

# Legislative Audit Division

State of Montana



Report to the Legislature

October 2001

## Performance Audit

### State Agency Land Exchanges

Department of Natural Resources and Conservation  
Montana Department of Transportation  
Department of Fish, Wildlife and Parks  
Montana University System

This performance audit examined the processes used by state agencies to exchange land including completing land exchanges, valuing land to be exchanged and complying with applicable laws. The report contains information on land exchange activity since 1994 and includes the following recommendations:

- ▶ Department of Natural Resource and Conservation use of cash equalization payments in trust land exchanges.
- ▶ Establishing procedures to implement land banking concepts as part of trust land management.
- ▶ Clarifying Montana Department of Transportation procedures regarding documentation of land values for land exchanges.
- ▶ Documenting the environmental decision-making process for all Montana Department of Transportation land exchanges.

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Members of the performance audit staff hold degrees in disciplines appropriate to the audit process. Areas of expertise include business and public administration, statistics, economics, accounting, logistics, computer science, and engineering.

Performance audits are performed at the request of the Legislative Audit Committee which is a bicameral and bipartisan standing committee of the Montana Legislature. The committee consists of six members of the Senate and six members of the House of Representatives.

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October 2001

The Legislative Audit Committee  
Of the Montana State Legislature:

This is our performance audit of State Agency Land Exchanges. We reviewed programs administered by the Department of Natural Resources and Conservation, the Montana Department of Transportation, the Department of Fish, Wildlife and Parks, and the Montana University System.

This report provides information to the legislature regarding the processes used by these state entities to exchange state land. The report contains information on land exchange activity since 1994.

Recommendations address potential improvements in trust land management and administration of land used for highway purposes. Written responses from the various entities are included at the end of the report.

We appreciate the cooperation and assistance provided to us by department personnel during the audit.

Respectfully submitted,

*(Signature on File)*

Scott A. Seacat  
Legislative Auditor

# **Legislative Audit Division**

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## **Performance Audit**

### **State Agency Land Exchanges**

**Department of Natural Resources and Conservation  
Montana Department of Transportation  
Department of Fish, Wildlife and Parks  
Montana University System**

Members of the audit staff involved in this audit were Susan Jensen, Kent Rice, Kris Wilkinson, and Mary Zednick.

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## Appointed and Administrative Officials

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Linda McCulloch, Superintendent of Public Instruction  
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Mike McGrath, Attorney General

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John Mercer  
Lynn Morrison-Hamilton  
Richard Roehm  
Mark Semmens  
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### **Fish, Wildlife and Parks Commission**

Dan Walker, Chair  
Tim Mulligan, Vice Chair  
John Lane  
Darlyne Dascher  
Michael Murphy

### **Department of Natural Resources and Conservation**

Bud Clinch, Director  
Tom Schultz, Administrator, Trust Land Management Division  
Clive Rooney, Chief, Special Use Management Bureau

### **Department of Fish, Wildlife and Parks**

Jeff Hagener, Director  
Paul Sihler, Administrator, Field Services Division  
Debby Dils, Land Section, Field Services Division

### **Montana Department of Transportation**

David A. Galt, Director  
Gary Gilmore, Administrator, Highways and Engineering Division  
John Horton, Chief, Right-of-Way Bureau

### **Commissioner of Higher Education**

Richard A. Crofts, Commissioner  
LeRoy H. Schramm, Chief Legal Counsel

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### Introduction

The process of “trading” or “swapping” lands is referred to as an exchange. During the last decade, the State of Montana was involved in a number of land exchanges. State land has been exchanged for private and/or other government-owned land. Based on public comments relating to exchanges of state land, the Legislative Audit Committee requested a performance audit of the exchange process.

We compiled and reviewed land exchange information at four entities: the Department of Natural Resources and Conservation (DNRC), the Montana Department of Transportation (MDT), the Department of Fish, Wildlife and Parks (FWP), and the Montana University System (MUS). These four entities were selected based on their significant land holdings, exchange activity, and constitutional and statutory provisions.

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### What is State Land and Who is Responsible for Management?

State land can be classified as either trust lands or fee (non-trust) lands. Congress approved the Enabling Act granting Montana statehood on February 22, 1889. The Enabling Act also granted sections 16 and 36 in every township within Montana to the state for support of common (public) schools. The total of all acreage granted to the State of Montana was 5,856,720 acres. These lands are referred to as “trust lands.” Each section of trust land is assigned to one of ten trusts. These trusts are permanent funds. Montana’s Constitution gives direct management authority for trust lands to the Board of Land Commissioners (Land Board). The Land Board consists of five elected Montana officials: the Governor, Superintendent of Public Instruction, State Auditor, Secretary of State, and Attorney General. Under the direction of the Land Board, DNRC is the agency responsible for daily management of trust lands.

In addition to trust lands, the State of Montana also holds fee title to lands (i.e., owns land). These lands are usually managed by the state agency holding title to the land. Some of the agencies holding title to non-trust lands include MDT, FWP, and MUS.

## Report Summary

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### State Land May be Exchanged

The Enabling Act and the Montana Constitution specify that “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 Constitution also specifies that “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.”

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### How Does a Land Exchange Work?

In its simplest form, a land exchange is an agreement between two landowners to swap ownership of two separate pieces of property. Landowner #1 trades property A for property B owned by Landowner #2. The deed to property A is transferred to Landowner #2 and the deed to property B is transferred to Landowner #1. The exchange is complete.

While this simplified scenario can occur, there are generally many more steps and/or possibilities involved in state agency land exchanges. There may be more than two landowners involved in an exchange, or there may be more than two pieces of property to exchange. In addition, the specific land involved in an exchange may not be identified up front. A pool of land may be proposed for exchange, but the actual acreage may not be identified until later in the process. These factors increase the complexity and amount of time involved in an exchange.

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### How Do Land Exchange Processes Compare to One Another?

Land exchange processes are generally similar among the four agencies. The public is usually involved in land exchange proposals, land no longer useful to the agency is exchanged, and appraisals are used to determine land value. Variations in processes exist due to the types of land exchanged (grazing versus timber), the purposes for exchanging land, and specific mandates and procedures used to complete an exchange. For example, DNRC exchanges are subject to the seven Land Board criteria. MDT does not have public notification requirements, nor does MDT have to obtain approval from the Land Board. There are few similarities between the

mission statements of the four agencies. As such, the lands managed by these agencies also vary. The biggest of these variations appears to be use and area or acreage.

We also obtained information on other state and federal land exchange procedures to compare to Montana's. Our review of other states was limited to trust land management in Washington, Colorado, Wyoming, Utah, and Idaho. We also briefly reviewed procedures used by the Bureau of Land Management and the United States Forest Service.

***Conclusion: State Agency  
Land Exchange Processes are  
Comparable***

State agency land exchange processes are comparable to one another and to other states and the federal government. There are differences in specific procedures, but in general, the processes are comparable.

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**State Land Exchange  
Processes Provide Benefits**

State agency land exchange processes appear to provide benefits to the state and the public by meeting the missions of the agencies involved. DNRC generates income for trusts and consolidates holdings. FWP obtains and/or protects land for wildlife management areas, parks, and fishing access sites. MDT obtains needed right-of-way and disposes of excess land. MUS adjusts boundaries and consolidates holdings to improve overall land management.

The Constitution, laws, and policy provide some flexibility in land exchanges. In general, agencies complied with land exchange requirements for those projects reviewed. Agencies use the broad authority of the Constitution and statutes to complete land exchanges. The land exchanges completed under agency procedures were reviewed by the public, in most instances approved by a governing board, and appear to have benefited the state and the public.

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**Cash Equalization Payments  
May Assist DNRC  
Exchanges**

Both FWP and MDT use cash payments to equalize the land values in an exchange. These are referred to as cash equalization payments. The Bureau of Land Management and United States Forest Service also use cash equalization payments to balance out land exchanges, as do all five other states we contacted.

## **Report Summary**

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DNRC does not use cash equalization payments for land exchanges. According to DNRC personnel, cash equalization payments cannot be accepted in a land exchange because it would then be considered a direct sale. By statute, direct sales of trust land are not allowed. Trust land sales are to be by public auction, and proceeds from sales are to be deposited to the permanent trust.

FWP and MDT use cash payments to help equalize values and achieve goals through land exchanges. While FWP and MDT lands are not school trust lands, these agencies are held to the same constitutional mandate regarding land exchanges: disposal of public land, in an exchange, must be for equal value. By statute (section 30-11-112, MCA), an exchange is an agreement to exchange “one thing for another, neither thing nor both things being money only.” Based on this definition, cash equalization payments appear to be allowable for trust land exchanges, and could provide the department with more flexibility for completing exchanges. We recommend DNRC use cash equalization payments as an option in trust land exchanges.

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### **Land Exchange is Only One Aspect of Land Management**

Exchanging land for other land is only one aspect of land management. There are a number of methods available which could make land management easier and potentially more profitable to the trust. These include land banking, consolidating land, developing land for commercial use, and selling land. One of these methods is discussed in the next section.

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### **Land Banking**

Land banking is a sale and replacement land management concept. Land is sold, but revenues generated from the sale are placed in an account with the intent of purchasing other land to replace the land sold. There is usually a limit placed on the amount of time available to acquire replacement property. If replacement property is not acquired within the time frame, the transaction is considered a sale and the revenue is managed according to statute and other regulations. This concept has numerous names including deferred land exchanges, non-simultaneous land exchanges, assembled land exchanges, and land replacement.

According to DNRC management, land banking has not been pursued due to advice from department legal counsel. The Enabling Act restricts land sales to public auction and sale proceeds must be deposited in the permanent trust. Department managers said the perception of land banking being a sales process has prevented pursuit of a program. However, a program structured to be consistent with procedures and statutes for land exchanges could help achieve goals related to the Land Board's seven exchange criteria.

Use of land banking for trust lands has been recommended and the previous Land Board approved a deferred exchange pilot program. In addition, entities external to Montana state government are using land banking as a land management tool. Land banking has potential for improving trust land administration. We believe DNRC should determine what actions are necessary to implement a land-banking program for trust lands.

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### **Roadblocks to Effective Land Management**

A number of conditions prevent DNRC from managing trust lands as effectively as possible. Some land has limited or no access, resources are limited, and the process takes time to complete.

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### **Some DNRC Tracts are Landlocked or have Limited Access**

The granting of sections 16 and 36 in every township created a checkerboard pattern of state land ownership across Montana. Adjacent landowners include state, federal, and/or private landowners. For DNRC trust lands, there are situations where one landowner owns all land surrounding the trust land parcel. This land is referred to as "landlocked." The revenue-generating capability of trust land can be impacted if the parcel is landlocked.

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### **Availability of Resources Can Impact Ability to Conduct Management Operations**

Personnel allocated to land management activities can impact operations. Constitutional and statutory mandates with regard to land administration must be addressed first. Other activities are completed as time allows. DNRC personnel indicated that identification of land for consolidation, sales or exchanges is not a mandated activity. As a result, the department does not have a program for identifying and disposing of land that is isolated and only generating minimal income to the trusts, and personnel do not

## Report Summary

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actively pursue land exchanges. Funding can also impact land management. Land purchases, cash equalization payments, development, etc. all require funding. If funding is not available, these management actions cannot be completed.

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### **Time Needed to Complete a Land Exchange Can Affect the Process**

The amount of time needed to complete land exchanges varies from agency to agency and project to project. Each exchange is different and different issues/concerns may arise, so each project can be delayed for different reasons at different phases of the exchange. The land exchange process seems to be a lengthy process. Of the four agencies in our review, DNRC has the lengthiest process.

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### **Summary**

Managing land involves a myriad of responsibilities. Numerous activities are conducted to accomplish responsibilities. Our review suggests land exchanges are an effective method of land management. Agencies use various procedures to complete land exchanges. There are numerous other activities included within the overall management of land, some of which are required by law, such as timber harvests and grazing leases. For DNRC, these mandates take priority over non-mandated activities, such as land exchanges. Other management activities like consolidation to dispose of unproductive land are also not priorities of the department. In a perfect world, DNRC would identify all unproductive land, dispose of it through exchange, or possibly even through land banking, and replace the property with land that is equal or greater in value, equal or greater in acreage, and generates more revenue for the trusts. The replacement property would consolidate state holdings and increase access to public lands.

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### **Other Land Exchange Requirements**

An objective of our review was to determine compliance with regulations within the Constitution, statutes, administrative rules, and other established criteria. Of specific interest was determining how the value of land is established, whether the state retained equal value, the environmental assessment process, and public involvement.

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### **How is Fair Market Value Determined?**

The Montana Constitution states that no public land shall be disposed of except in pursuance of general laws or until full market value has been paid. Public land can be exchanged for other land, public or private, but the land must be equal in value. Section 15-8-111(2)(a), MCA, defines market value as “the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.” A common method of determining fair market value is by appraisal. For 24 of 26 projects reviewed, market value was determined through appraisal by a certified appraiser. We did not specifically test whether use of certified appraisers increases the validity of appraisals; however, we did not note any negative effects on the appraisal process or determination of fair market value of land due to use of non-certified appraisers. All appraisals are reviewed and updated when appropriate.

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### **Did the State Retain Equal or Greater Value for All Land Exchanges?**

As part of our review, we compared land values to determine if the state retained equal or greater value for all exchanges. For all exchanges we reviewed, the state retained at least equal value on land it exchanged. MDT did not clearly document values retained for all its projects. We noted one MDT project where it appeared equal or greater value was not retained. After further explanation and clarification from department personnel, we decided equal value was retained for this exchange. However, the file did not clearly document the value MDT retained as a result of the exchange. We recommend MDT clarify procedures used for state land exchanges, specifically those related to documenting land values.

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### **Are Environmental Assessment and Antiquity Regulations Followed?**

As part of our audit, we reviewed agency compliance with the Montana Environmental Policy Act (MEPA) and the Antiquities Act. MEPA requires state government to be accountable to the people of Montana when it makes decisions that have potential impact on the environment. State agencies must analyze the significance of impacts on the environment associated with proposed actions. Exchanging trust and non-trust lands for other lands are actions that impact the environment. We noted MEPA documentation in most

## Report Summary

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files reviewed. MDT does not complete a formal environmental analysis when exchanging excess property. Discussions with MDT legal and environmental services personnel further affirmed that some sort of documentation should be completed. We recommend MDT document its environmental decision-making process for land exchanges.

Section 22-3-424, MCA, requires state agencies, in consultation with the Historical Society, to adopt rules for the identification and preservation of heritage properties and paleontological remains on lands owned by the state. We noted documentation indicating compliance with this requirement in all DNRC and MUS files. At FWP, we noted documentation in 9 of 11 files. Prior to May 2000, MDT did not conduct cultural resource reviews. As a result of a pending land sale, MDT identified the importance of cultural surveys and implemented policy for reviews. All MDT files we reviewed were completed prior to implementation of policy.

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### **Is the Public Adequately Involved with Proposed Land Exchanges?**

We checked files for public notification and public hearing information as required by Land Board policy and MEPA. Our purpose was to determine the level of public involvement in land exchanges. Notifying the public of proposed land exchanges, providing the public an opportunity to comment, and responding to public questions and/or comments as appropriate represents an effective process. Based on our review, it appears the public is properly notified of proposed land exchanges, and hearings are conducted as needed. While there may be disagreements with actions taken, nothing came to our attention indicating the public was not notified or provided an opportunity to comment as required.

# Chapter I - Introduction

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## Introduction

The process of “trading” or “swapping” lands is referred to as an exchange. During the last decade, the State of Montana was involved in a number of land exchanges. State land has been exchanged for private and/or other government-owned land. Based on public comments relating to exchanges of state land, the Legislative Audit Committee requested a performance audit of the exchange process.

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## Audit Objectives

The primary audit objective was to review land exchange procedures of several state agencies. The following objectives were designed to direct audit work:

1. Evaluate the timeliness of land exchange processes.
2. Examine the processes used to establish value of lands.
3. Assess compliance with constitutional and statutory mandates.
4. Compare state land exchange procedures to other states and federal agencies.
5. Determine the overall effectiveness of land exchange processes in terms of public notification, success, and land management.

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## Audit Scope and Methodology

To address our objectives, we compiled and reviewed land exchange information at four entities: the Department of Natural Resources and Conservation (DNRC), the Montana Department of Transportation (MDT), the Department of Fish, Wildlife and Parks (FWP), and the Montana University System (MUS). These four entities were selected based on their significant land holdings, exchange activity, and constitutional and statutory provisions. Their lands make up approximately 99 percent of land owned by the state.

To gain an understanding of the processes, we interviewed department personnel and reviewed numerous documents and information related to land exchanges including:

## Chapter I - Introduction

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- ▶ An audit report of state owned and leased land issued by the Legislative Audit Division in 1983.
- ▶ A United States General Accounting Office report (GAO/RCED-00-73) on federal land exchanges issued June 2000.
- ▶ The 1889 Enabling Act and Montana's Constitution.
- ▶ Statutes and administrative rules.
- ▶ Attorney General Opinions.
- ▶ Exchange files maintained by each entity.

The audit period was March 1994 through March 2001. This period was selected due to establishment of land exchange criteria in 1994 by the Montana Board of Land Commissioners (Land Board). We reviewed a total of 34 exchanges that were completed, denied, or in process during the audit period. While reviewing land exchange files, we developed a timeline for each exchange to evaluate time frames for major phases and the overall timeliness of the process, and documented the phases of the process.

We examined the methodology used by each agency to determine the fair market value of the lands exchanged. This included use of appraisers, appraiser qualifications, contracting of appraisers, and review of appraisals. We determined if the state obtained equal value for the land exchanges reviewed.

We attended Land Board meetings, accompanied staff on site visits of property, observed agency meetings discussing exchanges, and attended public hearings to understand and evaluate the exchange processes. We reviewed minutes and interviewed outgoing members of the Land Board to gain a perspective of Land Board involvement in exchange processes.

We contacted five states in the western region to determine similarities and/or differences in land exchanges. We also gathered information related to federal land exchange processes. We compared land exchange procedures from other states and the federal government with Montana's process to determine similarities and identify possibilities for improvements.

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### Compliance

We examined compliance with laws and rules throughout the audit. No significant compliance concerns were identified. However, we did question department personnel's interpretation of a law relating to Fish, Wildlife and Parks land disposal. Details on this issue are provided in Chapter IV.

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### Management Memoranda

During the course of our review, we identified issues related to land exchanges which we believe warrant management attention but are not the subject of recommendations in this report. We presented the following suggestions to agency management for possible operating improvements.

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### Department of Natural Resources and Conservation

We requested a listing from DNRC showing income from land before each exchange and current income from land received as a result of each exchange. The department does not routinely compile and report income to the trusts for land exchanges. Since income to the trusts is the department's main charge, it should consider expanding its use of outcome measures. We suggested DNRC compile and report the success of land exchanges, at a minimum in terms of income generated for the trusts, on a regular basis.

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### Department of Natural Resources and Conservation and Montana Department of Transportation

A Memorandum of Understanding (MOU) between DNRC and the Montana Department of Transportation requires differences in values for land exchanges to be "zeroed" out every three years. The MOU does not include language regarding how values will be equalized if land exchange and/or easement opportunities do not accomplish equalization within the three-year time frame. We suggested the departments clarify actions necessary in current and future exchange agreements for addressing unequal values at the end of the three-year term.

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### Department of Fish, Wildlife and Parks

The department does not have formal land exchange policies and procedures. Division personnel said the land exchange process is similar to FWP's acquisition process; however, the acquisition process lacks specifics to ensure documentation is maintained and decisions are supported. Formal, written policies and procedures will help guide personnel in performing program functions in a

## **Chapter I - Introduction**

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consistent and efficient manner. We suggested FWP develop formal land exchange policies and procedures.

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### **Montana University System**

We believe the university land exchange process could be improved by formally defining required information. We noted one exchange in which a letter requesting an antiquities review was not sent until 11 days prior to submission of the exchange for Land Board approval. If the review had shown the properties had significant historical value, an additional review by the Land Board could have been required. Additional reviews by the Land Board create time delays and decrease the efficiency of the process. Using a checklist to ensure required information is included in land exchange files would help ensure efficient and comprehensive reviews of proposed land exchanges. We suggested MUS develop a checklist of required information as part of its land exchange process.

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### **Report Organization**

The remainder of this report is divided into four chapters. Chapter II provides general background information on state lands. Chapter III addresses specific land exchange procedures used by the four agencies in our review. Chapter IV describes land management and how state agencies use land exchanges to manage state lands. Chapter V provides information on other land exchange requirements.

# Chapter II - Land Exchanges Background

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## Introduction

Land exchanges with government agencies and/or private individuals are used to augment the management and operations of Montana's state lands. This chapter provides information on the types of state land and the agencies and entities involved with management of that land.

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## What is State Land and Who is Responsible for Management?

State land can be classified as either trust lands or fee (non-trust) lands. The Department of Natural Resources and Conservation (DNRC) is responsible for management of trust lands. Various state agencies manage fee lands. The following sections discuss these two types of land.

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## Trust Land

Congress approved the Enabling Act granting Montana statehood on February 22, 1889. The Enabling Act also granted sections 16 and 36 in every township within Montana to the state for support of common (public) schools. For land within these sections that was sold or otherwise disposed of, or was within a military or Indian reservation, the State of Montana was granted authority to select other equivalent lands in lieu of losing the land. The total acreage granted to the State of Montana for public schools was 5,188,000 acres. Additional acreage was granted to the state under the Enabling Act for educational uses and for state institutions. The total of all acreage granted to the State of Montana was 5,856,720 acres.

These lands are referred to as trust lands. Each section of trust land is assigned to one of ten trusts. These trusts are permanent funds. Proceeds from rental, leases, the sale or permanent disposition of any trust lands, and all other actual income represent earnings to these trusts. Trust earnings are used for the support and maintenance of the public schools and institutions for which the lands were granted.

## Board of Land Commissioners Responsible for Trust Land

Montana's Constitution gives direct management authority for trust lands to the Board of Land Commissioners (Land Board). The Land Board consists of five elected Montana officials: the Governor, Superintendent of Public Instruction, State Auditor, Secretary of State, and Attorney General. Section 77-1-202(1), MCA, mandates the Land Board to administer trust lands and funds held in trust "to

## Chapter II - Land Exchanges Background

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secure the largest measure of legitimate and reasonable advantage to the state.” The Land Board has the authority to direct, control, lease, exchange, and sell trust lands.

### Department of Natural Resources and Conservation Manages Trust Land

DNRC is responsible for managing trust lands. Trust lands include a cross-section of all types of land including grazing, agriculture, forest, recreational, and commercial. The department’s mission is “to help ensure Montana’s land and water resources provide benefits for present and future generations.” To accomplish its mission, DNRC manages Montana’s trust land resources to produce revenues for the trust beneficiaries. The following table shows revenue generated from trust lands for fiscal year 2000.

**Table 1**  
**Revenue Generated by Trust Lands**  
**(FY 2000)**

<b>Activity</b>	<b>Total Revenue</b>
Grazing Leases	\$4,494,637
Agricultural Leases	\$9,331,416
Timber Sales	\$10,591,657
Mineral Rentals/Royalties	\$11,643,027
Special Use Management <sup>1</sup>	\$2,349,069
Trust Legacy Interest and Other Income	\$26,468,315
<b>TOTAL</b>	<b>\$64,878,121</b>

<sup>1</sup> Includes rights-of-way, cabin/homesite leases, land sales, special use leases/licenses, and recreational use licenses.

**Source: Compiled by the Legislative Audit Division from department records.**

## Chapter II - Land Exchanges Background

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Of the total revenue generated, over \$49 million in earnings and interest were distributed directly to Montana schools in fiscal year 2000. The remaining money was deposited in the appropriate trust fund.

Of the seven divisions within DNRC, it is the Trust Land Management Division's purpose to administer and manage timber, surface, and mineral resources for the benefit of public schools and the other endowed institutions in Montana. The Special Use Management Bureau within this division is directly responsible for conducting real estate functions, which include the disposal and acquisition of trust land through land exchanges.

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### **Fee (Non-Trust) Land**

In addition to trust lands, the State of Montana also holds fee title to lands (i.e., owns land). These lands are usually managed by the state agency holding title to the land. Some of the agencies holding title to non-trust lands include the Montana Department of Transportation (MDT), the Department of Fish, Wildlife and Parks (FWP), and the Montana University System (MUS). In addition, DNRC administers fee land for other state agencies including the Department of Labor and Industry and the Department of Public Health and Human Services. Revenue generated from non-trust land is transferred directly to the state agency holding title to the land.

### **Montana Department of Transportation Land**

Statutorily (section 60-4-102, MCA), MDT has general authority to acquire an interest in property it considers reasonably necessary for present or future highway purposes. MDT land can also include a cross-section of all types of land, but the land is usually used for highway or maintenance purposes. Section 60-4-202, MCA, provides MDT with authority to exchange its interest in real property needed for highway purposes.

The Right-of-Way Bureau within the Engineering Division of MDT provides real estate management services for all property owned or controlled by the department. When it is determined that land is no longer necessary for present or future highway purposes, it is classified as excess land and can be sold or exchanged.

## **Chapter II - Land Exchanges Background**

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### **Department of Fish, Wildlife and Parks Land**

Section 87-1-209, MCA, provides the department with authority to acquire, dispose of, and exchange lands or waters for various purposes. FWP fee lands are usually part of a state park, a fishing access site, or a wildlife management area. Statute (section 23-1-102, MCA) also gives FWP authority to acquire for the state, land that should be held and maintained as state parks, state recreational areas, state monuments, or state historical sites.

The Land Section within the Field Services Division is responsible for acquiring, selling and exchanging land for the department.

### **Montana University System Land**

The Montana Constitution (Article X, Section 9) provides the Board of Regents (the Regents) with the power, responsibility and authority to manage and control the Montana University System. Included in its authority is the management of university lands. University lands are non-trust lands acquired by the university through gift, purchase, grant, exchange, or other methods. These lands include various types of land which are usually used for educational purposes. Legal counsel for the Regents is responsible for oversight of university real estate transactions including land exchanges.

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### **State Land May be Exchanged**

The Enabling Act and the Montana Constitution specify “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 Constitution also specifies “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.”

According to the Montana Constitution (Article X, Section 11), all lands granted by Congress (trust lands) or acquired by gift, grant, or other devise from any other source (fee lands), shall be public (state) lands. Section 77-1-101(6), MCA, defines state lands as:

## Chapter II - Land Exchanges Background

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1. Lands granted to the state by the United States for any purpose, either directly or through exchange for other lands (trust lands).
2. Lands deeded or devised to the state from any person (fee lands).
3. Lands that are the property of the state through the operation of law (fee lands).

Statute further clarifies state land does not include:

1. Lands the state conveys through the issuance of patent.
2. Lands used for building sites, campus grounds, or experimental purposes by a state institution and are the property of that institution.
3. Land the Board of Regents has authority to dispose of pursuant to section 20-25-307, MCA (land held or administered by the Regents or MUS and held by the state for the use and benefit of the Regents or MUS).
4. Lands acquired through investments under the provisions of section 17-6-201, MCA (Unified Investment Program administered by the Board of Investments).

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### How Does a Land Exchange Work?

In its simplest form, a land exchange is an agreement between two landowners to swap ownership of two separate pieces of property. Landowner #1 trades property A for property B owned by Landowner #2. The deed to property A is transferred to Landowner #2 and the deed to property B is transferred to Landowner #1. The exchange is complete.

While this simplified scenario can occur, there are generally many more steps and/or possibilities involved in state agency land exchanges. There may be more than two landowners involved in an exchange, or there may be more than two pieces of property to exchange. For example, the FWP Alberton Gorge exchange involves three landowners, a conservation group, and eight tracts of land.

In addition, the specific land involved in an exchange may not be identified up front. A pool of land may be proposed for exchange, but the actual acreage may not be identified until later in the process. These factors increase the complexity and amount of time involved in an exchange.

## Chapter II - Land Exchanges Background

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### How Many Exchanges have Occurred?

We reviewed land exchanges for the period March 1994 through March 2001. We also reviewed some exchanges which were “in the process” during this time frame. The following table provides a breakdown of land exchanges for the four agencies in our review.

**Table 2**  
**Number of Land Exchanges**  
**(March 1994 through March 2001)**

Agency	Number of Land Exchanges	
	Approved	In Process
DNRC	7	17
MDT	19	12
FWP	17	6
MUS	2	1

**Source: Compiled by the Legislative Audit Division  
from agency records.**

In addition to the projects noted above, DNRC denied 14 other exchange proposals. Of the exchanges noted in Table 2, nine were between agencies, so there are some duplicate counts.

DNRC, FWP, and MDT also have several exchanges in process with the Bureau of Land Management and/or the United States Forest Service.

The following chapters describe specific details of the exchange processes used by the four agencies in our review and provide our findings and recommendations.

# Chapter III - Land Exchange Processes

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## **Introduction**

We reviewed land exchange processes for four agencies: 1) the Department of Natural Resources and Conservation (DNRC), 2) the Montana Department of Transportation (MDT), 3) the Department of Fish, Wildlife and Parks (FWP), and 4) the Montana University System. DNRC operations were the focal point of our audit, so much of the report discusses those activities. However, other agency operations are included and discussed as well. Our review concentrated on procedures used to complete land exchanges and track the timeliness of the process. This chapter discusses the processes followed by the four agencies reviewed and how those processes compare to other state and federal government processes.

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## **What Specific Land Exchange Procedures are Used by Agencies?**

The following sections discuss land exchange criteria and specific exchange procedures followed by the four agencies in our review.

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## **Department of Natural Resources and Conservation Exchanges**

The Board of Land Commissioners (Land Board) developed policy in 1994 to help guide the DNRC exchange process. According to policy, a “rule of thumb” for the Land Board is to approve exchanges that assure the trade is a “good deal” for the state. Criteria were developed to assist in evaluating how the Land Board will review the merits of a particular exchange to ensure it is a “good deal.” The criteria are:

1. Equal or greater land value.
2. Similar navigable lakes and streams.
3. Equal or greater income to the trusts.
4. Equal or greater acreage.
5. Consolidation of state trust lands.
6. Potential for long-term appreciation.
7. Equal or greater access to state or public lands.

DNRC and the Land Board are unable to waive fulfillment of the first three criteria based on legal requirements. The Land Board recognizes that some exchanges may be in the state’s best interest, but may fail to satisfy all seven criteria. In exceptional circumstances, where the presence of public benefits outweighs the

## Chapter III - Land Exchange Processes

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absence of one of the remaining four exchange criteria, the Land Board may waive satisfaction of the criterion.

### **The Exchange Process**

In general, the DNRC land exchange process is divided into three phases. Phase 1 consists of reviewing the exchange proposal, obtaining public comment, and presenting findings to the Land Board. Phase 2 involves a more detailed analysis of the exchange proposal including land appraisals, environmental and cultural review, additional public comment, and a report to the Land Board. Phase 3 finalizes the exchange with transfer of deeds. Each phase is discussed further in the following sections.

### **Phase 1: Preliminary Review**

Phase 1 always begins with solicitation of an exchange from a party outside DNRC. The proposer must complete an application and pay a \$100 non-refundable fee. An exchange proposal may not be considered unless the applicant covers the costs associated with the exchange. Applicant costs may include an environmental assessment, cultural inventory, public hearings, and appraisals. The department may elect on a case-by-case basis to assume or share expenses of any exchange.

Upon receipt of an application, DNRC field staff conduct a preliminary investigation of the proposed exchange including:

- ▶ Review of water and mineral rights.
- ▶ Research of records regarding legal descriptions, easements, and other land encumbrances.
- ▶ Evaluation of the revenue-generating capacity of all lands proposed for exchange.
- ▶ Comparison of proposal with the seven Land Board criteria.
- ▶ On-site reviews of all lands proposed for exchange.
- ▶ Completion of a report discussing findings.

The report of findings from the preliminary investigation is presented to department management for approval/denial. If department personnel determine the proposal will not benefit the state, further review of the proposal is declined. If department management determines the proposal has merit, field staff then solicit public comment. This step is referred to as public scoping. The department

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solicits public comment through mailings to interested parties, newspaper advertisements and/or public hearings. Additionally, prior to scoping and in compliance with law, the department provides notice of the proposed exchange to any person who leases or holds a license for any portion of trust land involved in the exchange.

Following the preliminary investigation and public scoping, department personnel create and forward a report on the proposed exchange to the Land Board for review. The preliminary report to the Land Board includes:

- ▶ A summary of how the exchange meets or exceeds the seven exchange criteria.
- ▶ A summary of public comments received.
- ▶ Maps, photographs, and other supporting documentation.
- ▶ Staff concerns or opinions on the merits of the proposed exchange.
- ▶ An indication of the applicant's commitment to fund the costs of the department's review or the department's commitment to assume or share costs.
- ▶ The department director's recommendation for approval/denial.

Upon receipt of the preliminary report, the Land Board considers the department's recommendations and public comments, and evaluates the merits of the land exchange. The Land Board determines whether further review and public hearings are justified. If further work is not justified, the process is stopped. Alternatively, the Land Board may direct the department to complete specific tasks, such as obtaining more detailed information on land values, and report back to the Board with findings before proceeding further with the exchange process. The exchange process continues with Land Board approval of the preliminary report.

### **Phase 2: Formal Land Exchange**

Phase 2 involves a detailed analysis of the lands proposed for exchange. Formal land and mineral title investigations are completed to determine ownership and encumbrances. Baseline inventories are taken of lands to be exchanged to determine types of soils and vegetation, range condition and carrying capacities, availability of water, and existence of wildlife. A final water rights

## **Chapter III - Land Exchange Processes**

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investigation and mineral resource assessment are conducted. As required by the Montana Antiquities Act (Title 22, chapter 3, part 4, MCA), a cultural resources inventory is completed to identify heritage properties and/or paleontological remains.

Appraisals are completed to determine market value of all lands involved in the proposed exchange. On-site visits must be made to all properties. Appraisals may be completed by DNRC personnel or may be contracted to a third party. Individuals involved in the exchange review each appraisal. Updates to the appraisal are completed based on reviews by department personnel, and DNRC personnel accept or reject the opinions of the appraiser.

This phase also includes preparation of an environmental document in accordance with Montana Environmental Protection Act (MEPA) requirements. The MEPA document may be completed by state or contracted personnel. A draft document is created and reviewed by individuals involved with the process. Internal comments are incorporated as needed, then a draft version is released for public comment. A public hearing is held in each county where land proposed for exchange is located. Public comments are incorporated into the draft, and a final document is released for public comment. After a 15-day statutorily mandated waiting period, the department issues a record of decision on the MEPA document.

Finally, staff presents a report and a recommendation for approval or denial to the Land Board for its review. The Land Board may require additional information prior to rendering a decision. As with Phase 1, if the Land Board does not believe the exchange would be good for the state, the proposal is denied.

### **Phase 3: Closing**

The third phase begins with final approval of the exchange by the Land Board. Formal closing procedures are initiated, similar to most

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real estate closings. This includes drafting deeds and other documents necessary to properly record ownership and encumbrances in the county where the lands are located. Department legal staff review draft documents. The Governor and the Secretary of State sign the final documents.

Included in this phase is settlement for any leaseholder improvements on the trust land being exchanged. Improvements may include fences, buildings, irrigation systems, fertilizer, and other items that add value to the property. Once lessee settlements are concluded, deeds are recorded. The process ends when deeds are recorded, transferring the property to the new owners.

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### Montana Department of Transportation Exchanges

Right-of-way is needed to expand and maintain Montana's transportation system. Department personnel are continually acquiring and disposing of land in order to accomplish MDT's mission. When land is no longer needed for transportation purposes, the department declares the property to be excess. Excess land owned by MDT may be sold or exchanged for other land or right-of-way. In addition, the department may acquire land through purchase or exchange, then exchange the newly acquired land for other needed land or right-of-way.

A land exchange may be initiated by department staff or individuals or agencies external to MDT. For department-initiated exchanges, field personnel contact the owner of the property the department is interested in acquiring to determine if the landowner is interested in an exchange. The process is similar to exchanges initiated by an external source; however, field personnel would then review the land proposed for exchange to determine if it is needed for present or future highway purposes.

If excess land is chosen for an exchange, MDT first ensures it has clear title to the property. If the title is clear for an exchange, department staff completes a legal description or exhibit of the tract. The next step in MDT's process is the appraisal of the properties proposed for exchange. According to MDT policy, land with a

## **Chapter III - Land Exchange Processes**

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preliminary value over \$10,000 requires an appraisal. Appraisals are completed by MDT staff or are contracted to private appraisers. MDT personnel review the appraisals and accept or reject the estimated value.

Once appraisals are accepted, MDT can complete the exchange. State law does not require public notice for MDT land exchanges. The final step in the process is conveyance of title to the properties. Deeds are approved by legal staff, signed by the Governor and Secretary of State, and recorded in the appropriate county.

### **MDT has Specific Agreement with DNRC**

MDT and DNRC entered into a Memorandum of Understanding (MOU) in January 1997. The MOU was designed to establish the obligations of both agencies in the acquisition and conveyance of right-of-ways for highway projects that involve lands under the jurisdiction of DNRC. The agencies completed an addendum to the MOU in December 1999 to address specific steps and requirements of land exchanges. This addendum was created to provide a working mechanism for MDT and DNRC to legally and equitably agree to exchange land for the mutual benefit of the agencies and the State of Montana. Specific requirements include addressing mineral interests and water rights on a case-by-case basis, requiring appraisals and review and approval of the appraisals by the respective parties, and creation and maintenance of an exchange ledger to track value differences.

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### **Department of Fish, Wildlife and Parks Exchanges**

FWP uses a general acquisition process approved by the Fish, Wildlife and Parks Commission (the Commission) when it acquires or exchanges land. A proposed land exchange usually begins at the regional office in which the land is located. Basic information on the lands proposed for exchange is collected, such as legal descriptions, type of land, and potential use/need by FWP. Staff then develop a preliminary proposal.

The proposal is presented to the Commission for its decision on whether to pursue the project. If the Commission gives preliminary approval, the exchange process begins. An environmental document

## Chapter III - Land Exchange Processes

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is completed to comply with MEPA. FWP personnel may complete this environmental review or it may be contracted to the private sector. A private contractor then appraises the exchange lands. FWP does not have appraisers on staff. Department staff review the appraisals and values are accepted or rejected. If values are rejected, FWP personnel may work with the appraiser to come to an agreement on the appraised value. Public meetings and a public comment period on the environmental analysis and appraised values are completed. If the exchange involves federal funding (cash, prior funding of the land being exchanged, etc.), additional requirements and approval from the appropriate federal agency are also required to complete the exchange.

Information obtained during the process is then presented to the Commission for its final decision. If the Commission approves the exchange, the process continues to the closing phase. If the project involves more than 100 acres or has a value of more than \$100,000, FWP is required by statute to present the exchange to the Land Board for its approval. If approved by the Commission and the Land Board, formal closing procedures are initiated to complete the exchange. Closing procedures for FWP are similar to those for DNRC and MDT.

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### Montana University System Exchanges

Legal counsel for the Commissioner of Higher Education is responsible for university system land exchanges. An exchange process was developed, through the Board of Regents (the Regents), which reflects statutory requirements. The process includes an appraisal by a private contractor to determine fair market value, public notification, environmental analysis, and compliance with antiquities laws.

Each exchange proposal is brought to the Regents for approval. Prior to 1995, the Regents disposed of university lands without involvement by the Land Board. Due to a lawsuit and passage of new legislation, the Regents now must obtain written concurrence from the Land Board prior to completing land exchanges. When an

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exchange is approved, formal closing procedures are initiated. As with other agencies, the process ends with the recording of deeds.

### **Interaction between the Land Board and the Regents**

In 1980, the Regents began disposing of select university lands through land exchanges and sales. Between 1980 and 1994, eight land exchanges and 23 sales were initiated by the Regents. Forty-two parcels of public land (comprising over 2,200 acres with a market value prior to disposition of approximately \$4.5 million) were transferred out of state-ownership, 19 through exchanges and 23 through sales. During this time, the Land Board did not assert authority over the disposition of university property.

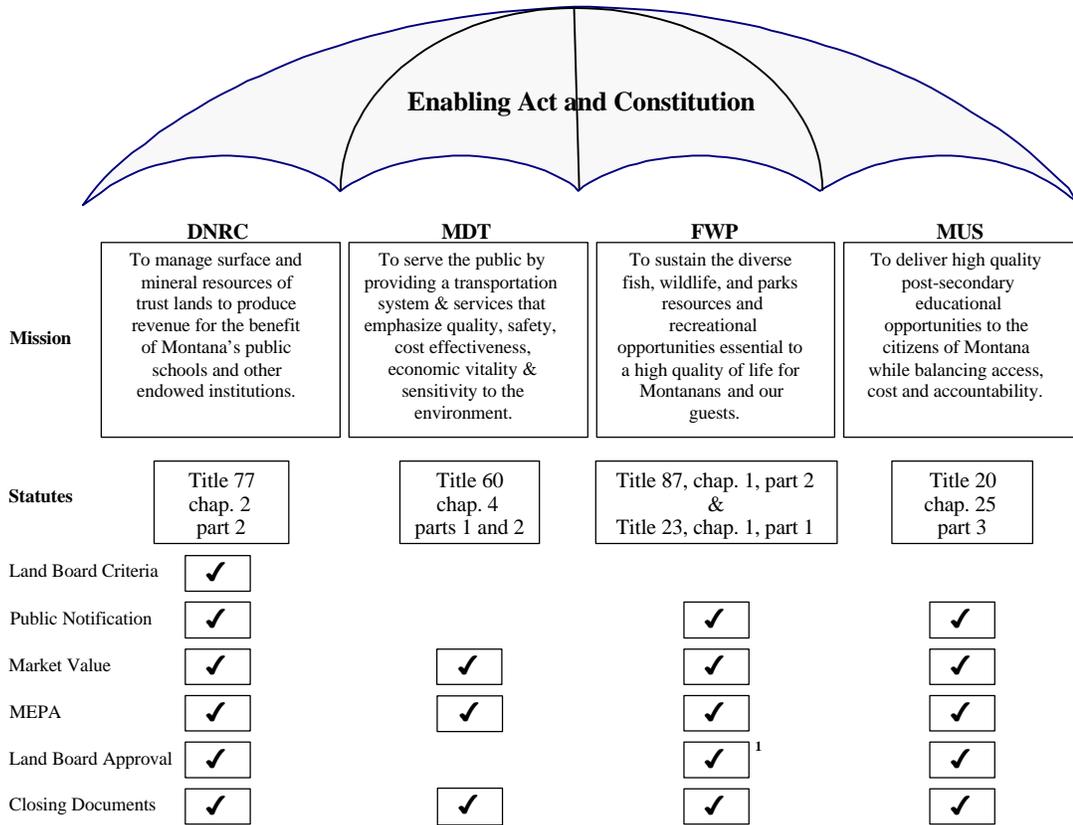
In an attempt to resolve the authority issue, the Land Board proposed legislation outlining the distinction between state trust lands and university lands. The 1995 Legislature passed a law (section 20-25-307, MCA) allowing for the disposition of land by the Regents. The law requires the Land Board to concur with all sales or exchanges of university land

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### **How do Land Exchange Processes Compare to One Another?**

Land exchange processes are generally similar among the four agencies. The public is usually involved in land exchange proposals, land no longer useful to the agency is exchanged, and appraisals are used to determine land value. Variations in processes exist due to the types of land exchanged (grazing versus timber), the purposes for exchanging land, and specific mandates and procedures used to complete an exchange. This can be seen in the following figure.

**Figure 1**  
**Land Exchange Processes for the Agencies in our Review**



<sup>1</sup> Only if project is > 100 acres or > \$100,000

**Source: Compiled by the Legislative Audit Division.**

The Constitution provides common requirements for all agencies regarding land exchanges: equal value and as closely as possible, equal area. As can be seen in the previous figure, there are few similarities between the mission statements of the four agencies. As such, the lands managed by these agencies also vary. The biggest of these variations appears to be use and area or acreage. For example, DNRC has entire sections of land totaling 640 acres used for

## Chapter III - Land Exchange Processes

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agriculture and/or grazing, whereas MDT owns property that is measured in square feet. Land exchanges can occur between agencies because while one agency may no longer need the property, another agency may be able to use it due to distinct differences in agency missions.

Figure 1 also illustrates variations in statutory mandates, which create some differences. DNRC exchanges are subject to the seven Land Board criteria. MDT does not have public notification requirements, nor does MDT have to obtain approval from the Land Board. The remaining steps are similar among the agency processes.

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### How does Montana Compare to Other States and the Federal Government?

We obtained information on other state and federal land exchange procedures to compare to Montana's. Our review of other states was limited to trust land management in the following states:

- ▶ Washington
- ▶ Colorado
- ▶ Wyoming
- ▶ Utah
- ▶ Idaho

All these states allow exchanges of state trust land. These states all have a board that grants final approval of exchanges. Land value is usually determined by appraisals. Land exchanges are a priority in Colorado, Utah, and Idaho, and consolidation of lands is a priority in Washington and Idaho.

We also briefly reviewed procedures used by the Bureau of Land Management (BLM) and the United States Forest Service (USFS). These agencies have authority to exchange land. Land values must be equal, or approximately equal, and are determined through appraisals. Environmental reviews are completed. A recent General Accounting Office (GAO) report on BLM and USFS land exchanges noted several concerns with these agencies not following procedures. In its report, the GAO indicated that these federal agencies did not ensure land being exchanged was appropriately valued or that

## Chapter III - Land Exchange Processes

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exchanges served the public interest. We did not identify these concerns during our review of Montana's land exchanges.

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***Conclusion: State Agency  
Land Exchange Processes are  
Comparable***

State agency land exchange processes are comparable to one another and to other states and the federal government. There are differences in specific procedures, but in general, the processes are comparable.



# Chapter IV - Managing State Lands

## Introduction

Audit scope for this project was limited to state agency land exchanges. Land exchanges are only one “tool in the toolbox” of land management. This chapter discusses aspects of land management and how land exchanges are used to manage state lands.

## State Land Exchange Processes Provide Benefits

State agency land exchange processes appeared to provide benefits to the state and the public by meeting the missions of the agencies involved. The Department of Natural Resources and Conservation (DNRC) generates income for trusts and consolidates holdings. The following table shows income for the six completed DNRC land exchanges we reviewed.

**Table 3**  
**DNRC Average Annual Income Comparison**  
**(unaudited)**

Exchange	----- INCOME -----	
	Prior to Exchange	Current (as of June 2001)
Starr	\$1,695	\$6,095
AA Ranch	\$75	\$2,775
Turner	\$13,288	\$84,166
Mead	\$130	\$0 <sup>1</sup>
Ulm/Makoshika	\$1,578	\$0 <sup>2</sup>
Crow Boundary Settlement Act	\$50,115	\$27,919 <sup>1</sup>
<b>Totals</b>	<b>\$66,881</b>	<b>\$120,955</b>

<sup>1</sup> Commercial development or timber sales planned

<sup>2</sup> Finalized late June 2001

**Source: Compiled by the Legislative Audit Division from department records.**

The Department of Fish, Wildlife and Parks (FWP) obtains and/or protects land for wildlife management areas, parks, and fishing access sites. The Montana Department of Transportation obtains needed right-of-way and disposes of excess land. The Montana University System adjusts boundaries and consolidates holdings to improve overall land management. The following sections present a

## **Chapter IV - Managing State Lands**

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summary of our findings and recommendations for improving land exchange processes.

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### **What is Land Management?**

Land managers direct and control what happens to land. At one end of the spectrum is total nonuse of land where nothing is done to or with the land. At the other end of the spectrum would be multiple use and total care of the land. The owner of the land is responsible for management. However, some of the rights and responsibilities for management may be sold or transferred to another entity. When DNRC leases trust land for grazing or agricultural use, the state retains ownership of the land but the lessee is responsible for things like maintaining fences and roads and controlling weeds.

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### **How do Agencies use Exchanges to Manage State Lands?**

There are numerous statutes and regulations which control state land management. The four agencies in our review were in compliance with related land exchange requirements. Several concepts used to manage state lands deserve discussion. These include:

1. Running accounts
2. Escrow accounts
3. Cash equalization payments
4. Land banking
5. Consolidating land holdings
6. Developing land for commercial use
7. Selling isolated tracts of land

The following sections describe these methodologies and concepts.

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### **DNRC Uses Running Accounts to Equalize Values**

We noted that DNRC uses “running accounts” for some of its exchanges with other state and federal entities. Running accounts are used when an exchange results in unequal land values. The difference in value is tracked and future exchanges are used to equalize values. For example, the department entered into a memorandum of understanding (MOU) with the Montana Department of Transportation (MDT) in December 1999. The MOU was established because of the Mead exchange between the two agencies resulted in a \$300,000-plus excess land value to the favor of DNRC. The purpose of the MOU is to equalize this excess value with subsequent land exchanges and/or highway right-of-way

easements. The next activity using the terms of the MOU is the Perma – Pictograph land exchange, which was being developed during our audit. Preliminary estimates indicate DNRC will receive approximately \$200,000 less in land value than it exchanges away. If the second exchange is approved and values equal preliminary estimates, the running account balance will be approximately \$100,000 in favor of DNRC.

A similar running account was used in the Crow Boundary Settlement Act. This exchange was between the DNRC and the BLM, and exchanged DNRC lands within the boundary of the Crow Reservation for BLM lands located off the reservation. There were three phases for this exchange, and the second phase resulted in DNRC receiving less value in the exchange. However, the first phase had a positive balance, so the overall exchange had DNRC receiving greater value. It should be noted that DNRC and BLM personnel tried to equalize land values prior to finalizing each phase of the exchange in order to avoid large excess land values.

We questioned the department about its authority for use of running accounts. According to DNRC personnel, authority lies within the general Constitutional authority of the Board of Land Commissioners (Land Board). Basically, the Land Board has authority to manage trust lands. In *Thompson vs. Babcock* (409 P2d 808(1966)), the court said that not every facet of the Land Board is set out in statute. In order to equalize the excess land value from an exchange, DNRC must receive less value than it exchanges away. Based on requirements for equal or greater value, this would be noncompliance. However, DNRC uses positive excess value as part of subsequent exchanges, so the overall balance is still positive and there is no noncompliance. In addition, from MDT's point of view, without the MOU the first exchange would have been a violation of the equal or greater value mandate.

***Conclusion: Running  
Accounts Help Agencies  
Complete Land Exchanges***

Running accounts help DNRC and other agencies complete land exchanges while meeting mandates. Montana's Constitution requires equal or greater value in land exchanges. However, the

## Chapter IV - Managing State Lands

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Constitution also allows for disposal of land according to statute. Laws relating to MDT land exchanges allow for disposal of land at less than market value. As a result, equal or greater value is not always required. Running accounts provide a mechanism for accomplishing legal and equitable land exchanges between government agencies.

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### **FWP Uses Escrow Accounts to Complete Exchanges**

Of the FWP files we reviewed, two used “escrow accounts” to complete the land exchange: 1) Bridger Mountain, and 2) Bozeman Ponds. In the Bridger Mountain exchange, FWP land adjacent to Bridger Bowl Ski Area was determined to be surplus. Bridger Bowl did not have land to exchange, but because it is a public recreation area, FWP decided to find suitable land to exchange for its surplus land. An escrow agreement was signed, and an escrow account was established to hold the money from Bridger Bowl and title to FWP’s surplus land pending completion of the exchange. FWP personnel identified two suitable exchange properties, which were purchased with money in the escrow account. Use of this methodology allowed for nonsimultaneous transactions, which are sometimes referred to as “deferred” exchanges.

The Bozeman Ponds exchange also used an escrow account. One of the exchange properties was involved in an ongoing subdivision review. An escrow account was established to hold money and titles until the subdivision was approved. In addition, a cash payment was made by the private party to equalize exchange values.

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### **Acreage Exchanged is Not Always Equal**

The Constitution provides authority to exchange land that is equal in value and, *as closely as possible, equal in area*. We found the four agencies do not always receive equal acreage in land exchanges. For example, in the Mead exchange, DNRC received fewer acres (~29) than it exchanged away (~106). Equal or greater acreage is one of the seven criteria that do not have to be met. The department believed the exchange should be predicated on land values rather than acreage. As another example, FWP exchanged approximately 67 acres for approximately 49 acres in the Happy’s Inn exchange with MDT. In the Zurich exchange, MDT exchanged about 20 acres

for about ½ acre. The Montana University System (MUS) exchanged approximately 54,000 square feet for about 12,400 square feet.

The Constitution contains language that provides latitude regarding equal acreage, so an exchange with acreage differences is allowable. As a result, the examples above, as well as other exchanges with acreage differences, appear to be permissible. The Constitution also requires equal or greater value. Requiring properties that are equal in value and acreage is realistically impractical because rarely if ever will values **and** acres be equal. Based on interviews with agency personnel and review of files, it appears to be difficult enough to obtain equal value in an exchange of two separate properties. The Land Board, in its exchange policy, interprets this constitutional language to allow consideration of exchanges that would not result in the exchange of virtually identical acreage. However, the policy further states that as a general rule, the Land Board prefers to receive equal or greater acreage and will only waive satisfaction of the criterion in exceptional circumstances.

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### **DNRC Did Not Always Meet the Seven Land Board Criteria**

For the projects we reviewed at DNRC, we noted one instance where one of the Land Board criteria was not met: equal or greater income to the trust. In the Ulm/Makoshika exchange, immediate income of newly acquired lands will be less per year due to trading croplands, which generate higher income, for grazing lands. Potential income opportunities from mineral development or other uses of lands acquired outside these parks was mentioned in the department's decision notice. However, this project did not meet the criteria of equal or greater income to the trust at the time the land exchange was completed.

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### ***Conclusion: The Constitution and Statutes Provide Broad Authority for Completing Land Exchanges***

The Constitution, laws, and policy provide some flexibility in land exchanges. In general, agencies complied with land exchange requirements for those projects reviewed. Agencies use the broad authority of the Constitution and statutes to complete land exchanges. Processes include running accounts and escrow accounts, and decisions are made regarding differences in acreage

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and compliance with criteria. The land exchanges completed under these procedures were reviewed by the public, in most instances approved by a governing board, and appear to have benefited the state and the public.

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### Cash Equalization Payments May Assist DNRC Exchanges

One procedure not yet discussed is the use of cash equalization payments. Both FWP and MDT use cash payments to equalize the land values in an exchange. For example, in the Gallatin Wildlife Management Area exchange, FWP paid the Rocky Mountain Elk Foundation \$17,300 to equalize the difference between land values. In the 1995 Thompson Chain of Lakes exchange, FWP received a cash payment from MDT to equalize the exchange. As another example, MDT received \$65,150 from the Confederated Salish and Kootenai Tribes to equalize values in the Copper Creek exchange. DNRC does not use cash equalization payments for land exchanges. The two Montana University System exchanges did not require cash equalization payments. The Bureau of Land Management (BLM) and United States Forest Service (USFS) also use cash equalization payments to balance out land exchanges, as do all five other states we contacted.

According to DNRC personnel, cash equalization payments cannot be accepted in a land exchange because it would then be considered a direct sale. By statute, direct sales of trust land are not allowed. Trust land sales are to be by public auction, and proceeds from sales are to be deposited to the permanent trust.

Equalizing values in a land exchange can be difficult and time consuming. If land values are unequal, an exchange will probably not occur. There could be a loss of benefit to the state as a result. FWP and MDT use cash payments to help equalize values and achieve goals through land exchanges. While FWP and MDT lands are not school trust lands, these agencies are held to the same constitutional mandate regarding land exchanges: disposal of public land, in an exchange, must be for equal value. By statute (section 30-11-112, MCA), an exchange is an agreement to exchange “one thing for another, neither thing nor both things being money only.”

Based on this definition, cash equalization payments appear to be allowable for trust land exchanges. Cash equalization payments could provide the department with more flexibility to complete land exchanges.

**Recommendation #1**

**We recommend DNRC use cash equalization payments as an option in trust land exchanges.**

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**Land Exchange is Only One Aspect of Land Management**

Exchanging land for other land is only one aspect of land management. For example, the purpose of the Trust Land Management Division within DNRC is to administer and manage trust resources for the benefit of public schools and other endowed institutions. The division is divided into four primary programs: 1) agriculture and grazing management, 2) forest management, 3) minerals management, and 4) special use management. Management activities of these various programs include agricultural leases, grazing leases, assessment of land condition, oversight of water developments, timber harvest, reforestation, mineral leasing, cabinsite and homesite leasing, right-of-way and easements, special use leases, and land exchanges.

There are a number of methods available which could make land management easier and potentially more profitable to the trust. These concepts are discussed in the following sections.

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**Land Banking**

Land banking is a sale and replacement land management concept. Land is sold, but revenues generated from the sale are placed in an account with the intent of purchasing other land to replace the land sold. There is usually a limit placed on the amount of time available to acquire replacement property. If replacement property is not acquired within the time frame, the transaction is considered a sale and the revenue is managed according to statute and other regulations. This concept has numerous names including deferred land exchanges, nonsimultaneous land exchanges, assembled land exchanges, and land replacement.

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The former Department of State Lands contracted with Bioeconomics, Inc., in 1993 to review numerous aspects of trust land management and survey operations in other states. This contracted study is known as the Duffield Study. The Duffield Study recommended the legislature authorize establishment of a land banking system for trust lands. The authors recommended selling less profitable lands and using revenues to purchase new lands that will generate significantly greater long-term income for the trusts. In addition, four of the five states we contacted (Washington, Colorado, Wyoming, and Idaho) use some form of land banking as part of land management.

In January 1997, the State Auditor brought the idea of a deferred exchange pilot program to the Land Board. The Land Board approved a pilot project on April 21, 1997, but the department has not pursued development of a program to date. In September 2001, the Land Board revisited the idea of a deferred land exchange program. No action was taken by the Land Board at the September meeting.

According to DNRC management, land banking has not been pursued due to advice from department legal counsel. The Enabling Act restricts land sales to public auction and sale proceeds must be deposited in the permanent trust. Department managers said the perception of land banking being a sales process has prevented pursuit of a program. However, a program structured to be consistent with procedures and statutes for land exchanges could help achieve goals related to the Land Board's seven exchange criteria.

### ***Conclusion: Land Banking Could Help DNRC Land Management***

The land banking concept is basically a modification of land exchanges. Use of land banking for trust lands has been recommended and the previous Land Board approved a deferred exchange pilot program. In addition, entities external to Montana state government are using land banking as a land management tool. Land banking has potential for improving trust land administration.

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We believe DNRC should determine what actions are necessary to implement a land banking program for trust lands.

**Recommendation #2**

**We recommend DNRC establish procedures to implement land banking concepts as part of trust land management.**

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### Consolidating Land

Section 77-2-203(2), MCA, mandates the Land Board to place priority on exchanges resulting in consolidation of trust lands into more compact bodies. According to Land Board policy, consolidation of trust lands facilitates land administration and aggregated land often has greater value and revenue potential. One reason for this possibility of improved revenue is due to increased competitive bidding. A larger, consolidated tract of land is more appealing for grazing, agriculture, or other uses. Thus, more individuals may want to acquire use of the property, which increases competitive bidding for leases. While consolidation is one of the seven criteria within the Land Board policy, it can be waived.

Consolidation of land holdings was a recommendation in the Duffield Study. In the study, the authors reported the objective of most land exchanges between state and federal agencies was consolidation. The study's survey of western states noted consolidation helps achieve better land management, lower administrative costs, and greater revenue generation.

A performance audit of state-owned land (#82P-17), completed by the Office of the Legislative Auditor in 1982, reviewed management of small parcels of trust land. This review indicated that many of the state's small isolated parcels are unproductive. Auditors recommended DNRC establish a program to remove unproductive land parcels and consolidate state lands into more manageable tracts. According to this audit report, the benefits would be:

1. Reduction of administrative costs.
2. Elimination of parcels with potential access problems.
3. Development of procedures in conjunction with statutes.

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According to a United States General Accounting Office report (GAO/RCED-00-73), the federal government started using exchanges in the early 1980's to dispose of fragmented parcels and to consolidate ownership patterns to promote more efficient management of land and resources. In addition, two of the six states we contacted use consolidation as a priority for land management.

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### Developing Land for Commercial Use

As discussed previously, there are numerous uses for trust land. One management option available to DNRC is development of property. For example, DNRC personnel are currently analyzing the potential for commercial development of a section of school trust land near Kalispell currently classified for agricultural use. This project is known as the Section 36 proposal. The idea behind development of property is to increase the revenue generating capacity of the land. According to section 77-1-601, MCA, "it is in the best interest and to the great advantage of the state of Montana to seek the highest development of state-owned lands in order that they might be placed to their highest and best use and thereby derive greater revenue for the support of the common schools, the university system, and other institutions benefiting therefrom, and that in so doing the economy of the local community as well as the state is benefited as a result of the impact of such development."

DNRC and the Land Board are reviewing options related to development of trust lands. The department is currently obtaining public comments on a programmatic environmental impact statement (EIS) concerning the management of trust lands. The programmatic EIS will provide alternatives and obtain public comment on the direction the department and Land Board should proceed in relation to development of trust lands. According to preliminary documents, trust lands have historically been managed primarily for sustained yield of crops, timber, minerals, and other natural resources. The department, the Land Board, and trust beneficiaries recognize the need and opportunity to generate increased and diversified revenues from alternative management strategies. One of these areas is commercial or industrial development.

DNRC has some specific properties it is currently developing or has plans for development in the future. The Mead land exchange between DNRC, MDT, and a private party resulted in DNRC acquiring two lots on Reserve Street in Missoula. According to DNRC personnel, these lots will probably be leased for commercial development. In September 2001, the department issued a request for proposals to solicit a realtor to market the property for lease. In addition, DNRC was analyzing another potential exchange with MDT that would result in additional commercial development property, if the exchange were approved as preliminarily proposed.

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### **Selling Land**

Land sales are another aspect of land management. There are various reasons for selling land, but the main reason noted in our review was a lack of need for continued ownership of the land. For example, if MDT land is no longer needed for highway purposes, it is considered excess and can be sold or exchanged. MUS may sell land to generate funds. Land sales are used more by the other three agencies in our review than by DNRC. In its annual report for fiscal year 2000, DNRC indicates it sold 14 residential lots and a 0.2-acre parcel. According to DNRC personnel, it was the policy of the past Land Board to not sell trust land. However, the Constitution and statute authorize the sale of trust land under certain limitations. Revenues from trust land sales must be placed in the permanent trust.

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### **Roadblocks to Effective Land Management**

A number of conditions prevent DNRC from managing trust lands as effectively as possible. Some land has limited or no access, resources are limited, and the process takes time to complete. The following sections discuss these topics.

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### **Some DNRC Tracts are Landlocked or have Limited Access**

The granting of sections 16 and 36 in every township created a checkerboard pattern of state land ownership across Montana. Adjacent landowners include state, federal, and/or private landowners. For DNRC trust lands, there are situations where one landowner owns all land surrounding the trust land parcel. This land is referred to as "landlocked." The revenue-generating capability of trust land can be impacted if the parcel is landlocked.

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In a landlocked situation, DNRC may or may not have access to the land. Access to a parcel of land depends on the public road system and adjacent landowners. If a public road crosses and/or borders a tract of land, the owner of the tract would have access to the property. If there are no public access options to a tract, access is controlled by adjacent landowners. An adjacent landowner must grant an access easement for access to be legal. An access easement may have limitations in order to control land use.

Without access, a landowner may not be able to utilize the resources of the land or may only be able to do so at increased expense. For example, timber can only be harvested by helicopter if there is no road access. Unproductive tracts of land hinder DNRC's ability to meet its mandate of administering the trusts to secure the largest measure of legitimate and reasonable advantage to the state.

According to department personnel, DNRC maintains it has authority to access trust lands to monitor lease agreements and land conditions. While DNRC personnel may have access to trust lands, the general public may not. Thus, the adjacent landowner of a landlocked parcel of land has control over land management.

The trust lands database at DNRC tracks revenue by land use. In other words, the database can report on revenue generated by grazing leases or cabinsite leases. The current database cannot provide information on adjacent landowners or lands generating minimal revenue. The department is in the process of hiring a contractor to develop a new tracking system. The new system should provide more information and data related to land management. While the department does not know the exact number of landlocked acres it manages, some department personnel estimate it could be as high as 50 percent.

To facilitate management of isolated parcels, the 1999 Legislature authorized DNRC to negotiate reciprocal access agreements (section 77-1-617(1), MCA). According to its fiscal year 2000 report, the department is actively pursuing acquisition of access to isolated

school trust lands to facilitate management and provide increased revenue to the trusts.

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### **Availability of Resources Can Impact Ability to Conduct Management Operations**

Personnel allocated to land management activities can impact operations. Constitutional and statutory mandates with regard to land administration must be addressed first. Other activities are completed as time allows. DNRC personnel indicated that identifying land for consolidation, sales or exchanges are not mandated activities. As a result, the department does not have a program for identifying and disposing of land that is isolated and only generating minimal income to the trusts. In addition, personnel do not actively pursue land exchanges.

Funding can also impact land management. Land purchases, cash equalization payments, development, etc. all require funding. If funding is not available, these management actions cannot be completed. DNRC did receive a legislative appropriation of \$116,000 for each year of the 2003 biennium for development of trust lands for commercial use.

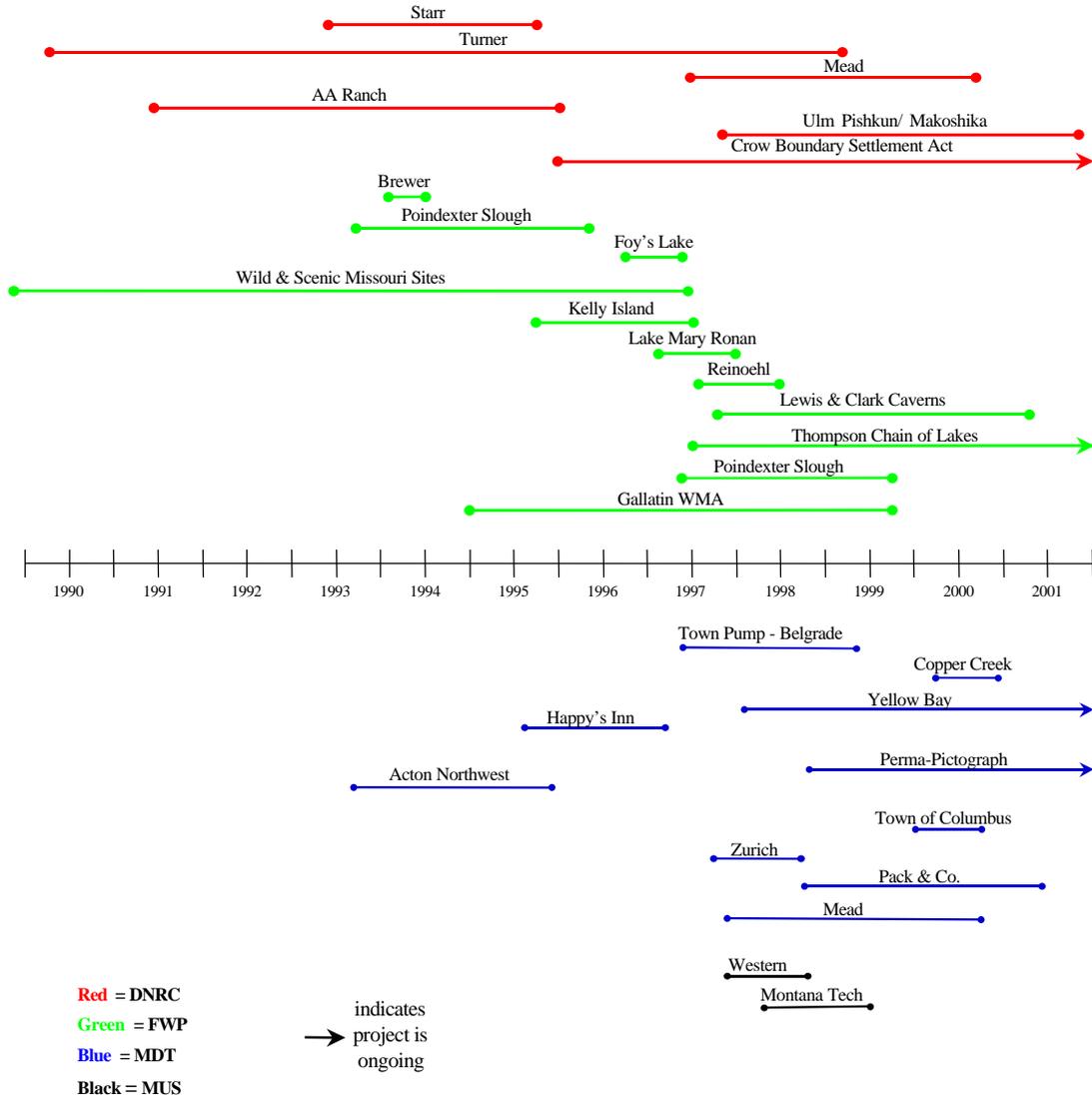
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### **Time Needed to Complete a Land Exchange Can Affect the Process**

The amount of time needed to complete land exchanges varies from agency to agency and project to project. The following chart shows the timelines for all land exchanges we reviewed.

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**Figure 2**  
**Time Frames for Completed Land Exchanges**  
**(March 1994 through March 2001)**



Source: Compiled by the Legislative Audit Division from department records.

The time frames in the table above are based on file documentation. DNRC exchanges take longer than other agencies. One reason for this is land exchanges are not a priority for DNRC. Other duties, which are mandated, such as administration of grazing and agriculture leases, timber sales, and special use licenses, take priority. As a result, the review of a new land exchange proposal may not be addressed for months.

Some specific details of the projects in Figure 2 should be noted. The Turner exchange (DNRC) was in the court system for 2 years and 4 months. FWP's Wild & Scenic Missouri Sites exchange with the BLM had Washington DC involvement due to federal funding of land proposed for exchange. The Mead exchange (MDT) was with DNRC. MUS completed only two exchanges during our audit time period.

In comparison, the time frames for completing land exchanges in the five states we contacted vary from six months to several years. BLM information indicates their exchange process ranges from 12 months to two years, if there are no critical issues.

### **Each Step or Phase in the Process Can Take Time**

The land exchange process is a lengthy process. Each step or phase in the process can cause time delays or lengthen the overall time frame. However, we did not identify a step or phase that consistently held up the process. Steps, which were noted to potentially add time to the process, include the following:

- ▶ Identifying lands to exchange
- ▶ Public notice and public hearings
- ▶ Presentation to a board
- ▶ MEPA analysis
- ▶ Appraisals
- ▶ Closing transactions

### **Time Frames for Completing Land Exchanges Vary**

Each exchange is different and different issues/concerns may arise, so each project can be delayed for different reasons at different phases of the exchange.

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### Can the Process be Shortened?

A United States General Accounting Office report (GAO/RCED-00-73) of BLM and USFS land exchanges indicates exchanges are an inherently difficult way to convey and acquire land. To exchange land, you must have two willing landowners who want to exchange land, have properties valued similarly, and the landowners must agree with the valuation. It further states that exchanges are complicated by difficulties in estimating fair market value. These statements hold true for Montana's exchanges. However, our review indicates that DNRC is the only agency of the four we reviewed that consistently appears to have a lengthy process.

We suggested proposals be taken to the Land Board earlier for preliminary approval. According to DNRC personnel, they go out for public comment (scoping) prior to taking a proposal to the Land Board based on Land Board direction. The Land Board indicated its desire to get public comments up front in order to avoid surprises and public conflict later in the process. Based on this direction and reaction from the department, as well as required time frames for specific steps, there does not appear to be other areas where improvements to the time frame are possible or realistic. However, cash equalization payments and/or land banking may help reduce time frames.

### The Land Exchange Process is Lengthy

The land exchange process seems to be a lengthy process. Of the four agencies in our review, DNRC has the lengthiest process.

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### Summary

Managing land involves a myriad of responsibilities. Numerous activities are conducted to accomplish responsibilities. Our review suggests land exchanges are an effective method of land management. Agencies use various procedures to complete land exchanges. We noted several areas where operations could be improved and made recommendations to agency management.

Land exchanges are only one aspect of land management. There are numerous other activities included within the overall management of land, some of which are required by law, such as timber harvests and grazing leases. For DNRC, these mandates take priority over non-

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mandated activities, such as land exchanges. Other management activities like consolidation to dispose of unproductive land are also not priorities of the department. In a perfect world, DNRC would identify all unproductive land, dispose of it through exchange, or possibly even through land banking, and replace the property with land that is equal or greater in value, equal or greater in acreage, and generates more revenue for the trusts. The replacement property would consolidate state holdings and increase access to public lands.



# Chapter V – Other Land Exchange Requirements

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## Introduction

An objective of our review was to determine compliance with regulations within the Constitution, statutes, administrative rules, and other established criteria. Of specific interest was determining how the value of land is established, whether the state retained equal value, the environmental assessment process, and public involvement. Our findings and recommendations are presented in the following sections.

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## Did the State Retain Equal or Greater Value for All Land Exchanges?

Land is an asset that has value, so when it is disposed of its value needs to be known. As part of our review, we determined how value is established for land proposed for exchange and whether the state retained equal or greater value.

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## What is Required?

The Montana Constitution generally regulates the disposition of land owned by the state. According to Article X, Section 11 of the Constitution, state land is public land held in trust for the benefit of the people of Montana. This section further states that no public land shall be disposed of except in pursuance of general laws or until full market value has been paid. Public land can be exchanged for other land, public or private, but the land must be equal in value.

Over the years, the legislature has enacted several laws relating to land value. Section 77-1-202, MCA, requires the Board of Land Commissioners (Land Board) to determine the value of the land after an appraisal by a qualified land appraiser. Sections 77-2-201 and 203, MCA, authorize land exchanges provided that the land is equal or greater in value. The latter section further requires value to be determined by an appraisal by a qualified land appraiser. In addition, policy approved by the Land Board requires equal or greater value for land exchanges and use of a certified appraiser to determine value. Policy further states the Department of Natural Resources and Conservation (DNRC) should consider intrinsic values in evaluating the value of land. Those mentioned include location, proximity to public lands, recreational opportunities, scenery, and other amenities.

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Statutes related to the Department of Fish, Wildlife and Parks (FWP) (section 87-1-209, MCA) provide the department and the FWP Commission authority to dispose of lands, without regard to other laws, as considered necessary and advisable. This section of law does provide the department authority to reject offers that do not equal or exceed full market value.

Section 60-4-201, MCA, allows the Montana Department of Transportation (MDT) to establish the manner, terms, and conditions for land exchanges. For land sales, which MDT uses as guidance for land exchanges, section 60-4-203, MCA, states land must be appraised within three months prior to the sale and a sale may not be made for less than 90 percent of the appraised value.

Section 20-25-307, MCA, requires the Board of Regents (the Regents) to obtain consideration that equals or exceeds full market value, which must be determined by appraisal by a certified or licensed appraiser. In addition, this law authorizes the Land Board to refuse to concur with the exchange if it determines that the exchange does not return full market value to the state.

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### **How is Fair Market Value Determined?**

Section 15-8-111(2)(a), MCA, defines market value as “the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.” A common method of determining fair market value is by appraisal. The Board of Real Estate Appraisers regulates the appraisal practice. This board issues licenses and certificates to qualified individuals. By law, terms commonly used in appraisal practice must be defined by the Uniform Standards of Professional Appraisal Practice (USPAP). USPAP defines an appraisal as “the act or process of developing an opinion of value.”

As noted in numerous appraisal documents in files we reviewed, the appraisal process is an orderly procedure of gathering information from the market that leads to an estimate of value. Market information can be obtained from numerous sources, but the most

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common source is sales of properties similar to the property being appraised. The three approaches to value are: 1) cost, 2) sales comparison, and 3) income.

While all three approaches can be used, for the projects we reviewed, the appraiser indicated the sales comparison approach was the most applicable method to use.

No matter what approach to value is used, the appraiser must determine the land's "highest and best use." Determination of highest and best use is one of the most important factors in estimating market value. There are four criteria that must be addressed in determining highest and best use:

1. Physically possible
2. Legally permissible
3. Financially feasible
4. Highest value

The land use that meets the first three criteria and results in the highest value return to the land is the property's highest and best use.

### **Are Appraisals Used by State Agencies?**

Of the 31 completed or in-process projects we reviewed in the four agencies, 26 were at a stage where land values had been determined. Of these 26 projects, 2 did not use an appraisal to determine market value. For the Lake Mary Ronan exchange at FWP, department personnel decided to forego an appraisal and use the "asking price" for land value. The asking price was \$2,500 per acre, which was set by the private party who owned the land. The decision to not complete an appraisal was based on department personnel's belief that an appraisal may result in a different value than the asking price, and that the private party may not accept another price. The FWP Commission and the Land Board approved this exchange.

At MDT, personnel used information from Farm Credit Services to estimate the value of private land in the Zurich exchange. Farm Credit Services provides agricultural and rural property appraisal

## Chapter V – Other Land Exchange Requirements

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services using certified appraisers. In addition, both properties in the Zurich exchange were valued at less than \$2,500.

In most instances, certified appraisers were used to determine market value. DNRC and MDT have certified appraisers as department employees. These department employees conduct appraisals as well as review appraisals completed by other department and contracted appraisers. MDT also uses right-of-way agents to conduct appraisals of lands preliminarily valued at less than \$10,000. Right-of-way agents are not licensed or certified appraisers. All four agencies have contracted for third-party appraisal services. Certified appraisers conducted all contracted appraisals. In addition, 18 of the 24 projects with appraisals had another individual review each appraisal.

### ***Conclusion: Appraisals are Used to Establish Market Value***

For 24 of 26 projects reviewed, market value was determined through appraisal by a certified appraiser. We did not specifically test whether use of certified appraisers increases the validity of appraisals; however, we did not note any negative effects on the appraisal process or determination of fair market value of land due to use of non-certified appraisers. All appraisals are reviewed and updated when appropriate.

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### **Was Equal or Greater Value Retained for Land Exchanges?**

As part of our review, we compared land values to determine if the state retained equal or greater value for all exchanges. For all exchanges we reviewed, the state retained at least equal value on land it exchanged. MDT did not clearly document values retained for all its projects. The following section discusses this issue.

### **Law Allows MDT to Accept Less Value**

From our review, it appears the law allows MDT to receive less than market value. According to section 60-4-201, MCA, the department has authority to exchange land and “to establish the manner and terms and conditions for the exchange.” This law provides the department latitude to negotiate a land exchange. Nonetheless, MDT personnel said they use land sale laws and policies as guidance for land exchanges.

## Chapter V – Other Land Exchange Requirements

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We tested MDT land exchanges for compliance with the statutory requirement to receive a minimum of 90 percent of the appraised value. We noted one project where it appeared this requirement was not met, and thus, equal or greater value was not retained. In this exchange, department personnel negotiated a cash payment from the private landowner to finalize the transaction. While negotiations began at equal value, the end result appeared to be that the department received 82 percent of appraised value. We reported this finding to the department, but personnel disagreed with our conclusion. After further explanation and clarification from department personnel, we agreed that equal value was retained for this exchange. However, the file did not clearly document the value MDT retained as a result of the exchange.

The department has procedures in place for administrative settlements when reasonable efforts to negotiate have failed. The Federal Highway Administration encourages states to use this process if it will avoid extraneous costs. The administrative settlement process was used for the exchange noted above, as well as for other exchanges we reviewed. According to department personnel, administrative settlements are used for property being acquired. In the example above, file documentation did not indicate that the difference between the values of the excess MDT land being exchanged and the right-of-way and property being acquired by the department was accepted as part of the administrative settlement. As a result, we concluded equal value was not retained. The administrative settlement process is basically an exchange equalization process.

The department has limited documented procedures for land exchanges. Although staff said they follow land sale procedures, there are noted differences in protocol for various land exchanges. While equal value was retained in the exchange noted above, the department needs to clarify its procedures for documenting value received for land exchanges. The bureau responsible for exchanges is currently updating its manual, including developing new procedures for exchanges. We recommend these include guidelines

## Chapter V – Other Land Exchange Requirements

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for documentation which clearly shows the values received for land exchanges. Department management agrees with our recommendation and plans to establish procedures and inform department personnel of the need to clearly document land exchanges.

### **Recommendation #3**

**We recommend MDT clarify procedures used for state land exchanges, specifically those related to documenting land values.**

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### **Are Environmental Assessment and Antiquity Regulations Followed?**

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#### **MEPA**

As part of our audit, we reviewed agency compliance with the Montana Environmental Policy Act (MEPA) and the Antiquities Act. The following sections summarize our findings.

MEPA requires state government to be accountable to the people of Montana when it makes decisions that have potential impact on the environment. State agencies must analyze the significance of impacts on the environment associated with proposed actions. Exchanging trust and non-trust lands for other lands are actions that impact the environment. During our review of files, we checked for the existence of MEPA documentation.

We noted MEPA documentation in all completed DNRC files reviewed. For FWP files, we did not locate/review all environmental documents; however, file documentation indicated an environmental analysis was completed. The two Montana University System (MUS) exchanges qualified for a categorical exclusion per Board of Regents policy (1003.6(VI)(B)) and an environmental analysis was not deemed necessary. We noted environmental documents in MDT exchanges with other governmental agencies, but not in all files. This issue is discussed further in the following section.

#### **Documentation of MEPA Decision-Making at MDT**

We determined MDT does not complete a formal environmental analysis when exchanging excess property. Department staff said if an analysis were requested, they would complete a formalized

## Chapter V – Other Land Exchange Requirements

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review; however, it is not normal practice to complete an environmental analysis for all exchanged parcels.

The idea behind MEPA is to determine the significance of environmental impacts from government actions. The MEPA process helps to ensure the public is informed of pending decisions, understands how decisions are made, and makes certain reasonable alternatives are considered. According to department personnel, MDT's legal staff has suggested completion of a checklist environmental assessment for land exchanges. Discussions with MDT legal and environmental services personnel further affirmed that some sort of documentation should be completed.

Without documentation of an agency's decision-making process, the public may not be fully informed of agency actions. This can impact an agency's accountability. Lack of documentation and reduced accountability do not meet the intent of MEPA.

According to department personnel, an environmental assessment or an environmental impact statement is unnecessary in many MDT land exchanges due to the insignificance of the action. We identified instances where a hazardous waste analysis was completed when a significant environmental concern was identified; however, the analysis is not completed for all exchanges. In addition, it is not clear whether a hazardous waste analysis would satisfy MEPA requirements. Development of a checklist form of assessment would at least provide documentation of the bureau's decision-making process. Department management agrees with our finding and is developing environmental assessment procedures and a checklist to complete for all exchanges.

### **Recommendation #4**

**We recommend MDT document its environmental decision-making process for land exchanges.**

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### **The Antiquities Act**

Section 22-3-424, MCA, requires state agencies, in consultation with the Historical Society, to adopt rules for the identification and preservation of heritage properties and paleontological remains on lands owned by the state. The State Historic Preservation Office (SHPO), under the supervision of the Historical Society, is responsible for surveying, identifying, documenting, and maintaining an inventory of heritage properties and paleontological remains. As part of our audit, we checked files for documentation indicating agency completion of cultural surveys and/or contact with SHPO to meet the antiquities mandate.

We noted documentation indicating contact with SHPO and/or completion of a cultural survey in all DNRC and MUS files. At FWP, we noted documentation in 9 of 11 files. Prior to May 2000, MDT did not conduct cultural resource reviews. As a result of a pending land sale, MDT identified the importance of cultural surveys and implemented policy for reviews. All MDT files we reviewed were completed prior to implementation of policy.

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### ***Conclusion: Environmental and Cultural Resources Regulations are Followed***

Based on our review of files, it appears environmental and cultural resources are reviewed in relation to land exchanges. While MDT does not complete MEPA documentation for all land exchanges, it appears personnel make informal decisions on the significance of department actions. In addition, MDT recognized the importance of cultural surveys and implemented policy to ensure reviews are completed.

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### **Is the Public Adequately Involved with Proposed Land Exchanges?**

We checked files for public notification and public hearing information as required by Land Board policy and MEPA. Our purpose was to determine the level of public involvement in land exchanges. Notifying the public of proposed land exchanges, providing the public an opportunity to comment, and responding to public questions and/or comments as appropriate represents an effective process.

DNRC has the most requirements for public notice of land exchanges. The public is notified and provided an opportunity to

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respond during the public scoping process prior to preliminary approval from the Land Board. DNRC is the only agency of the four we reviewed obtaining public comment during the initial phase of the process, as well as later in the process during the environmental analysis. FWP and MUS have statutory public notice mandates that allow the public to comment on land exchange proposals. MDT does not have statutory requirements for public notice of land exchanges. The prior owner or successor in interest of the MDT land to be transferred must be notified and can request the land be sold rather than exchanged. This statute was changed during the 2001 legislative session to require notification to adjacent landowners rather than the original owner. The new requirement does not go into effect until October 2001. There are public notification requirements for the sale of MDT land. Applicable public notice requirements were met for the files we reviewed.

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***Conclusion: The Public is Properly Notified***

Based on our review, it appears the public is properly notified of proposed land exchanges, and hearings are conducted as needed. While there may be disagreements with actions taken, nothing came to our attention indicating the public was not notified or provided an opportunity to comment as required.

# **Agency Responses**

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DEPARTMENT OF NATURAL RESOURCES  
AND CONSERVATION

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TRUST LAND MANAGEMENT DIVISION  
JUDY MARTZ, GOVERNOR

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STATE OF MONTANA

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September 28, 2001

Mary Zednick  
Performance Audit Manager  
Legislative Audit Division  
State Capitol, Room 160  
PO Box 201705  
Helena, MT 59620-1705



Dear Ms. Zednick:

The Department has reviewed the final report on the audit of our Land Exchanges. Your report contains two formal recommendations and two informal suggestions that we would like to comment on.

**Recommendation #1: The DNRC use cash equalization payments as an option in trust land exchanges.**

The report is correct in that the DNRC has not accepted cash in lieu of lands in "land exchanges". Prior to your audit the department believed that the use of the word "land" preceding the word "exchange" limited and restricted the components of an exchange to "land" as more particularly defined under Section 70-15-102 MCA. In addition, it was our understanding that the receipt of cash for fee simple title to land, regardless of the amount, constituted a sale.

Assuming the audit recommendation is legal, it fails to indicate to what extent dollars could be accepted in lieu of land. The DNRC feels it would be necessary to have identified sideboards and a definitive cap on the amount of money that could be accepted so that it in no way could be considered a sale.

Because of the subjective nature in which appraisals are conducted and values concluded, the DNRC believes it might be reasonable to consider an "accuracy rating or factor" of say up to 10% of appraised value. The DNRC intends to review and investigate this concept further and with approval of the Board, may propose legislation in the next couple of sessions. Such legislation might actually provide a waiver of differences of some percentage of appraised value similar to what the BLM did on the Crow Exchange or allow us to accept a cash payment in lieu of land of up to say 10% of

the designated appraised value with an absolute maximum currently thought to be around \$500,000.00. There is a caution however with any concept of this type in that private landowners we deal with may expect reciprocity in these types situations and we may not have the legal authorities or resources to do so.

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**Recommendation #2: The DNRC establish procedures to implement Land Banking**

DNRC feels land banking would be a very valuable management tool. However, we question whether there is current legal authority to implement any such program. In particular §11 of the Enabling Act says that "all lands granted by this act shall be disposed of only at public sale ..." and "With the exception of the lands granted for public buildings, the proceeds from the sale and other permanent disposition of any of the said lands and from every part thereof, shall constitute permanent funds for the support and maintenance of the public schools and the various state institutions for which the lands have been granted." The DNRC feels that the report does not adequately address these issues.

Further, the report fails to advise or direct the Department as to the current laws or case laws that might allow us to do this. Even if there were current laws, from a practical standpoint, the Department believes there are a limited number of people who would be financially able to participate. As your auditors found, the exchange process is lengthy and takes several years to complete. Potential viable scenarios would have their money tied up for several years while other lands are being acquired. Deeds would not transfer until replacement properties were found. The DNRC also feels that if the time it has to find other lands were limited to 3 or 4 years from the time it sold a particular piece of land, it could very well find itself compelled to acquire another piece of land simply to meet a deadline and that the resultant rushed decisions might not be the best for the trust (i.e. the amount of money available from the sales that have been completed might not be enough to purchase a good piece of property.)

As you know, the concept of land banking or deferred exchanges is not new to us. The Department and the Land Board have been contemplating this for years. It is likely that the DNRC and the Board will be revisiting this matter and investigating various ways to get the necessary laws and procedures developed for such a program over the next few years. It is our hope that given enough time, we would be able to identify viable options for the development of a program within the current legal framework and/or get the federal and/or state law changes necessary to implement such a program.

**Suggestion #1: DNRC compile and report the success of land exchanges on a regular basis.**

The DNRC intends to put together information similar to that which we provided to you, and which you included in the report (ref. Table 3 on page 22), and incorporate it in future Annual Reports.

The DNRC feels some clarification is needed as to a couple of income items on your table – in particular the current incomes shown as zeros that are attributable to the Mead and Ulm/Makoshika Exchanges.

The Ulm/Makoshika Exchange with the Department of Fish, Wildlife and Parks (FWP) was not finalized until June 26th of this year. The lands the DNRC acquired are currently better suited for grazing. They are being reviewed as to acceptable carrying capacities and are to be offered for lease before the end of this year so that grazing might begin next season. The lands the DNRC exchanged to FWP were a mixture of grazing, croplands, and some unsuitable lands that contained the majority of the bluff area of the Ulm Pishkun Buffalo Jump. The DNRC and the Board were fully aware that the lands we acquired may generate a lesser amount of income to the trust at the present time. However, fulfillment of the other exchange criteria and potential for land appreciation leading to some enhanced future use opportunities justified the exchange.

The Mead exchange was finalized last year in April. This was a 3-way exchange involving lands owned by the Montana Department of Transportation (MDT) and a private landowner (Mr. Mead). An important segment of the historic Mullan Trail ended up in the hands of the MDT and is better suited to be preserved and made available to the public under their management. The lands the DNRC received out of the exchange consisted of two lots in a commercial area on Reserve Street in Missoula. A recent re-appraisal of the lots indicates that since the land value has increased from \$4/sq.ft. to \$6. This value will be used to set the lease rate. As was pointed out in the report, the DNRC has been investigating leasing strategies and anticipates entering into a contract with a local realtor within the next couple of months to help find a suitable lessee for the property. Once implemented, lease rentals on these tracts are expected to be exponentially greater than the exchanged lands.

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**Suggestion #2: DNRC and MDT clarify their MOU with regard to unequal values at the end of the cited three-year term.**

The DNRC and MDT have met and agreed on language to amend the MOU and clarify the intent. This amendment will be presented to the Land Board for review and approval at its regular meeting on October 15, 2001.

Department staff enjoyed working with all the audit staff and feels the interactions and discussions were very worthwhile. It is good to have confirmation in this report that we are doing things properly and that we are in fact benefiting and improving the trust.

The DNRC welcomes the opportunity to further discuss any of the items addressed above with any of the audit staff and/or the Committee.

Sincerely,



Bud Clinch, Director

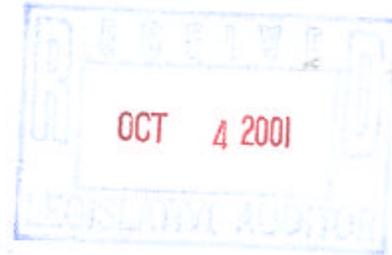
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c: Tom Schultz, Trust Land Administrator  
Clive Rooney, Chief, Special Uses Bureau  
Marylee Norris, Real Estate Manager



October 1, 2001

Jim Pellegrini  
Deputy Legislative Auditor  
Legislative Audit Division  
PO Box 201705  
Helena MT 59620-1705



Subject: Performance Audit of state agency land exchanges

Dear Jim,

Thank you for sending us copies of the final report from the audit of our state land exchanges. We have already taken action to clarify exchange procedures for documenting land values and implement an environmental assessment checklist. Our specific responses to the two recommendations applicable to this agency are as follows:

*Recommendation # 3 – “We recommend MDT clarify procedures used for state land exchanges, specifically those related to documenting land values.”*

MDT concurs with this recommendation. Our Right-of-Way Manual is being re-written and will include detailed procedures for land exchanges. Any administrative settlements will be made on the property MDT is acquiring. All exchanged properties will be for full fair market value and will be clearly documented in the file. All new procedures are now effect and the new manual should be completed in January 2002.

*Recommendation # 4 – “We recommend MDT document its environmental decision-making process for land exchanges.”*

MDT agrees that its environmental process for land exchanges needs to be improved. An environmental assessment checklist has been prepared by MDT's Environment Services. It is in the process of being reviewed and approved. Upon approval, all sales and exchanges of MDT properties will include a completed checklist. The procedure for utilizing this checklist has been presented to the right-of-way staff and will be included in our new Right-of-Way Manual.

We will continue to look for other ways that we can improve upon the terms and conditions of an exchange. This will include better clarification, documentation and uniformity of all our procedures.

Sincerely,

David A. Galt  
Director

copies: Gary Gilmore, Chief Engineer  
John Horton, Right-of-Way Bureau Chief  
Greg Hahn, Right-of-Way Operations Manager  
Barbara A. Smith, Right-of-Way Real Estate Services Section



P. O. Box 200701  
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Ref:DO0754-01  
October 1, 2001

Mr. Scott Seacat  
Legislative Auditor  
Legislative Audit Division  
Montana State Legislature  
P O Box 201705  
Helena MT 59620-1705

Dear Mr. Seacat:

Montana Fish, Wildlife & Parks (FWP) has reviewed your final report on the audit of State Agency Land Exchanges. I believe the audit accurately portrays FWP's land exchange process and program. Although the report makes no formal recommendations regarding the Department, I concur with your management suggestion that we develop formal land exchange policies and procedures. As we discussed with your staff, this change will be implemented.

Thank you for your review. We appreciate the opportunity to work with your staff on these issues.

Sincerely,  
  
M. Jeff Hagener  
Director

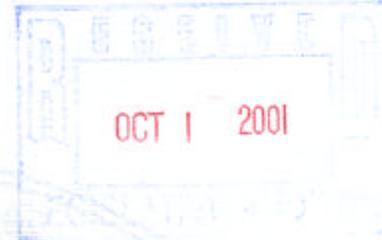
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MONTANA UNIVERSITY SYSTEM  
OFFICE OF COMMISSIONER OF HIGHER EDUCATION

2500 BROADWAY ♦ PO BOX 203101 ♦ HELENA, MONTANA 59620-3101 ♦ (406)444-6570 ♦ FAX (406)444-1469

October 1, 2001



Mr. Scott A. Seacat  
Legislative Auditor  
Legislative Audit Division  
State Capitol, Room 135  
PO Box 201705  
Helena, MT 59620-1705

Dear Mr. Seacat:

This letter acknowledges receipt by the Office of the Commissioner of Higher Education of the Legislative Audit Division's performance audit on State Agency Land Exchanges. We are gratified with the finding that the University System land exchanges for the period reviewed were conducted appropriately and consistent with legal requirements. We also appreciate the suggestion made that we consider developing a checklist of land exchange requirements to assist System managers as they envision future exchanges.

Sincerely,

A handwritten signature in black ink that reads "Richard A. Crofts".

Richard A. Crofts, Ph.D.  
Commissioner of Higher Education

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