November 12, 1997

Representative John Cobb
P.O. Box 388
Augusta MT 59410-0388

Dear Representative Cobb:

I am writing in response to your request for an analysis of the lease involved in Seven-Up Pete Joint Venture and the authority of the Board of Land Commissioners (Board) with regard to the McDonald Meadows project contemplated under the lease.

The issues involved are complex and require an analysis of The Enabling Act, various provisions of the Montana Constitution, state laws, administrative rules, and the lease. For purposes of this analysis, references to the "Department" are to the Department of Natural Resources and Conservation, the agency that succeeded to the functions of the former Department of State Lands in July 1995.

General legal background

A general discussion of the necessary legal framework may be helpful in understanding my response. The conditions imposed on state lands and the funds resulting from their sale or lease are generally found in The Enabling Act and the Montana Constitution. The conditions upon the disposal and use of lands granted to the state by the federal government at the time of Montana's admission to statehood have been fairly heavily litigated, so there is a significant body of case law concerning some aspects of state land law.

The federal government granted lands to the state for the following purposes: (1) support of common schools; (2) state government buildings at the capital; (3) university purposes; (4) a penitentiary; (5) support of an agricultural college; (6) a school of mines; (7) normal schools; (8) a reform school; and (9) an asylum for the deaf and dumb. There are some restrictions on the usage of some land grants that are not applicable to others.

In the case of State ex rel. Evans v. Stewart, 53 Mont. 18, 161 P. 309 (1916), the court discussed the limitations contained in The Enabling Act as follows:

> With respect to the lands granted for common school purposes, the Enabling Act fixes a minimum sale price and declares that the proceeds from such sales, together with five per cent of the proceeds from the sales of public lands in the state, shall constitute a permanent school fund the interest from which only shall be expended. It also provides that the lands granted may be leased under regulations prescribed by the legislature of the state, with a limitation upon the term of any such lease and upon the quantity which may be let to any individual, company or corporation. . . . Of the lands granted for university purposes it declares that they shall not be sold for less than $10 per acre, but may be leased in the same manner as provided in section 11 (common school lands). With reference to the grants for capitol building and penitentiary purposes, it prescribes no restrictions or regulations whatever. . . . The only limitation imposed with reference to the other grants enumerated above is that: "The lands granted by this section shall be held, appropriated, and disposed of exclusively for the purposes herein mentioned, in such manner as the legislatures of the respective states may severally provide." Id. at 22.

The distinctions placed on the various types of land grants came into play in a case involving the normal school land grant. The court found that the provision of The Enabling Act providing a land grant for normal schools pertained only to the manner of the management and disposition of the lands themselves. It did not control the funds derived from the sale or leasing of the lands. The funds derived from the sale and leasing of the lands passed to the state and could be disposed of as the state saw fit, subject only to the condition that the funds must be used exclusively for normal school purposes. The 1889 Montana Constitution, however, limited the usage of the normal school land grant proceeds. State ex rel. Haire v. Rice, 33 Mont. 365 (1906).

The 1972 Constitution has carried forward the pertinent restrictions on the use of state lands and land grant trusts from the 1889 Constitution. Article X, section 3, of the constitution provides that "The public school fund shall forever remain inviolate, guaranteed by the state against loss or diversion." Article X, section 5, of the constitution requires that 5% of the interest from the public school fund and 5% of all income from school lands must be added to the public school fund and become an inseparable and inviolable part thereof. Article X, section 10, of the

constitution provides that university system funds are inviolate and sacred to the purpose for which they were dedicated. They are also guaranteed by the state against loss or diversion. Article X, section 11, of the constitution deals with the disposition of all state lands and interests in state land as follows:

> **Public land trust, disposition.** (1) All lands of the state that have been or may be granted by congress, or acquired by gift or grant or devise from any person or corporation, shall be public lands of the state. They shall be held in trust for the people, to be disposed of as hereafter provided, for the respective purposes for which they have been or may be granted, donated or devised.
>
> (2) No such land or any estate or interest therein shall ever be disposed of except in pursuance of general laws providing for such disposition, or until the full market value of the estate or interest disposed of, to be ascertained in such manner as may be provided by law, has been paid or safely secured to the state.
>
> (3) No land which the state holds by grant from the United States which prescribes the manner of disposal and minimum price shall be disposed of except in the manner and for at least the price prescribed without the consent of the United States.
>
> (4) All public land shall be classified by the board of land commissioners in a manner provided by law. Any public land may be exchanged for other land, public or private, which is equal in value and, as closely as possible, equal in area.

The cases interpreting The Enabling Act and the constitutional provisions governing the land grants establish the parameters within which the Legislature may act in dealing with the lands. In State ex rel. Koch v. Barret, 26 Mont. 62 (1901), the court found that the lands granted by Congress became a trust. The funds derived from the lands were trust funds to be devoted exclusively to the purpose of the trust through the agency of the state. The leasing of trust lands was determined to be a viable method of fulfilling the trust responsibilities.

Factual statement

With this general framework established, I will address the specific issues raised by your request. Apparently, there are no significant factual disputes regarding the project. In 1986, the Board issued five mineral leases to Western Energy Co. In 1989, a sixth mineral lease was issued to Western Energy Co. The original primary term of all the leases was 10 years and so long thereafter as paying quantities of minerals were being produced. In 1991, Western Energy Co. assigned the leases to the Seven-Up Pete Joint Venture and the Board approved the assignment. At the time of assignment, the Seven-Up Pete Joint Venture consisted of Phelps Dodge Mining Co. as majority partner and Canyon Resources Montana Corp. as minority partner. Serious development of the leases began in 1994. By 1994, the leases were in danger of breach as a result of the failure of the lessee to diligently develop the properties. An application for an

operating permit had not been filed. At that point, Seven-Up Pete Joint Venture negotiated with the Department, and an agreement was reached. The modification was discussed with the Board. The modification consolidates the leases into a "managed unit" for the purposes of present and possible future mining operations and related surface uses. The primary term of the "managed unit" is extended for a period equal to the permitting period, including any delay related to judicial or administrative proceedings regarding the underlying leases. Pursuant to the modification, the production of minerals in paying quantities from any land contained in the project applies to all leases. In November 1994, Seven-Up Pete Joint Venture filed its proposed operating plan and permit application for the "managed unit", the proposed McDonald Meadows project. The proposed operating plan involves only three of the original leases. The proposed operating plan calls for all mined ore to be produced from only one of the original leases. The land subject to the producing lease was granted to the state by the United States for the School of Mines. The other two leases in the proposed operating plan will be used for waste rock storage. One of those leases involves land granted for the Montana School for the Deaf and Blind, and the other is school trust land. The other three leases in the "managed unit" involve land granted for the support of public buildings (capitol land grant) and school trust land. In September 1997, Phelps Dodge sold its interest to the minority partner. Several questions have been raised concerning the validity of the 1994 agreement and the authority of the Board concerning the project.

Specific allegations

It is alleged that the 1994 agreement and subsequent lease concerning the Seven-Up Pete Joint Venture are void or voidable for several reasons. The original reasons were expressed in an unsigned draft petition. The reasons were revised in a letter dated October 30, 1997, and faxed to the Board on November 4, 1997. In an attempt to finalize this analysis, I will address the issues as stated in the October 30, 1997, letter. Each purported reason will be analyzed separately.

(1) The 1994 agreement providing for the consolidation of the leases violates ARM 36.25.602(3) providing that a lease may not embrace more than one governmental section and may not embrace noncontiguous subdivisions of land unless the subdivisions are within an area comprising not more than 1 square mile.

The allegation is an accurate statement of the administrative rule. The rule was adopted in 1981 and has not been revised since the date of adoption. The rule was adopted by the Department of State Lands and the Board, even though the authorizing statute only authorizes the Board to adopt rules. The adoption of the rule was certified to the Secretary of State by the Department. The rule is allegedly adopted pursuant to the authority contained in section 77-6-104, MCA. That section was renumbered section 77-1-209, MCA, in 1983. The section authorizes the Board to prescribe rules that it considers necessary relating to the leasing of lands in order to contribute

in the highest attainable measure to the purpose for which the lands are granted. The rules specifically referred to in the statute relate to a procedure for establishing fees and rental rates. The procedure is to provide for notice, public comment, public hearing, and appeal. The rule allegedly implements section 77-3-102, MCA. That section grants the Board the discretion to lease state lands for the purpose of prospecting or mining. The leases may be for a period of time determined by the Board, subject to the conditions of the grants by which the lands or mineral rights were acquired. The leases are required to give the lessee, subject to compliance with the lease, the exclusive right to possession of the lands subject to reservations in the lease. The Board is directed to exercise business discretion subject to Title 77, chapter 3, part 1, MCA. Section 77-3-113, MCA, governs the quantity of land covered by a mining lease. It provides that a mining lease is required to cover the area of ground the Board determines to be reasonable and consistent with the character of the ground, the type of deposit or deposits for which the lands are to be mined, and the character and size of the operation contemplated, necessary, or reasonable in good mining practice for the profitable recovery of the mineral. Section 77-3-113, MCA, actually appears to be the section implemented by ARM 36.25.602(3). The rule is much more restrictive than section 77-3-113, MCA, and limits the discretion statutorily granted to the Board. It was recognized in the case of Newton v. Weiler, 87 Mont. 164, 286 P. 133 (1930), that the constitutional provisions relating to trust lands are limitations upon the power of disposal by the Legislature. Section 2-4-305(6), MCA, requires rules to be consistent with and reasonably necessary to effectuate the purpose of the statute. A rule in violation of this requirement is void. See Winchell v. Department of State Lands, 262 Mont. 328, 865 P.2d 249 (1993). The analysis of the rule contained in this paragraph indicates the need for the review of rules governing mining leases. The validity of ARM 36.25.602 is questionable and should not be a serious impediment to either the lease or the project.

(2) The 1994 agreement violates The Enabling Act and section 77-3-116, MCA. The lease of land for the support of the School of Mines is the source of all mined ore. Revenue from that lease may not be commingled with other accounts. The other two state leases in the project may not be credited with royalty income from the mine.

Article X, section 10, of the Montana Constitution requires the funds of the University System to remain inviolate and sacred to the purpose for which they were dedicated. The rental from the leased lands must be devoted to the maintenance and perpetuation of the respective institutions, in this case, Montana Tech of the University of Montana - Butte. The income from that parcel may not be commingled. Section 77-3-116, MCA, requires the Board to reserve a royalty in every mining lease. Each lease subject to the 1994 agreement contains a royalty reservation. Obviously, nothing contained in section 77-3-116, MCA, requires royalty income to be paid from nonproducing leases. Because there is currently no production, there is no royalty payment from any of the original leases. The 1994 agreement consolidates all of the original leases into a "managed unit". The agreement specifically allows the lessee to obtain surface leases for any

parcel in the mineral lease that is shown to be incapable of producing minerals in paying quantities. Royalty payments are not required for surface leases.

(3) The 1994 agreement violates sections 77-3-102(2) and 77-3-115(3),MCA, and ARM 36.25.605 requiring a lease to specify a term and directing that a lease be limited to a term of 10 years and as long thereafter as paying quantities of minerals are produced.

As pointed out in the analysis of issue # 1, section 77-3-102(2), MCA, grants the Board the discretion to lease state lands for the purpose of prospecting or mining for a period of time determined by the Board, subject to the conditions of the grants by which the lands or mineral rights were acquired. The leases are required to give the lessee, subject to compliance with the lease, the exclusive right to possession of the lands subject to reservations in the lease. The Board is directed to exercise business discretion subject to Title 77, chapter 3, part 1, MCA. Section 77-3-115, MCA, provides that the lease may contain reasonable requirements for the prosecution of work and for the prosecution of mining after the prospecting period. The lease must specify the term of the lease and reasonable forfeiture provisions. The lease may contain other provisions agreed upon by the Board and the lessee. ARM 36.25.605 provides that the term of a lease must be granted on a standard lease form for a primary term or period of 10 years and so long thereafter as minerals are produced in paying quantities. This rule is subject to the same analysis applied in response to issue # 1. The rule was adopted in 1981 and has not been revised since the date of adoption. The rule was adopted by the Department of State Lands and the Board, even though the authorizing statute only authorizes the Board to adopt rules. The adoption of the rule was certified to the Secretary of State by the Department. The rule is allegedly adopted pursuant to the authority contained in section 77-6-104, MCA. That section was renumbered section 77-1-209, MCA, in 1983. The rule allegedly implements section 77-3-111, MCA. That section states that applications for mining leases must be made to the Department on a form prescribed by it. The statutes that address the duration of a lease are section 77-3-102(2), MCA, which, as previously noted, provides that a lease may be for a period of time determined by the Board, and section 77-3-115(3), MCA, which provides that a lease must specify the term of the lease.

(4) The failure to conduct a qualifying study pursuant to section 77-3-112, MCA, negates the leases and the 1994 agreement.

Section 77-3-112, MCA, provides that before the Board leases any lands for mining the Department shall investigate the character of the lands for determining whether the lands warrant issuing a mining lease. If an application is filed for lands that have not been examined, the Board is granted discretion to require a deposit, of up to $500, to cover the cost of the inspection, and the excess amount may be repaid to the applicant. The Department is required to make and preserve complete records of the inspections. Obviously, the amount of money that the Board is authorized to charge would restrict the Department to a very cursory examination. This section

was enacted in 1937 and has not been substantively revised since enactment. The section obviously has some problems and should be reviewed by the Legislature. The section was enacted prior to the enactment of the Montana Environmental Policy Act (MEPA), Title 75, chapter 1, parts 1 through 3, MCA. A thorough analysis of the character of the land will be embodied in an environmental impact analysis.

The requirements for MEPA analysis with regard to state land leases were discussed in Ravalli County Fish and Game Association, Inc. v. Montana Department of State Lands, 273 Mont. 371, 903 P.2d 1362 (1995). In that case, the court determined that when the Department is made aware of changes in existing conditions or uses relating to an operation under a lease or permit and those changes have the potential to significantly affect the quality of the human environment, then the Department must evaluate those changes for significant impacts pursuant to MEPA. It is not a lease renewal or assignment that triggers MEPA analysis but a substantial change of use that may have a significant effect upon the human environment. After fully complying with MEPA procedure, an agency may determine that an action will result in significant impacts and approve the action. The goal of maximizing income derived from school trust lands does not exempt the Department from complying with applicable environmental laws. Income is "a" consideration -- not "the" consideration regarding school trust lands. Maximizing income is not paramount to the exclusion of wildlife or environmental considerations in the MEPA context.

Related analysis

A number of other statutes and decisions have bearing on the entire issue, including your question relating the Board's decisionmaking authority over the project. As pointed out earlier, the cases interpreting The Enabling Act and the constitutional provisions governing the land grants establish the parameters within which the Legislature may act in dealing with the lands and the Board.

Article X, section 4, of the Montana Constitution creates the Board of Land Commissioners and prescribes its duties as follows:

> The governor, superintendent of public instruction, auditor, secretary of state, and attorney general constitute the board of land commissioners. It has the authority to direct, control, lease, exchange, and sell school lands and lands which have been or may be granted for the support and benefit of the various state educational institutions, under such regulations and restrictions as may be provided by law. (emphasis added)

The Legislature has enacted several statutes in fulfillment of this authority. Section 77-1-202(1), MCA, provides that the Board has general authority over the disposition of state lands. The Board is to exercise its authority in accordance with the principle that the lands are held in trust

for the support of education and for the attainment of other worthy objects helpful to the well-being of the people of the state as provided in The Enabling Act. The Board is to administer the trust to secure the largest measure of legitimate and reasonable advantage to the state. Section 77-1-203, MCA, directs the Board to manage state lands under the multiple-use management concept so that they are used in a combination best meeting the needs of the people and the beneficiaries of the trust. The Board is directed to make the most judicious use of the land for some or all of those resources or services over areas large enough to provide sufficient latitude for periodic adjustments in use. The Board is also directed to coordinate management of the various resources so that productivity of the land is not impaired and consideration is given to the relative values of the various resources. If a parcel of state land in one class has other multiple uses or resource values that are of such significance that they do not warrant classification for the value, the land must be managed insofar as possible to maintain or enhance multiple-use values. Section 77-1-301, MCA, provides that the Department, under the direction of the Board, has charge of the classification and leasing of state lands. Section 77-1-601, MCA, provides that the state is to seek the highest development of state lands in order that they are placed in their highest and best use and thereby derive greater revenue for the purpose for which they were granted and so that the economy of the local community as well as the state is benefited.

The Legislature has also enacted a number of directives concerning mining leases. Section 77-3-102, MCA, grants the Board the discretion to lease state lands for the purpose of prospecting or mining. The leases may be for a period of time determined by the Board, subject to the conditions of the grants by which the lands or mineral rights were acquired. The leases are required to give the lessee, subject to compliance with the lease, the exclusive right to possession of the lands subject to reservations in the lease. The Board is directed to exercise business discretion subject to Title 77, chapter 3, part 1, MCA. Section 77-3-105, MCA, provides that in case of the assignment of a mining lease, the party assigning the lease is not relieved of any responsibility for operations until the Board has approved the financial and moral responsibility of the assignee and the assignment and consent of sureties or a new bond has been deposited with the Department. Section 77-3-113, MCA, provides that the Board shall determine the quantity of ground reasonable and necessary for the profitable recovery of minerals from the lease. Section 77-3-115, MCA, provides that the lease may contain reasonable requirements for the prosecution of work and for the prosecution of mining after the prospecting period. The lease must specify the term of the lease and reasonable forfeiture provisions. The lease may contain other provisions agreed upon by the Board and the lessee. Section 77-3-117, MCA, provides that the Board, with the agreement of the lessee, may amend or modify the terms and conditions of the lease. Section 77-3-121, MCA, authorizes the Board to enter into agreements for the pooling of acreage or yardage with others holding the mineral rights in adjoining lands for unit operation of placer mining and the apportionment of royalties in the case of placer deposits lying partly on state land and partly on land in which others hold the mining rights. The Board is also authorized to enter agreements for the unit operation of the placer mining deposits and apportionment of royalties on the basis the Board considers to be in the state's best interest.

There are very few cases dealing with mining leases for state land. There are a number of cases involving oil and gas leases and grazing leases that establish parameters and guidelines for the Board and the Department to exercise their discretion in dealing with their trustee responsibilities.

The use of land grants for an oil and gas leasing pooling arrangement was challenged in Toomey v. State Board of Land Commissioners, 106 Mont. 547, 81 P.2d 407 (1938). The court found that pooling of school lands with private lands for unit operation for the production of oil and gas and the apportionment of the royalties from the pool are not violative of The Enabling Act, which grants general authority to lease school lands for the extraction of oil and gas. If the pooling arrangement is treated as the sale of an estate or interest in the school lands, it still does not violate The Enabling Act because the requirement of public sale after advertising applies only when the whole interest in land is sold. When an estate or interest in the land is sold, the full market value of the estate or interest disposed of is ascertained "in such manner as may be provided by law". The Legislature is given ample power to determine the method by which to ascertain the full market value of the estate or interest.

Relying on State ex rel. Galen v. District Court, 42 Mont. 105, 114, 112 P. 706 (1910), to find that The Enabling Act is to be strictly construed, the court found that an oil and gas lease could not be extended beyond the time limitation in The Enabling Act. Texas Pacific Coal & Oil Co. v. State, 125 Mont. 258, 234 P.2d 452 (1951).

The problems engendered with the customary methods of oil leasing were encountered in the 1950s. The court found that the "royalty" collected under an oil and gas lease on school lands is required to be credited to the permanent school fund since royalties are based on production and production is a permanent disposition of an estate in the land. "Rentals" or cash bonuses collected under an oil and gas lease were required to be placed in the common school interest and income fund available for the maintenance and support of schools and institutions. State ex rel. Dickgraber v. Sheridan, 126 Mont. 447, 254 P.2d 390 (1953). This holding was clarified in State ex rel. Strandberg v. State Board of Land Commissioners, 131 Mont. 65, 307 P.2d 234 (1957). The court found that the Legislature, in leasing oil lands, is under an obligation to obtain the full market value of the estate or interest disposed of on a rental basis, as well as for the sale of the land itself or the oil and gas in and under the land. There could be no sacrifice of the rental for additional royalty without, at the same time, violating Article XVII, section 1, of the 1889 Constitution. The court upheld the legislative scheme because no hard-and-fast rule could be devised for determining the full market value of oil and gas leases involving both rentals and royalties.

In State ex rel. Morgan v. State Board of Examiners, 131 Mont. 188, 309 P.2d 336 (1957), the court apparently overturned the line of decisions dating back to Galen, supra., when it held that The Enabling Act must be liberally construed with the view of accomplishing the object sought

to be attained rather than strictly construed. The decision expressly overruled Bryant v. State Board of Examiners, 130 Mont. 512, 305 P.2d 340 (1956), limiting the uses of the capitol land grant. The Morgan decision allowed the capitol land grant fund to be used to repair old buildings and to install a roll call voting machine in the House of Representatives.

The statutory scheme of granting agricultural leases was challenged in State ex rel. Thompson v. Babcock, 147 Mont. 46, 409 P.2d 808 (1966). The court said that it is incumbent upon the Board, in leasing state-owned land held in trust for the people, to secure full market value for the lease. Full market value is determined by the value of a similar lease in the particular community, coupled with the applicant's ability as a farmer and other variables that allow the state to secure as large a return as possible, yet preserve the productive capacity of the land. The Board may not speculate but must secure sustained income continually benefiting the public in general. Preference rights of the lessee were held proper if bids received were within the range of market value. The sustained income or sustained yield concept articulated in Thompson was further elucidated in Jerke v. State Department of Lands, 182 Mont. 294, 597 P.2d 49 (1979). The court said:

> Sustained yield is the policy which favors the long term productivity of the land over the short term return of income. . . .
>
> The preference right seeks to further this policy by inducing the State's lessees to follow good agricultural practices and make improvements on the land. This is accomplished by guaranteeing that the lessees will not lose the benefits of their endeavors by being outbid when their leases terminate. They are preferred and may renew their leases by meeting the highest bid submitted.
>
> Where the preference right does not further the policy of sustained yield, it cannot be given effect. In such a situation, full market value can be obtained only by pure competitive bidding. Id. at 296, 297.

The court further stated that a grazing district holding the preference right did not even use the land, but subleased it. It could not use good agricultural practices or make improvements. The sublessee, who as a member of the district was prevented from bidding on the lease, was not motivated to further the policy of sustained yield because he was not assured that the land would be allocated to him. To allow exercise of the preference right in this instance would be to install the district rather than the Department as the trustee of the land, and sustained yield would have no place. Allowing an existing lessee who does not use the land to exercise a preference right constitutes an unconstitutional application of the preference right statute.

Jerke was followed in Skillman v. Department of State Lands, 188 Mont. 383, 613 P.2d 1389 (1980), and distinguished in Steffen v. Department of State Lands, 223 Mont 176, 724 P.2d 713 (1986), in which the lessee retained significant responsibility and control throughout the lease.

The Department has a duty to the state to secure the maximum return to the state with the least injury to the land. Section 77-6-205(2), MCA, does not create any obligation to third parties, only to the state. Sebena v. State of Montana, 267 Mont. 359, 883 P.2d 1263 (1994). A decision of the Department will not be reversed unless the decision is arbitrary or capricious. Jeppeson v. Department of State Lands, 205 Mont. 282, 667 P.2d 428 (1983). In Jeppeson, the court cited State ex rel. Thompson v. Babcock, 147 Mont. 46, 409 P.2d 808 (1966), and State ex rel. Gravely v. Stewart, 48 Mont. 347, 137 P. 854 (1913), for the proposition that the Board must have a large discretionary power. Every facet of the Board's action cannot and is not explicitly set forth in the Montana Constitution or statutes. As the trustee, the Board has a large discretionary power over the subject of the trust within the legal parameters of the trust.

In Gypsy-Highview Gathering System, Inc. V. Montana Department of State Lands, 231 Mont. 330, 753 P.2d 317 (1988), the Department had issued an oil and gas lease for 10 years and so long thereafter as commercial quantities of oil and gas were produced. After 10 years had expired and the lessees had never produced commercial quantities of oil and gas, the Department canceled the lease. The lessee contended that pursuant to the terms of the lease, only the Board could cancel the lease. The Supreme Court noted that section 77-1-301, MCA, empowers the Department to lease and manage state lands as directed by the Board. The Board had delegated the duties in question to the Commissioner of State Lands and to the Department, subject to review by the Board. In this case, the Board had reviewed the matter but had not overridden the Department's action. The court cited Jeppeson and noted that the lease expired because of the plaintiff's failure to produce commercial quantities of oil and gas during the primary term of the lease, not because of the Department's action. Since the lands granted to the state constitute a trust, the Department has a fiduciary duty to manage them for the state's utmost interest.

A fairly thorough analyses of trust responsibilities for school land is contained in Department of State Lands v. Pettibone, 216 Mont. 361, 702 P.2d 948 (1985). In Pettibone, the Department objected to the Powder River Preliminary Decree holding that title to certain water rights was vested in the respondents. The Montana Supreme Court held that water appurtenant to school trust land is an interest in the land and may not be alienated unless the school land grant trust receives adequate compensation for that interest. The court cited a number of cases for two main points: (1) an interest in school land may not be alienated unless the trust receives adequate compensation for the interest; and (2) any law or policy that infringes on the state's managerial prerogatives over school lands cannot be tolerated if it reduces the value of the land.

Conclusions

The Department should conduct a thorough review of the administrative rules governing the leasing of state lands to determine if the rules comply with appropriate statutory authority and current leasing practices.

The state should conduct a thorough review of the statutes governing the leasing and use of state lands to determine if there are outdated statutes that impose unnecessary responsibilities on the Department and the Board in light of current conditions and other statutory requirements.

The Board has ultimate responsibility for seeing that the purposes of the various trusts are fulfilled. The Board may delegate duties to the Department, subject to review by the Board.

As trustee, the Board must have a large discretionary power. Every facet of the Board's action cannot be and is not explicitly set forth in the Montana Constitution or statutes. As the trustee, the Board has a large discretionary power over the subject of the trust within the legal parameters of the trust. The legal parameters for the trust are established in The Enabling Act and the Montana Constitution, and statutes validly adopted within the constitutional parameters.

Subject to the restrictions contained in The Enabling Act and the Montana Constitution, the Legislature may enact statutes concerning the control, lease, exchange, and sale of state lands.

If you have any questions or if I can provide additional information, please feel free to contact me. Pursuant to your request, I am sending copies of this letter to the noted parties.

Sincerely,

Gregory J. Petesch
Director of Legal Services

cc: Governor Racicot
Attorney General Mazurek
Secretary of State Cooney
State Auditor O'Keefe
Superintendent Keenan
Senator Ken Mesaros
Todd Everts
Tommy Butler
Missoula County Commissioners
George Turman
Jeff Renz
Calvin Souther
Jon Krutar
Bill Snoddy

l55 7316gpxa.