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The Iron Range Resources and Rehabilitation Board: An Unconstitutional and Confused Delegation of Executive Power to Legislators

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**THE IRON RANGE RESOURCES AND REHABILITATION
BOARD: AN UNCONSTITUTIONAL AND CONFUSED
DELEGATION OF EXECUTIVE POWER TO
LEGISLATORS**

Neil W. Hamilton[†]

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I. INTRODUCTION

In the late 1930s, the northeastern portion of Minnesota started to experience economic decline as iron mines were being depleted.¹ In response, the Minnesota Legislature in 1941 created the Iron Range Resources and Rehabilitation Board (“the Board” or “IRRRB”) and the office of “the Commissioner” of the Board.² The primary purpose of the Board was, and is, to use its budget “in the development of the remaining resources of the [counties] and in the vocational training and rehabilitation of its residents”³ This includes the promotion of tourism.⁴ The area served by the IRRRB came to be known as the “Taconite Tax Relief Area”; a geographical region encompassing approximately 13,000 square miles, comprising most of the area commonly known as the “Arrowhead Region,” and including the following cities: Babbitt, Crosby-Ironton, Eveleth, Ely, Grand Marais, Grand Rapids, Hibbing, Silver Bay, Two Harbors, and Virginia.⁵

The Board’s mission has remained consistent throughout its

1. See WILLIAM E. LASS, MINNESOTA – A HISTORY 256-57 (2d ed. 1998).

2. See 1941 Minn. Laws ch. 544, § 4.

3. MINN. STAT. § 298.22, subd. 1(3) (1998); 1941 Minn. Laws ch. 544, § 4.

4. See MINN. STAT. § 298.22, subd. 1(3).

5. See IRON RANGE RESOURCES AND REHABILITATION BOARD, 1997-98 BIENNIAL REPORT 4 fig.1.0 (1999); Iron Range Resources and Rehabilitation Board, *About IRRRB* (visited Nov. 27, 1999) <<http://www.irrrb.org/>>.

history. It describes its mission as follows:

First, to be careful custodians of the public money entrusted to it. Second, to enhance the economic vitality of the Taconite Tax Relief Area through value-driven, cost-effective projects and programs designed for the long-range benefit of the region.⁶

The Board is an important public agency, serving a large geographic portion of the state and handling millions of tax dollars each year. At the end of its 1998 fiscal year, it had at its disposal approximately \$69,216,000.00, and at the end of its 1997 fiscal year, it had approximately \$79,440,000.00.⁷ The largest source of revenue for the Board is obtained through a tax on taconite production, although it does receive significant revenue through investments, bonds, loans and other sources.⁸ Additionally, in its 1998 fiscal year it had \$31,990,000.00 in expenditures, and \$37,794,000.00 in expenditures in 1997.⁹ Most of the Board's expenditures are in the area of programs, although it also makes expenditures in the areas of facilities and administrative services.¹⁰

This article analyzes both the constitutionality and the economic efficiency and effectiveness of the governance structure of

6. *See id.* at 4.

7. *See id.* app. I.

8. *See id.* For example, in the 1998 fiscal year the Board received \$17,657,000.00 from taconite production taxes, \$7,785,000.00 from investments, \$2,502,000.00 in loan revenues, and \$3,478,000.00 in departmental revenue. *See id.*

9. *See id.*

10. *See id.* For example, in the 1998 fiscal year the Board made expenditures in the following areas:

Programs

Business Development	\$5,618,000.00
Community Development	11,575,000.00
Taconite Assistance	6,578,000.00
Communications	209,000.00
Tourism	751,000.00
Research and Planning	705,000.00

Facilities

Giants Ridge Golf and Ski Resort	\$5,066,000.00
Ironworld Discovery Center	2,301,000.00
Mineland Reclamation	916,000.00
Trails	408,000.00
Maintenance/Shop	521,000.00
Building Demolition	247,000.00
Facilities Improvements	228,000.00

<i>Administrative Services</i>	\$1,541,000.00
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the IRRR Board and Commissioner. The article concludes the delegation of executive power to the IRRR Board, consisting almost entirely of legislators, is unconstitutional. The article also concludes that the existing governance structure is not effective in reaching the goals of the legislature. Finally, the article makes recommendations on how the executive and legislative branches can most effectively correct the deficiencies. The article is divided into four parts. Part II outlines the mission of the Board and Commissioner, and Part III outlines the governance structure of the agency. Part IV identifies management challenges for the agency. Part V considers opportunities for organizational and operational improvements and makes recommendations on how the executive and legislative branches can most effectively correct such deficiencies.

II. THE MISSION OF THE IRRR BOARD AND COMMISSIONER

While the legislature and the Board have defined the Board's mission in broad terms,¹¹ its mission is essentially guided by the statutory provisions governing its finances. The legislature has created a number of revenue sources for the Commissioner and the Board, and each source has its own objectives.

A. *The Board Account*

With respect to appropriations to the Board from the taconite tax under section 298.22, subd. 7 ("Board Account"), the Commissioner may use the appropriation: (a) to develop the remaining resources of counties in the Taconite Tax Relief Area, including the promotion of tourism;¹² (b) to provide vocational training and rehabilitation to residents of those counties;¹³ and (c) to foster economic development and tourism within the Giants Ridge recreation area.¹⁴ No part of the fund may be used for private loans to private businesses without governor approval.¹⁵

11. *See id.*; *see also* MINN. STAT. § 298.22, subd. 1(3) (1998).

12. *See* MINN. STAT. § 298.22, subd. 1(3).

13. *See id.*

14. *See id.* § 298.22, subd. 7.

15. *See id.*

B. The Environmental Fund Account I

With respect to appropriations under section 298.28, subd. 11 and section 298.227 to the taconite environmental protection fund (“Environmental Fund Account I”), the Commissioner shall administer the fund: (a) to investigate environmental issues; (b) to reclaim, restore, or reforest minelands; (c) to assist local economic development projects; and (d) to monitor mineral industry related health problems among mining employees.¹⁶

C. The Environmental Fund Account II

With respect to appropriations under both section 298.28, subd. 9b and section 298.2961 to the taconite environmental protection fund (“Environmental Fund Account II”), section 298.2961 authorizes the Board to use these funds for grants or loans to producers for either environmentally unique reclamation projects or certain pit or plant expansions or modernizations.¹⁷

D. The Economic Development Fund Account I

With respect to appropriations under section 298.28, subd. 9a to the taconite economic development fund (“Economic Development Fund Account I”), section 298.227 provides that the Board shall hold such funds for each producer, to be used for acquisition of equipment and facilities for the producer or for research and development in Minnesota on new mining technology.¹⁸

E. The Economic Development Fund Account II

With respect to appropriations under section 298.2213 to the Northeast Minnesota economic development fund (“Economic Development Fund Account II”), the Commissioner may use the money for projects that create and maintain skilled employment and encourage diversification of the economy.¹⁹

16. See *id.* § 298.223 (1998).

17. See *id.* § 298.2961 (1998).

18. See *id.* § 298.227 (1998).

19. See *id.* § 298.2213, subd. 2 (1998).

F. *The Economic Protection Trust Account*

With respect to appropriations under section 298.28, subd. 9 and 11 to the Northeast Minnesota economic protection trust fund ("Economic Protection Trust Account"), the Board and the Commissioner may, until January 1, 2002, use the trust's investment returns,²⁰ and subsequently, the trust itself, to approve projects for economic rehabilitation and diversification of industrial enterprises in the Taconite Tax Relief Area. Such projects must create additional long-term employment.²¹

G. *Tax Increment Financing Power*

The Commissioner is also given tax increment financing power for economic development projects within the Taconite Tax Relief Area.²²

III. THE GOVERNANCE STRUCTURE OF THE IRRR BOARD AND COMMISSIONER

A. *Statutory Analysis*

The Minnesota Legislature established the Board and Commissioner in 1941 under Minnesota Statutes chapter 298. Section 298.22, subd. 1 currently provides, "The governor shall appoint the commissioner of the iron range resources and rehabilitation under section 15.06."²³ Section 15.06 "applies to the following department or agencies," and lists the IRRR Commissioner as an agency.²⁴ The section sets forth the terms of office and general management powers of commissioners and deputy commissioners.²⁵

Section 298.22 also creates an "iron range resources and rehabilitation board."²⁶ Up to the 1999 legislative session, the board was to consist "of eleven members, five of whom shall be state senators appointed by the subcommittee on committees of the rules com-

20. There are several exceptions to this general restriction outlined in Minnesota Statutes section 298.296, subd. 2. See MINN. STAT. § 298.296, subd. 2 (1998).

21. See *id.* §§ 298.292, .296.

22. See *id.* § 298.2211, subd. 1 (1998).

23. *Id.* § 298.22, subd. 1 (1998).

24. *Id.* § 15.06, subd. 1 (1998).

25. See *id.* § 15.06.

26. *Id.* § 298.22.

mittee of the senate, and five of whom shall be representatives, appointed by the speaker of the house of representatives," for two year terms.²⁷ "The 11th member of said board shall be the commissioner of natural resources"²⁸ In the 1999 session, the legislature expanded section 298.22 to provide for thirteen members, consisting of five state senators, five representatives, and three non-legislators who reside in the Taconite Tax Relief Area.²⁹ The senate majority leader, the Speaker of the House, and the Governor each appoint one of the nonlegislator board members.³⁰ Section 298.22 also provides that at least a majority of the legislative members of the board shall be elected from state senatorial or legislative districts in which over fifty percent of the residents reside within the Taconite Tax Relief Area.³¹

With respect to the allocation of power between the Commissioner and the Board, chapter 298 has different language for each account listed in Part II above.

1. *The Board Account*

Section 298.22, subd. 1 provides that the Commissioner "may use whatever amounts of the appropriation that are deemed necessary and proper in the development of the remaining resources of each county and in the vocational training and rehabilitation of its residents."³² All other subdivisions of section 298.22 grant specific powers to the Commissioner, except subdivision 6, which provides, "The board may acquire an equity interest in any project for which it provides funding."³³

Prior to 1995, section 298.22, subd. 2 provided:

All expenditures and projects made by the commissioner . . . shall first be submitted to said . . . board *which shall recommend approval or disapproval or modification* of expenditures and projects for rehabilitation purposes as provided by this section, and the method, manner, and time of payment of all said funds proposed to be disbursed shall

27. *Id.* § 298.22, subd. 2.

28. *Id.*

29. See Act of May 25, 1999, ch. 223, art. 2, § 42, 1999 Minn. Sess. Law Serv. 1205 (West) (amending MINN. STAT. § 298.22).

30. See *id.*

31. See MINN. STAT. § 298.22, subd. 1(2) (1998).

32. *Id.* § 298.22, subd. 1.

33. *Id.* § 298.22, subd. 6.

first be approved or disapproved by said board.³⁴

A 1949 Opinion of the Attorney General advised that when the Commissioner proposes a project or expenditure and submits it to the Board for approval or disapproval, and the Board disapproves of either the proposed project or expenditure, the Commissioner, "Nevertheless has authority to proceed with the project or expenditure, since the Board exercises advisory powers only."³⁵

There is a redundancy in original language of this provision, both before and after the 1995 amendments. Prior to 1995, the first clause required that all "expenditures and projects" shall first be submitted to the Board for its *recommendation* and the second clause required "the method, manner, and time of payment of all said funds proposed to be disbursed shall be *first approved or disapproved* by said board."³⁶ The word "expenditure" means disbursement.³⁷ The Attorney General in 1949 apparently read the first clause creating Board advisory powers on expenditures to trump the second clause requiring prior board approval of the method, manner, and time of disbursements.

In 1995, the legislature amended section 298.22, deleting the language "which shall recommend approval or disapproval or modification," and substituting "for approval by at least eight board members."³⁸ The 1999 amendment reduces the necessary votes for approval to "a majority of the board."³⁹ The 1995 amendment dramatically reallocated power between the Commissioner and the Board with respect to the Board Account. Prior to 1995, the Board had advisory powers to the Commissioner. The 1995 language, by requiring that the Commissioner first submit *all* expenditures and projects for Board approval makes the Commissioner to a substantial degree advisory to the Board with respect to the Board Account.⁴⁰

34. MINN. STAT. § 298.22 (1994) (emphasis added).

35. Op. Minn. Att'y Gen. 416-B (July 11, 1949).

36. MINN. STAT. § 298.22 (1994) (emphasis added).

37. RANDOM HOUSE DICTIONARY OF THE ENGLISH LANGUAGE 463 (College ed. 1968).

38. There is no legislative history on the 1995 amendments, indicating that these changes were made in conference committee without hearings.

39. Act of May 25, 1999, ch. 223, art. 2, § 42, 1999 Minn. Sess. Law Serv. 1205 (West) (amending MINN. STAT. § 298.22).

40. A second redundancy in section 298.22, subd. 2, creates another interpretation issue. Note that "expenditures and projects" appears twice, the first time modified by the adjective "all," and the second time modified by the clause "for

The statutory language creates confusion regarding some major issues of governance. For example, the language itself does not provide the Board with the *explicit* authority to approve, disapprove, or modify the Commissioner's *proposed* fiscal year operating budget or the Commissioner's spending plans. The question is whether a budget is an "expenditure." In common understanding, a budget is not viewed as an actual expenditure, but rather anticipated revenues and expenses that may or may not come to fruition during the course of the year. There are a number of questions regarding the method and manner by which the agency can be appropriately administered and responsibly governed:

1. If the Board does not have the explicit authority to disapprove, approve or modify the agency's annual operating budget, is its vote on the operating budget then only a *recommendation*?

If so:

- a. Does the Commissioner possess the authority to disregard the Board's directive and/or perhaps not even submit the budget for consideration every year?
 - b. If the Commissioner implements the proposed agency budget, and if the statute requires that all actual expenditures and projects (but not budgets) be approved by the Board, must an official, public Board meeting be held to approve every expenditure when the *final decision* is made to commit the funds?
2. Alternatively, if the Board does pass a budget and proposed spending plan, is that enough to provide the required legal approval for each specific, line-item expenditure as it is realized throughout the fiscal year? If so, if the Commissioner elects to spend

rehabilitation purposes as provided by this section." MINN. STAT. § 298.22, subd. 2 (1998) (emphasis added). Subdivision 1(3) of section 298.22 grants the Commissioner the power to "use whatever amounts of the appropriation . . . that are determined to be necessary and proper in the development of the remaining resources of the county and in the vocational training and *rehabilitation* of its residents . . ." *Id.* § 292.22, subd. 3 (emphasis added). A possible interpretation is that subdivision 2 grants the Board the power of approval only over expenditures and projects for *rehabilitation* purposes, not over expenditures and projects "necessary and proper in the development of the remaining resources of the county and in the vocational training . . . of its residents." *Id.* § 292.22, subd. 2.

resources beyond the specific limitation imposed by the Board, must the Board hold an official public meeting to approve every expenditure once the final determination to expend those funds is made?

Another issue relates to the vague wording of the statute. For instance, the terms "expenditure" and "project" are not defined. Is a "project" any activity that is planned or is it just a major undertaking? Or does it relate to how the agency staff has used the word for accounting purposes to ensure certain programs are operationally funded?

However the above ambiguities may be resolved, it is clear that requiring prior board approval of *all* expenditures and projects by a majority of the Board and the method, manner, and time of payments of *all* disbursements puts the Board in charge not just of the overall direction and policy of the agency with respect to the Board Account but also of major elements of the operational management of the agency on these matters. The Board, in fact, interprets the statute to give it both policy and substantial operational control of the agency. The Board chair and other Board members sometimes direct staff without approval or knowledge of the Commissioner. At the July 1997 Board meeting, the Board passed a budget that cut a number of programs out of the Commissioner's budget. The Board directed that, for virtually any spending, the Commissioner either bring the matter to the Board for approval or get personal approval from a named senator or representative.⁴¹

2. *The Environmental Fund Account I*

Section 298.223 provides that this fund "shall be administered by the Commissioner."⁴² The Commissioner shall submit projects to be funded to the Board.⁴³ Upon approval of the majority of members of the Board, the projects shall be submitted to the Governor, who shall approve or disapprove, or return for further consideration each project.⁴⁴ In addition, "funds for a project may be expended only upon approval of the project by the board and gov-

41. Memorandum from Jim Gustafson, Commissioner, to Doug Gregor, Assistant Attorney General (Oct. 28, 1997) (on file with the author).

42. MINN. STAT. § 298.223, subd. 2 (1998).

43. *See id.*

44. *See id.*

error.”⁴⁵ This governance structure gives the Board co-equal power with the Governor over the account to determine which projects are to be funded. The meaning of the sentence, “Funds for a project may be expended only upon approval of the project by the board and governor,” is not clear. It appears that the governance structure of this account may be similar to the Board Account, where the decision to approve a project is distinguished from the decision to disburse the money for the project. Both decisions require prior board approval in the Board Account. If this sentence just means that funds may be disbursed whenever the Board and Governor approve the project, it seems redundant since the statute already requires that the Board and Governor approve all projects. The most reasonable interpretation of the sentence is that the Board and Governor have co-equal power to decide on disbursement of funds for approved projects.

3. *The Environmental Fund Account II*

Section 298.2961 creates this fund as a special account in the taconite environmental protection fund (“Environmental Fund Account I”). So presumably, as with that account, the fund shall be administered by the Commissioner. Section 298.2961, subd. 2 also provides, “To be proposed by the board, a project must be approved by at least eight . . . board members.”⁴⁶ The second sentence provides, “The money for a project may be spent only upon approval of the project by the governor.”⁴⁷ The third sentence requires that the Board “may submit supplemental projects for approval at any time.”⁴⁸

The meaning of the second sentence is not clear. If section 298.2961 is structured similarly to the Board Account and the Environmental Account Fund I, then the Board has sole power to approve a project, but the Governor has sole power to approve the disbursement of funds for the project. However, the first sentence begins, “To be proposed by the board, . . .” and the third sentence refers to board submission of projects “for approval,” which must

45. *Id.* Prior to 1995, the Board made recommendations to the governor regarding projects. See MINN. STAT. § 298.223, subd. 2 (1994). The 1995 legislation required projects to be approved by at least eight votes of the Board. See MINN. STAT. § 298.223, subd. 2 (1996).

46. MINN. STAT. § 298.2961, subd. 2 (1998).

47. *Id.*

48. *Id.*

mean to be proposed or submitted for approval to the Governor.

It seems most reasonable to interpret the governance structure for this account in light of the governance structure of other accounts. The Board and Governor share co-equal power to determine what projects are to be undertaken, and the Governor has the power to decide on disbursement of funds for approved projects.

4. *The Economic Development Fund Account I*

Section 298.227 directs the Board to release funds for each producer on the written authorization by majority vote of a joint committee of representatives of salaried and non-salaried employees of that producer.⁴⁹

5. *The Economic Development Fund Account II*

Section 298.2213, subd. 1 directs an appropriation from the general fund "to the commissioner."⁵⁰ Section 298.2213, subd. 4 provides:

To be proposed by the board, a project must be approved by at least eight . . . board members and the commissioner The list of projects must be submitted to the governor who shall . . . approve, disapprove, or return for further consideration, each project. The money for a project may be spent only upon approval of the project by the governor.⁵¹

The 1999 amendments changed the necessary vote for approval of a project to a majority of the board.⁵²

The governance structure of this account requires that the decision to undertake a project must have the approval of a majority of the Board, the Commissioner, and the Governor. All three have co-equal powers to approve projects for this account. The meaning of the third sentence regarding disbursement of money for a project only upon approval of the Governor is unclear. In light of the governance structure of other accounts, it seems most reasonable that only the Governor has power to approve the disbursement of

49. *See id.* § 298.227.

50. *Id.* § 298.2213, subd. 1.

51. *Id.* § 298.2213, subd. 4.

52. *See* Act of May 25, 1999, ch. 223, art. 2, § 42, 1999 Minn. Sess. Law Serv. 1205 (West) (amending MINN. STAT. § 298.22).

funds for a project.

6. *The Economic Protection Trust Account*

Section 298.296, subd. 3 states that the Commissioner shall administer the program under which funds are expended out of this account.⁵³ However, section 298.296, subd. 1 grants the Board the power to “prepare a list of projects to be funded” from the account and further provides:

To be proposed by the board, a project must be approved by at least eight . . . board members *and the commissioner* The list of projects shall be submitted to the governor, who shall . . . approve or disapprove, or return for further consideration, each project. The money for a project may be expended only upon approval of the project by the governor.”⁵⁴

The governance structure for this account is similar to that of the Economic Development Fund Account II.

B. Is the Board Part of the Executive Branch or the Legislative Branch?

Executive power consists of interpreting and implementing or enforcing laws enacted by the legislature.⁵⁵ This power includes determining budgetary calculations.⁵⁶ The United States Supreme Court has also found that executive power includes controlling the management of a government owned corporation.⁵⁷ The Office of the Commissioner, including all employees, is clearly an agency in the executive branch under traditional definitions and those contained in Minnesota Statutes sections 298.22, subd. 1 and 15.06, subd. 1.⁵⁸ What is the Board? Minnesota Statutes section 15.012

53. See MINN. STAT. § 298.296, subd. 3 (1998).

54. *Id.* § 298.296, subd. 1 (emphasis added).

55. See *Bowsher v. Synar*, 478 U.S. 714, 733 (1986); See also *State ex rel. Univ. of Minn. v. Chase*, 175 Minn. 259, 265, 220 N.W. 951, 954 (1928).

56. See *Bowsher*, 478 U.S. at 733.

57. See *Springer v. Philippine Islands*, 277 U.S. 189 (1928).

58. See MINN. STAT. §§ 298.22, subd. 1; 15.06, subd. 1 (1998). See also MINN. STAT. § 43A.02, subd. 22 (1998) (defining the “executive branch” to include all employees of the Board for purposes of the statutes relating to the Department of Employee Relations). Minnesota Statutes section 116J.871 defines “state agency” to include the Board for purposes of the statutes relating to the Department of Trade and Economic Development. See *id.* § 116J.871 (1998).

defines types of state agencies to include the following:

(a) An agency in the executive branch . . . whose primary purpose is to perform prescribed official or representative functions shall be designated a "board." To be classified as a board, an agency must have at least one of the following powers:

- (i) the power to perform administrative acts, which may include the expenditure of state money;
- (ii) the power to issue and revoke licenses or certifications;
- (iii) the power to make rules; or
- (iv) the power to adjudicate contested cases or appeals.

....

(d) An agency in the legislative branch composed exclusively of members of the legislature shall be designated a "legislative commission."⁵⁹

The Board clearly exercises executive power and performs administrative acts, including the approval of projects and expenditures in the Board's major accounts. It also cannot be a legislative commission because the three nonlegislators are members.⁶⁰ Therefore, the IRRR Board is an agency in the executive branch.

IV. UNCONSTITUTIONAL DELEGATION OF EXECUTIVE POWER TO LEGISLATORS

A. *General Analysis*

The Constitutional issues relate to the 1995 legislative amendments to the enabling legislation and the make-up of IRRR Board membership, which combine to provide the Board, consisting of ten legislators and three non-legislators, the explicit author-

59. MINN. STAT. § 15.012 (1998).

60. The Board has far broader management responsibilities than other legislative commissions. Those commissions have power only to review executive decisions by gathering information and holding hearings, and to make recommendations. *See, e.g.*, MINN. STAT. § 3.887 (1998) (for the Legislative Water Commission); MINN. STAT. § 3.85 (1998) (for the Legislative Commission on Pensions and Retirement).

ity to administer an executive branch agency. The composition of the IRRR Board, coupled with the specifically enumerated authority provided the IRRR Board, creates an unconstitutional usurpation of the powers exclusively reserved in the Minnesota State Constitution to the executive branch of government.

Earlier analysis in Part II.B established that the Office of the Commissioner of Iron Range Resources and Rehabilitation is clearly an agency of the executive branch. The IRRR Board, composed of ten legislators and the three nonlegislators, is an anomaly in state government. Unlike other boards, the IRRR Board is the only state board with any significant power that is composed almost entirely of legislators. While there are other very minor state boards with legislators as members, the legislators are far outnumbered by other appointed officials and the boards are advisory.⁶¹

Under Minnesota Statutes section 15.012, the IRRR Board is classified as a "board" within the executive branch.⁶² However, regardless of how the Board is classified under section 15.012, it has statutorily granted powers requiring its approval for all expenditures and projects made by the Commissioner. Members of the legislative branch are granted and are exercising substantial IRRR executive branch power and authority.⁶³

Article III of the Minnesota State Constitution states that "The powers of government shall be divided into three distinct departments: legislative, executive, and judicial. No person or persons belonging to or constituting one of these departments shall exercise any of the powers properly belonging to either of the others . . ." ⁶⁴ In addition, Article V delineates, in part, the authority of the Governor, by stating the Governor . . . "with the advice and consent of the Senate, . . . may appoint other officers provided by law . . . He shall take care that the laws be faithfully executed."⁶⁵

The composition of the Board (and the corresponding exer-

61. See, e.g., MINN. STAT. § 138.763 (1998) (creating St. Anthony Falls Heritage Board with four of the 22 members coming from the house of representatives and the senate); MINN. STAT. § 15.50 (1998) (creating the Capitol Area Architectural Planning Board with two of the eight members coming from the house of representatives and the senate).

62. See *id.* § 15.012, subd. 2.

63. Even if the IRRR Board is found to be exercising legislative rather than executive power, the arrangement would still violate the Presentment Clause of the Minnesota Constitution, providing that "Every bill . . . shall be presented to the governor." MINN. CONST. art. IV, § 23.

64. *Id.* art. III, § 1.

65. *Id.* art. V, § 3.

cise of the Board's statutorily-prescribed authority) violates the constitutional doctrine of separation of powers. The Minnesota Constitution states, in part, that "*No person or persons belonging to or constituting one of these departments shall exercise any of the powers properly belonging to either of the others . . .*"⁶⁶ As noted earlier, over the years the legislature modified portions of chapter 298 to require that the Commissioner submit all projects and expenditures to a Board comprised of almost exclusively legislators (who collectively can control the outcome of any vote) for their approval.⁶⁷ Neither the Commissioner nor the Governor can override their decision.⁶⁸ The Board now has substantial control over all administration of the agency.

Furthermore, the current legislative membership has significantly exercised the powers conferred upon the Board. For instance, since 1995 these legislative branch officials have interpreted the statute to give them both policy and operational control of the agency.⁶⁹ The Chair and other Board members sometimes direct staff without approval or knowledge of the Commissioner. The Board has passed budgets that cut a number of programs out of the Commissioner's budget. The Board has directed that, for virtually any spending, the Commissioner bring the matter to the Board for approval or get personal approval from a named senator or representative.⁷⁰ They have, in practice and effect, been operating as agency administrators and exercising authority traditionally reserved for the executive branch. In other words, the Governor, acting through his Commissioner, has little actual authority over the approval of projects and the expenditure of agency funds; actual and practical control has been substantially transferred to a board of legislators. This detailed involvement in administrative decision-making over a state agency by a board comprised of ten legislators (and three non-legislators) is a direct usurpation of executive branch powers. The statutorily mandated super-majority requirement for some of the accounts further strengthens the separation of powers argument. Because all expenditures and projects in significant accounts must be approved by an eight-vote majority of the

66. *Id.* art. III, § 1 (emphasis added).

67. *See* MINN. STAT. § 298.22, subd. 2 (1998).

68. *See id.*

69. *See* Memorandum from Jim Gustafson, Commissioner, to Doug Gregor, Assistant Attorney General, Minutes, IRRR Board Meeting, July 8, 1997 (Oct. 28, 1997) (on file with the author).

70. *See id.*

Board, even more power has been transferred from the executive branch to the legislative branch.

The major argument of IRRR Board members supporting the current governance structure is that the Board is purely advisory to the Governor, who makes all final decisions. This argument is simply not what the statute says. The Board has final power over the Board Account, and co-equal, not advisory, power with the Governor on the other accounts. The Governor cannot act to execute the laws without Board approval. Moreover, the Board had advisory power prior to the 1995 amendments. Clearly, the 1995 amendments direct the Board to exercise control.

When the Board imposed strict limits on the Commissioner's executive branch discretionary authority, it also interfered with the Governor's Constitutional responsibility under Article V to "take care that the laws be faithfully executed."⁷¹ Minnesota Statutes chapter 298 states that before the Commissioner can expend any resources, the Commissioner first must obtain the approval of the Board (ten of whom are elected legislators appointed by legislative branch leadership).⁷² Under the statute, the Board, comprised almost solely of legislators, could vote to withhold the approval of expenditures necessary to comply with the law.⁷³ Consequently, the Governor could not take any appropriate action to ensure that he fulfills his constitutional oath to "take care that the laws be faithfully executed."⁷⁴

The strength of the separation of powers doctrine in the Minnesota Constitution is buttressed further by Article IV, Section 5. Article IV, Section 5 provides, "No senator or representative shall hold any other office under the authority of the United States or the state of Minnesota, except that of post-master or notary public."⁷⁵ From the language used, it is clear that the service as a senator or representative is "an office" meaning a position of duty, trust or authority, or a position as an official. In examining whether a legislator holds a disqualifying office, the courts will look at whether the person has independent authority under the law, either alone or with others of equal authority, to determine public policy or to make a formal decision not generally subject to super-

71. MINN. CONST. art. V, § 3.

72. See MINN. STAT. § 298.22, subd. 2.

73. See *id.*

74. MINN. CONST. art. V, § 3.

75. *Id.* art. IV, § 5.

visory approval.⁷⁶ The two specific exceptions, “the office” of postmaster and “the office” of notary public, are low-level appointments. This indicates how broadly the constitutional language was intended to sweep. Even a notary public holds “an office.” The constitutional language and its interpretations prohibit a legislator from serving in any position of duty, trust, or authority or position as an official in the executive branch except postmaster or notary public.⁷⁷ Membership on the Board is clearly an “office” under the authority of the state, as the acts of its members are not generally subject to supervision. Joint service as a legislator and as a member of the IRRR Board making executive decisions violates the “incompatible offices” provisions of the Minnesota Constitution.

B. *Separation of Powers*

The Minnesota and United States Constitutions have similar separation of powers doctrines, and both support the conclusion that the IRRR Board’s composition is unconstitutional. The Minnesota Supreme Court has not decided a case where the legislature has delegated executive power to agents of the legislature; however, the court has defended the separation of powers in a number of cases.

In *State ex rel. University of Minnesota v. Chase*,⁷⁸ the Governor, through the Commission of Administration and Finance—created by an act of the legislature to centralize administrative responsibility in the Governor—claimed authority to supervise and control the making of contracts and the expenditure of all moneys by the University.⁷⁹ The court found, “The right to control University finances is the power to dictate academic policy and direct every institutional activity.”⁸⁰ The constitutional issue was whether this claim of power over the University violated Article 8, Section 4 of the Minnesota Constitution, providing, “All the rights, immunities, fran-

76. See *McCutcheon v. City of St. Paul*, 298 Minn. 443, 446, 216 N.W.2d 137, 139 (1974).

77. See Op. Minn. Att’y Gen. 28-B-1 (Sept. 22, 1948) (serving as a legislator and railroad and warehouse commissioner violates the “incompatible offices” provision); Op. Minn. Att’y Gen. No. 302, 265(1930) (member of legislature is not eligible to appointment as member of civil service board); Op. Minn. Att’y Gen. 280-H (Mar. 3, 1939) (member of legislature cannot be member of school board); Op. Minn. Att’y Gen. 280-H (Dec. 19, 1950) (member of legislature cannot be member of retirement board).

78. 175 Minn. 259, 220 N.W. 951 (1928).

79. See *id.* at 260, 220 N.W. at 952.

80. *Id.* at 260, 220 N.W. at 952.

chises and endowments heretofore granted or conferred are hereby perpetuated unto the University”⁸¹ The court noted that a corporation had been created in 1851, and was “perpetuated” by the Constitution in 1858 with “all the rights, immunities, franchises and endowments” which it then possessed.⁸² “Of that corporation the regents were both the sole members and the governing board.”⁸³ “So the University, in respect of its corporate status and government, was put beyond the power of the Legislature by paramount law”⁸⁴

The court found that the Minnesota Constitution meant that “. . . the whole executive power of the University having been put in the regents by the people, *no part of it can be exercised or put elsewhere* by the Legislature.”⁸⁵ The court noted that:

Generally, the distinction between the jurisdiction of the Legislature and that of the regents is that between legislative and executive power. Legislative power, as distinguished from executive power, is the authority to make the laws, but not to enforce them or appoint the agents charged with the duty of such enforcement.⁸⁶

In *Holmberg v. Holmberg*,⁸⁷ a case decided January 28, 1999, the Minnesota Supreme Court again defended the doctrine of separation of powers. The doctrine is based on the principle that when the government’s power is concentrated in one of its branches, tyranny and corruption will result.⁸⁸ The case presented the issue whether the administrative child support process created by the legislature violated the separation of powers doctrine by infringing upon the original jurisdiction of the district court.⁸⁹ The court, looking at Article VI of the Minnesota Constitution giving the district courts original jurisdiction in all court and criminal cases, determined that, “With the creation of the administrative process, the legislature has delegated to an executive agency the district court’s inherent equitable power. This delegation infringes on the district

81. MINN. CONST. art. VIII, § 4.

82. *Chase*, 175 Minn. at 259, 220 N.W. at 951.

83. *Id.* at 265, 220 N.W. at 954.

84. *Id.*

85. *Id.* (emphasis added).

86. *Id.* (citation omitted).

87. 588 N.W.2d 720 (Minn. 1999).

88. *See id.* at 723.

89. *See id.* at 725-26.

court's original jurisdiction."⁹⁰

In *Irwin v. Surdyks Liquor*,⁹¹ a case decided September 6, 1999, the Minnesota Supreme Court reaffirmed its commitment to vigorously defend the separation of powers doctrine.⁹² The court, looking at Article III of the Minnesota Constitution, concluded that the attorney fee provisions in the Worker's Compensation Act infringed upon the court's inherent power to oversee attorneys and attorney fees and therefore were unconstitutional.⁹³ The separation of powers themes found in Minnesota law are consistent with how the federal courts have addressed separation of powers issues. Since the inception of our nation, the separation of powers has been an important consideration, especially with regard to overreaching by the legislative branch:

The legislative department derives a superiority in our governments from other circumstances. Its constitutional powers being at once more extensive and less susceptible of precise limits, it can with the greater facility, mask under complicated and indirect measures, the encroachments which it makes on the co-ordinate departments. It is not unfrequently a question of real-nicety in legislative bodies, whether the operation of a particular measure, will, or will not extend beyond the legislative sphere.⁹⁴

The Constitution of the United States provides the basic outline for how our federal government is to operate. It defines three branches of government, and vests specific powers in each of these branches.⁹⁵ This division of power was instituted to prevent one branch from becoming too powerful.⁹⁶ The doctrine of separation

90. *Id.*

91. 599 N.W.2d 132 (Minn. 1999).

92. *See id.* at 137-42.

93. *See id.* at 142.

94. THE FEDERALIST No. 48, at 334 (James Madison) (Jacob Cooke ed., 1961).

95. *See* U.S. CONST. art. I, § 1 ("All Legislative Powers herein granted shall be vested in a Congress of the United States . . ."); *Id.* art. II, § 1, cl. 1 ("The Executive Power shall be vested in a President of the United States of America."); *Id.* art. III, § 1, cl. 1 ("The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish.").

96. *See* THE FEDERALIST No. 47, at 324 (James Madison) (Jacob Cooke ed., 1961). "The accumulation of all powers legislative, executive and judiciary in the same hands, whether of one, a few or many, and whether hereditary, self appointed, or elective, may justly be pronounced the very definition of tyranny." *Id.*

of powers prohibits the legislative branch, either directly or through its agents, from exercising executive power.⁹⁷

Although Minnesota courts have not decided cases where the legislature has delegated executive power to its agents, the United States Supreme Court has decided such a case. In *Metropolitan Washington Airports Authority v. Citizens for the Abatement of Aircraft Noise, Inc.* (“Washington Airports”),⁹⁸ the Court found unconstitutional a delegation of executive power to legislators that is almost identical to the executive power delegated to the IRRR Board.⁹⁹

Congress established an airport authority for the two major airports in the Washington, D.C. area, Dulles Airport and National Airport.¹⁰⁰ Congress created a Metropolitan Washington Airport Authority (“MWA”), which in turn was to create a Board of Review, consisting of nine members of Congress who served on the various transportation committees.¹⁰¹ Congress required the Authority to submit a number of decisions to the Board for approval, including the adoption of a budget, authorization of bonds, promulgation of regulations, endorsement of a master plan, and the appointment of the chief executive officer.¹⁰² The Court of Appeals for the District of Columbia held that “the Board was in essence a congressional agent with disapproval powers over key operational decisions that were quintessentially executive, and therefore violated the separation of powers.”¹⁰³

The Supreme Court affirmed the judgment of the court of appeals, noting that the Constitution contains two elemental restraints on Congress: first, that it may not invest itself or its members with either executive power or judicial power; and second, when it exercises its legislative power, it must follow the single, finely wrought and exhaustively considered procedures specified in Article I.¹⁰⁴ In discussing the first constraint, the Court cited its earlier decisions in *Springer v. Philippine Islands*¹⁰⁵ and *Bowsher v.*

97. See *Bowsher v. Synar*, 478 U.S. 714 (1986).

98. 501 U.S. 252 (1991).

99. See *id.* at 255.

100. See *id.* at 260.

101. See *id.*

102. See *id.* at 259.

103. *Id.* at 263.

104. See *id.* at 274 (citing *J.W. Hampton, Jr., & Co. v. United States*, 276 U.S. 394 (1928) and *INS v. Chadha*, 462 U.S.919, 951 (1983)).

105. 277 U.S. 189 (1928). *Springer* is also cited by the Minnesota Supreme Court in *State ex rel. University of Minnesota v. Chase*, 175 Minn. 259, 267, 220 N.W. 951, 954 (1928).

Synar.¹⁰⁶

In *Springer*, plaintiffs challenged the validity of acts of the Philippine Legislature that authorized a committee of three—two legislators and one executive—to vote corporate stock owned by the Philippine Government.¹⁰⁷ Because the statute authorized two legislators to perform the executive function of controlling the management of the government-owned corporations, the Court held the statutes invalid.¹⁰⁸

A similar result was reached in *Bowsher*, where the Court discussed the validity of a delegation of authority to the Comptroller General to revise the federal budget.¹⁰⁹ After concluding that the Comptroller General was an agent of Congress, the Court held that he could not exercise executive powers.¹¹⁰ As the *Bowsher* Court stated:

To permit the execution of the laws to be vested in an officer answerable only to Congress would, in practical terms, reserve in Congress control over the execution of the laws The structure of the Constitution does not permit Congress to execute the laws; it follows that Congress cannot grant to an officer under its control what it does not possess¹¹¹

The *Washington Airports* Court applied the standards of *Springer* and *Bowsher* and concluded that Congress had invested itself with executive power.¹¹²

In addressing the second constraint—that when Congress exercises its legislative power it must follow Article I procedures—the *Washington Airports* Court cited its decision in *INS v. Chadha*.¹¹³ *Chadha* involved the validity of a statute that authorized either house of Congress by resolution to invalidate a decision by the Attorney General to allow a deportable alien to remain in the United States.¹¹⁴ The Court struck down the statute, holding that Congress

106. 478 U.S. 714 (1986).

107. See *Springer*, 277 U.S. at 198.

108. See *id.* at 209.

109. See *Bowsher*, 478 U.S. at 714.

110. See *id.*

111. Metropolitan Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc., 501 U.S. 252, 274 (1991) (quoting *Bowsher*, 478 U.S. at 726).

112. See *id.* at 255.

113. See *id.* at 259 (citing *INS v. Chadha*, 462 U.S. 959 (1983)).

114. See *Chadha*, 462 U.S. at 959.

cannot exercise its legislative power to enact laws without following the bicameral and presentment procedures specified in Article I.¹¹⁵

Applying the principles set forth in *Springer*, *Bowsher*, and *Chadha*, the *Washington Airports* court held that the Board of Review's power was constitutionally impermissible:

. . . If the power is executive, the Constitution does not permit an agent of Congress to exercise it. If the power is legislative, Congress must exercise it in conformity with the bicameralism and presentment requirements In short, when Congress "[takes] action that ha[s] the purpose and effect of altering the legal rights, duties, and relations of persons . . . outside the Legislative Branch," it must take that action by the procedures authorized in the Constitution.

One might argue that the provision for a Board of Review is the kind of practical accommodation between the Legislature and the Executive that should be permitted in a "workable government." Admittedly, Congress imposed its will on the regional authority created by the District of Columbia and the Commonwealth of Virginia by means that are unique and that might prove to be innocuous. However, the statutory scheme . . . provides a blueprint for extensive expansion of the legislative power beyond its constitutionally confined role Congress could, if this Board of Review were valid, use similar expedients to enable its Members or its agents to retain control, outside the ordinary legislative process or the activities of state grant recipients charged with executing virtually every aspect of national policy Legislative "power is of an encroaching nature," . . . [and] the Board of Review is an impermissible encroachment.¹¹⁶

The *Washington Airports* decision relies on the elemental tenets of American democracy shared by Minnesota. "Legislative power . . . is the authority to make laws, but not to enforce them or appoint the agents charged with the duty of such enforcement."¹¹⁷ Or, as Chief Justice Marshall more generally observed: "It is the pe-

115. *See id.*

116. *Id.* at 276.

117. *Buckley v. Valeo*, 424 U.S. 1, 140 (1976) (quoting *Springer*, 277 U.S. at 189); *State ex rel. Univ. of Minn. v. Chase*, 175 Minn. 259, 264, 220 N.W. 951, 954 (1928) (quoting *Springer*, 277 U.S. at 189).

cular province of the legislature to prescribe general rules for the government of society; the application of those rules to individuals in society would seem to be the duty of other departments."¹¹⁸

In sum, Congress may not intervene in the decision-making necessary to execute the law.¹¹⁹ "The structure of the Constitution does not permit Congress to execute the laws; it follows that Congress cannot grant to an officer under its control what it does not possess."¹²⁰ Therefore, any scheme whereby Congress or the Minnesota Legislature—whether itself or through one of its committees, members, or agents—appoints, retains removal authority over, or otherwise exercises any type of continuing authority over a member of the executive branch violates the constitutional anti-aggrandizement principle. The doctrine of separation of powers prohibits the Minnesota Legislature, either directly or indirectly through its agent, from exercising executive power.

There is no question that the IRRR Board is an executive agency,¹²¹ and there is no question that it is composed nearly entirely of legislators who have the final determination on Board decisions. Clearly, from both the Minnesota and Federal cases, the legislature has violated the separation of powers doctrine by delegating executive powers to the IRRR Board, an agent of the legislature.

V. MANAGEMENT CHALLENGES FOR THE IRRR BOARD AND COMMISSIONER

A. *Basic Principles of Governance for Entrepreneurial Government Enterprises*

Through the statutory objectives for the various accounts listed in Part II above, the legislature has directed the Board and Commissioner to promote economic development, including tourism, to create long-term employment, and to restore minelands in the

118. *Fletcher v. Peck*, (6 Cranch) 10 U.S. 87, 136 (1810).

119. See *Bowsher v. Synar*, 478 U.S. 714, 733-34 (1986); See also *FEC v. NRA Political Victory Fund*, 6 F.3d 821 (D.C. Cir. 1993), *petition for cert. dismissed*, 513 U.S. 88 (1994) (nonvoting ex officio members of Congress, by their presence alone on an executive board, impermissibly influence an entity with executive powers).

120. *Bowsher*, 478 U.S. at 726.

121. Even if the power is legislative, the legislature must exercise it in conformity with the bicameralism and presentment requirements of the Minnesota Constitution. See MINN. CONST. art. IV, § 23.

Taconite Tax Relief Area.¹²² The first two elements of this mission are highly entrepreneurial.

The Board and Commissioner are given broad commercial powers to accomplish this entrepreneurial mission. For example, Minnesota Statutes section 298.22 dealing with the Board Account provides that the Commissioner "may use whatever amounts of the appropriation . . . that are determined to be necessary and proper in the development of the remaining resources . . . and in the vocational training and rehabilitation of its residents."¹²³ Section 298.22 further grants the Commissioner specific powers to acquire real estate and personal property by purchase or lease,¹²⁴ to lease property to others,¹²⁵ and, with respect to Giants Ridge recreation area, to acquire by purchase or lease real and personal property as well as to establish and participate in charitable foundations and nonprofit corporations.¹²⁶ The Board is given the power to acquire an equity interest in any project for which it provides funding.¹²⁷ The Board is similarly granted power to acquire an equity interest in projects in the Environmental Fund Account II.¹²⁸ The Board and the Commissioner are granted power to provide "loans, loan guarantees, interest buy-downs and other forms of participation with private sources of financing . . ." in Economic Development Fund Account II.¹²⁹ The legislature grants the same powers to the Commissioner and Board with respect to the Economic Protection Trust Account plus the power to invest in a venture capital fund or enterprise.¹³⁰

The combination of an entrepreneurial mission as a public investment banker and venture capitalist and substantial commercial powers to carry out the mission makes clear that the Board and Commissioner are, in effect, a form of government enterprise. The Board and Commissioner are clothed with the power of government but possessed of many of the powers of a private financial enterprise. Essentially, the legislature has directed the Board and Commissioner to promote economic development and create long-

122. See *supra* Part II and accompanying notes.

123. MINN. STAT. § 298.22, subd. 1 (1998).

124. See *id.* § 298.22, subd. 3.

125. See *id.* § 298.22, subd. 5.

126. See *id.* § 298.22, subd. 7.

127. See *id.* § 298.22, subd. 6.

128. See *id.* § 298.2961, subd. 2.

129. *Id.* § 298.2213, subd. 3.

130. See *id.* § 298.292.

term employment in the Taconite Tax Relief Area by making the most cost effective or efficient investments and loans that achieve the objectives.

There is a literature on government enterprise. The oldest legal form for operating a government enterprise is a government department proper or a subdivision of a government department. Under this legal structure, direct responsibility on all matters devolves on the director of the department and ultimately on the chief executive of the government. Personnel are subject to civil service regulation. The enterprise is financed by annual appropriations and is subject to the budget, accounting, and audit controls applicable to other government activities. The department has the sovereign immunity of the state.

A second alternative, the public corporation form, is not a government department because it has its own board of directors and accounts and the capacity to sue and be sued in its corporate name. Except for appropriations to provide capital or to cover losses, a public corporation is usually independently financed and is not subject to the budget, accounting, or audit procedures applicable to government departments.

A brief analysis of information costs and the need for flexibility in business decisions will assist in laying the foundation for a discussion of both forms. It seems clear that in everyday life there is an opportunity cost to the gaining of information; this is called an *information cost*. It also seems clear that perfect information does not exist; that is, no one knows *a priori* how to attain government policies at an absolute minimum cost. However, it is plausible to assume that the closer a decision-maker is to the market, the lower the information costs of the data necessary for a decision. The precise relationship of information costs and bureaucratic structure will depend on the characteristics of the industry and the regulatory mechanism utilized, but in general, decisions made further from the market will suffer from informational poverty. Because of the information loss that accompanies the transmission of information and judgments from lower levels of the hierarchy to higher levels, the ultimate basis of a decision may be misleading at best and erroneous at worst.

It also seems plausible to assume that the closer the decision-maker is to the market (all other things being equal), the more responsive to changing market conditions the decision-maker will be. Decisions made further from the market will suffer from response

lag.

It is axiomatic that business conditions change continually and rapidly and that both informational poverty and response lag lead to lost opportunities and higher costs. Underscoring the problem of informational poverty, Professor William Baumol observes:

[I]n a changing world there is much force to the argument that the manager of some business enterprise will generally be better informed than a government representative as to the requirements for the efficient operation of his plant The operation of any particular firm can rarely be mastered by proxy, and this is especially likely to be true where one attempts to operate many undertakings simultaneously which vary in detail.¹³¹

As for responsiveness, business institutions must be able to adjust quickly to changing conditions in order to survive.

Problems of informational poverty and response lag are evident in department-form enterprises, where efficient resource allocation is rendered problematic. Serious shortcomings of departments are both the failure to get correct information and act on it and the lack of flexibility necessary to give initiative and enterprise full reign.

An even more serious shortcoming of departments is their imperviousness to changing conditions because of red tape and bureaucracy. This lack of responsiveness was noted by Professor John Thurston, who commented:

[A] government department is notoriously poor at adaptation. Hampered by partisan control, operating on a fixed yearly budget, bound by rigid rules governing its purchases, accounting, expenditures, and personnel, unable to borrow on its own responsibility to provide for new capital equipment or to expand working capital quickly, embarrassed by immunity from suit and other legal rules affording special privileges to the government which destroy commercial confidence and make it impossible to carry on business in accordance with the usual commercial practice, the government department is a sorry failure

131. WILLIAM J. BAUMOL, *WELFARE ECONOMICS AND THE THEORY OF THE STATE* 159-60 (1952).

as an entrepreneur.¹³²

Rigid rules for the purchase of supplies, placing of contracts, and promotion of personnel are examples of stipulations inherent in government-department activity. These rules conflict with accepted commercial practices and hamper response to the market.

As an early United Nations report notes, it is theoretically possible to endow a government department with a high degree of operating flexibility, but in practice it is difficult to do so.¹³³ "As long as an enterprise is not clearly differentiated from other types of governmental activity, strong pressures will be brought to make it conform to standard government regulations and procedures"¹³⁴

This leaves the public corporation form. The autonomy from government control implicit in this form is intended to address the problems of informational poverty and response lag apparent in the department form. The key question concerns governance of these corporations. What is the optimal mechanism for definition of policy and operating objectives and assurance of efficiency? A 1995 congressional report states that a major challenge remains for government corporations: how can these corporations "be held politically accountable for their policies and operations while still being assigned the necessary financial and administrative discretion to function in a commercial manner?"¹³⁵

In the United States, events have moved more quickly than theory, and public corporations have been regularly created to meet crises. Guided by an unreasoned faith in autonomy from fiscal controls as the cure-all for the defects of the department form, policymakers in the United States have given cursory attention to corporate governance. The Tax Foundation in 1955 observed that "the only common characteristic that emerges from the history of government corporations is the quest for freedom from the usual government fiscal controls and procedures. The corporate struc-

132. JOHN THURSTON, *GOVERNMENT PROPRIETARY CORPORATIONS IN THE ENGLISH SPEAKING COUNTRIES* 7 (1937).

133. See UNITED NATIONS TECHNICAL ASSISTANCE ADMINISTRATION, *SOME PROBLEMS IN THE ORGANIZATION AND ADMINISTRATION OF PUBLIC ENTERPRISE IN THE INDUSTRIAL FIELD* 8 (1954).

134. *Id.*

135. RONALD C. MOE, *MANAGING THE PUBLIC'S BUSINESS: FEDERAL GOVERNMENT CORPORATIONS* ix (Apr. 1995) (report prepared for the Senate Governmental Affairs Committee).

ture provided the sought-after autonomy in budgeting, record-keeping and procedural matters."¹³⁶ Even today, there is little consensus on the most appropriate internal and legal characteristics of a public corporation.¹³⁷

Among the few giving thoughtful attention to the governance question, Thurston posited in 1937 that the defects of the department form could be remedied by a public corporation that could be "protected to the greatest possible extent from partisan interference while yet subject to *an appropriate degree of public control* on matters of broad policy. The device of a corporation, if properly applied, gives both independence and flexibility without sacrificing or endangering the public interest."¹³⁸

Thurston addressed directly the question of corporate governance in an attempt to define "an appropriate degree of control." He explained that the day-to-day administration of the corporation should be independent of the executive and the legislature, but "[i]n matters of general and public policy, the corporation must necessarily be subject to executive and legislative control."¹³⁹ In addition to having control over "general and public policy," the executive and legislature also should monitor the efficiency of the public corporation. However, Thurston perceived a dilemma in balancing the need "to ensure that the corporation functions efficiently and without waste," and the problem of "preventing unnecessary interference with details of administration."¹⁴⁰

Thurston identified government control of policy, management autonomy in operations, and the assurance of efficiency as the principal elements in the corporate-governance question, but his attempt to delineate a corporate-governance control mechanism failed because of his initial simplifying assumption. Thurston believed there are few policy questions left for the corporation because they are answered by the enabling legislation. As he stated, "The major question of policy was decided when it was determined to establish the corporation, and most problems thereafter are problems of management. . . . Indeed, once the corporation is established there are surprisingly few questions of policy remaining

136. THE TAX FOUNDATION, *CONTROLLING GOVERNMENT CORPORATIONS* 6 (1955).

137. See MOE, *supra* note 135, at xii-xiii.

138. THURSTON, *supra* note 132, at 8 (emphasis added).

139. *Id.* at 258.

140. *Id.* at 216-17.

...¹⁴¹

Implicit in this statement is the assumption that the board is essentially performing ministerial functions in carrying out the legislative policies, and the definition of policy is a minimal problem. This ignores the considerable policymaking discretion implicit in the delegation of authority to an agency to interpret legislation. In the enabling legislation for many of the transit authorities analyzed in my book, *Governance of Public Enterprise*,¹⁴² for example, legislative purposes were outlined with an extremely broad brush, leaving the boards to make critical policy decisions on modes and services. The lack of attention to issues of policy formation was a serious shortcoming.

Having made the assumption that the board's role is essentially ministerial, Thurston focused attention only on mechanisms for the government to exercise a check on the performance of the corporation. This he perceived as a problem of balancing efforts to monitor performance with problems of unnecessary interference in the details of administration.

Thurston posited that the principal control is in the power granted to the executive branch to appoint and to remove directors.¹⁴³ Another possible method of control is to have executive officers of the government serve as ex officio directors.¹⁴⁴ Thurston was concerned that this might lead to political interference and destroy the independence of management.¹⁴⁵

Audit of the corporation's accounts was considered necessary by Thurston to check for financial integrity and to determine if expenditures were made as authorized by law, but the auditor was only to report problems and not have power to disallow expenditures, as is normal with audits of government departments.¹⁴⁶ It also was believed preferable for the corporation to comply with generally accepted accounting principles and have an independent auditor than to be bogged down in the restrictions on expenditure imposed on government departments.¹⁴⁷

Thurston noted that corporate self-support was itself a consid-

141. *Id.* at 259.

142. NEIL HAMILTON & PETER HAMILTON, *GOVERNANCE OF PUBLIC ENTERPRISE* (1981).

143. *See* THURSTON, *supra* note 132, at 217-18.

144. *See id.* at 219.

145. *See id.* at 156.

146. *See id.* at 232-34.

147. *See id.* at 235-36.

erable check on management of government firms, but that a further competitive spur was necessary.¹⁴⁸ In order to ensure that management was not wasteful, Thurston advocated that some plan had to be devised to recapture the stimulus of competition or to find a substitute for it.¹⁴⁹ Uncertain how to accomplish this, he suggested further study on the possibility of comparisons among government corporations and management audits by experts.¹⁵⁰

The possibility of unnecessary government interference could be held in check by granting financial autonomy to the corporation. Thurston believed this would be the most effective means of minimizing political interference.¹⁵¹

These relationships among government supervision, management autonomy, and efficiency were unsatisfactorily defined by Thurston. The critical relationship of competition and efficiency was acknowledged but unresolved. Given no proposed substitute for competition, it seems doubtful that power of appointment and removal, audits, breakeven budget constraints, and corporate financial autonomy will approximate efficiency.

The role of the board regarding governance of operating management also was left almost totally undefined. Thurston commented only that "[a] board, moreover, is needed to stand between the corporation and political forces in order to protect it from popular and partisan demands."¹⁵²

Building on Thurston's work, I developed the public-corporation form further in my 1981 book *Governance of Public Enterprise*.¹⁵³ The public corporation board must be politically accountable for the formulation of a statement of policies reflecting the overall goals that the legislature has set for the government enterprise. Since the attainment of lowest-cost production of the goals is itself a critical goal, the board is also politically accountable for implementing conditions that are necessary to realize lowest costs in production. These conditions concern the articulation of operating objectives and performance criteria, management autonomy over operational decisions, and the introduction of pressures to minimize costs.

148. *See id.* at 259.

149. *See id.* at 215-17.

150. *See id.* at 268.

151. *See id.* at 256-57.

152. *Id.* at 150.

153. HAMILTON & HAMILTON, *supra* note 142.

1. *The Formulation of Objectives*

Consider first the formulation of general policies and operating objectives. It is clear that lowest-cost production has meaning only with relation to the type of output that is desired by the community. Without specific knowledge of the ends sought, management will be confused, leading to waste of resources and a blind, undirected transfer of income. To leave firms operating in uncertainty between straight commercial objectives and a vague sense of social responsibility is to invite both economic waste and inconsistent social choices.

In my case studies of mass transit, a lack of objectives resulted in a "management by crisis" approach to operating the firm. Responding only by way of "fire-fighting" problems on a last-minute basis inevitably raises costs by preventing selection of low-cost alternatives that require developmental lead times. These poor results attributable to inadequate policy formation may lead ironically to the possibility of greater government involvement in day-to-day operations.

Identically the same results follow from too many or too generalized objectives. "Laundry lists" of general policies, as were observed in my transit case studies, may make policymakers feel good, but are of no value in securing lowest-cost production. General policies can provide little direction to, and no control over, management. Management can trade off objectives as it desires. Furthermore, management cannot be expected to maximize more than a few variables at one time.

A necessary condition for business accountability is therefore to translate the statement of generalized policy necessary for political accountability into clear and unconflicting objectives. The objectives must define the policies in operational terms. In transit, for example, the movement of passengers, not empty seats, is the output of a transit system that provides utility. For the IRRR Board and Commissioner, it could be to maximum long-term private-sector employment in the Taconite Tax Relief Area.

The mere statement of clear objectives at least directs management efforts but does not provide a basis to measure the adequacy of management's performance. There also must be a means by which to measure the relative degree of attainment of the objectives. If objectives are defined without any method of measuring performance, evaluation is also subjective and calls forth only the minimum threshold effort that management believes will satisfy the

review. Objectives whose performance criteria define expected performance levels in specific measurable terms would provide this measurement capability. Criteria are essentially scaled operating objectives. In transit, for example, achievement could be defined by increases in the movement of handicapped. Transit efficiency is thus the lowest-cost production satisfying any given level of a mobility objective.

The design of performance criteria that reinforce management behavior leading to the fulfillment of the operating objectives is a difficult task. These standards must take into account the engineering and the social, political, and economic characteristics of a government corporation and its environment. Extreme care must be taken to monitor all criteria to prevent undesirable management response, since management, judged on the basis of the criteria, will seek to satisfy the criteria without reference to the objectives.

Cost minimization therefore requires a few clear operating objectives and performance criteria. Simplicity is desirable, since the fewer the policies and objectives, and the fewer the decisions in implementation and supervision, the more likely the policy will ultimately be realized. Implicit in clarity is the caveat that the objectives also must be consistent.

2. *Management Autonomy*

Assume that clear and consistent objectives and performance criteria have been framed. Management autonomy is a second critical condition for cost minimization. The board cannot work out cost-minimizing production strategy. This requires full-time work and inside knowledge of a business, its markets, its products, and its technologies. Management is in the most informed position to make resources productive in the pursuit of the enterprise's objectives. Stipulations dictated by the board lead to uninformed and unresponsive production decisions and consequently to waste and to lost opportunities. Therefore, if management lacks freedom to follow its own production strategy in pursuing operating objectives, it cannot be expected that lowest-cost production will be achieved.

3. *Distinguishing Policy from Management Decisions*

Underlying these simple conditions for business efficiency is a conceptual problem, as yet unresolved, concerning the distinction

between what is policy and what are operational or managerial decisions. Even though the dichotomy between day-to-day operations and policy determination is well recognized, it is not enough to say only that broad policy decisions must be distinguished from operational decisions and then to rely solely on the public corporation board's judgment to respect the distinction. With no clear theoretical distinction between policy and operating decisions, intractable practical problems are encountered in distinguishing the two.

The reason it is so difficult theoretically to distinguish policy from managerial decisions is that in fact the two concepts are just elements in a spectrum of decision-making ranging, for example, from the most general questions concerning what service is to be produced and for whom to specific questions concerning marketing, production, and finance. Realistically, there is no bright line separating policy from operations. Policy, for instance, can be framed as stipulations that limit management's role to minor administrative decisions.

The lack of a bright line does not render the matter hopeless. The attempts at lexical differentiation of policy and management decisions rest on an awareness that as policymakers dictate increasingly specific actions for management, there occurs a loss of both managerial accountability, because management is not responsible for decisions it does not make, and efficiency, because of both the informational poverty of officials removed from the market and their lack of flexibility and responsiveness in reacting to changing market conditions. Since political accountability subsumes business efficiency, policymakers are politically accountable for these results. Thus it is clear that as policymakers move along a continuum from allowing complete management autonomy to controlling completely all decisions, they are not trading business efficiency for political accountability. Indeed when the detail with which policy is articulated exceeds the minimum necessary to guide management, the efficiency losses just mentioned occur without any offsetting gains in welfare. Professor C. D. Drake observed, for example, that the scale and frequency of ministerial intervention in British public corporations grow without any corresponding increase in political accountability.¹⁵⁴

The benefits of limiting policymaking to general guidance are

154. See C. D. Drake, *The Public Corporation as an Organ of Government Policy*, in *GOVERNMENT ENTERPRISE: A COMPARATIVE STUDY* 26, 42 (W. G. Friedmann et al. eds., 1970).

clear, but the tendency toward the trivialization of political control is strong. Professor William Robson noted that regardless of what the legal texts say about powers, ministers in Britain gave little or no guidance on questions of policy but did show an increasing tendency to encroach on the details of management.¹⁵⁵ Similarly, in some systems in my transit research, boards were loath to lay down general policies but were eager to be involved in operational decisions.

To reduce the inherent ambiguity in the definitions of policy and operations and the risk of board interference in operations, statutory guidelines must spell out the distinction. A clear definition of the areas of management autonomy could be incorporated into the statutory language creating a public corporation. A possible approach would be to give management sole control over all decisions that require detailed knowledge of the production and market characteristics.

The grant of management autonomy in making production decisions also finds support in an analysis of the model of governance for private corporations. In this model, the board of directors theoretically makes policy and manages the firm, the executive officers are the agents of the board, and the shareholders elect the board and decide major issues. Professor Melvin Eisenberg points out that several factors seem relevant in addressing the question of the scope of management discretion independent of shareholders' approval within the model. First, the greater is the extent to which the matter requires specifically business knowledge, the more likely it is that the shareholders would want the decision to be made by management.¹⁵⁶ Second, the greater is the economic significance of the matter in terms of magnitude, risk, the time span of the effect, and the cost of reversal, the more likely it is that the shareholders would want to make the decision.¹⁵⁷ Third, the more frequent and routine is the matter, the more likely it is that management should make the decision.¹⁵⁸ Finally, the greater is the need for speed, the more likely it is that management should make the decision.¹⁵⁹

155. See WILLIAM ROBSON, NATIONALIZED INDUSTRY AND PUBLIC OWNERSHIP 79-80 (1960).

156. See MELVIN A. EISENBERG, THE STRUCTURE OF A CORPORATION: A LEGAL ANALYSIS 13 (1976).

157. See *id.*

158. See *id.*

159. See *id.*

Taking these factors into account, Eisenberg constructs a normative model of decision-making contemplated in state incorporation statutes by placing the kinds of decisions that arise into four general categories: business decisions in the ordinary course, business decisions out of the ordinary course, decisions involving substantial change in the structure of the enterprise, and decisions relating to the control apparatus of the entity in which the business is enveloped.¹⁶⁰ Several examples are used to clarify these categories. *Business decisions in the ordinary course* generally include hiring and firing, as well as selection of supplies and prices for materials.¹⁶¹ These are management decisions. Examples of *business decisions not in the ordinary course* are substantial expansion of plant capacity, contracts for significant portions of a firm's output, or recognition of a union.¹⁶² Shareholders through the board of directors, may expect to exercise power over such actions or to direct that such action be taken.¹⁶³ *Decisions involving substantial changes in the structure of the enterprise*, such as complete liquidation or sales of substantially all the assets, are seen as essentially shareholder decisions, as are *decisions relating to the control apparatus*, such as changes in share voting right or the number of directors.¹⁶⁴

As noted in a later article by Eisenberg, the model does not adequately describe reality.¹⁶⁵ As a practical matter, as the number of shareholders in a corporation increases, business complexity increases and management makes all business decisions, whether in or out of the ordinary course.¹⁶⁶ Moreover, it is not the board of directors that makes policy decisions and manages the firm, but rather the executive officers.¹⁶⁷ In light of practical reality, Eisenberg concludes that the principal function of the board of directors is to monitor the self-determined goals of the chief executive officer and his performance and to influence management through the selection and removal of the chief executive.¹⁶⁸ "Those who manage must be monitored to ensure that they are the right per-

160. See *id.*

161. See *id.* at 14.

162. See *id.*

163. See *id.*

164. See *id.* at 15.

165. See Melvin A. Eisenberg, *The Board of Directors and Internal Control* 19 CARDOZO L. REV. 237, 237 (1997).

166. See *id.* (explaining that boards are not able to manage because of their limited investment of time, typically meeting only six to twelve times a year).

167. See *id.*

168. See *id.* at 238.

sons for their jobs, and that they are managing in the shareholders' interests."¹⁶⁹ The monitoring model recognizes that evaluations and decisions are shaped by the information available to the decision-maker, and for this reason, executives are in a better position to make decisions.¹⁷⁰ This "monitoring" model of corporate governance is generally reflected in most modern corporation statutes, usually providing something to the effect that "the business and affairs of a corporation shall be managed by or under the direction of a board."¹⁷¹

The same divergence of theory and reality was observed in my transit case studies. Executive officers of the systems were carrying out both policymaking and management functions and had coopted information flows and the evaluation process as well. However, the lack of policy control is much more serious in a public corporation, for unlike a private corporation, where there exists a clear policy of profit-making, the policies to be pursued by a public corporation relating to income redistribution, for example, must be defined. The legislature and public corporation board must do this. However, once policy is set, the same theoretical dichotomy of business decisions in the ordinary course as opposed to extraordinary business decisions seen in the private-corporate governance model could be put to advantage in the public corporation model. The board, as representatives of the community, should exercise approval power over such decisions. The board should monitor decisions in the ordinary course on a spot-check basis, asking whether the process by which such decisions are made is sound. Decisions involving substantial changes in the structure of the public corporation or in the control apparatus should be referred to the legislature for its approval.

This division of responsibilities between the public corporation board and management clarifies to some degree the role of management and the role of the board in the regulatory process. A simpler, more understandable structure should reduce information costs incurred both by the board in monitoring management and by the community in monitoring the board.

169. *Id.*

170. *See id.* at 245-46.

171. *E.g.*, Revised MODEL BUS. CORP. ACT § 8.01(b) (1973); DEL. CODE ANN. tit. 8, § 141(a) (1998); MINN. STAT. § 302A.201, subd. 1 (1998).

B. *Summary of General Principles*

1. In order to fulfill its mission, government enterprise must be able to adjust quickly and flexibly to market conditions using the best possible information.
2. The management of a government enterprise is both substantially better informed about and responsive to the market than government representatives.
3. The operating management of a government enterprise should be independent of the legislature and the chief executive.
4. The government-department form of government enterprise fails to meet the above criteria. The public-corporation form can achieve the criteria.
5. In the public-corporation form, the following principles apply.
 - a. The legislature should set forth with clarity the overall mission and governance structure of the public corporation. The statute should spell out clearly the distinction between board policy and management operational responsibilities.
 - b. The public corporation board should formulate a clear statement of policies reflecting the legislative goals, as well as a few clear and unconflicting operating objectives and performance criteria.
 - c. Management should have autonomy over operational decisions. The board, lacking the necessary information and quick responsiveness to the market, cannot work out a cost-minimizing production strategy.
 - d. Simplicity, clarity, and consistency are highly desirable throughout the governance structure to maximize the likelihood the legislative goals will ultimately be realized.

C. *Application of the Principles to the IRRR Board and Commissioner Governance Structure*

The legislature has directed the IRRR Board and Commissioner essentially to make the most efficient investments and loans to produce long-term private sector employment in the Taconite

Tax Relief Area.¹⁷² The IRRR Board and Commissioner are a type of public investment banker and venture capitalist. Operational decisions on investments and loans require a knowledge of business management and finance.

The current governance structure of the IRRR Board and Commissioner cannot achieve the mission the legislature has directed. Operational management is substantially in the hands of the IRRR Board, consisting of legislators who, unlike private corporation officers or even directors, do not have knowledge of market conditions and who cannot adjust quickly and flexibly to changing market conditions. The super-majority board decision rules for some accounts mandated by statute substantially compound the lack of quick and flexible operational response to the market. A board consisting of legislators will politicize operational decisions, ensuring that resources will be wasted.

The governance structure is not clear, understandable, simple, or consistent. The legislature has created a number of major accounts through which revenue flows to the IRRR Board and Commissioner.¹⁷³ There is no consistency in the governance structure among the accounts. For example, in each account, the legislature apparently sought to separate the decision to undertake a project from the decision to disburse the funds to pay the project. The legislation sets forth four different models for these decisions

1. *The Board Account Model*¹⁷⁴

- a. The Commissioner is given the power to make necessary and proper decisions to carry out the mission, but the Board must approve all projects or expenditures.¹⁷⁵
- b. The Board must approve decisions as to method, manner, and time of payment of all funds proposed to be disbursed by a simple majority.¹⁷⁶

172. See MINN. STAT. § 298.22 (1998).

173. See *id.* §§ 298.22, .2213, .223, .296, .2961

174. See *id.* § 298.22.

175. See Act of May 25, 1999, ch. 223, art. 2, § 42, 1999 Minn. Sess. Law Serv. 1205 (West) (amending MINN. STAT. § 298.22).

176. See MINN. STAT. § 298.22.

2. *The Environmental Fund Account I*¹⁷⁷
 - a. The Commissioner shall administer the fund but the Board must approve all projects by a majority vote. The Governor must also approve each project.
 - b. Funds may be expended only upon the approval of the project by the Board and the Governor.¹⁷⁸

3. *The Environmental Fund Account II*¹⁷⁹
 - a. The Commissioner has power to administer the fund but the Board must approve all projects by an eight-vote super-majority vote. The Governor must also approve each project.
 - b. Disbursements may be made on a project only after approval by the Governor.¹⁸⁰

4. *The Economic Development Fund Account II and the Economic Protection Trust Account*¹⁸¹
 - a. In the Economic Development Fund Account II, the appropriation is to the Commissioner, and in the Economic Protection Trust Account, the Commissioner shall administer the program, but in both accounts the *Commissioner, the Board, and the Governor* must approve all projects. In the Economic Protection Trust Account, approval must be by an eight-vote supermajority of the board.
 - b. Disbursements may be made on a project after approval by the Governor.¹⁸²

The current statutes creating a governance structure for the IRRR Board and Commissioner are extremely poorly drafted and confusing. There is substantial ambiguity and confusion regarding allocation of responsibilities and lines of authority. The accountability of the Board and the Commissioner to the legislature, to the Governor, and to the public is undermined.

177. *See id.* § 298.223.

178. *See id.*

179. *See id.* § 298.2961.

180. *See id.*

181. *See id.* §§ 298.2213, .296.

182. *See id.* §§ 298.2213, .296.

VI. OPPORTUNITIES FOR ORGANIZATIONAL AND OPERATIONAL IMPROVEMENTS BY THE EXECUTIVE AND LEGISLATIVE BRANCHES

The current governance structure for the IRRR Board and Commissioner both undermines the goals of the legislature and is unconstitutional. The legislature should restructure the agency as a public corporation with a board of directors and operating management following the principles of governance outlined in Parts IV and V.

The Governor should appoint the IRRR Board of Directors subject to senate confirmation. Legislators cannot serve on the Board. The legislature can specify criteria for Board membership and could create an appointment selection committee to recruit and recommend candidates. The Governor could be required to choose from the list of recommended candidates. The legislature could create a legislative commission, consisting solely of legislators, to review agency decisions and to advise the legislature.

The legislature can be more specific in legislation regarding the allocation of the appropriation to certain counties or areas. This is a distribution of wealth question the legislature should resolve. However, policy and operational decisions on which investments or loans will maximize long-term private sector employment in the Taconite Tax Relief Area should be delegated to the board and management.

The legislature and Governor should act quickly to remedy the unconstitutionality of the current governance structure. Uncertainty concerning the constitutionality of the IRRR Board will undermine the Board and the Commissioner in negotiations with sophisticated investors. Everyone can be certain that litigation will eventually raise the constitutional issue.

