say, there's no question about that. You know as well as I senator, that in many businesses they put their lives and fortunes on a business operation on a ninety-nine year lease or a fifty year lease. I don't see any problem with the state of Idaho doing that, just so they get a fair market return whatever it is. And that seems to be, like I say I don't think there is any absolute perfect answer here. That seems to very nicely fit the situation that this committee, most respectfully, is ????

S. Noh: Ok. Mr. Hamilton, I might ask you, I've seen some information that indicates other states have leased periods I think ranging from what ten years to

ninety-nine years? Our good intern has been doing some research on this. Stan is that correct, or are you aware of other states' policies.

Hamilton: Mr. Chairman. Other states do have these types of leases and they do range from I guess about ten years up. I don't know of any in the ninety-nine year range—that doesn't mean there aren't any. The Forest Service had some for a while that were very, very long term. I think they have all tried to get away from a ninety-nine year term. But the bulk of them I would guess are probably in the ten to twenty, maybe thirty year term.

S. Noh: Ok. Other questions for Mr. Webb? Do you want to move on to other, well, Senator Beitelspacher.

S. Beitelspacher: Thank you, I'll try to keep it short Mr. Chairman. Mr. Chairman, Jay, I understand proprietary rights, whether they be water rights, whether they be grazing leases, or mining leases or even outfitters leases as it were, outfitters licenses. I've thought about that. I've tried to think through the conflict that you run into, like Senator Carlson raises, about who has what divine right to this in the future. And have you thought that out? What logic, what background do you bring to this, when you drafted this. Can you address that a bit please.

Webb: Well, Mr. Chairman, Senator ????, yeah, I got an array of complaints you know, from the folks around Boise about, you know, about being deprived of having a lot up in McCall. And my sense is, and I know there are people in the room that can better answer this than I, but leases are available up there. They are available on the high and low and mid-range levels, and people that are really keen, and I assume Priest Lake is essentially the same, but I don't know that. I think if you are really keen on getting a leasehold up there, I think you can do it. I don't know that as an absolute, but that is my sense.

S. Noh: Senator Beitelspacher.

S. Beitelspacher: Ok, well Mr. Chairman. I am going to ask you one short one. Well if there are so many available why in the devil are we fooling around with this? It's obvious that someone has a deep emotional attachment and wants to get the lease that someone else has. What are we talking about, some beautiful waterfront property that they want to get. If there are leases available, why is it that someone else wants to come in and get this particular homesite.

S. Noh: Mr. Webb.

Webb: Mr. Chairman, Senator Ron, I don't think there is any question that so many of these leases have really some very nice improvements on them. And when I use the word nice, I say it advisedly, because nice to me and nice to somebody else might be different. But I know people who take so much pride in their places up there that probably they haven't spent more than two and three thousand dollars into toilets and wood and what have you, but there are some others that have put a great deal of money in there, and its all relative. They take pride in those leases, pride in those improvements, great, they feel good about having provided those situations for their family, and their families to come. And I have difficulty changing that situation. Because I think Idaho is doing ok.

S. Beitelspacher: One last question Mr. Chairman.

S. Noh: Yes, Senator Beitelspacher.

S. Beitelspacher: And I appreciate the Chairman's patience here, I know there are other people signed up here.

S. Noh: That's fine, spend whatever time is necessary.

S. Beitelspacher: Uh, back to the conflict. We've. It's tough telling 200 girl scouts that you're not going to buy the land for them and give it to them with the taxpayers' money. Where are we going to be with the folks you represent, and others in your opinion, since you have done some research and kind of checked around with the folks in this area. When we're talking about 2 ½ percent of market value for an annual leasing fee. Are we going to be back in here with another piece of legislation saying "how can you do this to us, my God we've had it in the family for years and here you are trying to force me off by these exorbitant rents?"

S. Noh: Mr. Webb.

Webb: Mr. Chairman, Ron, I really don't have an answer for that. In my notes I've got girl scouts and a big question mark around it. Because they cannot be treated differently. You certainly know that, I know you're almost a lawyer but not quite. But you know that as well as I, Ron, we can't treat them differently.

S. Beitelspacher: Barely a lawyer.

Webb: (laugh) yeah. They have got to meet that bottom line like everyone else does. That's going to be a dreadful issue. But as far as I know, they are going to have to meet that test. That financial test of making sure that the State of Idaho receives what it should pursuant to the Constitution. They have to meet that.

S. Beitelspacher: Thank you. Thank you Mr. Chairman. Thank you Mr. Webb.

Webb: Yes sir. Thank you.

S. Noh: Lisa's notes here indicate, there may be qualifications on this, Oregon 99 years, Montana 40 years, Nevada non-mineral leases 99 years, California 10 years if it is residentially involved up to 50 years. Washington 10 years. Senator Carlson.

S. Carlson: Mr. Chairman, I just wish to make one observation. Possibly the reason you don't hear from anybody about the desire to lease land on, in these beautiful places, is, it's a foregone conclusion they're not available. You can't get them.

S. Noh: Senator Donnelsly.

S. Donnelsly: Mr. Chairman, is market rent as it appears on page two, lines 7 and 8, saying the fair market value, is that what is intended?

Hamilton??: Mr. Chairman, yes, that's certainly my understanding. Yes sir.

S. Noh: Senator Calibretta.

S. Calibretta: Well, Mr. Chairman and Committee, I guess I would like to speak to this availability that is presumed here by Mr. Webb. I just asked Mr. Hamilton that if I called or walked down stairs today whether I could, you know begin the paper work for a lot on Priest Lake. And he said no. And I said Payette Lake, and he said no. You would have to obtain a lease from some other leassee. We do not have any vacant lots.

S. Noh: Are we ready to move on to Mr. Miller? Tom Miller?

T Miller: Mr. Chairman, members of the committee. I am Tom Miller and I am an attorney with Hawley, Troxell, and Hawley. I got into this battle because one of my partners is the neighbor of the Smiths who have a cabin up at McCall. Robert and Celia Smith. And they pleaded for help and we're helping them. They're paying us what they can, but we're certainly not making a lot of money out of this. But I do, I have gotten to become immersed in the justice of their cause. In fact, my neighbor across the street, Mrs. Esquelagrea(??) 80 some years old struggling to keep her lease up in McCall. A lot of these lease holders are not wealthy people. But to answer Senator Beitelspacher, even though he didn't ask me directly, why did this problem arise. Why did they hone in on these leases. Well the answer is

because they could get them cheaper. They surveyed the situation, looked at what leases were coming up for renewal and picked out leases that were fairly nice and didn't have extensive improvements and maybe had done some background checks on the lessees and determined that they could not bid substantial amounts and so they figured they could walk in and bid and buy these for a song. ???? Because as far as I know, my clients and the other people, the Kings, who hasn't even hired an attorney, cannot afford to outbid the conflict applicant. So the way the law is now, it's a wealthy man's law. Pick out the easy target and leases are coming up for renewal and you file your application, and it's not an open auction, you don't bring in everybody. I'm sorry, I'm getting a little emotional up here. No, this is a closed auction between a fellow that surveyed the situation, picked on easy target and these existing lessees. And there's no assurance that the state is going to make a dime on it. The state has to pay for an appraisal, they don't get reimbursed, there is no assurance that the state is going to make a dime. So, you've got, we have to isolate this conflict bid situation from the general proposition of whether the leases are providing a maximum long term ??? Senator Carlson, I believe, someone asked, maybe Senator Calibretta, didn't these people know what they were getting into when they leased it. They know they would be subject to being ousted after ten years. Well Stan Tate, last August, bought a lease. One of the good staff members at the Department of Lands talked to him and said you realize that you could be conflicted, your may lose this, but it's never happened, so I wouldn't worry about it. So I think Mr. Webb was quite correct, in stating that it's just because of precedent and how things have gone and people have proceeded on the basis that they are going to be able to lease, build improvements and expand improvements and renew. There is no guarantee, however, that they are going to be able to continue to afford that rent. The state can raise that rent and the county can raise property taxes. And of course the sewer district passed a bond issue and laid a pretty heavy cost on for a sewer district. So these costs are becoming accumulative very, very high. These people do not have a free ride. But as far as the availability, if somebody wants to go in, I suppose you could go in and buy leases from one or more people along the lake. You'd have to take quite a bit of money. I think Mr. Hamilton said it was in the hundred thousand dollar range. But if the, if this conflict bid law is applied, and if the word gets around, I think those things would disappear. Because why would anyone pay a premium rental for a lease that could be jerked out from under you. And all they could get would be so-called value of the improvements with no assurance of what that is, whether that is replacement or fair market value. Mr. Scribner, some years ago, pointed out that there is a great distinction between fair market value of improvements on these leases and a replacement cost. And there is no assurance that these people are going to get repaid for the investment they made in the sewer district which

benefits the state land value, which will benefit subsequent lessees. Uh, Mr. Chairman, members of the committee, I thought maybe someone would ask how does the Land Board stand on this, so I talked to three of the Land Board members. Mr. Cenarrusa, Mr. Jones, and Mr. Williams, and they all indicated they were in favor of the bill. I called the Governor's office and I talked to Mr. Bruneel and he indicated the Governor is in support of the bill. I thought he was going to be here to say that himself.

S. Noh: He is here today.

T. Miller: I'm sorry. I was unable to tag Mr. Evans, I imagine he has bigger problems such as school final apportionment. But anyway, I think I have, anything I said more would be just cumulative and I appreciate the opportunity to be here and stand for questions.

S. Noh: Senator Tominaga I believe.

S. Tominaga: Mr. Chairman, I guess these are more questions for Stan than for Mr. Miller.

S. Noh: Ok. Stand by Mr. Miller, we may get back to you.

S. Tominaga: And it has to do with one of your comments too. So maybe you might be able to answer it also. Stan, I guess I'm hearing two stories. And maybe I had to step out for a little bit, and maybe this might have been asked. But, how are the leases advertised? Every ten years when they come up. Are they advertised, or through legal notices. Or are they just notified, the leasee is notified.

Hamilton: Mr. Chairman. The leasee or the lessee knows of course that it's coming up and we post them on the bulletin board in the county courthouse. That's the only advertising that's done on cottage site leases.

S. Noh: You might ask Mr. Miller in that regard if he's familiar with the, this does involve questions of process and equity. What was the time frame involved on the part of the people who have had this forty year lease between when they receive notice that there was going to be a conflict on their lease and when the act might have taken place.

Miller???: Mr. Chairman, are you asking about these specific . . .

S. Noh: In this specific case, which of course is the only case we . . .

Miller???: Mr. Chairman, I believe they were advised around August or September that there was a conflict filed.

S. Noh: And then, Stan, when might the potential action have taken place?

Hamilton: Mr. Chairman, the leases all expire on December 31st of the given year that they come up. The code requires that the conflict applications or the applications be filed by September 30th and then it requires that the Land Board take appropriate action on the applications sometime after November 1st. And I think, under normal circumstances, if it were grazing let's say, the auction would be held sometime in November or December, and then the Board would take its action, and it's pretty routine, the Board would take its action and the new lease would be isued on January 1st. These particular cases we extended it on a permanent basis until after the auction is held.

S. Tominaga: Mr. Chairman as a follow-up.

S. Noh: Yes, Senator Tominaga.

S. Tominaga: Mr. Chairman, Stan, Mr. Miller mentioned that there were property taxes paid on the lease, I mean on the property, oh its personal property not real property.

Hamilton: Mr. Chairman it's on the improvements, it's on the personal property that's owned by the lessees.

S. Tominaga: Ok that makes a difference, I understand now.

S. Noh: Mr. Miller

Miller: Mr. Chairman, Senator Tominaga, that is correct. They do have however a special benefit fee levied since 1985 on what it would be if they owned real property. So they are paying the equivalent of a property tax on the land. Although, since it is state land they can't be taxed. So they call it a special benefit fee.

Hamilton: Mr. Chairman

S. Noh: Any comments Stan?

Hamilton: If, while I'm here, if I could just offer one comment. I don't want to leave the committee with a misimpression. The question has been, what's the fee for transferring leases on an assignment. And my answer was that yes there is a

fee, a transfer fee, and some of them had been in the hundred thousand dollar range. I don't want to give the impression that all of them are. First of all, any person who wishes to transfer or assign a lease to a member of their immediate families, a child, or something like that, it is done for love and affection. And those leasehold interests vary from three or four thousand dollars to a hundred or hundred fifty thousand dollars, I think are the biggest ones we've ever seen. We see about, oh maybe fifteen transfers a year on these assignments, where somebody comes in and either purchases it in the market, and real estate people actually handle these, they are not handled directly by the Department. They are handled by real estate people. Only after they have reached an agreement do they come to us and then we go through the process. So, I don't want to leave the committee with the impression that all of these are in the hundred thousand dollar range, because they're not. Sometimes they're just in a few thousand dollars, depending on the value of the property and the desirability.

S. Noh: We might ask here, briefly too. Do any of our House members have a question or concern they want to raise? Yes.

Woman's voice??: I would Mr. Chairman. Have you considered making these leases read so they cannot be transferred for financial gain. That they can just be passed on as part of an estate but they can't be sold for the large fees.

S. Noh: Mr. Hamilton

Hamilton: Uh, Mr. Chairman, Representative. The Board has talked about some things like that, but as far as I know they have never gotten to the point where "yes, that's what we're going to do." I think it is possible to do that. But I don't think the Board, well I know, the Board has taken action to try to do that.

Woman's voice??: I know that's a completely different subject from this matter, but . . .

S. Noh: They're all related.

Woman's voice??: this statute appears to solve the challenge these questions quite well, but there are some things related to the philosophy of the cottage site leases that I think the discussion is very good.

S. Noh: Mr. Miller.

Miller: Mr. Chairman, if I'm not out of order, apropos the assignment, the premium fees on the assignment, as I recall the 1988 report of your Department,

indicated that the Department received about $90,000 that year from ??? if I read the report right. Which would jive with the number of assignments you're talking about. Furthermore that report indicated that the revenue from these cottage site leases was huge in comparison to the acreage involved as compared to agricultural ??? and other kinds of property. I don't think ?????

S. Noh: Senator Donnelsly

S. Donnelsly: Mr. Chairman, Stan, have there been examples of leases sold at speculation for much appreciated value.

S. Noh: Mr. Hamilton

Hamilton: Mr. Chairman, Senator Donnelsly. I kind of don't think so. The reason I'm hedging is I don't know, obviously. Most of these leases are held for quite a lot of time. We're talking about transfers to the second and sometimes third generation in some of these. I don't, I guess I can't tell you of any place that I know of, where there was a specific one for speculation. I come to one, it was a vacant lease, that we leased about two years ago and the person turned it over while it was still vacant a year later. And he didn't make a whole lot on it, but he did make some on it. And that I think was a case of speculation, but to be honest about it, I think that's the only one I know of. I think some people have taken obvious advantage of the fact that they got it for a very low price and they held it for a very long time and then when they turned it over they made some good money on it. But I don't consider that to be speculation, I guess. I think they really and truly enjoyed the lease while they had it and that was first and foremost in their mind and they disposed of it when it no longer fit their life style.

S. Noh: Mr. Donnelsly.

S. Donnelsly: Mr. Chairman, Stan, what you have just described, while it sounds acceptable on its face, you've described the benefit of enjoying the property and then selling it for a profit after the enjoyment of the property. Somewhere in there is a slice of the state given that it is state property being enjoyed, it's appreciating and the profit fomr the sale which is going into private pocket and now we're having a bill to protect that kind of a situation. So I was going along fine until you got to that last part, it looks to me like a double benefit. What has the Board considered to do to take a slice of that appreciation, or that value, or that enjoyment or whatever for the tax payers of this state. We're the ones footing the tab.

Hamilton: Mr. Chairman, Senator Donnelsly --

S. Noh: Mr. Hamilton.

Hamilton: Several years ago the Board did institute ten percent of that. They take ten percent of it. Now, different percentages have been discussed and may be discussed again. Depending on what happens with this legislation, I'm, I don't know what's going to happen, I have no idea. But that has been discussed and there have been figures bandied about up to 50 and 60 percent of it. Right now, it's 10 percent and depending on what happens on this legislation, I guess it's up for consideration.

S. Noh: Senator Calibretta I believe is next.

S. Calibretta: Yes. Mr. Chairman and I guess Mr. Hamilton. Just so I understood something that was said prior to this last series of questions. I believe it was said that you had realized $90,000 revenue in one year from the assignment. Is that correct?

Hamilton: Mr. Chairman, Senator Calibretta, that's not unreasonable.

S. Noh: Senator Calibretta.

S. Calibretta: So Mr. Chairman and Mr. Hamilton, follow my thinking so I'm not getting out of perspective here. That represents 10 percent of what the real value of those assignments was, in the occurrence of those assignments. Is that correct?

Hamilton: Mr. Chairman, yes it is.

S. Calibretta: So, roughly, a million dollars are transacted on state properties by the assignment of the lease and we get out of that ninety thousand, or a hundred thousand dollars in any given year.

S. Noh: Mr. Hamilton

Hamilton: Mr. Chairman, that's correct.

S. Calibretta: Thank you.

S. Noh: Senator Vance.

S. Vance: This question perhaps for Mr. Hamilton or Mr. Miller either one. In section 3 in the absence of the conflict applications they propose that the Board shall ensure that each lease lot generates market rent through the duration of the

lease. Now I'd like to know how they're going to ensure that if you preclude a real market evaluation. What criteria would be used for that.

S. Noh: Mr. Hamilton.

Hamilton: Mr. Chairman I guess I'm probably the one. Mr. Chairman, Senator, the only way that that can be done is by very careful follow-up by the Board and by Department staff. To make sure that the leases are appraised, that we do know what their value is, and that we do obtain a market rent for it. That's going to require some care. The reason that that's in there is because without that clause, without that statement, then this would not pass constitutional muster, even remotely.

S. Noh: Mr. Hamilton, would it not be true that this free market in leases that exists, the benefit of which generally is accruing to the private parties, would also probably serve as a basis for appraisals of the value of the leases, would it not, and the rentals on the land for everyone. Or am I missing something there.

Hamilton: Mr. Chairman, there are relationships. First of all the leasehold interest exists because by classic economic theory, a leasehold exists when rentals, when contract rentals are lower than market rentals. And I think that is general first economics 101. So I think there is a relationship there. As rents go up, the leasehold values do come down. And there is a relationship there that can be determined.

S. Noh: Well, what's -- Senator Peavy.

S. Peavy: Mr. Chairman I move that we send this out with a do pass.

S. Crapo: I second.

S. Noh: Moved by Senator Peavy, seconded by Senator Crapo. Discussion. Senator Peavy.

S. Peavy: Mr. Chairman, this is really a tough problem without any doubt, you know, it is a gut wrenching, heart rending problem. And it's one that you'd like to recognize the rights of the people from generation to generation their roots are there, the houses are there, all of the memories are there, it's really tough. And on the other hand you've got that free market theory that often times is great in theory but when applied to the real world it doesn't work that way. And I think this is one of those cases. Where the income to the state will actually be improved considerably because of the intimidation of going in, you've got three houses in a

row and you're going to bid on that lease in the middle. Where there's no way you're going to get along with the neighbor on either side of you for years. And it just inhibits the bidding process. I think the state would be better off financially, the schools with the system that's being proposed. Because of that intimidation factor. They'll be able to somehow arrive at somewhere close to a market value for those leases and the people are going to pay more than they would have if we'd left the old system in place I think. I think this is a good move for the state and I'm, the leaseholders, I'm sure will be happy until they, four or five years down the road when they have to pay more and more. And that's what they're facing.

S. Noh: Senator Donnelsly.

S. Donnelsly: Mr. Chairman, Senators. I've spent some time with Mr. Hamilton and his staff some months back and we talked about this for a couple of hours I think. It's truly a situation that I think needs to be addressed. As a matter of fact this morning and I think there is someone here named Jack who called me last night, yeah that was on the phone this morning first thing. And it is a hot issue. I would like to say just one thing, and that is I think that the bill is flawed because it doesn't give us a procedure once a lease has expired. I'm going to vote to send this out, but with the understanding among my fellow committee members that if somebody else doesn't bring one, I'm going to bring one to say that there's a right of first refusal to renew that should be written in any leases and should be implied into existing leases, because that's what's going to keep this thing from just being a wide-open bidding contest the next time a lease expires. I think just, that's a technical barrier that should be addressed and that's really the insurance for these people. The rest of it, the fee and what have you I think is addressed in the lease renewal market rent value analysis. Please don't be surprised if you see something following in the wings ?????

S. Noh: Well there may be some other aspects of this whole issue we would want to discuss at some point too. Senator Reed.

S. Reed: Well, Mr. Chairman, along that line, members of the committee. I think the Land Board has come to us to settle a policy question because it's kind of a hot potato and I think we're comfortable settling this particular policy question, but I think an awful lot of the questions that have come up today really relate to another policy which deals with the whole aspect of transfer. So I think we don't just need to deal with hot potatoes, perhaps, although there's nothing cool about the issue of transfer, but I think we really should put this on the legislative agenda and address that in the future. ??? should they be able to have assignments, and

big money and all this kind of stuff without passing along to the state their fair rate?

S. Noh: Any other discussion?

S. Beitelspacher: Yeah, Mr. Chairman. Just a couple of things. Members of the committee I got a letter here the other day and I'm sure some of you folks in Ada County have, along with this whole issue of what happens with the leases, there is an RV mobile home park called Lakeland Village, the state owned it, somehow someone died and the state has wound back up with it and now the state's going to look at doing something else with the land, and we're going to be hearing from people that lived there for, according to the letter I got, thirty some years. And all of a sudden they're going to have to uproot what they have and move. Be that as it may. The thing I don't understand about the return to the state, if I had a piece of ground and I was going to rent it or lease it, or sell it, I probably wouldn't go down in my basement, I certainly wouldn't go downstairs in the Idaho County Courthouse and put up a notice on the bulletin board, why in the devil don't you go to the realtors and put it on the open market like anybody else would. I'm at a loss to understand that. Maybe you could answer that for me.

S. Noh: Mr. Hamilton

Hamilton: Mr. Chairman. This will probably start a war.

S. Noh: Senator Bidelspacker, that's not fair to ask questions of agency heads and then get the budget book out. (laughter)

S. Tominaga: It's called intimidation.

S. Bidelspacker: Oh, Mr. Chairman, Stan, you really don't need to worry about your budget, I was going to look up and see what the income was. I wanted to follow that up. Why don't you put it out there. Who are you worrying about going to war with. Your job is not to keep these people from going to war, your job is to make sure that there is a return for the taxpayers of the state.

S. Noh: Mr. Hamilton

Hamilton: Mr. Chairman, the Board has had long standing policy that we would not advertise those leases. And beyond that I can't tell you. It's true that if we did advertise them I am sure we would have considerable interest in them from other places. It would essentially create exactly the situation that we're here today talking about, and I guess try to deal with. And the Department and the Board I

don't think have been very interested in trying to create that situation. Some of the comments about, if you're in the middle lot, if you conflicted and come into the middle lots, your neighbors aren't going to talk to you for probably twenty years. Because you'll still be the new kid on the block and they'll never forget how you got there.

S. Noh: Ok, any more discussion. Are you ready for the questions? All those in favor, anybody want a rollcall vote? All those folk in favor of the motion to go to the floor with a new pass, signify by saying aye.

Several voices "Aye."

S. Noh: Opposed no.

Two voices: "No."

S. Noh: The Chair is not in doubt, the ayes have it. A very difficult question. Senator Carlson.

S. Carlson: Mr. Chairman, it's so late I was going to move that they go back to the Land Board and they could settle this very easily, there's only five of them. (Laughter).

S. Noh: Ok, I guess we're adjourned.

Exhibit 29

Letter, IDL Director George Bacon to

Lawrence Wasden, Feb. 12, 2010

ADMINISTRATION
DIRECTOR'S OFFICE
300 North 6th St. Suite 103
Post Office Box 83720
Boise ID 83720-0050
Phone (208) 334-0200
Fax (208) 334-2339

IDAHO DEPARTMENT OF LANDS

GEORGE B. BACON, DIRECTOR
EQUAL OPPORTUNITY EMPLOYER

STATE BOARD OF LAND COMMISSIONERS
C.L. "Butch" Otter, Governor
Ben Ysursa, Secretary of State
Lawrence G. Wasden, Attorney General
Donna M. Jones, State Controller
Tom Luna, Sup't of Public Instruction

February 12, 2010

Lawrence G. Wasden, Attorney General
Office of the Attorney General
P.O. Box 83720
Boise, Idaho 83720-0010

Dear Attorney General Wasden:

Following is the department response to your February 11, 2010 letter, wherein you requested additional information and our opinion regarding the Cottage Site Subcommittee land board briefing material:

1. **How does the Subcommittee recommendation compare to the goals and objectives of the Land Board's Asset Management Plan with regard to cash return versus value appreciation?**
   The goal expressed in the asset management plan is to achieve a rate of return on investments by dividing the return equally between land appreciation and income to address the generational aspect of the board's trust mandate. For residential leases the target range is 3-12%, net of expenses. Assuming flat land value appreciation, net cash return under the Subcommittee recommendation would approximate 3.67%. Assuming a 10% year over year land value appreciation, net cash return would approximate 1.58%. Between 1997 and 2010, compound annual value appreciation averaged 4.8% at Priest Lake, 10.3% for Payette Lakefront and 6.3% for Payette second tier lots. Using these averages the cash return would approximate 2.43% at Priest Lake, 1.55% for Payette Waterfront and 2.14% for Payette second tier lots. Total return would average 7.23%, 11.85%, and 8.44%, respectively.

2. **Will the Subcommittee's recommendation "insure that each leased lot generates market rent throughout the duration of the lease"?**
   As stated in the PAG report, "Identifying market rent is complicated because of the unusual characteristics of the cottage site lease "market." First and foremost, ground leases for residential use are extremely rare (i.e. few states and private landowners do this sort of thing). Therefore there is no "market" for comparison purposes except, perhaps, other states. Other states have similar lands, but very different value and demand conditions which may not allow good comparisons. Also, the same political issues prevalent in cottage site leasing impacts other states, and even the federal government. Furthermore, the only sure way to establish market in Idaho, for Idaho properties, is to have regular competitive bidding. Currently, Title 58-310a precludes competitive bidding. Therefore, "market" is impossible to determine at any point in time; the best we can do is an approximation.

"Market" can be approximated over time. The competition or substitute demand for what we offer is the availability of fee simple properties for sale. Such demand will vary from lake to lake, and from time to time. It is further influenced by the availability of financing.

Based on the numerous studies previously commissioned and conducted by real estate experts, it appears as long as there is leasehold value, the rent charged is not at market. Even in today's "down" market, transactions are occurring with leasehold value on some properties (see Attachment 1).

The duration of the lease and other lease terms also will have some bearing on value to prospective purchasers.

The only system we can conceive that would guaranty that each leased lot will generate market rent throughout the duration of the lease is one where periodic conflict bidding is possible. We believe such a system can be easily derived, but 58-310a would have to be amended. Also, past experience tells us that conflict bidders are susceptible to intimidating behavior by organized lessees. To really achieve market, a system of sealed bidding or internet bidding would be needed.

I do not believe the Subcommittee's recommendation insures that each leased lot generates market rent throughout the duration of the lease, but neither does the current system.

3. **What are the financial implications of the Subcommittee's recommendation to extend the lease to 35 years?**
   - The longer term lease may increase the number of people interested and capable of leasing because improvements can be more readily financed with a 30-year mortgage.
   - If there were competitive bidding opportunities for a 35 year lease, it may increase the number of bidders and the return to the endowment.
   - If leases could be conflicted periodically i.e. every 5-10 years, the length of the lease may be of little importance, except for changes in land use proposed by the Department. In those cases, the Department would have to "buy-out" the lessees' improvements. However, the Department would have to first show that such an investment "paid-off" and would have to secure funding for that activity.
   - The longer term lease could foster speculative "investor" behavior and increase leasehold value.
   - Generally investors view long term transactions as bearing higher risk. Increased risk should be compensated by higher returns.
   - It seems incumbent on the Board to not commit to any long-term leases where rent methodologies have not been proved to meet the Board's Constitutional mandates and fiduciary responsibilities.
   - Likewise, long term leasing seems imprudent until the Board develops a long-term plan for this asset type, including what lands should be retained, acquired or disposed.

4. **What is the projected rate of return under the Subcommittee's recommendation?**
   The department agrees with the Subcommittee's use of a 10 year average lot value to help smooth lease payments. Resulting gross income as a percentage of 2010 values after phase-in equal 2.6% for Priest Lake lots and 2.7% of Payette Lake lots, compared to the current contract provisions yielding gross income of 2.5% of value (see Attachment 2). Because of recent rent freezes current rents yield cash returns of 1.3%-2.0%, depending on location (see Attachment 2). Future performance is difficult to determine. Attached are several worksheets that attempt to model performance using a variety of land value appreciation assumptions. Land value appreciation in excess of 5.2% appears to result in income performance less than the current contract rate (see Attachment 3).

5. **What is your opinion regarding the proposed lease terms?**
   We understand there are many positive changes to the lease language such as clarifying definitions, opening up the subleasing criteria, requiring annual verification of beneficiaries involved in leases held by a family trust, etc. However, we have not had an opportunity to review the final draft lease. We have heard the lease may contain language that requires the state to purchase improvements at inappropriate times, such as in a lease default, when improvements are not removed by the lessee, in a nonrenewal situation and other similar instances. Therefore, we cannot express an opinion without reviewing the final draft lease.

I hope this adequately addresses your questions.

Sincerely,

George B Bacon
Director

Attachments

Year	Month	Program	Instrument	Assignor Name	Assignee	Premium Rent	Full Sales Price	Leasehold Value	Assign Type	Area	Note
2008	Apr	Cottage	R1252	Dwight Calkins	Calkins Priest Lake Family Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2008	Aug	Cottage	R1104	David Stauffacher	Teresa Myrwang Holum	$63,378.60	$1,000,000.00	$633,786	Sale	Priest Lake	
2008	Aug	Cottage	R5209	Douglas Sabala	Sabala-Rose Trust, Douglas Savala Trustee	$0.00	$0.00	$0	Trust	Payette Lake	
2008	Feb	Cottage	R1021	Sandra Richards	Richards Family Priest Lake Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2008	Feb	Cottage	R5023	Richard Hoyle	Scott Suciu	$0.00	$0.00	$0	Family	Payette Lake	
2008	Jan	Cottage	R1123	Dale Reese	Frank Wagstaff	$17,000.00	$600,000.00	$170,000	Sale	Priest Lake	
2008	Jan	Cottage	R1196	Tana Mierz	Jack Lowrey	$0.00	$1.00	$0	Sale	Priest Lake	
2008	Jan	Cottage	R1202	George Manos	Darin Davidson	$39,223.40	$565,000.00	$392,234	Sale	Priest Lake	
2008	Jan	Cottage	R1301	Dale Peringer, Jr	Robert Ashton	$19,395.90	$575,000.00	$193,959	Sale	Priest Lake	
2008	Jan	Cottage	R5269	Richard A Mott	Richard T Mott	$0.00	$0.00	$0	Family	Payette Lake	
2008	Jan	Cottage	R5285	James Bunn	Carl Thomas	$7,881.00	$125,000.00	$78,810	Sale	Payette Lake	
2008	Jan	Cottage	R5287	Jennifer White	Serena Crowley	$0.00	$0.00	$0	Family	Payette Lake	
2008	July	Cottage	R1126	Hazel F O'Byrne	Mary K' O'Byrne	$0.00	$0.00	$0	Family	Priest Lake	
2008	July	Cottage	R1246	Eric & Jan Thompson	Eric Thompson	$0.00	$0.00	$0	Family	Priest Lake	
2008	July	Cottage	R5080	Marvin & Rebecca Strong	Zimmer Family Trust date 11/05/98; Trustees Edward E & Amy H Zimmer	$30,930.00	$800,000.00	$309,300	Sale	Payette Lake	
2008	Mar	Cottage	R5213	Andy Froehlke	Gregg Middlekauff	$12,305.00	$175,000.00	$123,050	Sale	Payette Lake	
2008	May	Cottage	R1166	Janean Edgemon	Edgemon Family Trust	$0.00	$0.00	$0	Family	Priest Lake	
2008	Nov	Cottage	R1140	Michael & Emma Sandau	David & Jan McRoberts	$45,573.10	$600,000.00	$455,731	Sale	Priest Lake	
2008	Nov	Cottage	R1269	Ron Mehlert & Karen Guthrie	John & Diane Brumley	$20,384.70	$250,000.00	$203,847	Sale	Priest Lake	
2008	Oct	Cottage	R1102	Darrell Irvin	Irvin Living Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2008	Oct	Cottage	R1235	Finley Trust, RW & NH	Jerald M Whitehead	$27,790.00	$575,000.00	$277,900	Sale	Priest Lake	
2008		Cottage	R5327	Christian & Terra Bourguignon	Patrick & Christine Miller	$0.00	$250,000.00	$0	Sale	Payette Lake	
2009	Apr	Cottage	R1064	Nancy Hanford	Hanford Family Priest Lake Cabin Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2009	Apr	Cottage	R1202	Darin Davidson	Ryan D Rein	$0.00	$0.00	$0	Trust	Priest Lake	
2009	Apr	Cottage	R1284	Anne Gilbert	James D Gunn	$33,057.10	$379,000.00	$330,571	Sale	Priest Lake	
2009	Apr	Cottage	R1310	Michael Day	Day/Wilson Family Living Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2009	Apr	Cottage	R5262	Shad Priest	Austin John Terry	$0.00	$0.00	$0	Family	Payette Lake	
2009	Apr	Cottage	R5346	Bruce Sherlock	Harvey & Kimberly Geis	$0.00	$0.00	$0	Family	Payette Lake	
2009	Apr	Cottage	R5350	Sarah Marie Mace	Steven M Hager	$0.00	$0.00	$0	Family	Payette Lake	
2009	Dec	Cottage	R1025	John Turner	John E Turner Living Trust dated May 10, 1995	$0.00	$0.00	$0	Family	Priest Lake	
2009	Dec	Cottage	R1357	Julie Pierce	Robert L. Delsman	$42,500.00	$425,000.00	$425,000	Sale	Priest Lake	
2009	Dec	Cottage	R5234	Pearman Trust	Steven Green	$1,386.00	$160,000.00	$13,860	Sale	Payette Lake	
2009	Feb	Cottage	R1246	Eric Thompson	Bryan & Mary Correll	$20,284.70	$235,000.00	$202,847	Sale	Priest Lake	

Year	Month	Program	Instrument	Assignor Name	Assignee	Premium Rent	Full Sales Price	Leasehold Value	Assign Type	Area	Note
2009	July	Cottage	R1001	William Norwood	Phippen Family Trust, John Phippen	$28,429.70	$500,000.00	$284,297	Sale	Priest Lake	
2009	July	Cottage	R1333	Alice E Chapman	G. Craig Lee and Sharon A. Lee	$0.00	$0.00	$0	Family	Priest Lake	
2009	July	Cottage	R1335	James E Lemping	Lamping/Ryan Cabin Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2009	June	Cottage	R1110	Dorothy Puryear	Elizabeth Puryear	$0.00	$0.00	$0	Family	Priest Lake	
2009	Mar	Cottage	R5243	Boyce Trust	Richard W Hoyle	$0.00	$70,000.00	$0	Sale	Payette Lake	
2009	May	Cottage	R1153	Jeanne H Gregg Trust	The Gregg Daughter's Recipient Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2009	May	Cottage	R1257	Kenneth Boone	Priest Lake Lot H Revocable Trust	$0.00	$0.00	$0	Trust	Priest Lake	
2009	May	Cottage	R1292	Nicol Living Trust	Carol Nicol Valk	$0.00	$0.00	$0	Trust	Priest Lake	
2009	Nov	Cottage	R5056	Craig A Sinkinson	Wendy M Edmunds	$0.00	$0.00	$0	Family	Payette Lake	This assignment is per court judgement - see file for order
2009	Nov	Cottage	R5071	James P Baker	Ronald W Guill	$70,650.00	$1,200,000.00	$706,500	Sale	Payette Lake	
2009	Oct	Cottage	R5064	James Blasco	Graye H. Wolfe	$56,962.00	$1,175,000.00	$569,620	Sale	Payette Lake	
2009	Oct	Cottage	R5073	William McGlynn	Christopher Thompson	$30,487.00	$715,000.00	$304,870	Sale	Payette Lake	
2009	Sept	Cottage	R1180	Kevin Bond	Scott Naccarato	$21,444.60	$350,000.00	$214,446	Sale	Priest Lake	
2009	Sept	Cottage	R5901	Stuart Toomey	John L Simmons	$23,668.00	$335,000.00	$236,680	Sale	Payette Lake	
2010	Jan	Cottage	R5225	Michael Marrs	Shawn & Juliene Benner	$2,233.00	$90,000.00	$22,330	Sale	Payette Lake	
2010	Feb	Cottage	R1018	Matthew & Darcie Becker	Thomas & Kathleen Trotter	$24,240.10	$400,000.00	$242,401	Sale	Priest Lake	
						$639,203.90		$6,392,039			

CABIN SITE PROJECTIONS
ANNUAL RENT and RETURNS

Method	RATE * 10 YEAR AVERAGE with 5 year phase in at a constant percentage rate
Rate	4.0%

Value Increase(Decrease) VALUE[1]		10 Year Average	
Calendar Year	2010	2002-2011	Variance
Priest Lake	152,995,367	98,391,109	(54,604,258)
Payette Lake Waterfront	86,235,870	57,561,691	(28,674,180)
Payette Lake 2nd Tier	12,662,202	8,666,265	(3,995,937)
TOTAL	251,893,440	164,619,065	(87,274,375)

RENT	2010 FROZEN	2011	2012	2013	2014	2015
Priest Lake	2,537,791	2,769,981	3,023,733	3,301,077	3,604,236	3,935,644
Payette Lake Waterfront	1,552,582	1,679,621	1,817,205	1,966,220	2,127,626	2,302,468
Payette Lake 2nd Tier	177,558	202,826	231,778	264,962	303,010	346,651
TOTAL	4,267,932	4,652,429	5,072,716	5,532,259	6,034,872	6,584,763

RENT % Increase(Decrease)	2010	2011	2012	2013	2014	2015
Priest Lake	0.0%	9.1%	9.2%	9.2%	9.2%	9.2%
Payette Lake Waterfront	0.0%	8.2%	8.2%	8.2%	8.2%	8.2%
Payette Lake 2nd Tier	0.0%	14.2%	14.3%	14.3%	14.4%	14.4%
Total	0.0%	9.0%	9.0%	9.1%	9.1%	9.1%

Effective Rate Rent/Asset Value)	Rent/2009 Asset Value	Rent/ 2010 Asset Value	Rent/ 2010 Asset Value	Rent/ 2010 Asset Value	Rent/ 2010 Asset Value	Rent/ 2010 Asset Value
Priest Lake	2.0%	1.8%	2.0%	2.2%	2.4%	2.6%
Payette Lake Waterfront	1.7%	1.9%	2.1%	2.3%	2.5%	2.7%
Payette Lake 2nd Tier	1.3%	1.6%	1.8%	2.1%	2.4%	2.7%
Total	1.7%	1.8%	2.0%	2.2%	2.4%	2.6%
Discount from Contract Rate - Due to 10 yr. value averaging						
Contract Rate Prior to 2010	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%
Priest Lake	-0.5%	-0.7%	-0.5%	-0.3%	-0.1%	0.1%
Payette Lake Waterfront	-0.8%	-0.6%	-0.4%	-0.2%	0.0%	0.2%
Payette Lake 2nd Tier	-1.2%	-0.9%	-0.7%	-0.4%	-0.1%	0.2%
Total	-0.8%	-0.7%	-0.5%	-0.3%	-0.1%	0.1%

[1]The Value used to calculate rent for the respective year.
Assumes 2009 values remain flat for 2010.

NO LAND APPRECIATION

RENT BASE YEARS	10	9	8	7	6	5	4	3	2	1
LOT VALUE	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000
2.5% RENT	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500
RENTAL RATE	4.00%									
LAND APPRECIATION	0.00%									
COSTS	6.00%									

LEASE YEAR	1	2	3	4	5	6	7	8	9	10
LOT VALUE	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000
2.5% RENT	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500
INCOME	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 500,000					$ 500,000				
TARGET RENT	$ 20,000					$ 20,000				
CONSTANT INCREASE	9.86%					0.00%				
RENT	$ 13,732	$ 15,085	$ 16,572	$ 18,206	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000
INCOME	$ 12,908	$ 14,180	$ 15,578	$ 17,113	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800
CONTRACT RATE	2.75%	3.02%	3.31%	3.64%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
EFFECTIVE RATE	2.58%	2.84%	3.12%	3.42%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	11	12	13	14	15	16	17	18	19	20
LOT VALUE	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000
2.5% RENT	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500
INCOME	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 500,000					$ 500,000				
TARGET RENT	$ 20,000					$ 20,000				
CONSTANT INCREASE	0.00%					0.00%				
RENT	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000
INCOME	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800
CONTRACT RATE	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
EFFECTIVE RATE	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	21	22	23	24	25	26	27	28	29	30
LOT VALUE	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000
2.5% RENT	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500
INCOME	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 500,000					$ 500,000				
TARGET RENT	$ 20,000					$ 20,000				
CONSTANT INCREASE	0.00%					0.00%				
RENT	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000
INCOME	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800
CONTRACT RATE	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
EFFECTIVE RATE	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%	3.76%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	31	32	33	34	35
LOT VALUE	$ 500,000	$ 500,000	$ 500,000	$ 500,000	$ 500,000
2.5% RENT	$ 12,500	$ 12,500	$ 12,500	$ 12,500	$ 12,500
INCOME	$ 11,750	$ 11,750	$ 11,750	$ 11,750	$ 11,750
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 500,000				
TARGET RENT	$ 20,000				
CONSTANT INCREASE	0.00%				
RENT	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000
INCOME	$ 18,800	$ 18,800	$ 18,800	$ 18,800	$ 18,800
CONTRACT RATE	4.00%	4.00%	4.00%	4.00%	4.00%
EFFECTIVE RATE	3.76%	3.76%	3.76%	3.76%	3.76%

TOTAL OF ALL LOT VALUES	$ 17,500,000
TOTAL OF ALL 2.5% RENTS	$ 437,500
TOTAL INCOME	$ 411,250
EFFECTIVE RATE	2.35%
TOTAL OF ALL 4% RENT	$ 683,595
TOTAL INCOME	$ 642,580
CONTRACT RATE	3.91%
EFFECTIVE RATE	3.67%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

4.80% LAND APPRECIATION

RENT BASE YEARS	10	9	8	7	6	5	4	3	2	1
LOT VALUE	$ 500,000	$ 524,000	$ 549,152	$ 575,511	$ 603,138	$ 632,088	$ 662,427	$ 694,225	$ 727,546	$ 762,468
2.5% RENT	$ 12,500	$ 13,100	$ 13,729	$ 14,388	$ 15,078	$ 15,802	$ 16,561	$ 17,356	$ 18,189	$ 19,062
RENTAL RATE	2.400%									
LAND APPRECIATION	4.80%									
COSTS	6.00%									

LEASE YEAR	1	2	3	4	5	6	7	8	9	10
LOT VALUE	$ 799,066	$ 837,422	$ 877,618	$ 919,744	$ 963,891	$ 1,010,158	$ 1,058,645	$ 1,109,460	$ 1,162,715	$ 1,218,525
2.5% RENT	$ 19,977	$ 20,936	$ 21,940	$ 22,994	$ 24,097	$ 25,254	$ 26,466	$ 27,737	$ 29,068	$ 30,463
INCOME	$ 18,778	$ 19,679	$ 20,624	$ 21,614	$ 22,653	$ 23,739	$ 24,878	$ 26,072	$ 27,324	$ 28,635
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 623,055					$ 787,649				
TARGET RENT	$ 24,922					$ 31,506				
CONSTANT INCREASE	5.51%					4.80%				
RENT	$ 20,112	$ 21,219	$ 22,388	$ 23,621	$ 24,922	$ 26,118	$ 27,372	$ 28,686	$ 30,063	$ 31,506
INCOME	$ 18,905	$ 19,946	$ 21,045	$ 22,204	$ 23,427	$ 24,551	$ 25,730	$ 26,965	$ 28,259	$ 29,616
CONTRACT RATE	2.52%	2.53%	2.55%	2.57%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%
EFFECTIVE RATE	2.37%	2.38%	2.40%	2.41%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	11	12	13	14	15	16	17	18	19	20
LOT VALUE	$ 1,277,014	$ 1,338,311	$ 1,402,450	$ 1,469,872	$ 1,540,426	$ 1,614,366	$ 1,691,856	$ 1,773,065	$ 1,858,172	$ 1,947,364
2.5% RENT	$ 31,925	$ 33,458	$ 35,064	$ 36,747	$ 38,511	$ 40,359	$ 42,296	$ 44,327	$ 46,454	$ 48,684
INCOME	$ 30,010	$ 31,450	$ 32,960	$ 34,542	$ 36,200	$ 37,938	$ 39,759	$ 41,667	$ 43,667	$ 45,763
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 995,724					$ 1,258,768				
TARGET RENT	$ 39,829					$ 50,351				
CONSTANT INCREASE	4.80%					4.80%				
RENT	$ 33,018	$ 34,603	$ 36,264	$ 38,005	$ 39,829	$ 41,741	$ 43,744	$ 45,844	$ 48,045	$ 50,351
INCOME	$ 31,037	$ 32,527	$ 34,088	$ 35,724	$ 37,439	$ 39,236	$ 41,120	$ 43,093	$ 45,162	$ 47,330
CONTRACT RATE	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%
EFFECTIVE RATE	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	21	22	23	24	25	26	27	28	29	30
LOT VALUE	$ 2,040,838	$ 2,138,798	$ 2,241,460	$ 2,349,050	$ 2,461,805	$ 2,579,971	$ 2,703,810	$ 2,833,593	$ 2,969,605	$ 3,112,146
2.5% RENT	$ 51,021	$ 53,470	$ 56,037	$ 58,726	$ 61,545	$ 64,499	$ 67,595	$ 70,840	$ 74,240	$ 77,804
INCOME	$ 47,960	$ 50,262	$ 52,674	$ 55,203	$ 57,852	$ 60,629	$ 63,540	$ 66,589	$ 69,786	$ 73,135
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 1,591,300					$ 2,011,677				
TARGET RENT	$ 63,652					$ 80,467				
CONSTANT INCREASE	4.80%					4.80%				
RENT	$ 52,768	$ 55,300	$ 57,955	$ 60,737	$ 63,652	$ 66,707	$ 69,909	$ 73,265	$ 76,782	$ 80,467
INCOME	$ 49,601	$ 51,982	$ 54,478	$ 57,092	$ 59,833	$ 62,705	$ 65,715	$ 68,869	$ 72,175	$ 75,639
CONTRACT RATE	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%	2.59%
EFFECTIVE RATE	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%	2.43%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	31	32	33	34	35
LOT VALUE	$ 3,261,525	$ 3,418,083	$ 3,587,151	$ 3,754,094	$ 3,934,291
2.5% RENT	$ 81,538	$ 85,452	$ 89,554	$ 93,852	$ 98,357
INCOME	$ 76,646	$ 80,325	$ 84,181	$ 88,221	$ 92,456
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 2,543,108				
TARGET RENT	$ 101,724				
CONSTANT INCREASE	4.80%				
RENT	$ 84,330	$ 88,377	$ 92,619	$ 97,065	$ 101,724
INCOME	$ 79,270	$ 83,075	$ 87,062	$ 91,241	$ 95,621
CONTRACT RATE	2.59%	2.59%	2.59%	2.59%	2.59%
EFFECTIVE RATE	2.43%	2.43%	2.43%	2.43%	2.43%

TOTAL OF ALL LOT VALUES	$ 69,261,464
TOTAL OF ALL 2.5% RENTS	$ 1,731,287
TOTAL INCOME	$ 1,627,409
EFFECTIVE RATE	2.35%
TOTAL OF ALL 4% RENT	$ 1,789,109
TOTAL INCOME	$ 1,681,762
CONTRACT RATE	2.58%
EFFECTIVE RATE	2.43%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

5.20% LAND APPRECIATION

RENT BASE YEARS	10	9	8	7	6	5	4	3	2	1
LOT VALUE	$ 500,000	$ 526,000	$ 553,352	$ 582,176	$ 612,497	$ 644,241	$ 677,747	$ 712,985	$ 750,060	$ 788,985
2.5% RENT	$ 12,500	$ 13,150	$ 13,834	$ 14,553	$ 15,310	$ 16,106	$ 16,944	$ 17,825	$ 18,751	$ 19,727
RENTAL RATE	4.00%									
LAND APPRECIATION	5.20%									
COSTS	6.00%									

LEASE YEAR	1	2	3	4	5	6	7	8	9	10
LOT VALUE	$ 830,094	$ 873,259	$ 918,669	$ 966,430	$ 1,016,694	$ 1,069,562	$ 1,125,180	$ 1,183,689	$ 1,245,241	$ 1,309,993
2.5% RENT	$ 20,752	$ 21,831	$ 22,967	$ 24,161	$ 25,417	$ 26,739	$ 28,129	$ 29,592	$ 31,131	$ 32,750
INCOME	$ 19,507	$ 20,522	$ 21,589	$ 22,714	$ 23,892	$ 25,135	$ 26,442	$ 27,817	$ 29,263	$ 30,785
EFFEGTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 634,797					$ 817,925				
TARGET RENT	$ 25,392					$ 32,717				
CONSTANT INCREASE	5.18%					5.20%				
RENT	$ 20,748	$ 21,823	$ 22,953	$ 24,142	$ 25,392	$ 26,712	$ 28,101	$ 29,563	$ 31,100	$ 32,717
INCOME	$ 19,503	$ 20,513	$ 21,576	$ 22,693	$ 23,868	$ 25,110	$ 26,415	$ 27,789	$ 29,234	$ 30,754
CONTRACT RATE	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	11	12	13	14	15	16	17	18	19	20
LOT VALUE	$ 1,378,113	$ 1,449,775	$ 1,525,168	$ 1,604,472	$ 1,687,904	$ 1,775,675	$ 1,868,010	$ 1,965,147	$ 2,067,334	$ 2,174,836
2.5% RENT	$ 34,453	$ 36,244	$ 38,129	$ 40,112	$ 42,198	$ 44,392	$ 46,700	$ 49,129	$ 51,683	$ 54,371
INCOME	$ 32,386	$ 34,070	$ 35,841	$ 37,705	$ 39,666	$ 41,728	$ 43,898	$ 46,181	$ 48,582	$ 51,109
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 1,053,882					$ 1,357,909				
TARGET RENT	$ 42,155					$ 54,316				
CONSTANT INCREASE	5.20%					5.20%				
RENT	$ 34,418	$ 36,208	$ 38,091	$ 40,072	$ 42,155	$ 44,347	$ 46,653	$ 49,079	$ 51,632	$ 54,316
INCOME	$ 32,353	$ 34,036	$ 35,805	$ 37,667	$ 39,626	$ 41,687	$ 43,854	$ 46,135	$ 48,534	$ 51,057
CONTRACT RATE	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	21	22	23	24	25	26	27	28	29	30
LOT VALUE	$ 2,287,927	$ 2,406,899	$ 2,532,058	$ 2,663,725	$ 2,802,239	$ 2,947,955	$ 3,101,249	$ 3,262,514	$ 3,432,165	$ 3,610,687
2.5% RENT	$ 57,198	$ 60,172	$ 63,301	$ 66,593	$ 70,056	$ 73,699	$ 77,531	$ 81,563	$ 85,804	$ 90,266
INCOME	$ 53,766	$ 56,562	$ 59,503	$ 62,588	$ 65,853	$ 69,277	$ 72,879	$ 76,669	$ 80,656	$ 84,850
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 1,749,643					$ 2,254,385				
TARGET RENT	$ 69,986					$ 90,175				
CONSTANT INCREASE	5.20%					5.20%				
RENT	$ 57,141	$ 60,112	$ 63,238	$ 66,526	$ 69,986	$ 73,625	$ 77,453	$ 81,481	$ 85,718	$ 90,175
INCOME	$ 53,712	$ 56,505	$ 59,444	$ 62,535	$ 65,787	$ 69,207	$ 72,806	$ 76,592	$ 80,575	$ 84,765
CONTRACT RATE	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

LEASE YEAR	31	32	33	34	35
LOT VALUE	$ 3,798,380	$ 3,995,907	$ 4,203,694	$ 4,422,286	$ 4,652,245
2.5% RENT	$ 94,960	$ 99,898	$ 105,092	$ 110,557	$ 116,306
INCOME	$ 89,262	$ 93,904	$ 98,787	$ 103,924	$ 109,328
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 2,904,737				
TARGET RENT	$ 116,189				
CONSTANT INCREASE	5.20%				
RENT	$ 94,865	$ 99,797	$ 104,987	$ 110,446	$ 116,189
INCOME	$ 89,173	$ 93,810	$ 98,688	$ 103,819	$ 109,218
CONTRACT RATE	2.50%	2.50%	2.50%	2.50%	2.50%
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%

TOTAL OF ALL LOT VALUES	$ 78,155,139
TOTAL OF ALL 2.5% RENTS	$ 1,953,878
TOTAL INCOME	$ 1,836,646
EFFECTIVE RATE	2.35%
TOTAL OF ALL 4% RENT	$ 1,951,963
TOTAL INCOME	$ 1,834,845
CONTRACT RATE	2.50%
EFFECTIVE RATE	2.35%

CURRENT 2.5% RENT METHOD

PROPOSED 4% RENT METHOD

6.30% LAND APPRECIATION

RENT BASE YEARS	1	2	3	4	5	6	7	8	9	10
LOT VALUE	$ 500,000	$ 531,500	$ 564,985	$ 600,579	$ 638,415	$ 678,165	$ 721,389	$ 766,837	$ 815,147	$ 866,502
2.5% RENT	$ 12,500	$ 13,288	$ 14,125	$ 15,014	$ 15,960	$ 16,955	$ 18,035	$ 19,171	$ 20,379	$ 21,663
RENTAL RATE	4.00%									
LAND APPRECIATION	6.30%									
COSTS	6.00%									

LEASE YEAR	1	2	3	4	5	6	7	8	9	10	
LOT VALUE	$ 921,091	$ 979,120	$ 1,040,805	$ 1,106,375	$ 1,176,077	$ 1,250,170	$ 1,328,930	$ 1,412,663	$ 1,501,650	$ 1,596,254	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 23,027	$ 24,478	$ 26,020	$ 27,659	$ 29,402	$ 31,254	$ 33,223	$ 35,316	$ 37,541	$ 39,906	
INCOME	$ 21,646	$ 23,009	$ 24,459	$ 26,000	$ 27,638	$ 29,379	$ 31,230	$ 33,197	$ 35,289	$ 37,612	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 668,399					$ 907,198					
TARGET RENT	$ 26,736					$ 36,288					
CONSTANT INCREASE	4.30%					6.30%					PROPOSED 4% RENT METHOD
RENT	$ 22,594	$ 23,565	$ 24,578	$ 25,634	$ 26,736	$ 28,420	$ 30,211	$ 32,114	$ 34,137	$ 36,288	
INCOME	$ 21,238	$ 22,151	$ 23,103	$ 24,096	$ 25,132	$ 26,715	$ 28,398	$ 30,187	$ 32,089	$ 34,111	
CONTRACT RATE	2.45%	2.41%	2.36%	2.32%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	
EFFECTIVE RATE	2.31%	2.26%	2.22%	2.18%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	

LEASE YEAR	11	12	13	14	15	16	17	18	19	20	
LOT VALUE	$ 1,696,818	$ 1,803,218	$ 1,917,362	$ 2,038,145	$ 2,166,548	$ 2,303,041	$ 2,448,432	$ 2,602,369	$ 2,766,314	$ 2,940,591	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 42,420	$ 45,093	$ 47,934	$ 50,954	$ 54,164	$ 57,576	$ 61,203	$ 65,059	$ 69,158	$ 73,515	
INCOME	$ 39,879	$ 42,387	$ 45,058	$ 47,896	$ 50,914	$ 54,121	$ 57,531	$ 61,158	$ 65,008	$ 69,104	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 1,231,313					$ 1,671,224					
TARGET RENT	$ 49,253					$ 66,849					
CONSTANT INCREASE	6.30%					6.30%					PROPOSED 4% RENT METHOD
RENT	$ 38,574	$ 41,004	$ 43,587	$ 46,333	$ 49,253	$ 52,355	$ 55,654	$ 59,160	$ 62,887	$ 66,849	
INCOME	$ 36,260	$ 38,544	$ 40,972	$ 43,553	$ 46,297	$ 49,214	$ 52,315	$ 55,610	$ 59,114	$ 62,838	
CONTRACT RATE	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	
EFFECTIVE RATE	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	

LEASE YEAR	21	22	23	24	25	26	27	28	29	30	
LOT VALUE	$ 3,125,849	$ 3,327,777	$ 3,532,112	$ 3,754,635	$ 3,991,127	$ 4,242,621	$ 4,509,906	$ 4,794,030	$ 5,096,054	$ 5,417,106	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 78,146	$ 83,069	$ 88,303	$ 93,866	$ 99,779	$ 106,066	$ 112,748	$ 119,851	$ 127,401	$ 135,428	
INCOME	$ 73,457	$ 78,085	$ 83,005	$ 88,234	$ 93,793	$ 99,702	$ 105,983	$ 112,660	$ 119,757	$ 127,302	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 2,268,302					$ 3,078,699					
TARGET RENT	$ 90,732					$ 123,148					
CONSTANT INCREASE	6.30%					6.30%					PROPOSED 4% RENT METHOD
RENT	$ 71,060	$ 75,537	$ 80,296	$ 85,355	$ 90,732	$ 96,448	$ 102,524	$ 108,983	$ 115,849	$ 123,148	
INCOME	$ 66,797	$ 71,005	$ 75,478	$ 80,233	$ 85,288	$ 90,661	$ 96,373	$ 102,444	$ 108,898	$ 115,759	
CONTRACT RATE	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	2.27%	
EFFECTIVE RATE	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	2.14%	

LEASE YEAR	31	32	33	34	35	
LOT VALUE	$ 5,758,384	$ 6,121,162	$ 6,506,795	$ 6,916,723	$ 7,352,478	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 143,960	$ 153,029	$ 162,670	$ 172,918	$ 183,812	
INCOME	$ 135,322	$ 143,847	$ 152,910	$ 162,543	$ 172,783	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 4,178,627					
TARGET RENT	$ 167,145					
CONSTANT INCREASE	6.30%					PROPOSED 4% RENT METHOD
RENT	$ 130,906	$ 139,153	$ 147,920	$ 157,239	$ 167,145	
INCOME	$ 123,052	$ 130,804	$ 139,045	$ 147,805	$ 157,116	
CONTRACT RATE	2.27%	2.27%	2.27%	2.27%	2.27%	
EFFECTIVE RATE	2.14%	2.14%	2.14%	2.14%	2.14%	

TOTAL OF ALL LOT VALUES	$ 109,437,956	CURRENT 2.5% RENT METHOD
TOTAL OF ALL 2.5% RENTS	$ 2,735,949	
TOTAL INCOME	$ 2,574,792	
EFFECTIVE RATE	2.35%	
TOTAL OF ALL 4% RENT	$ 2,492,232	PROPOSED 4% RENT METHOD
TOTAL INCOME	$ 2,342,698	
CONTRACT RATE	2.28%	
EFFECTIVE RATE	2.14%	

10.30% LAND APPRECIATION

RENT BASE YEARS	10	9	8	7	6	5	4	3	2	1
LOT VALUE	$ 500,000	$ 551,500	$ 608,305	$ 670,960	$ 740,069	$ 816,296	$ 900,374	$ 993,133	$ 1,095,405	$ 1,208,230
2.5% RENT	$ 12,500	$ 13,788	$ 15,208	$ 16,774	$ 18,502	$ 20,407	$ 22,509	$ 24,828	$ 27,385	$ 30,206
RENTAL RATE	4.00%									
LAND APPRECIATION	10.30%									
COSTS	6.00%									

LEASE YEAR	1	2	3	4	5	6	7	8	9	10	
LOT VALUE	$ 1,332,678	$ 1,469,943	$ 1,621,348	$ 1,788,346	$ 1,972,546	$ 2,175,718	$ 2,399,817	$ 2,646,999	$ 2,919,639	$ 3,220,362	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 33,317	$ 36,749	$ 40,534	$ 44,709	$ 49,314	$ 54,393	$ 59,995	$ 66,175	$ 72,991	$ 80,509	
INCOME	$ 31,318	$ 34,544	$ 38,102	$ 42,026	$ 46,355	$ 51,129	$ 56,396	$ 62,204	$ 68,612	$ 75,679	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 808,425					$ 1,319,828					
TARGET RENT	$ 32,337					$ 52,793					
CONSTANT INCREASE	1.37%					10.30%					PROPOSED 4% RENT METHOD
RENT	$ 30,620	$ 31,041	$ 31,467	$ 31,899	$ 32,337	$ 35,668	$ 39,341	$ 43,394	$ 47,863	$ 52,793	
INCOME	$ 28,783	$ 29,178	$ 29,579	$ 29,985	$ 30,397	$ 33,528	$ 36,981	$ 40,790	$ 44,991	$ 49,626	
CONTRACT RATE	2.30%	2.11%	1.94%	1.78%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	
EFFECTIVE RATE	2.16%	1.99%	1.82%	1.68%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	

LEASE YEAR	11	12	13	14	15	16	17	18	19	20	
LOT VALUE	$ 3,552,060	$ 3,917,922	$ 4,321,468	$ 4,766,579	$ 5,257,637	$ 5,799,063	$ 6,396,366	$ 7,055,192	$ 7,781,877	$ 8,583,410	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 88,801	$ 97,948	$ 108,037	$ 119,164	$ 131,438	$ 144,977	$ 159,909	$ 176,380	$ 194,547	$ 214,585	
INCOME	$ 83,473	$ 92,071	$ 101,554	$ 112,015	$ 123,552	$ 136,278	$ 150,315	$ 165,797	$ 182,874	$ 201,710	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 2,154,740					$ 3,517,810					
TARGET RENT	$ 86,190					$ 140,712					
CONSTANT INCREASE	10.30%					10.30%					PROPOSED 4% RENT METHOD
RENT	$ 58,231	$ 64,229	$ 70,844	$ 78,141	$ 86,190	$ 95,067	$ 104,859	$ 115,660	$ 127,572	$ 140,712	
INCOME	$ 54,737	$ 60,375	$ 66,593	$ 73,453	$ 81,018	$ 89,363	$ 98,567	$ 108,720	$ 119,918	$ 132,270	
CONTRACT RATE	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	
EFFECTIVE RATE	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	

LEASE YEAR	21	22	23	24	25	26	27	28	29	30	
LOT VALUE	$ 9,467,501	$ 10,442,654	$ 11,518,247	$ 12,704,627	$ 14,013,203	$ 15,456,363	$ 17,048,589	$ 18,804,594	$ 20,741,467	$ 22,877,838	CURRENT 2.5% RENT METHOD
2.5% RENT	$ 236,688	$ 261,066	$ 287,956	$ 317,616	$ 350,330	$ 386,414	$ 426,215	$ 470,115	$ 518,537	$ 571,946	
INCOME	$ 222,486	$ 245,402	$ 270,679	$ 298,559	$ 329,310	$ 363,229	$ 400,642	$ 441,908	$ 487,424	$ 537,629	
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	2.35%	
TEN YEAR AVERAGE	$ 5,743,147					$ 9,376,214					
TARGET RENT	$ 229,726					$ 375,049					
CONSTANT INCREASE	10.30%					10.30%					PROPOSED 4% RENT METHOD
RENT	$ 155,206	$ 171,192	$ 188,825	$ 208,274	$ 229,726	$ 253,388	$ 279,487	$ 308,274	$ 340,026	$ 375,049	
INCOME	$ 145,893	$ 160,920	$ 177,495	$ 195,777	$ 215,942	$ 238,184	$ 262,717	$ 289,777	$ 319,624	$ 352,546	
CONTRACT RATE	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	1.64%	
EFFECTIVE RATE	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	1.54%	

LEASE YEAR	31	32	33	34	35
LOT VALUE	$ 25,234,256	$ 27,833,484	$ 30,700,723	$ 33,862,346	$ 37,350,167
2.5% RENT	$ 630,856	$ 695,835	$ 767,506	$ 846,559	$ 933,754
INCOME	$ 593,005	$ 654,085	$ 721,455	$ 795,765	$ 877,729
EFFECTIVE RATE	2.35%	2.35%	2.35%	2.35%	2.35%
TEN YEAR AVERAGE	$ 15,307,529				
TARGET RENT	$ 612,301				
CONSTANT INCREASE	10.30%				
RENT	$ 413,679	$ 456,287	$ 503,285	$ 555,123	$ 612,301
INCOME	$ 388,858	$ 428,910	$ 473,088	$ 521,816	$ 575,563
CONTRACT RATE	1.64%	1.64%	1.64%	1.64%	1.64%
EFFECTIVE RATE	1.54%	1.54%	1.54%	1.54%	1.54%

TOTAL OF ALL LOT VALUES	$ 387,034,533	CURRENT 2.5% RENT METHOD
TOTAL OF ALL 2.5% RENTS	$ 9,675,863	
TOTAL INCOME	$ 9,095,312	
EFFECTIVE RATE	2.35%	
TOTAL OF ALL 4% RENT	$ 6,368,048	PROPOSED 4% RENT METHOD
TOTAL INCOME	$ 5,985,965	
CONTRACT RATE	1.65%	
EFFECTIVE RATE	1.55%	

Exhibit 30

Terry L. Anderson and Reed Watson,

Report to Idaho Attorney General Regarding Cottage Site Leases (2010)

REPORT TO IDAHO ATTORNEY GENERAL REGARDING COTTAGE SITE LEASES

Terry L. Anderson and Reed Watson

Scope of Report

The Idaho Attorney General's office requested an evaluation of several issues related to the Idaho Department of Lands Cottage Site Lease Program. The question of primary concern is whether the Cottage Site Lease Program as administered by the Board of Land Commissioners is consistent with its fiduciary duty as a trustee of the endowment lands. As requested, this report also provides a review of methodologies used and conclusions reached in existing cottage site market analysis reports prepared for the Idaho Department of Lands. This report concludes with our recommendation for a long-term cottage site management strategy in conformance with the "prudent investor rule," as defined by Idaho Code § 68-502.

Introduction

State endowment lands leased for single-family recreational cottage sites are unlike other public lands in that they are designed specifically to generate revenue for state institutions such as schools. They are not designed to provide free or subsidized recreation, low cost timber or grazing, or a stimulus to the economy. Article IX, Section 8 of the Idaho Constitution requires the Land Board manage state lands in such a way "as will secure the maximum long-term financial return" for endowment beneficiaries. The Idaho State Board of Land Commissioners specifically acknowledges and accepts its duty to "invest and manage the land trusts 'as a prudent investor would" and in so doing to "ensure real returns for each endowment . . . perform at or above [the] median compared to relevant peers"(State Trust Lands Asset Management Plan 2007, 4, 16)

In 1990, the Idaho Legislature enacted Idaho Code § 58-310A(3), which requires the Idaho State Board of Land Commissioners to "insure that each leased lot generates market rent throughout the duration of the lease." This statutory requirement is premised on the legislative finding that "maximum long-term financial returns to the institutions to which granted are best obtained through stable leases at market rent" (Idaho Code §58-310A(1)(h)). However, in our opinion, securing market rent through stable leases does not guarantee that the Land Board is maximizing the long-term returns. Thus, we conducted separate inquiries into whether the Land Board is fulfilling its statutory and constitutional duties.

History of the Cottage Site Leasing Program

The difficulty in assessing whether the Land Board is meeting its constitutional and statutory duties is evident in the history of this leasing program. Residential cottage site leasing began in 1924, though most cottage sites were not leased until the mid 1940s or early 1950s

(Cook and O'Laughlin 2008, 1). Initial contract rents were nominal, with rents for Priest Lake lots in 1945 set as low as $10 per year (Knipe 1998, 109). Rents were held relatively flat from 1945 to 1988, and no rent increases occurred from 1947 to 1961 (Knipe 1998, 109). In 1987, the Land Board adopted a flat contract rate of 2.5 percent of the cottage site market value, but a year later decided to phase-in corresponding rate increases over a ten year period. In 1986, the Department of Lands estimated that the state was currently receiving a return on asset value of 0.67 percent for all cottage site leases (Land Board Minutes, June 25,1986).

In 1990, the Idaho Legislature enacted Idaho Code § 58-310A. Subsection 2 of that statute exempts recreational cottage sites from the conflict application and auction provisions of the Idaho code. This exemption has the effect of removing market competition from the Cottage Site Leasing Program by prohibiting the Land Board from considering any and all conflict applications. Nonetheless, Idaho Code § 58-310A (3) requires the Land Board to ensure that each lot generate "market rent" throughout the duration of the lease. Together these mandates require the Department of Land to charge a contract rental rate equal to a "market rate" *estimated* by appraisal rather than *observed* through the conflict auction process. This approach is inherently inconsistent with an economic definition of a market.

In 1998, the Land Board commissioned appraisal reports for Payette and Priest Lake cottage sites. These were prepared by Bradford T. Knipe and John McFaddin, respectively, and both reports recommended higher rental rates than the existing 2.5 percent contract rate (Knipe 1998, 161; McFaddin 1998, 23). Both reports also noted that assignable cottage site leases have positive leasehold values (sales price less improvement value) and that the Land Board in 1981 adopted its "premium rent" policy which allows lessees to retain 90 percent of any leasehold value. These two facts offer compelling evidence of below market contract rates and, consequently, below market rent from cottage site leases (Knipe 1998, 151).

Market Rent - The Statutory Duty

Article IX, Section 8 of the Idaho Constitution requires the Land Board manage state lands in such a way "as will secure the maximum long-term financial return" for endowment beneficiaries. Based on the assumption that "maximum long-term financial returns . . . are best obtained through stable leases at market rent," the Idaho Legislature has interpreted the constitutional provision as requiring the Land Board to "insure that each leased lot generates market rent throughout the duration of the lease" (Idaho Code §58-310A). As previously noted, the efficacy of this assumption is questionable from an economic perspective.

"Market rent" is defined as the rental income that a property would most probably command in the open market (McFaddin 1998, 4). In order to evaluate whether the Land Board is satisfying the obligation of generating market rent for each lot, we turn first to the method by which the Land Board determines the annual rent payment. In the case of cottage site leases, the contract rental rate (CRR) multiplied by the lot's appraised market value (LV*) determines the annual rent payment:

$$\text{Annual Rent} = \text{CRR} \times \text{LV}^*$$

Use of this equation means the Land Board has a two-fold obligation. First, the estimated (appraised) market value of the residential cottage must accurately reflect the market value of those sites, i.e. LV* must equal the lot's actual market value. Second, the rental rate charged to lessees must equal the market rate for such leases, i.e. CRR must equal the market rental rate. Whether the Land Board is satisfying both requirements is evaluated in the following sections.

Land Value

Because annual rent payments are calculated by multiplying the appraised lot value by a contract rental rate, the Land Board must use accurate appraisals of the cottage site market values in order to generate market rents from cottage site leases. Put differently, if appraised values used for the annual rent payment calculation are below market values, the Land Board would have to charge above market contract rental rates in order to procure market rent from each cottage site, an apparent political impossibility.

Cottage site market values are influenced by several variables specific to the site such as the presence, quality and quantity of lake frontage, the quality of access to the site, and the suitability of the site's topography for building, to mention a few. For purposes of determining the market value of recreational cottage sites, however, the value of any lessee-owned improvements is entirely irrelevant. As discussed below, lot values and improvement values are entirely distinct though they may be difficult to accurately parse upon lease transfer. Both the McFaddin and Knipe appraisals rightly exclude improvements from valuation.

That the cottage sites are leased and not owned by the tenants is also irrelevant to the determination of cottage site market values. The market value used for calculating an annual rental payment is the land's fee simple value, and no less. This is not to say that the terms of the lease have no bearing on the rental payment. They do, but the lease terms influence the contract rental rate (CRR) instead of the cottage site's fee simple market value (LV*).

Previous appraisal reports to the Land Board explain this distinction. According to the Knipe report,

> the factors inherent to the land should be reflected in the land valuation (location, desirability, etc.), and the factors inherent in the lease (use restrictions, risk, uncertainty, etc.) ought to be reflected in the cap rate conclusion. Under no circumstances, however, should one discount a property's fee value for poor access, to use an example, then make a similar discount to the cap rate for that poor access. Even more blatant an error is penalizing the fee simple value conclusion of the lot for issues stemming from the lease – the fee value and the restrictions on the lease are entirely separate matters (1998, 115).

Similarly, as the McFaddin report explains, "It is not sensible that the market value estimates be reduced artificially to reflect a possible title problem *when the reason for the appraisal is to set rent*, and titles will not be transferred" (1998, 4, emphasis added). Both appraisal reports thus distinguish the question of market value from the question of lease rate.

The Policy Analysis Group (PAG) report fails to distinguish between issues of rate setting and lot valuation. According to Cook and O'Laughlin, "because of the unusual characteristics of the cottage site lease market . . . appraisals to determine market rent for cottage

sites are complex and stretch to the limit many of the assumptions on which standard real property appraisal methods are based." (Cook and O'Laughlin 2008, 2). The authors explain "the lack of a competitive, open market for single-family residential land leases on either Payette Lake or Priest Lake forces appraisers to make unusual adjustments to standard appraisal methods for determining opinions of value" (id., 1). Such adjustments are appropriate and may in fact be necessary for determining a contract rate (CRR) that generates a market rate of return, but these adjustments are unnecessary and indeed inappropriate for determining the market value of leased cottage sites (LV*).

As McFaddin notes, "the estimates of market value assume, by definition, the lots will be sold. They must be compared with sales of fee-owned lots" (1998, 5). For purposes of determining the market value of these lots, ignoring the terms of the cottage site lease contract allows for a broader comparables analysis and, therefore, a more accurate appraisal of market value. It also eliminates the possibility of "double counting" any differences in the legal rights conveyed under a residential cottage site lease and those conveyed under a fee simple property transfer. As both the McFaddin and Knipe reports explain, a leased lot's market value is its fee simple value for purposes of determining the annual rent payment.

Implicit in the requirement that appraised lot values accurately reflect the fee simple lot values is the requirement that market value estimates must also be current. The rapid appreciation of lot values in recent years, however, has generated a rapid increase in calculated rental payments and consequently significant pressure from lessees for the Land Board to slow rent increases due to lot appreciation. In response, the Land Board has adopted policies that phase in rental rate increases over ten years (adopted 1987) and that impose an annual cap on rent increases (adopted 1992).

The latter has the effect of artificially slowing the appreciation of leased lot market values. It also makes it practically impossible for the Land Board to ever catch up with asset appreciation over the duration of a lease. This, in turn, makes it impossible for the Land Board to capture market rent *throughout* the duration of the lease.

The lease terms and lessee improvements must have no bearing on the appraised market values if the Land Board is going to determine "market rent" by applying a rate of return to appraised market values. The underlying reason lot value must be estimated independent of rental rates is that the Land Board could divest itself of these properties and invest the proceeds in assets bearing higher returns. To cobble together the issues of rental rate and market value increases the likelihood of the Land Board generating below market rents from cottage site leases, as does any policy of gradually phasing in lot value appreciation.

Rental Rate

The second step in determining whether leased cottage site lots are generating "market rent" is determining whether the Land Board is charging a contract rental rate at least equal to the market rental rate. The contract rental rate should be determined by competitive financial markets such that, if lot value is increasing with time, the annual rents increase proportionately to ensure a competitive rate of return. As the Knipe report explains, "all other factors held constant, overall rates of return accepted by investors do not tend to decline with increasing values" (1998, 156). If annual rents are not increasing with lot value, the rate of return on the

asset will be below what the Land Board could earn regardless of accumulated appreciation. In such a case the Land Board should consider liquidating the asset and reinvesting the value in assets earning the higher rate of return.

The Land Board has described this very scenario with respect to residential cottage sites, stating that "increasing real estate values associated with lake side or lake view property results in escalating annual rent and produces pressure to maintain an artificially low return on asset" (State Trust Lands Asset Management Plan 2007, 21). However, maintaining an artificially low return from endowment owned cottage sites fails to ensure that each leased lot generates market rent for the duration of the lease as required by Idaho Code §58-310A.

Presently, cottage site lease rates are 2.5 percent of the appraised fee simple lot values. This rate is set by Land Board motion, rather than by competitive bidding. As such, there is no economic justification for describing 2.5 percent as a market rate for cottage site leases. The primary question thus becomes what rate must the Land Board apply to appraised lot values in order to procure market rent from each leased lot. A summary of previous recommendations made to the Land Board provides a good starting point for this analysis.

The 1998 McFaddin report recommends a contract rate of 3.5 percent of appraised fee simple value. Two methods of analysis were used to arrive at this number. First, the author calculated an average contract rental rate that would reduce leasehold prices to zero for 16 Priest Lake cottage sites (McFaddin 1998, 23). Estimated to be 2.12 percent of appraised fee simple value, this figure represents the market rental rate because a leasehold price of zero, by definition, suggests the market attaches no value to the lease itself.

The second method employed in the McFaddin report was to treat positive leasehold values as opportunity costs of the 2.5 percent contract rate. By applying an 8 percent discount rate to the leasehold prices of 16 Priest Lake cottage sites and adding that figure to the annual rent received, the McFaddin report arrived at an average rate of 4.23 percent of fee simple value.

The logic behind the two McFaddin methods is the same: positive leasehold values represent the market's valuation of below market rental rates. By calculating a rate that would dissipate positive leasehold values and by calculating the opportunity cost of below market rental rates, the McFaddin report demonstrates the 2.5 percent contract rate is significantly below market. Considering both methods of calculating "market rent," as well as comparable leases in other states, McFaddin concluded the market rate of return is in the range of 3 to 4 percent of appraised fee simple value (McFaddin 1998, 24).

The 1998 Knipe report also used two methods of determining an appropriate market rate. First, the Knipe compares the effective lease rates charged on ten "direct rental comparables" leased throughout the country, then reports a qualitative assessment of comparability to Idaho's Cottage Site Leasing Program (Knipe 1998, 122). The rationale is that by accounting for differences in lease terms, these rates convey information on the market for residential cottage site leases. The problem with this approach is the subjectivity of comparing lease terms and estimating a marginal difference in rental rates for those differences; but the Knipe report does at least acknowledge differences in the contractual terms.

The second and more economically sound approach employed in the Knipe report is the calculation of implicit rates of return using the Duffield model:

$$i = R_o (1 - L / V)^{-1}$$

where i = Market rate of return; R_o = Contract rate of return; L = Leasehold value; and V = Fee simple value.

Like the McFaddin calculations, the theory behind the Duffield model is that positive leasehold values reflect the buyer's valuation of below market rental rates. The higher the leasehold value, the higher the divergence between market and contract rates is perceived to be. The Duffield model is useful because it can be used to calculate an implicit market rental rate of return. Using the Duffield model, Knipe reports implicit rates of return near 6 percent of appraised market value. This number comports with the more subjective "direct rental comparables" analysis.

The 2008 Policy Analysis Group Report prepared by Cook and O'Laughlin include additional reference points suggesting the 2.5 percent contract rate is below market. The authors report annual rental rates used by other states' cottage site leasing programs (Cook and O'Laughlin 2008, 16). Of the stated rates reported in the PAG Report, California charges an annual rental rate of 9 percent of the appraised land value, and Wyoming charges 5.5 percent. Though not directly comparable because of differences in lease terms, these rates do indicate the Idaho Land Board is charging below market rates for cottage site leases.

Also reported in the PAG Report prepared by Cook and O'Laughlin are rates of returns for asset classes of comparable risk: 30-year fixed rate mortgages, 30-year government bonds and AAA corporate bonds (at 19). All investments significantly outperformed the 2.5 percent contract rental rate of the Idaho Cottage Site Leasing Program. Indeed, the historical rates of return on 10-year T-notes, arguably a risk-free investment, outpaced the 2.5 percent contract rental rate 660 months out of the 672 since 1953 (Federal Reserve 2010).

Cook and O'Laughlin argue that these rates of return include asset appreciation and therefore are not directly comparable to the "cash only" 2.5 percent contract rental rate of cottage site leases. They are not comparable because the Land Board is capturing only a portion of cottage site appreciation with the 10 percent premium rent policy (its share of the leasehold value at time of transfer). Therefore the realized rate of return is most likely even lower than the contract rental rate or "cash only" 2.5 percent rate. Indeed, in 1986 the Department of Lands estimated a 0.67 percent overall rate of return on asset value from the Cottage Site Leasing Program (Land Board Minutes, June 25,1986). Since the actual rate of return is likely below 2.5 percent, comparisons to these rates of return strongly suggest the Land Board is earning significantly less than it could by investing in other asset classes of similar or even lower risk when the political pressure to retain low rents is taken into account.

Similarly useful for comparing rates of return is the table included on page 22 of the PAG report.

Residential Real Estate Rates of Return (ROR) Implied by Various Market Measures

Market Measure	ROR%
Idaho Appraisers' Opinion:	
Priest Lake	3.5%
Payette Lake	6.0%
Residential Leases, MT, UT & WY	5.0-5.5%
Recreational Residence Leases, USFS	5.0%
Recreational Cabin Leases, California	9.0%
Residential Lease Program, CalPERS	8.0%
30-Year Mortgages	6.3%
30-Year Government Bonds	4.7%
AAA Corporate Bonds	5.7%
10-Year REIT	10.7%
35-Year REIT	13.3%
National Property Index	15.8%
Western Region NPI	18.3%

These rates summarize market rates from (1) other private rental contracts on Payette and Priest Lakes; (2) similar residential land leasing programs; (3) alternative investments of similar risk, including AAA corporate bonds and REITs; (4) benchmark rates of return for institutional investments; and (5) public auction. All of these rates exceed the 2.5 percent contract rental rate, suggesting that the current rate is significantly below market.

It is important to note, however, that not all rates of return are comparable, nor are all rental rates comparable. The 2009 report from Stanley Moe, Joe Corlett, and Ed Morse to the Cottage Site Subcommittee sets forth a wholly irrelevant comparison of rental rates. The "market rent methodology" contained therein compares cottage site lease rates with rental rates from 17 privately-owned residential and vacation properties in northern Idaho. The primary flaw in this methodology is that it extrapolates a market value-rental rate relationship without holding constant the myriad variables that unquestionably influence a property's market rental rate without impacting the property's market value.

The most obvious variables omitted from the Moe, Corlett and Morse market rent methodology are the differences between the private rental agreements compared to state-owned cottage sites leases. Cottage site lessees are allowed (1) to sell, mortgage, or bequeath a cottage site leasehold estate; (2) to construct improvements and receive reimbursement for those improvements upon lease transfer or non-renewal; and (3) are protected from market competition for cottage site leases as of result of Idaho Code §58-310A. While these characteristics unique to the state's Cottage Site Leasing Program clearly influence the market rental rate of cottage site leases, they were not considered in the Moe, Corlett and Morse market rent methodology. Tenant rights in residential leases are incongruous and irrelevant to any discussion of cottage site lessee rights; hence their market value-rental rate relationship makes little sense.

Comparing rates of return across asset classes requires an accounting of the variables that might influence investment risk. Similarly, comparing rental rates across different properties requires an accounting of different contractual terms of the leases. The rate comparisons that account for such differences all demonstrate the Land Board's 2.5 percent contract rental rate is significantly below market. The only rate comparison that suggests otherwise fails to account for the unique characteristics of the Idaho Cottage Site Leasing Program.

Consistent with the economically sound rate comparisons discussed above, the implicit rate calculations in the Knipe and McFaddin reports suggest the 2.5 percent contract rental rate for cabin site leases is below the market rental rate. Those reports demonstrate how the positive leasehold values generated by below market rental rates represent an opportunity cost of maintaining the 2.5 percent contract rental rates, a cost that can be avoided either by rental rate increases or by investment in other asset classes of similar risk.

Market Rent Conclusion

In order to secure a "market rent" from each cottage site, the Land Board must (1) use accurate and current appraisals of cottage site market values; and (2) charge a contract rental rate at least equal to the market rental rate. Policies that cap or phase-in rent increases attributable to lot appreciation ensure the Land Board will fail to meet this first requirement, as do appraisals that consider the terms of the cottage site leases in addition to the characteristics of the cottage site lots. As for the contract rental rate, positive leasehold values and rate of return comparisons to other asset classes *both* suggest contract rents have fallen below market rents. The McFaddin and Knipe implicit rate of return calculations support this conclusion and suggest specific contract rates of 3.5 to 6 percent.

In our opinion the current Cottage Site Leasing Program is failing to secure market rents for the duration of cottage site leases. The Land Board is charging below market contract rental rates against below market lot values. If the contract rental rate and the lot values cannot be increased to market levels, the Land Board should consider divesting itself of the cottage sites or seek to use these properties for purposes other than residential cottage sites.

Maximum Long Term Financial Return – The Constitutional Duty

Different Standards

In 1990, the Idaho Legislature found that the "maximum long-term financial returns" from state-owned cottages sites "are best obtained through stable leases at market rent" (Idaho Code §58-310A(1)(h)). This finding confused the Land Board's obligation of securing "maximum long-term financial return" with that of securing "market rents" through long-term leases. Such a substitution has little basis in economic reasoning because it assumes that *leasing* of cottage sites for single-family recreational use will forever produce higher returns than *any* other use of the land.

Indeed, other legislative findings in Idaho Code § 58-310A suggest the Legislature's substitution of "market rent" for "maximum long-term financial return" reflected the motivations of current cabin site lessees more so than economic reality. Specifically, the Legislature found that "the conflict application and auction procedures have caused considerable consternation and dismay to the existing lessee" and that "existing statutes allow the [land] board no discretion in rejecting applications." While exempting cottage site leases from the conflict application and auction process alleviated the "consternation" of current lessees, it also had the effect of reducing the financial returns to endowment beneficiaries by eliminating market competition from the Cottage Site Leasing Program.

The poor performance of the current Cottage Site Leasing Program since enactment of Idaho Code § 58-310A casts additional doubt on the legislative finding that "maximum long-term financial returns to the institutions to which granted are best obtained through stable leases at market rent" (Idaho Code § 58-310A(1)(h)). As we concluded in the previous section, the Land Board is currently failing to secure market rents from cottage site leases and has adopted policies such as freezing annual rents that are inconsistent with securing market rent. As a result, we must consider as a separate inquiry from the "market rent" analysis whether the Land Board is satisfying its fiduciary duty to endowment beneficiaries by securing the maximum long-term financial return for endowment beneficiaries.

The Prudent Investor Standard

The appropriate standard for evaluating whether the Land Board is satisfying its fiduciary duty is the prudent investor standard as described in Idaho Code §68-502. The prudent investor standard requires that a trustee exercise reasonable care, skill and caution in the management of trust assets. Relevant to trust beneficiaries, the prudent investor standard requires a trustee to balance total returns from income with capital appreciation; the financial return cannot be *entirely* appreciation or *entirely* income. Instead, the allocation of total returns between appreciation and income must be consistent with the funding requirements of the current and future trust beneficiaries.

It is important to note that the prudent investor standard does not dictate a minimum rate of return above which a trustee presumptively satisfies its fiduciary duty. In other words, there is no benchmark "prudent investor rate of return" that applies to every investment and every situation. Instead, the risk of each investment must be considered when evaluating whether that investment and corresponding rate of return comport with the prudent investor standard.

Additionally, the factors listed in Idaho Code §68-502 such as the possible effect of inflation or deflation, liquidity needs and general economic conditions must also be considered.

At first glance, securing the maximum long-term financial return for endowment beneficiaries seems like a straightforward charge, but meeting this constitutional requirement is easier for some lands than others. For example, grazing lands generate an annual flow of forage that can be leased to livestock owners. Because there is a competitive market for grazing units, it is relatively easy to determine the value of those units and therefore to assess whether the Land Board is meeting its fiduciary responsibility to maximize long-term financial return on the asset.

Assessing whether the fiduciary responsibility is being met for other assets, such as cottage sites, is more difficult for several reasons. First, as with grazing lands, an asset might yield an annual return as it appreciates over time. In this case, the long-term financial return has two components – the annual rental rate and the appreciated market value. Consider this in the context of a financial asset such as a bond. The Land Board could buy a bond with a fixed maturity value. Given the initial purchase price and the face value of the bond, the annual rate of return is straightforward. However, if the market forces drive up the price of the bond after it is purchased, the prudent investor would have to balance holding the bond to maturity against selling it at the current higher market value and the prospect that the market value before maturity might rise even more. In either case, maximizing the return on the bond requires more than just considering the annual return at the time of purchase; it requires considering the appreciated (or depreciated) value over time.

Investment decisions are complicated even more if the annual rent from an asset is difficult to determine which it may be for two reasons. First, unlike grazing where the annual rent is determined by the value of forage to the livestock owner, the value of a cottage site leases is more subjective. It depends on individual preferences regarding recreation, solitude, relaxation, and so on. Second, unlike a competitive bond or grazing land market, there are few if any comparable rental markets for cottage lease sites. Competitive financial markets make the asset value clear, but for assets such as land with unique characteristics and limited amounts of transactions, such clarity is lacking.

Cottage lease sites are a case in point. Each site has unique characteristics determined by outside factors such as proximity to roads and utilities, other recreational opportunities, and site specific investments, to mention a few. Moreover, in cases where the state owns most of the cottage site land, there will be few comparative sales and the sales that do exist will be quite different if they transfer land title as opposed to leasehold opportunities. To the extent that the rate of return on an asset depends on its appreciated value, that return will be difficult or impossible to capture if the asset cannot be liquidated. In the case of state trust lands, legal and political constraints make liquidation difficult.

The Split Ownership Problem

The problem with assessing fiduciary responsibility with respect to cottage sites is further complicated when there is an annual flow of returns or services from the assets, when the total asset value is appreciating, and when the total asset value results from the site value owned by the state combined with site-specific investments owned by private parties. If the total estate – land and improvements – were owned by one entity most of these problems would disappear.

To see how split ownership causes problems, we must untangle the value of the total market value of cottage sites. One component of the total value will be the value of the raw land, which in turn will be a function of external factors such as proximity to access roads, other amenities values (e.g. vistas, ski areas, fishing, etc.), call this, LV. The other component will be the value of the improvements made by the lessee, call this CV. Therefore,

$$\text{Total Market Value of Cottage Site} = LV + CV.$$

Following the prudent investor standard, a single owner of a cottage site would maximize the total value. If the total estate is split between two owners, one who owns the land and one who owns the cottage (including all other improvements), each would maximize his or her value. The problem, of course, lies is determining LV and CV.

Consider two identical cottage sites including both physical attributes, amenities, and improvements. Site A is privately owned, and the owner has made investments on the property. Site B has split ownership wherein the land is held in trust by the state and leased to a lessee who has made investments identical to site A. Now suppose that with time demand for each site has risen in value due to population growth, income growth, increased value of nearby amenities, increased value of the investments (e.g. rustic cabins may now be in vogue or replacement costs may have risen), or some combination of all these or other factors. If full ownership of site A and the leasehold right for site B are offered for sale at the same time in a competitive market, their total values will be the same. However, the sales price of site A will be greater than the sales price of site B due to split ownership.

Site A, which includes the title to the land and improvements, will sell for P_A, the combined value of LV and CV while Site B will have a lower sales prices because the buyer of the lease right to the state owned cottage site must make rental payments to the Land Board. Therefore P_B will be less than P_A by the discounted value of the expected rental fees payable to the Land Board, call it R_B. If the Land Board is maximizing its return on the cottage site in a competitive market, P_B plus R_{Bmax} will equal P_A. In other words, the cottage lease selling price, P_B, will equal the market value of the improvements on site B, call it CV_B, no more and no less.

If the Land Board is not maximizing its rental return on the cottage site (i.e. $R_B < R_{Bmax}$), the lessee selling the improvements and transferring the lease will receive a premium (R_{Bmax} - R_B) called the leasehold value, i.e. $P_B > CV_B$. This means that the lessee is capturing part of the land value of site B, call it LV_B, value the Land Board is required to capture.

Not surprisingly, leasehold values are the subject of contention. Some claim that cottage sites are not selling because the leasehold value is negative due to cottage site rental rates that are too high (presumably higher than R_{Bmax}) (see Cook and O'Laughlin 2008, 20). Such an inference, however, does not follow. If the seller of a cottage site lease sets P_B higher than CV_B and the Land Board is charging R_{Bmax}, buyers will avoid purchasing state owned cottage sites at the asking price greater than CV minus R_{Bmax}. Assuming that the Land Board is capturing the full value of LV_B through annual rents, the only way that there can be positive leasehold value $CV_A > CV_B$ is due to a higher value of improvements on site A versus site B.

In conclusion, the complication imposed by the split ownership of cottage sites and cottage site improvements makes it difficult if not impossible for the Land Board to maximize

the long-term financial returns from cottage sites. Differences in the appreciation of the state-owned lots versus lessee-owned improvements create investment-specific risk *and* return measurement uncertainty intolerable under the prudent investor standard. The generation and division of large, positive leasehold values reveal the inconsistency of the Cottage Site Leasing Program with the prudent investor standard. A prudent investor would not allow such leasehold values to generate in the first place, as these leasehold values represent unrealized returns from the cottage site assets. Moreover, a prudent investor owing a fiduciary duty to endowment beneficiaries would not allow transferring lessees to capture 90 percent of these returns because they are owed to the endowment beneficiaries. Under the current Cottage Site Leasing Program, the Land Board has allowed both. Therefore, in our opinion, the Land Board's cottage site leasing decisions fail to meet the prudent investor standard for maximizing long-term financial returns.

Post Contractual Opportunism

Split ownership leases will always make it difficult for the Land Board to meet its fiduciary responsibilities to maximize long-term financial returns. Recall from the above analysis that the total value of a cottage site is composed of LV + CV. In a competitive market with identical land parcels, identical cottage investments, and little change in the total or relative value of LV and CV, it might be possible to separate the two, but when none of these factors hold, meeting the prudent investor standard will be complicated.

The professional economics literature addresses the consequences when two owners of inputs contribute to the total value of a product and when it is not easy to separate the relative contributions (Klein, et al. 1978). For example, consider a restaurant for which the owner of the building and other restaurant capital hires a talented chef at a fixed wage. If the restaurant is successful, there is a question of whether the success is due to location and ambiance or due to the chef's culinary skills. In such a case, the chef might threaten to withhold his or her services (e.g. the chef might call in sick) unless he or she is paid a higher share of the profits. This is referred to in the economics literature as "post-contractual opportunism" because the owner of a specialized input – the chef - can act opportunistically to capture a larger share of the total value.

Solving the post-contractual opportunism problem requires eliminating split ownership. This explains why, in the case of unique restaurants, typically the chef is either part or full owner of the business.

In the case of cottage sites, the Land Board is charging the cottage owner a fixed rental amount for a period of time. The cottage owner adds to the total value to the property by making investments, such as buildings, roads, and wells, which are not easily separable from the land. The cottage owner also forms expectations regarding whether, when and by how much the Idaho Land Board will change the rents. If the lessee decides to sell her lease right, she will attempt to capture as much of the total value as she can. The amount captured above and beyond CV is the leasehold value.

Given that it is not easy to separate the contribution of LV and CV to the total value, opportunistic behavior is likely. The lessee may act opportunistically by putting political pressure on the Idaho Land Board to enact policies that favor lessees at the expense of the endowment beneficiaries. This is known as "rent seeking" because it uses politics to give the

private owners a larger share of the land rents (Krueger 1974). Rent seeking is particularly prevalent when a small well organized group receives the benefit from a policy while the costs are diffused over a larger group. With the benefits concentrated, the small group can afford to exert political pressure for a policy which benefits it; with the costs diffused, however, it is not worth it for anyone in the large group to organize political opposition. In the case of cottage site leasing, the lessees are the former while the trust recipients are the latter.

Several Land Board policies reflect this rent-seeking dynamic. First among them is charging below market value rents. Extended periods of flat or declining rents despite significant land appreciation have benefitted cottage site lessees at the expense of endowment beneficiaries guaranteeing that the latter receive less than maximum long-term financial returns from the asset. The Land Board policy of only collecting a 10 percent premium rent upon lease transfer gives cottage site lessees the lion's share of leasehold value when much of that value is the result of below market cottage site rents. Lessees engage in rent seeking by using political pressure to keep cottage site rents below market value and characterize efforts by the state to collect even 10 percent, and certainly more, as a tax on their property value. Until ownership of the cottage site and improvements thereon are unified, rent seeking by lessees will continue and the trust beneficiaries will be left with less than their share of the value of cottage sites.

Another obvious example of rent-seeking and post-contractual opportunism in the Cottage Site Leasing Program is the statutory exemption of cottage site leases from the Idaho code's conflict application and auction provisions. This exemption completely removes market competition from the Cottage Site Leasing Program and, with it, the Land Board's ability to maximize financial returns through competitive bidding. The legislative findings that preface this exemption explain its purpose is not to maximize the returns to trust beneficiaries but to alleviate the "considerable consternation and dismay to the existing lessee" caused by the code's conflict application and auction procedure (Idaho Code § 58-310A(1)(e)). This is the hallmark of rent-seeking, a small group of cottage site lessees using the political process to capture more of the benefits from and impose more of the costs on a larger group.

Such rent-seeking is particularly surprising given the Land Board's fiduciary duty to trust beneficiaries, a duty that is clearly stated in Idaho's constitution. Cottage site lessees, presumptively aware of this duty, have effectively engaged in post-contractual opportunism to the detriment of trust beneficiaries. In other political lands, such as U.S. Forest Service or Bureau of Land Management grazing leases where there is no fiduciary standard, such rent-seeking is frequently observed and somewhat predictable because the residual claimant, i.e, the group harmed by the rent-seeking, is the entire U.S. population. That such rent-seeking pervades Idaho's Cottage Site Leasing Program despite the Land Board's constitutionally mandated loyalty to the trust beneficiaries suggests a systematic flaw in the Program. That systematic flaw is split ownership of the lots and improvements.

The post-contractual opportunism and continued rent-seeking means the split ownership problem must be overcome if the Land Board is to meet its fiduciary responsibility. Whether the problem is eliminated by the lessee buying the land from the state or the state buying the improvements from the lessee is beyond the scope of this report. The important point is that split ownership makes meeting the prudent investor standard difficult if not impossible for the Land Board. A prudent investor would not accept the risk of post-contractual opportunism and rent

seeking on the part of lessees implicit in the split ownership of cottage sites and cottage site improvements. The Land Board's continuing acceptance of this risk and of the resulting suboptimal returns is inconsistent with the prudent investor standard. The prudent investor would seek to invest in other investments without such risk.

Conclusions and Recommendations

The Idaho State Board of Land Commissioners has a constitutional obligation to "secure the maximum long term financial return" from these lands and to act in such a manner "as a man of good business sense and judgment would act in regard to his own affairs." As such, the Land Board's cottage site leasing decisions must comport with the prudent investor standard. By statutory requirement, the Land Board must also "insure that each leased lot generates a market rent throughout the duration of the lease."

In our opinion, the evidence clearly demonstrates that the Land Board is not meeting its statutory or its constitutional obligations with respect to recreational cottage sites. First, by charging below market rates on undervalued lots the Land Board is failing to secure a market rent from the cottage site leases. Second, the Land Board is managing the cottage sites in a manner that generates significant positive leasehold values, 90 percent of which are captured by transferring lessees.

For the Land Board to capture a market rent on cottage site leases, it must increase the contract rate and ensure that the basis for lot values accurately reflects market value. To the extent, however, that the asset is not appreciating as rapidly as other investments or that rate and basis increases are politically impossible the Land Board will be unable to secure the maximum long-term financial returns for endowment beneficiaries through long-term cottage site leases. In order to comply with the fiduciary duty imposed by the constitution, the Land Board should consider ways to divest the recreational cottage sites or to devote these properties to uses other than residential cottage sites. Either option would allow the Land Board to increase the return to endowment beneficiaries, ostensibly at less administrative or management expense than the status quo.

A prudent investor would not tolerate the financial risks associated with the split-ownership for the historically low and politically contentious returns from cottage site leasing. Even if the contract rental rate and premium rent were increased, the threat of post-contractual opportunism persists under split ownership and significantly reduces the risk-adjusted returns to trust beneficiaries. Therefore, in our opinion, the Land Board should adopt a two-part strategy for fulfilling its fiduciary duties: (1) the Board should adopt an interim plan that will achieve market rent for the duration of cottage site leases, (2) the Board should implement a long-term plan for the consolidation of ownership of each cottage site parcel with the objective of maximizing long-term financial return consistent with the prudent investor standard.

References

Cook, Philip S. and Jay O'Laughlin. 2008. "Analysis of Procedures for Residential Real Estate (Cottage Site) Leases on Idaho's Endowment Lands". Report No. 28 Policy Analysis Group, College of Natural Resources, University of Idaho.

Federal Reserve Statistical Release, Select Interest Rates, Historical Data. 2010. Available on-line at: http://www.federalreserve.gov/releases/h15/data.htm.

Duffield, John. 1998. "Economic Analysis of the Values of Surface Uses on State Lands". Commissioned report for Montana Dept. of State Lands.

Klein, Benjamin, Robert G. Crawford and Armen A. Alciah. 1978. "Vertical Integration, Appropriable Rents, and the Competitive Contracting Process". Journal of Law and Economics 21 (2): 297-326.

Knipe, Bradford T. 1998. "Complete Appraisal, Self-Contained Report, and Market Rent Analysis of 14 Payette Lake Cabin Sites". Commissioned report for Montana Dept. of State Lands.

Krueger, Anne. 1974. "The Political Economy of the Rent-Seeking Society". American Economic Review 64 (3): 291–303.

State Trust Lands Asset Management Plan. 2007. Idaho State Board of Land Commissioners.

Exhibit 31

Terry L. Anderson and Reed Watson,

Analysis of Subcommittee Recommendation to the Idaho Board of Land Commissioners (2010)

Anderson and Watson
February 12, 2010

ANALYSIS OF SUBCOMMITTEE RECOMMENDATIONS TO THE IDAHO BOARD OF LAND COMMISSIONERS

Terry L. Anderson and Reed Watson

I. Introduction

On January 11, 2010 the Cottage Site Subcommittee submitted to the Idaho Board of Land Commissioners (Land Board) a draft report regarding the future management of state-owned cottage sites on Payette and Priest Lakes. The Subcommittee's report recommends several changes to the existing cottage site leases, which all expire on December 31, 2010.

We evaluate the Subcommittee's recommendations under two distinct criteria. Specifically, we evaluate whether the Subcommittee's recommended method of calculating annual rent is likely to "insure that each leased lot generates market rent throughout the duration of the lease," as required by Idaho Code § 58-310A. This standard applies to the recommendations pertaining to target rent calculation and phasing-in rent increases. We evaluate the Subcommittee's other recommendations under the Land Board's constitutional obligation to "secure the maximum long-term financial returns" for endowment beneficiaries. This standard applies to the Subcommittee's recommendations regarding premium rent, lease term, and lot disposal.

The dual standard is warranted by the legislative finding that "maximum long-term financial returns to the institutions to which granted are best obtained through stable leases at market rent" (Idaho Code § 58-310A(1)(h)). To achieve that goal, the Land Board must be able to adjust annual rent consistent with obtaining maximum long-term financial returns. If the Subcommittee's recommends changes that make it more difficult for the Land Board to secure market rent, it would be not be meeting its statutory duty or its constitutional duty. Because the Subcommittee's recommendations regarding premium rent, lease term, and lot disposal do not directly affect the calculation of annual rent amounts, we evaluate those recommendations only by the prudent investor standard required by the state constitution.

II. Subcommittee's Recommendations

The Subcommittee Report recommends the following changes to the existing cottage site lease terms:

- that the target annual lease rent equal 4 percent of the average appraised value of each lot over the most recent ten years;
- that the actual rent increase annually at a constant percentage rate to reach the target rent in five years;
- that the premium rent (i.e., the portion of the leasehold value paid to the State upon lease transfer) increase from the existing 10 percent to 50 percent over the next five years

(increasing by 10 percent each year) and that the premium rent remain at 50 percent for the remainder of the lease;

- that the duration of future leases be 35 years; and
- that the Department of Lands conduct the necessary analysis and recommend to the Land Board specific long term plans for continued leasing, development, or disposal of cottage sites.

III. Target Rent Calculation – Market Rent is the Standard

A. Contract Rate

According to the Subcommittee, "[t]he 4% used in the formula falls within the range of rates mentioned above [i.e. rates documented in other Land Board reports] and will still generate interest in the market. It provides a reasonable rate of return and generates an average 9% per year increase over the first five years to the beneficiaries" (Subcommittee Report, 2). We emphasize at the outset that this is the lease rate, not the market rent, which is what Land Board is legally required to target for maximizing long-term financial returns.

The recommendation that the annual lease rate be increased is a step in the direction of obtaining a market rent, but the recommendation still does not meet the prudent investment standard for two reasons.

1. Though four percent indeed falls within the range of rates suggested in previous reports to the Land Board, it is decidedly at the lower end of that range. The proposed contract rental rate remains below the rate charged by several other states with comparable cottage leasing programs and well below the rates of return available from institutional investments of similar or less risk.[1] The proposed rate also falls below the 6 percent implicit rates of return calculated using the Duffield model and reported in the Knipe report. Though the Subcommittee's proposed contract rental rate of 4 percent is an improvement of the current 2.5 percent contract rental rate, comparisons to other states' cottage site leasing programs, to similar asset classes, and to implicit rate calculations all suggest 4 percent is below market. Moreover, the Subcommittee's recommendation of 4 percent has no credibility as a "market" rate other than the fact that it falls within the broad range of 3.5 to 18 percent recommended by the various appraisal reports.

2. The proposed 4 percent is also fixed, meaning it does not change with changing market conditions. Given that market rates of return are continually moving, a prudent investor would adjust his expected rate of return to equal the market rate. This could mean that rates would increase to the benefit of the state or decrease to the benefit of the lessee depending on market movements. That a 4 percent contract rental rate provides a "reasonable rate of return" is irrelevant; the contract rental rate must generate a market

[1] As discussed in our report to the Idaho Attorney General's Office dated February 12, 2010, rates of return for institutional investments typically include asset appreciation as well as the periodic or "cash-on-cash" returns. The total rate of return for cottage site leases should therefore include both the contract rental rate and the realized appreciation rate earned by Department.

rent to secure the maximum long-term financial return for endowment beneficiaries. By fixing the rate at 4 percent over a long period of time, Land Board would be missing upturns in market rates and not meeting its fiduciary responsibility.

B. Appraised Value

According to the Subcommittee, "[a]pplying a rate to a land value that adjusted annually has caused drastic swings in annual rental fees. Using a 10 year average of the land value in calculating the rent would smooth out the impact of those rapid swings, and provide greater stability than is currently the case" (Subcommittee Report, 2). While it is true that using a ten year rolling average to calculate annual rent would reduce rapid swings in annual rental fees, such averaging will also make it virtually impossible for the Land Board to charge lessees "market rent," as required by the Idaho Code.

Consider how averaging appraised land values over a ten year period would affect annual rental fees if land values are depreciating or appreciating. If land values are depreciating, contract rents would actually *exceed* market rent because the average land value would exceed the land's market value. The opposite outcome would result if land values were appreciating over the ten year averaging period as they have been for long-term. During either depreciation or appreciation, contract rents would not equal market rents, and the Land Board would find itself in violation of its statutory obligation.

Using the ten year average of appraised land values also means that the state will always be earning rents based on past rather than current land values and therefore, especially during times of appreciation, will continually be below market rents. This would be the equivalent of a bond investor basing investment decisions on a ten year average of bond prices rather than on current bond prices. Doing so would mean that the current price of the bond would only get a one-tenth weight in financial calculations when, in fact, the current price is what the bond is worth and what determines the rate of return. Given this approach, it is not surprising that the Land Board itself calculates an effective rate of return closer to 2.5 percent than to the 4 percent rate proposed by the Subcommittee.

Another argument against appraising lot values annually is cost. Indeed, appraising 522 lots annually is both expensive and administratively burdensome for the Land Board. However, during periods of rapid appreciation or depreciation, changes in land value and, consequently, changes in annual may overwhelm appraisal costs, but this will not always be the case. Therefore, the Land Board should only consider using long-term averages if land values were expected to remain relatively constant thus reducing the need for annual appraisals. Such an expectation seems unjustifiable given the significant appreciation of lot values in recent decades. Thus the recommendation appears inconsistent with the Land Board's statutory obligation.

C. Phase-in Period

The subcommittee recommends that the actual rent increase (or decrease) annually from the prior year's rent at a constant percentage rate to reach the target rent in five years. The Subcommittee report does not state a specific rationale for phasing in the target annual lease rent over a five

year period, but presumably the policy is intended to slow the immediate impact on lessees of increases in the contract rent.

Even if one assumes that the targets are correct approximations of "market rent," adjusting rents or rates over a five year period guarantees that the state is not securing market rent for the five year adjustment period. If the target annual rent equals the market rent for a cottage site lease at the end of the five-year phase-in period, the *market* rent will obviously exceed the *contract* rent during the phase-in period, as the contract rental rate "catches up" to the target and, presumably, to the market rate. If the target annual lease rent is below the market rent, as the above analysis suggests, then the contract rent will be below market rent not only during the phase-in period but also for the remainder of the lease.

Delaying the acquisition of that target for five years will prevent the Land Board from securing "market rent" during the phase-in period, and as with using the ten year average appraisal value, this guarantees that the actual return will be less than the prudent market return.

IV. Lease Terms and the Prudent Investor Standard

A. Premium Rent

"Since 2003, cottage site owners have realized in excess of $25 million for the use of State endowment land while the endowment received only $2.7 million" (Subcommittee Report, 2). According to the Report, "[t]he Subcommittee believes that a 50% premium rent rate will have the effect of maximizing the return to beneficiaries, and that any higher rate would be counterproductive, and act as a disincentive for selling leaseholders to be active in seeking the maximum sale price" (Subcommittee Report, 3).

As discussed in our report to the Idaho Attorney General's Office entitled "Report to the Idaho Attorney General's Office Regarding Cottage Site Leases" dated February 12, 2010 ("first report"), positive leasehold values demonstrate that the market is placing a premium on the value of the cottage site lease plus any value of improvements over and above their appraised value. Though it is difficult to separate how much of the leasehold value is due to the lease and how much is due to the improvements, we can be sure that below market rents constitute a share of the $25 million premium and probably a share significantly above 10 percent.

The Subcommittee's recommendation to increase premium rent from 10 percent to 50 percent of the leasehold value validates that the board has not been charging market rents, that below market rents have contributed to leasehold values, and that the state has been missing out on revenues that a prudent investor would have captured. Until the ownership of the lot and of the improvements is unified, there will be conflict over the appropriate division of leasehold values. At the 10 percent premium rent, the state is missing some of its rightful and prudent investor revenues while the lessees contend that the premium rent is essentially a tax on their property. As discussed in our first report, the portion attributable to below market rents is not easily

distinguishable from the portion attributable to inaccurate improvement appraisals.[2] This fact makes it all the important that the Land Board increase contract rents to equal market rents as soon as possible so as to eliminate any contribution that below market rents make to leasehold values.

Aside from split ownership complicating leasehold division, the five year phase-in of the premium rent increase creates an incentive for lessees contemplating transfer to consummate such deals sooner rather than later. By so doing, they receive a larger portion of the leasehold value (90 versus 50 percent). This incentive is more likely to influence those lessees who acquired cottage site leases for speculative purposes that it will those longstanding lessees who lease cottage sites more for recreational opportunities as opposed to profit. Assuming the purpose of the phase-in period for premium rents is to avoid "severely impairing or eroding longstanding business relationships with our lessees," while still meeting the Land Board's fiduciary obligations, the phase-in period is likely to fall short in both respects. "Speculating" lessees will consummate transfers at 10 percent premium rents – at the expense of trust beneficiaries – while the longstanding, recreation-motivated lessees will transfer leases when they no longer desire the recreational value, most likely after the premium rent has increased.

B. Lease Duration

This extension had been contemplated previously, when the Land Board unanimously approved a motion to seek legislation allowing an increase in the lease duration. The Land Board's stated rationale was that longer lease terms would allow tenants to secure traditional longer-term mortgages. However, both the proposed and current leases contain provisions allowing "the Board to cancel the lease and sell or exchange the property upon prior notice" (Subcommittee Report, 3), which reduces the security of the investment for the lessee.

If the purpose of the 35 year duration is to allow lessees to secure longer-term mortgages, it is not clear that it will help given that the state can terminate the lease with 180 days notice. Therefore we do not see a rationale for increasing the lease term to 35 years. The cancellation provision invalidates the claim that extending the lease term will enable lessees to procure more traditional and favorable financing terms, particularly because the Subcommittee is simultaneously recommending that the Land Board investigate divestment – an option that would likely require invocation of the cancellation provision.

Such an extension would further entrench lessee beliefs that cottage site leases convey more property rights than they actually do. Moreover, as explained in our first report, extending lease terms from 10 to 35 years will actually reduce the Land Board's ability to adjust rates commensurate with market changes in order to procure a market rent that will maximize long-term financial returns for trust beneficiaries, especially with fixed lease terms (at 16). If the contract rate is put in place for 35 years, the share of leasehold value attributable to below market rents will increase and further complicate implementation of premium rents. If the Land Board

[2] By "inaccurate," we simply mean improvement appraisals may not reflect the subjective preferences of an acquiring lessee who places a higher value on a lessee-owned improvement than did an objective appraisal. Such an improvement premium could constitute a portion of the leasehold value, but would not be attributable to below market rent and therefore should not accrue to the endowment beneficiaries.

insists on establishing 35 year leases, it must, at a minimum, include a lease provision that allows the board to adjust the rental rate commensurate with the prudent investor standard.

C. Lot Disposal

"The Subcommittee believes that the long term solution to the never ending cottage site imbroglio is to dispose of the lots in a reasonable, market savvy manner. The proceeds could then be invested in other assets which could better enhance the endowments." Here, we could not agree more the Subcommittee's recommendation. As explained in our first report, the split ownership of the cottage site lots and improvements makes it practically impossible for the Land Board to know what share of any leasehold value belongs to the endowment beneficiaries. In turn, the split ownership issue makes it practically impossible for the Land Board to maximize the long-term financial return to trust beneficiaries.

Regardless of whether the Land Board acquires ownership of the improvements or whether lessees acquire fee simple title to the lots, unification of ownership will resolve the issue of leasehold value division and allow the Land Board to fulfill its fiduciary obligation. We concur with the Subcommittee's recommendation that special emphasis be put on finding ways to consolidate ownership.

V. Conclusion

The Subcommittee's recommendations regarding the cottage site lease terms may be an improvement over the status quo because they raise the rental rate, but they nonetheless prevent the Land Board from securing the maximum long-term financial return for the trust beneficiaries. The Subcommittee's recommendations also preclude the Land Board from securing "market rent" from cottage site leases because the averaging of appraised lot values, phase-in period for attaining the target annual lease rent, and the extension of the lease term would all have the effect of artificially reducing annual rents below what the evidence suggests could be earned in an open, competitive leasing market or in other investments. Moreover, the contract rental rate is still below prudent market rates of return including rates charged by other states for similar properties (5 to 5.5. percent). At a minimum the rental rate should equal the implicit rates of return calculated using the Duffield Model (6 percent).

The Land Board should heed the Subcommittee's recommendation to research the divestment option for state-owned cottage sites. In addition, the Land Board should consider other ways to unify the ownership of the cottage site lots and the improvements on them, as this is absolutely essential for securing the maximum long-term financial return to trust beneficiaries.

Exhibit 32

[deliberately left blank]

Exhibit 33

Transcript, Land Bd. Cottage Site

Subcommittee Meeting (April 22, 2008)

STATE BOARD OF LAND COMMISSIONERS

COTTAGE SITE SUBCOMMITTEE MEETING WORK GROUP

APRIL 22 2008 – 1:00 P.M.-5:00 P.M.

IDAHO DEPARTMENT OF LANDS, 300 N 6TH STREET, SUITE 103, BOISE ID 83720-0050

CHAIRMAN: BEN YSURSA, SECRETARY OF STATE

MEMBER: TOM LUNA, SUPERINTENDENT OF PUBLIC INSTRUCTION

AGENDA TOPICS:

- BRAINSTORM TOPIC: COTTAGE SITE LEASES EXPIRING IN 2010
- HOW DO WE HANDLE THE SHORT-TERM VERSUS LONG-TERM ISSUES
- DEVELOPMENT OF PROCESS
- ROUNDTABLE DISCUSSION ON MARKET RENT
- PRESENTATION BY STAN MOE, APPRAISER
- DISCUSSION/COMMENTS BY ED MORRIS, APPRAISER
- DISCUSSION/COMMENTS BY JOE CORLETT, APPRAISER
- DISCUSSION/COMMENTS FROM MEMBERS OF PRIEST LAKE COTTAGE SITE ASSOCIATION
- DISCUSSION/COMMENTS FROM MEMBERS OF PAYETTE LAKE CABIN OWNERS ASSOCIATION
- DISCUSSION/COMMENTS BY DEPARTMENT OF LANDS STAFF
- DISCUSSION/COMMENTS BY LAND BOARD STAFF MEMBERS

STATE BOARD OF LAND COMMISSIONERS

COTTAGE SITE SUBCOMMITTEE MEETING

APRIL 22, 2008

Start: 1:04 p.m.

End: 4:10 p.m.

Location: Department of Lands, 300 North 6th Street, Suite 103, Boise

---

SPEAKERS:

- Ben Ysursa, Secretary of State, Chairman of the Subcommittee
- Tom Luna, Superintendent of Public Instruction, Subcommittee Member
- Bonnie Butler, Office of the Governor
- Chuck Goodenough, Office of the Secretary of State
- Clive Strong, Office of the Attorney General
- George Bacon, Director, Department of Lands
- Jason Hancock, Office of the Superintendent of Public Instruction
- Brad Hoaglun, Office of the State Controller
- Loren Macey, Cottage Site Owner, Payette Lakes
- Chuck Lempesis, Counsel, Priest Lake Cottage Sites Association
- David Leroy, Counsel, Payette Lakes Cabin Owners Association
- Karen Young, Cottage Site Owner, Payette Lakes
- Jim Young, President, Payette Lakes Cabin Owners Association
- Bud Belles, Cottage Site Owner, Priest Lake
- Ed Morris, Appraiser
- Stan Moe Appraiser
- Jane Wright, IDL
- Kathy Opp, IDL
- Craig Thompson, IDL

- Josh Boyd, Cottage Site Owner, Payette Lakes
- Joe Corlett, Appraiser
- Denny Christenson, Leaseholder, Priest Lake
- Mike Fery, Leaseholder, Payette Lake

Secretary of State Ben Ysursa: (tape delay) – one of the two co-chairmen of the subcommittee on the cottage sites. Superintendent Luna is out of the state and will be unable to be here. He is represented by a staff member and expresses his regrets for not being here.

Who was that? Luna? I thought he was out – he just told me a lie.

I thought you were in Pittsburg?

Superintendent Luna: In about an hour now.

Secretary of State Ysursa: Well, welcome. I was expressing your regrets.

Superintendent Luna: Oh. Well, can I still sneak out?

Secretary of State Ysursa: If you want to leave, you can. Nice to have you here, Tom.

So Tom surprised me as I said that. Don't take that as an indication of my candor and truth today in the meeting by saying he's out of state and shows up right here.

The reason for the meeting obviously is so the working group gets some ideas of where we're headed on the leases that are expiring, as we all know, in 2010. This group is together to work on some areas that we've all heard about before and to make

56 recommendations to the Board. Tom and I are just two members of the Board, as you well
57 know, and we could make some recommendations.
58
59 My idea is if we're going to have to have more than one meeting obviously I'd like to –
60 hopefully we could get this down to two or three and then be able to make some
61 presentation to the Board on the recommendations.
62
63 Having said that, as I was asking earlier here, we have a short-term issue facing us yet again
64 versus the long-term issue. The Board has to give six months' notice of any increase in
65 rental. That is in – that's July first. So in June we have to come up with something that
66 we're going to do for calendar year 2009. That again faces us with what's going to happen,
67 but we'll approach that.
68
69 The idea here is to get some methodology, some agreement, whatever. The idea today is
70 to make a few comments, get to – Mr. Moe will give a presentation and kind of like a
71 methodology of how he is very knowledgeable in the Priest Lake area and has done the –
72 not only the state lots up there but the federal lots. And the bottom line on all this, we've
73 all talked about it. We can talk about multipliers. We can talk about values. Number one,
74 we need to get to what's market rent. The lessees have indicated that they have no
75 problem paying – well, they may have a problem paying it – but no – the object is to pay
76 market rent. That's our mandate, 310a. You can call it market rent. Article 9, Section 8,
77 maximize income for the endowments. Inherent in that mandate is market rent.
78
79 Having said that, there are umpteen numbers of ways to talk about what is market rent. So
80 the idea here, at least today – we'll have – Mr. Moe could give some of his insight and then
81 I believe the – Dave and Chuck and some other folks from the Associations – I think you
82 have a couple of folks who want to talk a little bit about methodology. The Director,
83 George Bacon, will have some comments, and we'll go from there, including trying to set up

84 future meetings and where we're headed. I – it will come up, but it's not my intention to
85 get in to an elongated discussion about premium rent, 10%, 100% and whatever. That can
86 be left for a special day on that.
87
88 Obviously it encompasses the whole scheme of how we get to market rent and whatever,
89 but I do not want to have a discussion on that. That – the previous time we had a
90 subcommittee meet, that actual final discussion was for the Board itself on the premium
91 rental. Whatever. Certainly we can make recommendations and talk about it later today. I
92 would prefer that we keep that kind of off the table directly talking about premium rent.
93 So we can get down to my idea today and quit talking too long and certainly allow Tom to
94 say a few words before he takes off. But it is so – let's talk about valuation and
95 methodology. That was the main idea today. I talked a little bit with Jim beforehand, a few
96 – a month ago or so – saying that we really want to see if there is a different way to skin a
97 cat on this, or whatever but bottom line is – market rent. We can talk about what 310a
98 meant. I've read everything you want to know about 310a. We know what it means. The
99 whole idea was to do away with conflict auctions every ten years. That has been done. So
100 the idea of stable leases in there was the fact that leases that were long and lasting were
101 not being able to be conflicted. That has been accomplished. They are not conflicted. So
102 we also have consensus. We – legislation was passed up to thirty-five years for lease terms.
103 I think there's some nuances to that that the Director can talk about or whatever, but there
104 was certainly consensus among Board members. That was a request from the Board to the
105 Department through the Legislature to extend that. So that is a – that's a given. Don't
106 waste your breath on saying we ought to have thirty-five year leases because we're going
107 to.
108
109 Having said – some other – where there seems to be consensus in some Board members,
110 staffs can certainly speak up if they wish, is the fact that we ought to be doing independent
111 appraisals and have the same methodology at both lakes. Though as time goes by, I

112 wonder how – oh, and I would like an update, just real quick before we get going too far,
113 the update of the lawsuit in Payette Lake on the appraisal method. Did anybody get any
114 insight on where that's at in the legal process?
115
116 **Mr. Jim Young:** Mr. Secretary, I do not know what the status of that lawsuit is. I haven't heard, you
117 know, where it's at recently. Maybe it – yeah, I just don't know.
118
119 **Mr. David Leroy**: Ben, we had hoped that Tony Park would be able to join us. If he can come, you'll
120 be up to the minute on that. If we don't get that information to you today, I'll get you a
121 memo on it.
122
123 **Secretary of State Ysursa:** That's fine. I was just curious if there was any – I'm sure if there was a
124 breakthrough on that, we would have heard about it.
125
126 **Mr. Leroy:** I presume it's still before the District Court.
127
128 **Secretary of State Ysursa:** Yeah. And – anyway, the consensus on having – abandoning the Payette
129 – Valley County assessments as the basis there and rather go to independent appraisals –
130 so I don't want to get too long and talk your time away, Tom, so why don't you –
131
132 **Superintendent Tom Luna:** You already did, Ben.
133
134 **Secretary of State Ysursa:** Do you want to interject some things here?
135
136 **Superintendent Luna:** I think you said it all. I'm learning as we go. You've lived this half of your life
137 now. But I think we have the right people at the table. This is an opportunity to, you know,
138 figure out a way for us to meet our obligations on the Land Board to bring some stability
139 and, you know, to these cottage site leases and, you know, for those who own those leases.

140 So, like I said, I think you have the right people at the table now unless there may be
141 somebody here still learning all the details about where we're currently at and how we
142 move forward. So that's all I have for now.
143
144 **Secretary of State Ysursa:** Thanks, Tom.
145
146 They – some other consent – ideas that are out there – we can talk about two and a half
147 percent – two and a half percent of what. We're talking about what today, other aspects of
148 the lease. Seasonal rental limitations. That's something that the – we at the state certainly
149 want your input and feedback on.
150
151 Currently there's a fourteen-day limitation written into the lease. Read real closely. That's
152 without consent. Seems to me that should be longer with consent, but that's another
153 question about the leases. But any input there, I think the Department and the Land
154 Board's very receptive to any sort of suggestion from the associations on relaxing those
155 limitations. So that's there. I know the Department has some questions on whether we –
156 again, specific questions on the lease, and I think that could be in a more smaller working
157 group on some legal input on insurance requirements and things like that, but I know the
158 Department has some questions about letting those be raised up.
159
160 Evaluation appeal process. Again, we have an appeal process that's in the lease now – the
161 current lease. The new lease had a little – the new lease, which I consider frankly dead but
162 has never been used – we had two – that was going to be used on the auction of the two
163 lots at Priest Lake. We know how those went. So it's never been used. I – I think there was
164 no significant discussion about the appeal process change that was in that lease. The Board
165 – the Board spent most of the time – the Board spent most of the time talking about
166 whether we ought to go for the six percent or five percent. The Board opted for five
167 percent and – but that has never been in place either because, as you know, what

168 happened to those auctions. That's where I'd like to go today is to have Mr. Moe give a
169 presentation.
170
171 Again, follow up, Dave and Chuck. What's your plan of attack for some of your – I had a
172 letter from Jim about Mr. Corlett and Mr. Morris – or somebody having a methodology
173 discussion also. Correct?
174
175 **Mr. Young:** That's right.
176
177 **Secretary of State Ysursa:** And then George will have some comments overall –
178
179 One key thing, and I don't want to get too much into the federal side of things, but anytime
180 – I know the Department is looking at, and I certainly think it's a positive thing, Forest
181 Service is right down the hall from my new temporary office. I talked to them and said I'd
182 like to see what the appraisals were on the federal lots at Priest Lake and Sawtooth area,
183 Pettit Lake and whatever. I'd like to – interesting. We're going through that process right
184 now. I'd like to see those. Made the request just down the hall, and it came back to me,
185 and he just happens to be a good friend of mine, Andy Brunelle, and he came back and said
186 well, we, uh, the Department, Deputy Director of something, kind of put an embargo on
187 information and – while they're looking at it. The obvious problem is, in my humble
188 opinion, because of the way they artificially constrained market rate in the statute and with
189 their inflation index, they're looking at horrendous increases and so for them to be put up
190 as the model of clarity and whatever is not a very good idea, in my humble opinion,
191 because they're in the same mess we are and they don't have the strong mandate.
192
193 So having said that, any sort of value has to have some – either an annual appraisal method
194 or a decent annual index that doesn't slam you too bad and then three or four years later
195 with no increase you get slammed anyway. But we do think it's broken. If you have a – in

196 ten years at Payette Lake have an annual increase of twenty-five percent average that is
197 getting to be rather out of sight. And that's counting the zero in 2008. So you can – I know
198 I'm preaching to the choir here, but if – if any other comments – but I'd like to have
199 Mr. Moe give us his methodology or how he's doing it or his insight to what's going on in
200 Priest Lake. I would say that he is – he helps the state.
201
202 You have some comment?
203
204 **Superintendent Luna:** Yes, when you're done, and before Mr. Moe –
205
206 **Secretary of State Ysursa:** Okay.
207
208 **Superintendent Luna:** Could you – could we have – go around the table real quick (inaudible) – I'm
209 curious who's here.
210
211 **Secretary of State Ysursa:** Oh, introduce themselves? Okay. Well, we did have a – okay. That's
212 fine. Go ahead, Chuck.
213
214 **Mr. Chuck Goodenough:** Chuck Goodenough with the Secretary of State's office.
215
216 **Mr. Chuck Lempesis:** I'm Chuck Lempesis. I represent the Priest Lake State Lessees' Association.
217
218 **Mr. Bud Belles:** I'm Bud Belles. I'm the President of Priest Lake State Lessee's Association.
219
220 **Mr. Ed Morris:** Ed Morris, appraiser. I've been retained by both Priest and Payette Lakes.
221
222 **Mr. Joe Corlett**: Joe Corlett, Mountain States Appraisal on behalf of Payette Lakes.
223

224 **Mr. Denny Christiansen:** Denny Christiansen, board member of Priest Lake Lessees' Association.

225

226 **Mr. Josh Boyd:** Josh Boyd, member of the Payette Lake Lessee Association.

227

228 **Ms. Kathy Opp:** Kathy Opp, Deputy Director for Idaho Department of Lands.

229

230 **Ms. Jane Wright:** Jane Wright, Financial Analyst, Idaho Department of Lands.

231

232 **Ms. Susan Terry:** Susan Terry, Department of Lands.

233

234 **Ms. Karen Young:** Karen Young, leaseholder, Payette Lake.

235

236 **Mr. Brad Hoaglun:** Brad Hoaglun representing the State Controller Donna Jones.

237

238 **Mr. Jason Hancock:** Jason Hancock, Deputy Chief of Staff, State Department of Education.

239

240 **Mr. Mike Fery:** Mike Fery, representing leaseholders at Payette.

241

242 **Ms. Loren Macey:** Loren Macey, Payette leaseholder.

243

244 **Mr. Stan Moe:** Stan Moe, Columbia Valuation Group, Coeur d'Alene.

245

246 **Mr. Craig Thompson:** Craig Thompson, Commercial Program Manager, Department of Lands.

247

248 **Mr. Jim Young:** Jim Young. I'm the president of the Payette Lake Cabin Owners' Association.

249

250 **Mr. David Leroy:** Dave Leroy, Attorney at Law, representing Payette Lake and formerly a member

251 of the Board in the '70s when we faced this issue.

252

253 **(Male Voice):** Why didn't you fix it then?

254

255 **Mr. Leroy:** I thought we did.

256

257 **Secretary of State Ysursa:** He was planning ahead for billable hours.

258

259 **Director George Bacon:** George Bacon, Director, Department of Lands.

260

261 **Secretary of State Ysursa:** Okay. Without further ado, Stan Moe, please.

262

263 **Mr. Moe:** Well, thanks. I –

264

265 **Secretary of State Ysursa:** This has been a very informal type thing. Anybody wants to take their
266 coats off, please do, and relax. Thank you.

267

268 **Mr. Moe:** Well, I wasn't given a whole lot of specific instruction or direction here so I'm going to
269 take your lead and start out by just talking about differences between methodology,
270 federal and state laws.

271

272 I've been involved with this process for quite a while, too. I started out representing the
273 Payette Lake Cabin Owners – cabin users – when the rate was contested twenty years ago,
274 and at that point helped with the rate, and that's been the rate ever since. Then seven or
275 eight years ago we got involved with the Priest Lake cabin users in an appeal of the
276 appraisals that were done there, and we did about seventy-five appraisals on Priest Lake at
277 that time for the cabin users and went through the appeal process. And then after that,
278 the Department of Lands came and – to me – and said we'd like you to do the next round of
279 appraisals, which we did. So we now have appraised every lot, every state lot, on Priest

Lake. We just finished doing the federal lots on Priest Lake. It's in review at this point. In fact, he's reviewing it today as we speak. That's why you can't get any information.

I guess my point is I'm not here as an advocate or to promote one side or the other. I think you're doing a good thing by bringing both sides together at the table and trying to work this out.

That being said let me go through just a few differences between the federal and the state lot valuation methods. Actually they're very similar. The federal lots are now under a new act called CUFFA, Cabin Users' Federal Fairness Act, which dictates the methodology of appraisals. It is essentially identical to the way it was ten years ago when we did the federal lots. We did exactly the same thing. The only changes that they have made that I can see of substance is that now they require the Forest Service to provide the appraiser with an inventory. That inventory has to do with the improvements that were supplied by third parties for the Forest Service.

The intent there is to get back to what they call a native and natural state of just before anything was done, but they don't want to charge or include in the value any improvements done by the lessees, or the permittees in that case. They're real sensitive about that. It's the same thing on the state side. We've been asked to appraise them. I mean, they don't like – the state doesn't like native and natural so we call it – it's the natural state and in this state excluding any improvements that are done by the leaseholders or third parties. So in that regard, they're identical. Both are.

The intent is to exclude improvements done by either the agencies or any third parties from the valuation – or those are included, I should say. Yeah. Any improvements done by the lessees or permittees are excluded from the property. But if you have a public road

307 coming by there, a county road, that's considered. But if there's a mile long private access
308 road into the tract, that's excluded from the valuation.
309
310 Some other things. The federal lots are appraised in groupings. They have what they call a
311 typical lot, and that typical lot will represent any where from five to thirty lots in a group.
312 Those groupings have been determined by the permittees and federal employees together,
313 and they've come up with a consensus and say okay these fit within that group. Once it's
314 set, then the appraised value for that typical lot applies to all lots in the group. So it saves a
315 lot of effort on the appraisal side. There is a process for changing from one group to the
316 other. It's like an appeal process they can go through.
317
318 On the state side, every lot is appraised individually. I won't get into lease rates. You said
319 you've already done that.
320
321 Indexing is different. Right now the indexing on the federal side is based on a fixed rate.
322 They've got a – I can't tell you what the specific index is, but it has nothing to do with the
323 value of federal lots. But it is indexing at a fairly nominal rate –
324
325 **Secretary of State Ysursa:** It's the GNP implicit price deflator, whatever the heck that is.
326
327 **Mr. Moe:** Yeah. You know that's under five percent a year. So what's happening is every ten years
328 now they're getting every year the spread between market, the way we're defining market,
329 and the actual lease rate is getting greater. So if you have it for a ten-year period, they're
330 going to be hit with a whopping increase. Can't give you the numbers, but I can tell you
331 that in 2004 the average lot value at Priest Lake that we appraised was $220,000. If they
332 approve our appraisal on the federal lots this year for 2007, the difference is going to be
333 less than two percent in value. That's a market increase for the – a real huge increase for

334 federal lots. Part of that is due to the time difference. There's a three-year time
335 difference.
336
337 **Secretary of State Ysursa:** Stan, can you go over that one more time? You say that the value is –
338
339 **Mr. Moe:** Do you want value for state lots?
340
341 **Secretary of State Ysursa:** State lots.
342
343 **Mr. Moe:** In 2004 it was $220,000 on Priest Lake. The average value for federal lots on the water
344 will be less than two percent different, assuming we get our approvals. Now why is that
345 different. There are some physical differences – uh, differences. The federal lots do not go
346 to the water. So in looking at those, we considered that there's a strip of land that varies
347 from thirty feet to fifty, sixty feet sometimes of public land between the actual lot and the
348 lake, and so you can't call it a waterfront lot. So our method of evaluation there is not price
349 per front foot, although we look at that. We're looking at a lot value.
350
351 Now, Priest Lake, the way I did it was to arrive at a typical or a base value for a waterfront
352 lot and then adjust that for these differences and in setback from the lake. Being next to a
353 campground, where you have a lot of public access, and then the other things, like – like,
354 uh, uh, access to utilities – some have sewer, water; others have nothing. Those we do
355 with both (inaudible) – adjust for those.
356
357 In the state – on the state side, the majority of lots abut one another. So you've got lot, lot,
358 lot – no public land. I don't think there's a single lot – but maybe a few on the federal side
359 – where you actually have lot length of like – there's public strips between each one. And
360 the public can come in and set up a camp and whatever they want in there. One permittee

361 says they came in and picked all my huckleberries. Well, they weren't hers. I mean, people
362 take ownership.
363
364 Those are probably the primary differences in the physical setting in the way they're laid
365 out. The methodology is virtually the same as far as we're looking for the fee simple value
366 of a lot. And then the lease rate is applied to that, and I have nothing to do with the lease
367 rate.
368
369 Well, that – I mean that's pretty much the bottom line of you're going to have a lot of
370 controversy on the federal side this year, too.
371
372 **Secretary of State Ysursa:** I know.
373
374 **Mr. Moe:** A lot. And they may hold out for a year or two on making their decision. They're just in
375 the middle of the process. Most of those haven't been reviewed yet. I have some thoughts
376 on methodology, too, but I'm not going to – they've got – I appreciate the fact that Ed and
377 Joe are here because I don't think you need to go out of state to find experts on this stuff.
378 They've been involved with these for a long time. They're both friends, and we can sit
379 down to the table and talk about it, and I think that's where you go with some of these
380 issues.
381
382 **Secretary of State Ysursa:** Go ahead, Chuck.
383
384 **Mr. Goodenough:** Mr. Moe, I know you can't consider the value of the improvements in part of the
385 land value, but can you consider the ability of the lessee to build a, you know, given type of
386 structure. Does that enter into the value of the lot? Because I mean we have some very
387 sumptuous housing on Priest Lake and Payette Lake both, whereas on the federal lots on
388 Priest Lake, they're all pretty federal campground-looking buildings.

Mr. Moe: Yeah. Well, the feds will tell you, and this is the direction we have, that's a permit issue. So that's considered in there in what they call the five percent rate. They lump it all together, see. That's another valuation issue. That's the permit rate issue on these holders.

Secretary of State Ysursa: Dave.

Mr. Leroy: Mr. Chairman, Stan, I'm a little bit unclear as to at this point precisely what your assignment is for the state. Do you have a written charter you are to go forward and do this, this and this? I want to know that because I want our experts – we want to shape our direction to them appropriately to mimic what you're doing or supplement what you're doing or contrast what you're doing. What is your job and how was it defined?

Mr. Moe: Well, we did reappraisal in 2004. It will be coming up again in 2009. We will have a shot at that. We don't have any agreement arrangement for that yet. What we are doing is indexing. And so each year the way it's set up on the state side is they're taking an average rate of increase for the previous five years. And that –

Mr. Leroy: How do you compute that? Do you –

Mr. Moe: Well, you – let's just say you have five years. In one year it was twenty percent; one year it was twenty-five; one year it was fifteen; one was ten; one was zero. So the average in there is going to be twelve to fifteen percent, something along those lines.

Mr. Ed Morris: That's the rolling average you're using –

Mr. Moe: It's a rolling average, yeah.

417

418 **Mr. Leroy:** And those are off appraisal – Valley County appraisal numbers?

419

420 **Mr. Moe:** No, those are off our appraisals.

421

422 **Mr. Leroy:** Independent appraisals.

423

424 **Mr. Moe:** Each year. Yeah.

425

426 **Mr. Leroy:** At both – at both lakes.

427

428 **Mr. Moe:** Well, we're only doing Priest Lake.

429

430 **Secretary of State Ysursa:** Priest Lake.

431

432 **Mr. Leroy:** And nothing yet at Payette.

433

434 **Mr. Moe:** No. Payette, as I understand it, is still going with the –

435

436 **Secretary of State Ysursa:** County assessor.

437

438 **Mr. Moe:** Yeah. But the problem with that, in both places there are no more, or very few, vacant
439 lots. So that process is going to become muddled. If you don't have good sales data to
440 base that annual increase on, it's very questionable, and we could talk a lot about different
441 methods for abstraction – abstracting improvements and that sort of thing. But that's
442 going to be a very difficult issue in the future.

443

444 **Mr. Leroy:** Ben, follow up?

So at this point, you don't have any – any pre-authorized assignment, or concept, as to Payette Lake. You – you don't have an actual assignment.

Mr. Moe: None.

Mr. Leroy: Okay.

Secretary of State Ysursa: Now, the reason we wanted Stan to talk was that he does – he's very familiar with Priest Lake. And earlier on there was a request to talk a little bit about the federal side. And, while we had him and he was down here, while we had him here to talk about some of that – he can't disclose much about it because it's under an embargo, but wanted to kind of get that information out there that that is not necessarily the arc of the covenant of how you can lease this. This is not the federal side, notwithstanding some of the comments sent to us earlier on.

The – Stan, where are you now? We need to index again for 2009.

Mr. Moe: We're coming up on that –

Secretary of State Ysursa: Up at Priest Lake.

Mr. Moe: – at Priest and actual going into that – that should be coming, I would guess, in the next couple of months, though.

Secretary of State Ysursa: Well, I hope you get a go-ahead rather quickly.

George.

473

474 **Mr. Moe:** But that's going to be problematic because there are no sales. No sales of vacant lots. So
475 what are we going to base that value on?
476

477 **Secretary of State Ysursa:** Well, one year drops off. Another year with hardly anything gets on,
478 right?
479

480 **Mr. Moe:** Yeah. And it's certainly going to go up because we still have 2004 and 2005 that are built
481 into that formula. So even though there may be no increases this year, it's still going to go
482 up.
483

484 **Secretary of State Ysursa:** That was some of the comments or criticism of that from Priest Lake is
485 that it's – the rolling five years – it's catching – the high ones are going to stay in it for a
486 while – for about a year.
487

488 **Mr. Moe:** Well, you get a break when it shoots up unusually high. When it went up fifty, sixty, a
489 hundred percent, the rates didn't go up like that. Well, they did on Payette. At Priest
490 there's a rolling average so you'd get hit easier during the high increase years, but then it
491 lags for a few years afterwards so it takes some time to catch up.
492

493 **Secretary of State Ysursa:** But just for the sake of the record, the last 2000 – let's take 2006. The
494 index at Priest, you went – Priest Lake went up eight percent in 2007; Priest Lake went up
495 12%, 2008 – Priest Lake went up 15%. Using that index is what you're telling us.
496

497 **Mr. Moe:** And those – the big years were 2004, 2005. The big years of increase – it continued to go
498 up some of 2006, but I just off the top of my head, I'm going to say 2000, 2008 or 7 and 8
499 are going to be relatively flat.
500

501 **Secretary of State Ysursa:** So on the – I would urge George and others to get to Stan, who's doing
502 our indexing. We need to have that information by our – latest by our June meeting,
503 obviously, because we still have – we have a short-term decision to make about 2009 with
504 rents at both lakes, like I indicated, and the date of the index data report from Mr. Moe last
505 year was May 24th so if that's any indication of where we need to be.
506
507 **Mr. Young:** You need it in two days?
508
509 **Secretary of State Ysursa:** Well, a month and two days.
510
511 So – any other questions from the group for Mr. Moe?
512
513 Yes, sir.
514
515 **Mr. Morris:** May I ask Mr. Moe some questions?
516
517 **Secretary of State Ysursa:** And he will be able to ask you questions, if you want. I don't want this as
518 an adversarial thing. But go ahead. We'll –
519
520 **Mr. Young:** You may want to identify yourself for the record.
521
522 **Mr. Morris:** For the record, my name is Ed Morris, and I'm an appraiser. And I've been retained by
523 both of the associations to look at a number of issues regarding this, and one of our major
524 concerns is methodology. Generally speaking, the definition of market rent in my
525 profession is what similar properties are renting for in the marketplace. So the last time –
526 in fact, maybe the last two times these cottage site lease issues have come up, there's
527 always been a discussion about what data do we look at and what methodology do we
528 apply. And so I guess, from what I'm understanding, you're – Stan, your description was

529 essentially using the indexing process, and you have not been engaged to do the
530 reappraisal for the '09 or the 2010 new leases. Is that – is that correct?
531
532 **Mr. Moe:** Yeah.
533
534 **Mr. Morris:** Okay.
535
536 **Secretary of State Ysursa:** He did do the appraisals on the right – this one at Priest Lake. You have
537 appraised state lots.
538
539 **Mr. Moe:** 2004, we did everybody.
540
541 **Secretary of State Ysursa:** Yeah.
542
543 **Mr. Moe:** Three hundred and sixty-five. Yeah.
544
545 **Secretary of State Ysursa:** And market rent and the definition and your instructions then should be
546 no different than now.
547
548 **Mr. Morris:** And do you envision that you'll use the same set of appraisal instructions then?
549
550 **Secretary of State Ysursa:** Until somebody comes up with something better, I would say yes. We're
551 trying to get to market rent, and this is what we – bare land, simple – fee simple bare land
552 value is what was the instructions given at Priest Lake and Payette Lake.
553
554 I don't see where we should be – somebody has an idea that that appraisal method, you
555 know, if we're going to use independent appraisers, you guys know a hell of a lot more
556 about appraisals and what rate of market rent or what the market is than we do, but that

was the instructions given in 2004, and that's the instructions that I would see being given as we go down the way, unless somebody has a better idea. But I want to make it clear, I think there was an indication that he hadn't appraised state lots. He has appraised state lots under the current method.

Mr. Moe: And I would say the rate was not an issue that we were dealing with either for the feds or the state. That's set (inaudible).

Secretary of State Ysursa: Nor should it (inaudible). That wasn't your charge (inaudible).

Mr. Moe: That's how I did get involved twenty years ago to some degree.

Secretary of State Ysursa: You mean what the multiplying factor ought to be?

Mr. Moe: Yeah.

Secretary of State Ysursa: Yeah, I've read that, too.

Mr. Lempesis.

Mr. Lempesis: Well, go ahead. I don't want to interrupt Mr. Morris of all things.

Mr. Morris: I had a question about the improvements, and this is going to relate much more towards Priest Lake than Payette. Native and natural is probably a federal term. I like the terminology raw and unimproved land simply because it reflects the state of the land and the condition it was originally leased to the lessee. But on some of the lots in Priest, there are privately-owned sewer hookups and other types of improvements that belong to the lessee and are not easily replicated for any other use. There's also, you know, different

585 types of utilities that enter into that. Have you looked at, or researched, any particular
586 types of adjustments for those extractions when making comparisons to get the land
587 value?
588
589 **Mr. Moe:** Yes. We used to have a good working relationship with the Huckleberry Bay Company
590 before they closed their records to everybody and won't talk any more. We were able to
591 get some good figures out of them on sewer costs and water costs and streets (inaudible).
592 I've worked with two different sewer districts on the west side of the lake. The last one
593 was – oh, what's the north end there – they're putting in a new system right now so – we
594 had costs for the whole works up there. And, you know, depending on what the final costs
595 ought to be – it would be ten to fifteen thousand dollars a lot for that sewer system to be
596 put in.
597
598 **Secretary of State Ysursa:** Go ahead, Chuck.
599
600 **Mr. Lempesis:** Mr. Secretary, I want to follow up on something you said, which I think is the most –
601 I'm Chuck Lempesis, Priest Lake – I think it's the most germane point of the day. You and I
602 and many others here – this has been an intractable problem for most of our careers. And,
603 since I'll want to retire some day, I don't have to keep this going, you know – so the kids are
604 on (inaudible) –
605
606 **(Male Voice):** Yeah, kids are out of school. I think we can do something different.
607
608 **Mr. Lempesis:** (tape change) – the progress from the last time you did this, frankly, from where we
609 were to where we are, but we're hardly there. One, I agree that probably the lawyers and
610 some other reasoned people ought to look at the lease and screen up some things in there
611 – items that we thought would work but didn't work or don't work as well. The second
612 thing, though, is we keep coming back every time we revisit this issue to a percentage or

613 multiplier times fee simple rate. Then what are the appraisal instructions. How do we keep
614 up with the growth of the – or the inflation rate and not surprise people and ruin their day?
615 I just have a gut feeling, if nothing else, that there are other methodologies out there that
616 could be employed to find market rent that might be substantially less burdensome on the
617 state or us. And I'm trying to build some consensus here.
618
619 I know all three of these experts. I mean, we've used – and this is the usual suspects and
620 they're the best you can buy, okay. Seriously. It would seem to me that phase two, other
621 than looking at the lease, Ben, would be, and Mr. Superintendent, would be to look at what
622 methodologies there are. Maybe there is no other way. Maybe there's nothing that would
623 work. But I think tasking these gentlemen and others to make a – and Moe's shaking his
624 head – I think Mr. Morris, Mr. Corlett can make an examination and report back on that. It
625 could pay tremendous dividends. And on the third phase is whatever methodology seems
626 to surface as appropriate, then you could calculate how you're going – what value the
627 Board's going to put on it. But – I – I'd like to – I really urge all of us to look at those
628 methodologies as a starting point.
629
630 **Mr. Josh Boyd:** If I could just interject real quickly, it's something that maybe is on people's minds –
631
632 **Mr. Leroy:** Identify yourself.
633
634 **Mr. Boyd:** Josh Boyd, Payette Lake Cabin Owners' Association. And to parrot some of your words,
635 Secretary Ysursa, you said that, you know, as a Board, you guys don't know what market is
636 – it's these guys' job. And then we went on just in the next sentence – we said, well, he
637 doesn't get involved in rate. He gets involved in what the fee simple value of the land is,
638 and then you guys apply the rate. So it's like you said, we don't understand what market
639 rent is. We pay these guys to figure it out, but then at the end of the day, we just slap a
640 rate on top and that's what the lease is. I compare that with what Stan said in the middle

641 of his discussion where he said that, you know, it's going to become a problem because
642 there's no sales, and eventually this method is getting problematic. And so, to me, those
643 kind of two comments are a perfect segue to Chuck's comments about why don't we find a
644 method that works that maybe actually links to market rent. So – and I don't know what
645 the method would be, whether it's a rent survey or what, but seemingly it seems like, it
646 was Stan saying that his method's got problems, you know. You're saying these guys are
647 the experts, but the old method, you know, when you just took a value and then you
648 basically decide what market rent was by putting the rate on it – I mean, it seemed like kind
649 of those statements lead me to say that the – you know, we should be looking at this other
650 method, market rent, you know, something that actually determines what market is and
651 what people are paying versus the current.
652
653 **Secretary of State Ysursa:** Well, I think that that's well taken, but you know we've been at this for a
654 hell of a long time, and I haven't seen any brilliant suggestions from anybody on a different
655 way to do it and, not that we wouldn't entertain something, but it's been a giant vacuum
656 out there for any new thoughts. It's just fighting over five or two and a half or have the
657 Supreme Court of Montana say they weren't doing it right and they should go higher and
658 things like that and having the feds putting up a five percent rate and a phony five percent
659 limit and now they're in trouble. I mean there's a lot of suggestions out here that prove to
660 be absolutely bogus. And I would love to see something that would hold up. I have no
661 problem with a different way to skin a cat, but this idea of market rent is where we are.
662 And unfortunately market rent to you and market rent to us a lot of times are different.
663 We'd like to get to something that is defensible and meets our mandate obviously. But,
664 yeah, I'm open to suggestions, as one Board member, of other methodologies, but other
665 people have rented these cottage sites. The feds certainly have. Like I said, they're not the
666 model of clarify. Montana lawsuits, you know. Studies being done years ago being used by
667 McFadden and Knipe and these others. If you've all read those appraisals, I can't believe
668 somebody a lot smarter than myself and others and the appraisal field haven't come up

669 with something if there was something out there that was tenable. I don't want to be a
670 pessimist, but Lord knows this issue is déjà vu all over again.
671
672 Yes, Ed. You've got one.
673
674 **Mr. Morris:** Well, let me just – let me just back up here a little bit, Mr. Secretary, because markets
675 change and markets evolve over time. And we've seen a huge change over the last ten
676 years in this Priest Lake, Coeur d'Alene Lake, Pend Oreille Lake market. And I think many of
677 the same things, even perhaps to a higher degree on Payette, where they have developed,
678 and there is an active market for rentals for some of those cabin site properties. For other
679 litigation, I've done rent studies on those kinds of things on Coeur d'Alene Lake and the
680 Spokane River and there is an entirely different set of market data than anything that I've
681 seen the state ever look at, which is what do these properties rent for during their primary
682 season. And I think that that kind of data would be appropriate, highly probative, and it
683 would fit within the definition of market rent, which is what properties – similar property –
684 rents for in the actual marketplace.
685
686 **Mr. Leroy:** In line – uh, Dave Leroy – in line with your suggestion of how we commence the
687 meeting, why don't we call on our two presidents just to make a couple of opening
688 comments and then let's flip it to Ed and Joe to talk about this – this alternative concept if
689 we can suggest it.
690
691 I brought around to each of your offices that packet of materials that was an opening
692 statement by Jim Young, and attached to that were two documents – a form, a checklist, a
693 rental data confirmation and then sort of a concept of market rent with a definition of – a
694 professional definition of market rent and raw land as Ed was talking about. But if we make
695 just a brief opening statement and then kind of throw it that direction, that would be, I
696 think, maybe helpful in framing the discussion.

697

698 **Secretary of State Ysursa:** I have no problem with that.

699

700 But, Tom, I know you're getting – you have to leave in a little bit or –

701

702 **Superintendent Luna:** (inaudible)

703

704 **Secretary of State Ysursa:** Any comments or –

705

706 **Superintendent Luna:** No, I'm just listening and learning and paying attention.

707

708 **Secretary of State Ysursa:** Yeah, I think most of us received this from Jim.

709

710 George, you had a copy. You're cc'd. And we had all this.

711

712 So go ahead, Jim. Do you want to make some comments about your comments?

713

714 **Mr. Young:** Maybe I'll defer it to let Bud open it up, but I'd like to (inaudible).

715

716 **Mr. Bud Belles:** I'll go ahead.

717

718 **Secretary of State Ysursa:** Okay.

719

720 **Mr. Belles:** Bud Belles. Back in November of last year we had that meeting where there was lots of
721 emotion and all that, and the thing that I brought out was that at Priest Lake what we want
722 is a fair lease and one that we can predict what we're going to be paying into the future,
723 and I think that's what we're here today to talk about. I think that there are some ideas in
724 that document that Jim gave to you and that we participated in developing a little bit that

725 does suggest some different ways to achieve a market rent, and I really thank you for
726 putting this meeting together to get that ball rolling. And that's about all I have to say right
727 now.
728
729 **Secretary of State Ysursa:** Well, go ahead.
730
731 **Mr. Young:** Mr. Chairman, I also first off want to thank you and Secretary Luna and Director Bacon
732 for, you know, giving us the opportunity to have this meeting and discuss the issues. And
733 we did provide you kind of our opening thoughts about the issues that are on the table and
734 there are, you know, there are a number of issues there, probably ten or twelve, that
735 Mr. Leroy has outlined and need to – probably need to resolve in getting to a new lease.
736 But it seems like that it all centers around this definition of market rent, and I was very
737 encouraged that in your opening comments you basically said the same thing and identified
738 that as the crux of the issue and whether or not how you interpret that 58-310a, you know,
739 I'm going to leave that to you guys, you guys are the lawyers on that, but it – you're exactly
740 right. It's market rent and – and how do we arrive at it. And it seems like there's got to be
741 a better way to skin the cat than what we've done in the past because it has not achieved,
742 in my humble opinion, market rent nor has it provided stability. I mean, we just have to
743 take a look at where we're at at Payette Lake to see that we can (inaudible) stability there.
744
745 Unfortunately, it's in a state where – it's in a sad state of instability. So – so I think we all
746 recognize that it's broken and it needs to be fixed and that we need to come up with
747 something different. And I don't see, you know, if we head down this path again, appraisal
748 value and applying a rate on appraisal value, I think we're going to be right back where
749 we're at of – in a situation of instability. And I'm not sure that that is reflective of market
750 rent, and I guess I would, on that note, defer to the experts. And we have three really
751 smart guys in the room here and hopefully they can guide us and lead us in determining

752 what that market rent ought to be. So on that note maybe I defer to Ed and Joe and
753 Mr. Moe here and hopefully we can get there.
754
755 **Secretary of State Ysursa:** Joe or Ed, do you want to comment?
756
757 **(Male Voice):** You haven't said anything –
758
759 **Mr. Joe Corlett:** I haven't said a word. I'm Joe Corlett by the way and I'd ask the Secretary –
760
761 **Secretary of State Ysursa:** Be quiet and be thought a fool and open one's mouth and remove all
762 doubt.
763
764 **Mr. Corlett:** I've been sitting there just being real quiet.
765
766 **Secretary of State Ysursa:** I don't follow that idea though.
767
768 **Mr. Corlett:** Well, I thought that – in 2001, I had the same thought because I was hired by the
769 federal cabin users to represent the appraisal thought in the CUFFA act. And CUFFA was a
770 big deal. It got me to a point where I had the pleasure and privilege of testifying in front of
771 Congress. What happened in CUFFA is there were a whole bunch of different appraisal
772 techniques that different appraisers were using, and it was being approved, disapproved,
773 whatever, and they weren't necessarily analyzing the natural native land as discussed in the
774 Forest Service handbook. They also used leasehold sales, which are now precluded from
775 being used. In other words, you're supposed to go out and find a similar sale. And one
776 thing the federal, more so than the state, never recognized in the appraisal process was the
777 fact that many of these federal lots were legally non-conforming, pre-existing uses, which
778 meant that you could have a quarter acre or a half an acre in like Blaine County, for
779 example, at Pettit Lake, with a ten-acre minimum zoning. So there's kind of an accrual

780 there of about nine and three quarters to nine and a half acres of famine real estate you
781 really don't have to buy, but you're willing to pay a little bit more, or a lot more, to have
782 that right. So that was taken out in CUFFA, and then the inventory was a big issue as to
783 what the permittees had put in to the various lots. And so I can see the problems with that
784 and, you know, it's where the sovereign supersedes the county zoning and that. But, in
785 getting back to Payette Lakes, one of the first things is all these years we've been appraising
786 these lots, we've never been asked to estimate a market rent, which we're all three trained
787 to do. And there are a couple of different ways of getting market rent, but it's all driven by
788 the market. It's not driven by a legislative percentage. It's what the market will bear. Well,
789 I would broadly make the – just a general suggestion that the higher the value of something
790 in residential real estate probably the lower the percentage you would expect back as – in
791 the form of rent. These are not income producing properties so they're highly restricted.
792
793 So we've never been asked to really estimate a market rent or what something should rent
794 for in this market. And it goes back to Ed's comment as market rent is pretty clearly
795 defined in our literature as more or less what a willing lessor is willing to take from a willing
796 lessee without undue duress in the market. So what we've seen is this dramatic increase in
797 the assessments in Valley County and that's a fact. It hasn't been a fact for the last year
798 and a half. We don't have any sales – stand sales – that really are giving us direction. One
799 thing the Valley County Assessor had as what I consider a flaw is in their verification
800 process for their re-indexing of value. In other words, their re-valuation. They would get
801 some of these verification forms and the verification form would say, yeah, we paid two
802 million dollars for this property. Well, they say great. We got a verified sale. Well, they go
803 back to the assessment and they have it assessed for two hundred thousand, a hundred in
804 improvements and a hundred to land. So now they say okay we've got to get rid of those
805 improvements in the new sale so we take a hundred thousand out of the two million and
806 come up with a million nine for the land. Well, that's not really the appraiser way to do it.
807 You know, I mean, you really have to try to figure out what the contribution of those

808 improvements is so your process for getting to the vacant land value was not very accurate
809 in my opinion.
810
811 **Mr. Morris:** It was biased.
812
813 **Mr. Corlett:** It – well –
814
815 **Mr. Morris:** Biased based on the allocation.
816
817 **Mr. Corlett:** Right. It was just – they're using a bad number coming out of a good number so that
818 exacerbated the Department's problem especially since we're tied to a percentage of the
819 assessor's market value, you know. And I had the opportunity to work with the appealers
820 up there through the tax appeals so I kind of have some knowledge on both sides of both
821 the leasehold and the fee simple types of issues, but more or less we've never been asked
822 to come to a market value –
823
824 **Mr. Morris:** A market rent.
825
826 **Mr. Corlett:** A market rent. It's always been market value.
827
828 **Mr. Morris:** I think Stan's got a comment, and then I'll make a comment after Stan, unless,
829 Mr. Secretary, you've got a different perspective.
830
831 **Secretary of State Ysursa:** No.
832
833 Go ahead, Stan. I love the battle of the appraisers.
834
835 **Mr. Moe:** Well, it's not a battle. I mean, these are my thoughts.

836

837 **Secretary of State Ysursa:** Agreement of the appraisers.

838

839 **Mr. Moe:** Yeah. Some thoughts that I had picked out, and almost parallel with Joe, is that when
840 you go to use sales of properties that were improved and extract the improvements out of
841 it, it's just fraught with problems. There are a number of things that you have to look at.
842 The buyer and seller will never tell you that the improvements are worth the same thing.
843 You start out with you don't know if they use it for a while, they got some use out of that
844 house before they tore it down, just a number of things in that order that complicate the
845 method. That's why I was so emphatic that we've got a problem. There are no more
846 vacant lots.

847

848 The other thing I wanted to bring up, just informational-wise, is an update as of this
849 morning that there are five state lease lots on the market with the MLS at Payette Lake.
850 They're – the lowest is $750,000. The cabin on there – the size is – it says zero to six
851 hundred square feet so you know it's a very small cabin. So the perceived issue here is the
852 state is losing a lot of what I call leasehold value. It's being claimed by the permittees or
853 the lessees here. A cabin on that order might cost a hundred thousand, so you've got eight
854 hundred thousand representing their leasehold value.

855

856 In Priest Lake, there are twelve state lease lots on the market right now. And they're
857 averaging six to eight hundred thousand dollars, and I haven't appraised every one, but I
858 could pretty well say that there's no improvements on those worth more than three
859 hundred thousand. So they're also looking for this two to three hundred thousand dollar
860 bonus of selling their lots.

861

862 So that's the perception. And that's the reality is that they are getting that – they have
863 gotten that. What I see as the reason for that is the lease rates are too low. And what

that's – whether it should be two and a half, five or what, I'm not going to go there. For sure, they're too low at Priest Lake.

Secretary of State Ysursa: Yes, Ed.

Mr. Morris: Stan brings up a whole different issue which relates to premium rent, which I think we really want to leave that off the table at this point in time. And the issue of premium rent is even more complex because you've got different issues that created or may create it at these two areas because in the Priest Lake area, this – this non-conforming use premium accrues to the owner of the improvement and every one of those are non-conforming uses up there on Priest Lake.

Secretary of State Ysursa: Not every one.

Mr. Morris: Well, almost every one. They're un-platted lots and they – they exceed the minimum lot size requirements under zoning, and they've never been legally platted. So generally speaking, that increment of value would accrue to the improvement owner, not the land owner.

Secretary of State Ysursa: Unless we're going to sell it.

Mr. Morris: Pardon me?

Secretary of State Ysursa: Well, we'll discuss – leave the discussion about zoning and how it applies to state endowment lands, and as long as we hang on to them rather than sell them –

Mr. Morris: And I think that's –

892 **Secretary of State Ysursa:** But that's another issue.

893

894 **Mr. Morris:** But that's an important issue because of the whole concept of market value and this is
895 – this sovereignty issue of we don't have to comply with zoning. The whole concept of
896 market value is the market – the private market place where you measure these things
897 because those individuals in the private market interact that economically create these
898 transactions do have to comply –

899

900 **Secretary of State Ysursa:** Right.

901

902 **Mr. Morris:** – and so market value, or market rent, must be measured within the context of those
903 local laws and ordinances. But I think even more important than that is to get back to this –
904 this concept of market rent. Many of these governmental lease situations are driven by
905 political wars, profit making, political decisions, and so I'd like to read within my profession
906 what the excepted definition of market rent is because I think it's got a number of elements
907 in here that touch on issues that we talked about – most probable rent that a property
908 should bring in a competitive and open market reflecting all conditions and restrictions of
909 the specified lease agreement – big issue – including term, rental adjustment, revaluation,
910 permitted uses, use restrictions and expense obligations. The lessee and lessor each acting
911 prudently and knowledgeably assuming the consummation of a lease contract as of a
912 specified date, passing of the leasehold from lessor to lessee under conditions whereby
913 lessor and lessee are typically motivated both parties are well informed and well advised
914 acting in what they consider to be their best interest, in other words, free market, lack of
915 duress. Reasonable time is allowed for exposure on the open market. Rental payments
916 made in terms of cash or U.S. dollars. Rental amount represents the normal consideration
917 for the leased property unaffected by special fees or concessions granted by anyone
918 affected with the lease transactions.

919

920 Now there's an awful lot of conditions and elements to that, many of which have been
921 items of contention in this process before, many of which the state specifically has
922 restricted or prohibited their appraiser from going into, but they're material essential,
923 essential elements in determining what market rent really is. And I would invite the
924 subcommittee and the Board to authorize a team of appraisers to look into these issues
925 and report back on methodologies and methods to determine market rent.
926
927 **Mr. Leroy:** Talk about this form, also, that you presented.
928
929 **Mr. Morris:** Well, that's a form that I think is included in the correspondence, which is a market
930 data confirmation grid and analysis framework which outlines all types of property data
931 and information to be able to accumulate the research and the factual information that
932 would provide an analysis framework for an appraiser to go through and start extracting
933 out components to do residual analyses and rental analyses on rents that are taking place
934 out there in the market. The vast majority of things that are rented are improved, but we
935 might run into a few unimproved lake lots or – or land rentals, but most of the data is going
936 to be improved. And this is a data sheet form to accumulate all the necessary information
937 from expenses, (inaudible), real property improvements, land descriptions and all the
938 documentation to perform analyses from the – from the information.
939
940 **Mr. Leroy:** Mr. Chairman, I have a question for these two guys.
941
942 **Secretary of State Ysursa:** Okay, Dave, go ahead. I will – the Department – I will be asking the
943 Department to comment on this – this is in the back of what they gave us a month ago or
944 April 10th.
945
946 Have you guys looked at it and have any response to the – what they're just going to say?
947

948 Go ahead Dave.

949

950 Think about it George.

951

952 **Mr. Leroy:** Well, having sat on this Board and part of what I think the Board needs to do to set the
953 same kind of predictability and civility that the leaseholders want, can you construct a
954 formula that captures this data and projects market rent with an equal degree of certainty
955 that you can assess fee simple values and will it be predictable, transparent, defensible if
956 these political leaders, who are charged with getting market rent and maximum income,
957 are doing their duty with the new formula. Can it be as simple as the old formula. Can it be
958 as professionally comfortable as the old formula.

959

960 **Mr. Morris:** You're asking me? You asking me? I think the answer to that certainly is yes, with
961 certain qualifiers. I think we can determine market rent with an equal degree of certainty
962 or accuracy that we can determine market value. In terms of what those value trends or
963 rental trends are going to be over time, there generally are tradeoffs between accuracy and
964 expediency and every time that I've been aware and involved in this process, which has
965 been maybe fifteen years or twenty years, a long time, this issue of indexing and revisiting
966 an adjustment, the tradeoff usually is formula versus reappraisal. And I think some – if you
967 look at the whole area of commercial leasing and lease terms, and those are common
968 tradeoffs that are dealt with continually in the private sector, you want in the leasing realm
969 leases to track market. So how do you do that? Do you generally go through the longer the
970 term lease the more adjustments you need? You know we've been go – we've been
971 looking at annual or five year or rolling adjustments – on a ten-year lease, you're going to
972 need some sort of similar mechanism even if we go out to twenty years or thirty years. But
973 that's got to be, you know. You can use both tracking mechanisms and you can use
974 appraisal process and you can use – get as laborious as going through reappraising it every
975 year, or you can use a combination of those which would trade off between the two as you

976 get more data and track rents. I think you'll find that rents are much more stable than
977 values because values are subject to immediate supply and demand and constriction when
978 the market changes. But at the same time you never really looked at rental trends in the
979 private market places on these lakes, and I think, with years worth of data to be able to
980 track those, you can predict them with an equal degree of accuracy and certainty.
981
982 **Mr. Goodenough:** Chuck Goodenough, Deputy Secretary of State. You've done appraisals in
983 bunches for litigation on Lake Coeur d'Alene and the Spokane River, Mr. Morris.
984
985 **Mr. Morris:** Correct.
986
987 **Mr. Goodenough:** What's the average term of those leases. Are there any thirty-five year leases or
988 ten-year leases? These are all short term –
989
990 **Mr. Morris:** They're all short-term leases.
991
992 **Mr. Goodenough:** Okay.
993
994 **Mr. Morris:** I take that back.
995
996 **Mr. Goodenough:** But what short term is it. Is it three years? One year?
997
998 **Mr. Morris:** I take that back. There are some – there are some leases that are private leases on
999 Pend Oreille, at least they have – they have been up there on waterfront lots through 2006,
1000 I think. I don't know that I've – I've confirmed their existence since that time. But they've
1001 essentially been five- or ten-year rollover leases, and they've been renewed on a long-term
1002 basis.
1003

1004 **(Male Voice):** Are they year to year now?

1005

1006 **Mr. Morris:** Are they year to year now? Uh –

1007

1008 **Mr. Leroy:** Who's the landlord in those instances?

1009

1010 **Mr. Moe:** Green family.

1011

1012 **Mr. Morris:** Yeah, I think it is or used to be. It might be an estate now, but it's from –

1013

1014 **Mr. Moe:** We just did that appraisal. They've got fourteen lots. They're non-conforming lots.
1015 Couldn't sell any. And they're an older couple that's trying to do some estate planning.
1016 They just look at that as kind of a gravy income. They've never done any analysis to see if
1017 what they're getting is the maximum. They're three to five thousand dollars a year a piece.

1018

1019 **Mr. Morris:** But if you look at the private rental market, there's also been developed on the lakes
1020 private rental markets where they will either lease on a seasonal basis or a weekly basis
1021 improved property, and those are entirely organized marketplaces for lakefront property.
1022 And I can't tell you off the top of my head what those are going to indicate because I
1023 haven't tried to track them over long periods of time, but I know there's a lot of data up
1024 there and highly organized rental markets for that kind of recreational real estate.

1025

1026 **Secretary of State Ysursa:** Chuck Lempesis.

1027

1028 **Mr. Lempesis:** Yeah, I just had a quick question of my friend, Stan Moe, here, who I have a high
1029 regard for. He's been our expert; he's been my expert in court. Everybody here – I don't
1030 think there's a lot of bias in these appraisers. I just don't. So I go back to the core question
1031 I had – is there a better way of doing business, and I'm hearing from Joe and from Ed

1032 examining this methodology has value to it and that it might lead to something. I heard
1033 you say earlier that we have problems with the present methodology without elaboration.
1034 Is this worth looking at? Is there something that the three of you could bring to us that
1035 might eliminate some of the problem?
1036
1037 **Mr. Moe:** I say absolutely it's worth looking at. I'm not so sure how clear it's going to be, but I
1038 talked to the Forest Service – the reviewer that I worked with – and I said how do you guys
1039 set your rates. Well, we call other states and other agencies. So they just do sort of a
1040 market research of other government agencies, and they think this is right. But is that a
1041 market research? No. You know, it has nothing to do – it's just – everybody's in the same
1042 boat, and it's never been really taken down to the level that Joe and Ed were talking about
1043 that I know of. We tried it with little bits and pieces. I just did this with a seasonal RV park
1044 there one day. I wanted to see where it came in and with all the weaknesses of that
1045 extraction method I came in with about five and a half percent return rate to the land.
1046 That's a commercial operation. There's no limitation on seasonal use or renting to others
1047 or operating it for a business.
1048
1049 **Mr. Leroy:** Well, Mr. Secretary, it would seem to me that where Idaho does lead the nation in
1050 progressive thoughts, this might be worth while. Well, what's funny?
1051
1052 **Secretary of State Ysursa:** Well, I know Tom has to go, but when this – let me read page seven of
1053 ten here. Other methods must be utilized – this is from what Jim Young sent us – other
1054 methods must be utilized. This is from what Jim Young sent us. Other methods must be
1055 utilized to determine and track market rent. I had this highlighted. The most viable
1056 method is to compare actual privately-owned comparable rental properties around Payette
1057 and Priest lakes. Using generally accepted MAI appraisal methods, privately-owned rental
1058 information should be gathered, compared and analyzed to arrive at market rent. For this
1059 reason, the Associations have commissioned experts to analyze and study to assemble

1060 relevant information and conceptualize a new formula. That's what we've been talking
1061 about.
1062
1063 **Mr. Leroy:** Yeah.
1064
1065 **Secretary of State Ysursa:** I have a comment that I placed in here that says I, for one, am willing to
1066 look at this. Tom is also, being the other member of the subcommittee, has made the same
1067 comment. He and I together. So I think it's certainly worth looking at. I certainly have a
1068 sneaking suspicion that this four million dollars we get out of rent might go down quite a
1069 bit. Who knows.
1070
1071 But what I am – what I do want to hear is, George, anybody from the Department, have any
1072 comments on that suggestion or their comments in particular –
1073
1074 Tom, thanks for coming. Have a safe flight.
1075
1076 **Mr. Leroy:** Sorry you're going to Pittsburg.
1077
1078 **Secretary of State Ysursa:** You going to go vote in that primary?
1079
1080 **Mr. Leroy:** I'm (inaudible) Pittsburg. First prize is a week in Pittsburg. Second prize is two weeks.
1081
1082 **Secretary of State Ysursa:** George or Kathy or anybody.
1083
1084 **Director Bacon:** Well, I think my staff may have more specific comments, but as I examined it, the
1085 first thought that crossed through my mind was if we do an analysis of market rents, it will
1086 probably show that it's two and a half percent of appraised or assessed land value because
1087 basically we are the market. And I see difficulty finding a good correlation or a big enough

1088 sample. So that would be my first concern. I – I hear what you're saying and the idea
1089 intrigues me, but where do you get the information is one concern. I guess I have an
1090 assumption, and maybe it's wrong, that the properties at Payette Lake are unique to
1091 Payette Lake and you can't really compare it to Lake Coeur d'Alene although that may be a
1092 better correlation than Bear Lake in Eastern Idaho or Lake Pend Oreille or Priest Lake, you
1093 know. How far afield do you go? Do you have to draw maybe some connection to – can
1094 you draw some connection – is this legitimate. Shows I had to think about this. Rents in a
1095 community like in all of McCall compared to market but compared to property value versus
1096 lakefront compared to property value. I mean does that even correlate so you have a
1097 bigger pool of rents?
1098
1099 **Secretary of State Ysursa:** Yeah, respond, please.
1100
1101 **Mr. Morris:** It is – for the record, this is Ed Morris, and it's my perception – first of all, we want to
1102 compare like with like whenever we can. And that's the essence of a credible comparison
1103 in the appraisal profession is to compare like with like and adjust for the differences. So
1104 the best comps for Payette are going to be Payette. The best comps for Priest are going to
1105 be Priest. When you run – when you get into the problems of let's call the land managers
1106 of six other states in the western U.S. and ask them what they want or what do they think
1107 they're getting or what they're requiring, we don't think that that's a very representative or
1108 credible indication of market rent because those rates of return come out of different
1109 markets, different demographics and a big issue is different climatic factors. And these lots
1110 up at Priest Lake have a very, very short time period where they can be used because of
1111 climate and snow and you've got different climatic factors, and actually different
1112 community factors. Down in Payette you've got some of the same climatic factors and high
1113 elevations, but you've also got the ski resort down there that may affect the rental market
1114 or may not affect the rental market. So the best comps are the most similar comps and I
1115 think we've got to be very, very careful about that. That's the same thing about land value.

1116 The best comps are the most similar that require the least adjustments, and that's why I
1117 say one of the weaknesses and one of the perhaps unfair things about the current situation
1118 is your desired rate of return may not – may or may not reflect all of those things in each
1119 locational, climatic different market in which you're operating. So I think it's important to
1120 look at those things and look at the data that is best and the data that is secondary and
1121 then try and reach some reasoned conclusion.
1122
1123 **Secretary of State Ysursa:** Joe.
1124
1125 **Mr. Corlett:** I'll add to that a little bit. Joe Corlett again. When we're doing a lively acquisition or a
1126 federal job we're constrained by the Uniform Appraisal Standards for Federal Land
1127 Acquisitions, and we can not use data that has one of the parties being involved is – as a
1128 sovereign government because of – in other words, it just can't be a public entity that is
1129 one of the parties in the transaction and that pretty much disqualifies the only data that
1130 you can really see from those government leases is a willing lessee – yeah, lessee is wanting
1131 to pay for that site. That is maybe a market indicator, but I still think that you would want
1132 to go to the private market and the individual location and see if you can determine what is
1133 being paid as a rent for that particular property. It's an extraction process if it's improved
1134 and that creates another level there that we have to deal with. We're more or less trained
1135 to deal with that through area analysis and trying to allocate appropriately.
1136
1137 **Director Bacon:** Maybe I didn't express myself (inaudible). My concern was – is how do we garner
1138 that data when – when – well, Payette Lake, maybe there's a little more private activity
1139 going on, but Priest Lake – I mean, where do you get the data?
1140
1141 **Mr. Morris:** I – I think – I think there's rental data at Priest Lake just like there is at Payette. I don't
1142 think very many people have ever gone looking for it in the past, but I think if somebody
1143 asked the questions, I suspect that the three of us could come up with something.

1144

1145 **Mr. Corlett:** It's reiterating – Joe Corlett again – that we've never been asked for market rent.
1146 We've just always been asked for market value.
1147

1148 **Director Bacon:** Now, if – to answer your question, if staff has any –
1149

1150 **Ms. Wright:** Of course, we have opinions. Not sure we should say them, but – on the rental, the
1151 rental market, the new lease term for leaseholders is thirty-five years and a significant
1152 component of a lease is the term of that lease. So to find a comparable with that kind of
1153 term, I would think, would be virtually impossible. Rental markets in the recreation market
1154 are generally timeshares, monthly, a weekend, maybe two weeks. So I – I appreciate the
1155 forum here, but when we get the high rent and the low rent by season are you going to
1156 extrapolate that to a twelve-month period of time? The leaseholders don't take your cabin
1157 off during time periods in which it isn't leased. So I'm – I'm not – I – I appreciate the
1158 Secretary's willingness to look at that as – but we in the Department are having trouble
1159 seeing it right now just on terms and being available as timeshares on recreation property.
1160

1161 **Secretary of State Ysursa:** Stan.
1162

1163 **Mr. Moe:** She makes a good point because if you're – if you don't find leases that are on a
1164 year-round basis, which we're trying to establish as an annual rate here, then you're –
1165 you're faced with trying to get properties that are leased out for short terms and add up
1166 the income they get for the year and then take your rate from that. Well, that's different
1167 than what we're talking about here. Though I'm not as optimistic as maybe Ed is about
1168 finding that data right now, but I don't know if it's available or not.
1169

1170 **Secretary of State Ysursa:** Any other comments? Is there someone who hasn't spoken for the first
1171 time before we recognize Chuck Lempesis for the twelfth time?

1172

1173 **Mr. Lempesis:** It hasn't been twelve. I think we're on eleven. Well, my only question is –

1174

1175 **Secretary of State Ysursa:** Go ahead, Chuck.

1176

1177 **Mr. Lempesis:** I understand the way you guys work, and I'm not – I don't have any expertise in
1178 appraisals. It would seem to me that there may be some general consensus that market
1179 rent, by looking at other rents, okay, might be a good way to go. The problem is where's
1180 the data. Okay. Well, right now, we don't have data on anything else either. I mean when
1181 we start looking at this five percent, four percent or whatever it is, we go to Possum
1182 Meadows, New Mexico, or some place, and say – or Lido Isle – I've seen Lido Isle, California,
1183 honest to God, so – but it would seem to me that even if you couldn't find the data at Priest
1184 Lake that you would then go to maybe to Coeur d'Alene Lake or Pend Oreille and
1185 extrapolate data from there. It would at least be closer than Possum Meadows.

1186

1187 **Mr. Moe:** Can I respond to that? Yeah. I think by limiting it to a geographic area that's a mistake.
1188 You need to look at the property type. These are residential properties, not commercial,
1189 but residential single family. So if we could expand the search to include all single family
1190 residential, we're going to get a much better source of data.

1191

1192 **Secretary of State Ysursa:** Yes. Go ahead.

1193

1194 **Mr. Morris:** The nature of most of these cabin sites – well, I don't know that about Payette, but
1195 most of the cabin sites at Priest, are seasonal in nature. I mean the roads aren't even
1196 plowed to get up – to get up to them. Climatic factors up there essentially limit those to
1197 three-to-four months' worth of use.

1198

1199 **Mr. Moe:** Right.

1200

1201 **Mr. Morris:** I think it's important to look at similar types of property. If – if it's residential property,
1202 then you're going to gravitate to residential income property in urban areas because you've
1203 got a high degree of rental data there whereas what we're really leasing is recreational
1204 property in more remote pristine areas and so the essence of comparing like with like and
1205 understanding not trying to redefine the problem to make it easier to solve is highly
1206 important there.

1207

1208 **Mr. Moe:** And I'm in agreement with you, but I really think we're going to run into data issues in
1209 finding good data for year-round leases on that type of property. At least by expanding it
1210 to include other residential properties you're going to have a better chance of finding
1211 (inaudible). Your point is well taken. I agree with it.

1212

1213 **Secretary of State Ysursa:** Any other comments from the Department side? Any other Land Board
1214 folks that want to interject anything? Jason?

1215

1216 **Mr. Jason Hancock:** I was wondering about the – just the comparability of looking at rents. I mean,
1217 it seems like in a normal rental-type property if I want to come in and rent something you
1218 know I rent it if it's an apartment or if it's a home or something like that. Maybe I bring
1219 some furniture with me and when I'm done leasing it I take my furniture with me and I walk
1220 away. And you know with these properties we're talking about a land lease where in order
1221 – you know as a leaseholder – in order to have the property be useable for me, I'm going to
1222 go in and spend six figures on putting a house up on this place so – maybe less if I'm just
1223 putting a shack up – but I'm just wondering about how you compare that kind of lease
1224 arrangement with the more normal instruments that you have going on in the market.

1225

1226 **Secretary of State Ysursa:** Any comments on that?

1227

1228 **Mr. Morris:** I have one. If you are leasing a commercial property – we're talking residential –
1229 commercial – you have a ground lease, you go in and build your store. You have to make
1230 that ground lease at least as long as your mortgage (inaudible) so you're making a twenty
1231 to twenty-five year lease (inaudible) in fifty and sixty so that – and those situations do exist
1232 in a private market.
1233
1234 **Mr. Hancock:** Okay. But more on the commercial side –
1235
1236 **Mr. Morris:** More on the commercial side than residential side. Yeah. But we'll be looking for that
1237 kind of thinking in residential as well where you have a ground lease and then go in and
1238 build on it. It's going to be hard.
1239
1240 **(Male Voice):** And there's more and more comps.
1241
1242 **Mr. Corlett:** There are more and more comps and more and more pressure. I mean because of the
1243 1031 exchange issues. You can't sell out of a leasehold per a 1031 – trade property unless
1244 it has thirty years.
1245
1246 **Secretary of State Ysursa:** Any other comments about this? Tom has left and we're both in
1247 agreement that at least it ought to be explored. We don't have anybody – we haven't
1248 talked (inaudible) that issue from our end. I don't think. I don't know if Stan is still working
1249 for us or not.
1250
1251 **Mr. Leroy:** If he's not, we'll pick him up.
1252
1253 **Mr. Morris:** I would just say if this is going to be explored, a decision ought to be made on whether
1254 it is explored on a collaborative basis – whether it's explored by the – whatever party wants
1255 to explore it, so to speak, and –

1256

1257 **Secretary of State Ysursa:** Well, I would hope that we could do it on a collaborative basis and come
1258 up with – because right now we're in an information gathering mode and about anything's
1259 on the table. And if we have time, we'll talk about that – the elephant in the room called
1260 premium rent. But the new methodology of getting comparable rents or, you know, let's
1261 be specific on the charge to the people who would be collaborating and working on that. I
1262 think it would be similar to what you mentioned, Ed, but I think it ought to be collaborative.
1263

1264 Also, you know, this is a – and I always like to say – this is kind of a – I look at it as a
1265 partnership with the state and the lessees. But there is a senior partner, and that's the
1266 state that will decide, and it's the Land Board. So, you know, giving that caveat that it
1267 ought to be collaborative, but we, as a subcommittee, whatever we recommend here will
1268 have to be to the full Board and that's just a political reality. But I think working together,
1269 and some other sort of methodology that will again meet the Board's mandate to get
1270 market rent throughout the duration of the lease under 310a, I'm willing to look at it. I
1271 don't think we shut the door on anything and this is something that I think we ought to
1272 explore collaboratively. And – well, we don't have –
1273

1274 George, what do you think?
1275

1276 **Director Bacon:** Well, it most certainly needs to be looked at closer. I don't disagree with you.
1277

1278 **Secretary of State Ysursa:** We all agree on the charter? The two people – what you just
1279 mentioned, I mean it's in that – that handout. I assume that's – again, you know, my
1280 daughter is a part-owner in Hearthstone up there at McCall. The rents they get when they
1281 charge to private folks I guess we could multiply that by fifty-two and we'd be all right.
1282 That's not even on the lake. That would be pretty lucrative. I'm sure you're not talking
1283 about that simplistic an approach.

1284

1285 **Mr. Morris:** No, Mr. Secretary, it won't be that simplistic.

1286

1287 **Secretary of State Ysursa:** Or expensive.

1288

1289 **Mr. Morris:** If you look at the data items in that sheet to get down to rent attributable to the land,
1290 there's a lot of deducts, you know, everything from personal property to real property
1291 improvements, management expenses and all of those items. But at the same time that
1292 data can provide a framework for what this property, this type of property in this market, is
1293 renting for. That gets you to market rent. We've really never looked at that before.

1294

1295 **Secretary of State Ysursa:** No, I – that's what's intriguing about it. Some way to factor in and I'm
1296 not saying it's the gospel of what it is up there at Payette, but you can call it atrocious or
1297 whatever, but twenty-one thousand square foot sticks in – or front foot – sticks in my head.
1298 While it's been supported by two or three appraisals on market value –

1299

1300 **Mr. Morris:** But I think there – I think it also attests to the fact that market has been somewhat
1301 destabilized by some of these rent increases because it's looked at value. It's never looked
1302 at rent.

1303

1304 **Secretary of State Ysursa:** Well, go ahead.

1305

1306 **Mr. Goodenough:** I was told in law school that the ownership of property is analogous to a bundle
1307 of sticks. I'm sure some of you have heard that. We're talking about unique properties
1308 here. If these properties were dropped on a piece of ground you know twenty miles east of
1309 Payette on a meadow, they wouldn't be, you know, property wouldn't be worth much,
1310 neither the house nor the thing as a whole. The lakes, both of them, are unique. That's
1311 one element here. The lakes are unique. Without the lake nobody would be building these

1312 structures. Another thing that makes it unique is simply the fact that you know we're
1313 talking ten to thirty-five year leases. We're not – we're not talking about somebody who's
1314 going to be gone next month. We're talking about people who have been there for
1315 generation after generation and some of the letters that we got last summer we're talking
1316 about people, you know, having been – grandparents cremated and poured into the lake
1317 and things like that. So we've got not just investment of funds, but investment of some
1318 sentiment. So you know it has elements of a commercial lease due to the length of the
1319 lease. It has elements of a recreational property because it's – that's obviously, you know,
1320 a good part of what it is. It's on a lake. It's not stuck away in the back end of some forest.
1321 And it has residential elements. I'm told all the time that some people live in these
1322 structures year round. So these are – these are, to my mind, unique properties and, you
1323 know, what somebody paid for a month-long lease on Lake Coeur d'Alene or the Spokane
1324 River – hard leasing is particularly relevant to me.
1325
1326 **Secretary of State Ysursa:** Any other comments on that? We can take about a five minute break
1327 and then we'll come back and, discussing in the same vein, we might as well discuss
1328 premium rent a little bit if that's agreeable to folks.
1329
1330 **(Male Voice):** (inaudible)
1331
1332 **Secretary of State Ysursa:** No, because I've seen – talked about comparables is the fact that we all
1333 know we own that and the assignments would be you don't see that in another comparable
1334 area there in rentals that somebody had signed something and gets this value. That's not a
1335 factor in what we're looking at initially.
1336
1337 Right, Ed?
1338

1339 **Mr. Morris:** I can't answer that question without getting into the difference between Payette and
1340 Priest. And there are components of values in some of these leases where you've got non-
1341 conforming uses. And based on appraisal authority, that component of value goes to the
1342 owner of the improvement, not the owner of the land. And that's why a simple extraction
1343 based on cost out of what they sold their leasehold for is not necessarily an accurate or
1344 appropriate way to determine leasehold value or a basis for premium rent. It's a really,
1345 really complex, not just a complex, a really, really complex appraisal problem.
1346
1347 **Secretary of State Ysursa:** Stan.
1348
1349 **Mr. Moe:** Your sale at Priest was unsuccessful, but – this is hearsay – but it's pretty good hearsay.
1350 There were people in the room willing to spend three to four hundred thousand dollars for
1351 the right to rent that vacant lot had you left the rate at two and a half percent. It's the five
1352 percent that scared them off.
1353
1354 **(Male Voice):** That solves it.
1355
1356 **Secretary of State Ysursa:** Would they be scared if it was six? I got it down to five.
1357
1358 (A brief recess was taken.)
1359
1360 **Secretary of State Ysursa:** Okay. We'll get started again. I know that it was ironic we're meeting in
1361 a building that we had a cottage site exchange to get this building, Capitol Park Plaza. The
1362 Director had an idea about an additional thought on – not an original one, but an additional
1363 one – additional thought on the – the thought – looking at rental comparables and
1364 whatever and, George, why don't you throw it out there for –
1365

1366 **Director Bacon:** Yeah, I wish I could draw on the white board. It would make it easier. I'm not
1367 allowed to, and I don't know how to use it, so I'm not (inaudible). And I'm not an attorney,
1368 and I'm not an appraiser, so I'm really hobbled here. All I am is an old forester that kind of
1369 went to seed. I like to think that foresters and loggers and people who work in the
1370 outdoors, ranchers, are common sense, but that's probably why this is never going to work.
1371 But we were talking at break and the first problem with the rent idea, I mean conceptually,
1372 it makes sense to us if there's a big enough sample to look at and factor in the uniqueness
1373 of the properties, or lack of uniqueness if that's the case. Either direction. And I know
1374 appraisers have ways of compensating for that. But the lack of a sample, and in a given
1375 community or area, which we kind of touched on a little bit, was bothering me more than
1376 anything. And that's when I started thinking and that's why you're listening to me now and
1377 we're all in trouble. But what I was thinking is you take a situation like McCall and what
1378 we're endeavoring to do with our cottage sites is long-term leasing. We just got the code
1379 changed to up to thirty-five years. The comparable, if you're trying to establish a rent
1380 market, would be like a similar property, you can correct me when I get it wrong, similar
1381 properties that are rented for similar purposes and time periods. That would be the most
1382 ideal, would it not?
1383
1384 **Mr. Morris:** Certainly it would be if we had that kind of data. I think we're going to get to the point
1385 where we look at all rentals. It would be great if we could find long-term rentals. It's going
1386 to be, I think, almost as good if we look at short-term rentals and look at what those rates
1387 are. But the issue about sample size – if you think sample size is important on rentals, think
1388 for a moment about sample size on sales. How do we determine sample size for appraisal
1389 purposes for evaluation. Are we equally concerned about sample size because you just
1390 heard from your expert we've got almost no sales and the weakness of – from an economic
1391 standpoint the comparative process used in appraisals is you generally use only the last few
1392 sales to measure the market, which only gives you a snapshot in time? At least rentals that
1393 sell is one transaction at one point in time. Rentals generally have a time dimension or a

1394 time rent-per-unit dimension to them that is kind of built into the process, maybe short
1395 term, maybe moderate term, maybe long term. Okay.
1396
1397 **Director Bacon:** Okay. Well, there still may be a big hurdle to overcome because what I'm thinking
1398 is we could probably develop a fairly large sample size in the community using McCall and
1399 Payette Lake, again, just looking at all home rentals recognizing that –
1400
1401 **Mr. Morris:** I would say you guys have somewhat prejudiced yourself about sampling rental
1402 markets by restricting it within your own lease. You understand what I'm saying?
1403
1404 **Director Bacon:** No.
1405
1406 **Mr. Morris:** You prohibit – you limit the ability to sublease for a two-week period of time in your
1407 own lease.
1408
1409 **Director Bacon:** Right. Right. Everything's on the table right now as far as we're concerned. But –
1410 but just conceptually try to get your arms around a whole new paradigm, basically.
1411
1412 **Mr. Morris:** Uh-huh.
1413
1414 **Director Bacon:** Instead of basing rents on property values, like we've been doing, talk about basing
1415 rents on rent value. And I can see us being able to look at rents out in the community.
1416 Single family homes over by the trailer park, over by the high school, wherever. They're
1417 paying so much for rent. They're long-term leases. It's not a time share or that type of
1418 thing. We could probably develop a big pool of that kind of information of what people are
1419 paying for rent and the trick is how do you interpolate that to we need (inaudible). And the
1420 equalizer would be property value. So if out over by the high school I'm paying three
1421 hundred dollars a month for a hundred thousand dollar property, should I be paying three

1422 thousand a month for a million dollar property on the lake. I know that's real simplistic, but
1423 this is a concept. Is it something that has legs or do we go talk about something else.
1424
1425 **Mr. Moe:** One thing is we would try to focus around the lake – lake frontage. In other words, that's
1426 the big issue right now. The – there's another layer in there – it's what's being paid for
1427 monthly rent. You've got improvements and we're trying to get to the land. So that – that
1428 complicates it. It makes it a little bit more difficult. You're talking about a shadow
1429 investment or shadow kind of analysis where (inaudible) appears ten to one. What is it
1430 down here? You know, is it a two or twenty-to-one or what's the ratio? And I think
1431 appraisers can do that if they have enough data. But it's fairly complex.
1432
1433 **Mr. Leroy:** What I heard George say is if at any location you don't have a large enough sample size
1434 of truly comparable rental properties can you – can you bridge that gap by taking, as you
1435 said, we're going to measure anyway, the entirety of the rental market and adjust for
1436 valuation to give you – to give you a proper rental value on the lake if there are no – an
1437 insufficient number of lake comparables. I mean, assuming we're going to have to make
1438 some assumptions. Assuming we're going to have to pick some arbitrary rate in place of
1439 five percent, six percent or two and a half percent, can we adjust in that way and still get
1440 closer to market rent if there's not enough data to give you market rent. I think that's a
1441 great idea.
1442
1443 **Mr. Morris:** And I guess my response is we need to look at that. I'm not so sure that the answer
1444 isn't to expand the sample size for lake frontage property rather than to expand the sample
1445 size to non recreational lake frontage property within the community. But I – because I'm
1446 not so sure that by going to a different property type you don't get the different – a
1447 different answer. But I think those are both legitimate issues that within the research
1448 model that somebody needs to look at or at least arrive at some sort of a reasoned
1449 conclusion.

1450

1451 **Secretary of State Ysursa:** A very controversial issue is leasehold value and premium rent. Less
1452 controversial – I mean there's some other issues that we could discuss rather than that. If
1453 we wanted to get contentious, we can talk about leasehold value. Chuck says let's go for it.
1454 Lempesis. Let me read you – if we're going to talk about it, let's talk about it.
1455

1456 Leasehold value. We all know what we're getting right now. It's ten percent premium rent,
1457 whatever you want to call it. Lessees would prefer that be zero. A previous cottage site
1458 survey by the Land Department, which caused a lot of consternation, said a hundred
1459 percent ought to come to – a reasonable person would say somewhere between a hundred
1460 and ten is where it's going to end up, if still there or whatever you want to say. I have two
1461 definitions here of leasehold value, where it came from. I don't want to make editorial
1462 comments about some comments made. It was not intended by the Land Department to
1463 destroy value of the lessee.
1464

1465 This is out of the December 15th, 1998 minutes of the Land Department, which is actually
1466 the cottage site subcommittee report. The Department – leasehold value results from
1467 economic principle that a buyer will pay a premium to a current leaseholder to assume a
1468 lease when the lease rent is less than market rent. When market rent is reached, leasehold
1469 value should be nearly zero on the market for cabins. This is where I underlined – should
1470 remain active. This principle is reiterated in both appraisals at Priest Lake and Payette Lake.
1471 Here are – here's another view of leasehold value from Mr. Young's comment. The Idaho
1472 Department of Lands has taken a negative view of leasehold value. They have attempted
1473 to erode leasehold value through premium rent making rents beyond market rents contrary
1474 to IDL policy. Leasehold value is positive and should be encouraged. Leasehold value in no
1475 way diminishes return to the state. Just the opposite. Leasehold value has a positive
1476 influence on rent, encourages development in personal properties, which leads to further
1477 enhancement of market conditions. Lessees can justify paying higher rents and making

investments with appreciation of leasehold values. Without leasehold value there's no incentive to make investment and improvements to the property. The property becomes one dimensional use-based rental property. The burden of making these improvements can be obligation of the lessor. Those are the two statements on what leasehold value is.

(Male Voice): (inaudible)

Secretary of State Ysursa: I know the – there was a statement made earlier, and I was kidding, but if you heard that – that Stan Moe made that the rents in Priest Lake were too low because of some leasehold values –

Mr. Moe: Perception.

Secretary of State Ysursa: Perception. Okay. That was my perception, I guess.

Mr. Moe: No, that's the market perception overall.

Secretary of State Ysursa: And, uh – but it is unique. What I could tell looking at certainly the cottage site survey, looking at other states and whatever, and frankly that was put in recognizing you can tell in all the old minutes, whatever, and being around the Board, recognizing this quote, unquote, sweat equity and why is it at two and a half when we had studies out there, quote, unquote, saying it ought to be (inaudible) market value. Again, we can talk about that. But be it Knipe, be it McFadden, be it the gentleman out of Montana, whatever, that we were low at two and a half. And the Board at that time, and it was put in in the early '80s – '81, I think – and to go with the ten percent premium. That has been a point of contention ever since.

1505 The minutes of '98, where I just read this, further up was do away with ten percent
1506 premium rent, was one of the recommendations ten years ago. So here we are. Let's put it
1507 on the table. I said we wouldn't discuss it, but we have a little bit of time so let's discuss it.
1508
1509 I think I fairly presented what the Department thinks about it – that and the leasehold
1510 values. As we know, we think it will operate again to the point where if we are at market,
1511 the leasehold values – the economic principle is that it would be zero. Now the counter to
1512 that –
1513
1514 Jim, why don't you –
1515
1516 And we think that's where we're – that will show we're at market rent. There's no –
1517 there's no advantage – on the land is where the actual rent is for rental use. Period. And
1518 that means we attained our goal of market rent. That's our theory. Not that, as was stated
1519 earlier, means necessarily that my goal was to get to zero leasehold value. It is, but only by
1520 achieving market rent, and that's our take on it. I'd like you guys' take, which I did read.
1521
1522 **Mr. Young:** Thank you, Mr. Secretary. Well, as I had stated in our little paper here, we think that
1523 the premium rent ought to go away and for a couple of reasons. Number one, if we're
1524 talking about market rent, there is no – or at least we don't know of any – precedent out
1525 there in the market under market conditions where there is a premium rent that is like the
1526 one that the Idaho Department of Lands' has instituted on cottage sites. It's just, as I said,
1527 it was an invention of the Department of Land and as far as I can tell maybe – maybe, you
1528 know, if we look at it and study it, maybe there is a question about that. But we certainly
1529 have not seen anything like a premium rent in the market place so if we're truly trying to
1530 get these leases to reflect what would be normal in the market place, then, you know, I
1531 can't see a justification for premium rent.
1532

1533 Now, I think I would defer – I want to again call upon Ed and have him comment on – on
1534 this issue of premium rent. I think that – and Ed can probably speak to this better than I
1535 can – but the idea that we are being charged a percentage of improvements that we – we
1536 may own anyway, I mean, we – we have not diminished the state's value of the land at all
1537 by creating a leasehold value. It doesn't impact the value that the state owns. But there is
1538 value there that the leaseholders have put into these properties and that value is reflected
1539 in the leasehold – in the value of the leasehold. And so to more or less tax us, or take part
1540 of that at the exchange, again, it just is not reflected in the market. And I'll – I'll defer to
1541 you on that because you certainly are the expert.
1542
1543 **Secretary of State Ysursa:** You don't buy our self-fulfilling prophecy that as we approach market
1544 rent those leasehold values get to zero?
1545
1546 **Mr. Young:** No, I don't. I don't think that that is necessarily the case. Although if we look at the
1547 situation at Payette Lake, right now one could argue that there is no leasehold value as it
1548 currently is because you can't sell them anyway. So, you know, all these people that – all
1549 these lessees that have invested in these properties, you know, have seen their values
1550 evaporate, and that's a little disconcerting. And I think it has a long-term negative effect.
1551 So my argument and, you know, my other argument that leasehold value ought to be
1552 encouraged by the Department of Land because it does stimulate the market and it does
1553 encourage people to invest in these properties and it also allows people to justify paying a
1554 higher rent if they can view this property as an investment. There are those factors too,
1555 but just looking at – just looking at, you know, the value and who that value is attributed to
1556 –
1557
1558 **Secretary of State Ysursa:** Well, we almost think it's attributed to our land.
1559
1560 Go ahead.

1561

1562 Ed.

1563

1564 **Mr. Morris:** Well –

1565

1566 **Secretary of State Ysursa:** Point, counter point.

1567

1568 **Mr. Morris:** This is – before I launch in to my premium rent discourse, I wish to emphasize that we
1569 numerous times in this discussion have raised the issue about – and this will get to it also –
1570 about property rights. And, you know, is it attributable to your land or is it attributable to
1571 their improvements? And those are, for some of these reasons, very complex and very
1572 important issues. This – the definition that you read on leasehold value is a typical
1573 commercial definition that arises from the situation where the landlord owns all the
1574 property. And what is simplistic and almost misleading about that – particularly as it was
1575 used by prior Department of Lands' staff members, who did not have a good grounding in
1576 appraisal principles and methodology, is they took that literally because they didn't
1577 understand that all these cottage site lessees owned cottages and owned improvements
1578 and they owned the utility, sewer hookups and water hookups and all kinds of things –
1579 elements that made physical economic components of value to the leasehold.

1580

1581 So if you drove their leasehold value to zero, you confiscated their property because they
1582 own a building and that's what's not reflected in that definition because most landlord-
1583 tenant relationships are not a situation where the tenant owns the building improvements.
1584 So in order to get to any type of a realistic leasehold analysis, you've got to do a very
1585 complicated analysis of what are the building improvements worth out of the sales price in
1586 order to make an abstraction, or an allocation, of whether there is and how much leasehold
1587 value is there. That's where – that's the difficulty where the rubber meets the road.

1588

It's my recollection what's been done in the past is to try to use assessor values, or things like that, which are cost-based, and they used costs that are – would not be higher for a urban typical in-town lot versus an out-of-town lakefront recreational count. And so the whole issue of valuation and expediency to measure it was never accurate. It was set low. I don't think it's ever been litigated, but those are some of the background issues that you're going to have if you change it – if you change it by much – is who owns what, how do you measure it and how do you measure it fairly and accurately because if you really try to drive the leasehold value to zero, you've just confiscated everybody's cottages.

Secretary of State Ysursa: Yes, Stan.

Mr. Moe: Counterpoint. And this is in a friendly way. I think this is – the terminology is incorrect. We're not talking about a leasehold value on the property. You're only addressing the leasehold value in the land. And the method of estimating that, or coming to that value, has been for an appraiser to go out, and we've entered the sale, they estimate the value of the improvements. That's deducted from the sales price and what's left over then is what we're referring to as a leasehold value in the land only.

Mr. Morris: Correct.

Mr. Moe: So Ed's right. If you drive the whole leasehold value to zero, you've taken all the improvements so you have to isolate the land first and that's not easy to do. And that brings you back to the method of evaluation. Trying to get a rate still requires that we do an appraisal to put market value on the lots. That's not going to – it's only going to continue that difficult process of having to do appraisals every year or every five years. If there was some way to tie the premium rent, let's call it that, leasehold value in the land to the lease rate, it would eliminate that step. So that's not going to be done by a market analysis that I can see.

1617

1618 You might have to make an administrative decision is that we're going to value the
1619 leasehold interest in the land by deducting the cost of all the improvements.
1620 Improvements to include roads put in, a factor for the profit for putting the roads in, all
1621 these other issues that have gone into making that a habitable building site for the building
1622 lot. What's left over then is truly the pure land value. It's not easy to estimate, but it's
1623 probably easier than getting market value of vacant land when there are no sales. You can
1624 do it through a cost approach. You can even factor in a profit factor.
1625

1626 When that excess or premium rent value exceeds a certain percentage of, well, let's say
1627 you got the last four (inaudible) on the lot sales were seventy-five, eighty thousand for bare
1628 lots up there. This time none sold, but there's good reason to believe they would have.
1629 What's a reasonable level for leaving the leasehold interest in the land allowing that to be –
1630 some of it to go to the lessees. Maybe that's fifty thousand dollars. Maybe it's twenty. I
1631 don't know, but at some point you're going to get down to a level where you can say, yeah,
1632 that seems fair. We don't need to raise our rents anymore. You can raise rents gradually
1633 to get to that point, but it's going to be a long process.
1634

1635 **Secretary of State Ysursa:** Jim.
1636

1637 **Mr. Young:** Mr. Secretary, it seems like, again, this issue comes back to determining market rent.
1638 And, if we do a good job, the appraisers do a good job, in coming up with market rent and
1639 terms, lease terms, that would be typical and normal in the market place, then we've done
1640 our job. The idea of premium rent, again, it just is – it's foreign to the market place. It' just
1641 not – it's just not done out there. And so – I mean truly if we're trying to get to market, and
1642 it sounds like we are, that ought to be our major concern and forget about this whole
1643 premium rent.
1644

1645 **Secretary of State Ysursa:** Premium rent has been pretty good up until –

1646

1647 Craig, you know – you have these figures on –

1648

1649 **Mr. Craig Thompson:** Yeah, I can – I can talk about (inaudible) –

1650

1651 **Secretary of State Ysursa:** (inaudible) things were high (inaudible)

1652

1653 **Mr. Thompson:** Priest Lake – it has been about twelve leasehold sales over the course of the last
1654 twelve months, and the average leasehold sale was $304,000, I believe. So we got about –
1655 what would that be - $360,000 in premium rent.

1656

1657 **Secretary of State Ysursa:** We're at thirty thousand in sales. There have been twelve sales at Priest
1658 Lake?

1659

1660 **Mr. Thompson:** Twelve leasehold sales, yeah. And they ranged from about a hundred and sixty
1661 thousand to, I think the highest was six hundred and fifty thousand for the huge – it was a
1662 huge (inaudible).

1663

1664 **Secretary of State Ysursa:** How many sales at Payette Lake?

1665

1666 **Mr. Thompson:** Zero.

1667

1668 **Secretary of State Ysursa:** I was going to say –

1669

1670 **Mr. Thompson:** There has been some silence. It's been – it was one sale that was started before all
1671 this started, but it was – it was somebody acquiring it from an old man who just wanted to
1672 get rid of it, and it wasn't very much.

1673

1674 **Mr. Leroy:** How long ago was that?

1675

1676 **Mr. Thompson:** It was completed – it was – it was Mr. Hoyle's.

1677

1678 **Mr. Leroy:** Yeah.

1679

1680 **Mr. Young:** Was it lakefront?

1681

1682 **Mr. Thompson:** (inaudible)

1683

1684 **Mr. Young:** Okay. I have a question. Just a question.

1685

1686 **Secretary of State Ysursa:** Go ahead.

1687

1688 **Mr. Young:** You mentioned –

1689

1690 **Secretary of State Ysursa:** (inaudible)

1691

1692 **Mr. Young:** You mentioned in your opening remarks, Mr. Secretary, that premium rent was
1693 designed to apply when the rent is less than the market rent. Okay. So what we're trying
1694 to get at is market rent. So if we're getting – if our study comes back and we're able to
1695 achieve market rent, doesn't the premium rent go away?

1696

1697 **Secretary of State Ysursa:** Yes. (inaudible) It's a self-fulfilling prophecy like I said. If – if we really
1698 are at market rent, we shouldn't be seeing that leasehold value.

1699

1700 **(Male Voice):** (inaudible)

1701

1702 **Secretary of State Ysursa:** That's why – that was our point that – to leave it in there. And if – to
1703 really get down to brass tacks – why that was put in was to justify 2.5, which was low from
1704 every other study that was done. And that's why it was put in. That's the – one of reasons
1705 it was put in and – the two – you know, even reading from the minutes, 2.5 percent rate
1706 recognized and takes into consideration the lessee sweat equity and lessee improvement.
1707 Then we, by the way, added the ten percent premium to do that.
1708

1709 **(Male Voice):** So theoretically if the percentage –
1710

1711 **Secretary of State Ysursa:** Theoretically if we're correct and we get to market rent, this goes away.
1712

1713 **(Male Voice):** But it – in reality if the market rent comes back, especially at Priest if we're – if it's
1714 true that we're not paying enough and it needs to be indexed up, right, then we have to – if
1715 we have to index, increase the rent more radically every year to get up to market rent then
1716 the leasehold value of this premium rent would disappear over time, is that correct?
1717

1718 **Secretary of State Ysursa:** Yes. We lose the $300,000 and does it get offset by our (inaudible) –
1719 One – the one – the only one thing that bothered me in our minutes of December 15th,
1720 1998, because I underlined it, the concept is still there. When market rent is reached,
1721 leasehold value should be – should be nearly zero and the market for cabins should remain
1722 active. I don't think it's remained very active at Payette Lake. But – have we reached
1723 market rent or not?
1724

1725 Yes.
1726

1727 **Mr. Leroy:** Well, Ben, Dave Leroy. I think market rent, however, and premium rent and sale price
1728 and sales are all tied together, and I think what's happened over the years is that with the

1729 buyer and seller knowing that premium rent is at ten percent, they were able to still strike
1730 some deals and make some sales when the lease conditions were predictable and the rents
1731 were predictable. But if I think – if you – and what I believe effectively happened was the
1732 sellers added that ten percent to their price and everybody could kind of predict that's
1733 what would be required to get into a lease, and they could also predict that that's what
1734 would be required to get out of a lease. I think if you – if you announce a radical increase in
1735 that that will have the net effect of chilling the market, killing sales and destabilizing it on
1736 that factor alone. It's not just such a nice-nice as splitting theoretical profits.
1737
1738 I think the premium rent gets added up front to the sales price and the buyer has to make
1739 an estimate of what the relation with the state is going to be if and when they attempt to
1740 turn that lease over to somebody else. So if a hundred percent premium rent was a bad
1741 idea, I would argue that fifty percent premium rent is almost as much a bad idea.
1742
1743 My clients – as you heard Jim say a couple of times – are eager to have premium rent go
1744 away. I've advised them in my opinion that it's politically probably not going to happen. So
1745 I would argue that if you can't make it go away, as Payette Lake would like, let's at least
1746 keep it at ten percent where buyers and sellers are used to factoring that in as a feature of
1747 the sale so that you don't increase it to the point where it once again kills sales and
1748 eliminates either premium rent or any other alienation of the property for our
1749 leaseholders.
1750
1751 **Secretary of State Ysursa:** Any other comments.
1752
1753 Bud.
1754
1755 **Mr. Belles:** I have one. Yes. It's Bud Belles. You know, I've done some Googling on things like those
1756 terms that we've been using – leasehold value – and you find terms and descriptions of

1757 them similar to what you have, Mr. Secretary, and you Google premium rent practically you
1758 get no hits. Or it's just – there are none of them out there. You know, and I keep thinking
1759 about the auctions. You know, you were thinking the lots should bring in like three
1760 hundred thousand to get that lot and I looked at that as leasehold value. So you're getting
1761 the three hundred thousand of leasehold value on those lots that are auctioned off. The
1762 existing leases that we have, if I had gone in and bought one of those and put in roads,
1763 sewer, electricity, all those utilities, and then said oops, I can't afford to build my cabin, a
1764 death in the family, whatever happens, and then go to sell that, I put that money in, plus
1765 the three hundred thousand, and I sell it say for three hundred thousand or four hundred
1766 thousand, you know, you get forty thousand of that if it sold for four hundred thousand. If I
1767 had to sell it for three hundred thousand, I just lost a whole bunch of money.
1768
1769 **Mr. Lempesis:** Or if it was fifty percent –
1770
1771 **Mr. Belles:** Well, if it was fifty percent, it was (inaudible) – a lot of money. So I think there's an
1772 argument that says leasehold value should be to the lessor – lessee. On the other side of
1773 that (inaudible), if we could reverse our roles and you were to come in and buy all of our
1774 cabins and then just rent them back to us, what could you rent those for.
1775
1776 **Secretary of State Ysursa:** Market rent.
1777
1778 Yes, Jim.
1779
1780 **Mr. Young:** Mr. Secretary, one other factor I think that needs consideration on all of those lessees
1781 that have invested large amounts of money into these properties and, you know, recently
1782 the people that have come into them and purchased those, which the state has benefited
1783 from and participated in at the ten percent level – to change the rules on them mid stream

1784 would be devastating to those – to those lessees – those recent lessees. And I know we
1785 have one of them here in the room, and maybe –
1786
1787 Loren, maybe you could speak to that.
1788
1789 **Ms. Loren Macey:** I mean, the market – the premium rent that was paid on the property that I
1790 bought in 2005 was based on the Valley County Assessor's values, which the building was, I
1791 think, valued at about fifty to sixty thousand dollars, and we paid close to eight hundred
1792 thousand dollars for that lease. If you propose fifty percent and I have to turn around and
1793 sell this, which actually it – we may still have to – we've been just waiting for this to settle
1794 out – there would be a huge financial burden, I mean, it would. And – and it would be
1795 more – it would be – for the people who have come in and bought these things in the last
1796 five years. It's going to be incredible if something like that is done. It's going to be
1797 devastating.
1798
1799 So I just want to make sure that you understand the ramifications for some people and
1800 what they feel that they might have to do to settle that out. It would be devastating, and I
1801 think that it would – I think that at Payette Lake if you raise the premium rent above the
1802 ten percent you will once again stifle the sales, stifle the free market, stifle the sales of
1803 leasehold property because people either will be, you know, motivated not to sell or
1804 people will say I can't sell and what do we do now. Walk away from it?
1805
1806 **Mr. Corlett:** Mr. Secretary, I just wanted to comment – the – when this is all said and done, I think
1807 the goal for the state and all the lessees should be to have a lease that we all agree on. We
1808 may not all be happy about it, but we might all agree on it and that will enhance your
1809 ability, the state's ability, on future lot sales.
1810

1811 You know well what happened at the auction – it didn't work so hot. Well, you're best
1812 agents for sales are your existing lessees so if they can believe in a lease, they have
1813 confidence in the state that it's going to – that it's fair and equitable, and then you're going
1814 to be able to sell your lots. There's a lot of opportunity to increase revenue to the state at
1815 Priest Lake at least. There's more lake front property. There's a ton of secondary property,
1816 if you choose to do that. So I wouldn't worry so much about – or I would – could be very
1817 much concerned that we arrive at a first class lease now that everybody can get behind.
1818 And for the state's – looking at it from the state's viewpoint, they'll be a lot better off
1819 selling lots later on. It's – you know, it's a pain now.
1820
1821 **Secretary of State Ysursa:** Selling the right to lease or selling the lots?
1822
1823 **Mr. Corlett:** Yeah, selling the right to lease. Excuse me.
1824
1825 **Secretary of State Ysursa:** Okay.
1826
1827 **(Male voice):** Yes (inaudible).
1828
1829 **Secretary of State Ysursa:** That's another issue.
1830
1831 **(Male Voice):** Yeah.
1832
1833 **Secretary of State Ysursa:** George, any comments from the Department on premium rent?
1834
1835 **Director Bacon:** Yeah, I think we're kind of playing wait and see. I mean, I think it's already been
1836 identified here that we think the first step is let's determine what the base rent is going to
1837 be and see how all these other things play in. Now maybe that can't be done. Maybe
1838 you've got to look at it all at once, but it certainly gets a lot more complicated that way. I

1839 guess I was hoping that if all the parties came to agreement on a phased rent, premium
1840 rent and all those other things would kind of naturally solve themselves, and it wouldn't be
1841 as much of an issue. So I think that's where we need to continue to concentrate and, you
1842 know, we may never get agreement on what that base rent might be, but certainly we can
1843 get everybody's input and make the best decision possible.
1844
1845 **Secretary of State Ysursa:** Well, they have to know – I mean – the Department's monitoring
1846 assignments and checking leasehold value to see where we go and whatever, but we –
1847 when it comes time to sign on the dotted line for a thirty-five year lease, everybody's going
1848 to want to know what up front premium rent is and everything else. We can't – frankly
1849 that was a red herring issue in those auctions at Priest Lake. Premium rent was – was in
1850 (inaudible). It was ten percent or latest Land Board policy or rule that is outdated. That
1851 was not a good lease and was going to cause some problems later. Land Board policy in the
1852 other one was ten percent and is ten percent right now. But more than a few people
1853 inquired about what was premium rent going to be on the new lease because it wasn't very
1854 clear. That didn't help our situation anyways and I don't know if the lessees up there
1855 pounced on that and had this paranoia passed around but they did.
1856
1857 **(Male voices)**: (inaudible)
1858
1859 **Secretary of State Ysursa:** Any other comments? Land Board folks? Clive, any comments? Bonnie?
1860
1861 There's no resolution. We know well your position. Our position is – it's retained and I for
1862 one would say it's not going to – it's not going to be a hundred percent, let's face it. We'll
1863 see. I haven't talked to Tom specifically about that or – or other Board members. They,
1864 like George, they'd like to see it.
1865

1866 If our principle is correct, we'd like to see it kind of phase away that we really ought to
1867 come to this magical formula that we actually are at market rent. And that's all we're
1868 entitled to. But we also get a little leery when we back out improvements and let's say you
1869 get some reasonable prices on improvements that folks are – if I could reinvent the wheel, I
1870 would have had a huge written disclaimer on every lease that says don't consider this
1871 investment property. You can't do that. And dammit it still should not be considered
1872 investment property, but that horse is out and has been running for seventy years.
1873 Because it shouldn't be. Should be the life of the lease and not to make – not to make a
1874 profit on the state's land. That profit ought to go to the endowment and that's our view on
1875 that so – I don't think we're going to have a resolution on that. We could – it will be all but
1876 three out of five members of the Board think what premium rent ought to be. Right now
1877 it's not going away. But what amount I – we'll see.
1878
1879 Questions from Mike.
1880
1881 **Mr. Mike Fery:** Secretary Ysursa, Mike Fery. A question actually for each of the appraisers.
1882
1883 First of all, how many land leases, excluding federal and state, have you appraised or used
1884 as comps over your appraisal years – as a qualifier. Just – uh –
1885
1886 **Mr. Moe:** I've been appraising for a long time. Thirty or forty.
1887
1888 **Mr. Fery:** Thirty or forty.
1889
1890 **Mr. Morris:** It will be the same range.
1891
1892 **Mr. Moe:** Are you talking about long-term land use? What kind of land use?
1893

1894 **Mr. Fery:** Any kind of land lease.

1895

1896 **Mr. Moe:** Any kind of land lease.

1897

1898 **Mr. Morris:** Agricultural leases – I just did a job down at Fort Hall that I think we had hundreds of
1899 land leases involved in that one project. But, you know, I think you're – if you're looking for
1900 long-term land leases, they're much less and particularly residential property long-term –
1901 much, much, much less common. But within the commercial realm and the agricultural
1902 realm, they're very, very common.

1903

1904 **Mr. Moe:** Just a follow up, if I can. You could also maybe Google the Irvine Company and find out
1905 what went on in Southern California on long-term land leases if you want an interesting
1906 case study.

1907

1908 **Mr. Fery:** It's interesting because I actually have a couple of – not the Irvine Company, but a
1909 number in the Palm Springs area on long-term land leases, one of which is my folks have
1910 one that they just renegotiated. And I've got one in – it's four, five years old for Nampa,
1911 Idaho, that's on a land lease. And I've negotiated eleven with between the City of Boise,
1912 the Port of Portland, the J. R. Simplot Company, which is actually in McCall as of a year and
1913 a half ago, and what I guess my question to you after that comment is in all those leases
1914 you looked at how many of them had premium rent in those leases – what percentage.

1915

1916 **Mr. Moe:** (inaudible) In a commercial marketplace there is no such – no such thing – no such
1917 concept.

1918

1919 **Mr. Fery:** That's what I found in mine except I was just curious on your leases.

1920

1921 **Mr. Moe:** No. But the theory is if you've got market rent there would be no leasehold value
1922 created. The state has created this by having lower rents. That's the theory. And in the
1923 conventional open market, there's no such thing.
1924
1925 **Secretary of State Ysursa:** Any other comments about premium rent? Okay.
1926
1927 Another issue that has been brought up, and I'd like some of the Board or the Department's
1928 input too, is possible inclusion, purchase options, exchange options – where are we on that,
1929 whatever. Purchase of property is public auction by Constitution. Everybody knows that.
1930 That's the – not the stickler in the process, but lots go up for sale there any where, Payette,
1931 Priest, any endowment land. We have to by Constitution have a public auction and the
1932 wealthy person from out of state can win every time. And that led to – frankly led to
1933 58-310a, conflicts on leases.
1934
1935 So anyway, we have – obviously in Payette we have a disjointed ownership pattern,
1936 certainly some lake fronts, secondary and then in between them private lots, whatever.
1937 There have been sales – some not successful, some successful. Whatever you want to say.
1938 At Priest Lake we have not as a Board had any sales up there as you well know and have not
1939 really approached that as to changing that policy at all right now. But as we look down the
1940 future, and I think this is all we're looking at here and then I'll bring up exchange, too, we
1941 have exchanged in Payette. Should we continue to exchange or not – I think all this – I've
1942 talked with George about it and with Kathy some. We have an asset management policy.
1943 Does it fit into that. We have folks looking at it. Should we change our makeup of
1944 properties, whatever. I – I'm all in favor of exchanges myself continuing if it fits the
1945 mandate and the asset management plan and our portfolio. I don't think they ought to be
1946 taken off the table. I do not think the Board has given very clear direction to the
1947 Department on that except we did approve the asset management plan, and I think we
1948 ought to proceed under that. I don't know.

1949

1950 Kathy, do you have any observations on exchanges and sales and all that.

1951

1952 **Ms. Kathy Opp:** Sure. Thanks, Ben.

1953

1954 One of the things that we need to get through, I think, is determine the status of this asset
1955 type. Residential leasing is a valuable component to the portfolio. We make no bones
1956 about it in the asset plan. We're heavily dependent on timber markets. It's over eighty
1957 percent of our return and the Board was very specific about needing to continue to
1958 augment diversity in the portfolio. And so when we look at options, obviously we also
1959 stated in the asset management plan we'd like to offer more properties for lease in the
1960 cottage/residential arena. We do have some that are already platted up on Priest Lake.
1961 We have some opportunities elsewhere as well. So it's something that we're looking at.

1962

1963 Obviously it would have to – any exchange that we entertained I think we need to solidify
1964 where this asset type is going long term so that we get a fair comparison between
1965 properties that would be exchanged. We'd also like to grow other asset types that help
1966 diversification – commercial properties, agricultural lands, things like that. So that's kind of
1967 where we're going. We have a process to have that come before the Department and the
1968 Board and basically we look at return on asset. And a big component of that is not only the
1969 cash rent but the value appreciation in the asset so we don't – do look at both sides of that
1970 equation in terms of the return on asset for any asset classification. But fundamentally the
1971 Board and the Department are charged with providing a revenue stream so it can't all be in
1972 value appreciation. So that's how we will be approaching the examination of those
1973 offerings in the future. And, as Ben said, it's – you know, we're not excluding it. We'd like
1974 to get a holistic plan for this asset with regards to the total portfolio and where we may go
1975 with the infrastructure, things that we need to do to make these properties even more
1976 marketable. I think all of that is on the table to be developed (inaudible) future strategy.

1977

1978 **Secretary of State Ysursa:** Comments from the Association on what you just heard about what our
1979 –
1980

1981 **Mr. Young**: Well, yes. Thank you, Mr. Secretary.
1982

1983 Just – I think it would be very helpful if there was clear definition of what is acceptable to
1984 the Department of Land when considering an exchange and if we are able to bring a good
1985 solid property to the table that if we have – if we have a defined set of criteria then we'll
1986 know what to bring to the table if – that would be very helpful to us. There are a number
1987 of lessees that would be very interested in exchanging out so – I know that we have one of
1988 those here in the room – so we would be very receptive to any kind of guidelines that
1989 would define what that criteria would be.
1990

1991 **Secretary of State Ysursa:** I think our asset management plan has a parcel nomination process or
1992 something. Kathy, who helped, if not wrote it all, helped write it all – okay.
1993

1994 Go ahead (inaudible).
1995

1996 **Ms. Opp:** A lot of those guidelines are in that plan in terms of the distribution between value
1997 appreciation and revenue streams that we're looking at. You know, that ideal distribution
1998 on each asset type and the peer return ranges that we'd be expecting to look at and also
1999 the concept of we can't get there just yet with the Board, but what should the overall
2000 diversification of the portfolio, including the financial assets, look like and you have
2001 something that the Endowment Fund Investment Board is still completing their
2002 components to this plan. Once that is done, then we will have an opportunity to work with
2003 the Board to define that asset mix and how we move towards that to alleviate some of that
2004 dependence on timber and other asset types and –

2005

2006 **Mr. Young:** So it sounds like it is coming up in the next like –

2007

2008 **Ms. Opp:** The asset management plan related to lands is on our web site and the peer range of
2009 returns for asset types related to land is in that document and how this would – a return on
2010 asset should play out and other things that will work out for performance. So that is all
2011 articulated in that document.

2012

2013 **Secretary of State Ysursa:** George.

2014

2015 **Director Bacon:** Just – you know, from my perspective so that we're clear here, we have different
2016 land asset types. We have forest land, range land. We have ag land. We have
2017 residential/cottage sites. We have commercial property. We want to calculate and make
2018 some recommendations to the Board of how much of each is the right mix to have a fairly
2019 diverse state portfolio so when we do that modeling it may tell us we need more cottage
2020 sites, not fewer. So why get rid of any. And until we know that we can't make those kind
2021 of decisions, and we get into a chicken-and-egg thing here because you can't really
2022 calculate that value until you know what the lease is going to be bringing in over a thirty-
2023 five year period, or wherever we go, so we're in a do-loop here on that whole issue. So –

2024

2025 **Mr. Young:** So, Mr. Director, Ben, if I'm hearing you right then this issue is – as far as exchanges or
2026 sale, probably exchanges, will not be resolved until we get this lease resolved. Is that kind
2027 of fair to say?

2028

2029 **Director Bacon:** That's my anticipation. We're kind of in limbo with – with – with it (inaudible). We
2030 may be making a big mistake for the endowments to divest of some of these properties and
2031 then individual properties will have to be looked at and there'll be criteria.

2032

2033 **Secretary of State Ysursa:** Mr. Fery.

2034

2035 **Mr. Fery:** If I recall, the percentage of assets in class, commercial real estate versus the cottage
2036 sites, is about three percent each respectively, give or take. So it's pretty close. So if you
2037 did one cottage site exchange, it wouldn't probably significantly change the endowment, or
2038 if you did ten cottage site exchanges, it wouldn't significantly change your number relative
2039 to a risk exposure. So my thought is I'm hearing one thing relative to Board direction, or at
2040 least your thought is that you're willing to look at them on a case-by-case basis if they make
2041 sense. And also I'm hearing I understand you've got – your policy is until we analyze
2042 everything and figure everything out we're not going to do cottage site exchanges. I guess
2043 I'm just curious to see where we're at.

2044

2045 **Secretary of State Ysursa:** Where we're at on exchanges? Where I'm at is that I think they're on
2046 the table and can be done. Again, the Department and, you know, we've looked and
2047 looked at yours and had discussions about it with (inaudible). It's never really – it kind of
2048 got pushed on the back burner as we got into these other issues, and I've – I for one – I
2049 don't know if it's good or if it's bad for the endowment. I think we need to have a look at it,
2050 but I'm not – at one point in time we had stopped it – the exchange list – and I'm not saying
2051 we go back to it. To do that there was a – really a directive. The Board at that time
2052 stopped them, unless they were within a football field of the Capitol building. If they were
2053 outside of that, we had kind of an agreement we weren't going after them. And frankly
2054 some of our properties we have now – this is a nice one – whatever, but my personal view
2055 is if an exchange makes sense for the endowment, we ought to proceed with it. And that's
2056 where I am. (inaudible) the sale frame is over here. And, you know, the aspect of previous
2057 citizens' commissions saying we ought to get – if it was for the headache factor, we'd sell
2058 them all, but that's not our – you know, you people are great people, but I don't necessarily
2059 like to come talk to you if we (inaudible) or whatever about the headache factor we'd get
2060 rid of the – we'd start selling them periodically – get out of the business. Let Larry Johnson

2061 and the endowment fund invest them for us. But I'm having trouble as an old Basque guy
2062 here looking at how fast recreational property around these lakes are appreciating versus
2063 our assets. And it's not even close. So – and we're not making any more lakes, and I just
2064 don't see the price of that – of the land going down. Yeah, we've taken hits. Valley County
2065 – I don't know what the assessor is doing this year, but Tamarack and other things there –
2066 Valley County's in trouble for a while but it'll come back. And, you know, do we exchange?
2067 Do we do this? We need a little more long-term direction on it, but I for one, and
2068 Department staff may shoot me, but I think we ought to continue forward on exchanges
2069 that make sense obviously for the endowment. That shouldn't be off the table. That's
2070 where I am.
2071
2072 Comments. Any others. Sale thing – your folks ever bring up sale to you and they thought
2073 he had? They're ready to go to public auction? No, I don't think they are.
2074
2075 **(Male Voice):** Probably not.
2076
2077 **Secretary of State Ysursa:** (tape change) We could have sold two lots at Priest Lake since we and
2078 the federal side and the state side – there's a scarcity of fee lots at Priest Lake and that with
2079 the pretty good market. Again looking at the whole picture, what should we be doing and
2080 then a comprehensive plan with Bonner County and all these other questions are working
2081 for us, but are we really going to destroy the view shed, blah, blah, blah. A lot of questions
2082 that we have on our table beyond necessarily the bang for the buck, but that's what we
2083 have to look at and – so anyway.
2084
2085 Any other questions on the – there's some others. I think we've talked about it. I think a
2086 key point if we do come up with some formula for market rent, what constantly comes up
2087 and has come up in some of the comments, is do we put a cap on annual increases or put in
2088 a cap. We obviously do not have a cap on now as Valley County and others will certainly

2089 attest to and Payette Lake, both. I have trouble reconciling the phrase ensuring that the
2090 leases receive market rent throughout the duration of the lease. That's right out of 310a.
2091 And if we have rapidly escalating values or – which we did have – how do we – I agree –
2092 when you look at a long-term lease you need predictability, but how do you put a cap on
2093 that meets our mandate to get market rent throughout the duration of the lease, and that's
2094 a struggle.
2095
2096 Yes, sir. Mr. Morris.
2097
2098 **Mr. Morris:** Thank you, Mr. Secretary. You make an excellent point, but I just wanted to point out
2099 and highlight what you've been looking at in value you have not – a value certainly can
2100 change. It can change rapidly. At some times those changes can almost be explosive,
2101 particularly when you have a market situation where there's very little private land for
2102 private transactions in the market place, which is the situation you've got certainly at Priest
2103 between the federal ownership and the state ownership. It's my recollection that around
2104 ninety percent of the frontage is in state and federal hands, but you never tracked what the
2105 trend line is for rent. You only tracked what those trends are for fee sale prices.
2106
2107 **Mr. Corlett:** There's one thing about cap rates. I think Stan and Ed would agree with me in
2108 capitalization rates are – in other words, the net income divided by the sales price of a
2109 particular property. That's the link into income versus value. And we watched cap rates
2110 drop from maybe ten percent ten years ago to six percent today for investment grade
2111 property. What the two and a half percent is is more or less a cap rate. So what we may
2112 see as going up in value still is driving the return down, and the cap rate down, and that's I
2113 think I've just kind of restated what Ed just said then. That's what's changed. The rent has
2114 remained relatively constant.
2115
2116 **Secretary of State Ysursa:** Jim is probably (inaudible).

2117

2118 **Mr. Young:** Yes, Mr. Secretary. I totally agree that it appears, and I'm certainly not an expert, but it
2119 appears as if from the data that rents, market rents are much more stable than land values,
2120 and I think that was the point I was trying to make on this is that you get these wild swings
2121 in valuation, but overall rents appear to stay fairly stable.
2122

2123 **Secretary of State Ysursa:** Yes, sir.
2124

2125 **Mr. Young:** How will our experts be working together? If we're resigned to the fact that there may
2126 be a better mouse trap out there if we –
2127

2128 **Secretary of State Ysursa:** We haven't formalized or we need to get together with George and do
2129 that before we leave here.
2130

2131 **Mr. Leroy:** Okay. Great.
2132

2133 **Secretary of State Ysursa:** And get that going.
2134

2135 **(Male Voices):** (inaudible)
2136

2137 **Secretary of State Ysursa:** I gave you that thing a month ago. Okay. Let me see. What do I have
2138 here. I didn't hear a lot about it. If we get to market rent, you guys are going to live with it,
2139 right, because you don't think it's going to go up as fast as the values of the property.
2140

2141 **Mr. Young:** Don't know. I –
2142

2143 **Secretary of State Ysursa:** Right answer. I don't either.
2144

2145 **Mr. Young:** I think that's why we've got to engage the experts to look at it.

2146

2147 **Mr. Leroy:** Ben, has there been any talk by Board members or with staff about '09 rents at this
2148 point or are we – as you point out, we're on a relatively short track on that and we – if
2149 you've got some action or thinking – you want some action or thinking from us – what
2150 should we contemplate.

2151

2152 **Secretary of State Ysursa:** Whether we wanted it or not we'd probably get your action or thinking –

2153

2154 **Mr. Leroy:** True.

2155

2156 **Secretary of State Ysursa:** I appreciate comments from the associations about what we ought to do
2157 with the 2009 rent. We're going to have to make that decision in June at the latest.

2158

2159 Right, George?

2160

2161 **Director Bacon:** Yes, sir.

2162

2163 **Secretary of State Ysursa:** And I'm very curious what our assessor's doing – going to do in Valley
2164 County and just look at those and Craig's going to inform me as soon as he knows what
2165 they're up to there. And –

2166

2167 **Mr. Thompson:** I'll take some boxes of chocolate –

2168

2169 **Secretary of State Ysursa:** And I don't know if we've had enough time to engage Stan again to get
2170 going on the index at Priest, but we haven't really – and frankly I'd start looking at all this
2171 and the session just ended and whatever you start looking at trying to get this going and
2172 then I say, you know, that as I stated earlier here that six-month notice provision in the

2173 lease for any increase is fast approaching so we haven't had a lot of discussion on it yet, but
2174 we will and get it going. We're very cognizant of some happenings in Valley County on one
2175 of our other lessees who's south of McCall and we know what's happening around there.
2176
2177 **Mr. Leroy:** We'll get you a memo on the litigation to the extent that's (inaudible).
2178
2179 **Secretary of State Ysursa:** Yeah. And any comments. I have an idea what you might think the rent
2180 increase ought to be but – at Payette and, of course, Priest. But we'll look at it. The Board
2181 will have to decide in June – before July – so we meet the six-month notice requirement.
2182 But any input is appreciated. Okay. Anything else?
2183
2184 George, for the good of the order?
2185
2186 **Director Bacon:** Well, a couple of comments for closing.
2187
2188 **Secretary of State Ysursa:** Sure.
2189
2190 Any other comments. I mean we do need a lot – stay around – we need to formalize
2191 something that's come out of this is to have a collaborative effort to come to some other
2192 way to approach market rent. And again I note Superintendent Luna and myself are both
2193 very – we're open to that and want that to occur and so how we put that together I think
2194 we – about everybody needs to stay for that to get that going and then come set up
2195 another meeting and come back with some – mainly with that topic on there. If that can
2196 get halfway resolved, that would be a major, major step. If we – if we think there's a better
2197 mouse trap and the Board and with the other staff members of the Board relaying it to
2198 their principals to know if we're headed in the right direction or if we're going to hold up
2199 and go two and a half, three and a half, five, whatever we're going to do on the other end.
2200

2201 So what was the other question you had, David. That was it?

2202

2203 **Mr. Leroy:** That was it.

2204

2205 **Secretary of State Ysursa:** About 2009? We'll find out in June.

2206

2207 **Mr. Leroy:** We'll give you some thoughts.

2208

2209 **Secretary of State Ysursa:** I'm sure you will. Anything else for the good of the order?

2210

2211 Kathy, anything you want to interject?

2212

2213 Any other Board member's staff member? Since I started out lying saying that Tom was in
2214 Pittsburg and he shows up? Is he back? He missed the plane. He missed the plane.

2215

2216 **Mr. Leroy:** Thanks for your leadership and hospitality, Ben.

2217

2218 **Secretary of State Ysursa:** Well, thank you and that – I think we can get there. It's not rocket
2219 science. Sometimes I wonder if it is. And, oh, appeal valuation process. We have that –
2220 that was an issue we have in our lease. The new lease had something different. Again,
2221 ready for any thoughts on that. But again we need to have some scribes sit down and do
2222 the lease. That needs to be a working group, I would think, of the Attorney General's
2223 office; Clive maybe taking the lead on that with whomever you want to and Chuck
2224 Goodenough – whomever you want in on that. Does that sound all right?

2225

2226 **Mr. Leroy:** Yeah, why don't you –

2227

2228 **Secretary of State Ysursa:** And, of course, Jason.

2229

2230 **Mr. Leroy:** Why don't you have Chuck and I representing the respective groups –

2231

2232 **Secretary of State Ysursa:** To look at the lease itself. And you need – and inserted in that you need
2233 to come up with the Board – I haven't talked to any Board member who has any problem
2234 with looking at that fourteen-day provision and changing it to something else.

2235

2236 **Mr. Leroy:** There's also an insurance provision. I think it proved unworkable for the Department.

2237

2238 **Secretary of State Ysursa:** The Department has made recommendations on that to us increasing
2239 the insurance and whatever.

2240

2241 **Mr. Lempesis:** Is there – excuse me. Is there a problem that you perceived with an abuse of the
2242 appeal process or is the appeal process working? I think it's been pretty –

2243

2244 **Secretary of State Ysursa:** That was brought up as one of the issues. I think the process that – you
2245 worked on that a lot the last time –

2246

2247 **Mr. Lempesis:** Forever.

2248

2249 **Secretary of State Ysursa:** – cranking that out. No. I don't – if it's agreeable to – I think the
2250 Department thought it was confusing.

2251

2252 **Mr. Thompson:** I think we were seeking a little more clarity in the steps.

2253

2254 **Mr. Fery:** I think it's confusing from a tenant standpoint.

2255

2256 **Mr. Lempesis:** Well, I'm glad I gave such help.

2257

2258 **Mr. Fery:** Sorry.

2259

2260 **Mr. Lempesis:** It's okay, Mike. I have feelings.

2261

2262 **Secretary of State Ysursa:** But Chuck, you would work with Clive on that.

2263

2264 **Mr. Lempesis:** I'd be happy to.

2265

2266 **Secretary of State Ysursa:** Chuck Goodenough.

2267

2268 **Mr. Lempesis:** Oh.

2269

2270 **Secretary of State Ysursa:** And Chuck Lempesis.

2271

2272 **Mr. Lempesis:** I don't even get a shot at it.

2273

2274 **Secretary of State Ysursa:** Whatever it is.

2275

2276 **Mr. Leroy:** Well, we – it seems like we've got to get to a rent formula before we can even talk about
2277 an appeal.

2278

2279 **Secretary of State Ysursa:** Oh, yeah. Before you put it in. There'll be some key points on that. I
2280 think the key out of this meeting is to the ladder to get to some market rent methodology .
2281 Could be different than what we're talking about. We'll have to see what it is. Agreeable?

2282

2283 **Mr. Leroy:** Yes.

2284

2285 **Secretary of State Ysursa:** All right. Again, thank you all for coming and we'll – we'll plot forward
2286 on this thing.
2287
2288 ---
2289 COTTAGE SITE SUBCOMMITTEE MEETING
2290 APRIL 22, 2008
2291 MISSION STATEMENT SECTION OF TAPE
2292 (From 4:10 [regular meeting end] through 4:20 p.m. [short after-meeting])
2293 ---
2294
2295 **Secretary of State Ysursa:** Who are you going to (inaudible) collaborating – your appraisers?
2296
2297 **Mr. Leroy:** Uh –
2298
2299 **Secretary of State Ysursa:** We need to come up with a charge for this (inaudible) –
2300
2301 **Mr. Leroy:** Well, it's a little premature because we – we haven't done anything other than just
2302 engage these guys to say –
2303
2304 **Secretary of State Ysursa:** Why don't we get back together here and communicate on what the
2305 charge of this collaborative group should be.
2306
2307 **Mr. Leroy:** Okay.
2308
2309 **Secretary of State Ysursa:** All right.
2310
2311 **Mr. Leroy:** What I think we'll make our people do is –
2312

2313 **Secretary of State Ysursa:** Similar to coming up with something like the market rent. We need to
2314 come up with a specific charge – a mission statement of what the collaboration is going to
2315 look at, which would be the – namely a lot of the –
2316
2317 **Mr. Leroy:** Is there sufficient data – what it – from what areas will we pull that. Is there some – is
2318 there some mechanism that we would have to adjust that if it's insufficient, you know,
2319 what are the definitions? What's the definition of market rent the Board would – that
2320 professionals would advocate and the Board would adopt. It would be consistent with the
2321 statutes.
2322
2323 **(Male Voice):** And to withdraw other alternative models – but why don't we just ask them to do a
2324 mission statement. They're the guys that probably can design their mission statement.
2325
2326 **Mr. Morris:** We can do it, but I guess, you know, one of my questions is going to be who do we
2327 deal with? How do we involve staff in it? Do we deal with Mr. Moe – is he authorized to –
2328 you guys hired him – authorize us to deal with him or – or how do we approach this thing.
2329
2330 **Secretary of State Ysursa:** Well, first thing we need to do is get an agreed upon mission, uh, the
2331 charge, the statement.
2332
2333 **Mr. Leroy:** right.
2334
2335 **Secretary of State Ysursa:** Once that happens, we'll have enough time – George – George is
2336 (inaudible) too and to look at it and to come up with our own ideas and communicate that
2337 back. And then with George dealing with Stan, and whatever, and that will all be clarified in
2338 the near future.
2339
2340 **Mr. Leroy:** Okay.

2341

2342 **Secretary of State Ysursa:** But I think we need to have (inaudible).

2343

2344 **Mr. Leroy:** Well, why don't we work with our experts to propose – to propose a mission and send it
2345 to –

2346

2347 **Mr. Lempesis:** And send it to perhaps George –

2348

2349 **Mr. Leroy:** And questions that the experts would define and issues that would be addressed by this
2350 legal working group in the lease.

2351

2352 **Mr. Lempesis:** And that's the separate issue.

2353

2354 **Mr. Leroy:** Well, yeah. It's a separate – it's a separate issue.

2355

2356 **Mr. Lempesis:** I mean ideally the legal team would be able to look at this lease. They would go out
2357 and do their mission and would come back and report to the subcommittee and evaluate if
2358 we've done anything at all.

2359

2360 **(Male Voice):** Okay.

2361

2362 **Mr. Lempesis:** Right.

2363

2364 **Secretary of State Ysursa:** There isn't – in my mind – there's not a lot of tweaking to be done to the
2365 lease itself, but the guts of the lease, which is this –

2366

2367 **Mr. Leroy:** (inaudible)

2368

2369 **Mr. Lempesis:** Yeah, Yeah. There were a couple of unworkable things I know that were part of this,
2370 but most of it is good to go. Just make it thirty-five years, and we'll be dead by then and
2371 won't have to deal with that so –
2372
2373 **Mr. Leroy:** So what you want, Ben, is the framework – the framework of a process, a list of players
2374 and a concept and direction.
2375
2376 **Secretary of State Ysursa:** Right. And, George, you're the –
2377
2378 **(Male Voice):** Point man – contact.
2379
2380 **Secretary of State Ysursa:** Contact (inaudible) on that. And then he'll decide what grandiose sign
2381 he's going to give Stan to do this and all that.
2382
2383 **Mr. Lempesis:** Stan didn't volunteer to do this?
2384
2385 **Secretary of State Ysursa:** He may have to tie in to some other way –
2386
2387 **(Male Voice):** (inaudible)
2388
2389 Mr. Lempesis: Your public service (inaudible). This is for the good of (inaudible).
2390
2391 **(Male Voices):** (inaudible)
2392
2393 **Mr. Lempesis:** I would if I could. I'm answerable to my wife. She's kind of the CEO of our company.
2394
2395 **(Male Voices):** (inaudible)
2396

2397 **Secretary of State Ysursa:** The lease terms – Chuck Goodenough, you take the lead.

2398

2399 **(Male Voices):** (inaudible)

2400

2401 **Secretary of State Ysursa:** With the AG's office on the lease.

2402

2403 **Mr. Goodenough:** (inaudible)

2404

2405 **Secretary of State Ysursa:** He already nodded. He agreed. He agreed.

2406

2407 **Director Bacon:** So for my benefit, since I stepped out for a little while, if we could review the next
2408 steps. We're – the Department's going to look at the market rent concept a little bit
2409 deeper. I need (inaudible).

2410

2411 **Secretary of State Ysursa:** Yeah, you're going to have to get comfortable informing – we're going to
2412 have to have – we're going to have more communication and agreed upon a mission
2413 statement for the collaborating group.

2414

2415 **Director Bacon:** Appraisers. And that's what's going to come back from here.

2416

2417 **Secretary of State Ysursa:** Right.

2418

2419 **Director Bacon:** Okay.

2420

2421 **Secretary of State Ysursa:** And you're going to talk to them and whatever. I think we're probably
2422 pretty close, but it's fresh for everybody. So I think we – a reflection on that would do that,
2423 but sooner rather than later.

2424

2425 **Director Bacon:** Well, I understand that, and that's what I wanted to discuss a little bit. I'm leaving
2426 tonight for Coeur d'Alene. I'm going to be up there until Friday.
2427
2428 **Secretary of State Ysursa:** You don't have to do it tonight.
2429
2430 **Director Bacon:** No, I recognize that. And then I'm on vacation for two weeks. I'll be back on the
2431 9th –
2432
2433 **Secretary of State Ysursa:** Now we're talking.
2434
2435 **Director Bacon:** – of May. And then I'm leaving for the Western Forestry Leadership Coalition
2436 meeting in Manhattan, Kansas, for a week.
2437
2438 **(Male Voices):** (inaudible)
2439
2440 **Director Bacon:** That's where their tree is. But –
2441
2442 **Secretary of State Ysursa:** You have capable staff and email.
2443
2444 **Director Bacon:** That's where I was going.
2445
2446 **Secretary of State Ysursa:** Blackberrys, or whatever they are.
2447
2448 **Director Bacon:** Jane, uh, Jane Wright, who is down there, and Kathy, will be taking the lead
2449 (inaudible) –
2450
2451 **Secretary of State Ysursa:** Okay.
2452

2453 **Director Bacon:** – on this if I'm not around. So – just wanted to let you know (inaudible).

2454

2455 **Mr. Leroy:** Well, we'll get – we'll get to the Department, and to you and Tom, courtesy copies to
2456 the other members of the Board, the lawsuit memo regarding what the status is, our
2457 comments on what ought to be done on 2009 lease rates and a written proposal for a
2458 mission statement that talks about who, what, issues and process.

2459

2460 **Mr. Lempesis:** And then Chuck is going to organize the –

2461

2462 **Mr. Leroy:** Working group –

2463

2464 **Mr. Lempesis:** – the legal plane for us, and we'll communicate through your name to the
2465 Department.

2466

2467 **Secretary of State Ysursa:** We went over some of the lease when we were doing the new one for
2468 your (inaudible).

2469

2470 **(Male Voices):** (inaudible)

2471

2472 **Secretary of State Ysursa:** Yes, sir.

2473

2474 **Mr. Moe:** One thing, I know it's going to be real tempting in setting forth a mission statement for us
2475 to set some parameters. Then I would ask that you leave it as open as possible without any
2476 boxes that could (inaudible).

2477

2478 **Mr. Leroy:** I didn't understand that. Say it again.

2479

2480 **Mr. Moe:** It's going to be real tempting to build boxes. Here's what we want you to do within these
2481 parameters, and I would ask that you not do that leaving this open to let us look at every
2482 feasible option.
2483
2484 **Mr. Leroy:** What if it just simply said, and let me offer this up, what we said earlier, which was to
2485 explore whether there are reasonable and feasible alternatives to determine market rent
2486 that would be an improvement over the present processes (inaudible).
2487
2488 **Mr. Moe:** Simple as that. Simple as that.
2489
2490 **(Male Voice):** (inaudible) Isn't that what you're looking to?
2491
2492 **Mr. Leroy:** But I also –
2493
2494 **Secretary of State Ysursa:** But as it goes down, though.
2495
2496 **Mr. Leroy:** Yeah, I also heard implied here that if we can supply some direction about questions or
2497 issues or process or even timetable, those would not be unattractive, but you guys will all –
2498
2499 **Mr. Moe:** As long as we're authorized by both of our clients to communicate. We're okay?
2500
2501 **(Male Voice):** Oh, yeah.
2502
2503 **Mr. Moe:** Then definitely.
2504
2505 **Mr. Leroy:** Why don't you – why don't you propose all three of you together initially back to the
2506 respective presidents and they'll get Chuck and I involved. Once you do a draft of a mission
2507 statement and then we'll augment that.

2508

2509 **Secretary of State Ysursa:** Get it to George. But you'll be on vacation.

2510

2511 **Mr. Leroy:** Yes, do an initial draft – the three of you guys – and then get it to us and we'll try to
2512 screw it up.

2513

2514 **Mr. Moe:** We could email.

2515

2516 **Secretary of State Ysursa:** Yeah, I was – I mean, Stan, I would agree that you don't want to box you
2517 in, and this is something new to look at that and if it doesn't make sense to staff or to the
2518 Board then so be it. We won't follow it.

2519

2520 **(Male Voices):** (inaudible)

2521

2522 TAPE TRANSCRIPT END

Exhibit 34

Transcript, Land Bd. Cottage Site Subcommittee Meeting (May 18, 2009).

STATE BOARD OF LAND COMMISSIONERS

COTTAGE SITE SUBCOMMITTEE MEETING

MAY 18, 2009

IDAHO DEPARTMENT OF LANDS DIRECTOR'S OFFICE, BOISE

Secretary of State Ysursa: Members of the Board are here – of the Cottage Site Subcommittee. I want to express my appreciation to – we have a lot of things to go over today. My hope is to have the Subcommittee come out of here with some sort of recommendation for us to present to the Land Board. Our charge is to give a recommendation at the June 16th meeting, and we have some ideas. We conversed a little bit back and forth with Mr. Leroy and Mr. Lempesis about some things, and I do want to thank the Land Department staff for their fine work, especially Jane Wright on helping out. And I certainly appreciate what the cottage site folks have done, and the appraisers report and their methodology, and we read it very closely. Have some questions about it. But I think we see the agenda here – we are ready, willing and able to have a presentation on the methodology used. Then the Department will have a kind of a point-counterpoint scenario and then some other discussion.

But without further ado, whoever wants to lead the way with the discussion of the appraisers' methodology and any whistles and bells you've got to show us.

Mr. Lempesis: Mr. Secretary, with your permission, I think Mr. Morse prepared a very brief presentation which may help clarify some things, and if not, you'll be the first to let him know.

23

24 **Mr. Morse:** Can everybody hear me if I speak in this tone of voice up here? Okay. I'll try and lead you
25 through briefly what the appraisers did. We were charged with putting together a model and
26 having all three appraisers agree on an approach to try to determine market rent. We have
27 previously been through up at Priest – with some additional research done at Payette –
28 analyzing short-term rentals. And Stan Moe felt pretty strongly that we ought to look at
29 monthly to annual rentals, longer term rentals that were more standard in the real estate
30 market. So we performed a lot of research on rentals after – excuse me – and looked at
31 methodology. So we started out with joint research and analyzing actual rentals out in the
32 marketplace to determine rates of return. Most of the rentals in the marketplace are improved
33 lots. The state has a very unique atypical product in that they are renting lands and other
34 people have the improvements and they rent that land long term.

35

36 So the rental data in the marketplace consists generally of improved properties that then one
37 must extract that rental. We used primarily rentals that were rented on a monthly to an annual
38 basis rather than short term weekly, daily rentals for recreational-type things. We put a few of
39 those into the rent for analysis to find out whether or not the results would be consistent, and
40 they were. But most of the rentals in the model simply represent longer term actual rents.

41

42 The appraisers agreed on the model, and one of the I think most important conclusions is we
43 find rents and rates of return vary inversely with property value. And if you do very much rental
44 research in the marketplace, I think you can understand how we came to that conclusion. If you

look at residential investment real estate, you'll notice that the types of real estate they build for investment purposes in a residential area are on the low end of the price range – apartment houses and mobile home parks. They do – nobody – no investors build million dollar homes and few investors build million dollar or two million dollar lakefront homes for rental property purposes. There are relatively few renters up in those price ranges, and consequently we found that there is a significant difference in the rent that is generated and the rates of return.

We call this an inefficient market, or an inefficient return, when there's – when there's a significant difference between segments in the market, and we're dealing with a market segment that has significantly less efficient rates of return.

So these observations about the data coincide with what we found in the marketplace, and then that – those rates of return were applied and graphed. And that is a graph of rates of return in relation to land values and how the relationships were revealed by data analysis.

We found that the data fits consistent patterns. It conforms to what we consider the logic market observations and economic trends. Investors are not out buying waterfront lots, or large expensive home sites, and then trying to lease that type of real estate product. Nonetheless, there is a market. It is somewhat active. It does exist and it can be measured.

Once we got our data in our rent curve, we performed a number of different types of statistical analysis on it to try to find out what patterns that data fit. And this is the – this is one set of that

data. This is another set of the same data right there. And that really – both of these show a significant change in relationship to property value and rate of return. We fit regression lines to that data to determine what's called the best curve fit, and then based on that curve fit information, we can calculate with a value input a corresponding rate of return for rent for any particular property value. These conclusions are what we would call market derived. It's got a high ease of use. It can be updated with both current and local rental information as well as the most recent changes in property values. So with any – there are two inputs once you've got your rent curve. With either one of the inputs, you can calculate the other.

What we've got in terms of Priest Lake lots are not what we would call typical rental lots. They are not platted. The lots are much larger than typical. They're great lots. They're expensive lots, but they are not what we would consider to be efficient rental property. However, the nature of the model is if we're looking at the value, or rate of return for land from a five hundred thousand dollar site, we've got five hundred thousand dollars – the rate of return for a five hundred thousand dollar site after we've made an allocation to improvements and then that would be the same type of rate of return for a Priest Lake lot or a view lot that was overlooking Coeur d'Alene Lake.

All economic and real estate market conditions have been affected by the downturn in property rates. The analysis that I've done throughout the Panhandle counties show slower, higher inventories, slower sales rates, declining prices and lower rates of return, and that's just the economic times that we're in.

You can not get around those economic facts. Kootenai County's foreclosure rate is the third highest of the Idaho forty-four counties, and Kootenai County ranks ninetieth nationwide in foreclosure rates. Generally speaking, the analysis that I've done on cottage sites, they indicate that they are just about holding steady. But there is a difference in the pattern of leaseholds – leasehold value in relation to sales price appears to be declining. All regional and national markets are similarly affected, and the CPI graph which follows will show you just what's being done to the CPI over the last six months. CPI is now negative. In my life I've never seen a negative CPI.

We looked at a number of Payette rents and calculated some rent curves down on Payette. And although that was not part of the data input in this model, it was consistent with the same kinds of patterns, and the same kinds of rent curves, and only slightly, slightly different rates of return. And since we felt our charge was simply to determine the model and the viability of the technique, rather than to try and solve the entire problem at one time, we did not either consolidate all the data or try to do two separate – separate rent curves. But I think if you were going to apply this, you would probably input a set of Payette data and a set of northern Idaho data to find out whether it was any statistically significant difference.

This – the output in the data is also comparable with other rental indications in the market. There are only two unimproved waterfront land rents that I'm aware of in northern Idaho. One is up in the Pend Oreille Lake area, and the other one is on Sunup Bay on Coeur d'Alene Lake.

Both of them are un-subdivided acreage. One is at thirty-six hundred per year; the other one is at thirty-two hundred per year, plus another twelve hundred per year for a boat slip. Both of those would fall probably towards the middle, or below the middle, of the data that we came up with.

Conclusions, the method's market derived. We feel it reflects market rent, which is the professional, and we believe the legal standard. It's got ease of use. The regression model uses value inputs. It can be easily updated. An appraiser can update and input that data at whatever the appropriate intervals would be, whether it would be every five years or every year to look at those changes.

I'd be happy to answer any questions if anybody's got any.

Secretary of State Ysursa: We are going to have on the agenda the Department of Lands' response. Then maybe the questions. I guess one question that pops up to me – and more than one – one of the graphs as you start – it starts climbing at eight hundred or nine hundred thousand. We've got lots in Payette Lake waterfront going from one million to two million. Is it going back up on your graph? That's the way it looked if you take it. That's just a question.

Mr. Morse: You'll notice how – what – what we do is we calculate a line that fits the best curve in here. There are so few data points out here at this price range point, we simply, at this point in time, don't have much value. The data – this data is North Idaho. It's not Central Idaho. And in terms

133 of applying this method in the Payette area, my response would be we need more data. In fact
134 we need more data points all along here, but this was to demonstrate the viability of a method.
135 And I really would be amazed if that goes up. It may well be that because you look at all of
136 these relationships here, this transaction may well reflect motivation, long-term relationship,
137 family associations, some things like that that we may or may not (inaudible), and that's what
138 we measure. But that – I mean, it went from one and a quarter percent to two and a half
139 percent.
140
141 **Secretary of State Ysursa:** Tom, do you have any specific questions there?
142
143 On the agenda, and, Ed, we're going to ask you some more questions (inaudible) probably later
144 on. If we could have Jane Wright – I believe Jane is going to talk from the Department
145 perspective and, number one, thank you, Ed and Joe and Stan Moe about some – the idea is to
146 have the Department's perspective on this and anytime – and then we have some ideas. I know
147 Jason has some ideas and others, but – and I have some more questions for Ed and others, but,
148 Jane, why don't you just lead it off from the Department perspective and then we'll ask
149 questions later then.
150
151 **Ms. Wright:** Okay. Thanks, Ben.
152
153 From the Department's perspective, I just want a very brief overview of who worked on this
154 project with me. We have a certified appraiser on staff, Perry Whittaker, who closely reviewed

155 the market study with me. We have a Deputy Director that has a Master's Degree from
156 Northwest Nazarene College, and myself, who worked reviewing the market study. And I – you
157 can see from my designations I'm a Certified Public Accountant. I'm also an internal auditor.
158 But what isn't on there is I spent twenty years in the State of Arizona as a licensed real estate
159 broker. So I'm familiar with appraisals. I'm familiar with rent markets. I'm familiar with the
160 money market, and so I understand that. In addition, when I took this position, I went on the
161 Institute of Certified Public Accountants website and took a few of their continuing education
162 classes on appraising just to keep me up to speed.
163
164 So we looked at it with, of course, a critical eye – a very analytical eye – and an eye with a lot of
165 expertise. And the data that spoke back to me was the cash that the Department received as
166 revenue. And I had data from fiscal year 2003 to fiscal year 2009. What I was after is what was
167 – my question was what was the total revenue that the Department received in what we all
168 know as leasehold value. The client had received two million eight hundred twenty-eight dollars
169 – excuse me, two million eight hundred twenty-eight thousand, seven hundred sixty-four
170 dollars. So I said okay. What's a hundred percent of that. Just divide that by ten percent. A
171 hundred percent of that money was twenty-eight thousand, two hundred eighty-seven
172 thousand, six hundred forty-two dollars.
173
174 **Secretary of State Ysursa:** Twenty-eight million.
175
176 **Ms. Wright:** Yeah. Thank you.

I work for the state (inaudible). Okay. So the cabin owners' proceeds is ninety percent of that. Get ninety percent, right. So the cabin owners' proceeds is twenty-four million, seven hundred ninety-nine thousand, nine hundred and twenty-three dollars. IDL's total income from premium rent, rent and any late fees, was twenty-four million, seven hundred ninety-nine thousand, nine hundred twenty-three dollars.

Mr. Goodenough: That's the same number.

Ms. Wright: Same number. (inaudible) Ten percent is two million eight so a hundred percent was twenty-eight million. Leasehold value, cash that was paid out to those who transferred leases, was twenty-five million plus fifteen thousand eight hundred seventy-eight. Idaho Department of Lands' total income, premium rent, net and everything, was twenty-four million, seven hundred ninety-nine thousand, nine hundred twenty-three. The leasehold value for those who transferred their leases is greater than total IDL income.

My basic premise on the market rent methodology is that the regular rental market of short term, and short term meaning less than ten to thirty years, which these are, is not at all congruent with this market. Let's look at it a little different way, and I hope I can write on it this time.

Voice: Just don't make any mistake.

199

200 **Ms. Wright:** Okay. We see the rate of return – the rate that we're using. And currently the rate that
201 we're multiplying the value by is 2.5%. That's right in here. Well, it's right here. With the rent
202 rate at two and a half percent, that leasehold value was way out here. As your rates increase,
203 what's going to happen to your leasehold value. It's going to go down because the market is
204 going to determine that. And at a two and a half percent rate, we saw seventy-eight cabin
205 owners have more money than the Department did on five hundred and sixty-two leased lots.
206
207 So what happens right now to the premium rent for the ten percent. This is not looking at a
208 market that you think might be comparable. It's looking at the market we're looking at. It's the
209 actual market. The same thing's going to happen if you go up this line on charging premium
210 rent. The market for premium rent is going to go down, and that is determined by the market.
211
212 The basis of the market rent study was on short-term rents, six months to twelve months. The
213 difference between the lease agreement for those properties, and the one enjoyed by cabin
214 owners, is just significant. The leasehold value at transfer is certainly one of those. The other
215 one is the right to mortgage. You build your own property; your own structure on the property.
216 You have the right to bequeath and transfer the leasehold rights to your heirs, and then at such
217 time they will benefit from this leasehold value. There's no conflict leases. They go into
218 perpetuity. There's no restrictions or additional deposits regarding as far as pets are concerned.
219 And there's a split ownership in a market that is referred to in the market study. There isn't a
220 split ownership.

The only things that are congruent from the market study to the property that the Department of Lands has is you have the right to occupy it. The lessee is responsible for the improvements, and a default in payments results in termination of the agreement. That is also the state.

In the first document that the appraisers presented to the Department on the methodology, and in the paragraph you referred to long term mortgage rates, and in the Policy Advisory Group, published out of the University of Idaho, they quoted a study. It wasn't their quote. It was the experts' quotes from – and I can give you those references – that these terms should accommodate typical terms for conventional financing, which is twenty to thirty years, not two weeks, not thirty days or a year, but twenty to thirty years. As much as thirty-five years. Legislation was just changed a year ago so those leases would be thirty-five year instruments. Even while into a lease term, changes in the interest rate will (inaudible) incentive for the lessees to refinance.

So along with the different terms in the lease, not at all congruent with those that were used in the market study, the inability to get good statistical data, as you can see as you run out there on the higher end that that data, was not available, and the experts – and I've read all the studies – and I don't say when I've read them I've just read them. I've studied them, that the Department has had for the ten, fifteen years, and you're right in your market study in saying it's unique and it's new that the methodology, the foundation to which it's based on, I just simply can not agree with it.

Where should it be? My first smart-alecky reaction was – after I saw this – don't charge me anything. We'll just take the leasehold value. We'll make more money. There's yeah-buts to everything. Yeah, but – we, the Department, in working on behalf of our beneficiaries will need consistency in how we would lease the program over all, but I believe with the numbers that we're looking at, and I know the market's changed, but there're right in here between that five and six percent rate. And then this lies where it does. If I were the Grand Pooba, I'd give it to you. I don't know that we're ever – are able to (inaudible) except in looking back in history because we have the market out here (inaudible).

You put the rate up here. What I can hear going on, possibly, is those who don't transfer their leaseholds and want to stay there, it's been in their family for lots and lots of years, and I understand that argument's out there, but the Representative Black back in the fifty-fourth Legislature, in about 1998, brought forth Senate Bill – House Bill 791, which taxpayers paid seven point six million dollars for fifty-six acres of land on Payette Lake so all people could join in enjoying the waters and the beach on Payette Lake, not a select few. This Department is charged in the Constitution and that would be the caveat (inaudible).

Secretary of State Ysursa: Okay. We have – thank you, Jane.

(tape change) – leave it up to the discussion. And I tried like – not to necessarily discourage a lengthy discussion on methodology, but my basic problem with market rent is that you have to

265 in any appraisal go out and get a comparable, and I have consistently stated, and I'll continue to
266 state, that we have no comparable market on our state-owned lots. And we can talk all we can.
267 I mean the methodology about attributing expenses and things like that to the private sector,
268 how many of these rentals were – in essence you had a ten year with the 310a provision and no
269 conflicts, if you were a good doobie you had them into perpetuity. And these things aren't
270 comparable. And just a couple of statements were made in other documents by an appraiser
271 who believed that basing market rent on the use other than the highest and best use is a flawed
272 appraisal premise. Basing market rent on income from seasonal cabin rental is inconsistent with
273 the highest and best use. The highest and best use is not for income producing purposes but
274 rather for residential or recreational residential purposes.
275
276 I guess my basic reaction is as much work as you did, and everything else, Ed and others, I just
277 don't think they're comparable. And that's – that's the number one problem in the whole –
278 whole thing. And please comment.
279
280 **Mr. Morse:** I think if you go back and talk to the appraiser that made those statements, he's been
281 enlightened and reeducated that –
282
283 **Secretary of State Ysursa:** You disagree with the statements I made?
284
285 **Mr. Morse:** Yes.
286

Secretary of State Ysursa: You don't think we ought to be going after comparables?

Mr. Morse: No. No. No. That's not the part – but what I disagree with is the statement that you read that said that if they're not being used or rented to their highest and best use then you should disregard them. The – I believe the appraiser that made that was Mr. Moe, who has now joined in this market study and has been re-educated on that point. To determine market rent there is no highest and best use test. If you've got a product, and you want to know what the market rent of it is, you go out and research rents for that type of product in the marketplace and maybe –

Secretary of State Ysursa: In a publicly-owned entity who has waterfront property?

Mr. Morse: Mr. Secretary –

Secretary of State Ysursa: And how many of those do we have? Ownership – no, I'm asking you about a comparable, Ed.

Mr. Morse: None. Because you've got an inefficient product and it –

Secretary of State Ysursa: You don't have a comparable.

Mr. Morse: –you don't have the exact –

309

310 **Secretary of State Ysursa:** We gave you an impossible task.

311

312 **Mr. Morse:** Okay. You don't have people in the exact situation trying to do what the state is doing
313 because you have a unique burden or charge, and you have a unique product. Most people out
314 in the private marketplace are not going to rent long term and have somebody else put the
315 improvement on their property. Those – a leasehold under that situation is quite risky contrary
316 to Jane's perspective. So when people are building on property that they don't feel that they've
317 got a long-term position in, and they're incurring mortgages in that, that's a highly risky
318 situation unless you get longer terms or the ability to roll over and some things like that. These
319 were done to facilitate the marketability and as the property values rose to be able to handle
320 these kinds of things. Now the issue about no perfect comps relates to my comments about
321 we've got an inefficient rental process out there in the market and to simply say, well, you can't
322 determine what the rent is because it's – that, you know, either we own it, and that makes it
323 special, or it's got some different characteristics to it. It doesn't mean that you go out and
324 ignore everything that's happening in the marketplace because you can't get to six percent or
325 five percent rates of return for this value of property based on everything that's out there in the
326 marketplace. So there's a number of different distinctions here that I think we've got to be
327 careful about. Market rent based on the comps we can find. Market rent is based on actual
328 transactions that people are doing out in the market. The market's not perfect. But by looking
329 at these patterns, and looking at any and all kinds of rentals, you can come to some supportable
330 conclusions. You know, if you were to be starting over again, you know, my advice to the state

331 would be don't do two hundred waterfront lots. That's not a particularly efficient design. But
332 that's what we've got, and we've got people that have their cabins in the middle of them. And
333 when you've got that kind of a situation to look at the highest and best use, the highest and best
334 use of the state's real estate is to redevelop it and re-subdivide it into something else, if you
335 could do it. I don't think you want to do it, and I don't think you want to get into a fight about
336 who's going to buy out the ownership or the improvements that's on there. We've got to take
337 what we've got and look at the data in the marketplace. That's the hand we're dealt. And
338 we've looked – we've looked at this thing for a long time. The most recent data that I've run on
339 the leaseholds indicates that the leasehold sales price is going down contrary to what comments
340 by the staff would indicate. And to just arbitrarily pick some numbers out that you think is going
341 to drive leasehold prices to zero, without any support in the marketplace, I think is irresponsible.
342 You've got to look at what actual transactional data place in the market is doing.
343
344 **Secretary of State Ysursa:** But all these figures are based on what's actually happened. There's not –
345 she's not necessarily (inaudible) –
346
347 **Mr. Morse:** Five or seven percent isn't.
348
349 **Secretary of State Ysursa:** No. We – the ones before that found the less – just getting ten percent –
350 getting ninety percent the sale on premium rent made more money than the state did.
351
352 **Mr. Chuck Lempesis:** It doesn't.

Secretary of State Ysursa: It did.

Mr. Lempesis: It doesn't.

Secretary of State Ysursa: No. No.

Mr. Morse: Let's go back and –

Secretary of State Ysursa: Those are based on actual sales, and as we speak, in April of this year, which I would think would be one of the worst markets, there were three assignments in Priest Lake that got the state seventy thousand dollars, and which means the lessees got six hundred and thirty off of the value of our land. So as far as Payette Lake and where the market is, it's dried up as far as premium rent, but she's basing – what Jane talked about the figures before are actual transactions. How much the premium rent was taken in.

Mr. Lempesis: Hold up. Mr. Secretary, would you pull up that – that slide is flawed.

Secretary of State Ysursa: I'm technologically challenged here. Who's going to pull up the slide?

Jane, pull up your slide. And please comment on it.

375 **Mr. Lempesis:** It's – it's erroneous data, Mr. Secretary, and at first it did not dawn on me. But if you pull
376 up the slide and look at the curve, it's deceiving. And as soon as it gets up, I'll try to see if I can
377 muddle my way through this.
378
379 **Secretary of State Ysursa:** That's all I was talking about is the money in the transaction.
380
381 **Mr. Lempesis:** And I (inaudible) I really do appreciate that. I don't want to be disrespectful. If you take
382 this, that's a given. Okay. Then the ideal share of the premium rent is two million, eight
383 hundred twenty-eight thousand, seven hundred sixty-four dollars for that period of time. The
384 question, as properly posed, is what does the state pay for that. And the reality is on a net
385 basis, nothing. That is a share of an ongoing revenue stream, ten percent of what everybody's
386 giving. Please appreciate this.
387
388 **Secretary of State Ysursa:** Why should we pay for it? It's our property.
389
390 **Mr. Lempesis:** When you look at this figure, what I'm going to compare is the net worth. If you look at
391 this figure right here, you can take the twenty-eight million, two hundred and eighty-seven
392 thousand dollar figure, that's gross. That's what people got for that and received from another,
393 correct? What it doesn't take into consideration then is what anybody paid for it. When you
394 look at this figure, you can have the state receiving substantially more than what the renter
395 (inaudible) what the lessee gets. If I paid four hundred thousand dollars when I acquired that,

and I sell it for four hundred and fifty thousand, you would get forty-five thousand dollars. I would lose money.

Ms. Wright: The leaseholder didn't pay anything toward (inaudible).

Superintendent Luna: I didn't follow your last point there because this – the state only gets ten percent. You were saying just the opposite I thought. I (inaudible) hear you saying four hundred to four fifty that the fifty thousand dollar increase the state would get forty-five and the lessee would get five. I thought it was just the opposite.

Mr. Lempesis: What you would get is ten percent of whatever that gross sale price is. Correct? (inaudible) for the leasehold (inaudible). But if it was a hundred thousand dollars, you would get ten thousand dollars. Correct?

Superintendent Luna: Correct.

Mr. Lempesis: And I would get ninety thousand. Correct?

Superintendent Luna: Correct.

Mr. Lempesis: What if I paid a hundred and ten thousand dollars for it is my point. This disregards what the lessee may have purchased it for from another. (inaudible)

418

419 **Superintendent Luna:** I guess I assumed that we were getting (inaudible) of the capital gain.

420

421 **Multiple Voices:** (inaudible)

422

423 **Mr. Lempesis:** And that is the fatal flaw in this whole analysis. And I think if you'd parse those numbers,

424 you'd find this is not exactly what it appears to be. People – you know – we've – we've talked

425 about this for years. No, well, people are paying two hundred and fifty, three hundred thousand

426 dollars for these leasehold interests, right? Yes, they are. And when they go to sell it for three

427 hundred and fifty thousand dollars, the state gets their ten percent. And, in many instances, our

428 people break even or lose money.

429

430 **Superintendent Luna:** Is that what your statement is – many instances?

431

432 **Mr. Lempesis:** Well, you just got 2008/09s, right.

433

434 **Mr. Morse:** I just – I found a sale in 2008 and a sale in 2009, both the same sales price. The person that

435 bought it lost money. The state was the only one that made money on that transaction.

436

437 **Superintendent Luna:** How long had they held that lease?

438

439 **Mr. Morse:** Just a year.

Superintendent Luna: Seems like trying to flip it.

Multiple Voices: (inaudible)

Secretary of State Ysursa: Got caught flipping.

Mr. Morse: (inaudible)

Secretary of State Ysursa: Well, that's what I mean. That's what I mean – that's when you get caught, Ed.

Mr. Leroy: I'd say we got lucky flipping that one.

Mr. Lempesis: But Mr. Secretary, all I'm asking is please respect the fact that those figures do not take into consideration the reality (inaudible).

Secretary of State Ysursa: I would love to see, for the sake of fairness, your analysis of those figures.

Mr. Lempesis: I'd be more than happy –

Superintendent Luna: Do we know the seventy some-odd sales –

Mr. Lempesis: You would know every one. Would you agree, though, without a doubt that the lessees didn't make twenty-four million dollars? That's the part that I think is unfair. They didn't even – yeah, because that's like saying you sold your house, Ben, and you got three hundred thousand dollars for it, and we're going to tax you on that, but you paid two eighty-five for it. I mean, come on, I just don't – fair is fair.

Secretary of State Ysursa: Take personal improvements out of it and then get down to the land.

Mr. Boyd: That doesn't take into account when people (inaudible) –

Voice: (inaudible)

Secretary of State Ysursa: The rental income was included in our income.

Mr. Boyd: But not in the bases.

Secretary of State Ysursa: From the other positions, no, not all of them.

Mr. Lempesis: You had the TB of the money just incorporated in your base. It's not – not yet. I just hope you respect – because I don't want you relying on those numbers by looking at the

483 windfall for the lessees because that is absolutely flawed. That's all I'm saying. We'll make
484 whatever decision the recommendation says, but please don't do it based on flawed data.
485
486 **Mr. Goodenough:** No. And another thing that all this premium rent doesn't even approach is the loss in
487 what could be premium rent if we were collecting it based on the love and affection
488 transactions. We don't get a dime off those.
489
490 **Mr. Lempesis:** That's because you're into love and affection, Chuck.
491
492 **Voice:** You want to tax love and affection?
493
494 **Mr. Lempesis:** Thank you. There is a man I'd vote for right there. He doesn't tax love and affection.
495
496 **Multiple Voices:** (inaudible)
497
498 **Mr. Bridges:** Mr. Secretary.
499
500 **Secretary of State Ysursa:** Yes.
501
502 **Mr. Bridges:** I'd also point out that the disconnect from the market is we know for a fact, in fact going
503 back to December 06, everyone on the Land Board unanimously acknowledged the market is
504 dead and broken so far as Payette is. And, in addition, I would join in the comments of our

505 neighbors to the north that you have to look at the basis in terms of – you have to look at what
506 profit, if any, is being made, and from the day you enter into this transaction, no matter when
507 you sold it, if you sold it six months later or sixty years later, you have to make, by definition,
508 more than ten percent than appreciation to even come out even just on the sales price. And we
509 know that there haven't been sales at Payette. So the market analysis, when it says it's looking
510 from 2003 to 2009, it really is 2003 by definition at Payette until 2006, and that's at a time when
511 we get into the other problem with the skyrocketing appraisal price. That's what got us here in
512 the first place. That's just recognizing – in my view what that shows is recognizing what we all
513 agreed to a couple of years ago. The system is broken.
514
515 **Secretary of State Ysursa:** Well, for the record, the premium rent at Payette rose considerably in 2-0-4,
516 2-0 – these are fiscal years, 2-0-4, 5, 6, 7, dropped off the plan in 08 and in 09.
517
518 **Mr. Bridges:** Which is recognizing that same astronomical rent increase that we all recognize was the
519 foundation of the problem which –
520
521 **Secretary of State Ysursa:** Which led us to this, and which we have, we think, a solution for. The
522 unbelievable escalation. But we'll get to that in a few seconds.
523
524 Any other comments from anybody on the – either the appraisers' methodology and how it was
525 presented or the Land Department's questions about it?
526

527 Yes, Josh.

528

529 **Mr. Boyd:** I have a couple of questions as it leads to understanding the comparables. And just – and I'll

530 pose them to Ed.

531

532 So in a typical market, if you annualize the rent rate and you take short-term rents, so people

533 who say – of course, this is not comparable – but (inaudible) paid by the week for a cabin versus

534 if they said I'm going to rent it the whole year. Would you expect the short-term one to be

535 higher if you annualize it? Or do you expect the annual one to be higher just in the normal

536 economic environment.

537

538 **Mr. Morse:** Generally speaking, short-term rates are higher than long-term rates because long-term

539 rates generally have more security to them, and they're structured to provide less turnover, less

540 management burden, less risk, which – than a short-term rent. Now that being said, there are a

541 number of people that have looked at – that own property in the waterfront rental market –

542 and they have decided that over a short-term basis, the three months in the summer they think

543 they can in relation to cost in relation to management burden and their net returns, they can

544 come out better with owning the improvement and the furnishings doing short-term rentals.

545 There are other people that feel that is too big of a management burden, and they will rent on a

546 long-term basis. We've looked at both of those. They correlate fairly well. This most recent

547 study we looked at the longer term rents. Previously up at Priest Lake, Vogel looked at shorter

548 term rents. The state objected to it because there were deductions for management and

549 utilities and things like that in it because of all the services that were provided for short-term
550 rentals. When you're renting something short term, it's furnished, and you've got the housing
551 improvements in it. You've got to consider that to get to a land rate.
552
553 **Mr. Boyd:** I think my point on that one, and I think it's something probably people understand, is that a
554 short-term rate is going to result – a short-term rate as a – as put into the market rent study is
555 going to result in a slightly higher rent than you would get if you leased the whole thing out for
556 thirty years and actually had that comparable. The thing I'd like to point out is that we didn't
557 ask to say okay find the best comparable you can find. Find what's going on in the market and
558 then adjust it down because we're going to sign up for twenty years, thirty years. And I don't
559 think that's what we've ever said because that's problematic. That would be terrible to
560 negotiate, and we've never said that. So I think in one regard there's one issue with those
561 comparables that is definitely helping the state out. We haven't asked for some adjustment to
562 say we'll sign up for thirty years give us ten percent off, and I don't think we will do that.
563
564 The other question I had is that as general asset classes go, somebody who's renting out land
565 only, and somebody who's renting out land plus the building, where they have the expectation
566 of having to take an entrepreneur to build the building, maintain the building, have insurance on
567 the building, my assumption is that person who rents out a building and land is going to expect
568 and derive from the market greater rent as a percentage of the asset value than somebody who
569 just rents out a plot of land and says, you know, there you go, you know, I'm not involved. You
570 just rent out the land.

571

572 **Mr. Morse:** That's true. I mean the pure rate of return to the land is going to be lower when that's all
573 you're leasing. If you've got a building ownership there, that's got a significant recapture
574 involved with it, and that's important to be able to understand and distinguish here. And I think
575 that's one of the things that the state's comments, or the staff's comments, don't reflect that
576 the actual leasehold ownership here that they seem to somewhat envy, they're forgetting that
577 there are building improvements that are involved and a very risky ownership position because
578 this lease keeps changing and the rates of return keep changing. And so there's all kinds of
579 people that bought these things and are not in a position where they are going to make money.
580 That relates to the inherent riskiness of the ownership of the leasehold position versus the
581 ownership characteristics of the state position, and the market is clearly recognizing that if you
582 look at the leasehold sale statistics that I just passed out.

583

584 **Mr. Boyd:** And I think I made that last point because, like with any alternative methodology or the old
585 methodology, you're always going to have that problem where you don't have direct bare land
586 comparables. You always have to take the improvements off. It doesn't matter what
587 methodology you have. It just – there's not bare land sales out there. There's not bare land
588 rent out there. So I think that's another thing that I thought is key to get past. When you look
589 at market rent study, just realize that whether it's the old method or the new method, you
590 always have that problem.

591

592 **Mr. Morse:** But that's not uncommon in –

Secretary of State Ysursa: If I may interject, I love the soliloquy between you two, but there is a dialogue – let's move on. (tape change) – the rabbit out of the hat, and the methodology here has not dissuaded me from that problem. Now, having said that, I think we need to discuss some other possible scenarios that we're looking at recognizing that the number one problem in this whole scenario is the lack of predictability and the rapid escalation, especially in – it was certainly led by the Payette Lake waterfront in Valley County assessments. But it's also been rising at Priest and whatever. And the rapid escalation, the over forty percent raises, the projected second tier raise in Payette of eight-eight percent after a thirty-two percent. Things like that. That's what led to this problem. And I for one am very sympathetic to the plight of the cottage site owners as far as predictability and stability as far as those rapid escalations of rents. And having said that, the last time we had Director Bacon talk about it, but the idea of some sort of ten-year scenario to look at – some sort of averaging, whatever – led to some discussions. And if I now would turn it over to Jason Hancock and Jane Wright, if they want to discuss what we've been looking at on a possible scenario on getting to some sort of predictability in this rent and do away with those spikes in the process.

So Jason, if you wish to take it away.

Mr. Hancock: Sure.

Secretary of State Ysursa: And, Jane, I don't know if you have – do you have anything on this?

615

616 **Ms. Wright:** I have –

617

618 **Secretary of State Ysursa:** A slide or two?

619

620 **Ms. Wright:** Well, just an Excel spreadsheet that shows you how it's calculated. I don't know if he's

621 going to use that or not.

622

623 **Secretary of State Ysursa:** Okay. And you have some –

624

625 **Mr. Hancock:** I just have this thing from last time.

626

627 **Ms. Wright:** Let me go through the Excel.

628

629 There are a couple of authors of this. One being Jason; the other being Director Bacon. As Ben

630 said to you, and he has certainly transferred that message to us on staff, the spikes in this

631 market – this is just a little graph that shows – here's Priest Lake in red; Payette Lake here;

632 Payette second tier; this one – this is – any methodology that went forward would be included

633 in pools to smooth those spikes and it would – and to provide some stability in that market –

634 and there's – we considered a methodology in which there are two ways to smooth it. First of

635 all, use a ten-year average. And this, I just took a lot to explain how it works, lease number

636 7777. The rent in 2009 was $6,500. That is not the two point five percent times the appraised

value. That is rent in 2009. And rent had been forgiven or not increased (inaudible). So then we took the assessed value for ten years. We used the assessed value for this lot, and said okay, and let Excel calculate the average. What's the average of these numbers in cells D3 to (inaudible) –

Voice: Jane, just a quick question. Is that a Payette lot? And is it a lakefront or second tier or is it a –

Ms. Wright: This is a Priest Lake example.

Voice: Okay.

Ms. Wright: But I have the other one, if you would like to see it.

So there's the average – ten-year average – and that was step number one to smooth the spikes. And the second step to smooth the spike, Jason said well they want to know what the rate is and we don't want the big jump even if we use the ten-year average. If that was a big jump, whatever our – let's calculate our target rent, which would be – in this case I used this as a rate at four percent (inaudible) – not my rate, mine's five or six. And here's a rate at four percent and multiply that times the average. That would be the target rent rate. And then what would that rent total charge have to increase over the next five years to make it a steady climb instead of a sharp increase, and that's what this percentage does. Well, going toward appraised value. Then at Priest Lake –

Voice: Appraiser –

Ms. Wright: Appraiser value, yes. Well, all my data is in one big column where (inaudible). So this – the lot – excuse me – the rent for 2010 is one point – one six point nine percent times this average assessed value, and in 2011 it's the 2010 rent times one point six, and the range is when you take all the lots into consideration, there are some decreases. There aren't any with real significant decreases. I think seven over ten percent. And then in year 2015, you'd have to use assessed values and again calculate your target rate and the process starts over again. So there's two ways to smooth it. Ten year rolling average – multiply ten year rolling average times the rate, and then if that number is greater than the 2009 rent, then it gradually goes up. If it goes down, it just goes down. (inaudible) And so –

Jason, do you have any clarification.

Mr. Hancock: I'll go ahead and hand this one sheet out. Just hand it around. Thank you.

This essentially is doing what Jane has done, but just looking at it in the aggregate for each of the three categories, you can kind of see what the average changes would be at these different benchmarks – for Payette lakefront, Payette secondary, Priest – and as Jane said, what essentially it's trying to do is it looks at the last ten years of values and derives the average for the last ten years and then applies a rate. And I've got four different rates shown here so you

can see what some of those different benchmarks look like. There's – the first box is at four percent, then three point seven five, three point five then three. You can see what those benchmarks are.

Now what you do once you have that trailing ten-year average value, you apply that percent to it and that establishes your target rent that you plan on reaching in five years. And then you calculate what kind of a percentage change in how much rent is being paid needs to be made each year in order to hit that target in five years. And then in five years, you go back and do the same exercise again. You look at – at that point – the ten most recent years of value, multiply it against whichever chosen benchmark you have here, three to four percent, and then that is your target rent for five years forward from there. And you calculate what kind of a percentage increase or decrease you need to impose each year in the amount of rent paid in order to hit that target in five years. So it's the same percentage change for each of those five years that gets you to that target. You can see that under a four percent benchmark the average Payette lakefront would be a three point two percent increase each year for the next five years, for Payette secondary ten point four, Priest five point eight. That ranges down if you go as low as the three percent benchmark to a minus two point six percent per year at Payette lakefront, four point two Payette secondary, minus zero point one for Priest.

So those were kind of the benchmarks that we looked at here, and then there were some other discussions on premium rent, which is not really covered in this. But I wanted to kind of get that methodology out there.

Mr. Lempesis: Where does this number come from? The top number that shows the current 09 values.

We just –

Mr. Hancock: Believe that's the current amount of rent being paid.

Mr. Morse: The 2-5-37-7-91?

Mr. Lempesis: With the freeze in effect?

Mr. Hancock: Correct. That's what's being paid right now.

Mr. Bridges: If I could ask, where did you get your benchmarks from?

Mr. Hancock: You mean the three, three and a half, three point seven five, four?

Mr. Bridges: Right.

Mr. Hancock: They were just mock up numbers.

Mr. Bridges: So there's nothing based on the market to determine that.

725 **Mr. Hancock:** No. This was just to try and create a methodology to put whatever percentage you want
726 as a benchmark against this model and then it will crank out your increases or decreases.
727
728 **Mr. Bridges:** But it's just an arbitrary selection of a number.
729
730 **Mr. Hancock:** Yeah. I just wanted to show a range with some numbers. You know, the main thing was
731 to show how the methodology would work.
732
733 **Secretary of State Ysursa:** Anybody have other comments about that?
734
735 **Mr. Hancock:** It would give some smoothing. It would give some predictability to kind of see, you know,
736 where you were going to be pointed for the next five years.
737
738 **Mr. Bridges:** Mr. Secretary, I have some comments. I wanted to get the question out –
739
740 **Secretary of State Ysursa:** Well, the question – yeah, your question is a very good question. Where'd
741 we pull these numbers out of the hat between three and four. You may have noticed that some
742 of the revenue – about three and a half – is right about what we're getting now in value. I, as
743 one member of the subcommittee, am not going to recommend to the State Land Board that we
744 go up and significantly reduce the income we're getting out of cottage sites after a two-year
745 freeze in Payette and a one-year freeze in Priest. That's just the lay of the land. And everybody
746 wants to say, well, where'd you pull the number out of the hat. Where'd you pull the number

747 out of the hat on the freeze as far as the appraisers' methodology. I'd like to use three as the
748 ceiling and 1.75 as the floor. Why would I want to do that? Because that gets us about the
749 same amount of money we're getting now. But you can do anything you want with your figures.
750 And I am not, and I don't think it's our article 9, section 8 duty as Land Board members to meet
751 our trust responsibilities to be recommending to the State Land Board that we ought to
752 significantly reduce our $4.3 million we get off cottage site leases. That is not going to happen.
753
754 **Mr. Bridges:** If I may, Mr. Secretary, I think – and back in October 06 I said the same thing to this
755 subcommittee that I understand constitutional law and constitutional responsibilities and
756 fiduciary responsibilities and I said then, and I will, with all due respect, say it again. I think your
757 fiduciary duty as a Land Board is to fix what's broken. And in that connection there is a – there
758 is statutory law which talks about being market-based and market-driven. And each of these
759 scenarios it appears to me appear to start backwards. Appear to start from a desired result and
760 then come up with some sort of application to get to that desired result when there are three
761 experts who were jointly selected who are using approved methodologies, as I understand it,
762 and all of whom agree with their formula to show that right now the rents are significantly
763 above market. And that market reality, in addition to the legal issues which we can obviously
764 debate, also has to be factually driven because in this marketplace you're going to need lenders.
765 You're going to need lenders who are willing to lend under modified standards after the
766 economic price we've got today where they say this makes market sense because they're going
767 to be lending on it and have a stake in it. And if they don't see that market approach, if they
768 don't see this as being justified by the market, or the ability of their perspective borrowers to

borrow that money, the market's not going to return. And I don't think in this situation it is possible for the state to take what to me would appear to be an arbitrary back-ended position, particularly at the same time when, as I understand it, the state as a tenant is going to its landlords and seeking rent reductions because of the economy, which is what I understand is going on today by the same Department. So I don't think that is – is fairness. We got to the freeze issue as the landlord said, and as you've stated, we got to the freeze issue because continuing with the broken system was going to generate even higher rents than the freeze did and exacerbate that existing problem. It doesn't seem to me that smoothing out a problem fixes the problem. It may lessen the rate of exacerbation, but it doesn't fix it. And I think that's the responsibility of the Land Board. To be fair with the lessee and the lessee to be fair with the state and to pay those market rents.

Secretary of State Ysursa: Well, I respectfully disagree on again getting back into what you think a market rent is versus what I think a market rent is when I know – and I know you want to throw in the cabin sites. You know, at one time, attorneys for both associations were praising the feds. Now it's fun to kick the feds because they don't have any justification for five percent, and they pulled that out of somewhere. And – and they are the model thing to follow and they're in a big mess. I haven't heard you guys praise them lately.

Mr. Lempesis: I have never praised the federal government about anything.

Secretary of State Ysursa: The cabin users' fairness act. Anyway, you raise some valid points. My – my point is – is to the trust and what we've got and where we can't do this in a vacuum. And I just – I just don't think the data we've got – and you did a heck of a job – but the data we got, to me, aren't comparables. Am I – am I – did I create – it was very discouraging in the last meeting, but you guys wanted to plow ahead and fine. And I think you did a good job. But, well, we don't have data. You don't have anything comparing the waterfront rents in Payette at all. You've got a line well it might or might not go. And I know. And to give you credence on that, and to recognize, well, we need more data, we need more data. You've got other governmental entities. That's what people looked at before. Who has leases like ours. Well, the federal government has them, and they're charging 5%, right. (inaudible)

Mr. Lempesis: Substantially different valuation process.

Secretary of State Ysursa: And a very different bundle of rights.

Mr. Lempesis: Yes.

Secretary of State Ysursa: Much less of a bundle of rights than the state lessee holders have.

Mr. Lempesis: That's why their values are substantially less.

Secretary of State Ysursa: Granted. And they're not.

812

813 **Mr. Lempesis:** Okay.

814

815 **Secretary of State Ysursa:** And we can get into that but – and we have our – a neighboring state of
816 Montana, who's sole Supreme Court told them that three and a half was too low, you better go
817 to five of market value. So those are some things that we're looking at. We have a fellow
818 agency, who I'm sure has an attorney here listening in this and an association – you never seem
819 to mention Heyburn in front of us, Chuck, but that's okay. It's a different client. What's going
820 on there? And – everybody's on punting and holding.

821

822 **Mr. Lempesis:** Heyburn? They just arbitrarily reduced the valuations that Scot Auble did, Auble and
823 Associates, probably one of the most respected appraisers in the –

824

825 **Secretary of State Ysursa:** Twenty percent.

826

827 **Mr. Lempesis:** By twenty percent.

828

829 **Secretary of State Ysursa:** Yes, I have that appraisal there.

830

831 **Mr. Lempesis:** So I would say that's telling in and of itself, isn't it? Are we reducing all of ours?

832

833 **Secretary of State Ysursa:** Is there – we'll go to five percent. Reduce them.

Mr. Lempesis: Well, they – have they decided to go to five percent?

Secretary of State Ysursa: Well, last time I heard, I don't know where they are, and that's probably irrelevant. But they, as a governmental entity, were going to five. They have five now. I think they're looking at that, taking it under advisement. Correct?

Mr. Lempesis: That is very correct.

Secretary of State Ysursa: Don't ever ask the question you ought to know the answer to. That's why you asked it.

Mr. Lempesis: Well, we went to school (inaudible) –

Secretary of State Ysursa: So I agree. You know, everything is what – you know, what – where we're coming from. Two and a half percent of appraised value right now. The methodology the appraisers – we said we're hung up on that. I think we are getting some sort – any type of plan we would have would use assessed values – appraised values, assessed values, whatever you want to call them, but by the county assessor, which means we'd have a statutory change for Priest Lake. We also would have a built-in appeals process that that affords folks. Folks in Payette wouldn't think that's much of an appeal process, but it is there.

The number one concern to me was to be fair. And to get rid of the spikes and the rapid escalations that were going out of sight. I think that's where we're headed to. Having said that, it's not a monologue here, please chime in, Tom, on your observations.

Superintendent Luna: Well, I want to respond to the gentleman's comments about trying to smooth out a problem doesn't make a problem go away. I guess that was what I suspected we were trying to address all along was the fact that there was no – there was no predictability. Because if it's a broke system, it seemed to be working just fine until, you know, you know, the market went crazy up one year and down the next. And it was my feeling when we had people before us is they weren't complaining about the methodology, they were complaining about spikes in the, you know, that they couldn't afford these ridiculous increases, and I agreed with them. So I don't think you're ever going to be able to create a situation where it's a truly market-driven system because you have this weird relationship between government and private. You know, the government owns the land, and the owner does the leaseholder improvements. And so my comment is – is that's been my goal – is to find an acceptable plan that creates some stability and predictability in what these increases will be every year. I don't know if it's four percent or three percent. Like Jason said, you can plug any percent you want into this model and it will show you the results, but that's what I'm trying to find is an acceptable way of smoothing this out.

Mr. Bridges: If I could just respond for moment, Mr. Superintendent, those clearly – and – those were clearly two elements of the problem, but not the complete problem. And the complete problem

is we're at rates that bear – at total rates that bear no reality to the marketplace. And it's one thing to say, you know what, I'm going to take something that's worth – for purposes of illustration – a thousand dollars, and I'm going to charge you ten thousand dollars for it. But I'm going to smooth out your payment structure. It's still ten thousand dollars you're paying, and if that's above the marketplace, the marketplace is not going to buy that product, and that's not going to continue that revenue stream that the trust fund needs. The trust fund assumes, just like the state statute says, that if you have stable leases, that's the stable part, that predictability part, at market rent. Then that's the best way to preserve that money coming into the trust fund. Making it predictable and stable is of prime importance. But what's predictable and stable still has to bear some reality to the marketplace, and I think the appraisers have said in response to the charge they were given, there is a way to do it. It could be done cheaply. We can plug it in, and we can – we can negotiate and talk about the transition and how that fits. But I would ask you as you sit here today, what in 2010 dollars, or 2009 dollars, is five to six percent more than it was in 2007 with this economy. Nothing.

Superintendent Luna: Let me push back just a bit. Because you can do all the appraisals and assessments you want, but the true value – the true market value is what somebody is willing to pay.

Mr. Bridges: Correct.

899 **Superintendent Luna:** And apparently we had what somebody was willing to pay up until a couple of
900 years ago. That's when the pushback came. And so regardless of all the appraisals and all the
901 assessments and all the announcements, the true value is what somebody is willing to pay.
902 That's the true market value. We've established that, I think, up until a couple of years ago
903 when we had to impose freezes because the cost was greater than the market value. So if we
904 use that as the base, and then use a model like this where you have anticipated increases and
905 it's smoothed out, I don't know how much time and effort we spend to try to determine what
906 the real market value is because the market value is what someone is willing to pay. And I think
907 we established that in with the current model, but then the model showed its flaw when we saw
908 these ridiculous swings in appraised – or assessed value.
909
910 **Mr. Bridges:** But establishing what someone would pay for it in 2006 doesn't establish what someone
911 would pay for it in 2009. In fact the record shows that you can't get 2006 prices now and part of
912 that problem is maybe if in 2006, if the market had remained and we smoothed out these
913 tremendous changes, it would have helped in the ability to pay for it if you truly had something
914 that was going like Tamarack was going and everything else and where we're involved, and that
915 value was there. But no one is paying 2006 prices.
916
917 **Superintendent Luna:** Well, but this – isn't this based on – we froze this for two years.
918

919 **Secretary of State Ysursa:** Well, I think Mr. Bridges, the last time I looked everybody's paying their rent.
920 And that's what Mr. Luna is alluding to. Well, if we were so far out of whack in the last three to
921 four or five years, why are you guys still paying on your rent?
922
923 **Mr. Bridges:** I think we're paying it – I think we're paying it because, among other things, we have
924 improvements on it.
925
926 **Secretary of State Ysursa:** Because you put massive improvements on our land.
927
928 **Mr. Bridges:** We have investments –
929
930 **Secretary of State Ysursa:** That's why you pay it.
931
932 **Mr. Bridges:** – that we would have lost. And because we believe we're here in good faith working with
933 the state to fix a problem for the next thirty-five years. It was with recognition of that problem.
934 We also recognize, as did the state, that two years of freezes wasn't the fix for the problem.
935 That's why we talk about the need to fix it. And that fix is having a system that truly measures
936 that market value as well as predictably and stability and allows us to take care of those
937 fluctuations. And as I sit here now I'm saying there's no market data I'm aware of that shows
938 that anybody is paying 2006 prices for the very same thing today, which is why I say the state is
939 going to people and asking for a rent reduction.
940

941 **Superintendent Luna:** I don't – I don't believe that at all. I think there's plenty of businesses that signed
942 five-year leases in 2005 with annual increases that are eating it because they didn't see this
943 change, but they signed a five year lease. And I'm sure that the property that they're leasing for
944 their businesses has gone down in value, but they're still paying what they agreed to in 2005
945 with annual increases.
946
947 **Mr. Bridges:** All I would say to that is the slides put up there showed that there was at least a – in
948 Canyon County – a fifty or sixty or eighty percent foreclosure rate. Those people aren't paying
949 those rates. They're, in fact, having their business fail. And my understanding from our own
950 membership, who are landlords, is the state is going to people today and saying cut our rent.
951
952 **Secretary of State Ysursa:** I don't know who that is, but it's not – they're not under the endowment
953 principle.
954
955 **Mr. Lempesis:** Let me make a couple of observations. I'm not sure we're way off track here, and I
956 appreciate the very real viewpoints that contest here. I mean that. And I would like to just tell
957 you, and I have hardly ever been a sycophant in terms of our relationship, gentlemen, but I do
958 not doubt for a minute that you have made an extraordinary effort to try to be fair. I believe
959 that. Okay. I don't think you're here wasting your time (tape change). Truly, we believe
960 strongly that comparative rents are the way to go. I don't think we're going to win that war
961 today. But I would ask you to think about this. I am troubled as well by perhaps a lack of
962 comparables, but what I heard Ed say, and what I heard three appraisers say, is I'm not sure we

963 asked them to go out and get every comparable in the world. We asked them to give us a
964 model to show how it would work. But what I did hear him say it's measurable and it's
965 quantifiable, and that's the most important thing, I think, in valuation to the appraisers –
966 measurable and quantifiable. Now moving off that for a minute, I see the biggest rub here
967 twofold. We see the rents that went up, and as the Superintendent said, just skyrocketed. I
968 mean astronomically a couple of years ago because the market was – none of us had ever seen
969 it before, and I'll tell you, we'll never see it again regrettably because we could have made a
970 buck off this deal. But we won't see that again, and we shouldn't see that again. It was out of
971 control. But that is really the data we're working with today. When we start working about –
972 where we're looking at base rents, where we're looking at those valuations, not 2010 valuations
973 when this is going to take effect, which I dare say will be substantially less, that's one problem.
974 The other problem that just compounds this – it's really – it's problematic – is we are in the
975 worst economy we have seen in our lifetime and most things candidly are down. I don't – really
976 I don't know any client I have that's making as much money as they used to or getting the rents
977 they used to if they could rent something out. Now if you do decide to go down this path, and
978 that's – that's what we elect you to do, nobody elected me to do it – is if you go down this path,
979 then I ask you to take those into consideration at least. You can't work from a baseline that
980 began with the astronomical increases we saw, and I would encourage you to look at the
981 economy we're in now. I do like the idea of smoothing this. Always have. I think predictability
982 is job number one. I think that benefits the state, benefits the lessees. But I do hope as you
983 massage these figures in your recommendation, I don't know that you have to start at three, I
984 mean, we're at two and a half now and quite frankly in this economy I would think that's it.

985

986 **Mr. Goodenough:** The economy should be reflected in the valuations of the property, not the
987 appropriate rate of return on the value of the property.

988

989 **Mr. Lempesis:** Well, I do represent the – Chuck – the Heyburn lessees, who I just frankly just got
990 involved with them. I do know that Auble went back and reviewed his appraisal. We were at a
991 hearing a week ago and diminished it just arbitrarily twenty percent without sampling, just said
992 it's gone down dramatically. So –

993

994 **Mr. Goodenough:** We've got an opinion from the Supreme Court of a neighboring state that three and a
995 half was too low and five was – five has since then been okayed. And that's cutting them. They
996 don't have – they don't have premium rent.

997

998 **Mr. Lempesis:** Chuck, you're talking Montana.

999

1000 **Mr. Goodenough:** Yeah, I know.

1001

1002 **Secretary of State Ysursa:** In where we are, I mean, for the record, we're like at one point six eight on
1003 Payette –

1004

1005 **Mr. Lempesis:** Is that what it is.

1006

1007 **Secretary of State Ysursa:** – and we're like two point three at – we've never – Priest has been there.
1008 They weren't this last year because they had a one-year freeze. And eighty-eight percent on
1009 second tier has never been reflected. We know that. We looked at these trying to smooth it
1010 out looking back. Someone mentioned five. Those are the two – you're catching all the
1011 astronomical increases so we went back ten and then redo it every five. We've also been in
1012 close contact with the Valley County assessor. We hope to see – they should have their figures
1013 finalized here any day, which should be going down. The other problem, both in what that
1014 recent appraisal and correction, so to speak, at Heyburn that I was looking at was – what the
1015 assessors are tied in with is that they have access to the assessment coming out right now is as
1016 of January 1st – the values as of January 1st. So the last five months it doesn't – we've seen a real
1017 downward – downward spiral. It's not reflected in some of the assessments we've seen. The
1018 assessments you see now are as of January 1, and it's gone down since then so those are some
1019 of the things we've looked at and considered.
1020
1021 Mr. Leroy.
1022
1023 **Mr. Leroy:** Ben, I understand the position of my client. He has several representatives here today
1024 (inaudible), but we mostly just wanted to listen and kind of then take back your points to our
1025 association and get more directly specific feedback. But I do think it might be useful if – since
1026 we've got association leadership here from both associations – we advise the state of any initial
1027 reactions we have to this methodology structure with both the combination of the ten-year

1028 average and the five year fixing and predicting, as opposed to some of these other rather
1029 unsophisticated caps that we've previously talked about.
1030
1031 My initial reaction is that this is a very unique and quite valuable contribution to this piece of
1032 the puzzle regardless of where you start and regardless of whether you use assessed values or
1033 appraised values or some other kind of combination of values or even the market rent
1034 approach. It seems to me that this combination of those two features in working in tandem
1035 with a proper rate, and with a proper base, are exactly what we had hoped to achieve in terms
1036 of both predictability and a smoothing. I don't know whether you, Chuck, and your people are
1037 in a position to give the state an attaboy on that or whether we want to think about it, but it
1038 seems to me if we can give them some feedback on that, that might be something upon which
1039 we can group.
1040
1041 **Mr. Lempesis:** Our president is here – not President Obama, but our president. And he is our president
1042 as well. You want to go there.
1043
1044 **Secretary of State Ysursa:** We need a bailout, Bud.
1045
1046 **Mr. Lempesis:** The – Bud might even speak to that, but I think I've already said that we would much
1047 prefer comparative market rents as the fair determinate. But, if not, I think the two things you
1048 have to take into consideration are realistic values in 2010 and an equation of the current
1049 economy. Is that a fair statement?

1050

1051 **Mr. Belles:** It's fair.

1052

1053 **Mr. Lempesis:** Or do you want to yell at anybody?

1054

1055 **Mr. Belles:** Well, I don't completely understand the chart that you handed out so I – I'm kind of slow at

1056 some of these things.

1057

1058 **Mr. Lempesis:** Yeah, you're real slow, Bud.

1059

1060 **Mr. Belles:** But I'd like to understand that – (inaudible)

1061

1062 **Mr. Lempesis:** Dumb as a fox.

1063

1064 **Mr. Leroy:** Any Payette reaction? Mike or (inaudible)?

1065

1066 **Secretary of State Ysursa:** Mr. Fery.

1067

1068 **Mr. Fery:** Boy, I – I don't even know where to begin.

1069

1070 **Secretary of State Ysursa:** Keep it short and simple, Mike. Come on.

1071

Mr. Fery: In looking around the table, I think I'm the only one that makes a full-time living in real estate, and to be honest with you, I've never – I can't understand the other methodologies being close frankly. Stable leases at market rent – I disagree and I respectfully on – you know, if you keep paying your payment that means you accept the rent and that's market rent. In an apartment, you move into an apartment, you don't like the rent, you move out. When you build –

Superintendent Luna: Not if you sign a long-term lease you don't.

Mr. Fery: At the end of that six months or whatever or a year –

Superintendent Luna: Well, that's not long term.

Mr. Fery: But that's – but that's the term of the lease. And that's the –

Superintendent Luna: Well, why don't they tell other people renting apartments?

Mr. Fery: What's that?

Superintendent Luna: I don't think we're talking about people renting apartments for three to six months.

1093 **Mr. Fery:** Well, my point is that when you rent an apartment and you don't like the rent, you move out
1094 at the end of the term. In this case, it's different. You say you're unhappy with it and you try to
1095 sell it, you're basically walking away from a lot of the improvements. I mean, or you stop
1096 making your payment – what happens to my cabin. I mean, it's – it's a duress situation. It is not
1097 an arms-length negotiation.
1098
1099 **Secretary of State Ysursa:** We wouldn't tear yours down. I guarantee it.
1100
1101 **Mr. Fery:** Well, whatever it's going to be, but that's –
1102
1103 **Mr. Goodenough:** It's a self-imposed duress.
1104
1105 **Mr. Fery:** Or it could be a taking.
1106
1107 **Mr. Goodenough:** I don't know.
1108
1109 **Mr. Fery:** There's a lot of ways to look at that. But the point is that the methodologies being proposed
1110 are methodologies that I use every day in three different lines of real estate-oriented
1111 businesses. And so I guess – I'm sitting here thinking, gosh, what's wrong with Ed, what's wrong
1112 with, you know, Stan Moe, your own appraiser, your hired party, and Joe Corlett. Three experts
1113 come up with a methodology, which is tough for three guys to agree on anything, and they
1114 come up with a methodology. Again, a methodology is not an exact science for every single lot.

1115

1116 They developed this methodology and then we're just going to throw it out the door because
1117 we don't like the rent. Well, I'll be real honest with you, the state has come to us as landlord
1118 saying cut your rent, cut your rent, cut your rent. And I can tell you a dozen other developers in
1119 town they've asked, they've come back and said cut your rent. They're in long-term contracts,
1120 but they can also pull the trigger with an appropriations clause and say, you know what, I'm
1121 leaving because we didn't get the appropriations for X agency or Y agency.

1122

1123 The point is that I have not seen anyone present real statistical data based on an MAI or
1124 whatever, and all I've seen is more revenues dropping. My revenue is dropping in my business.
1125 I don't like it either. Yours is too and I feel for you. But the point is it's not market. I mean
1126 we've developed a market-oriented system. Let's use it.

1127

1128 **Secretary of State Ysursa:** Now, again, I guess my comment on that, when I keep hearing market, I keep
1129 hearing this and the same people – we were here – the folks that threw that term out – there
1130 was actually – well, it was written with a lot of help from lessees back in 1990. And then two
1131 and a half was chosen, which was frankly a low figure because of a – in 81 we decided to put in
1132 premium rent to kind of soften the fact that two and a half was lower than any governmental
1133 entity around that leased similar property. I guess I get back to my basic point. I don't think
1134 they're comparable properties we're talking about and comparable lease terms and comparable
1135 situation. And that's the basic number one premise of any appraisal. That is my basic problem
1136 from day one on this that I was trying to discourage last time, but you've done a heck of a lot of

work, and it needed to be vetted and out on the table. And I just respectfully disagree that what we've seen are comparables to our situation and maybe we asked for an impossible task.

That's where I am on the scenario. And you know what we did look at. I mean it's tough. They were given a tough task. They've come up with it. I applaud them for their methodology as far as – but I just don't think we're in the same boat with the seventeen properties or whatever you looked at and plugged in. I just don't think they're comparable. We had one lot, I think the closest you came to anything on the waterfront was taking a Coeur d'Alene lot or something that was – had five – leased for five thousand a month or something up there, and you know it's tough because Lord knows if everybody had to do it over again, these things allowed these wonderful improvements on somebody else's property. It's – we're in a unique situation – a governmental situation – and that's what we're struggling with, and we really are trying to be fair, and that's the number one.

And are there any other comments from anyone about where we are.

Go ahead, Bud.

Mr. Belles: I have a question for you. What would be a comparable that you would say is fair. Is it something that we – just plain doesn't exist?

1158 **Secretary of State Ysursa:** Well, that's a good question, Bud. I guess from my simplistic world looking at
1159 what other governmental entities do, and we already know what they do, how many other
1160 entities are out there leasing property that somebody else has built improvements on. There's
1161 not a lot of those. And maybe I –
1162
1163 **Mr. Belles:** Does it have to be waterfront?
1164
1165 **Secretary of State Ysursa:** No, or secondary or around the lake.
1166
1167 **Mr. Belles:** It has to be somewhere around the lake.
1168
1169 **Secretary of State Ysursa:** Well, I'm big on comparables. And then I – did we do – is it an impossible
1170 task? It may have been. But the appraisers wanted to get together, and there was an
1171 agreement and Tom and I indicated that we were willing to look at it – willing to consider it.
1172 Were we going to buy off on it? We never made that promise. And here we are. You've come
1173 up with your methodology. We vetted it pretty well I think. We've – not just in this meeting – it
1174 was out on – and I appreciate that you're meeting kind of our deadline of April 15th, and we've
1175 looked at it and looked at it and looked at it. And you know are the lots going up questions and
1176 whatever, but that's just where I am. I just do not think they're comparable to the scenario that
1177 we're in. And, you know, we're removing – we recognized your plight. We took the legislation.
1178 You recommended, I think Mr. Fery and others, we need longer term leases. We turned around
1179 and ran legislation to get up to thirty-five years, and we're trying – we're trying to help here and

1180 we agree and, you know, 10(a) and notwithstanding possible – no, I won't go there on the
1181 Constitution and that.
1182
1183 There aren't any conflicts allowed. You pay your rent, you're going to be there. The state
1184 doesn't have a history of doing a lot one way or the other but detrimental at being that tough a
1185 landlord that people this and that. You know we haven't even talked about lease terms because
1186 I don't think that's the guts of what we're talking – of where we have to go. But I'm just stuck
1187 on the fact I, in my heart of hearts, and I respectfully disagree that these are comparable.
1188
1189 Yes, sir.
1190
1191 **Mr. Christensen:** You mentioned – my name is Denny Christensen – you mentioned that maybe the only
1192 comparables might be those that we've gotten or that you know about from other states, i.e.,
1193 the five percent and experience in Montana. But it could be the reason there aren't any
1194 comparables is because this methodology that our appraisers came up with has not been
1195 available until now. They're probably pulling numbers out of the hat just like the State of Idaho
1196 is and so we're really not getting anywhere. So what we have now is – since there aren't any
1197 comparables, well, what are you left with. We have a viable model presented by these
1198 appraisers that they all agree on. If there aren't any comparables, there aren't any
1199 comparables. Nothing is going to change it. And perhaps this model that our appraisers have
1200 come up with, the state's and the lakes', is the model that could be used for other states and
1201 other entities. Maybe it's the correct one.

1202

1203 **Secretary of State Ysursa:** Now that's – we want to be trail blazers on this but, no, you raise a good
1204 point. But again, I just – you heard me, I don't want to say it for the tenth time where I am.

1205

1206 **Mr. Hurst:** The problem I have with the methodology that the appraisers came up with is they – they
1207 made a good argument for typical rents and for regression rates, but then they come back and
1208 say but this doesn't – this is a different situation. Now when you look at the chart that they
1209 came up with, it looks like it's almost an inverse bell curve. Anything going above eight hundred
1210 thousand dollars – is it going to continue to go up? But they're making the assumption that no,
1211 it's going to continue to go down, and I don't – I don't think there's enough data there to show
1212 that their regression rate analysis actually fits this property and this situation.

1213

1214 **Mr. Morse:** One – in response to that, I think we've said routinely the data selected was to show the
1215 viability of the model, not to determine ultimately what those factors would be. And both
1216 additional rental research and additional value inputs are going to be needed to employ it. I
1217 think all three of us felt that we were charged not with doing the final project, but with doing
1218 the research necessary to show how it would work.

1219

1220 **Mr. Hurst:** I agree with that. But what I'm also hearing from some people around the table is that
1221 they're putting everything on this saying that this does work and it doesn't necessarily – doesn't
1222 necessarily work without, like you said, additional information.

1223

1224 **Mr. Morse:** If the question is whether when you get out here rates come up, which – which would tend
1225 to defy logic, but if that's where the market is, that's what the rental rate's got to reflect. And
1226 so since it's a market-derived method, whatever that market is, it needs to be reflected in the
1227 model. None of us would disagree with that.
1228
1229 **Mr. Hurst:** Okay. But I just don't think – I haven't seen enough evidence and I've heard – I've read the
1230 report and listened to you talk about it. You talked about that regression analysis rates, and
1231 then you come back and say but this doesn't apply to normal rental property. We have a
1232 different situation. We have – you don't walk away from it, and there's – I just – it's good, but I
1233 don't think it applies a hundred percent to what we're doing to this lakefront property. So I
1234 think there's still a problem with that.
1235
1236 **Mr. Morse:** Well, I – may I respond to him.
1237
1238 **Secretary of State** Ysursa: Yes.
1239
1240 **Mr. Morse:** I think the comments about this is a different market relates to the comments about
1241 nobody's walking away from their leases. If the current lessees have huge investments in the
1242 improvements in these leases, it's unlike the house rental situation that you rent a house and if
1243 you don't like the rent, you can simply pack up your furniture and move at the end of the lease.
1244 These people have hundreds of thousands of dollars in improvements invested on their
1245 leasehold, and that's the reason why they're not walking away from these things.

1246

1247 **Mr. Hurst:** I agree with that.

1248

1249 **Mr. Morse:** And that's why the issue of rent – market rent on the land – is separate and apart from the
1250 sale of the leasehold properties themselves that are improved, something that apparently the
1251 staff doesn't fully understand. The issue of rent to the land has got to be measured typically by
1252 what land rental rate, comparable rate information, would indicate would be the rental rate.

1253

1254 **Mr. Hurst:** I agree with that. And I again go back to what the Secretary has said is that we don't have
1255 comparable rental rate value information. And you said that in your presentation that we don't
1256 have comparables.

1257

1258 **Mr. Morse:** I said that the nature of this product, the unimproved lakefront land, is inefficient, and it's
1259 unique and that – part of the nature of that is we've got un-subdivided – at Priest Lake we've
1260 got un-subdivided and improved lots.

1261

1262 **Secretary of State Ysursa:** We knew you'd talk about your plat – we knew you'd go there, Mr. Morse.

1263

1264 **Mr. Lempesis:** Will you talk about one?

1265

1266 **Secretary of State Ysursa:** True. Aren't we all predictable? That's the only thing predictable. Has
1267 anybody ever explored should there be a premium – not on the ten percent – but a premium

1268 paid on the regular rent because you have the ability – you have all those rights that normal
1269 lessees don't. You have the ability to put McMansions on our property. Maybe you ought to be
1270 paying a lot more than you're paying now. Anybody explore that avenue?
1271
1272 **Mr. Lempesis:** Tax and spend.
1273
1274 **Secretary of State Ysursa:** Of course not. That wasn't your charge.
1275
1276 **Mr. Lempesis:** Tax and spend. Tax and spend.
1277
1278 **Secretary of State Ysursa:** Of course not. That wasn't your charge. Should there be? I mean, these are
1279 unique. Shouldn't there be a special premium paid to rent property and then have the ability to
1280 almost into perpetuity use it, put your own McMansion on it?
1281
1282 **Mr. Boyd:** (tape change) - be a lower rate for land only.
1283
1284 **Secretary of State Ysursa:** You personally had it?
1285
1286 **Mr. Boyd:** No, but I did talk to the Vice President of Steward Development, and he's signed hundreds of
1287 leases over the last twenty some years. He's worked with Albertson's and Supervalu and I
1288 talked him through these comparable issues and about land only versus improved and about,
1289 you know, just these different issues that are coming up. Actually I had two conversations. I

1290 had one where he actually thought it was a work project, so I might get in trouble for that one,
1291 and he gave me some answers and then I took those back and I talked to him the next week and
1292 I said listen, this wasn't for work, this was for this project. Do your answers change and he said
1293 no. It's economic fact. It doesn't change. So –
1294
1295 **Secretary of State Ysursa:** Well, we're getting no where fast. We ought to move on. We –
1296
1297 Tom, what do you want to do on the – do you want to move on the agenda or do you want to
1298 listen to Mr. Bridges lecture us.
1299
1300 Go ahead, Drew.
1301
1302 **Mr. Bridges:** I hope not to lecture you but –
1303
1304 **Secretary of State Ysursa:** How about a minute.
1305
1306 **Mr. Bridges:** Very well. I do notice one fact. If I hit the numbers right on my Blackberry, and that is on
1307 the new cottage site lease methodology that you handed out, if I go to the bottom box and I add
1308 the three numbers on the bottom –
1309
1310 **Superintendent Luna:** Are you talking about the three percent?
1311

1312 **Mr. Bridges:** Yeah. Million three sixty-one, two eighteen – two hundred and eighteen thousand, two
1313 million five twenty-five, and I compare that to what the appraisers say the market rent is
1314 according to their study, we're at a two hundred and forty thousand dollar difference with that
1315 chart. And all I would ask you is to consider I think the rest of the world recognizes whether
1316 there may not be exact comps, Mr. Secretary, and while I would tend to disagree with you, there
1317 is some science to that methodology. And for us to be here, at least on the bottom box, with a
1318 two hundred and thirty-nine thousand one hundred thirty-six dollar difference, I would like to
1319 think that at the end of the day that's something in good faith that we can negotiate with some
1320 science to back it up to use on thirty-five years going forward rather than relying on, with all due
1321 respect, we don't like the answer, so let's work backwards and find another problem. If we can
1322 get there coincidentally by adding two hundred and forty-thousand dollars difference, then let's
1323 negotiate over that difference and rely on the science going forward. That's all.
1324
1325 **Secretary of State Ysursa:** Well, I think that's a good point. You just proved the points you've criticized
1326 that you took the figure that was the closest to your desired result that you have been
1327 complaining about.
1328
1329 **Mr. Bridges:** And I did that for illustration purposes to show that at the end of the day every once in a
1330 while –
1331
1332 **Secretary of State Ysursa:** And where is that box on the Payette Lake?
1333

1334 **Mr. Bridges:** – a blind squirrel finds an acorn. I mean –

1335

1336 **Secretary of State Ysursa:** Where is that box on Payette Lake?

1337

1338 **Mr. Bridges:** Which box on Payette Lake?

1339

1340 **Secretary of State Ysursa:** Well, I don't know. You're telling me the boxes –

1341

1342 **Mr. Bridges:** The box right here at the bottom. It says, if I understand it, Payette lakefront is the first

1343 column.

1344

1345 **Secretary of State Ysursa:** Oh, right here.

1346

1347 **Mr. Bridges:** Payette secondary is the second. This is the state's exhibit.

1348

1349 **Secretary of State Ysursa:** All right.

1350

1351 **Mr. Bridges:** Priest is the third column, and if I add those up and subtract them from what the appraisers

1352 said was the current value of the market rent, $3,865,014, that's our difference - $240,000.

1353

1354 **Secretary of State Ysursa:** How about getting the appraisers' methodology report, and I'm looking on

1355 page three and you run your Blackberry on a figure.

1356

1357 **Mr. Bridges:** Okay.

1358

1359 **Secretary of State Ysursa:** On Payette – on scheduled rent, market rent, difference and tell me what the

1360 percentage is if we're going to look at boxes and compare.

1361

1362 **Mr. Bridges:** Okay. Which ones did you want me to add?

1363

1364 **Secretary of State Ysursa:** Well, you've got scheduled rent on Payette, two million six hundred –

1365

1366 **Mr. Bridges:** Right.

1367

1368 **Secretary of State Ysursa:** Market rent, one point four, difference – twelve percent difference, wouldn't

1369 be – wouldn't be the twelve over the twenty-six –

1370

1371 **Mr. Bridges:** Show the difference?

1372

1373 **Secretary of State Ysursa:** Yeah. That far right column.

1374

1375 **Mr. Bridges:** You're asking me to verify that they're correct that that goes down 39.2%? Is that what

1376 you're asking me to do?

1377

1378 **Secretary of State Ysursa:** No, I'm just curious about that figure.

1379

1380 **Mr. Bridges:** Okay. So –

1381

1382 **Secretary of State Ysursa:** While we do that, let's move on because (inaudible). I'd like to get out of

1383 here before the next lease is up.

1384

1385 Go ahead, Bud.

1386

1387 **Mr. Belles:** Just on a personal point, when I saw the report, I thought I don't like this. But then I – then I

1388 understood what he had done and put in there and I made it very personal. I looked at my lot.

1389 It was very similar to what I'm paying now. This tells me that there's some value to the

1390 technique. It's not perfected like Ed has said. It needs to be refined and –

1391

1392 **Superintendent Luna:** Are you talking about this paper here?

1393

1394 **Mr. Belles:** No.

1395

1396 **Multiple Voices:** (inaudible)

1397

1398 **Mr. Belles:** My personal lot would be about the same.

1399

Secretary of State Ysursa: Pardon me?

Mr. Belles: My lot would be about the same rent. I think that needs to have some – and I think most people's lots rent will be about the same or way different than market. And the other thing I think is that you guys are going to come out with more money in the future (inaudible) because you know rents are going to go up as values go up, values are going to go down the next year (inaudible). And that's all I've got to say.

Secretary of State Ysursa: Thanks, Bud.

Mr. Bridges: I come up with forty-six (inaudible).

Secretary of State Ysursa: Yeah, so did I, but the appraisers' methodology final figures – Priest Lake, (inaudible) negative – from our current figures, negative three point one percent, Payette waterfront negative forty-one percent and second tier plus one hundred seventy-five percent. On – and we – and I happen to be looking at revenues. That's applying the methodology. And as one Board member, I'm not going there recommending that to the rest of the Land Board. And so we haven't gone off no matter what we might do – I'd like to talk about some other areas before everybody has to leave. And Tom and I – I mean, please run the scenario, Mr. Lempesis, Mr. Leroy, by some folks and we've got to get with it – you knew a little bit about it before.

1422 Let's go to a premium rent discussion. Are we going to keep premium rent or not keep premium
1423 rent? That's the elephant in the room. It does depend on the rate we choose. Any comment? I
1424 know where – I believe the associations want us to get rid of premium rent, period. And we, as
1425 a state, want it there because of our low rate. Again, it's tied into what Tom and I are going to
1426 recommend to the Board, which is up in three so – what's your thought on premium rent?
1427
1428 **Superintendent Luna:** Well, I guess I showed that maybe I hadn't done as much homework as I should of
1429 when I realized today that premium rent was not based on capital gain type of a scenario but it
1430 was on the actual whatever you sold it for regardless of what you bought it for so I had the –
1431
1432 **Secretary of State Ysursa:** (inaudible) Well, I think that what Mr. Lempesis raised – and others – is a
1433 valid, I mean, observation. We could look at that.
1434
1435 **Superintendent Luna:** Because in the way it was discussed, it was all this money these people made.
1436 Well, that's, you know, that's not the case. And I don't know how –
1437
1438 **Secretary of State Ysursa:** Well, it's gross versus gross on the state side, too. We didn't take away our
1439 quote, unquote, expenses that we have. But –
1440
1441 **Mr. Lempesis:** What expenses?
1442
1443 **Secretary of State Ysursa:** Well, you guys attributed us at one time thirty percent, didn't you?

1444

1445 **Mr. Lempesis:** (inaudible)

1446

1447 **Secretary of State Ysursa:** But Jane and others – legitimate question about that scenario on the
1448 premium rent. Do you – you probably don't think it's valid, but we could come up with some
1449 scenarios and look at it. We – don't we – do we have to look at what we consider people who
1450 are buying and selling or people who bought and put up or – you tell me. You criticized us.
1451 What scenario do you want us to put down as the cost?

1452

1453 **Mr. Lempesis:** Well, I – my criticism is that I just – and I – it's – in deference to Jane, who did an
1454 admirable job in trying to figure all this mess out, that I just don't want us to be operating off
1455 flawed data whatever it is, and that's what I see.

1456

1457 **Superintendent Luna:** What I'd like to know is what they paid for the land, not what they paid for the
1458 improvements.

1459

1460 **Multiple Voices:** (inaudible)

1461

1462 **Mr. Lempesis:** But that's the same thing. It's the leasehold interest.

1463

1464 **Voice:** Yeah, because they're not selling the land either. They're selling the leasehold so –

1465

1466 **Mr. Lempesis:** Can we drain the swamp – go back to drain the swamp? Make sure everybody knows
1467 because you and I and some of us were regrettably on board back then, but this premium rent
1468 came about as a compromise – I think Kent Hulbert, president of the association back then –
1469 because the state was willing to keep at a two point five percent factor, this was like 92, 91 –
1470
1471 **Secretary of State Ysursa:** Premium rent came into play in 81. We go back, Chuck.
1472
1473 **Mr. Lempesis:** Was it 81?
1474
1475 **Secretary of State Ysursa:** We kept it –
1476
1477 **Mr. Lempesis:** Gosh, I'm getting old, Ben.
1478
1479 **Secretary of State Ysursa:** We kept it in the new lease.
1480
1481 **Mr. Lempesis:** Yeah, okay. That's what it was. But it was a tradeoff for that so –
1482
1483 **Secretary of State Ysursa:** To keep two and a half.
1484
1485 **Mr. Lempesis:** It was a tradeoff for keeping the factor low. So now having said that, one thing that you
1486 might look at, and I would – I think premium – if you're going to increase rents at all, I think

1487 premium rent should go the way of the buffalo. But if you're not going to do that, the real fair
1488 methodology may be in some sort of capital gains or –
1489
1490 **Superintendent Luna:** Buffalo herds have increased huge – is that what you're saying you want?
1491
1492 **Mr. Lempesis:** It's an old saying, you know.
1493
1494 **Secretary of State Ysursa:** I want to get to a rational – and you brought up some good valid points. I
1495 want to get a sampling of the premium rents. We have all the information, don't we, Jane and
1496 Mike? And we – but we don't know what necessarily, you know – walk me through, Chuck, how
1497 you would set out the scenario – the cost. I mean, let's get down to it.
1498
1499 **Mr. Lempesis:** Well, in my analysis, our association –
1500
1501 **Secretary of State Ysursa:** Of ten sales in –
1502
1503 **Mr. Lempesis:** Our association has not made that analysis, but my point today is simply this. Someone
1504 pays X number of dollars. There was a lady here who was the classic example –
1505
1506 **Secretary of State Ysursa:** Lauren Macey probably.
1507

1508 **Mr. Lempesis:** Is that her name? And they had just paid like four or five hundred grand for a leasehold
1509 interest, and so if she were to sell that today for what she had into it, and particularly given if
1510 rents increase or we don't resolve this phase of it, and she goes out and sells it for the same that
1511 she paid for it, if she's lucky enough to do that in today's market, she'd pay forty-five grand to
1512 the state, and she'd take a hit for forty-five grand effectively, plus costs to keep it right. So the –
1513 it would seem to me that the denominator is the leasehold interest. You're not paying – you
1514 pay for the improvements separately, right. (inaudible) so that goes there. And then so if
1515 you're paying two hundred thousand dollars for a leasehold interest, that's for the right to own
1516 the lease, which is what the premium rent is based upon. So wouldn't that be the (inaudible) –
1517
1518 **Secretary of State Ysursa:** And if, in fact –
1519
1520 **Mr. Goodenough:** Do we want to guarantee these people's investments and other contents or just the
1521 investment in the leasehold –
1522
1523 **Voice:** You're not guaranteeing (inaudible) –
1524
1525 **Mr. Fery:** But you only tax gain – I mean, in this context we're taxing gain.
1526
1527 **Mr. Goodenough:** We're not taxing.
1528
1529 **Mr. Fery:** But you are.

1530

1531 **Mr. Boyd:** Chuck, you want to do what the market (inaudible). You don't want the government to

1532 interfere. You want –

1533

1534 **Mr. Goodenough:** I want the endowments to receive market rent.

1535

1536 **Multiple Voices:** (inaudible)

1537

1538 **Secretary of State Ysursa:** We're interfering big time.

1539

1540 **Mr. Boyd:** Yeah.

1541

1542 **Secretary of State Ysursa:** Mr. Fery.

1543

1544 **Mr. Fery:** In – I guess the folks that deal with land leases, I have seven different land leases from Port of

1545 Portland to JR Simplot Company and I can go on, I'm sure you've looked at a lot of land leases.

1546 I'm sure you've looked at a lot of land leases. Setting aside these cottage sites, do you – can you

1547 name one lease that has premium rent? I know the answer is no because I've never heard of

1548 that. I mean, it's never –

1549

1550 **Secretary of State Ysursa:** Well, can you name me one lease that builds on somebody else's property?

1551

1552 **Multiple Voices:** (inaudible)

1553

1554 **Secretary of State Ysursa:** And own it for thirty-five years?

1555

1556 **Multiple Voices:** (inaudible)

1557

1558 **Mr. Morse:** It's not that uncommon. But that's different from your recreational leases.

1559

1560 **Mr. Goodenough:** And I'm sure the Port of Lewiston is waterfront.

1561

1562 **Mr. Fery:** Actually, it's not the Port of Lewiston. That's an independent party. The JR Simplot Company

1563 is actually in McCall. It was negotiated two years ago.

1564

1565 **Mr. Goodenough:** Well, but if it were the Port of Lewiston, it would be waterfront, but it's not quite the

1566 same waterfront what with the cranes and all that.

1567

1568 **Secretary of State Ysursa:** Well, I want to get to our – we had a premium rent analysis – the –

1569 Mr. Lempesis and I and Mr. Leroy does too, the reason we have premium rent was to quote,

1570 unquote, it was stated if you want to look at all the minutes, which I have ad nauseam, talked

1571 about rewarding the sweat equity of the lessees and a way to justify why we in the State of

1572 Idaho were getting two and a half percent when every other governmental entity was at the

1573 five. And we had studies telling us we should be at six or three and a half or five. That was one

of the main reasons, if not the main reason, we went with premium rent because it's a way to justify why we're sitting and because of the freezes, we were not attaining as we speak two and a half percent of appraised value. And that's why we have premium rent. And then we see an analysis that says gross was twenty-five million for the lessees. Correct? And net – I don't know what. I want to get down to that analysis. If we're all wet, I want to know why and where.

Mr. Lempesis: Well, I think you are all wet on that issue, with all due respect. And I don't know how to make it any clearer. I don't pay – I mean, my business does not operate on gross profit. I wish it would. When you're talking about ten percent, you just can't use those numbers and say the lessees got all this money. They just didn't because they paid something to get the money and then at the time value of the investment to go to (inaudible) and so the basis factor –

Mr. Goodenough: Why – why are people investing in properties in houses that they build on somebody else's land?

Mr. Lempesis: Well, they do everywhere. They do everywhere.

Mr. Fery: Because that's what you're selling.

Multiple Voices: (inaudible)

1595 **Mr. Fery:** That's what you're doing. That's your business. And why are you in this business? That's the
1596 real question.
1597
1598 **Mr. Lempesis:** Yeah, why are you.
1599
1600 **Mr. Fery:** Why are you in this business then? I mean that's the whole point. I mean – I don't know why
1601 you do it. It doesn't make sense.
1602
1603 **Multiple Voices:** (inaudible)
1604
1605 **Secretary of State Ysursa:** Well, but – you know, Josh, you always say that and but for the headache
1606 factor, which I can say this is, massive –
1607
1608 **Mr. Lempesis:** Well, we get to see each other and –
1609
1610 **Secretary of State Ysursa:** But for the headache factor, I haven't heard lately, and I know why, oh, we
1611 could sell this stuff and go out and the endowment investment people would get us all this
1612 money. Well, we're obviously talking about how well they're doing in this economy. But do I
1613 believe, and it's been asked by a citizens' committee and others, do I believe that we will get –
1614 discounting, and maybe that's a huge discount, a headache factor? Is this property going to be
1615 worth more in the future around these lakes that God made, more than another investment out
1616 here? What's going to be more valuable in the future? And that question was asked. And I

1617 happen to think they are. I think the land is. I think the lots are. I might be all wet but the
1618 headache factor of the cost of not – you know, it's all about price. You guys want to pay the
1619 lowest; we want to get the highest. But – and what we're struggling with is, yes, we think
1620 they're more valuable – I think they're more valuable in the future. They're not making that
1621 kind of – they aren't making lakes anymore, hopefully. They had an earthquake there in LA the
1622 other day that that is going to be more valuable in the future, and it's not just today. I'm talking
1623 thirty, forty, fifty years down the road if we have a way to capture that appreciation as a person
1624 under article 9, section 8. How do we capture that appreciation? One of the ways we capture it
1625 is in the – in our premium rent scenario and besides keeping the other rent halfway in the low
1626 and middle end and that's why premium rent came in. You know that and I know that. And it
1627 was a way to charge less on the lower rate, quote, unquote, the two and a half, and yet have a
1628 rational way to explain why you're low there but yes, but, we're going to get – we get ten
1629 percent when they transfer the leasehold. And that's why we have premium rent.
1630
1631 **Mr. Leroy:** Could you go to premium rent on net proceeds instead of gross proceeds?
1632
1633 **Voice:** Sure.
1634
1635 **Voice:** Mr. Secretary, if you –
1636
1637 **Secretary of State Ysursa:** I'd like to explore any methodology on the premium rent, but unless you
1638 quote, unquote, bought one yourself and paid premium rent and kept flipping it or want to flip

1639 it, which – that's what I'm getting at, what's your cost? What's your basis? How much you put
1640 up? We're not talking the improvements. If you were one of the original lessees and passed it
1641 through your family and finally at the end sold it for a profit –
1642
1643 **Mr. Lempesis:** Then you're going to get (inaudible) on that basis.
1644
1645 **Secretary of State Ysursa:** That is –
1646
1647 **Mr. Lempesis:** There's going to be a big (inaudible) –
1648
1649 **Secretary of State Ysursa:** That is a big – and how many of these seventy-eight sales were those? I don't
1650 know. But you assume they all were flippers. I don't.
1651
1652 **Mr. Lempesis:** I didn't assume anything.
1653
1654 **Secretary of State Ysursa:** No, you assumed we have flawed data. How flawed is it.
1655
1656 **Mr. Lempesis:** Well, it is flawed. Well, I guarantee you –
1657
1658 **Secretary of State Ysursa:** That's what I want to find out.
1659
1660 **Mr. Lempesis:** Is there any doubt in your mind that that would be an accurate way (inaudible) –

1661

1662 **Secretary of State Ysursa:** Gross or gross. No.

1663

1664 **Mr. Bridges:** Mr. Secretary –

1665

1666 **Mr. Morse:** It ignores the initial investment –

1667

1668 **Secretary of State Ysursa:** Yes.

1669

1670 **Mr. Bridges:** If I understood you, you said it was put in there to capture the appreciation.

1671

1672 **Secretary of State Ysursa:** It was put in there as a way to justify why we were at two and a half percent.

1673

1674 **Mr. Bridges:** And to capture the appreciation if (inaudible) –

1675

1676 **Secretary of State Ysursa:** Oh, a way to do it. Sort of.

1677

1678 **Mr. Bridges:** Appreciation by definition is only the (inaudible) so it's a net concept and as used, if that
1679 was the intention, it's been used inartfully because it's been on the gross. Because appreciation
1680 – and no one is guaranteeing it, Chuck – if there's no appreciation, if you bought the lease and
1681 you made it on that transaction, if I bought a lease for two hundred thousand dollars, okay, and
1682 that was the value you would get under the present scenario of twenty thousand dollars, so

1683 you've made it on that transaction. If I sell it and I sell it and it's only worth a hundred and
1684 eighty thousand, I haven't made anything. As it reads right now, you (inaudible) another
1685 eighteen thousand dollars yet I've lost twenty thousand dollars on that appreciation. On the flip
1686 side, if I bought it for that two hundred and sold it ten years out for three hundred, if the plan
1687 was to capture appreciation, we don't think it should be there at all but if it's appreciation, it
1688 should be whatever the rate is on the – that hundred thousand dollar increase. That net
1689 increase. Assuming your basis is only your cost of the lease that there's not something else that
1690 gets put in there.
1691
1692 **Mr. Lempesis:** We will get you a position paper within ten days on what the association's position is on
1693 premium rent – just some scenarios. Is that a fair way to approach it?
1694
1695 **Secretary of State Ysursa:** Yes. And obviously with an analysis of why you think our data was flawed.
1696
1697 **Mr. Lempesis:** You really need more analysis than a –
1698
1699 **Secretary of State Ysursa:** No.
1700
1701 **Mr. Lempesis:** You need more analysis than just (inaudible) –
1702
1703 **Secretary of State Ysursa:** I don't think these seventy-eight people are all flippers.
1704

1705 **Mr. Lempesis:** Oh, well, okay.

1706

1707 **Multiple Voices:** (inaudible)

1708

1709 **Secretary of State Ysursa:** And you assume they are.

1710

1711 **Superintendent Luna:** I don't see how anybody could flip out of that scenario when you have that ten

1712 percent penalty. You'd have to have a ten percent increase before you –

1713

1714 **Mr. Lempesis:** That was also part of the rationale, remember, was to discourage people from flipping it.

1715 You're right.

1716

1717 **Secretary of State Ysursa:** Made a fortune off of it. (inaudible)

1718

1719 **Mr. Leroy:** So that's – the issue of premium rent and the numbers are still open to the Subcommittee –

1720

1721 **Secretary of State Ysursa:** Well, as far as I can see, there were valid concerns raised about the data, and

1722 whatever, and I think we need to take a look at it.

1723

1724 **Mr. Lempesis:** May I – can I make sure that we – I understand what you have said today. Really, could

1725 you go –

1726

1727 **Secretary of State Ysursa:** We're not done yet.

1728

1729 **Mr. Lempesis:** Oh, okay. I'll shush.

1730

1731 **Secretary of State Ysursa:** I hope not. We've got other things to talk about. Notice how I never – we
1732 never get a conclusion on anything. I just keep going to new items. I'm trying to get one where
1733 we could probably agree on – maybe to adjourn. I don't know.

1734

1735 Premium rent discussion, you're going to give us a paper, right.

1736

1737 **Mr. Lempesis:** Yeah, I – that's fair to give to our board. I can't (inaudible) –

1738

1739 **Secretary of State Ysursa:** Well, I – okay. Quickly – we're under time constraints, which gets into my
1740 item six, but item five, lease provisions other than rate.

1741

1742 **Mr. Lempesis:** We've never seen it.

1743

1744 **Secretary of State Ysursa:** We have folks from the AG's office here. Where are we on the rate on the
1745 lease?

1746

1747 **Mr. Follett:** I'm working on a lease that's based on the current lease and modification of that. We're
1748 working on some of the terms, including the assurance, the subleasing and the improvements.

1749 By the end of the week I hope to have a lease that's been vetted internally that we hope to be
1750 able to get out to the folks outside.
1751
1752 **Secretary of State Ysursa:** Make sure when you do get that done, send it to Mr. Lempesis and Mr. Leroy.
1753 They'll get it to their –
1754
1755 **Mr. Lempesis:** With all due respect, that's how we left the meeting last time –
1756
1757 **Secretary of State Ysursa:** I know.
1758
1759 **Mr. Lempesis:** – with an anticipation that –
1760
1761 **Secretary of State Ysursa:** There was some personal tragedies involved.
1762
1763 **Mr. Lempesis:** Then I stand mute on that subject in that case.
1764
1765 **Mr. Bridges:** Will it also address the issues that we raised in the draft we provided?
1766
1767 **Secretary of State Ysursa:** Frankly, we had a lease. We worked from our lease. The way it was going
1768 back and forth on red and white and whatever, I don't – we're using our lease and Bob Follett
1769 will get you a copy of that.
1770

1771 **Mr. Murphy:** If I might comment, Mr. Secretary, we'll put out this lease that Robert and the Department
1772 has been working on. I think that will be an opportunity for you to take a look at that and see
1773 where you have issue with it and that might get to the answer, which is fair given the question
1774 you just asked.
1775
1776 **Mr. Boyd:** Are you going to provide a Word version to redline?
1777
1778 **Secretary of State Ysursa:** And I apologize for some of the delay there, but there is – there were some
1779 other issues.
1780
1781 **Mr. Lempesis:** We all have lives, and we understand if there's a problem there.
1782
1783 **Secretary of State Ysursa:** So we don't need to elaborate too much on that. But anyway, number six, we
1784 get back to where you think what we have accomplished today. Implementation timeline. Until
1785 we agree to something, there's no implementation timeline, I suppose.
1786
1787 I'm having trouble with 58-307, six months notice. Where are we going? We've got leases in
1788 place. I, for one, abhor the thought of going to McCall for a meeting, where we're going by the
1789 way, in June, which I think George ought to be shot for doing that.
1790
1791 **Voice:** Where'd George go?
1792

1793 **Secretary of State Ysursa:** He left –

1794

1795 **Multiple Voices:** (inaudible)

1796

1797 **Secretary of State Ysursa:** I don't plan on wearing my winter parka at that meeting so you folks can ask

1798 for another freeze.

1799

1800 **Mr. Lempesis:** That's bad.

1801

1802 **Secretary of State Ysursa:** That's bad. I know. Trying to put a little levity in this. The – I think there's

1803 still work to do on three and four, and that's the guts. And I don't want to get into another

1804 delay. We have to – we have to give six months notice before any increase, as you –

1805 everybody's all aware. That happens to be July 1st so –

1806

1807 **Mr. Lempesis:** But you could give notice and reserve the right to revisit that, if necessary.

1808

1809 **Secretary of State Ysursa:** We could give notice and reserve the right to decrease anything we said we'd

1810 do, which we've done. You guys seem to know how to do that.

1811

1812 **Mr. Lempesis:** Mr. Secretary, here is – I want to be real straight on this. Here's my concern about what

1813 I've heard today, and it leaves me a little bit – not panicked, but deeply concerned. When we

1814 started this process, nobody agreed to anything other than we all agreed there might be a

1815 better way to do it. There was a better way to build a mouse trap. And we've looked at that
1816 and it's totally in your discretion, or the Board, to examine the proposals made by the appraisers
1817 or not. But when we look at where we really are today, for us as lessees, we're between a rock
1818 and a hard place because in the worst economy in the history of my lifetime, and yours, what
1819 you're really saying is in your analysis today, rents are going up. Okay. That's really what you're
1820 saying. The premium rent is not only probably not going away but may get increased. And
1821 there's absolutely no relief for these people who you froze their rents two years ago because
1822 their rents were so astronomical as to be unconscionable. I mean, balance those for me, if you
1823 will. But do you see what I'm saying? I mean, what we've accomplished is to just say, well, let's
1824 be the only probably government agency in the world, much less the only landlord in the world,
1825 that's going to ask for more money. Is that what you're saying?
1826
1827 **Secretary of State Ysursa:** To say we haven't recognized your plight is another way for me to say what
1828 you said, I put it in my phraseology –
1829
1830 **Mr. Lempesis:** Okay. That's fair.
1831
1832 **Secretary of State Ysursa:** After we have frozen Payette Lake for two years, frozen Priest Lake for one
1833 year –
1834
1835 **Mr. Lempesis:** And we had a fifteen percent-er at Priest.
1836

1837 **Secretary of State Ysursa:** That's chump change compared to what the folks at Payette did to them.

1838

1839 **Mr. Lempesis:** Okay.

1840

1841 **Secretary of State Ysursa:** And then go to the Legislature right off the bat and go to thirty-five years as a
1842 possible lease term, I think we have bent over pretty good for the lessees. And predictability –
1843 what's happening – I'm waiting with great anticipation of what Valley County is going to do on
1844 assessments. I'm also waiting with great anticipation of what Mr. Moe is going to do on
1845 appraisals that are going on right now at Priest Lake. There may be – who knows. I don't –
1846 based on that other person's appraisal on the Heyburn, but again that was a different
1847 timeframe.

1848

1849 So – as far as predictability, we're looking at softening spikes, but as to increases or status quo
1850 or close to it, we are – I am not going to go recommend a decrease after we have in essence
1851 frozen them for two years and then one year. You may say very – I'd love to see some county
1852 assessors face reality and lower some things.

1853

1854 **Mr. Lempesis:** Well, when you – let me just be as blunt as I customarily am in life, are you saying when
1855 you – I heard repeatedly, and I respect, not agree, but respect the position that I'm not going to
1856 go into the Land Board and say we're going to take less money, boys and girls, okay. But what I
1857 haven't heard you say is I'm not going to ask for more, and I – and what I'm hoping to hear, as a
1858 baseline for this discussion after all this, is that we're not going to go to three percent. We're

1859 not going to go to three and a half. We're not going to go to twenty percent premium rent on a
1860 gross factor. Can I hear that from either of you distinguished gentlemen? Is anybody holding
1861 the line for the American citizen today?
1862
1863 **Secretary of State Ysursa:** You're not going to hear that yet.
1864
1865 **Mr. Lempesis:** Okay. I like yet.
1866
1867 **Secretary of State Ysursa:** Because there are some value discussions we need to have and – but we – to
1868 go in and constantly freeze and freeze and freeze just delaying and delay and delay is not an
1869 answer.
1870
1871 **Mr. Lempesis:** We agree.
1872
1873 **Secretary of State Ysursa:** But you'd love to have it frozen. And most likely we'll go into a letter
1874 campaign if we don't, which is fine. I've been around the block.
1875
1876 **Mr. Lempesis:** Well, is your home phone number the same –
1877
1878 **Secretary of State Ysursa:** There's a lot of us in the book but –
1879
1880 **Mr. Lempesis:** And George?

1881

1882 **Director Bacon:** I won't send any letters.

1883

1884 **Secretary of State Ysursa:** Oh, George got back after scheduling our meeting in McCall, you rat.

1885

1886 Yes, sir.

1887

1888 **Mr. Goicoechea:** Mr. Chairman, I think we'll receive just as many calls and letters as we have in the past

1889 along reasonable rate of return for us as the trustees is (inaudible) straight at the end of the day.

1890

1891 **Mr. Lempesis:** I'm going to do a Freedom of Information Act on that tomorrow night and invite you to

1892 tell me how many calls you have ever received in the last ten years about that. Let's do it.

1893

1894 **Mr. Fery:** What is a reasonable rate of return?

1895

1896 **Mr. Goicoechea:** That's my question, Mr. Fery. That's where the question is.

1897

1898 **Mr. Fery:** That'd be perfect. That's where we ought to end it and that'll settle –

1899

1900 **Mr. Goodenough:** Where's this reasonable rate of return come from? That's not the term. The term is

1901 maximum long-term benefit to the endowed institutions.

1902

1903 **Multiple Voices:** (inaudible)

1904

1905 **Mr. Fery:** What is that (inaudible) – give me the percentage? What is that number?

1906

1907 **Secretary of State Ysursa:** Well, currently everybody signed a lease at two and a half percent of

1908 appraised value so – I mean that's what lease we signed, right?

1909

1910 **Mr. Fery:** If the state would derive a two and a half –

1911

1912 **Secretary of State Ysursa:** No, I asked you a question. What lease did you sign, and where are we right

1913 now. Two and a half percent of assessed value, correct?

1914

1915 **Mr. Fery:** Correct.

1916

1917 **Secretary of State Ysursa:** You signed it. We didn't have a gun to your head.

1918

1919 **Mr. Fery:** We're trying to work on a new lease. I understand where we are.

1920

1921 **Secretary of State Ysursa:** I know.

1922

1923 **Mr. Fery:** I'm not going to argue that (inaudible) –

1924

1925 **Secretary of State Ysursa:** Well, but my point is on the timeline –

1926

1927 **Mr. Fery:** The thing is, what's your rate of return (inaudible) – that's – what is that – is it a hundred

1928 percent or ten percent or is it two percent or five percent? What is that number? I mean,

1929 because it's like we're playing, you know, where's the rabbit. I mean, what is – what's the

1930 number? What's –

1931

1932 **Secretary of State Ysursa:** Well, let's go to the methodology of it. Between four and one, I guess.

1933

1934 **Mr. Fery:** Okay.

1935

1936 **Secretary of State Ysursa:** Of what? Of what?

1937

1938 **Mr. Fery:** If the state derives twelve –

1939

1940 **Secretary of State Ysursa:** Of what?

1941

1942 **Mr. Fery:** – of your investment in your property.

1943

1944 **Secretary of State Ysursa:** Of what?

1945

1946 **Mr. Fery:** – which is zero. I mean that doesn't –

1947

1948 **Mr. Lempesis:** Probably Admissions Act.

1949

1950 **Director Bacon:** I think the –

1951

1952 **Secretary of State Ysursa:** Go ahead, George.

1953

1954 **Director Bacon:** – Department's goals for these types of properties, residential leasing, it's between

1955 three and eight (inaudible).

1956

1957 **Secretary of State Ysursa:** Well, the Asset Management Plan is any where from – and you have to

1958 remember half of that in our Asset Management Plan is supposed to be attributed to

1959 appreciation of the asset rather than cash on cash, cash on value.

1960

1961 **Director Bacon:** I understand, but he asked a question and that was kind of a –

1962

1963 **Secretary of State Ysursa:** I think it was three to twelve. And that's in the Asset Management Plan.

1964

1965 **Mr. Fery:** The point is that you can set that, we could –

1966

1967 **Secretary of State Ysursa:** Who set that?

1968

1969 **Mr. Fery:** Well, that your total return is derived three ways. The rent you receive, the premium rent you

1970 get and the appreciation on the property, right?

1971

1972 **Secretary of State Ysursa:** Uh-huh.

1973

1974 **Mr. Fery:** Okay. Just wanted to make sure I understand that.

1975

1976 **Mr. Bridges:** Because you're way above those numbers on that basis. Way above those numbers.

1977 Astronomically above.

1978

1979 **Mr. Fery:** At the present deal.

1980

1981 **Superintendent Luna:** You mean, under this type scenario?

1982

1983 **Mr. Fery:** Oh, that is –

1984

1985 **Mr. Lempesis:** That's even more.

1986

1987 **Mr. Goodenough:** Because the money was given to us – or the land was given to us by the federal

1988 government?

1989

1990 **Mr. Fery:** No, honest appreciation.

1991

1992 **Secretary of State Ysursa:** Using your way of assessed value – on the assessed value that you guys think

1993 is outrageous?

1994

1995 **Multiple Voices:** (inaudible)

1996

1997 **Mr. Fery:** That's the other thing is I don't know the lease –

1998

1999 **Secretary of State Ysursa:** Well, the problem is, Mike, we can all talk about return and percent of.

2000 You've got to get to what X is. What percent of X?

2001

2002 **Mr. Boyd:** What people are willing to pay in a market.

2003

2004 **Secretary of State Ysursa:** You guys haven't walked. Don't keep saying what you're willing to pay.

2005

2006 **Mr. Fery:** Will you buy my improvements?

2007

2008 **Mr. Goodenough:** Somebody else might, and we will give you the proceeds of that sale. That's –

2009

2010 **Mr. Fery:** I mean I'd love to get out of my improvements so I – if I could do that –

2011

2012 **Secretary of State Ysursa:** I've heard the Gold Coast guys say that so often. I wish you would. We
2013 wouldn't have these headaches.
2014
2015 **Mr. Goodenough:** I mean, that's what the statute says. We'll sell your property and give you the
2016 proceeds.
2017
2018 **Voice:** Will you maximize my return?
2019
2020 **Mr. Goodenough:** And, you know, the line has been very short to undergo that process, and it's not
2021 been voluntary when it did have a line.
2022
2023 **Mr. Bridges:** Mr. Secretary, on behalf of our association with my fellows here, we have been here
2024 throughout asking for – asking for a fix to the problem, not a continuing freeze. We agree with
2025 you there. And I have said repeatedly the fix to the problem is a new lease because that will
2026 allow, Chuck, those who want to exit to exit. They can't exit until a bank is going to finance this
2027 and that's why on top of all the other reasons, legally we could argue about the Constitution and
2028 how that's amplified by the statute, practically speaking at the end of the day we need to be
2029 able to have something that we can take to the bank with a buyer's credit application that's
2030 saleable to the bank. That's going to require the bank to sit there and say that it's worth my
2031 putting this money to build this McMansion or whatever and that's why you're getting that
2032 premium price on the lot because someone wants to do that. I need to be able to show that
2033 that borrower one can predict what the rent is going to be, that his or her income will be able to

2034 pay that rent so he doesn't get foreclosure, with you trying to take the bank's position, so that's
2035 why at the end of the day, the fix needs to be something that we can take to the bank. And that
2036 at the end of the day is going to be that willing buyer and seller. Are they willing to loan and
2037 take a position on that piece of property and banks are going to require something that they can
2038 understand and that replicates the market. And that's why I go back to the realization I made
2039 earlier that a wholly fortuitous matter in my view if we're two hundred and forty thousand
2040 dollars apart from your bottom and what we believe the science says, which I think the banks
2041 will understand, we ought to be able as reasonable people who went to Jesuit schools, to come
2042 to some understanding here and be Jesuitical about this.
2043
2044 **Multiple Voices:** (inaudible)
2045
2046 **Secretary of State Ysursa:** Yes, Mr. Luna.
2047
2048 **Superintendent Luna:** Here's where I think we're at, Ben, is that you're still waiting to see a lease, other
2049 than the rate, the lease provisions other than the rate, and where we want to get from you a
2050 white paper on premium rent discussion.
2051
2052 **Mr. Lempesis:** Yes, sir.
2053

2054 **Superintendent Luna:** So – and it sounds to me like there's a possibility of this scenario not necessarily
2055 because we may – we may fall into something that we can work on and come to an agreement
2056 on because the end result is it will meet the –
2057
2058 **Mr. Bridges:** I'd like to say let's agree on a number if we can fit – it fits the science.
2059
2060 **Superintendent Luna:** Right.
2061
2062 **Mr. Bridges:** – that we can take to the bank.
2063
2064 **Superintendent Luna:** Right. Right. So maybe we're closer than we think. But there's still some more
2065 information that they're waiting to see – you're waiting to see the lease. I'd like to see your
2066 white paper on premium rent and then have further discussions about this rolling, smoothing
2067 proposal that Jason put out before you.
2068
2069 **Secretary of State Ysursa:** Well, I think that's – you're pretty good in capsulization, but let's get moving.
2070 I still have a problem in the timeline and what we're going to accomplish in June. And if we
2071 don't accomplish – we need to really get I think the lease, and, Drew, I don't know what you
2072 wanted in the lease and whatever, I think I saw – what was – I think any landlord, you work with
2073 the landlord's lease. The tenants don't write the lease.
2074
2075 **Mr. Bridges:** And we did it to start the discussion.

2076

2077 **Secretary of State Ysursa:** And the landlord's got to do the lease and if we – Robert, if you can get that

2078 out as quick as you can.

2079

2080 **Mr. Follett:** Yes.

2081

2082 **Superintendent Luna:** That's what I was going to ask you is you said you could have your response to

2083 this premium rent in ten days?

2084

2085 **Mr. Lempesis:** Yes, and I always overstate my case.

2086

2087 **Superintendent Luna:** And how about the lease? How soon can they have the lease?

2088

2089 **Secretary of State Ysursa:** And would they – do you have all the information you need? I think you need

2090 to work with Jane and Mike Murphy. Make sure you work on the – if you need figures –

2091

2092 **Mr. Lempesis:** Appreciate that. We – Ed and I were just wondering about that.

2093

2094 **Secretary of State Ysursa:** You need the figures and make – and the Land Department's got the figures.

2095 You guys probably do, too, but – and go from there. So I mean there's no – don't give

2096 information, whatever. The information's out there. It's public record and whatever. So –

2097

2098 **Mr. Lempesis:** I just think our association needs to poll the board to see where it's headed.

2099

2100 **Secretary of State Ysursa:** You need to talk about it. Tom and I – I think, Tom, I can fairly state that we
2101 are considering, with all due respect, the methodology put forth. We're both – and when we
2102 lean, we lean pretty hard. We're leaning towards a – some sort of a methodology dealing with
2103 ten-year average and –

2104

2105 **Mr. Lempesis:** You mean you're carrying more weight than the other (inaudible)

2106

2107 **Secretary of State Ysursa:** Well, I didn't say that. I could say that. People in glass houses can't. And
2108 Murphy can help us out on that end. So – we're leaning towards the methodology presented by
2109 Jane and Jason. And the number – and we're not – something on, you know, whether it's
2110 something on this sheet or not, it's pretty close to it. So we'll –

2111

2112 **Superintendent Luna:** And then we'll want some more information, Jane, on just the premium rent, how
2113 much they spent –

2114

2115 **Secretary of State Ysursa:** Well, that will all be there. I'm sure - I'm sure the Department is listening to
2116 this and will look at that.

2117

2118 **Voice:** (inaudible)

2119

2120 **Secretary of State Ysursa:** No, it isn't. We all know that's the problem. We're trying to fix something

2121 that should never have been put out as an investment-type thing.

2122

2123 **Mr. Lempesis:** Would you sell us the lots?

2124

2125 **Secretary of State Ysursa:** We can sell the lots. However, we need to go with the – the Constitution

2126 dictates how we sell lots.

2127

2128 **Mr. Lempesis:** Must be another office building you folks want you could go buy.

2129

2130 **Secretary of State Ysursa:** How about – do you want to buy the PUC?

2131

2132 **Mr. Lempesis:** Have you ever looked at Banner Bank?

2133

2134 **Secretary of State Ysursa:** So are we – doing it fast is the key point here, and we'll stay together through

2135 the associations and my office and Chuck –

2136

2137 **Mr. Lempesis:** And Chuck's been very good about communicating seriously with us, and I do appreciate

2138 that. Thank you.

2139

2140 **Secretary of State Ysursa:** Mr. Belles.

2141

2142 **Mr. Belles:** I say still there's some urgency in the lease – is there?

2143

2144 **Voice:** We've got another year to work on that, right.

2145

2146 **Mr. Boyd:** The market is not repaired until the lease is put in place.

2147

2148 **Secretary of State Ysursa:** Well, and I'd like that fleshed out because –

2149

2150 **Mr. Lempesis:** It's part of this.

2151

2152 **Secretary of State Ysursa:** It's part of the whole battle but, you know, we hear urgency here – we quote,
2153 unquote, have a lease now, but we also have provisions in it that people aren't really fond of,
2154 and we're not necessarily that fond of some of them. The guts of this whole thing is price, but
2155 people want to – you know, I've heard – bear with me here for a minute – I've heard various
2156 things. Let's – we get a new lease if we can ever agree on a rate, we tear them up and start
2157 anew. Or do we go and if quote, unquote, we have a different premium rent proposed, right
2158 now it's ten percent. If there is something new proposed, people are going to sign on to the
2159 new one. Are they going to stay with the old one? Well, we'll try to have a fire sale to get the
2160 ten rather than another figure. There are issues about getting a new lease done and out there
2161 and tear up one and whatever. I don't have the answers, Bud.

2162

2163 **Mr. Belles:** In that case, should we –

Secretary of State Ysursa: I mean, I hear from Josh and Drew here that they'd like to have a new lease yesterday.

Mr. Belles: Should we set another meeting so that we can try and get together?

Secretary of State Ysursa: Well, let's take that under advisement that maybe meetings, or on the phone or whatever – getting this many people together every time, it gets a little – it's important, we need to do it, but the next Land Board meeting, besides tomorrow, is in June at – in McCall.

Mr. Bridges: Is that the 16th? Is that the (inaudible) –

Secretary of State Ysursa: But I'd like to try to get some things done, and then if we need to convene a meeting, you know, what recommendations we have for the Board right now, they're not there. We're waiting to hear some other things. And I don't want to delay – delay leads to the freeze and then and then and then we haven't done a damn thing.

Mr. Bridges: We want to move as swiftly as you can.

Mr. Lempesis: We might even move swiftier.

2185 **Secretary of State Ysursa:** More swiftly. Jesuits would have said more swiftly. Thank you and the
2186 discussions got kind of heated, but I appreciate everybody. And really I – we can agree to
2187 disagree, but I appreciate everybody's good faith effort to get this thing cranked out.
2188
2189 **Mr. Lempesis:** Mutual.
2190
2191 **Secretary of State Ysursa:** Thank you very much.
2192
2193 Meeting end 4:15 p.m.

COTTAGE SITE SUBCOMMITTEE MEETING

MAY 18, 2009

SIGN-IN SHEET

1. Dan Goicoechea, Office of the State Controller
2. Sherm Furey, Office of the Attorney General
3. Craig Thompson, Department of Lands
4. Steven Strack, Office of the Attorney General
5. George Bacon, Department of Lands
6. Bonnie Butler, Office of the Governor
7. Mike Fery, Payette Lakes Cabin Owners' Association
8. Josh Boyd, Payette Lakes Cabin Owners' Association
9. Drew Bridges, Payette Lakes Cabin Owners' Association
10. Dave Leroy, Attorney, Payette Lakes Cabin Owners' Association
11. Chuck Goodenough, Office of the Secretary of State
12. Jason Hancock, Office of the Superintendent of Public Instruction
13. Chuck Lempesis, Attorney, Priest Lake State Lessee's Association
14. Ed Morse, Appraiser
15. Tim Hurst, Office of the Secretary of State
16. Mike Murphy, Department of Lands
17. Robert Follett, Deputy Attorney General, Department of Lands
18. Denny Christenson, Priest Lake Lessee

Exhibit 35

Transcript, Agenda Item 10,

Cottage Site 2010 Rent Changes and

Update on Cottage Site Subcommittee,

Land Bd. Meeting

(June 16, 2009)

State Board of Land Commissioners

June 16, 2009

Off-Site Meeting - Idaho First Bank, 475 East Deinhard Lane, McCall

Agenda Item 10: Cottage Site 2010 Rent Changes and Update on Cottage Site Subcommittee

---

Speakers:

- C. L. "Butch" Otter, Governor
- Ben Ysursa, Secretary of State
- Lawrence Wasden, Attorney General
- Donna Jones, Controller
- Tom Luna, Superintendent of Public Instruction
- George Bacon, Director, Department of Lands
- Mike Murphy, Department of Lands
- Charles Lempesis, Priest Lake State Lessees' Association
- Jim Young, Payette Lake Cabin Owners' Association
- Josh Boy, Payette Lakes Cabin Owners' Association
- Drew Bridges, Payette Lakes Cabin Owners' Association

Governor Otter: Mr. Bacon.

Director Bacon: Governor, members of the Board, I draw your attention to tab ten in your books. This subject is the 2010 rent changes for both Payette Lake and Priest Lake cottage sites. I've asked Mike Murphy to come and present this issue. Mike's our bureau chief of our Surface Leasing. And also I know there are representatives from both lakes here who may want to address the Board.

Governor Otter: Mr. Murphy.

Mr. Murphy: Mr. Governor, members of the Board, my name is Mike Murphy, Bureau Chief of Surface and Mineral Resources for the Department of Lands. I am here to present this agenda item related to cottage sites.

As background, and in accordance with the Payette Lake and Priest Lake cottage site leases, the Department is required to provide a hundred and eighty day notice to the lessees regarding any pending rent increases. Normally those increases – those letters of notification – are sent out the first – excuse me, the last week of June in order to meet the July 1st deadline. The actual invoices for those are mailed in November with the first half rent due on January 1st and the second half due on June 1st.

Moving on to the discussion of Payette Lakes' cottage sites, the Payette Lakes' cottage sites – their rent is two and a half percent of the assessed land value as determined by the Valley County Assessor. The Department receives this information annually and applies the rent formula for the forthcoming rental year.

The 2009 assessment data indicates that both the waterfront and secondary lots will decrease five percent from their 2008 assessed values. As you know you, the Land Board froze the rent for 2008 and 2009 for the Payette Lakes' cottage sites based on the dramatic increases from 2007 and 2008. However, those dramatic increases are not significantly decreased by that five percent decrease. In fact if you were to look at the rent, if there were no rent freezes instituted, the actual cottage site rent would be thirty-nine percent higher for waterfront and seventy-eight percent higher for the second tier lots.

Moving on to Priest Lake, the Priest Lake cottage rent is based on two and a half percent of the appraised land value as determined by the Department's appraisal contractor. The appraisals are conducted every five years with an indexing process applied in non-appraisal years. For 2010, it's an appraisal year for sixty of our 354 cottage sites with the 294 remaining to be indexed.

In table – or excuse me – in attachment two you'll find a table that shows the sixty appraisals, the values for those, completed by Columbia Valuation Group. And note that those values are about 7.2% higher than if the indexing process had been applied, and that's something that you would expect in an increasing market that the indexing process would drag slightly below the appraised values.

Based on the information provided by CVG, the indexing percentage for the 295 – excuse me – 294 cottage sites is plus twenty-six percent. This percentage is based on market data from the past five years, and it includes a market decline for 2008 of negative twenty percent. A copy of this report is included in attachment three, and if you were to read that report, you'd note that CVG actually recommended a fifteen percent increase. However, the Department's review of that information indicates that they used a six-year span instead of five. The Department made that adjustment to five years to be consistent with the lease and that yielded a plus twenty-six percent increase.

As you know, the 2009 rent for Priest Lake was frozen by you, the Land Board, in December of last year as a result of the significant increases. At that time CVG had indicated a twenty-three percent increase by indexing was appropriate, however, your action eliminated that increase.

I'd like to move ahead to the recommendation, and I'll circle back to the Land Board Subcommittee information. Based on the information I just provided, and the Land Board's past action to freeze the 2008 and 2009 rent for Payette, the Land Board's action to freeze the 2009 – 2009 rent for Priest Lake, and the significant increases that were a result from the implementation of the 2009 Valley County assessed values and the CVG appraisals and indexing information – based on this information, the Department's recommendation is to have the Land Board leave the 2010 rental rate for all cottage sites at their existing 2009 level.

Circling back to the Land Board Subcommittee, a Land Board Subcommittee was formed in June of 2007 to review alternative methodologies for the two lakes and for all the leases that are set to expire in December of 2010. Since its formation the Subcommittee has met formally with the cottage site lessees on several occasions, most recently on April 22nd of 2009, to research and discuss the following issues: current valuation methodologies; valuation methodologies proposed by the lessee representatives, including a seasonal rental rates; appropriateness of using land values to determine rental rates; buffering land value; market spikes; deferred market valuation approaches; premium rent; subleasing; lessee insurance – insurance requirements; general lease provisions; and current market conditions.

Based on this work the Department anticipates that the Subcommittee will be making a recommendation to the Land Board next month in July regarding a new rent methodology. The methodology will likely include the calculation of an annual rent by multiplying a fixed percentage – anticipated to be somewhere between three and five percent – and multiplying that by the average county assessed land value for the past ten years. This calculation would identify a target rental rate for five years in the future. Rental rates for years one, two, three and four in the future would then be identified by taking the existing rental rate, calculating annual adjustments that would evenly stairstep to the targeted rental rate for year five. The process then would be repeated each five year period.

The percentage which the subcommittee ultimately recommends will be applied to – that will be applied to the average county assessed value from the previous ten years will have a direct impact, and actually an indirect impact, on the percentage of premium rent that the Subcommittee recommends. In other words the more – the higher fixed percents up to five percent would probably cause the premium rent percentage to decline.

With that, I would stand for any questions.

Governor Otter: Questions of this witness.

Secretary of State Ysursa: Mr. Chairman, Mike, thank you for the report, and I know things were a little hectic trying to get the timing, getting the valuations from the – actually it took longer to get the Priest Lake valuations than it did to get the county assessment this year from Valley County.

Governor, totally up to you. We do have representatives from the associations –

Governor Otter: No, I intend to do that.

Secretary of State Ysursa: – here. I was prepared to do a motion. There is an action item in front of us, but we can wait on that if you wish to.

Governor Otter: I would prefer – because once we have a motion before us, then it's pretty much limited to the testimony of the members or questions of the members themselves.

Secretary of State Ysursa: That's why I brought it up.

Governor Otter: Before we make the motion I would invite anybody in the audience that represents the associations, or whatever, to – if you have something that you'd like to say –

Mr. Young.

Mr. Lempesis.

Mr. Lempesis: Governor.

Secretary of State Ysursa: I assume one will speak for Payette?

Mr. Young: If it's okay, Mr. Secretary, I think we have a couple of people that would like to testify.

Governor, members of the Board, Jim Young. I'm the President of the Payette Lake Cabin Owners' Association and appreciate being here once again. And hopefully you won't have to see me too often here, and we can come to a resolution on this – this issue.

First off, I want to thank Secretary Ysursa and Superintendent Luna for their dedication and hard work on the Subcommittee. We appreciate your efforts. I also want to acknowledge the other board members here – Josh Boyd, our numbers guy, and very helpful Drew Bridges, and also Tony Park, former Attorney General, in the audience. There's also many members of the Payette Lake Cabin Owners' Association in attendance here as well as a number of realtors and interested parties on this issue.

Secretary of State Ysursa: We've noticed. I thought they were here for timber issues.

Mr. Young: Well, as you know, this is a hot topic. And this is an important issue that has a rippling effect throughout the entire economy, particularly here in Valley County. And I don't need to tell this Board the grim economic picture, the unemployment rate throughout the state is at a twenty-two year high 7.8%. But particularly hit hard is Valley County and neighboring Adams County with unemployment rates of 10.8 % and Valley County – or at Adams County at 11%. Friends in north Idaho are facing similar situations. And of course the economies here are particularly influenced by the real estate market and, as you all know, the real estate market has been hit particularly hard. It's – one could say it's almost a depression-era crash with properties discounted at forty, fifty and sixty percent of selling prices just a few years ago. Even the coveted lakefront property, the most recent sales we're seeing are about sixty percent of what they were at the peak.

Commercial leases throughout the country and Idaho – we are seeing those leases being renegotiated. There was an article recently about Starbucks renegotiating all their leases at a target of twenty-five percent discount. Even the State of Idaho, who is the largest lessee of

property in the State of Idaho, in the process of renegotiating their leases and at an average of a 17% reduction from previous rates.

We know that the cottage site program is broken. And we've looked at a variety of formulas. We've had three appraisers, expert appraisers, report to the Subcommittee on the methodology – on a methodology that would be proposed by an appraisal method, and all three appraisers agree that market rent should be based on comparable market rents. The IDL has also proposed a method that's based on averages, which is an arbitrary outcome, but whatever the outcome, we know that it has to be based on market reality. We understand that this Board has a fiduciary responsibility to get the highest financial return. We know that it can't be below market. But also it has to be based on market reality because if it's above market, sooner or later that system will implode and we'll be right back here at the table.

So I know the IDL is proposing an averaging method. We have serious, serious reservations about that proposal. What is not included in this is what that – what the impact of that averaging would look like in future years. Out ten, fifteen, twenty – *(tape change – dialogue in progress)* – on the long term.

Potential buyers and lessees ask themselves do I rent or do I buy. And they have alternatives. The decision to rent a cottage site – it has to be as good or better than the alternative of buying a cottage site. There are cottage sites available so you have to look at these market realities and – otherwise, it becomes a dysfunctional system, which that's the situation we're currently in.

So we want a sound program that's going to be workable for the long term. The proposal made by the IDL we can certainly live with. The idea of rents where they are – we believe that some rents are – that we're paying are above market. I think that all lessees would – would agree that they could live with the current rents.

The one thing I would ask is that we push forward with getting a resolution to this that this Board – and, Governor, you asked the various state agencies to continue on this path and come to a resolution as soon as possible. There are a number of people that are waiting for a resolution on this issue.

And with that, I'd ask Josh to – I think he's got a few comments.

Mr. Boyd: So I have three topics I want to review. The first two topics are a segue, and they're related to what Jim just discussed.

Governor Otter: Would you identify yourself for the record.

Mr. Boyd: I'm sorry. My name is Josh Boyd, and I'm on the board of the Payette Lake Cabin Owners' Association.

The first two topics are related to what Jim just reviewed, and I spent this last week with Secretary Ysursa, and Tim Hurst on his staff, and with Jason Hancock from Superintendent Luna's staff. It was on Friday, I think, that the Superintendent was in eastern Idaho. And we reviewed kind of what happens with the current proposed methodology, or what could happen if you expanded upon it thirty-five years. And so beyond the fact that it's not market based, it in effect acts as a teaser rate, and it looks fine if you look at the first five years. But if you sign up for it, you may find that five, ten, fifteen years down the road, we're in the same exact boat we're in today where we have rents that are something that, you know, are priced out of the market. Your average person, or your average person that might be interested in something up here, cannot afford them.

Further, the current proposition glosses over the issues with the current appraisal regime. It assumes that the Valley County Assessor's appraisements are fine, and that process is fine, and that's another major issue we have. So I think those discussions were fairly good, and I don't

230 know if Jason had a chance to brief you in yet, but we had a discussion over what the current
231 scenarios proposed look like.
232
233 The next piece that I spoke with Jason about – I haven't had a chance yet to speak with
234 Secretary Ysursa about – is the buy versus lease analysis I put together. And basically what I did
235 is I ran it at a break even, and I ran it at one percent higher each year, assuming a different
236 escalation in each one of those scenarios, for thirty-five years. And a buy versus lease analysis,
237 for those who aren't – maybe that's a business term some folks aren't familiar with – is when
238 somebody goes to look to invest in something, or buy something – what traditionally is done is
239 you'll lay out all the cash flows for the buy scenario. So that's – here's what the mortgage costs,
240 here's the impact of interest, here's the taxes you're going to pay on it – you lay all that out.
241 Then you go – you look at the lease scenario, and you lay out all the costs and cash flows in the
242 lease scenario, and then you go and you look at all the cash flows over that timeframe, in this
243 case we laid it out for thirty-five years, and you say, well, which would you be better off doing.
244 You know, if it was your money, which in the lessees' case here it's their money, what would
245 you be better off doing. And I think that document is an important one, and I think I probably
246 do need to spend a little more time with the Subcommittee going over that or going over their
247 questions. But what it lays out is not only is the initial rent going in very important, but the
248 appreciation over the long term, like thirty-five years, is extremely important. And the analysis
249 shows that anything – you know, anything over, you know, a handful of percent gets you into
250 trouble very quickly and gets folks who are making that lease by decision gets them to lean very
251 heavily toward a buy decision, which means different things at different lakes.
252
253 At Priest Lake, it may mean leaving the lake. At Payette Lake, certainly there is private property
254 for sale all the time, or it may mean that folks are just going to spend their vacation and family
255 travel money somewhere else. Maybe they're going to buy a place in Sun Valley. Maybe
256 they're going to go to Disneyland. I don't know. But certainly that buy versus lease scenario is
257 something that everyone should look at before they sign up on a new lease. I think it also is a
258 market reality for the folks making the decision today. So I just wanted to give a little more

259 detail on those, and certainly I want to spend some more time should the Subcommittee
260 members appreciate that with them answering any questions.
261
262 The third topic I want to cover today, and this is the one that's maybe the most apropos for
263 today's discussion, is a document – one-page document that I'll hand around. And I apologize
264 we don't have a projector for the rest of the folks here to see. But essentially what it is is it's the
265 recent comparables that are available that Valley County has chosen to in some cases ignore,
266 and in other cases it's a little outside their appraisal window or assessment window. And the
267 first one here is one that has sold in this year. It went on the market in September, sold in
268 December. And what's interesting is you'll notice the second one went on the market the exact
269 same time and was exposed to the market for twice the amount of time. The first was exposed
270 for ninety-five days; the second for a hundred and eighty-four.
271
272 The first comparable falls within the Valley County's assessment window. When I asked them
273 about comparables they had, it was interesting – the first thing they said was, well, this is a non-
274 appraisal year. We don't have to look for comparables. We don't even have to look at this,
275 which is interesting. I don't know if the Land Board knows that. Even though rents are set each
276 year, and even though somehow they've come up with thirty, forty, eighty percent increases
277 over the years, within their methodology they can just say, oh, this is a non-appraisal year, we're
278 not going to look at it.
279
280 And what's unfortunate is when the market goes sour, there's many – or much fewer –
281 comparables than when the market is hot, of course. So as this thing escalated – there's, you
282 know, maybe ten or fifteen sales over the last four or five years as the thing escalates – but then
283 as it dives off, you can see there's two comparables, and I think this is over the last year or
284 maybe more, which is unfortunate for the methodology. But what you can see, and I'll just go
285 to the bottom line here, you can see that in the first sale, which was exposed ninety days, the
286 frontal foot that it sold for was thirteen thousand six hundred and seven dollars. The current
287 assessment is at twenty-two thousand dollars, so this would indicate a forty percent reduction

versus the five percent reduction that the Valley County is proposing or selling to the public and, of course, I think they were quoted in the newspaper recently.

If you go to the other assessment, it's interesting. This other one was on the market for twice the amount of time. Now it closed outside their assessment window. You'll see that three twenty date on the second row on the right. But what you'll notice is an additional ninety days on the market didn't really help – didn't really get the seller probably what they were bargaining for. Certainly they had an original asking price that was high enough, but by the time it got down to contract, you'll notice they sold it for ten thousand per frontal foot for the land. When you compare this to the current assessment, that's a fifty-five percent reduction.

What's most important is the bottom two lines here and the – the line up from the top is the current value for frontal foot that is the basis for the current rent in 2009 and is what the Department is suggesting the rent should be in 2010. Well, you'll notice if you compare to that, and of course we only have two comparables – it's unfortunate the market is tanked and that's all we have – but you'll notice that the first comparable indicates there should be a fourteen percent reduction; the second comparable indicates it should be almost a thirty-seven percent reduction. So I wanted to bring this to the attention of the Land Board because I don't know that you always get the best information or that Valley County is always doing what you assume they're doing. But certainly these are – these are the only comparables recently, I believe, for the last twelve to eighteen months. This is what the market looks like. And while it's nice that they're proposing a freeze, we really feel the market is no where near where they – where the Valley County says it is and where the Idaho Department of Land has suggested you should set rents by.

Mr. Bridges: Governor, members of the Board, my name is Drew Bridges. I'm a member of the Payette Lakes Cabin Owners' Association Land Board, or Board, and I'd just like to complete our presentation by thanking the Subcommittee for the work that they've done, and tell you we are

316 heartened by the fact that the Department in its report indicates it intends to come back to you
317 at your July meeting with a recommendation for a new calculation method for the new lease.
318
319 While we disagree with what is stated to be the likely recommendation for many of the reasons
320 that Jim and Josh both mentioned, and why we continue to speak with the members of the
321 Subcommittee about the fact that over the long term we believe that will create a problem that
322 is as great, if not greater, than the present problem we are experiencing.
323
324 We believe based upon our last board meeting, and given a look at the short-term numbers,
325 that we are in a position to be really closer to finding an ultimate solution than some of the
326 other presentations may have suggested. And that is some of the short-term revenue
327 expectations that the Department is looking for we think can be reasonably met with some give
328 on both sides by – based upon a market-based rent system that will comply with both the
329 Constitutional mandate and the statutory mandate that will allow us, with some give and take,
330 to reach that and have a system that is not subject to fluctuation, that's based on the market
331 going forward.
332
333 Obviously that's something that we are going to continue to discuss with the Subcommittee,
334 and we recognize that they are not in agreement with that approach at this time. We believe,
335 though, that it is an appropriate approach, and we can have a win-win situation. And that's
336 what we need and that's what we need to come to with a lease that – a new leasing program in
337 place.
338
339 I asked our host today, Mr. Lovell, earlier today, about the ability for those members who need
340 to exit and obtain financing for purchases or those who want to enter, and he confirmed what
341 we've been saying and know, and that is that banks and financial institutions are not able to
342 make that loan commitment on a lease that's got eighteen months or a year left to run. So once
343 we find the fix on the rental calculation, I would urge, and have urged, the Subcommittee, as we
344 all have, that we come forward and present to the Land Board the terms of a new lease that

345 could be put in place immediately, not waiting for the expiration of the current lease, because
346 only then will we be able to begin to restore the market. Only then will people be able to exit
347 and enter, and we'll be able to get this started and start the repair. So we are pledged to
348 continue that work with the Subcommittee and hope to be back to you jointly with a
349 recommendation that we can all support for that purpose. And thank you very much for the
350 opportunity to address you.
351
352 **Governor Otter:** Thank you. Why don't you just stay at the table.
353
354 And, Chuck, we'll have you go ahead – Mr. Lempesis, we'll have you go ahead with Priest Lake.
355 Then we'll open it to questions and comments.
356
357 **Mr. Lempesis:** Thank you, Governor. I will be extremely brief. I just want to publicly express the
358 appreciation of the Priest Lake State Lessees' Association for the very hard work that was
359 contributed by a number of individuals, most of all by Secretary Ysursa and Superintendent
360 Luna, who did more than merely a placebic job, but rolled up their sleeves to try and resolve a
361 very difficult problem. We're grateful for that.
362
363 I also want to thank publicly Mr. Bacon and the members – and the good staff of the
364 Department. They have been in most instances transparent working in good faith to help in
365 every way they can to also ameliorate the difficulties that we have in the economy and to work
366 to a solution that will be long lasting.
367
368 I also want to tell you that your own representatives, who have attended and served on the
369 Subcommittee, have also brought good ideas. I think we are perilously close to resolving an
370 issue that's been intractable for years. I would reserve any comments I have, or
371 recommendations, for future Subcommittee meetings or perhaps in the July meeting where I
372 think you might – they might be better received. I would urge you on behalf of our lessees to

adopt the recommendations of the Department as were previously offered by Mr. Murphy, and I want to thank you for your time and patience.

Governor Otter: Thank you, Mr. Lempesis.

Further discussion.

Mr. Ysursa, Mr. Chairman of the Subcommittee.

Secretary of State Ysursa: That's a dubious honor, I think.

I'd like to express my appreciation, and this is still an ongoing journey. It seems like the Ark of the Covenant was done better, but, anyway, it – just a few comments. I don't want to be too cryptic about it, but anytime you're looking long term, and you're looking at a thirty-five year lease – and, Josh, you're great at the numbers. You can run them and show shock value of what things do. You project in those numbers that it's eight percent a year. That certainly has been shown in the past. I'm not too sure that's going to be happening.

Anyway, we don't have a crystal ball, but any percentage you put in – call me Simple Simon, but you put eight percent in, just by its operation by the old rule of seventy-two, you double in nine years and then you double again and then you double again. Will some of these rates go way up? Well, if you keep that pace – if you keep that going. But that's simple compounding. And, yeah, I can play sticker shock. You can too by running it out thirty-five years. Do you want to go to a five-year lease? You guys don't want to see those figures. I mean, we went to the Legislature and got that law changed to go to thirty-five. Now you're exasperated because at the end of thirty-five, it may be this astronomical figure. Yeah, it might. But that's compounding. So the sticker shock value has fallen on deaf ears as far – to me – on that scenario.

The other scenarios – we need to redo a rent – redo the lease. I am exasperated by the slowness on our part of getting some lease provisions, and that needs to be done quickly. But tearing it up and getting it in because some folks are upside down in some recent investments they made, we need to tear up the lease for a certain few, we need to do it right first. And we will. But I can – I've been at this thing for thirty-five years – as long as these new leases are going to be. And you want me to quote some rates that were being paid? Like a second tier lot in Payette in 1970 for ninety-six bucks a year. Sounds astronomical now to be paying eighteen hundred or two thousand for the same thing. I mean, we can play the sticker shock game so don't – I'm urging you not to continue to play it as far as this Subcommittee member is concerned.

The other scenario on – Mr. Young, you said, you know, are we seeing – are the two sales – the big problem we have – there's no market – there's comparables we're having trouble finding. I'm sure the County Assessor is having trouble finding anything on the market – on the lakefront. You said we're seeing sales that were sixty percent less than the peak. Are those some of the sales that were submitted? Do you have other data that shows that beyond the two that Josh mentioned? One.

Mr. Young: No, I was going to make a comment.

Secretary of State Ysursa: And – I mean, do we have any others? I mean, you said it went down sixty percent from its peak. What specific sale are you referring to?

Governor Otter: Mr. Young.

Mr. Young: Governor, Mr. Secretary, this is one – there are sales. These are the only two lakefront sales that are leasing.

Secretary of State Ysursa: Okay.

Mr. Young: That I'm aware of.

Secretary of State Ysursa: But anyway I don't want to rehash. It's our goal – and as a member of the Subcommittee, and Tom, of course, has been most helpful, and his staff, on doing this – if you remember the Board's recommendation, or the Department's recommendation, is to come back with their review in the July meeting. We're not putting this off. We have to go. We have to get this resolved. But the initial recommendation is to discuss, and the issue before us is the 2010 rents. What should they be – are they going to be – we have to decide today. The Department has made a recommendation. I concur with the recommendation. I'm going to make a motion to approve those – that when – what does that entail? It means we are freezing the rents at both lakes at last year's rate. What does that mean in the – in how we have tried to help? What's that mean in Payette? Three years of a rent freeze. It means two years of a rent freeze in Priest Lake.

So this Board has been most agreeable, amenable to your plight, and we'd like to get a resolution. I don't think we're that far off. Figures are figures. I can fool around with them, too. But the main thing is good people in good faith efforts come to a solution. Well, do I think we'll put it to bed and thirty-five years from now will be the only time we're going to bring this up again? I – I'm not that naïve. But we're making a good effort at it; and – but every two steps we take forward, let's not take one back. And – we're very cognizant of what the economy has not done, and what it's doing, and how you can raise – any time you average or index, you're not picking up the latest. It gets melded in with the previous. Everybody knows – you know, the term twenty percent has been thrown around at least certainly on the north Idaho lakes. Both up in Heyburn and both in Mr. Moe's analysis, and yet we have a recommendation to raise rents in the teeth of what we know is a declining market. Why? Because we're using figures from the past and we have not. And we're not going to have a Kumbaya session and rates when we do not recognize the fact that we have not – in Payette especially – recognized the – those last years of unbelievable increases that were forty-nine percent on the lakefront and eight-eight

percent on the second tier. Those have not been put in place. And to go forward and put those in place in an average or in an index is going to bump it up. You cannot simply ignore that. Why do we like a ten-year average? Because what we're looking for is predictability and stability. We wanted to lower the unbelievable fluctuations, and we think we've come to a fairly decent way to do that.

And I know you have brought up, to your credit, a new methodology. I have been exasperated by it. I don't think it has comparable data to what we are doing, and I've said that a thousand times. And I'll say it a thousand and one. I just did. So – I don't want to go on, but as Chairman of the Subcommittee, and around this for thirty-five years, I can go back and look at the minutes, and if we have the old tapes it would be a Yogi Berra scene. It's déjà vu all over again. And we just need to have a resolution, and I think we're going to get there, but some comments today were looking a gift horse in the mouth. We went for a freeze, and we were getting a little bit of criticism for that. So I will, after that long winded preface, make a motion that we approve the recommendation to freeze the rents at Payette Lake and at Priest Lake.

Controller Jones: I second the motion.

Attorney General Wasden: Second.

Governor Otter: It's been moved and seconded that we adopt the Department's recommendation to freeze the rent at the cottage sites at both Priest and Payette lakes. Before I do that, I do have – before I put the motion, I do have a question on this pass out for the comparables. Was that million five hundred thousand dollars the original asking price?

Mr. Boyd: Yes.

Governor Otter: And the two million one was the original asking price?

Mr. Boyd: Yes.

Governor Otter: Okay.

Superintendent Luna: Governor.

Governor Otter: Yes.

Superintendent Luna: I don't bring the years and breadth of experience that the good Secretary does. I think thirty-five years ago I was sitting in a classroom in the eighth grade.

Mr. Lempesis: Oh, that was harsh. Harsh.

Governor Otter: (inaudible) classroom you're now running.

Superintendent Luna: That's right. But – but – but I have learned a lot in – as a member of this Subcommittee, and I do think that we are awfully close to finding a solution that will in the short term and the long term bring some stable – stability, predictability and fairness to this whole issue. I'm going to support this motion. I think it's fair to freeze this again for the second and third year because I think the real important decision that we will make that will have the most effect on this whole process and program will be the decision that we'll make next month at our Land Board meeting. So I know we have some things that still have to be addressed.

I still have some questions about premium rent and the fair way of establishing that. And there are other issues to be looked at, but I think we've made a lot of progress, especially in the last couple of meetings. And I look forward to bringing this to a conclusion and having this put to bed for at least a number of years, and so I'm going to be supporting this motion, and then working diligently over the next month to make sure that we come back at our July meeting

with a plan that everyone can support that will bring some stability and predictability to this lease process.

Governor Otter: Further discussion.

No further discussion. It's been moved and seconded that we adopt the Department's recommendation on freezing the rent at Payette and Priest lakes. All those in favor signify by saying aye.

(All say aye.)

All those opposed nay. The ayes have it, and the Department's recommendation has been adopted.

Thank you.

Mr. Lempesis: Thank you, Governor.

END OF THIS AGENDA ITEM

Exhibit 36

Transcript, Agenda Item 7.

Recommendation of the

Cottage Site Subcommittee,

Land Bd. Meeting

(Feb. 16, 2010)

State Board of Land Commissioners

February 16, 2010

Regular Meeting

7. Recommendation of the Cottage Site Subcommittee

SPEAKERS:

- C. L. "Butch" Otter, Governor
- Ben Ysursa, Secretary of State
- Lawrence Wasden, Attorney General
- Donna Jones, Controller
- Tom Luna, Superintendent of Public Instruction
- George Bacon, Director, Department of Lands
- Jim Young, President, Payette Lake Cabin Owners' Association
- Josh Boyd, Payette Lake Cabin Owners' Association
- Charles Lempesis, Attorney, Priest Lake State Lessees' Association
- Bud Belles, President, Priest Lake State Lessees' Association
- Mike Schmitz, Priest Lake State Lessees' Association
- Karen Escheverria, Executive Director, Idaho School Boards' Association
- Terry Anderson, Executive Director, Property and Environment Research Center, Bozeman, MT

Governor Otter: Mr. Secretary.

Director Bacon: Governor, the only remaining item on your agenda is in the Regular Agenda, and that's the recommendation of the Cottage Site Subcommittee. And with that, I guess we turn it over to the Subcommittee.

Governor Otter: Mr. Secretary of State is recognized.

29 **Secretary of State Ysursa:** Mr. Chairman, Governor, members of the Board, before I get into my
30 substantive remarks on the Subcommittee's recommendation, I'd just – I'd like to make just a
31 few comments.
32
33 I feel I must make the record clear about possible misconceptions pertaining to my openness
34 and availability for meetings with the cottage site lessee associations. I have been available and
35 open to meetings with individual lessees or groups of lessees at a moment's notice. I believe
36 Mr. Belles, Mr. Lempesis, Mr. Leroy, Mr. Fery and educators and others can attest to that. We
37 also have almost two hundred pages of meeting transcripts detailing meetings outside regular
38 Land Board meetings. Superintendent Luna and I did not agree to a facilitated or mediated
39 meeting because we felt it was an improper delegation of our decision-making authority.
40
41 The key element in dispute with the cottage site lessee associations, which will be thoroughly
42 discussed later, is the Subcommittee's disagreement with the lessees' market rent methodology
43 presented by the three appraisers. I would point out that the fact we disagreed with the
44 methodology did not mean we didn't listen or study it. Any statement that I have not been
45 open or accessible in this matter is simply incorrect.
46
47 Now to the – it's in your book, the Cottage Site Subcommittee Report. I want to make sure I – I
48 stick to this since Mr. Popkey's already written the article about it. But –
49
50 Governor, members of the Board, I – I respect all of you. I know you are all competent readers.
51 You can read the report. This has been a – the best phrase I could come up with, and I will get
52 into that a little bit later, was the term imbroglio. And you look that up in the dictionary and a
53 condensed heap is what it comes out with.
54
55 We have struggled with this issue for years with the cottage site folks. I don't – we don't need
56 to go through everything that's happened over the years and whatever. Superintendent Luna
57 and I were appointed June 12, 2007 as a Subcommittee. I, in an illucid interval, volunteered to

be chairman. The – I have over my thirty-five years with the State and the Secretary of State's Office, certainly as a Deputy for Secretary Cenarrusa and others, been involved in more cottage site meetings and more discussions about this issue than anybody in this room. And there are a lot of folks in this room who have been through a lot of it.

So it's a tough issue. Very tough. And this Board has dealt with it. Previous Boards have dealt with it. We haven't – we are not without sympathy or empathy. And the bottom line in this entire matter is balancing our constitutional mandate in article 9, section 8, statutes, prudent investor standards, whatever you want to say, with the long-term relationship that we have with the lessees.

So I'd just like to go to the script now under recommendations, and I think we're going to fully vet this later on. But the Subcommittee is well aware of the constitutional mandate of article 9, section 8, and the duty of undivided loyalty to the beneficiaries of the endowment trust. However, we also recognize that severely impairing or eroding long-standing business relationships with our lessees is not in the best interests of our trust beneficiaries. We're also aware that raising rents too high would result in these lands going unleased to the detriment to the beneficiaries.

Therefore your Subcommittee is proposing the following. And some of you, this has been an evolving report moving things around. I think the number one recommendation from the Subcommittee is – the number one recommendation – the Subcommittee believes that the long-term solution to the never ending cottage site imbroglio is to dispose of the lots – and this is key – in a reasonable market savvy manner.

Reading the story today in the Statesman, and then reading comments to it, I need to emphasize – certainly we all recognize that the real estate market is probably not in the best of shape right now, and this would not be a good time to sell. As trustees, it would be a violation of our duty to sell at this point in time. It's a depressed market. We don't – that's why the term market

87 savvy is very key. The proceeds could then be invested in other assets which could better
88 enhance the endowments.
89
90 In that vein, we recommend that the Department conduct the necessary analysis and
91 recommend to the Land Board by January 2011 specific long term land development plans of
92 state endowment land on or adjacent to cottage sites. These plans shall deal with the sale or
93 exchange options where practicable and in the best interest of the trust, keeping in mind the
94 unique circumstances, including public and private ownership, at each lake. I think that's a key
95 point. We have two – as we all know, we have two lakes that we're involved with. Over three
96 hundred leases up at Priest Lake – a different dynamic up there in ownership. Part of – one side
97 of the lake at Priest Lake is – are federal lots; the other side of the lake are state lots. There's
98 not a lot of private ownership up at Priest Lake. Payette Lake's a different matter. We have a
99 very disjointed ownership pattern. Lake – or lots have been – cottage sites have been sold,
100 exchanged. We have buildings downtown. We've done it for timber property and whatever.
101 And there's disjointed ownership up in Payette. So obviously any study – you'd look at that
102 pattern and others, but I don't want to presuppose what's going on.
103
104 I think a key point to know regardless of what length of lease we enter into, the lease provisions
105 have for the last twenty years, and will continue to have, a provision that – and the code – the
106 Idaho Code does also – it's in the lease 1-1H of Part N that we can sell or exchange these lots.
107 It's been in your lease; it's still in your lease – upon proper notice. The current lease was altered
108 to go from ninety to at least a hundred and eighty days. The – so I think that's a very key point.
109 That's in there right – and it has been in there for twenty years, and it's in the State code. That's
110 item number one recommendation.
111
112 Recommendation number two, you've seen the figures. They're out there. They're in your
113 book. They've actually not been changed much since they were floated out earlier as a four
114 percent rate. Now what that four percent rate – and I would – I would – I think it's – whatever
115 exhibit it is – but it's in here – it's in your book – the four percent rate is of a ten-year average,

and it's a five-year target of that ten-year average. So it's not four percent of current market value as we speak. Now what does this four percent rate do as I have proposed it and the Subcommittee has proposed it. Current – current rates bring in four million two hundred and sixty-seven thousand nine hundred and thirty-two dollars. What this will do in five years? It will average – again, different lakes have different rates of increase as in the proposal – the Priest Lake lakes would be an average of about 9.1% a year; the Payette Lake waterfront average about 8.2% a year; the Payette Lake second tier, an average of about fourteen percent a year.

The other – the totals, at the end of five years, would have a – gross receipts of six million five hundred and eighty-four thousand seven hundred and sixty-three dollars. That would be a fifty-four percent increase in total as you compound that nine percent average. At the end of each five-year's period under the lease the target rent will be recalculated at four percent of the average value for the duration of the lease. The four percent used in the formula falls within the range of rates mentioned above and will still generate interest in the market. It provides a reasonable rate of return and generates nine percent per year increase over the first five years to the beneficiaries. And remember the beneficiaries of the endowment are the Public Schools at Priest Lake; Payette Lake, it's the Normal Schools and the Hospital South – all of them endowment beneficiaries.

Premium rent is part three. Premium rent was created – it's – people point out that it's an invention of the State Land Board. It is. It was done in 1981 – the ten percent premium rent. Why did we quote unquote invent premium rent? Premium rent was put in in 1981 and continued at the ten percent of leasehold value, of gross, to offset, which is what was acknowledged to be low rents. The difference between contract rent and market rent. Premium rent is supposed to – the leasehold value fills that gap, and we were getting ten percent of the leasehold value. That was the – certainly a point – a key point in the Attorney General's opinion, which I'm sure he can talk about in a few minutes, that dealt with who was getting this appreciation in the land value. Certainly some of it went to improvements that would – that you could try to quantify that went to the land, but by far, most of this went to the

appreciation in the land, and the land belongs to the endowment beneficiaries, not the lessees. And that's a key point. So when part three, premium rent, was – since 2003, cottage site owners have realized – and this is gross – an excess of twenty-five million for the use of state endowment land while the endowment received two point seven million. That was a key point in the Attorney General's analysis.

Number three, as part of the premium rent, to correct this inequity, the Subcommittee recommends that the premium rent be increased gradually to fifty percent of the leasehold value upon transfer of the lease. Subcommittee believes that a fifty percent premium rent will have the effect of maximizing the return to the beneficiaries and that any higher rate would be counterproductive and act as a disincentive for selling leaseholders to be active in seeking the maximum sale price. You may remember that there was a cottage site survey that was released a few years ago that really put gasoline on the fire that was recommending a hundred percent premium rent. That was never brought before the Board to vote on and – but that argument has been made and that came from the Department and others. So included in our recommendation, the lease language will include a leasehold premium rent calculation that will be phased in as follows – 2011 – the situation we have now, ten percent to the State; ninety to lessees; it will then be – go up to 2015 – at ten percent a year up to 2015.

The Subcommittee believes the rental rate described above, coupled with premium rent formula, meets the Land Board's fiduciary responsibility and provides sound business practices to protect the market for cottage site lessees. A key point, and you won't see this in the script, in the Subcommittee's report is the lease term. We have a history of ten-year leases. In fact the statute used to say up to ten years. The cottage site lessees came in and suggested in one of our meetings that we consider expanding the lease term to thirty-five years. First it said thirty, but then to go five years beyond normal term for individuals to get long-term financing on improvements. That was looked at very seriously by this Land Board and we at that time voted to go to the Legislature and the Land Department took the legislation up there – or up to the

173 third floor, not here – in the Statehouse – and the legislation was passed for cottage sites to go
174 up to thirty-five years. It's not a mandatory, but it's up to and that's something we looked at.
175
176 Now as this Subcommittee report evolved, and – I really haven't had a chance to talk to my
177 fellow Board member much on this issue – the Subcommittee member – it became clear for a
178 number one goal eventually to get out of this scenario is to sell or exchange. It seems counter-
179 intuitive to go to extending the leases to thirty-five years. So as one Subcommittee member, I
180 am certainly amenable to – to a real lively discussion about the lease term and whatever
181 because of the – some of the comments that will be made I think later on. With the ability to
182 sell or exchange, which is in the lease and is on our plan – a lender looking at this – they'll – it's
183 been brought up, and we've asked lenders, and they say, oh, the State's never done it – you're
184 not going to invoke that clause. Well, people should be on notice that the State is looking at
185 doing that; it is in the lease, and we could invoke that clause and could – and will. So that I think
186 will be a disincentive for any lender, especially in this climate, to – to finance improvements. So
187 I am not – going against my own recommendation, I think we need to thoroughly vet – well,
188 everything we've presented, but I think the lease term – and I think the Department has made
189 some comments on that, and I think the consultant that the Attorney General retained has
190 made some comments on it and will make further comments.
191
192 So, Governor, without further ado, I'll certainly answer any questions, but I think we – and I
193 think the tone here to the lessees and everyone involved is that we feel your pain. We have
194 frozen rents for three years at Payette. We have frozen them two years at Priest. We have –
195 and my goal is to be fair to everyone. That includes the endowment beneficiaries.
196
197 Governor, that's my initial comments, and I'll certainly sit for any questions from the Land Board
198 members.
199
200 **Governor Otter:** Are there any questions at this time?
201

Mr. Wasden.

Attorney General Wasden: Thank you, Governor. I just want a point of clarification from the Secretary. First of all, I appreciate his effort in trying to resolve this issue. I know that he and Superintendent Luna have spent a tremendous amount of time, tremendous amount of effort, a lot of discussions, a lot of headaches, and I appreciate their work. I just want one point of clarification, and that is the written documentation indicates a lease term of thirty-five years. Is that still the recommendation from the Subcommittee subject to further discussion?

Governor Otter: Mr. Ysursa.

Secretary of State Ysursa: At this time, I don't want to digress from that, but I have not had a chance to vet this with my Subcommittee co-member, but I, like I indicated, I'm amenable to changing that to a ten-year lease. We have vetted – we have changed the order – I have – with Tom's concurrence – of presentation, and if our number one goal is to in a market savvy manner get out of this situation, I think signing a thirty-five year lease sends a mixed signal. So is this – we can chat for two seconds, but I think the Subcommittee – I'm willing to go to ten years.

Governor Otter: If I might, when we discussed this – I think it was last year – and went to the Legislature or – with a bill – we contemplated a term of lease similar to a mortgage –

Superintendent Luna: Right.

Governor Otter: – for the leaseholder improvements and the lease to be in one package. So as I recall that discussion, I think we did contemplate thirty to thirty-five years –

Secretary of State Ysursa: Yes, we did.

Governor Otter: – which would be a mortgage –

Secretary of State Ysursa: Yes, we did, Governor –

Governor Otter: – term.

Secretary of State Ysursa: – and a point of clarification there, we had not in the same vein – in that same meeting – everything – and I've got the minutes of the legislative testimony – and the testimony and whatever, it was all about long-term financing. But we did not – that was to the legislative committee, but the discussion in here had to do with the same thing. We did not at that time discuss this first recommendation that we think disposal or unifying the ownership is our primary – our number one recommendation, and in that vein I think the landscape has changed a little bit.

Governor Otter: Mr. Luna.

Superintendent Luna: Mr. – Governor and members of the Board, I agree with the Secretary of State that the obvious answer to me is to sell these lots even – even at the four percent of market value, which is our goal, is – which is the high number, but it's small compared to the return that can be realized by investing in commercial property – taking these dollars, selling these properties and investing that money in commercial properties or other investments that will return high – returns much higher than four percent. So if the thirty-five year lease is an obstacle to fulfilling our number one recommendation, which is to move towards getting out of the business we're currently in with cottage site leases, then I – I support that.

Governor Otter: Further questions.

Ms. Jones.

Controller Jones: Just a comment and maybe a question for the Chairman of the Subcommittee.

So we would – you could see us possibly changing that lease term to ten years for the cottage site owners. Our lessees would have an opportunity to still get financing as – for the thirty-five years with special – under special conditions or – tell me how it would affect them.

Secretary of State Ysursa: Governor and State Controller –

Governor Otter: Mr. Ysursa.

Secretary of State Ysursa: – as this was evolving, as we saw a lot of information come in late. Any time you set a deadline, expect information to come in about two seconds before the deadline, and we are on a deadline. These leases – April 30th – an application to renew by State code – all these leases that expire at the end of the year, which they do – all these leases expire then. It's in – we all know that. So does the press or they should. And they all end the end of December of this year, 2010. So by April 30th of this year, applications for renewal by State code have to be in. That's the time crunch we're under. But as this information came in, I looked at what Montana does. Montana being another state that – very similar, other than values, in what they do on leasing, and they're in their own imbroglio themselves. But they had a provision in there – they had a default lease – I think theirs is fifteen years – but they would go five years past a normal financing term if necessary and if shown by the – a need by the lender. But they also do not have that number one recommendation that we've come with about sale or exchange. So that – that's the point of clarification since our conversations.

Controller Jones: Thank you.

Thank you.

Governor Otter: Further discussion.

Mr. Wasden.

Attorney General Wasden: I guess I'm still unclear. My understanding of what the Subcommittee's recommendation is is a four percent return based on a ten-year rolling average, premium rent with a five-year rollup from ten percent to fifty percent, and a lease term of, I believe, thirty-five years with a discussion to perhaps go to ten. I'm just trying to figure out exactly what the lease term recommendation is from the Subcommittee.

Secretary of State Ysursa: Mister –

Governor Otter: Mr. Ysursa.

Secretary of State Ysursa: Mr. Chairman, Mr. Attorney General, I think with the – you just heard our recommendation is ten years.

Attorney General Wasden: Oh. Good. I just wanted to make certain I understood.

Governor Otter: Mr. Wasden.

Attorney General Wasden: Thank you, Mr. Secretary.

Governor Otter: Further discussion.

Secretary of State Ysursa: Mr. – Governor, members of the Board, that's the recommendation. Remember, and I'm sure you're going to set the ground rules, no motions are going to be made until we hear all the discussion. So this Board, I think, collectively will vet out what motions get passed and what don't and – at that time.

Governor Otter: Well, as the committee knows, once a motion is made, it cuts off discussion with the exception within the committee itself or by leave of the committee. And so, Mr. Ysursa is absolutely right. We're not going to entertain any motions until we at least go through this list of folks that have indicated a desire to testify, and we'll now move to Attorney General Wasden.

Attorney General Wasden: Yes, Governor.

Governor Otter: You or your representative. I guess you.

Attorney General Wasden: I will be speaking. I have a voice again, Governor.

Secretary of State Ysursa: I liked it better when he couldn't talk, Governor.

Attorney General Wasden: There's a lot in this crowd who I believe would support that motion, Mr. Secretary.

Secretary of State Ysursa: I think so.

Attorney General Wasden: But I do have a couple of questions that I would like to pose to George Bacon and also to Kathy Opp so I would ask for the opportunity to do that, Governor.

Governor Otter: Gentleman has the floor.

Attorney General Wasden: George, are you familiar with the submission by the lessees with regard to these properties.

Director Bacon: Excuse me, if I understand the question, the proposal by the lessees for their – I am and staff is even more fully acquainted with that.

Attorney General Wasden: Excellent. And in your opinion, will the proposal by the lessees achieve market rent for the duration of the lease.

Director Bacon: Mr. Attorney General, Governor –

Governor Otter: Mr. Wasden – Mr. Bacon.

Director Bacon: No, I don't believe that the proposal put forward by the lessees – now, there's two different proposals. The first one was developed by three appraisers. One of them –

Governor Otter: If I may stop just a – are we talking about all the lease lots, Priest Lake and McCall?

Attorney General Wasden: It is the proposal, Governor, that was offered by the lessees. We're going to talk about that a little bit later so –

Governor Otter: Okay.

Attorney General Wasden: We – we could hold these questions until that presentation is made and then this – this would make a little more sense.

Governor Otter: I really think that it would bring more to point –

Attorney General Wasden: Excellent.

Governor Otter: – if we –

Attorney General Wasden: Then let's – then let's wait on this, Governor, until we have the presentation by the lessees.

375 **Governor Otter:** Okay. You still have the floor.

376

377 **Attorney General Wasden:** Governor, I will reserve my questions for George and for Kathy and for
378 Mr. Anderson until we've heard from the lessees.

379

380 **Governor Otter:** Okay, then I'll now give you your time to ask Mr. Anderson –

381

382 **Attorney General Wasden:** Again, Governor, that – we need to –

383

384 **Governor Otter:** That, too?

385

386 **Attorney General Wasden:** That, too, because – because the presentation by the lessees is going to be
387 important to that discussion. It will make a lot more sense.

388

389 **Governor Otter:** Well, how many bites at the apple do you want?

390

391 **Attorney General Wasden:** Until the apple's gone, Governor.

392

393 **Governor Otter:** I think it's gone.

394

395 All right. Well, then at this time we would ask the Payette Lakes' rep – cottage site lessees'
396 representative – to come forward.

397

398 Mr. Young.

399

400 **Mr. Young:** Hello, Governor –

401

402 **Governor Otter:** Mr. Young.

403

404 **Mr. Young:** – members of the Board. Pleasure to be here again. My name is Jim Young. I'm the
405 President of the Payette Lake Cabin Owners' Association. And we have a few other board
406 members, Mike Fery over here; Josh Boyd and former Attorney General Tony Park is also in
407 attendance, and as well as many lessees in attendance. So I'd like to recognize them.
408
409 And before we get started, first off I'd like to just recognize all of the members of the Land
410 Board for your public service in this very difficult time that we're in, and it's a tough job I know
411 that you guys have and oftentimes a thankless job – particularly now in this financial crisis. And
412 there aren't a lot of easy answers, and even though we might have differences of opinion on
413 occasion, we still respect and thank you for your public service and the service to the citizens of
414 Idaho.
415
416 So this recession that we're in, this great recession that it's been dubbed, that's hit everybody
417 really hard, public sector and the private sector. And it's a tragedy when people lose their jobs,
418 and it certainly makes your jobs more difficult when the tax revenues are off or severely
419 reduced. I'm a home builder, and I can tell you that it's more than a recession. It's a disaster for
420 my sector of the economy as it is for many other people. And I know that Superintendent
421 Luna's scrambling for tax revenue to fund schools, and, Governor Otter, you're trying to keep a
422 lid on the budget, and it's a tough job.
423
424 But this whole great recession that we have was triggered by this near collapse in the banking
425 system, and it was really a result of lending that was out of control. All of the credit default
426 swaps, the mortgage-backed securities and the derivatives – it was all a house of cards that
427 came crashing down, and at the base of that house of cards were ordinary citizens. Ordinary
428 people that made really bad decisions – foolish decisions – by entering into long-term financial
429 obligations that they had no business and could not repay – they had no business entering into
430 and could not repay. And then you had the financial institutions that were offering aggressive
431 lending – you know, the deferred payments and no down – all of these financial trickery to
432 entice lenders to – or entice borrowers to enter into these long-term mortgages that they had

433 no business getting involved with. And it was just poor judgment on the part of the borrower
434 and the lender. Foolish decisions.
435
436 So the big lesson, or the great lesson from the great recession, should be that you never, ever
437 enter into a long-term financial obligation that you cannot repay. That should be the lesson of
438 this great recession. And you probably know where I'm heading with all of this. The cottage site
439 program has provided a steady and reliable cash flow to the endowment, but the proposal that's
440 on the table jeopardizes the cash flow to the endowment. And I will say that I am very, very
441 happy to hear Secretary Ysursa say that the number one priority is to exchange or to sell the
442 cottage sites. I believe that the cottage lessees would whole heartedly support this endeavor
443 and work with the state on the possibility of owning these properties. We have recommended
444 that. Former Governor Batt recommended that. The Idaho Statesman. So I think it's right in
445 line with – with the recommendations that have come from pretty much all quarters that you
446 know this is probably not a good investment for the endowment, and there are probably other
447 investment vehicles or assets that will yield a higher cash flow and a better return than
448 residential real estate.
449
450 But from a lessee's point of view, this proposal is problematic, and we're talking about should it
451 be thirty-five years, should it be ten years – if – either way, if it's thirty-five years or ten years –
452 no one should enter into a long-term obligation unless the payment stream is clearly defined.
453 Right now the way it is, especially under the thirty-five year proposal, the payments are
454 unlimited. Nobody knows. I can point to these graphs that are up here, and we've got some
455 projections, and I think we've provided those projections to the Subcommittee as far as what
456 might happen at various inflation levels. But the fact of the matter is, nobody knows. Nobody
457 knows what the payment stream is going to be down the road for these properties because
458 there's no cap on the escalation.
459
460 So nobody really should enter into a long-term financial obligation unless they have a very clear
461 idea of what they're getting involved with. A long-term lease is a financial instrument just like a

462 mortgage. And the good – the good thing about having a thirty-five year lease is the
463 opportunity to acquire financing. It becomes very difficult for a lessee to get financing unless
464 they have a long-term lease. But on the other hand, if you don't know what your payment
465 stream is over that thirty-five year period of time, how can you get involved with that or how
466 can you – how could someone commit themselves to that? It could result in financial disaster,
467 especially for somebody that's on a fixed income – retirees and we've got a lot – a lot of lessees
468 that are retirees that are on a fixed income. We could go through a period of inflation, and
469 given the deficit spending that we've got going on, it's pretty likely that down the road we could
470 be looking at some serious inflation. And even the high end of those graphs, the red could be
471 higher than that. So somebody that's on a fixed income, it could spell financial disaster for that
472 person.
473
474 Long-term leases have caps on them. The State of Idaho is the largest lessee of property in the
475 State, I believe. And you guys have policies and procedures for entering into leases. Your own
476 policy is is that you do not enter into a long-term lease with anything greater than a three
477 percent escalation cap. And most of the leases that you have have no – no inflation cap or zero
478 inflation. So this is common. I mean this is pretty normal out there that there is some type of
479 limitation so that the lessee can project the extent of their risk.
480
481 This lease is unlimited. No one should enter into a lease that has unlimited escalation. We
482 entered into a lease ten years ago that had no escalation limit. And we know what happened to
483 that one. We were facing these huge increases – forty-six percent, eighty-eight percent. And
484 we came to the Land Board and the testimony was, well, nobody really contemplated those type
485 of escalations at the time that that lease was entered into. And that's true. Nobody would have
486 entered into that lease had those escalations been known. And so here we are looking at a
487 lease that has the same type of feature. No escalation limit.
488
489 So, Governor, members of the Board, I – I would ask that you take a look at this lease and define
490 for the lessees what the payment stream is going to be. I think a thirty-five lease is very

491 necessary to obtain financing. It's absolutely necessary. And it would be a hardship on lessees if
492 we did not have that opportunity, but there's got to be a definition as to what those payments
493 are and so that people know what they're signing up for.
494
495 The second reason that this lease, as it is currently drafted, I mean the draft that we – that we
496 saw that came out – is that there is no release provision in the – in the lease. If you sign this
497 lease, and if we're talking about a thirty-five year lease or a ten-year lease or something in
498 between – once you sign, you're locked in. Even if you sell that lease to somebody else, or
499 assign it to somebody else, you're obligated. If it's sold or assigned two or three times or four
500 times down the road and that person defaults because the escalation is now five hundred
501 thousand dollars a year, which it could be, we don't know – if that person defaults, you're on
502 the hook. So lessees – you do not sign a lease that has no release. It would be foolish.
503
504 So, Governor, members of the Board, I would ask – urge you to provide lessees with a
505 reasonable release clause. This is not unreasonable to ask this kind of a provision. And we –
506 you know, we surveyed our lessees, and ninety-two percent of the lessees said that they are
507 either currently selling their property – ninety-two percent currently selling their property or will
508 sell their property if this lease is approved. The problem is – is if you sign this lease, even if your
509 plan is to sell it or dispose of it later on, you're on the hook. So a release provision is not
510 unreasonable. And, by the way, it's a startling statistic that ninety-two percent of lessees are
511 dissatisfied with this program and want to wash their hands of the whole thing. This – you're in
512 the business of leasing, and to tell you the truth I've never seen a business so eager to run their
513 customers off as this program.
514
515 The third reason that lessees should not enter into this agreement as it is currently drafted is
516 that the lease payments are irrational and illogical. In other words, a rational person that is
517 looking at this, Governor and members of the Board, if you're looking at this payment stream as
518 best you can estimate it, and again, we're talking about estimates because we really don't know
519 what the payment stream is, but as best you can estimate it, the – if we – if you do a lease-buy

520 analysis, and we've provided you with a number of lease-buy analysis – it is much better to buy
521 the property, or similar property, than to lease it. I mean, it's not even close. The numbers
522 aren't even close. If you run a present value of future cash flow – I mean, we've provided all of
523 this. We provided the – the three appraisers – all of those reports indicate that the rent amount
524 exceeds what a rational person would enter into.
525
526 The formula – the ten year – the four percent ten-year rolling average formula – has not been
527 tested. We don't know if it's going to work. Secretary Ysursa said that there would be interest
528 in the market with the four percent ten-year rolling average. Well, I don't know how we arrive
529 at that conclusion since it has not been tested. It's an arbitrary formula that was arrived at. I'm
530 not sure exactly how it was arrived at. But what if it's wrong? What if there is no interest in the
531 market with this particular formula? Why not test it? Why not test it before you put all your
532 eggs in one basket? There's ample opportunity to test this prior to – prior to going out there
533 and making this the formula across the board for all five hundred and some-odd leases.
534
535 Now the Attorney General's opinion, I guess, advocated conflict auction, and, you know, the one
536 good thing about conflict auction is that it would determine what market is, and I think that we
537 are certainly in favor of market rent – market rent. There's some problems with conflict
538 auction. The biggest problem was how would you deal with the existing lessees? How would
539 you compensate them for the improvements and their investment in the property? And there's
540 other problems, like perpetuity, and, you know, the legacy value that – and that's the reason the
541 Legislature passed the 58-310a. But it would be interesting to establish a value for this bundle
542 of rights if we were to auction off – you know, what's the value of somebody using that property
543 for thirty-five years if you were to auction that off today as a lump sum number, you know.
544 What are you going to pay for a two hundred thousand dollar lot to use it for thirty-five years?
545 Well, more than likely you would not pay more than two hundred thousand dollars because
546 you'd just buy something for two hundred thousand dollars. So probably that bundle of rights,
547 the present value of that bundle of rights, is less than the value of the land. The problem with
548 the four percent ten-year rolling average, as best we can project it, the present value of the

549 future cash flow exceeds the value of the land. Now that's irrational. That's illogical. And that's
550 what I'm talking about. It doesn't work. So nobody should enter into a payment stream where
551 the value of the payment stream is greater than the underlying asset. Okay. So I would – I
552 would urge the Board to take a look at this formula before you implement it, and let's look at
553 the market values. We provided a market value study. It was rejected. But the underlying idea
554 behind it was agreed to by three very well known appraisers that comparable market rent will
555 arrive at market rent. We don't have that right now. So let's study this.
556
557 The fourth reason, I'm getting close here, the fourth reason that –
558
559 **Governor Otter:** I would just remind you – you have ten minutes left.
560
561 **Mr. Young:** All right. I'll – I'll get there, Governor. Thank you.
562
563 The fourth reason that – and this is the last reason – there are others, but I'm going to keep it at
564 four reasons – is – is this issue of premium rent. You know, in the past – in the past there has
565 been leasehold value, and one would probably argue that leasehold value is created by
566 undervalued rent, and I don't disagree with that although I think that there are other factors
567 that create leasehold value. At the present time, I question whether or not there is any
568 leasehold value. I don't – I don't know, but the last couple of sales – I think there's been a gross
569 misallocation of leasehold investment rather than leasehold value.
570
571 But assuming there is leasehold value, the idea of profit sharing, which I believe is really what
572 we're after here, you know, it – it makes some sense. Profit sharing is used by companies all the
573 time to incent people – incent their managers and their employees. So it's – it's not a – it's not
574 an idea that does not have merit. It creates value. I mean – I think – I think profit sharing
575 creates value or incents people to create value. But let's define what profit is here.
576
577 **Secretary of State Ysursa:** I figured you were going there.

578

579 **Mr. Young:** That's where I'm headed with this. Profit is the selling price minus the cost equals the profit.
580 So as a retailer, if you're selling something for a hundred – you buy the inventory for a hundred
581 dollars, you sell it for a hundred and fifty dollars, your profit is fifty dollars. That's profit. So –
582 but that's not what we're talking about. We're talking about fifty percent of the gross selling
583 price. So if you buy a leasehold value for a hundred thousand dollars, you sell it for a hundred
584 thousand dollars, you haven't made anything on it. Yet under this formula, you would owe fifty
585 percent of the selling price. Now that's a disincentive. It's a disincentive to the seller, to the
586 buyer – it's a disincentive to create value. I think that lessees would be whole heartedly
587 agreeable to a formula that creates value that incents people, lessees and buyers, to create
588 value. That would be a formula based on the net profit. I mean not even the – not even the IRS
589 takes your gross amount. You know, they – they understand what profit is. Selling price minus
590 the cost is profit. So if we're going to have a formula, let's base it on the net profit. That would
591 – that would provide incentive for everybody.
592
593 How am I doing?
594
595 So in summary –
596
597 **Secretary of State Ysursa:** In time or presentation?
598
599 **Mr. Young:** In time.
600
601 **Governor Otter:** I'll only comment on the time.
602
603 **Mr. Young:** Okay.
604
605 **Governor Otter:** You've got seven minutes.
606

607 **Mr. Young:** All right. In summary then – then we all respect the very serious obligation that you all have
608 as far as your constitutional obligation to maximize the long-term return to the endowment.
609 But the best way to maximize the long-term return to the endowment as it relates to the
610 cottages sites is to have a functional and healthy leasing program that provides a steady cash
611 flow to the endowment.
612
613 The four items that I just mentioned – putting some reasonable limits on the escalation; giving
614 the lessees a release when they transfer; setting the rates at a sustainable level that represent a
615 reasonable lease-buy analysis or a present value analysis; and also reflect market rent; and then
616 providing a premium rent program that provides incentive rather than disincentive. I think if
617 you did those four things, we would have a healthy program that we could rely on indefinitely
618 and would allow the time to implement the exchange program that you're talking about,
619 Secretary, and a steady cash flow to the endowment. These are not unreasonable requests, and
620 they're very common terms that we find in everyday leases.
621
622 So – you know rather than – rather than engaging in a protracted expensive non-productive
623 confrontation, it would be much better to engage in a dialog that would achieve a solution to
624 this problem. I think we're on our way. I think we can get there with these adjustments that I
625 just mentioned and the idea of the exchanges. We would fully support the Board in
626 implementing this program.
627
628 So I appreciate your time, and if I have a few minutes, I would yield to the Priest Lake
629 association.
630
631 **Governor Otter:** We have allotted thirty minutes for them as well.
632
633 **Mr. Young:** Okay.
634
635 Any questions of me, Governor, members of the Board?

636

637 **Governor Otter:** Let me cut off your time.

638

639 Okay. Mr. Ysursa.

640

641 **Secretary of State Ysursa:** Governor and Jim, thank you for your presentation. It's been very
642 informative. I've heard a lot of it before.

643

644 **Mr. Young:** Right.

645

646 **Secretary of State Ysursa:** But I appreciate you bringing it. I just have a couple of questions. I have a lot
647 more than that, but a couple of them – I – how would you suggest we test our four percent
648 scenario? You say it would easily be tested. What's your suggestion there?

649

650 **Mr. Young:** Governor, Mr. Secretary, you know, you did do a test at Priest Lake. Now it – it failed
651 miserably, but – and some would argue, well, it was interfered with, or the other possibility is it
652 was just out of line. That is the other possibility. So, you know, we could have a test – not only
653 do you have lots at Priest Lake, you have lots at Payette Lake that have not been leased. And,
654 boy, we could test this program by putting those lots out there under a conflict auction,
655 however you'd want to do it, and see what the market is. That's what I would suggest.

656

657 **Secretary of State Ysursa:** But –

658

659 **Governor Otter:** Mr. Ysursa.

660

661 **Secretary of State Ysursa:** Mr. Chairman and Jim, a follow up there. We need to talk apples and apples,
662 and I appreciate you bringing that up. It is in our Subcommittee report. This Board put up two
663 lots at Priest Lake a couple of years ago at a five percent of current market value. As you well
664 know, the suggested four percent of a rolling ten-year average of the five-year phase-in is not

665 talking current market value. It's talking less than four percent current market value. It's talking
666 about where you agreed to be when you signed originally ten years ago. So let's not necessarily
667 talk about – we need to compare apples to apples and the – and I agree. The five percent of
668 current was put up at Priest Lake. Now there could have been other factors that discouraged
669 bidding up there, and we, you know, we can speculate all we want on that. But I wanted to say
670 that was a comparison. Another question – on conflict auctions and bidding. I think there's a
671 conflict in why it was brought. The – 1990 the lessees brought the legislation to the Legislature
672 because they did not want any conflict auctions. They did not want people – and 310(a) was put
673 into – into place for that specific purpose that you would not have any conflict auctions. In
674 other words, having a lease, if you paid the freight, you had a lease in perpetuity. Now that the
675 freight is getting a little heavy, do you agree that we ought to go repeal 58-310(a) and have a
676 conflict auction in a market savvy manner?
677
678 **Mr. Young:** Governor, Mr. Secretary –
679
680 **Secretary of State Ysursa:** Does your association want to do that? I would certainly –
681
682 **Mr. Young:** Actually, I was not suggesting that we support conflict auction. What I was – what I was
683 suggesting is what we support is market rent however we arrive at that. And I think there is
684 opportunity to test the market and find out exactly what the market is before we implement a
685 program that may or may not work. How about we test it? And would you agree that there is
686 opportunity for determining what the market rent is under an auction?
687
688 **Governor Otter:** Mr. Ysursa.
689
690 **Secretary of State Ysursa:** Mr. Chairman – Governor and Jim, you alluded – that has been a very elusive
691 term for everybody – the term market rent.
692
693 **Mr. Young:** Yes.

694

695 **Secretary of State Ysursa:** And we may – well, we probably agree to disagree what it is. We – you didn't
696 flesh out – we have it here – the Board members have seen it. The three appraisers called it the
697 regression methodology and whatever – that basically on Payette Lake waterfront, getting one
698 percent of current market value is what was presented in your methodology. Is that correct?
699

700 **Governor Otter:** Mr. Young.
701

702 **Mr. Young:** It was – Governor, Mr. Secretary, the report from the appraisers is a matter of record, and it,
703 as I recall, it's a regression-type curve, and it depends on the value of the property. And I think
704 it's pretty well proven that the greater the value of the property, the lower the percent of rent
705 to value the market rent would be.
706

707 **Secretary of State Ysursa:** Mr. Chairman –
708

709 **Governor Otter:** Mr. Ysursa.
710

711 **Secretary of State Ysursa:** And Mr. Young, I appreciate that, but a lot of times, and folks out here, be it
712 media or whatever, people on the Board, it's all about the bottom line and what the money is.
713 If I had a two million dollar lot, which I certainly won't, but if I had one in – at Payette Lake,
714 waterfront, assessed at that value, the regression methodology says instead of paying – we have
715 folks in that range now that are paying thirty-four, thirty-five, thirty-seven thousand dollars, and
716 the study from the appraisers, regression, said that this Board ought to reduce those by forty
717 percent and get twenty-two thousand dollars. Is that not correct? That's presented in the
718 record. I'm just obviously trying to get some of the figures out for general consumption of what
719 was presented to us and what it is.
720

721 **Mr. Young:** Right.
722

Secretary of State Ysursa: Suggesting a significant reduction in the rent from the Payette Lake waterfront, number one, and then it would regress. The second tiers would go – it went from one to four percent, let's just say that, depending on that market value. Same thing in – Priest Lake is a little different dynamic, but the methodology was the same depending on the bracket and what you indicated, it went up. And I'm just saying that that – one, the methodology and I guess another question –

Governor, I don't want to dominate the questions, and we need to get on but –

Governor Otter: You could have fooled me.

Secretary of State Ysursa: I'll go. I've – thirty-five years of looking at this – I know a lot of extraneous facts. But anyway, I appreciate what you're saying. We're not without empathy. We've shown that. Again, I can – freezes and then another freeze in a ten-year lease term at Payette, and, yes, the escalations were unbelievable. That's why – why do I go – why does the Subcommittee go to an average and then even a five-year phase-in – an escalation – in an attempt to smooth out the forty-nine percent, the eighty-eight percent, whatever. Eighty-eight – and remember, we have not implemented those forty-nine percents or the eighty-eight percent on the second tier yet. That's what is part of the smoothing process that we tried to bring forth as a – not necessarily a cap but a double smoothing effect. And you'll hear testimony later, I believe, from the Attorney General's consultant that's saying that we're – that just delays the inevitable of us being behind – us being the State and the endowment beneficiary. So – rapid escalation and whatever – and what is true market rent – I just wanted to when – in a nutshell, your presentation and the written presentations that Mr. Fery dropped by as a member of your association, says our goal is to get market rent.

Mr. Young: Yes.

751 **Secretary of State Ysursa:** You have a study that you believe ought to be relied on that shows we're
752 overcharging, and we're getting too much market rent, so to speak. We're overcharging. And
753 we need to reduce it in some of the areas. And in essence it's an overall reduction. But in a nut
754 – I don't want to say – and then – then we can – we can – I – and I won't and I could go ad
755 nauseam on premium – premium rent, and I'll let other people talk. Thank you very much for
756 your presentation.
757
758 **Mr. Young:** Governor –
759
760 **Governor Otter:** Response.
761
762 Mr. Young.
763
764 **Mr. Young:** – can I respond? I'll make it brief. There's a couple of points. There is the appraisal report
765 that tells us – gives us some indication of market rent. There is lease-buy analysis. There is
766 present value of cash flow analysis. All of those things tell us, or give us, a pretty good idea of
767 what market rent should be. So I believe that if we look at all of those things – particularly the
768 lease-buy – I think it's very strong and tells us something. And also the present value of cash
769 flow tells us perhaps what that cash flow should be. All of those will be a good indication of
770 what market value should be. Let us not – not forget that that return on investment is not
771 determined by what you want. It's determined by what the market will bear. And so we may
772 want, or you may want, a six percent return or an eight percent return, and an economist can
773 say, well, that's what we ought to be getting. Well, that's all fine to say that, but by golly, it's
774 the market that tells us what kind of rate of return we're going to get. My 401k, my investment
775 advisor told me you ought to be getting eight percent, but my 401k is a 201k right now. I did not
776 get eight percent, and it's – it was the market that did it to me that slapped me up at the side of
777 the head. So it – we need to rely on the forces of the market, and when you have ninety-two
778 percent of your lessees telling you that they want out, I think that's a pretty good indication that
779 something's wrong.

780

781 **Governor Otter:** Well, I would tell you that ninety-two percent of this Board wants out, too.

782

783 **Secretary of State Ysursa:** I think it's higher than that.

784

785 **Governor Otter:** We don't know where to surrender here yet. We're finished up.

786

787 **Mr. Young:** Okay. Thank you, Governor, members of the Board.

788

789 **Governor Otter:** Unless you have more questions.

790

791 **Attorney General Wasden:** I have questions.

792

793 **Superintendent Luna:** And I have just one question.

794

795 **Governor Otter:** Mr. Wasden.

796

797 **Attorney General Wasden:** Thank you, Governor.

798

799 Mr. Young, I'm looking at an appraisal report prepared by Mr. Moe, Mr. Corlett and Mr. Morse.

800

801 **Secretary of State Ysursa:** Corlett and Mr. Morse.

802

803 **Mr. Young:** Yes.

804

805 **Attorney General Wasden:** It's dated July 14, 2009, and I believe we received it seven or eight days ago

806 approximately. I have a question for you. I notice that the regression --

807

808 *(Governor Otter left the meeting at 10:21 a.m.)*

809

810 **Mr. Young:** Can I respond to that or –

811

812 **Secretary of State Ysursa:** Well, go ahead, Mr. Young.

813

814 **Mr. Young:** That report has been available since it was issued, and I believe we did deliver it to the
815 Subcommittee at the time it was issued or thereabouts.

816

817 **Secretary of State Ysursa:** Mr. – I'll talk to Mr. Chairman. That's me right now. As a member of the
818 Subcommittee and whatever, this was not delivered to us. We have seen – the Subcommittee
819 had this. It was the same – from what I looked at it – this was not delivered to me until about a
820 week ago.

821

822 **Mr. Young:** Well, let us not forget that Mr. Moe is your contractor.

823

824 **Secretary of State Ysursa:** Well – let us – I – and I don't want to say who the other two are when we
825 have a euphemism of Larry and Curly. But anyway, we do understand that but where they're
826 from the Subcommittee's report, this appraisers' report given to us in – before – is there any
827 new data in this document that the Attorney General is referring to? Is there more
828 comparables? We had trouble with there wasn't any more data. Has there been an update to
829 this? Does that reflect? And this document was not delivered per se, but I think we're arguing
830 about minutia. We don't need to, and as Chairman, I would allow Mr. Attorney General to
831 continue.

832

833 **Attorney General Wasden:** Thank you. My question for you is directed to the regression analysis which
834 appears on pages twelve through fifteen of that document. And what I'm trying to do is get the
835 range of potential rates of return, or contract rental rates actually, that appear in that regression
836 analysis which appears to me that it ranges from one percent on some – I didn't count them up
837 – twenty or so lots – to a high of four percent which applies on one lot. That appears on page

number fifteen. So the range would be, and the terms of the contract would range, from one percent to four percent. And I just want to get right what your proposal is with regard to that contract term. Is that accurate?

Mr. Young: General, do you mind if I can –

Attorney General Wasden: Please.

Mr. Young: Yes, General, that's what it says.

Superintendent Luna: What was the answer?

Attorney General Wasden: The answer was yes.

Superintendent Luna: Thank you.

Attorney General Wasden: At least – I don't mean to put words in your mouth, but I think your answer to me was yes.

Mr. Young: Yeah. To the extent of this study, that's what this study shows.

Attorney General Wasden: Okay.

Governor.

Governor Otter: Excuse me.

Attorney General Wasden: I have a follow-up question.

867 Thank you, Governor.

868

869 **Governor Otter:** Mr. Wasden.

870

871 **Attorney General Wasden:** Mr. Young, I listened very carefully, and I'm trying to determine what the
872 elements of your proposal are. I heard thirty-five year lease, reasonable limit on escalation,
873 reasonable release provision, no ten-year rolling average, that market is achieved by auction,
874 net on premium rent, and then I'm assuming that the rate is one percent to four percent in
875 accordance with that regression analysis. Is that the proposal that you are presenting to this
876 Board?

877

878 **Governor Otter:** Mr. Young.

879

880 **Mr. Young:** Actually – Governor, General, our proposal – I believe that we, as an association, and I'm
881 speaking for the association, would be very willing to accept Secretary Ysursa's formula, the
882 rolling average formula, under – first off, if it has an escalation limit. And I think the two are tied
883 in. What is the escalation limit and then what is the percent. But I think that we're not that far
884 off if we could put a reasonable escalation limit on the formula so that people could accurately
885 project what the limit of their liability is. I believe that we could get there. So I don't think
886 we're that far off.

887

888 **Governor Otter:** Mr. Wasden.

889

890 **Attorney General Wasden:** Governor, thank you.

891

892 Mr. Young, I was very specific with the Subcommittee because I wanted to know what their –
893 what their proposal was, which is four percent, the ten-year rolling average, premium rent with
894 a five-year roll-up, a lease term of ten years. That's what their proposal is. I'm trying to identify
895 what your proposal is, and – and so I'm confused a little bit because you've said thirty-five year

896 lease. You've said now we will use Ysursa – Secretary Ysursa's, not Ysursa's, I'm sorry,
897 Mr. Ysursa. You're willing to agree to Secretary of State's formula with an escalation limit.
898 What I'm trying to pin down – what is it that you're proposing? I need to know what the terms
899 are that you're proposing. Can you lay them out for me so that I understand them.
900
901 **Governor Otter:** Mr. Young.
902
903 **Mr. Young:** This study indicates that the market rent is an equivalent of two point two –
904
905 **Mr. Boyd:** Two.
906
907 **Mr. Young:** – two percent.
908
909 **Mr. Boyd:** Using that formula.
910
911 **Mr. Young:** I think that the lessees, as I mentioned, if the escalation cap were similar to the policy of the
912 State of Idaho, which is a maximum of three percent annually, if we could have an escalation
913 cap of three percent annually, then the percentage of rent would be subject to – and we've
914 talked about a three percent or three and a half percent, and I believe the lessees would be very
915 accommodating in that range with an escalation cap in the range of three percent.
916
917 **Governor Otter:** Mr. Wasden.
918
919 **Attorney General Wasden:** Thank you, Governor.
920
921 Mr. Young, so my understanding now is that the proposal you are making is two point two two
922 percent with a three percent escalation cap; no ten-year rolling average; premium rent on net;
923 and thirty-five year lease.
924

Mr. Boyd: No. No.

Attorney General Wasden: I'm –

Governor, Mr. Young, what I'm asking for is lay the terms out for me so that I understand them.

Mr. Boyd: So what Jim's mentioning –

Attorney General Wasden: Would you –

Governor, we do need him to identify himself – he needs to identify himself.

Governor Otter: Identify yourself.

Mr. Boyd: Josh Boyd. I'm on the Payette Lake Cabin Owners' Association. What Jim's trying to clarify is that the methodology of a ten-year rolling average is perfectly fine. It's if you equate a kind of a market rent equivalent. So what Jim is saying is two point two two percent times the ten-year rolling average. So that is an apples-to-apples comparison to Secretary Ysursa's four percent. But I think what Jim is saying is, you know, there's room to negotiate if you have reasonable other terms.

Governor Otter: Mr. Wasden.

Attorney General Wasden: Governor, Mr. Young and – I'm sorry I forgot your –

Secretary of State Ysursa: Mr. Boyd.

Attorney General Wasden: Mr. Boyd. So one of the terms is two point two percent times ten-year rolling average. What are the rest of the terms that you're proposing?

954

955 **Governor Otter:** Mr. Young or Mr. Boyd.

956

957 **Mr. Young:** Governor, General, I – you know, the terms are tied together. So I would ask the question,
958 what is the escalation cap that the State would provide in that lease?

959

960 **Governor Otter:** Mr. Wasden.

961

962 **Attorney General Wasden:** Governor, Mr. Young, Mr. Boyd, it's your proposal. I'm trying to get you to
963 tell me what it is you're proposing. I want to understand what it is you're proposing.

964

965 **Mr. Young:** What we're proposing, General, is that the rent should be fixed to a market rent formula.
966 Now if that formula is based on a ten-year rolling average or a percent of land value, as long as it
967 reflects market, we would be very agreeable to that. Probably the most important point is that
968 the payment stream must be defined. It would be foolish for anyone to enter into this
969 agreement if the payment terms, or the payment stream, is not defined or it has an unlimited
970 escalation.

971

972 **Governor Otter:** Mr. Wasden.

973

974 **Attorney General Wasden:** Thank you, Governor.

975

976 Mr. Young, Mr. Boyd, that's precisely what I'm trying to get to is the specific terms that you are
977 proposing so that persons could understand what that income stream is. Please, I'm asking you,
978 help me understand what is the – what are the proposals, what are the lease terms that you are
979 proposing, lay them out for me so that I can understand them, and I can do some measure of
980 analysis. Please help me.

981

982 **Governor Otter:** Mr. Young.

983

984 **Mr. Young:** Governor, General, we would propose that the escalation limit be no more than the policy of
985 the State of Idaho, which is three percent, and that the payment reflect current market rent. If
986 there is evidence to support a three percent on a ten-year rolling average, or a three and a half
987 percent on a ten-year rolling average, the association would be very agreeable to that. But the
988 escalation limit should be no more than three percent.

989

990 **Superintendent Luna:** I think I was next.

991

992 **Governor Otter:** Mr. Luna.

993

994 Or Mr. Wasden.

995

996 **Attorney General Wasden:** Thank you, Governor.

997

998 Mr. Young, Mr. Boyd, I'm still trying to get the terms that you're proposing. Two point two two
999 percent times a ten-year rolling average with an escalation limit of three percent; current
1000 market rent; thirty-five year lease term. Is that what you are proposing?

1001

1002 Governor **Otter:** Mr. Boyd.

1003

1004 **Mr. Boyd:** I think that's correct.

1005

1006 **Attorney General Wasden:** Okay. Thank you.

1007

1008 **Mr. Boyd:** I think it – the two point two two percent is an equivalent to the Subcommittee's
1009 recommendation at four percent. So it's an apples-to-apples comparison. The market rent
1010 study shows two point two two percent. Just so we're clear.

1011

1012 **Attorney General Wasden:** Okay. Thank you.

1013

1014 **Governor Otter:** Mr. Luna.

1015

1016 **Superintendent Luna:** Governor, I just have a quick question. The Attorney General laid out the
1017 recommendations of the Subcommittee. I don't think he touched on what we believe is our
1018 most important recommendation, and I'd like you – your opinion on this. Do you believe that
1019 the long-term solution to this cottage site situation is to dispose of the lots in a reasonable
1020 market savvy manner?

1021

1022 **Governor Otter:** Mr. Young.

1023

1024 **Mr. Young:** Governor, Superintendent Luna, in my opinion the best long-term solution for the
1025 endowment is to dispose of these cottage site leases and to use those funds to invest in other
1026 types of assets that will yield a higher cash flow for the endowment.

1027

1028 **Superintendent Luna:** So we do agree on that one recommendation. All right.

1029

1030 **Attorney General Wasden:** Governor.

1031

1032 **Governor Otter:** Mr. Wasden.

1033

1034 **Attorney General Wasden**: Thank you, Governor. I need to be clear on this point, and that is that
1035 unification of the title in these properties is essential to ultimately resolving this issue. It can
1036 come in a variety of ways. It can be selling the underlying dirt. It can be acquiring the
1037 improvements. It can be exchanges or a variety of things. But this problem will never go away
1038 until there is unification of the improvements and the dirt. Absolutely not. This problem will
1039 not go away until that happens.

1040

1041 **Governor Otter:** Further discussion.

1042

1043 Let me – I want to ask Secretary Ysursa – the Chairman of the Subcommittee a question. In your
1044 market savvy –

1045

1046 **Secretary of State Ysursa:** Manner.

1047

1048 **Governor Otter:** – liquidation, would that include trade – property for property as well as cash?

1049

1050 **Secretary of State Ysursa:** Governor, members of the Board, I think all options are on the table.
1051 Whether you want to say unification of ownership, sale, exchange, trade, whatever, anything
1052 that pencils out for the endowment beneficiaries that gets us out of this headache. I personally
1053 believe the real estate around the lake is going to appreciate better than most investments;
1054 however, I do not believe we're ever going to capture it in a manner that we don't go through
1055 these trials and tribulations. And so, yes, trade, exchange, whatever. I think all options should
1056 be studied to extricate ourselves from this situation.

1057

1058 **Governor Otter:** Well, the reason I ask that question is because your market savvy – the difference
1059 between trade – property for property – and cash is time sensitive. For instance, the values of
1060 property, let's say, in the Treasure Valley have dropped. Have they dropped the same amount
1061 in Valley County or – in other places?

1062

1063 **Secretary of State Ysursa:** Well, they should. I don't know what the assessor's doing, but –

1064

1065 **Governor Otter:** Well, my point is – is that if I were trying to interpret market savvy right now, I'd say
1066 don't sell them for cash. But I would entertain trading asset for asset is what I'm saying because
1067 the values have may be not – may be not the same.

1068

1069 **Secretary of State Ysursa:** Governor –

1070

1071 **Governor Otter:** And that would be a negotiable point.

1072

1073 **Secretary of State Ysursa:** Governor, I don't think there's any question. You have been much more
1074 market savvy dealing with property than I would ever think of so you know more than I do.

1075

1076 **Governor Otter:** I was. I got rid of all my Payette Lake property. Not entirely by choice.

1077

1078 Anyway, is there – is there further discussion. Further discussion. Okay. We will now then
1079 move to Priest Lake.

1080

1081 Mr. Lempesis.

1082

1083 **Mr. Lempesis:** Governor.

1084

1085 **Governor Otter:** Mr. Lempesis, you have thirty minutes. And then I would also remind the beneficiaries'
1086 representative will also – representatives – will also have thirty minutes.

1087

1088 Mr. Lempesis.

1089

1090 **Mr. Lempesis:** Governor, distinguished members of the Board, and most of all friends, my name is Chuck
1091 Lempesis. I hail from Post Falls, Idaho, and represent the Priest Lake State Lessees' Association.
1092 With me at my side today is Bud Belles, who is the – has the honor – dubious honor – of being
1093 the President of that association. We also have another member who will testify, and if time
1094 permits, two others who will make very brief comments.

1095

1096 For the public record, and I hope that Mr. Popkey publishes this, this is my first imbroglio. I have
1097 no clue what an imbroglio is, but I'm starting to get the drift. And I don't want to be an
1098 imbroglier, especially not a serial imbroglier.

1099

1100 I think with that said, what I'd like to do is let Mr. Belles make a general statement as to the
1101 position of the Priest Lake State Lessees. To save time, let me inform, Governor, the General
1102 and others that our proposal is a matter of record in writing as an amendment to the lease,
1103 which was proposed and is very clear, and we can expound upon that.

1104

1105 With your permission, Governor, Mr. Belles.

1106

1107 **Governor Otter:** Without objection.

1108

1109 **Mr. Belles:** Governor, other Land Board members, Director Bacon. I'm Bud Belles, President of Priest
1110 Lake State Lessees. My wife and I have owned or leased lot 80A at Priest Lake in Cavanaugh
1111 Bay. My family has held that lease since 1948. I had a PowerPoint presentation, which I cannot
1112 show, which I apologize. I have given the – a set of those slides to Susan and hopefully that can
1113 be distributed later on. There is some information on those slides that I am not showing or will
1114 be mentioning in my prepared speech.

1115

1116 I think we're here today because we're trying to define market rent. You know, everybody has
1117 these different definitions, and I have to say that after eight hundred and forty or eight hundred
1118 and thirty-two days, I'm disappointed that we haven't been able to negotiate something. I think
1119 we've done more negotiation while Jim was up here just recently – just a couple of minutes ago
1120 – than we've done in the past eight hundred and thirty-two days. There's an open discussion
1121 about how – about this – how – about that.

1122

1123 You know, prior to our first meeting, which was on April 22, 2008, you know, there was a
1124 number of other studies that talked about market rent. I'm going to mention three of those
1125 today. One was the Duffield study, which was commissioned by the State of Montana in 1993;
1126 the Knipe and Knipe study done for the State of Idaho in 1998; and the study done at the
1127 University of Idaho by their Policy Analysis Group of Cook and O'Laughlin in 2008. All three of

1128 those studies define market rent in similar terms. I'm not going to read all three of those, but
1129 the Cook and O'Laughlin report provides a very short definition in simpler terms. They say
1130 market rent is the prevailing rental price for comparable properties in the marketplace. Pretty
1131 simple. And that's what Jim was saying. We have to pay market rent. It's only fair. The same
1132 report goes on and states that the research literature leads one to question whether market
1133 rent, as the term is conventionally used, can be established for cottage site leases because so
1134 many characteristics of the market are unusual.
1135
1136 On April 22nd as of 2008, your Subcommittee met with the representatives of Priest Lake and
1137 Payette Lake. At the end of the meeting we agreed to collaboratively study – or have a
1138 collaborative study – involving all three stakeholders that would define a market or a
1139 methodology to calculate market rent. Each stakeholder selected an appraiser. The Idaho
1140 Department of Lands selected Stan Moe. We selected Ed Morse, and Payette chose Joe Corlett.
1141 All three are among the highest-rated appraisers in the State of Idaho.
1142
1143 On March 19th of 2009, we met again. The three appraisers presented their market rent
1144 methodology. It mostly consisted of twenty-one rentals at Priest Lake. Net rent was calculated
1145 by subtracting expenses from income. Pretty simple. Then they took a land contribution which
1146 was figured by dividing the land value by the total value of the land and the improvements. And
1147 market rent was simply calculated by multiplying the net income times the land contribution.
1148 And this – this study was meant to show a methodology, not provide an estimate of return to
1149 the State. In other words, it needed some perfection. This was rejected because it didn't return
1150 sufficient money to the State. At the end of that meeting, we agreed to have the appraisers
1151 redefine their methodology. Excuse me.
1152
1153 On May 15th of 2009, the third meeting was held. The appraisers presented a methodology
1154 based upon home rentals. It included a formula that permitted calculation of rent as a function
1155 of land value, similar to the previous report. From this study, we did learn that the cap rate for
1156 higher valued properties was lower than the cap rate for lesser valued properties. All three

appraisers agreed that this is a characteristic of residential rentals. The report was rejected because it was felt that the comparisons used were not valid.

The Department of Lands presented the deferred market value method at the second meeting. It was subsequently changed at this last meeting and is the method used in the lease presented today. We feel that this method still presents major issues for our lessees and that many of the current lessees will be forced to sell. This is the worst time to be selling in many years. Several cabins have already been on the market at Priest Lake for over two years and haven't even sold at reduced prices.

If a fee simple value is to be used to calculate rent, we feel that an adjustment should be made to either the value itself or the multiplier. Fee simple property has a number of unique rights that it – to – excuse me – fee simple property has a number of rights unique to fee simple property. These rights can be likened to a bundle of sticks. You know, many of these sticks are just not included in the bundle that the lessee is entitled to in like we can't sell it, we can't lease it and so on.

The reports mentioned previously suggest a lease property value should be between twenty to sixty percent less than the fee simple property. Tacoma Power uses a forty percent of appraised lake – appraised value at the property that they own and lease out at Lake Cushman. The Knipe report states two additional points that are noteworthy. First, it is interesting to note that the lessor does not view their program as generating a four percent minimum return. Rather he views it as generating a ten percent minimum return on the real value of a commodity. That it's forty percent of fee simple land. The results are the same, but from the lessor's perspective, Tacoma Power is achieving a ten percent return on the worth of the land. Excuse me.

The proposed lease uses a four percent multiplier. I don't know where that number came from. As of Friday, ten year Treasury Notes were yielding 3.69 percent. A ten-year Treasury Inflected – excuse me – Treasury Inflation Protected Security, a TIP5, sold for 1.43 percent. A number that I

1186 found very interesting when talking about the cash-on-cash return at Priest Lake and at Payette
1187 Lake – using the numbers that I have from 2006 to 2009, which are the values of the properties
1188 that were appraised in 2004 and 2007, Priest Lake returned seventeen point nine percent return
1189 on your investment. And you can think of that as buying some stock for seventy-eight point
1190 eight million dollars, which was the value of the land in 2004, adding the rent collected and
1191 premium rent and then selling it in 2009 at a hundred and forty-three point three million. That's
1192 a nice return.
1193
1194 A projection of rents from 2011 to 2015 on a current proposed lease indicate that rents at Priest
1195 would increase between six and ten percent a year. Recently fee simple sales in the north – or
1196 in the Priest Lake area on Pend Oreille and – excuse me – on Coeur d'Alene Lake have been
1197 dropping twenty to thirty percent. Pend Oreille, I'm told, is less – excuse me – is a higher
1198 percentage of – you know, this is – that's really hard to accept, you know, as a person paying out
1199 ten percent more a year on a property that's going down in value.
1200
1201 We feel that there is only one solution to this issue, and that's what was proposed today to my
1202 surprise. I applaud you. You should sell the cottage sites. And we're suggesting until that can
1203 be worked out, we'd like to see the following changes made. The multiplier instead of four
1204 percent should be three percent. We could accept that. And that – that's justifiable based upon
1205 the rights that we get with a leased property versus a fee simple property.
1206
1207 We feel that caps should be in place. As Jim mentioned, we would accept three percent either
1208 way. And we feel that a formula should be interjected into it so that higher valued properties
1209 would pay a lower rate. And that would be something that we would negotiate. And we feel
1210 that premium rent should be set at ten percent of the net leasehold value. And Mike Schmitz,
1211 who is another board member from our association, is here today along with – let's see, where
1212 are they – there's two other board members here today and some other members from our
1213 association. I think this might be a record number of people from Priest Lake to one of your
1214 meetings.

But in summary, we would – I'm asking myself – would an informed buyer agree to this lease? And I say no, you know, and it's already been mentioned that nobody, you know, bid on the two lots that were auctioned off in 2007. Now why would we sign this lease? We have a significant investment sitting on that land from fifty thousand dollars up to some that are approaching two million dollars. And those investments have increased the value of the land.

I hope that you agree with the points that I've discussed and that we can agree to things in the future. I thank you. Do you have any questions?

Governor Otter: Is that it?

Chuck.

Mr. Lempesis: Governor, I have some remarks, if I may.

Governor Otter: The man has the floor.

Mr. Lempesis: Thank you. Let me start by expressing my personal appreciation and that of my clients for the hard work of the Subcommittee. Superintendent Luna and Secretary Ysursa did go beyond the pale and beyond the call to try and facilitate meetings that were open and honest and very transparent and forthcoming, and I appreciate that as I appreciate the attention of all of the Board members. We have a fundamental disagreement today, and I want to outline it for you as best I can and then implore you not to make a decision today. And I do so based upon the credibility I hope I have established with you and the members of this Board over the years.

I think you're perilously close to resolving this problem. Closer than we think, and I have said that. But I think there is some breaking news today that may not only complicate matters but can be of value in resolving this problem. I'm anxious to know exactly what the headline in the

1244 Idaho Statesman did today to the value of leases in Priest Lake, for instance. If you're a
1245 perspective purchaser to find out today that the State may divest itself of ownership, whether
1246 it's tomorrow or ten years from now, certainly comes to play in the open market.
1247
1248 But I think we could go back to the table and resolve this and avoid what could result in – not
1249 only – and this hardly threatening, that is not my style, but I think there is certainly a prospect of
1250 protracted litigation in this matter, and I think there's also misunderstandings that could be
1251 avoided by a frank and transparent discussion.
1252
1253 I also want to make very clear that I think that there are those that for the first time, and I've
1254 been doing this issue for at least fifteen or sixteen years, I have found this Board and its
1255 members and its predecessor members to be open and honest. We have always walked away
1256 from these discussions both feeling like we got the raw end of the deal. I learned in the first
1257 year in law school that that was the makings of a good settlement as I'm sure the General did.
1258 But there has never been anything but honest give and take. I think there has been injected this
1259 year an aurora of sleazy politics that didn't need to be there. And it hasn't been injected by this
1260 Board or the associations to the best of my knowledge. But the notion that there are high
1261 powered lobbyists out trying to cut deals with state officials is absolutely inappropriate and
1262 false.
1263
1264 For the record, I am not a high powered lobbyist, and I think all five of these members could
1265 attest to that as most of the State of Idaho. The second fact is I've never had a private meeting
1266 with any of these people concerning this issue though that would not have been unusual or
1267 anything to be – to create an uproar, and third, I've not so much as bought them lunch or even
1268 sent them a Christmas card, but I do want to thank Secretary Ysursa and General Wasden for
1269 theirs and you, too, Governor.
1270
1271 Having said that, let's move to the germane issue and how may – how we may resolve these
1272 issues. There's really three components, or maybe four, to this issue. The first is this. If you

1273 were looking at a straight real estate deal the best thing you can do is look at the customer, see
1274 what the market will bear and grab it. And if the only interest of the State of Idaho, and I've said
1275 this now for darn near twenty years, is to get the highest value out of Priest Lake, not only
1276 should you divest yourself of these cabin sites, and that may be the best course of action at this
1277 point, but you could have put time-share condos there. You could have made hotels from coast
1278 to coast. But there was always something more and that was to preserve the character of one
1279 of the crown jewels of Idaho, which is Priest Lake – to preserve that, the romance and the
1280 character of a rustic lake in its natural setting. And that has been well worth the money and the
1281 resources.
1282
1283 The other thing is that in searching to find out what is the right value, and it was said best in a
1284 report that was tendered to you from Paul, I believe it's Henneman, who is a managing member
1285 of one of the most respected appraisal and commercial real estate firms, but you look for
1286 equilibrium. It isn't a point of seeing how much anybody can gouge in their rents, but how
1287 much the market will bear without devaluing the property. And I hope that you do certainly
1288 respect that by increasing rents you can kill the goose that laid the golden egg. There is a
1289 certain equilibrium that you can go past in which the cost of owning or renting becomes such
1290 that nobody wants them anymore. And whether it is in the private or the public domain, the
1291 values then decline rapidly. So by raising rents, you can effectively devalue the asset.
1292
1293 Let me also point out for you that based upon the 2007 plan for asset management in this State,
1294 it was estimated that residential real estate should have a rate of return on an ROA, Return on
1295 Asset, of between two and twelve percent. Both Payette and Priest Lake have dramatically
1296 exceeded that rate of – rate – Return on Asset. So the State is getting a reasonable rate of
1297 return. That's above reproach.
1298
1299 Let me deal with three issues. On the lease, first of all, it is not completed. I responded this
1300 week somewhat tardily, but let me also say that the lease was not tendered for months, and I
1301 think we would all agree that that was delayed. But the lease had not been completed. There

1302 are defects in that lease which would make it malpractice for me to permit my clients to sign the
1303 same.
1304
1305 Among my two greatest concerns is the absence of a cap upon the increases. If they signed the
1306 lease as it states, as Jim Young said, they would be writing a blank check for either a ten or
1307 thirty-five year commitment to guarantee those payments when there's no limit to the
1308 escalation.
1309
1310 The other thing that concerns me most, perhaps as a lawyer and just in the notion of
1311 fundamental fairness, is that the appeal process described on Exhibit C for Priest would be this –
1312 if we disagree, it will come to this Board and you'll decide it. Now I know that may be
1313 convenient, and it may seem fair to you, but if we disagree we think that we should reserve the
1314 same rights that we have had all along, which is to go to district court on the issue of valuation
1315 and to have our case heard. That appeal process has never been abused or over abused, but
1316 that needs to be looked at very strenuously. I do not believe that my colleagues here who are
1317 attorneys sitting on this Board or any other member could disagree that there's some notion of
1318 fundamental fairness to be employed.
1319
1320 On the issue of premium rent, let me say this. If – I understand premium rent much like the
1321 Secretary. It was done to compensate for low rents. If we're getting up to where the rents are,
1322 why are we doing premium rent? It is nothing more than a disguised tax. But let me warn you
1323 of the can of worms that you are opening. If premium rent in the amount of fifty percent is
1324 appropriate for Priest Lake and Payette, I would send out a notice to all of your grazing leases
1325 that the same thing should apply to the cattle they are selling. If indeed cattle are raised and
1326 fed upon state lands and derive a market price and an increase in value, then the State should
1327 certainly be entitled to fifty percent of the value of those fattened calves. There is no clear case
1328 in point. So – preview of coming attractions, but I think you want to seriously consider that.
1329 Premium rent was a short-term fix when we had rents that weren't perceived to be at market
1330 rent.

1331

1332 I implore you to go back to the table. I know you want to make a decision today, but I want the
1333 opportunity to visit at least one or two more times in the open to address these issues. I think
1334 you've heard today that we are very close. I believe that. But now throw into the mix this
1335 notion of selling the lots. There are things that we can do. The General's predecessor,
1336 Mr. Lance, and I proposed that more than twelve years ago. It was ill-received by this Board at
1337 the time. There is a way to do that through quasi-municipal trusts that could be significantly
1338 advantageous to both the State and the owners because keep in mind that many of the people
1339 that occupy those residences can't today buy them – can't afford to. But through the trust
1340 concept could.

1341

1342 I will end saying what I said probably thirteen years ago. I came to this issue to help resolve it. I
1343 believe that we can, and I believe that we are close. I want the opportunity to do that. To go
1344 forth today on what has been proposed would be not in concert with the best interests of either
1345 the State or the lessees.

1346

1347 Thank you, Governor.

1348

1349 **Governor Otter:** Questions. Comment.

1350

1351 Mr. Wasden.

1352

1353 **Attorney General Wasden:** Thank you.

1354

1355 Mr. Lempesis.

1356

1357 **Mr. Lempesis:** Mr. Wasden – or General Wasden.

1358

1359 **Attorney General Wasden:** First of all, I – I greet you again. Thank you for being here.

1360

1361 I wanted to outline – I realize it's a matter of record what your recommendation is.

1362

1363 **Mr. Lempesis:** Yes.

1364

1365 **Attorney General Wasden:** But I would like to outline it, and at least in my understanding, because I

1366 think I've heard a couple of things here today, three percent rate, correct?

1367

1368 **Mr. Lempesis:** Correct.

1369

1370 **Attorney General Wasden:** And then you proposed a cap should be placed upon any increases or

1371 decreases.

1372

1373 **Mr. Lempesis:** That is correct, sir.

1374

1375 **Attorney General Wasden:** Premium rent; ten percent of net, although I've also heard no premium rent,

1376 and I need a clarification on that.

1377

1378 **Mr. Lempesis:** Governor, General Wasden –

1379

1380 **Governor Otter:** Mr. Lempesis.

1381

1382 **Mr. Lempesis:** Our position for positions is no premium rent. We would be delighted if it were at ten

1383 percent, and we can live with that. And we do think it should be of net for obvious reasons as

1384 would the grazers.

1385

1386 **Attorney General Wasden:** Okay. And Governor –

1387

1388 **Governor Otter:** Mr. Wasden.

1389

1390 **Attorney General Wasden:** Mr. Lempesis, high value sites at a lower rate of some sort, and I'm not
1391 certain how that is to be determined, but that has been one of the recommendations as well as
1392 a process for adjudication in district court. Have I understood your proposal for this lease
1393 operation?

1394

1395 **Mr. Lempesis:** Indubitably.

1396

1397 **Attorney General Wasden:** Thank you very much, Governor.

1398

1399 **Governor Otter:** Further questions or comments?

1400

1401 Mr. Luna.

1402

1403 **Superintendent Luna:** Yeah, a quick question, Governor.

1404

1405 You've made a good case for your concerns. Is there – is there anything with what's been
1406 proposed that would inhibit our ability to – to sell these properties sooner rather than later?

1407

1408 Governor **Otter:** Mr. Lempesis.

1409

1410 **Mr. Lempesis:** Governor, Mr. Superintendent, I take that question is there anything in the proposal that
1411 is on – no, sir. I don't believe there is – that there would be any impediment nor has there been
1412 any impediment to do that. But I think there are – are portions of the lease that are fatal right
1413 now, and I think there are things based upon that that could be incorporated in the lease that
1414 would preserve the marketplace in the meantime for the benefit of the State and the lessee
1415 because that's going to create somewhat of a furor and uproar in the market that we could
1416 appease some of that by inclusions of provisions in the lease which give more assurances.

1417

1418 **Governor Otter:** Further comments.

1419

1420 Mr. Lempesis, couple of questions about the cap.

1421

1422 **Mr. Lempesis:** Yes, sir.

1423

1424 **Governor Otter:** It's not unusual for there to be either a LIBOR or a CPI or as a max in thirty-year leases,
1425 is there?

1426

1427 **Mr. Lempesis:** Governor, respectfully, you're absolutely correct, and I can assure you that in your
1428 lifetime you have never executed a lease without such a cap.

1429

1430 **Governor Otter:** Further comments. Questions.

1431

1432 Mr. Ysursa.

1433

1434 **Secretary of State Ysursa:** Governor, members of the Board, and Mr. Lempesis, number one, it's always
1435 a pleasure to see you. I appreciate your professionalism and courtesy, and it's continued that
1436 way for twenty-plus years.

1437

1438 The – I made a comment earlier, and I – I just kind of want your sense of it. I made a lot of
1439 comments, but your sense of it that we do have two completely – let's say unique, different
1440 scenarios between the lakes on ownership and what – what we have at Payette Lake, the
1441 disjointed ownership, the privates, the whatever – up at Priest, which you know a lot better
1442 than I do, but it's ninety-plus percent federal and state and over three hundred and some lots.
1443 A lot of folks who are here are from Payette and we're – there's three hundred lots up at Priest
1444 Lake. They're all lakefront lots. This pattern of trying to dispose of those or exchange or
1445 whatever would be much more of a – I think a long term difficult task, but compared to – we've

1446 already done a lot of exchanges and things like that in the Payette area. Do you have any sense
1447 of how you feel about that scenario?
1448
1449 **Governor Otter:** Mr. Lempesis.
1450
1451 **Mr. Lempesis:** Governor, Mr. Secretary, I'm glad you asked that question, and I do and we explored that
1452 in some detail with even financiers some years ago when the Honorable Al Lance brought that
1453 to my attention. I think there's a grave distinction between the two. I think you could easily
1454 divest yourself of the properties at Payette, and I'm not speaking for the Payette people at all,
1455 without any probable prospect of either environmental or ambient damage to the lake nor any
1456 adverse effect on adjoining state properties, okay, because you have adjoining state properties
1457 with timberlands adjacent. That's always been one of the concerns.
1458
1459 At Priest, I am of the mind in my stream of conscious, that selling individual lots is fraught with
1460 serious issues, okay, while my clients may disagree with me, but it is. And that the manner to do
1461 that would be a fairly creative means of creating a quasi-public trust in which you would sell
1462 those in and let someone else – the owners themselves – manage their rent of other lots where
1463 people can't buy them, but there is a creative way of doing that and keeping them intact to a
1464 large extent, which would help preserve the character of the lake and also create value to the
1465 State in its – in not creating an adverse climate for its timber harvest and management of
1466 adjacent lands.
1467
1468 **Governor Otter:** Mr. Ysursa.
1469
1470 **Secretary of State Ysursa:** Governor and Mr. Lempesis, I appreciate that. What do you – and this Board
1471 has some other long-range plans on maybe the Constitution and all that – when we dispose of –
1472 right now, we cannot dispose of our property without going to public auction –
1473
1474 **Mr. Lempesis:** Right.

1475

1476 **Secretary of State Ysursa:** – as required by Constitution.

1477

1478 **Mr. Lempesis:** Correct.

1479

1480 **Secretary of State Ysursa:** Would you think a change is merited there or some other option be made
1481 available before we could actually proceed on some of this stuff.

1482

1483 **Governor Otter:** Mr. Lempesis.

1484

1485 **Mr. Lempesis:** Governor, Mr. Secretary, it would be incompetent for me to even speculate or render an
1486 opinion on that without making a really good analysis. I don't know.

1487

1488 **Secretary of State Ysursa:** I – I can appreciate that.

1489

1490 **Governor Otter:** Further questions.

1491

1492 Mr. Wasden.

1493

1494 **Attorney General Wasden:** Thank you, Governor.

1495

1496 Mr. Lempesis, in my earlier question I think I failed to leave out one important term, and I
1497 wanted to clarify, and that is that your proposal is for a thirty-five year lease term. Is that
1498 correct?

1499

1500 **Governor Otter:** Mr. Lempesis.

1501

1502 **Mr. Lempesis:** Governor – Governor, General, that is correct.

1503

1504 **Attorney General Wasden:** Thank you.

1505

1506 **Governor Otter:** Any other questions.

1507

1508 Chuck – or Mr. Lempesis – help me on premium rent. You know, I'm aware that many times
1509 depending upon the location, location, location where a – let's say a hotel room with regular
1510 bed, bathroom, all the amenities, everything is the same, even a terrace, only it's looking the
1511 wrong way.

1512

1513 **Mr. Lempesis:** Yep.

1514

1515 **Governor Otter:** I'm on one side of the building, and it cost me a hundred bucks; I go to the other side of
1516 the building, and it cost me a hundred and fifty dollars.

1517

1518 **Mr. Lempesis:** You usually get the better one; I usually get the bad one, Governor.

1519

1520 **Governor Otter:** Isn't that what we're talking about when we talk about premium rent? Location,
1521 location, location?

1522

1523 **Mr. Lempesis:** Governor, in –

1524

1525 **Governor Otter:** Listen, if you all want to answer the question, go ahead. But I asked Mr. Lempesis.

1526

1527 **Mr. Lempesis:** You've got a way of handling things, don't you.

1528

1529 Governor, in all – with due respect, I don't think – I think in the classic circumstance, your
1530 analysis is on target. In this scenario, it's been a different – it's distinguished not by location or
1531 anything else. It was merely in the context of these leases a stop gap that said – and J. D.
1532 Williams, former Controller Williams, said it best. He said okay we'll go to the two point five,

1533 but we're not backing off the premium rent because we'll pick it up there. It's always been a
1534 pick it up there philosophy that that made up the difference.
1535
1536 So if you get to market rent, or anywhere close to market rent, as has also been the observation
1537 of most of the Board members in the past and present, you wouldn't need premium rent. Now
1538 let me offer this, if I may, Governor, in the remaining few moments that we have. We brought
1539 with us today Mike Schmitz, who is probably the best expert on that topic as it relates to the
1540 market at Priest Lake, who could – if we could segue way to that, sir, he can answer that far
1541 better than I.
1542
1543 **Governor Otter:** Thank you. And I would ask him to come forward.
1544
1545 One of the reasons that I – I think it's important to identify –
1546
1547 **Mr. Lempesis:** Yeah.
1548
1549 **Governor Otter:** – exactly what we mean is that it's going to continue to conflict at a point in time when
1550 we do want to sell it –
1551
1552 **Mr. Lempesis:** Correct.
1553
1554 **Governor Otter:** – because there'll be a premium price on premium rent.
1555
1556 **Mr. Lempesis:** Governor, you couldn't be more right, and the problem with the premium rent scenario,
1557 and I'm saying this as a citizen of Idaho as much as the lawyer for the Priest Lake State Lessees,
1558 is in that scenario, if your goal is to sell these, it is counter-intuitive to be doing what you're
1559 doing because you're going to drive down prices ultimately in the valuations. I really believe
1560 that, and we could go through that in a scenario, but you may be wishing for something you
1561 don't want in that scenario.

1562

1563 **Governor Otter:** That's why I think it's important that we spend a little time on this.

1564

1565 Mr. Schmitz.

1566

1567 **Mr. Schmitz:** Hello, my name is Mike Schmitz, Mr. Governor, members of the Board. To just give you a
1568 little background, when – when – the premium rent is what I'm here to talk about in specific,
1569 and I personally think that the escalation from the ten percent of the gross to fifty percent of
1570 the gross of the leasehold value and premium rent is a mistake. And I think it's got a lot of
1571 adverse effects that would go along with it. I've been a real estate broker for the last twenty
1572 years, and of that twenty years about eleven of it I specialized in lakefront property sales and
1573 development both in Washington and Idaho and, in specific, Priest Lake was one of my main
1574 lakes that I sold on.

1575

1576 In our opinion, this imposition of the fifty percent premium rent will kill the market. It'll drive
1577 the leasehold value to zero. No discerning and informed buyer will buy something that the next
1578 day is worth half of what they purchased it for. No lender's going to lend on it either. So you'll
1579 bring it to zero. There's a lot of ripple effects on that as well. Once those leases go down in
1580 value, all you're going to be buying is the leasehold improvements. Those leasehold
1581 improvements will then be the competition for all other products on the water. So every other
1582 federal lease in Priest Lake's case, or fee simple properties, will then have to compete with the
1583 lower-valued state lease properties and as such they're going to have to drop their price.
1584 Anybody that's going to go up there and say I can either spend eight hundred thousand dollars
1585 on this fee simple property or a hundred thousand dollars on this state lease property – it's a
1586 pretty easy choice.

1587

1588 So with that, you drop in value, which as you know is what you've been calculating your
1589 leasehold values on. That's going to drop as well. Furthermore, the other thing that's going to
1590 happen is you're going to decline in values. People aren't going to invest more into their

1591 properties. They're not going to fix them up; they're not going to build them. They're not going
1592 to spend the money out. So you're going to be losing jobs in the area as well. The suppliers, the
1593 contractors, the resorts in the area – they're going to all see a decline in value in our opinion. I
1594 just think it's – it's a big mistake, and I think that you're going to have a lot of adverse effects
1595 that are going to go along with it.
1596
1597 The State of Idaho, the Parks Department did a – hired an appraiser out of Spokane to do an
1598 evaluation on Heyburn State Park up at Coeur d'Alene, and they saw a decrease in value of
1599 between fifteen and thirty percent over the last two years. I think you're going to see that
1600 effect hit harder and stronger at both Pend Oreille and Priest as it may have already hit. I don't
1601 – there's been very few sales up there so we don't know exactly what's going to happen at this
1602 point. But with the imposing in the lease fees and the premium rent, I think it only could cause
1603 a stronger effect and decrease in values over – over all. I submitted this letter as well to all
1604 Board members and Governor, and if you've got any questions, I'd be happy to answer what I
1605 can.
1606
1607 **Governor Otter:** I was interested in – in reading through your letter, and especially the information on
1608 premium rent. And one of the reasons I wanted to pursue this is I think there was a
1609 misconception out there of what we meant by premium rent –
1610
1611 **Mr. Schmitz:** Okay.
1612
1613 **Governor Otter:** – or what was intended. And it's very hard to define because you probably won't find
1614 such in any other contract anywhere.
1615
1616 **Mr. Schmitz:** I've never seen it, and I currently deal in a lot of leases – commercial leases – throughout
1617 eastern Washington, northern Idaho, and it's never – I've never seen it. Kind of – kind of – you
1618 know, you're not talking apples to apples because most tenants in a commercial building say
1619 don't have a whole lot in the way of – of – of their own money, if you will, into that property. So

1620 it's a – that's different in that regard. They also aren't emotionally attached to a property like –
1621 like a lake property, and that's how do you put a value on that.
1622
1623 **Governor Otter:** Mr. Ysursa.
1624
1625 **Secretary of State Ysursa:** Governor and Mr. Schmitz, thank you very much for your presentation.
1626 Premium rent and what we have – the concept, and Mr. Lempesis is absolutely right, it's kind of
1627 the stop gap measure because over the years we – we had a – a lease rate that was lower than
1628 any other of these studies, be it Duffield, be it Knipe, be it McFadden, be it others. They were
1629 saying we should be getting five percent, four percent maybe on Knipe if there were – we didn't
1630 have caps or something. You mentioned Heyburn Park. You mentioned it. I didn't. Three point
1631 – do you know that what their current formula is?
1632
1633 **Mr. Schmitz:** I'm not familiar with it, no.
1634
1635 **Secretary of State Ysursa:** Well, I – I have a hunch it's three point seven five percent of the current
1636 value. We are not there. And they are not under a trust mandate. So the balancing act that we
1637 have, even use the term premium rent, is the fact that we're lower – on the low end. And we've
1638 heard it before and Mr. Lempesis said it. If we were out there getting what we consider
1639 absolute – there's always going to be some leasehold value involved. You've got a lease;
1640 somebody else wants it at times, we hope. But there's going to be some leasehold value in
1641 there, but where is the fairness, again, to the endowment for folks to assign leases and receive a
1642 pretty good kick. Now, okay, lately we haven't or whatever. Just in that six-year period when
1643 things were hot of twenty-five million dollars and we received two million dollars when the
1644 value was significantly and substantially because of our land. Not their land – our land. And
1645 who should be capturing that value in your respected opinion.
1646
1647 **Mr. Schmitz:** Well, I agree with Mr. Lempesis. I'm going to digress just a little bit, if I may. It's my
1648 understanding that with – with what they found at Heyburn, they dropped the lease amounts

1649 due. So they've actually done a reduction in those leases because of the loss in value on
1650 property so –
1651
1652 **Secretary of State Ysursa:** They did. They went from five down to three point seven five.
1653
1654 **Mr. Schmitz:** Okay. So – so the whole story would be the best in my opinion. I think there should be a
1655 sharing of it. To what degree, I don't know. That's something that would have to be negotiated
1656 out. The other part of it is it doesn't make any sense in my world to say fifty percent or any
1657 percent of the gross value. If a person buys a place for a hundred thousand dollars today, and
1658 has to sell it for a hundred thousand dollars tomorrow, whether it be ten or fifty percent, he
1659 loses that much money. It's not a reasonable request.
1660
1661 **Governor Otter:** Mr. Wasden.
1662
1663 **Attorney General Wasden:** Thank you, Governor.
1664
1665 Mr. Schmitz, I also appreciate your presence here and your letter, which we received this
1666 morning. Would you agree with me that if these leases were at market rent, there would be no
1667 need for premium rent?
1668
1669 **Mr. Schmitz:** I suppose theoretically, yes.
1670
1671 **Attorney General Wasden:** Okay. Great.
1672
1673 No additional questions, Governor.
1674
1675 **Governor Otter:** Mr. Lempesis.
1676

1677 **Mr. Lempesis:** Governor, with your pleasure, may I just respond to Secretary Ysursa on the Heyburn
1678 issue real quickly because there's a – there's a distinction here.
1679
1680 **Governor Otter:** Certainly.
1681
1682 **Mr. Lempesis:** And let me disclose, as Mr. Ysursa or Secretary Ysursa knows, I represent the Heyburn
1683 Park –
1684
1685 **Secretary of State Ysursa:** You can fill us in.
1686
1687 **Mr. Lempesis:** – lessees, but – that it's hard to compare that – you and I both like apples for apples, and
1688 the problem there is that Heyburn's values of the lots we're talking about are de minimis
1689 compared to Priest.
1690
1691 **Secretary of State Ysursa:** They're low.
1692
1693 **Mr. Lempesis:** And that's the reason three and a half percent of a fifty thousand dollar lot pales in
1694 significance to three and a half percent of a half a million dollar lot. So they're – and they did
1695 devalue the actual market values as part of that –
1696
1697 **Secretary of State Ysursa:** Yes.
1698
1699 **Mr. Lempesis:** – negotiation by fifteen or twenty percent.
1700
1701 **Secretary of State Ysursa:** And I – I would assume that will be reflected in our Priest Lake –
1702
1703 **Mr. Lempesis:** Yeah.
1704
1705 **Secretary of State Ysursa:** – index –

1706

1707 **Mr. Lempesis:** Yeah.

1708

1709 **Secretary of State Ysursa:** – this time.

1710

1711 **Mr. Lempesis:** Thank – thank you for letting me make that clear.

1712

1713 **Governor Otter:** Mr. Luna.

1714

1715 **Superintendent Luna:** Governor, thank you. I have a question for Mike.

1716

1717 Mike, in your last comment, you made the – you made the statement that who would buy
1718 something with these kinds of terms. And – and – you used that term buy and that's the thing
1719 that I've been struggling with, and I don't even know exactly how to articulate it. But let me ask
1720 you the question – do you think there's a difference between what a person should expect on a
1721 return if they've leased something versus buying it? Because this is a lease, and I keep going
1722 back and forth on this trying to figure out what – what is fair. And I know when I lease a piece of
1723 property I'm entitled to the leaseholder improvements, but not necessarily to the increase in
1724 the value of the lease. If I lease a car, I take it back at the end of that lease, and I'm not entitled
1725 to anything. I've basically paid to use the car for X number of months and X number of miles.
1726 So anyways, I'm trying to figure out the question in my own mind, but I'll just ask you that
1727 question – you know, you mentioned buying it, but you're not buying it – the land – you're
1728 leasing it, and does that have, in your mind, have an influence then on – on what the
1729 leaseholder should be entitled to when the lease changes hands and for – for a price.

1730

1731 **Governor Otter:** Mr. Schmitz.

1732

1733 **Mr. Schmitz:** Yes, sir. When I use the term buy, certainly you're buying the improvements. That's an
1734 outright purchase. And then you're buying, if you will, the rights to the lease. We call it the

1735 leasehold value. So my understanding of the question is what kind of return would you expect
1736 or would you desire –
1737
1738 **Superintendent Luna:** Or would it be the same? Do you think in your mind whether you bought the
1739 land or you're leasing it that when it changes hands, you should be entitled whether you bought
1740 it or leased it – there's no difference in what you should be entitled to in the – in the proceeds.
1741
1742 **Mr. Schmitz:** I'm going to digress just a little bit in that when you're buying a, if you will, a vacation
1743 home, generally people – generally speaking people don't expect or don't look at it as a
1744 investment with a return. They look at the return as time with their family, that sort of thing.
1745 So do they pencil it out like on a commercial building and say do I expect a three percent or six
1746 percent or nine percent or whatever return on my cash and investment, they look at it
1747 dramatically different because it's a lot more like purchasing a home, like a primary residence.
1748 That being said, do most people expect a – to – to receive that return, if you will, or increase in
1749 value at the end of the term? Most people do, but most people don't expect to see a whole lot
1750 in the way of a cash increase in value return, generally speaking, when they're buying a lake
1751 home. Certainly there's investors out there that that's what they've tried to do. It's proven
1752 unsuccessful. But overall it's really – they're buying a place to get away, and they're not really
1753 looking at it for a fixed return.
1754
1755 **Governor Otter:** Mr. Schmitz, what about the opportunity – they're going to study an opportunity cost
1756 here – if I'm using the money to put it up here, I can't use the money to put it someplace else
1757 and so –
1758
1759 **Mr. Schmitz:** Absolutely. Generally speaking that opportunity cost, Mr. Governor, is do I buy this
1760 vacation home and what does it cost me, or do I go to Hawaii, what does that cost me. It's not a
1761 do I buy this vacation home or do I buy this commercial building. I've never run into that. Or do
1762 I rent it – Hills Resort – for three weeks or two weeks or whatever it may be, or do I buy this
1763 place and use it all the time and or rent it out to the person at cost or whatever it may be. But –

but I've never seen it, in my experience, I've never seen someone say do I buy this vacation home or do I buy this investment property.

Governor Otter: Well, I don't doubt that it – I wouldn't give a certain amount of value to the environment that I'm creating for myself and those who I'm going to share it with but –

Mr. Schmitz: Yes.

Governor Otter: – if – if I have to hock my inventory at my plant in order to buy that vacation home, I'm going to – I'm going to review the opportunity cost and that present time use of that money.

Mr. Schmitz: Absolutely.

Governor Otter: Mr. Lempesis.

Mr. Lempesis: Governor, may I take a shot at just supporting that – what you're saying because I think you're absolutely correct, and that's how I have always seen this on the premium rent issue is if I'm looking at buying a lease at Priest Lake, and I spend umpteen hundred thousand dollars or whatever it is to do that, I don't have a lot of money, but I have vacation property – I'm not going to put that there without the notion of getting it back, okay, somehow. If I buy property, those payments I make historically in America, wonderful place to live, when I sell my home someday all that investment I make comes back to me. Okay. That's always been the notion. When we were young people buying our first home, well, it's like a savings account, right. Well, when you're leasing those lots at Priest Lake, you don't get that back, do you. So the only place that the lessees ever see that to come back in making their analysis of whether they should buy that lease, as Mike has phrased it, is when I do sell my leasehold, I will recover some of that. Otherwise it would be nothing more than tickets to Disneyland. You'd never get it back. I don't know if that helps.

1793 **Governor Otter:** Further discussion.

1794

1795 If –

1796

1797 Mr. Ysursa.

1798

1799 **Secretary of State Ysursa:** Governor, members of the Board and Mr. Lempesis, I guess you brought to
1800 my mind another question I've always had, and it's probably maybe just an observation because
1801 we've – we've fostered the environment that these are investments.

1802

1803 **Mr. Lempesis:** Uh-huh.

1804

1805 **Secretary of State Ysursa:** And that horse has been out of the barn and running. Premium value – I call
1806 them – conveniently call the people – and in no derogatory terms – flippers.

1807

1808 **Mr. Lempesis:** Uh-huh.

1809

1810 **Secretary of State Ysursa:** And that was when the real estate was just flying.

1811

1812 **Mr. Lempesis:** Uh-huh.

1813

1814 **Secretary of State Ysursa:** Especially at Payette, but that same degree, a little lesser amount, at Priest
1815 Lake. And what was the purpose of these initially? Now having said we've – we've really gotten
1816 off the track. These – what about the person this is supposed to be a real nice vacation
1817 residential lot – I don't – that people do not have the opportunity to have around a lake like
1818 Priest –

1819

1820 **Mr. Lempesis:** Uh-huh.

1821

1822 **Secretary of State Ysursa:** – around a lake like Payette. And the ability just to have that – not as an
1823 investment –
1824
1825 **Mr. Lempesis:** Uh-huh.
1826
1827 **Secretary of State Ysursa:** – it should be the opportunity to have a recreational site on the lake, the lake,
1828 the lake.
1829
1830 **Mr. Lempesis:** Uh-huh.
1831
1832 **Secretary of State Ysursa:** And when they sell these, i.e., assign them, and make – I don't want to say a
1833 profit – just make money off of – the reason for the appreciation is the lake, the lake, the lake.
1834 The beneficiary, the beneficiary, the beneficiary –
1835
1836 **Mr. Lempesis:** Yeah.
1837
1838 **Secretary of State Ysursa:** – should be getting that value, not the people who put – and you want it to
1839 be – and what we've got is a very quote, unquote –
1840
1841 **Mr. Lempesis:** This is good.
1842
1843 **Secretary of State Ysursa:** – no – irrational market because how rational is it for people to put
1844 substantial improvements on somebody else's property. We're all irrational.
1845
1846 **Mr. Lempesis:** Nobody –
1847
1848 **Secretary of State Ysursa:** And now –
1849
1850 **Mr. Lempesis:** Governor –

1851

1852 **Secretary of State Ysursa:** – the problem with this whole thing is – is in our opinion there was quite a
1853 sweet deal going on, and we're taking the sweetener out and folks are upset. We know that.

1854

1855 **Governor Otter:** Mr. Lempesis. Response.

1856

1857 **Mr. Lempesis:** Governor, Mr. Secretary – Ben – I share with you that we have jointly created a
1858 nightmare here or a monster. And now we need to in the most fair manner we can –

1859

1860 **Secretary of State Ysursa:** Extricate ourselves.

1861

1862 **Mr. Lempesis:** – clean it up. But the difference – I think you answered your own question in your
1863 analysis. And it brought to mind something that I really hadn't distilled, and it's an important
1864 point. When I buy my three bedroom, one and a half bath rancher to live in with my family, at
1865 the end, whether it appreciates or not, I have a return of my equity, okay, because I have paid
1866 down my mortgage. So at some point, I get my payments back. That's the savings account I was
1867 referring to.

1868

1869 If the State took all of the premium rent or all of the profit, if they were entitled to that, I would
1870 never do that in this circumstance. And I think that – if you think through that, maybe not even
1871 right now, that may be the largest distinction is there's no return of even the equity other than
1872 through what I can sell my leasehold interest for. You don't get any of those payments back on
1873 any lease.

1874

1875 **Governor Otter:** So then – so then why wouldn't I get an offer of look, you get your ante back – you get
1876 your sunk back – and then we split everything after that.

1877

1878 **Mr. Lempesis:** Well, in all honesty, Governor, I was just going down some of that path, or maybe that –
1879 maybe it's the first in, first out – FIFO – sort of thing. That's why I want to go back to the table,

1880 Governor, I really do, and see if we can work some of this out if you're obliged to do so. But I
1881 think you may be on to something that if I owned it for ten years, and I've paid two hundred
1882 thousand dollars, maybe that's the first money to come out and we split the rest or you get the
1883 next part or – I think there's a fairer play there than just saying off the gross we take fifty
1884 percent. That to me is a little ludicrous or over reaching. That's all.
1885
1886 **Governor Otter:** I don't agree with the final part of what you said. I think you owe something as far as
1887 the rent goes, but if I bought an existing improvement –
1888
1889 **Mr. Lempesis:** Right.
1890
1891 **Governor Otter:** – on a piece of state land –
1892
1893 **Mr. Lempesis:** Right.
1894
1895 **Governor Otter:** – and I paid a hundred thousand dollars for that, and this is we're still arguing over
1896 premium rent –
1897
1898 **Mr. Lempesis:** Yeah. All right.
1899
1900 **Governor Otter:** I think you're entitled to the hundred thousand back. Not any of the rent you paid, but
1901 you're entitled to the hundred thousand back, and then – but you should share the rest of it in
1902 order to satisfy, I think, what Ben has as a reasonable – or Mr. Ysursa – has a reasonable
1903 argument.
1904
1905 Anyway. Any other questions.
1906
1907 **Attorney General Wasden:** Governor, if this discussion portion is over, I was wondering if we might be
1908 able to take a few minutes break.

1909

1910 **Governor Otter:** Okay. Let's take a five-minute break. We stand adjourned subject to the call of the
1911 Chair.

1912

1913 *(At 11:27 a.m. a brief recess was taken. The meeting resumed at 11:36 a.m.)*

1914

1915 **Governor Otter:** State Board of Land Commissioners' meeting will come back to order. Prior to going at
1916 ease we had just completed with the Priest Lake presentation. We will now have the
1917 beneficiaries' presentation, and we will start with – for one half hour – and we will start with
1918 Children's Land Alliance Supporting Schools or CLASS.

1919

1920 Representative.

1921

1922 Oh, good.

1923

1924 **Ms. Escheverria:** Thank you, Governor, members of the Land Board. I assure you I will not take thirty
1925 minutes this morning. So thank you for the opportunity to be here today to speak with you
1926 about the cottage site lease issue.

1927

1928 **Secretary of State Ysursa:** Karen, I certainly know who you are, could you identify yourself –

1929

1930 **Ms. Escheverria:** I apologize, Mr. Ysursa. It's Karen Escheverria, and I'm the Executive Director of the
1931 Idaho School Boards' Association. And I'm here today speaking on behalf of the Idaho Children's
1932 Land Alliance Supporting Schools, also known as CLASS. CLASS is a coalition of education
1933 organizations that act as guardians on behalf of the beneficiaries of Idaho's school trust lands.
1934 Our alliance is committed to advocating for the prudent and profitable management of the
1935 school trust lands in permanent funds to sustain each child's birthright to the best possible
1936 education. I would like to quickly acknowledge the other members of CLASS who are here with
1937 me today – Robin Nettinga from the Idaho Education Association; Laurie Boeckel, Jan Sylvester

1938 and Cindy Schiller with the PTA; and Wayne Davis with the Idaho Association of School
1939 Administrators.
1940
1941 We understand that the issue of cottage site leases has been discussed and debated for years.
1942 We've read and reviewed many documents that resulted from studies of this issue, and we met
1943 with Secretary of State Ysursa and Chief Deputy Tim Hurst who explained the plan that is before
1944 you today. However, neither I nor any of my CLASS members consider ourselves experts on this
1945 technical issue. We do, however, understand that the Constitution requires the Land Board to
1946 manage the endowment lands solely for the financial benefit of the beneficiaries. That includes
1947 the two hundred and seventy-five thousand current school children and the future school
1948 children of Idaho.
1949
1950 Several weeks ago we received a copy of Attorney General Wasden's opinion about this issue,
1951 and we wholly concur with that legal opinion. We appreciate the work of Secretary of State
1952 Ysursa and Superintendent Luna that they've put into this plan. We also understand that the
1953 plan makes great strides to improve the financial benefits to the beneficiaries. Again, we just
1954 don't think it goes far enough.
1955
1956 We are here to urge you to adopt the lease rate plan that will ensure the state endowment
1957 lands achieve the greatest financial benefit for our State's current and future children. We are
1958 cognizant of the various political pressures with which you must wrestle today. However, in the
1959 end we are confident that your constitutional obligation will far outweigh any of those political
1960 pressures.
1961
1962 Thank you for allowing CLASS to address you this morning, and thank you also for your service to
1963 the State of Idaho. We appreciate your work on behalf of the beneficiaries.
1964
1965 **Governor Otter:** Questions.
1966

1967 Mr. Wasden.

1968

1969 **Attorney General Wasden:** Governor –

1970

1971 Karen, I wanted to thank you for being here today. Oftentimes in this Board we've heard much
1972 from a variety of people over many years, but it's really great to have the beneficiaries here, the
1973 recipients of what we're trying to do actually here to speak to us. So I wanted to thank you for
1974 being here, and invite you to return often to monitor what it is we are doing and making certain
1975 that we are fulfilling our constitutional responsibilities. So thank you.

1976

1977 **Ms. Escheverria:** Thank you, Attorney General Wasden.

1978

1979 **Governor Otter:** Mr. Luna.

1980

1981 **Superintendent Luna:** Karen, thanks for being here. And I have a question. I guess – I thought maybe
1982 that's where the Attorney General was going, but could – could – you've mentioned what I think
1983 we all want, and that is the maximum return for the beneficiary. You know, the Attorney
1984 General went through great lengths to get those who presented to tell us what would your
1985 definition of that be. What would be the terms then that you and your group would agree
1986 would meet our constitutional obligation? Are – are you prepared? Do you have any –

1987

1988 **Ms. Escheverria:** Governor, I received –

1989

1990 **Superintendent Luna:** I'm not trying to put you on the spot. If not, I understand. But I'm just curious,
1991 you know. You've seen the proposal that the recommendation that is being – been made.
1992 What would your recommendation be that would be different?

1993

1994 **Ms. Escheverria:** Governor Otter, Superintendent Luna, I'm – unfortunately, again, I – I'm not familiar
1995 enough with the technical issues to address specific pieces of the plan.

1996

1997 **Superintendent Luna:** But –

1998

1999 **Governor Otter:** Mr. Luna.

2000

2001 **Superintendent Luna:** But you're convinced that the recommendations that are put forward aren't
2002 going far enough.

2003

2004 **Ms. Escheverria:** Governor Otter, Superintendent Luna, correct.

2005

2006 **Superintendent Luna:** Okay. Thanks.

2007

2008 **Governor Otter:** In which direction?

2009

2010 **Ms. Escheverria:** Governor Otter, we would like to see that get closer to market value than what the
2011 plan is right now.

2012

2013 **Governor Otter:** Any other questions?

2014

2015 Mr. Ysursa.

2016

2017 **Secretary of State Ysursa:** Governor and Karen, I'm not going to ask you what your definition of market
2018 rent is and what it ought to be. I think we've heard enough of –

2019

2020 **Governor Otter:** Premium rent.

2021

2022 **Secretary of State Ysursa:** – the premium rent. I think we've heard enough on that. And, again, I just
2023 want to echo the comments and thank you for the presentation. And I think both last week and
2024 this week, if anything I think we've had some fruitful discussions and that the Land Board has

2025 some very important issues, and our number one mandate is article 9, section 8 and that's to
2026 get moneys for our endowed – our endowment institutions, and obviously our biggest
2027 endowment is Public Schools. So I thank you for your testimony.
2028
2029 **Ms. Escheverria:** Thank you.
2030
2031 **Governor Otter:** Karen, I'd be interested if your organization or the organizations that are in support of
2032 the beneficiaries – all we've talked about – we've talked an awful lot, I should say, about cash
2033 flow. What we get month to month, year to year. But what about the – what about the idea of
2034 liquidating these assets and putting the corpus or trading for a new asset that would also
2035 hopefully cash flow.
2036
2037 **Ms. Escheverria:** Governor Otter, as long as that were a benefit, a greater benefit to the beneficiaries, I
2038 think we'd be in favor of that.
2039
2040 **Governor Otter:** Any other questions or comments?
2041
2042 Thank you.
2043
2044 **Superintendent Luna:** Thanks, Karen.
2045
2046 **Ms. Escheverria:** Thank you.
2047
2048 **Governor Otter:** Are there any other beneficiaries here that would like to be heard?
2049
2050 Good. Okay.
2051
2052 **Attorney General Wasden:** Governor.
2053

2054 **Governor Otter:** Your turn, yes.

2055

2056 **Attorney General Wasden:** That is correct.

2057

2058 **Governor Otter:** Attorney General – are you going to call somebody or are you going to testify?

2059

2060 **Attorney General Wasden:** I would actually call only one individual to speak, Governor, and that's Terry
2061 Anderson.

2062

2063 **Governor Otter:** Okay.

2064

2065 I had – I must admit, Attorney General, I had anticipated Terry going earlier and other people
2066 testifying. So what I'm going to do is after we hear Terry, if there are some rebuttals to that by
2067 those who have testified earlier, I'm going to permit a certain amount of time for that.

2068

2069 **Attorney General Wasden:** That's fine with me, Governor.

2070

2071 **Governor Otter:** Okay.

2072

2073 Mr. Anderson.

2074

2075 **Mr. Anderson:** Governor, distinguished members of the Board, it's a pleasure to be here. I'm from
2076 Montana so I feel pretty close to home, but you can't really get here from there so you have to
2077 go to Utah first. I'm Executive Director of an organization called Property and Environment
2078 Research Center, a research institute in Bozeman, Montana. I'm a Professor Emeritus from the
2079 Montana State University where I taught economics for twenty-eight years. I've been an
2080 adjunct professor at the University of Cornell Law School, Stanford Law School and Stanford
2081 School of Business. I'm also a Senior Fellow with the Hoover Institution at Stanford University,

2082 which allows me to escape a bit of spring in Montana, which is not a place one wants to spend
2083 time.
2084
2085 I was asked by the Attorney General and his office to review what the Land Board has been
2086 doing and what is being proposed as a professional economist and that charge revolves around
2087 one specific goal, to evaluate what the Land Board has done, is proposing to do based on its
2088 constitutional requirement and its statutory requirement. That means that we have to focus on
2089 the Prudent Investor Standard and that alone for my purposes. I should interject, by the way,
2090 that I was joined in this project by a colleague, Reed Watson. I'll speak in the first person
2091 singular, but he deserves some of the credit, or blame, depending on which way you'd like it to
2092 go.
2093
2094 As a prudent investor, it's crucial, I think, to focus on two aspects of asset management. One is
2095 the rate of return on the asset, and one is the value of the asset as has been discussed already.
2096 The rate of return is really something that is outside the hands of the people in this room,
2097 outside the hands of the people in this city, this state. It's in the hands of Adam Smith's – it's in
2098 Adam Smith's invisible hand of the marketplace. It's determined whether you're the federal
2099 government, a state agency or a private investor. It's determined by what markets tell you the
2100 prudent rate of return is. And therefore it's up to the Land Board, I believe, to investigate what
2101 are rates of return that a Board like this should be receiving on the assets that it manages. If it
2102 were getting a very, very low – even lower than two point five percent, that would not be
2103 prudent in a market of the kind even that we're in today.
2104
2105 So first and foremost, the Land Board, I think, to meet its prudent – to meet the Prudent
2106 Investor Standard must consider rates of return. Second, it must consider the value of its assets.
2107 And it must ask itself what do - does the Board think will happen to the value of those assets
2108 over time.
2109

2110 There was a time, not too many years ago, when we all would have said well, they're going up in
2111 value, duh. Now we're a little more questioning of whether our land, our houses, generally real
2112 estate and other assets, will always rise as they did during those good old years. That said, then,
2113 the Land Board has a crystal ball it must look into to determine this because there is not a clear
2114 market standard by which one can estimate what will happen to those land values.
2115 Nonetheless, it's part of what the discussion so far this morning has been about with respect to
2116 divestiture and rates of return on asset.
2117
2118 Let me emphasize at the outset that in thinking about this from a prudent investor investment
2119 perspective, this has nothing to do with fair; this has nothing to do with pristine quality of lakes.
2120 This has nothing to do with the kinds of subjective values that all of us at this table and in this
2121 room hold. We all have standards of fairness. We all have standards of what we think the
2122 environment should be like, but those are not necessarily what the prudent investor should
2123 consider unless such things as that value of the lake contributes to the value of the asset near
2124 that lake.
2125
2126 With that in mind, let me turn to the questions then of what constitutes market rent and market
2127 value and do so in the context of leasehold value, terms that have been focused on a great deal
2128 so far this morning. And let me say from the outset that to think about what is the value of the
2129 asset, it is strictly a matter of separating the two components, the land value and the cottage
2130 value or the improvement values. There's nothing more; nothing less there. The buyer of that
2131 bundle purchases the bundle and purchases it with some subjective value associated with it.
2132
2133 The problem is separating those two in trying to determine what this Board should do. And
2134 separating them is difficult because of the split ownership. If I own the land and I own the
2135 cottage on that land and I sold that land, I would get the whole value. And, quite frankly, it
2136 wouldn't matter to me how much was attributable to the land and how much was attributable
2137 to the improvements. They're all mine. In this case, they're not. Those values don't belong to
2138 one entity and they have to be divided. If the state is charging the market value of the rent,

2139 then that value to the buyer of a leasehold when it's sold will be zero. That person purchasing
2140 the land will know that he or she is paying the market rent from now through the term of the
2141 lease. And so there'll be no value attached to that.
2142
2143 Let me use the cattle example that was used earlier but not quite appropriately. Namely,
2144 permits on federal lands generally are leased out to the permit holders at rates below market
2145 value. The result is when a permittee sells the base unit, in this case his ranch, the result is a
2146 higher value for the overall package of fee simple land that sold because it includes the right to
2147 graze on – I'll use federal lands to keep the State Land Board out of this one – the right to graze
2148 on federal lands. That premium is a part of what is being called here the leasehold value. And
2149 it's a premium that exists because the rent charged for the grazing is below what it's really
2150 worth.
2151
2152 If the Land Board is charging a rent below what it's worth, there will be a share of the leasehold
2153 value in excess of that rent because I think, just like the grazer thinks, I'm getting a good deal
2154 from the Land Board. If the Land Board is charging market rents, then stop worrying about
2155 leasehold value attributable to the land that you control – it ain't there. There is no such thing.
2156 If you're charging market rents, the only way there's leasehold value is if the purchaser of the
2157 property believes that the improvements are worth more than the appraised value. Pure and
2158 simple.
2159
2160 Therefore, in my professional opinion, the first and foremost goal of this Board should be to get
2161 the rents up to market rent so that the leasehold discussion disappears. I'll come back to that in
2162 a moment. Since that's even a very difficult task, and I'll come back to how it might be achieved
2163 and how I think the proposals on the table move in or not in the direction of so achieving, let me
2164 just emphasize as has been stated before here, the problem will never go away until the split
2165 ownership is dealt with. So I agree with everything else. I was sitting next to someone from the
2166 Land Board – or from the Department of Lands and she said it might be her task to help divest of
2167 these lands. I said getting there is where you want to be. It's just getting from here to there

2168 that's the problem. But that's not my task. My task is to evaluate the rents that have been
2169 charged, the rents that are being proposed and how those relate to the fiduciary responsibility
2170 of the Board.
2171
2172 First let me turn to rental rates and again emphasize that these are rates that aren't determined
2173 in this room, aren't determined in this city. They're determined in a global marketplace and the
2174 Board has a fiduciary responsibility to ask itself are we earning the market return on our asset.
2175 Two point five percent doesn't come close. We could debate whether it should be two point
2176 eight, but I don't think it would be much of a debate. Four percent gets closer. If you look at
2177 the studies that have been done and quoted here by Duffield, et al., you'll find that those rates
2178 are upward of four percent, not downward of four percent. And therefore I think that the Board
2179 needs to recognize and consider rates that are upward of four percent.
2180
2181 In my professional opinion the work done by John Duffield, proposing – estimating – a six
2182 percent probably comes as close as any. And, yes, as someone said earlier, that's higher than
2183 the rate of return on Treasury bonds, but you really are dealing with a – well, now that I think
2184 about the deficit, this may not be true. I was going to say you're dealing with a more risky asset,
2185 but then given the deficit who knows how risky the federal debt may be. Still I think you're
2186 dealing with a more risky asset, and therefore have to understand that a rate of return above
2187 Treasury bills is appropriate. So I think you need to start with a rate of return that is upward of
2188 four percent, not four percent, and Reed and I suggest in our final analysis that six percent is a
2189 good target.
2190
2191 Furthermore, I think that that rate needs to be indexed because those rates move all the time.
2192 Setting a rate equal to whatever it is and leaving it there misses the fiduciary responsibility of
2193 any investor to move the rate commensurate with what's happening to the market. And I think
2194 the best way to do that is to index it to Treasury bills. It's a simple clear way in which these
2195 kinds of contracts are indexed all the time.
2196

2197 I could go into – and am happy to but that will surely get people to leave the room – I won't
2198 bore you with the details unless you ask. I was thinking earlier as I was listening to the speakers,
2199 there's a joke about economists that says if you laid all the economists in the world end to end
2200 they wouldn't reach a conclusion. I thought we could probably add appraisers to that. There's
2201 another one that says if you laid all the economists in the world end to end it would be a good
2202 thing, and I'll hope you don't believe that when I'm finished.
2203
2204 So I think that first and foremost, the Board should focus on – on a rate of return to start with
2205 that reflects a market rate, that that should be indexed over time. Secondly, the Board needs to
2206 focus on its asset value. That asset value is hard to determine. The only way you'd really get it
2207 is to auction off those lands periodically and find out what they're worth. But we can't do that.
2208 We don't do that. We use proxies. And despite my previous remark about appraisers, we use
2209 appraisals and those appraisals are an effort to tell us what we think the land is worth given
2210 what these people know about the marketplace. And so using the appraisals is an appropriate
2211 way to then apply a market rate to an appraised value that we think approximates what the
2212 asset is worth.
2213
2214 Averaging that over five years, ten years, twenty years, any number of years, makes absolutely
2215 no sense from a prudent investor's perspective. It would be like trying to decide whether to buy
2216 or sell some bonds in your portfolio by saying I think I'll use the average of bonds over the last X
2217 number of years. It's just not relevant to whether you want to buy or sell bonds. What you
2218 want to know is what do you expect is going to happen to this asset value, what is the asset
2219 value now and do the beneficiaries, who just spoke, get a market return on that asset. Using the
2220 appraised value is the best proxy we have. There is no way around that. So our
2221 recommendation is that you use the appraised value, and where necessary if they need to be
2222 adjusted because you can't simply appraise everything, perhaps you can adjust those using
2223 assessed value – changes in assessed value.
2224

2225 Thirdly, as you look at how well you're doing, it does require looking at the rate of return on the
2226 asset. And there's been lots of discussion today on what has happened to that rate of return. I
2227 think the Department of State Lands has clouded this issue a little bit, with due respect to the
2228 Director, by including in some of the calculations what is happening to the value of those lands
2229 as part of the rate of return. If I tell you that my balance sheet as of this year is ten percent
2230 greater than it was last year, we know my net worth is greater. That's all we know. But we
2231 don't know anything about the rate of return on my asset. The rate of return is quite simply
2232 how much revenue did I take in from the assets I held at the beginning of the year. Nothing
2233 more; nothing less.
2234
2235 Now, I may at the end of the year sell some of those assets and use them for other purposes, in
2236 which case I'll say in addition to the revenue I got, I got some gain on my asset. And, yes, that
2237 will a part of a rate of return I would calculate. But I wouldn't calculate that until such time as I
2238 sold the asset. Given that these trust lands have typically not been sold, it makes no sense to
2239 include what has happened to them over time as part of the rate of return and to try to justify a
2240 lower rent on those assets because they've gone up in value. Indeed, the counter would be if
2241 they've gone up in value then the Land Board and its beneficiaries should be getting more
2242 revenue from the asset. If I have a bond that's gone up in value, then I better be getting a
2243 higher return from that higher value. So these questions of rates of return should be separated
2244 again from issues of asset appreciation so that there isn't confusion as to just how much rate of
2245 return the State is getting for its beneficiaries.
2246
2247 This comes back to the question really of premium rent and leasehold value, and I'll repeat what
2248 I said earlier. If the market rent is being charged, there will be no leasehold value associated
2249 with the land. You're getting it. You're getting it in the rent that you charge. There still may be
2250 leasehold value, but that's leasehold value due to what the people who have those sites and
2251 have improved them have created and, in my opinion, have a right to. To say that the State
2252 should collect ten percent if it's charging the market rate is wrong. To say that it should collect
2253 fifty percent is even more wrong. If it's collecting the market rent at the outset, there is no need

2254 to worry about leasehold value. And for that reason, we propose that the State increase its
2255 rates, base those rates on appraisals and thereby collects the market rent of return on its land,
2256 and forget all about leasehold value so the good people who have made the improvements can
2257 go forward with the right incentives to collect on the improvements they've made. You're
2258 collecting on the asset that belongs to you.
2259
2260 Finally, regarding the terms. The land that you are leasing is fee simple land. Pure and simple.
2261 It's not encumbered. It's land that belongs to this – in effect, this Board. As fee simple land,
2262 there's only one way to value it – at its fee simple value, and therefore comparing the value of a
2263 site with nothing on it on Priest Lake facing to the southeast having a view of this mountain or
2264 that mountain with this kind of bay in front of it and these kinds of fish is exactly the same as
2265 the value of the lot next to it with no improvements and all the same characteristics. They're
2266 both fee simple pieces. Both are assets and both should earn a rate of return commensurate
2267 with their asset value as fee simple.
2268
2269 As the Land Board considers other terms, such as should it be ten or thirty-five years, once
2270 again, if it's really charging a market rent, then the terms don't matter a whole lot to the Board
2271 because it's getting each year the rents that it should be getting as a prudent investor for its
2272 beneficiaries.
2273
2274 In this case, however, there is the other aspect of the – of the asset appreciation. If the Land
2275 Board locks itself into thirty-five years, it makes it far more difficult to manage its portfolio in
2276 terms of does it want to divest of the land and put the money into other assets. Therefore, I
2277 think expanding the leases to thirty-five years is a real mistake, and it's even more of a mistake if
2278 you're going to consider what the Subcommittee proposed, namely carefully weigh the benefits
2279 and costs and study divesture or consolidation of the split ownership problem.
2280
2281 Thirdly with respect to terms, you can't be a prudent investor and cap returns. First, start with
2282 the simple one, and I agree with whoever it was earlier who said watch out for inflation. I think

2283 it's going to come. When it comes, if you lock yourself into a three percent cap, and some of
2284 you are as old as I am perhaps and remember the late 1970s when we were looking – looking at
2285 inflation rates of way into the double digits – interest rates to cover that inflation into the
2286 seventeen percent, twenty percent rates. If you lock yourself into a three percent cap of
2287 increases in the rents, and the interest rates in the marketplace go up because of inflation, you
2288 cannot look yourself in the mirror and say you're prudent. So I would admonish you not to think
2289 about putting caps on these kinds of – on these leases – to put those into the terms is to
2290 guarantee, I think, you will not be prudent investors.
2291
2292 So let me summarize and leave open for questions what I think the Board has been doing, what I
2293 think is before it and what I think it should be doing. It has not been charging rates of return
2294 commensurate with its fiduciary responsibilities. I think everybody has said they agree to that.
2295 Two point five percent is not doing that. I think that the Subcommittee's proposal gets closer to
2296 that by increasing the rate. Unfortunately, the phase-in over ten years – using a ten-year
2297 average – fails to capture the current value of the asset and therefore is not prudent.
2298 Furthermore, to try and phase in a target rent over a five-year period means, again, you're
2299 missing a period of time when you're not capturing the rents. And to suggest that the Board
2300 should be charging a ten percent premium rent or a fifty percent premium rent is to say guilty of
2301 not being a prudent investor.
2302
2303 If you had been following the Prudent Investor Standard there would be no premium rent that
2304 you should be collecting. The best way to get out of that is to eliminate it by charging a market
2305 rent. So where should you go? In our final report we suggest that you raise the rate. We say to
2306 six percent. That you index that to Treasury bills. That you apply that to the appraised value.
2307 That you ignore completely leasehold value and let the buyers and sellers of lots enter into
2308 whatever agreements they wish. That especially at this time you consider nothing larger –
2309 longer than a ten-year lease. That you put no caps on any of the increases, and finally and most
2310 importantly, but this is not my task, that you consider the last recommendation of the
2311 Subcommittee and take it very seriously – study how to get out of the split ownership problem.

2312 It is the problem. It won't go away. If you followed everything that in my professional opinion
2313 you ought to follow, you still are going to have debates over should it be six percent, five
2314 percent, four percent, four point eight percent, and should it be the appraised value or the
2315 appraised value less some amount or the appraised value plus some CPI – it will go on forever.
2316 It'll always be a question, and it won't be solved until one entity owns both the land and the
2317 improvements.
2318
2319 Thank you very much. I'd be happy to answer any questions you might have.
2320
2321 **Governor Otter:** Mr. Ysursa.
2322
2323 **Secretary of State Ysursa:** Governor, Mr. Anderson, thank you very much for your presentation, and I
2324 know since we switched it around a little bit that last recommendation of the Subcommittee –
2325 the last shall now be first on divestiture, and your phrase, I think, is unification of the ownership
2326 pattern there.
2327
2328 I have a couple of questions – well, I have a lot of questions. I have a couple of questions. One,
2329 you did have the opportunity from – to look at the appraisers' methodology, the regression
2330 methodology that the cottage site association had put forth.
2331
2332 **Mr. Anderson:** Uh-huh.
2333
2334 **Secretary of State Ysursa:** Do you have a – what was your opinion of that?
2335
2336 **Mr. Anderson:** I – I saw –
2337
2338 **Secretary of State Ysursa:** What is your opinion of that?
2339

2340 **Mr. Anderson:** – I saw a summary of that. I didn't have all the details of the regression analysis. As an
2341 economist, I'd be capable of looking at the statistical techniques used, but I – I didn't have those
2342 data or the techniques used. So I can't – I won't speak to whether they were the right or wrong
2343 techniques. I'll only speak to the point I think you're really getting at which is should the –
2344 should a prudent investor think about a lower rate of return on higher valued land assets. Is
2345 that closer to really the question?
2346
2347 **Secretary of State Ysursa:** It's the regression theory.
2348
2349 **Mr. Anderson:** Yeah. And – and my response is regardless of what those data tell us, I'll just stipulate
2350 that they're correct – I – because I haven't analyzed the data themselves – my response is if you
2351 have to accept a rate of return, a lower rate of return on higher valued assets then move that
2352 first agenda item up even faster and get rid of those higher-valued assets. It makes no sense to
2353 think about taking a low return just because it's a high-valued asset. That would be like saying,
2354 well, let me see I'm getting, what was the comment earlier, I didn't look at T-bill rates recently,
2355 three point eight percent I think was the number on T-bills – and I have a ten thousand dollar
2356 T-bill or a hundred thousand dollar T-bill. Well, gosh, I'll buy the hundred thousand dollar one if
2357 they give me one point six percent. Nobody in this room would think that would be prudent. So
2358 if it's really true that you get lower rates on higher-valued land, you talked about trading earlier,
2359 then here's – here's my suggestion. You take all those higher-valued lots and you trade them
2360 for lower-valued lots only at commensurate amounts. So if you've got a lot worth a hundred
2361 thousand dollars, trade it for ten worth ten thousand dollars and get a higher return. I mean
2362 that just can't really be very sensible even if we stipulate that the data are what the appraisers
2363 suggest they are.
2364
2365 **Governor Otter:** Mr. Ysursa.
2366
2367 **Secretary of State Ysursa:** Mr. Anderson, I was thinking maybe we'd wait until the lots got to three
2368 million dollars and then we'd be paying them.

2369

2370 **Mr. Anderson:** Well, that's another way to do it.

2371

2372 **Secretary of State Ysursa:** On regression. If we were at one percent at two million – never mind.

2373

2374 **Mr. Anderson:** Yeah, and then I'd stick with the fifty percent on the premium and in fact I'd try and get
2375 ninety-five or something.

2376

2377 **Secretary of State Ysursa:** Well, a serious question here –

2378

2379 **Governor Otter:** That's good. The last one wasn't as humorous as you thought.

2380

2381 **Secretary of State Ysursa:** No, it wasn't. Thank you, sir.

2382

2383 A serious question here on the – you don't – pardon this phrase, but you come here without the
2384 millstone of history around your neck. You have made an observation, and I'm sure you were
2385 asked that. Forget history. Make your subjective – objective analysis without knowing our – or
2386 caring about our previous course of dealings that we've had with the cottage sites for umpteen
2387 number of years. So what I'm getting at – what is the percent increase that you're suggesting
2388 and you're – when you say six percent, you're saying six percent of current value, I believe.
2389 Correct?

2390

2391 **Mr. Anderson:** Correct.

2392

2393 **Secretary of State Ysursa:** And if we are currently getting, depending on which lake, of current value,
2394 two percent at Priest Lake, one point seven at the Payette Lake lakefront and about one point
2395 four or something on the second tier, we are looking at hundreds of a percent increase right off
2396 the bat, correct?

2397

2398 **Mr. Anderson:** Correct.

2399

2400 **Secretary of State Ysursa:** I don't want to ask you if you think that's fair, and I won't.

2401

2402 **Mr. Anderson:** And I wouldn't answer.

2403

2404 **Secretary of State Ysursa:** But we – what I'm getting at obviously – I could ask you another question. If
2405 we, as the current Board members voted for freezes along the way, were we complicit in these
2406 current scenarios that we – that we are in right now of not getting to market by – and
2407 everybody on this Board, two out of the – at least two out of the three times have voted for
2408 freezes. We're part of the problem. So – and as Mr. Lempesis said earlier, that the State helped
2409 create the imbroglio that we're in, and what I'm suggesting, and the Subcommittee is
2410 suggesting, we didn't get into this mess overnight. We need to get out of it and have some
2411 measure of fundamental fairness involved when we do come out of this. To immediately put a
2412 three, four hundred percent increase on the lessees is in my opinion unconscionable, and that's
2413 – I guess that's more of a comment.

2414

2415 **Mr. Anderson:** Well, let me respond. Again, I'll repeat my task was to use the Prudent Investor Standard
2416 and say are you there and how – you know, what would put you there. It's a bit like the
2417 divestiture getting from here to there is – I'll see you later, I'm going back to Montana. That's
2418 your problem. But let me first say that I think it's important to understand that I don't – I can't
2419 imagine that anybody buying a cabin, a cottage site lease, and the improvements, didn't know
2420 that it was trust land. And if they bought it and didn't know there was a constitutional
2421 constraint on what those rates should be, then they were not a very good buyer. If a realtor was
2422 involved and didn't tell them that they were buying a piece of land that had a constitutional and
2423 statutory shadow hanging over it, then again, they weren't good buyers or the realtors weren't
2424 good at performing their duties.

2425

2426 So I think that in one sense you're off the hook by saying look, that was there. But I would agree
2427 – and I would agree with the people who sit behind me I suspect in owning these that you were
2428 complacent – or you did contribute to this and therefore, you know, this is not professional
2429 witness talking now, but if I were in your shoes, I would look at some sort of a phase-in of the
2430 increased rates applied to the current values. I wouldn't roll it in by doing ten-years appraised.
2431 That's saying well, you know, we kind of did something wrong so, well, let's gobbly-goop this
2432 thing together, cobble it together in a way that tries to make us feel better. Get to the bottom
2433 line. What does a market rent mean? It means getting a market return on the value of the
2434 asset. And once you stipulate that, how you get to that market return is – is, you know, phasing
2435 that in makes sense. But trying to phase it in with this rolling appraised value, and phasing it in
2436 with some target rent, not target rate, target rent, is not a good way to appease your
2437 conscience.
2438
2439 **Secretary of State Ysursa:** One – just one more.
2440
2441 **Governor Otter:** Mr. Ysursa.
2442
2443 **Secretary of State Ysursa:** One more. In – in defense of the Land Department and how we come with a
2444 return on asset, and I – and maybe we ought to revisit that in our what I call the Ark of the
2445 Covenant these days, that's the asset management plan, it does include and it sets out the
2446 formula on asset appreciation being figured in on the rate of return and what we have. And as I
2447 mentioned previously, the problem is is we don't capture that appreciation. But that is in – and
2448 for other Board members – that is in our asset management plan that that's part of the formula
2449 that we figure out.
2450
2451 **Mr. Anderson:** Let me be clear. I'd – there's nothing wrong with doing it that way. I think it just
2452 confuses these different rates of return. It confuses the rate of return that the Board should be
2453 focusing on as a return on asset versus an appreciation in the corpus value. And, you know, as
2454 long as everybody's clear that that's not the same – that that calculation as laid out in the asset

2455 management plan is not the same as a calculation of how much did I get on my passbook
2456 savings account. Then okay. Because we know the passbook savings account isn't going to
2457 appreciate. It's just going to earn interest, and that's what I'm saying is the responsibility of the
2458 Board to look at.
2459
2460 So I don't think it's inappropriate to make that calculation, but it needs to be made clear to
2461 everyone that comparing a rate of return that includes an asset appreciation when it hasn't
2462 been realized is not a very good way to do financial business. And every one of us who has any
2463 kind of assets recognizes that we have – you know, we may look at our – our – our financial
2464 statement at the end of the month from whatever brokerage firm or company we have and say
2465 wow, this statement – you know, market value last month was a hundred thousand, this month
2466 it's a hundred fifty. I made fifty percent. Well, yeah, but if next month it's seventy-five that
2467 doesn't matter. So – you know – what I really want to know is – is what's the rate of return over
2468 the long haul on the asset, and if – if you're going to include appreciation or depreciation then
2469 you ought – you ought to make that calculus.
2470
2471 One more point I should emphasize, and I think is important on both the rate and the asset
2472 value, if you set a rate and you get there, let's say over what period of time, I don't care, but you
2473 get it to the rate that is a market rate and you then index it to something like T-bills, that rate
2474 can go up and it can go down. So that the cottage site owner should understand that they're –
2475 they're benefiting in a down market like this. Secondly, if you tie it to the appraised value,
2476 nineties looks wonderful for the State Land Board. Today it doesn't look so wonderful because
2477 the trend hasn't been upward in those values. So – but again, that's just what prudent investing
2478 is about.
2479
2480 **Secretary of State Ysursa:** Thank you.
2481
2482 **Governor Otter:** Mr. Wasden.
2483

2484 **Attorney General Wasden:** Thank you, Governor.

2485

2486 Some three and a half – give or take a few minutes – three hours ago or so we heard a
2487 presentation, and I will just refer to it as the Payette Lakes presentation. And I can go through
2488 the elements of it, but I think you were present in the room. You heard what their presentation
2489 was. And so not to misstate anything – I – as you've listened to that, in your view, in your
2490 professional opinion, if we were to apply the proposal as was made before us today, would we
2491 as this Board be fulfilling our fiduciary duty and fulfilling our constitutional responsibility to
2492 obtain the maximum long-term return and or would we be fulfilling our statutory duty to – to
2493 produce market rents for the duration of the lease.

2494

2495 **Mr. Anderson:** In my professional opinion you would not be starting with number one, the cap. Putting
2496 a cap on these is – is a sure way to ensure you are not going to meet fiduciary responsibility. So
2497 that's first.

2498

2499 Secondly, the rates that I recall being talked about in both – both the presentations before me
2500 were – were well below market rates. They were two point two, three percent and so on. I
2501 don't – again, I'd have to look back at the record to get the exact numbers.

2502

2503 And – and finally I don't think using a rolling average of appraised value is a way to meet
2504 fiduciary responsibility. Let me just emphasize. If the value is going up and you use the
2505 appraised value, whatever market value you use, if the value is going up over a period of time, it
2506 means that you're – you know, you've got these time periods back there that you're throwing in
2507 these lower values to. And so it's – you're just not going to get there. But flip it around. If the
2508 value is going down, it means you're using last year's values, which were higher, to create this –
2509 to estimate this appraised value, which means you're getting more in a sense than you should
2510 be getting. So that phase-in is just – is, again, not a very – not a fiduciarily responsible
2511 mechanism.

2512

2513 **Attorney General Wasden:** Governor. Governor.

2514

2515 **Governor Otter:** Mr. Wasden.

2516

2517 **Attorney General Wasden:** Thank you, Governor.

2518

2519 Terry, you also heard the presentation by which I will refer to as the Priest Lake presentation,
2520 and I pose the same question. And that is, if we were to apply that – that model, would we
2521 achieve – would we fulfill our constitutional obligation to obtain the maximum long-term return;
2522 secondarily, would we fulfill our statutory duty to produce market rent for the duration of the
2523 lease. And I'm ultimately going to ask you what's the difference between those two things, but
2524 I'm asking those two questions.

2525

2526 **Mr. Anderson:** In my professional opinion, again, is that it also would hamstring the Board in meeting its
2527 fiduciary responsibility. It included a cap, which has to hamstring that – that ability. It included,
2528 I believe, a three percent return, which in my professional opinion is below where the market is
2529 today, which is – is where I would start from. And I believe – those are the two things I
2530 remember most about it, but neither would get you to being – meeting either the constitutional
2531 or the statutory requirements.

2532

2533 **Governor Otter:** Mr. Wasden.

2534

2535 **Attorney General Wasden:** Thank you, Governor.

2536

2537 Terry, would you address for a moment or two the distinction between the constitutional duty
2538 to obtain maximum long-term return, and the statutory duty to obtain market rent through the
2539 – for the duration of the lease.

2540

2541 **Mr. Anderson:** Well, my professional opinion is that that the statutory requirement focuses on the
2542 market rent, and says what it is and therefore takes into account the current market value times
2543 the current market rate of return for an appropriate asset class. And, therefore, the Board's
2544 responsibility under the statute is to obtain that market rent computed in that way. If it uses a
2545 lower value of the asset, it's not getting the market rent. If it uses a lower rate of return than
2546 the market rate of return, it's not getting the market rent. So I think that's the statutory
2547 requirement.
2548
2549 I think the constitutional requirement is a broader one and appropriate for a class of assets held
2550 in trust, which means then you really do have to focus more on this number one issue. Do you
2551 divest or hold on. That means, in my professional opinion, the constitutional requirement as a
2552 prudent investor means that you take into account the expected long term value of the asset,
2553 and its asset – and its revenue generating possibilities, not just what would the market rent be.
2554 And so, again, if we had blinders on, and we looked at the last four years, you'd be saying, oh,
2555 my gosh, we've got to get out of this asset. We don't – you know, suppose it were as liquid as
2556 bonds, and we had two classes of bonds – one that was going down as clearly as real estate
2557 prices have recently. We'd be saying get out of those bonds and into some other class where
2558 that wasn't happening, if we could find such a class. So we'd be readjusting the corpus, the
2559 structure of the corpus portfolio rather than just the rents obtained from them.
2560
2561 **Governor Otter:** Mr. Wasden.
2562
2563 **Attorney General Wasden:** Thank you, Governor.
2564
2565 Terry, in terms of this dichotomy between the constitutional duty and the statutory duty, it's my
2566 understanding that the only way to really resolve that is for there to be a market activity that
2567 would produce market rents, but in fact we're precluded by doing that by – by statute. Is that
2568 your understanding and can you comment on that?
2569

2570 **Mr. Anderson:** Yes, I think you are – well, let's see. Precluded by statute. You mean by the – by the –
2571 uh, uh –
2572
2573 **Attorney General Wasden:** By –
2574
2575 **Secretary of State Ysursa:** 310a.
2576
2577 **Attorney General Wasden:** By – yeah, 310a.
2578
2579 **Mr. Anderson:** 310a. Okay. I just couldn't remember the number. Yeah, I think you're precluded from
2580 that, and therefore you are forced to use proxies. And so you say, well, is it four percent, five
2581 percent, six percent, four point eight percent. That's a – you know, that's a proxy. It's not, you
2582 know – I – I have a professional opinion for where it should be, and I've stated that in the
2583 written report to you. You use appraised values. That's a proxy. If you had competitive
2584 auctions, and every time a lease came up you could put them up, then you'd be gathering those
2585 data. But to the – back to the split ownership issue, to have a competitive auction, you know, if
2586 I had a tent on one of your cabin sites, then it's not such a problem. I'd just say I'm packing up
2587 my tent and going home. But these are not tents, and it's that separation that again is the – is
2588 the key problem. The economics literature is filled with examples and discussions of the
2589 problems this creates. And all of that literature points straight to the exact same point.
2590 Consolidate ownership in some way.
2591
2592 **Governor Otter:** Mr. Wasden.
2593
2594 **Attorney General Wasden:** Thank you, Governor.
2595
2596 Terry, you've also seen the proposal by the Subcommittee, and I think even as it's been
2597 enunciated and clarified here today. So I pose the same question. That is, following the
2598 proposal as its been issued by the Subcommittee, would, in your professional opinion, would

that allow us, or would it – would we be completing our constitutional duty to obtain the maximum long-term return and or would we be complying with our statutory duty to impose market rent for the duration of the lease.

Mr. Anderson: Well, at least when I answer this one I'll be facing the people who are going to shoot at me as opposed to having them at my back, which is a little safer, I guess, although they may have bigger guns. I'm not sure. I do not think that it does. I've already stated I think four percent is at the very bottom end of anything that you should consider to be a prudent rate of return. I think averaging it over the past ten years of appraisals misses the boat, not just in terms of getting more revenue for the beneficiaries; it misses the boat by not getting the right number as I just explained a minute ago. If they're going up, it's one thing; if they're going down, it's another. I think trying to hit a target rate and phase it in over five years is again maybe the way you have to do it to – to face your colleagues and your friends tonight at dinner, but it's just not a very effective way to get – get to a fiduciarily responsible mechanism. I don't think you should – should in any way be looking at fifty percent of – of leasehold values if you get the rents up. You just get rid of that. It's just – it gets you out of that mess entirely and gets the incentive right for the lease – the lessees to make the proper investments.

Thirty-five years, again, I think would be a mistake in light – not just of the – the potential of divesting of the land. I think it would be a mistake because it locks in, especially in the terms that are suggested there over a period that would not be responsible, and I – I didn't mention this earlier, but it's another reason to really avoid that ten percent, fifty percent increase in the – increase from ten to fifty percent in the premium rent. It gives every incentive for anybody sitting on one of these sites to sell sooner rather than later. Would you rather have ninety percent of whatever the value is or fifty percent of the value? And if you're thinking about selling – and if – and I don't know the distribution of the people holding these sites, but there are people out there who bought them on speculation, I know what I'd be doing. I'd be getting rid of them while it's ten percent, not waiting to the fifty percent.

2628 **Attorney General Wasden:** Thank you, Governor.

2629

2630 **Governor Otter:** Mr. Luna.

2631

2632 **Superintendent Luna:** Yeah, Terry, quickly, is it your opinion then that unless we immediately go to six
2633 percent that we're not meeting our constitutional responsibilities? Anything less than that –

2634

2635 **Mr. Anderson:** Well, I – I think six percent should be your target. Immediately, I understand the position
2636 you're in. I understand the position that's been taken by the lessees that if you immediately go
2637 to that you may lose some long standing good customers. And I think you do need to weigh that
2638 in the equation. But I think you ought to be moving in the direction of something closer to five –
2639 sorry, to six percent than the two and a half and three that have been bantered about earlier,
2640 and then the four that you had in your Subcommittee report. But again, I'm – you know, I can
2641 sit here as a professional witness saying I'm going to evaluate you on what you're doing right
2642 here and now – is it prudent, is it meeting your responsibility and say no, it's not. This is where
2643 you should be. But again, I think that as a – as a State Board worried about long-term clientele,
2644 then phasing in to get there makes some sense. I don't – with all due respect, I think you can
2645 phase-in in better ways than – than the ways that the Subcommittee suggested.

2646

2647 **Governor Otter:** Mr. Luna.

2648

2649 **Superintendent Luna:** Terry, I'm assuming you're aware that we had two lots that were auctioned or up
2650 for auction on Priest Lake for five percent, and we had no bidders.

2651

2652 **Mr. Anderson:** I am aware of that.

2653

2654 **Superintendent Luna:** Help me understand then how six percent is fair market value when we had no
2655 bidders at five percent.

2656

2657 **Governor Otter:** Mr. Anderson.

2658

2659 **Mr. Anderson:** Well, I don't think that it says six percent is wrong, or five percent in that case is wrong. I
2660 think that it says that – that what the people – the marketplace in this auction assesses to be the
2661 over – the long range – ten years we'll call it if they were ten – I don't recall – were they ten
2662 years?

2663

2664 **Superintendent Luna:** Yeah, I believe so, yes.

2665

2666 **Mr. Anderson:** Over the ten years the – that the rents that are going to be charged are, and the basis on
2667 which they will be charged, is at least uncertain enough to not make them want to put bids in.

2668

2669 **Superintendent Luna:** So –

2670

2671 **Mr. Anderson:** I mean, I don't – you can help me some. I just don't recall the details. I've looked at
2672 stacks –

2673

2674 **Superintendent Luna:** Yeah, I'm not going to –

2675

2676 **Mr. Anderson:** – and stacks.

2677

2678 **Superintendent Luna:** – I'm not going to try to spar with you because I think you're – you could clean my
2679 clock if we get too deep here –

2680

2681 **Mr. Anderson:** I wouldn't count on it but –

2682

2683 **Superintendent Luna:** But that's okay. I'm going to press you – I'm going to press you just a little bit
2684 because you started off by saying that it's, you know, the principles of Adam Smith, which,
2685 you're exactly right. It's the market that's going to ultimately determine the value, and we – we

used, you know, an auction so that the market could determine, and we had no bidders. And so how do we – how do we then find what the market will bear when, you know, if it's six percent is – is the – is the number that, in your opinion, gets us to meeting our constitutional responsibility. We had leases that were auctioned at five percent and nobody bid on them. You know, we're at four – the recommendation is at four percent. Help me understand what role the market plays then?

Mr. Anderson: Well, again, I'm going to – I just don't recall how the auction was run. But it was – it wasn't a case of me saying to the Board I'll give you a dollar if you'll give me that land for ten years. It was you want five percent on, I believe it was appraised value, but I don't remember.

Secretary of State Ysursa: Yes, it was.

Mr. Anderson: Okay. And the market was saying five percent times whatever I, as a possible bidder, think that appraised value is going to be over these next ten years is more than I think that lot's worth. That just tells – it doesn't tell me five percent is wrong. Five percent is the Adam Smith market price. The problem is that the people didn't think that the basis upon which that was going to be charged was a good proxy for what the value would be over time. Now, again, I'm just telling you as a professional to think about market rent, it would be this rate of return, determined in a marketplace for a comparable set of asset class, applied to the value of the asset. And you're using a proxy for – the best one you have – and the market's saying I don't like your proxy. I think that's what the auction tells you. So –

Governor Otter: Mr. Luna.

Superintendent Luna: I – then how do we determine the value if we put it on the market and the market says that what we're asking is not acceptable? Then I don't think we would raise the price. I don't think we're going to get more bidders. And so we would lower it then.

Mr. Anderson: Well, I'm stepping out of – of my – of my charge so – as providing the documents I provided, but so be it, I've never shied away from that. I am a professor so, you know, it doesn't matter whether I know anything about it, I'll still talk.

In this case I think I know a little about it. I have followed some of the literature on auctions. If I were to give you a proposal, it would be to say put up for bid one of these lots and make it an auction. Say what will you give us for a ten-year lease and put in whatever terms. You want paid, you know, on the first of the month, twice a year, you know, put in whatever terms you want and say what will you give us? You'll get bids. They may not be bids you like, but they will tell you what the market is saying. And then you will know if five percent is the going rate that you ought to be getting on your portfolio, or four percent, whatever it is. Take that four percent back out of it – what then is this asset worth – and what it tells me is people are saying this is not a very valuable asset. And then it tells me to tell you – sell it. Get rid of it. Get to an asset that will earn you ten percent.

I mean – I don't – I hope I've made clear. The rate of return that a prudent investor looks at is not something you just pull out of the hat. As somebody earlier said, I'd like – well, heck, I'd like twenty-five percent, but I can't get that. The market tells me what my rate of return is going to be. The market also tells you what that asset is worth. You've been appropriately using appraisals in my opinion. The market is saying the appraisals aren't getting it right. We think – we the marketplace is saying we think the lots aren't worth that much. Gasoline prices are higher. My income is down. My wealth is down. All those things have depressed market prices. And so if you – you just put it out there at terms saying make us an offer for ten years, you'll get bids. They may not be ones you like, but you'll have better market information.

Governor Otter: Mr. Ysursa.

Mr. Anderson: I'm – I didn't –

2744 **Governor Otter:** Go ahead.

2745

2746 **Mr. Anderson:** Who's in charge? Oh, I guess you are. Sorry.

2747

2748 **Superintendent Luna:** The Governor's in charge.

2749

2750 **Governor Otter:** Who's got the hammer?

2751

2752 **Mr. Anderson:** Okay. I yield. No, no, no, I was trying to carry on the debate here but –

2753

2754 **Secretary of State Ysursa:** Okay. Mr. Chairman.

2755

2756 Mr. Anderson, just a point of clarification on that, and it's kind of ironic – the original offer on
2757 our – our leases – the original procedure was as brought by the Land Department. There were
2758 two lots up there. They were both – they were just recent – they were appraised, and they
2759 were both going at four hundred and fifty thousand was the appraisal and five percent was
2760 going to be the rate. But about three months before that, the Department came in and said six
2761 percent. So I thought it was a bit of irony that the – and it was my motion that lowered it to five
2762 and, of course, we did have the – and in some of your information before, when we do auctions
2763 and other people in here, unless we change our procedures, if we ever did auctions we weren't
2764 auctioning the rate. The rate was set. We were auctioning off if there was somebody going to
2765 pay a premium, just like the ones we do on the grazing leases. If we want to be grazing then we
2766 do auction those off in a comparison there. You're paying the same AUM rate. Here the five
2767 percent times the four hundred and fifty thousand would have been what – twenty-two five was
2768 going to be the annual lease on those two lots. But you – if you wanted competition, we were
2769 bidding on a premium – the ability to get those lots. And we can talk about other factors and
2770 why we did it and certain time of year, whatever, I mean, various things may be – I can't
2771 speculate, but I think the Superintendent brings up a good point. We have tried a little bit of
2772 this, and it didn't prove to be too successful. But did we do it in the proper manner? Is there a

2773 better way to do an auction? Do we have to change our Constitution? Do we get out of the
2774 internet? Do we do this and that? But it has been tired, and I think it's wise to bring it up. And
2775 it didn't seem to attract much.
2776
2777 **Mr. Anderson:** Well, again, I would just say that the message I take from that auction of those two lots is
2778 that you don't have an asset that's as valuable as you – you think it is in a way.
2779
2780 **Secretary of State Ysursa:** The battle of the appraisers?
2781
2782 **Mr. Anderson:** Yeah. I mean, I – I'm not saying the appraisers are not doing it the way appraisers do it.
2783 I'm just telling you the market's saying that ain't the right number. That's – that's my
2784 interpretation of it.
2785
2786 **Governor Otter:** Mr. Luna.
2787
2788 **Superintendent Luna:** I'll just – I guess I just can't get my head around what you're saying. You're saying
2789 that the market demonstrated that five percent is too much. Then how do we then put us on an
2790 immediate course, or a long-term course, for six percent if the market told us that five percent is
2791 too much.
2792
2793 **Mr. Anderson:** I think you and I are just ships passing in the night.
2794
2795 **Governor Otter:** George, do you want to help with this?
2796
2797 **Director Bacon:** Well, I – I hope I can help a little bit, but maybe it will just complicate it. My memory of
2798 the situation, of course, was I think it was two lots, five percent –
2799
2800 **Mr. Anderson:** Of –
2801

2802 **Director Bacon:** – and – of appraised value – but the competition that was out there in the marketplace
2803 was you could potentially purchase an existing lot at two and a half percent. So there's that
2804 dynamic. What did that do to the potential bidders because why – why tie into a five percent
2805 lot when I can just wait and maybe pick up an existing lot. So I don't know how that came into
2806 play, and I say this for Mr. Anderson's benefit to give him a better idea of the picture. And then
2807 I think there was also a general awareness that we were going to be having this meeting
2808 someday and that the rules of the game might change. And I believe, staff would have to
2809 correct me, but I believe those leases said regardless of the deal at five percent, whatever
2810 changes came out of this meeting, the leases would be converted. So I think there was a lot of
2811 uncertainty and using those offerings to judge market would be a big mistake for the Board.
2812
2813 **Mr. Anderson:** I appreciate the Director's points and think that they, at least in my mind, clarify it.
2814 Whether I can get it to come out my mouth is another question. We'll see. The person deciding
2815 whether to bid on those lots has to ask what's my alternative. And the Director's suggesting
2816 that the people said well I get a ten-year lease; I pay five percent of the appraised value; I make
2817 a calculation of what that – what that amounts to over time using correct time value of money,
2818 and compare that to what could I get in another lease or buying fee simple land with the notion
2819 I sell it at the end of ten years if ten years is all I want it for. And again the fact that the auction
2820 generated no bids tells us a lot about five percent times the appraised value. And mostly, in my
2821 opinion, it tells us that the appraised values and the expectations of the would-be bidders were
2822 such that they didn't jive. They foresaw the value of land not being as high as the appraisal
2823 suggested; that they could go out and buy or lease from private individuals with more certainty
2824 as the Director suggested.
2825
2826 **Governor Otter:** You know, I think in part, we've created a lot of noise ourselves, which has caused
2827 confusion. And the result of that confusion has also reflected itself in not only the invisible
2828 hand, but the silent voice. Hence we didn't sell anything up in Priest Lake. But one of the things
2829 that warms cash to an investment is stability – is predictability. And we've been able to offer
2830 neither, I think, in the last – at least since I became – and before I was President of this Board.

And I don't know – I don't know how, other than trying to set some hard fast rules that we're going to follow from now on, that you give that comfort of an expectation of this is the way it's going to be tomorrow, and this is the way it's going to be the next day. Hence we've gone through two freezes, as I recall –

Secretary of State Ysursa: Three. Three at Payette and two at Priest.

Governor Otter: So we've constantly changed, if you will, sort of the environment for attracting investment. One of the things that I think we've – and I don't want us to forget it – maybe – I think everybody's aware of it – but one of the things that we've done today is always talked about this being like a second home, like an investment – like another place that we go to, you know. And I'm aware in some cases this is the home. This is the homestead. This is the home front. So – but we treat it at least I think in the semantics that we've used, the terminology that we've used is this is – this is someplace that people can elect to go to or not go to depending upon the season. And – and what they enjoy. But where I want to go is when you say no caps, I'm not aware of a lease that doesn't have a cap in some way.

Secretary of State Ysursa: Ours.

Governor Otter: Pardon me.

Secretary of State Ysursa: Our current lease.

Governor Otter: Yeah, and all the ones that we've successfully leased. My point is – is that all leases have caps in them. Now they may be moveable and they may be flexible and they may be tied to T-bills, but you yourself said tie them to Treasuries. That's a cap. Isn't it?

Mr. Anderson: You're –

2860 **Governor Otter:** Or at least a model – a model of here's – here's what your expectation can be. Here's
2861 what the stability is that we're offering.
2862
2863 **Mr. Anderson:** Yeah and you can't offer stability if it – and be fiduciarily responsible if that means here's
2864 a lease forever and ever at this price. Never worry. Just, you know, write your check out and
2865 send it to us on the tenth of the month. To do that is to definitely violate the fiduciary
2866 responsibility. The stability you can offer is here's a rate; here's something it's tied to; this
2867 Board doesn't control T-bill rates, if that's what you decide to tie it to. That's what it's tied to so
2868 you can – you – there's stability in the sense that the lessees know what it's tied to. You say
2869 we're going to use appraised values. If you think they're somehow not right, then, you know,
2870 less ten percent, plus ten percent, you know. Those again are proxies. So you can – but – but if
2871 you lay that out, that's stable. It would not – it would be – for this Board to somehow suggest
2872 that it could set a – a rate of increase over time, let's say, and lock that in and leave the lessees
2873 faced with that locked in rate would be to their detriment. But flip the mirror around. If they
2874 come and say, well, we'd like to lock you into a rate, that doesn't work. So I think the stability is
2875 not in terms of caps where it's three percent and no more, but rather let's all agree. There's a
2876 mean marketplace out there we all have to live in, and we're all going to adjust accordingly and
2877 – and – and the stability this Board can offer is in the way it makes those calculations.
2878
2879 **Governor Otter:** Mr. Ysursa.
2880
2881 **Secretary of State Ysursa:** Mr. Governor.
2882
2883 Mr. Anderson, are you aware of what your home state does on their leases and what they have
2884 just proposed on a cap between the – I think it's an average of the CPI and the Real Estate Index
2885 over twenty-five years between three point two five and something else – six –
2886
2887 **Mr. Anderson:** I don't know all the details. I'm aware that they've done it.
2888

2889 **Secretary of State Ysursa:** They have capped.

2890

2891 **Mr. Anderson:** Yeah. And once again, I – I would do things like T-bills and so on. But, you know, the CPI
2892 is a way to make at least a share of these adjustments, especially for rates. If you've hit the rate
2893 to begin with, over the long term, I mean hundred years and more, the – the rates of return on
2894 similar class assets, less the inflation component, haven't changed a whole lot. So if you get that
2895 rate, and you adjust to CPI, it'll work.

2896

2897 **Governor Otter:** Mr. Ysursa.

2898

2899 **Secretary of State Ysursa:** Governor.

2900

2901 Mr. Anderson, I think I couldn't agree with you more there, and I – I think we at times want to
2902 parse 310a and get hung up on market rent throughout the lease. To me, as everything I've
2903 heard, market rent seems to be a moving target. At any one time during – I mean we're going
2904 to be out of the market for a bit and even if you put a – the – a realistic cap or whatever makes –
2905 makes some sense. However, if the market, i.e., went up twenty percent, and we have a cap at
2906 three or five, are we meeting our fiduciary duty for that one year? Are we not? We get hung up
2907 on market rent throughout the lease. If we went to your suggestion and took six percent of
2908 current, which is a huge increase, but that's just an editorial comment, and then tied it to the
2909 Treasury bill, well, what if the market went up from there ten percent and the Treasury bill went
2910 up one – are we meeting the market rent throughout the lease concept?

2911

2912 **Mr. Anderson:** You know, I think yes because you have a – a tool for making the adjustments that's
2913 acceptable in – in financial markets, which is really what I think the fiduciary responsibility leans
2914 back to. If – if so, if you say index to T-bills or index to the CPI, those are measures that prudent
2915 investors in the marketplace use. If you said I think I'm just going to base it on how I feel when I
2916 get up in the morning, that doesn't work and – and that – if I – again, with all due respect, going
2917 back to the averaging, the ten years and so on, it's – I can understand –

2918

2919 **Secretary of State Ysursa:** No fair going back to mine.

2920

2921 **Mr. Anderson:** I would understand why you'd want to do that because it is fairer, if you will. But it – it,
2922 you know, that – that's not the way – I don't think you'd go out in the marketplace and say, how
2923 does this sound to you down there at – at whatever financial firms you – you deal with. They
2924 would say what? So – and I wanted – I come back to this notion of capping and think of – my
2925 wife and I rent a house out to people. Well, you know, we've said here's a rent and we give
2926 them some expectation they're going to be able to live in the house for a period of time. In our
2927 case we don't have a long-term lease for it. But we're looking at that rent and saying, you know,
2928 it's not a house we ever intend to live in, and we're looking at it saying how does that rent
2929 compare to what we think the asset is worth and what we think we could get if we sold that
2930 house today and bought something else for it. And that – that – you know, I'm – we're certainly
2931 not rocket-science investors, but that's fiduciarily responsible for us, I think. And it's what I
2932 think this Board should be doing.

2933

2934 **Governor Otter:** Any further questions or comments.

2935

2936 You know, I'm reminded of what we went through last week because – because – what do we
2937 make a year on –

2938

2939 **Secretary of State Ysursa:** Four point three million.

2940

2941 **Governor Otter:** Four point three million dollars and we suddenly make a decision here to go up in the
2942 market. All of those, let's say in one way or another, become non-performing. Another part of
2943 our fiduciary responsibility, at least the way we looked at it, was to keep a certain amount of
2944 money so that if schools were going to get so much money every year, and so anything we do to
2945 disrupt that thirty-one point one million dollars, you can argue whether it ought to be that much
2946 or not, that's not my argument. My argument is that they need to know that there's a certain

amount of predictability and stability in what they're going to get as well. And it's our responsibility to make sure that we at least come close to their expectation or don't fool them and do something to disrupt what their expectation is that they're going to get out of that. And I – you know, I can see that if – that we would fail article 9, section 8 as well if we did violence to that movement – to the degree that we interrupted that four-plus million dollars in rent.

Okay. I'm going to give, if they want to take it, both Priest and Payette five minutes each for rebuttal.

Superintendent Luna: Thank you, Terry.

Mr. Anderson: Thank you, Governor. Thank you, Board.

Governor Otter: Thank you.

Mr. Lempesis: Governor Otter.

Governor Otter: Appreciate it.

Mr. Lempesis: I'd first ask you, sir, would it be – I would usually ask the expert some questions. I don't know if you want me to do that. I would do so in a civil manner, but I don't know even enough about one fact he's adduced or arrived at these opinions but –

Governor Otter: Well, I'm – I'm an expert at anything, Chuck, so you can ask me –

Mr. Lempesis: Well, we both are and we've proven that through the years, haven't we?

Governor Otter: We have.

2976 **Mr. Lempesis:** Maybe I'll just summarize and tell you my concerns with the testimony that's been –

2977

2978 **Governor Otter:** All right. Yeah. Please.

2979

2980 **Mr. Lempesis:** – elicited. And I want to do this in a manner that is certainly complimentary to the good
2981 witness who described himself, may I add, as a professional witness.

2982

2983 I will tell you as an officer of the court in Idaho that the opinions he just rendered here he could
2984 never make in court. Okay. He could never arrive at a conclusion as to the ultimate question to
2985 be decided by the trier of fact and render that opinion. Second of all, I will also tell you unless
2986 he is a licensed appraiser in the State of Idaho, okay, the opinions that he has just rendered are
2987 not only erroneous, they're unlawful. He just rendered an opinion as to what the value of a lot
2988 to be leased at Priest Lake should be by identifying six percent of its fair market value. That's an
2989 appraisal question. And only an appraiser honestly can answer that question.

2990

2991 Taking nothing away from his other good credentials, if he were here, I would ask him whether
2992 he would have executed a lease as proposed by the State of Idaho. And if his answer were yes,
2993 let me tell you what he would have been answering to. At six percent, if it were six percent that
2994 we were going today or even anywhere close, Jim Young's lot at Payette would be a hundred
2995 and twenty thousand dollars a year.

2996

2997 Is that correct, Jim?

2998

2999 **Mr. Young:** That's right.

3000

3001 **Mr. Lempesis:** Mike's lot back there – Fery's lot – would be seventy-eight thousand dollars starting
3002 today. At four percent as a prudent investor, the lessee now, not the lessor, but we also need to
3003 be somewhat prudent, at four percent, if you took lot thirty-five at Payette – or pardon me, if
3004 you took the average lot at Payette and only assumed a, oh, eight percent escalator, in year

3005 thirty-five, the annual lease payment would be three hundred and twenty-six thousand dollars
3006 to lease that lot. If it went to fourteen percent due to high inflation for any period of time with
3007 that escalator, the annual lease payment without any cap, and that's why caps become so
3008 important, would be a million six-hundred and fifty-three thousand seven hundred and twenty-
3009 six dollars to lease a lot at Payette, Idaho. A million six-hundred and fifty-three thousand
3010 dollars.
3011
3012 I don't know whether anybody's ever visited Priest Lake, but I will also in the spirit of being
3013 collegial, of being respectful, tell you I heard no fact, not one single fact adduced by that witness
3014 that says I'm arriving at this conclusion. You ought to target six. You've breached your fiduciary
3015 duty. You violated the Constitution. You may all be going to prison, okay. But, by the way, I
3016 didn't give you a fact to support what my opinion is. Not one fact. I didn't hear one comparable
3017 – not one comparable – that said, by the way, at XYZ Lake in Bemidji, Minnesota – they're
3018 getting four point seven five percent and their Constitution looks just like yours.
3019
3020 My point is this. I appreciate that testimony. I appreciate its purpose. But the fact remains that
3021 we have an intractable problem we're trying to muddle through in the State of Idaho in a unique
3022 property in a situation we've created together, and that there are better resolutions than
3023 merely coming up with a bottom line of saying six percent of this or four percent of this. What
3024 we all have agreed to today is that divesting yourselves of those assets would result in more
3025 money probably for our schools in the long term, and we need to meet to determine how we're
3026 going to get there from here and have leases in the meantime that can accommodate that
3027 objective.
3028
3029 And I thank you for your time.
3030
3031 **Governor Otter:** Jim.
3032

3033 **Mr. Young:** Governor, members of the Board, and I also appreciate Mr. Anderson's credentials and his
3034 academic background and his academic view of – of this situation. Although I – I would say that
3035 I heard him contradict himself more than once when he first said that none of us in this room
3036 can determine what the market rent is because it's determined by the invisible hand. Yet then
3037 he turned right around and said that the market rent should be at six percent. I don't believe
3038 that Mr. Anderson has done any market survey of what' going on at Priest Lake or Payette Lake
3039 to determine if that is, in fact, market rent or if it's sustainable.
3040
3041 I think Superintendent Luna hit it – the nail on the head when he was asking well, what if
3042 nobody shows up. Nobody showed up at five percent. How can we go to six percent? When
3043 we have ninety-two percent of our lessees saying, hey, I want to get out of this, I think that
3044 we've reached the maximum that the market will bear.
3045
3046 The other thing I did like – the other point that I did like from Mr. Anderson is he kept using the
3047 word prudent investor. What would a prudent investor do? And a prudent investor, if they ran
3048 a lease-buy analysis on the cash flow, they would surely determine that it is much better to buy,
3049 and it makes no sense to lease under the formula that we have right now, which would indicate
3050 that the market is – the rent is too high. The present value of cash flow analysis shows us the
3051 same thing. That – that the present value of the future cash flow is greater than the underlying
3052 asset. That doesn't make any sense. So I agree with him that a prudent investor needs to look
3053 at this, but a prudent investor would not invest in – in the lease as its set up.
3054
3055 I did like the idea that he suggested in auctioning the rent value as opposed to establishing a
3056 rent and then seeing if somebody will pay a premium for that. It's a pretty good idea to just put
3057 the rent out there and say how much will somebody pay for this rent over the course of the
3058 term of the lease. That would get us to market rent. So I thought that was a very good
3059 suggestion on the part of Mr. Anderson, and I would support a trial basis like that. And perhaps
3060 we should try that. I would suggest maybe the Board look at trying that idea at Priest Lake with
3061 the two lots that were auctioned before and or the available lots at Payette Lake. Let's put

3062 them up for auction and ask people, well, how much will you pay in rent per year for that lot for
3063 X number of years? That's a good idea.
3064
3065 That's all I had. Thank you.
3066
3067 **Governor Otter:** So you're ready to do that next year?
3068
3069 **Mr. Young:** I'm ready to do that, Governor.
3070
3071 **Secretary of State Ysursa:** Would that be a market savvy way to do it?
3072
3073 **Governor Otter:** I don't think so.
3074
3075 Thank you.
3076
3077 Okay. Mr. Chairman of the Subcommittee and member of the Subcommittee, your summation.
3078
3079 **Secretary of State Ysursa:** Since I've been quiet all day, Governor. Well, Governor, you've heard the
3080 details of our imbroglio. One of my favorite words of the day. Groucho Marx used to bring it
3081 down, remember?
3082
3083 I still believe we do have a – certainly a consensus that the number one item in our
3084 recommendation should be to – and that is in our recommendation – is to seek ways to call it
3085 unify ownership, whatever you want to do, sale, exchange, whatever, and look at that and come
3086 back.
3087
3088 So to get the ball moving – I – I am – I'm not reluctant to meet, continue to meet and do
3089 anything I can to help, but we're facing some deadlines. And – and we get into this intractable
3090 situation where we have some of the folks still wanting to throw out the appraisers'

3091 methodologies and we talked about comparables. And, you know, we could – we could ask the
3092 Department to comment now, but I think we've heard enough from about everybody about
3093 what is wrong with the – and Mr. Anderson – and he did write about – or somebody did – in – in
3094 the report that – about the lease that – or about the, you know, study done by Mr. Moe and
3095 Mr. Corlett and what they thought were some of the fallacies and the faults are in it. And my
3096 main concern is not that I didn't like it. I didn't think, and I said this before, I think we gave the
3097 appraisers an impossible task. Find me comparables. That includes the landlord and the tenant.
3098 And by saying that, you know, I've studied the Montana situation extensively. They're facing the
3099 same thing. They're at five percent of X, but X went up too fast. So they manipulated how
3100 they're going to do X.
3101
3102 It's a scenario that – that begs for us to obviously recommendation number one through sale or
3103 exchange or other ways to dispose. So frankly to get the ball moving, there were some things
3104 on – that were brought up about the lease itself, not counting the – the rate or the premium
3105 rent or anything else about the release language. I was going to have someone speak to that,
3106 but those are some minutia that I think we can work out. My default is if we had it in the lease
3107 before, it probably ought to stay in there. Same way on the appeal. But we can work that out.
3108 We've talking the guts of this proposal now is, bottom line, what are we going to pay. As a
3109 Subcommittee member, and I appreciate, yeah, why are we doing an average? Why are we
3110 doing a five-year phase-in of the average? It's recognizing the fact that we helped create this
3111 problem. It's a way to extricate ourselves in what I still think is – is a fundamentally fair way to
3112 do it and yet still go up an average of nine percent a year and have a fifty-four percent increase
3113 in five years. What happens after that? Do low ones come off? High ones go in? Are the rates
3114 coming down, whatever. I think we are going to see them coming down. And I – I believe – I
3115 should say the values coming down. I think it's a fair way to do it and gives us time. And I –
3116 again, the other proposal was ten-year lease. Now that's our proposal. And then as we go
3117 through that cycle, if in fact there are some lots that never should be disposed of, and that study
3118 is made, the lease term could be adjusted. You know, after a ten-year period, maybe the next
3119 one is thirty-five. I don't know.

But I think to get this off the mark, I would – I would make the motion that we go with the Subcommittee's recommendation, which I – I just talked about. And that is the sale, number two, the four percent, five-year phase-in. That is predictability for five years after that, and then we have the phase-in there. We do not have a cap in there. Frankly the lessees are getting a double smoothing. We don't need a cap in my opinion because of that. Premium rent – a very contentious issue. You know, others may want to do a division of the question or whatever. I still think that we heard about that. I couldn't agree more with Mr. Anderson that if we get the initial rate high enough, you don't have to worry about premium rent or leasehold value and whatever. But we're not there. And to get there – to get to six percent of current – or even four percent of current – four percent of current is a hundred and thirty-six percent increase in one year, and then let's do an index off of that. To me that's unconscionable. And unfair to those people that we currently have a business relationship with, and that, you know, if we – you know, let he without sin cast the first stone. If we weren't complicit in this problem, and everybody on this Board who voted for freezes, and I'm one of them, but to then turn around and hit them over the head with a sledge hammer is unfair. And that's where I am. Yet we do have to know who we are in business for, and that's the endowment beneficiaries. And I don't believe that nine percent a year is an unreasonable increase, and fifty-four percent increase in five years. Mindful of the fact we've had a three-year freeze and a two-year freeze.

So I – I would move the recommendation of the Subcommittee.

Governor Otter: Okay. Just so I've got that – before I entertain the second. It's a liquidation plan.

Secretary of State Ysursa: Yes.

Governor Otter: Number one. Number two, a four-percent five-year phase-in.

3148 **Secretary of State Ysursa:** Four percent of a ten-year average on a five-year phase-in. We have the
3149 figures. The figures that we have used is – are based on – and those will be adjusted – are based
3150 on flat this year on assessments, and we would think they're coming down. So they're not going
3151 to be quite as high.
3152
3153 And the other one is a ten-year lease –
3154
3155 **Governor Otter:** Premium rent?
3156
3157 **Secretary of State Ysursa:** Premium rent. Keep the same premium rent that we have for the first year,
3158 and then it goes up ten percent –
3159
3160 **Governor Otter:** I see.
3161
3162 **Secretary of State Ysursa:** – twenty, thirty, forty, fifty.
3163
3164 **Governor Otter:** So there were –
3165
3166 **Secretary of State Ysursa:** And it's on the gross.
3167
3168 **Governor Otter:** Five elements – four elements to your motion.
3169
3170 **Secretary of State Ysursa:** Right.
3171
3172 **Superintendent Luna:** Mr. Chairman, I'm going to second this motion so that we can have discussion,
3173 but I'm anticipating that our discussion may create some changes to the motion perhaps but –
3174
3175 **Governor Otter:** Motion has been made a seconded. Is there further discussion?
3176

3177 **Secretary of State Ysursa:** I doubt it.

3178

3179 **Superintendent Luna:** Mr. Chairman.

3180

3181 **Governor Otter:** Mr. Luna.

3182

3183 **Superintendent Luna:** Here's – here's a couple of things that I would like to consider as we move
3184 forward. I'd like to see some more focus – time specific language dealing with our first
3185 recommendation, and that is liquidation. Because I – if anything has become even more clear to
3186 me today it's that we need to get out of these things. I think the first time you dealt with this,
3187 Ben, I was graduating from high school. So we need to – you know, we need to –

3188

3189 **Secretary of State Ysursa:** (inaudible), Tom, that hurts. You're as bad as this guy.

3190

3191 **Superintendent Luna:** The other – the other thing that – that – listening to Mr. Anderson and others, it
3192 seems to me like the closer we get to market value, then premium rent should be going down,
3193 not up, and it appears we're doing just the opposite because we're escalating – you know, we're
3194 getting closer and closer to the four percent, which is closer to market value. At the same time
3195 we're raising premium rent. If I understand Mr. Anderson and the rest of them correctly, it
3196 should be higher premium rent until we get to market value, and as we get closer to market
3197 value, premium rates – rent should be going down. So I'd like to have those discussions in light
3198 of your – of the motion that I've just seconded.

3199

3200 **Governor Otter:** Discussion.

3201

3202 **Secretary of State Ysursa:** Mr. – Governor and Mr. Superintendent, now, I think that's a quasi-valid
3203 point. The closer we do get to – I guess my point is the four percent, and again, the way I've –
3204 we've structured that, it's not necessarily – it's being fair to the point. It's not four percent of

current. We – I would – I would submit that we're still, in my opinion, quite a ways away from market rent.

Superintendent Luna: Because of the ten-year, five year –

Secretary of State Ysursa: Correct. And after five, if you had it flat, we're still just a few – few points above what they had agreed to in 2000 of two and a half percent of the current. So when we throw figures out, I mean, the percentage is out, it's nice to say, but the smoothing effect that we have in there has really made the effective rate lower than the four percent. So we're still quite a ways away from a – if you think a target should be four percent, or anyone does, we still have a ways to go even under our scenario.

Superintendent Luna: Mr. Chairman.

Governor Otter: Mr. Luna.

Superintendent Luna: I – I understand what you're saying, Ben, but the closer we get to the four percent then premium rent should be going down. I mean, it might take us many, many years under the five-year, ten-year scenario, but – but rents are going to go up fifty-five percent in five years –

Secretary of State Ysursa: Five years.

Superintendent Luna: – five years. It seems to me like that's getting us closer to market value, and the closer we get to market value, the premium rent should be going down.

Secretary of State Ysursa: No, that's – suppose we ought to start at fifty and go down to ten.

Superintendent Luna: Well, that's what I'm – I don't know but that's –

3234 **Governor Otter:** Well, during the earlier discussion, Ben, we talked about getting their ante back. For
3235 instance, if somebody bought the lease with the owner improvements on it –
3236
3237 **Secretary of State Ysursa:** The net.
3238
3239 **Governor Otter:** – that – and they paid a hundred thousand dollars for that quote leasehold value, that
3240 they would get that hundred thousand dollars back and then go to the net, and that would be
3241 shared fifty-fifty.
3242
3243 **Superintendent Luna:** No. We're not talking about net, Governor.
3244
3245 **Secretary of State Ysursa:** We're talking about –
3246
3247 **Governor Otter:** No, I understand that. But why aren't we?
3248
3249 **Secretary of State Ysursa:** Why aren't we talking about net?
3250
3251 **Governor Otter:** Why aren't we talking about net?
3252
3253 **Secretary of State Ysursa:** Well, Governor, right now we're at ten percent of gross. The value in the
3254 appreciation – the people in here that – and I'm sure there'll be some interjection by others on
3255 that, is the idea of the investment that anybody is getting this other than the endowment
3256 beneficiaries. I mean, reverse it. Why should anybody other than the endowment beneficiaries
3257 get the amounts of money being transferred that is totally – well, quite a bit of it – remember,
3258 we're not talking improvements. We're talking what they're paying to lease our land, for the
3259 right to lease it. And some would say, well, you're trying to get the money that we have
3260 foregone. Somebody else made it. When – when the argument first came up, well, we made
3261 twenty-five – twenty-five million. That's wrong. There was net. That's not the – that's not the
3262 net. But what is definite is that the State, i.e., the beneficiaries, did not get any of it. Who got

3263 it? The previous lessees. The State did not get a dime other than the ten percent. And that – I
3264 just think that there – you know, while you're making up the problems in the past or those in
3265 the future or whatever, but I think we get into this gross and net scenario – it's fraught with
3266 problems and games being played on values.
3267
3268 **Governor Otter:** I understand that, Ben, but it – it seems like we're assigning the action of a few flippers,
3269 as you called them, to –
3270
3271 **Secretary of State Ysursa:** It depends on what you mean by few.
3272
3273 **Governor Otter:** Or – we're assigning the actions of those people to even the – to everybody. So what
3274 I'm saying is if somebody got that lease without – without any basis, there's no basis at all in it,
3275 then you split it fifty-fifty. Then you're getting a whole lot more than you are now.
3276
3277 **Secretary of State Ysursa:** If there was no – the basis – if somebody has no basis, and they got X number
3278 of dollars –
3279
3280 **Governor Otter:** Somebody has no basis in the leasehold – that they've paid for the leasehold. That –
3281 that they've paid for the leasehold value.
3282
3283 **Secretary of State Ysursa:** Right. You go gross or net. We're going to get fifty percent of all of it in five
3284 years.
3285
3286 **Governor Otter:** If they have no basis. But why would – you know. I think it was a valid question, and I
3287 need you to answer that. Why would – why would I buy somebody's leaseholder improvements
3288 and then also pay a premium for the leasehold?
3289
3290 **Secretary of State Ysursa:** Governor – Governor –
3291

3292 **Governor Otter:** If it was going to be halved tomorrow?

3293

3294 **Secretary of State Ysursa:** It's very – some of these questions are well founded, but to me the biggest
3295 problem is – is we're dealing with people in an irrational market. Why would anybody in the last
3296 quarter of '09 at Payette Lake have four sales that had one point – or four assignments that
3297 garnered one point six million in leasehold value. And I know there'll be people who want to
3298 dispute how we compute leasehold value, but who in their right mind would be doing that in
3299 this market with this uncertainty of the Land Board of what we're going to do? It's hard for us
3300 to be rational and explain the actions of why we are in an irrational market putting beautiful
3301 expensive improvements on somebody else's property.

3302

3303 **Governor Otter:** I've offered my mea culpas that we're part of the confusion –

3304

3305 **Secretary of State Ysursa:** Yes.

3306

3307 **Governor Otter:** – and the noise over the last three years or – and longer.

3308

3309 Anybody else got anything they want to offer?

3310

3311 Question is, shall the –

3312

3313 **Attorney General Wasden:** Governor.

3314

3315 **Governor Otter:** Yes.

3316

3317 **Attorney General Wasden:** I do have a statement I would like to make.

3318

3319 **Governor Otter:** Yes, Mr. Wasden.

3320

3321 **Attorney General Wasden:** I was just waiting and listening to the debate.

3322

3323 Today this Board has an opportunity to begin fashioning a solution to a problem that has
3324 bedeviled this and past Boards for almost thirty years. Namely, how to fulfill the Board's
3325 fiduciary duty to the trust beneficiaries to achieve the maximum long-term financial return from
3326 cottage site leases. As we've discussed many times, past Boards have treated this issue as a
3327 political football figuratively punting the ball down the field to future Land Boards.
3328 Unfortunately we have caught that punt.

3329

3330 In the early 1980s the Board, rather than seeking a market return on the cottage site leases,
3331 adopted a policy of premium rent, the effect of which we now know has been to create state
3332 leases that generate large leasehold values and inure primarily to the lessees and not the
3333 endowment beneficiaries. Indeed a recent Department of Lands' study showed that
3334 seventy-eight lease transfers generated twenty-six million dollars in leasehold value of which
3335 only ten percent went to the beneficiaries. In 1990 the Board did not oppose the move to
3336 legislate away the conflict auction process, which in my opinion was dictated by the
3337 Constitution. The stated reason for exempting cottage site leases from the conflict auction
3338 process was to reduce consternation among the lessees and thereby create a stable market.
3339 The focus of this legislation was on the consternation among the lessees rather than the benefit
3340 to the trust beneficiaries.

3341

3342 In lieu of the conflict auction process, the Board was legislatively directed to ensure market rent
3343 throughout the duration of the lease. Yet throughout the last twenty years, just the opposite
3344 has occurred. Lessees and the Board have repeatedly clashed over how to determine market
3345 rent and successive Boards, out of frustration and political pressure, have frozen the contract
3346 rental rate at two and a half percent despite numerous expert reports commissioned by the
3347 Board demonstrating that two and a half percent is significantly below market rent. Indeed, I
3348 must admit I fell into this trap by agreeing at some point to freeze the rental rate. It made sense
3349 at the time of such a vote and, perhaps in retrospect, that was not such a wise choice. In

3350 summary, this Board and past Boards have pursued policies that preclude achieving market rate
3351 of return on cottage sites, which in turn has prevented the Board from meeting its fiduciary duty
3352 to the trust beneficiaries.
3353
3354 I recount this history not to cast blame on cottage site lessees or the Land Board. The lessees
3355 are simply advocating for the preservation of their family traditions. Many of them have held
3356 state leases for years and built family memories around Payette and Priest Lakes. While the
3357 lessees efforts to preserve their family traditions are ones I personally commend and admire,
3358 nothing in the Idaho Constitution provides that the Board should seek, in the administration of
3359 this trust, to preserve family traditions.
3360
3361 Idaho's Constitution has different, but explicit, priorities for the Land Board. As explained by the
3362 Idaho Supreme Court in the context of grazing leases, the Constitution expressly requires the
3363 Land Board to exercise a duty of undivided loyalty to the endowment beneficiaries.
3364
3365 In 1996 the Court stated that the Board must find authority in the Constitution and statutes for
3366 its actions. Again in 1999, the Court held that rather than seeking to provide income to the
3367 schools and the State in general, article 9, section 8 requires the State consider only the
3368 maximum long-term financial return to the schools in the leasing of school endowment public
3369 grazing lands. In other words, the Board in its trust capacity cannot take into account matters
3370 other than the maximum long-term financial return to the trust beneficiaries.
3371
3372 While this Board's constitutional mandate is clear, it is difficult in practice for individual
3373 members of the Board to adhere to this mandate because of the inherent conflict between this
3374 duty and each member's duty as a statewide officer. Economic literature describes the problem
3375 confronting each member of this Board as rent seeking. Rent seeking occurs when the benefits
3376 of a policy are concentrated in a small group, but the costs of the policy are diffuse. In such a
3377 situation, the small group has an incentive to use the political process to advocate for lower
3378 rental rates because the cost to the large group – the larger group, the beneficiaries, is too

3379 diffuse to lead to organized resistance to the proposed policy. Since there has been no
3380 organized call for the Land Board to achieve a market rate of return, past Boards have simply
3381 followed the path of least resistance. Again, this is not accusatory. It is simply a matter of
3382 history.
3383
3384 The Subcommittee's recommendation if adopted, in my opinion, will simply continue the past
3385 practice of punting this political football down the field. The Director and Assistant – excuse me
3386 – the – Terry Anderson, Professor of Economics, indicated his view that fulfilling that policy
3387 would – that the members of this Board would fail to meet their statutory and constitutional
3388 duty.
3389
3390 Today is the day to put this matter to rest and not to punt this problem to a future Land Board.
3391 Thus, I must respectfully vote in opposition to the Subcommittee's proposal. While I respect the
3392 Herculean effort of the Secretary of State and the Superintendent of Public Instruction to find a
3393 solution to the cottage site problem, and I commend them for the extreme amount of effort and
3394 the personal commitment they have shown and the personal abuse they have endured, based
3395 upon the record before this Board, the Subcommittee's proposal falls short of meeting this
3396 Board's constitutional duty to achieve the maximum long-term financial return to the
3397 endowment beneficiaries. For the same reasons, I must also oppose the cottage site lessees'
3398 proposals. When acting and voting as a member of the Land Board, I'm acting as a member of a
3399 constitutional board that is charged with making financial decisions that will ensure the
3400 endowment beneficiaries receive the maximum long-term financial return from the endowment
3401 assets. By law, I have a duty of undivided loyalty to them. My duty, and therefore my choice
3402 today, is clear. I must defend the interests of the current and future beneficiaries despite
3403 pressure to do otherwise.
3404
3405 Thank you.
3406
3407 **Governor Otter:** Further discussion.

3408

3409 Mr. Luna.

3410

3411 **Superintendent Luna:** Mr. Chairman, I appreciate Lawrence's comments, and I think he's wrestling with
3412 what Ben and I have been wrestling with since this Subcommittee was formed.

3413

3414 I will – it – it's clear from the testimony from Mr. – from Terry Anderson that anything less than
3415 six percent immediate increase to six percent would be a violation of what our constitutional
3416 mandate is yet we know that we've offered these lots at five percent, and we had no takers.
3417 Here's – here's the point I would like to get to. The Secretary of State has said that he is willing
3418 to have further discussions and and – and, you know, we've heard some things today that we
3419 hadn't considered. I'm more than willing to continue to meet and pursue some of the ideas
3420 we've heard. We've heard from other – the other parties that – who expressed their
3421 willingness. I guess I'm just not comfortable in casting a vote today on the only motion that we
3422 have before us. I would like – I don't know what this does for our timeframe. I know people
3423 have travelled long distances to be here, but I just don't think it would be wise, at least on my
3424 part, I'm not comfortable voting knowing that all parties are willing and wanting to meet to have
3425 further discussions about disposing of these properties, about premium rent. I don't know how
3426 much more time we have. I know we have an April deadline, but I guess – I'll – I won't make a
3427 motion. I don't know if I can because I seconded the Secretary's motion, but I'll throw that out
3428 on the table for discussion about whether we have more time and if more time would be –
3429 spending more time on this effort would be productive.

3430

3431 **Governor Otter:** Well, I'll tell you, at least in part you've answered your own question. We've got April –

3432

3433 **Secretary of State Ysursa:** 30th –

3434

3435 **Governor Otter:** – 30th bearing down on us.

3436

3437 **Secretary of State Ysursa:** – for the application to renew –

3438

3439 I'm sorry, Governor. I didn't go through the Chair.

3440

3441 **Governor Otter:** So that's – that's at least a partial answer to your question.

3442

3443 Yes.

3444

3445 **Secretary of State Ysursa:** Governor, members of the Board and Tom, I respect that. I also certainly
3446 respect the Attorney General's comments. In that vein, rather than – and I appreciate your
3447 voting no.

3448

3449 What are you in favor of that we ought to do? Are you – are you advocating a six percent of the
3450 current, Mr. Attorney General?

3451

3452 **Governor Otter:** Mr. Wasden.

3453

3454 **Attorney General Wasden:** Governor, I've made no motion.

3455

3456 **Secretary of State Ysursa:** You're just against mine.

3457

3458 **Attorney General Wasden:** Governor, Mr. Secretary of State, I will be voting no on this motion.

3459

3460 **Secretary of State Ysursa:** As a fellow Board member, Governor and Lawrence, it would be nice to know
3461 what – what would meet your approval. I think that's a fair question.

3462

3463 **Attorney General Wasden:** Governor, Mr. Secretary of State –

3464

3465 **Governor Otter:** Mr. Wasden.

3466

3467 **Attorney General Wasden:** Certainly as outlined by the expert in this matter, Mr. Terry Anderson, it
3468 would require six percent tied to T-bills, assessed value, ten-year leases.

3469

3470 **Governor Otter:** Mr. Luna.

3471

3472 **Superintendent Luna:** Lawrence, are you saying immediately go to six percent then?

3473

3474 **Governor Otter:** Mr. Wasden.

3475

3476 **Attorney General Wasden:** Thank you, Governor.

3477

3478 There was some discussion with some kind of phase-in period. I don't think we investigated that
3479 very much – a lot with Mr. Anderson. In his view the ten-year rolling average did not work. I
3480 certainly would like to at some point perhaps know a little bit more about that phase-in because
3481 I do think there's an issue there. But really that's – that's the parameters.

3482

3483 **Governor Otter:** Mr. Ysursa.

3484

3485 **Secretary of State Ysursa:** Governor, appreciate that, Lawrence.

3486

3487 Governor and members of the Board, in response to Tom's inquiry, I am willing to meet day and
3488 night, outside Lincoln day banquets that we all have, to try to get some resolution of this. The
3489 answer we come up with will be something everybody could hate, which means we're probably
3490 close. But I think the motion, and I think – Tom, correct me if I'm wrong – I think we have some
3491 consensus and agreement even – and even from the Attorney General or Mr. Anderson that
3492 part one of the Subcommittee's motion, people agree to.

3493

If it's on division of the question or whatever, let's – let's divide the question. But let's – let's don't leave here today without agreeing to some – something. If we need to continue to work, if there's really a difference on the Board on the premium rent issue, then so be it. I'm trying to make some – kick the can down the road, so to speak, and get some progress if we can. I think we saw a consensus from everyone – I guess that's what consensus is hopefully – about disposal or exchanging or other ways of unifying ownership. I think that we all agree with. Okay. Let's go with that. Two, ten-year lease right now. Maybe if there's no – because of the uncertainty and where we're going, and if our goal is to get rid of properties or exchange and get out of them, I think we send mixed signals by suddenly saying we're going to do a thirty-five year lease. And then I've vacillated on that, and I got pushed over the edge reading more last night. And now that's where I came from this morning. Okay, the ten-year lease we can agree to. Maybe it stops there.

The rent – the figure – at least from a fellow member of the Subcommittee that I proposed, the four percent of the ten-year average and five-year phase-in, do we have agreement there at least of a majority of the Board. Let's kick it down the road – not delay, delay, delay. Easy thing to do would be to issue a – let's issue somebody a one-year lease, and let's think more about it. I – I don't believe that's what we should do or hire it on to do. And – and we need to get moving on this, and there are major decisions being made. If I'm a lessee out there, what are these folks going to do? What lease am I going to sign? And April 30th is the last day to do it. Well, I think they would like to have more than about three days to look at something that's in final form and where we're headed. Or do we continue to do let's do an interim thing and figure it out later. I'm amenable to do anything, but let's kick it down the road. Let's make some progress.

Superintendent Luna: Governor.

Governor Otter: Mr. Luna.

3523 **Superintendent Luna:** I think, well, my goal – and I'm sure everyone's goal – is to get maximum return
3524 for the beneficiary. And we know that even with the scenarios that we're looking at, the four
3525 percent or even the six percent, that that's less than what we can make in other investments.
3526 So I – you know, if we divide the question or however that is – happens, you know, I'm
3527 agreeable to that. If we want to focus and kick this can down the road at least a ways, then let's
3528 talk about the first recommendation, and that is to begin a process – not a long drawn out
3529 process, but begin a process where we put together a plan to begin to liquidate these properties
3530 in a market savvy manner so that we can put them – that – those either invest in commercial
3531 properties or other investments that will far outpace the four percent or six percent that we're
3532 currently debating. That's how – that's how I think we're going to realize maximum return for
3533 the beneficiary. How we structure the lease and – and premium rent – we can – maybe we do
3534 need to separate those so that we do move this down the road a ways.
3535
3536 **Governor Otter:** Mr. Wasden.
3537
3538 **Attorney General Wasden:** Governor, I do think that I've – or at least that I've tried to be very clear
3539 today that my view is that this problem will never go away until there's unification of the title to
3540 these properties. It is the improvement and the dirt. And that – that has clearly got to be part
3541 of what we try to accomplish here. Now, when I say that, I don't mean necessarily we look only
3542 at the sale of these properties. I think it needs to look at both aspects of that – that is either
3543 acquiring the improvements and associating them with the real estate or selling the underlying
3544 dirt and whatever happens to the real estate. I think that in order for us to be market savvy, as
3545 our Subcommittee has recommended and with which I agree, is that we should have the
3546 Department undertake a study and report back to us about the process that should be used to
3547 get there, including all of the elements on the table, exchange, sale –
3548
3549 **Secretary of State Ysursa:** Unification.
3550

3551 **Attorney General Wasden:** Exactly. Anything that would be of value in the process. And I know – and
3552 I'm not using that term value in a – in a dollar sense necessarily, but to – to examine the entire
3553 issue of let's build a strategy that will give us the return ultimately, and the key to that has got
3554 to be unification of title on these properties. That's essential. We cannot solve this problem in
3555 the absence of doing that.
3556
3557 **Secretary of State Ysursa:** Governor, members –
3558
3559 **Governor Otter:** We've got – excuse me.
3560
3561 Mr. Ysursa.
3562
3563 **Secretary of State Ysursa:** Governor, members of the Board, I couldn't agree more. I – I don't believe
3564 that our number one recommendation and the unification are mutually exclusive. I think
3565 they're mutually inclusive and should be part of the one item we can agree on today and start
3566 down the road. But I think it's exactly the same thing – what Mr. Anderson said in his report and
3567 whatever. It's whether we call it unification of ownership, whatever. I think that's part of our
3568 number one recommendation.
3569
3570 **Governor Otter:** Mr. Wasden.
3571
3572 **Attorney General Wasden:** Governor, Mr. Secretary of State, I couldn't agree more.
3573
3574 **Superintendent Luna:** Governor, could –
3575
3576 **Governor Otter:** I would –
3577
3578 **Superintendent Luna:** – I just ask a point of order here?
3579

3580 **Governor Otter:** Yes.

3581

3582 **Superintendent Luna:** You know –

3583

3584 **Secretary of State Ysursa:** We can withdraw everything, if you want.

3585

3586 **Superintendent Luna:** – how do we divide this then? I've never participated in that before.

3587

3588 **Governor Otter:** You could – well, you could ask for a division of the question –

3589

3590 **Superintendent Luna:** I can as a second?

3591

3592 **Governor Otter:** Well, somebody would. I'm not sure the seconder can without the permission of the
3593 maker. I don't know if that's the correct protocol.

3594

3595 **Secretary of State Ysursa:** He has my permission to do about anything.

3596

3597 **Governor Otter:** Okay. But you could ask for a division of the question and divide the question into such
3598 parts as each would stand on its own. It would become a motion all by itself. So that's why I
3599 continued this. We've got a four part, basically four parts. One is unifying ownership.

3600

3601 **Controller Jones:** Right.

3602

3603 **Governor Otter:** – through –

3604

3605 **Secretary of State Ysursa:** Whatever. All means.

3606

3607 **Governor Otter:** – liquidation, sale, et cetera. Second is a four-percent, five-year phase-in on a ten-year
3608 plan. The third would be dealing with the premium rent. The fourth would be a ten-year lease.

3609 Now, you could have four divisions – you could have a division – each one of those standing
3610 alone is a proper question. Or you could combine two or three that you thought was going to
3611 be successful in passing. And I would entertain such a –
3612
3613 Yes, Mr. Wasden.
3614
3615 **Attorney General Wasden:** Governor, just a comment about that, and that is that in terms of separation
3616 possibilities here, item number one I think is a separate – could be separated as an issue and
3617 dealt with.
3618
3619 **Governor Otter:** Uh-huh.
3620
3621 **Attorney General Wasden:** The other three, particularly numbers two and three, really seem to be so
3622 intertwined that you can't really divorce one from the other. And perhaps even item number
3623 four, less so perhaps, but the rate that is being charged against the value in terms of whether it
3624 produces premium rent or doesn't produce premium rent really seem to be very closely tied.
3625 You can't really separate those two.
3626
3627 The ten-year issue, or the thirty-five year issue, as either of them have been described, can
3628 apply – has an impact on the other two, and probably should be considered jointly, but actually
3629 could, I think, be separated in determining how long that lease is going to be. Probably the best
3630 approach is to have all three of those things in the same mixing bowl, I guess for lack of a better
3631 term.
3632
3633 **Governor Otter:** I'll do whatever you can get a majority vote for. But I would sure agree – I think
3634 premium rent is a standalone. It could be a – divisible from the other three; however, in
3635 number two, the four percent, ten-year plan with a five-year phase-in, also encumbers this
3636 number four. So actually what you're down to is – you can be down easily to three questions.
3637

3638 **Secretary of State Ysursa:** Governor, would it clean it up parliamentary-wise –

3639

3640 **Governor Otter:** Or you could –

3641

3642 **Secretary of State Ysursa:** – if I withdrew my motion and started making other motions?

3643

3644 **Governor Otter:** With the consent of your second.

3645

3646 **Superintendent Luna:** I consent.

3647

3648 **Secretary of State Ysursa:** All right. Let's – Let's get –

3649

3650 **Governor Otter:** Motion withdrawn.

3651

3652 Mr. Ysursa. Oh, excuse me. Ms. Jones.

3653

3654 **Controller Jones:** No, I agree.

3655

3656 **Governor Otter:** Okay.

3657

3658 **Controller Jones:** I agree.

3659

3660 **Governor Otter:** Okay.

3661

3662 **Secretary of State Ysursa:** Governor and members of the Board, I – I would move that we adopt the
3663 Subcommittee recommendation number one, and include maybe other language or whatever,
3664 with the intent of following – of unifying the ownership of the land either by sale, exchange or
3665 other means, and everything's on the table there, and have the Land Department – we've got
3666 January 2011 and to report back to us by then. And that would be my motion.

3667

3668 **Attorney General Wasden:** Second.

3669

3670 **Superintendent Luna:** Is – Mr. Chairman –

3671

3672 **Governor Otter:** Mr. Luna.

3673

3674 **Superintendent Luna:** – I just – is –

3675

3676 **Secretary of State Ysursa:** Just number one.

3677

3678 **Superintendent Luna:** – is a year – I mean, that seems like a long time, but I'm not going pry into it too
3679 much, but it seems like a long time.

3680

3681 **Secretary of State Ysursa:** The Department would tell you it's probably not long enough.

3682

3683 **Governor Otter:** There's a motion. Is there further discussion? The motion has been made and
3684 seconded. All those in favor, signify by saying aye.

3685

3686 *(All say aye.)*

3687

3688 Opposed nay. The motion is passed.

3689

3690 Mr. Ysursa.

3691

3692 **Secretary of State Ysursa:** Oh, I got another one, huh.

3693

3694 **Governor Otter:** It's your show.

3695

Secretary of State Ysursa: It's not going to win an Oscar.

The – my second motion would be to have the lease, because I think it ties into that. If our real intent is to extricate ourselves and get out of here, I think get out of the situation – not necessarily out of here – and to give the mixed message of going to thirty-five years, and remember, these leases have the provision in them that we can sell or exchange upon a hundred and eighty days notice, and whatever, I would move that we go to a ten – uh, the new leases be offered for ten years.

Controller Jones: I would second that.

Governor Otter: With the proviso –

Secretary of State Ysursa: Oh, yes –

Governor Otter: – a hundred and eighty-day notice.

Secretary of State Ysursa: It will be in there.

Governor Otter: Okay. It's been moved and seconded. Further discussion. Hearing no discussion, the question is, shall the motion prevail. All those in favor signify by saying aye.

(All vote aye.)

Those opposed, nay. The ayes have it, and the motion has passed.

Secretary of State Ysursa: Mr. Chairman.

Governor Otter: Mr. Ysursa.

3725

3726 **Secretary of State Ysursa:** I would make a motion that the items – where are we – two and three of the
3727 Subcommittee report be deferred for one month, and during that interim time the
3728 Subcommittee and any and all other Board members, staff, legions of citizens, whatever, will
3729 meet and try, and especially, and I'm not teasing, the cottage site representatives, Mr. Lempesis
3730 and others, and try to iron out some – something we can come back to in a – in a month certain
3731 – the next meeting.

3732

3733 **Superintendent Luna:** Mr. Chairman, I'll second that.

3734

3735 **Governor Otter:** You've heard the motion. Is there further discussion?

3736

3737 **Superintendent Luna:** I'd just like – Mr. Chairman, I – when we come back in a month, it's – I would
3738 expect we are going to make a decision.

3739

3740 **Secretary of State Ysursa:** That would be my sincere hope. Keep hope alive.

3741

3742 **Governor Otter:** Further discussion.

3743

3744 Now I – I'm going to reluctantly – I'm going to reluctantly support this, but, you know, I heard a
3745 lot of testimony today both from both groups that they are sincere. They think we're close. In
3746 fact I've heard that mentioned several times. But I would – I just want to put you on notice,
3747 even if I'm standing alone, I'm not going to delay it another month. I mean after –

3748

3749 **Secretary of State Ysursa:** Correct. We're going to –

3750

3751 **Governor Otter:** I'm going to quit tomorrow. Tomorrow starts Lent. So I'm going to quit tomorrow.

3752

3753 **Secretary of State Ysursa:** Yes. I figured this is the last day to eat red meat.

Governor Otter: That's right.

Further discussion. Being no further discussion, the question is, shall the motion prevail. All those in favor, signify by saying aye.

(All vote aye.)

Motion is passed.

Secretary of State Ysursa: Governor, I move we adjourn.

Superintendent Luna: Second.

Attorney General Wasden: I want to debate that motion, Governor.

Governor Otter: Moved and seconded that we now adjourn. It's non-debatable. All those in favor, signify by saying aye.

(All vote aye.)

We are adjourned.

Meeting adjourned at 1:41 p.m.

TRANSCRIBER'S CERTIFICATE

STATE OF IDAHO)
) ss.
COUNTY OF ADA)

I, Susan Terry, a Notary Public in and for the State of Idaho, residing at Nampa, County of Canyon, State of Idaho, do hereby certify:

That the foregoing transcript of the proceedings relating to the matter of *Recommendation of the Cottage Site Subcommittee* for the State Board of Land Commissioners of the State of Idaho, recorded on February 16, 2010, was produced via audio recording and thereafter reduced to typewriting by me, and that the foregoing one hundred thirty-one (131) pages contains a full, true and correct record of the oral conversations related to said matter, to the best of my ability, given the speakers' enunciation and the quality of the audio recording itself.

I hereunto set my hand and seal this 23rd day of February 2010.

Susan Terry

SUSAN TERRY
Notary Public for Idaho
Residing at Nampa, Idaho
My Commission Expires 8-30-2011

Exhibit 37

Addendum to Cottage Site

Subcommittee Report

(March 16, 2010)

Addendum

Cottage Site Subcommittee Report

To

The Idaho State Board of Land Commissioners

March 16, 2010

Following the February 16, 2010 meeting of the Board of Land Commissioners, the Subcommittee met with representatives of the lessees and of the endowment beneficiaries. The Subcommittee is revising the recommendation with regard to premium rent.

The Subcommittee recommends that premium rent be calculated at 10% of the gross leasehold value or 50% of the net leasehold value, whichever is the greater amount for the endowment. Net leasehold value shall be calculated by subtracting the original leasehold value (sales price less the value of tenant improvements) of the lessee who is transferring the lease from the leasehold value (sales price less the value of tenant improvements) when a transfer occurs.

Exhibit 38

Spreadsheet Comparing Annual Rents to Leasehold Sales, 2001-2009, provided by Idaho Department of Lands in response to request from Attorney General Lawrence Wasden (March 11, 2010)

COPY

STATE OF IDAHO

OFFICE OF THE ATTORNEY GENERAL

LAWRENCE G. WASDEN

March 10, 2010

VIA STATEHOUSE MAIL

George Bacon, Director
Idaho Department of Lands
300 North 6th Street, Suite 103
Boise, ID 83702

Re: Cottage Sites

Dear Director Bacon:

In order to better understand the impact of past Land Board decisions on revenue from cottage site leases, and the implications for the Board's pending decision on cottage site rental rates, I request that you prepare a spreadsheet with the following information for the years 2001 through 2009:

- Total annual rent received each year from cottage site leases.
- Total premium rent received each year.
- Total annual income received each year from cottage site leases (annual rent and premium rent).
- Number of leasehold sales each year.
- Money lessees received each year from cottage site leasehold sales.

Given the pending Board decision on cottage site leases, I would like to have this information as soon as possible.

Sincerely,

LAWRENCE G. WASDEN
Attorney General

LGW:dd

P.O. Box 83720, Boise, Idaho 83720-0010
Telephone: (208) 334-2400, FAX: (208) 854-8071
Located at 700 W. Jefferson Street, Suite 210

From: Susan Terry [mailto:STerry@idl.idaho.gov]
Sent: Thursday, March 11, 2010 2:22 PM
To: Carter, Janet
Cc: Deck, DeLayne; George Bacon; Bob Brammer; Kathy Opp; Mike Murphy; Jane Wright; Patrick Hodges; Follett, Robert; Lisa Johnson; Francine Gonzales
Subject: FW: FY01-FY09 Cottage Revenue_LWasden.xlsx

Please see the attached spreadsheet. This is being sent in response to Attorney General Wasden's request from yesterday afternoon.

Susan Terry
Office of the Director
Idaho Department of Lands
(208) 334-0242
sterry@idl.idaho.gov
www.idl.idaho.gov

From: Jane Wright
Sent: Thursday, March 11, 2010 2:18 PM
To: George Bacon; Susan Terry; Kathy Opp; Bob Brammer
Subject: FY01-FY09 Cottage Revenue_LWasden.xlsx

Susan:
Please forward the attached worksheet to Mr. Wasden.
It includes data he requested, on March 10, 2010.
If you need additional assistance, please let me know.

Jane Wright
Strategic Business Analyst
P.O. Box 83720
Boise, ID 83720-0050
Office: (208) 334-0223
FAX: (208)334-2339
e-mail: jwright@idl.idaho.gov

Please consider the environment prior to printing this email.

Cottage Program Revenue	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009
Total Annual rent	2,127,608	3,912,075	2,601,213	2,732,604	2,734,414	3,302,375	3,927,898	4,264,205	4,223,610
Total Premium Rent			126,422	400,493	375,236	720,301	516,351	384,060	305,901
Total Annual Income	2,127,608	3,912,075	2,727,635	3,133,097	3,109,650	4,022,676	4,444,249	4,648,265	4,529,511
Number of Leasehold Sales	28	19	21	12	15	9	11	5	10
Lessees Proceeds (Premium * 90%)			1,137,798	3,604,437	3,377,124	6,482,709	4,647,159	3,456,540	2,753,111

Premium rent Data not available for FY2001 and FY2002

Source of Data: IDL Financial System, STARS

Exhibit 39

Letter, Karl Klokke to

Land Board members (Feb. 24, 2010)

RECEIVED
FEB 25 2010
OFFICE OF THE
ATTORNEY GENERAL

February 24, 2010

From:
Karl Klokke
1109 North 21st Street
Boise, Idaho 83702 1-208-412-9411

To: State Board of Land Commissioners
Governor: C. L. Butch Otter
Office of the Governor
P. O. Box 83720
Boise, Idaho 83720

Secretary of State: Ben Ysursa
Office of the Secretary of State
P. O. Box 83720
Boise, Idaho 83720-0080

Attorney General; Lawrence Wasden
Office of the Attorney General
P.O. Box 83720
Boise, Idaho 83720-0010

Superintendant of Public Instruction: Tom Luna
Idaho Board of Education
P.O. Box 83720
Boise, Idaho 83720-0037

Controller: Donna Jones
Office of the State Controller
P. O. Box 83720
Boise, Idaho 83720-0011

Re: Cabin Site Leases, Payette Lake, Idaho

Lady and Gentlemen,

I have been a Payette lake front cottage site leaseholder for four years. The purchase of the leasehold interest was made on the premise that the State would substantially continue their previous Cottage Site leasing policies.

I also have been in the construction/real estate business all of my professional life and truly understand that for the State to continue in the cottage site leasing business will be an endless stream of insufficient returns on the current values of the State assets, political turmoil and high administration costs.. The State will improve its position by tens of millions of dollars by that move. Although I strongly as a citizen of the State of Idaho

believe that the Land Board is on the right track; it is going to cause people like myself substantial financial harm.

My wife and I spent $750,000 to buy our leasehold interest in 2005 and we have spent another $100,000 to demolish existing buildings, trees, build retaining walls and earthwork to prepare the building site. We never built a home on the site. Today I think I could sell the leasehold for around $300,000 and maybe less after the final decisions of the Land Board are made. The State did approve the transaction and accepted a $75,000 fee for doing so. Unfortunately the past policies of the Land Board allowed the previous leaseholder to make very substantial profits at the expense of the State and to myself.

I however, was not the party who set the policies to allow the previous leaseholder to be unjustly enriched. I did purchase the leasehold interest with the faith that the current leasing policies (as poor as they were for the State) would be substantially maintained going forward. Because of the sudden change in policies of the Land Board I will be financially damaged in the neighborhood of $500,000. A small percentage of the leaseholders who bought late in the game at high prices are in a similar position.

Most of the leaseholders have had their properties for a long time and enjoyed many years of low rents with minimal up front investment. Some families will have to make social adjustments to give up their leases; however they will not be financially damaged. I do not believe they are owed anything if they have to sell their leasehold interest, forced to buy their properties or pay higher rents in the future.

I am very opposed of the State being enriched by the possibility of charging a high premium rent on the entire sales price when I will be selling at a substantial loss. That is simply adding insult to injury. With the current proposal if it took me 5 years in a very depressed real estate market to sell my leasehold interest for $300,000 I would end up paying the State $150,000 for premium rent on a transaction that I have already lost of over $500,000. That is simply not right.

If the state is going to charge a premium rent; it should charge only it on the increase of sales price of the leasehold interest. For example if someone bought in the 1970's for $50,000 and if they could sell their leasehold interest today for $300,000; the State should be entitled to a very substantial part if not all of the gain of $250,000.

I realize the State has gotten itself into a very undesirable situation. The Land Board is on the road of a good solution. The equitable thing to do is try to work out compensation to those who have had seven figure losses because of the past policies of the Land Board. I put some thoughts below as a brainstorming exercise:

- Don't charge a premium rent on a resale of a leasehold interest where there has been a substantial loss upon the part of the current leaseholder. Establish a premium rent rate on the increase in value only.
- Consider of a refund of the premium rent paid by the previous leaseholder to the current leaseholder. It was an unjust fee because the Land Board is proposing not to deliver the implied benefits of that transaction.

- Extend the period of low rents to those who have paid high prices so they have some chance of getting some reasonable value for their leasehold purchase. This right to low rent for a period of time could be transferred to a future buyer so that current leaseholder could sell a stream of low rents and recapture some of his loss. In my case I could get an arrangement where I have the right to lease the property for 20 years at $30,000 per year (twice what the rent was when I bought it) then have a forced purchase to occur at the end of the 20 years would be a step of trying to provide some compensation to me.

All I trying to express is that a few of the leaseholders have been very severely damaged by sudden changes in the policies of the Land Board. We have been wrong by these changes. The Land Board was on a regular basis approving transactions to new leaseholders were expecting these implied benefits. The Land Board surely was aware of the representations of local brokers and did nothing to refute what was being represented. During the approval process of the transfer of the leasehold interest no one sent a letter or warning that the past policies would not likely be continued For good reasons it is in the best interest of the State to change their policies; I only ask the Land Board to at least partially compensate those who entered into an implied contract which looks will not be honored.

I believe no one should profit by being a Cottage Site leaseholder but at the same time it is only equitable that a few of us have been mislead and harmed by the previous policies of the Land Board should get relief. The improved position of the State by getting out of the Cottage Site leasing business will be far greater than any costs associated with making amends to those were severely damaged by these changes.

Sincerely,

Karl C Klokke

Karl Klokke

Exhibit 40

Letter, Terry Copple

to Land Board members

(March 15, 2010)

Davison, Copple, Copple & Copple, LLP
Attorneys at Law

Direct Contact:

Terry C. Copple
Direct: (208) 342-3766

E-Mail: tc@davisoncopple.com
http://www.davisoncopple.com

199 North Capitol Boulevard, #600
Post Office Box 1583
Boise, Idaho 83701

Telephone: (208) 342-3658
Facsimile: (208) 386-9428

March 15, 2010

SENT VIA HAND DELIVERY

State Board of Land Commissioners
c/o Idaho Department of Lands
300 North 6th Street, Suite 103
P.O. Box 83720
Boise, Idaho 83720-0050

Re: Cottage/Residence Lease Renewal

Dear Chairman and Members of the Board:

As you are aware, this office has been retained by the Payette Lake Cabin Owners Association (the "Association") in order to vigorously contest the cabin site lease agreements proposed by the Board of Land Commissioners (the "Board") to subsume the previous leases. The undersigned is aware that the Board intends to make a decision regarding the foregoing proposal on March 16, 2010. In advance of that date, the undersigned submits this letter respectfully urging the Board to reject the lease proposal and to adopt the plan submitted by the Association.

The proposal submitted by the Board is problematic for numerous reasons. However, in light of the fact that the two issues before the Board on March 16, 2010, will be: A.) The Rental Rate, and B.) Premium Rent, this letter will solely address the foregoing matters.

Before doing so, the undersigned would note that the Association is in agreement with the Board's choice to engage in land exchanges so as to effectively remove the Board from the business of leasing its endowment lands. However, the Association's position differs from the Board's in one respect - the Association prefers that the land exchanges be expedited and occur

before December 31, 2010. In other words, the Association believes that the foregoing exchanges should occur sooner rather than later. As to the issues referenced above, i.e., rental rate and premium rent, the undersigned represents as follows:

A. Rental Rate

Section D of the proposed lease agreement is the provision addressing the rate at which rent will be charged. Sub-section 1.1 thereof states, *inter alia*, that rent will be calculated yearly "at 4% of the average appraised value of the lot ... over the most recent 10 years." In essence, rent will be determined in a three-step process: 1.) Procure the appraised value of the lot for each of the previous ten years; 2.) Add those values together and divide by ten; 3.) 4% of the number left over is the lessees' rent.

While the simplicity of the foregoing methodology of calculation may be seductive, it is rife with difficulties.

First, there is no empirical data of which the undersigned is aware that supports the contention that the calculation contained in Section D (1.1) of the proposed lease will result in "market rent." In the absence of data supporting such a notion, why should the Association or anyone believe that the foregoing methodology of calculation will produce market rent? Bolstering this argument is the fact that the calculation is tied to the ten year average valuation of the lot in question. Even if the methodology of charging 4% of the value of the Leased Premises was a valid way of charging market rent for a given year, averaging that total with the value of the Leased Premises for the previous ten years does not give one current market rent; it simply produces an arbitrary number and does so under the assumption that current market rent is somehow achieved by deferring to the economic conditions of the previous decade.

Second, as much as this Board wants to ignore the issue, the Board can only charge market rent for endowment leaseholds. As noted in prior correspondence, I.C. § 58-310A states in no uncertain terms that "maximum long-term financial returns to the institutions to which granted are best obtained through stable leases at market rent." I.C. § 58-310A is the law in this State and the Board is charged with faithfully executing the laws of Idaho. I.C. § 58-310A states that the Board can only charge market rent. Accordingly, any deviation therefrom is an act inconsistent with the general laws and is null, void, and *ultra vires*. *See Roeder Holdings, L.L.C., v. Board of Equalization of Ada County*, 136 Idaho 809, 813, 41 P.3d 237, 241 (2002) ("When a conflict exists between a statute and a regulation, the regulation must be set aside" and yield to the statute).

The Board's response to the foregoing position has been to simply point to the verbiage of Article IX, Section 8 of the State Constitution. Implicit in this response is the Board's

contention that I.C. § 58-310A runs afoul of the State Constitution and is therefore entitled to no deference by the Department of Lands. The problems with this position are two-fold:

1.) I.C. § 58-310A is constitutional. The foregoing provision does not run afoul of Article IX, Section 8; rather, it represents a policy decision by the legislature as to how to achieve "maximum-long term financial returns" and thereby fulfill the Board's Constitutional mandate. *See State ex rel. Kempthorne v. Blaine County*, 139 Idaho 348, 79 P.3d 707 (2003) ("[t]he judicial branch of government must respect and defer to the legislature's exclusive policy decisions") (citations omitted) (emphasis added).

2.) Even if I.C. § 58-310A is unconstitutional, it remains Constitutional until a judge declares otherwise – in the absence of judicial declaration, the professional annotations of others are irrelevant. In other words, the province of this Board is solely to faithfully execute the laws of the state – it is not the province of the Board to determine the Constitutionality of such laws or pick and choose which laws it will or will not obey based on its own interpretation of the laws of the State. Therefore, any argument that the Board's decision is valid because I.C. § 58-310A is unconstitutional is completely without merit as that provision has never been declared unconstitutional by a Court of law. *See* 16 C.J.S. Constitutional Law § 354 ("The core power of the executive branch is to implement or carry out legislative policies as embodied in enacted legislation or as declared by the legislature. In other words, under our system of government, it is the function of the executive department, honestly and efficiently, to administer, enforce, or faithfully execute the laws, as interpreted by the courts ... In performing such function, executive officers may exercise some discretion, but they may not select the laws which they will enforce or the persons whom they will protect") (emphasis added).

Third, the proposal contains no cap limiting the amount by which rent could rise. This puts lessees in a situation of intolerable financial vulnerability. Without a cap, the amount of rent that lessees might be forced to pay is limitless. Compounding the validity of this concern is the fact that the terms of the lease themselves state that the Board "reserves the final right to determine the value of the Leased Premises for the purpose of establishing rent in accordance with its Constitutional mandate in accordance with Article IX, Section 9." According to the lease, this determination can be carried independent of any assessment made by the county. Thus, the Board has written into the proposed lease a clause that allows the Board to essentially charge whatever rent it chooses. Such a clause is unconscionable on its face and if the Board insists on its presence, it should at least be offset by an additional covenant limiting the amount by which rent could escalate.

B. Premium Rent

Premium Rent is a creation by this Board in order for the State to procure some modicum of compensation if a lessee is being charged less than market rent. Essentially, Premium Rent simply makes up for any instances in which a lessee is paying less than market rent. Accordingly, Premium Rent is best understood as the value difference between market rent and actual contract rent.

The foregoing conception of Premium Rent makes good sense in the above context. After all, if the Board is indeed to charge market rent and market rent alone, rent at sub-market levels would result in a windfall to the lessee and a detriment to the State. Accordingly, it is important to have a mechanism in place to fill the interstice when contract rent drops to below market levels.

The problem with the Board's proposal is that Premium Rent is not used in the above manner. Rather, the Board has converted Premium Rent from serving a compensatory function to solely being a means of profit sharing. On its face, this is not completely objectionable. If the Board is looking to increase revenues, but is willing to compromise, Premium Rent may be the best avenue to effectuate that concession, assuming no change in the rate of rent. However, the Board's proposal is not a compromise, nor a concession. According to the Board's proposal, the Board will both increase the rental rate to above market levels and charge Premium Rent. This is inconsistent with the underlying purpose of Premium Rent. Employed in this manner, Premium Rent is a disguised way to tax those who seek to transfer their leasehold and thereby reap a share of the profit incurred by virtue of the assignment. The burden of Premium Rent on lessees is increased further in light of the fact that the terms of the proposed lease increase the amount owed by one-hundred percent (100%) each year until a Premium Rent of fifty percent (50%) is reached. This is not true Premium Rent; nor is this charging market rent. It is an out and out tax on the transfer of a leasehold estate and is therefore unconstitutional and illegal.

Proponents of Premium Rent argue that it should be included in the terms of the lease because lessees should not be making so much money off of land that the State owns. However, this position neglects the fact that the legislature has commanded the Board to only charge market rent. The way the Board is using Premium Rent exceeds the Board's own mandate. Moreover, regardless of the Board's opinions regarding the Constitutionality of I.C. § 58-310A, the Board has no choice but to faithfully execute the foregoing provision until it receives a judicial opinion to do otherwise. What this means is that it may only charge endowment lessees market rent and market rent alone.

We sincerely urge the Board to take a balanced approach with regard to the foregoing issues and consider adopting the Association's proposal – a proposal which is fair to all sides of this very serious issue.

Respectfully submitted,

DAVISON, COPPLE, COPPLE & COPPLE, LLP

By: _____
Terry C. Copple, of the firm

By: _____
Alexander P. McLaughlin, of the firm

APM/vr

Exhibit 41

Transcript, Land Bd. Cottage Site

Subcommittee Meeting

(March 1, 2010)

Cottage Site Subcommittee

March 1, 2010 – 3:00 p.m.-5:00 p.m.

Department of Lands – Director's Office, Boise

TOPIC: Cottage Site Premium Rent

SPEAKERS:

- Ben Ysursa, Secretary of State, Chairman, Cottage Site Subcommittee
- Tom Luna, Superintendent of Public Instruction, Cottage Site Subcommittee Member
- Bonnie Butler, Office of the Governor
- Sherm Furey, Office of the Attorney General
- Dan Goicoechea, Office of the State Controller
- George Bacon, Director, Department of Lands
- Robert Follett, Deputy Attorney General, IDL
- Mike Murphy, Chief, Bureau of Surface and Mineral Resources, Department of Lands
- Laurie Boeckel, Idaho Parent-Teacher Association (PTA)
- Payette Lake Cabin Owners' Association
    - Jim Young, President, Payette Lake Cabin Owners' Association, Lessee
    - Terry Copple, Legal Counsel, Payette Lake Cabin Owners' Association
    - Robert Williams, Appraiser
    - Patrick Miller, Payette Lake Cabin Owners' Association, Lessee
    - Mike Fery, Payette Lake Cabin Owners' Association, Lessee
    - Chuck Hervey, Payette Lake Cabin Owners' Association, Lessee
- Priest Lake State Lessees' Association
    - Bud Belles, President, Priest Lake State Lessees' Association, Lessee
    - Charles Lempesis, Legal Counsel, Priest Lake State Lessees' Association
    - Dennis Dahl, Priest Lake State Lessees' Association, Lessee
    - Denny Christenson, Priest Lake State Lessees' Association, Lessee

Secretary of State Ysursa opened the Cottage Site Subcommittee meeting at 2:59 p.m.

Secretary of State Ysursa: Superintendent Luna is testifying today in front of the House Education Committee. He will be here, he hopes, shortly depending on how that goes. I, of course, am Ben Ysursa, Secretary of State, and the Chairman of the Cottage Site Subcommittee. We – I think everybody knows what happened in the last Board meeting. We agreed on a couple of items from the Subcommittee, and there were some other items that wanted to be discussed. And my goal today is to limit the discussion and talk about premium rent. There has been a record completely replete with information about the rate, and it's my hope today to primarily focus, if not exclusively focus, on premium rent.

So with – if some way down the line it becomes an issue that we need to throw a little bit of rate discussion in there, I'm sure it will come up, but that is not my goal here. And my goal is to get out of here in a reasonable amount of time, whatever reasonable means. But we know all about the issues. I certainly do. Enough said. I've read every minute of the Board of Examiners' – Board of Land Commissioners' meetings and others.

And just a brief history on premium rent, for those of you who don't know, it was invented, so to speak, by the Land Board in 1981 in recognition that the rate being charged certainly appeared to be awful low because people were paying quite a premium to take over our State leases. And that little handout, that's from a Mr. Duffield. It was quoted from Knipe, and if you – if you don't know who Mr. Duffield is, then you probably shouldn't be in this room. But that's the study, and the individual who did the study, in the court case in Montana that was relied on. And he talked a lot about leasehold value, what we ought to be getting, a formula to get to it in reverse, on how much leasehold value was there, what the leasehold value ratio was compared to the assessed value, and – and if people were getting a fifty percent premium, then we ought to be doubling our rate.

So it's a – that's the study that was done in the State of Montana. And it is part of their record. It's also on their web site. The Montana web site, if you ever looked at it is a very good web site. They happen to have the same issue in front of them, remarkably. And they have some good information on the – on the Duffield study.

So my intent today is to, like I indicated, to limit the discussion to a degree on premium rent and what we call that. The current situation is the Board has a policy since 1981 of charging ten percent. We call it premium rent. You can call it leasehold value. The State gets quote, unquote, ten percent of the leasehold value, and the lessee gets ninety percent of it.

There's a Subcommittee recommendation that that percentage remain at ten for 2011 and then go up ten percent a year until 2050 – until 2015 at which it hits fifty percent. And that is on the gross leasehold value. I believe we will have some discussion today on gross versus net, just a wild guess. So I'd like to start with the Payette Lake Association and their statement on what they think premium rent ought to be, or where we ought to go as a Land Board.

March 16th is the Land Board meeting. And it's very clear from the Governor, and myself for that matter, we're not – that's it. Decisions will be made March 16th – the further decision. Mainly rate and premium rent. Those are kind of two sticklers.

The term of the lease has been voted on unanimously. It's ten years. The other – the other items that have been voted on unanimously, is our number one recommendation, is to not have these meetings periodically and get out of the leasing business. Dispose, exchange, unify ownership, whatever. Key phrase used there is market savvy manner. Though I work for the State, I'm not really thinking it's a real hot real estate market to be selling in right now. Somebody told me that.

Anyway, that's where we are. We don't need to rehash where we've been, but – so my intention is to have the Payette Lake Association make a presentation if they wish, and I'm sure they do. Then to have Priest Lake. And if there's a difference – Payette Lake, when I say that, we have Payette Lake folks that have lakefront lots; we have Payette Lake folks who have second tier lots. So I think it's A and B there. And sometimes they're not on the same page. So anyway, we'll hear that.

And then the Priest Lake folks make a presentation, and then if there's anyone here from the education community that wishes to make a presentation, that would certainly be welcome. But –

Pardon me?

Mr. Lempesis: I could do that if you need me to, Mr. Chairman.

Secretary of State Ysursa: Or Mr. Lempesis can do all these presentations at a modest rate, I'm sure.

So anyway that's where we're headed. Without further ado, and please sign up, and this all is being recorded as well as there will be a transcript, as there was in the last meeting. And there's a voluminous record being created for anyone who wants to know, and we will proceed right now.

And, Mr. Young, you're head of the Payette Lake folks. Turn it over to you.

Mr. Young: Thank you, Mr. Secretary. Actually I'm going to introduce Terry Copple, who's an attorney that we've engaged, and I'm going to ask Mr. Copple to speak on our behalf on this subject.

Secretary of State Ysursa: Mr. Copple.

113

114 **Mr. Copple:** Yes, thank you very much.

115

116 **Secretary of State Ysursa:** You bet.

117

118 **Mr. Copple:** Basically, the board of directors and the officers of the association have met and carefully
119 reviewed the proposal that's in the current draft of the lease for the premium rent. The way we
120 understand premium rent has continued to operate under your IDAPA rules is that if there's
121 below market rent, then the State is entitled to collect a premium rent, or a profit if you will, at
122 the time that the property is sold. So the critical determination of lease value is whether there
123 is a market rent. Obviously you have already made a determination that you want to move the
124 rent up because the Board feels that, in fact, the rent is below market. We respectfully
125 disagree. That's something probably we're never going to agree upon so –

126

127 **Secretary of State Ysursa:** I agree with that.

128

129 **Mr. Copple:** – so therefore we don't think that premium rent is really due because we think that we're
130 paying what market rent is. But it's obvious that the determination has been made that there is
131 going to be premium rent. And so how do we go about making sure that it's – it's absolutely
132 fair.

133

134 First of all, if you use the definition again from the Board's IDAPA rules about the fact that you
135 are now charging below market rent, then you are entitled to collect some when the property
136 sells. Then if you're going to be increasing rent, phasing it in to a market rate, then the premium
137 rent should phase out as the rent goes up because it would be inconsistent to go to what you
138 feel is a full market rent and, at the same time, leave the premium rent in place. In essence
139 you'd be converting the premium rent, in essence a transfer tax, which of course there is no
140 authority in the law for that. So there has – they have to be tied together. You can't increase

the rent and at the same time keep your premium rent. That would be the first concept that we think really needs to be looked at very carefully.

The second concept is – is that the calculation of the fifty percent on the gross and whether that's fair or not. It's been our position, and will continue to be, that if you're going to collect premium rent, if you're going to take profit out of the rental relationship for the State, then it must be based upon the net profit that the lessee has. To charge a (inaudible) on profit that doesn't exist would be, in our opinion, confiscatory and very unfair. So we're urging you to study very carefully adopting a ten percent premium rent based upon the net profit that the tenant or the lessee would realize from a sale. And it could be very simple. It doesn't have to be complex. Obviously the tenant, the lessee, knows what their cost is in acquiring the property, that is the land. We know what the sale is going to be when there's a contract of sale. The Department's forum for transfers, and that sort of thing, and the IDAPA rule very carefully has representations under oath from the tenant, and that sort of thing, about the sales price. So we believe if you're going to be charging premium rent that it should be on the net purchase price because that's the profit that's being realized. And if the State wants to share in that profit, then that's where it should be calculated at. We can't think of any other arrangement that would be more fair than that. But on the gross, we feel is – is simply not appropriate.

Secretary of State Ysursa: One question. What's the percentage you think ought to be on this shared appreciation?

Mr. Copple: The ten percent.

Secretary of State Ysursa: Ten percent of the net profit.

Mr. Copple: That's right.

169 **Secretary of State Ysursa:** And what would you attribute that profit to? The appreciation in the land
170 value?
171
172 **Mr. Copple:** Well, it would, under the way that you have the formula.
173
174 **Secretary of State Ysursa:** And – and whose land is it?
175
176 **Mr. Copple:** It belongs to the State –
177
178 **Secretary of State Ysursa:** So the appreciation of our property, you ought to get ninety percent of it?
179
180 **Mr. Copple:** Well, because we have a long-term renewable lease, we feel that we have, as a tenant, that
181 we do have a long-term property interest in that property.
182
183 **Secretary of State Ysursa:** What's the long-term interest of our endowment beneficiaries?
184
185 **Mr. Copple:** Well, that's an interest, too. I mean this is –
186
187 **Secretary of State Ysursa:** Yes, it is.
188
189 **Mr. Copple:** – this is – I agree with you that it is a competing balance of what is right for the beneficiary
190 and for the property owners who have invested the time and effort into this.
191
192 **Secretary of State Ysursa:** Just a gut reaction would seem to be that we ought to start at fifty percent
193 and go up. If the vast majority of that appreciation in the value is because of the land value, yes,
194 a nice improvement does help the land, no question about that. But I don't think it – well, that's
195 my own personal opinion. And I don't want to stop you or interject too much here, but I think
196 there's some statements that just have to be countered a little bit that if the vast majority of the

197 profit quote, unquote, is attributed to location, location, location, land value, land value, land
198 value, then endowment beneficiaries ought to be getting the lion's share of that because that's
199 who owns the land.
200
201 **Mr. Copple:** But I would point out that, in response to that, two things. Number one, of course, all of
202 the improvements, the roads, the wells, the septic systems, the fact that you have a community
203 environment, the docks – all of that is created by the tenants. And that was the way it was
204 originally intended. It was designed to encourage people in times that, of course, were not as
205 economically as affluent as we have been in the last fifty years, but to encourage people to
206 create that value out there on property that otherwise was fairly unused – totally unused.
207 Secondly, lease – the concept of lease value is a function not of the value of the land. The way
208 the Department has historically attributed it, it is based on the value of the land. In reality, the
209 leasehold value is that difference between the market rent and the contract rate. That is the
210 value. That could be no value. It could be a huge value. And that is what is, in essence, being –
211 that is the premium rent. The property could go up and down in value. Theoretically, land could
212 go up and down, but the spread, if you will, could not change and still have value.
213
214 So there is a substantial disagreement between us and historically how it has been defined.
215 Because if you say it's just purely based on land value, that in our opinion is not the proper
216 appraisal way to look at the value of a leasehold interest – that is that lease value. It's really the
217 spread. And I think the Department, in other purposes, kind of recognizes that. So I don't think
218 that it is an all win one way or the other. I think that we can find a balance where the State can
219 share in that profit, if you will, but at the same – same time allow the owner to share in that
220 profit as well when really the State has done nothing to create the value other than simply own
221 the fee title.
222
223 **Secretary of State Ysursa:** That's what happens when you have valuable property on a lakefront.
224

225 **Mr. Copple:** That's right.

226

227 **Secretary of State Ysursa:** You simply own it, and it goes up in value then – and that's it.

228

229 **Mr. Copple:** But it's valuable in that historically –

230

231 **Secretary of State Ysursa:** One question. The difference – I couldn't agree with you more, Terry, or
232 Mr. Copple, on the capturing the gap between market rent and contract rent. Now your
233 position is right now there's no gap. You're saying market rent. You say contract rent is – or
234 market rent is below contract rent or whatever you're saying at this point in time. Well, that's
235 part of the disagreement. But if you're capturing the difference here, and that's what – that's
236 what the people have done. The people that have paid these, you know, and I always have
237 Payette in front of me in knowing some of the values, the eight hundred thousands and the nine
238 hundred thousands or the seven hundred thousands. I can – I know why they're upset. They
239 are, frankly, about some of the few people that have paid market rent. They captured the
240 difference between the low contract rent and where market rent should have been. And if I was
241 one of the few people that only paid the market rent, I'd be howling like a Banshee too. And
242 therefore we get the noise. And – but – over the years – and now – now it may have – you
243 know, I – I thought it was done. And then we had some interesting transactions at the end of
244 the last calendar year that for a dead – dead market seemed to be rather high. Again, I talked
245 about it at the Land Board meeting. I think we're trying to talk about rational markets with
246 irrational individuals at times in the way they handle their transactions there. But again, this will
247 go on forever if I make my commentary. So go ahead.

248

249 **Mr. Copple:** Well, the – the market in these kind of properties is an irrational market. And I think one of
250 the things that the State struggles with is that these properties, if you appraise them as just bare
251 ground on a lake, what would it rent for for ten years where, in fact, you would have to remove
252 the improvements every ten years. That income generated from that kind of property is not an

253 economically profitable position. That's why you don't see landlords leasing this kind of
254 property in the private market, and that's what everybody's struggling with. They're
255 aesthetically desirable. It's a lifestyle. People are paying for a lifestyle, and that's an emotional
256 decision. In reality, people who develop recreational properties for a living, you know, large ski
257 resorts or places on the islands and things like that, know that the leasing of the property is just
258 a way of paying expenses. In reality, on recreational properties, the payday is the sale. You
259 lease it; the tenant takes care of the place. They improve it. They create value. They create
260 that aesthetic enjoyment. What happens, then, of course, is that the developer eventually sells
261 the condos to single family dwelling sites around the golf course or on the coast of the ocean,
262 and then that's the payday.
263
264 So in reality, in the private business world, the developer looks at the overall cost of rental
265 income that's coming in, and whatever it is, it's great because usually that's just helping him pay
266 expenses and to maintain the property. But then the goal is not to be a long-term landlord. You
267 don't want to own a golf course, for example. Every developer turns them over to a non-profit
268 entity because, guess what, they don't make money. What – where your return as the land
269 owner comes from is from the ultimate sale of this position. Just like you have concluded in
270 your analysis from all the appraisers and the experts and everything, everybody says from an
271 economic standpoint trying to force people to pay these kind of rents for this kind of property is
272 not sustainable because what will happen is the people will make a decision it simply isn't worth
273 it. Especially if the premium rent is so exorbitant that at the end of the day I might as well just
274 dump it and go buy a fee simple interest in a property.
275
276 So from the State's perspective, the direction you're taking is appropriate to go ahead and sell it.
277 And, of course, from the State's perspective, the people that are going to pay the most will be
278 the people in occupation of those premises now because it's worth it to them. But I'm afraid
279 that if you make your premium tax the way it – that you consider it now, fifty percent of the
280 gross, people are not going to do it. I think – I think it's a very unwise decision. But I – and so

that's why I think closing the spread the way you philosophically are doing it, even though we disagree with it, should lower the premium coupled with an ultimate sale of the property where the State gets its payday on the property, and the values that have been created by the owners themselves and by market conditions is where you'll – you'll get your return. If you think recreational users are going to pay these kind of prices, they're not because, you know, you can sit down and talk to them. I've talked to clients – several clients – who have property at Payette Lake, and they have young families and they're basically saying they're at the tipping point. And so when you consider this, I think you need to get a rate of return. It's fair that you get a premium rent, if you think it's below market, but at a certain point it has to stop. So that's our – our position that we'd like to emphasize to you that you – you really need to be careful about this premium rent because that's going to be a killer. The base rent is one thing, but at fifty percent of the gross on a transfer is going to be really confiscatory.

Now we also – we did ask an expert – we do – he is available today – Robert Williams – to do a short analysis. It's only two or three pages – on the premium rent issue. I'd like to give you three copies. He is available. Robert Williams is present – there he is – to give a brief review. He isn't going to sit down and talk about the rental rate, per se, but it does bear upon the premium rent. So we would like to put this into the record –

Secretary of State Ysursa: Sure.

Mr. Copple: – if we may.

Secretary of State Ysursa: You bet.

Mr. Copple: And then I'll turn it over to Robert to give a short discussion.

Mr. Williams: Do you want me to do it from here?

309

310 **Mr. Copple:** Or you could stand up.

311

312 **Mr. Williams:** I'll sit.

313

314 **Mr. Lempesis:** Would you like to sit here? Why don't you sit here while you're doing that, and I'll go
315 against the wall where I used to be at the junior high school proms.

316

317 **Mr. Williams:** I didn't sign that sign-in sheet by the way.

318

319 **Secretary of State Ysursa:** (inaudible) I gave your name – just state your name for the record.

320

321 **Mr. Williams:** Robert Williams.

322

323 **Secretary of State Ysursa:** Robert Williams. Okay.

324

325 The floor is yours, sir.

326

327 **Mr. Williams:** Thank you. Yes, I'm a real estate appraiser. I'm based out of Boise. I talked to Mike Fery
328 about your issues here a little bit, and I wrote him a letter. It's about a page and a half kind of
329 just briefly talking primarily about premium rent, and I can just read that to you. That way you
330 can follow with me.

331

332 **Secretary of State Ysursa:** Sure, whatever you want to do.

333

334 **Mr. Williams:** This was addressed to Mike Fery. He's a representative of the Payette Lake Cabin
335 Owners' Association.

336

337 Dear Mr. Fery:

338

339 Per your request, the following is a brief discussion of two issues related to cottage sites in
340 Idaho. The first item relates to land rental rates and a study conducted by three veteran Idaho
341 certified appraisers. The second item is a discussion of the concept of premium rent. It is
342 understood that the cabin owners' association intends to use this document in their
343 negotiations with the Idaho State Land Board concerning cottage sites.

344

345 With respect to the study and rent rate model developed cooperatively in 2009 by Mr. Stan
346 Moe, MAI, Mr. Ed Morse, MAI, and Mr. Joe Corlett, MAI, the methodology, techniques and type
347 of data used in their analysis are considered appropriate and properly used. This is considered
348 to be a reasonable and market representative method of determining rent rates. This
349 methodology should indicate an estimate of market rent that is equitable and provides for a full
350 market rate of return on the land asset for this type of property class.

351

352 Premium rent is an unusual concept. The appraiser could not locate the term premium rent in
353 the Appraisal of Real Estate or the Dictionary of Real Estate Appraisal published by the Appraisal
354 Institute. The concept was described as a means of making up for a deficit rent, not paid during
355 the lessee's holding period, by charging an additional lump sum rent payment when the
356 property is sold to a new lessee. If the ongoing rent charged is at a market derived rate, i.e.,
357 market rate, then anything additional charged the lessee would be classified as excess rent. For
358 either one of these scenarios to occur at the time of a lease – at a time the lease is being
359 negotiated – often reflects uninformed parties or extraordinary motivation on the part of one of
360 the parties.

361

362 The premium rent described is also based on a potential profit on the sale of the property,
363 which is called a positive leasehold position. The typical method of calculating if a profit or
364 actual gain is made on a real estate transaction is by determining the total basis in the property,

which would be the original purchase price plus capital improvements, and then subtracting from that amount the net cash proceeds of the resale, which is the sale price minus the cost of disposition. This is sometimes referred to as the net reversionary interest.

The premium rent concept contemplates that the contract rent, which the Idaho Department of Lands is charging on a yearly basis, is below or less than market rent. Therefore to calculate how much below market rent the contract rent is, and to determine the total rent that the lessee pays over the holding period, is correct. You would need to know what market rent actually is in order to calculate if there is a deficit rent or premium rent due, be it ten percent, fifty percent or zero percent of the net sales proceeds. When you are trying to maximize the long-term financial return to the institution, or whether you desire market rent to be a controlling factor in order to be fair and equitable to all parties, then you have to determine what market rent is up front at the time of the lease negotiations.

It is concluded that the best way to calculate market rent is by following the methodology which was developed by the three local exports, Mr. Moe, Mr. Morse and Mr. Corlett, and presented to the Idaho State Land Board in 2009. This approach is considered a reasonable and market derived method of calculating market rent and is based on industry accepted techniques. If you apply a market-generated rate and charge market rent on a yearly basis over time, then there would be no need for premium rent. This is considered the most straight forward and contemporary solution to this issue.

Respectfully submitted,

Rob Williams

Secretary of State Ysursa: Mr. Williams, thank you for that. Are you – have you looked at or studied at all or needed to have something to read before you went to bed at night – the report of

393 Mr. Duffield or others about leasehold value, premium rents on cabin sites in Montana? Are
394 you aware of his study?
395
396 **Mr. Williams:** No.
397
398 **Secretary of State Ysursa:** You're not aware of that.
399
400 **Mr. Williams:** No, I'm not.
401
402 **Secretary of State Ysursa:** How about the Knipe study that was done on this? How about the McFadden
403 study?
404
405 **Mr. Williams:** No.
406
407 **Secretary of State Ysursa:** Okay. But you did look at the methodology presented by the three
408 appraisers, obviously.
409
410 **Mr. Williams:** Yes, I did. I didn't – I didn't try to form an opinion as to whether what they came up with
411 was correct as far as the numbers – simply is this a good way to go about this. And that issue of
412 premium rent, and if it makes sense or not, or what it is you're trying to accomplish in relation
413 to what seems to be maximizing your return, but also at, you know, a long-term stable basis at
414 market rent, and how does that affect things or does it account for what the appropriate return
415 should be based on that type of property.
416
417 **Secretary of State Ysursa:** Okay.
418
419 **Mr. Williams:** Typically when you're looking at a – that type of a term, it's like what is – what is the rent
420 over the holding period that your – a large part of your return is also when you sell the asset on

421 the end, which is the reversionary interest. When you combine that, that gives you your total
422 rate of return over that holding period. So you still own the land. At some point you could sell
423 that, and that has to come into the play of the whole formula if you're trying to calculate what
424 your interest rate or internal rate of return or what you're actually making on that asset over
425 your holding period.
426
427 **Secretary of State Ysursa:** I appreciate that. I don't want to digress too much, but if there's any staff
428 members of the Land Board that wish to ask a question, I'd certainly allow that at this time of
429 anything that's been brought up so far. We have people from the Attorney General's office, the
430 Controller's office, everyone but the Superintendent's office, who has nobody here. Any
431 questions for anybody out there to Mr. Williams or to Mr. Copple?
432
433 **Mr. Goicoechea:** No, Sir. No, the questions that you asked were the relevant questions I would have
434 had for the last presenter, Mr. Chairman. Thank you.
435
436 **Secretary of State Ysursa:** You're Basque and I'm Basque. We think the same or don't think the same.
437
438 **Mr. Goicoechea:** I'm no more Basque than Mr. Miller, though.
439
440 **Secretary of State Ysursa:** Does that conclude your presentations right now?
441
442 **Mr. Copple:** Yes, it does.
443
444 **Secretary of State Ysursa:** Okay.
445
446 **Mr. Copple:** And I'd just like to end on one note, though.
447
448 **Secretary of State Ysursa:** Sure.

449

450 **Mr. Copple:** Of course, statutorily what we're supposed to do is charge market rent. Not less; not more.
451 So at the end of the day, your return that you do get has to be calculated in light of all of that.
452 And I think the premium rent, the way it's couched right now, is absolutely unfair.
453

454 **Secretary of State Ysursa:** I appreciate those comments.
455

456 Payette Lake, part two. Anybody from the second tier wish to make any comments or
457 presentation about premium rent at this time?
458

459 **Mr. Miller:** Mr. Secretary, I'll weigh in here if you don't mind.
460

461 **Secretary of State Ysursa:** Okay.
462

463 **Mr. Miller:** I don't know if there's a record being taken but –
464

465 **Secretary of State Ysursa:** State your name. Patrick Miller.
466

467 **Mr. Miller:** Pat Miller. Thank you, Mr. Secretary. Thank you for holding this meeting. I with, some
468 trepidation, will jump in here. I notice that across from me is a person with a PTA tag on, and I
469 presume that's a beneficiary of the endowment. My wife was a teacher in the public schools
470 until last year when she got laid off because of budget cuts, right after we bought a cabin in
471 McCall. So – so I feel like I was contributing to the endowment at the same time that – by no
472 direct return to my family.
473

474 We all like to talk in metaphors sometimes. One – one that I'd like to point out is how cigarette
475 companies were known for handing out cigarettes on the corner to teenagers. And the purpose
476 was to get them hooked on cigarettes with the idea that they had a lifelong customer. The fact

477 that they then could charge that person for life for a package of cigarettes was an economic
478 reality. It didn't make it particularly ethical or appropriate, but they did it. The fact that we all
479 have a sense of duty to the beneficiaries, and the fact that the endowment could now that
480 people have spent lots more money than I have, frankly, on improvements to their property and
481 are somewhat over a barrel, vis a vis the endowment, and the endowment could certainly
482 extract from them a beyond market rent doesn't mean that the foundation has to engage in
483 behavior that a tobacco company would engage in.
484
485 Now I'm not asserting – you know, obviously we speak in hyperboles sometimes and maybe
486 overstate our case for purposes of an example. But here what we have is we have, I think, a
487 situation in which the endowment could have auctioned lots. And if it had auctioned lots with
488 no security for the purpose – for the person who bought it, that person would not have
489 invested. That person would not have been willing to pay much for that lot knowing that it
490 could be subject to turnover to another person in four or five years or even ten years. You're
491 not going to invest substantial assets if you don't have some assurance that you're going to be
492 able to continue to use it. So if auction was not a good solution to earn money for the
493 endowment, because ostensibly it was assumed that would have brought only ten dollars, well,
494 if you can by providing security, by providing stable rent at market rates for the long term, you
495 then incent people to lease for a longer period of time and invest in the property. And in that
496 sense you have perhaps formed a partnership with that lessee, and that partnership is that they
497 will agree to invest in the property and pay market rent. Now at times that may result in value
498 being created in a leasehold interest. But I would assert that the way to deal with that is like a
499 partner would deal with it is split that profit, split that revenue.
500
501 Now we talked – you, Mr. Secretary, mentioned that the concept of premium rent started as a
502 way to assure that market rent was being paid. I think the concept has morphed beyond that
503 and now into a concept of trying to recapture revenue. And I would suggest that rather than try
504 to recapture revenue that went to the person who sold the property – it didn't go to the person

who bought the property, it went to somebody who's not at this table. The people that sold their property for lots of money aren't here. They went somewhere else with their money. So – so I would suggest, and we did this actually in a letter to you a couple of weeks ago, that the way to view it is – is splitting that profit. And so I think what we proposed was that the premium rent be a lesser of – a greater of, excuse me – the greater of ten percent of the actual leasehold value or a higher percentage. We suggested thirty percent, could be fifty percent, of the profit and the profit being if I bought – if I had to pay somebody who's now not at this table premium rent of ten dollars, and I can now sell the property for – paid – or if I paid leasehold value of ten dollars and now the leasehold value is twenty dollars, but that's a ten dollar profit, I shouldn't get all of that profit. Now, I invested in the property, continued to pay rent more than the State would have received by auction. So the State's benefited. The endowments benefited from what it otherwise would have. But some of that money is attributable to the fact that the value of that property has gone up. The value of the property that belongs to the endowment. So I should split that with the State would be my deal.

So just on the premium – the other thing I'd like to talk about premium rent goes to this idea of leasehold value, and I would assert that there is a false assumption that every dime of that leasehold value is solely attributable to the fact that market rent's not being paid. There are other reasons people will pay upfront money to a (inaudible) place when it's held by others other than just the market rent. If I were to buy a house, a lot of people would tell me that even if I have cash to put down, I should borrow the money for thirty years because I can make more money in the stock market on that money. But for the purposes of planning and retirement and being able to stay in the house, I may choose to pay that off in fifteen years. I may choose to put a lot of cash down on that. I'm not motivated by pure economics of the best investment. I'm motivated by a plan, and I may make a decision that to an economist is not the best economic decision, but one that lets me sleep at night. And for that same reason, people may be willing to pay premium rent to get into a property with an expectation of paying less rent in the future because they can plan around that. I, for example, am around fifty years old, would

like to retire when I'm sixty-five. I would like to have the – Yeah, Terry's saying no way, forget that. You're a lawyer (inaudible) works forever.

The reality is – is that I want to be able to plan for that, and I would like to pay fair market rent but have some expectation that it's not going to get beyond my means in time. So I would be willing to pay more up front to have that expectation in the future. That's not to say that when there is the gap between what's the leasehold value – that when there is leasehold value that none of it is attributable to the value of the land. I'm not suggesting that. You know, one of the things we always say in our law firm is that people argue over money and will often (inaudible). I know that would surprise everybody here. And what we always try to encourage people to do is to look at making the pie bigger as opposed to trying to grab a bigger piece of the pie. You know, there's a – the old saying about the monkey with his hand in the jar who won't let go of the fruit, and he can't get his hand out. Well, part of that philosophy, I think, is that if you go back and look at the idea that if it were just pure auctions, the State would not have made near as much money, that by going to a system where there's security and providing people an opportunity to invest, there could be shared value is the way to look at it – to look at it as a partnership. And I think that does morph the concept of premium rent. I'd just (inaudible) there not be premium rent, but I think if that's the proposal then as a customer of the endowment I would come back with a counter proposal and say okay, you're saying there should be premium rent, then my proposal is to say okay let's view it as what we are relatively adding to the table, and I should pay premium rent and I would propose that it be the lesser of ten percent of the leasehold value. So if I buy it for ten dollars, it never goes up. I still have to pay a thousand dollars when I sell it. If I pay ten dollars and it goes up to twenty, then I have to split that profit with the State rather than when I sold it at twenty having to pay the State ten or half of that profit.

The notice that I got for this meeting suggested that there may also be an opportunity to talk about value. I understand that that is now not on the table. I did read, however, the expert

561 witness report of Mr. Anderson and Watson and at an opportune time would like to maybe
562 provide my comments in writing to the (inaudible).
563
564 **Secretary of State Ysursa:** Please do. If you wish, you – as far as a written record, we have received
565 materials from other folks who *(tape change)* – a brief comment, but if you want to do it in
566 writing, I know it's not going to be brief, but it's – the – just one observation. This idea of
567 auctioning. At one time the State was trying to have the best of it. We were leasing for years,
568 ten-year leases. And at the end of each ten-year lease there was a – there's a State code that
569 indicates that you can be conflicted – have an auction. And that was vehemently opposed, and
570 a new provision came in called 58-310a in 1990 pushed by the lessee associations to not have
571 that auction ability to conflict. And that is – that helped maybe exacerbate some of the
572 problems we have here.
573
574 **Mr. Miller:** Well, and I guess I would comment back. It's created a problem, but it also created an ability
575 to earn more revenue for the State because, by creating the expectation of security in the
576 property, people were more willing to invest and paid more for the property. Again, if I were
577 being worried about being dispossessed of my property every year, I would never invest in it.
578 I'm not going to pay much rent for a property that I don't know if I'm going to be able to get my
579 improvements back out of it. But if you give me some expectation of security, then I would pay
580 more. So again, I would suggest that that statute actually helped the endowment because it
581 created the opportunity for security that people would be willing to invest. Again, if this is
582 auctioned for ten years, I'm not going to invest in – I'm not going to invest in it anyway, but let's
583 take the extreme example of somebody who wants to build a million dollar home. They're not
584 going to do that, and they're not going to want to pay rent commensurate with that kind of
585 property if it's all at risk. So if you give them security, they're going to be willing to pay more.
586 And that then gets us in this completely – and, as many – and I actually started to read all this
587 stuff, you know, and I'm back and I've looked at the Duffield –
588

589 **Secretary of State Ysursa:** You're sick.

590

591 **Mr. Miller:** I am sick. My wife tells me that. I'm obsessive. But when I look at that, you know, the
592 report from the University of Idaho, the O'Laughlin report –

593

594 **Secretary of State Ysursa:** Yeah.

595

596 **Mr. Miller:** You know, I thought that – I kind of thought that was pretty well done in the sense that they
597 acknowledge that it does create a very difficult problem with arriving subjectively at a rent rate.
598 But the alternative is not all that – is not all that great either. But I think by doing that, by
599 creating the statute that we did, we created some opportunity for uncertainty and difficulty.
600 We also created opportunity for profit for the endowment. I guess we just – I'd again just go
601 back to the point that just because the endowment can – if it – if it led people to invest, and
602 then under the threat of taking away those – that real – the improvements, the risk of those
603 improvements can leverage people into paying more than what is fair, and they may be able to
604 do that, but I'm not sure that the Prudent Investment Standard requires somebody to be
605 unethical.

606

607 **Secretary of State Ysursa:** You have – both – both counsels here love to point to the statutes a little bit.
608 I kind of like to point article IX, section 8 a little bit too.

609

610 **Mr. Miller:** I've read that, too.

611

612 **Secretary of State Ysursa:** Yeah, I'm sure you have. That talks about maximizing funds for the
613 endowments and – and I think your point's well taken. It may have really created an incentive
614 and had some values in there. Unfortunately, the people not at this table are the ones that
615 captured those values and, you know, even the six-year figures that we see, the 203, 209 and
616 whatever, the twenty-five million dollars in leasehold value and the fact the State got two

617 million and the previous lessees got twenty-three. That has led to some of this. Obviously led
618 to an Attorney General's opinion about 58-310a. And so anyway that's just rehashing. I
619 appreciate your comments and –
620
621 **Mr. Miller:** And I'd be happy to continue the debate, but I'm guessing I'm not going to get much further.
622 So –
623
624 **Secretary of State Ysursa:** Please – no – please submit – feel free, and anyone here, submit written
625 comments, and we'll have quite a record anyway. We already do have quite a record.
626
627 I know there's some second tier people still from Payette here – at least one I know from the
628 last thousand years. Chuck Hervey.
629
630 Do you have any comments or just tired of all this?
631
632 **Mr. Hervey:** Not at this time.
633
634 **Secretary of State Ysursa:** Okay.
635
636 Then we'll entertain the folks from Priest Lake.
637
638 Mr. Lempesis. Mr. Belles is here.
639
640 **Mr. Lempesis:** We wanted to entertain you actually.
641
642 **Mr. Belles:** Thank you, Mr. Secretary. I'm going to do kind of what the Payette folks did and turn it over
643 to our representative, our counsel. But first I – we have a member here from our association

644 that recently purchased a piece of land at Priest Lake, and I'd like to have him go through his
645 thought process in dealing with the premium rent issue. His name is Dennis Dahl.
646
647 **Secretary of State Ysursa:** Mr. Dahl, could you – you have sent us a letter.
648
649 **Mr. Dahl:** I have.
650
651 **Secretary of State Ysursa:** And could you just identify yourself for the record so we can –
652
653 **Mr. Dahl:** My name is Dennis Dahl, and I'm a leaseholder at Priest Lake.
654
655 **Secretary of State Ysursa:** D-a-h-l.
656
657 **Mr. Dahl:** D-a-h-l. Correct. What he's asked me to talk about is our decision process when we bought
658 our place. We bought in 2006. That's at or near the top of the bubble. We had some money
659 set aside to either invest and what we decided – invest for profits – we decided to take that
660 money and invest in our family and put it into a property at Priest Lake, enjoy that property, not
661 look to make a return on it – the return would be the enjoy ability that we get out of using such
662 a beautiful place as Priest Lake is. The one issue when we bought – it was concerning – was the
663 ten percent premium rent. I didn't – I understood it and I didn't understand it. But at ten
664 percent, we accepted it as part of the package and purchased our property anyway. The – and if
665 you'll allow me to continue on premium rent for just a minute, the suggestion that you have on
666 the – I'm at an age now where the screen goes blank every now and then so excuse me – the –
667
668 **Secretary of State Ysursa:** Proposal –
669
670 **Mr. Dahl:** – proposal – there's the word – proposal, okay, to move it to fifty percent –
671

Secretary of State Ysursa: Yes, in five years.

Mr. Dahl: – in five years – a person – if we chose to sell our property, the buyer knows it's fifty percent. He's buying on fifty percent. He's going to reduce his offer accordingly because he's not buying at ten. I think the Governor said, you know, if – (inaudible) at ten, and they won't because the purchaser's buying fifty and he'll take that into consideration. But essentially at fifty percent, if property turns over twice, you've basically sold the property and still own it. You still hold title to it and the full value of it and you received all the value off that land. That's the part I have a real hard time getting my head around. I also think that at fifty percent I don't think you'll have any buyers. All my friends who invest thought we were crazy in buying the place anyway because it is leased land. At fifty percent, I don't think there's anybody that could get around it. I think you – I think you – I think you drive the value down in doing that. I think you go right against your fiduciary and statutory requirements of earning the most you can off that land. I think it's (inaudible) reduce values.

Secretary of State Ysursa: Appreciate those comments.

Mr. Dahl: I have some others that I can say unless you want me to just go ahead and be done.

Secretary of State Ysursa: Don't put those words in my mouth. Go ahead and be done, will you.

Mr. Dahl: I'll be done right now then.

Secretary of State Ysursa: Go – go ahead, Mr. Dahl.

Mr. Dahl: One has to do with leasehold value, and I'll be short on it. That was my main – when I came to the prior meeting, that's what I wanted to speak about. Leasehold value, by what it says, leasehold, the value belongs to the leaseholder. That's why it's called leasehold value. That

value goes, as it's been said, up and down. Right now I would say it's down, headed down, as a result of the market. But I don't think the State has any grab on that. I think you want leasehold value. I think you want leasehold value to create demand in that property, which bleeds over on other properties. It increases more spending in the areas. I think it's a good thing. Without it, I think you lose – you can lose the people that would invest in the properties that you have. Our hope when we bought was that we'd simply get that money back at some point. We weren't in it to make a dollar. If we can enjoy this property for probably five, maybe ten years, but our decision would be five years, if we can get that back, then our investment was lifestyle, enjoyment for our kids, memories for our family and simply forego the whatever two percent I guess you get today or one and a half.

A point now on selling, you've – you've – and I know I'm not supposed to go here, but I'm going here anyway until you tell me to shut up –

Secretary of State Ysursa: I run a tight ship, don't I?

Mr. Dahl: – you – in the last meeting you voted to move toward selling lease lands. And I have tried to get my head around that issue, and I just can't do it. I don't know enough about Payette. To me, they're two entirely different markets. They act differently. They're used differently. The values are different. So the decisions you make as a Board are going to be good for one and not so good for the other and back and forth. But it seems to me, and I think this was brought out in the meeting, that if you're going to have to change your Constitution to be able to get around the auction issue –

Secretary of State Ysursa: Public auction.

Mr. Dahl: – which I think you mentioned that, what I would encourage you to do would be to further change that Constitution and separate these two pieces of land. Payette, from what I've just

728 looked on the internet and got some information, you've got a city of around seven thousand
729 people there, and I don't know if that's – that might be old numbers. It might be more than that
730 or less than that now. You've got infrastructure. You have jobs. You have services. You've got
731 year-round living. At Priest Lake, we have Coolin, and that's a population 226. The – see
732 (inaudible) now I can't remember his name – Leonard Paul Store. If you want to go get groceries
733 that's a thirty-five, forty minute trip, unless you want to buy it at the local places and pay the
734 price for it, which people do. There isn't anything there. If you go up to Priest Lake right now –
735 this – this might be a little different. You might find a couple people there, but in a normal
736 winter, you're not going to find anybody there in the wintertime. It's a very short season. And
737 so people aren't going to invest a lot of money to spend a few short weeks at Priest Lake. Just
738 not going to do it. That's why your sale of those two lots failed. At five percent, simply the
739 value was too much. They're not willing to pay twenty-two thousand five hundred dollars to
740 camp at Priest Lake for a couple of weeks. It's just not going to happen.
741
742 I think I'll stop there.
743
744 **Secretary of State Ysursa:** Okay. Thank you, Mr. Dahl. Appreciate your comments. As you remember
745 from the Board meeting, and since I was the one that made the motion, one, we said market
746 savvy manner on the sale or disposition; two, there was talk about the differences between the
747 two lakes and the disjointed ownership, so be it, in McCall where – Payette Lake – where there's
748 been – there's three or four private lots, public – state lots, other disjointed ownership. We
749 have had exchanges and sales there already. I think that's more the primary area, but the whole
750 endowment issue on the leases. Priest Lake, different scenario as far as one side of the lake is
751 owned by the federal government, the other side by the state government. Not a lot of private
752 lots out there. It's been said to some folks we – if we would have put those two lots up for sale,
753 not for lease, then we would have made a killing. Who knows. We hear a lot of things on why
754 that did or didn't go. But we recognize – certainly the Department does – we have some timber
755 around Priest Lake there that we're also interested in in what we do. So we know the

differences between the lakes unique characteristics and – but they're endowment land, endowment land, endowment land. They're different endowments, but the same charge is there, article IX, section 8. We wouldn't suggest to treat endowments differently in a constitutional requirement. But we – when I mentioned the constitutional requirement, it was, and it's being discussed, an item that gives the Board a little more – hopefully a lot more – flexibility in how we would dispose and exchange, additional flexibility and being transparent also. That's the main thing. Not that we're – want to get rid of the public auction requirement, but keep that in there and add some other opportunities that would maximize the return to the endowment. And just put another arrow in the quiver that we would have the ability to do that, and now we believe we're a little hamstrung by it. So that's – that's where we're headed on that. We hope.

Mr. Dahl: Can I make one more comment?

Secretary of State Ysursa: Yes, sir.

Mr. Dahl: I made this in my letter. I made it very strong that – and to the endowment steady and predicable cash flow. If you ask any business person the value of that, they're going to tell you that is what business is about. The increased value of your lands doesn't help – doesn't pay for schools in the State. The steady consistent cash flow, and especially right now, that's what's paying for it. The value has nothing to do with it. You won't know how you've done until you – according to Mr. Anderson, you won't know how you've done until you sell the land and then further to that, you're looking at getting out of the leasing business because it's fraught with headache. Well, my experience with investing is when you go from one that you know something about to another one that you may not know so much about, or know as much about, the headaches don't get any less. You have a lot of history with leasing lands. You know more about – this Land Board probably knows more about it than most any land board in the state – in the United States. It may be a headache, but your charge is to manage that and

personally I think it's – I think you've done a good job of it. I think – I think you get a good return off those lands.

Secretary of State Ysursa: Appreciate that.

Bud, where are we at?

Mr. Belles: Mr. Lempesis.

Secretary of State Ysursa: Yeah, you paid him. Don't let him charge you for being quiet.

Mr. Lempesis: I make a buck where I can.

Mr. Secretary of State, distinguished members of the committee and good friends and staff, first of all, I want to thank you as I always do, and I say it sincerely. It's one of my few sincere moments in life. Thank you for having this meeting. I don't think sometimes even you may recognize how valuable these are for us or for the people of Idaho, and it always just inspires me a little bit that this is how we do business in Idaho. That we sit down. The State could easily have come to a meeting two years ago and say here's what we're going to do. We're going to take you to five percent. We're going to jack it up (inaudible) in premium rent. If you don't like it, sue us. That is what we call the California model. You don't. And I think it also bodes well for this.

While you may be loath the criticism from some quarters about how you've given away the store, not getting enough or not getting enough or didn't get enough or whatever it is, I don't think there's a better definition of doing your fiduciary duty than for a lessor to negotiate at arm's length in protracted litigation – in protracted negotiations as we have.

Secretary of State Ysursa: Did you have a slip of the tongue there?

Mr. Lempesis: I'm just used to saying protracted litigation. But hell, that's just a preview of coming attractions, Ben.

Mr. Belles: That's how you negotiate.

Mr. Lempesis: Yeah, that's how we negotiate. It's a Freudian approach. That's what we call the Lempesis model.

In all candor, though, we – I don't think there is a better proof in the pudding than to sit down lessor and lessee and have these sorts of protracted negotiations that we've had and come up with an arm's length decision. Now, having said that, I'm not going to be a strong advocate today, but I'm going to share with you some thoughts that I have had because I made a pledge to Governor Otter on the way out the door the other day, and I've told you and this group from day one that I would try and help rather than just see if we can wind up in a lawsuit or fight. So let me share with you some stream of conscious random thoughts that I have had since the time of our last meeting in February and today to see if you can put them, or distill them, into something that might have value in your decision making because when all is said, Mr. Secretary, it's your decision that counts and it's not going to be what I think, okay.

At first blush, there is no question that this appears to be a debate between two parties, one of which has a fiduciary charge under the Idaho State Constitution to get the maximum return, okay, period. Nobody questions that. And one from natural quarters in the private sector who have a – they don't need a constitutional charge, it's kind of human nature to pay as little as we can. That's what it appears on its surface. And I think to some degree that's true. Though when I analyze the situation, I think we have much more in common than we do apart because we have two common interests that do not evaporate ever. One is it is beneficial for both of us to

840 have stable market rents and provide stability in the marketplace. Without it your property is
841 diminished and so is ours. If we destroy that marketplace in terms of what our leasehold is
842 worth, we don't have to have these meetings anymore because there'll be nothing to share.
843 And if we do that, we will devalue the property, which is the second thing we have in common.
844 All of us have a keen interest in maintaining the highest value of that property. We really do.
845
846 With that said, and if those are our goals, and I looked at certain factors, the biggest one for me
847 that has come clear since our last meeting, and maybe this is an epiphany, although I've never
848 had one. I've always wanted one ever since I was a teenager. But if I ever had an epiphany, it
849 would be this. When we talk about return on asset, as Mr. Fery likes to, or return on
850 investment, as I like to, somehow the State made eighty million dollars in the last eight to nine
851 years at Priest Lake. Eighty million, okay. In my business, we call it retained earnings to some
852 degree or increase in equity. Let me tell you why I think that. Now I am not a mathematician. If
853 I was, I would have gone to medical school and made an honest living. But I can add and
854 subtract.
855
856 The average lot at Priest Lake went up two hundred grand over 2002 to 2010. If you look at the
857 valuations in 2002, I think the average lots about a hundred and ninety, two hundred grand.
858 Those lots today are like four hundred and fifty grand. Just follow my thinking here. By my
859 calculation, that's an increase of like two hundred and fifty grand. Okay. Let's just say it's two
860 hundred thousand, okay, on the average lot over eight or nine years and you take that times
861 four hundred lots, that's eighty million bucks.
862
863 So if you're talking about a return on asset or a return on investment, we're not talking about
864 two and a half per cent per year. You've got to plug that eighty million bucks in there over the
865 last eight years and say that's not bad. Give you an example. In 1982 I bought in office building
866 in Post Falls, Idaho, which is the intellectual metropolis of the Pacific Northwest. And I overpaid
867 for it like four hundred and eighty grand because I didn't even know what an appraisal was. I

was a moron. But I kept it, and because I knew that if I held it long enough it'd be worth a lot of money. And so I really scraped, and I lost money every year for like the first ten years. In the private sector we do that. Sometimes we make investments that don't even cash flow, but we see a future to them. And so by about year ten, I was just hoping – you remember the '80s – I mean, you were eleven, but you remember the '80s, they were tough, and I would just, you know, literally pray and stay up all night hoping one of my tenants didn't leave me with their fifty cents a foot rent or something, right. Well, I held on to the building long enough I made like a million four on it, okay. But I lost money every year. I didn't even get two and a half percent return. None of that became really through to me, because I'm dense, until the last meeting for the first time the State said here's the problem. And this is what I hope all of our beneficiaries understand. The problem isn't that we're not charging enough on those leases because if we charge much more, honest to God, whether it's premium rent or other, we're going to tear that market down. I'm not lying to you. I'm not exaggerating. You know it. There is a point where we will devalue properties and create such instability in the market nothing will be worth nothing.

Our problem is the money's in the wrong place. It's a great idea to hold all these lots and keep that crown jewel of Idaho, but if the goal is to have a return on investment, the money would be better placed elsewhere, and that's what you decided last meeting. Once you decided that, you know what came into play? The fact that you made eighty million dollars. Before when we've always had these discussions, all we ever looked at on the return on asset was we get two and a half percent and ten percent of premium rent. That ain't enough. Well, I don't disagree. But now plug that eighty million in over ten and ask yourself what kind of return on asset that was. I don't know that anybody in the last ten years in America did any better than the State Land Board of Idaho, okay. That's one thing I think we need to think about, and to me that was an epiphany, and I'm sure it wasn't to any of you but okay.

895 Here's two other things that I want to plug into this discussion. If you go – first of all, we told
896 you at the last meeting we didn't lie to you. We just like to vacillate and be indecisive. We told
897 you that a fifty percent net or something like that would be okay. Forget the number. We're off
898 of this net – of the split of the net. Net works if you bought your property last year or two years
899 ago. But for our members, a very large majority of them have owned them since God was
900 young. Really. And so their values, if you will, where they paid zip and now it's worth 400k just
901 get raped in that analysis, okay.
902
903 It may sound good to that deal, but it doesn't. If you're going to do net we'd like to have ten
904 percent, too, but I will be equally candid. If you want to preserve the stability in the
905 marketplace, and we're going to already create a perception, if nothing else, and a reality that
906 rates – rents are going up and it's now four percent, I would leave the premium rent right where
907 it is. Just don't mess with it. It isn't broken, and you're going to sell those lots and let me tell
908 you, don't wish for something you don't want because when the State goes to sell those lots
909 and the money goes to the children of this state for education, you don't want to devalue them.
910 But I'm telling you, the one-two punch of going to four percent and then fifty percent premium
911 rent, Dennis is absolutely right. We know it's just not going to work. So you can take my word
912 or everybody else's word at that or not but that's a fact.
913
914 The last thing is, when you're talking about the premium rent, here's what the State – see, we're
915 dealing with the State when in the private sector it would be easier, but when you're talking
916 about the State, let's assume somebody made two hundred thousand dollars over the last ten
917 years on their lot, like I was talking – or on their leasehold, and somebody's willing to pay them
918 four hundred and fifty for it. What becomes problematic is that's – if you were to charge fifty
919 percent of that, that's not all they're going to pay. They still have to pay federal capital gains tax
920 on that – at a minimum, unless they treat it as straight income for short term, but they've got to
921 pay federal capital gains tax and Idaho income tax because we're lucky enough to have a state
922 that has an income tax, and the last time I checked I was paying eight percent. So you've got

923 twenty-three percent with fifty percent. We want to be sharing, but at some point there's
924 absolutely –
925
926 Mr. Superintendent –
927
928 *(Superintendent Luna arrived at 4:05 p.m.)*
929
930 Let me start over because I've been talking here. This was good. Oh, he's got it. Listen to what I
931 – I really was on a roll here, Mr. Luna.
932
933 **Secretary of State Ysursa:** He was. He was.
934
935 **Mr. Lempesis:** But that's all – it comes out like seventy percent. I mean, the – actually the lessee's
936 walking away with less than thirty percent when you take the taxes and the State has taken fifty.
937 Again, I'm not a mathematician, but I implore you to look at this on several fronts. One is the
938 stability in the marketplace. You cannot neglect the fact the State of Idaho has made eighty
939 million dollars at Priest Lake. Is it eight million or eighty?
940
941 **Director Bacon:** I don't think there's any way we made eighty.
942
943 **Mr. Lempesis:** You did – you did.
944
945 **Director Bacon:** (inaudible)
946
947 **Mr. Lempesis:** If you have two hundred thousand a lot, and there's four hundred lots, how much is it?
948
949 **Director Bacon:** Are you talking about rent?
950

Mr. Lempesis: I'm talking about anything.

Secretary of State Ysursa: No, no, no. The value; the value.

Mr. Lempesis: Equity. Because in the private sector where most of us –

Secretary of State Ysursa: If we capture it.

Mr. Lempesis: Correct. But you can't – but when we start talking about market rents and values, that is a private sector concept. The State's in the business now. And in business, your return is based not only on what you're receiving year by year, but on the equity you're building. And if lots appreciated almost a hundred and fifty percent, that's eighty million dollars in increased equity. And I'm saying any fair minded person has to say we didn't just get two and a half percent because we had that cash flow, because we could hold those lots, because we could maintain them, because we could pay the folks at the Department of Lands to manage them as capably as they do, okay. We now have increased our base by eighty million bucks. That's part of the take.

With that, I will say what I said to start with. I really did come here wanting to help. I think we're close to getting it done. I would not raise that premium tax one nickel, especially if you're thinking of selling these puppies. And I don't know that net, as much as I admit was the first one to ever mentor that mess, is the best way to do it. So don't do what I did. Don't wish for something you don't want. Don't wish for all these increases if you want to preserve lot value and stability. Thank you very much. I stand for questions.

Secretary of State Ysursa: Anyone – again, it's open – what was stated by the Priest Lake Association folks, from other Board members, staffs or whatever.

978 I want to welcome Superintendent Luna. He had a bed of hot coals to lay on. He'd rather do it
979 than listen to cottage sites. No, I believe he had to testify about education to the Legislature so I
980 think he'd rather be here – wouldn't you? Or would you?
981
982 **Superintendent Luna:** I'm not exactly sure. I'll know in a few more minutes.
983
984 **Mr. Lempesis:** Read it in the Statesman in the morning. It's less painful over coffee.
985
986 **Secretary of State Ysursa:** The –
987
988 **Superintendent Luna:** It might be an accuracy issue, but I'll (inaudible) –
989
990 **Secretary of State Ysursa:** Any other – now we're – Denny?
991
992 **Mr. Christenson:** Yes. Yes, sir. Thank you for having us. We appreciate that. I just want to make a
993 couple of comments.
994
995 **Secretary of State Ysursa:** Say your name for the record.
996
997 **Mr. Christenson:** My name is Denny Christenson. I'm a – on the board of Priest Lake lessees'
998 association. I just want to make a couple of comments relative to premium rent, and they may
999 seem repetitive. But in answer to your question about, Secretary Ysursa, about the Duffield and
1000 Knipe studies and the Cook and O'Laughlin studies, the Duffield study did list the paragraph that
1001 you put out here, but it did not address – Montana does not have premium rent. They did not
1002 address premium rent as being applied in Montana. Knipe and Knipe also did not address, that I
1003 could find in the report, premium rent. Cook and O'Laughlin did in reference to premium rent
1004 to Priest Lake, but none of the other lakes did. And it's not that they may not have been aware
1005 of it, but maybe they considered it and discarded it as a slippery slope. Because when premium

1006 rent is increased, if I were to sell my lot, my lot's valued at let's say three hundred thousand
1007 dollars, the dirt, the leasehold value. If I was to sell my lot at fifty percent premium rent right
1008 now, a person – let's say I sold it to you, Mr. Secretary, the minute you sign that paper that you
1009 would agree to that transfer, the value of that – of your dirt just depreciated a hundred and fifty
1010 thousand dollars. So would that make a good deal – business deal to you? Would that be
1011 something you would be willing to invest in? I think most people would look at that and say I
1012 don't want any part of that deal. It's already – the existing lease is fraught with enough
1013 problems for a lot of people – a lot of people right now don't – they get – they got into their
1014 leases because they were – they made an emotional decision. They don't know what premium
1015 rent is. They don't know the definition of leasehold value. Now that rents have – the value of
1016 the lands has escalated so much in the recent decade, they're quickly learning what those terms
1017 mean and how it affects their pocketbook. I don't think an educated buyer would buy a lot. I
1018 don't think you could sell. I don't think I could sell my lot at fifty percent premium rent. So
1019 what's that do to the values of the lots? You're going to get a hundred percent premium rent.
1020 It's going to be a hundred percent of zero because there won't be any value left. And so then
1021 that affects your endowment claim. A hundred percent of nothing is nothing. Fifty percent of
1022 nothing is nothing. So I don't think premium rent is – raising premium rent is the answer. The
1023 answer is to provide a lease to lessees that they can boast about. That they can go ahead and
1024 tell their neighbor or tell their friend, hey, I got a deal for you up at Priest Lake. That's the way it
1025 used to be up there. I think when we screw around with the lease, we – it's like the ecosystem.
1026 We're messing something up. We're trying to fix something and we end up messing it up.
1027
1028 Five years – ten years ago you could – there weren't any signs – there weren't any properties for
1029 sale at Priest Lake. You'd never see one come up because – I had like four or five guys that
1030 would be saying, hey, if you ever hear of a deal at Priest Lake, I'd like to hear about it. And so
1031 they would buy those lots, and they would pay their premium rent. And they would pay their
1032 rent – their leasehold rent and the market escalated. The market went up. The market didn't
1033 go up because the property got any more sexy. The market went up because the value that

these people could – these people could afford to take it over and were willing to pay the rent. When you pay – when you charge additional rent and additional premium rent, the market just is going to get trashed and – at least it will up at Priest Lake because people just won't do it. You can only – and there aren't – and we used to say okay, well, there's going to be somebody come along that's smart – excuse me, not smart, but rich and stupid, that will buy a lot – buy a lease and sign one of these leases. Those people don't exist anymore. They've gotten smart. They've gotten wiped out – those people like that. So the fat cats with a lot of money that were willing to sign a stupid lease, they've learned their lesson and that's not going to happen. And that's – that's all I had to say.

Just – just one thing that we learned recently about lake property in our neck of the woods. Coeur d'Alene Lake – one of our board members, Mike Schmitz, went to an inventory – went to a – *(tape change)* seminar. He's been a lake guy for twenty years at Priest. The speaker at Coeur d'Alene said there is a fourteen-year supply of inventory lakeholds currently on the market at Lake Coeur d'Alene, and that the sales prices averaged ten percent less than the asking prices. The asking prices are down thirty percent from two years ago. The number of sold lake properties have declined forty percent. Forty-seven percent in the last two years. So there's no doubt that everybody knows that the market's tanking. And we're – we're maybe falsely assuming that maybe lakefront properties weren't tanking. People were going to be more – hang on to them a little bit harder. It's not happening. And some of the fat cats want out. They can't afford them anymore. So the market's already sliding down hill. I can't understand how the Land Board could consider making the – raising the rent – raising the premium rent and causing that depreciation of their land values to increase – decrease even more.

Secretary of State Ysursa: Appreciate your comments. And one – just one observation. The reason I – you asked about Duffield or Knipe or McFadden or the O'Laughlin and others report, you won't see – yeah, you'll see a little bit about Idaho's premium rent, but they won't have premium rent.

1062 What's Montana? They don't have premium rent. What those studies pointed out was the gap
1063 between contract rent and market rent. And their goal in Montana and these other state –
1064 Idaho, again – is what should market rent be? That's what those studies did. And they –
1065 everything that came out said we're not at market rent and that's why we quote, unquote,
1066 invented premium rent. And if we want to go, I mean, I don't even know if that's the proper
1067 phrase. Call it a Hobson's choice. If folks in here want to get rid of premium rent, there was a
1068 suggestion made at the last Land Board meeting. Do you want to go to six percent of current
1069 value and have your rates raised two hundred and fifty-four percent in one year?
1070
1071 **Mr. Christenson:** Well, my response to that, Mr. Secretary, would be whatever happens –
1072
1073 **Secretary of State Ysursa:** My comment was that's unconscionable, but the idea to get to market rent is
1074 our goal.
1075
1076 **Mr. Christenson:** Right. I understand.
1077
1078 **Secretary of State Ysursa:** In a fair manner, in my opinion.
1079
1080 **Mr. Christenson:** Believe me, I can speak for the rest of the lessees at Priest Lake. We don't want to
1081 deny the Idaho endowment fund one penny. We don't want to do that. That's not our purpose.
1082 What I'm saying is you got yourself in a fix here. The State of Idaho has their self in a fix.
1083 They're never going to be able to, in my opinion, achieve the return on their investment, from
1084 rents alone, that they want. They can only achieve a return on their investment by selling the
1085 land, and now they've probably realized that. So anything you do now, regardless of what's
1086 happened before – whether we're paying market rent or not, whether we're paying enough
1087 premium rent or not, it doesn't make any difference. It's going to be whatever a buyer will buy.
1088 If a guy doesn't – if you don't buy it, it doesn't make any difference what the rate is. So you –
1089 you've got yourself in a fix. And I think you're accepting it reluctantly, but I think by messing

1090 with the existing lease, or going beyond four percent and going beyond ten percent premium
1091 rent, you're really going to screw up the market. And it's just – and you're going to find out that
1092 you created a lot of unintended consequences. And we just want to make you aware that these
1093 are the consequences.
1094
1095 **Secretary of State Ysursa:** Thank you for that. Do we have the – some representatives from the
1096 education folks ready to make a presentation or a few comments, be it the PTA or whatever.
1097
1098 What – could you identify yourself?
1099
1100 **Ms. Boeckel:** Thank you. My name is Laurie Boeckel.
1101
1102 **Secretary of State Ysursa:** Pardon me?
1103
1104 **Ms. Boeckel:** My name is Laurie Boeckel –
1105
1106 **Secretary of State Ysursa:** Laurie Boeckel, okay.
1107
1108 **Ms. Boeckel:** I'm with the State PTA. I'm on the executive board, and I serve as a volunteer. And I'm
1109 here today to just basically let you know that our position, that the Idaho PTA has adopted for
1110 years, has been that the Idaho PTA encourages Idaho state officials to take all the necessary
1111 steps to manage the school trust lands and school endowment funds in accordance with its trust
1112 duties and principals, including undivided loyalty to the beneficiaries and a duty to make trust
1113 property productive in long term, as well as short term, ways. Idaho PTA, as a member of the
1114 Children's Land Alliance, could not support anything that precludes the beneficiaries from
1115 receiving the full value of the endowment lands. We ask that the Land Board, when they're
1116 making this decision on premium rent or any others, have the undivided loyalty to the
1117 beneficiaries.

1118

1119 **Secretary of State Ysursa:** Appreciate those comments. Anyone else from the education folks that are
1120 here wish to make a comment?
1121
1122 Mr. Young has been raising his hand here in a very calm manner.
1123
1124 **Mr. Lempesis:** He'd like to speak on behalf of education.
1125
1126 **Secretary of State Ysursa:** Mr. Young.
1127
1128 Identify yourself for Susan over there. I'm sure she knows who you are.
1129
1130 **Mr. Young:** Mr. Secretary, Jim Young, President of the Payette Lake Cabin Owners' Association. And I
1131 wanted to set the record straight because at the Land Board – the last Land Board meeting – the
1132 Attorney General grilled me pretty good on what our position is, and I don't think as well on my
1133 feet as Mr. Lempesis or Mr. Copple does so let me just clarify that our position is consistent with
1134 exactly what the young lady said about the beneficiaries. And that is that we want to be in
1135 compliance with the Constitution and S8-310a, which is stable lease at market rent. That is our
1136 position. And, you know, what is that? The only people that can really determine that are
1137 qualified appraisers, other than the market itself. But short of the market would be appraisers
1138 that base their information on science and data. And, you know, what – what we have right
1139 now, and what has been referred to regularly, is the Knipe report, which is a twelve-year old
1140 report, very outdated as to what is current with this market.
1141
1142 The market has changed in twelve years a great deal. And so we really don't have any good data
1143 or science other than the most recent information, which was collected by the three appraisers.
1144 Now whether you agree with it or you disagree with it, you may think that it's invalid because
1145 there's not enough data there. Perhaps that is true and maybe more data is needed to arrive at

1146 a good scientific conclusion. But the results should be based on science rather than an arbitrary,
1147 you know, what we should be getting as a rate of return or this sounds good or this doesn't
1148 sound good. I think our goal, and I think the goal of the beneficiaries would also agree that we
1149 ought to base this on real data – data today as to what is happening out in the marketplace.
1150
1151 So if we can arrive at a true market rent, it would solve this problem of premium rent and take
1152 care – take care of the whole issue. Unfortunately we have this program that was created. This
1153 – this is the State's program. This is not the lessees' program. This is the State's program. Now,
1154 of course, we – you know, we negotiated over the years, but it is the State's program and we
1155 just followed that program. We bought into it over the years. So you have these folks that have
1156 bought into and invested a great deal of money based on the representations of the State and
1157 the program that was established by the State. Now if the State is now saying, well, we were in
1158 error, we should have been collecting this twenty-five million dollar number that's been tossed
1159 around, which I – I disagree with how exactly – the calculation there – but as you pointed out,
1160 Mr. Secretary, those people are no longer at this table. And so to penalize the folks that in –
1161 that invested in that program, the State's program, to penalize those folks is unfair and is really
1162 unconscionable to say that they must pay for the State's errors, if that's what we're saying. So,
1163 again, I think that the equitable – the equitable position, as pointed out by Mr. Miller, is to
1164 adopt more of a profit sharing approach and either or, you know, the ten percent program was
1165 very acceptable for many, many years. But if you're looking at what is equitable, a net formula
1166 really gets down to a true profit sharing number – a profit sharing position.
1167
1168 **Secretary of State Ysursa:** Thank you. Any other comments?
1169
1170 Mr. Lempesis, did you have a comment?
1171

1172 **Mr. Lempesis:** Mr. Secretary, I just wanted to ask you if before we conclude this meeting – I have to
1173 apologize, but I'll have to leave about a quarter of five. I have a 5:45 flight. I think I can – if I
1174 leave at quarter of five I'm good, aren't I? Yeah, this is Boise. Okay.
1175
1176 I wanted to ask if before we left if I could just touch (inaudible) – if we could touch upon three
1177 things. One, what is the plan assuming that the Land Board makes a decision – will make a
1178 decision in March. How do we come to closure on the lease?
1179
1180 **Secretary of State Ysursa:** Lease document itself.
1181
1182 **Mr. Lempesis:** Right, sir.
1183
1184 The second is I was going to request on behalf of my clients that if there is going to be a
1185 discussion had, or discussions had, that we would like to be at the table on the issue of the sale
1186 of the lots by the State. And let me tell you why I think that's important. We will do so again in
1187 a spirit of cooperation that realizes that not only is the State dramatically affected by that but
1188 we are. Just the innuendo, inferences, what public statements are made or where that
1189 discussion is going could have a dramatic effect on our values and interest in the leasehold
1190 interest so if we could be included in those discussions, we would like to be and we'd try to be
1191 of help.
1192
1193 Finally, while it was not on the agenda for today's meeting, I was hopeful that I might be able to
1194 once again assert that I strongly believe that there needs to be a cap, and possibly even a floor,
1195 but certainly a cap on the annual increases in the lease that's proposed. Otherwise we're really
1196 locking people in to a legal document to sign a blank check that if Jimmy Carter, Jr., became
1197 President tomorrow, we could be in a world of hurt. That wasn't a slam really on Jimmy Carter,
1198 but just his son.
1199

1200 **Secretary of State Ysursa:** In relation to those, we are – there were some questions about – we're well
1201 aware, and it's replete in the record, that both the Payette Lake Association and the Priest Lake
1202 Association argued quite strenuously for some sort of cap. The other I think about the lease
1203 document itself, I know there were some concerns from the Payette side about the release
1204 language, and Robert Follett is here from the Attorney General's office –
1205
1206 Raise your hand, Bob.
1207
1208 – who has worked on the document and is – if we have some discussions on how that release
1209 language – I think there was some later language you may not have seen. Anyway, I think we
1210 can get to the bottom of that.
1211
1212 Mr. Lempesis, I think you had some questions on the appeal language. We are working on that.
1213 The current appeal process seemed to have worked, but what I noticed about it, it was devoid of
1214 any timeframes.
1215
1216 **Mr. Lempesis:** Good point, Mr. Secretary.
1217
1218 **Secretary of State Ysursa:** It seemed rather open. So we've talked a little bit with the Department folks,
1219 but we've got everybody's emails and we'll keep working on those documents as quick as we
1220 can. We are faced timewise – remember the Land Board – we expect to make a decision
1221 March 16th because we cannot wait.
1222
1223 George, what's your plan for the Department to – applications for renewal are April 30th by
1224 code.
1225
1226 **Mr. Lempesis:** Can we state for the record that all of our lessees at this time intend to renew. And if you
1227 need that in writing, I can actually handwrite it. Seriously. I mean, if that is an impediment to

1228 you. The other thing is if the written lease, Mr. Secretary isn't done, we can certainly do that
1229 post March 15th if we had to, right?
1230
1231 **Secretary of State Ysursa:** Well, yeah, I mean, the fact that they are going to renew the lease we haven't
1232 finalized yet is kind of an interesting assertion.
1233
1234 **Mr. Lempesis:** Well, it just sets me up for malpractice (inaudible).
1235
1236 **Director Bacon:** Mr. Secretary, just to answer your question, and Mike can help me if I'm wrong, but
1237 we're shooting for – if the Board does finalize action, like we hope they will in March, that will
1238 give us time to send out both a title lease with the new methodology, whatever it is, premium
1239 rent and everything included, and folks can get – can look at that for up to forty-five days
1240 because we would like to have applications back by April 30th. And we want them back by
1241 April 30th because there's always people that are kind of slow, drag their feet, because really we
1242 have until May 30th to clean up, mop up any mistakes, right?
1243
1244 **Mr. Murphy:** You're basing the May 30th date on what?
1245
1246 **Director Bacon:** Another – if they don't get it in by April, we go hound them –
1247
1248 **Mr. Murphy:** Right. Correct.
1249
1250 **Director Bacon:** – for a month – the hounding date. And then if we don't have anything by the end of
1251 May –
1252
1253 **Mr. Murphy:** We would assume that they are not going to renew.
1254

1255 **Director Bacon:** – they're not going to renew. So we'd like to stay with that timeframe for obvious
1256 reasons because people need – if we're going to miss somebody, they're going to need a little
1257 extra time because they're traveling, didn't get the message or whatever.
1258
1259 **Secretary of State Ysursa:** And with the internet these days, I would assume that we will try to get as
1260 much as we can about cabin site instructions or what's going on, updates, get it on the web
1261 page on the Department of Lands because if you look at the Department of – Montana's
1262 department, they have quite a lot – you click on a link – cabin site folks, this is where you go to
1263 find out about information, and I think we need to do that here and use it.
1264
1265 **Director Bacon:** We can do that.
1266
1267 **Secretary of State Ysursa:** Yes, sir.
1268
1269 **Mr. Young:** Mr. Secretary, can I just ask a question of Mr. Bacon on – this is kind of a procedural
1270 question. If a lessee finds the new lease so onerous and unacceptable that they cannot sign the
1271 lease, what is the procedure in that case?
1272
1273 **Director Bacon:** Mr. Secretary –
1274
1275 **Secretary of State Ysursa:** Go ahead, George.
1276
1277 **Director Bacon:** I think that's a question for the attorney. Basically, I think the way the current leases
1278 read is if they decide not to renew and – current terms – current leases have been reviewed
1279 pretty thoroughly – is if they decide not to renew, then they have to remove their
1280 improvements and restore the ground to its previous condition.
1281
1282 **Mr. Lempesis:** Or get a restraining order with conjunctive relief (inaudible).

1283

1284 **Director Bacon:** And I don't know if there's any other option in that. I think the lease allows that the
1285 Department could try to purchase. I'm not sure how it's worded.
1286
1287 Robert, I guess I'm looking to you –
1288
1289 **Mr. Follett:** Yeah, I mean, the – the worst case scenario option would be the obligation to purchase,
1290 which is the length – the obligation to remove the improvements, which is what the lease
1291 actually currently reads. So in a worst case scenario, that would be, you know, if some
1292 resolution couldn't be agreed to otherwise.
1293
1294 **Mr. Young:** So – so let me just ask this question. If a reasonable person using prudent investment
1295 decisions finds this lease unacceptable, then are you saying that you're going to toss that guy off
1296 his – out of his cabin, out of his home and tell him that he's got to remove his home from that
1297 property? Is that the position?
1298
1299 **Mr. Follett:** Well, certainly one of the questions would be, you know, is it unreasonable. Are the terms
1300 onerous. And, you know, I was involved with most of that lease, and so I personally honestly
1301 don't think they are commercially unreasonable. But, you know, that can certainly be discussed.
1302
1303 **Mr. Young:** So – so I mean is that the position or is that the position of the State that –
1304
1305 **Mr. Follett:** To not make – we don't have anything to take a position with at this point. It would all be
1306 (inaudible) –
1307
1308 **Mr. Young:** I think it's obviously important. It's an important point for lessees to understand the
1309 position of the State if they find the lease unacceptable. Is there some provision contemplated
1310 if lessees cannot afford this formula that is being proposed? What's their alternative? Are they

1311 – and also if, because of the action of the State, there is no possibility to sell their
1312 improvements, what is the position of the State?
1313
1314 **Mr. Follett:** Ultimately that will be the decision of the Land Board.
1315
1316 **Secretary of State Ysursa:** Spoken like our attorney down there.
1317
1318 **Mr. Copple:** Well, Mr. Secretary, can I – can I ask –
1319
1320 **Secretary of State Ysursa:** I'm sure Mr. Copple would share his legal opinions, too. Not.
1321
1322 **Mr. Copple:** I'm just wondering if a policy is going to be instituted in that event.
1323
1324 **Secretary of State Ysursa:** Let's use a classic phrase. We'll take that matter under advisement. You've
1325 heard that before haven't you?
1326
1327 **Mr. Copple:** Yes, I have, Mr. Secretary. May I ask a question?
1328
1329 **Secretary of State Ysursa:** Yes.
1330
1331 **Mr. Copple:** I think Chuck's point about consistent with the collaborative process that we're trying to do
1332 with regard to the procedures for ultimately selling the property and the approaches that are
1333 taken, how can we be part of that process in a constructive way? It would be really helpful if we
1334 could get some kind of a commitment from the Department that, you know, we could be
1335 involved in that instead of receiving anything that sort of is already prepared, that would be
1336 great if we could have something like that.
1337

1338 **Secretary of State Ysursa:** I, as one Board member, and I'm sure Tom could – he can obviously speak for
1339 himself, but as we move down the road of disposal, whatever, exchange, unifying ownership in a
1340 market savvy manner, I think we ought to – we would – it would obviously behoove us to work
1341 closely with our current lessees at both lakes, and I'm sure the Department is going to come
1342 back with a plan. I think we gave you a year deadline there and obviously working with folks.
1343 Again, it may be not tempered but we have to recognize the unique characteristics of both lakes
1344 and where they may or may not be in a sort of process on sale or exchange.
1345
1346 Is that okay, George?
1347
1348 **Director Bacon:** Mr. Secretary, it is. I think the Department will have to take a look at things at a high
1349 level, independent and just from the trust perspective, but also everyone may be able to help to
1350 remind me – I don't know that the Board's motion was necessarily to sell or exchange but to
1351 somehow – somehow combine the lease estate, which may mean buying –
1352
1353 **Secretary of State Ysursa:** Sell, exchange, dispose or unify ownership. It was all inclusive.
1354
1355 **Director Bacon:** So the Department really may have to take a look at whether there's an option or an
1356 opportunity for us to purchase the improvements as opposed to selling the land. So we've got a
1357 lot to look at.
1358
1359 **Secretary of State Ysursa:** Yes, you do.
1360
1361 Mr. Hervey, second tier lot person for –
1362
1363 **Mr. Hervey:** I didn't have any comment initially, but now that Mr. Luna, my boss, is here.
1364

1365 I am a teacher at Morley Nelson School so I'm impacted in more than one way. We as teachers
1366 are feeling pressures. Mr. Luna's dealing as well as he can with that and no one knows the
1367 pressure more than me and the teachers that I work with. I see someone here from the PTA. So
1368 the teachers are – we're looking at the – what is best for our children, and I have always done
1369 that. And the leaseholders have too. All I ask is that we use, reiterating what Jim has said, the
1370 experts on the – the appraisers, who did a lot of that, there's emotion and all that and factoring
1371 that into rates and others. I know you will, Ben, because we've worked together for two
1372 hundred and fifty years on this problem. And I'm only asking now (inaudible) we feel the pain,
1373 and we as leaseholders, we want to carry our fair share, and we will continue to do that. I look
1374 forward to paying my own salary (inaudible) in the future (inaudible).
1375
1376 **Secretary of State Ysursa:** Thank you, Chuck.
1377
1378 Remarkably silent so far – Mike Fery.
1379
1380 **Mr. Fery:** Mr. Secretary, Superintendent Luna, I have been silent on this. It's – to be honest with you,
1381 frustrating for me just because I spent my livelihood for the last twenty years developing
1382 commercial real estate, all types of commercial real estate. So the discussion – a lot of the
1383 discussion is not normal or customary in real estate terms. The procedures are not normal or
1384 customary that have been talked about here. So it's definitely frustrating from that perspective.
1385
1386 I really have two questions. One would be the existing lease agreement, the current lease
1387 agreement. Since the motivation is to unify, dispose, sell, exchange in a market savvy manner –
1388 thank you – why not use the existing lease document and do a lease amendment, which would
1389 be somewhat normal, and modify it through the amendment the rent, the methodology, the
1390 term, the premium rent provision, if it so be, and the ability to purchase it, exchange, et cetera,
1391 however you can do that, versus creating a whole new lease document and a whole bunch of
1392 issues that may or may not be beneficial to the beneficiaries, because it could hurt the value. It

1393 could hurt the salability to those that are trying to get out of their cottage sites. So why not do
1394 an amendment, a very simple amendment, which is the basic terms that are changed. That's a
1395 question. You don't have to answer it now, but the second part of that is I understand that
1396 getting out of these in a market savvy way, that makes a lot of sense. I'm not sure really what
1397 that means though. I know what it would mean for me. I would do somewhat of a dollar cost
1398 averaging to get out of these because you never know when the top of the market is and if
1399 anyone ever tells you when the top of the market is, they don't know. So the best thing to do is
1400 to sell so much per year. Now is that five percent, ten percent, whatever. But it's to dispose of
1401 a percentage of those each year and just – you'll never time the market. I mean, that's a
1402 guarantee, and I hate to have that word guarantee.
1403
1404 Having said that, if you look at exchanges, exchanges will bring dollars to the education system
1405 faster than any other mechanism because if two markets have dropped in value, and you do the
1406 exchange at that point, it doesn't matter what the values are because they both dropped. So by
1407 doing the exchanges as soon as tomorrow, as you get one worked through, the educators will –
1408 the education system will derive more cash flow, which is really what it's all about. It should be
1409 the endowments. She's good. She's helping me here.
1410
1411 And, as you know, and it's been stated, I do have an exchange that's currently sitting in front of
1412 the cottage or in front of the Land Board or the Department staff, and I'd love to share that with
1413 the PTA and others to show them how much cash flow exchanging two lakefront lots for one
1414 commercial building will derive year one about a hundred and seventeen thousand dollars of
1415 extra cash flow. Is that one teacher, two teachers – is that two teachers and supplies? I don't
1416 know. I don't know what the salary ranges are, but that's immediate cash flows to you guys.
1417 And so I really – I guess the question is are you going to do exchanges immediately or are you
1418 going to study those until next year. To me studying exchanges when you've done them before
1419 at Payette lake, there's a system in place that's – because it's been done so many times in the
1420 past, why not get after those as soon as possible. So that's a question and a comment all in one.

1421

1422 **Secretary of State Ysursa:** As far as your asking me, I think any exchanges or whatever ought to be on
1423 the table if it makes sense for the endowment. That's always been – and with the Department
1424 has – for the record, it has been submitted to the Land Board record in the last materials, the
1425 specific exchange you're referring to is part of our voluminous record we have in front of the
1426 Land Board and others, and if other folks want to look at what you've presented to us and an
1427 association did in the last package, they're welcome to it. It's all public record. And – but it'd be
1428 – if it makes sense for the endowment, it ought to be done. If it doesn't make sense for the
1429 endowment, then we shouldn't do it. And I don't – with all the uncertainty around what was –
1430 and I'm not saying we're going to get rid of all that uncertainty – I think the Department's been
1431 a little reluctant to proceed on just about anything until they get some clear – clear direction
1432 from us. And if you look at the asset management plan, it basically says what I said. If it makes
1433 sense for the endowment, we ought to be doing it. And that's the best answer I can come up
1434 with.

1435

1436 Bonnie.

1437

1438 **Secretary of State Ysursa:** I did have a question for the beneficiaries. If they – you know, when you're
1439 establishing your policy to maximize the revenues, do you have any criteria that you've set? I
1440 mean, you've heard the criteria from these guys and everything. Do you have any criteria that
1441 you would – you considered for maximizing revenue – return to the endowment.

1442

1443 **Ms. Boeckel:** The Idaho PTA does not have a specific position on what actions the Land Board should
1444 take related to percentages, but what we do trust is that through their staff and experts and
1445 information that's made available for them, that they will follow the direction that leads them to
1446 meeting their fiduciary obligation.

1447

1448 **Superintendent Luna:** Can I ask now?

1449

1450 **Secretary of State Ysursa:** Of course.

1451

1452 **Superintendent Luna:** So does the current plan that was being discussed a couple weeks ago, does that
1453 meet your standard? Do you think with all the information available that the four percent and
1454 the premium rent as it was outlined that that is adequate?

1455

1456 **Ms. Boeckel:** Well, again, Superintendent Luna, as you know, I certainly am not an expert in this area,
1457 and I don't profess that our executive board is as well. We would certainly whatever decision
1458 the Land Board chooses to make based on all the information that has been provided, as well as
1459 documentation that is part of the public record, we would then evaluate whether that was
1460 actually met. Does that answer your question?

1461

1462 **Superintendent Luna:** Kind of. I mean that information's available now. And part of my frustration is
1463 that we have people telling us we are, you know, that we're not meeting our constitutional
1464 mandate, or they expect us to, but they won't tell us whether what we've laid on the table in
1465 their view meets that requirement.

1466

1467 **Ms. Butler:** Yeah, it's just what criteria you use to evaluate whether they're –

1468

1469 **Ms. Boeckel:** Well, as you know in our previous testimony when Ms. Escheverria represented the
1470 Children's Land Alliance, she stated that we supported Attorney General Wasden's report that
1471 came out related to maximizing the revenue. So I can just tell you that we're relying on you and
1472 those who are your experts to give you the information and we trust that (inaudible).

1473

1474 **Superintendent Luna:** Then I'll just say that when pressed, Attorney General Wasden did not offer a
1475 motion that he said would meet the constitutional mandate. He just objected to the motion
1476 that was on the table. So again what is it? You know, what is – you know, if we have to choose

1477 between two, then what are they and currently we have one offer on the table. If it's not
1478 constitutionally – if it's not – if it doesn't meet our constitutional mandate then what does and
1479 the Attorney General didn't even offer a motion to – he just said that this did not, and he did not
1480 propose a motion that would.
1481
1482 **Ms. Boeckel:** And Superintendent Luna, I'm not just focusing on Attorney General Wasden's report that
1483 we mentioned. I guess what I'm saying is we don't believe that we are the experts nor do we
1484 feel that the leaseholders necessarily are the experts to advise you. We actually look for you to
1485 take your advice from those that are supposed to help you when you're making your fiduciary
1486 duty.
1487
1488 **Superintendent Luna:** Okay. Thanks.
1489
1490 **Secretary of State Ysursa:** Mr. Furey is Chief of Staff for the Attorney General. He may have a comment.
1491
1492 **Mr. Furey:** Yeah, I just wanted to clear up – the General did not make a motion, but he did indicate what
1493 he felt would have been the appropriate methodology to use and also the rate. And it's the six
1494 percent. And I think actually, Mr. Ysursa, you hit the nail on the head when you said if we got
1495 market rent, we don't need to talk about premium rent. I mean we're – a lot of talk's going on
1496 about premium rent. It's probably totally irrelevant if we're getting market rent. That's really
1497 the issue. And that was the proposal he made. He said, you know, the ten year rolling average.
1498 You've got to get rid of that because you'll never make the market rent using that. He felt six
1499 percent was what should be done. Throw the premium rent out and go with a ten-year lease
1500 and so he did give what his recommendation is. So that is out there.
1501
1502 **Secretary of State Ysursa:** After rather persistent questioning from the – his friend on his left, which is
1503 myself, he did.
1504

1505 **Mr. Furey:** And he did.

1506

1507 **Secretary of State Ysursa:** He did indicate six percent of current market value plus probably a thirty-year
1508 Treasury as an index.

1509

1510 **Mr. Furey:** Yes.

1511

1512 **Secretary of State Ysursa:** And yes, it was not a motion, but that – what that did equate to, if you run
1513 the figures, with six percent of current market value is an average like of two hundred and fifty-
1514 four percent increase in one year. That's – that's the one that I think is – and I did have some
1515 questions about – those of us, and me included, and Superintendent Luna and two out of three
1516 times voted – and I voted three times – but for a freeze, and we have been complicit, so to
1517 speak, in the problem of – we had a three-year freeze in Payette and a two-year freeze in Priest
1518 Lake. And, yeah, we're – what you see is there is going to be a consensus of the Board, if not
1519 total, an increase in rent. I don't think you guys are that naïve to think that – we are going to
1520 increase the rent, and we do recognize that is right in the teeth of a horrible economy and the
1521 fact of the real estate scenario. But we also need to have the knowledge that we recognized
1522 this before and had empathy for the folks. There's a reason we froze rents for three years and
1523 two years at Priest. Seeing those valuations in Valley County go through the roof and go up like
1524 a rocket and come down like a broken glider. I don't know about that, but I try to get her – well,
1525 her – the Assessor to say where they might be headed this time. Well, they're going down, but
1526 we don't know how much in Valley County.

1527

1528 But anyway that's where we are. I think – well, I don't want to preach. I think fundamental
1529 fairness demands us to share in the problem. If we were in a vacuum and didn't have the –
1530 another one of my great quotes I suppose, but the millstone of history around our neck that we
1531 helped create, we'd be saying go to market rent right now. I know there's – we agree to
1532 disagree on what market rent is obviously, but you know where we are. I agree. If we were at

1533 market rent, we wouldn't need premium rent. You folks agree to that too. You just have a
1534 different idea of where market rent is than we do, and that's where we are and that's what's
1535 going to happen. Now the premium rent discussion today I think was most informative and
1536 we're going to head on from here, but we've got to kick this can down the road and come up
1537 with a decision.
1538
1539 Mr. Fery.
1540
1541 **Mr. Fery:** Mr. Secretary, I guess for the AG's office, I'm not sure everyone's read the Knipe report in
1542 1998, which I have a summary of right in my hands here so I won't misquote. But everyone
1543 always likes to say that the Knipe report says six percent. Well, it says –
1544
1545 **Secretary of State Ysursa:** Four to six depending on the lease term.
1546
1547 **Mr. Fery:** Let me just be exact –
1548
1549 **Secretary of State Ysursa:** Go ahead.
1550
1551 **Mr. Fery:** – if I may, sir. It would – he's recommending six percent, but rent should be either flat for ten
1552 years – for the ten year lease or indexed at an annual CPI, and he recommended three percent.
1553 Second thing, it has to have these provisions in order to keep the six percent; second thing is
1554 that the lessees be given a window of opportunity to terminate the lease each year, okay. The
1555 third point is lessees should be given a clear path to purchase the lots, okay. So these are his
1556 words, not mine. So that's – that's what he's recommended at six percent. Then he says if you
1557 don't do all of these things, not some of them, but all of these things, then you – he would look
1558 back to his analysis and the lowest was three point six percent, and he's saying using four
1559 percent would be more equitable. But again he comes back to talking about, you know, these –
1560 you'd have to know what the fixed increases are because you can't have an unlimited escalator.

1561 He never talks about adding premium rent on top of that, okay. So I'm not trying to bring up
1562 rent. I just wanted to clarify this misconception that all these experts keep saying six percent,
1563 including the gentleman from Montana. It's not six percent. It's six percent if you do all these
1564 other things. So there's a lot of devil – a lot of details lost in the –
1565
1566 **Secretary of State Ysursa:** Well, Mr. Fery, that's a very good point. It's also – when we say four percent,
1567 or what the Subcommittee came up with four percent, we all know that's not four percent of
1568 current, also. So we're not – four percent of current is – even four percent of a current ten-year
1569 average, we have a five-year phase-in of a ten-year average is what the Subcommittee
1570 suggested to get rid – to get rid of that and just say four percent of a ten-year average right now
1571 is fifty-four percent average across the board because we're taking five years under the
1572 Subcommittee's formula to get to that fifty-four percent. It's about a nine year percent average
1573 compounded –
1574
1575 **Superintendent Luna:** Nine percent every year.
1576
1577 **Secretary of State Ysursa:** Yes. And you know the figures and I know the figures and I had to correct you
1578 on your figure on the first year on your own rent. You said twelve and it's nine. Right. About
1579 eight is what it is.
1580
1581 **Mr. Fery:** Eight point one six.
1582
1583 **Secretary of State Ysursa:** Yeah. But that's not twelve that you suggested. Somebody else called me
1584 and said twelve. *(tape change)*
1585
1586 **Mr. Christenson:** One short one, Mr. Secretary. Denny Christenson again. In all this discussion of
1587 market rent, we have experts create scientific methods to determine it, but they're not
1588 determining it. They're estimating it. They can only best estimate the market value. The

1589 market value is proven when the transaction happens. When a willing buyer and a willing seller
1590 get together and agree on terms. So whatever comes out of the discussion on what market rent
1591 is estimated to be by the experts or by the State or by the lessees or anybody, it won't be
1592 proven until the actual transaction happens. That means when Bud or I or Mike or Jim decide to
1593 sell their place and is there any leasehold value left and that's what I'm warning against is that
1594 for the benefit of the endowment fund, don't destroy the leasehold value.
1595
1596 **Mr. Hervey:** One point – I'm sorry – let me just say –
1597
1598 **Secretary of State Ysursa:** Chuck Hervey, go ahead.
1599
1600 **Mr. Hervey:** Under the first tier average rent using the IDL's method of four percent rent and a two to
1601 nine percent value escalation on first tier in thirty years the rent will be five hundred and
1602 fourteen thousand dollars a year. Who wants to buy that deal? Back lot, same methodology, it
1603 would be forty-four thousand dollars a year for a back lot. Who wants to buy that deal? This is
1604 the methodology you're talking about Ben, isn't it?
1605
1606 **Secretary of State Ysursa:** Well, Chuck, we'd have to look at that again. We've changed some of our –
1607 on our terms. You know, the shock value of using thirty-five years versus ten or the first five
1608 that we talked about. We can all –
1609
1610 **Mr. Hervey:** So we're talking still about the mix –
1611
1612 **Secretary of State Ysursa:** Yeah.
1613
1614 **Mr. Hervey:** Okay. Thank you very much.
1615
1616 **Secretary of State Ysursa:** Mr. Follett.

1617

1618 **Mr. Follett:** I just wanted – I wanted to clarify the question about the current lease. I said the worst case
1619 scenario would be to have the lessee remove the improvements, which is clearly a contractual
1620 term that everybody signed onto. The other option would be what it says in K.14.C and that is
1621 that when there is a new lessee, the new lessee would be paying for the improvement. So if
1622 there were some time of – between the primary lessee and a subsequent lessee, the primary
1623 lessee would simply wait for a secondary lessee to come in and purchase those. The State
1624 would not necessarily opt to purchase the improvements under that circumstance. So I wanted
1625 to clarify that.

1626

1627 **Secretary of State Ysursa:** Thank you.

1628

1629 Is that bye, Bud, or you want to talk?

1630

1631 **Mr. Belles:** I would like to.

1632

1633 **Secretary of State Ysursa:** Go ahead.

1634

1635 Mr. Bud Belles.

1636

1637 **Mr. Belles:** Mr. Secretary, I'm Bud Belles, President of Priest Lake Association. I've got a little bit of a
1638 problem with my throat today so hope you can hear me. I keep thinking back twenty years ago
1639 when the federal side of our lake raised the rates out of the sky and a number of my friends had
1640 to sell. They couldn't afford it because they're like I am today, retired, and we don't have much
1641 to do – work with other than what we have coming in, you know, kind of a steady income. They
1642 sold and after a lot of negotiation, and I don't know all the details of that, the end result was
1643 that prices came down and the people that bought those lands received a credit. So they were

able to, you know, enjoy the lower rents and a credit that applied to those rents for the next few years.

Every time I think I've come into one of these things I've asked for a fair and equitable lease of some kind. I think we're there – or almost there. And I just ask you to consider that there's a lot of us up there that are in the position where we can't sustain a ten percent increase or nine, whatever it is, and that we don't know how long that could (inaudible) so I'd like to see the caps put in it. And that's all I have to say. Thank you.

Secretary of State Ysursa: Appreciate that. Any other comments?

Mr. Young: Just one closing comment, sorry Mr. Secretary.

Secretary of State Ysursa: Yes, go ahead.

Mr. Young: Just –

Secretary of State Ysursa: Mr. Jim Young is speaking. I think you know him.

Go ahead.

Mr. Young: Just a comment that, you know, we talk about this four percent in the Knipe report. I just want to remind everyone that the Knipe report is twelve years old, and the market has changed. Percentages don't necessarily correspond exactly if the market – if land prices are whipsawing up and down. And so I would urge the committee to, or the board to, consider more data, more science until a good conclusion can be arrived at. The six percent number is based on old science and old data and really may not have any bearing to what is currently relevant in this market today. So I know we all want to get this thing done, and we're sick of it. But if it takes

more data, more data collecting, I would urge the Board to consider doing that until we have arrived at a good conclusion.

Secretary of State Ysursa: Yes, sir. Mr. Dahl.

Mr. Dahl: Dennis Dahl again. I have two questions. As I understood Mr. Anderson in the last meeting, six percent included the sale of the property, and what you're saying is that you want six percent of the value going each year for our rent and then when you sell the property that will add to that six percent going way over six percent. So I think something less than six percent probably get you to where you want to go if – when you sell the property. Does that make sense?

Secretary of State Ysursa: Sort of.

Mr. Dahl: Okay. Second –

Secretary of State Ysursa: I wasn't advocating the six percent.

Mr. Goicoechea: The committee's four.

Mr. Dahl: I'm just hearing this six percent –

Mr. Furey: Are we talking about the premium rent again?

Secretary of State Ysursa: Well, I think we're getting mixed up a little bit on – and Mr. Dahl was –

Mr. Dahl: Mr. Anderson stated that six percent return is what you should be getting on those lands.

1700 **Secretary of State Ysursa:** The Attorney – the Attorney General's position is that he – well, and Sherm, if
1701 I misstate it, correct me – six percent of current market value with zero premium rent.
1702
1703 **Mr. Furey:** Yes, that's accurate.
1704
1705 **Secretary of State Ysursa:** Because he was saying that was market rent.
1706
1707 **Mr. Furey:** That's correct.
1708
1709 **Mr. Dahl:** And if I understood Mr. Anderson correctly, he said six percent included what you would
1710 make on the sale of that property. That your six percent return was an overall return. That's
1711 what I heard him say.
1712
1713 **Mr. Furey:** Actually what Mr. Anderson said was that if you're getting market rent –
1714
1715 **Secretary of State Ysursa:** You don't need premium rent.
1716
1717 **Mr. Furey:** – you don't – you shouldn't be. It would be unconscionable to be asking for it.
1718
1719 **Secretary of State Ysursa:** And I think everybody here agrees with that basic premise.
1720
1721 **Mr. Dahl:** Well, for premium rent. Yeah. But what I heard him say was that the six percent included not
1722 only what you got as a lease payment off the land but also the growth in value of that land when
1723 you sell it.
1724
1725 **Secretary of State Ysursa:** No, I think you misinterpreted what he said.
1726
1727 **Mr. Dahl:** I could have.

1728

1729 Second question I have has to do with premium rent. Our particular piece of property has sold
1730 twice in the last ten years. And the person we bought it from was not a flipper. He –
1731

1732 **Secretary of State Ysursa:** That phrase is going to come back and haunt me, isn't it?
1733

1734 **Mr. Dahl:** – he died last spring of cancer, and his dream was to die on that lake, and we gave him that
1735 opportunity. So that premium rent that's been paid on our specific piece of property, does that
1736 go against the property or is that a (inaudible) to a pool? Some properties haven't changed at
1737 all so they haven't paid any of the premium rent –
1738

1739 **Secretary of State Ysursa:** Correct.
1740

1741 **Mr. Dahl:** – (inaudible) the lot – our specific lot is – is paid for twice in the last ten years. So is that – is
1742 that going to go against – does that go against an account on our property or does it go into the
1743 pool? Are we paying premium – the premium rent (inaudible) –
1744

1745 **Secretary of State Ysursa:** It goes into the big pot of endowment receipts and up in Priest Lake, it's
1746 Public School.
1747

1748 **Mr. Dahl:** Okay. I understand.
1749

1750 **Secretary of State Ysursa:** In Payette Lake, it's Normal School and Hospital South. But I always say that,
1751 but I also remind folks that's all endowment land, and we're under the same constitutional
1752 charge.
1753

1754 I guess we can wrap this up.
1755

Tom, do you have any words of wisdom?

Mr. Luna: Yeah. I think the sooner we sell these the better.

Secretary of State Ysursa: I couldn't concur more. Well, that will wrap up the meeting with those comments and number one, appreciate everybody being here. We are – we do need to keep Robert and the lease document itself with Mr. Lempesis and Mr. Young, if you have it – or should that be to Mr. Copple on some of those lease –

So, Robert, Mr. Lempesis and Mr. Copple would be the contacts there.

Mr. Follett: Okay.

Secretary of State Ysursa: And Robert Follett, Terry, is the –

Mr. Copple: Great. Thank you.

Secretary of State Ysursa: Thank you. I imagine we'll see a lot of you on March 16th and we'll get this done. Appreciate it. Thank you.

END OF RECORDING

The meeting ended at 5:03 p.m.

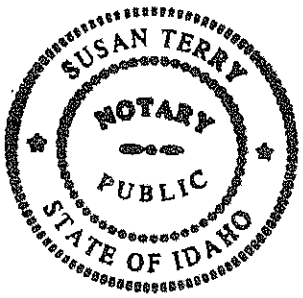
TRANSCRIBER'S CERTIFICATE

STATE OF IDAHO)
) ss.
COUNTY OF ADA)

I, Susan Terry, a Notary Public in and for the State of Idaho, residing at Nampa, County of Canyon, State of Idaho, do hereby certify:

That the foregoing transcript of the proceedings relating to the matter of Cottage Site Premium Rent for the State Board of Land Commissioners' Cottage Site Subcommittee, State of Idaho, recorded on March 1, 2010, was produced via audio cassette and thereafter reduced to typewriting by me, and that the foregoing sixty-four (64) pages contains a full, true and correct record of the oral conversations related to said matter, to the best of my ability, given the speakers' enunciation and the quality of the tape itself.

I hereunto set my hand and seal this 9th day of March 2010.



Susan Terry
Notary Public for Idaho
Residing at Nampa, Idaho
My Commission Expires 8-30-2011

Exhibit 42

Transcript, Agenda Item 8,

Recommendation of the

Cottage Site Subcommittee,

Land Bd. Meeting

(March 16, 2010)

State Board of Land Commissioners

March 16, 2010 Regular Meeting

8. Recommendation of the Cottage Site Subcommittee

SPEAKERS:

- C. L. "Butch" Otter, Governor
- Ben Ysursa, Secretary of State
- Lawrence Wasden, Attorney General
- Donna Jones, Controller
- Tom Luna, Superintendent of Public Instruction
- George Bacon, Director, Department of Lands
- Kathy Opp, Deputy Director, Department of Lands
- Charles Lempesis, Legal Counsel, Priest Lake State Lessees' Association
- Bud Belles, President, Priest Lake State Lessees' Association
- Alexander McLaughlin, Legal Counsel, Payette Lake Cabin Owners' Association
- Tony Park, Payette Lake Cabin Owner
- Laurie Boeckel, Idaho PTA

Governor Otter: Prior to going at ease, the State Board of Land Commissioners' was at the eighth order of business.

Mr. Bacon.

Director Bacon: Governor, members of the Board, tab number eight in your books is a recommendation of the Cottage Site Subcommittee, and Mr. Ysursa is the Chairman of that Committee so I guess we will turn things over to him.

Governor Otter: Mr. Ysursa.

29

30 **Secretary of State Ysursa:** Governor, members of the Land Board, as you are aware, the
31 Committee met last – the Board met last month and passed two motions – one, dealing
32 with the unification of ownership, sale, exchange, disposal, disposition of some – in a
33 manner and have the Department come back to us with a plan in January; two, we went
34 to – we decided to have a ten-year lease. Left on the table were two items. One, the
35 rate; and the connecting item with the rate is imposition of premium rent, if at all or
36 whatever.
37
38 So in that vein, the Subcommittee did have a meeting again with the lessees' groups and
39 others; some beneficiary groups were there. And what was on the table basically was
40 the premium rent because the rate issue was not discussed very much at all due – with
41 some other factors being stated. But we did talk about premium rent. But –
42
43 Governor, at your pleasure, I can get into doing a motion, or I'll do what – we can wait.
44 We had voluminous testimony last time about the rate issue. We also had quite a bit of
45 testimony on premium rent and –
46
47 **Governor Otter:** But is there –
48
49 **Secretary of State Ysursa:** The Subcommittee has altered its recommendation on the premium
50 rent issue, and I suppose there could be some comments on that. But the
51 Subcommittee recommendation, which I'll shortly read again, we have not – we have
52 not gotten off the four percent – the four-ten-five. But I will get into that, if you wish, at
53 this time or however you want to conduct the meeting.
54
55 **Governor Otter:** Well, I – unless members want to hear more about rate, rent and four-ten-five,
56 which we referred to, four percent increase, ten-year average, five-year –
57

Secretary of State Ysursa: Five-year phase-in.

Governor Otter: – five-year phase-in. But I think it – it probably – if we're changing the direction that we were going on premium rent, or we've got a new – a new twist on premium rent, that – I would like to hear your explanation of what will be offered now prior to closing the discussion to everybody else. And on the making of the motion, without leave of the Committee, of the Board, I should say, once the maker and the second of the motion is made, why, that closes off all discussion outside the Board.

So with that, would you give us an explanation of the premium rent that's going to be offered.

Secretary of State Ysursa: Well, Governor, members of the Board, after a lengthy discussion about the premium rent issue, and what was originally proposed was a gross premium rent. Currently we have ten percent of the gross of the leasehold value. That's been in place since 1981. There was a recommendation – we didn't come forward with it, but we were going to ratchet that up from ten to twenty, thirty, forty, fifty of gross over a five-year period. After discussion with some of the folks at the Subcommittee meeting and others, it was pointed out that that's really a disincentive for our lessees to keep their improvements and others and add to the value of this property.

I would think the overall issue we need to recognize, even when we quote rates from other studies for people, we are in a scenario where we have made a motion. We are in a disposal mode. Call it a transition, if you will. But I think we have to decide some of these issues with that overall action plan in front of us that a lot of the other studies we looked at were not in that mode. We are in the mode to try to get out of the leasing situation and use those assets in a better way for the endowment. So the least amount of chaos or disruption would be the road to go while we're in this transitional mode in the Subcommittee's estimation.

So in that vein, the addendum that was in your book about premium rent is the fact that we would retain the ten percent of gross on the leasehold value, which has been in place since '81, or we would go to fifty percent of net gain shared by the lessee and the State, whichever is greater to the endowment.

In that vein, we keep – we hear – we constantly hear changing the deal. Well, the ten percent gross is still part of the deal, but both in the Attorney General's opinion and others, when he wrote about 58-310a and the fact that the leasehold values that went through the roof, the prior lessees were getting that value. The State was getting ten percent, not the current lessees. We're talking about the amounts of money that over the what – the 203 to 209 in the realm of like twenty-five million dollars in leasehold value, and we got two and the previous lessees got twenty-three. That is not a situation that we believe is equitable.

So that's why the Subcommittee decided to – when I'm talking about the new recommendation on premium rent – is to keep what we have and not to go backwards. And we, being the endowments, keep what we have, and then if, in fact, somebody made a – improved their position financially, mainly because of – because of our land and the value of the land going up, that we share in that fifty percent net. So that was the equitable sharing aspect of it, but that is the change.

I can repeat the whole motion now, Governor, if you wish, but I did want to articulate the change on the – the premium rent because that is different than what was articulated a month ago. And I think comments directed to that may be germane. It depends on what you want to do.

Governor Otter: Is there a member of the Board that wishes to hear additional input from the – from the lessees or other members of – other stakeholders in public lands relative to premium rent and the changes?

Hearing none, I guess I would ask – I feel compelled to ask of the audience that if there is – is there – I would accept two sides, because I think there's only two sides on this.

Mr. Lempesis: I would ask for five minutes, Mr. Governor.

Governor Otter: I'll give you three.

Mr. Lempesis: I'll split – four (inaudible).

Governor Otter: You've got three.

Mr. Lempesis: Thank you.

Mr. Belles: I want to be your partner.

Mr. Lempesis: He holds my hand.

Governor Otter: Three between you.

Mr. Lempesis: Oh, yeah. He's not speaking. He's –

Mr. Belles: He gets nervous.

Mr. Lempesis: I'm here to catch my anchor, Governor and members of the Board. But before I do, I want to help. I said I'd help. I will help.

My name's Chuck Lempesis, Priest Lake State Lessees' Association.

I want to make sure you know what you're doing, because I think this is catastrophic for both of us. If you go through with the motion as proposed, here is what will transpire at Priest Lake, and speak for none others. In five years rents will go up fifty-three percent. We have not argued about the four percent. Don't intend to. Okay.

Governor Otter: And don't even talk about that.

Mr. Lempesis: Didn't even mention it.

Governor Otter: You're here to talk about premium rent.

Mr. Lempesis: On the premium rent issue, though, when you couple that, you're – Mr. Secretary of State said it best. As you look to divest yourself of these lands in some reasonable manner, this will destroy the marketplace. I am telling you. I am not misleading you, exaggerating, arguing, advocating. Who in their right mind would buy anything, particularly within the next year, for any value where they are going to pay a premium of several hundred thousand dollars for a lot with the word out there that the State's now going to sell them? What are you buying? Even with the ten percent premium rent, transfer of those properties is highly questionable. And who would sell under those circumstances by reason of the fact that if you took fifty percent of the net, and then added the federal capital gains of fifteen percent, and that eight percent we love to pay in addition at twenty-three percent and a real estate fee, there is nothing – nothing – or hardly anything that the seller gets.

I want to propose to you an alternative for consideration. Okay. I would like to see, until the State makes their report at the end of this year on divesting themselves and

how that sale would occur, in which case we should include those provisions in the forthcoming lease, okay. The lease should address that so there's some understanding in the mortgage markets and others how all that will happen. That you have a one-year lease; that you do the same terms as you have proposed, which is the four percent of the DMV, for lack of better terminology; that you keep the ten percent premium rent; that you abate the notion of this fifty percent net for at least the forthcoming year. It will destroy this marketplace. You are driving down – I cannot tell you how strongly I feel – you are driving down the values that you, as the Endowment Fund, want to get if you do that. We will both catch the anchor together. And I don't think that's what you want to do. So that's my proposal. I think I'm within three minutes, and I've very thankful for the gracious three minutes that you've granted.

Questions.

Governor Otter: I'll come to that after I hear Mr. –

Mr. Lempesis: Just say hi.

Mr. Belles: Oh. My name's Bud Belles. I'm President of the Priest Lake State Lessees' Association, and I'm just here to support Chuck.

Governor Otter: Oh.

Mr. Belles: I have no comments.

Mr. Lempesis: Yeah, he's just –

Governor Otter: Good luck on both counts.

Questions. Comments.

Yes, Mr. Ysursa.

Secretary of State Ysursa: Governor and Mr. Lempesis, the – I appreciate what you say. I always do. I don't necessarily agree with it. But, anyway, putting a one-year lease and whatever, like the Department's going to come up with a plan that's going to identify five hundred and twenty-plus lots and what our – our sale, exchange, unification, disposition is on those, that's an impossible task. I – we don't expect that as a Board of the Department. They're going to have a – we're going to have a laid out plan for all five hundred and twenty-two lots; three hundred-plus up at Priest Lake; the rest down in Payette Lake. And we all noticed, and even commented on it at length, the difference between the lakes; the dynamic difference between the lakes on – on current ownership pattern in Payette versus what it is in Priest and would there be dispositions, unifications, whatever. So I appreciate what you're saying.

I think – I think what needs to be pointed out is – is the other side, and who speaks for the beneficiaries. And I'm trying to be fair for both sides – both sides being one, the lessees; two, the beneficiaries in the endowment, who over the years, and even now, the ten percent, whatever – that leasehold value is still attributed mainly towards our land, our beneficiaries' land, not to work you've done or lessees' have done and whatever. It's mainly land values that have escalated.

Now what's going to happen now? The discussion of premium rent may be irrelevant because of the depressed market anyway for the next few years. I don't know. But it's – it's a scenario that – that the one-year lease scenario, and then go back and wait for the plan from the Department, I think it puts them in an untenable situation that we're going to have a plan on every – every lot by January. And that's – and write it into the lease. I don't think that's in the cards.

Governor Otter: Mr. Lempesis.

Mr. Lempesis: Mr. Governor –

Sir, and Mr. Secretary, what I'm saying isn't that. What I'm saying is two things. If – right now in the marketplace the announcement is, well, the State's going to sell all these lots. Well, what am I buying if I buy a lease? What am I buying if I buy your improvements? I have no clue. We can at least incorporate language in this lease once we know what the State's intentions are that deals with first right of refusal, what the terms of purchase may be, all kinds of things like that will at least temper the marketplace.

The second half of this is I am going to represent to you – I've been wrong many times, but in our experience together, I've been right a few times – I'm going to tell you that the people who will suffer the most, if you impose today this fifty percent net premium rent, will be the beneficiaries of the endowment. It will drive down prices substantially of the value of those properties, and when you really think through that, as a purchaser, perspective purchaser, seller or landowner, who in their right mind would pay the values they do today for property that is in such flux, in such turmoil, and is subject to absolutely no upside once there is a fifty percent premium of net, plus the capital gains, plus the State income tax, plus costs of sale. You'd be buying nothing, and that can only, in the free market, drive prices down. That's all I'm saying.

Secretary of State Ysursa: I appreciate that.

Governor Otter: Further discussion.

Mr. Wasden.

Attorney General Wasden: Thank you, Governor. I simply wanted to say thank you to Mr. Lempesis and Mr. Belles for being here and participating in this. Your presentation was concise and short. I appreciate that very much. Short is appropriate to me.

So thank you very much, Governor.

Governor Otter: Further discussion.

Thank you, Mr. Wasden.

Mr. Lempesis: Thank you, General.

Governor Otter: Further discussion.

Mr. Lempesis, how are you going to – how are you going to keep the quote, unquote, premium rent concept honest anyway. If – if, let's say, I pay a hundred thousand for a leaseholder value –

Mr. Lempesis: Yes.

Governor Otter: – and the cabin on the place is worth five hundred thousand. So I've got a six hundred thousand dollar total. Two years from now I sell it to the buyer, and I agree to sell him my cabin for six hundred and fifty thousand and the leaseholder improvements for fifty.

Mr. Lempesis: Right.

Governor Otter: Answer.

288

289 **Mr. Lempesis:** Governor, members of the Board, you're absolutely correct. In every contract I
290 do for franchises I represent –
291
292 **Governor Otter:** You do that.
293
294 **Mr. Lempesis:** No, I gross.
295
296 **Governor Otter:** Okay.
297
298 **Mr. Lempesis:** I gross. I go off gross always. And I think the ten percent gross has worked
299 efficiently, but we're not going to lose anything by doing that one more year. This isn't
300 to drag this out. I am telling you. If you go to fifty percent of net, you're going to take
301 that market down.
302
303 **Governor Otter:** I'm – I'm not persuaded that we need to delay it, Chuck. And I'll tell you why.
304 A year from now, whether this is the same Board or not, they can say this is our new
305 program.
306
307 **Mr. Lempesis:** Okay.
308
309 **Governor Otter:** But this is going to give us at least a point of beginning, and I'm willing to
310 discuss for the next year, if I'm the Chairman next year, I'm willing to discuss anything to
311 divest ourselves of these headache – or these cabin lots.
312
313 **Mr. Lempesis:** He was referring to –
314
315 **Governor Otter:** I never felt that was the proper ownership, but I understand that in the
316 benevolence of the federal government, when they gave us the land and in some of the

317 acquisitions that we made, they were – they were all done for good and pure purposes.
318 But I'm going – I'm going to stick with the Subcommittee's recommendations now, and
319 if for no other reason to move forward whether it's beginning today, and if we change
320 that a year – if that's changed a year from now, whoever changes it, fine. But I'm going
321 forward.
322
323 **Mr. Lempesis:** I appreciate your time, Governor, members of the Board, and I want to thank the
324 Subcommittee for the courtesy that's been extended continually.
325
326 **Governor Otter:** Thank you.
327
328 **Mr. Belles:** Thank you.
329
330 **Secretary of State Ysursa:** Thank you, guys.
331
332 **Mr. Lempesis:** Where's that anchor?
333
334 **Controller Jones:** It's below you.
335
336 **Secretary of State Ysursa:** It's coming.
337
338 **Governor Otter:** Yes, sir?
339
340 **Mr. McLaughlin:** My name is Alex McLaughlin. I represent the Payette Lake lessees. I'd like a
341 few moments to talk –
342
343 **Governor Otter:** Okay.
344
345 Chuck, you represented Priest Lake.

346

347 **Mr. Lempesis:** Yes, sir.

348

349 **Governor Otter:** Okay.

350

351 On premium rent?

352

353 **Mr. McLaughlin:** Yes.

354

355 **Governor Otter:** And I welcome former Attorney General Tony Park.

356

357 **Mr. Park:** Thank you, Governor.

358

359 **Mr. McLaughlin:** As stated, my name is Alex McLaughlin. I'm here on behalf of Terry Copple.
360 We represent the Payette Lake lessees.

361

362 With regards to the issue of premium rent, our position has been elucidated in prior
363 correspondence, whether through Mike Fery's presentation and prior letters to this
364 Board. Briefly, you can't talk about premium rent without addressing Idaho Code
365 58-301a, and that provision states in very clear terms that this Board is to charge market
366 rent and market rent alone.

367

368 **Governor Otter:** Excuse me. Your citation was?

369

370 **Secretary of State Ysursa:** 310a, I believe.

371

372 **Mr. McLaughlin:** 3-0-1a.

373

374 **Secretary of State Ysursa:** 3-1-0.

Attorney General Wasden: 3-1-0.

Secretary of State Ysursa: 310.

Mr. McLaughlin: 3-1-0.

Governor Otter: Okay. Have we decided what it is?

Mr. McLaughlin: I stand corrected.

Secretary of State Ysursa: We've decided it's fifty-eight dash three-one-zero-a.

Governor Otter: Would you accept that?

Mr. McLaughlin: I would accept it, Governor.

Governor Otter: Okay, so will we.

Mr. McLaughlin: But where premium rent comes in is that it's a concept when contract rent is under market levels. In that sense, premium rent can enable the State to get market returns by making up the difference between contract rent and market rent. Now, this makes good business sense insomuch as when we look within the specific context of the Board's charge of charging market rent. But this is not how it's being used in this proposal.

As it's used, premium rent has really nothing to do with rent at all. It's almost a misnomer. It's really just a tax imposed at the time of transfer of a particular leasehold. Transfer taxes are of – can be of questionable legality unless there is authority to do so.

And a transfer tax is certainly anathema to the market and the principle that the Board is only to charge market rent.

With that, I ask that the Board take into consideration the comments and points elucidated by the Association in this matter and adopt a proposal that's consistent with those points.

Thank you.

Governor Otter: Did anything you've just said differ from your letter on premium rent?

Mr. McLaughlin: It offers one more particular legal point.

Governor Otter: Okay. And that's the fact that it's a tax instead of a –

Mr. McLaughlin: The transfer aspect as opposed to something within the market.

Governor Otter: Mr. – Tony. Did you have something you wanted to add? Do you support that?

Mr. Park: Not specifically.

Governor, members of the Board, not specifically on the sole issue of premium rent, but what I wanted to say to the Board includes premium rent, and I have a suggestion for the Board that I'd like them to consider.

Governor Otter: Is this the one that you've sent us?

Mr. Park: I did not send anything to the Land Board myself, Governor.

433 **Governor Otter:** You didn't send me a letter and –

434

435 **Mr. Park:** I sent you a letter, and I had discussed with Bonnie Butler some of the points of
436 compromise that I would particularly recommend and –

437

438 **Governor Otter:** Okay. But you didn't share that with the rest of the Board?

439

440 **Mr. Park:** No. My assignment was to share it with you.

441

442 **Governor Otter:** Okay.

443

444 **Mr. Park:** But let me – let me just say – first of all, Governor, members of the Board, I've been a
445 civil litigator in the Boise Treasure Valley area for upwards of forty years now. The first
446 thirty-five of which were spent as a litigator, and the last ten of which have been as a
447 mediator. I've devoted my entire professional efforts, such as they are, to being a
448 certified mediator and arbitrator.

449

450 Now, we – in this situation, members of the Board, we have four basic, I think, sticking
451 points. And it has the rent, premium rent, the rate for the rent, premium rent,
452 escalation clause in the lease, whether there should be a cap and so forth. But there are
453 precise and defined points of contention.

454

455 A good mediator – folks, a good mediator – and there are plenty around this area; I'm
456 thinking of Merlyn Clark. I'm thinking of Judge Duff McKee. I'm thinking of John Magel.
457 There – there are a number of mediators here who are highly qualified, and their task
458 has now been – if this were to be submitted to mediation – their task has been made
459 infinitely easier by this Board's policy now, as announced at the last meeting, to unify
460 title to these – to these – to the lots and the improvements.

461

I believe that a mediator could resolve these points if the Board would allow a mediation to occur. Prior to going into the whole process of unification of title, and I would recommend to this Board that it consider submitting the lease issues to mediation, and I believe that if it could be done – Mr. Lempesis talked about a one-year lease, that makes sense; a two-year lease – to work through some of these issues with the aid of a skilled mediator, and allow this Board to have some breathing room to get on with the big task at hand, which, of course, is the unification of title that this Board has decided it needs to accomplish.

So that is my proposal, Governor, members of the Board. And I can tell you, having done hundreds – hundreds of mediations myself, that this process would be susceptible to a successful mediation. I would highly recommend it.

Governor Otter: Further discussion.

Mr. Wasden.

Attorney General Wasden: Thank you, Governor.

Mr. McLaughlin, I think this is the – maybe the first time you have appeared before the Board so I wanted to welcome you and send you greetings. And, Mr. Park, it's always a pleasure to welcome a member of the Board, a former holder of this Office, a predecessor of mine, and I appreciate your participation.

Mr. Park: Thank you, General.

Governor Otter: Further discussion.

490 I would – Mr. – Tony, you know, you've got an advantage over us having been a
491 contributing member of this Board for quite some time during your term as the
492 Attorney General. Probably weren't faced with this question as often as we have been.
493
494 **Mr. Park:** No.
495
496 **Governor Otter:** And then operating as a civil litigator and then a mediator on issues like this.
497 It's hard for me to ask you this question because I know it's – it's difficult – it would be
498 difficult for you to extract yourself from the sentiments of at least the side of the cabin
499 owners, but would you let this continue for another year and engage in mediation
500 without going forward now knowing full well that for a couple of years we froze those
501 prices? We did nothing. And that there's a serious question as to whether or not we
502 are fulfilling the spirit of, the moral of, our article IX, section 8 constitutional
503 requirement here?
504
505 **Mr. Park:** Governor, members of the Board –
506
507 Governor, I'm not recommending that we put the process in abeyance. What I'm
508 recommending is that we submit the matter to mediation immediately. Designate the
509 mediator. Get through – the mediation wouldn't – shouldn't take more than a few days.
510 And hopefully we can come out of that mediation in the next – I'm saying in the next
511 thirty days with a – with a recommendation to this Board that everyone can live with.
512 And put the – put the new lease in place as soon as possible, but I'm – I'm not
513 recommending any delay whatsoever in that – in – in that whole process, Governor.
514
515 **Governor Otter:** So then what's to stop us from going forward with the motion that we know
516 we're anticipating from the Subcommittee, and going forward with mediation. Going
517 forward with every effort to draw a reasonable, constitutional and – and forward

518 looking decision on this because you know full well that with four years, there was
519 constant change of former policy of this Board by the Board. Right?
520
521 **Mr. Park:** Oh, yes. That's correct.
522
523 **Governor Otter:** So if we adopt the motion that says this is where we're going – four, five and
524 ten or four, ten and five, excuse me, and then we – we engage in the mediation
525 investigation process and everything, by September or October we come up with some
526 magical process that goes forward, or if we don't, the next Board assumes responsibility
527 for that, and if it's this same Board, then we go forward with that. So what's to stop us
528 from adopting today the motion that's going – that we anticipate being made by the
529 Subcommittee?
530
531 **Mr. Park:** Governor, members of the Board, I'm fearful that if the motion as presently conceived
532 is adopted by the – by the Board today, that that will unleash the litigation mode. And
533 what I'm saying – what I believe can happen is if we set aside another thirty days to try
534 to mediate these four sticking points, and include – and hopefully reach agreement on
535 those sticking points – and include those in the new lease, that we don't have that. That
536 will obviate the need for litigation, and we can still go forward according to statutory
537 process.
538
539 **Governor Otter:** I've got nine –
540
541 **Mr. Park:** That's what I'm saying.
542
543 **Governor Otter:** We've got nine beneficiaries and fourteen entities out there that also are
544 stakeholders in this. And so if we – if we satisfy going forward without litigation from
545 your side, what's to stop the other side from going forward? In fact, I would anticipate
546 that.

Mr. Park: Governor, members of the Board, the other side – you mean –

Governor Otter: With litigation.

Mr. Park: Yeah, well, the other side is the State of Idaho. Our side are the two – the Payette Lakes and Priest Lake –

Governor Otter: The five hundred and twenty-two.

Mr. Park: – cabin owners' association.

Governor Otter: I understand that. But what I'm saying to you is the Superintendent of Public Instruction is – is – and his department is the largest, two hundred and seventy-five thousand students that are the beneficiaries of our actions. Then there's – then there's eight other beneficiaries – I don't know if they all have lake lots – but, anyway, my point is – is that if I were a stakeholder on the other side, and as a father and grandfather, I think I kind of am – what would stop me from saying they're not getting enough for those lots, and there's not a future in where they're going. And so I want to see a future in where they're going, and I think the – and I'm anticipating the motion by the Subcommittee, I admit, but I think going forward with that doesn't negate us from going forward with some of your ideas as well in anticipating that maybe we can get something done before Lempesis turns the lights out again.

Attorney General Wasden: Governor, the record should reflect that he, in fact, just turned the lights out.

Governor Otter: I'm sorry (inaudible).

576 **Mr. Lempesis:** No, you're not.

577

578 **Mr. Park:** Governor, members of the Board, obviously I can't – I can't assure this Board that
579 there couldn't be litigation in any event by the beneficiaries or representatives of the
580 beneficiaries, among others. I'm – I'm just saying that we could accomplish the same
581 thing, I think, and have just as much a chance to prevent that from happening by
582 attempting to mediate a lease that both sides can agree on and that both sides can
583 represent to those beneficiaries that we – that we have satisfied the constitutional
584 mandate.

585

586 **Governor Otter:** Further discussion. Questions.

587

588 Okay. Thank you, gentlemen. That was a little more than three minutes.

589

590 Do we have any other stakeholders that would like to be identified?

591

592 **Secretary of State Ysursa:** About premium rent.

593

594 **Governor Otter:** About premium rent.

595

596 Representing the PTA.

597

598 **Ms. Boeckel:** Yes, I am, sir. Thank you for inviting me today. My name is Laurie Boeckel. I am
599 with the Idaho State PTA. I am a member of the Executive Board, the Legislative Vice
600 President.

601

602 I'm here today based on what has been put in front of us related to premium rents to
603 ask the Board, when they are making their decision, to act in a manner that has the
604 undivided loyalty to the beneficiaries, which are the children in public education now

605 and in the future. And I would also respectfully request that in light of the fact that
606 there's been discussion on mediation, that if that decision is made that we would also
607 be extended the invitation to be at any mediation.
608
609 **Governor Otter:** Further discussion.
610
611 Mr. Wasden.
612
613 **Attorney General Wasden:** Thank you, Governor.
614
615 And Ms. Boeckel, I just wanted to welcome you. I really appreciate when the
616 beneficiaries of these trusts are here to discuss these matters with us, and I appreciate
617 your presence today.
618
619 Thank you.
620
621 **Ms. Boeckel:** Governor, Attorney General Wasden, thank you. I appreciate your kind words.
622
623 **Governor Otter:** Mr. Luna.
624
625 **Superintendent Luna:** Ms. Boeckel, thank you for being here. You sent me a letter recently, and
626 you – well written and good – good arguments – you mentioned in the letter that two
627 million dollars had been lost to the endowment this year alone, and I – what – what you
628 didn't include in the letter was what – what numbers did you build upon to determine
629 that we've left – that we've lost two million dollars. You know, what – what rate should
630 rent have been? What should premium rent should have been in your view to get to
631 the two million dollars?
632
633 **Governor Otter:** Ms. Boeckel.

634

635 **Ms. Boeckel:** Governor, Superintendent Luna, Idaho PTA does not have a position specifically on
636 what the rent should be. What we do go off of is the fact, or the information that has
637 been made available to us, including the Attorney General's opinion that I believe he
638 released, and I think in our editorial we said December, but I think it was actually last
639 summer, as well as the fact that we understand that there's been studies done by the
640 Land Board ongoing for numerous years, and we believe that that number would reflect
641 that two million dollars.

642

643 **Superintendent Luna:** Can I –

644

645 **Governor Otter:** Mr. Luna.

646

647 **Superintendent Luna:** – just a quick follow up.

648

649 And I'm not trying to put you on the spot here. I was just curious what formula you
650 used to get to two million dollars. A specific, you know, formula and – that would
651 include, you know, the lease rent amount and also premium rent, you know, so we can
652 compare your formula with the formula that we currently have and the formula that's
653 going to be part of the motion made. How – how does – you, know, so we can compare
654 the three and see where we were lacking.

655

656 **Ms. Boeckel:** Governor –

657

658 **Governor Otter:** Ms. Boeckel.

659

660 **Ms. Boeckel:** Superintendent Luna, again, when we take the information that we have had,
661 which is based on the fact that we assume that the Attorney General, as well as the
662 Land Board studies, are acting in the best interest, we do not specifically have a study

663 for our organization, but we can take information that we believe has been made
664 available to Land Board members to make an educated decision on what that rate
665 should be, and that would be our recommendation as far as where that number came
666 from.
667
668 So specifically to a formula, I can tell you that we do not have a specific formula, but we
669 did rely on the numbers that have been made available by the Attorney General's office,
670 as well as the studies by the Land Board.
671
672 **Governor Otter:** That constant reference, Mr. Wasden – where did you get your figures?
673
674 **Attorney General Wasden:** I am uncertain, Governor, as to what specific set of figures.
675
676 **Governor Otter:** Well, Ms. Boeckel has referenced the figures that you used in a guest opinion
677 or something or a letter back to the PTA. I just wanted to know what was the source of
678 your figures.
679
680 **Attorney General Wasden:** The – the information I think that she is referring to is an Attorney
681 General's opinion, which was issued last summer –
682
683 **Governor Otter:** Okay.
684
685 **Attorney General Wasden:** – Governor.
686
687 **Governor Otter:** And where did you get those figures?
688
689 **Attorney General Wasden:** Those – the figures that we discussed were supplied to us by the
690 Department.
691

692 **Governor Otter:** We're running in a circle here.

693

694 **Superintendent Luna:** I guess, Governor – I think the point, and, Governor, I think maybe you've
695 made it – is we keep hearing that there's X number of dollars that were left on the table
696 that haven't been collected, but numerous times now we've asked people to tell us
697 what – what numbers they would change in the formula we currently have in order to
698 realize this two million dollars, and it just keeps going in a circle.

699

700 **Attorney General Wasden:** Governor –

701

702 **Governor Otter:** Mr. Wasden.

703

704 **Attorney General Wasden:** Governor, I think this discussions a little bit out of the realm of what
705 we were discussing, which was premium rent, as I recall.

706

707 **Governor Otter:** Two million dollars was premium rent, wasn't it?

708

709 **Superintendent Luna:** That was my understanding.

710

711 **Governor Otter:** Yeah.

712

713 **Attorney General Wasden:** Well, the numbers we received were from the Department as to the
714 premium rent paid both to the – to the lessees and to the Department or to the
715 beneficiaries.

716

717 **Governor Otter:** Mr. Ysursa.

718

719 **Secretary of State Ysursa:** Governor, members of the Board, I believe the Attorney General's
720 Opinion got into the premium rent figures from 2003 to '09 and how much the previous

721 lessees' got and how much we got and whatever. I – I think those are the numbers that
722 Ms. Boeckel's talking about, but – in fact, I have referenced some of those numbers
723 earlier in my discussion today, about the twenty-five million and that we got two and
724 they got twenty-three and whatever. So the Attorney General's Opinion on 58-310a,
725 which was out this summer, is, I believe, where those figures came from, and those
726 were taken from Department figures.
727
728 **Governor Otter:** Ms. Boeckel.
729
730 **Ms. Boeckel:** Governor Otter – and I'd just like to follow up with that. I'm not sure where the
731 Subcommittee – I know I was at that meeting – I'm not sure what study that you guys
732 relied on to get the numbers that you're bringing forth today. So the only numbers that
733 I'm aware of is – is based on what the Department of Lands has done that seemed to be
734 a neutral party that should be directing the Land Board.
735
736 **Governor Otter:** Further discussion.
737
738 Thank you very much, Ms. Boeckel.
739
740 **Ms. Boeckel:** Thank you.
741
742 **Governor Otter:** Is there anyone else?
743
744 **Attorney General Wasden:** Governor.
745
746 **Governor Otter:** Mr. Wasden.
747
748 **Attorney General Wasden:** With regard to that, I would indicate there is a letter that I sent on
749 March 10, 2010 to Director George Bacon concerning cottage sites, and in response to

750 that letter, I received a Cottage Program Revenue document and that gives those
751 numbers. You actually had that in your hand just a moment ago, and I – and that is part
752 of the record, and I just wanted to make certain that you knew that was part of the
753 record.
754
755 **Governor Otter:** Okay. Well, whenever somebody referenced these numbers that somebody
756 else gave them, then it's important, I think, that we go to the origin of those numbers
757 and find out where they were – where they were gleaned from, and I was not surprised
758 that they were the Department's. But I just wanted to know the numbers you referred
759 to were the same ones that the Department had come up that we've been talking about
760 all the time.
761
762 So – discussion is ended.
763
764 **Secretary of State Ysursa:** Governor, members of the Board, as Chairman of the Subcommittee,
765 I am prepared to make a rather lengthy motion.
766
767 **Governor Otter:** (inaudible)
768
769 **Secretary of State Ysursa:** The Subcommittee is well aware of the constitutional mandate of
770 article IX, section 8 and the duty of undivided loyalty to the beneficiaries of the
771 endowment trust. However, we also recognize that severely impairing or eroding long
772 standing business relationships with our lessees is not in the best interest of our trust
773 beneficiaries. We're also aware that raising rents too high could result in lands going
774 unleased to the detriment of the beneficiaries. We believe these rates – that we will be
775 providing a reasonable rate of return during this transitional period when we are trying
776 to extricate ourselves from the leasing scenario.
777

What our recommendation is on the rate is the four-ten-five, which has been out for quite a while, even published in the paper at the Idaho Statesman. Basically, a four percent of the ten-year average phased in over five years. This, under the current scenario, would be an average, about. A reasonable rate of return generates about a nine percent average increase per year in the first five years. Overall about a fifty-four percent over the five-year period. Various lake – the lakefronts at Payette is in the eight range; the second tier is in the fourteen percent range; the Priest Lake folks are at a nine-percent range.

And I use the term four, and I've been – and I've stated this many a time, at the end of a five-year period, this, frankly, gets them to a little bit over what they agreed to ten years ago on two point five of current. I find it incredulous at times that the lessees are outraged that I would suggest this type of rate when it, in fact, is very close to the two point five percent of current that they agreed to ten years ago. Why aren't we at current?

We, as a Board, all – everyone on this Board has voted for a freeze at least two times; some of us three times. We are complicit in the problem that we're at – that we're not even at the two point five. And we need to be reasonable and fair in the way we extricate ourselves, and I believe that immediately going to a huge increase goes against all sense of fairness to both sides. And I know we have to be fair to the beneficiaries, that's our number one mandate. We also have to be fair to the folks that we've dealt with over the last forty, fifty years, in my opinion. And I don't believe in – in the fact that they are upset with these raises. It doesn't give me comfort. I figure with what we've come up with, there's something here for everybody to hate. So it might be a pretty good resolution. But the – that is the recommendation on the four-ten-five scenario, and also included in that, and I have already articulated what the premium rent would be on the ten percent of gross or the fifty percent of net, whichever is greater for the endowment.

807

808 Do we acknowledge that we're not at market rent by using the term premium rent?
809 Yes. We've done that since 1981. The huge disconnect here between us and the
810 lessees is what goes back to the basic. We can mediate it to death, if you want to.
811 What is market rent? I do not believe it's one percent on a two million dollar lot, and
812 that's a suggestion in the appraisers' methodology that is pushed by the Payette Lake
813 folks and the Priest Lake folks. And to get a forty percent reduction for those on the
814 Payette lakefront. That is not in the cards for me, and I don't think other members of
815 this Board. That is the basic disconnect. It's all about money. It's all about the bottom
816 line. It's all about what is market rent. And we have a basic severe disconnect and
817 disagreement over what market rent is. Let's face it. That's what this is all about, and
818 sugar coat it, do everything else we want. That is the reason for the disconnect. And
819 the rapid escalation and what's the assessor think the values are and what's going to
820 happen. All that stuff is peripheral. It's what am I going to pay. That's the bottom line.
821
822 Anyway, I've kind of waxed a little long on what the motion would be, but that's the –
823 that's the motion of the Subcommittee. The four-ten-five, and the premium rent. And I
824 would move that as my recommendation.
825
826 **Superintendent Luna:** Second.
827
828 **Governor Otter:** It's been moved and seconded.
829
830 **Superintendent Luna:** Whatever we just –
831
832 **Governor Otter:** A little long. It's like saying King Kong is just another monkey.
833
834 **Secretary of State Ysursa:** I resemble that remark.
835

Governor Otter: So the essence is a four-ten-five; four percent over a ten-year average, five-year phase-in.

Secretary of State Ysursa: Correct.

Governor Otter: Second part, and I would entertain a division of the question, if need be –

Secretary of State Ysursa: I made it as one motion.

Governor Otter: I understand that, but I also recognize –

Secretary of State Ysursa: If you wish –

Governor Otter: – the value of it.

Ten percent gross or fifty percent of the net –

Secretary of State Ysursa: Whichever is –

Governor Otter: – on premium rent.

Secretary of State Ysursa: – greater.

Governor Otter: Whichever is greater. That's the essence of the motion.

Secretary of State Ysursa: Yes.

Governor Otter: It's been moved and seconded. Is there a discussion?

865 **Attorney General Wasden:** No. I just wanted to clarify. Your clarification now has highlighted
866 exactly what the motion is. That's all I needed, Governor.
867
868 **Governor Otter:** All the other stuff notwithstanding.
869
870 **Secretary of State Ysursa:** You mean I ran a little long?
871
872 **Attorney General Wasden:** I wouldn't say that.
873
874 **Governor Otter:** Ms. Jones.
875
876 **Controller Jones:** Mr. Chairman and fellow Board members, especially the Secretary. Thank you
877 so much for what you've done over the last year. You have put so many hours in it, and
878 I do appreciate. I do disagree with your rental rate recommendation. Just – I don't
879 think that will bring us to a true market rent, as you said. And by continuing to collect
880 the premium rent, we're openly acknowledging that our rental rate is too low. That was
881 – that would be my comments. Thank you.
882
883 **Governor Otter:** Further discussion.
884
885 Mr. Wasden.
886
887 **Attorney General Wasden:** Governor, I think my – my voice has been heard on this. About a
888 month ago at our previous Land Board meeting I reiterated my concerns. We have an
889 obligation to obtain the maximum long-term return. Those are words that mean a lot to
890 all of us. I – I cast no aspersions regarding that. We have an obligation to act as a
891 prudent investor. We have an obligation to have undivided loyalty to the beneficiaries,
892 and we are statutorily required to get market rent for the duration of the lease. I do not

893 believe we will be fulfilling that responsibility with regard to this motion. I will be voting
894 no.
895
896 **Governor Otter:** Any further discussion.
897
898 I would only mention from a couple aspects. Number one, I think there's a great value
899 in stability – knowing who your lessees are; also stability to the market. And whether or
900 not this brings stability and predictability to the market, I believe it will. But I also
901 believe that we're obligated to go forward with perhaps some of the suggestions that
902 Mr. Park has made relative to the mediation.
903
904 I, for one, really think it's important that we get on a program to, whether it's market
905 savvy manner or a – a certain factor of the rent that's paid or whatever, but in some
906 way trade ourselves out of, auction ourselves out of, sell ourselves out of these lots.
907 And I think I've made myself clear on that.
908
909 To that end, I have one question of the Secretary in the Department of Lands. A couple
910 of figures were constantly thrown out, and in discussions that I've had with the
911 Subcommittee and discussions I've had with people who have been requested to – to
912 answer some lease and premium rent discussions, on the one hand, we took into
913 consideration the cost of our doing business with leases. On the other hand, we
914 weren't. As a landowner and as a property owner, unless I was figuring triple net, and if
915 that's what these leases are, then I understand it, but what percentage-wise of the
916 money we get right now is the cost of doing business on the leased sites.
917
918 **Director Bacon:** Governor, members of the Board, staff may correct me if I'm wrong, but I
919 believe historically over the last several years, our costs for this program have been
920 about five percent of our income, and last year it was closer to six. So I believe it's
921 floating in there somewhere.

922

923 **Governor Otter:** Is this established to correct their (inaudible)?

924

925 **Secretary of State Ysursa:** Sometimes – sometimes three.

926

927 **Director Bacon:** Yeah, it's – it's –

928

929 **Secretary of State Ysursa:** Sometimes three.

930

931 **Director Bacon:** Yeah, who wants to –

932

933 **Secretary of State Ysursa:** About three to six.

934

935 **Governor Otter:** I actually – I actually – I went back and tried to find in the minutes when your
936 plan – management – when your business plan was brought forward, and it was closer
937 to two and seven-eighths or something like that. It was closer to three than it was the
938 other factors that's been thrown out, five, six percent.

939

940 **Director Bacon:** Governor, if I may, that – that maybe due because of the rental freezes that
941 where we've seen costs continue to be impacted by inflation, we haven't necessarily
942 seen rents increase because of the freezes. So that may be one factor at play.

943

944 **Governor Otter:** I see. But don't we have a software system where we say this is what it is and –

945

946 **Director Bacon:** Well, I – I think I brought with me the 2009 information for income. The
947 residential leasing program last year cost us – or grossed, four million, five hundred
948 twenty-nine thousand, five hundred and eleven dollars, and the costs of the program –
949 they're split out both by direct costs and –

950

951 **Secretary of State Ysursa:** And managerial overhead – it's about five to six, I think.

952

953 **Director Bacon:** – overhead. So it would take a little calculation. But the net income for the
954 residential then would have been four point two three three. So the difference
955 between four-five and two-nine and four-two-three-three is about three million dollars
956 so three million – three hundred thousand dollars. So three hundred thousand dollars
957 divided by four million would have been our cost.

958

959 **Governor Otter:** To manage. And the value of the land – of the land is –

960

961 **Director Bacon:** Kathy, anybody know the value of the land?

962

963 **Secretary of State Ysursa:** Upwards of two hundred and fifty million.

964

965 **Deputy Director Opp:** Governor, members of the Board, the value would be over two hundred
966 and fifty million dollars.

967

968 **Secretary of State Ysursa:** (inaudible)

969

970 **Governor Otter:** Thank you.

971

972 Is there further discussion on the motion?

973

974 **Superintendent Luna:** Governor.

975

976 **Governor Otter:** Mr. Luna.

977

978 **Superintendent Luna:** Couple points that I – first off, you know, this is the second or third time
979 we've discussed this easily, and if – if what the Subcommittee has put forward as a

980 proposal – if the rent is too low, or if it doesn't meet our constitutional obligation, then I
981 would be interested in hearing a motion that does. And – and we've asked and had this
982 conversation before. If this motion does not, then what – then, again, I would be
983 interested in entertaining a motion that does meet – that – where the rent is high
984 enough where we are meeting our constitutional obligations. And we haven't heard
985 one. And apparently we're not going to hear one today. So all we have before us is this
986 – is the motion of the Subcommittee.
987
988 The other point, Governor, is we're never going to maximize earnings for these
989 properties, or this asset, until we sell them. And not just unify title, but to sell them in a
990 market savvy manner, as we've discussed, because we know that even if we could get
991 six percent for return on these properties that we know we can make more than that if
992 we get out of these investments and invest this money elsewhere. We're never going to
993 see true market rent, or true market value, as long as there's this comingling of
994 government and private sector. It's never worked, and more government intrusion is
995 not the answer.
996
997 So the – if we're truly interested in maximizing the benefit for the beneficiary, then we
998 have to move to sell these properties, or trade them for other assets, but we – we've
999 been doing this for decades; we've never realized our full return to benefit the
1000 beneficiary, and I would assume that because of the direction we gave the Department
1001 at our last meeting that we will be moving towards liquidating our – these assets and
1002 moving that – those moneys into other investments that will earn us far more than the
1003 four or six percent that we are trying to gain today.
1004
1005 **Governor Otter:** I would agree with your summation, and especially it's been pointed out to me
1006 – especially on recreational properties. Especially.
1007
1008 Further discussion.

1009

1010 Hearing no further discussion, the question is, shall the motion made by the Chairman
1011 of the Subcommittee, Mr. Ysursa, be adopted.

1012

1013 That motion is number one, the four-ten-five; four percent, ten-year average, a five-year
1014 phase-in. Second part of that motion is either ten percent gross or fifty percent of the
1015 net, whichever is greater, on premium quote, unquote, premium rent – leaseholder
1016 value.

1017

1018 You've heard the motion. The Secretary will call the roll.

1019

1020 **Recording Secretary:** Secretary Ysursa.

1021

1022 **Secretary of State Ysursa:** Aye.

1023

1024 **Recording Secretary:** Attorney General Wasden.

1025

1026 **Attorney General Wasden:** No.

1027

1028 **Recording Secretary:** Controller Jones.

1029

1030 **Controller Jones:** No.

1031

1032 **Recording Secretary:** Superintendent Luna.

1033

1034 **Superintendent Luna:** Aye.

1035

1036 **Recording Secretary:** Governor Otter.

1037

1038 **Governor Otter:** Aye.

1039

1040 **Recording Secretary:** Three, two, passed.

1041

1042 **Governor Otter:** The motion shows three ayes, two nays, the motion prevailed.

1043

1044 Mr. Secretary.

1045

1046 ---

1047 End of this agenda item.

1048 ---

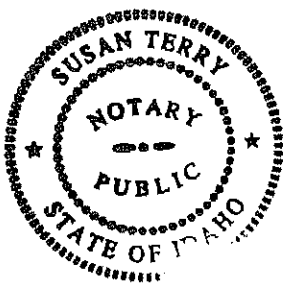
TRANSCRIBER'S CERTIFICATE

STATE OF IDAHO)
) ss.
COUNTY OF ADA)

I, Susan Terry, a Notary Public in and for the State of Idaho, residing at Nampa, County of Canyon, State of Idaho, do hereby certify:

That the foregoing transcript of the proceedings relating to the matter of *Recommendation of the Cottage Site Subcommittee* for the State Board of Land Commissioners of the State of Idaho, recorded on March 16, 2010, was produced via audio recording and thereafter reduced to typewriting by me, and that the foregoing thirty-seven (37) pages contains a full, true and correct record of the oral conversations related to said matter, to the best of my ability, given the speakers' enunciation and the quality of the audio recording itself.

I hereunto set my hand and seal this 17th day of March 2010.



Susan Terry

SUSAN TERRY
Notary Public for Idaho
Residing at Nampa, Idaho
My Commission Expires 8-30-2011

Exhibit 43

Idaho Department of Lands Cottage Site Considerations & Recommendation (draft circulated to Land Board staff on March 9, 2010)

IDAHO DEPARTMENT OF LANDS
COTTAGE SITE CONSIDERATIONS & RECOMMENDATION

Considerations:

- Article IX, Section 8, of the Idaho Constitution provides that the State Board of Land Commissioners manage state endowment lands in such manner as will secure the maximum long-term financial return to the endowed institutions.
- Trust principles established in Idaho code and case law (*Idaho Watersheds Project v. State Bd. Of Land Com'rs, 1999*) require the Board to manage trust assets with an undivided loyalty to the trusts.
- 58-310A(2), Idaho Code establishes that leases for single family, recreational cottage sites and home sites shall not be subject to conflict applications and auctions.
- 58-310A(3), Idaho Code further requires that, in the absence of the conflict auctions, the board insures that each leased lot generates market rent throughout the duration of the lease.
- An Attorney General's opinion of August 5, 2009 indicates that a reviewing court would likely find the prohibition of conflict auctions in 58-310A a violation of the Idaho Constitution because disposals of endowment lands must occur by public auction.
- Absent competitive bidding, the Board must establish a surrogate to determine market rents. Studies conducted over the last twenty years, including Duffield, Knipe, and McFadden, indicate rental rates need to be in the range of four to six percent of land value.
- The surrogate studies indicate that as rental rates approach market rents, leasehold values will approach zero. Therefore, assumptions about rental rates relative to market rates can be derived by tracking leasehold values.
- The economic theories and rates expressed in the surrogate studies remain accurate and have been recently validated by O'Laughlin and Anderson.

Recommendations:

1. The Board establish a rental structure that achieves rental rates between four and six percent of land value, with the ability for the Board to change the rate from year to year.
2. The Board establish a mechanism in the lease that will allow the Department to monitor leasehold values during lease assignments and make annual recommendations to the Board for adjustments to the rental rate.
3. The Board direct the Department to determine land values annually as is currently done (county assessed value at Payette Lake and indexed appraisals at Priest Lake), and include lease language that allows the land valuation to be done by a qualified employee of the State, a county assessor's office, an MAI appraiser or SRI appraiser, at the sole discretion of the State. This authority provides flexibility in the event the state is unable to obtain assessor data or encounters any other impediment in determining value.

IDAHO DEPARTMENT OF LANDS
COTTAGE SITE CONSIDERATIONS & RECOMMENDATION

4. The Board eliminate premium rent collection once it deems rental rates to be reflective of market.

5. The Board consider whether the provisions of 58-310A that prohibit conflict applications and auctions for cottage sites is appropriate and requires legislative action to repeal.

6. Absent competitive bidding, the Board consider whether the provisions of 58-310A that requires the Board to generate market rent for each leased lot throughout the duration of the lease is reconcilable with the prohibition against conflict auctions, or even possible.

DRAFT

Exhibit 44

Letter from Attorney General Lawrence Wasden to Governor C.L. "Butch" Otter (Feb. 12, 2010)

STATE OF IDAHO

OFFICE OF THE ATTORNEY GENERAL

LAWRENCE G. WASDEN

February 12, 2010

VIA HAND DELIVERY

The Honorable C. L. "Butch" Otter
Governor
State of Idaho

Dear Governor Otter:

I request that the attached documents be included in the official record of the Land Board's deliberation on the Cottage Site Subcommittee Report:

1. Attorney General Opinion 09-01;
2. Anderson and Watson Report to Idaho Attorney General Regarding Cottage Site Leases;
3. Anderson and Watson Analysis of Subcommittee's Recommendation to the Idaho Board of Land Commissioners; and
4. Letter to Attorney General Lawrence Wasden from Director George Bacon, Department of Lands, dated February 12, 2010, with attachments.

Thank you for your assistance.

Sincerely,

LAWRENCE G. WASDEN
Attorney General

LGW:dd

attachments

P.O. Box 83720, Boise, Idaho 83720-0010
Telephone: (208) 334-2400, FAX: (208) 854-8071
Located at 700 W. Jefferson Street, Suite 210