

The Federally Granted Trusts: What Makes Them Unique January 5, 1999

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I. History of the Federally Granted Trusts

The practice of providing grants of land for the support of educational institutions has a long if obscure history going back to the English middle ages. In America, before the federal constitution was written, the framers of the Articles of Confederation committed to provide land grants for the support of a public school system. The General Land Ordinance of 1785 reserved section 16 in each township "for the maintenance of public schools within the said township"(1).

At the time each new state was added to the Union the federal government made land grants for the support of schools and other specific beneficiaries. Since 1802, when Ohio joined, every new state has benefited from that policy. In 1849, Michigan became the first state to become the direct grant recipient. Prior grants were made directly to the township. (2) The purpose of the grants and any restrictions or limitations were identified in the Enabling Act approved by Congress and Constitution of each individual state. (3)

The land grant system has not been static. As new states were added, the size of the grants to the schools was increased, grants to universities and other institutions were added and the nature of the grants was refined. The federally granted lands are currently managed by twenty-two state programs under differing legal structures that have evolved over 200 years of history resulting in variations on the same central theme.

The lands are subject to complex state laws that are sometimes in tension with each other and difficult to apply. These tensions and difficulties in interpretation and management have resulted in a number of federal and state court cases that have provided further direction and clarity to the nature of the grants and their management.

Despite these differences, each state's Enabling Act, Constitution, state statutes and resulting case law draw commonality from a deep, clear past with a consistent core. Chief among these commonalities are:

- the trusts are managed to provide financial support for specific, named beneficiaries (4),
- the trusts are perpetual (5),
- the trusts are managed by public entities,
- the trusts are subject to the same federal and state laws as private lands,
- in addition to the laws of general applicability the trusts are subject to specific state law governing the management of the trusts (6).

These common elements make federally granted trust land management appropriately unique from private and other public land management.

II. Federally Granted Land Compared to Other Land Management

Contained above are the core characteristics of the Federally Granted Trusts. These form major differences between Federally Granted Trusts and 1) other trusts and 2) private and public land management. These distinctions are often ignored, misunderstood or misused by occasional observers or those wishing to see grant lands managed to meet their own ends. In this section, the specific differences between federally granted trust land management and other land management frameworks are reviewed.

A. Private Trusts:

The courts have ruled that the federal grants constitute real and enforceable trusts (7), and where the documents that created the trust are silent, the common law principles governing the administration of private trusts apply (8). As a result, federal grant land management is subject at a minimum to the same array of rules and enforcement mechanisms that surround any private trustee, such as a banker managing funds for a client's grandchild.

The Restatement (Third) of Trusts (1990) (9) identifies and discusses the following relevant duties of a trustee:

- a duty to administer the trust,
- a duty to manage trust assets with undivided loyalty,
- a duty to delegate trustee duties only when reasonable,
- a duty to keep and render accounts,
- a duty to furnish information to beneficiaries,
- a duty to exercise reasonable care and skill in managing the trust,
- a duty to take and keep control of trust property,
- a duty to preserve trust property,
- a duty to enforce claims held by the trust,
- a duty to defend actions that may result in loss to the trust,
- a duty to keep trust property separate from other property,
- a duty to use reasonable care regarding bank deposits,
- a duty to make the trust property productive,
- a duty to pay income to the beneficiaries,
- a duty to deal impartially with beneficiaries,
- a duty to use reasonable care to prevent breach of the trust by co-trustees, and
- a duty to follow the direction of persons given control over the trustee.

These duties should not be viewed as individual legal obligations, but rather as, touch points to guide the trust manager in achieving the primary goal of the trust-to provide the greatest support to the named beneficiaries in accordance with the terms and conditions of the grant. What makes the federal grant trust system unique, is not the goal or the specific duties which The trust managers are responsible for, but rather, how the duties are applied (10).

The following sections contrast and compare private and federally granted trust application of the six most relevant trustee duties.

1. Undivided Loyalty: The common law duty of undivided loyalty to trust beneficiaries is fundamental to management of trust assets. This principle requires that trust land and its assets not be diverted to benefit others at the expense of the trust beneficiaries without compensation. There is, however, no requirement to avoid providing others with collateral benefits (11). The trustee simply must make all decisions with the beneficiaries' interest first and foremost in mind (12).

This opportunity to provide collateral benefits while protecting the interest of the beneficiaries, coupled with the aspiration and legislative direction to provide benefits to the general public, makes grant land management atypical from private trust management.

For example, states may wish to provide for a sustainable flow of resources from grant lands, both through time and across the geographic regions of the state. This strategy will promote both public objectives (to support community stability and reduce environmental impacts) as well as, the trust objective of adding to the stability of beneficiaries' revenues. The trust mandate does not prevent the manager from scheduling the sale of resources to simultaneously meet both social and trust goals so long as the trust is the same or better off.

Providing public benefits is permissible even in the case where benefits to the trust are reduced, so long as the trusts are compensated for such lost revenue opportunity. This places a responsibility on the manager to assure that the trusts are compensated for any reduction in benefit that results.

For example, in 1988, the Washington State Department of Natural Resources in its "Strategic Plan for Forest Resource Management" created a special lands program to identify trust lands which have significant social value. The lands are to be transferred out of trust status, but only when the trust can be compensated for land value and reasonable holding costs.

The department recognized that because of their sensitive nature, these lands would have high management costs if managed for timber harvest. The expected return from holding these land for eventual transfer to protected status was equal to, or greater than, that expected from managing or selling the land for timber production.

As a result, grant lands identified as having special characteristics desirable for eventual movement to protected status have produced hundreds of millions of dollars in revenue through sales to state parks and other state programs. (13) In all likelihood, this revenue would have never been realized by the trust had the lands continued to be managed or sold for timber revenue production. This has been accomplished at lower management cost than would be required for resource extraction. At the same time, the citizens of the state have benefited and will benefit for generations to come from the environmental, recreational, and spiritual values these lands provide.

Similarly, in areas where revenue potential from traditional sources is low, large blocks of low productive land may be leased to the state's wildlife department for habitat enhancement. Timber growing on these lands and nonrenewable resources will be available to provide financial benefits at some point in the future, even though the lands have been removed from the current harvest base. The trust retains the right to cancel these leases for higher and better use should unforeseen opportunity for greater revenue production for the trusts arise.

The trust mandate, rather than precluding the use of grant lands for aesthetic, environmental and recreational uses, requires the trust manager to find ways for the trusts to benefit from these or other noncommercial opportunities (14). The private trust manager has less incentive or opportunity to do so.

The grant land manager often finds itself between two competing interests. Some resource users sometimes claim that any action the manager takes beyond complying with the minimum legal requirements, violates a trust duty to provide revenue for trust beneficiaries. Others believe the trust manager, as manager of public resources, has a higher "duty" than maximizing revenue, and should be held to a higher standard of stewardship. Neither point of view reflects a complete understanding of the trust duties of undivided loyalty (15). It is the manager's responsibility to sincerely weigh the potential benefits and risks to determine what is in the best interest of the beneficiaries and to act accordingly.

2. Deal Impartially with Beneficiaries: This duty is relatively straightforward for private trust managers where the beneficiaries are finite and known. Since the federal granted trusts are perpetual, the vast majority of beneficiaries have not been born, and the future financial needs are unknown. This puts an added burden on the manager of considering not just the total amount of benefits, but the timing of benefits as well. The perpetual nature of the federally granted trusts, coupled with the duty to deal impartially with beneficiaries, leads to the prominence of the concept of sustainability and intergenerational equity in their management. This is unique, compared with private trust or private land management where the focus is on current beneficiaries. As a result, rather than being primarily fixed on the here and now, federal grant trust managers are focused on providing sustainable benefits, and careful management of the corpus as it supports sustainability of benefits.

3. Preserve Trust Property: The perpetual nature of the federally granted trusts requires that the manager take a longer term view of protecting trust property. In preserving trust property, the private trust manager appropriately focuses on strategies related to protecting the financial value of the trust property from short term risk. The granted trust manager, by contrast, must be more concerned about long term risks such as inflation and loss of the underlying productivity of the land.

For revenue generation to be sustained, basic elements of the corpus--soil, water and growing capacity--must be maintained. Revenue to current beneficiaries must be balanced against the risk of reducing revenues to future beneficiaries. All generations have an interest in current management decisions. In making a decision, the federal trust manager must consider not just the potential benefits to today's beneficiaries, but the impact on the opportunities that will be available to future generations of beneficiaries who are not yet able to speak for themselves.

For example, in the case of forestry, cutting timber at younger ages may increase current revenues but may also reduce the long term productive capacity of the overall forest to produce timber and revenue in the future.

4. Making the Trust Property Productive: The duty of making the trust productive of revenue is fundamental to providing benefits to the named recipients. This does not require that the manager maximize current economic return when to do so would conflict with the duty to preserve the

productivity of trust property to provide benefits for future generations.

This conflict is heightened in the case of the federal grant lands because of the perpetual nature of the trust and the manager's responsibility to future generations of beneficiaries. By contrast, private trusts generally have a finite term, and the trustee's responsibility is limited to current beneficiaries, that are often few in number, such as a trust for the benefactor's children.

The courts have recognized this aspect of federal grant land management. In Oklahoma Education Ass'n, Inc. v. Nigh (16), the court noted, "the duty to in return to the trust estate from the trust properties is subject to the taking of necessary precautions for the preservation of the trust estate". The Montana Supreme court in Thompson v. Babcock (17) concluded that maximization of immediate income was, in effect, secondary to the need to preserve the trust properties.

The conflict between classes of beneficiaries is, however, not unique to the grant lands. As stated by the Restatement (Third) of Trusts, "the interests of the life beneficiary are almost inherently in competition with those of the remainder beneficiaries." As guidance to the trustee, the restatement advised, "These conflicting fiduciary obligations result in a necessarily flexible and somewhat indefinite duty of impartiality. The duty requires the trustee to balance the competing interests of differently situated beneficiaries in a fair and reasonable manner." In the case of the granted trust, these differently situated beneficiaries are infinite. To be fair and reasonable, the manager must provide for sustainability of the resource indefinitely.

'The states' administration of the federally granted trust lands heightens some of the already recognized tensions inherent in satisfying the duties of productivity and preservation, as well as that of impartiality. The impact on management is best illustrated by the emphasis on sustainability in grant trust management. All states have addressed assuring sustainability of resources as a cornerstone of their management strategies.(18) This regard for sustainability has two sources: perpetuating revenues for the trust beneficiaries and avoiding roller coaster fluctuations in annual revenues. (19)

5. Diversification: A common law duty that also presents distinction between private trust management and the grant land trust, is that of diversification. Except as otherwise provided by the terms of the trusts, all trustees are under a duty to the beneficiary to distribute the risk of loss by a reasonable diversification of investments, unless under the circumstances it is prudent not to do so.(20) The restatement adds that "diversification concerns do not necessarily preclude an asset allocation plan that emphasizes a single category of investment, as long as the requirements of both caution and impartiality are accommodated in a manner suitable to the objectives of the particular trust".

The structure of the federal land grants, and the surrounding legal framework, limit the degree of diversification that appears practicable or appropriate by the states. The grants were made in a single asset class--land, and other than those states with a permanent fund no mechanism or opportunity outside of land ownership is made available to the managers of the granted trusts.

The state legislatures have not provided the authority for the managing agency to diversify beyond land holdings and in fact have often provided additional limitations on the degree of diversification. For example, in Washington State the legislature has directed the department to neither deplete the publicly-owned land base nor reduce the publicly-owned forest land base. (21) These restrictions seem consistent with the perpetual nature of the granted trust, and those states that have retained more of the trust corpus in land are better able to provide greater sustainable support for the beneficiaries.

6. Public Management: The public nature of the management relates to the last duty of a private trust manager "to follow the direction of persons given control over the trustee". The public nature of the environment in which the federally granted trust manager operates, provides the greatest difference between the private and public manager and the greatest management challenge to the granted lands trust manager.

The visibility of public management opens the federally granted trusts to risks not faced by private trusts. Without exception, these lands have been classified and are thought of as public lands. Their visibility has increased rapidly as the importance of public lands is increasingly recognized. Recent controversies generally revolve around the public use.(22)

Simultaneously, all government officials have a duty to act fairly and openly to the extent possible when dealing with the public.(23) A manager must conscientiously balance their responsibility to the federal

trust with equal responsibility to serve the public.

Some state agencies have environmental requirements not faced by private trust managers.(24) State environmental rules in many states require an environmental review of the agency's program, as well as individual actions that may impact the environment. This may result in higher costs than private trust management, but provides additional protections to the corpus of the trust.

Public management gives the beneficiaries additional opportunity to receive information on the management of trust assets as well as to express their opinion on how the trust assets should be managed. Trust beneficiaries have the opportunity to appeal to the state legislature and presumably Congress if they are unsatisfied with the agency's management.

The public has benefited greatly from grant lands. State legislatures have directed management agencies to provide benefits to the general public where to do so can be compatible with the paramount purposes of the trust.(25)

B. Private Land Management

Private land management can be classified into two types: direct, where the owner of the resource is also the manager; and indirect, where the management is separated in some way from ownership. In the following section private corporate management will be compared to public granted trust management.

Generally, the managers of the corporation administer the corporation's assets on behalf of the stockholders and their oft-stated objective is to provide the benefit to current stockholders by maximizing the value of the stock. Future income and costs are only valued to the extent they impact the current value of the stock. This leads to the classic economic solution of maximizing present net worth as a guide to decision making. Present net worth is calculated by discounting projected revenues and expenditures to determine present value.

So while a company may be perpetual, the objective of managers is very much focused on the present. By contrast, the grant trust manager must consider the impact of their decision on all future as well as current generations, treating each generation impartially. Since revenue to each generation of beneficiaries is just as important to them as current benefits are to today's beneficiaries (26), it follows that revenue to each generation should have equal weight in the decision making of the manager. Therefore, the use of a discount rate which gives higher value to income for the current generation of beneficiaries over future beneficiaries is drawn into question.

A Management of Other Public Lands

Federal and state agencies manage a wide array of lands on behalf of the public. These include historical properties, parks, shorelines, aquatic lands, wildlife refuges, public buildings, State and National Forests and other resource lands.

One of the main distinctions between these lands and the Federal Grant lands is that they are not managed primarily for revenue production. Most are managed for specific purposes, others like the National forests are managed to provide multiple benefits. Financial benefits from these lands are but one of many benefits that must be weighed against other public benefits in determining the use of the land. Federal public lands are managed under a "multiple-use" statute that guides management of the Forest Service and Bureau of Land Management lands - "the management of all the various renewable surface resources of the national forests so that they are utilized in the combination that will best meet the needs of the American people". (27)

The clarity of the federal grant trust mandate is a key distinction between trust land management and federal land management. -- the state trust lands are managed to achieve a specific goal: raising money to support clearly identified beneficiaries. These goals enable the managers of the federally granted trusts to be uncommonly clear about what they must sustain. By contrast, the management of federal lands has been plagued by the multi-pronged nature of the management mandate.

HL Summary

The mandate to manage the lands in the interest of the named beneficiaries has given the managers' clear direction. This mandate to provide financial support to beneficiaries is tempered by the perpetual nature of the trust which beckons the managers to pay careful attention to preservation of the corpus. Managers should exercise care to assure that the future productivity of the trust to provide revenue to the named beneficiaries is not unduly jeopardized by a zeal to produce current income.

The perpetual nature of the federal grant lands gives the manager a responsibility to treat each generation of beneficiaries equitably. This draws into question the traditional economic measure of present net worth which gives much greater weight to net benefits received by current beneficiaries over those to be received by future beneficiaries. Rather the states have moved toward a goal of providing sustainable flow of resources from the lands they managed and providing special care in protecting the elements of the corpus that support sustainable resource production.

The public nature of the management provides added opportunities for the trust beneficiaries, as well as others interested in the management of these lands, to receive information about the management of trust assets. It also provides opportunities for the managers to provide collateral benefits for the general public. When this reduces current or potential income, the manager has a duty to seek compensation for the beneficiaries. Ownership by the states, designation as public lands, and management by a state agency exposes the trust to legal and political risks not faced by private managers. As a result, managers of the granted trust must use extra prudence in managing these lands to protect the trust against such risk.

The manager of the granted lands as an agent of the people is under special duties to carry out their public duties fairly and openly. There's a presumption that all laws are legal until declared otherwise by the courts, and the manager is duty-bound to seek clarification and then carry them out even if they may seem in conflict with the trust obligation. The manager should interpret all statutes in a manner that is consistent with constitutional requirements. (28)

Conclusion

The unique characteristics of the federal grant lands are the basis for clear and real differences in the management of these lands resulting in more conservative, prudent, and environmentally sensitive management. Today more than 132 million acres are managed by the states under federal grant trust status. The impact of management goes beyond just these land management, as they provide a model for private and federal as well as other state lands. The management of federally granted lands is providing an example for private management of agricultural and grazing lands.

Those interested in the well being of the beneficiaries and in the management of these lands must recognize the special nature of the land grant trust. It is this unique history that provides the foundation for current management strategies and decision making. This history must also be considered as states establish performance standards that guide future management of these trusts.

End Notes

1. The section reserved was located as near the center of the township as possible to minimize the maximum distance any student would have to travel to reach the school.

2. Grants made directly to the townships created a problem as townships had no formal governing bodies.

Granting the school lands to the state rather than to the individual townships required the state to establish a school fund to receive and disburse the funds to the schools. This fund evolved into a perpetual permanent school fund. States enacted increasingly elaborate provisions for supplementing the fund and for protecting it against loss and diversion.

The process is still on going. States are now looking for ways to protect not just the nominal value of their school funds but the actual purchasing power of the permanent funds.

3. Together, the Enabling Act and Constitution form the compact by which each new state is invited into and agrees to join the United States of America. The Enabling Acts passed by Congress outline the provisions by which the new state may join the Union. Each new state must agree to the provisions of

the Enabling Act offered to it and submit a State Constitution to Congress. Through these documents, each state's federal grant trusts were established.

4. Although individual states' Enabling Acts differed, they all identify specific beneficiaries of the grants. They also included some management requirements. For example, that sales are at public auctions for not less than fair market value of the property.

5. Trusts are not necessarily perpetual. A trust might be liquidated, for example, at the instruction of the grantor, when a beneficiary reaches a certain age, or when the purposes for which the trust was established are achieved. The purposes for which the federal granted lands trusts were created "for the support of the common schools", "for educational purposes" and the support of other named state institutions seems unlikely to ever be fulfilled. Thus, the trusts appear to be as perpetual as the state's need to educate its citizens.

The trust purposes can also be changed or the trust terminated if the purpose for which the trust was established is no longer reasonable. This of course would take no less than an act of Congress. The states cannot unilaterally revoke the trust as in every instance, as the "compact irrevocable" language underscores, statehood was an actual exchange whose terms and conditions were explicitly stated in the Enabling Act and constitution under which each state entered the Union. (Souder p.27)

The perpetual nature of the federally granted trust is bolstered by the requirement of a permanent fund. Only the interest can be used.

Throughout the twentieth century, the state trust programs have increasingly coveted their land assets, and evolved gradually toward a commitment to retention and active land management as a prudent trust management strategy for a perpetual trust.

6. For example, the Washington State Constitution specified that the lands are held in trust for all the people of the state. In the area of forest resources, RCW 79.01.124 provides that "the best interest of the state" must be considered before timber or fallen timber is to be sold. RCW 79.01.212 further requires that the state find "that the best interests of the state may be subserved" before a confirmation of a timber sale is entered.

7. Viewing the land grants as trusts has evolved over time, the strongest language is in the - New Mexico and Arizona accession (1910) and this strong language (through case law) has been applied retrospectively and with increasing clarity to all the grants. Sec. 10 of New Mexico and Arizona's Enabling Act specifically provided that lands granted to the state were to be held "in trust" and declared that it was the duty of the attorney general of the United States to enforce in court the provisions relating to the application and disposition of the lands, the products thereof, and the funds derived therefrom. (Souder p.26)

This may partially explain why key U.S. Supreme Court decisions are unusually likely to involve cases about those two states. The general trust rule is that, once a trust is established, the settlor has a very limited role in its administration. However, the U.S. government is not a typical settlor. (Souder p. 307)

8. Skamani 102Wn.2d at 129; see also State ex rel. Hellar v. Young, 21 Wash. 391,392,58p.220 (1899)

9. Restatement (Third) of Trusts chs. 170-171, 181, 183-185.

10. The Washington Attorney General's office found that while the duties of a private trustee apply to the federal grant land, these duties are more flexible in application to the federal grants, and this flexibility may be highlighted in the context of federal grant land administration. (Washington AGO 1996 No. 11)

11. Collateral benefits seem fundamental to the original purpose of the trust. One of the requirements included in the enabling acts of many states is that all sale of land and valuable material be made at public auction. This provision has a double purpose, it assures that the trusts receive "fair market value" and provides equal opportunity to the public to purchase trust resources when they are offered for sale. Other provisions limit the size of individual sales and limit the total quantity that can be sold in certain periods. Again, these provisions appear to have been aimed at achieving both trust and social goals.

12. Washington State Forest Resource Plan, p.B-2.

13. Under Washington law, the portion of the revenue identified as timber value is transferred to the designated beneficiary, the land value is reserved to purchase replacement land to support future timber harvest and revenue to the beneficiaries. As a result, the sustainable harvest from trust lands has been increased.

14. Despite what is at first glance a rather narrow and restrictive management mandate, the states' managers appear to be quite flexible in their approach to resource management. They managed for all the "traditional" income production uses-- grazing, timber, oil, gas coal. But they also take an aggressive approach to developing alternative income sources that might benefit the trust, quickly reacting to changing market conditions, and new income producing opportunities. (Souder and Fairfax p.8)

15. Forest Resource Plan (FRP), Policy Plan, Washington State Department of Natural Resources, July 1992, Appendix.

16. Oklahoma Education Ass'n, Inc. V. Nigh, 642 P.2d 239 (Okla. 1982).

17. State ex rel. Thompson v. Babcock, 147 Mont. 46, 409 P.2d 808 (1966)

18. Not all sustained yield directives are mandated by statute. In Montana, the state supreme court found in Jerke v. Department of State Lands that the notion of sustained yield is *implicitly* contained in the constitutional direction to achieve full market value for trust resources.

19. The forestry profession's ideological commitment to sustained yield has become an important component of timber management on trust lands. It constitutes a significant addendum to the commitment to maximize revenues on trust lands. (Souder p. 167)

20. Restatement (Second) of trusts.

21. Revised Code of Washington (RCW) 79.66.010

22. On one hand, these controversies are couched in terms of the public's asserted right of access to their "public" lands - the right has traditionally been advocated by hunters and anglers but increasingly by other non-consumptive outdoor recreationalists who are increasingly in conflict with each other because of increased use. This is being driven not just by the increased level of use overall, but by the reduction in opportunities on private and other public lands. At the same time there is increased pressure to maintain the existing biological value and composition of the trust lands. These "uses" are sometimes in conflict with both income production and other active recreational uses of trust lands.

23. Known as the sacred trust duty, managers in government have a duty to conduct their official duties in the public's interest, not for personal gain nor for private, specific gains to others. This duty applies to all appointed state employees.

24. In Washington, the State Environmental Policy Act (SEPA), RCW ch. 43.21c, directs that to the fullest extent possible, policies, regulations and laws of Washington are to be interpreted and administered in accordance with the state's environmental policies as set forth in the act. All branches of government, including the agency responsible for trust land management, are to follow the guidelines and procedures specified in SEPA in planning and decision-making. These include determination of the environmental impacts of agency actions.

25. The Washington State Multiple Use Act (RCW 79.68), directs that a multiple use concept be utilized by the Department of Natural Resources in the management and administration of stateowned lands under the jurisdiction of the department where such a concept is in the best interests of the state and the general welfare of the citizens thereof, and is consistent with the applicable trust provisions of the various lands involved.

Multiple uses may include recreation, educational or scientific use, maintenance of rights of way, greenbelts, scenic and historic areas, and watershed protection. If such additional uses are not comparable with the financial obligations in the management of trust land they may be permitted only if

there is compensation for such uses satisfying the financial obligations (RCW 79,68.050).

26. Pat McElroy, former deputy supervisor of Washington State Department of Natural Resources from an unpublished memo on file with the Washington State Department of Natural Resources.

27. Multiple-Use Sustained Yield Act of 1960, 16 U.S.C. ch. 531-4(a)

28. Grant v. Spellman, 99 Wn.2d 815, 819, 664 p.2d 1227 (1983).