

**IDAHO  
ATTORNEY  
GENERAL'S  
ANNUAL REPORT**

**OPINIONS**

**SELECTED INFORMAL  
GUIDELINES**

AND

**CERTIFICATES OF REVIEW**

FOR THE YEAR

**2000**

**Alan G. Lance**  
Attorney General

Printed by The Caxton Printers, Ltd.  
Caldwell, Idaho

**This volume should be cited as:**

**2000 Idaho Att’y Gen. Ann. Rpt.**

**Thus, the Official Opinion 00-1 is found at:**

**2000 Idaho Att’y Gen. Ann. Rpt. 5**

**Similarly, the Informal Guideline of February 16, 2000  
is found at:**

**2000 Idaho Att’y Gen. Ann. Rpt. 39**

**The Certificate of Review of March 22, 2000  
is found at:**

**2000 Idaho Att’y Gen. Ann. Rpt. 69**

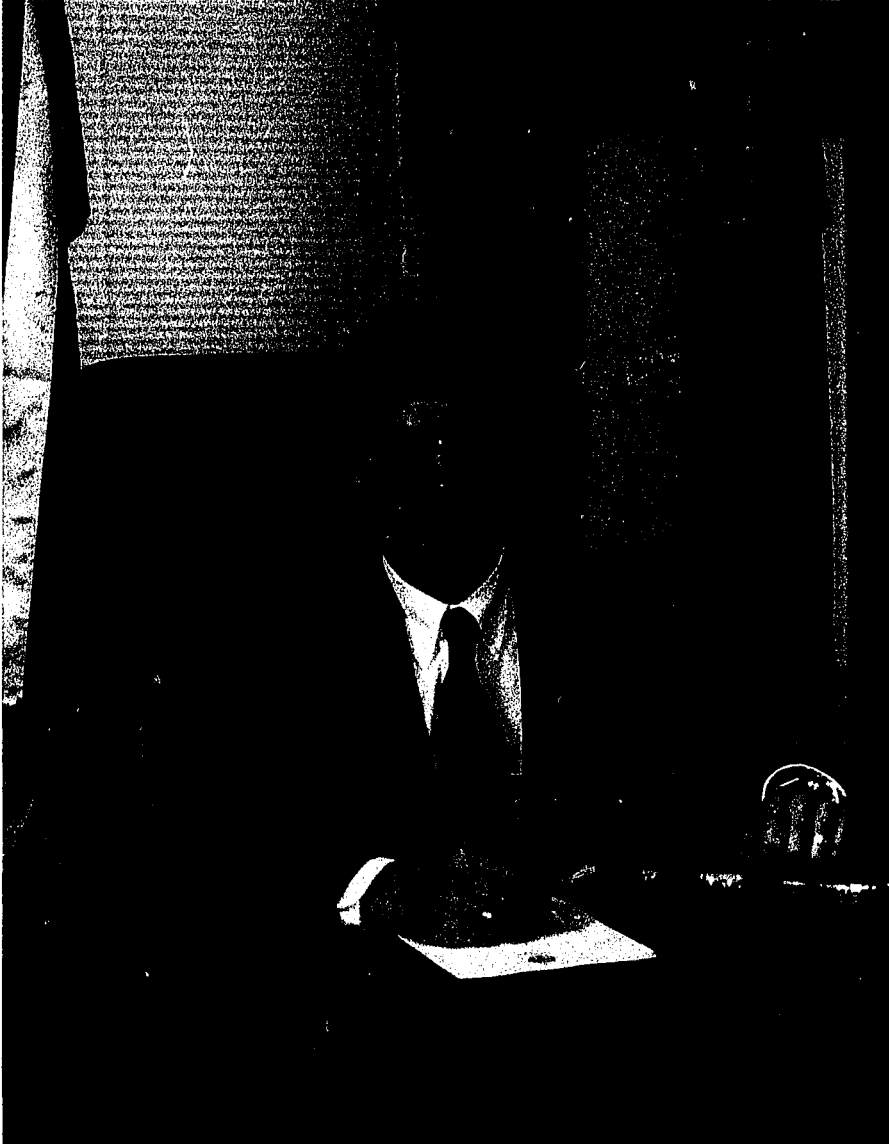
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## **ATTORNEYS GENERAL OF IDAHO**

GEORGE H. ROBERTS	1891-1892
GEORGE M. PARSONS	1893-1896
ROBERT McFARLAND	1897-1898
S. H. HAYS	1899-1900
FRANK MARTIN	1901-1902
JOHN A. BAGLEY	1904-1904
JOHN GUHEEN	1905-1908
D. C. McDOUGALL	1909-1912
JOSEPH H. PETERSON	1913-1916
T. A. WALTERS	1917-1918
ROY L. BLACK	1919-1922
A. H. CONNER	1923-1926
FRANK L. STEPHAN	1927-1928
W. D. GILLIS	1929-1930
FRED J. BABCOCK	1931-1932
BERT H. MILLER	1933-1936
J. W. TAYLOR	1937-1940
BERT H. MILLER	1941-1944
FRANK LANGLEY	1945-1946
ROBERT AILSHIE (Deceased November 16)	1947
ROBERT E. SMYLIE (Appointed November 24)	1947-1954
GRAYDON W. SMITH	1955-1958
FRANK L. BENSON	1959-1962
ALLEN B. SHEPARD	1963-1968
ROBERT M. ROBSON	1969
W. ANTHONY PARK	1970-1974
WAYNE L. KIDWELL	1975-1978
DAVID H. LEROY	1979-1982
JIM JONES	1983-1990
LARRY ECHOHAWK	1991-1994
ALAN G. LANCE	1995-



**Alan G. Lance**  
Attorney General

## INTRODUCTION

Dear Fellow Idahoans:

As I begin my seventh year as your Attorney General, it is as apparent as ever that the most significant issues on Idaho's legal and political landscapes are those arising from disputes over water or land. Although the contents of this volume of the Attorney General's Annual Report do not reveal the extensive nature of my office's work in the natural resources law area, it would not be a true reflection of the year 2000 unless I detailed some of our more important cases involving Idaho's water and land.

The State of Idaho is typically quite active in the natural resources area of law, due to the fact that 69.11% of Idaho's land is publicly managed, including 63.7% or 33,738,380 acres managed by the federal government. Idaho is also home to five Wilderness Areas, totaling 3,961,501 acres, as well as seven National Parks, Monuments and Recreation Areas, totaling 1,376,124 acres. The level of interest and concern shared by Idahoans in this area of law has been on the rise as federal compensation to counties (PILT, Taylor Grazing, Mineral Leasing, and Forest Receipts) plunged from \$33,029,236 in FY 1995 to \$8,354,480 in FY 1999.

The lawsuit I filed on behalf of the Idaho State Board of Land Commissioners against the United States Forest Service is a testament to two important factors in Idaho's law office. The lawsuit charged the Forest Service with violating the National Environmental Policy Act (NEPA) in promulgating the so-called "roadless rule." The roadless rule would lock up over 9 million acres of federally managed Idaho lands, putting further strain on the interior portions of Idaho from the Wyoming border to Canada. The roadless rule would affect almost 60 million acres nationwide, lands located in almost every state. The fact that a sparsely populated state like Idaho would lead the effort to challenge this Washington, D.C.-created policy should not surprise anyone. Natural resource policy will generally affect Idaho as much as or more than any other state in the country.

The second factor is that I was able to call upon expertise from attorneys in my office assigned to three different legal divisions. Thanks to the Legal Services Consolidation Law passed in 1995, the Attorney General is able to quickly assemble experienced state lawyers from different locations to battle the often impressive number of lawyers who represent opposing parties and special interest groups. Attorneys from my Divisions of Natural Resources, Intergovernmental and Fiscal Law, and Civil Litigation formed my core team on the roadless issue. They represented the State of Idaho's case against Washington, D.C.-based federal attorneys and San Francisco-based attorneys representing environmental groups. My team won a ruling from the federal district court that the roadless rule "conclusively" was the product of an "obvious

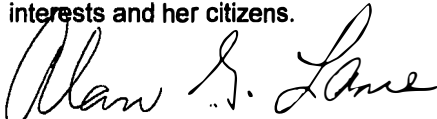
violation of NEPA," and a temporary injunction prohibiting implementation of the rule until the court issues a final decision on a permanent injunction.

The massive and complex Snake River Basin Adjudication (SRBA) produced three important decisions during the last year. First, the Idaho Supreme Court, in reversing an earlier decision it made, ruled that the Wilderness Act of 1964 did not create implied federal water rights in three of Idaho's wilderness areas. Second, the Idaho Supreme Court ruled against a federal reserved water right for the Sawtooth National Recreation Area. Third, the Idaho Supreme Court ruled against the United States' claim for implied federal reserved water rights for the Deer Flat Wildlife Refuge. Of the more than 3,700 federal reserved water rights claims submitted by federal agencies in the SRBA, all but eight have been defeated. The SRBA is ongoing, and my office will continue to vigorously defend Idaho's water rights in 2001, but I believe we are getting closer to the time where this special adjudication process will be a part of Idaho's history.

In other areas of law, the Criminal Law Division was occupied with several lawsuits in 2000, challenging the constitutionality of Idaho's domestic violence law. A number of lower court decisions cast doubt upon the law, and many other cases were held in abeyance until the Idaho Supreme Court resolved the constitutional issues. The Criminal Law Division's efforts resulted in a clean sweep in six court decisions where the law was being challenged as vague, overbroad, and violative of equal protection. In short, the Idaho Legislature's intent to codify a crime and punishment for those who willfully cause traumatic injuries to other members of their household was upheld.

Finally, my office continued its efforts in the consumer protection area, recovering \$905,055 for consumers, \$546,132 in civil penalties, fees and costs, and \$20.7 million for the State of Idaho pursuant to the historic tobacco settlement. Other efforts aimed at protecting consumers' financial privacy, stopping deceptive and misleading tactics in sweepstakes promotions and telemarketing, and battling an influx of pyramid schemes, made 2000 a busy and successful year for consumer protection in Idaho.

I hope you find the contents of the 2000 Attorney General Annual Report to be useful. I look forward to the next year as I continue to vigorously defend Idaho's interests and her citizens.



ALAN G. LANCE  
Attorney General

# ANNUAL REPORT OF THE ATTORNEY GENERAL

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## OFFICE OF THE ATTORNEY GENERAL ALAN G. LANCE ATTORNEY GENERAL

### 2000 STAFF ROSTER

#### ADMINISTRATION

Lawrence Wasden Chief of Staff	Thorpe Orton Deputy Chief of Staff	Janet Carter Executive Assistant	Sandra Rich Administrative Secretary/Receptionist
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#### DIVISION CHIEFS

Tara Orr, Administration & Budget	Jeanne Goodenough, Human Services
David High, Civil Litigation	William von Tagen, Intergovernmental & Fiscal Law
Terry Coffin, Contracts & Administrative Law	Clive Strong, Natural Resources
Michael Henderson, Criminal Law	

#### DEPUTY ATTORNEYS GENERAL

Willard Abbott	Ron Christian	Donald Howell	Clinton Miner	Nicholas Spencer
Lawrence Allen	Doug Conde	Ron Howen	Scott Muir	Marcy Spilker
Stephanie Altig	Cheri Copsey	Karen Hudelson	Robert Naftz	Myrna Stahman
Peter Ampe	Kimberly Coster	Mary Hughes	Deborah Nelson	Dan Steckel
LaMont Anderson	Rebekah Cude	Blair Jaynes	Kent Nelson	Alison Steiglitz
James Baird	Christy Cunningham	J. Scott James	Brian Nicholas	Steve Strack
Stephanie Balzarini	Brett DeLange	Kenneth Jorgensen	Kirsten Ocker	Ken Stringfield
David Barber	Keith Donahue	Rinda Just	Carl Olsson	Weldon Stutzman
Mary Jo Belg	Thomas Donovan	Paul Kime	Paul Panther	J. Ron Sutcliffe
Nancy Bishop	Darrell Early	C. Nicholas Krema	Steve Parry	Evelyn Thomas
Craig Bledsoe	Mary Feeney	Lisa Kronberg	Eric Pfost	Geoffrey Thorpe
Brian Blender	Curt Fransen	T. Paul Krueger II	Victor Ramirez	Melissa Vandenberg
Jo-Ann Bowen	Sherman Furey III	David Lloyd	Phillip Rassler	Bridget Vaughan
Carol Brassey	Roger Gabel	Kay Manweiler	Kenneth Robins	Karl Vogt
Dallas Burkhalter	Michael Gilmore	Rene Martin	Donald Robertson	Kirsten Wallace
Cheri Bush	Stephen Goddard	Candice McHugh	Kevin Satterlee	Wili Wheian
Michelle Butts	Brad Goodsell	Matthew McKeown	Steve Schuster	Peggy White
James Carlson	Joanna Guilfoxy	John J. McMahon	Jason Selms	Timothy Wilson
Sandra Carter	Susan Hamlin	Tim McNeese	Sandra Shaw	Scott Woodbury
Jody Carpenter	Harriet Hensley	Mark Mimura	Michael Sheeley	Mary York
Corey Cartwright	John Horman		Theodore Spangler	Charles Zalesky

#### INVESTIGATORS

Russ Reneau, Chief	Jackie Allor	Scott Birch	Bill Buile	Gary Deulen
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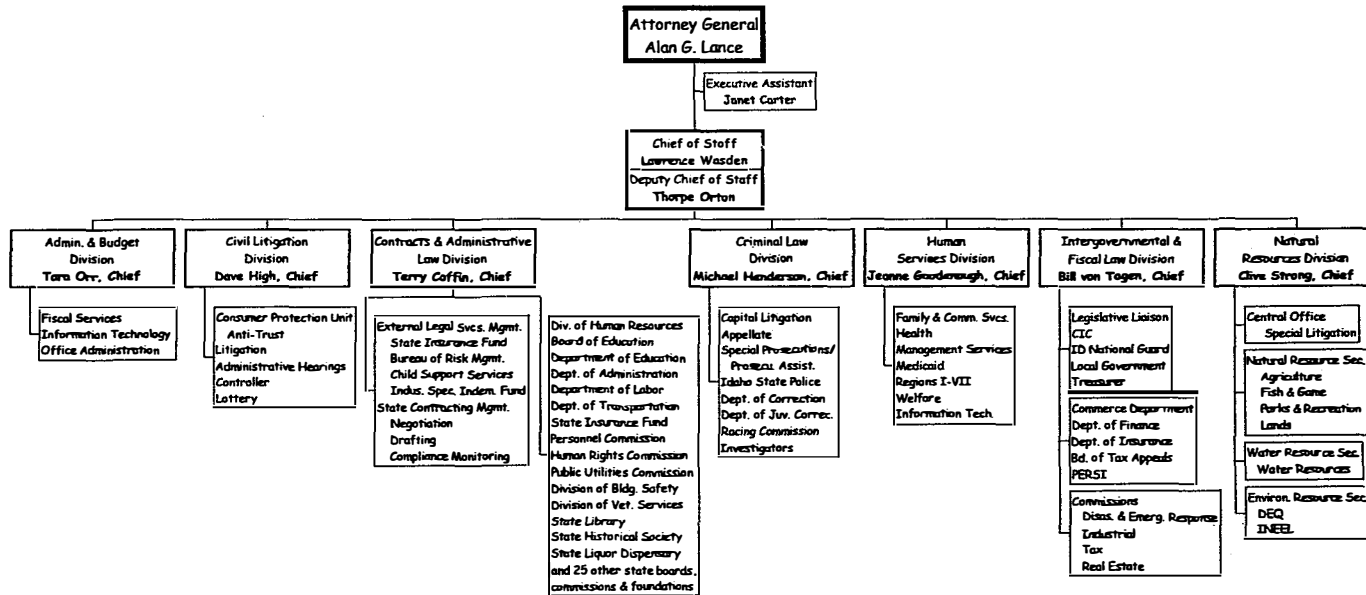
#### PARALEGALS

Kathie Brack	Vicki Kelly	Vicky Music	Jean Rosenthal
Janice Crawford	Marlene Klein	Bernice Myles	Kristina Schnur
Paula Gradwohl	Linda Mirelez	Lori Peel	Robert Wheller
Becky Harvey	Dora Morley	Brett Phillips	

#### NON-LEGAL PERSONNEL

Rachel Balcerzak	Marnie Burt	Bethany Garner	Gerry Karpavich	Lynn Mize	Micki Schlapla
Susan Baldwin	Robert Cooper	Leslie Gottsch	JoAnn Lanham	Ruth Miller	Debbie Stuffbeame
Prudence Barnes	Suzanne Crockett	Luanna Hibdon	Don Larson	Rebecca Moss	Olga Valdivia
Kriss Bivens	Sharon DeWitt	Trudy Jackson	Lynette Lloyd	Renda Newman	Melissa Ward
Patricia Boehm	Marilyn Freeman	Kelly Jennings	Pat McCoy	Roseann Newman	Deena Williams
Karen Bolian	Colleen Funk	Cecil Jones	Patty McNeill	Sharon Noice	
Wanda Brock	Kathy Funk	Courtney Jumigan	Ronda Mein	Almee Price	

Office of the Idaho Attorney General  
Organizational Chart - 2000



**OFFICIAL OPINIONS  
OF  
THE ATTORNEY GENERAL  
FOR 2000**

**ALAN G. LANCE**  
ATTORNEY GENERAL  
STATE OF IDAHO



**ATTORNEY GENERAL OPINION NO. 00-1**

To: The Honorable Bruce Newcomb  
Speaker, Idaho House of Representatives  
P.O. Box 757  
Burley, ID 83318

Per Request for Attorney General's Opinion

**QUESTION PRESENTED**

You have requested an opinion as to whether Idaho's tiered premium tax statutes violate: (a) the Commerce Clause of the United States Constitution; (b) the Equal Protection Clauses of the United States and Idaho Constitutions; or (c) the rights to substantive due process under the United States Constitution and the Uniformity Clause of the Idaho Constitution.

**SHORT ANSWER**

None of the premium tax statutes implicated, Idaho Code §§ 41-340, 41-402 and 41-403, violates Art. I, § 8 of the United States Constitution, the Commerce Clause, as that provision does not apply to the regulation and taxation of insurance.

Idaho's general base rate statute, Idaho Code § 41-402, does not violate the Equal Protection Clauses (U.S. Constitution amend. 14, § 1, and Idaho Constitution art. 1, § 2); the Due Process Clause, amend. 14, § 1 of the United States Constitution; or the Uniformity Clause, art. 7, § 5 of the Idaho Constitution. Similarly, Idaho's retaliatory premium tax statute, Idaho Code § 41-340, would likely withstand a constitutional challenge under the equal protection clauses, substantive due process, or the uniformity clause.

It is unclear whether Idaho's reduced rate for Idaho investments statute (hereinafter reduced rate or reduced tax statute), Idaho Code § 41-403, standing alone, or its cumulative effect with the retaliatory tax statute, Idaho Code § 41-340, violates the equal protection provisions of the United States and Idaho Constitutions, notwithstanding sound arguments to the contrary. A similar conclusion applies regarding any potential challenge based on the uni-

formity clause or substantive due process. Although no cases are directly on point, authority from various courts can be used to support arguments on either side. Ultimately, only the courts can establish certainty regarding these determinations.

## **ANALYSIS**

Your questions arise out of the recent litigation brought by the American Trucking Associations, Inc. in the Fourth Judicial District (American Trucking Associations, Inc. v. Idaho Transportation Department, CV OC 9700724D), which resulted in a settlement where the state agreed to pay a significant sum of money. The limited commodity use fee at issue in the trucking case, Idaho Code § 49-434(9), was struck down on Commerce Clause grounds. You've asked us to review the premium tax statutes in light of the recent successful challenge in the trucking case.

### **1. Description of Premium Tax Statutes**

The general base rate of premium tax is set forth in Idaho Code § 41-402(2). This section provides that the current base premium tax rate is 2.75% (except for title insurance companies, whose rate is 1.5%). This statute applies equally to all insurers within the respective lines of business.

Insurers can qualify for a reduced tax rate of 1.4%, rather than the applicable higher rate under Idaho Code § 41-402(2), upon showing that they have 25% of their total assets (or 25% of total required reserves for life insurers) invested in specified Idaho investments. Idaho Code § 41-403. As originally enacted in 1961, the reduced rate for Idaho investments was available only to domestic insurers. In 1983, however, Idaho Code § 41-403 was amended by H.B. 198 to change the applicability of the section from "any domestic insurer" to "any insurer." According to the committee minutes and the statement of purpose for that bill, the change was intended to encourage foreign insurers to invest in Idaho. Idaho Code § 41-403 currently reads as follows:

Provided that it shall comply with rules and standards duly promulgated by the director of insurance for the purposes of assuring the establishment and maintenance in this state of

services and facilities consistent with the nature and extent of its operations, any insurer, other than a life insurance company, having at all times throughout the year with respect to which the tax is payable twenty-five percent (25%) or more of its assets invested in the investments set forth below, shall, with respect to premiums on which taxes are to be computed under section 41-402, Idaho Code, compute and pay such tax at the rate of one and four-tenths percent (1.4%) instead of at any higher rate provided for under section 41-402, Idaho Code; and provided further, any life insurance company, in order to qualify for a tax rate of one and four-tenths percent (1.4%) instead of any higher rate provided for under section 41-402, Idaho Code, shall maintain throughout the year with respect to which tax is payable at least twenty-five percent (25%) of the reserve required under section 41-706(4), Idaho Code, invested in the designated investments set forth below:

(1) Bonds or warrants of this state, or of any county, city or incorporated town or district within this state authorized by law to be issued; or

(2) Taxable real estate within this state; or

(3) First mortgages upon improved, unencumbered real estate situated within this state; or

(4) Stocks or bonds of corporations organized under the laws of, or maintaining their home office and principal administrative records in this state if such stocks or bonds are lawful investments of the insurer under chapter 7 (investments) of this code; or

(5) Bonds authorized by law to be issued against the revenues derived from the operation in this state of domestic water and sewage systems or off-street parking facilities; or

(6) Time deposits, or other deposits for interest income purposes, in any Idaho branch of any bank, or trust

company, or savings and loan association, or any other legally organized and approved financial institution with one (1) or more branches in this state and insured by any instrumentality of the United States government.

Between 1985 and 1987, Idaho Code § 41-403 allowed non-life companies to qualify for the reduced rate through one of two alternatives. During this time, in addition to the current 25% of admitted assets basis, non-life companies that had 75% of their total premiums written in Idaho invested in Idaho assets could also qualify for the reduced rate. Life companies could qualify for the reduced rate during that time by investing in Idaho assets 75% of the required reserves for Idaho-only business, as opposed to the current measure, which is 25% of all required reserves.

Idaho Code § 41-340 imposes a "retaliatory tax" (as well as other retaliatory provisions) on foreign insurers. This section essentially provides that if an Idaho insurer would have to pay a higher rate of tax under the laws of a foreign company's state of domicile than under Idaho's law, then the foreign company will be taxed at that higher rate. In other words, the Idaho Department of Insurance compares Idaho's rate with the rate Idaho companies would have to pay in the foreign company's home state, and then the department taxes the foreign company at the higher of these two rates. Idaho Code § 41-340 provides in relevant part:

(1) The purpose of this section is to aid in the protection of insurers formed under the laws of Idaho and transacting insurance in other states or countries against discriminatory or onerous requirements under the laws of such states or countries or the administration thereof.

(2) When by or pursuant to the laws of any other state or foreign country or province any taxes in the aggregate, are or would be imposed upon Idaho insurers, or upon the agents or representatives of such insurers, which are in excess of such taxes in the aggregate, directly imposed upon similar insurers, or upon the agents or representatives of such insurers, of such other state or country under the statutes of this state, so long as such laws of such other state or country continue in force or are so applied, the same taxes in the

aggregate, shall be imposed by the director upon the insurers, or upon the agents or representatives of such insurers, of such other state or country doing business or seeking to do business in Idaho. Any tax imposed by any city, county, or other political subdivision or agency of such other state or country on Idaho insurers or their agents or representatives shall be deemed to be imposed by such state or country within the meaning of this section.

In 1985, the reduced rate statute was amended to exempt foreign insurers with qualifying Idaho investments from the effects of the retaliatory tax. In 1987, the legislature removed this exemption. Currently, a foreign insurer qualifying for the reduced tax based on Idaho investments is still subject to the retaliatory tax. In other words, if the reduced tax rate is lower than the rate that a similarly situated Idaho insurer would pay in the foreign insurer's state of domicile, then the foreign insurer is nevertheless taxed in Idaho at the higher rate imposed by its home state, even if it satisfies the requirements of the reduced rate statute.

The reduced tax and retaliatory tax statutes serve different purposes. The reduced rate provision appears to be aimed at encouraging investment in Idaho (although there are many other reasons that may support the statute, e.g., increased regulatory control and better protection of consumers), while the retaliatory tax is intended to deter foreign states from imposing high rates of tax on Idaho companies. Excluding title insurance and in general terms, four states currently impose rates lower than Idaho's reduced rate, approximately 35 states impose rates lower than Idaho's regular rate. The reduced rate provision might benefit insurers from these states.

Idaho's base premium tax rate statute is constitutional. Similarly, the retaliatory tax statute, standing alone, is likely constitutional. The primary constitutionality questions are: (a) whether the reduced rate statute is unfairly discriminatory, denies foreign insurers substantive due process, or violates the Idaho uniformity clause because it requires that foreign insurers invest an unreasonable amount of their assets in specified Idaho investments, and (b) whether the reduced rate and retaliatory rate sections, when taken together, result in unfair discrimination against foreign insurers, constitute a denial of substantive due process, or violate the uniformity provision of the Idaho Constitution.

## 2. Constitutional Standards

### A. U.S. Const. Art. I, § 8—Commerce Clause

In Western & Southern Life Insurance Co. v. State Bd. of Equalization of Cal., 451 U.S. 648, 101 S. Ct. 2070, 68 L. Ed. 2d 514 (1981), the Supreme Court held that the Commerce Clause does not apply to the authority of states to regulate and tax the business of insurance based on the McCarran-Ferguson Act (codified at 15 U.S.C. §§ 1011 – 1015), which gives the states exclusive authority over the regulation of insurance<sup>1</sup>. Because the Commerce Clause is inapplicable to the business of insurance, and the Privileges and Immunities Clause does not apply to corporations, “[o]nly the Equal Protection Clause remains as a possible ground for invalidation” of Idaho’s premium tax statutes under the United States Constitution. See Western & Southern Life Insurance Co. v. State Bd. of Equalization of Cal., 451 U.S. at 656, 101 S. Ct. at 2077.

### B. U.S. Const. Amend. 14, § 1; Idaho Const. Art. 1, § 2—Equal Protection

Regarding the standard to be applied in any challenge to Idaho’s premium tax, Idaho courts have held: “While a legislative act is presumed constitutional [citation omitted], whether it is reasonable and not arbitrary is a question of law for determination by the courts.” Sterling H. Nelson & Sons, Inc. v. Bender, 95 Idaho 813, 815, 520 P.2d 860 (1974). “It is generally presumed that legislative acts are constitutional, that the state legislature has acted within its constitutional powers, and any doubt concerning interpretation of a statute is to be resolved in favor of that which will render the statute constitutional.” Olsen v. J.A. Freeman Co., 117 Idaho 706, 709, 791 P.2d 1285, 1288 (1990). Therefore, the burden to overcome the presumptive constitutionality of any statute rests with any challenger.

The Equal Protection Clause provides: “No state shall make or enforce any law which shall . . . deny to any person within its jurisdiction the equal protection of the laws.” U.S. Const., amend. 14, § 1. When analyzing claims based on equal protection, courts must: (1) identify the challenged classification and (2) determine the applicable standard. The Idaho Supreme

Court recently summarized the applicable standards for an equal protection challenge:

For equal protection challenges to statutes based on the Fourteenth Amendment, three levels of scrutiny are used. These are strict scrutiny, intermediate scrutiny and the rational basis tests. The analysis of equal protection claims under the Idaho Constitution is very similar. "Three standards of equal protection analysis have been recognized in Idaho: strict scrutiny, means-focus, and rational basis."

Meisner v. Potlatch Corp., 131 Idaho 258, 261, 954 P.2d 676, 679 (1998) (citations omitted). The strict scrutiny test is applied to classifications involving a fundamental right or suspect class. *Id.* The intermediate scrutiny test has been applied by the United States Supreme Court only to classifications based on gender or illegitimacy. *Id.* The Meisner court further stated:

The means-focus test, while similar to the intermediate scrutiny test, has not been limited by Idaho courts to cases involving gender and illegitimacy; rather it has been applied to cases "where the discriminatory character of a challenged statutory classification is apparent on its face and where there is also a patent indication of a lack of relationship between the classification and the declared purpose of the statute . . . ." This Court, however, "has limited review under [the means-focus] standard to statutes of a blatantly discriminatory nature." Economic and social welfare [laws], such as the workers compensation statutes, are not subject to the means-focus test unless they create a suspect or invidiously discriminatory classification or involve a fundamental right.

Meisner v. Potlatch Corp., 131 Idaho at 261-62, 954 P.2d at 679-80 (citations omitted); *see also* Packard v. Joint School Dist. No. 171, 104 Idaho 604, 608, 661 P.2d 770, 774 (Ct.App. 1983) (asserting that "rational basis" test incorporates a "means-focus" analysis, and thus the two tests are not conceptually different). None of the tests by strict scrutiny test, intermediate scrutiny or means-focus would apply in review of Idaho's premium tax statutes; therefore the proper standard is the rational basis test.

The Idaho Supreme Court has stated, “a classification for tax purposes is reviewed on the rational basis test.” Bon Appetit Gourmet Foods, Inc. v. State Dept. of Employment, 117 Idaho 1002, 1004, 793 P.2d 675, 677 (1989), *addendum on rehearing* (1990); *accord V-1 Oil Company v. Idaho State Tax Comm’n*, Opinion No. 75 (Aug. 1, 2000). Similarly, the United States Supreme Court has stated that under the Equal Protection Clause, a state may not impose “more onerous taxes or other burdens on foreign corporations than those imposed on domestic corporations, unless the discrimination between the foreign and domestic corporations bears a rational relation to a legitimate state purpose.” Western & Southern Life Insurance Co. v. State Bd. of Equalization of Cal., 451 U.S. at 668, 101 S. Ct. at 2083. The Court stated that two questions must be answered in determining whether any challenged classification is rationally related to achievement of a legitimate state purpose: “(1) Does the challenged legislation have a legitimate purpose? and (2) Was it reasonable for the lawmakers to believe that use of the challenged classification would promote that purpose?” *Id.* “In the equal protection context, however, if the State’s purpose is found to be legitimate, the state law stands as long as the burden it imposes is found to be rationally related to that purpose, a relationship that is not difficult to establish.” Metropolitan Life Insurance Company v. Ward, 470 U.S. 869, 881, 105 S. Ct. 1676, 1683, 84 L. Ed. 2d 751 (1985). As discussed below, any substantive due process argument is likely subsumed in an equal protection analysis.

The statute involved in Bon Appetit Gourmet Foods, Inc. excluded certain types of persons from the independent contractor exemption to the unemployment tax. In a 3-2 decision, the court in that case held that the statute was unconstitutional. The court rested its decision on the lack of any evidence in the record supporting a rational reason for the classification. The issue of constitutionality was not addressed below, as this was an appeal from the industrial commission. The majority indicated that no rational reason was presented by the state, and the court was unable to proffer any rational reason. The dissenting opinions criticized the majority of the court for what was, in their view, effectively ignoring the presumption of constitutionality and requiring an affirmative showing of constitutionality, rather than requiring the challenger to demonstrate unconstitutionality. The court held that the statute violated the Equal Protection Clauses of the United States and Idaho constitutions on its face, and as applied to Bon Appetit Gourmet Foods, Inc., because no rationale or reasons supported the law. Bon Appetit Gourmet

Foods, Inc. v. State Dept. of Employment, 117 Idaho at 1004, 793 P.2d at 677. The court did not articulate any separate standard or analysis for a determination of unconstitutionality “as applied” as opposed to a determination of unconstitutionality apparent within the statute.

When applying the rational basis test, the mere presence of some inequality will not render a statute unconstitutional, i.e., “[a] statutory discrimination will not be set aside if any statement of facts may be reasonably conceived to justify it.” Olsen v. J.A. Freeman Co., 117 Idaho at 711, 791 P.2d at 1290 (*quoting Jones v. State Bd. Of Medicine*, 97 Idaho 859, 866, 555 P.2d 399, 406 (1976), *quoting McGowan v. Maryland*, 366 U.S. 420, 425-26, 81 S. Ct. 1101, 1105, 6 L. Ed. 2d 393 (1961)); *accord Meisner v. Potlatch Corp.*, 131 Idaho at 262, 954 P.2d at 680.

C. U.S. Const. Amend. 14, § 1—Due Process  
Idaho Const. Art. 7, § 5—Uniformity Clause

It appears that any challenge based on substantive due process would parallel the required analysis based on an equal protection challenge and not result in a different outcome. The Idaho Court of Appeals characterized substantive due process as “the right to be free from arbitrary deprivations of life, liberty or property.” State v. Reed, 107 Idaho 162, 167, 686 P.2d 842, 847 (Ct. App. 1984). In first determining that the challenged law was in the social and economic domain, and thus the deferential standard of review applied in a substantive due process analysis, the court held that the challenged statute requiring motorists to carry liability insurance served a reasonably conceivable and legitimate objective. The court of appeals noted that the principle of equal treatment for similarly situated persons “obviously shares a common nexus with substantive due process.” *Id.* The court also stated that the rational basis test for equal protection analysis “is analogous to the deferential test of substantive due process applied to social and economic legislation.” State v. Reed, 107 Idaho at 168, 686 P.2d 848. This encompasses the essence of the standard set forth earlier by the Idaho Supreme Court when it held “that the sole standard applicable to the due process provisions of the federal and state constitutions is whether the challenged law bears ‘a rational relationship to the preservation and promotion of the public welfare.’” Jones v. State Bd. of Medicine, 97 Idaho at 866, 555 P.2d at 406.

While it is also conceivable that a challenger could also raise the Uniformity Clause, art. 7, § 5 of the Idaho Constitution, as a basis to attack the constitutionality of Idaho's premium tax statutes, the analysis would similarly mirror that of rational basis under an equal protection challenge. The Idaho Supreme Court has stated that although "various standards have been articulated under" the Uniformity Clause and the Equal Protection Clause, "there is little practical distinction between the two." Justus v. Board of Equalization, 101 Idaho 743, 746, 620 P.2d 777, 780 (1980). "A taxing plan offensive to one also violates the other." *Id.*

### **3. Retaliatory Tax Statute (Idaho Code § 41-340)**

Idaho's retaliatory tax, standing alone, likely would withstand a constitutional challenge. Retaliatory premium taxes have a long history and are used in most states. In Western & Southern Life Insurance Co. v. State Bd. of Equalization of Cal., the United States Supreme Court upheld the constitutionality of California's retaliatory premium tax. Like Idaho, California imposed the tax when a foreign company's state of domicile imposed a tax rate higher on California companies than that imposed by California on the foreign company. After dismissing the taxpayer's challenge based on the Commerce Clause pursuant to the McCarran-Ferguson Act, the Court also found that California's retaliatory tax did not violate the Equal Protection Clause of the Fourteenth Amendment. The Court pointed out that the purpose of California's retaliatory tax statute "is not to generate revenue at the expense of out-of-state insurers, but to apply pressure on other States to maintain low taxes on California insurers." Western & Southern Life Insurance Co., 451 U.S. at 669-70, 101 S. Ct. at 2084. The court held that this purpose of promoting domestic industry by deterring barriers to interstate business, was a legitimate state purpose, and California's legislature could rationally have believed the retaliatory tax would promote this purpose.

Other retaliatory tax statutes have withstood constitutional challenge as well. See Prudential Ins. Co. of America v. Commissioner of Revenue, 709 N.E.2d 1096 (Mass. 1999) (applying pressure on other states to maintain low taxes on Massachusetts insurers, and thus promote Massachusetts insurers, was a legitimate purpose, and it was "at least debatable" that the operation of the taxing system had a rational relationship to that purpose); Executive Life Insurance Company v. Commonwealth, 606 A.2d 1282 (Pa. 1992) (retaliato-

ry tax statute does not violate Equal Protection Clause of the United States Constitution, nor the Uniformity Clause of the Pennsylvania Constitution); Gallagher v. Motors Insurance Corp., 605 So. 2d 62 (Fla. 1992), *cert. dismissed* 506 U.S. 1074, 113 S. Ct. 1036, 122 L. Ed. 2d 179 (1993) (discussed below); *see also* American Southern v. State Dept. of Revenue, 674 So. 2d 810 (Fla. Dist. Ct. App. 1996) (upholding Florida's construction and application of the term "similar insurer" within its retaliatory tax statute).

Similar to California's retaliatory tax law at issue in Western & Southern Life Insurance Co., Idaho's retaliatory law is expressly for the purpose of protecting Idaho domiciled insurers "against discriminatory or onerous requirements under the laws of" foreign states or countries or the administration of those laws. Any direct constitutional challenge to the retaliatory tax statute would likely fail. As alluded to earlier, a constitutional challenge to Idaho's premium tax structure would likely focus on the reduced rate statute standing alone or its interplay with, *i.e.*, deference to, the retaliatory tax.

#### **4. Potential Challenges To Reduced Rate Statute (Idaho Code § 41-403)**

##### **A. Case Authority**

Two years after Idaho's law was changed to make the reduced rate available to all insurers, the Supreme Court decided Metropolitan Life Insurance Company v. Ward, 470 U.S. 869, 105 S. Ct. 1676, 84 L. Ed. 2d 751. At issue in Ward was Alabama's premium tax, which taxed foreign insurance companies at either 3 or 4% (depending on the type of insurance sold) but taxed all domestic companies at 1%. A domestic insurer was defined as a company incorporated and having its principal office in Alabama. Foreign companies could reduce their tax rate by investing prescribed percentages of their worldwide assets in specified Alabama assets and securities, but could never bring their rate down to the level applied to domestic insurers. Domestic insurers were entitled to the 1% rate even if they had no investments in Alabama.

Alabama successfully argued in state court that the disparate premium tax classification was constitutional because it bore a rational relationship

to at least two legitimate purposes other than raising revenue: “(1) encouraging the formation of new insurance companies in Alabama, and (2) encouraging capital investment by foreign insurance companies in the Alabama assets and governmental securities set forth in the statute.” Metropolitan Life Insurance Company v. Ward, 470 U.S. at 873, 105 S. Ct. at 1679. On appeal, the insurers stipulated that the statute was reasonably related to the two purposes, so the only issue before the Supreme Court was whether the purposes were legitimate. In a 5-4 decision, the U.S. Supreme Court reversed the state appellate court and remanded the case for further action. Applying the rational basis test, the Supreme Court concluded that neither of the two purposes was legitimate “when furthered by discrimination” and, as a result, the classification violated the Equal Protection Clause.

In light of conclusions by other courts that encouraging formation of new domestic insurers, promoting domestic investment, and similar goals are legitimate state purposes, one cannot help but wonder whether the Ward Court might have concluded that the stated purposes were legitimate, but further that the Alabama statute was not reasonably related thereto, had the parties not stipulated to the existence of a reasonable relationship. See e.g. Gallagher v. Motors Ins. Corp., 605 So. 2d 62 (encouraging the formation of new insurance companies was a legitimate state purpose). The Supreme Court’s reasoning and conclusion in Ward rested largely on the obvious discriminatory nature of Alabama’s tax framework. The Supreme Court distinguished California’s retaliatory tax at issue in Western & Southern Life Insurance Co. by noting that Alabama’s “domestic preference tax gives the ‘home team’ an advantage by burdening all foreign corporations seeking to do business within the state, no matter what they or their states do.” Metropolitan Life Insurance Company v. Ward, 470 U.S. at 878, 105 S. Ct. at 1682. It seems that, but for the stipulation, the Supreme Court could have reached the same conclusion by alternatively reasoning that the obvious discriminatory means by which Alabama sought to achieve its purposes, which purposes were legitimate, was not “reasonably related” to the state purposes.

In State v. Alabama Municipal Insurance Corporation, 730 So. 2d 107 (Alabama 1998), *rehearing denied* (1999), the Alabama Supreme Court upheld an amended premium taxation system that resulted from the United States Supreme Court’s invalidation of the previous statutory framework in Metropolitan Life Insurance Company v. Ward. As discussed above, the

United States Supreme Court in Ward held that the prior statutory scheme was an unconstitutional domestic preference because it precluded foreign insurers from achieving parity with domestic insurers and was not dependent on the manner in which Alabama insurers were treated in respective foreign states, as with a retaliatory tax. After Ward, the foreign insurance companies entered into a settlement with the state, whereby the plaintiffs dismissed their action in exchange for the legislature's redesigning the insurance premium tax system. State v. Alabama Municipal Insurance Corporation, 730 So. 2d at 108. The Alabama legislature enacted the Insurance Premium Tax Reform Act of 1993, the constitutionality of which was challenged in this case.

In calculating the appropriate premium tax amount, Alabama's 1993 act provided for an "office credit," which included incremental reductions in an insurer's tax rate for each office it operated within the state, and a "property credit," consisting of incremental reductions in an insurer's tax rate based on the amount of investment in real property the insurer had made within Alabama. The Alabama Supreme Court reversed the trial court and upheld the taxing system, concluding that the "credits" were not unconstitutionally discriminatory.

In concluding that the challenged "credits" did not violate the Equal Protection Clause, the court found that: "The tax credits employed reasonable classifications designed to reach the legitimate legislatively determined goal of encouraging investment in the state and encouraging insurers to employ Alabama citizens and to open offices in rural areas." State v. Alabama Municipal Insurance Corporation, 730 So. 2d at 112. The court found that, in the words of the Western & Southern Life court, whether the challenged tax "credits" are rationally related to these goals is "at least debatable," and that it is reasonable that the legislature would believe that these goals would be promoted by the adoption of the credits. In reaching its decision to uphold the taxing framework, the court made the following findings:

The statute in question imposes a flat premium tax rate on all insurers, foreign and domestic, without exception. The credits challenged are based on objective, clearly ascertainable criteria. Although we recognize that some companies are economically unable at this time to qualify for the credits, we must also recognize that their inability to qualify is a result of

their own business decisions and their own economic performance. . . . [T]he statute does not discriminate [by creating] classes of insurers to be treated differently from other classes. . . . “[A]ny difference of effect that may have arisen from the [statute] [brackets in original] is the result, not of discriminatory treatment, but of the unique financial situation of individual insurance company taxpayers.”

State v. Alabama Municipal Insurance Corporation, 730 So. 2d at 111 (quoting John Hancock Mutual Life Ins. Co. v. Commissioner of Revenue, 497 N.W.2d 250, 254 (Minn. 1993) (“Elimination of tax offset option was rationally related to the legitimate state goal of tax simplification [and] any difference of effect that may have arisen from the . . . amendment . . . is the result, not of discriminatory treatment, but of the unique financial situation of individual insurance company taxpayers.”). The court applied the rational basis test in reaching its conclusion that the commissioner’s application of the statute did not violate the Equal Protection Clause of the Fourteenth Amendment nor the Uniformity Clause of the Minnesota Constitution<sup>2</sup>.

Following the Ward decision, successful challenges of premium tax laws were brought in North Dakota, Michigan, and Alaska. However, unlike Idaho’s statute, in each of these cases the law at issue expressly treated foreign and domestic companies differently. For example, in Metropolitan Life v. Commissioner of Department of Insurance, 373 N.W.2d, 399 (N.D. 1985), the North Dakota Supreme Court ruled unconstitutional a law imposing a 2-1/2% premium tax on only foreign insurance companies. The state argued that the law was justified because domestic companies were subject to the state income tax. Evidence was produced, however, showing that the different treatment resulted in foreign companies paying a much higher tax rate than domestic companies. Similar to the conclusion of the Supreme Court in Ward, the court found that none of the purposes advanced by the state in support of the statute, including promotion of the domestic insurance industry and encouragement of capital investment in the state, were legitimate purposes when advanced by discrimination.

In Penn Mutual Life Ins. Co. v. Dept. of Licensing & Regulation, 412 N.W.2d 668 (Mich. Ct. App. 1987), Michigan’s premium tax on foreign insurers was ruled to be unconstitutional. Like North Dakota, Michigan imposed

a 2 or 3% premium tax on foreign insurers, but not on domestic insurers. Domestic insurers were required to pay a "single business tax." The effect of this tax system was to impose a greater tax burden on foreign insurers. The court found the purpose asserted by the state to be legitimate (increasing the availability of certain types of insurance), but concluded the different treatment afforded foreign companies was not rationally related to achieving the purpose.

Alaska's premium tax statute imposing tax on foreign insurers at double the rate applied to domestic companies was ruled unconstitutional in Principal Mutual Life Insurance Co. v. Division of Insurance, 780 P.2d 1023 (Alaska 1989). The Alaska Supreme Court found that the purposes asserted by the state in support of the higher rate for foreign insurers were either not legitimate, or there was no evidence to support that they were advanced by the state's classification system.

A notable departure from this line of cases is Gallagher v. Motors Ins. Corp. In Gallagher, the Florida Supreme Court upheld a premium tax law that exempted insurance companies that were organized under Florida law, maintained their home offices in Florida, and maintained their records and assets in Florida. The law also granted a 50% reduction in tax to foreign insurers that elected to own and maintain a regional home office in Florida and to keep therein certain records of their activities within the state. The state argued that the purpose of the law was to acquire a greater degree of regulatory control over insurance companies. The trial court found that this was a legitimate state purpose, and further found that "the legislature could have believed" that the different tax treatment would have the effect of causing a company to change its state of domicile and therefore increase the state's ability to regulate such companies. The Florida Supreme Court found the trial court's findings to be supported by competent substantial evidence, and upheld the trial court's ruling that the tax was constitutional.

The Gallagher court noted that although the regulatory goal was not set forth in the statute, the statute incorporated regulatory requirements set forth elsewhere and, "an intent to gain regulatory control was discernible from the statutory scheme itself." The record supported the conclusion that Florida had more control and regulatory influence over a domestic insurer than over a foreign insurer and that Florida would be in a better position to

protect the interests of Florida policyholders in the event of an insurer's financial instability if the insurer were domiciled in Florida. The court did not believe that taxing foreign insurers at a higher rate than domestics in order to gain greater regulatory control was the type of discrimination that the Equal Protection Clause was intended to prevent. It went on to say, "[a] rational relationship exists where, as here, it is found that the legislature rationally could have believed that the challenged statutory scheme in fact would promote the asserted legislative objective. Whether the statutory scheme in fact would promote the legislative objective is not dispositive."

**B. Analysis of Idaho's Reduced Rate Statute**

As discussed above in section 2.B., the reduced rate statute would most likely be reviewed under the rational basis test. Recognizing that a statute is presumed to be constitutional, if the reduced rate is challenged, a court might require the state to show that the tax is rationally related to a legitimate state purpose. The state might point to the following as a legitimate state purpose advanced by the statute: encouraging foreign companies to redomesticate to Idaho, heightening regulatory control over companies by having more assets in Idaho and therefore more security in the case of financial problems, encouraging in-state investment for the general welfare of the state, and encouraging greater service and commitment to Idaho insureds by their insurers by virtue of greater investments and contact with this state.

In making the showing of a rational relationship to a legitimate state purpose, the state should not be limited to the facts considered by a legislative committee or any express purpose. The Supreme Judicial Court of Massachusetts in Prudential Ins. Co. of America v. Commissioner of Revenue, stated that it is irrelevant for constitutional analysis whether a reason for legislation advanced on appeal is the same reason that motivated the legislature. Similarly, the United States Supreme Court has stated that when there is a "plausible" reason for a statute, it is "constitutionally irrelevant whether this reasoning in fact underlay the legislative decision." United States R.R. Retirement Board v. Fritz, 449 U.S. 166, 178-79, 101 S. Ct. 453, 461, 66 L. Ed. 2d 368 (1980) (*quoting Fleming v. Nestor*, 363 U.S. 603, 612, 80 S. Ct. 1367, 1373, 4 L. Ed. 2d 1435 (1960)). In School Dist. No. 25 v. State Tax Comm'n, 101 Idaho 283, 290, 612 P.2d 126 (1980), where the Idaho Supreme Court reversed the district court and determined that a tax statute

was not unconstitutional, the court used different language to express the same conclusion: "Every reasonable presumption must be indulged in favor of the constitutionality of an enactment." The Idaho Supreme Court recently confirmed that: "A legislative choice is not subject to courtroom fact-finding and may be based on rational speculation unsupported by evidence or empirical data.'" V-1 Oil Company v. Idaho State Tax Comm'n, Opinion No. 75 (Aug. 1, 2000) (quoting F.C.C. v. Beach Communications, Inc. 508 U.S. 307, 315 (1993)).

Idaho Code § 41-403 affords a reduced tax rate to insurers who invest 25% of their total assets in enumerated Idaho investments. (See Idaho Code § 41-403 quoted above). Accordingly, the classification made by the statute is not based on foreign versus domestic insurers, but rather those insurers that invest the requisite portion of assets in the permissible Idaho investments.

Although a state may enact laws with the purpose and effect of encouraging domestic industry, "a State may not constitutionally impose a discriminatory burden upon the business of other States, merely to protect and promote local business." Metropolitan Life Insurance Company v. Ward, 470 U.S. 887, 105 S. Ct. 1681, n.6. Despite this rule, it appears that the majority of courts have concluded that promotion of local economic development and investment, described in a variety of manners, is a legitimate state purpose. The conclusion in Ward to the contrary appears limited to the circumstance where the discriminatory effect is pervasive and blatant. Regarding the determination that there was no legitimate purpose behind the statute, the Ward decision should also be read in light of the fact that the court was hamstrung by the parties' stipulation that the statute was reasonably related to the state's purposes.

A prior version of Idaho's reduced rate tax, though not challenged using the same theories as might be relied upon today, was upheld by the Idaho Supreme Court in Idaho Compensation Co. v. Hubbard, 70 Idaho 59, 211 P.2d 413 (1949). In Idaho Compensation Co., the insurer, an Idaho domestic company, had been paying premium tax at the rate of 1%, which amount of tax had been accepted by the commissioner for several years. For tax years 1945 and 1946, the Idaho Commissioner<sup>3</sup> of Insurance required, and Idaho Compensation Co. paid tax at the rate of 3%. The company brought an action for declaratory judgment construing the applicable statute, Idaho Code

section 41-808 then in effect, and for a refund of the taxes paid in excess of 1%. The commissioner took the position that the complaint, even if true, failed to state a claim for relief. The trial court found in favor of the company, and the commissioner appealed. On appeal, the Idaho Supreme Court reversed the trial court and ruled in favor of the commissioner, confirming his imposition of the higher tax rate.

In so ruling, the court quoted from the applicable code section, 41-808:

Any insurance company transacting business in this state having more than fifty per cent of its assets invested in bonds or warrants of this state... or in taxable property within this state, or in first mortgages upon improved, unencumbered real estate within this state, shall pay a tax of one per cent upon the premiums collected in this state on risks located in this state, in lieu of the tax provided in the preceding sections.

Idaho Compensation Co., 70 Idaho at 61. This quoted section is a precursor to the current reduced rate statute, Idaho Code § 41-403.

The court in Idaho Compensation Co. concluded that the company did not have more than 50% of its assets invested in qualifying investments. The bulk of the company's investments was in U.S. bonds that, in the commissioner's opinion, did not qualify as a permissible investment for purposes of obtaining the reduced 1% tax rate. One of the company's contentions was that the statute unfairly discriminated against, not the insurer, but, rather, U.S. bonds. The company asserted that the statute's failure to recognize U.S. bonds as a permissible investment for the reduced tax rate amounted to an effective indirect tax against the bonds. The Idaho Supreme Court held that, "the classifications made [by not including U.S. bonds within the scope of recognized investments for purposes of satisfying the applicable version of the reduced rate tax] were clearly a reasonable exercise of legislative judgment and discretion . . . ." Idaho Compensation Co., 70 Idaho at 64, 211 P.2d at 416.

This holding in Idaho Compensation Co. may not be enough to defeat a constitutional challenge. First and foremost, the issue that might be presented in the future, a potential challenge based on unconstitutional discrimination against foreign insurers in favor of domestics, was not presented to the court. The Idaho Supreme Court has long held the view that it will not address issues not raised by the parties or argued. Taylor v. Browning, 129 Idaho 483, 927 P.2d 873 (1996). Second, the statutory language and the realities of the market are different today, fifty years later. Third, the courts have continued to refine the standards and analyses based on intervening case law. Therefore, it would be unwise to conclude that the reduced rate statute will withstand constitutional challenge simply based on Idaho Compensation Co., despite the fact that the case can only help support a position defending the constitutionality of the statute.

Because Idaho's reduced rate statute does not expressly differentiate between foreign and domestic insurers, it probably would not be found unconstitutional pursuant to Metropolitan Life Ins. Co. v. Ward. However, at the present time, only domestic insurers are taking advantage of the reduced rate, although at least one foreign insurer has qualified since 1988. As a result, it is possible a court might conclude that, although neutral on its face, the effect of the law is to provide an improper advantage to domestic insurers.

Though the language of the statute may pass constitutional muster, there is still a risk that a court might determine that the effect of the statute is not rationally related to achieving the stated goal. Insurers may argue that the proportion of assets/reserves required to be invested in Idaho to obtain the reduced rate, 25% of the total, is unreasonable, and this fact indicates an improper discriminatory motive or negates any rational relation between the reduced tax statute and the state purpose(s). Foreign insurers could argue that this level of investment is impractical or essentially impossible, especially given the relative size of Idaho compared to the economies of large states such as California, Florida, New York and Texas. While no recent reported premium tax cases have been located which specifically address the issue of a constitutional challenge to a reduced rate tax statute based on investments as applied, there is some authority to support a claim of unconstitutionality.

The United States Supreme Court held in Bethlehem Motors Corp. v. Flynt, 256 U.S. 421, 41 S. Ct. 571, 65 L. Ed. 1029 (1921), that a licensing tax statute that imposed only 20% of the regular tax amount upon companies that had submitted a sworn statement to the effect that three-fourths of the manufacturer's entire assets were invested in bonds or property of North Carolina was unconstitutional. The local sheriffs levied on vehicles owned by non-resident vehicle manufacturers in order to satisfy their full-rate tax obligations. The vehicle manufacturers sought a preliminary injunction to bar the sale, which injunction was initially granted, and then dissolved. The North Carolina Supreme Court affirmed the order dissolving the restraining order "thereby sustaining the license tax and the levy upon the automobiles made to enforce it." The Supreme Court noted that the act did not facially delineate between foreign and domestic manufacturers; however, the challenging manufacturers asserted that the provision was so onerous as to constitute illegal discrimination because only domestic manufacturers could qualify. The state argued that a foreign manufacturer could satisfy the condition just as easily as a domestic company. In reply, the Supreme Court stated:

To this we cannot assent. The condition can be satisfied by a resident manufacturer, his factory and its products in the first instance being within the state; it cannot be satisfied by a nonresident manufacturer, his factory necessarily being in another state, some of its products only at a given time being within the state. Therefore, there is a real discrimination, and an offense against the Fourteenth Amendment, if we assume that the corporations are within the state.

Bethlehem Motors Corp. v. Flynt, 256 U.S. at 426, 41 S. Ct. at 573.

Insurers may claim that the effect of the reduced rate law is not rationally related to achieving goals or purposes of the statute. Insurers challenging the reduced rate statute might assert that the purpose is revenue shifting from qualifying domestic companies to foreign companies.

Large insurers might argue that the reduced rate tax unfairly discriminates against them because it may be more difficult to invest 25% of their large amount of assets in Idaho, as compared to smaller insurers. The inverse of this argument was made in State v. Alabama Municipal Insurance

Corporation. In that case, the trial court found that the tax credits unfairly discriminated against smaller insurers because the tax credits increased incrementally based on the number of offices and employees located in Alabama. The Alabama Supreme Court rejected this argument, however, noting that an insurer's inability to take advantage of the credit "is a result of [its] own business decisions and [its] own economic performance." 730 So. 2d at 111 (*see full quote above*). As noted in footnote 2 above and discussed previously, however, there is other authority to support a potential argument by insurers that the effect of the statute is discriminatory.

For these reasons, foreign insurers might argue that the statute, though not facially discriminatory, is impermissibly discriminatory in its effect. It is impossible to give any meaningful prediction as to how a given court will decide the issue of whether the statute is unconstitutional in its effect.

C. Potential Challenge To Combined Effect of Reduced Rate Statute & Retaliatory Tax Statute

Foreign insurers may assert that the fact that the retaliatory tax statute will still be applied, even if a foreign insurer meets the criteria of the reduced rate statute, further establishes either the illegitimacy of the purpose of the reduced rate statute, or the lack of any rational relationship between the classification or distinction made by the statute and the purpose(s). The argument might be that given the retaliatory tax, foreign companies' motivation to invest in Idaho would be stymied by the effective superiority of the retaliatory tax. If a given foreign insurer's domiciliary state imposes higher taxes than the reduced rate, that foreign insurer will not receive the benefit of the reduced rate statute, even if the insurer satisfies the prerequisites thereof. This fact, a challenger might argue, shows that the reduced rate tax is not rationally related to achieving any legitimate purpose(s), or, alternatively, the purpose(s) is not legitimate because it constitutes in reality the improper shifting of a revenue raising burden to foreign companies. It might also be argued that the statute is not a rational means of encouraging Idaho investment because it only encourages investment by foreign insurers whose home states impose tax rates significantly lower than Idaho's regular rate.

One straightforward response to such an argument is that, presuming both statutes are valid, one of them must control. In effect, the Idaho Legislature has determined that of the two possible adjustments to the base rate, the retaliatory tax is of paramount importance. The fact that the legislature placed a greater weight on the retaliatory tax than on the reduced rate simply evidences the greater importance the legislature placed on promoting fair and equal treatment of Idaho insurers by other states.

In Board of Insurance Comm'rs v. Prudential Fire Insurance Co., 167 S.W.2d 578 (Ct. Civ. App. Tex. 1942), *rehearing denied* (1943), the court affirmed a judgment in favor of the insurer against the insurance regulator for taxes paid under protest. In this case the regulator unsuccessfully argued that the retaliatory tax law effectively trumped the reduced rate law. At that time, Texas imposed a base premium tax rate of 4.05% but imposed a reduced rate of 1.5% upon any insurer investing one-fourth of its entire assets in Texas. Oklahoma did not have a reduced rate; it simply had a flat 4.0% rate. The Oklahoma insurer qualified for the reduced rate in Texas and paid the reduced rate tax computed at 1.5%. However, the Texas regulator determined that Oklahoma charged a higher rate because it would not recognize a reduced rate even if a Texas insurer invested one-fourth of its assets in Oklahoma. Therefore, Texas concluded that application of the retaliatory law required that the Oklahoma insurer pay an additional 2.5% of tax (difference between the 1.5% reduced rate already paid and the 4.0% Oklahoma rate). The Oklahoma insurer paid this under protest, sued for this amount and prevailed in the trial court and on appeal.

While the issue of the constitutionality of the applicable Texas premium tax statutes was never addressed in Board of Insurance Comm'rs v. Prudential Fire Insurance Co., the case is of some use to the analysis. The nature of the court's review was to merely construe how the retaliatory tax statute should be applied. In reaching its conclusion, the court addressed its view of what the purpose of the reduced tax statute was. The court stated:

This optional provision for investment of assets rather than pay the higher tax is necessarily a finding by the Legislature that it regarded the payment of the 1 fi% on gross receipts plus the investment of 25% of assets in Texas property as being equivalent to the higher rate of 4.05% on gross receipts

required of all corporations, domestic or foreign, which do not desire to make the investment in Texas property. To hold otherwise would convict the Legislature of requiring a larger occupation tax of corporations, both foreign and domestic, not making the investment in Texas property than it required of those making the investment. No specific reason is stated in the statute for the right to pay the lower tax, but . . . no doubt the Legislature thought that a compliance with the option to invest assets in Texas property would make this valuable property subject to taxation and that in view of such additional taxation it was but just to reduce their occupation tax. In addition the Legislature no doubt thought that the investment of the assets of insurance companies, both foreign and domestic . . . would help to furnish a large and needed market for such securities . . . .

Board of Insurance Comm'rs v. Prudential Fire Insurance Co., 167 S.W.2d at 579. The court held that because the premium tax law "provides that the payment of the 1 fl% rate on gross receipts plus the investment in Texas property requirement is equivalent to the payment of the higher 4.05% flat rate; and since such flat rate is higher than the 4% flat rate levied by the Oklahoma statute, the provisions of [the] retaliatory tax statute, do not apply." *Id.* at 579-80.

It is clear that the Texas court in Board of Insurance Comm'rs v. Prudential Fire Insurance Co. concluded that the primary reason for the reduced rate was the legislature's view that the lower rate combined with other tax presumably paid on the invested property would constitute an equivalent amount of tax. Despite the fact that the Texas court did not address the constitutionality of the applicable statutes, it should not go unnoticed that the court modified the application of the retaliatory law as calculated in conjunction with the reduced rate tax by concluding that, under the facts presented, the foreign insurer, who had paid out of pocket only the reduced rate taxes, had effectively paid the higher base rate so as to preclude collection of the difference between the reduced rate and the insurer's domestic rate.

In this office's opinion, the most obvious reason for permitting a reduced rate, such as Idaho Code § 41-403, is not to serve as an alternative

mechanism to pay the same amount of tax. Achieving such parity would be speculative and likely inexact given the various types of qualifying investments and the fact that the 25% limit is a minimum or floor proportion. Rather, the primary goals seem to be economic stimulation and greater potential regulatory control, or variations thereof.

The lack of an unequivocal conclusion regarding the constitutionality of the effect of Idaho Code § 41-403, as applied in concert with Idaho Code § 41-340, is based on the potential that a court could find practical discrimination, despite the facial neutrality of the reduced rate statute. Since 1983, the language of Idaho Code § 41-403 has applied equally to foreign and domestic companies, yet foreign companies might be able to convince a court that the statute is unfairly discriminatory against foreign companies and not reasonably related to a legitimate state purpose. Based on the circumstances and relatively recent court decisions, any definite opinion regarding the constitutionality of the reduced rate statute, as applied in relation to the retaliatory tax statute, would be imprudent.

### CONCLUSION

Any Commerce Clause challenge to Idaho's premium tax statutes will fail because the Commerce Clause does not apply to the states' regulation and taxation of insurance.

Courts will likely use the equal protection rational basis test in analyzing any potential constitutional challenge to the premium tax statutes grounded on the equal protection clauses of the United States and Idaho constitutions, substantive due process, or the uniformity clause of the Idaho Constitution. Under this test, a statute, which is presumed to be constitutional, will be struck down only if it is determined that the classification made by the law is not supported by a legitimate state purpose or if the classification is not reasonably related to achieving the otherwise legitimate state goal. Idaho's statutes addressing premium tax rates are not facially unconstitutional under an equal protection analysis by virtue of effecting express discrimination against foreign insurers.

The retaliatory tax statute seems to be well within the scope of permissible legislative regulation. Regarding Idaho's reduced rate statute, stand-

ing alone, or its combined effect with the retaliatory tax, several state goals or purposes can be proffered in an effort to defeat any potential prospective constitutional challenge. Uncertainty lies in whether any given court will find that the potential reasons for the reduced rate statute constitute legitimate state purposes and, assuming legitimacy, whether the statute is reasonably related to achieving those purposes. As is apparent from the case law, the judges and courts that have wrestled with these issues have not been of one mind. Many cases have been reversed on appeal, and many appellate decisions have flowed from closely split courts. In light of the premium tax and equal protection jurisprudence, any effort to predict how a potential Idaho or federal court would rule would be presumptuous and risk misleading the reader. Therefore, this office expresses no opinion on the constitutionality of the reduced rate statute, standing alone or as applied with the retaliatory tax.

### AUTHORITIES CONSIDERED

**1. United States Constitution:**

Art. 1, § 8.  
Amend. 14, § 1.

**2. Idaho Constitution:**

Art. 1, sec. 2.  
Art. 7, sec. 5.

**3. Idaho Code:**

§ 41-340.  
§ 41-402.  
§ 41-403.

**4. Idaho Cases:**

Bon Appetit Gourmet Foods, Inc. v. State Dept. of Employment, 117 Idaho 1002, 793 P.2d 675 (1989), *addendum on rehearing* (1990).

Idaho Compensation Co. v. Hubbard, 70 Idaho 59, 211 P.2d 413 (1949).

Jones v. State Bd. Of Medicine, 97 Idaho 859, 555 P.2d 399 (1976).

Justus v. Board of Equalization, 101 Idaho 743, 620 P.2d 777 (1980).

Meisner v. Potlatch Corp., 131 Idaho 258, 954 P.2d 676 (1998).

Olsen v. J.A. Freeman Co., 117 Idaho 706, 791 P.2d 1285 (1990).

Packard v. Joint School Dist. No. 171, 104 Idaho 604, 661 P.2d 770 (Ct. App. 1983).

School Dist. No. 25 v. State Tax Comm'n, 101 Idaho 283, 290, 612 P.2d 126 (1980).

State v. Reed, 107 Idaho 162, 686 P.2d 842 (Ct. App. 1984).

Sterling H. Nelson & Sons, Inc. v. Bender, 95 Idaho 813, 520 P.2d 860 (1974).

Taylor v. Browning, 129 Idaho 483, 927 P.2d 873 (1996).

V-1 Oil Company v. Idaho State Tax Comm'n, Opinion No. 75 (Aug. 1, 2000).

**5. Federal Cases:**

Bethlehem Motors Corp. v. Flynt, 256 U.S. 421, 41 S. Ct. 571, 65 L. Ed. 1029 (1921).

Metropolitan Life Insurance Company v. Ward, 470 U.S. 869, 881, 105 S. Ct. 1676, 1683, 84 L. Ed. 2d 751 (1985).

Western & Southern Life Insurance Co. v. State Bd. of Equalization of Cal., 451 U.S. 648, 101 S. Ct. 2070, 68 L. Ed. 2d 514 (1981).

United States R.R. Retirement Board v. Fritz, 449 U.S. 166, 178-79, 101 S. Ct. 453, 461, 66 L. Ed. 2d 368 (1980).

**6. Other Cases:**

American Southern v. State Dept. of Revenue, 674 So. 2d 810 (Fla. Dist. Ct. App. 1996).

Board of Insurance Comm'rs v. Prudential Fire Insurance Co., 167 S.W.2d 578 (Ct. Civ. App. Tex. 1942), rehearing denied (1943).

Executive Life Insurance Company v. Commonwealth, 606 A.2d 1282 (Pa. 1992).

Gallagher v. Motors Insurance Corp., 605 So. 2d 62 (Fla. 1992), *cert. dismissed* 506 U.S. 1074, 113 S. Ct. 1036, 122 L. Ed. 2d 179 (1993).

John Hancock Mutual Life Ins. Co. v. Commissioner of Revenue, 497 N.W.2d 250 (Minn. 1993).

Metropolitan Life v. Commissioner of Department of Insurance, 373 N.W.2d, 399 (N.D. 1985).

Penn Mutual Life Ins. Co. v. Dept. of Licensing & Regulation, 412 N.W.2d 668 (Mich. Ct. App. 1987).

Principal Mutual Life Insurance Co. v. Division of Insurance, 780 P.2d 1023 (Alaska 1989).

Prudential Ins. Co. of America v. Commissioner of Revenue, 709 N.E.2d 1096 (Mass. 1999).

Republic Insurance Company v. Commissioner of Taxation, 138 N.W.2d 776 (Minn. 1965).

State v. Alabama Municipal Insurance Corporation, 730 So. 2d 107 (Alabama 1998), *rehearing denied* (1999).

Dated this 21st day of September, 2000

ALAN G. LANCE  
Attorney General

**Analysis by:**

Thomas A. Donovan  
Wm. A. von Tagen  
Deputy Attorneys General  
Intergovernmental & Fiscal Law Division

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<sup>1</sup>The Commerce Clause was the basis of the Fourth Judicial District Court's February 22, 2000 decision that the limited commodities use fee at Idaho Code § 49-434(9) was unconstitutional in American Trucking Associations, Inc. v. Idaho Transportation Department, CV OC 9700724D.

<sup>2</sup>Other courts have cast doubt on the justification that an insurer is truly free to make its own investment decisions: "... it is not an answer to say that the Texas law is nondiscriminatory [for purposes of determining whether to apply the retaliatory tax – not used in the constitutional equal protection context] because an out-of-state company may adjust its investment portfolio so as to avail itself of equal treatment under the Texas law. This observation ignores the realities of the insurance business. It should require no statistics to demonstrate that the Texas statute operates to the advantage of domiciliary insurance companies. When a company organizes and begins business, its home state obviously becomes its major market. Its volume, surplus, and physical plant are developed in the local market and it can be expected that it will invest largely in local securities and property." Republic Insurance Company v. Commissioner of Taxation, 138 N.W.2d 776 (Minn. 1965). There was no constitutional question posed in Republic Insurance Company. The only issue before the court was whether the graduated reduced rate schedule in Texas law would forgo imposition of the higher Texas rate of 3.85% versus the Minnesota rate of 2% pursuant to the Minnesota retaliatory law. The board of tax appeals concluded that because the Texas insurers qualified for the lower rate in Texas of 1.1% based on investment in Texas securities, and other Minnesota companies had so qualified in Texas, it should not apply the higher Texas rate based on the retaliatory law. In reversing the board, the Republic Insurance Company court used the Texas decision in Board of Insurance Comm'rs v. Prudential Fire Insurance Co., 167 S.W.2d 578 (Ct. Civ. App. Tex. 1942) rehearing denied (1943), which had determined that the Texas graduated rate was in effect the full 3.85% rate (due to the fact that the other Texas investments would be subject to some tax), and therefore applied that rate to the Texas insurers. See also Bethlehem Motors Corp. v. Flynt, 256 U.S. 421, 41 S. Ct. 571, 65 L. Ed. 1029 (1921), discussed below.

<sup>3</sup>Per amendments to the code in 1974, the "commissioner" became the "director." See Idaho Code §§ 41-202, 41-203.

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**ATTORNEY GENERAL'S  
SELECTED  
INFORMAL GUIDELINES  
FOR THE YEAR 2000**

**ALAN G. LANCE**  
ATTORNEY GENERAL  
STATE OF IDAHO



## INFORMAL GUIDELINES OF THE ATTORNEY GENERAL

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February 16, 2000

The Honorable Douglas R. Jones  
House of Representatives  
STATEHOUSE MAIL

### **THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE**

Dear Representative Jones:

You have asked the Attorney General's Office to provide legal guidance regarding the Idaho State Department of Agriculture's (ISDA) statutory authority to allow a dairyman, whose permit to sell milk for human consumption is temporarily revoked, to donate the forfeited proceeds from the sale of such milk to a charity of his choice. Specifically, you asked:

May I please have an opinion on the Department of Agriculture policy of fining a dairy operation and then letting the dairy determine a charity to receive the money. Please explain the statutory authorization for this practice.

Our conclusion is that the governing statutes do not specifically address this practice. However, it is also our conclusion that the ISDA may, under certain conditions, enter into a consent agreement with a dairyman that allows for the donation of forfeited funds to a charitable organization. ISDA may not, however, allow a dairyman to determine which charitable organization receives such funds.

### **BACKGROUND**

Your question focuses on the ISDA's authority to impose penalties upon a dairy that is not in compliance with applicable standards of sanitation or any other law of this state. Chapter 4 of title 37 of the Idaho Code governs the sanitary inspection of dairies as well as the issuance of permits allowing the sale of milk for human consumption. This statute also governs the revocation of such permits. Your question concerns those situations in which the inspected dairy products comply with statutory and regulatory standards, but

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the sanitary conditions of the dairy facility itself do not. Therefore, we focus only on the provisions of the statute governing violations of sanitary condition requirements.

### ANALYSIS

Idaho Code § 37-401 authorizes the ISDA to inspect the sanitary conditions of facilities producing dairy products intended for human consumption. Idaho Code § 37-401 states:

The director of the department of agriculture is hereby authorized and directed to . . . make sanitary inspection of . . . containers, utensils, equipment, buildings, premises or anything whatsoever employed in the production, handling, storing, processing or manufacturing of dairy products or that would affect the purity of the products. Inspections, examinations and tests shall be made to meet the requirements of the laws of the state and of the United States for the sale of the products or their transportation in both intrastate and interstate commerce. . . . The director or agent shall issue a permit authorizing the sale of milk for human consumption to all dairy farms that meet the requirements of this chapter, and rules promulgated pursuant to this chapter.

Section 37-401 places an affirmative duty upon the ISDA to inspect dairies and to issue a permit authorizing the sale of milk for human consumption to dairy facilities that are in full compliance with state and federal law.

Idaho Code § 37-403 requires the ISDA to issue a report of its findings and conclusions upon inspection of dairy farms, including dairy waste systems. This section states:

Whenever, under any law of this state, the director of the department of agriculture or any agent is required to inspect dairy farms and dairy waste systems for compliance with rules prescribed by the department, or determine the sanitary condition of anything referred to in section 37-401,

## INFORMAL GUIDELINES OF THE ATTORNEY GENERAL

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Idaho Code, . . . the director shall make or cause to be made an examination and inspection and shall report his findings and conclusions.

Section 37-403 authorizes the ISDA to revoke a permit to sell milk for human consumption only upon the basis of a written report. Idaho Code § 37-403 states:

When the issuance or the revoking of any license or permit by the department of agriculture is required to be made after an inspection . . . the issuance or revocation of license or permit shall be based upon the report or reports so made by the director.

In addition, the legislature has authorized the ISDA to seek criminal prosecution and injunctive relief through the district court in the county in which a violation occurs. Idaho Code § 37-408 provides:

Anyone failing to comply with any of the provisions of this chapter or any standards, rules or orders promulgated hereunder shall be guilty of a misdemeanor and upon conviction shall be subject to a fine not exceeding two hundred dollars (\$200) or imprisonment in the county jail not to exceed three (3) months, or by both a fine and imprisonment. The director of the department of agriculture may bring civil actions to enjoin violation of this chapter or the standards, rules or orders promulgated thereunder.

In summary, when a dairyman fails to comply with statutory and regulatory standards, this statute authorizes the ISDA to do one or all of the following: (1) revoke a permit to sell milk for human consumption; (2) seek an injunction in district court; (3) request that the prosecutor in the county where the violation occurred bring criminal charges against the dairyman.

The statute does not expressly authorize the ISDA to impose sanctions other than those listed above. Thus, the ISDA cannot require a dairyman to donate forfeited proceeds from the sale of milk to a charitable organization. It is our understanding, however, that ISDA, in some instances, has

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entered into voluntary agreements whereby the forfeited funds from the sale of milk are donated to charitable organizations as an alternative to simply discarding the milk produced during the time period in which the dairymen's permits were temporarily revoked.

In principle, this practice is authorized by the Idaho Department of Agriculture Rules of Practice and Procedure, IDAPA 02.01.01, et seq., and the Idaho Administrative Procedure Act (APA), Idaho Code §§ 67-5201, et seq., which address the procedures for disposition of contested cases. Under the APA, a contested case is defined as any proceeding "that may result in the issuance of an order." Idaho Code § 67-5240. An "order" is an "agency action of particular applicability that determines the legal rights, duties, privileges, immunities, or other legal interests of one (1) or more specific persons." Idaho Code § 67-5201(11). Clearly, the revocation of a dairy's permit to sell milk is an agency action determining the privilege of such dairy. Therefore, when the ISDA issues a notice of intent to revoke a dairy's permit to sell milk for human consumption, the ISDA has initiated a contested case.

The ISDA Rules of Practice and Procedure and the APA control agency decisionmaking procedures in the absence of more specific statutory requirements. Pursuant to the ISDA Rules of Practice and Procedure, the ISDA has broad discretion to settle contested cases and is, in fact, encouraged to do so. IDAPA 02.01.01.302.01 states in relevant part:

These rules encourage the use of informal proceedings to settle or determine contested cases. Unless prohibited by statute, the agency may provide for the use of informal procedure at any stage of a contested case.

Under IDAPA 02.01.01.302, the ISDA may conduct informal settlement negotiations and enter into voluntary settlement agreements with violators. It is important to note, however, that a contested case is not settled until all parties agree to the terms of the settlement "in writing." IDAPA 02.01.01.302.02. This language refers to a written document that memorializes the nature of the violation and the steps the violator must take to avoid formal administrative proceedings. The written document, generally referred to as a settlement agreement, stipulation or consent order, is signed by the violator and the director of the ISDA. These settlements lead to the entry of an

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order by the director, which gives the ISDA continuing jurisdiction over the dispute and the power to enforce the agreement.

It is our understanding that the majority of administrative enforcement proceedings within the ISDA result in voluntary settlement agreements. In the course of settling enforcement actions, agencies may include voluntary undertakings in administrative consent decrees that they could not impose directly on a regulated entity. The question then is whether the ISDA, in agreeing to the terms of a voluntary consent agreement, has exceeded its statutory authority. We have found no Idaho cases dealing with this issue. However, the federal caselaw regarding agency consent agreements that implicate interests beyond those of private parties is instructive. When federal courts are required by law to approve an administrative agency consent decree, the courts generally review a proposed consent decree to ensure that it is "fair, adequate, and reasonable; that the proposed decree will not violate the Constitution, a statute, or other authority; [and] that it is consistent with the objectives of Congress." Durrett v. Housing Auth., 896 F.2d 600, 604 (1st Cir. 1990). See also, United States v. City of Alexandria, 614 F.2d 1358, 1362 (5th Cir. 1980) (consent decree proposed by a private defendant and government agency may be overcome if decree contains provisions which are unreasonable, illegal, unconstitutional, or against public policy).

Applying these standards here, ISDA has broad discretion to settle contested cases and may choose from a range of potential remedies. These settlements are lawful so long as they do not violate federal or state or constitutional principles; advance the purposes of the statutes that are the basis of the enforcement action; and evidence some connection between the penalty and the state of Idaho's interest. Thus, although the selection of administrative sanctions is vested in the agency's discretion, that discretion is limited by statute, Knight v. Dept. of Ins., 124 Idaho 645, 650, 862 P.2d 337, 342 (Ct. App. 1993), and by the standards outlined above. The ISDA may exercise its sound discretion to ensure that these standards are met.

## CONCLUSION

Although the ISDA is authorized to pursue statutory goals through informal proceedings, the agency, in so doing, must ensure that the terms of a settlement agreement do not violate state or federal constitutional princi-

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ples. The terms of a settlement agreement between the ISDA and a dairyman must also advance the purposes of chapter 4, title 37, Idaho Code, related statutes and rules. Those purposes include the protection of the public health, safety and welfare. The ISDA must exercise its administrative authority to ensure that a donation to a charitable organization adheres to both requirements. Therefore, it is our opinion that the ISDA may not allow a dairyman unfettered discretion as to which charitable organization forfeited funds are donated.

Sincerely,

Harriet Hensley  
Deputy Attorney General  
Natural Resources Division

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March 15, 2000

Harold W. Davis, President  
Idaho State Board of Education  
P.O. Box 2147  
Idaho Falls, ID 83403-2147

### **THIS CORRESPONDENCE IS A LEGAL GUIDELINE OF THE ATTORNEY GENERAL SUBMITTED FOR YOUR GUIDANCE**

Re: University Endowment Funds

Dear Mr. Davis:

This letter is in response to your request for an opinion of the Office of the Attorney General with regard to the appropriation of income from the University Endowment Funds. Your letter contains several questions which stem from a common factual background. We will first set forth the factual background and then each of your questions, with our answers, will be set forth in turn.

#### **A. Factual Background**

The State of Idaho, like all western states, received land grants from the federal government prior to or at the time of statehood. The primary purpose of these land grants was to use the proceeds of the land to support public education at the primary, secondary and postsecondary levels. As stated by the United States Supreme Court in Andrus v. Utah, 446 U.S. 500, 507, 100 S. Ct. 1803, 1807 (1980), "the United States agreed to cede some of its land to the States in exchange for a commitment by the States to use the revenues derived from the land to educate the citizenry." The historical context of such federal land grants originates in the fact that the federal government retained ownership of most of the land west of the 13 original states:

When the 13 original colonies formed the United States, each held sovereign control over the land within its borders. Those lands provided a tax base for financial governmental functions, including public education. As the United States expanded westward, additional states were created on lands

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which belonged to the United States as territories. The federal government retained ownership over much of the land within those states. Because land owned by the federal government was exempt from taxation by the states, the states had a smaller tax base for financing public education. To provide a source of revenue for public education, Congress granted new states federal lands to be used for the support of public schools.

National Parks and Conservation Association v. Board of State Lands, 869 P.2d 909, 917 (Utah 1993). At the time of Idaho's admission to the Union in 1890, more than 3.5 million acres of land were granted to Idaho by the federal government for the express purpose of benefiting public education. A majority of the land was dedicated to the public school system and the remainder constitutes specific grants for university and other higher education purposes. The specific grants for higher education purposes are found in Sections 8, 10 and 11 of the Idaho Admission Bill. 26 Stat. L. 215 ch. 656.

Upon Idaho's entry to the Union, Idaho received sections numbered 16 and 36 in every township of the state for the benefit of the public school system. This land formed the basis of the public school endowment for elementary and secondary education. In addition, other land was granted for higher educational purposes that formed the basis for the university endowments. The full quantity of 72 sections was granted for the maintenance of a land grant university (the University of Idaho), 90,000 acres of land pursuant to the Morrill Act for the maintenance of an agricultural college, 100,000 acres for the establishment and maintenance of a scientific school, 100,000 acres for the establishment and maintenance of state normal schools, and an additional 50,000 acres for the support and maintenance of the University of Idaho. Finally, 150,000 acres were granted for such other charitable, educational, penal and reformatory institutions as the state so selected<sup>1</sup>.

The stated purpose of the Idaho Admission Bill land grants was to fund the support and maintenance of public education in Idaho. The sanctity of the endowments, the manner and method of the investment of the proceeds from the land, and the use of the funds has been the subject of numerous court cases and official Opinions of the Office of the Idaho Attorney General throughout Idaho's history. The 1998 Idaho Legislature made significant changes to the Endowment Fund investment laws based upon a change to the

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Idaho Admission Bill approved by Congress and two constitutional amendments approved by the Idaho voters<sup>2</sup>. The changes to the Endowment Fund investment laws become relevant in the questions that will be addressed.

With the above background in mind, we now turn to the questions you have presented<sup>3</sup>.

**B. Question 1: “Under Black and the related cases, Attorney General’s Opinion 76-85, the provisions of the Idaho Admission Bill and Idaho Constitution, may the Legislature legally limit the spending authority for the income from such endowment funds by not appropriating that money to the colleges and universities?”**

This is a question upon which the Idaho Attorney General’s Office has already opined and upon which the Idaho Supreme Court has already ruled.

In the case of Melgard v. Eagleson, 31 Idaho 411, 172 P.655 (1918), the Idaho Supreme Court decided the question of whether funds distributed pursuant to federal endowments for the maintenance of designated colleges could be considered part of the general fund of the State of Idaho. The Idaho Supreme Court ruled that:

It is apparent that the fund in question cannot properly be placed in the general fund of the State of Idaho. The exclusive supervision of the fund is vested by the act of Congress in the trustees of the institution designated by the state legislature as the beneficiary entitled to receive the fund. Under the acts of Congress, the state treasurer . . . [has] a mere clerical or ministerial duty to perform, that is, to pay over the fund immediately to the treasurer of the board of trustees, in this case the board of regents, upon their order. The acts of the [state treasurer and state auditor], in this instance, of placing this fund in the general fund by making appropriate entries upon their books to that end were mere nullities. Under the acts of Congress in question, the state auditor has no duty whatever to perform with respect to this fund and no authority over it. It is therefore apparent that the

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[state treasurer] has but one duty to perform in the premises, and that is to pay over the sum in controversy immediately to the [university].

31 Idaho at 414-15, 172 P. at 656. This case settled that funds distributed pursuant to the Morrill Act are required to be paid immediately to the state board of education<sup>4</sup> without control by the state treasurer or state auditor (now state controller).

In Evans v. Van Deusen, 31 Idaho 614, 174 P.122 (1918), the issue the court decided was whether the state was required to separately account for the income of the endowments and whether such income was properly appropriated to the university. In this case, the then state auditor was holding certain endowment income because the auditor's office was concerned that there was no actual appropriation by the legislature of such funds to the university. The Idaho Supreme Court held that endowment funds required no such appropriation. The court stated that the funds were "declared by the Constitution to be trust funds, [and] are not, strictly speaking, subject to appropriation. They were appropriated or set apart for certain purposes designated by the terms of the [endowment land] grants which had been accepted by the state." 31 Idaho at 620, 174 P. at 122 (emphasis added). Thus, the income from the endowments is not subject to appropriation by the legislature as such money is already set aside to the universities based on the grants from Congress.

Finally, in the case you mentioned in your question, Black v. State Board of Education, 33 Idaho 415, 196 P.201 (1921), the Idaho Supreme Court further discussed the appropriation concern. The court stated that:

[T]he proceeds of federal land grants, direct federal appropriations and private donations to the university, are trust funds, and are not subject to the constitutional provision that money must be appropriated before it is paid out of the state treasury. Claims against such funds need not be passed upon by the board of examiners, and the moneys in such funds may be expended by the board of regents subject only to the conditions and limitations provided for in the acts of Congress making such grants and appropriations, or the conditions imposed by the donors upon the donations.

33 Idaho at 427, 196 P. at 201 (emphasis added).

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The issue was again presented in 1976 when the administrator of the division of budget (predecessor to the current division of financial management) requested an opinion of the Attorney General regarding whether the income from endowments must be "allotted" as required by law and whether the approval of the auditor (now controller) or state board of examiners was required prior to certain expenditures of such income. This office issued Opinion No. 76-65 concluding that the allotment process and expenditure approvals were not required for expenditure of funds from the endowments. The Opinion explained that while such funds were "listed in the appropriation bill to the State Board of Education, that this listing of funds in the appropriation bill is not an actual 'appropriation.' Rather, it is a mere listing of fund sources which the Legislature includes on the appropriation bill to determine the amount of the appropriation." 1976 Idaho Att'y Gen. Ann. Rpt. 280 (citation omitted). In other words, while the legislature may list this money in an annual appropriation, the university Endowment Fund income is not actually appropriated by such bill because it is already "appropriated" by the acts of Congress that require such income to be distributed to the universities.

It is worthy of note that the legislature apparently has recognized this long standing conclusion with the Standard Budget Act of 1945, codified as part of chapter 36, title 67, Idaho Code. Idaho Code §§ 67-3608 and 67-3609 exempt money from the university endowments and federal land grants from the requirement that monies obtained by the universities be deposited in particular accounts and appropriated back to the institutions<sup>5</sup>.

Thus, the legislature may not limit the spending authority for the income from the university land endowments by simply not appropriating that money to the colleges and universities. The primary reason is that all income from the university endowments is already "appropriated" to the colleges and universities as required under the terms of the congressional land grants.

This conclusion follows a long history of legislative encroachment upon the university endowment funds. Throughout Idaho's history, the education endowments have been considered inviolate trusts. The constitutional framers first coined the phrase "sacred" when they debated the constitutional provisions regarding the endowments and stated that "perhaps there is no other fund so sacred." Idaho Constitutional Convention Proceedings, Vol. I at 647. The Idaho Supreme Court has adopted the sacred trust terminology and has called the several endowments "a trust of the most sacred and high-

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est order.” Moon v. State Board of Examiners, 104 Idaho 640, 642, 662 P.2d 221 (1983).

In 1905, the Idaho Supreme Court called attention to legislative encroachment upon the university endowment funds. In Roach v. Gooding, 11 Idaho 244, 81 P. 642 (1905), the court stopped the legislature from appropriating endowment income for the payment of bonds by concluding that “the legislature had no power or authority to appropriate or set apart for the payment of the interest or principal of the bonds. . . .” 81 P. at 646. However, in addition to the conclusion, the court noted that “it is shown by several acts passed by the legislature of the state during the pasts several years that an effort has been made to appropriate not only the interest and income of the permanent school fund, but a part of the fund itself. . . .” *Id.* The court, in ruling such action “unconstitutional and void” stated that the legislative “tendency has been to encroach upon the public school fund, and divert it from purposes for which it was created.” *Id.*

In fact, earlier in 1897, the Idaho Supreme Court had made the inviolate nature of the endowment fund, and its income, very clear. The court, in holding the legislature was without power to pass laws that would impede the right to foreclose on loans made from the endowment funds, stated that the legislative act:

would deplete the permanent school fund, in violation of both the act admitting Idaho as a state, and . . . the constitution which declares that said public school fund shall remain inviolate and intact, and that the interest thereon only shall be expended in the maintenance of the public schools of the state. The people . . . have thus declared for what purposes all interest on the permanent fund shall be applied. . . . Any law enacted by the Legislature diverting one dollar of principal or interest of said fund to other purposes would be unconstitutional.

State v. Fitzpatrick, 5 Idaho 499, 51 P.112, 114 (1897). Following these cases came Melgard v. Eagleson, Evans v. Van Deusen, and Black v. State Board of Education, all cited above, in which the Idaho Supreme Court held that the legislature’s power did not extend to appropriating the income from the university endowments.

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In 1939, the Federal District Court for Idaho, in holding a statute of limitations inapplicable to endowment loans, stated that the funds must remain forever inviolate and that any statute enacted by the legislature putting time limits on collecting endowment funds was void. United States v. Fenton, 27 F. Supp. 816 (D. Idaho 1939). The Idaho Supreme Court also struck legislative enactments regarding the investment of the permanent endowment funds as such investments could not provide the type of inviolate guarantee required in investing endowment funds. Engelking v. Investment Board, 93 Idaho 217, 458 P.2d 213 (1969).

In 1977, the Idaho Supreme Court held unconstitutional a legislative attempt to appropriate income from the endowment funds to pay the expenses of the Endowment Investment Board. The court said that "the legislation authorizing this practice, and the practice itself, is in violation of article 9, § 3 of the Constitution of the State of Idaho." Moon v. Investment Board, 98 Idaho 200, 201, 560 P.2d 871, 872 (1977).<sup>6</sup>

Thus, long has there stood a barrier against legislative encroachment and appropriation of university endowment fund income. Nothing in the change to the Idaho Admission Bill or in the change to the Idaho Constitution alters this inviolate nature of the endowment or the income the endowment produces.

**C. Question 2: "Is the answer to Question 1 different for the three University of Idaho endowment funds than the answer for the Endowment Funds currently dedicated to Idaho State University and Lewis-Clark State College?"**

The answer to this question is no. All income from the university endowment funds derived from the federal land grants is perpetually appropriated by such federal land grants regardless of the statutory or constitutional beneficiary.

Your question addresses the issue of whether the University of Idaho's constitutional status under article 9, section 10 of the Idaho Constitution provides a different answer than the analysis of university endowment funds dedicated to other colleges and universities created by statute. It is worthy of note that even though the other colleges and universities may be created by statute, the Idaho State Board of Education's supervi-

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sion over such institutions is still constitutional in nature pursuant to article 9, section 2 of the Idaho Constitution.

Generally speaking, the federal land grants were not made to individual colleges or universities. The grants were to the states. The states were then charged with the duty to devote such funds to the purposes named. Wyoming Agricultural College v. Irvine, 206 U.S. 278, 27 S. Ct. 613, 51 L. Ed 1063 (1907).

The State Normal School Fund originally consisted of lands under Section 11 of the Idaho Admission Bill providing for 100,000 acres for creation of state normal schools. At the time of Idaho statehood, the term “normal schools” referenced what are now commonly known as colleges of education for the training of teachers. Each of Idaho’s four-year colleges and universities currently maintains a college of education. Given that fact, it appears that under the terms of the federal grant, the legislature could designate any or all of Idaho’s four-year colleges and universities as a recipient of the income of the State Normal School Fund. The legislature has split the proceeds of the State Normal School Fund between Idaho State University (ISU) and Lewis-Clark State College (LCSC) to support their colleges of education. Idaho Code §§ 33-3302 and 33-3304. Once that income is so designated by the legislature, however, such income from the endowment is already perpetually appropriated by the act of Congress and requires no further legislative action for the spending authority for such funds.

The Charitable Institution Fund also originates from Section 11 of the Idaho Admission Bill granting 150,000 acres for “other state, charitable, education, penal and reformatory institutions.” Again, the legislature may designate the beneficiary of the income from such fund and has done so by granting four-fifteenths (4/15) of the income of such fund to ISU. Idaho Code § 66-1106. The legislature is free to either grant that four -fifteenths (or any other portion) to ISU, to one of Idaho’s other colleges and universities, to other education sources, or to any other purpose defined in Section 11 of the Idaho Admission Bill, i.e., penal or reformatory institutions or other charitable institutions. However, once the legislature has designated the beneficiary, no further appropriation is required, for the same reasons as set forth above.

Thus, in answer to your second question, the result is not different for the university endowment funds dedicated to ISU and LCSC. The income

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from the university endowment funds in which ISU and LCSC are the stated beneficiaries is already appropriated and requires no further act of the legislature. The legislature may not limit the spending authority of the income from such endowments.<sup>7</sup>

**D. Question 3: “Does the Division of Financial Management have the authority to restrict the spending authority on the income from the Endowment Funds?”**

No. While the Division of Financial Management (DFM) has the authority to regulate certain spending by state agencies under chapter 35, title 67, Idaho Code, such authority does not extend to the income from the university endowments.

His question was also answered in Attorney General’s Opinion 76-65. In addition, it is clear that the Idaho Supreme Court has held that the spending authority over such income from the endowments is vested in the board of trustees of the designated institution and not in the State of Idaho in general. (The state has the mere clerical or ministerial duties to pay such funds over to the board of trustees. Melgard v. Eagleson, 31 Idaho 411 (1918).)

If the income from the endowments is beyond the authority of the legislature to appropriate, then it follows that it would necessarily be beyond the authority of DFM to regulate such spending. The Idaho Legislature is the only constitutional entity charged with the appropriation of all public funds as allowed by law. If it is beyond the legislature’s authority to appropriate the university endowment fund income, then it would clearly be beyond the authority of DFM, as a statutory agency granted authority by the legislature, to limit the spending authority of the colleges and universities for the income from the endowment funds.

**E. Question 4: “Do the 1998 HB 643 changes to the University Endowment Fund, the Scientific Endowment Fund, and the Agricultural Endowment Fund legally give the Legislature power over the appropriation of the income from such funds? In other words, are such changes constitutionally appropriate?”**

**Question 5: “Do the 1998 HB 643 changes to the Normal School Endowment Fund and the Charitable Institutions Endowment**

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**Fund legally give the Legislature power over the income from such funds? In other words, are such changes constitutionally appropriate?"**

Given our answer to Question 2 above, Questions 4 and 5 are being considered together.

### **1. Background**

The 1998 legislature requested by HJM 9 that Congress change Section 5 of the Idaho Admission Bill in order to effect changes to the Public School Endowment investment laws. Following that request, Congress passed House Resolution 4166 as Public Law 105-296 on October 27, 1998. This measure amended the Idaho Admission Act by amending Section 5 to read as follows:

#### **SEC. 5 SALE, LEASE, OR EXCHANGE OF SCHOOL LAND.**

##### **(a) SALE-**

(1) **IN GENERAL** - Except as provided in subsection (c), all land granted, under this Act for educational purposes shall be sold only at public sale.

##### **(2) USE OF PROCEEDS-**

(A) **IN GENERAL** - Proceeds of the sale of school land-

(i) except as provided in clause (ii), shall be deposited in the public school permanent endowment fund and expended only for the purpose of public schools; and

(ii)(I) may be deposited in a land bank to be used to acquire, in accordance with State law, other land in the State for the benefit of the beneficiaries of the public school permanent endowment fund; or

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(II) if the proceeds are not used to acquire other land in the State within a period specified by State law, shall be transferred to the public school permanent endowment fund.

(B) **EARNINGS RESERVE FUND** - Earnings on amounts in the public school permanent endowment fund shall be deposited in an earnings reserve fund to be used for the support of public schools of the State in accordance with State law.

(b) **LEASE** - Land granted under this Act for educational purposes may be leased in accordance with State law.

(c) **EXCHANGE-**

(1) **IN GENERAL** - Land granted for educational purposes under this Act may be exchanged for other public or private land.

(2) **VALUATION** - The values of exchanged lands shall be approximately equal, or, if the values are not approximately equal, the values shall be by the payment of funds by the appropriate party.

(3) **EXCHANGES WITH THE UNITED STATES-**

(A) **IN GENERAL** - A land exchange with the United States shall be limited to Federal land within the State that is subject to exchange under the law governing the administration of the Federal land.

(B) **PREVIOUS EXCHANGES** - All land exchanges made with the United States before the date of the enactment of this paragraph are approved.

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- (d) **RESERVATION FOR SCHOOL PURPOSES** - Land granted for purposes, whether surveyed or unsurveyed, shall not be subject to preemption, homestead entry, or any other form of entry under the land laws of the United States, but shall be reserved for school purposes only.

In addition to HJM 9, the 1998 Idaho Legislature passed HJR 6 and HJR 8 which amended article 9, sections 3, 4, 8, and 11 of the Idaho Constitution with respect to the public school endowment land and fund. Following the amendments to the Idaho Admission Bill and to the Idaho Constitution, the legislature passed 1998 HB 643. House Bill 643 provided a comprehensive Idaho Code revision relating to all state endowment lands and funds. The amendments were designed to bring Idaho Code into line with the Idaho Admission Bill changes and constitutional amendments for the public school Endowment Fund investment reform.

The subject of your questions 4 and 5 speaks specifically to Sections 14, 19, 24, 28 and 59 of 1998 HB 643. Each of these sections applies, respectively, to the income funds created for the University Endowment Fund, Scientific School Endowment Fund, Agricultural College Endowment Fund,<sup>8</sup> State Normal School Endowment Fund and Charitable Institutions Endowment Fund. Although there are a few minor differences among the various sections, they all primarily provide that money in the "income fund shall be used for the benefit of the beneficiaries of the endowment and distributed to current beneficiaries of the [endowment name] pursuant to legislative appropriation." (Emphasis added.) Your query is whether the language "pursuant to legislative appropriation" in effect "legally give[s] the legislature power over the appropriation of the income from such funds?"

As noted above, this question has been answered under current law by both the Idaho State Supreme Court and this office. The Idaho Supreme Court has stated that "the proceeds of federal land grants . . . are not subject to the constitutional provision that money must be appropriated before it is paid out of the state treasury." Black v. State Board of Education, at 33 Idaho at 427, and Evans v. Van Deusen, 31 Idaho at 619 (1918), and this office has opined that although the endowment fund sources are listed in the appropriation bill to the State Board of Education, that this listing of funds in the appropriation bill is not an actual 'appropriation.'" 1976 Atty. Gen. Ann. Rpt. 280. Given that this was clearly the state of law prior to the enactments of HJR 6,

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HJR 8, the amendment to the Idaho Admission Bill and 1998 HB 643, the operative question is whether these enactments change that conclusion.<sup>9</sup>

### 2. Changes to the Idaho Admission Bill

Section 5 of the Idaho Admission Bill, as amended in 1998, makes no express reference to whether the expenditure of university endowment income is subject to state legislative appropriation. There are, however, three notations in the section that refer to the expenditure of endowment fund income generally. Section 5(a)(2) is entitled "Use of Proceeds." Subsection (A)(i) provides that proceeds "shall be . . . expended only for the support of public schools. . . ." Subsection (B) provides that money from the earnings reserve fund shall be "used for the support of public schools of the state in accordance with state law."

There are several references in the congressional record as to the intent of the amendment to the Idaho Admission Bill. In the "Background and Need for Legislation" section of the House of Representatives Report, the report states that the purpose of the legislation is "to generate additional income from the endowment lands for public schools and other beneficiaries . . . to provide a more predictable income stream to the beneficiaries, provide increased and stable funding for public education and other beneficiaries. . . ." In addition to the stated purpose of the legislation, each of the four members of Idaho's congressional delegation commented in the Congressional Record as to the purpose of the legislation. Representative Michael Crapo, the bill's sponsor, stated that "this is an opportunity for us to generate increased revenues for Idaho's public schools, with no tax increase and with simply a reformed management of our public lands. . . . HR 4166 is going to provide the state of Idaho the ability to increase funding for public education by at least \$20 million, if not much more, annually by restructuring the management of our endowment lands." Congressional Record for September 15, 1998, page H7760. Representative Helen Chenoweth stated that the reason Governor Batt pursued the endowment fund investment reform was a "vision on how to gain more money for Idaho's schools without raising taxes on the state's taxpayers. . . ." *Id* at H7761.

In the United States Senate, the identical version of HR 4166 was S2226. Although introduced by Idaho Senator Larry Craig, S2226 was withdrawn in favor of HR 4166. In speaking to S2226, Senator Craig stated that

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the purpose of this "identical legislation" was to "bring about the better management of state lands to the financial benefit of our public schools." Congressional Record for June 25, 1998, page S7188. Senator Craig further noted that the bill was providing for "increased and stable funding for public education. . . ." *Id.* In particular, Senator Craig noted that only four changes were to occur based upon the amendment to the Idaho Admission Bill:

First, it allows the Board of Land Commissioners to exercise its fiduciary responsibility as managers of the state endowments by treating both land and fiscal assets as one trust.

Second, the proposal creates an earnings reserve account that will serve as a "shock absorber" to allow the endowments to provide a more predictable income stream.

Third, it provides increased and stable funding for public education by allowing investments in assets that will provide higher rates of return. The state committee projected that through this single change, public education in our state could receive up to \$20 million or more annually without raising taxes.

Fourth, it establishes a land bank account for proceeds from the sale of endowment lands. The account gives the Board of Land Commissioners the flexibility to re-invest in other real property for the land trust.

*Id.*

Finally, Idaho Senator Dirk Kempthorne stated that the legislation "will provide the ability to increase Idaho public education funding at least \$20 million and possibly \$30 million annually. And it will do so without raising taxes, cutting services or asking the federal government for one thin dime." *Id.* at S7189. Senator Kempthorne further stated that the legislation "will substantially increase funds available for Idaho schoolchildren . . . the bottom line is that the bill provides more money for educating our kids. . . ." *Id.* Finally, Senator Kempthorne noted that the solution to funding issues

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was that this legislation was designed “to allow the fund to be invested in a broader array of investments. . . .” *Id.*

In addition to Idaho’s congressional delegation, two other members of the U.S. House of Representatives spoke in favor of HR 4166. Representative Hansen of Utah stated that the purpose of the changes was to produce “a stream of income for the schools.” Congressional Record for September 15, 1998, at page H7760. Also, Representative Faleomavaega from American Samoa stated that “the purpose of the changes, as I understand them, is to generate additional income for Idaho’s permanent endowment fund.” *Id.*

Thus, it appears clear that the congressional intent was to increase the income funded to Idaho’s public education system. This was to be accomplished through a new method of investing and managing the endowment funds. However, there is no mention of making the income from such funds, once earned, subject to any type of appropriation or other limitation.

In summary, nothing in the 1998 changes to the Idaho Admission Bill changes the conclusion that the income from the several university endowments are dedicated, pursuant to federal law and congressional enactment, to the universities. Thus, even given the 1998 amendment to the Idaho Admission Bill, the Idaho Legislature has no appropriation authority over the income from the university endowments.

### 3. Changes to the Idaho Constitution

Only one section of the Idaho Constitution amended by 1998 HJR 6 and 1998 HJR 8 speaks to legislative appropriations. In HJR 8, article 9, section 3 of the Idaho Constitution speaks to the creation of the “Earnings Reserve Fund.” Article 9, section 3, as amended by 1998 HJR 8, states that “funds shall not be appropriated by the legislature from the public school earnings reserve fund, except as follows: the legislature may appropriate from the public school earnings reserve fund administrative costs incurred in managing the assets of the public school endowments including, but not limited to, the real property and monetary assets.” This amendment appears to be in line with the amendment to the Idaho Admission Bill and in line with prior decisions of the Idaho Supreme Court. The Idaho Supreme Court has held that the use of endowment fund earnings to pay for the expenses incurred in man-

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aging endowment lands is permitted under the Idaho Admission Bill. Moon v. State Board of Land Commissioners, 111 Idaho 389, 724 P.2d 125 (1986).<sup>10</sup>

Thus it appears that it is proper for the legislature to appropriate funds from the newly created Earnings Reserve Fund to pay certain administrative costs in managing the assets of the university endowment funds. However, no language in the amended article 9, section 3 of the Idaho Constitution authorizes legislative appropriation of the income, once earned and distributed by the Land Board, from the university endowments. In fact, the express terms of article 9, section 3 limit the legislature's appropriation authority to paying the administrative costs. No other legislative appropriation is constitutionally authorized. Thus, there appears to be no intent by the people of the State of Idaho, in amending their Constitution, to provide for anything other than the dedication of such university endowment fund income perpetually to the university endowment beneficiaries.<sup>11</sup>

### **F. Conclusion**

Under current law, it is well settled that the income from the university endowments is distributed to, and used by, the colleges and universities outside the appropriation process. After July 1, 2000, since neither Congress nor the people of the State of Idaho expressed any intent in changing the perpetual dedication of such funds, it appears that all income from the university endowments will still be outside the constitutional appropriation process.

We hope this letter satisfactorily answers your inquiry. If we can be of any further assistance, please do not hesitate to contact us.

Sincerely,

Terry E. Coffin  
Chief, Contracts &  
Administrative Law  
Division

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<sup>10</sup>Other grants of land were made for purposes such as an insane asylum or a state penitentiary. However, such land grants are beyond the scope of this advisory.

<sup>11</sup>One of the Idaho constitutional amendments, 1998 HJR 6, has, at the time of the drafting of this opinion, been stricken by the Idaho State Supreme Court.

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<sup>3</sup>In answering your inquiry, this opinion is limiting the scope of the response to the scope of your question, i.e., the university related endowments. We do not direct our response to any issue related to the public school endowment or any other endowment. Thus, as used herein, the term "university endowments" includes the University Fund, the Scientific School Fund, the Agricultural College Fund, the State Normal School Fund and that portion of the Charitable Institutions Fund currently dedicated by statute to Idaho State University.

<sup>4</sup>The State Board of Education serves as the Board of Regents and the Board of Trustees of all of Idaho's public institutions of higher education. See Idaho Constitution art. 9, § 2, and art. 9, § 10, and Idaho Code §§ 33-101, 33-2802, 33-3003, 33-3102 and 33-4002.

<sup>5</sup>This is not to say that the repeal or amendment of the Standard Budget Act would change the result. It only points to legislative recognition of the congressional and constitutional requirements.

<sup>6</sup>The court later held that using income to pay the costs of maintenance and management of endowment land, not the fund, was constitutionally appropriate. Moon v. State Board of Land Commissioners, 111 Idaho 798, 724 P.2d 125 (1986).

<sup>7</sup>It is worthy of note that the legislature clearly may change the beneficiary of the State Normal School Endowment and the Charitable Institutions Endowment within the requirements of the Idaho Admission Bill. However, under the holding in Black v. State Board of Education, the income from the University Fund, the Scientific School Fund and the Agricultural College Fund appear to be vested in the Board of Regents of the University of Idaho by article 9, § 10 of the Idaho Constitution. Thus, barring any change to article 9, section 10 of the Idaho Constitution, the legislature may not be free to alter the dedication of the income from those endowments.

<sup>8</sup>In addition to the 72 sections of land provided for in Section 8 of the Idaho Admission Bill, the University of Idaho was also granted 50,000 acres of land under Section 11 of the Idaho Admission Bill. While this later 50,000 acres does not appear in 1998 HB 643 at Section 11 establishing a new Idaho Code § 33-2909 creating the University Endowment Fund, it was likely the intent of the legislature to include such 50,000 acres in the University Endowment Fund. However, since this was not expressly done, the status of those 50,000 acres (and their proceeds) is unclear.

<sup>9</sup>Again, in answering your inquiry, this opinion is limiting the scope of the response to the university related endowments.

<sup>10</sup>However, in the Moon case, there appears to be no specific discussion of the Morrill Act lands. The Morrill Act (codified as 7 U.S.C. §§ 301-308) is the federal law under which the agricultural endowment lands were granted to the states. Section 10 of the Idaho Admission Bill clarified that Idaho received 90,000 acres for an agricultural college under the Morrill Act land grants. Section 3 of the Morrill Act (7 U.S.C. § 303), as that provision has remained unchanged since 1862, provides:

All the expenses of management, superintendence, and taxes (of the land) . . . and all expenses incurred in the management and disbursement of the moneys which may be received therefrom, shall be paid by the states to which they may belong, out of the treasury of said states, so that the entire proceeds of the sale of said lands shall be applied without diminution to the purposes hereinafter mentioned.

(Emphasis added.) Thus, under the terms of the Morrill Act grant, the states cannot pay any expenses out of the agricultural college endowment fund income.

<sup>11</sup>In fact, article 9, § 11 of the Idaho Constitution clearly notes that the investment of university endowment funds is different from the other endowment funds.



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**ATTORNEY GENERAL'S  
CERTIFICATES OF REVIEW  
FOR THE YEAR 2000**

**ALAN G. LANCE**  
ATTORNEY GENERAL  
STATE OF IDAHO



## CERTIFICATES OF REVIEW OF THE ATTORNEY GENERAL

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March 22, 2000

The Honorable Pete T. Cenarrusa  
Secretary of State  
**HAND DELIVERED**

Re: Certificate of Review  
Proposed Initiative Related to Annexation  
of Adjacent Unincorporated Property

Dear Mr. Cenarrusa :

An initiative petition was filed with your office on March 15, 2000, which would repeal Idaho Code § 50-222 and replace it with two new code sections. Pursuant to Idaho Code § 34-1809, this office has reviewed the proposed initiative and has prepared the following advisory comments. It must be stressed that, given the strict statutory timeframe in which this office must respond and the complexity of the legal issues raised in this proposed initiative, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only," and the petitioners are free to "accept or reject them in whole or in part."

### **BALLOT TITLES**

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles should impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares the titles, if petitioners would like to propose language with these standards in mind, we would recommend that they do so and their proposed language will be considered.

### **MATTERS OF SUBSTANTIVE IMPORT**

The initiative would make a number of changes to the manner in which annexation of adjacent unincorporated property is accomplished under Idaho law. New section 50-221A would require municipalities to hold hear-

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ings and conduct an election within an area proposed for annexation before actually annexing the area. Under new section 50-221A(6), a municipality may only proceed with a proposed annexation after a majority of the qualified electors in the area proposed for annexation have voted in favor of the annexation. The cost of the election would be borne by the municipality proposing the annexation.

Upon review, it is the opinion of this office that there is no constitutional or statutory impediment to the petitioners' proposed changes to the current procedure for annexing adjacent unincorporated property.

Sincerely,

Alan G. Lance  
Attorney General

**Analysis by:**

Matthew J. McKeown  
Deputy Attorney General

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