



STATE OF IDAHO

OFFICE OF THE ATTORNEY GENERAL

BOISE 83720

January 10, 1985

JIM JONES  
ATTORNEY GENERAL

TELEPHONE  
(208) 334-2400

The Honorable Terry Sverdsten  
Idaho State Senator  
District #3  
Statehouse  
Boise, ID 83720

THIS IS NOT AN OFFICIAL ATTORNEY GENERAL OPINION  
AND IS SUBMITTED SOLELY TO PROVIDE LEGAL GUIDANCE

Dear Senator Sverdsten:

During the last legislative session you raised some questions concerning timber sales on state endowment lands and requested that this office provide you with some legal guidance on the issue prior to the 1985 legislative session. Your request has been forwarded to me for response.

ISSUE:

Can the State of Idaho deduct from the gross proceeds of an endowment timber sale the administrative costs of conducting the sale without violating the endowment provisions of the Idaho Admission Bill or the Idaho Constitution?

CONCLUSION:

The Idaho Admission Bill does not appear to preclude recovery of timber sale administrative expenses from endowment trust proceeds. However, although several credible arguments can be made for the proposition that the Idaho Constitution ~~does not~~ prohibit the deduction of timber sale expenses from the gross proceeds of a sale, it appears that a 1977 Idaho Supreme Court decision may prevent such practice.

ANALYSIS:

Before addressing your specific question, the present method of accounting for revenues and expenses on endowment timber lands should be reviewed. Currently, the cost of

preparing timber sales together with general timber management expenses are paid for from the general funding of the department of lands, but the money earned is placed in the endowment fund. Capital expenditures which enhance the market value, productivity, and income capacity of specific endowment lands are paid for by the "ten percent fund." This is a special fund consisting of a percentage of the income from specific endowment lands, which can only be used as a reinvestment upon the lands from which the monies accrued. Idaho Code § 58-1140. Finally, appraisal and scaling costs are defrayed by the use of a surcharge on timber sales. Idaho Code § 58-301 and Idaho Code § 58-416.

The State of Idaho holds endowment lands under an express trust for the benefit of the designated beneficiaries. Idaho Const. art. IX, § 8; Ervien v. United States, 251 U.S. 41, 64 L.Ed. 128 (1919). If there are no conflicting terms or purposes expressed in the enabling act or the state constitution, it is generally accepted that the state is bound by the rules applicable to private trusts. Barber Lumber Co. v. Gifford, 25 Idaho 654, 139 P. 557 (1914); United States v. Swope, 16 F.2d 215 (8th Cir. 1926); Oklahoma Education Ass'n, Inc. v. Nigh, 642 P.2d 230 (Okla. 1982). Thus, resolution of the issue posed requires an examination of the language of both the Idaho Admission Bill and the Idaho State Constitution.

Sections 4, 5, 6, 8, 10, 11, and 12 of the Idaho Admission Bill enumerate the state land grants and their purposes. An examination of the Admission Bill discloses no express provision requiring the state to bear the costs of administration from its general revenues. The language in sections 5, 8, and 12, however, might arguably be interpreted as requiring the state to assume the costs of administration.

The three critical phrases in the Admission Bill that might be construed as requiring the state to assume administrative expenses associated with state endowment lands are as follows: First, section 12 states that, "Lands granted by this section shall be held, appropriated, and disposed of exclusively for the purposes herein mentioned. . . ." Second, section 8 requires that income generated by university lands be used "exclusively for university purposes." Finally, both sections 5 and 8 require that "proceeds [from sale of school endowment lands are] to constitute a permanent school fund."

Though it can be argued that exclusively means no other use and proceeds means gross proceeds, c.f., Opinion of the Justices, 47 So.2d 729 (1950), most courts and state legislatures that have considered the issue interpreted the words so as not to preclude the state from recovering administrative expenses. See, e.g., United States v. Swope, 16 F.2d 215 (8th Cir. 1926); State ex rel. Greenbaum v. Rhoades, 4 Nev. 312 (1868); Bourne v. Cole, 53 Wyo. 31, 77 P.2d 617 (1938); Wash. Att'y Gen. Op. 59-60, No. 150 (1960); 32 Mont. Att'y Gen. Op. No. 8 (1967).

New Mexico is the only state that has litigated the administrative expense issue extensively. Its experience is particularly relevant to our state for two reasons. First, it is the only state where both federal and state courts have interpreted an enabling act. Since the grant involves both federal and state interests, the litigation gives a fairly accurate view of the intent behind the state land grants. Second, the section of the New Mexico Enabling Act being construed by the courts is substantially similar to Idaho's Admission Bill. For example, neither act makes reference to administrative costs; they merely require that the "proceeds" be placed in a permanent fund and prohibit the commingling or use of the fund for any other object than the one specified in the grant.

The first interpretation of the New Mexico Enabling Act occurred in 1919. At issue was a state statute directing the state land commission to expend three percent of the annual proceeds from the trust lands to publicize the advantages of living in New Mexico. In Ervien v. United States, 251 U.S. 41, 64 L.Ed. 128 (1919), the Supreme Court held Congress could not have intended for the proceeds of such trust lands to be used for general governmental purposes.

Approximately seven years later, the United States Eighth Circuit Court of Appeals considered the constitutionality of a New Mexico statute that appropriated twenty percent of the income derived from any trust lands for the purpose of paying expenses incurred in the administration of the lands. In United States v. Swope, 16 F.2d 215 (1926), the court upheld the statute. Relying on the trust analogy in Ervien, the court stated:

It is conceded that the grant of lands was upon an express trust. The rule of construction of such trusts is that the absence of a provision for the payment of the reasonable and proper costs and expenses of administering the trust does not throw such expense upon the shoulders of the trustees, but the trustees have an inherent equitable right to be reimbursed for such expenses incurred.

Id. at 217. The persuasiveness of the Swope opinion becomes more apparent after considering that the federal government had specifically required New Mexico to bear the costs of administration of lands granted for an agriculture or a mining college but made no express reference to such costs in the other grants. (See also, State ex rel. Greenbaum v. Rhoades, 4 Nev. 312 (1868). Nevada's enabling act also resembles Idaho's Admission Bill.)

The last two cases involving the New Mexico Enabling Act make explicit the implicit rule developed in Ervien and Swope. In State v. Mecham, 250 P.2d 897 (1952), the New Mexico Supreme

Court struck down a statute that appropriated five percent of the trust funds to defray general governmental expenses. After considering Ervien and Swope, the court held that Congress did not intend for the trust funds to be used for general administrative expenses. In United States v. State of New Mexico, 536 F.2d 1324 (10th Cir. 1976), however, the United States Court of Appeals reconfirmed the state's right to reimbursement for expenses arising exclusively from the administration of trust property.

Since the Idaho Admission Bill constitutes a federal grant, the grantor's intent should be controlling. Thus, the fact that two federal courts have interpreted an enabling act similar to Idaho's as allowing the deduction of administrative expenses resulting from the management of trust property provides a significant basis for arguing that the Idaho Admission Act does not preclude such action. Whether the Idaho Constitution precludes such deductions, however, is less certain.

The sections of the constitution critical to analysis of this issue are as follows: Article IX, § 8 of the Idaho Constitution provides for the disposition of state endowment lands. Section 8 states that the State Board of Land Commissioners shall provide for the sale of the land and "for the sale of timber. . .and for the faithful application of the proceeds thereof in accordance with the terms of said grants. . . ." Further, the board is charged with securing the "maximum long-term financial return. . . ." Article IX, § 4, defines the public school fund as including "the proceeds of such land as has heretofore been granted, or may hereafter be granted, to the state by the general government as school lands. . . ." Finally, art. IX, § 3, requires that the fund is to remain "inviolate and intact forever." It states, further, "[n]o part of this fund, principal or interest, shall ever be transferred to any other fund, or used or appropriated except as herein provided."

As in the Idaho Admission Bill, the Idaho State Constitution contains no specific provision requiring the state to bear the expense of administration of trust lands. If a duty to bear expenses is to be found, it must be based upon an interpretation that proceeds means gross proceeds not net proceeds.

Although the Idaho Supreme Court did not define "proceeds" in the case of Moon v. Investment Bd., 98 Idaho 200, 5760 P.2d 871 (1977), the court's decision in Moon poses a substantial impediment to the use of sale proceeds to pay the expenses of the sale. The following discussion will first consider the Moon decision and then will detail some arguments supporting a more liberal interpretation of the term "proceeds."

The Idaho Supreme Court has taken a very protective stance toward the endowment lands. In State v. Peterson, 61 Idaho 50, 97 P.2d 603, 604 (1939), the court said:

[T]hese public school endowment funds are trust funds of the highest, most sacred order, made so by Act of Congress and the Constitution so considered by members of the constitutional convention and so recognized and declared by this court.

Thus, it is not too surprising that the supreme court strictly construed art. IX, § 3, of the Idaho Constitution in Moon.

At issue in Moon was an appropriation of trust income for the purpose of defraying the investment board's trust management expenses. In a per curiam opinion with Justice Shepard dissenting, the court held that the legislation authorizing the transfer violated art. IX, § 3, of the Constitution of the State of Idaho. Id. at 201. Justice Shepard, in a persuasive dissent, argued that there was a presumption of constitutionality of legislative action. Id. He found it difficult "to conceive that the drafters of the constitution, while specifically providing that the corpus of the public school funds should remain 'inviolable' in requiring the makeup of all losses to said fund, also meant that the gross earnings from the investment are similarly 'inviolable' from all costs reasonably incurred in the investment process. . . ." He added, "[i]n my judgment the general law is clear that a trustee is entitled to reimbursement or setoff of those expenses reasonably incurred in the investment and administration of the trust corpus." Id.

Though the Moon decision is distinguishable because it involved the money in the school fund rather than what is to be deposited into the fund (gross or net proceeds), the court's superficial treatment of § 3 suggests that it will be an uphill battle to convince the court that administrative expenses are a proper deduction. Yet, there are four credible arguments for such an interpretation.

First, nothing in the constitutional convention suggests such a restrictive reading. The entire debate centered on the issue of whether the endowment lands should ever be sold. There was no discussion of expenses of administration per se. In fact, the expense of administration was only mentioned twice, and both times it was assumed by the speaker that the administrative expenses would be deductible from the proceeds. 1 Idaho Const. Conv. 739, 744-45 (1889) (Mr. Claggett and Mr. Grey speaking). While these passing comments alone offer little assistance in ascertaining the drafters' intent, when combined with the absence of debate on the issue and the drafters' specific reference in art. IX, § 8 to, applying the grants to the purposes for which Congress made them, they suggest that the convention did not intend a more restrictive interpretation than did Congress. If the drafters had intended a more restrictive reading they could have clearly expressed their intent. Therefore, the term "proceeds" is subject to being interpreted in light of Swope and Rhoades. See, State ex rel. Forks Shingle Co., Inc. v. Martin, 83 P.2d 755 (Wash. 1938).

Second, since the drafters used the legal term "trust" in art. IX, § 8, it must be assumed that they were familiar with the existing body of trust law and the right of setoff. This assumption would not be inconsistent with the protective attitude of the drafters because trust rules place well defined limitations on diversion of trust assets. Impliedly, the Washington Supreme Court adopted this reasoning in upholding a statute that directed that trust properties bear the timber sale costs. State ex rel. Forks Shingle Co., Inc. v. Martin, supra.

Third, art. IX, § 8, requires the board to protect the lands for the purpose granted. Presumably, the federal government and the drafters of the state constitution would not have relied on the uncertain nature of future appropriations by the state to guarantee the preservation of the trust lands. Uppermost in their minds was a perpetual base of funding for the benefit of all the designated beneficiaries.

Fourth, all of the states operating under similar constitutional provisions have assumed that administrative expenses are deductible from the trust assets, and their interpretation should be given some deference. See, e.g., Wash. Rev. code § 76.65.030 (1981); Wash. Att'y Gen. Op. 59-60, No. 150 (1960); 32 Mont. Att'y Gen. Op. No. 8 (1967).

A review of the Idaho Code suggests that the legislature has followed the uniform practice. For example, Idaho Code § 58-140 appropriates ten percent of the monies received from the sale of standing timber, from grazing leases and from recreation site leases for the maintenance, management, and protection of state-owned lands. Interestingly, the statute goes on to adopt the Ervien--Swope reasoning to require that the proceeds only be applied to the trust lands from which they were generated.

In conclusion, the Idaho Admission Bill does not appear to preclude recovery of timber sale administrative expenses from endowment trust proceeds. However, although several credible arguments can be made for the proposition that the Idaho Constitution does not prohibit the deduction of timber sale expenses from the gross proceeds of a sale, it appears that a 1977 Idaho Supreme Court decision may prevent such practice.

If this office can be of further assistance, do not hesitate to contact us.

Sincerely,



Rinda Ray Just  
Deputy Attorney General  
Natural Resources Division