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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH, CENTRAL DIVISION

JAKE C. PELT, et al., Plaintiffs, vs. STATE OF UTAH, Defendant	**MEMORANDUM IN OPPOSITION TO PLAINTIFFS' MOTION FOR PARTIAL SUMMARY JUDGMENT RE: UTAH'S DUTY TO DEMONSTRATE IN ITS ACCOUNTING THAT IT COMPLIED WITH ITS DUTY TO INVEST** **And** **IN SUPPORT OF DEFENDANT'S CROSS-MOTION FOR PARTIAL SUMMARY JUDGMENT RE: UTAH'S DUTY TO INVEST IN FISCAL YEARS 1987 - 1991** Case No. 2:92-CV-639 Judge Tena Campbell

STATEMENT OF ISSUES AND FACTS

Summary Of The Issues

Utah does not question the basic premise that it had a duty to prudently invest surplus portions of the Royalty Fund that were not being expended. Utah disagrees, however, with how the plaintiffs characterize that duty. It is properly defined by Utah statutes that are specific to the Royalty Fund, including the State Money Management Act, and not by the federal statutes that

the plaintiffs reference or by general rules of investment such as the common law versions of the "prudent investor" rule or the "prudent man" rule. The duty to prudently invest is limited to money held by the Royalty Fund itself; once that money is "expended," there is no ongoing duty to insure that the recipient prudently invests the expended funds. Thus, Utah's duty to prudently invest does not extend to any investment activity by UNDC or UNI of those entities' own surplus funds.

Furthermore, the Plaintiffs' Memorandum misses a key point: Because of the nature and purpose of the Royalty Fund, loans were made from the Royalty Fund to UNDC, UNI, and UNI affiliated businesses such as Henry Hillson Company. Those loans were approved "conditional expenditures" of the Royalty Fund for the "health, education and general welfare" of the Beneficiaries, and were intended to "promote, encourage, subsidize or otherwise assist Navajo industrial, agricultural or business enterprise;" they were not "investments" of Surplus Royalty Funds subject to a duty to prudently invest. Utah is not required to show that those loans were prudent investments; instead Utah need only show that it was entitled to expend the money for the designated purposes under the 1933 Act, as amended by the 1968 Act.

During fiscal years 1987 through 1991 (July 1, 1987 – June 30, 1991), Utah's duty to invest was defined by the State Money Management Act, and in particular by Utah Code section 51-7-11. The undisputed facts show that Utah's investments of Surplus Royalty Funds during those years complied with the State Money Management Act, and that the interest generated by those investments was returned to the Royalty Fund. Therefore, Utah should be granted partial summary judgment establishing that it properly invested Surplus Royalty Funds during fiscal year 1987 - 1991.

Response To Plaintiffs' Statement of Undisputed Facts

Utah responds to the plaintiffs' statement of allegedly undisputed facts as follows:

Alleged Fact 1: By act of Congress, Act of March 1, 1933, 47 Stat. 1418 ("1933 Act"), as amended by Public Law 90-066, 82 Stat. 121 (1968) ("1968 Act"), Utah is trustee of the NTF. *Pelt v Utah*, No. 2:92-CV-639 TC, Order and Mem. Decision [Doc. 1017] at 3 (Jan. 11, 2006)("2006 Order").

Response: Utah admits that the Tenth Circuit Court of Appeals has held in this action that by the 1933 Act "Congress intended to create a discretionary trust for the benefit of the San Juan Navajos with the State of Utah as trustee … ." *Pelt v. Utah*, 104 F.3d 1534, 1544 (10th Cir. 1996). Neither the 1933 Act nor the 1968 Act uses the terms "trust" or "trustee." Judicial decisions starting with *Sakezzie v. Utah Indian Affairs Comm'n*, 198 F.Supp. 218 (D. Utah 1961) have determined that Utah occupies "a position of trust and confidence toward the Indian beneficiaries" but have also noted that "within the limitations of the said Federal Act of March 1, 1933, 47 Stat. 1418, the defendants of necessity must have, and do have, a wide administrative discretion in determining the management and expenditure of said fund." 198 F.Supp. at 224. Utah uses the term Royalty Fund (rather than "NTF" or "Navajo Trust Fund") to refer to the funds accrued under the 1933 Act and the 1968 Act prior to the enactment of Utah Laws 1992, chapter 195, sections 4 – 10, which created the "Navajo Trust Fund" as a defined entity.

Alleged Fact 2: Plaintiffs ("Beneficiaries"), a group of Navajo Indians and other statutorily specified Indians residing in San Juan County, Utah, are the beneficiaries of the NTF. *See*, 1933 Act, as amended by 1968 Act; 2006 Order at 3.

Response: Utah admits that the original 1933 Act defined the class for whom the Royalty Fund was to be administered as "the Indians residing" on "lands hereby added to the Navajo Reservation" and that the 1968 Amendment redefined both the class and the geographical boundaries of residence as "the Navajo Indians residing in San Juan County." 47 Stat. 1418 (1933) (the "1933 Act"); 82 Stat. 121 (1968) (the "1968 Act").

Alleged Fact 3: The Beneficiaries and those whom they represent are largely impoverished and isolated from modern services and utilities. *See*, *Sakezzie v. Utah Indian Affairs Comm'n*, 198 F.Supp. 218, 220 – 22 (D. Utah 1961)("*Sakezzie I*"); *Sakezzie v. Utah Indian Affairs Comm'n*, 215 F.Supp. 12, 22 (D. Utah 1963)("*Sakezzie II*"). They are also largely uneducated and without opportunity for employment other than traditional livestock herding. *See id.*

Response: Utah denies this alleged fact. Moreover, the plaintiffs have failed to cite any record evidence in support of this allegation. The findings of fact in the two cited *Sakezzie* decisions only establish the status of the Beneficiaries as of 1961 and 1963. They say nothing about the current status of the Beneficiaries. Utah disputes that current conditions, with respect to poverty, and isolation from modern services and utilities, are the same as existed nearly 50 years ago when the *Sakezzie I* and *Sakezzie II* decisions were issued. Utah further disputes that current educational and employment opportunities are currently the same as existed 50 years ago. Plaintiffs cite no record or other authorities supporting the allegation that conditions for the San Juan County Navajo are the same as existed 50 years ago. Furthermore, this alleged fact is irrelevant to this motion.

Alleged Fact 4: The NTF corpus is 37.5% of royalties derived from certain oil and gas leases within a specifically defined portion of the Navajo Nation in the State of Utah. 1933 Act, as amended by 1968 Act; *Pelt v. Utah*, 104 F.3d 1534, 1544 (10th Cir. 1996).

Response: Utah believes that use of the term "corpus," which is not found in either the 1933 Act or the 1968 Act, can be potentially confusing in the context of this motion. Trusts typically are set up so that the corpus is not invaded except under limited circumstances, and the trustee typically spends the income generated by the corpus for the trust purposes. Much of the case law governing trusts assumes that trusts have those characteristics, and therefore emphasizes both the need to preserve the corpus and the need to maximize revenue from investment, since that is the primary method by which the trust performs its functions. The 1933 Act and the 1968 Act, however, direct Utah to expend the royalties instead of holding on to them to form a traditional "corpus." *See*, Additional Material Fact 7, below. Thus, any money held in the Royalty Fund is better characterized as "Surplus Royalty Funds" – funds that are available for investment while awaiting expenditure – rather than as the normal "corpus" of a trust.

Alleged Fact 5: Through the years, the leases in which the NTF has an interest produced significant quantities of oil and gas and substantial sums of money were generated from those leases. See, e.g., *Sakezzie I*, 198 F.Supp. 219.

Response: Other than noting that the terms "significant" and "substantial" are vague, Utah does not disagree with the assertions of this alleged fact for purposes of this motion.

Alleged Fact 6: In this litigation, the Beneficiaries seek a complete and accurate accounting from their trustee, Utah, containing detailed information on income, expenses, disbursements, and investments of the NTF. See, Verified Compl. at pp. 18 – 19, 23 –24.

Response: Utah agrees that the Fifth Cause of Action (Interest and Investment) asserts at paragraph 63 that Utah "was under a duty … to invest Trust funds so that they would produce income." *See*, Verified Complaint, ¶ 63.

Statement Of Additional Material Facts

Utah asserts that the following facts are material to the resolution of this motion:

Additional Fact 7: Under the 1933 Act, "said 37½ per centum of said royalties shall be expended by the State of Utah in the tuition of Indian children in white schools and/or the building or maintenance of roads across the lands described in section 1 hereof, or for the benefit of the Indians residing therein." The 1968 Act redefined the purposes for which the 37½% could be expended to include spending "for the health, education, and general welfare of the Navajo Indians residing in San Juan County," but did not change the concept that the money was to be **expended**, and not saved as a permanent "corpus." *See*, 47 Stat. 1418 (1933) (the "1933 Act"); 82 Stat. 121 (1968) (the "1968 Act").

Additional Fact 8: The Utah legislature created the Utah Indian Affairs Commission by enacting Utah Laws 1959, chapter 120, sections 1 through 6, codified as Utah Code sections 63-22-1 – 6: **Indian Affairs Commission**. Those statutes address the permissible expenditures of the Royalty Funds and the permissible investment of those funds:

> 63-22-3. **Moneys received under Act of Congress – How expended.**
> All moneys received by the state under the provisions of the Act of Congress of March 1, 1933, 47 Stat. 1418, extending the Navajo Indian Reservation in Utah shall be expended under the direction of the commission in accordance with the provisions of the said act and such amendments thereto as may be from time to time enacted by the United States Congress.
>
> §63-22-4. **Powers of commission – The commission may:**
> … (4) to invest any surplus funds not anticipated to be spent by the commission at least within one year from the date the investment in United States government bonds or

> securities, or bonds or securities of the state of Utah at the highest interest rate that may be available at the said time, provided that the bonds or securities shall be redeemable not more than five years after the date of their issuance.

See, Statutory Appendix, Part I: Indian Affairs Commission Act of 1959, submitted with this memorandum. Note that section 63-22-4(4) refers to investment of "any surplus funds" and not "the corpus of the trust."

Additional Fact 9: In 1967, the Utah Indian Affairs Commission was replaced by the Utah Board of Indian Affairs (the "UBIA"). Utah Code sections 63-22-1 through 6 were repealed and replaced by Utah Code sections 63-36-1 through 8: **Indian Affairs**, pursuant to Utah Laws 1967, chapter 174, sections 154 through 161. The new statutes again specified how funds could be invested and expended:

> §63-36-3. **Board of Indian affairs – Powers and duties – Investments.**
> … Funds which will not be used within one year from the date they become available to the board shall be invested in United States government bonds or securities, or bonds or securities of the state of Utah at the highest rate that may be available at the time, provided that the bonds or securities shall be redeemable not more than five years after the date of their issuance.

> 63-36-7. **Moneys received under Act of Congress – How expended.**
> All moneys received by the state under the provisions of the Act of Congress of March 1, 1933, 47 Stat. 1418, extending the Navajo Indian Reservation in Utah, shall be expended under the direction of the board of Indian affairs in accordance with the provisions of the said act and such amendments thereto as may be from time to time enacted by the United States Congress.

See, Statutory Appendix, Part II: 1967 Statutes Creating The Utah Board Of Indian Affairs. Note that section 63-36-3 specifically defines the funds to be invested as those "which will not be used within one year" and not as "the corpus of the trust," even though this statute was passed after the two *Sakezzie* decisions.

Additional Fact 10: Utah Code section 63-36-7, regarding expenditures, was substantially expanded in 1977, per Utah Laws 1977, chapter 238, section 1, to better define the permissible uses of the Royalty Fund:

> 63-36-7. **Moneys received under Act of Congress – How expended.**
> All moneys received by the state under the provisions of the Act of Congress of March 1, 1933, 47 Stat. 1418, extending the Navajo Indian Reservation in Utah, shall be expended under the direction of the Board of Indian Affairs in accordance with the provisions of the said act and such amendments thereto as may be from time to time enacted by the United States Congress. The board may, within the limits and consistent with the provisions of the act, **expend monies to promote, encourage, subsidize or otherwise assist Navajo industrial, agricultural or business enterprise in San Juan County for the improvement of economic conditions and employment prospects of San Juan County Navajos**.

See, Statutory Appendix, Part III: 1977 Amendment To Utah Code Section 63-36-7 (emphasis added). Note that the first UBIA authorized loan, to the Henry Hillson Company, did not occur until July 21, 1978, after section 63-36-7 was expanded to clarify that money could be expended to "subsidize" Navajo business enterprise. The expanded version of section 63-36-7 remained unchanged until the repeal of Utah Code sections 63-36-1 through 8: **Indian Affairs** by Utah Laws 1991, chapter 284, section 27. The successor statute is the Navajo Trust Fund Act, Utah Code sections 63-88-101 through 107. *See*, Statutory Appendix, Part VI: 1992 Utah Navajo Trust Fund Act.

Additional Fact 11: The criteria for investment of Surplus Royalty Funds were removed from Utah Code section 63-36-3 and a new section 63-36.5 was added pursuant to Utah Laws 1978, chapter 10, section 2, which made investment of the Surplus Royalty Funds subject to the portion of the Utah State Money Management Act that governs investment of public funds, Utah Code section 51-7-11:

> §63-36-3.5 **Investments.**
> Funds not allocated for use by the Board of Indian Affairs shall be invested in accord with Section 51-7-11.

See, Statutory Appendix, Part IV: 1978 Amendment Creating Utah Code Section 63-36-3.5. Note that it is "[f]unds not allocated for use," in other words Surplus Royalty Funds and not the traditional "corpus" of a trust, that "shall be invested."

Additional Fact 12: Utah Code section 63-36-3.5 remained unchanged until it was repealed by L. 1991, ch. 284, §27 (effective April 29, 1991). It was replaced by the passage of the Navajo Trust Fund act, Utah Code sections 63-88-101 through 107, L. 1992, ch. 195, §§4 – 10. The investment provision of that act requires the Utah State Treasurer to comply with the State Money Management Act:

> §63-88-102. **Trust Fund – Creation – Oversight**
> (4)(a) The state treasurer shall invest fund monies by following the procedures and requirements of Title 51, Chapter 7, State Money Management Act.
> (b)(i) The fund shall earn interest.
> (ii) The state treasurer shall deposit all interest or other revenue earned from investment of the fund back into the fund.

See, Statutory Appendix, Part VI: 1992 Utah Navajo Trust Fund Act. In short, prior to 1978, investments were to be in "United States government bonds or securities, or bonds or securities of the state of Utah at the highest rate that may be available at the time, provided that the bonds or securities shall be redeemable not more than five years after the date of their issuance." See, Utah Code §63-22-4, repealed and replaced by §63-36-3. Subsequently, investments were to be made in accordance with the State Money Management Act.

Additional Fact 13: The referenced portion of the State Money Management Act, Utah Code section 51-7-11, had been amended by Utah Laws 1974, chapter 27, section 19 and read as of 1978 as follows:

> 51-7-11. **Authorized deposits or investments of public funds.**
>
> (1) **All public funds, other than** funds of the state retirement board, **funds of the board of Indian affairs,** the permanent school fund and other funds of the division of state lands, the state insurance fund, and funds of member institutions of the state system of higher education not transferred to the state treasurer by section 51-7-4, may be deposited or invested only in such of the following as meet the criteria of section 51-7-17:

The quoted section was followed by a lengthy list of permissible types of investments. *See*, Statutory Appendix, Part V: Utah State Money Management Act Excerpts (emphasis added).

Additional Fact 14: Utah Code section 51-7-11 has been amended repeatedly over the years. However, the language excluding "funds of the board of Indian Affairs" from the list of authorized investments continued until the revision of Utah Code §51-7-11 by Utah Laws 1992, chapter 285, section 20, effective April 27, 1992:

> 51-7-11. **Authorized deposits or investments of public funds.**
> (3) All public funds, other than funds of the permanent land grant trust funds established pursuant to the Utah Enabling Act and the Utah Constitution, and funds of member institutions of the state system of higher education acquired by gift, devise, or bequest, may be deposited or invested only in the following assets that meet the criteria of Section 51-7-17:

See, Statutory Appendix, Part V: Utah State Money Management Act Excerpts.

Additional Fact 15: As of 1978, the State Money Management Act contained a prudent man rule, as amended by Utah Laws 1974, chapter 27, section 22:

> § 51-7-14. **Prudent man rule for management of investments--Sale of security or investment for less than cost.**
> (1) Selection of investments as authorized by Sections 51-7-11, 51-7-12, and 51-7-13 shall be made with the exercise of that degree of judgment and care, under circumstances then prevailing, which men of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation but for investment, considering the probable safety of their capital, as well as the probable benefits to be derived and the probable duration for which such investment may be made, and considering the investment objectives specified in Section 51-7-17.

> (2) A public treasurer may sell or otherwise dispose of at less than cost any security or investment in which public funds under his jurisdiction have been invested if such sale or other disposition shall tend to maximize the benefits that may be derived from such changed investment.

Utah Code section 51-7-14 was amended in 1984. The legislature changed the phrase "disposition shall tend to maximize" to "disposition tends to maximize." There were no other amendments until after the time period at issue in this lawsuit. *See*, Statutory Appendix, Part V: Utah State Money Management Act Excerpts.

Additional Fact 16: Utah State Treasurer Edward T. Alter is the government official who is charged by law with investing state money, including the Surplus Royalty Funds. Mr. Alter is the government official who is most responsible for interpreting Utah laws relating to the investment of state money, including interpreting the State Money Management Act and the statutes relating specifically to investment of the Royalty Fund. Mr. Alter is an expert in managing government trust funds in general, and the Royalty Fund in particular. He has substantial knowledge concerning what is considered acceptable and appropriate business practices regarding the management of state trust funds. *See*, Affidavit Of Utah State Treasurer Edward T. Alter Re: Navajo Royalty Fund Investments And Royalty Fund Loans, attached hereto as Exhibit "A," ("Treasurer Alter's Affidavit"), at ¶¶ 3 – 9.

Additional Fact 17: Kelly R. Johnson is Utah's primary forensic accounting expert in this case. He has approximately 18 years experience as a certified public accountant, specializing in forensic accounting. His professional designations, in addition to a CPA, include being Accredited in Business Valuation (ABV) and a Diplomate of the American Board of Forensic Accounting (DABFA). *See*, Affidavit of Kelly Johnson Re: Navajo Royalty Fund

Investments And Royalty Fund Loans, attached hereto as Exhibit "B," ("Johnson Investments And Loans Affidavit"), at ¶¶ 2 – 4, 7.

Additional Fact 18: From at least February 3, 1960, Utah has consistently invested Surplus Royalty Funds in order to earn interest on those funds. An accounting, showing both a statement of investments and a statement of investment activity for the Royalty Fund for each year from Fiscal Year 1960 (starting July 1, 1959) through Fiscal Year 1992 (ending June 30, 1992) is attached hereto as Exhibit "C" (the "Investment Accounting"). Each year of the Investment Accounting is comprised of two documents: A "Statement of Investments" is a ledger that shows the investments held at the close of the fiscal year (on June 30th); a "Statement of Investment Activity" shows all purchases, redemptions, and other investment activities during the fiscal year. The Investment Accounting is essentially derived from the accounting provided in Utah's First Supplemental Accounting, which was produced on August 29, 2000. *See*, Johnson Investments And Loans Affidavit, ¶¶ 8 – 10,which explains the nature of the accounting and the minor differences from the First Supplemental Accounting, Docket No. 677.

Additional Fact 19: Except for the one CD that was pledged as security for a loan from a bank to FNAC (discussed in Additional Fact 29, Loan "E-6," below) all investments shown on the Investment Accounting were redeemed, interest was earned, and none were written off as losses. All interest earned on investments, as shown by Exhibit "C," was added to the Royalty Fund. *See*, Exhibit "C"; Johnson Investments and Loans Affidavit, at ¶ 20 – 21.

Additional Fact 20: The 1974 letter attached to the Plaintiffs' Memorandum as Exhibit "A," from the Acting Deputy Commissioner of Indian Affairs of the United States Bureau of Indian Affairs to "area directors" regarding the investment of federally controlled Indian trust

funds, has no relevance and lacks foundation. It is not directed to any Utah state government official and there is no evidence that it was intended to be sent to, or was received by, any Utah government official. Nothing in the letter states that it applies in any way to Utah. Mr. Alter states in his affidavit that he had never seen the letter prior to the filing of the Plaintiffs' Memorandum. *See,* Treasurer Alter's Affidavit, ¶ 11.

Additional Fact 21: As the Utah State Treasurer, Mr. Alter is obliged to follow Utah Code provisions, including those set forth above, unless those provisions have been declared unconstitutional. Since the provisions governing investment of the Surplus Royalty Funds were never declared unconstitutional, Mr. Alter had no option but to follow them, and could not have chosen to apply a common law "prudent man" or "prudent investor" standard. During the time the Mr. Alter has been the Utah State Treasurer, compliance with the State Money Management Act has been the relevant standard for prudently investing the Surplus Royalty Fund (and after 1992, the Navajo Trust Fund). As a result, the Surplus Royalty Funds are invested with the same level of care and risk as other state money for which Mr. Alter has been responsible *See*, Treasurer Alter's Affidavit, ¶ 13 – 15.

Additional Fact 22: Treasurer Alter has reviewed the investments shown on the Investment Accounting for the time period covered by fiscal years 1987 – 1991, beginning with the Statement of Investments as of June 30, 1986, which shows the Surplus Royalty Fund investment portfolio as of the beginning of fiscal year 1987. He has concluded that each of the investments shown on the Investment Accounting for that time period, including investments in the Public Treasurer's Investment Pool, satisfied the standards of the State Money Management Act and was a prudent investment. *See,* Treasurer Alter's Affidavit, ¶ 23 – 24.

Additional Fact 23: The State Money Management Act permits a wide variety of investments of varying degrees of risk. For example, Utah Code section 51-7-11(i) permits investment in fixed rate, publicly traded corporate obligations (i.e. bonds) that are "A" rated by Moody's Investors Service or Standard and Poor's, but which are not guaranteed. Such securities are not risk free, and the degree of risk, while generally low, varies among bonds, and between bonds and other permitted classes of investments. Because of the vast number of potentially permissible investments under section 51-7-11, and the varying risk factors from investment to investment, it is impossible to say that any particular pool of State Money Management Act investments achieved the highest possible rate of return. The version of the "prudent man" rule that applies to investments under the State Money Management Act, as set forth in Utah Code section 51-7-14, does not require that investments achieve the highest possible rate of return. *See*, Treasurer Alter Affidavit,, ¶ 16.

Additional Fact 24: The Utah Navajo Development Council ("UNDC"), Utah Navajo Industries ("UNI"), and Henry Hillson Company (subsequently known as First Native American Corporation, or "FNAC") are entities that were owned or substantially controlled by San Juan County Navajos during the times relevant to this lawsuit. The UNDC is a Utah non-profit corporation that ran programs that were funded by the Utah Board of Indian Affairs ("UBIA") to promote the health, education and general welfare of San Juan County Navajos. UNI, Henry Hillson / FNAC were related for profit businesses run primarily by San Juan County Navajos. *See*, Treasurer Alter's Affidavit, at ¶¶ 17 – 18; Johnson Investments and Loans Affidavit, at ¶ 11.

Additional Fact 25: Beginning on July 21, 1978 (during Fiscal Year 1979), the UBIA approved, and Utah funded, certain loans from the Royalty Fund to the UNDC, UNI, and Henry

Hillson Company / FNAC. An accounting, showing both a statement of loans and a statement of loan activity for the Royalty Fund for each year from Fiscal Year 1979 (starting July 21, 1978) through Fiscal Year 1992 (ending June 30, 1992) is attached hereto as Exhibit "D" (the "Loan Accounting"). Each year of the Loan Accounting is comprised of two documents: A "Statement of Loans" is a ledger that shows the outstanding loans at the close of the fiscal year (on June 30th); a "Statement of Loan Activity" shows all loans, repayments, write offs, and other loan activities during the fiscal year. The Loan Accounting is simply a copy of the relevant pages of the accounting provided in Utah's First Supplemental Accounting. None of the pages were altered. The backup documentation for the Loan Accounting, such as promissory notes and UBIA meeting minutes, was produced as part of Utah's original UDIA Accounting. *See*, Johnson Investments And Loans Affidavit, ¶¶ 12 – 13.

Additional Fact 26: The Utah Division of Indian Affairs ("UDIA") always kept the investments shown on the Investment Accounting, Exhibit "C," separate on its books from the loans shown on the Loan Accounting, Exhibit "D." Investments were recorded on UDIA's general ledger under account numbers 0290("investments"), 0291 ("investments in treasury pool"), and 0292 ("Indian affairs investments"); loans were recorded under account numbers 0150 ("loans receivable") and 0151 ("loans receivable"). Furthermore, all of the loans were made to either UNDC, UNI or Henry Hillson / FNAC, while there were no investments involving any of those related entities. From this, and the other evidence he reviewed, Kelly Johnson concludes that UDIA's accountants consistently viewed the investments and loans as being different types of transactions. *See*, Johnson Investments And Loans Affidavit, ¶ 14.

Additional Fact 27: There is a critical difference between the "investment" of Surplus Royalty Funds and the loan of funds for approved purposes to the UNDC, UNI or Henry Hillson / FNAC. In the expert opinions of both Mr. Alter and Mr. Johnson, the loans shown on the Loan Accounting should not be considered investments of Surplus Royalty Funds, but rather "conditional expenditures" of Royalty Funds. The purpose of those "loan" transactions was not to invest conservatively with the goal of earning a safe rate of return – the purpose was to promote "the health, education, and general welfare of the Navajo Indians residing in San Juan County," as required by the 1968 Act.

The loans shown on the Loan Accounting can best be thought of as "conditional expenditures" because they were not absolute – there were conditions under which the expenditures could be recouped or avoided (i.e., repayment of the loan, reductions in future grants below budgeted amounts, or payment of underlying debts without causing foreclosure on the collateral). In short, the loans represent situations in which the UBIA was willing to expend Royalty Funds for purposes authorized by the 1968 Act, but the UBIA hoped that conditions would prevail that would allow it to ultimately avoid the expenditure. *See*, Treasurer Alter's Affidavit, ¶¶ 19 – 20; Johnson Investments And Loans Affidavit, ¶¶ 15 – 16.

Additional Fact 28: There are numerous reasons why it would have been logical and prudent from a financial standpoint for Utah to set up expenditures of funds to the non-profit UNDC, and the for profit UNI and Henry Hillson Company / FNAC (collectively "UNI Companies") as conditional "loans" rather than as outright grants. For example, with regard to the UNDC, the UBIA generally approved an annual budget for the UNDC, which was typically paid quarterly. In November of 1982 UBIA approved a line of credit for UNDC to assist with

cash flow problems that UNDC was experiencing between UDIA's quarterly payments, apparently as a result of other government entities not paying UNDC promptly for services rendered. See, Additional Fact 29, Loan "E-2." It was rational for the UBIA to conclude that it was more prudent to permit the UNDC to have a reasonable revolving line of credit that the UNDC would need to repay, rather than having UNDC maintain an expensive line of credit with a bank, or having the UBIA authorizing numerous special grants to cover UNDC's cash flow needs.

With regard to loans to the UNI Companies, it would have been logical and prudent to loan rather than grant money to those Navajo controlled enterprises. By using loans, UBIA could attempt to encourage sound financial management practices. Even if some loans were eventually written off, having the loans on the books could encourage the UNI Companies to value their capital and budget for repayment of the loans. By using loans instead of grants, it was possible to more accurately determine the profitability of the UNI Companies. Also, by giving "seed money" in the form of loans, UBIA made it easier for the UNI Companies to ultimately return the money to the Royalty Fund if the ventures had been successful. Otherwise, as "for profit" corporations, if the UNI Companies had become profitable they would have needed to have made charitable contributions in order to transfer the money back to UDIA. These are just some examples of financially sound reasons why was prudent for UBIA to have approved conditional expenditures in the form of loans, rather than absolute expenditures in the form of grants when UBIA chose to support economic development for San Juan County Navajos through the UNI Companies. *See*, Johnson Investments And Loans Affidavit, ¶ 17 – 18; Treasurer Alter's Affidavit, ¶ 21.

Additional Fact 29: The loans shown on the Loan Accounting vary significantly in their details. Examples of some of the loans and their supporting documentation are attached to this memorandum as Exhibit "E." Those examples include the following loans:

Loan "E-1": This was a $350,000 economic development loan made on August 17, 1979 by the UDIA to the UNDC for the purpose of providing seed money for housing in the town of Montezuma Creek, on the San Juan County portion of the Navajo Reservation, a purpose that clearly falls within the scope of the 1968 Act. The loan was converted to a grant nearly 10 years later. The March 17, 1989 minutes of a special meeting of the UBIA tells the story:

> Montezuma Creek Housing - $350,000
> Mr. Parashonts gave a brief history of this loan made to UNDC by the Office of Indian Affairs about 10 years ago to build homes on designated UDIA property. There are 37 units involved, two units to be kept by UNDC. UNDC was then going to sell these homes at fair market value to the Navajo's, [sic] minus the gratuity, and then payments would revert back to UDIA to pay off the loan. Only $8,000 has been paid back so far. Mr. Glover gave a history of the units and stated that UNDC is asking the UDIA board in light of recommendations of the auditors, that this loan be written off, and that 35 homes would be given a $10,000 UNDC housing grant, to be recognized in the sale of these homes, which would then equal the $350,000.
> …
> Motion: Mr. Sawyer moved that the UDIA Board ratify the resolution of UNDC concerning the $350,000 Montezuma Creek Housing loan. It will be written off and changed to grant status this year. Marion Cita Holly seconded the motion and the motion carried unanimously.

The original $350,000 loan, which consisted of an interest free promissory note, was intended to provide seed money to build housing for San Juan County Navajos residing in Montezuma Creek, and was not intended as an "investment" of Surplus Royalty Funds. It was perfectly reasonable to originally underwrite the housing construction seed money as a loan in the hopes that the homes would sell at fair market

value and the money would be repaid. When that did not occur, it was equally reasonable to convert the loan to a series of $10,000 grants, thereby lowering the cost of housing for San Juan County Navajos.

Loan "E-2": This loan was a revolving line of credit that the UBIA approved for the UNDC as of November 13, 1982 UBIA meeting. Again, the minutes explain the loan:

> In previous meetings the problem of UNDC cash flow has been discussed. For various reasons, agencies contracting with UNDC have been unpredictable in reimbursing UNDC for services provided. As a result, UNDC has had to establish a line of credit with the local bank. This has been beneficial, but has cost UNDC substantial amounts in interest payments. Mr. Worthy Glover proposed to the Board that rather than borrow from the bank, a line of credit should be established with Utah Division of Indian Affairs.
>
> After discussion of the merits of this proposal, upon motion of Dr. Sawyer, seconded by Mr. Lyman, and unanimously carried, it was
>
> RESOLVED, that a line of credit in the amount of $150,000.00 be established and that UNDC is authorized to borrow against this line of credit at no interest, each loan not to exceed 90 days.

The purpose of this loan was to lower the UNDC's administrative and operating expenses, which would allow more of its funds to be used for programs that benefit its constituency, the San Juan County Navajos. The unsecured, interest free line of credit was not an "investment;" it was a form of economic subsidy for UNDC. The specific transaction included in Loan "E-2" is the first use of the line of credit, $150,000 that was borrowed on November 19, 1982 and promptly repaid, on or about January 31, 1983.

Loan "E-3": This $53,255.10 loan was one of a series of loans to UNI for the benefit of Henry Hillson Company, or to Henry Hillson Company directly. It is apparent from the January 19, 1979 UBIA minutes that these loans were made on a quarterly-annual basis to support UNI and Henry Hillson Company. They bear interest, in this case

10 ½%, but the ongoing nature of the loans and the specific dollar amount,[1] coupled with the description in the Board Minutes, evidences that these were more in the form of an economic subsidy than any sort of "investment" for profit. The minutes read:

> Mr. Parry informed the Board that UNI had requested a loan for the Henry Hillson Company quarterly payment. A request has been made for $53,255.10. Upon motion of Mrs. Mojado, seconded by Mr. Timbimboo, and unanimously carried, it was
>
> RESOLVED, that the requested amount of $53,255.10 for the quarterly payment to the Henry Hillson Company to UNI be approved. The loan is made at an interest rate of 10 ½%

Apparently, the UBIA wanted UNI to acquire Henry Hillson Company, wanted the company to succeed, and was willing to expend money each quarter to assist in that goal, but the UBIA also preferred to treat the transaction as a loan so that the Royalty Fund would be repaid if Henry Hillson Company was profitable.

Loan "E-4": This $237,874.48 loan of January 11, 1980 to UNI for Henry Hillson was, according to the December 20, 1979 UBIA minutes "to pay the balance owed Mr. Hillson as specified in the purchase agreement between Utah Navajo Industries and Mr. Henry Hillson." In short, its purpose was to help finance the purchase by UNI of a company that provided significant employment and management training opportunities for San Juan County Navajos.

Loan "E-5": This $1,017,985.99 loan made on March 27, 1986 was for the purpose of paying off a commercial loan that UNI took out in order to finance a glove factory that employed San Juan County Navajos. The March 27, 1986 UBIA minutes tell the story:

[1] The loan was obviously carefully calculated for some purpose, which, based upon other documents in the UDIA Accounting, appears to have been related to the acquisition of Henry Hillson Company by UNI. *See,* Loan "E-4."

> $1 Million Glove Project Loan – Mike Allison
>
> The $1 million loan that was borrowed from Commercial Security Bank for the Glove Project investment is due April 1, 1986. UNI does not have the money to pay it back. Travis informed the UDIA Board that the UDIA Trust Fund has the $1,017,985.99 that is the exact amount due at this time. The Treasurer's Office suggested that it would be wiser to use the money that UDIA has available now than to cash in any other investments. This would leave the UDIA trust fund a balance of approximately $200,000. The $1 million loan should be paid off to put an end to the interest costs.
>
> UNI passed out a proposed $1 million glove loan reduction plan as follows:
>
> [A table showing a 5 year repayment plan based on UNI's projected budget was inserted here.]
>
> Motion: Bill Redd motioned to pay off the $1,017,985.99 loan and accept UNI's proposed budget loan reduction of $310,000 the first year and $300,000 for the next four years. The motion was seconded by Marion Holly and the UDIA Board approved unanimously.

This loan was intended to subsidize UNI and keep it solvent, by paying off a commercial loan that UNI could not afford to pay off, so that UNI could continue to provide jobs and economic development opportunities for San Juan County Navajos.

Loan "E-6": This is the only "loan" made during the period covered by fiscal years 1987 – 1991. This transaction technically was not a loan at all. FNAC, the former Henry Hillson Company, which was a UNI subsidiary and a significant employer of San Juan County Navajos, was looking for a source of funding. Rather than giving the money directly to FNAC as a grant, or even loaning it to FNAC directly, UBIA agreed to partially collateralize a $750,000 loan from the National Bank of Albuquerque to FNAC, by pledging a $500,000 CD that UDIA owned to National Bank of Albuquerque. FNAC in turn gave UDIA a mortgage on ten lots of land. FNAC thereafter went into bankruptcy

and National Bank of Albuquerque foreclosed on the CD. UDIA eventually recovered a portion of the $500,000 through the FNAC bankruptcy.

The "Recitals" portion of the 1990 FNAC – UBIA Agreement Concerning CD Pledge And Security Agreement shows that it was an "expenditure," intended to support and subsidize an important provider of benefits to the San Juan County Navajos:

> WHEREAS, Public Law 90-306, 82 Stat. 121, provides that the Trust Fund Monies be expended for the "health, education and general welfare of the Navajo Indians residing in San Juan County;"
>
> WHEREAS, FNAC has agreed to expend all monies received from National Bank of Albuquerque from the loans secured by the Bank Loan Pledge ("Loan Monies") to benefit the health, education, and general welfare of the Navajo Indians residing in San Juan County in accordance with the use of proceeds schedule attached hereto as Exhibit J.
>
> WHEREAS, the Bank Loan Pledge will benefit the health, education and general welfare of the Navajo Indians residing in San Juan County, by among other things, benefiting FNAC, which is a wholly owned for-profit subsidiary of Utah Navajo Industries ("UNI"), which is a wholly owned for-profit subsidiary of the Utah Navajo Development Counsel ("UNDC"), which is a non-profit Utah corporation in which Navajo Indians residing in San Juan County have a beneficial interest;
>
> WHEREAS, UBIA and FNAC's desire is to protect and preserve the Trust Fund Monies; and
>
> WHEREAS, FNAC has agreed to use proceeds generated by the Loan Monies to benefit the health, education, and general welfare of the Navajo Indians residing in San Juan County by dividending or advancing such monies to UNI to be used to make the payments under the 1989 Loan Payback Agreement with UDIA; …

This "loan" is a perfect example of a "conditional expenditure" of Royalty Funds, since no money at all would have been spent if the hoped for outcome – a business turnaround by FNAC – had occurred. The guarantee was strictly a matter of promoting economic development by supporting a major employer of San Juan County Navajos. Note that the underlying CD itself was an "investment" listed on the Investment Accounting. Treasurer Alter opines that the CD was a prudent investment within the

scope of the State Money Management Act. *See*, Treasurer Alter's Affidavit, ¶ 22 – 23; Johnson Investments And Loans Affidavit, ¶ 19.

Additional Fact 30: Since the 1992 adoption of the Navajo Trust Fund Act, Utah Code sections 63-88-101 through 107, there have been no additional economic development loans made to businesses with the intent to provide economic development for San Juan County Navajos, although there is now a specific provision, Utah Code section 63-88-106, which sets forth detailed criterion for Navajo Trust Fund expenditures that are investments (whether characterized as loans, capital investments, or otherwise). *See,* Loan Accounting; Statutory Appendix, Part VI: 1992 Utah Navajo Trust Fund Act.

Additional Fact 31: UNDC received income from numerous sources in addition to the Royalty Fund money. For example, UNDC appears to have received money from other Federal and State programs, from various grants, and other sources. UNDC received a quarterly allocation of funds from UDIA. Upon receipt, that lump sum was allocated on the UNDC books to multiple sub-accounts for expenditure purposes throughout the UNDC accounting system. Each of those sub-accounts is for a specific expenditure purpose, such as natural resources, transportation, housing, etc. But UNDC did not differentiate by source of funds with regard to UNDC's investments of its own surplus funds.

In fact, UNDC did little by way of investing during the time period that Mr. Johnson has preliminarily reviewed (fiscal years 1987 – 1991) because it needed the quarterly allocations from UDIA and other funds that it received for short term operating expenses. Indeed, as the Loan Accounting shows, from as early as November of 1982 UNDC had a line of credit with UDIA because of cash flow problems that UNDC encountered. In general, UNDC earned a

limited amount of interest on its bank account funds during the fiscal year 1987 – 1991 period. None of that interest was recorded on UNDC's books as originating from, or belonging in any way to, UDIA or the state of Utah. *See*, Johnson Investments And Loans Affidavit, ¶ 22.

Additional Fact 32: Treasurer Alter opines that Utah's obligation to prudently invest and to account for interest ends when the money is "expended" from the Royalty Fund for an approved purpose, whether expended unconditionally in the form of a grant or conditionally expended in the form of a loan. At that point, the money no longer belongs to Utah, and any interest generated from the further investment of the money belongs to the entity that received the money – such as UNDC or the UNI Companies – and not the Royalty Fund. Of course, Utah has an obligation to determine whether the principal and any interest on conditional expenditures such as loans made to UNDC or the UNI Companies was remitted to Utah; however Utah does not have an obligation to determine how or whether UNDC or the UNI Companies invested money while it was in those entities' possession. In Treasurer Alter's opinion as an accountant, an expert in trust management, and the person primarily responsible for interpreting the laws governing the investment of Surplus Royalty Funds, it would be improper to hold Utah responsible to account for how UNDC or the UNI Companies invested their surplus funds. *See*, Treasurer Alter's Affidavit, ¶ 25 – 26.

ARGUMENT

Point I: The Royalty Fund Is Mandated To Spend The Royalties, Not To Preserve And Invest Them.

The Royalty Fund is unusual in that, unlike typical trusts, it was not designed to preserve the corpus and "live off" the interest, but instead was designed to expend the royalties for the designated purposes under the 1933 Act and the 1968 Act. Investment of surplus funds to generate interest is therefore ancillary to the primary purpose of the Royalty Fund, which is to spend money for the "health, education and general welfare" of the beneficiaries.

Point II: There Is A Critical Distinction Between "Investments" That Are Designed To Generate Income For The Royalty Fund, And "Loans" That Are Expenditures Of Royalty Funds For Authorized Purposes.

The plaintiffs' motion begs the fundamental question: What is an "investment" in the context of the Royalty Fund, as established by the 1933 Act and the 1968 Act? This critical issue is never addressed in the Plaintiffs' Memorandum. As the Statement of Additional Facts demonstrates, there is a fundamental distinction between true investments of Surplus Royalty Funds in order to generate income, and economic development loans to UNDC or the UNI Companies. The distinction between "investments," as recorded on the Investment Accounting, and "loans," as recorded on the Loan Accounting, was maintained on UNDC's books and records from the time of the first loans in 1978.

The key difference between investments and loans is that the loans were substitutes for outright grants of Royalty Fund money. As discussed in the Statement of Additional Fact 28, there are numerous valid reasons why Utah may have chosen to make loans instead of grants in order to promote the "health, education and general welfare" of the Beneficiaries, in the words of the 1968 Act. Both Utah State Treasurer Edward T. Alter and forensic accountant Kelly Johnson

state in their affidavits that it is their expert opinions that the loans should be viewed as "conditional expenditures," rather than as traditional investments.

The loans were made only to a few select entities that were directly involved in providing benefits for the San Juan County Navajos. Only UNDC and the UNI Companies received loans, and Utah never listed any transaction with UNDC or the UNI Companies as an investment. As the Court is aware, the UNDC is a non-profit corporation that exists specifically to provide health, education and other assistance to the Beneficiaries. The UNI Companies were for profit corporations affiliated with UNDC that provided economic development opportunities for the Beneficiaries, including employment and management training. As the example loans described in Statement of Additional Facts 29 show, the loans were made for the purpose of subsidizing and supporting programs and entities that benefited the San Juan County Navajos, not for the purpose of obtaining the highest safe yield on investments.

Utah Code section 63-36-3.5, which was in effect from 1978 through 1991, supports this distinction. It reads: "Funds not allocated for use by the Board of Indian Affairs shall be invested in accord with Section 51-7-11," which is part of the State Money Management Act. The statute does not require that all funds be invested – only those "not allocated for use." A loan by UBIA in furtherance of the purposes mandated by the 1968 Act is an "allocation for use" of the money. Therefore, such a loan need not be "invested in accord with Section 51-7-11."

This distinction between "loans" and "investments" is an interpretation of the 1933 Act and the 1968 Act by the agencies that are charged with enforcement of those acts, and is therefore entitled to substantial judicial deference. As the United States Supreme Court explains:

> When a court reviews an agency's construction of the statute which it administers, it is confronted with two questions. First, always, is the question whether Congress has

> directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.[FN9] If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute,[FN10] as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute.[FN11]
>
> FN9. The judiciary is the final authority on issues of statutory construction and must reject administrative constructions which are contrary to clear congressional intent.
>
> FN10. See generally, R. Pound, The Spirit of the Common Law 174-175 (1921).
>
> FN11. The court need not conclude that the agency construction was the only one it permissibly could have adopted to uphold the construction, or even the reading the court would have reached if the question initially had arisen in a judicial proceeding.

Chevron USA, Inc. v Natural Resources Defense Counsel, Inc., 467 U.S. 837, 842 – 843 (1984) (lengthy footnote string citations omitted). Congress delegated "great latitude" in the management of the Royalty Funds to Utah, *Pelt v. Utah*, 104 F.3d 1534, 1544 (10th Cir. 1996). Utah in turn delegated management to the UDIA, the UBIA and the State Treasurer. Since the 1933 Act and 1968 Act are silent as to how investments are to be handled, Utah's interpretation of its duty to invest, and what constitutes an investment, should be upheld so long as it is permissible under those statutes.

It is beyond the scope of this motion to evaluate each individual loan in order to determine whether it was an appropriate conditional expenditure of funds[2] – it is possible that the plaintiffs will assert exceptions, claiming that some of the loans represent expenditures that should not have been made, whether in the form of a loan or a grant. The appropriate standard to

[2] The only transaction listed as a "loan" during the fiscal year 1987 – 1991 time period is discussed in the Statement of Additional Facts, ¶ 29, Loan "E-6," and in the Argument with regard to Utah's cross-motion for summary judgment for those years.

be used to evaluate Utah's decisions to make those loans is the same standard that will be used to evaluate any other exceptions to expenditures of Royalty Funds: Utah is entitled to "great latitude in its decision making processes." *Pelt v State of Utah*, 104 F.3d 1544 (10th Cir. 1996).

In short, only true investments, as documented in the Investment Accounting, are subject to evaluation under concepts of prudential investing. If Utah could have expended Royalty Funds outright through a grant of money to UNDC or the UNI Companies, but instead chose to make a conditional expenditure in the form of a loan, it is still an "expenditure" that should be evaluated under the same broad discretionary standards as all other expenditures, and not an "investment." Utah's consistently documented administrative interpretation as to what was a loan and what was an investment is a permissible interpretation of its authority under the 1933 Act and the 1968.

Point III: Only Surplus Funds Retained By The State Of Utah Are Subject To Any Fiduciary Duty To Invest. Once Money Went From The Royalty Fund To UNDC, UNI or Any Other Program It Was "Expended" And Not Subject To Any Fiduciary Duty To Invest.

As Treasurer Alter explains, Utah's duty to prudently invest Surplus Royalty Funds is limited to the funds in the possession of the State of Utah at a given time. Once those Royalty Funds were transferred, they were "expended" and no longer available to invest. Any income derived by UNDC or the UNI Companies as a result of each entity's investments belonged to that entity, and not to the Royalty Fund. UNDC's books do not differentiate interest paid on its bank account by source. Since UNDC and the UNI Companies were not government agencies, Utah did not exercise control over those investments, and the State Money Management Act did not apply to those entities. Thus, Utah should not be required to account for income derived by those entities as part of its accounting. Treasurer Alter's Affidavit, at ¶¶ 25 – 26.

Point IV: Utah Can Meet Its Burden Of Accounting For Investment Income Through Its Prior UDIA Accounting.

Utah has already provided an accounting for UDIA, including an original accounting which was submitted on December 12, 1999, see docket number 612, and a supplemental accounting which was submitted on August 29, 2000, see docket number 677 (collectively the "UDIA Accounting"). The Investment Accounting, attached hereto as Exhibit "C," shows all of Utah's investment activity concerning the Surplus Royalty Funds. It is a slightly clarified version of the Supplemental UDIA Accounting. The Investment Accounting for each fiscal year includes a Statement of Investments, which itemizes the investment portfolio at the end of the fiscal year (the June 30th date is actually the last day of the prior fiscal year, so the June 30, 1986 Statement of Investments shows the portfolio at the beginning of fiscal year 1987), and a Statement of Investment Activity, which shows all purchases and sales during the fiscal year. The annual volumes of the original UDIA Accounting include copies of the backup documentation for the transactions shown on the Statement of Investment Activity for each year.

The level of detail of the Investment Accounting, along with the backup documentation provided in the prior UDIA Accounting, is adequate to permit the beneficiary class to form an opinion through its counsel and accounting expert as to whether Utah met its duty (as defined below) to prudently invest Surplus Royalty Funds.[3]

[3] The plaintiffs' memorandum asserts, at footnote 2, page 4, that Utah has a duty to make the accounting "readily ascertainable" to even the least educated of the Beneficiaries. That issue is not properly before the Court in this motion, and Utah disagrees with that assertion. In this class action it is sufficient if the accounting is readily ascertainable to the class of beneficiaries as represented by their counsel and accounting expert. It is questionable whether it is ever possible to create any accounting that will be intelligible to a person who is so ill educated that he or she does not understand interest rates or the difference between stocks and bonds. Furthermore, *Sakezzie II*, cited by the plaintiffs, actually supports Utah's position. Paragraph 2 of Judge Christensen's order addresses future accounting requirements and states that the accounting shall be made "available to the plaintiffs and to those whom they represent, *through their counsel and other representatives designated by them*," which presumably could include their accountants. 215 F. Supp at 24 (emphasis added). Nothing in that paragraph requires that the

Because Utah needs to account only for investments of the Surplus Royalty Funds while those funds were under the control of UDIA and before they were disbursed, and Utah does not need to account for any investment activities by UNDC or the UNI Companies, no further accounting for interest income needs to be performed (except to the extent that Utah identifies additional evidence in response to the plaintiffs' exceptions or Kelly Johnson's further research).

Point IV: The Federal Standards For Investing Indian Funds Do Not Apply To Utah.

A significant portion of the plaintiffs' memorandum argues that federal investment standards govern how Utah was required to invest the Surplus Royalty Funds. According to the Plaintiffs' Memorandum, those standards are set forth in 25 U.S.C. §§161a – 161b, as interpreted by federal case law.[4] Interestingly, the plaintiffs never quote the text of the statutes upon which they rely. Yet even a cursory review of 25 U.S.C. §§161a – 161b shows that those statutes on their face cannot apply to Utah because they apply only to funds held in trust by the United States government and carried on the books of the United States Treasury:

> **§ 161a. Tribal funds in trust in Treasury Department; investment by Secretary of the Treasury; maturities; interest; funds held in trust for individual Indians**
>
> **(a)** All funds held in trust by the United States and carried in principal accounts on the books of the United States Treasury to the credit of Indian tribes shall be invested by the Secretary of the Treasury, at the request of the Secretary of the Interior, in public debt securities with maturities suitable to the needs of the fund involved, as determined by the Secretary of the Interior, and bearing interest at rates determined by the Secretary of the Treasury, taking into consideration current market yields on outstanding

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accounting be provided directly to the beneficiaries or that the accounting be translated into Navajo or that meetings be held to explain the accounting itself. The requirements to call meetings of Navajos, use interpreters, and permit questioning comes from paragraph 3 of the order, which required Utah to "to institute and carry out an effective program for the canvassing of the needs, desires and recommendations of the Indians" on a one time basis, prior to spending any more of the Royalty Funds. *Id.* Although Utah was to provide "comprehensive information concerning the administration of said fund and the problems, plans and policies of the Commission," at the meetings in order to permit a reasonable discussions of the Indians' needs and desires, it is clear from paragraph 2 that the actual accounting was to be provided to plaintiffs' counsel and their representatives.

[4] A copy of 25 U.S.C. §§ 151 – 166, referred to herein as the "federal statutory scheme" is contained in the Statutory Appendix, Part VII.

marketable obligations of the United States of comparable maturities.

(b) All funds held in trust by the United States and carried in principal accounts on the books of the United States Treasury to the credit of individual Indians shall be invested by the Secretary of the Treasury, at the request of the Secretary of the Interior, in public debt securities with maturities suitable to the needs of the fund involved, as determined by the Secretary of the Interior, and bearing interest at rates determined by the Secretary of the Treasury, taking into consideration current market yields on outstanding marketable obligations of the United States of comparable securities.

§ 161b. "Indian Money, Proceeds of Labor" fund; separate accounts for respective tribes; rate of interest

All tribal funds arising under section 155 of this title on June 13, 1930, included in the fund "Indian Money, Proceeds of Labor," shall, on and after July 1, 1930, be carried on the books of the Treasury Department in separate accounts for the respective tribes, and all such funds with account balances exceeding $500 shall bear simple interest at the rate of 4 per centum per annum from July 1, 1930.

25 U.S.C. §161b is the source for the plaintiffs' assertion that Utah is subject to a 4% investment "floor" because, at worst money invested under that statute would yield 4%. However, section 161b only applies to "[a]ll tribal funds arising under section 155." Section 155, however, excludes Utah's Royalty Fund:

§ 155. Disposal of miscellaneous revenues from Indian reservations, etc.

All miscellaneous revenues derived from Indian reservations, agencies, and schools, except those of the Five Civilized Tribes and not the result of the labor of any member of such tribe, **which are not required by existing law to be otherwise disposed of**, shall be covered into the Treasury of the United States under the caption "Indian moneys, proceeds of labor", and are made available for expenditure, in the discretion of the Secretary of the Interior, for the benefit of the Indian tribes, agencies, and schools on whose behalf they are collected, subject, however, to the limitations as to tribal funds, imposed by sections 123 and 142 of this title.

25 U.S.C. §155 (emphasis added). The 37 ½% oil and gas royalty revenues at issue in this case are "derived from Indian reservations," but they are also "required by existing law to be otherwise disposed of" by the terms of the 1933 Act and the 1968 Act, which transferred the money to Utah, rather than carrying the money on the books of the Treasury Department of the

United States. Thus, the Royalty Funds are not "funds arising under section 155" for purposes of 25 U.S.C. §161b, and the 4% "floor" cannot apply.[5]

The plaintiffs argue that: "The statutes that govern the investment of funds held in the trust by the government also define the government's fiduciary responsibilities." Plaintiffs' Memorandum, pg. 8. The federal statutory scheme, however, is limited by its express terms to funds "held in trust by the United States" and "carried in principal accounts on the books of the United States Treasury" and speaks only in terms of investments to be made by the Secretary of the Treasury.[6] Under the 1933 Act and the 1968 Act, the Royalty Fund is held by the State of Utah and carried on the books of the State of Utah. It is invested by the Utah State Treasurer, Edward T. Alter – not the United States Secretary of the Treasury. Thus, the federal statutory scheme for the investment of Indian trust funds by its explicit terms does not apply to the Royalty Fund.

The cases cited by the plaintiffs rely upon the federal statutory scheme adopted by Congress as the legal basis for the duties that they impose with regard to investment of Indian trust funds. *See, Osage Tribe of Indians v United States*, 72 Fed.Cl. 629 (2006), *Chippewa Cree Tribe of the Rocky Boy's Reservation v United States*, 69 Fed. C. 639, 656 (2006), *Mitchell v United States*, 664 F.2d 265 (1981), *Cheyenne – Arapaho Tribes of Indians of Oklahoma*, 512 F.2d 1390 (Ct. Cl. 1975). For example, the lengthy discussion in *Osage Tribe*, under the heading

[5] The issue of a 4% interest rate "floor" is something of a factual red herring. During the very early years, 1960 – 1964, interest rates earned by the Surplus Royalty Funds were between 3% and 4%. By 1965 the interest rates had permanently risen above 4%. Interest rates earned by the Surplus Royalty Funds rose significantly after 1978, when Utah Code section 63-36-7 replaced narrow investing in government bond and securities with broader discretion to invest according to the State Money Management Act. By 1981 it was not uncommon to see investments, mainly corporate bonds, earning in the range of 10% to 17%. *See*, Investment Accounting.

[6] If any part of the federal statutory scheme set forth in 25 U.S.C. §§151 – 166, concerning the investment of Indian trust funds were to be held to apply to the Royalty Fund, then the plaintiffs' claim for that interest would be against the Secretary of the Treasury of the United States, since that official is the one who is statutorily designated to do the investing, and not against Utah, which is given no authority to invest under those statutes.

"Whether Investments Were Made in Accordance With the Law," is premised almost entirely upon a detailed analysis of the federal statutory scheme, particularly 25 U.S.C. §§ 161a and 161b, and pays only lip service to common law trust principles. 72 Fed.Cl. at 667 – 671. The other cases cited by the plaintiffs' memorandum are all referenced within that portion of the *Osage Tribe* opinion. The *Osage Tribe* court summarized those cases:

> The Court of Claims has addressed the **statutory obligations** under 25 U.S.C. §§ 161a, 161b, and 162a on a number of occasions and has uniformly held the United States responsible for investing Indian trust funds in the highest yielding investment vehicles available to the funds in question.

72 Fed.Cl. at 668 (emphasis added).

The requirement to fully maximize trust income as among the investments allowed by 25 U.S.C. §161a, asserted by the plaintiffs, is a unique byproduct of the federal statutory scheme. The allowable investments under that scheme are limited by 25 U.S.C. §162a to a defined group of investments – essentially United States government bonds or securities, including those of agencies, and bank accounts secured by United States obligations.[7] The plaintiffs recognize this fact: "The allowable investments under the federal statutes are all safe investments because they are government-guaranteed." Plaintiffs' Memorandum, at pg. 10. Faced with a relatively short list of federal government guaranteed investments, courts have repeatedly held that the federal government is required to maximize trust income from the investments on that list. In essence, the federal government is held to the standard of paying the highest rate of interest that it was itself willing to guarantee from among that list of investments.

[7] For a detailed discussion of permissible investments under the federal scheme, including a list of twelve specific legal investments, see *Cheyenne – Arapaho Tribes*, 512 F.2d at 1395 – 1397.

Conversely, a trustee whose investment options are not limited by such a narrow list cannot be required to guess which among the infinite number of potentially prudent investments will generate the highest yields in light of varying degrees of risk. Judged in hindsight, even an investor as savvy as Warren Buffet could have improved investment yields if he had always guessed right. Requiring a trustee to maximize investment income from a wide range of investment options, as opposed to the narrow list in the federal statutory scheme, is to impose a "superman" standard instead of a "prudent man" standard.

Nothing in the 1933 Act or the 1968 Act addresses the investment of surplus funds, or sets forth any rule of prudential investment for those funds. Although federal law is clear in requiring that federal Indian trust funds must be invested in specific manners and must bear interest that is accrued to those federal Indian trusts, there is no federal law that even requires that money in the Royalty Fund bear interest. Thus, the question of how Royalty Fund monies should be invested, and what rules of prudential investment should apply, is left up to Utah.

This is consistent with the holding in *Pelt v State of Utah*, 104 F.3d 1534 (10th Cir. 1996). The primary issue addressed by that opinion was whether there exists a private cause of action to sue Utah for the mismanagement alleged in this lawsuit. The Tenth Circuit held that there is a private cause of action under *Cort v Ash*, 442 U.S. 66 (1975), noting that: "The fourth prong of the *Cort* test asks whether the right is one that is traditionally a state concern and therefore inappropriate for a federal cause of action." 104 F.3d at 1544. In that context, the *Pelt* opinion held that "this case involves an area of law not within the purview of the states, but rather one that is solidly within the federal realm." *Id.* However, *Pelt* also held that "this discretionary trust provides the state with great latitude in its decision-making processes.." Id. Thus, in the

absence of any federal statute referencing how the Surplus Royalty Funds were to be invested, Utah is entitled to "great latitude in its decision-making process." That is particularly true in light of Utah's adoption of a specific statutory scheme that imposes reasonable fiduciary duties on Utah with regard to the investment of the Surplus Royalty Funds, as discussed in the next point.

Point V: The Relevant Standard For The Prudent Investment Of Utah's Surplus Royalty Funds Is Found In Utah Statutes That Directly Govern The Utah Board Of Indian Affairs, Including The State Money Management Act

Because the 1933 Act and the 1968 Act are silent as to how any Surplus Royalty Funds are to be invested, and because no other federal law directly addresses how Utah is to invest those funds, Utah is free to legislate the appropriate standards so long as they do not conflict with the express provisions of those acts. *Chevron*, 467 U.S. at 842 – 843.

Since approximately when royalties began to be generated, Utah has had a specific statutory scheme in place defining both how Royalty Funds were to be spent and how Surplus Royalty Funds were to be invested, which has evolved over time. That specific statutory scheme has consistently imposed reasonable, defined duties of care with regard to the investment of Surplus Royalty Funds; it therefore constitutes a permissible series of interpretations of Congress's intent under the 1933 Act and the 1968 Act. The Utah statutes that are specific to the Royalty Fund take precedence over any general common law principles of prudential trust fund investments, as might be found for example in the Restatement of the Law Third – Trusts, as well as any more general Utah statutes dealing with trustees of private trusts.[8] See, e.g., *Jensen v. IHC Hospitals, Inc.*, 944 P.2d 327, 336 (Utah 1997).

[8] The history of Utah's statutory scheme is described in detail in the Statement of Additional Facts 8 – 15.

Under Utah's statutory scheme, prior to 1978 Surplus Royalty Funds that would not be needed for one year were to have been "invested in United States government bonds or securities, or bonds or securities of the state of Utah at the highest rate that may be available at the time, provided that the bonds or securities shall be redeemable not more than five years after the date of their issuance." Utah Code § 63-36-3 (Supp. 1967) (replacing nearly identical language in §63-22-4(4)(1959)). The phrase "United States government bonds or securities" was not defined, however it presumably included investments in bonds issued by United States government agencies in addition to Treasury instruments.[9]

After 1978, the standard for prudent investment changed, allowing for the Surplus Royalty Funds to be invested in a broad range of investments permitted under the State Money Management Act. See, Utah Code §§ 63-36-3.5, 51-7-11. Indeed, Utah Code section 51-7-11 expressly permits investment of the Royalty Fund even more broadly than the list of investments permitted by that code section. However, all investments under the State Money Management Act are required to meet the "prudent man" requirements of Utah Code section 51-7-14.

One important distinction between the pre-1978 statutory scheme and investment under the State Money Management act is that the earlier scheme narrowly limited the types of investments that could be made. Since the pre-1978 investments were limited to safe government bonds whose yields could be easily compared, Utah was required to obtain "the highest rate that may be available at the time" from among those bonds that have 5 year or shorter maturities. The State Money Management Act, however, does not contain any "highest

[9] Cf. *Cheyenne – Arapaho Tribes*, which found that the language in 25 U.S.C. §162a permitting investment in "any public-debt obligations of the United States and in any bonds, notes, or other obligations which are unconditionally guaranteed as to both interest and principal by the United States" included investments such as "[b]onds, notes, and other evidences of indebtedness of the Tennessee Valley Authority." 512 F.2d at 1395.

rate available" language. Even within the limits placed upon investments by Utah Code section 51-7-11's list, there are too many possibilities to guarantee the "highest rate." For example, the current version of section 51-7-11 permits the purchase of publicly traded "A" rated corporate bonds – of which there are an extremely large number in the marketplace, with differing levels of risk. Thus, from the time in 1978 that Utah adopted the State Money Management Act as the basis for prudent investment of the Surplus Royalty Funds, there was no longer any requirement that Utah maximize the rate of return. The only requirement was that Utah invest the Surplus Royalty Funds with the same level of care that Utah used to invest its own, non-trust funds. This is completely congruent with the basic premise underlying all of the various common law formulations of rules for prudent investing, namely that the trustee use the same care with regard to investing the trust as the trustee would use in the prudent management of the trustee's own affairs (taking into consideration the purpose of the trust and other relevant circumstances).

By comparing entries in the Investment Accounting with the relevant Utah statutes governing investment of Surplus Royalty Funds at the time, the plaintiffs can readily determine whether they wish to make an exception to any investment on the basis that it violated the standard of care established by Utah's statutory scheme.

Point VI: Utah Is Entitled To Summary Judgment On Its Cross-Motion With Regard To Fiscal Years 1987 – 1991.

The undisputed facts establish that all of Utah's investments of Surplus Royalty Funds during Fiscal Years 1987 - 1991 were made in compliance with the State Money Management Act and thus Utah complied with its fiduciary duty to properly invest the Surplus Royalty Funds. *See*, Treasurer Alter's Affidavit, at ¶ 23.

Utah made only one "loan" during Fiscal Years 1987 – 1991. That loan was actually a pledge of a CD as collateral in support of a guarantee issued in favor of the National Bank of Albuquerque so that FNAC could obtain a commercial loan. *See*, Statement of Additional Facts, 29, Loan "E-6." That transaction, which is listed on the Loan Accounting, is not an "investment." The underlying CD was an "investment" but the pledge of that CD as collateral was no different than pledging a building or other asset, and is properly viewed as a conditional expenditure of Royalty Funds for a purpose that purports to comply with the 1968 Act. In other words UBIA, exercising its "great latitude in its decision making process," *Pelt*, 104 F.3d at 1544, chose to guarantee and collateralize a loan to FNAC, a Navajo run business that provided employment to San Juan County Navajos. That meant that UBIA had made a conditional expenditure – unlike a direct grant, if FNAC had done well there would have been no expenditure from the Royalty Fund, but because FNAC did poorly and ended up in bankruptcy, UBIA ended up expending a portion of the collateral (to the extent that money was not recovered in the FNAC bankruptcy).[10] *See*, Treasurer Alter's Affidavit, at ¶ 22; Johnson Investments and Loans Affidavit, at ¶ 19.

Other than the CD used as collateral for the FNAC loan, all investments during fiscal years 1987 – 1991 paid in full, and the interest earned went to the Royalty Fund. The CD itself was a prudent investment in compliance with the State Money Management Act – the fact that the CD was conditionally expended did not change the propriety of the investment itself. *See*, Treasurer Alter's Affidavit, at ¶¶ 22 – 23; Johnson Investments and Loans Affidavit, at ¶ 21.

[10] Utah emphasizes that it is not asking the Court to rule on the question of whether the UBIA's decision to make the loan guarantee was appropriate. The plaintiffs may choose to make an exception concerning that decision, which would then be evaluated in light of Utah's broad discretion to make expenditures under the 1933 Act as amended by the 1968 Act. Utah is merely asking the Court to determine that the transaction was not an "investment" that needs to comply with the standards of prudent investing set forth in this memorandum.

Because all of the investments of Surplus Royalty Funds made by Utah during fiscal years 1987 – 1991 complied with the State Money Management Act, and Utah has provided a full accounting for those investments, Utah is entitled to partial summary judgment holding that Utah properly met its duty to invest Surplus Royalty Funds during those fiscal years.

CONCLUSION

Utah had a duty to properly invest Surplus Royalty Funds that were not needed for operational purposes. The attached Investment Accounting, coupled with Utah's earlier UDIA Accounting and Supplemental Accounting, adequately shows how Utah invested those funds. There is a logical distinction, always maintained on UDIA's books, between "loans" to UNDC and the UNI Companies in furtherance of the purposes of the 1968 Act and true "investments" of Surplus Royalty Funds. Utah was not required to treat the loans as investments that are subject to the rules of prudent investing – it was enough that UBIA in the exercise of its judgment chose to make conditional expenditures of Royalty Fund money, instead of giving outright grants.

The federal statutory scheme for the investment of federally held Indian trust funds by the United States Treasurer, and the cases interpreting that scheme such as *Osage Tribe*, do not apply to Utah. The proper formulation of Utah's fiduciary duty to prudently invest Surplus Royalty Funds is found in Utah's own statutory scheme that is specific as to the use and investment of those funds. Under that scheme, prior to 1978, Utah could only invest those funds in government bonds or securities. Subsequently, Utah could invest Surplus Royalty Funds in any way that complied with the State Money Management Act.

Utah's investments during the fiscal years 1987 through 1991 complied with the State Money Management Act; therefore Utah met its duty to prudently invest during that time.

For those reasons, Utah asks the Court to rule as follows on the plaintiffs' motion and Utah's cross-motion:

1. The federal statutory scheme for the investment of federally held Indian trust funds by the United States Treasurer as set forth in 25 U.S.C. §§151 - 166, and the cases interpreting that scheme such as *Osage Tribe*, do not apply to Utah.
2. The proper formulation of Utah's fiduciary duty to prudently invest Surplus Royalty Funds is found in Utah's own statutory scheme that is specific as to the use and investment of those funds.
3. Utah's duty to prudently invest is limited to true investments, as shown by the Investment Accounting, Exhibit "C," and does not extend to loans to UNDC and the UNI Companies, as shown in the Loan Accounting, Exhibit "D."
4. Loans to UNDC and the UNI Companies, as shown on the Loan Accounting, were expenditures of Royalty Funds that were conditional in nature. Any challenges by the plaintiffs to those loans would be in the form of exceptions and would be evaluated in light of the "great latitude" to which Utah is entitled in its "decision making processes" concerning expenditures from the Royalty Funds.
5. Utah is not required to account for income that UNDC or the UNI Companies may have made off of the investment of money in the possession of those entities.
6. Subject to the plaintiffs' right to make exceptions, Utah has met its burden of accounting for investments of Surplus Royalty Funds by producing the Investment Accounting, the Supplemental Accounting, and the original UDIA Accounting with its backup documentation.

7. Utah prudently invested the Surplus Royalty Fund during fiscal years 1987 – 1991 (July 1, 1986 – June 30, 1991).

DATED this 12th day of October, 2007.

MARK L. SHURTLEFF
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CERTIFICATE OF SERVICE

I hereby certify that on this 12th day of October, 2007, I electronically filed the foregoing **MEMORANDUM IN OPPOSITION TO PLAINTIFFS' MOTION FOR PARTIAL SUMMARY JUDGMENT RE: UTAH'S DUTY TO DEMONSTRATE IN ITS ACCOUNTING THAT IT COMPLIED WITH ITS DUTY TO INVEST** with the Clerk of the Court, using the CM/ECF system, which sent notification of such filing to the following:

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