
Background

CHAPTER 1

The federal government granted Minnesota land “for the benefit of schools.”

The policy of granting federally owned land for the support of schools was common throughout the American colonial period, beginning before the federal Constitution was adopted. The General Land Ordinance of 1785 began the program of land grants for schools, providing that section 16 in every township would be reserved “for the maintenance of public schools.” The Northwest Ordinance, enacted in 1787, provided a system for establishing a territorial government and organizing for statehood that applied specifically to Ohio, Indiana, Illinois, Michigan, Wisconsin, and Minnesota east of the Mississippi. As the Northwest Ordinance was implemented, its procedures for statehood and its commitment to grant land for schools were applied to other states.¹ The U.S. Congress granted school land to the states at the time each state joined the Union, beginning with Ohio in 1803 and ending with Alaska in 1959.²

Throughout this time period, the nature of the land grants varied from state to state. The land grants increased from one to four sections of each township and general language was replaced with more complex and specific provisions. What is consistent, however, is that the federal government made grants of land in support of public schools and that states, in accepting the grants, entered into an “irrevocable compact” with the federal government. The states made clear and specific promises in return for the granted land. States agreed to use the proceeds from initial land sales to establish permanent school funds, the principal of which would be inviolate and undiminished forever. The income earned from the investment of the fund’s principal would be used to support public schools in each state.

To provide a context for our discussion of the management of Minnesota’s school trust land and Permanent School Fund principal in later chapters, this chapter provides background information on the history and key components of Minnesota’s school land grant. This chapter addresses the following questions:

- **What was the origin and purpose of Minnesota’s school land grant?**

¹ Sally K. Fairfax, Jon A. Souder, and Gretta Goldeman, “The School Trust Lands: A Fresh Look at Conventional Wisdom,” *Environmental Law* (22) 1992: 803-813, and Jon A. Souder and Sally K. Fairfax, *State Trust Lands: History, Management, and Sustainable Use* (Lawrence, Kansas: University of Kansas, 1996), 17-24.

² The thirteen original colonies and three other states (Vermont, Tennessee, and Kentucky) did not receive school land grants when they became states. See Souder and Fairfax, *State Trust Lands*, 19.

- **What legal principles govern the management of trust land making it different from other state-owned land?**
- **What is the current management structure for Minnesota’s school trust land and Permanent School Fund principal?**
- **What revenues have been added to the Permanent School Fund principal from mining rents and royalties, timber sales, leasing, and land sales since 1986?**

To answer these questions, we reviewed national literature and previous reports about Minnesota’s school trust land, along with the Minnesota Constitution, state statutes, and case law relating to school trust land. We also analyzed state financial information on revenues deposited in the principal of the Permanent School Fund (PSF), and we conducted telephone interviews with managers of school trust land in 15 other states.

The state holds the land in trust for the benefit of public schools.

The land granted to the state by the federal government is held in trust for the support of schools. According to our analysis, the trust is governed by the same fiduciary principles that apply to private trusts. A trustee’s primary responsibilities are to the trust, not to other considerations. While the trust land can be used for any public purpose, if other uses result in decreased or foregone income to the trust, then the trust fund should be reimbursed.

Mining, forest management, and land sales added \$4.8 million in 1996 and \$4.4 million in 1997 to the PSF principal. Each of these land management activities accounted for about one-third of the revenues added to the PSF principal during these years. Between 1986 and 1997, these land management activities contributed a total of \$41 million to the principal of the PSF. The sale of assets including mining rents and royalties and land sales accounted for about 84 percent of all deposits into the PSF principal during this time period, while net revenues from forest management activities accounted for 16 percent of total deposits.

HISTORY OF MINNESOTA’S SCHOOL LAND GRANT

The State of Minnesota entered the Union on May 11, 1858. Minnesota’s grant of school trust land and the conditions attached to the grant were contained in a series of federal congressional acts that were part of the process of Minnesota becoming a state. The Organic Act of 1849, which created the territory of Minnesota, reserved sections 16 and 36 in each township “for the purpose of being applied to the schools in said territory.”³ The Enabling Act of 1857, which authorized the people of the territory to write a constitution and prepare for statehood, actually granted this land to the state. The Enabling Act stipulated:

³ *An Act to Establish the Territorial Government of Minnesota*, March 3, 1849, sec. 18, in *Minn. Stat.*, volume 1, xli. This act is commonly called the Organic Act of 1849. A section is one square mile, or 640 acres.

That the following propositions be and the same are hereby offered to the said convention of the people of Minnesota *for their free acceptance or rejection, which, if accepted by the convention, shall be obligatory on the United States, and upon the said State of Minnesota* to-wit:

First - That sections numbered sixteen and thirty-six in every township of public lands in said State, and where either of said sections, or any part thereof, has been sold or otherwise disposed of, other lands, equivalent thereto, and as contiguous as may be, shall be granted to said state *for the use of schools*.⁴ [Emphasis added.]

The citizens of Minnesota accepted the land grant for the use of schools on October 13, 1857, when they voted to adopt a state constitution. The constitution stated that “the propositions contained in [the Enabling Act] are hereby *accepted, ratified, and confirmed and shall remain irrevocable without the consent of the United States.*”⁵ [Emphasis added.]

The Enabling Act and the Minnesota Constitution established the framework for school trust land.

The Enabling Act and the Minnesota Constitution of 1857 established a legal framework for the school trust land. In addition to authorizing the establishment and maintenance of public schools, the Constitution contained additional conditions relating to the school land grant. The language relating to school trust land in the current Minnesota Constitution remains substantially unchanged from the original language, requiring that:

1. Income from the sale or other disposition of the land is to be deposited in the Permanent School Fund, the principal of which “shall be perpetual and inviolate forever;”
2. The “net interest and dividends arising from the [permanent school] fund shall be distributed to the different school districts of the state in a manner prescribed by law;” and
3. School trust land shall be sold only “at public sale, and in a manner provided by law.”⁶

There are some distinctions among states in the restrictions contained in federal enabling acts and state constitutions accepting the school land grant. Minnesota illustrates the simple conditions attached to the federal land grant in states admitted to the Union before the mid-1880s. The federal government simply provided the land “for the use of schools.” In contrast, the federal government attached detailed restrictions on school land grants made after the 1880s.⁷ Arizona’s Enabling Act, for instance, requires that land may be sold only at public sale, after advertising, and at not less than the fair market value, and rental revenues from trust land must be deposited into the permanent fund.

⁴ *Act Authorizing A State Government*, February 26, 1857, sec. 5, para. 1, in *Minn. Stat.*, volume 1, xliii. This act is commonly called the Enabling Act of 1857.

⁵ *Minn. Const. 1857*, art. II, sec. 3. Currently, this provision is found in *Minn. Const.*, art. II, sec. 1.

⁶ *Minn. Const.*, art. XI, sec. 8.

⁷ Brief for defendant at 17, *Segner v. State Board of Investment et al.*, No. C5-87-489319, (Ramsey Co. Dist. Co., August 11, 1988), and Souder and Fairfax, *State Trust Lands*, 26-33.

Minnesota added other federal land grants to the school trust land.

Minnesota was one of the first states entering the Union to receive a school land grant of two sections per township instead of one.⁸ Minnesota's original school trust land grant consisted of approximately 2.9 million acres.⁹

Minnesota added other federal land grants to the school trust land. Minnesota received internal improvement land to foster railroad and other economic development. It also received swampland, the proceeds of which were to be used for the construction of dams, levees, and drainage systems. Over time, the state combined these lands with the original school trust land.¹⁰

As a result of these changes, since 1974 school trust land in Minnesota has consisted of a combination of lands granted to the state for school, drainage, and internal improvement purposes. The current Minnesota Constitution defines the Permanent School Fund as:

(a) the proceeds of lands granted by the United States for the use of schools within each township, (b) the proceeds derived from swamp lands granted to the state, (c) all cash and investments credited to the permanent school fund and to the swamp land fund, and (d) all cash and investments credited to the internal improvement land fund and the lands therein.¹¹

Other constitutional amendments relating to the management of school trust land have been adopted over the years. In 1914 an amendment authorized the state to designate and manage certain timber on school trust land as state forests. The amendment permitted the state to use the net revenue from forest activities on the land to finance forest management costs.¹²

Two constitutional amendments, in 1938 and 1984, authorized the state to exchange school trust land for other public or private land, contingent upon the unanimous approval of the Land Exchange Board, consisting of the Governor, Attorney General, and State Auditor.¹³ Finally, in 1984 a constitutional amendment vested the responsibility for "administering and directing the investments of all state funds," including the Permanent School Fund principal, with the State Board of Investment.¹⁴

⁸ Ohio, Wisconsin, and other states entering the Union in 1848 or earlier received one section per township. After 1896, the federal government granted new states four sections per township. Utah, Nevada, New Mexico, and Arizona were given four sections because the land was arid and more of it was needed to support schools. Souder and Fairfax, *State Trust Lands*, 27.

⁹ Samuel T. Dana, et al, *Minnesota Lands: Ownership, Use and Management of Forest and Related Lands* (Washington, D.C.: American Forestry Association, 1962), 92. Some sources list the number of school trust land acres granted as 2,888,608. Because some land located in sections 16 and 36 was underwater, or had already been homesteaded, Minnesota was allowed to select other land in lieu of those sections that were not available. These lands are referred to as "indemnity" lands.

¹⁰ For a detailed discussion of this topic see: Minnesota Department of Natural Resources, *School Trust Land Management Report* (St. Paul, 1983), 7-8; and Office of the Legislative Auditor, *Evaluation of State Land Acquisition and Disposal* (St. Paul, 1983), 9, 83-84.

¹¹ *Minn. Const.*, art. XI, sec. 8.

¹² *Minn. Const.*, art. XI, sec. 11.

¹³ *Minn. Const.*, art. XI, sec. 10.

¹⁴ *Minn. Const.*, art. XI, sec. 8.

DIFFERENCE BETWEEN SCHOOL TRUST LAND AND OTHER STATE-OWNED LAND

A trust relationship that governs school trust land was created when the federal government granted specific land to the state and the state accepted the land for the use of schools. Minnesota's school trust land and the principal of the Permanent School Fund are held in trust for public school districts pursuant to the federal enabling act and the state constitution.

Although the Minnesota Constitution does not specifically identify a trustee, when the state accepted the terms and conditions of the federal land grant, it accepted the position of trustee for public schools in Minnesota. The U.S. Supreme Court has recognized the State of Minnesota as trustee of the federal land grant and acknowledged that "the legislature was the body representing the state."¹⁵ A broader legal interpretation might hold that, in Minnesota, entities of government with authority to make management decisions affecting the school trust land and fund should also be considered trustees. Since the Minnesota Legislature has delegated such responsibilities to the Department of Natural Resources and the State Board of Investment, these agencies also serve as trustees.¹⁶ In contrast, the constitutions in many other states provide for the creation of state land boards, composed of various combinations of constitutional and executive branch officers, to serve as trustees of school trust land.¹⁷

**The
Legislature,
DNR, and SBI
are trustees for
public schools.**

The trust status of the federal land grant imposes constraints and obligations on the trustees that would not apply if the state owned the land outright. There have not been any court cases on the nature of the trust relationship related to school trust land in Minnesota. We examined cases from federal district courts and circuit courts of appeals that could be applicable to Minnesota. A great deal of case law and commentary have emphasized that:

- **The trust is a real trust that should be governed by the same fiduciary principles that apply to the management of private trusts.**

The Washington Supreme Court in 1984 noted that the federal land grant trusts were created to benefit certain beneficiaries and that "[e]very court that has considered the issue has concluded that these are real enforceable trusts."¹⁸ For further support of this interpretation, the court cited the U.S. Supreme Court, which concluded:

¹⁵ *Stearns v. State of Minnesota ex rel. Marr*, 179 U.S. 252-53, 45 L. Ed. 162 (1900).

¹⁶ Interview with Assistant Attorney General Andrew Tourville, June 18, 1997.

¹⁷ Of the states we examined, Colorado, Idaho, Montana, Nebraska, Oregon, South Dakota, and Wisconsin have constitutionally created state land boards.

¹⁸ *County of Skamania v. State*, 102 Wn.2d 129, 132, (1984) as cited in Opinion of the State of Washington's Office of the Attorney General (AGO 1996 No. 11), 9.

There have been intimations that school land trusts are merely honorary, that there is a “sacred obligation imposed on (the state’s) public faith,” but no legal obligation. These intimations have been dispelled by *Lassen v. Arizona* This trust is real, not illusory.¹⁹

As a result, the state has several responsibilities in managing school trust land. First, the state must manage the land according to the terms of the trust as established in the enabling act and the state constitution. In Minnesota these conditions are fairly simple to: sell school trust land at public auction, deposit income from the land sales in the Permanent School Fund, and distribute interest from the fund to school districts.

Second, common law principles governing the administration of private trusts must be applied to the state in managing the school trust land. The Washington Supreme Court, in *County of Skamania v. State*, concluded that fiduciary principles apply to state actions regarding federal land grants. The opinion stated that the federal grant land trusts “impose upon the State the same fiduciary duties applicable to private trustees.”²⁰ As a practical result, a legislature may be constrained with respect to enactments affecting school trust land.

The duties of a trustee are summarized in Figure 1.1. A trustee is required to act prudently in managing a trust.²¹ The trustee should manage the trust to serve the interests of the trust beneficiaries. Cases from other states that address trustee duties have concluded that “undivided loyalty” to the trust beneficiaries is a trustee’s chief duty. In other words, the trustee’s primary responsibilities are to the trust, not to other considerations.

For instance, in *Skamania* the court ruled that the state as trustee may not use trust assets to pursue other state goals. The court held that the state had violated its duty of undivided loyalty to trust beneficiaries and its duty to act prudently by enacting a law aimed at benefiting the timber industry and the state economy in general at the expense of trust beneficiaries. The Nebraska Supreme Court (in *State ex rel. Ebke v. Board of Education Lands and Funds*) ruled that the state may not enact legislation for the benefit of lessees of public school land at the expense of the beneficiaries of the trust. In *State v. University of Alaska*, the Alaska Supreme Court ruled that the state had breached its duty to administer the trust solely in the interests of beneficiaries by failing to compensate the trust for the value of university land included in a state park.²²

A trustee is required to act prudently in managing a trust.

¹⁹ *United States v. 111.2 Acres*, 293 F. Suppl. at 1049, (E.D. Wash. 1968), aff’d, 435 F.2d 561 (9th Cir. 1970) as cited in Washington Opinion, 9.

²⁰ *County of Skamania v. State*, 102 Wn.2d 129, 132, (1984) as cited in Washington Opinion, 4, 11-12. The state must comply with common law duties in administering the federal trust lands. However, the state’s management decisions are given deference not granted a private trustee because of the presumption of constitutionality that applies to state legislative authority.

²¹ A trustee’s duties are enumerated in American Law Institute *Restatement (Second) of the Law: Trusts* and *Restatement (Third) of the Law: Trusts* (St. Paul: American Law Institute Publishers, 1959 and 1990), secs. 169-185.

²² *Skamania* 136-139, *State ex rel. Ebke v. Board of Educ. Lands and Funds*, 154 Neb. 520, 525-26 (1951), and *State v. University of Alaska*, 624 P.2d 807, 813-814 (Alaska 1981), as cited in Washington Opinion, 13-14.

Figure 1.1: Duties of a Trustee

Duties of a trustee include to:

- Administer the trust;
- Demonstrate undivided loyalty;
- Delegate trustee duties only when reasonable;
- Keep and render accounts;
- Furnish information to beneficiaries;
- Exercise reasonable care and skill in managing the trust;
- Take and keep control of trust property;
- Preserve trust property;
- Enforce claims held by the trust;
- Defend actions that may result in loss to the trust;
- Keep trust property separate from other property;
- Use reasonable care regarding bank deposits;
- Make trust property productive;
- Pay income to the beneficiaries; and
- Follow the direction of persons given control over the trust.

SOURCE: American Law Institute, *Restatement (Second) of the Law: Trusts and Restatement (Third) of the Law: Trusts* (St. Paul: American Law Institute Publishers, 1959 and 1990), secs. 169-185. Opinion of the State of Washington Attorney General's Office (1996 AGO No. 11), 13.

Trustees of perpetual trusts should balance short- and long-term interests of beneficiaries.

Some duties of a trustee, such as making the trust productive, or maximizing its economic returns, have different standards for application than others. The trustees of a perpetual trust, such as the school trust land, must reasonably balance the short- and long-term interests of the current and future trust beneficiaries. While a trustee must make the trust economically productive at the present time, a trustee must also protect the productivity of the trust in the long run. In other words, a trustee cannot simply be concerned with maximizing current income.²³ The conflict between maximizing economic returns and preserving the trust property may be more pronounced with trust land because of its perpetual nature.

Washington State statutes adopting a sustained yield policy for the state-owned forested land reflect consideration of the common law duty of making the trust productive over time. Sustained yield requires managing the forest to provide for harvesting a specific amount on a continuing basis so that there is not a major prolonged curtailment of harvest.

Some beneficiaries of federal grant land have suggested that the trust need only comply with general laws if the laws serve the beneficiaries' economic interest. The courts have held, however, that state legislatures may pass laws that apply

²³ Washington Opinion, 2.

generally, such as environmental laws, and that those laws apply to trust land just as they apply to all other land in the state. This same argument applies to federal laws of general application.²⁴

The Minnesota Constitutional Study Commission in 1972 discussed some of these issues and concluded that school trust land should be managed in the interest of the trust beneficiaries, not for other purposes. Outside interest groups suggested that the Natural Resources Committee of the Study Commission endorse a constitutional amendment to authorize the use of school trust land for strictly non-income producing purposes (such as scientific and natural areas) without compensating the trust. The Committee rejected the suggestion in its November 1972 report to the Constitutional Study Commission. While noting that school trust land is included in state forests and thus is available for many recreational and scientific purposes, the Committee concluded in its report that:

The trust fund lands should be managed for income, although ecological considerations are important in the minds of those responsible for their administration. A scientific or natural area is probably not income producing. Hence, *trust administrators would consider such use of trust fund lands a violation of their obligations*

While the state forests are, in one sense, investments of the public in the natural resources of the state, they can also serve to provide other uses to the citizens. . . . *Since the state committed itself, when accepting these lands, to use the proceeds for school purposes, the principal objective must be sound management for income consistent with overriding public concerns. . . .*

There are very good arguments for preserving and protecting wilderness areas, scientific areas, and parks. The Legislature can accomplish this by appropriating the necessary funds for the purchase of land. In proper circumstances it ought to do so. The stream of future finance for the schools, which the trust fund lands represent, ought to be protected too.²⁵ [*Emphasis added.*]

The state should manage the trust in the interest of trust beneficiaries.

According to our interpretation, the state is constrained in how it may manage the school trust land and revenues from the land in a way that it would not be if the state held the land outright. Most important, the state should manage the trust in the interest of the beneficiaries of the trust, current and future, and should not sacrifice the economic interests of the beneficiaries of the trust by using trust assets to serve other purposes. The long-term objective should be to receive as much revenue as possible to aid public education for both current and future beneficiaries.

²⁴ Washington Opinion, 3, 18-21.

²⁵ As cited in Office of the Legislative Auditor, *A Review of the Department of Natural Resources' Operation and Management of the Permanent School Fund* (St. Paul, 1981), 12-13, and Minnesota Department of Natural Resources, *School Trust Land Management Report* (St. Paul, 1983), 21-22.

MANAGEMENT OF MINNESOTA'S SCHOOL TRUST LAND AND FUND

Between 1861 and 1969, the administration of Minnesota's school trust land shifted from the State Board of Commissioners of School Lands (1861), to the State Land Office with the State Auditor serving as commissioner ex officio (1862-1931), and then to the Department of Conservation (1931-1969). In 1969, the Department of Conservation was reorganized into the Department of Natural Resources which maintains responsibility for managing the trust land.²⁶

The original policy of the state was the speedy survey and sale of the best school trust land to generate income for the trust fund and to support public schools. The Permanent School Fund principal was established in 1862, when the first 38,000 acres of school land were sold for approximately \$243,000, an average price of \$6.35 per acre.²⁷ Land good for farming or near populated areas was sold first and was largely disposed of by the 1880s. The remainder of the trust land was never sold, leaving large tracts of school trust land in the northern part of the state.

The early actions of the state to liquidate school trust land were consistent with the popular conviction that private enterprise would drive economic development. The Legislature began placing limitations on the sale of state-owned land, including school trust land, in the early 20th century. Limitations included reserving mineral rights when state-owned land was sold (which passed in 1901), prohibiting the sale of state-owned land bordering or adjacent to public waters (1923), and removing land containing commercial peat deposits from sale (1935).²⁸ This shift to retaining state land occurred for three reasons: (1) the most productive and valuable land had already been sold for development; (2) there was a growing recognition that the PSF would have fewer future opportunities for growth if more of the school and swamplands were sold; and (3) there were growing pressures on the state to reserve some land for public use and enjoyment and to increase its own role as a land manager in the public interest.²⁹

Current Management Structure

The responsibility for managing Minnesota's school trust land and investing assets of the Permanent School Fund is currently divided among several state agencies. Figure 1.2 illustrates the current structure for administering Minnesota's school trust land and PSF principal. As noted above, the Minnesota Department of Natural Resources is responsible for managing school trust land. The Commissioner of the Department of Natural Resources "shall have charge and control of all the public lands, parks, timber, waters, minerals . . . of the state

The state sold much of the school trust land in the 1800s.

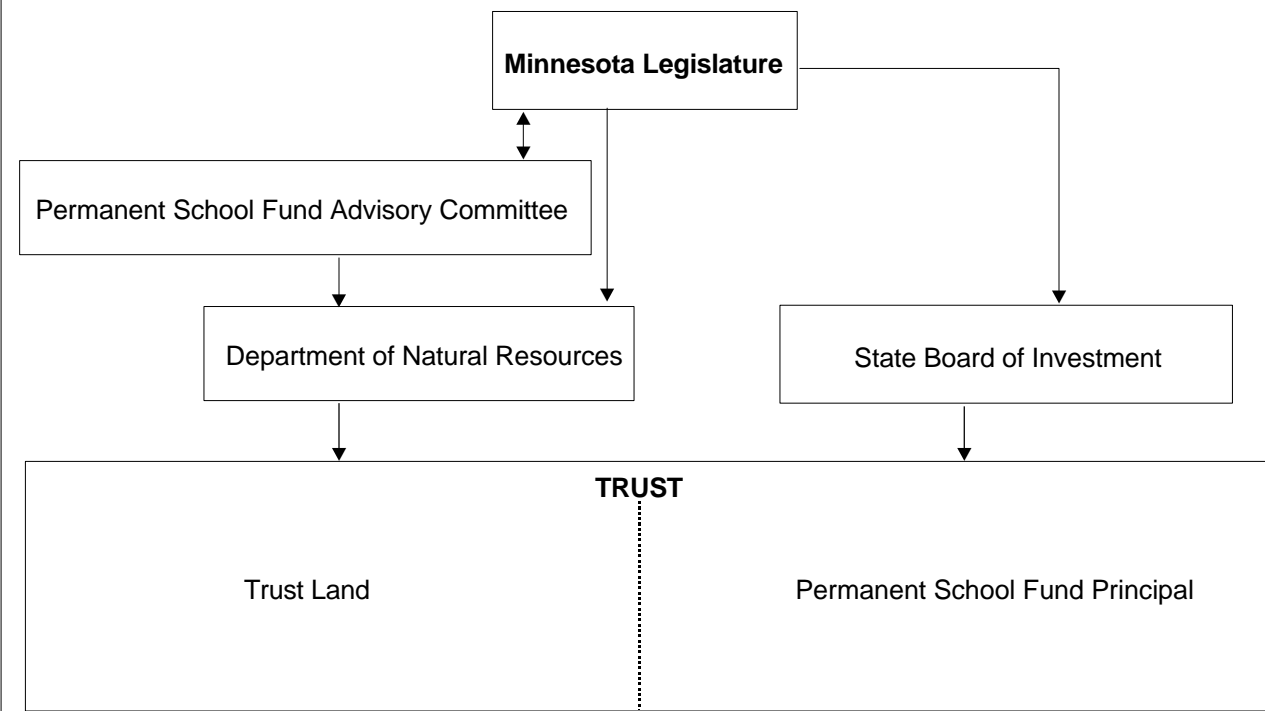
²⁶ Office of the Legislative Auditor, *A Review*, 4-5.

²⁷ Dana, *Minnesota Lands*, 134.

²⁸ *Minn. Stat.* §§93.01, 93.02, 93.04, 92.45, and 92.461, subd. 1.

²⁹ Office of the Legislative Auditor, *Evaluation of State Land Acquisition*, 12.

Figure 1.2: Management of Minnesota’s School Trust Land and Permanent School Fund



SOURCE: Office of the Legislative Auditor.

and of the use, sale, leasing, or other disposition” of those lands.³⁰ The State Board of Investment (SBI) is responsible for investing the PSF principal, while the Department of Finance is responsible for managing the PSF.³¹

In 1981, the Financial Audit Division of the Office of the Legislative Auditor reviewed DNR’s management of school trust land and found, among other things, that the department had not established objectives for the overall management and use of the land. The report also concluded that DNR “should not have the sole decision-making authority over the use of school trust land” and it recommended that “some management oversight be established outside of the organizational structure of the [DNR].”³²

In response, the 1982 Legislature established the seven-member Permanent School Fund Advisory Committee to “advise the Department of Natural Resources on management of permanent school fund land, which is held in trust for school districts of the state.” The advisory committee was directed to “review the policies of the Department of Natural Resources on management of school trust fund lands” and to “recommend necessary changes in policy and

³⁰ *Minn. Stat.* §84.027, subd. 2.

³¹ *Minn. Const.* 1988, art. XI, sec. 8; and *Minn. Stat.* §11A.16, subs. 3 and 4.

³² Office of the Legislative Auditor, *A Review*, 6-7, 15-16.

implementation in order to ensure provident utilization of the permanent school fund lands.”³³

In 1985, the Legislature adopted the following goal for management of the school trust land:

The legislature intends that it is the goal of the permanent school fund to secure the maximum long-term economic return from school trust lands, consistent with the fiduciary responsibilities imposed by the trust relationship established in the Minnesota Constitution, with sound natural resource conservation and management principles, and with other specific policy provided in state law.³⁴

Statutes call for DNR to maximize the trust’s long-term economic return consistent with natural resource principles.

Based on this goal, DNR is supposed to maximize the long-term economic return from the school trust land to the trust. In addition, this goal provides that school trust land may be managed according to “sound natural resource conservation and management principles.” This means managing trust land to preserve unique characteristics or values (such as wildlife habitat), or to serve the public benefit by providing recreational opportunities.³⁵ While trust land can be used for public purposes, DNR has acknowledged that if such uses result in decreased or foregone income to the trust, then it should seek a method of compensating the trust. DNR policies and practices on compensating the trust for the value of diminished or lost revenues are examined in Chapter 2.

Flow of Funds

The principal of the Permanent School Fund includes cash and investments generated from mining rents and royalties, land sales, timber sales, and lakeshore and other leases on school trust land. Figure 1.3 illustrates the flow of funds within the Permanent School Fund.

Based on constitutional language, revenues from the sale of school trust land and royalties and rents from mining should be deposited in the Permanent School Fund. Revenues from forestry management activities, such as timber sales and land leasing, are deposited in a special account called the Forest Suspense Account. The Minnesota Constitution and state law allow DNR to deduct the costs of protection, improvement, management, and administration of state forest trust land and construction and improvement of forest roads from the revenues earned by this land.³⁶ Any balance in the Forest Suspense Account after deducting forestry management costs is deposited in the PSF. Since 1988, up to 50 percent of the revenues from lakeshore leases have been deposited in another special account, called the Lakeshore Account, to finance the costs of appraising, selling, and leasing lakeshore lots.³⁷ The remainder of revenues from lakeshore leases are deposited in the Forest Suspense Account.

³³ *Minn. Stat.* §124.078.

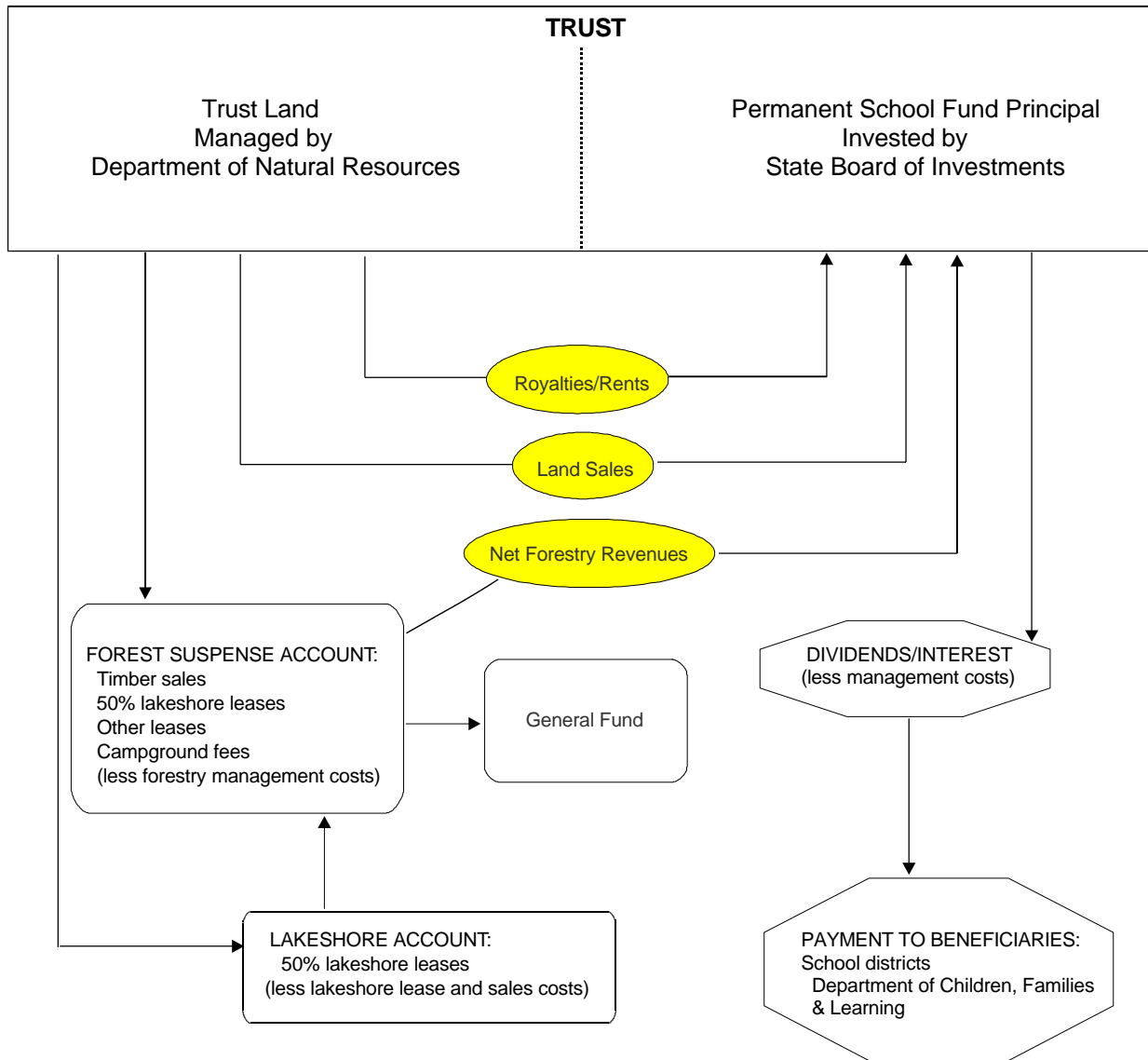
³⁴ *Minn. Stat.* §124.079.

³⁵ Minnesota Department of Natural Resources, *School Trust Land Management Report*, 22-24.

³⁶ *Minn. Const.*, art. XI, sec. 11, and *Minn. Stat.* §16A.125, subd. 5.

³⁷ *Minn. Stat.* §92.46, subd. 1 (c).

Figure 1.3: Flow of Funds



SOURCE: Office of the Legislative Auditor.

At the end of each fiscal year, the income earned from investment of the PSF principal is distributed by the Commissioner of Children, Families, and Learning to school districts as part of the state’s general education aid payments.³⁸ This income is distributed twice a year, on the first Monday in March and September, based on average daily membership during the preceding year.

³⁸ *Minn. Stat.* §§124.08 and 124.09. The revenue from the PSF is transferred to the Endowment School Fund, an expendable trust fund, and then distributed to school districts.

Existing Trust Assets

The primary assets of Minnesota's school trust consist of the trust land and the Permanent School Fund principal. As noted earlier, Minnesota's school trust land totaled about 2.5 million acres in July 1997.

Sixty-two percent of the remaining 2.5 million acres of school trust land was from the swampland grant, as shown in Table 1.1. Minnesota has retained about one-third each of the original school trust and swampland grant acres, while few internal improvement lands remain. In 1997, Minnesota's school trust land was concentrated in the northern part of the state; more than 92 percent of the school trust land was located in ten northern Minnesota counties as shown in Table 1.2 and Figure 1.4. Minnesota has about 2.5 million acres of mineral rights on school trust land, including about 1 million acres of "severed mineral rights"

School trust land is concentrated in northern Minnesota.

Table 1.1: Distribution of School Trust Land by Type of Grant

Type of Grant	Original Acres Granted	Acres Retained in 1997	Percent Retained
School	2,900,000	950,264	33%
Swampland	4,706,503	1,552,989	33
Internal Improvement	500,000	6,668	1
Total	8,106,503	2,509,921	31

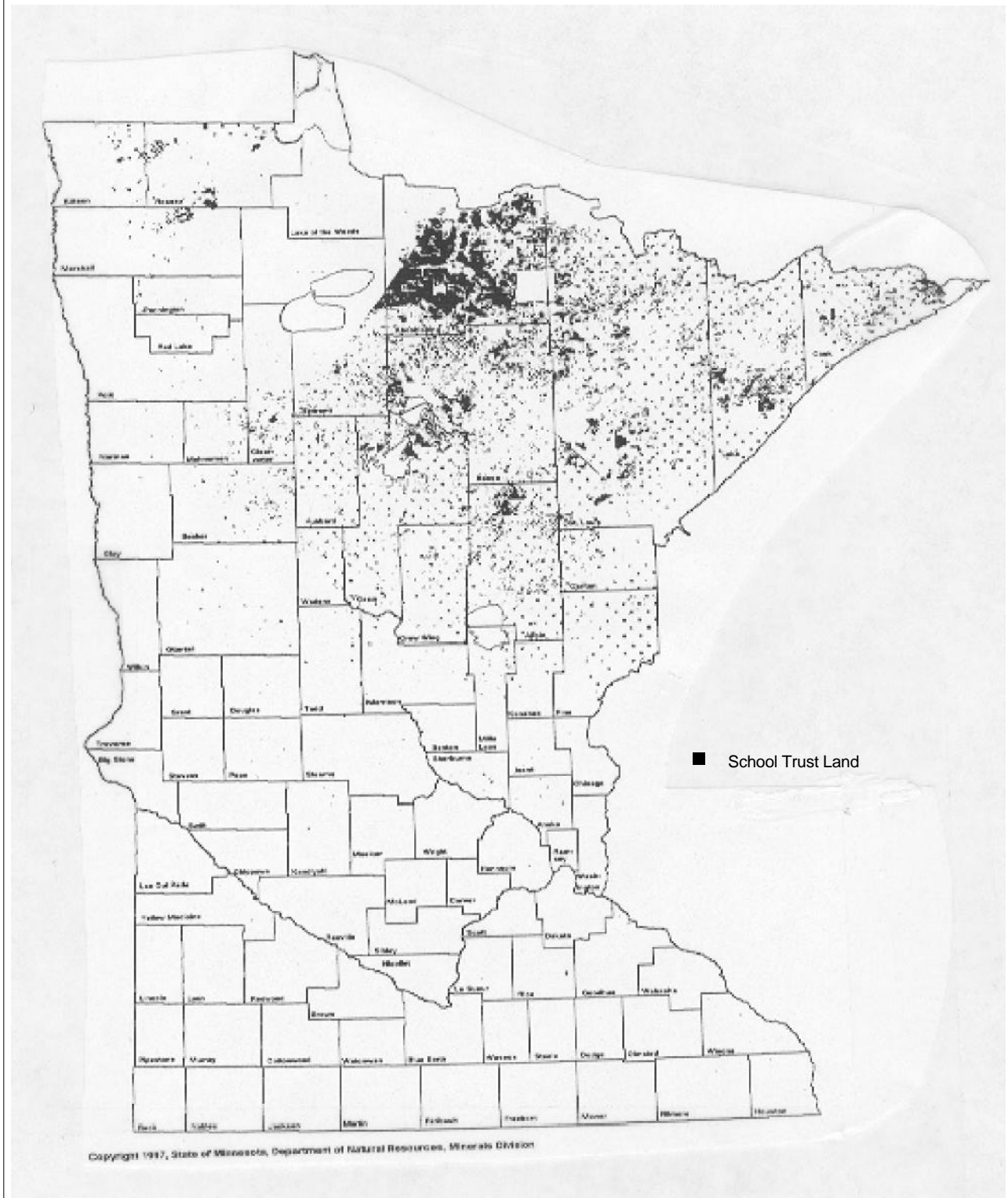
SOURCES: Office of the Legislative Auditor, *Evaluation of State Land Acquisition and Disposal* (St. Paul, 1983), and Department of Natural Resources, unpublished data.

Table 1.2: Distribution of School Trust Land by County, 1997

County	Acres of Trust Land	Percent of Total	Cumulative Percentage
Koochiching	853,771	34.0%	34.0%
St. Louis	481,666	19.2	53.2
Itasca	292,364	11.6	64.8
Lake	159,346	6.3	71.1
Cass	140,182	5.6	76.7
Aitkin	138,025	5.5	82.2
Cook	120,066	4.8	87.0
Beltrami	60,576	2.4	89.4
Roseau	46,649	1.9	91.3
Hubbard	29,163	1.2	92.5
Remaining Counties	188,113	7.5	100.0
Total	2,509,921		

SOURCE: Department of Natural Resources, unpublished data.

Figure 1.4: School Trust Land in Minnesota, 1997



on school trust land that has been sold. Severed mineral rights occur when the state sells the land but retains subsurface rights.

Of the 2.5 million acres of school trust land, 1.9 million acres are in DNR management units, as shown in Table 1.3.³⁹ The Division of Forestry manages approximately 94 percent of school trust land: 67 percent of the school trust land that is in state forests and another 27 percent that is not located in any management unit. About 3 percent of the school trust land is in wildlife management areas, 2 percent is in scientific and natural areas, and less than 1 percent is in state parks and other recreational units.

The Division of Forestry manages most school trust land.

Table 1.3: Estimated School Trust Acres by DNR Management Unit

Management Unit	Trust Land Acres	Percent of Trust Land
State Forests and Campgrounds	1,737,123	67%
Wildlife Management Areas	85,681	3
Scientific and Natural Areas	51,000	2
State Parks	5,745	**
Riverways	756	**
Water Access	<u>2,880</u>	<u>**</u>
Subtotal	1,883,185	73
Outside of Management Units	<u>706,800</u>	<u>27</u>
Total	2,589,985	100

NOTES: Data represent DNR's estimate of total school trust land acres in each management unit. The total acres add to a number greater than the total acres of school trust land because some parcels are in more than one management unit.

** = Less than 1 percent.

SOURCES: Department of Natural Resources, MIS/GIS Section, unpublished data, June 1996; Division of Parks and Recreation; Scientific and Natural Areas Program.

We compared the original federal land grant and acres of school trust land retained in Minnesota with selected other states and found:

- **Minnesota has retained more of its school trust land than surrounding states, but less than most western states.**

Table 1.4 illustrates that Minnesota currently retains 31 percent of the 8.1 million acres of original school trust land, swampland, and internal improvement land granted by the federal government. In contrast, Iowa, Michigan, Wisconsin, and Ohio have little or no school trust land left, while South and North Dakota have

³⁹ It is not possible to accurately identify how many acres of school trust land are located within each DNR management unit because this information is not maintained in the department's main land records database. We obtained information on acres from various divisions and programs in DNR.

Table 1.4: Original and Current Surface Acres of School Trust Land

<u>State</u>	<u>Acres of Original Trust Land Granted</u>	<u>Surface Trust Land Acres, 1996</u>	<u>Current Trust Land Ownership as a Percentage of Original Grant</u>
Arizona	8,400,000	8,191,711	98%
Montana	5,188,000	4,620,487	89
New Mexico	8,600,000	6,765,000	79
Washington	2,376,391	1,783,000	75
Idaho	2,982,683	2,095,944	70
Colorado	4,382,240	2,640,368	60
Utah	6,000,000	3,573,978	60
Nebraska	2,894,000	1,509,000	52
MINNESOTA	8,106,503^a	2,509,921	31
North Dakota	2,500,000	635,469	25
South Dakota	2,733,084	652,448	24
Oregon	3,399,360	772,000	23
Wisconsin	1,243,721 ^b	4,068	<1
Ohio	704,204	1,232	<1
Iowa	1,000,679	0	0
Michigan	1,021,867	0	0

^aAcres include swampland and internal improvement land grants that were added to the original school trust land grant of 2.9 million acres.

^bAcres include swampland grant.

SOURCE: Office of Legislative Auditor telephone surveys and interviews, July-August 1997 ; and various annual reports from other states on file in the Office of the Legislative Auditor.

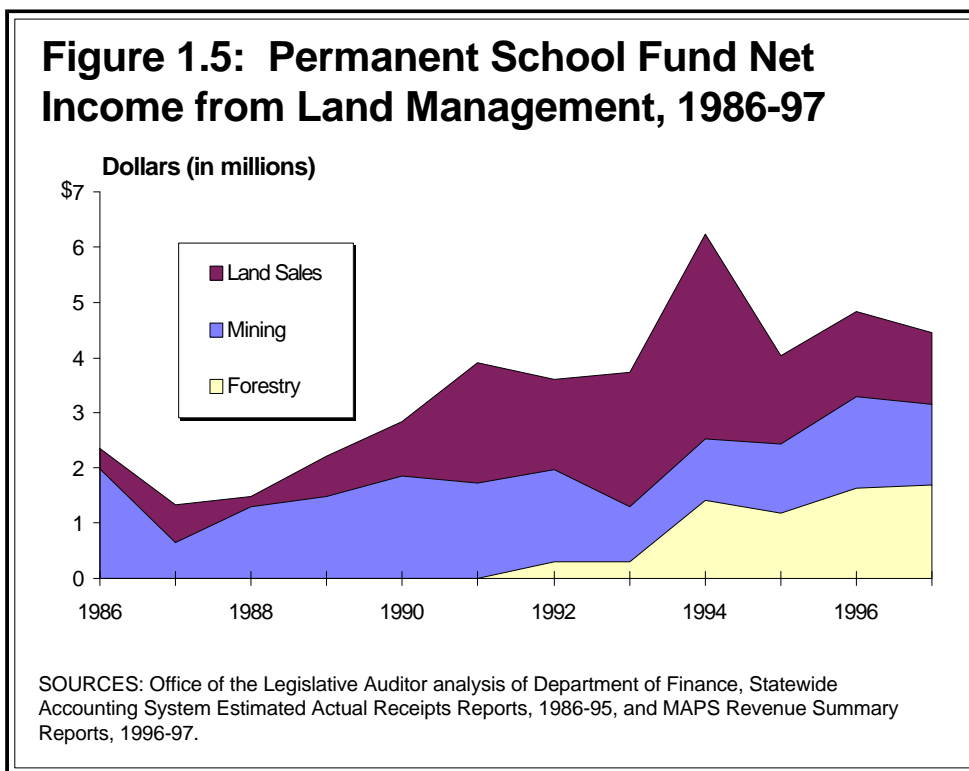
Minnesota still has more school trust land than most neighboring states.

24 to 25 percent of their original trust land grants. Most of the western states we examined, however, have retained between 60 and 98 percent of the federal school land grant.

From Minnesota's remaining school trust land, the PSF principal continues to receive revenue from mining rents and royalties, forestry management activities, and land sales. Forestry management activities include both timber sales and leasing of trust land. Our analysis of revenues from land management activities shows that:

- **Since 1986, the sale of assets including mining rents and royalties and land sales accounted for 84 percent of the deposits into the PSF principal, while net revenues from timber sales and trust land leases accounted for 16 percent of deposits.**

Figure 1.5 shows the net revenues from land management activities added to the PSF principal since 1986. Management of trust land contributed about \$41 million to the principal of the Permanent School Fund between 1986 and 1997, or



an average of \$3.4 million per year. Mining activities and land sales, predominantly the sale of lakeshore lots, accounted for the majority of deposits into the Permanent School Fund, with the remainder coming from forestry management activities, primarily timber sales.

Mining, land sales, and timber sales each accounted for about one-third of income in 1997.

There was considerable variation in the source of revenues deposited in the PSF between 1986 and 1997. Mining rents and royalties have provided the most stable source of revenue to the PSF, generating an average of \$1.4 million in revenues each year. Net revenues from forestry management activities, including timber sales and land leases, increased from zero in 1991 and preceding years to nearly \$1.7 million in 1997. Trust land sales, most notably the sale of lakeshore lots in the late 1980s and early 1990s, represented an increasing revenue stream for the PSF beginning in 1988.

Revenues from mining, land sales, and forestry management activities added \$4.8 million and \$4.4 million to the Permanent School Fund principal in 1996 and 1997 respectively. These revenues were nearly evenly divided between mining, land sales, and forestry management activities, with each accounting for about one-third of all revenues, as illustrated in Figure 1.5.

The market value of the PSF principal was about \$437 million as of June 30, 1997. Over the past 12 years, the distribution to school districts has been between \$29 million and \$36 million each school year. During the 1995-96 school year, nearly \$31 million was distributed to schools, comprising less than one percent of all state revenues to K-12 schools.

SUMMARY

This chapter has shown that the federal government's grant of land to Minnesota for the use of schools and the state's acceptance of the grant created a real, enforceable trust. The trust consists of both the school land and the Permanent School Fund principal arising from the proceeds of this land. When the State of Minnesota accepted the terms and conditions of the federal land grant, it accepted the position of trustee for public schools in Minnesota. The trustee relationship extends to the Minnesota Legislature, which has delegated responsibilities to the Department of Natural Resources for managing the trust land and the State Board of Investment for investing the assets of the Permanent School Fund.

Fiduciary principles governing private trusts apply to school trust land and the Permanent School Fund.

According to our research, the trust status of the federal grant lands imposes obligations and constraints on how the state may manage school trust land that would not apply if the state held the land outright. The same fiduciary principles that govern the administration of private trusts apply to trustees of school trust land and the Permanent School Fund principal. Case law emphasizes that the trustee's primary responsibilities are to the trust, not to other state goals, policies, or considerations.

The Minnesota Legislature, DNR, SBI, and other trustees manage the school trust land and PSF in the interest of the current and future beneficiaries. According to our understanding, the trustees should not sacrifice the economic interests of the trust beneficiaries by using trust assets to serve other purposes. The trust concept that applies to grant land establishes a recognition of the cost of withdrawing the land from income production. While granted land can be used for any public purpose, if such use decreases income to the PSF principal, then methods should be sought to compensate the trust. Chapter 2 analyzes how DNR has managed the school trust land in light of the above trust principles.

