

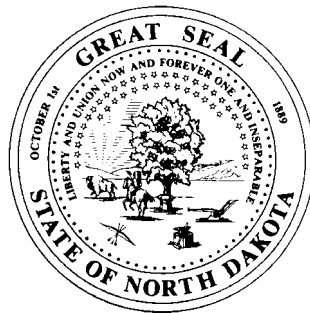
**State Of
North Dakota**

***BOARD OF UNIVERSITY AND
SCHOOL LANDS***

State Land Department

Fifty-sixth Biennial Report

to the
Governor
and
Secretary of State



July 1, 2003 to June 30, 2005

The Honorable John Hoeven
Governor of North Dakota
State Capitol
Bismarck ND 58505

The Honorable Alvin A. Jaeger
Secretary of State
State Capitol
Bismarck ND 58505

Dear Governor Hoeven and Mr. Jaeger:

It is my privilege to present the 2003-2005 Biennial Report for the Board of University and School Lands. The report presents an overview of the Board's authority under the Constitution and state law, and the activity of the Board as reported by each of the Land Department's division directors and the Energy Development Impact Office.

I am pleased to report that all trust funds remain healthy as the combined permanent trust funds grew by over \$147 million during the biennium, a remarkable 25 percent rate of increase. Approximately one-half of the growth came from investment appreciation and two-thirds of the remaining corpus growth coming from energy related receipts. Higher oil and natural gas prices and advancements made in technology is driving an increase in exploration activity. As reported by the Minerals Management Division Director, several hot oil plays have taken place as evidenced by the strong and near historic records for lease bonus collections starting with the August 2004 lease sale. Short-term interest rates have also started to increase, and the equity markets performance improved during the biennium adding to trust fund growth and future distribution potential.

The Board's investment policies and asset allocations are continually being honed. The implementation of several consultant recommendations during the biennium provided further diversification of the portfolio and enhanced performance returns.

Special recognition and appreciation is owed to the Land Department employees for their dedication and inspiration to the benefit of trust beneficiaries. Trust beneficiaries are being well served.

Respectfully submitted,



Gary D. Preszler
Secretary, Board of University
and School Lands
Commissioner, State Land Department

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POLICY OF NON-DISCRIMINATION ON THE BASIS OF DISABILITY

The State Land Department does not discriminate on the basis of disability in the admission or access to, or treatment or employment in, its programs or activities. A coordinator has been designated to ensure compliance with the non-discrimination requirements contained in §35.107 of the Department of Justice regulations. Please call (701) 328-2800 for information concerning the provisions of the Americans with Disabilities Act, and the rights provided thereunder as they relate to the agency and access to its records.

Historical Overview

On February 22, 1889, Congress passed "An act to provide for the division of Dakota into two states, and to enable the people of North Dakota, South Dakota, Montana and Washington to form constitutions and state governments . . ." This Act is commonly known as the Enabling Act. Section 10 of this act granted sections 16 and 36 in every township to the new states "for the support of common schools." In cases where portions of sections 16 and 36 had been sold prior to statehood, indemnity or "in-lieu" selections were allowed. In North Dakota, this grant of land totaled over 2.5 million acres.

Under sections 12, 14, 16 and 17 of the Enabling Act (and other acts referred to therein), Congress provided further land grants to the state of North Dakota for the support of colleges, universities, the state capitol and other public institutions. These additional grants totaled approximately 668,000 acres, bringing the grand total of Enabling Act land grants to nearly 3.2 million acres.

CONSTITUTIONAL AUTHORITY

North Dakota's Constitution (Article X), adopted on October 1, 1889, entrusted the management of these lands (both acquired land and grant land) to the "board of university and school lands" (the Board). The Board was initially made up of the governor as chairperson, the secretary of state as vice-chair, the attorney general, superintendent of public instruction, and the state auditor. On June 10, 1986, a constitutional amendment replaced the state auditor with the state treasurer.

The Land Board currently consists of the following members:



Governor John Hoeven
Chairman



Alvin A. Jaeger
Secretary of State
Vice Chairman



Wayne Stenehjem
Attorney General



Dr. Wayne Sanstead
Supt. of Public Instruction



Kelly Schmidt
State Treasurer

COMMISSIONER OF UNIVERSITY & SCHOOL LANDS

Under N.D.C.C. § 15-02-01, the Board of University and School Lands is required to appoint a commissioner to act on its behalf. Specific responsibilities of the Board and the Commissioner are set out in N.D.C.C. ch. 15-01 through ch. 15-08.1.

Generally, the Commissioner of University and School Lands is responsible for the following:

- ◆ Acting as the general agent for the Board.
- ◆ Supervising all aspects and activities of the State Land Department.
- ◆ Having general charge and supervision of all grant lands and associated records, maps, books and papers.
- ◆ Enforcing the Unclaimed Property Act (N.D.C.C. § 15-02-05.2 and ch. 47-30.1).

The office of the Commissioner of University and School Lands has been commonly called the State Land Department.

In 1989, the Energy Development Impact Office became a division of the Office of the Commissioner, however, the EDIO Director is appointed directly by the Board of University and School Lands (N.D.C.C. § 57-62-04).

LAND SALES & ACQUISITIONS

Since statehood in 1889, much of the grant land has been sold. Beginning in 1939, whenever the state sold grant land, it reserved five percent of the minerals. In 1941, the reservation was increased to 50 percent; and, since July 28, 1960, the North Dakota Constitution has mandated a 100 percent mineral reservation. Today, the Land Department manages in excess of 660,000 of the original, grant land surface acres, and over 1.8 million of the original mineral acres. Approximately 51,000 acres have since been acquired through foreclosure or other means, bringing the total surface acreage to approximately 714,000 acres.

In 1977, the legislature transferred management authority for minerals acquired by the Bank of North Dakota and for the minerals under sovereign land (navigable rivers/lakes) to the Department. This brings the total mineral acres managed to over 2.5 million acres.

Agency Overview

The Land Grant to the State from the federal government and the State Constitution provides that the Board shall manage the land, minerals and proceeds from the land for the exclusive benefit of the institutions for which they were granted. The income earned is to be distributed according to N.D.C.C. ch. 15.03-05.2, again, for the exclusive benefit of those trust beneficiaries. (See "Schedule of Net Asset Balances" and "Schedule of Distributions by Trust", page 18.)

This income is generated through prudent management of trust assets, consisting of approximately 714,000 surface acres, over 2.5 million mineral acres, and over \$782 million of financial assets. The surface acres are leased to ranchers and farmers across the state. The 2.5 million mineral acres are offered for oil, gas, coal, gravel and scoria leasing. Revenues from all sources are deposited in trust funds and are invested in the Farm Loan Pool administered by the Bank of North Dakota, U.S. Treasury notes and bonds, and corporate bonds and stocks. The income from these investments, together with surface and mineral rentals, is distributable to schools (public grades K-12), educational and other public institutions at specified intervals throughout the biennium. (See "Investments", pages 13-17, and "Surface Management", pages 9-11.)

The following is a list of beneficiaries of the various trust funds administered by the Land Department pursuant to Article IX of the North Dakota Constitution:

- | | |
|----------------------------------|--------------------------------|
| 1) Common Schools | 8) Mayville State University |
| 2) North Dakota State University | 9) Industrial School |
| 3) School for the Blind | 10) State College of Science |
| 4) School of the Deaf | 11) Schools of Mines |
| 5) State Hospital | 12) Veterans Home |
| 6) Ellendale State College* | 13) University of North Dakota |
| 7) Valley City State University | 14) Capitol Building |

** The beneficiaries of this trust are now Dickinson State University, Minot State University, MSU-Bottineau, Veterans Home, School of the Blind, State Hospital, and the State College of Science.*

Common Schools Trust Fund

The largest trust administered by the Land Department is the Common Schools Trust Fund. Distributions from the Common Schools Trust Funds are a part of the tuition apportionment payments made to the various school districts each year. Distributions during the 2003-2005 biennium were approximately \$287 per student per year for each child in kindergarten through grade 12.

Besides the sources of revenue listed above, the Common Schools Trust Fund receives 10 percent of the oil and gas extraction tax (ND Constitution Article X, Section 24) amounting to approximately \$3.68 million per year, which is invested according to the policy of the Board in the permanent funds of that trust fund. (See "Schedule of Permanent Fund Receipts by Trust", page 18.)

The Common Schools Trust Fund also receives 45 percent of the proceeds from the tobacco class-action lawsuit settlement (N.D.C.C. § 54-27-25). These funds become part of the permanent funds and are invested according to the policy of the Board. (See "Schedule of Permanent Fund Receipts by Trust", page 18.)

Lands and Minerals Trust Fund

The Land Department is the trustee for the Lands and Minerals Trust Fund created by N.D.C.C. ch. 15-08.1 and § 61-33-07. This trust fund consists of approximately 704,750 mineral acres formerly owned by the Bank of North Dakota, and the minerals located under navigable streams, rivers, and lakes, which are owned by North Dakota as a sovereign state. All monies collected in this fund are subject to legislative appropriation each biennium. This fund serves as a collection vehicle for repayment of the developmentally disabled facilities loans funded by the Common Schools Trust. The Bank of North Dakota administers the loans. The principal and interest payable to the Common Schools Trust is appropriated from the Land and Minerals Trust Fund. (See "Schedule of Other Funds", page 18.)

Coal Development Trust Fund

The Coal Development Trust Fund was established by N.D.C.C. § 57-62-02 and pursuant to Section 21 of Article X of the North Dakota Constitution. The Fund receives 30% of the coal severance tax. The fund must be held in trust and administered by the Board for loans to coal impacted counties, cities, and school districts as provided by section N.D.C.C. § 57-62-03, and for loans to school districts pursuant to N.D.C.C. ch. 15.1-36. The unloaned balance is invested according to the policy of the Board. (See "Investments", page 13 and "Schedule of Other Funds", page 18.)

Unclaimed Property

The Land Department administers the Uniform Unclaimed Property Act (N.D.C.C. ch. 47-30.1). In this capacity the Department collects "unclaimed property" (uncashed checks, unused bank accounts, etc.), and via various methods of publication, provides an opportunity for the owner to be reunited with the property. Property acquired under this Act is held in trust in perpetuity on behalf of the owner; therefore, owners have one place they can search for their property. The interest income from unclaimed property is distributed to ND public grades K-12. (See "Unclaimed Property Division", page 12.)

Energy Development Impact Office

The Energy Development Impact Office (EDIO) (N.D.C.C. ch. 57-62) is also a part of the Land Department. The EDIO allocates funds appropriated by the state legislature to assist local political subdivisions in dealing with problems arising from oil development. In the allocation of these funds, the Director of the office accepts applications for funding, travels to visit with subdivisions requesting the funding, allocates the funds, and administers the payout of the funds to the grantees. (See "Energy Development Impact Office", page 6.)

Mission Statement

The mission of the State Land Department, under the direction of the Board of University and School Lands, is to serve as a trustee for the benefit of the common schools (public grades K-12), various institutions of higher education, and certain other state institutions.

Land Department Statement of Goals

The primary goal of the Department is to maximize distributable income and trust growth within the parameters allowed by state law, board policy, the prudent investor rule and sound land and mineral management practices. To achieve this primary goal, the following subgoals have been established:

1. To obtain a "fair market" return from the surface lands while improving their condition and value.
2. To develop and pursue a strong, effective minerals management program which maximizes revenue to the trusts.
3. To develop and pursue an aggressive, fair minerals audit program to ensure that the trusts receive all royalties.
4. To continue to raise awareness of the Uniform Unclaimed Property Act among businesses and potential claimants.

5. To preserve the purchasing power of the trusts by maintaining and increasing, relative to inflation, the income distributable to trust beneficiaries.
6. To manage the permanent financial assets of the trusts within the guidelines of the Prudent Investor Rule.

Energy Development Impact Office Statement of Goals

The primary goal of the office is to ensure that local subdivisions hosting energy activity are not required to bear a disproportionate share of the costs associated with that activity (both in its "boom" and "bust" cycles.) The guiding principle of the office is to ensure that the benefit to all of the people of North Dakota, from the extraction of energy resources will not be gained at the expense of those whose lives or property are disturbed, without adequate compensation, in the process.

Funding Sources and Expenses

- Funding for the State Land Department is received through the State Lands Maintenance fund. This fund consists of fees charged for services, plus a portion of interest and income earned by the various trusts (N.D.C.C. § 15-03-01.1).
- Funds for oil impact grants are requested from the Oil Impact Grant Fund. The administration expenses of the Energy Development Impact Office are paid out of the Oil Impact Grant Fund.

Land Department Statement of Appropriations and Expenditures

Land Department and Energy Development Impact Office	2003-2005 Appropriations	2003-2005 Expenditures	Unexpended Appropriations
Salaries and wages	\$1,876,162	\$1,828,293	\$47,869
Operating expenses	753,222	549,734	203,488
Capital Assets	6,350	6,350	0
Contingencies	50,000	0	50,000
Grants	4,888,100	4,888,100	0
Total	\$7,573,834	\$7,272,477	\$301,357

Other Land Department Information

PUBLICATIONS

In addition to this report, the Department publishes:

- A semi-annual newsletter which is distributed to surface lessees and other interested parties.
- Lists of tracts to be leased at quarterly oil and gas lease sales, together with a summary of the results of these sales.
- Lists of individuals entitled to unclaimed property (N.D.C.C. § 47-30.1-19.1).
- Summaries of grant awards made by the Energy Development Impact Office.
- An informational brochure relating to owners of unclaimed property.
- An informational brochure relating to holders of unclaimed property.
- An informational brochure relating to the operations of the State Land Department.

Notice of the leasing and sale of surface and mineral tracts is given by publication in the official county newspaper where the land is located. Newly reported unclaimed property owners are published in the official county newspaper of the owner's last known address.

MEETINGS

The Board of University and School Lands meets monthly, unless there is insufficient business to require a Board meeting. The regular meeting day is the last Thursday of the month.

Minutes of the Board and other information regarding the activities of the State Land Department can be obtained from:

*State Land Department
1707 N 9th Street
P.O. Box 5523
Bismarck, ND 58506-5523*

General Information 701-328-2800
Fax 701-328-3650

WORLD WIDE WEB ADDRESS

The Land Department maintains a web site at:
www.land.state.nd.us

ND STATE LAND DEPARTMENT PERSONNEL

Employee	Position	Land Department Employment Dates
Bayley, Keith	Account Budget Specialist	1988-Present
Brand, Mike	Director of Surface Management	1979-Present
Bren, Travis	Auditor	2002-2004
Engleson, Jeff	Director of Investment Division	1986-Present
Erdmann, Levi	Programmer Analyst	2003-Present
Fisher, Linda	Administrator of Unclaimed Property; Leasing Coordinator	1991-Present
Froemke, Debra	Audit Technician	2001-2004
Glanville, Monica	Administrative Assistant	2003-Present
Grasl, Marian	Auditor	2005-Present
Gudvangen, Peggy	Director of Audits	2005-Present
Humann, Mike	Land Conservationist	1987-Present
Haupt, Mike	Range Specialist	1987-Present
Jacobs, Debra	Administrative Assistant	1998-Present
Larson, Rick	Deputy Commissioner; Director of Minerals Management & EDIO	1987-Present
Pascua, Jayden	Data Processing Information Specialist	1999-Present
Pazdernik, Bonnie	Office Assistant	1997-Present
Preszler, Gary D.	Commissioner	2001-Present
Saude, Jerry	Land Management Specialist	1991-Present
Schell, Judith F.	Administrative Assistant	2000-Present
Tober, Loa	Administrative Assistant	1998-Present



*First row (left to right): Loa Tober, Judith Schell, Marian Grasl, Bonnie Pazdernik, Monica Glanville
 Second row: Keith Bayley, Jerry Saude, Jeff Engleson, Levi Erdmann, Rick Larson, Peggy Gudvangen, Mike Haupt
 Third row: Deb Jacobs, Linda Fisher, Gary Preszler, Mike Brand, Mike Humann, Jayden Pascua*

Energy Development Impact Office

Rick D. Larson, Director

The Energy Development Impact Office (EDIO) was organized in 1975 by Legislative authorization of the Coal Development Impact Program under N.D.C.C. ch. 57-62. On July 1, 1989 the EDIO was combined with the Land Department and is currently under the direction of the Board of University and School Lands. The coal program began in 1975 and expired in 1989. The Oil Impact Grant Program began in 1981 and is still in existence.

During the 2003-2005 biennium, the Oil Impact Grant Program helped reduce the financial hardships of local political subdivisions which resulted from activities of the oil industry. The program is funded by 6.67 percent of the Oil & Gas Gross Production Tax. For the 2003-2005 biennium, that allocation reached \$5 million. The allocation cannot exceed \$5 million for a biennium.

During the 2003-2005 biennium, the office conducted grant rounds in the spring of 2004 and the spring of 2005.

To receive funding, applicants must show:

1. That oil activity in the area has created a financial hardship which cannot be handled without help from the Oil Impact Grant Program;
2. That the project will alleviate the hardship that resulted from oil activity; and
3. That the applicant's financial resources to handle the project are insufficient (this implies that the applicant has made a diligent local taxing effort to accomplish its goal).

These funds are awarded by the EDIO Director after conducting visits with the local political subdivisions requesting the funding. Following these visits, the Director considers information received during these meetings, the information included in the application, and any other compiled data relating to oil production, oil taxation, and property taxation. Information is also obtained through the state's automated records from the Oil & Gas Division of the Industrial Commission showing oil wells, oil production, and salt water production, which helps establish the degree of oil-related traffic in each township. Also, the EDIO collects oil tax and property tax data from various sources, including the State Treasurer's Office, the State Tax Commissioner's Office, the State Department of Public Instruction, and the ND League of Cities.

2003-2005 Biennium Oil Impact Grant Applications and Awards			
Summary by County			
County	\$ Requested	\$ Awarded	%
Billings	\$ 80,795	\$ 5,000	0.1
Bottineau	1,365,475	490,500	10.0
Bowman	7,004,471	610,000	12.4
Burke	931,940	399,500	8.2
Divide	610,270	296,000	6.0
Dunn	752,520	234,000	4.8
G. Valley	1,221,451	336,000	7.5
Hettinger	5,000	0	0.0
McHenry	69,500	50,000	1.0
McKenzie	1,544,582	214,700	4.4
McLean	10,000	7,000	0.1
Mercer	32,446	12,000	0.2
Mountrail	1,143,273	294,800	6.0
Renville	1,919,590	440,800	9.0
Slope	645,800	151,000	3.1
Stark	3,270,247	385,000	7.9
Ward	184,500	48,000	1.0
Williams	10,914,237	895,700	18.3
TOTAL	<u>\$31,706,097</u>	<u>\$4,900,000</u>	<u>100.0</u>

2003-2005 Biennium Oil Impact Grant Applications and Awards			
Summary by Class of Subdivision			
Class	\$ Requested	\$ Awarded	%
County	\$ 9,091,473	\$1,387,800	28.3
School	3,394,418	376,000	7.7
City	12,018,038	850,000	17.3
Park District	243,500	0	0.0
Airport Auth.	502,262	38,000	0.8
Township	3,652,332	1,503,100	30.7
Fire Ambul.	2,804,075	745,100	15.2
TOTAL	<u>\$31,706,097</u>	<u>\$4,900,000</u>	<u>100.0</u>

The tables on this page summarize the amounts allocated by county and by class of subdivision for the oil impact grant program. Counties and townships accounted for 59 percent of the total amount awarded, most of which was for road projects. Altogether, the EDIO allocated grants totaling \$4,900,000 during the 2003-2005 biennium.

A total of 523 grants were issued in the two grant rounds to counties, cities, townships, schools, fire and ambulance districts and other local units of government in an area west of a line from Bottineau to Bowman. The EDIO is a program that successfully channels financial help to where it is most needed, at minimum operational expense to the State of North Dakota.

Minerals Management

Rick D. Larson, Director

The Minerals Management Division administers mineral interests held in trust for the benefit of various schools and institutions of North Dakota. The Division also administers mineral interests formerly owned by the Bank of North Dakota, plus the minerals under navigable rivers and lakes.

OIL AND GAS ACTIVITY

The high price of oil and gas has finally shown up in increased leasing activity. In August and November 2004 we leased more acreage, 85,206 acres and 90,285 acres respectively, at one sale than we have since November 1980. Lease sales are conducted by public auction. The high prices were just part of the story. Advances in horizontal drilling techniques further provided oil companies with incentives to once again explore in North Dakota's Williston Basin.

Oil and gas royalty increased dramatically from \$16,348,984 the previous biennium to \$28,200,594 this biennium. Additionally, the 2003-2005 lease sales generated \$19,135,241 in bonuses for the trust beneficiaries and the State, which amounts to an average of \$60.29 per mineral acre. That compares to \$6.05 per acre average for total bonuses of \$473,112 in the 2001-2003 biennium.

High prices, horizontal drilling, new field discoveries and favorable response to unitization have all been factors that contributed to these dollars that provide additions to the permanent trust funds and the State's general fund. The high prices and leasing activity were mentioned above, but unitization of existing fields and new discoveries have also contributed. The Cedar Hills Red River units in Bowman County operated by Burlington Resources Oil and Gas Company and Continental Resources Inc. have increased production by water or air injection. Bowman County is now the highest producing county in the State, which accounts for over one-third of the State's monthly oil production.

Zinke and Trumbo, Inc. has had tremendous success in McKenzie County drilling horizontally into the Ratcliffe formation. Whiting Petroleum Corporation, BTA Oil Producers, Petro-Hunt Corporation and FH Petroleum Corporation have been exploiting the Birdbear formation in Billings and Golden Valley Counties. Finally, many companies are looking at the Middle Bakken formation in the Williston Basin. The Bakken activity across the line in Montana is expected to extend deep into North Dakota. Companies drilling in Divide, Billings, McKenzie, Mountrail, and Dunn Counties are searching for the right techniques to economically make that formation work.

COAL PRODUCTION

Total coal royalty revenue for this biennium was \$1,039,893. Falkirk Mining Company, BNI Coal, Ltd., and Dakota Westmoreland Corporation (formerly Knife River Mining Company) were actively mining tracts where the state owned a mineral interest. We have seen little new leasing activity, but active mines should in the future be mining toward more state minerals which are already leased and thereby provide further royalty payments.

Oil and Gas Leasing Activity

	<u>2001-2003</u>	<u>2003-2005</u>
Gross Mineral Acres Owned*	2,552,453	2,556,068
Acres Under Lease	280,728	539,281
# of Oil/Gas Lease Sales	8	8
Net Mineral Acres Leased	78,119	371,731
Ave. Bonus/Net Mineral Acre	\$6.05	\$60.29

**Approximate acreage only. Total acreage will vary due to estimates of the acreage owned by the state under navigable rivers and lakes.*

Mineral Division Receipts

	<u>2001-2003</u>	<u>2003-2005</u>
Oil and gas royalty	\$16,348,984	\$28,200,594
Oil and gas bonus	\$473,112	\$19,135,241
Coal royalty and bonus	\$1,192,316	\$1,134,293
Oil and gas rental	\$384,622	\$1,344,397
Seismic and other damage payments	\$162,219	\$399,240
TOTAL	<u>\$18,561,253</u>	<u>\$50,213,765</u>

OIL AND GAS LEASE SALE RESULTS

North Dakota State Minerals

COUNTY		Aug-03	Nov-03	Feb-04	May-04	Aug-04	Nov-04	Feb-05	May-05	TOTAL
BILLINGS	TOTAL \$	\$1,360.00	\$39,478.16	\$40,600.28	\$3,520.00	\$204,299.57	\$128,160.00	\$163,200.00	\$168,000.00	\$748,618.01
	MIN. ACRES	720.00	4,564.76	1,408.08	320.00	4,172.05	1,520.00	1,800.00	480.00	14,984.89
	\$/MIN ACRE	\$1.89	\$8.65	\$28.83	\$11.00	\$48.97	\$84.32	\$90.67	\$350.00	\$49.96
BOWMAN	TOTAL \$	\$4,660.00	\$0.00	\$260.00	\$6,780.00	\$0.00	\$0.00	\$6,265.50	\$9,600.00	\$27,565.50
	MIN. ACRES	80.00	0.00	260.00	1,180.00	0.00	0.00	660.22	368.00	2,548.22
	\$/MIN ACRE	\$58.25	\$0.00	\$1.00	\$5.75	\$0.00	\$0.00	\$9.49	\$26.09	\$10.82
BURKE	TOTAL \$	\$0.00	\$0.00	\$1,504.99	\$0.00	\$82,840.00	\$383,600.00	\$1,146,050.35	\$89,277.81	\$1,703,273.15
	MIN. ACRES	0.00	0.00	48.03	0.00	2,200.00	1,440.00	17,515.44	4,793.71	25,997.18
	\$/MIN ACRE	\$0.00	\$0.00	\$31.33	\$0.00	\$37.65	\$266.39	\$65.43	\$18.62	\$65.52
BURLEIGH	TOTAL \$	\$1,876.97	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1,876.97
	MIN. ACRES	1,876.97	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1,876.97
	\$/MIN ACRE	\$1.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1.00
DIVIDE	TOTAL \$	\$0.00	\$63,301.32	\$81,168.88	\$0.00	\$399,996.91	\$1,905,239.38	\$104,885.94	\$123,862.50	\$2,678,454.93
	MIN. ACRES	0.00	1,701.46	2,357.84	0.00	5,813.75	28,343.23	896.22	2,831.85	41,944.35
	\$/MIN ACRE	\$0.00	\$37.20	\$34.43	\$0.00	\$68.80	\$67.22	\$117.03	\$43.74	\$63.86
DUNN	TOTAL \$	\$1,120.00	\$0.00	\$320.00	\$124,094.24	\$366,387.18	\$42,400.00	\$25,299.28	\$70,692.70	\$630,313.40
	MIN. ACRES	560.00	0.00	320.00	1,271.72	16,782.12	800.00	667.97	474.66	20,876.47
	\$/MIN ACRE	\$2.00	\$0.00	\$1.00	\$97.58	\$21.83	\$53.00	\$37.87	\$148.93	\$30.19
EMMONS	TOTAL \$	\$6,275.60	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$6,275.60
	MIN. ACRES	6,275.60	0.00	0.00	0.00	0.00	0.00	0.00	0.00	6,275.60
	\$/MIN ACRE	\$1.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1.00
G. VALLEY	TOTAL \$	\$1,040.00	\$0.00	\$0.00	\$0.00	\$72,560.00	\$0.00	\$65,872.00	\$2,400.00	\$141,872.00
	MIN. ACRES	80.00	0.00	0.00	0.00	2,960.00	0.00	164.68	160.00	3,364.68
	\$/MIN ACRE	\$13.00	\$0.00	\$0.00	\$0.00	\$24.51	\$0.00	\$400.00	\$15.00	\$42.17
LOGAN	TOTAL \$	\$257.88	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$257.88
	MIN. ACRES	257.88	0.00	0.00	0.00	0.00	0.00	0.00	0.00	257.88
	\$/MIN ACRE	\$1.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1.00
MCHENRY	TOTAL \$	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$797.55	\$0.00	\$797.55
	MIN. ACRES	0.00	0.00	0.00	0.00	0.00	0.00	797.55	0.00	797.55
	\$/MIN ACRE	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1.00	\$0.00	\$1.00
MCINTOSH	TOTAL \$	\$4,096.27	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$4,096.27
	MIN. ACRES	4,096.27	0.00	0.00	0.00	0.00	0.00	0.00	0.00	4,096.27
	\$/MIN ACRE	\$1.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$1.00
MCKENZIE	TOTAL \$	\$39,423.73	\$72,102.37	\$83,600.85	\$902,133.20	\$2,364,749.23	\$1,163,141.52	\$1,175,601.03	\$285,471.00	\$6,086,222.93
	MIN. ACRES	3,075.73	5,744.20	2,434.49	16,497.28	22,124.36	18,713.46	5,722.69	2,231.40	76,543.61
	\$/MIN ACRE	\$12.82	\$12.55	\$34.34	\$54.68	\$106.88	\$62.16	\$205.43	\$127.93	\$79.51
MCLEAN	TOTAL \$	\$0.00	\$0.00	\$0.00	\$0.00	\$160.00	\$0.00	\$960.00	\$80.00	\$1,200.00
	MIN. ACRES	0.00	0.00	0.00	0.00	80.00	0.00	960.00	80.00	1,120.00
	\$/MIN ACRE	\$0.00	\$0.00	\$0.00	\$0.00	\$2.00	\$0.00	\$1.00	\$1.00	\$1.07
MOUNTRAIL	TOTAL \$	\$0.00	\$12,215.68	\$0.00	\$2,080.00	\$1,026,228.65	\$2,056,930.95	\$866,662.09	\$39,760.00	\$4,003,877.37
	MIN. ACRES	0.00	1,526.04	0.00	40.00	20,395.27	12,534.45	21,834.09	800.00	57,129.85
	\$/MIN ACRE	\$0.00	\$8.00	\$0.00	\$52.00	\$50.32	\$164.10	\$39.69	\$49.70	\$70.08
RENVILLE	TOTAL \$	\$0.00	\$0.00	\$160.00	\$871.00	\$240.00	\$240.00	\$0.00	\$0.00	\$1,511.00
	MIN. ACRES	0.00	0.00	160.00	391.00	240.00	240.00	0.00	0.00	1,031.00
	\$/MIN ACRE	\$0.00	\$0.00	\$1.00	\$2.23	\$1.00	\$1.00	\$0.00	\$0.00	\$1.47
STARK	TOTAL \$	\$12,962.05	\$2,664.00	\$12,431.53	\$17,075.23	\$4,080.00	\$0.00	\$0.00	\$0.00	\$49,212.81
	MIN. ACRES	2,330.41	328.00	725.87	415.03	560.00	0.00	0.00	0.00	4,359.31
	\$/MIN ACRE	\$5.56	\$8.12	\$17.13	\$41.14	\$7.29	\$0.00	\$0.00	\$0.00	\$11.29
WARD	TOTAL \$	\$80.00	\$0.00	\$0.00	\$0.00	\$373.01	\$80.00	\$1,000.00	\$978.66	\$2,511.67
	MIN. ACRES	80.00	0.00	0.00	0.00	373.01	80.00	1,000.00	954.66	2,487.67
	\$/MIN ACRE	\$1.00	\$0.00	\$0.00	\$0.00	\$1.00	\$1.00	\$1.00	\$1.03	\$1.01
WILLIAMS	TOTAL \$	\$480.00	\$41,597.67	\$168,546.30	\$585,919.25	\$1,179,885.50	\$1,087,709.42	\$0.00	\$3,925.37	\$3,068,063.51
	MIN. ACRES	480.00	978.87	4,893.49	9,166.92	9,505.08	26,614.11	0.00	401.37	52,039.84
	\$/MIN ACRE	\$1.00	\$42.50	\$34.44	\$63.92	\$124.13	\$40.87	\$0.00	\$9.78	\$58.96
TOTALS	TOT BONUS \$	\$73,632.50	\$231,359.20	\$388,592.83	\$1,642,472.92	\$5,701,800.05	\$6,767,501.27	\$3,556,593.74	\$794,048.04	\$19,156,000.55
	MIN. ACRES	19,912.86	14,843.33	12,607.80	29,281.95	85,205.64	90,285.25	52,018.86	13,575.65	317,731.34
	\$/MIN ACRE	\$3.70	\$15.59	\$30.82	\$56.09	\$66.92	\$74.96	\$68.37	\$58.49	\$60.29

Surface Management

Michael D. Brand, Director

This division leases and manages surface acres held in trust for various schools and institutions. The major source of income on these lands comes from grazing and agricultural leases, with additional revenue being generated from rights-of-way, salt water disposal, and gravel and scoria mining.

The objective of surface management is to obtain a "fair market" return from the lands while maintaining or improving their condition and value.

LAND MANAGEMENT

Much staff time is spent on day-to-day land management projects that are not remarkable individually but in aggregate result in significant improvement in school trust lands. These projects include:

- Grazing management plans for the improvement of range condition and productivity.
- Reseeding of marginal cropland with native grasses.
- Development of dams and dugouts for livestock water and wildlife enhancement.
- Cooperative clean-up of trash sites and sealing abandoned water wells.
- Reclamation of oil well sites, pipeline rights-of-way, gravel mines and coal mines.
- Monitoring flood affected tracts.

Many of these projects are initiated and completed each biennium while some, such as grazing management plans, require 10-15 years to achieve results.

Another major responsibility of the surface management division is to review and issue easements and permits. The most common easements are for electrical lines, and for oil and gas pipelines and roads. The demand for pipelines and roads has increased because of increased interest due to several active plays and the higher price for oil and natural gas. The larger spacing units associated with the longer horizontal laterals (typically now up to 1,280 acres) means that there are fewer pipelines and roads compared with the 160 acre spacing common to vertical wells.

FIELD PERSONNEL

Roger Martin, Napoleon	1992-Present
Chris Hansen, Napoleon	1998-Present
Robert Meeks, Bismarck	2000-Present
Miles Johnsrud, Watford City	2002-Present
Larry Veikley, Minot	2002-Present
Dale Ferebee, Beach	2005-Present

LEASING

A total of 1,654 grazing and agricultural leases were issued this biennium. Public auctions were held each spring and fall with the leases going to the highest bidder. Leasing success continues to be high with a success rate over 99 percent. Flooding has continued to be a problem in the northeastern part of the state.

Total rental collected for the biennium increased by 3 percent to \$9.2 million from last biennium. This increase is due primarily to changes to the minimum acceptable bids as calculated with the Fair Market Value Method (FMVM). The FMVM tracks changes to the agricultural rental market in various leasing regions, and uses this information to calculate the minimum acceptable bid at public auction for each tract of school trust land.

The rental market for grazing lands has remained strong with an unexpected long run of increasing private land rental rates. Neither reopening of the Canadian border to cattle imports into the United States nor the finding of two cases of BSE (Bovine Spongiform Encephalopathy, or mad cow disease) in the United States has had any noticeable affect on the demand for grazing land.

At the fall 2004 lease auctions we asked 585 lessees if they had internet access and found that 57 percent do. Our web site has proven to be an important source of information for lessees and the general public. During this biennium an interactive web based grazing calculator was developed to estimate the number of grazing days on a tract of school trust land based on the numbers, weight and kind of animal grazed. Lessees can use this calculator to determine stocking rates for the school trust land that they lease. A series of twelve fact sheets was also developed covering most aspects of school trust land management and is available on the web and on compact disc mailed to all new lessees.

Land Sales and Acquisitions 2003-2005

Acquisitions:	Acres
Farm Loan Pool	951.48
Railroad Abandonment	52.19
Total Acquisitions	1,003.67
Sales:	
Oakville Prairie	639.00
Capital Electric	5.20
Total Sales	644.20

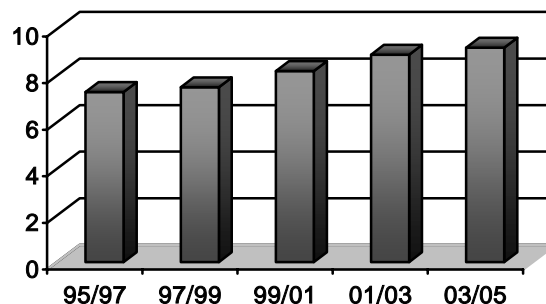
NOXIOUS WEED CONTROL

Biocontrol with flea beetles has continued to show excellent results in controlling leafy spurge on school trust lands. This has increased the income for the trusts and reduced spraying expenses on many tracts. As before, sandy soils are still poor habitat for flea beetles and spraying continues to be the only effective control method on those sites.

No new infestations of spotted knapweed were found on school trust lands and known infestations continued to be monitored for effective control. Saltcedar is being found in new areas throughout the state and the counties have implemented aggressive monitoring programs to identify new infestations. Saltcedar continues to be a major concern because of its aggressive expansion into areas such as brushy river bottoms where it is difficult to find and easily spreads.

A new concern is the spread of Canada thistle. While it used to be considered a cropland weed, it has now aggressively spread into native rangelands. To

Surface Rental \$ in Millions



combat the growing threat, The Department implemented a program to pay for 100 percent of the costs of controlling Canada thistle, knapweed and saltcedar on school trust lands. The Division needs to aggressively control the spread of these weeds to prevent significant losses to income in the future.

SPECIAL PROJECTS

An effort to develop a wind energy easement was initiated in this biennium by the Commissioner. PPM Energy proposed the largest wind farm project in North Dakota to be located in Pierce County. This wind farm will generate 150 megawatts and is scheduled for completion in 2006. One wind turbine is planned for school trust land. Additional turbines will likely be proposed in Burleigh and Oliver Counties in projects being planned by Florida Power and Light Energy (F.P.L.). F.P.L. has been collecting meteorological data from a tower on a tract of school trust land in Burleigh County since 2002 and is ready to construct a wind farm to take advantage of the abundant wind resources.

On August 15, 2004 a large prairie fire (Magpie Camp Fire) burned across a section of school trust land in Billings County and ignited several fires in coal seams. The coal seams continued to burn through the winter of 2004/05 and threatened a salt water disposal well, a road and several pipelines. Most of the coal seam fires were shallow at 4-6 feet deep with one fire being about 20 feet beneath the surface. Coal seam thickness was about 4 feet. In a cooperative project with the ND Public Service Commission, these fires were excavated and extinguished in June 2005. One known fire remains and will be extinguished in the winter, 2005/06.

FORECLOSED AND OTHER PROPERTY

There was only one foreclosure this biennium that resulted in property being deeded to the Board. In addition 52.19 acres of railroad right-of-way were recovered upon abandonment and removal of the rails and ties. One sale of note was the sale of Oakville Prairie in Grand Forks County to the University of North Dakota. This section of native tall grass prairie has served as an outdoor laboratory for over 20 years and is a valuable addition to the University's research and educational programs.

Surface Acres by Trust Fund As of June 30, 2005

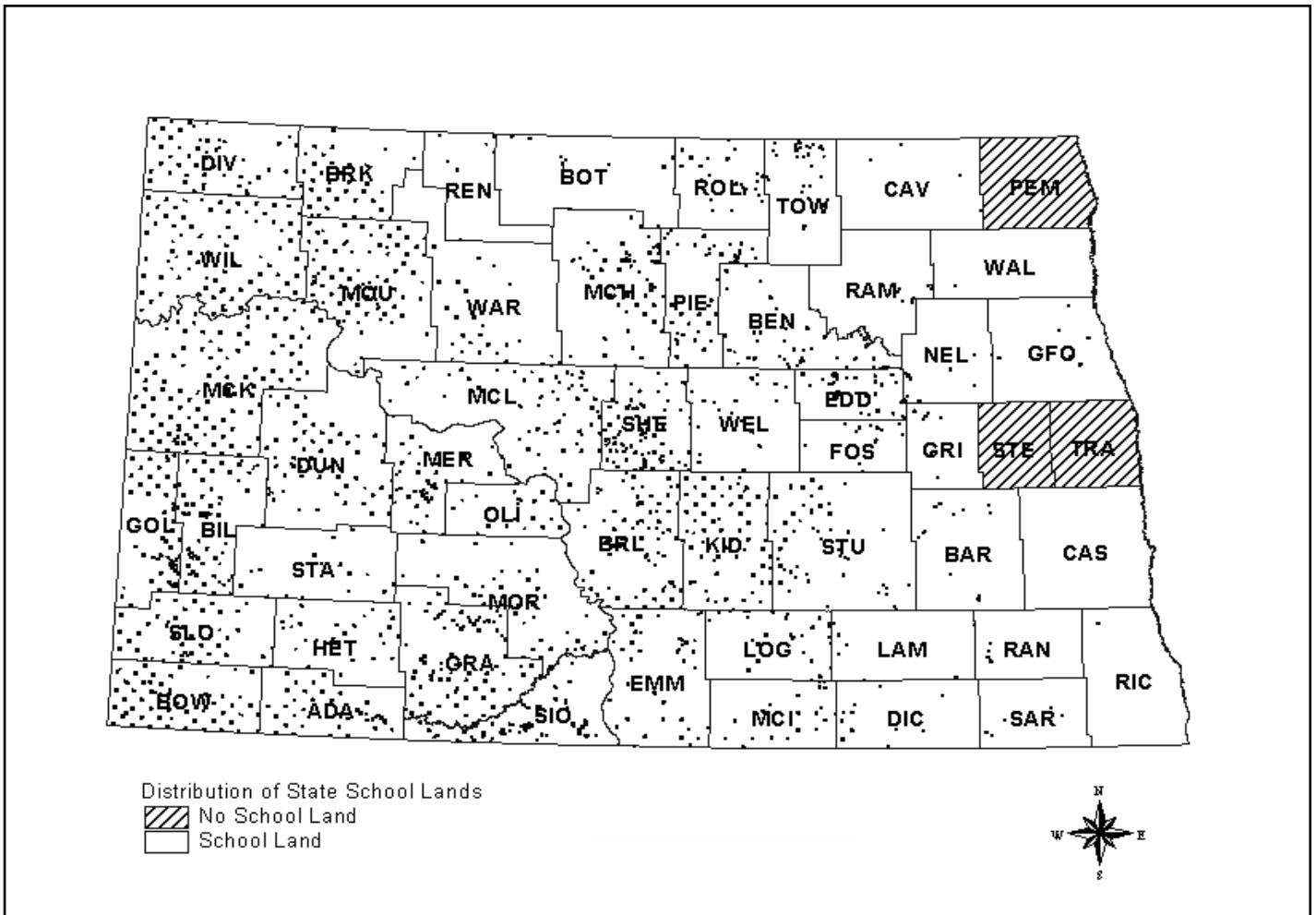
Trust Fund	Acres
Common Schools	635,574.11
School for the Blind	3,481.69
State Capitol	9,991.85
School for the Deaf	4,828.85
Ellendale State College ¹	4,984.17
State Hospital	2,203.91
Industrial School	3,899.43
School of Mines ¹	3,392.03
N.D.S.U.	15,117.68
Veterans' Home	2,913.69
U.N.D.	8,977.98
Valley City State University	640.00
ND State College of Science	3,731.31
Mayville State University	640.00
Valley City/Mayville ²	6,818.08
Farm Loan Pool ³	6,799.48
Total	<u>713,994.26</u>

1. Income from the assets held by the Ellendale Trust Fund is allocated equally among the following institutions: Dickinson State University, Minot State University, NDSU-Bottineau, School for the Blind, Veterans' Home, State Hospital, and State College of Science. The benefits of the original grant to the School of Mines are distributed to the University of North Dakota.
2. Receipts from acreage held jointly by Valley City and Mayville State Universities are allocated 62.5% to Valley City and 37.5% to Mayville.
3. Receipts from this acreage is distributed by formula to all of the above funds except the State Capitol fund.

SURFACE ACRES BY COUNTY

As of June 30, 2005

County	Acres	County	Acres	County	Acres
Adams	17,115.78	Golden Valley	28,983.55	Ramsey	2,056.50
Barnes	2,803.32	Grant	33,638.72	Ransom	1,120.00
Benson	12,725.28	Griggs	1,741.24	Renville	1,910.12
Billings	31,082.07	Hettinger	9,879.60	Richland	513.68
Bottineau	3,597.94	Kidder	28,643.79	Rolette	6,822.88
Bowman	29,310.48	LaMoure	1,435.72	Sargent	1,127.79
Burke	16,119.43	Logan	9,404.92	Sheridan	26,244.81
Burleigh	27,890.13	McHenry	23,360.56	Sioux	23,411.56
Cass	45.47	McIntosh	6,369.87	Slope	23,605.98
Cavalier	596.47	McKenzie	64,714.78	Stark	6,142.64
Dickey	3,980.69	McLean	21,039.90	Stutsman	15,664.01
Divide	21,127.12	Mercer	14,969.38	Towner	8,076.00
Dunn	26,122.70	Morton	19,065.37	Walsh	201.02
Eddy	10,274.62	Mountrail	32,445.36	Ward	11,198.98
Emmons	14,476.80	Nelson	2,853.66	Wells	5,248.63
Foster	3,111.51	Oliver	7,588.41	Williams	38,399.32
Grand Forks	1,434.77	Pierce	14,300.93	Total	<u>713,994.26</u>



Unclaimed Property

Linda Fisher, Administrator

The Unclaimed Property Division administers and enforces the Uniform Unclaimed Property Act (N.D.C.C. ch. 47-30.1). The purpose of the Act is: to collect and safeguard property remitted by holders; to make efforts to locate owners, and to support the Common Schools Trust Fund with interest earned on funds that remain unclaimed. The Act has been in effect since July 1, 1975.

CURRENT UNCLAIMED PROPERTY ISSUES

Gift Certificates and Gift Cards. The popularity and convenience of gift cards skyrocketed during this biennium. Statistically, large percentages of those cards are never redeemed or are only partially redeemed. Nationwide, business owners are aggressively working legislatively to exempt, or keep exempt, reporting unredeemed balances. Since 1997, gift certificates have been by statute "exempt" from the unclaimed property reporting requirement, and an attempt to remove the exemption and again require reporting was defeated by the 2005 Legislative Assembly. Currently, 36 states have varying degrees of reporting requirements; 14 states exempt gift certificate and gift card reporting completely.

Securities Management. While the majority of unclaimed property received comes in the form of cash, the number of securities-related reports is steadily increasing. Securities management is intensely time consuming and more complex than cash management. Thus, many states are reducing the length of time for which they hold securities in securities form prior to liquidation. Likewise, our office reduced our holding period from three report years to one report year in this past biennium.

Operation Rightful Owner. Still in conceptual stages, this initiative proposes that State Unclaimed Property Offices enter into a cooperative agreement with the Federal Treasury to establish a program to reunite uncashed and matured Savings Bonds with owners.

PROGRAM ENHANCEMENTS

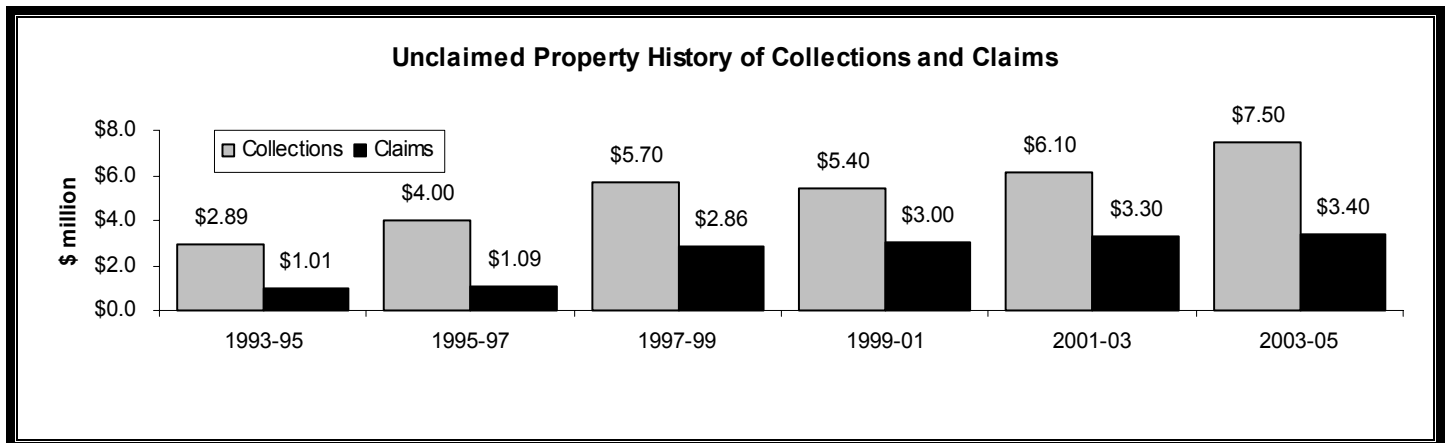
The establishment of an Audit Division in the Department early in 2005 provided an opportunity for a full-time staff person to be heavily involved not only in seminar and group education settings, but also with one-on-one holder contacts with businesses that have never submitted an unclaimed property report. Furthermore, more staff time is being devoted to educating accounting and finance professionals who more and more are the parties responsible for unclaimed property compliance for their clients. The intent is to increase awareness of the statutes and the requirements set out therein without having to enter into actual audit situations wherever possible.

LEGISLATIVE CHANGES

2005 legislation eliminated property values from publication requirements, thereby significantly reducing the temptation for the filing of fraudulent claims.

BIENNIAL HIGHLIGHTS

Demutualization. As shown in the chart below, unclaimed property proceeds increased significantly in the past two fiscal years, but the amount of claims paid stayed fairly level (at approximately 2,000 claims per year). The increase in revenue was largely due to receiving proceeds from mutual insurance companies which were "demutualized" over the past several years. The demutualization process resulted in funds being owed to policy holders and beneficiaries - many of them on policies that were written as far back as the 1930s. Naturally, many of the people entitled to these funds have either passed away or have moved from the address the insurance companies had on file for them. Three of the most notable companies to submit demutualization property in this biennium were John Hancock, MetLife, and Prudential.



Investments

Jeff Engleson, Director

The Investment Division is responsible for directing, implementing, coordinating and monitoring all aspects of the Land Board's investment program.

As of June 30, 2005, the total value of investment assets managed by the Division was approximately \$782.95 million. The bulk of these assets (\$718.46 million) are owned by the 13 permanent education trusts under the Board's control, while the remainder are owned by the Coal Development, Land & Minerals and Capitol Building trust funds. Listed below is a breakdown of the investment assets managed by the Division, by asset type:

- ◆ **Marketable Securities and CDs:** The total value of investment securities and Certificates of Deposit managed by the Board as of June 30, 2005 was \$720.27 million. \$713.30 million of investment securities are held in trust by our custodian bank, The Northern Trust Company, and are managed by investment professionals that are hired by the Board to achieve specific investment goals and objectives. The Land and Minerals Trust owns \$6.40 million of CDs purchased from the Bank of North Dakota (BND). The Capitol Building Trust owns \$570,000 of BND CDs.
- ◆ **Farm Loan Pool:** As of June 30, 2005, the total value of the Board's pool of farm real estate loans was \$22.84 million. Although BND handles the day-to-day administration of the farm loan pool, the Investment Division works closely with the bank in developing and implementing policies, goals and strategies for farm loans and in monitoring and evaluating the program on an ongoing basis.
- ◆ **Loans to Political Subdivisions:** As of June 30, 2005, the Board had total outstanding loans, to various political subdivisions, of \$39.84 million. Legislatively directed loan programs from the Coal Development Trust Fund total \$36.45 million as of that date, and include \$34.42 million in school construction loans and \$2.03 million in loans to various energy impacted political entities. In addition, the Common Schools Trust Fund has two outstanding loans, totaling \$3.39 million, which have funded the building and furnishing of group homes for the developmentally disabled.

INVESTMENT GOALS AND OBJECTIVES

The type of investment assets owned by each trust fund managed by the Board is determined by the nature or purpose of the fund, and investment goals and objectives of the fund.

The 13 educational trust funds managed by the Board are permanent in nature, and were established to provide funding for education in North Dakota, both today, and for future generations. The long range goal for the permanent trusts is to have an investment program that will allow trust assets and distributions to beneficiaries to increase at a rate that meets or exceeds the historic annual rate of inflation (4 percent/year). To that end, the Board developed a long-term investment allocation plan to include a well diversified portfolio of stocks, bonds and other assets.

The primary purpose of the Coal Development Trust Fund is to provide loans to political subdivisions, as directed by the Legislature. The Board is responsible for administering the trust, and investing any moneys that have not been loaned. As of June 30, 2005, outstanding loans to political subdivisions totaled \$36.46 million, while the Board invested the remaining \$21.07 million of this trust's assets. Because of the limited authority the Board has over this trust, its assets are invested in a relatively short-term, high-quality bond portfolio, that can be liquidated as needed, to fund loan programs adopted by the Legislature.

The expendable nature of the Land & Minerals and Capitol Building trust funds result in these trusts being invested in short-term, high-quality bonds and CDs, that have minimal chance of principal loss.

During the 2003-05 biennium the Board underwent an asset allocation study and began implementing significant changes to the permanent trust funds' investment program as a result of the study. Over time, we expect to continue to develop and improve an investment program that already incorporates the purpose and nature of each trust into an investment plan that meets the goals and objectives of the trust.

PERMANENT TRUST INVESTMENT ASSETS

DiMeo Schneider Investment Study:

Prior to the current biennium the Board had successfully implemented an asset allocation plan that significantly increased the permanent trusts' exposure to equity securities while also bringing distribution rates down to more sustainable levels. Although the plan had been very successful, in late-2002, the Board hired the investment consulting firm of DiMeo Schneider & Associates to perform an investment study. The purpose of the study was to help the Board further develop its investment program to better manage the trust funds. The results of the DiMeo Schneider study were presented to the Board in April 2003.

The study included a number of recommendations that were intended to help the Board maintain trust distributions during a time when interest rates were at or near historic lows. The study also included recommendations designed to help improve the Board's investment program over the long-run. During the biennium, the Board began to implement the recommendations that were included in DiMeo Schneider investment study.

Portfolio Changes:

Many of the recommendations in the DiMeo Schneider study involved adopting a more diverse asset allocation. The change in asset allocation was designed to both increase the amount of income generated by the portfolio and also reduce the overall risk of the portfolio. The table below compares the permanent trusts' asset allocation prior to the study to the Board's target asset allocation for the trust funds on June 30, 2005.

ASSET ALLOCATION CHANGES									
	US Bonds & Loans	High Yield	Non-US Bonds	Cash Equiv.	Convertible Securities	Sm/Mid Cap Equities	Large Cap Equities	Intl Equities	REITs
June 30, 2003	45%	6%	0%	1%	11%	11%	15%	11%	0%
June 30, 2005	35% (1)	8%	5%	1%	10%	10%	15%	10%	6%
% Change	-10%	+2%	+5%	0%	-1%	-1%	0%	-1%	+6%

During fiscal year 2004, the Board added three new asset classes to the permanent trusts' investment portfolio, including Real Estate Investment Trusts (REITs), Foreign Bonds, and Treasury Inflation Protected Securities (TIPS), which are included under the US Bonds & Loans heading in the above table. These changes should help reduce portfolio risk while also increasing the amount of income generated by the portfolio. The Commissioner and staff continue to work on other recommendations from the study. These include adding a growth component to the large cap equities portfolio and converting the international equities portfolio from a passive index fund to more actively managed portfolio.

Constitutional Measure #1:

The DiMeo Schneider study contained one recommendation that could have a major impact on the permanent trusts funds for generations to come. That recommendation was to change from the current "income" based approach to the trust management to a "total return" approach to trust management. Under a total return approach to trust management, distributions are determined based on the amount of assets in the trusts and the growth of those assets over time. Under the current approach, distributions are based on the amount of "interest and income" generated by trust assets during a given year.

During the 2005 legislative session, HCR 3037, which is a proposed amendment to Article IX of the N.D. Constitution, was introduced by legislative leaders at the Board's request. HCR 3037 changes the way trust distributions are determined from the current income approach to a total return approach. HCR 3037 was passed by the House by a vote of 84-1 and passed by the Senate by a vote of 41-4.

If approved by North Dakota voters in the November 2006 general election, Constitutional Measure #1 will:

- Help protect the state educational trust funds from the impact of inflation.
- Result in stable, reliable distributions to trust fund beneficiaries.
- Give the Board the ability to more optimally invest trust fund assets to meet its responsibilities to both current and future beneficiaries.

Fixed Income Investments:

When the Board adopted an asset allocation plan in 1995, it decided that the primary objective of the fixed income portfolio would be to generate the long-term, predictable, income and cash flows needed to meet distribution goals. To meet this objective, a fixed income portfolio was built that consisted primarily of high quality, relatively high yielding, loans and fixed income securities, that is managed in more of a "buy and hold" manner than most institutional fixed income portfolios. The fixed income assets managed in this yield-oriented strategy include long-term government and corporate fixed income securities, mortgage backed securities, farm real estate loans, and developmentally disabled loans (DD Loans) #2 and #3. The total amount dedicated to the yield-oriented fixed income portfolio was over \$201 million as of June 30, 2005.

FIXED INCOME ASSETS MANAGED FOR YIELD FOR PERIODS ENDED JUNE 30, 2005, 2004 AND 2003					
<i>Manager/Asset Class</i>	6/30/05 Alloc. (\$ million)	% of Total Portfolio	FY Ended 6/30/05	FY Ended 6/30/04	FY Ended 6/30/03
Bank of North Dakota	\$ 15.56	2.2%	7.22%	7.23%	7.22%
Payden & Rygel Long Term	\$115.36	16.0%	6.03%	6.15%	6.54%
Avg. Yield on Cost – Fixed Income Securities	\$130.92	18.2%	6.20%	6.40%	6.78%
Farm Loan Pool	\$ 22.84	3.2%	7.30%	7.38%	7.84%
DD Loans #2 & #3	\$ 3.39	0.5%	9.00%	9.00%	9.00%
Avg. Yield on Cost – Loans	\$ 26.23	3.7%	7.54%	7.61%	7.78%
Payden & Rygel GNMA/Short Bond Funds	\$ 44.01	6.1%	3.60%	3.01%	3.35%
Avg. Yield on Cost – All Fixed Income Investments	\$201.16	28.0%	5.84%	5.78%	6.46%

With interest rates at or near historic lows the past few years, the average yield of the yield-oriented portfolio declined by about 10 percent during the biennium. With rates so low, principal prepayments and loan payoff in the BND and farm loan pool accounts have continued and the rates at which this principal can be reinvested have declined. Although much of this money has been invested temporarily in the much lower yielding Payden & Rygel GNMA/Short Bond account, the Board has now redeployed some of these funds into other fixed income strategies.

The Board added two new fixed income strategies to its portfolio during the biennium and also hired a new high yield bond manager. Because of the nature of these assets, they are managed for total return, not yield. The Northern Trust TIPS portfolio and Evergreen international fixed income portfolios were added to provide further diversification to the permanent trusts' overall investment portfolio. Lazard was hired as the Board's high yield bond manager after the portfolio team that had previously managed this portfolio moved to Lazard from the previous high yield manager.

FIXED INCOME ASSETS MANAGED FOR TOTAL RETURN FOR PERIODS ENDED JUNE 30, 2005						
MANAGER - Strategy Index	6/30/05 Alloc. (\$ million)	% of Total Portfolio	Last 1 Year (%)	Last 3 Years (%)	Since Incep. (%)	Inception Date
NORTHERN TRUST – TIPS Index Fund	\$47.12	6.6%	9.19	N/A	8.70	6/1/04
LB US Treasury Inflation Notes Index			9.34	N/A	8.63	
EVERGREEN – Intl. Fixed Income	\$36.33	5.0%	8.23	N/A	7.67	4/5/04
ML Broad Global Bond (Ex-US) – Hedged			9.21	N/A	8.74	
LAZARD – High Yield	\$57.72	8.0%	8.00	N/A	6.55	1/1/04
Merrill Lynch HY Bond Index			10.65	N/A	7.92	
Merrill Lynch HY BB/B Index			10.50	N/A	7.73	

During the biennium the Board continued to make a conscious decision to maintain the credit quality of the fixed income portfolio, even if that meant generating less income from the portfolio. Although lowering the credit quality of the portfolio could increase yield, the Board is unwilling to increase the risk of principal loss in order to generate more income.

Equity Securities:

The purpose of the permanent trusts' equity and convertible securities portfolio is to provide the growth needed to reach the Board's ultimate goal of increasing both trust assets, and distributions, at a rate greater than or equal to inflation. In order to help accomplish this goal, the Board has increased the permanent trusts' exposure to equity securities from approximately 33 percent in 1995 to 52 percent on June 30, 2005.

The permanent trusts' equity asset mix includes allocations to large-capitalization U.S equities, small- and mid-capitalization U.S equities, real estate investment trusts (REITs), international equities and convertible securities. The current weighting of each asset class in the equity portfolio is based on the DiMeo Schneider study. The schedule below summarizes the position of our combined equity and convertible securities portfolio as of June 30, 2005, and its performance since the Board implemented an asset allocation plan in August 1995.

EQUITY & CONVERTIBLE SECURITIES NET RETURNS FOR PERIODS ENDED JUNE 30, 2005							
<u>Asset Class MANAGER</u>	<u>6/30/05 Allocation (\$ mil.)</u>	<u>% of Total Portfolio</u>	<u>Last 1 Year (%)</u>	<u>Last 3 Years (%)</u>	<u>Last 5 Years (%)</u>	<u>Since Inception (%)</u>	<u>Inception Date</u>
<i>Benchmark/Index</i>							
<u>Large Cap U.S. Equities</u>							
<i>STATE STREET - S&P 500 Index Fund</i>	\$70.91	9.9%	6.32	8.27	-2.38	4.21	2/1/98
<i>S&P 500</i>			6.32	8.28	-2.37	4.22	
MISSOURI VALLEY PARTNERS	\$35.11	4.9%	6.17	8.88	7.28	6.86	4/1/00
<i>Russell 1000 Value</i>			14.05	10.99	6.55	5.26	
<u>Small/Mid Cap U.S. Equities</u>							
NORTHERN TRUST GLOBAL ADVISORS	\$72.53	10.1%	10.81	10.88	9.10	13.05	3/1/96
<i>NTGA Benchmark (composite index + 2.00%)</i>			13.30	15.00	8.88	11.94	
<u>Real Estate Investment Trusts (REITs)</u>							
DELAWARE INVESTMENT ADVISERS	\$46.95	6.5%	31.60	N/A	N/A	26.07	12/1/03
<i>NAREIT Equity REIT</i>			32.67	N/A	N/A	26.39	
<u>International Equities</u>							
	\$69.25	9.6%	13.69	12.11	-0.54	3.22	3/1/99
<i>STATE STREET - EAFE Index Fund</i>							
<i>MSCI EAFE</i>			13.65	12.06	-0.51	3.19	
<u>Convertible Securities</u>							
TRUST COMPANY OF THE WEST	\$70.12	9.8%	-0.38	8.37	-2.65	9.16	6/30/90
<i>1st Boston/Merrill Lynch Convertibles</i>			1.28	10.25	0.69	9.98	
Combined Equity and Convertibles	\$364.87	50.8%	10.21	10.84	2.35	9.81	8/1/95

All total return figures for periods of 1 year or greater have been annualized.

The permanent trusts' combined equity and convertible securities portfolio continues to perform well, posting an average annual return of 16.83 percent during the biennium. This includes a return of 23.85 percent during fiscal year 2004 and 10.21 percent during fiscal year 2003. The combined equity and convertible securities portfolio has earned an annualized total return of 9.81 percent since August 1995, slightly below the 10 percent total return expected to earn from a diversified portfolio of equity and convertible securities over time.

MONITORING AND EVALUATING PERFORMANCE

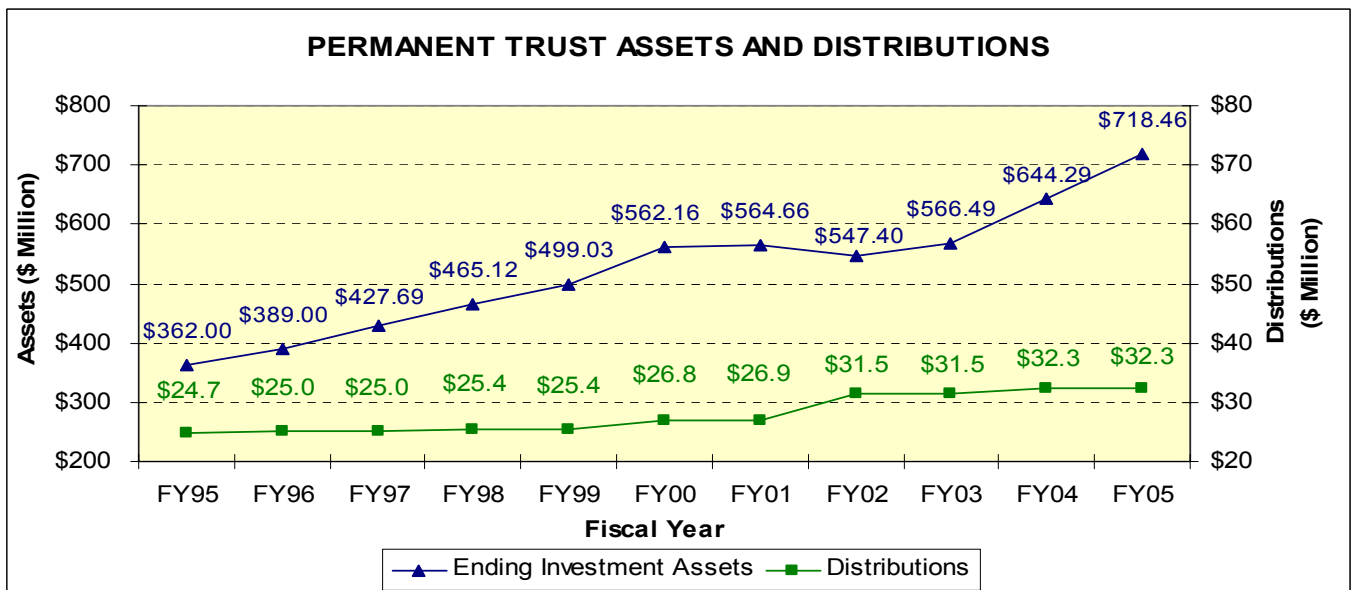
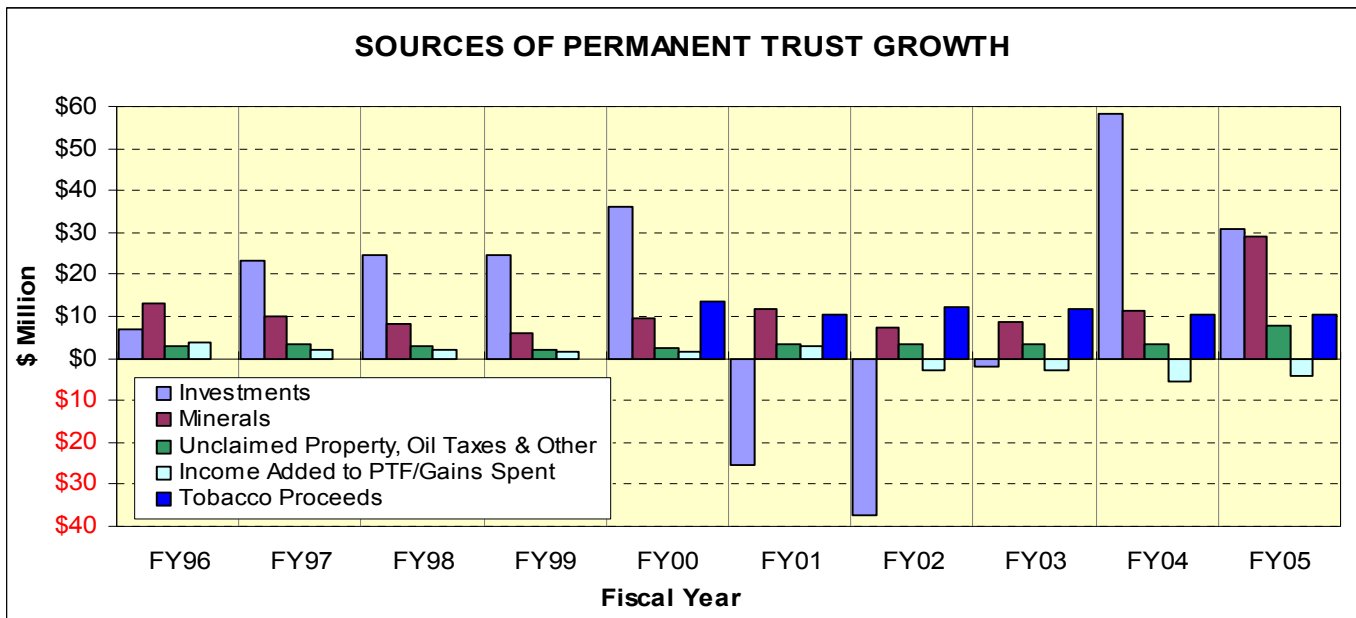
The Investment Division continued to prepare quarterly performance reports for the Board that summarize both the performance of the investment program as a whole and the performance of individual managers, and compares it to established benchmarks and goals. The reports are reviewed by an independent accounting firm to help ensure that accurate data is being presented to the Board.

The Investment Division also performs other functions, as needed, to ensure that the portfolio's overall performance meets the Board's goals and objectives.

SUMMARY

The Land Board's investment program went through numerous changes during the 2003-2005 biennium that were designed to help it better meet the needs of both current and future beneficiaries.

These changes, as well as the changes that will occur if Constitutional Measure #1 is passed by North Dakota voters in November 2006, should result in more stable and consistent distributions to beneficiaries and larger trust growth over the long haul, two things that will benefit all North Dakotans for years to come.



Audit Division

Peggy J. Gudvangen, Director

In 2005, the Audit Division was created to ensure the state trust funds receive their entitled proceeds from abandoned property, mineral royalties and other programs offered through the State Land Department. In addition, the Audit Division evaluates the internal control structure and accounting systems of the Department and provides those results to the Commissioner.

UNCLAIMED PROPERTY

The Audit Division's main objective is to help businesses gain a better understanding of the Uniform Unclaimed Property Act reporting requirements, and assist them with compliance. The Division is accomplishing this through compliance telephone calls, on-site visits and educational seminars to individual businesses throughout the State.

MINERAL ROYALTIES

The Audit Division is responsible for reviewing royalty transactions on mineral leases to ensure payments are in compliance with the oil and gas lease terms, rules and regulations and North Dakota statutes. A comprehensive audit program for conducting mineral royalty audits of lessees is currently being developed.

Permanent Funds

	Schedule of Net Asset Balances		Schedule of Income Available for Distribution by Trust	
	6/30/03	6/30/05	7/01 to 6/03	7/03 to 6/05
Common Schools	\$549,247,497	\$688,309,788	\$67,184,401	\$68,599,421
North Dakota State University	9,502,265	11,328,423	1,373,472	1,334,030
School for the Blind	1,729,801	1,998,611	261,209	247,386
School for the Deaf	2,588,771	3,204,541	386,905	380,835
State Hospital	2,785,894	3,691,446	356,887	364,430
Ellendale State College	1,628,372	1,853,735	272,247	262,417
Valley City State University	2,093,231	2,439,274	317,581	309,345
Mayville State University	1,459,822	1,652,806	225,180	215,472
Industrial School	3,490,100	4,139,172	512,651	491,076
State College of Science	2,616,653	3,256,892	364,820	362,921
School of Mines	2,757,757	3,544,902	379,816	382,889
Veterans Home	2,083,680	2,403,353	284,569	273,265
University of North Dakota	5,234,393	6,657,761	706,604	747,002
Total	\$587,218,236	\$734,480,705	\$72,626,342	\$73,970,489

	Schedule of Distributions By Trust		Schedule of Permanent Fund Receipts By Trust	
	7/01 to 6/03	7/03 to 6/05	7/01 to 6/03	7/03 to 6/05
Common Schools	\$57,793,000	\$60,000,000	\$45,394,594	\$69,195,362
North Dakota State University	1,316,081	1,141,089	281,942	643,447
School for the Blind	250,425	215,476	11,682	64,924
School for the Deaf	385,193	323,948	70,180	289,633
State Hospital	336,410	292,000	181,444	528,080
Ellendale State College	267,540	234,062	1,872	38,051
Valley City State University	308,749	269,600	44,650	96,344
Mayville State University	218,662	186,000	8,921	19,531
Industrial School	494,294	398,756	40,216	201,311
State College of Science	351,622	308,205	87,410	311,308
School of Mines	358,863	312,000	106,777	421,374
Veterans Home	276,302	238,016	40,348	70,327
University of North Dakota	634,235	634,000	530,199	719,145
Total	\$62,991,376	\$64,553,150	\$46,800,236	\$72,598,837

Schedule of Sources of Income Available for Distribution

	7/01 to 6/03	7/03 to 6/05
Investment Income	\$40,169,511	\$40,773,189
Loan Income	8,828,901	4,553,500
Rents	8,628,655	9,505,149
Amortization of Gains & Losses	15,144,145	19,037,877
Other	(144,870)	100,774
Total	\$72,626,342	\$73,970,489

Schedule of Sources of Permanent Fund Receipts

	7/01 to 6/03	7/03 to 6/05
Mineral Bonus	\$520,741	\$14,229,794
Oil Extraction Taxes	4,014,425	7,350,267
Tobacco Collections	23,998,745	20,977,122
Royalties	15,518,119	26,207,056
Unclaimed Property	2,748,206	3,834,598
Other	-	-
Total	\$46,800,236	\$72,598,837

Other Funds

	Schedule of Net Asset Balances		Schedule of Distributions	
	6/30/03	6/30/05	7/01 to 6/03	7/03 to 6/05
Capitol Building Fund	\$308,985	\$666,421	\$1,000	\$37,500
Coal Development Fund	56,464,579	57,853,452	3,590,000	2,767,981
Land & Minerals Fund	641,126	6,820,582	3,545,102	2,000,000
Total	\$57,414,690	\$65,342,460	\$7,136,102	\$4,807,486