

April 15, 2024

Kemp Smith
Idaho Department of Lands
300 N. Sixth Street
PO Box 83720
Boise, ID 83702

RE: Comments for Negotiated Rulemaking for Docket 20-0313-2401 -Cottage Sites Administration

Dear Mr. Smith:

These are comments regarding the above noted rulemaking for administration of cottage sites. I attended the public meeting on March 27, 2024 and offered suggestions and comments at the meeting. These comments are intended to supplement the discussions at the meeting which were recorded for the record.

Cottage sites are a unique component of the state's endowment trust lands. They represent the highest value per acre, provide the highest revenue per acre, have the highest appreciation rate, and are the most economical of lands to administer. They are special. Unfortunately they are burdened by politics at its worst.

Going back even prior to the days of the old Eberle Berlin land trade, they have been treated as a political perpetuation tool, being conveyed from the endowment as political favors and/or or as a means to avoid having to deal with fiduciary obligations. The mismanagement of cottage sites was exemplified by allowing leasing at less than fair rates for decades. Unwilling to meet its fiduciary obligations, the Land Board eventually hit upon a solution- just get rid of them and save Land Board members and the IDL the overwhelming difficulty of having to send a bill to leaseholders. This mismanagement of cottage sites has been aided by a few lines of regulations which fail to provide any significant direction or control or process on how to administer the sites and ensure endowment beneficiaries are protected. Unrestrained by the sadly deficient regulations, the Land Board and the IDL have embarked on a multi-years effort to dispose of cottage sites—regardless of the financial impacts to the endowment beneficiaries. The Land Board and the IDL have refused to evaluate or analyze the disposals to date or reconsider their ill-advised decision. Now, instead of a rulemaking to deal with obvious problems, the negotiated rulemaking has been driven by entirely different motivations.

As discussed at the March 27 negotiated rulemaking session, cottage site mismanagement continues unabated. Here is what we have seen in only the past few years:

The Land Board breach a valid existing lease—a lease signed by the Governor and the Secretary of State and approved by the Attorney General's office- of a cottage site and other endowment land based on unexplained reasons after political pressure was brought to bear. This caused the IDL to pay over

\$350,000 in damages to the lessee. The breach of the lease damaged the reputation of the Land Board and the IDL and called into question dozens of existing leases;

The IDL accept applications and fees to lease cottage sites only to refuse to process the applications;

The IDL refuse to conduct conflict auctions for cottage sites in order to protect existing lessees;

The IDL allow an appraiser to increase the value of improvements to benefit an existing lessee seeking to buy his leased cottage site;

The IDL implement auction procedures for cottage sites to benefit existing lessees and dissuade competing bids;

The IDL allow the existing VAFO process to be used to benefit existing lessees, allow conflicts of interest by having a single appraiser value cottage sites and lessee improvements, and solicit potential uses for cottage sites which the IDL had no intention of permitting.

Existing regulations helped allow these abuses to occur. The ongoing negotiated rulemaking provides an opportunity to address the problems identified above, yet no effort has been made to do so. Instead, the process has been used to simply reduce the number of words in the current regulations—not a single substantive measure has been proposed.

The negotiated rulemaking has thus far been a façade. It is, rather than a negotiated rulemaking, simply a notice and opportunity to submit comments. Responses, discussions, or feedback by the IDL as part of the process are nonexistent. Ostensibly announced as a means of complying with Executive Order 2020-1, the draft changes to the current regulations do not even attempt to comply with the order. The order requires a retrospective analysis of the current rule to ensure it is meeting its purposes. This is followed by a prospective analysis of any proposed changes or new rules to ensure the changes meet certain objectives. IDL acknowledges it did not do any retrospective analysis, and the prospective analysis form posted by IDL is anything but an analysis. IDL admits its only effort was directed towards reducing the number of words in the existing rule. IDL's explanation? "We just did what DFM told us." It is not clear that anyone at IDL has even read the order. (A Public Records Request to DFM was ignored by DFM.) A rulemaking effort such as this and a draft rule as currently proposed by IDL ignores the identified problems especially those with the VAFO auction process. This creates obvious fiduciary obligation concerns and indicates IDL does not understand what a fiduciary obligation entails. Adoption of the current draft rule by the Land Board would do likewise.

The existing rule for administering cottage sites has been demonstrated to be completely inadequate to address the arbitrary management of cottage sites by the IDL. The draft rule only enhances the problems and does nothing to meet the fiduciary obligations of the IDL and the Land Board. The VAFO auction process in particular works to the financial advantage of existing lessees and disadvantage of the endowment beneficiaries. The negotiated rulemaking process should be a good faith effort to address problems, not a game of "whack-a-word". The IDL needs to go back to the drawing board and do a true negotiated rulemaking—after it completes its retrospective analysis.

Regards,

Bruce Smith

2809 S Shadywood Way

Boise, ID 83716

Attachment 1: March 27,2020 Letter to Land Board Re-Investment Subcommittee

Cc: Appropriate Parties

Bruce M. Smith
2809 S. Shadywood Way
Boise ID 83716

March 27, 2020

Governor Brad Little
Attorney General Lawrence Wasden
Mr. Irving Littman
P.O. Box 83720
Boise, ID 83720

Re: Endowment Reinvestment Subcommittee
Sale of Public Lands/Cottage Sites and Commercial Property

Dear Members of the Endowment Reinvestment Subcommittee,

The recent deliberations and data reviewed by the Endowment Reinvestment Subcommittee (Committee) have been helpful in understanding the current status of the state endowment funds and related endowment land issues. The Committee has unearthed several important questions and is to be commended for its efforts. In fact, the discussions, questions, and dialogue among the Committee members have exceeded discussions and dialogue among the collective Land Board members during the entirety of the year. One of the most obvious outcomes from the Committee's efforts is that it is time to end the process of selling leased and unleased cottage sites. Doing so is a matter of fiduciary obligations and being a prudent investor. The Land Board should also reconsider the selling of commercial properties

I have had the opportunity to observe many of the deliberations of the Land Board and the Committee, at least those that have been public. Since the Committee is preparing to provide recommendations to the entire Land Board, it is particularly relevant at this stage to consider some of the more salient aspects of the Committee's deliberations. Committee members have made the following points:

1. Governor Little correctly noted the importance for periodic review of underlying facts, assumptions, and data when making investment decisions dealing with endowment lands. Annual review of the investment hurdle rate was one telling example.
2. Attorney General Wasden and Land Board counsel noted the Land Board is limited in some of the actions it can take such as the prohibition on selling timberlands, and that there are potential conflicts between statutory and constitutional obligations that would require the Land Board to resolve the conflicts as part of its decision making. For

example, redefining timberlands as cottage sites or another class so they could then be “sold” would certainly be unconstitutional, a breach of fiduciary obligations, and the Prudent Investor Rule. The Attorney General noted fiduciary obligations extend to present and future beneficiaries.

3. Governor Little, Attorney General Wasden, and Mr. Littman all emphasized the fiduciary obligations of the Land Board members, as well as the critical nature of the Prudent Investor Rule.
4. All three members acknowledged that political considerations can play no role in investment decisions. The endowment investment advisor agreed. Mr. Littman also pointed out questions regarding whether the Land Board could consider tax implications for counties. The unanimous response was “no”. The same principle applies to existing cottage site lessees. For example, on one leased cottage site in the Payette Lake area, a 2019 appraisal valued the lot at \$1,008,000.00. A second appraisal in 2020, 12 months later, valued it at only \$800,000.00 -- in a market that is supposed to be increasing. The effect is to shift at least \$208,000.00 of “value” to the lessee, thus benefitting the lessee at the expense of the endowment. Problems with the VAFO program are numerous and serious.

The above details of the Committee’s deliberations require that the sale of public lands such as leased and unleased cottage sites be ended. The sale of commercial properties likewise needs to be carefully considered. In other words, the Land Board needs to slow down, take a deep breath, and think about this before permanent mistakes are made. Business as usual will not do and will not meet Land Board fiduciary obligations. Each Land Board member needs to make an independent, individual assessment of this situation and their own obligations, in particular since some members were not on the Board in 2010.

The beginnings of the current cottage site sales program, as described in the 2010 Heartland LLC report, began around 2009. All Land Board members at the time recognized the program was designed largely as an ill-disguised effort to transfer ownership of state cottage sites at Payette Lake and Priest Lake to current lessees. The Heartland report uses statements, assumptions, and data from 2010 and prior years to justify its recommendations. It also references the political aspects of the decision to sell cottage sites. The Heartland report has never been revisited or updated. Continuing to make investment decisions using the outdated Heartland report only exacerbates the original concerns, including the political implications embedded in the report’s recommendations. The current Land Board is not bound by and should not be making investment decisions using outdated assumptions by some previous Land Board members.

Cottage sites and commercial properties represent individual asset classes that add critical balance and diversification to the endowment portfolio. These two asset classes provided, and have the potential to continue providing, the highest returns per acre of any asset class. Their rates of return are approximately three-to-five times that of other classes. For the past three years, cottage sites and commercial properties have appreciated approximately three-to-four times the rate of other asset classes. Selling off these public lands is an irretrievable

disposition of valuable endowment assets. The Land Board can buy stocks and bonds all day long – not so with cottage sites at Payette and Priest Lakes. Cottage sites, once sold, are likely gone forever, thus foreclosing significant revenues that out compete all other classes.

Governor Little pointed out in the March 12, 2020 meeting that approximately 80% of cottage sites and commercial properties have been disposed of since 2011. Over 342 cottage sites at Payette and Priest Lakes have been sold, the vast majority being sales at no more than the minimum appraised value to existing lessees holding potentially illegal leases. For most sales to existing lessees under the VAFO program, there is no competitive bidding at all, in part due to questionable auction procedures. These circumstances alone should alert a fiduciary/prudent investor and generate scrutiny and questions as to substance and process. That sales have continued for so many years with no review of underlying assumptions, data, and procedures should be a concern for the Land Board, with constitutional concerns at the fore. No fiduciary/ prudent investor would sell, through constitutionally suspect procedures, the most valuable, highest returning assets from their “Sacred Trust” portfolio in 2020 based on 2010 assumptions and data that have not been updated or reviewed.

The Committee has had an opportunity to examine many aspects of the endowment in much greater detail than the Land Board as a whole. The Committee needs to recommend, and the Land Board needs to take, immediate action to stop the sale of public land cottage sites and commercial properties. The Land Board needs to make certain its information is timely, and that its actions comply with constitutional and statutory obligations before even considering selling these lands. Each member of the Land Board needs to fully understand and grasp their individual obligations. As seen in the recent undertakings regarding Lease 500031 in McCall, mixing constitutional questions and political considerations creates a toxic brew. Constitutionally questionable sales pose a two-prong risk of devaluing the overall trust fund and jeopardizing previous sales agreements.

Sincerely,

Bruce M. Smith

cc: Superintendent of Public Instruction Ms. Sherri Ybarra
Secretary of State Mr. Lawrence Denney
State Controller Mr. Brandon Woolf
Director Dustin Miller