

The State Land Board met in regular session on April 6, 1999 in the Land Board Room of the State Lands Building, 775 Summer Street NE, Salem, Oregon 97310.

Present were:

Phil Keisling Secretary of State

Jim Hill State Treasurer

Assistants

Paula Burgess
Rollie Wisbrock
Rick Hanson

Staff

Paul Cleary
John Lilly
Steve Purchase
Gary Van Horn
Gail Lowry

Dept. of Justice

Bill Cook
Roger Alfred

Secretary of State Keisling called the meeting to order at 10:07 am. 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 NE, Salem, Oregon 97310 (phone: (503) 378-3805).

CSF

Annual review of the Common School Fund investment policy and performance, and discussion of alternative distribution policies.

Director Cleary said 1998 was another outstanding investment year with the Common School Fund value increasing about \$130 million or 22.6 percent to \$704 million. He stated that in the past six years the Fund balance has almost tripled. Cleary introduced Dan Smith, Director of the Investment Division of State Treasury, to provide an overview of the investment strategy.

Smith agreed that it had been an excellent year in terms of the market, with the returns on stocks being up 28.3 percent annually the past three years and exceeding 20 percent annually for the past four years in a row. The total Common School Fund returned 20.7 percent for the year and 18.6 percent compounded annually for the three-year period.

He noted the investment strategy the Oregon Investment Council (OIC) has been following is to move the equities to the highest possible level consistent

with the Land Board's distribution policy, while also keeping within the statutory limit of 65 percent at cost (currently at about 40-44 percent).

Smith reported the equity allocation, combining international and domestic, is 67 percent of the Fund's market value; and the fixed and short-term income investments are at about 33 percent of the Fund's market value. State Treasurer Hill commended Smith and the investment staff for the work they have done.

State Representative Al King said the Common School Fund is a remarkable example of financial stewardship and a rare example of Oregon's investing for our future. He said we should be thankful for the financial oversight and the planning of earlier Land Boards and the Division of State Lands for the excellent management responsibility toward the Common School Fund.

King said he supports continuing the balanced approach to managing the securities portfolio of the Trust Fund and its continued growth to eventually become a multi-billion dollar portfolio; but said that distributions from the Fund could be increased to address intergenerational equity between current and future students. He recommended the Land Board adopt a policy of reviewing the most recent five-year period when the Legislature is in session. He proposed if the total five-year average annual return is ten percent or greater, the distribution rate should be five percent per annum for the two years of the biennium. When the five-year average return rate is below eight percent, he suggested the distribution rate should be one-half of the average return rate, but never falling below two percent.

King added that the Board should consider the fiscal responsibility of the Legislature and their resolve to address the school funding needs by providing a strong K-12 budget. He said if the Legislature applies too little General Fund commitment for school funding, then the Common School Fund should not be used as a fiscal crutch to encourage a lack of vision about school funding issues.

King provided a list showing the average five years' returns over the past seventy years for the S&P 500 Index and a Common School Fund 10-year revenue projection chart. King said he has submitted a House Joint Resolution for the Legislature to urge the Board to adopt a five percent distribution rate from the Common School Fund during times of investment prosperity.

Secretary of State Keisling said the Fund was distributing about 4 percent a few years ago, but has fallen to about 1.6 percent currently. He said this happened through a combination of good investments, performance and a decision to keep a modest but sustainable level of distributions to build up the portfolio.

Director Cleary agreed saying the decline in distribution levels starting in 1988 reflected a movement into equities. He said as this occurred, all the new revenues were put into equities with a decision to retain dividends and capital gains in order to grow the Fund as quickly as possible (a policy adopted by the Board in 1992 and reviewed again in 1994). In the 1990s a decline in bond earning based distributions occurred because the bond climate was changing.

In 1996 the Board decided to reverse the downward trend by fixing distributions beginning at \$10 million a year and increasing 5 percent annually. At that time distributions were between 3-5 percent of Fund value, taking land management expenses into account.

Representative King added that the reason the distributions declined to 1.6 percent was not due to varying from the distribution rate, but because the asset had grown larger.

Representative Lundquist applauded the Board for the fiscal responsibility they have brought to the process. He said education is the foundation of our society and nation and stressed the importance of adequate funding for K-12 students. He said the Board has the opportunity at this time to step up and be a leader in an area needing some leadership. He said if the state can spend 4.95-4.96 million dollars, this will allow some investment dollars to be put back into K-12, instead of disinvesting. He said this probably won't happen without some help from the Board increasing their distributions, as stated by Representative King. Lundquist added that he also agreed with Representative King that if the Legislature is not willing to fund education in an adequate way, then the Board shouldn't raise the distributions.

State Treasurer Hill said the decision to change distributions rests on the Land Board itself, working within the legal framework of the Constitution. He commented that sometimes people look at the Common School Fund as a "slush fund," which it is not, but rather it is a trust fund that the Board is to protect and they have guidelines to do that. He commended the legislators for bringing the proposal to them, but emphasized that if the Fund were left invested and allowed to grow (and perhaps the Legislature would even make contributions to it), it could later pay a substantial amount of the total cost of education.

Hill said that since he became Treasurer the Fund assets have gone from \$200 million to \$700 million dollars, and this has been achieved years before it was expected. He commented that the Fund distribution is a relatively small amount of money compared with the very large problem of fully funding education, but again reiterated that the Fund could pay great dividends in the future if left alone.

Hill commended Representative Lundquist's and King's support for education. He reminded them that the Board needs to look at the legal constraints placed upon them by the Constitution as to what can be done with the Common School Fund.

Representative Lundquist said the distribution using Representative King's proposal could be a rather significant portion of the extra needed funding. Lundquist said he doesn't believe we can wait a number of years before investing in the schools and fixing the system.

Secretary of State Keisling remarked that both King and Lundquist stressed the Board's partnership with the Legislature, noting that the Legislature has the primary obligation for school funding. Keisling asked by what gauge the Land Board would know that the Legislature has fulfilled its obligation. He believes there should be a compromise on both sides. King said there is a mandate to build prisons, but added that the strongest mandate of all may be educating our children.

Keisling said he has been struck with the failure of the Legislature over the past 15 years to look at the future or, as he described it, to play the ant in the kid's story of the ant and the grasshopper. The only place he's seen the forethought of the ant in state government, he said, is with past Land Board decisions that looked to the future, allowing us to be here today with \$700 million in the bank.

He said if the state had invested the kicker money into the Common School Fund, rather than returning it since 1983, the Fund today would be at \$3.7 billion. A five percent distribution of that amount to the schools would be \$180 million per year. In the year 2008, the Fund could be at \$8.5 million, assuming a nine percent investment return. Keisling added that these are amazing numbers. He asked whether there had been discussions at the Legislature of taking just a portion of the kicker and investing it in the Common School Fund. Neither King nor Lundquist were aware of plans for that. Keisling said he'd like that to be considered for the future biennium.

Hill said in 1982 when he was elected to the Legislature, the state was doing poorly economically, but seemed to take better care of the schools at that time than currently when the economy is much stronger. Touring the schools today convinces him that education isn't receiving the funding it deserves. He characterized education as the great equalizer in our economy, saying it's a shame that in this time of prosperity we're skimping on funding schools. If the problem is solved temporarily with a quick fix, he questioned what plan there would be for steady funding for the future, to prevent having to fight over this each session. Lundquist agreed with the issue saying that everyone needs to be willing to commit to changing that. He said a successful dialogue needs to take place about this with Oregonians. He said if this doesn't happen, we'll be back in two years from now with the same problem. In which case, he said, the money should be left in the Common School Fund to grow.

Keisling thanked both Representative Lundquist and Representative King for their leadership in bringing the proposal forward. He said the message is clearly a challenge and an opportunity.

Cleary noted that agenda materials were available containing several charts showing distributions at different levels of assumed Fund growth and what the effect of increasing distributions today would have on the future Fund balance. He said the Board is ahead of the schedule that predicted the Fund would grow to \$884 million by 2006. Cleary commented that the Board is faced with the issue of whether to revisit the strategy of distributions. He reported that the agency has made a request for advice regarding expenditures and distributions from the Attorney General's Office. He said the Division has been asked to run projections using some bear market scenarios. He added that the agency plans to return to the June Board meeting with this information and perhaps the Attorney General's advice, if ready, to allow the Board to review the Common School Fund distribution levels and policies.

State Treasurer Hill moved the Board should provide general guidance on distribution goals and policies for the 1999-2001 biennium with staff to develop additional recommendations for consideration at the Land Board meeting in June. Secretary of State Keisling seconded the motion, and the approval was unanimous.

Easement

Request by AT&T Corporation for a statutory easement for an oceanic fiber optic communication cable corridor over state-owned submerged and submersible lands of the Territorial Sea and landing at Bandon.

Director Cleary introduced this request by AT&T for an easement for two additional oceanic fiber optic communication cables in the same general vicinity of cables laid in 1994. He said a number of discussions have occurred with AT&T and various fishing interests regarding how to best resolve potential conflicts between the cable location and fishermen. Cleary said while fishing is not legally prohibited over the cables, it is actively discouraged due to damage potential, liability concerns, and individual safety concerns. An addendum was given to the Board regarding the agreement between AT&T and representatives of the fishing industry on measures to mitigate conflicts. The agreement needed fine tuning, which Cleary said had been worked on that morning. Cleary introduced Ellen Brain, Deputy Director of cable operations for AT&T, and Scott McMullen of Astoria, representing the fishing industry.

McMullen said he is chairman of the Oregon Fishermen's Undersea Cable Committee, a group formed to facilitate discussions between WCI, a cable company in the process of bringing a cable from Alaska into the Oregon waters and ashore near Rockaway. He said he also had been part of the negotiating group of fishermen meeting with AT&T to discuss this cable project called China US Network. He said he's pleased to report that some agreements have been reached after several months of discussion, with assistance from the Department of Fish and Wildlife, Division of State Lands, Department of Land Conservation and Development, the Governor's Office, and representatives of the Coastal Caucus.

Brain said there has been a breakthrough in working with the fishing industry to more cooperatively benefit both the industry and AT&T. She said AT&T is thrilled that they have an agreement with the fishermen. She said they know there will continue to be issues and concerns, but that this will provide a learning experience of benefit to both groups. Brain outlined the fine tuning that took place this morning in their discussions. She said two changes were made since the April 5 letter outlining the agreement. One of those changes was the way in which expenses would be handled. She said the expenses of the fishermen to date (travel, living, tolls and meals) would be covered by AT&T in full, with payment made by AT&T for one-half of the fishermen's hours as they were involved in negotiations for the agreement. She added that the fishermen have been reasonable and cooperative (though tough) in their dealings with her.

The second change was to remove the last sentence of paragraph four, dealing with a possible reduction in financial terms based on some conditions. Brain added that AT&T plans to continue to work with the fishermen to select the most appropriate route for any future cables. McMullen said, based on their agreement with AT&T, the fishermen would urge support and approval of AT&T's permit and easement.

Cleary said the decisions made today were the details for minimizing impacts on the fishermen, but the basic previous agreement remains the same. He reviewed the three components of the agreement: AT&T, in consultation with the fishermen, will relocate a portion of the southern leg of the proposed cable inside the two existing cables to cut down on the width of the corridor; all of the provisions of the separately negotiated California agreement will be implemented here in Oregon; and in recognition for the great potential for conflict and the higher value of fisheries off the Oregon Coast, AT&T has agreed to a one-time payment of \$1.25 million that will capitalize a trust fund that will be dedicated to fishery enhancement and research projects.

Another concern that surfaced during the review was the question of local access to AT&T's cable optic network both seaward and landward of the Bandon facility. Cleary said AT&T was encouraged to work with coastal communities by doing a profile of existing system technologies and specifications, so those in the area could realize what they have, be able to take full advantage of it and be able to market it. AT&T is to work with the community to evaluate existing and potential telecommunication needs within the various sectors of the economy, and do a technical and cost feasibility analysis of the desired service and infrastructure improvements. Cleary said AT&T was requested to complete this by the end of this calendar year when the line is scheduled to go into operation.

Laura Imeson, AT&T State Government Affairs, said they have been in discussions with the members of the Coastal Caucus about community needs, as well as talking to people in the community. She has engaged the network planning part of AT&T in a discussion about facilities in the coastal community and said she will be having further discussions in the community to work on a plan to ensure that all needs are addressed. A report will be sent back on these findings by the end of the year.

Cleary said their recommendation is that the Board approve the issuance of the easement for the two new Bandon cables for a 20-year term that would include a governing law provision that if the law changes the Division has the opportunity to recover a consideration payment. All the other standard terms will apply and the easement would be subject to the AT&T Oregon fishing industry agreement. In addition, AT&T committed to cooperatively address telecommunication capabilities and needs in the Coos Bay area.

Darla Hamblin, at the request of Representative Ken Messerle, presented information about her company, Consolidated Media, LLC, that has recently reached an agreement with AT&T to bring fiber optic DS-3 to their facility in Coquille. She said her company's primary interest in this direct, high-speed connection is to facilitate the serving of the company's quality search engine directory and the Internet broadcast network.

She said it also offers opportunity to provide dial-up, networking and co-location services to the entire south coast region. Her company proposed an internship program to AT&T for education and economic development in cooperation with Southwestern Oregon Community College and the local area high schools, in addition to being able to guarantee connectivity to every point in Coos County. She said though the latter efforts have been overlooked, they are hopeful that AT&T will join them in their partnership in efforts to renew and invigorate the local global economy in Coos County through the infrastructure of digital fiber.

Hamblin said the fiber optic cable entering from the Pacific to this region is a huge opportunity for the economy and quality of life. She said it should be utilized to the benefit of the entire south coast area.

Onno Husing, Director of Oregon Coastal Zone Management Association and a member of the Oregon Policy Advisory Council, thanked all involved in this process. He said there will be a lot of other cables and companies wanting to place cables and he stressed the need to have a broader framework in place for how these cables are handled, so the process that has gone on over the last few months isn't repeated. He said the state needs to establish some corridors and encourage these kinds of cables to go through them.

Cleary recognized Ellen Brain, Steve Pfeiffer, Gary Smith, Laura Imeson, Scott McMullen, and the other fishermen for their efforts. Cleary added that they have taken to heart the advice from Husing and individuals from several coastal Ports regarding the need for holding a public meeting in the affected area of any future cables and looking for better routing, cable corridors and for a long-range strategy. He said the Division will also seek for a consideration payment for the state easement, if the statutes can be changed.

State Treasurer Hill moved approval of the easement and agreement as described by Director Cleary. Secretary of State Keisling seconded the motion and the approval was unanimous.

Easement Request by Pacific Fiber Link for an easement for a fiber optic communication cable conduit over state-owned submerged and submersible lands on the Willamette River in Clackamas County near Canby.

Cleary introduced this item for an inland fiber optic communication cable running from Portland to Springfield. He said the only state land involved in this is the stretch of the Willamette River 1750' long by 15' wide near Canby. The cable use is not a regulated activity, environmental issues have been handled and it doesn't

qualify for free-of-charge easement, so a consideration payment of one-third of the adjacent upland value would be required, equal to \$16,890. Cleary said the agency's recommendation is to approve the cable easement for the 20-year period for \$16,890.

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

Consent Agenda

Administrative Rule Request for authorization for the Division to file a temporary rule concerning renewal of removal-fill permits and to initiate permanent rulemaking.

NHAC Request for approval of (1) the addition of eight sites to the Oregon Register of Natural Heritage Resources, six owned by the Oregon Parks and Recreation Department and two owned by The Nature Conservancy; and (2) the addition of a tract to a Nature Conservancy site already listed on the Register.

Territorial Sea Request for adoption of the Minerals Management Service's 1998 Supplemental Official Outer Continental Shelf Block Diagrams for the State Seaward Boundary of the State of Oregon.

Minutes Request for approval of the minutes of the February 9, 1999 State Land Board meeting.

Cleary briefly reviewed each of the four items on the Consent Agenda. State Treasurer Hill moved the items on the Consent Agenda be approved. Secretary of State Keisling seconded the motion and the approval was unanimous.

Informational Agenda

Waterways Status Report on Waterway Improvement Inventory.

Forests Status Report on Draft Northwest and Southwest Forest Management Plans and Draft Western Oregon Habitat Conservation Plan.

Legislation Legislative Update.

Director Cleary said that written materials were available for the status report on the Waterway Improvement Inventory and the legislative update.

Cleary introduced Mike Bordelon, State Forest Manager, and Jim Young, Manager on the Elliott State Forest. Mike Bordelon discussed the development of the drafts for the Northwest Forest Management Plan, the Southwest Forest Plan and the Western Oregon Habitat Conservation Plan.

Bordelon said there has been an excellent partnership and cooperation since the inception of the process with the Oregon Department of Fish and Wildlife. He commented that the plans are as much about how to develop fish and wildlife habitat, as they are how to produce timber and revenue. He said Forestry's management philosophy is one of concurrently producing timber, while protecting threatened and endangered species. With the development of the Habitat Conservation Plan, he said there has been excellent collaboration with the US Fish and Wildlife Service (USFWS) and the National Marine Fisheries Service (NMFS).

He said as they have developed conservation strategies for threatened and endangered species, they worked closely with the biological staff of these organizations and got close to agreement on a variety of areas, such as riparian, owl and murrelet strategies. Within the next few months these conservation strategies will be finalized with USFWS and NMFS and brought back before the Board of Forestry and the State Land Board for review and approval.

He discussed the process which emphasized an early and continuous public involvement. Thirty public meetings, two workshops and six field trips with members of the public took place. In addition, two advisory committees were formed; one for the forest management plans and the second specifically for the Habitat Conservation Plan (HCP). The second, the Public Interest Committee, involved a variety of interest groups and stakeholders--representatives of the Division of State Lands, counties, fishermen, and other persons with recreational interests. Liaison members included those from USFWS and NMFS, Representative Bryan Johnston chaired the Committee and skilled facilitators were hired to oversee the process. USFWS commented that the HCP Forestry is developing has had more public involvement than any other HCP on the west coast.

Forestry commissioned Oregon State University to conduct an independent scientific review of the draft HCP and Forest Management Plans. Twenty-six different scientists were employed to review the conservation strategies and provide a thorough critique of the draft plans. Bordelon said Dr. John Hayes, coordinator of the review, applauded Forestry for its work.

Bordelon said they are at the point of taking the information from these committees, from the public and from the technical side of the reviews and blending the information together.

Jim Young, District Forester for the Coos District Department of Forestry, said a Task Force was formed last fall with a number of local representatives from Coos County, the Department of Fish and Wildlife, Department of Environmental Quality, Division of State Lands, USFWS, NMFS and two local watershed associations to examine riparian aquatic strategies on the Elliott State Forest. The group will develop recommendations to the Department on whether changes are needed—ensuring fish are being protected in the streams on the Elliott.

The Task Force has met four times, reviewed material on the forest and management of state lands in general and had a field trip where they viewed sites on the Elliott. They compared the strategies of the Elliott and the Western Oregon HCP in some detail. He said they will probably continue meeting until late in the summer, at which time they will make recommendations to the Department.

Secretary of State Keisling asked about stream buffer requirements, and what kind of effects these will have on harvest levels. Young said rough estimates show the requirements may reduce the amount of harvest by about two percent.

Young added that information on timeframes is available in the material packet the Board received. He said the Department plans to return to the Board of Forestry in September, then afterward to the Land Board with a request to submit the Western Oregon HCP to the federal services.

Other Issues

Cleary said there has been some interest in Astoria regarding proposals to use North Tongue Point for ship demobilization and recycling activities (shipbreaking) and a public town hall meeting is scheduled with the city council and Cresmont for next Monday. Steve Purchase will attend with Cleary and they will report back.

This afternoon the Senate Water and Land Use Committee is taking up a navigability bill/recreational use/floatage easement bill that reflects concepts the agency shared with the joint interim committee and Cleary will support the bill in an attempt to try to reach a balanced resolution of the problems we've been struggling with as a state for 140 years.

Bill Montgomery spoke briefly on the proposed waterway leasing rates. He said in the public meetings he has attended, the overwhelming public support has been for the graduated flat rate model and against the choice model. Montgomery also provided the Board with written testimony. Secretary of State Keisling reminded Montgomery that this issue would be discussed at the June Land Board meeting and that he would be welcome to provide additional testimony at that time.

The meeting was adjourned at 11:37 am.

John A. Kitshaber, Governor

Paul R. Cleary, Director