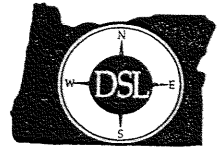


Oregon



The Oregon State Land Board met in regular session on April 11, 1995 in the Land Board Room of the State Lands Building, 775 Summer Street N.E., Salem, Oregon 97310.

Present were:

John Kitzhaber Governor
Phil Keisling Secretary of State
Jim Hill State Treasurer

DIVISION OF
STATE LANDS

STATE LAND BOARD

JOHN A. KITZHABER
Governor

PHIL KEISLING
Secretary of State

JIM HILL
State Treasurer

Assistants

Paula Burgess
Cynthia Griffin
Rollie Wisbrock

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Following a photo session, the meeting was called to order at 9:20 am by Governor Kitzhaber. The topics discussed and the results of those discussions are listed as follows. Further details of the discussions may be obtained in the written transcript of the meeting available at the Division of State Lands, 775 Summer Street N.E., Salem, Oregon 97310 (phone: 378-3805).

Minutes

Request for approval of minutes of
February 14, 1995 State Land Board meeting.

Secretary of State Keisling asked that an amendment be made to the draft minutes submitted to the Board, to more clearly represent his statements at the February 14, 1995 Land Board meeting. The following text was added to page 9 of those minutes.

"He stressed that the Board's fiduciary obligations make it paramount that these lands be used in accord with the activity which will provide the greatest return to the Common School Fund over the long term. He further emphasized that the Board should not create any artificial barriers to maximizing revenue from these lands. Secretary of State Keisling also stated his preference to sell the rangelands if they cannot be managed for revenue production."

Secretary of State Keisling moved the amended minutes be approved. State Treasurer Hill seconded the motion and the approval was unanimous.

Director Gustafson reviewed the history of the Board's approval of the Common School Fund (CSF) investment policy. During the Board's discussion of this issue last December, Gustafson said a request was made for the agency to follow up on several options. The first was enhancing the size of the principal of the fund by reducing or halting distributions for a period of time. Gustafson said this can only be done after a constitutional change, and will need careful involvement with kindergarten-12th grade (K-12) school beneficiaries, due to the impact upon distributions to the schools. Gustafson recommended this option not be pursued farther at this time, except for discussions with the beneficiaries and the Treasurer.

The second option is investing a portion of the fund's bonds and equities into international markets. Gustafson said that after discussions with the Treasurer's Office and Wilshire and Associates, they recommend that up to 20 percent of both the bond and equities portion of the Common School Fund be invested in international markets.

The third option is to eliminate the goal the Board previously set for the Common School Fund--to provide five percent of the total K-12 educational costs. Gustafson said for a variety of reasons, the Fund is moving further away from that goal. He said the goal needs to be reexamined, but it is premature at this time to abandon the goal. He recommended the next year be spent analyzing the other issues outlined in the agenda item; while working with Treasury, the Department of Education, and school beneficiaries. He said in a year, the issue should be revisited to determine whether the goal should be adjusted.

A fourth option is to increase revenues generated by the Division's programs. Gustafson said a number of program areas have been identified with potential for increased revenue, such as in waterway leasing and filled lands. However, he added that in order to increase revenue, it is often necessary to incur additional expenditures.

The fifth option is increasing the percentage of the CSF principal diverted to equities as a means of increasing growth, since equities are the most lucrative return on investments. Gustafson said this could not be done without a statutory change, and also requires some consensus building.

Option number six is to use the CSF to support local school construction projects. Gustafson said start up costs required for engineering and feasibility studies would need to be examined. He said that due to schools' ability to obtain favorable loan rates, this is a scenario that is probably not feasible at the present time, but should be explored further.

Option number seven is to diversify the fund further by investing in real estate. During a previous meeting, Wilshire and Associates advised strongly against real estate investments, saying the fund is not large enough to bear further diversification in a high-risk investment portfolio such as real estate. Gustafson said investment in the Dammasch property near Wilsonville was a unique and rare opportunity. At this time, though, he said the staff recommendation is not to proceed with further real estate investments unless a similar opportunity arises.

An eighth option is to use the fund to support state (as well as possibly local) government capital construction projects. For example, the Division of State Lands' building has proven to be a productive investment of the Common School Fund. A formal recommendation on this option will be made later, after further scrutiny.

Gustafson then reinforced the recommendation to leave the current goal of contributing five percent of the total costs for K-12 education intact for another year. He also restated the recommendation for investing up to 20 percent of each of the Common School Fund equity and bond portfolios into an international stock index fund and international bond fixed-income fund.

Dan Smith, Director of the Investment Division of the Treasury, reviewed the progress made in implementation of the investment policy target that the Board had previously adopted--45 percent fixed income, 50 percent equity, and five percent cash. He said these targets are essentially met. The value of the CSF has increased from \$245 million to \$303 million in the last three year period.

Smith said Treasury agrees with the recommendation to invest up to 20 percent of each of the equities and the fixed income portfolio internationally. Treasury recommends beginning with moving toward a ten percent allocation in both.

Jay Fewel, Senior Equities Investment Officer at Treasury, discussed the equities market performance over the past ten years and the portfolio of the CSF investments in relation to equities.

Bill Unverzagt, Senior Fixed Income Officer at Treasury, discussed the bond portion of the fund. Regarding investment in international funds, he recommended using the EFA and Wells Fargo index to allow for diversification and to take advantage of attractive market returns.

Secretary of State Keisling asked whether the 50 percent target on equity investments is a ceiling set in the constitution. Smith affirmed that it was. Keisling asked if the Board should

consider removing or modifying that ceiling. Smith said that would allow greater flexibility, but that would be a Land Board policy decision.

State Treasurer Hill moved that the Board 1) initiate discussions with the Department of Education regarding reducing the goal of the CSF contributing five percent of the cost of K-12 education, and 2) authorize Treasury to invest up to 20 percent of each of the CSF equities and bond portfolio in the international stock index fund and international bond fixed income fund. Secretary of State Keisling seconded the motion and the decision was unanimous.

Scenic Waterway Request by Rogue River Jet Boat Tours to renew their removal-fill permit to enhance channel depth within the Rogue River Scenic Waterway.

Gustafson said authorization for this channel deepening is necessary once every three years to allow for navigability of all types of craft. He said the work is done in the early morning on one day, so impacts are localized and not substantial. The application is consistent with the provisions of the Scenic Waterway Act, and other authorizing agencies with responsibility are in agreement. Spawning of Chinook salmon is not known to occur in this stretch of the river. Gustafson said this is an existing permit that would be renewed, if approved by the Board. He said the project is also necessary for safety to allow watercraft to travel the river.

Governor Kitzhaber asked when the work was last done and if there was any degradation of fish habitat. Gustafson replied that it was last done 3-4 years ago, and that no degradation of habitat has been noted.

Secretary of State Keisling moved the item be approved. State Treasurer Hill seconded the motion and the approval was unanimous.

Scenic Waterway Request by Rogue Mail Boat Services, Inc. to renew their removal-fill permit to enhance channel depth within the Rogue River Scenic Waterway.

Gustafson said this is a similar request to the one from Rogue River Jet Boat Tours, but involves a general authorization for propwashing to blast out sediments within pockets of the river where there have been accumulations (in up to 44 different locations in the lower 23 miles of the river). He said since this application is in the extreme lower end of the river, there is no known salmon spawning activity. The project has been reviewed by all applicable state agencies and the US Forest Service, who has upland ownership in the area. Gustafson

concluded by saying this project is consistent with the provisions of the Scenic Waterway Act.

Secretary of State Keisling noted that renewals will not automatically occur for existing permits such as these. He said each will be considered on an individual basis to ensure there are no adverse consequences. Secretary of State Keisling moved the item be approved. State Treasurer Hill seconded the motion and the approval was unanimous.

Scenic Waterway Request for approval of a scenic waterway emergency removal-fill permit issued to the Oregon Parks and Recreation Department for work in the Deschutes River Scenic Waterway.

Gustafson said that flooding late last January resulted in a wash-out of the access road into Heritage Landing State Park, as well as a bridge abutment. An emergency removal/fill permit granted by the Division allowed State Parks to rebuild the access road and the bridge to provide for public access into the state park. Gustafson said the permit request was reviewed by all of the agencies and was found consistent with the emergency provisions in the scenic waterway permit rules as well as applicable law.

State Treasurer Hill moved the item be approved. Secretary of State Keisling seconded the motion and the approval was unanimous.

Legislative update

Director Gustafson reported that the agency's initial budget review had been favorable. He said nine of the Division's 11 program option packages were approved by the Ways and Means Natural Resource Subcommittee. The agency must still go before the Joint Legislative Committee on Information Management and Technology for a review of the computer request and the related position.

Gustafson reported there was concern among some Ways and Means subcommittee members regarding implementation of the indigenous salmonid habitat program (Senate Bill 81 from last session) without adequate funding. He said rule hearings for this program are currently in process with draft rules set to require permits for any amount of removal done in the specially designated habitat areas. The funding for this program is through lottery dollars that will extinguish at the end of the current biennium. The program would then have to be absorbed by the agency without funding. The committee wanted to explore other options for funding of the program.

Gustafson said a number of other bills could potentially affect the agency, and these are outlined in the written agenda materials.

Short-term Agenda Update

Director Gustafson reviewed the 4-year short-term agenda with the Board. The written materials indicate how the agency has progressed on each item. Gustafson said that the Board should keep the existing agenda, not adding items to it until after the directives come out of the legislative session. In six months, after the session is over, Gustafson said the agency would return to the Board to recommend elimination of some items that have been completed and to propose new items.

Secretary of State Keisling noted his concern regarding the Legislature setting artificial barriers which preempt or otherwise interfere with the Division's ability to generate revenue. Waterway leasing is a good example. He underscored the importance of the Division providing the legislature with examples of these barriers.

State Treasurer Hill asked when the Asset Management Plan would be finished. Director Gustafson responded that it is slightly behind schedule, but is anticipated to be finished in the fall of this year (1995).

Long-range Forest Management Planning Update

Jim Brown, State Forester, gave a general overview of the long-range planning efforts for the common school forest lands. Jill Bowling, State Lands Program Director, discussed the three long-range plans. The first, a draft plan for the Elliott State Forest, includes a Habitat Conservation Plan (HCP) developed in conjunction with the U.S. Fish and Wildlife Service (USFWS) to allow an incidental take permit for both owls and murrelets on the Elliott Forest. The draft plan, along with the environmental assessment, an implementation agreement and the permit application were submitted to USFWS in December of last year. Since then the documents have gone through further review, negotiations, and changes to meet the USFWS' legal requirements. The next step is for USFWS to place a notice in the Federal Register, with a 30-day public comment period. After that period, USFWS will analyze the comments and make a determination whether to issue a permit through the HCP. Bowling said the process has taken longer than originally anticipated, but they hope to have the Elliott long-range plan to the Board for approval later this year.

Governor Kitzhaber asked why there had been delays. Brown said, among other things, one issue had been a constant changing of USFWS biologists, each with a different set of views on what the basic contents of the plan should be. Governor Kitzhaber said his office would get involved, since they have a scheduled meeting with Mike Spears, the USFWS regional director.

Bowling said the Eastern Oregon Plan has been a simpler process. It is scheduled to be completed by October 1995. The planning team is finalizing a draft plan to be reviewed by staff, then released for public comment in May. The draft plan should be brought as an informational item to the Board in August, then a final plan for approval in October.

The Northwest Forest Plan began in early 1994. Most efforts to date have been concentrated on data collection and analysis. Guiding principles and draft goals have been developed and are being reviewed at public meetings. The next step is to begin developing strategies designed to meet the goals. One of the next major decisions is to determine whether the federal Endangered Species Act obligations can best be met through a habitat conservation plan process or through another approach. The draft plan should be to the Board in March 1996, with a final plan anticipated to the Board in November 1996.

Asset Management Plan update

John Lilly, Assistant Director for Policy and Planning, reviewed the progress on the Division's asset management plan. Lilly said that decisions on the Land Board's real estate investments had been largely made on an ad hoc basis over the last 130 years. The Asset Management Plan, he expects, will be a usable, working document to direct decision making over the next five to ten years. Lilly recognized the work of Jim Owens and Arnold Cogan from Cogan Owens Cogan, the consultants on this project. He also recognized the contributions of David Blum and Jeff Kroft of the Division.

Lilly said a draft plan should be brought to the Board sometime in August, with the public involvement process in the fall. A final plan is expected to be to the Board next fall for consideration.

Secretary of State Keisling asked if information was available to break down costs for determining the return on investments with a level of detail that allows us to prioritize. Lilly said information is available for that. He said they are attempting to do some of that, but also trying to stay at the policy, decision-making level, in the development of the plan.

Secretary of State Keisling said the Elliott represents ninety-six percent of the actual value of our land assets. The return on the Elliott was only approximately 1.3 percent last year. Because of this, he said a high level of detailed information for this property is necessary.

In the past, when discussions have occurred regarding sales of rangeland assets, he said these discussions usually centered around the isolated parcels. He said the Board must also seriously consider selling larger areas that are blocked, especially if the court decides to lock us into extremely

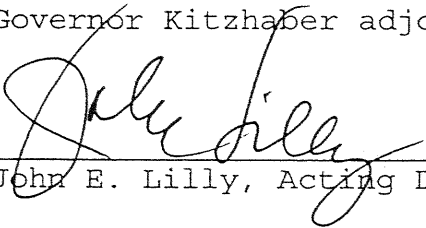
long-term contracts, or if the legislature puts a ceiling on lease rates. He said information must be available to the Board to allow them to make those decisions.

State Treasurer Hill asked if there were studies showing the benefits of selling the assets versus retaining them. Lilly said he is working with subconsultants to try to model this currently in a spreadsheet fashion with the variables, charting results over time.


Other Items

Director Gustafson announced that Cresmont, Inc. (with whom the Division has a lease at North Tongue Point) has signed a five-year sublease (with a five-year option to renew) with Pacific Marine and Steel, Inc. As a result, Gustafson said Cresmont expects to be able to add 150-175 new jobs to the Astoria area. This is the first large sublease commitment which will help ensure fulfillment of the terms of the Division's lease with Cresmont.

Governor Kitzhaber adjourned the meeting at 10:25 am.



John E. Lilly, Acting Director



John A. Kitzhaber, Governor