ARIZONA STATE LEGISLATURE
AD HOC COMMITTEE ON STATE TRUST LAND REFORM

Minutes of the Meeting
Monday, June 14, 2004 – 1:00 p.m.
Senate Hearing Room 1

MEMBERS PRESENT:

Senator Bennett, Cochair	Representative Deb Gullett (alternate to Representative Flake, Cochair)
Senator Bee	Representative Chuck Gray
Senator Blendu	Representative Landrum Taylor
Senator Brown	Representative Lopez
Senator Cannell	Representative Nelson
	Representative Boone

MEMBERS ABSENT:

Senator Allen (Excused)	Representative Flake, Cochair

STAFF:

Kerri Morey, Senate Natural Resources and Transportation Committee Research Analyst
Kimberly Martineau, Senate Assistant Research Analyst
Kathi Knox, House of Representatives Deputy Director of Research
Kristine Stoddard, House of Representatives Assistant Research Analyst

Senator Bennett called the meeting to order at 1:16 p.m. and attendance was noted.

Staff Presentation on Proposed Constitutional Amendments and Session Law

Kerri Morey, Senate Natural Resources and Transportation Committee Research Analyst, reviewed the State Trust Land Reform Stakeholder Proposed Draft dated May 24, 2004 (Attachment A). An explanation of the draft along with questions and answers are highlighted below.

Ms. Morey noted that section 1, page 1, contains the purpose clause and 14 components of the proposal.

Representative Lopez asked whether the purpose would be voter protected. Ms. Morey responded that everything in the proposal would be voter protected and would be placed on the ballot.

Senator Bennett stated that careful consideration should be given as to whether the purpose needs to be included in the House Concurrent Resolution (HCR) (Attachment B). He noted Item "A" in Attachment A of the draft and commented that the process needs to be balanced.

Ms. Morey stated that section 2, pages 2-6, is a conforming change to section 9 of the proposal, which will be discussed later in the meeting.

Ms. Morey noted that section 3, establishes the State Land Commissioner (Commissioner) and the Board of Trustees (BOT). The Commissioner is appointed by the Governor, subject to Senate confirmation, and must have experience with matters within the Commissioner's authority including land use planning and disposition of land. The new BOT reviews matters pertaining to the management, planning and disposition of trust land. The BOT consists of seven members, appointed by the Governor to four-year terms. Four of the BOT members represent public schools and universities. The members of the BOT are subject to Senate confirmation and must have substantial experience in matters within the scope of the BOT's authority and may only serve two consecutive terms.

Representative Landrum Taylor asked why the Commissioner and BOT are included in the Constitution. Ms. Morey responded she would defer that question to the stakeholders.

Richard Hubbard, Deputy Commissioner, State Land Department (SLD), responded that the appointment of the Commissioner is currently in the Constitution. Consequently, the management of the SLD and the introduction of the BOT would require inclusion in the Constitution. He deferred the issue to Constitutional attorneys, and noted that the parameters of the BOT's responsibility are outlined in statute.

Senator Cannell referred to section 2, paragraph B, voicing his concerns regarding lands in the rural areas, and questioned the necessity for that paragraph. Mr. Hubbard responded that the paragraph is included to further confirm the role of priority of the Commissioner. He said based on discussions, the concept of attention to the rural areas is open for consideration by the coalition as an addition to the proposal.

Representative Landrum Taylor echoed Senator Cannell's remarks and indicated there is currently a court case reviewing this issue.

Representative Gray referred to the same paragraph and questioned the use of the word "may" in the first sentence. Mr. Hubbard stated that the semantics of the language should be crafted to ensure that the Commissioner maintains his fiduciary obligation and acts in the best interest of the trust at all times.

In response to Representative Nelson, Mr. Hubbard responded that the SLD prioritizes in this manner acting in the best interest of the trust in order to maximize value.

Representative Lopez asked about the Legislature's role regarding prioritization of the land. Mr. Hubbard explained that the Commissioner is the executive of the agency and acts as a trustee. To a certain extent the Commissioner is controlled by the Legislature through the process; however, the Commissioner is generally the exclusive authority subject to judicial review.

Representative Gullett asked what would happen if the word “may” is changed to “shall” in that paragraph. Mr. Hubbard replied he does not see any distinction.

Senator Blendu referred to “may prioritize” and asked Mr. Hubbard to comment on that language. Mr. Hubbard responded that the fiduciary obligation language is consistent and clear within the Constitution, Enabling Act, and case law. Senator Blendu stated that prioritization differs between Maricopa County and northern Arizona and wanted to know the value judgment placed on the various parcels. Mr. Hubbard replied that the prioritization and the fact that the urban areas of metropolitan Phoenix and Maricopa County are receiving attention are based on value and the SLD staff. He explained that the SLD could not justify diverting staff time in multi-million dollar deals with transactions of a comparatively lower value.

Senator Blendu referred to the land sales in 2003 and wanted to know how much of 15% of those sales was allocated to the SLD. Mr. Hubbard responded he did not have that particular number at the moment. He explained that there was a significant number of multi-million dollar sales; however, most of those were term sales where 10% down was received and the balance would be received over time.

Representative Gray stated it is his understanding that the 15% also includes 15% of royalties and income from leases. He asked Mr. Hubbard if he has a number on those items. Mr. Hubbard replied that is correct, and he would also gather that data for the Committee.

Representative Landrum Taylor referred to a member being “removed for cause” on page 7, line 17, and asked Mr. Hubbard to explain that item. Mr. Hubbard responded he believes it would fall under the “breach of fiduciary duty” as determined judicially. In response to her question on page 7, line 21, regarding a “quorum,” Mr. Hubbard said he is not in a position to comment because it is not a SLD issue. He said there has been discussion on that point as raised by the Legislature. Representative Landrum Taylor said she is concerned that three people would make decisions affecting the future of our State.

Representative Nelson asked for an explanation of the quorum issue. Ms. Morey explained that a quorum of the BOT would comprise four members of the seven. She noted that if only four members were present, three votes would be needed to take action.

Representative Lopez referred to the State Board of Education’s quorum requirements. She said in order to adopt any changes, a majority of the Board is required. She said a board could be structured so that a majority of the board is needed to adopt any kind of action.

Senator Bennett explained that within State government, situations exist within a committee or board that a majority of the full board is required to take action. He said other areas have references to a quorum defined as the majority of those present. He commented the issue becomes a threshold question as to whether a majority of the quorum or a majority of the full board is required to take action.

Senator Blendu asked whether this particular language is to be included in the Constitution. Ms. Morey responded in the affirmative.

Senator Bennett referred to page 6, section 1, paragraph C, and page 7, item C-1. He said it would seem that the only people having substantial experience in managing, planning and disposing of trust land would be current or former employees of the SLD. Since four of the seven members of the BOT are from the education community, he is curious as to who would have the all the necessary experience needed in handling trust lands. Mr. Hubbard replied that the language needs to be refined. He said the intent is to have members of the BOT who have experience in various land issues in general, and to find people in school districts who have that type of experience. Senator Bennett noted that there are thousands of people who have experience in managing, planning and disposing of land; however, experience in trust land narrows the universe substantially. He asked Ms. Morey whether there are definitions of "substantial experience" and "substantial involvement." Ms. Morey replied in the negative.

Senator Blendu asked whether a rancher with 20 to 30 years of experience could serve on the BOT. Ms. Morey responded that unless that individual had experience in the managing, planning and disposition of trust land, that person would not be eligible to serve on the BOT. Senator Blendu commented that since "disposition" experience of trust land is required, there would not be many people having that experience except those in the SLD.

John Wright, Vice President, Arizona Education Association, explained the intent of the qualifications for the BOT members is to ensure that they have the interest of the beneficiaries of the trust and the experience to effectively carry out their responsibilities. He said the coalition in drafting the language worked under the assumption that a rancher has significant experience in managing and disposing of the land through leasing. He explained the qualifications of a teacher/professor in planning, managing and disposing of land vs. those of a rancher to serve on the BOT.

Senator Blendu pointed out that under the language to be included in the Constitution, a person serving on a school board could not serve on this BOT because of lack of experience in disposing of State trust land. He said he is concerned that this proposal is being rushed through the process and yet some of these types of issues have not been resolved after all the discussions that have taken place over the past three years.

Mr. Wright explained the intent of experience requirements for members of the BOT was not that it be their primary livelihood, but to bring their experience and expertise to the BOT.

Senator Bee referred to the BOT and asked for examples of people who would qualify to serve. Mr. Wright responded the intent is to Constitutionally establish the beneficiaries' interest in the management, planning and disposition of State trust lands through the BOT. He noted that those who benefit most directly from the proceeds of the permanent fund are in a position to exercise oversight and work with the SLD and the Commissioner. They would ensure that the actions taken are to the greatest benefit to the beneficiaries without infringing on the other uses of open space, ranch land or other purposes of the State trust lands. He commented that among the education universe, there are a number of individuals and families with ranching experience in leasing land, planning, managing, and disposing of trust land.

Senator Bee asked whether there is a reason for including this language in the Constitutional portion rather than in the statute portion. Mr. Wright responded that since the role of the Commissioner and SLD are currently in the Constitution, it makes sense that the Constitution is the most appropriate place to include the language and the changes regarding the roles now carried out by the Commissioner.

Representative Gullett stated that it would be helpful for the Committee to have a description of the language currently in the Constitution regarding the SLD and the Commissioner. She said it would also be helpful to have the Constitutional provisions for some of the other offices, such as the Board of Regents and the State Board of Education. Ms. Morey clarified that the Commissioner is not currently established in the Constitution, and she indicated that she would provide the information requested.

Representative Nelson commented that if the Committee is looking at statutory language, it needs to be properly defined. Ms. Morey replied the focus of this meeting is not on the statutes, but rather the Constitution. She said if it would be easier for the Committee to review it, she could provide copies of the Constitution without the amendments. Representative Nelson pointed out that if this language is intended for the Constitution, perhaps there should be language inserted "as further defined in statute" to allow further work at the legislative level.

Senator Blendu commented at some point he would appreciate an evaluation on how much is really needed to change the Constitution versus how much could be included in statute to accomplish the same thing. He said at some point in the distant future there may be the need for a person versed in technology to sit on the BOT. He has concerns with including this language in the Constitution instead of in statute where there is some flexibility.

Senator Cannell asked whether the BOT has the power to override the Commissioner and questioned how conflicts are handled. Ms. Morey responded that the relationship between the Commissioner and the BOT is not as clear as it could be. She said the bill requires the BOT to approve certain management, planning and disposition of trust land issues. It also directs the Commissioner to prioritize the management, planning and disposition of trust lands.

Senator Bennett referred to page 6, section 1, C, which he interprets to mean that the BOT can override or reject decisions by the Commissioner relating to planning, management and disposition of trust lands.

Representative Gray referred to the same language and asked how much workload is perceived going to the new BOT and how often it would have to meet to keep up with that workload. Mr. Hubbard replied the intent was that the BOT would have monthly meetings to review the significant decisions of the Commissioner, such as participation agreements and land use plans negotiated in conjunction with cities and towns and major dispositions outlined in statute.

Representative Gray asked Mr. Hubbard if he could foresee any delays at the SLD based on monthly meetings and having to review everything. Mr. Hubbard responded the intent is not to review everything delineated in statute. He remarked that Ms. Knox clarified that statutorily the BOT is required to meet quarterly. He said the intent is to have a five-year disposition plan, which will lay out the manner in which the SLD will dispose of State trust land and would include a significant part of the planning.

Representative Gray commented that if the BOT is only meeting quarterly, he believes the language needs to be re-worked because it now includes oversight and review of the "disposition" of State trust lands.

Senator Bennett referred to page 6, section 1, B, line 39, regarding the Commissioner and the words "disposition of land in cities and towns." He questioned whether that language means government lands, State trust lands, or anyone's lands in cities and towns and also whether it includes counties. Mr. Hubbard replied that the theory behind this qualification is based on the fact that the most complicated transactions facing the Commissioner are the disposition of urban State trust lands.

Representative Gray asked whether that would include city council members around the State who have been involved with the sale of land through their city council position. Mr. Hubbard responded he believes it is subject to later interpretation of the statute and the role of the Legislature and confirmation of the Commissioner.

Senator Blendu commented he is not sure who would qualify under these conditions. Secondly, he said since the BOT serves at the Governor's pleasure, perhaps the Governor could make the appointments rather than include it in the Constitution. Mr. Hubbard responded the beneficiary interest and some of the development interest wanted to ensure that the qualifications of the Commissioner include urban land experience.

Senator Blendu emphasized that there are many items that do not need to be included in the Constitution and believes this type of language does not serve the public well.

In response to Senator Bennett, Mr. Hubbard stated it is the opinion of the coalition that the current Commissioner would meet these guidelines and he outlined the Commissioner's qualifications.

Ms. Morey continued her explanation of the draft referring to section 5, pages 7-11. Highlights of the grazing lease portion include the following:

- The Commissioner authorizes grazing leases for a term of up to 10 or 25 years.
- Grazing leases do not require advertisement or auction.
- If a lessee is determined to be in substantial compliance with a grazing lease, there is no competitive bidding process.

- A new type of grazing lease is established for leases of up to 25 years and is not subject to cancellation, if the land is reclassified for another use.
- Both types of grazing leases require an annual report by the lessee, compliance inspections by the Commissioner, and specific management practices to promote rangeland health.

Ms. Morey noted that other Commissioner's authorities include:

- Selling or leasing trust land for up to 99 years for environmental mitigation without auction.
- Selling natural products of trust land in small quantities without advertisement or auction.
- Disposing of trust land for conservation or rights-of-way without advertisement or auction.
- Disposing of certain conservation easements on grazing trust land without auction.
- Leasing trust land for mineral purposes without auction.
- Public notice requirements for all sales and leases are reduced from ten weeks to five weeks in a local newspaper.

Ms. Morey noted this section also provides the following:

- Allows commercial sales and leases to include delayed payment from future sales or leases of the land.
- Bidders must have financial capability.
- Allows the use of one or more economic terms by which the highest bid is determined.

Representative Landrum Taylor referred to page 8, lines 43-45, which states "without advertisement, auction or competitive bidding, in a manner prescribed by law." She asked how that language would maximize the true value to the trust in a lease for 25 years.

Bas Aja, representing Arizona Cattlemen's Association, responded that this provision will protect the SLD from having to spend immense amounts of revenues administering a chaotic leasing system, which basically had no scoring. He said the provision that refers to "without auction" was provided for any lease of ten years or more, and allows for a more manageable system to deal with those leases.

Senator Blendu referred to the same provision and indicated that since it states "in a manner prescribed by law," a safeguard or process would be established whereby those kinds of issues could be resolved in statute. Mr. Aja responded that is correct.

Representative Landrum Taylor referred to the 10 years or less commercial leases without the ability for auction, and asked whether there would be any type of loss to the trust. She wanted to know how many of those types of leases are in State trust land currently. Mr. Aja replied all leases of 10 years or less can occur today without auction as provided in the Constitution. He noted that the longer-term leases must have an auction provision as provided in the Constitution currently. Representative Landrum Taylor said she would like to know the value over the long term. Mr. Aja replied currently there are approximately 1300 leases of 10 years or less. He said there are no leases of which he is aware that are in the 10 to 25 year period. He spoke about the value and commented on the SLD encouraging improvements on the land with investors' own resources. He said the value over the longer term would be increased investment by lessees and less administration by the SLD. Representative Landrum Taylor commented she is still not clear on how going to 25 years will increase the value for the trust.

Suzanne Gilstrap, representing the Nature Conservancy, responded one of the items to keep in mind is the reference to grazing leases and some of the requirements that have been included in statute or session law that go towards enhanced management of these lands. She indicated that whether referring to short-term or long-term disposal of the lands, it is very critical to ensure that they be properly managed in order to maintain the value. She noted that currently the SLD has no tools or personnel to be able to ensure that the lands are properly managed. Therefore, the requirements that will be included in this piece of legislation will help in maintaining value, particularly as it relates to the longer-term leases. Representative Landrum Taylor commented she believes there would be more of an increase in value if the bidding process were allowed to occur more frequently as in the 10-year leases.

Mr. Aja explained that leasing subject to an auction requirement very seldom occurs in the public or private sector and drew an analogy to an apartment complex or rental property. He said the auction requirement on a permanent disposition is quite different, which could show greater revenues under most marketing scenarios. He said time has shown that a leasing system subject to auction requirements is not the best managed and is very costly to administer.

Representative Lopez wanted to know how "substantial compliance" is determined as noted on page 8, line 43. Mr. Aja explained the package views these enhanced requirements that are contained in:

- The Annual Report provided by the lessee to the SLD
- At least once within the term a visit to the site occurs to promote the rangeland health, the ecological sustainability of the soil and other resources.

Mr. Aja commented it is just like any other review that occurs through a range monitoring situation. The SLD would then determine if the lessee was in compliance with the provisions of the lease.

Representative Gullett referred to the testimony at the last meeting where the Commissioner discussed having three people randomly inspecting grazing leases with some lands never being inspected, and asked whether someone could comment on what is being done to ensure the health of these lands. Mr. Aja responded that the tools being specified would grant much greater ability to the SLD to ascertain the health of the lands. However, he said more range people will need to be hired in order to enforce the program. Mr. Aja referred to the real value and noted that there are two key items that have been attributed to lessees for over a hundred years:

- There is someone living on the land and managing and paying for the lease.
- The SLD is able to cancel the lease whenever it chooses to sell the land.

He indicated that the additional tools for the rangeland health would take the SLD beyond where it is today.

Representative Gray referred to the discussion regarding the increased value of the land and asked Mr. Aja to address the issue of any destruction of the land in a lease situation, such as illegal dumping, diseased livestock, and other contaminations and abuses. Mr. Aja replied one of the greatest benefits in contributing towards value is that the ranchers leasing the land "know" the land and he provided specific examples.

Representative Boone asked whether there is a maximum term currently regarding leasing trust land. Mr. Aja responded there are two levels:

- The Constitution provides for a lease of ten years or less without auction.
- Land could be leased for more than 10 years up to 99 years with an auction.

Representative Boone referred to the 10 year lease, and asked whether the courts interpret that auction is not required if it is 10 years or less currently. Mr. Aja responded that the section in the Constitution dealing with this provision used to state "as prescribed by law." The Legislature had prescribed a 10-year leasing system without auction by law. He noted that a number of lawsuits have occurred over the past several years regarding the definition of that section. He said the coalition was attempting to develop a program that allows for enhanced rangeland management and efficiency, but also would not include burdensome requirements that brought less value. Representative Boone asked whether the 10-year to 25-year leases for grazing purposes are currently allowed for auction. Mr. Aja responded that today those leases could occur with an auction. Representative Boone asked whether the intent is to now preclude the auction situation for leases over 10 years to 25 years. Mr. Aja replied the Constitution currently states "without advertisement." He referred to page 9 of the proposed language in the Constitution, and noted that the Legislature prescribed a system that did not require an auction. He said a recent court case ruled that the SLD cannot summarily overlook the conflicts. He indicated that the SLD has three years' experience with this current conflict situation, which has cost an estimated over $1 million while receiving less than $15,000 in extra revenues.

Representative Boone asked whether leases are subject to being cancelled currently without cause. Mr. Aja replied under current law leases are subject to cancellation if the lessee is not compliant and permits waste. He indicated that the SLD could cancel a lease without cause by reclassifying the land and canceling the lease.

Representative Landrum Taylor referred to page 9, lines 19-21 stating "the lease is not subject to cancellation on reclassification of the land for another use" and wanted to know how this could be in the best interest of the trust. Mr. Aja replied this refers to the 10 to 25 year lease and the SLD has complete discretion. He explained that a lessee has to submit an intensive management plan to the SLD demonstrating what investment actions will be taken over the term of the lease that will increase the value. In exchange for that investment, a level of certainty is granted by the SLD from 10 to 25 years. Representative Landrum Taylor stated she is concerned with the way the language reads and questions how it could be in the best interest of the trust. Mr. Aja referred to line 20, which states "not subject to cancellation on reclassification of the land for another use." He said the SLD could cancel that least if the lessee does not abide by the management plan, compliant with the rangeland health standards or otherwise violates the lease. He pointed out that the land cannot be converted to a different use within the term of that lease. He said that provision was held to be very important by conservationists and other collaborative groups.

Representative Boone referred to page 8, which he noted appears to be the introduction to the entire section. He said it appears that language is being added where there is no advertising, auctions, or competitive bidding. He said this language not only applies to grazing, but also to rights-of-way and other areas in the draft. He wanted to know how the beneficiaries are protected when there is no specific process whereby the highest and best bidder is obtained regardless of the purpose of the lease. He commented that it appears many exceptions are being added to the general rule of which he has concerns.

Mr. Aja responded the mosaic of land patterns that represent the trust consists of every conceivable type possible, and he cited examples. He said the way the SLD seeks to achieve the best value was to have a Grazing Land Evaluation Commission, which sets the rate for the grazing leases and provides protection from obtaining less than the value.

Senator Blendu stated he looks upon this language as protection for the State to avoid situations of unscrupulous lessees.

Representative Gray asked what portions should be in the Constitution versus statute, so that the Legislature could fix an unscrupulous situation. Mr. Aja responded it is the intent to work with the Committee to minimize Constitutional language.

Senator Cannell stated it appears the only change being made is the 25-year lease and protecting the land from reclassification, which is handled in the Constitution. He referred to the Grazing Land Evaluation Commission and asked for an explanation. Mr. Aja responded it is a Commission appointed by the Governor and at least every five years conducts an appraisal of the value of the grazing fee charged for each animal on the land. The process is conducted through the normal appraisal process in determining the land lease values in the State. He said a formula recognizes the lessee's improvements and associated costs, and the process is included in current statute. He noted that procedure is not being changed with this proposal.

Senator Cannell referred to page 9, section 4, regarding selling or leasing trust land for a term of up to 99 years without auction for environmental mitigation and asked for an explanation. Ms. Morey explained the language is associated with section 404 permits. If there is a discharging area or if an area is being developed, this provision allows wetlands to be set aside on State land.

Mr. Hubbard stated there are several statutes affecting State land and disposition as mentioned by Ms. Morey. There are also endangered species acts and the rules and regulations of the Environmental Protection Agency (EPA). He explained that mitigation leases allow for urban State trust land or other private land to be developed in exchange for certain land where such habitat or washes exist to be preserved. He said the SLD would enter into a 99-year lease and attempt to negotiate whether or not the SLD could have compatible uses on such property, for example, grazing or satellite towers, subject to the conditions of the federal agencies. He indicated it then allows the SLD to take those lands that are not generating income to obtain some income, and also fosters the development of land that should be developed. He stated that since it is federal agency, a long-term 99-year commitment is required.

In response to Representative Boone, Mr. Hubbard clarified that up to 99-year leases can be done now through auction; however, there may be difficulty due to reclassification of the property.

In response to Senator Blendu, Mr. Hubbard clarified the environmental mitigation language. He said that development would not take place on land subject to a mitigation lease.

In response to Senator Cannell, Mr. Hubbard said there have been discussions among the agricultural interests regarding the time commitment needed to recoup investments in improvements and also to limit any reclassification in the longer leases.

Senator Bennett asked for clarification regarding BOT approval**.**

Edward Fox, Vice President, Communications, Environment and Safety, Arizona Public Service Corporation, explained it was agreed after much discussion, that the BOT should not be involved in running the day-to-day business of the SLD except where something of significance was being changed, such as removing an auction. He said in the 10-year to 25-year leases, it was decided to have the BOT involved because of the public process. Senator Blendu asked whether a Constitutional change was necessary in this instance versus handling it through statute. Mr. Fox responded the consensus was that those kinds of situations should be in the Constitution.

Senator Bennett referred to page 10, paragraph 11, line 41a, “bidder experience.” He asked whether a first-time bidder would be precluded because that bidder had not bid up to that point. Mr. Fox replied that this section deals with Participation Agreements regarding large parcels of property that require significant amounts of private sector investment. He indicated that this is a minimum set of criteria that would allow flexibility for someone with experience and financial capabilities to be included in the bidder pool. Senator Bennett said he is concerned that if a bidder has financial capability but no bidder experience, that person would be effectively “locked out” of the process. Mr. Fox responded it was not the intention to "lock out" anyone, although development experience is important to participate in the qualified bidder pool.

Senator Blendu commented with the Participating Agreements, the SLD could become the largest developer in the State and questioned whether that is a good idea. He noted this is a new direction for the State and asked if this is the direction that the SLD would like to pursue. Mr. Fox replied there is a Participation Agreement provision currently, but it is not used very often because of the way it is structured. He indicated there are some large tracts of land that need to be planned and dealt with at the same time. He said regardless of the choices made, there are risks associated. He commented that protections are in place providing the SLD with the tools to do Participation Agreements that require BOT approval and is a public process. He noted that because of the land holdings, the SLD would be involved in "land development." Senator Blendu said he is concerned that the BOT could possibly approve the biggest development in the State's history because of the number of members and quorum needed to vote. Mr. Fox responded debate took place regarding the quorum issue, which could be discussed further if anyone has a major concern. He said there are risks involved as in anything, but protections for the SLD have been incorporated. He commented that real estate cycles are a reality, and these situations would enable the SLD to sustain and benefit from the ups and downs of a real estate cycle.

Senator Bennett referred to page 10, lines 41 through page 11, line 4, and asked whether all those items (a,b,c and d) would be required in order to accomplish Item 11 on page 10, line 36. Mr. Fox replied in the affirmative.

Representative Nelson commented on the release structure of parcels that are sold in a major development, which creates value. He asked whether this system protects the value of State trust lands that are being developed in real estate cycles. Mr. Fox explained the reason in establishing one or more phases is to not turn over title to more land than would be appropriate. In those instances, the SLD would sustain a downward real estate trend because it would hold title to the remaining parcels. Representative Nelson commented on the downturn of the real estate market in 1973 and in the late 1980s and early 1990's and asked whether the current language relates to that type of situation. Mr. Fox responded the Participation Agreements would probably have language that if the developer went bankrupt, the SLD would retain or take back title to the property subject to other liens and financial commitments.

In response to Representative Boone, Mr. Fox commented that there are currently Participating Agreements, but they are not functional because of the uncertainty that a developer has in the planning and auction process resulting in a lack of investment by the developer.

Representative Lopez referred to page 10, Item 10 (a), and asked for an explanation. Mr. Fox responded that the provision was intended to deal with the "checkerboard" areas of the State, where State trust lands and private lands are intermixed. He said this provision was proposed by the conservation community to deal with those areas. Mr. Fox noted that Ms. Culp from the Arizona League of Conservation Voters could better define that provision.

Susan Culp, Arizona League of Conservation Voters, explained the intent of this provision is to provide an incentive for landowners in northern Arizona whose land is of a "checkerboard" pattern, which creates management difficulties for private landowners and the SLD. She indicated that the amount of land involved includes approximately 2 million acres in northern Arizona. She said it is a good and necessary tool for certain areas, such as the Williamson Valley watershed area for the Verde River. Representative Lopez commented that she has concerns about this section because it involves significant acreage without auction, which limits the benefit to the trust in terms of the amount of money that could be raised for the trust. Ms. Culp responded that there would be relatively little impact to the trust because the land would remain in grazing and the SLD would still be collecting revenues from those activities. However, she noted that the land could not be sold for development at that point.

Representative Nelson provided a perspective from a rancher's standpoint who may have land surrounding State land, and asked what would happen if conditions exist which would eventually force a rancher out of business. He wanted to know the prospect of recovering the investment from sales of private land that go on the market under that scenario. Ms. Culp replied that is a concern because the rancher could subdivide his land, which would cause habitat fragmentation and future use and value of that land.

Representative Gray referred to page 10, item 8, lines 6-9, and asked if the "rights-of-way" language appears in statute since it includes language "in a manner prescribed by law." Mr. Hubbard replied the language "in a manner prescribed by law" is the process in which the "rights-of-way" are conveyed. He emphasized that this is an important component of the package with respect to the future development of urban State trust land. He explained that most landowners deal with cities, towns and counties in negotiating for infrastructure services and the landowners dedicate land without compensation. In exchange for that dedication, the landowners receive benefits such as increased zoning, installation of infrastructure, or other municipal services. He said that component of private development is vital to increasing the value of land that will ultimately be developed for residential and commercial use. He indicated the SLD is prohibited from doing that because of the Constitution and Enabling Act, which states that the SLD must receive value for every piece of land conveyed. He said this provision allows the SLD to dedicate land for infrastructure and municipal services to increase the value of the land for development, which requires approval by the BOT with the Commissioner and BOT acting in the best interest of the trust. Mr. Hubbard commented that this provision would require a change to the Enabling Act.

Representative Gray asked whether the intent would include allowing access of rights-of-way across State trust lands for power lines to be built without actually selling the trust land that those power lines are crossing. Mr. Hubbard responded he is reluctant to indicate that the land would be given away for free because there has to be a value given in the form of a benefit to other State trust land. He explained that the trust fund would receive compensation for land being disposed for any purpose. Representative Gray questioned the process of allowing "rights-of-way" currently on State trust lands only for future benefits. Mr. Hubbard explained this portion of the proposal is designed for immediate benefit and development of

State trust land, focused primarily in the urban areas. He said this provision does not prohibit the ability of the SLD to receive compensation for rights-of-way in the future.

In response to Representative Landrum Taylor on that point, Mr. Hubbard said although he mentioned urban areas, it does not exclude the rural areas. Representative Landrum Taylor said she is concerned about the future and questioned how the current situation would provide benefits in the long run. Mr. Hubbard responded that the lack of this tool is the reason for the current leapfrogging of development between developers and cities and towns. He said the proposed tool has a bargaining chip in the planning and development of State trust land in the urban areas, which would increase the value of the permanent fund.

Senator Blendu asked whether it would make more sense to lease the rights-of-way rather than dispose of the land not being used. Mr. Hubbard replied the issue is compensation and the State is obligated to demand appraised value for the small pieces of land. Therefore, the entity using the property would still have to pay the State, whether it is through lease or sale. Secondly, he noted if the city has an obligation to maintain the land, it would be more prudent for the city to own the land rather than lease because of the risk associated with possible loss of the land. Senator Blendu stated he believes the SLD would be acting in the best interest of the trust by leasing the land not being used for rights-of-way in order to develop land elsewhere. Mr. Hubbard explained the problem is that there are not many entities willing to pay for leases.

Representative Landrum Taylor commented that it appears some of these provisions could be handled without including them in the Constitution. She said the key is to make sure the SLD has enough staff to accommodate these issues. Mr. Hubbard responded that from an Enabling Act and Constitution standpoint, this particular provision would need to be in the Constitution with a corresponding provision in the Enabling Act primarily because of the conflict with the current United State Supreme Court case based on the Enabling Act language.

Representative Gray stated he believes Senator Blendu has a good point because the State leases grazing land and has a value for the leasing. He believes the rights-of-way provision could be leased in the same manner, and asked whether the State is currently receiving ongoing perpetual income from those types of leases. Mr. Hubbard responded that the State currently receives revenue from those types of leases. He explained the lease and the valuation of those types of leases has to be at an appraised value based on highest and best use. He said the highest and best use of grazing land is grazing. In the areas of urban development, the highest and best use is for residential or urban development at significant revenues per acre, which is the issue. Mr. Hubbard noted that the highest and best use determination of the land is conducted by independent appraisers using professional standards.

Representative Gray asked whether this provision to lease rights-of-way could be handled through the Legislature using a particular tool. Mr. Hubbard responded that it could satisfy the need, provided a Constitutional and Enabling Act change occurred.

Representative Nelson commented on the leapfrogging situation, and asked whether it would make more sense for all entities to work together rather than to have a series of major developments with totally different infrastructure systems in place. Mr. Hubbard replied the unification of all infrastructure systems would work more effectively and add value, if that could happen. Representative Nelson noted that infrastructure adds inherent value to adjacent properties. Mr. Hubbard responded that is the goal of the proposal and that the value would need to be proven to the BOT.

Senator Bennett announced he would like to recess for five minutes and upon reconvening would continue with the agenda. He noted that the Wednesday meeting scheduled at the SLD is cancelled and will be rescheduled for Tuesday, June 22. He added that the next meeting of the Committee would be held on Thursday, June 17, at 1:00 p.m. in Senate Hearing Room 1.

Senator Brown commented on the excellent work conducted in the past on preserving the millions of acres of State lands to this point. He noted this issue has been ongoing for the past three years with meetings and discussions including people in the education community. He said he believes time is pressing and everyone needs to be committed and to be confident of those who have worked hard in the past. He said it is important to move forward without getting bogged down in detail to be finished by June 30, in order to place this measure on the ballot.

Senator Bennett agreed with Senator Brown's comments. He said before the Committee recesses, Senator Blendu would like to pose a question to Jim Drake, House of Representatives Rules Attorney.

Senator Blendu stated he is perplexed with the language needed in the Constitution versus that which will be on the ballot, and asked Mr. Drake to provide clarity in that area.

Jim Drake, Rules Attorney, House of Representatives, explained that the current proposal is intended to be presented to appear on the ballot as a single proposition and would encompass both Constitutional law and session law. He said he believes both cannot be accomplished at the same time in a single package because of a provision in Title XIX, 125b, which states "proposed Constitutional amendments shall be placed by themselves at the head of the ballot column followed by the measures referred." He said both could be placed on the ballot, but cannot be placed in a single proposition. He indicated he conducted research on this issue and that statute was enacted during the First Special Session in May 1912.

Senator Blendu commented one of his concerns is that this issue needs to be well thought out prior to being placed on the ballot in order to prevent any lawsuits. He asked whether two ballot measures are needed in order to comply. Mr. Drake replied in the affirmative. He explained that one HCR could direct the Secretary of State to put provisions 1-7 in the Constitutional pieces in the 100 block of propositions, and divide the other 17 provisions to be placed in the 300 block. He indicated he is not sure that arrangement serves the process well, and believes having two resolutions would make the process easier. Mr. Drake commented on his research conducted on similar historical issues, and believes it is not proper to put both items as a single package on the ballot. In response to Senator Blendu, Mr. Drake stated he has discussed this issue with the Senate Rules Attorney. Senator Blendu voiced his concerns and said he would also speak to the Senate Rules Attorney on this issue.

Senator Bennett recessed the Committee at 3:40 p.m.

Senator Bennett reconvened the meeting at 4:00 p.m.

Representative Lopez questioned if anyone was drafting a bill containing the concerns and issues raised in the meetings. Senator Bennett explained that a bill has been drafted with the understanding that changes could be made based on the discussions in Committee. He added that staff members are compiling notes and as the Committee members agree on any changes, they could be amended into the bill language.

Representative Landrum Taylor wondered if there was enough time to prepare all of the changes. Senator Bennett suggested that the Committee is working toward that goal.

Richard Stavneak, Director, Joint Legislative Budget Committee (JLBC), distributed a document entitled State Trust Land Financing (Attachment C) and summarized the aspects of the financing, focusing on how the trust earnings process works from a distribution standpoint. He also discussed the SLD budget and referred to a letter from the Speaker of the House and President of the Senate, noting that he would be addressing their issues throughout his presentation.

Referring to the handout, Mr. Stavneak pointed out that there are two categories of trust land monies – Permanent Fund and expendable earnings. As of June 2003, the Permanent Fund has deposits of $1.1 billion, and each year, new revenues are deposited into the fund from four contributing sources.

In response to Senator Bennett, Mr. Stavneak replied that $73.2 million in land sales were distributed into the Permanent Fund in fiscal year (FY) 2003, representing the amount of cash collected. He provided an example that if there was a $100 million land sale, 10% or $10 million would go into the Permanent Fund. In future years, as the principal is paid off, that money would go into the Permanent Fund. Each year interest is paid on the amount with the monies going into the expendable earnings. If there is a seven-year payment schedule associated with a land purchase, for each of those seven years there would be a deposit into the Permanent Fund and expendable earnings.

Mr. Stavneak next talked about the five contributing sources to the expendable earnings category. The SLD controls the following sources: natural resource rental, commercial leases, and sales contract interest. He discussed the distribution of expendable funds, noting that K-12 receives approximately 90% of those funds. Some of the other areas benefiting from the expendable earnings category include universities, the State hospital, miner's hospital, penitentiaries, and the School for the Deaf and Blind.

Mr. Stavneak suggested that because of a drop in the Treasurer earnings, it is predicted that expendable monies will decline in FY 2004; however, there should be a recovery period in FY 2005. He explained that Proposition 102 (enacted in 1998) was designed to increase Treasurer earnings, allowing investments of up to 60% of the Permanent Fund in stocks and requires the Permanent Fund to grow by rate of inflation. In 2003, a new formula for computing the Treasurer expendable earnings was established and is based on a five-year average of the rate of return.

Mr. Stavneak explained that Proposition 301 enacted a provision that everything received in the common school fund above $72 million would be devoted to the classroom site fund. All dollars below $72 million would continue to go to K-12 for its existing purposes. The $72 million was used to defray the current cost of the basic State aid formula, as well as for debt service.

Mr. Stavneak next provided information about the SLD budget, noting that it has increased slightly since FY 2001. He pointed out that the reform proposal would significantly increase the SLD resources, permitting the SLD to have 15% of the five-year average of sales and earnings. If the proposal were in effect in FY 2005, it would generate an additional $24 million for the SLD. The proposal would also cap the unexpended funds at twice the operating budget and the Legislature would not oversee these new monies.

In response to Senator Cannell, Mr. Stavneak indicated that the "hold harmless provision" monies came from the Permanent Fund's earnings.

In response to Senator Bee, Mr. Stavneak replied that the Permanent Fund, although referred to as one fund, actually has 13 Permanent Funds. Senator Bee voiced a concern that there is no oversight as to where the monies are spent. For the next ten years (until the anti-supplanting provision is eliminated), the $14 million will continue to go to the SLD budget, as well as the monies generated from the 15% of the average of sales.

In response to Representative Gray regarding the current value of the 300,000 acres of conservation land, as well as the 400,000 acres of conservation options land, Mr. Stavneak replied that JLBC does not have the necessary financial data to estimate the value.

Representative Lopez asked if the 15% came from the amounts distributed to the Permanent Fund. Mr. Stavneak indicated that he would need to review the language of the ballot proposition as to whether it means 15% of the total or 15% of the annual proceeds.

Representative Gray wondered if JLBC had information to determine at what point in the future the SLD would run out of trust land to sell. Mr. Stavneak replied that he did not have that information; however, the question has been posed to the SLD.

Ms. Morey next explained that Section 6 allows legal title to State trust land to pass without the trust receiving full payment for the true value of the land in a number of circumstances, including before payment of a share of the revenues generated by future leases or sales of state land. This has been referred to as Participation Agreements. It also grants public rights-of-way for new and existing land or pursuant to a land use plan that includes land designated as suitable for conservation. This section also authorizes the conservation of additional land without auction, advertisement or further consideration in conjunction with an agreement with a local government. The value of this additional conserved land is determined in that same agreement and may include non-monetary forms of consideration as well as deferred payment.

In response to Representative Lopez, Ms. Morey noted that the SLD would receive some money up front and then receive a percentage of all subsequent sales after a development was built.

In response to Senator Bennett, Mr. Hubbard indicated that if there is duplication regarding the grant language for rights-of-way, it was unintentional. Senator Bennett offered that there is a duplication of the participation agreement as well. Mr. Hubbard explained that he believes it was the intent to put the Participation Agreement language in the value section because they will be conveying small portions of State trust land for infrastructure and other uses without consideration.

Representative Gray stated that he is having difficulty understanding the conveyance of conservation land. Mr. Hubbard replied that part of the Participation Agreement would allow for the ability to create assessments for infrastructure on State trust land. However, the bill language provides a requirement that there is ample additional security for payment of any taxes so that the foreclosure of State trust land would be prevented. In response to Senator Bennett, Mr. Hubbard indicated that he feels the word “ample” in the previous statement means that the BOT would ensure that the possibility of foreclosure of State trust land is not possible. The goal is to prevent foreclosure.

Mr. Hubbard noted that the SLD has a schedule and a release schedule, meaning that the SLD sells the property, and does not convey title. The SLD issues a certificate of purchase, which gives the landowner every right to operate on the land without the title. As the buyer pays down the remaining monies on the loan, the ability exists to release property. The release price is the value of the land plus a percentage. This is to ensure the SLD is not left holding the worst property in the package. Senator Bennett mentioned that although the purchaser by the third year would have paid 30% of the principal owed, only 15% of the land would have been released. Under the proposed bill, the rights and process currently afforded the State in a default situation will continue to exist.

Mr. Hubbard next talked about Participation Agreements. He noted that the SLD would be required to have independent security in the form of a letter of credit, a cash bond, or some other financial instrument that would first be seized in the event of default. In that instance the property would not be foreclosed and the SLD would retain the property. That would be flushed out through the Participation Agreement process and the BOT process.

In response to Senator Bennett's question regarding non-monetary forms of consideration, Mr. Hubbard explained the shift in value in planning and other processes used in development of State trust land. He noted the formula for the planning is in statute.

Representative Gray wanted to know about the risk to the State regarding the Participation Agreements. Mr. Hubbard explained that the BOT would have an obligation to protect the State. Representative Gray referred to how the proposal was structured after three and one-half years and wondered what assurance the Legislature has that the BOT or whoever is negotiating the deals ensures that these things happen. Mr. Hubbard replied that the BOT has the public scrutiny of the deal. Additionally, there is increased funding to hire highly-skilled individuals to address the various risks. Representative Gray noted his concern as to whether the BOT would have the expertise to fulfil their responsibilities adequately.

Senator Bennett indicated that he was unable to find in the proposal a definition of conservation. Ms. Morey replied that the definition is found on page 19. Senator Bennett questioned if line 5 on page 13 was covered by the same definition. Ms. Morey explained that the definition of conservation is defined in session law and only applies to Sections 11, 12, and 13 of the proposition and Article X of the Constitution.

Ms. Morey pointed out that Section 7 of the draft requires the Legislature to establish the Trust Land Board of Investment (Board) to serve as trustees of the Permanent Fund. This Board includes the State Treasurer and a public school representative who also sits on the BOT. Secondly, the trust land management fund is established for the administration, management, planning, and disposition of trust land. The Board may transfer from the Permanent Fund an amount of up to 15% of the five-year annual proceeds from the sale, lease or other disposition of trust land. These monies do not lapse or revert unless the fund grows to two times the operating budget for the next fiscal year.

In response to Senator Cannell, Ms. Morey replied that this is not a subcommittee of the BOT.

Representative Gray stated it appears that someone from the Board, who is one person, and the State Treasurer, will decide how to allocate and invest the funds with the Treasurer's office. He questioned whether this means that the member of the Board will actually influence the Treasurer's decisions related to other investment monies. Ms. Morey clarified that the only two members mentioned in the Constitution for the Trust Land Board of Investment are the two already mentioned. It does state that the Legislature will establish that Board to serve as trustees. She indicated that she feels the Legislature would be responsible for appointing other members to the Board.

Representative Gray questioned whether the Legislature would create an investment board for trust lands that would affect just State trust lands or would they also be able to affect all the other investments that the Treasurer currently is given the charge to invest. Ms. Morey referred to page 13, line 30, where the proposal mentions Trust Land Board of Investment and reference to the Permanent Fund. She noted it refers to the Permanent Fund only.

Representative Lopez indicated that the statutory language includes information about the investment board. Ms. Morey replied that she is not prepared to speak to what is in the 150-page bill. She reiterated that the Legislature is authorized to establish a Trust Land Board of Investment. In response to Representative Lopez regarding the number of members on the Board, Mr. Hubbard explained that he feels there needs to be additional clarification. He suggested that the intent of the coalition was that the Board of Investment exists to invest State monies. There is no representative of the beneficiaries. The intention is to form a subcommittee of the Board that includes all members of the investment board and one of the beneficiary members of the BOT who would deal exclusively with the investment decisions of the Permanent Fund. They do not address any other areas.

Senator Bennett questioned how the anticipated new dollars for education would be used. For instance, should these monies be used to address any inequities that currently exist between the districts or will the dollars be used to move the schools forward equally but still maintain the existing inequities. Mr. Hubbard replied that question should not be addressed by the SLD, because they are charged with earning the revenue and where the revenue goes is not part of its mission. Senator Bennett reiterated the question to Mr. Hubbard as a member of the coalition who sat at the table whether there was any discussion on that topic. Mr. Hubbard stated that he believes the beneficiaries intend to address that issue in their presentation after the SLD presents its information regarding revenues.

Senator Bennett related information about why he posed the previous question. He explained that several years ago when he chaired the Senate Education Committee, he posed the idea of a lock box for a portion to the K-12 dollars to go into a fund that would be used exclusively for teacher salaries. There was concern as to whether they could possibly put enough money in that fund to give teachers a substantial raise and maybe hire enough new teachers to seriously address class size. At the time, it was predicted that if they put about 35% of the total dollars from K-12 into that fund just for teacher's salaries, there would be enough money to give every teacher a $10,000 a year raise, which is approximately a 25% increase and reduce class sizes by one-fifth. Although he thinks the numbers were accurate, the idea was met with a lot of hesitation, reservation, and disbelief. However, more importantly, after the proposal was presented, the first two district representatives that came into his office told him that their average teacher salaries were already $10,000 above the average. He determined that if there are districts who are already more than $10,000 above the average teacher's salaries, there must be many districts that are $10,000 below the average. This would indicate that some real inequities exist in the net per pupil funding. He said he has felt for several years that the only way to address those inequities was not by taking from the "haves" to give to the "have-nots," because that does not work politically or practically. He suggested that they should at least consider giving the teachers below the average an extra share while giving the ones above the average an additional share, but maybe not as much as those below the average. So that over time, the gap could be closed while everyone was receiving new dollars.

Ms. Morey explained that Section 8 begins on page 15, noting that the preferential lease renewals apply only to leases of ten years or less.

Senator Bennett announced that the next meeting is scheduled for Thursday, June 17, 2004 at 1:00 p.m. in Senate Hearing Room 1. Senator Brown asked when the next meeting after that meeting would be held. Senator Cannell asked if they would be meeting on Monday or Tuesday of the following week. Senator Bennett indicated that part of the reason of scheduling a meeting on Tuesday is that the Speaker of the House of Representatives is back on Monday and can be here beginning on Tuesday. If the members desire to have additional meetings this week, he would like to know. Senator Brown indicated that he would prefer to also meet on Friday. Senator Bennett tentatively scheduled another meeting for Friday. Representative Lopez suggested that if they do meet on Friday to schedule it in the morning.

There being no further business, the meeting was adjourned at 5:15 p.m.

Respectfully submitted,

Nancy L. DeMichele
Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115.)