



STATE BOARD OF LAND COMMISSIONERS

Dirk Kempthorne, Governor and President of the Board
Ben Yursa, Secretary of State
Lawrence G. Wasden, Attorney General
Keith L. Johnson, State Controller
Marilyn Howard, Superintendent of Public Instruction

Winston A Wiggins, Secretary to the Board

Final Minutes Regular Land Board Meeting January 13, 2004

The regular meeting of the Idaho State Board of Land Commissioners was held on Tuesday, January 13, 2004 in Boise, Idaho. The meeting began at 8:02 a.m. The Honorable Dirk Kempthorne presided. The following members were present:

Honorable Secretary of State Ben Yursa
Honorable Attorney General Lawrence G. Wasden
Honorable State Controller Keith L. Johnson
Honorable Superintendent of Public Instruction Marilyn Howard

Secretary to the Board Winston A Wiggins was absent for this meeting.

Matthew Haertzen, CFA, Manager of Investments, Endowment Fund Investment Board, provided background information for the regular agenda item.

• REGULAR SESSION

➤ **To Consider the Recommendations of the Endowment Fund Investment Board Regarding Distribution Policy** – *Presented by Matthew Haertzen, CFA, Manager of Investments*

EFIB Recommendation: That the State Board of Land Commissioners approve a 4.0% spending policy beginning in fiscal year 2005 as recommended by the Endowment Fund Investment Board. This reduction is recommended due to the prolonged equity market drop and decline in timber revenue.

DISCUSSION: Governor Kempthorne stated he met with Mr. Haertzen earlier on this matter, and he has a couple of concerns. One concern is when you look at the pooled entities, there is a larger percentage impact to those agencies. For example, included in the pooled fund is State Hospital North. For State Hospital North to make the reduction from 7.5% to 4% is a 12.4% change in the FY 2004 general fund appropriation. The Division of Veterans' Services is a 14.6% change and State Hospital South is an 8.5% change. With regard to public schools, if we have the opportunity to go to 5% for this coming year, as opposed to 4%, they can have full expectation of those payments. Then the following year we would go to 4% and still meet our ultimate objective. So that is the first question. Mr. Haertzen stated he believes the 5% payout can be met, but that counts on receipts coming in exactly as expected, particularly on the Lands side. That is the big number for the earnings reserve pool. We do not have a lot of play factor at 5% so there is some risk. Governor Kempthorne stated the difference between 4% and 5% is roughly \$4.5 million to public schools.

Another option discussed with Mr. Haertzen is the concept of taking the pooled and going to 7% for 2005, 6% for 2006, 5% for 2007 and then 4% for 2008. Public schools would go to 5% in 2005 and then to 4%. Governor Kempthorne asked Mr. Haertzen where he would put the probability of meeting the payout if it went to 5%. Mr. Haertzen stated he believes we can meet 5%. However, there is some risk that the payout could be a little short.

Dr. Howard commented when the Land Board meets, they put on their Land Board hats. The Land Board worries about bouncing around from one year to the next. However, when she puts on her Superintendent hat, she would like to have the 5% this year because of the other reductions going out to schools. It would be a source of revenue. But it worries her a bit on the aspect of long-term planning. That is, with Land Board hats on, what the Board was trying to think through earlier. Part of that had to do with how long it would take to get that sense of security that the reserve fund was intended to give. Mr. Haertzen stated he feels a 1% difference is a sufficient tradeoff if it helps with school budgeting in a difficult year. It will not have a huge impact on the fund, and it can be made up over the long term without affecting the long-term stability in the growth of the earnings reserve.

Dr. Howard commented that under our present system, the Land Board and the funds are picking up the cost of Lands, which previously were paid out of general funds. There has been a \$10 million reduction each year from money that might have been available for this kind of distribution because of the Department of Lands costs. She asked if there is any possibility of the Legislature picking up a portion of the cost of Lands, as they did in the past, to share this burden. Governor Kempthorne responded he would not pin the Board's decision on the fact that they would be able to do so. The budget is tight in all categories.

Dr. Howard commented that another factor is Lands personnel are state employees and that needs to also be factored into deliberations. We are not only dealing with the endowments to the schools, but we are also in charge of paying a workforce out of those funds. That is not a discussion we have had in any depth at any time about budget. So another issue is growth and how it is going to accommodate not only the needs of schools and what we might project for next year, but also acknowledging that we have people doing work who have to be treated equitably.

Attorney General Wasden asked Mr. Haertzen how confident he feels that the 5% payout can be met. Mr. Haertzen stated if a probability curve of confidence levels were assigned, he would say 95+%. In addition, Attorney General Wasden commented there is 5% on school funding, and there is a graduated level on the pooled funds. How much additional time will that cause in terms of health to the fund that we are trying to reach? Instead of going to 4% now, a graduated process is being suggested which will extend the time at which we are going to have what we feel is a healthy fund. How much is that going to extend it, and how much more risk does that graduated level on the pooled funds cause? Mr. Haertzen stated it is about \$6 million the first year and then it gradually goes down from there. The pooled, just from the nature of the lands that are owned in the pooled endowment fund, have a little more cushion in the earnings reserve right now. That is why the 7, 6, 5, 4 schedule can be met. Mr. Haertzen stated he is comfortable with the Governor's recommendation of taking the steps on the pooled side because we are starting with a larger buffer. On the public school side, that buffer is completely gone. Controller Johnson stated we can revisit this issue in the future if we do not meet those expectations. We may have to escalate the stair-stepped approach. Mr. Haertzen concurred.

Secretary of State Ysursa asked if the payment in July 2004 would be met for public schools at the original level. Mr. Haertzen stated at this point the forecast is that the payment will be about \$2 million short at the 7.5% payout level. Secretary of State Ysursa commended Governor Kempthorne for focusing attention on the impact of a cut to a small agency.

Dr. Howard commented that she supports the 5% payout because, as others are doing, this is phasing down. Governor Kempthorne added when you consider going from 8.5% to 8%, 7.5% and then to 4%, it is a glide slope. And then for the pooled funds – 7, 6, 5, 4. Everyone is on notice.

They know the schedule now that they will need to work into their future budgets and that we are all going to arrive at 4%. That is where we will level off and stay until we reach the ultimate objective.

Based on the Governor's 2005 proposed budget, Dr. Howard stated we are looking at numbers that are listed for 5% this year. But next year she does not understand whether we would be considering numbers projected for the 4% or whether that figure would fluctuate depending on what happens. Mr. Haertzen stated that figure will fluctuate because the percentage is calculated on a three-year moving average. We will include the June 30, 2004 number in that calculation. For clarification, Governor Kempthorne asked Dr. Howard if she is referencing the actual dollar amount and not the percent. Dr. Howard stated that is correct. She is thinking about what could be expected in that category. If we have two years that are relatively flat, then that is good to know. Mr. Haertzen added one point on that is when we incorporate the June 30, 2004 value. When you take 4% of that it is actually going to be a higher number barring a collapse between now and June 30.

Governor Kempthorne commented he appreciated the last joint meeting with the Endowment Fund Investment Board. He feels we are all beginning to see things the same way and understand one another's responsibilities. He also complimented Mr. Haertzen for doing an excellent job managing this, but, more importantly, for his ability to communicate the information in layman's terms.

Board Action: A motion was made by Attorney General Wasden that the Endowment Fund Investment Board payout be reduced in FY 2005 from 7.5% to 5% for public schools; in FY 2006, the payout will be reduced to 4%. The pooled resources in FY 2005 will be reduced to 7% in FY 2005 followed by a reduction to 6% in FY 2006, 5% in FY 2007 and 4% in FY 2008. Secretary of State Ysursa seconded the motion. The motion carried on a vote of 5-0.

There being no further business to come before the Board, the meeting adjourned at 8:27 a.m.

IDAHO STATE BOARD OF LAND COMMISSIONERS

/s/ Dirk Kempthorne
President, State Board of Land Commissioners and
Governor of the State of Idaho

/s/ Ben Ysursa
Ben Ysursa
Secretary of State

/s/ Winston A Wiggins
Winston A Wiggins
Director

The final minutes above were approved by the State Board of Land Commissioners at the February 10, 2004 regular Land Board meeting.