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SENATE NATURAL RESOURCES

EXHIBIT NO. 6

DATE 3/21/11

BILL NO. SB 409

Admitted in
Montana &
Washington
(*currently inactive)

March 21, 2011

TO: Members, Senate Committee on Natural Resources

FROM: Roy Andes

Re: **Comments on S.B. 409, 2011 Legislature**

Thank you for this opportunity to comment on this proposed legislation. I have served as general counsel to Montanans for The Responsible Use of the School Trust ("MonTRUST") since its founding in 1996, however, these comments are solely mine. They reflect what I perceive as the interest of the trust beneficiaries in light of general principles of trust law. While SB 409 contains some generally good ideas, I believe the legislation must be defeated as written.

1. Competitive bidding. (New sec. 1). In general, MonTRUST has always advocated a return to competitive leasing of cabin sites. Historically, the cabin site lessees strongly opposed competitive bidding. The preamble to the 1983 legislation abolishing it specifically complained that it made lease prices too high, allowing "out-of-staters" to acquire Montana cabin sites. So a move toward a legitimate system of competitive bidding is a *good* thing from the beneficiaries' point of view. However, the devil is in the details. Unfortunately, the details in this proposed legislation are largely a thinly veiled gift to the 800 existing cabin site lessees .

I note a huge contradiction/uncertainty involving New Section 1(1)(a), and existing 77-1-208(3) [as amended]. The new language commands that competitive bidding will be used "for *all* vacant cabin site properties." But the old language in 208(3) retains a non-competitive valuation option. As construed under the present law, the language in 208 grants an automatic right of renewal to current lessees at an administratively determined rental. It is unclear, at best, whether SB409 will continue to give existing lessees this option, or whether it rejects automatic renewal, altogether. As a matter of trust law, *any* form of automatic renewal right, or exclusion of competitive bidding, discourages obtaining full market value.

2. Minimum bids. (New sec. 1). This proposal puts the minimum bid dangerously low, at 1.5% of the most recent cabin site appraisal value. A rental rate of 3.5% was rejected by Judge McCarter as unconstitutional for cabin sites in the first MonTRUST case in 1999, and a permanent injunction exists against applying that figure to all leases. As a mere minimum, this *may* pass constitutional muster. However, since

the injunction rather non-specifically requires the state to collect "fair market value" for the leases, the state remains at risk of contempt of court if the new procedures produce the kind of results found by Judge McCarter to be unconstitutional.¹

Senator Tutvedt has told me he believes the injunction no longer applies. But I am not aware of any such limitation. Senator Tutvedt has also told me he believes that current rental rates are too high, comparing them to his personal grazing and agricultural leases. But, with respect, that comparison is apples to oranges, at best.² *Under the changing circumstances, the court, alone, will decide how extensively it will choose to enforce its injunction.*

3. Existing lessee option. (New section 1(2) & 2(4)(b)). This allows existing lessees to abandon their leases and re-bid, or elect to directly initiate a competitive bid process. Both constitute rather flagrant gifts to current lessees at the expense of the trust. It allows a lessee to default on a legitimate legal contract *without any penalty*, and still retain all his rights. If a lessee defaults, she should be penalized, by a collection action to collect unpaid rental amounts, and certainly by forfeiting the right to re-bid for the lease. Likewise, allowing a lessee to "time the market" for invoking competitive bidding, without any discretion allowing the Board to refuse to allow them to do so, will drive down the value of all leases (a manifestly unreasonable practice under the state's trustee duty of "prudence.")

4. Rental Averaging. New Section 2(b) creates a system that averages winning bids by "geographic location." This unusual invention deprives the trust of most of the benefit of competing bids, and therefore undermines the whole concept. As written, a winning bid, would *never* be a winning bid. It would always be adjusted (most typically downward) by the geographic norm. It would likely prevent obtaining true market valuation of any individual lease property. (An alternative interpretation of this ambiguous language would adjust ALL leases in that geographic location based on the

¹Those results consisted of a number of sales of cabin site improvements containing a "leasehold value;" that is, improvements that sold for more than their appraised value, thus reflecting in-tandem assignment of below-market leases. Prior to DNRC's implementation of Proposal 3b last year, as predicted by MonTRUST during negotiated rulemaking, the system produced *large* numbers of leasehold value improvement sales.

²Agricultural and grazing leases are generally on very large tracts of mostly undeveloped land with no particular scenic or recreational value, as compared with most cabin sites which are small parcels located in choice recreational sites— often on or near recreational water bodies. In addition, the leased uses of agricultural and grazing tracts are either contractually, or practically limited to certain seasonal activities, not year-round unlimited personal use.

newly determined "average," every time a new lease issues. That would create huge uncertainty and administrative cost, by adjusting large numbers of lease rentals at essentially arbitrary intervals).

5. Vacancies. SB409 triggers competitive bidding based on vacancies, without defining what that means. The result could be substantial numbers of un-leased properties producing no income for the trust in violation of the trustee duty of productivity. It would be far better to trigger competitive bidding well *in advance* of any lease expiration, so that the bid process could take place before the lease ends, to avoid interrupting the income stream.

6. Discrimination between existing lessees and competing bidders. All such discrimination is suspect under trust law, as it tends to discourage competing bids, and drive down prices. This legislation contains several.

a. *Lease terms.* New section 1(1)(b)(iii) specifies that bidders "other than the current lessee" must be for a minimum 15 years. The legislation specifies that current lessees get automatic 15 year leases. Any such distinction chills bids, and reduces income.

b. Section 3 amends 77-1-208 (at p.4, lines 1&2) to say that a subsequent lessee may not assume occupancy until both the lease, and sale of improvements have been finalized. But it does not impose similar constraints on out-going lessees required to comply with constitutional duties (e.g., pay rent at the newly established rate so long as their improvements occupy state land, therefore violating ¶¶ 43-51 of the Supreme Court's decision in *MonTRUST*, 989 P.2d 800, at 808-810).

7. CPI rental adjustment. (New Section 1(1)(b)(iv)). Adjusting lease values annually is probably a good idea. But for it to be valid, the procedure establishing the lease value initially needs to be valid.

8. Board responsibility. In several places, this legislation puts the onus on the Land Board to promulgate rules to implement it, and also comply with constitutional obligations (in my opinion, an oxymoronic undertaking). It would thus be the Land Board that takes the heat for an essentially unworkable process.

9. Right to sublease. (Section 3 amending 77-1-208(4)(b)(iii)). This changes current law by allowing lease holder to sublease. In a true competitive bid situation this would be a good thing for beneficiaries, because it would encourage bidders to offer more for this right. But in this hybrid, mostly one-sided system, it simply allows lessees to take advantage of entrepreneurial opportunities that are not ultimately reflected in

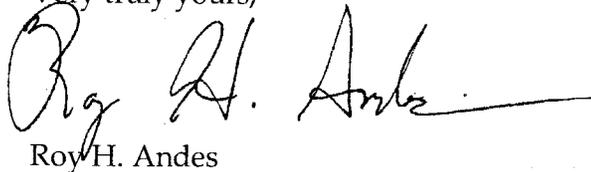
the rents they pay.

10. Repeal of 77-2-319. This is a *good* thing. This statute has inappropriately encumbered fiduciary duties, and should not be on the books. The Board has sufficient discretion to protect choice properties by simply not putting them up for sale.

Conclusion

While nominally invoking competitive bidding for cabin site leases, the details in SB409 largely make it an existing-lessee benefits package. A true competitive bidding process, that legitimately taps the free market for establishing lease value, would put existing and competing bidders on equal footing. It would be triggered by objective events, such as lease expiration, rather than giving options and trigger decisions to the rather small class of existing lessees. Thank you very much.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Roy H. Andes", with a long horizontal line extending to the right.

Roy H. Andes