

Trust Land Performance: Charting a Course for the Future

For Washington State School Directors' Association
April 12, 2021

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Agenda

- Part 1 - Common School Trust, State Forestlands, Background Information



- Part 2 - Valuation Findings



- Part 3 – Initial Ideas for Moving Forward and Next Steps



Department of Natural Resources

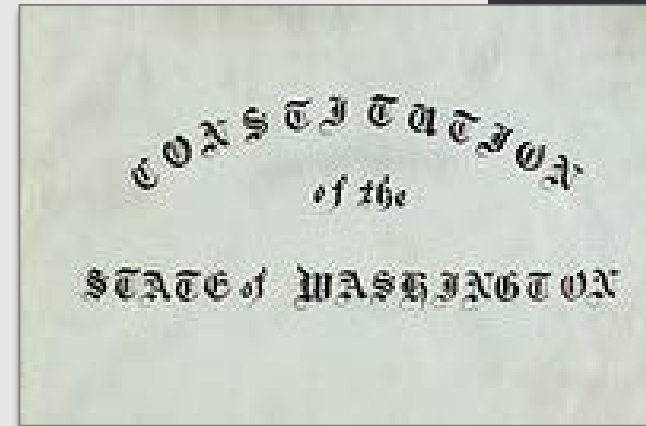
Trust Manager
~2.9 million acres
of
State Trust Lands
in Washington



Trust Responsibilities

As manager of state trust lands, DNR has legal fiduciary responsibilities to:

- Generate revenue and other benefits for each trust, in perpetuity
- Preserve the corpus of the trust
- Exercise reasonable care and skill
- Act prudently to reduce the risk of loss for the trusts
- Maintain undivided loyalty to beneficiaries
- Act impartially with respect to current and future beneficiaries



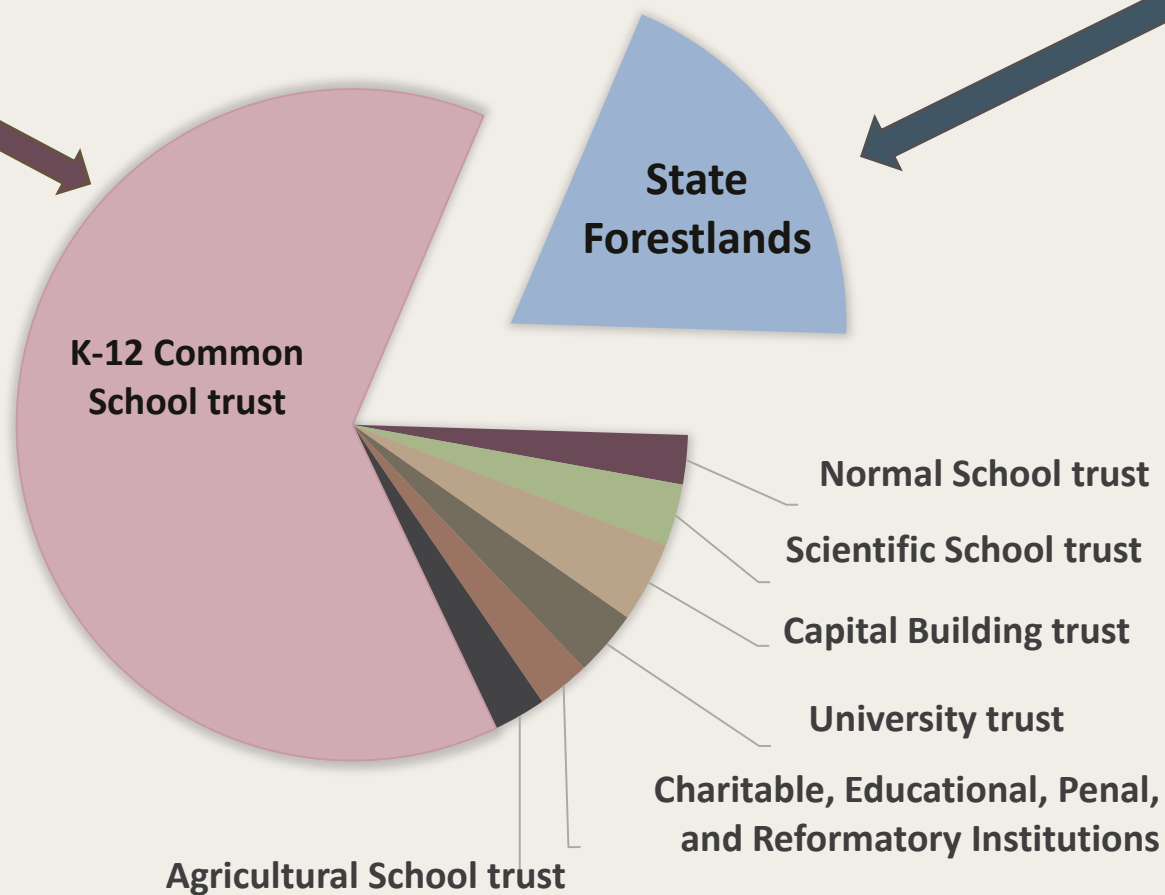
State Trust Lands

~2.9 Million Acres of State Trust Lands

State Lands

Federally granted lands

- Enabling Act (25 U.S. Statutes at Large, c 180 p. 676)
- State Constitution
- Revenue is generated from a variety of sources
- Source of financial support, primarily for public schools and colleges

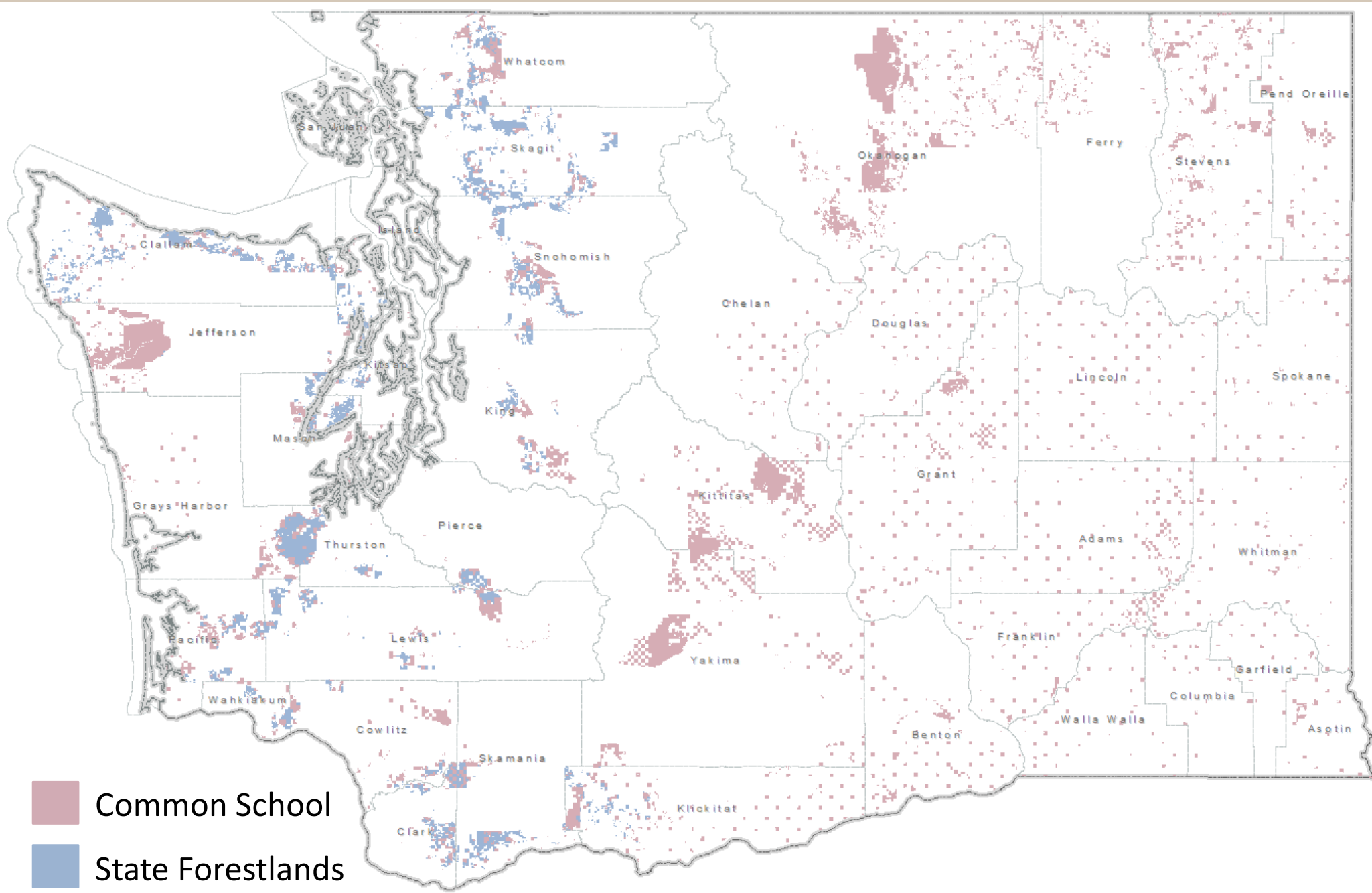


State Forestlands

- Two types: Transfer and Purchase
- > 617,000 acres*
- Transfer lands acquired by counties through tax foreclosures.
- Statutory Trusts
- Revenue helps fund county services, state schools, and junior taxing districts
- 21 counties

* Source : Deloitte Report 2020, Appendix D





Common School
State Forestlands



Common School

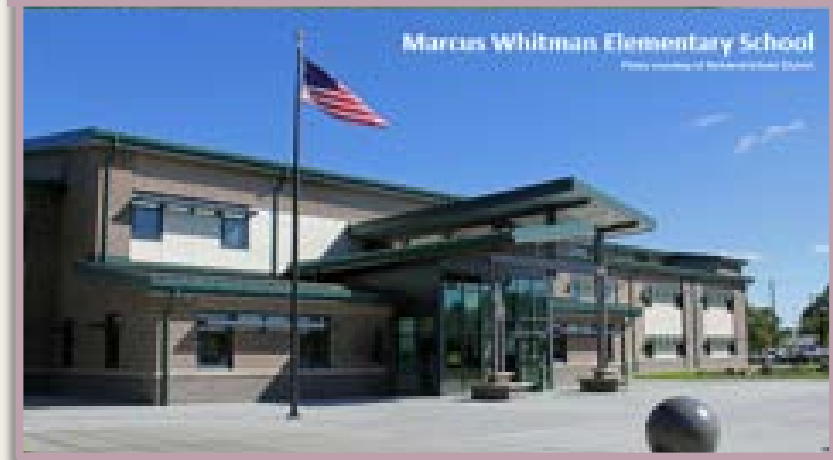


Common School Granted Trust Lands

(K-12 Common School)

- Present in all counties
- Revenue is generated from a variety of sources
- Revenue distribution is not linked with location generated
- ~1.79 million acres statewide

Income from these state grant lands supports construction of state public kindergarten through 12th grade schools



Common School Revenue from DNR

59% from Timber/ Timber-Related Activities/ TLT/ Land Sales

41% from Leases and Other Sources

(average from 2015-2019)

Year	Sales (Timber sales, timber-related, TLT, land)	Leases (Agriculture, Special Use, Commercial Real Estate, Mineral, Communication Sites, ROW, Special Forest Products)	Other Revenue (interest, permits, fees, non-trust)	Total Revenue
2015	\$ 40,585,320	\$ 31,601,638	\$279,406	\$ 72,466,364
2016	\$ 59,318,811	\$ 34,813,523	\$ 198,594	\$ 94,330,928
2017	\$ 50,427,750	\$ 35,147,682	\$ 278,453	\$ 85,853,885
2018	\$ 53,414,104	\$ 39,805,593	\$ 1,622,268	\$ 94,841,965
2019	\$ 56,616,216	\$ 36,822,199	\$ 1,110,867	\$ 94,549,281

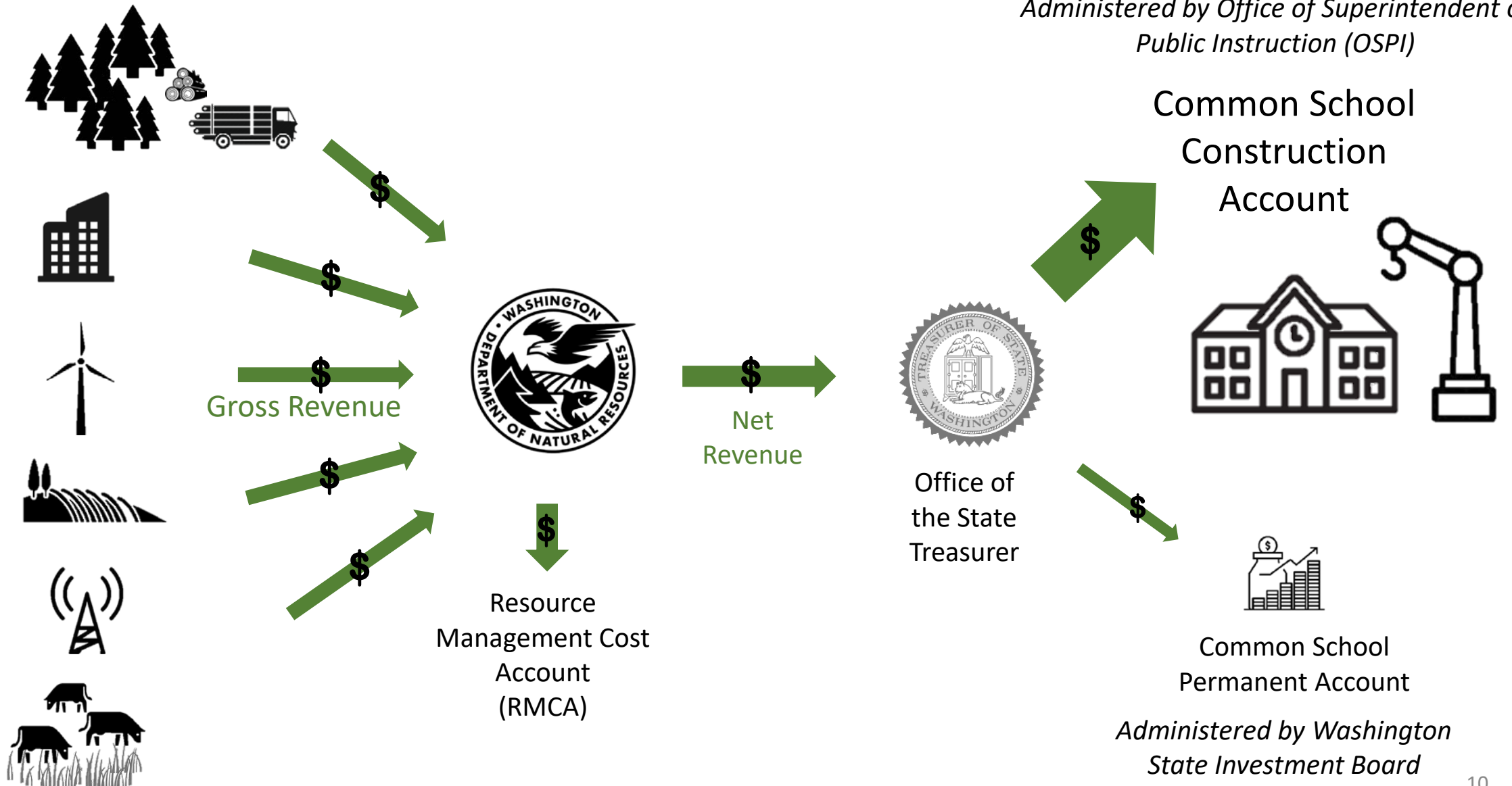
From DNR Annual Reports (based on Fiscal Year)

NOTE: Includes revenue from Indemnity and Escheat Trust Lands also

Common School Revenue and Distribution

RCW 28A.515

Administered by Office of Superintendent of Public Instruction (OSPI)





State Forestlands



State Forestlands are FOREST LANDS

a few key points in time*...



- **1923 Present Reforestation Act enacted**
State Forestlands originate in the Reforestation Act
- **1923 State Forest Board was created**
- **1923 Forest Board PURCHASE lands were authorized**
State Forest Board could acquire lands that were chiefly valuable for developing and growing timber and designate them as state forest lands
- **1927 State Forest TRANSFER lands established**
Forest lands acquired by counties through tax foreclosure could be offered to the state as forest lands
- **1957 Department of Natural Resources established**
- **1969 Reconveyance for parks authorized**
- **1971 Changes in distribution of proceeds from the State Forest Board Transfer land (25%)**
- **1986 County representative added to the Board of Natural Resources**

* Source : DNR- State Forest Board Lands: A Report to the Counties, 1987

State Forestlands Revenue from DNR

State Forestlands Revenue = **95%** from Timber

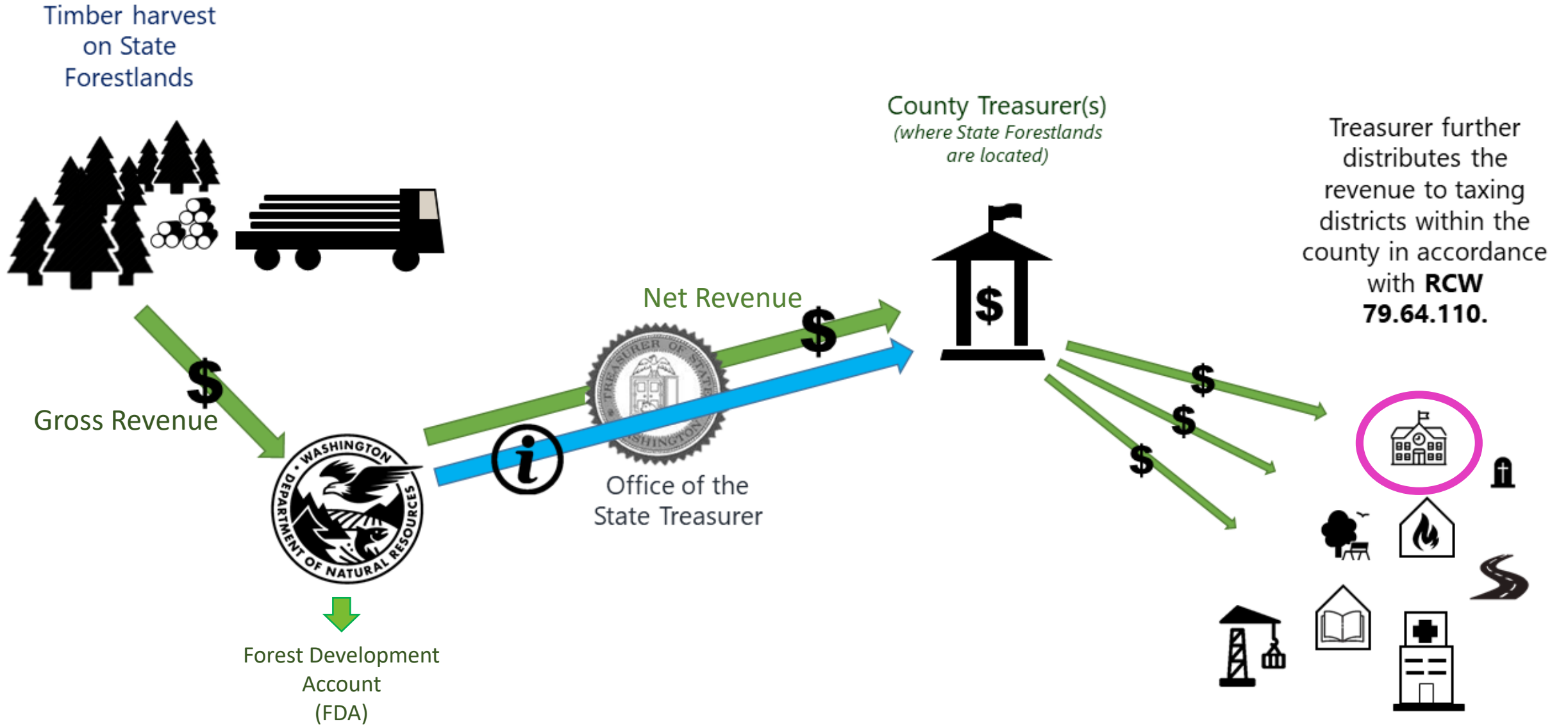
(average from 2015-2019)

Year	Timber Revenue	Non-Timber Revenue	Total Revenue	Timber Revenue % Total Revenue
2015	\$ 87,259,350	\$ 3,432,249	\$ 90,691,599	96%
2016	\$ 79,822,528	\$ 3,314,629	\$ 83,137,157	96%
2017	\$ 80,480,572	\$ 6,968,298	\$ 87,448,870	92%
2018	\$ 81,051,787	\$ 2,982,762	\$ 84,034,549	96%
2019	\$ 94,133,991	\$ 7,101,884	\$ 101,235,875	93%

From DNR Annual Reports (based on Fiscal Year)

State Forestland Revenue Distribution

RCW 79.64.110



State Forestlands

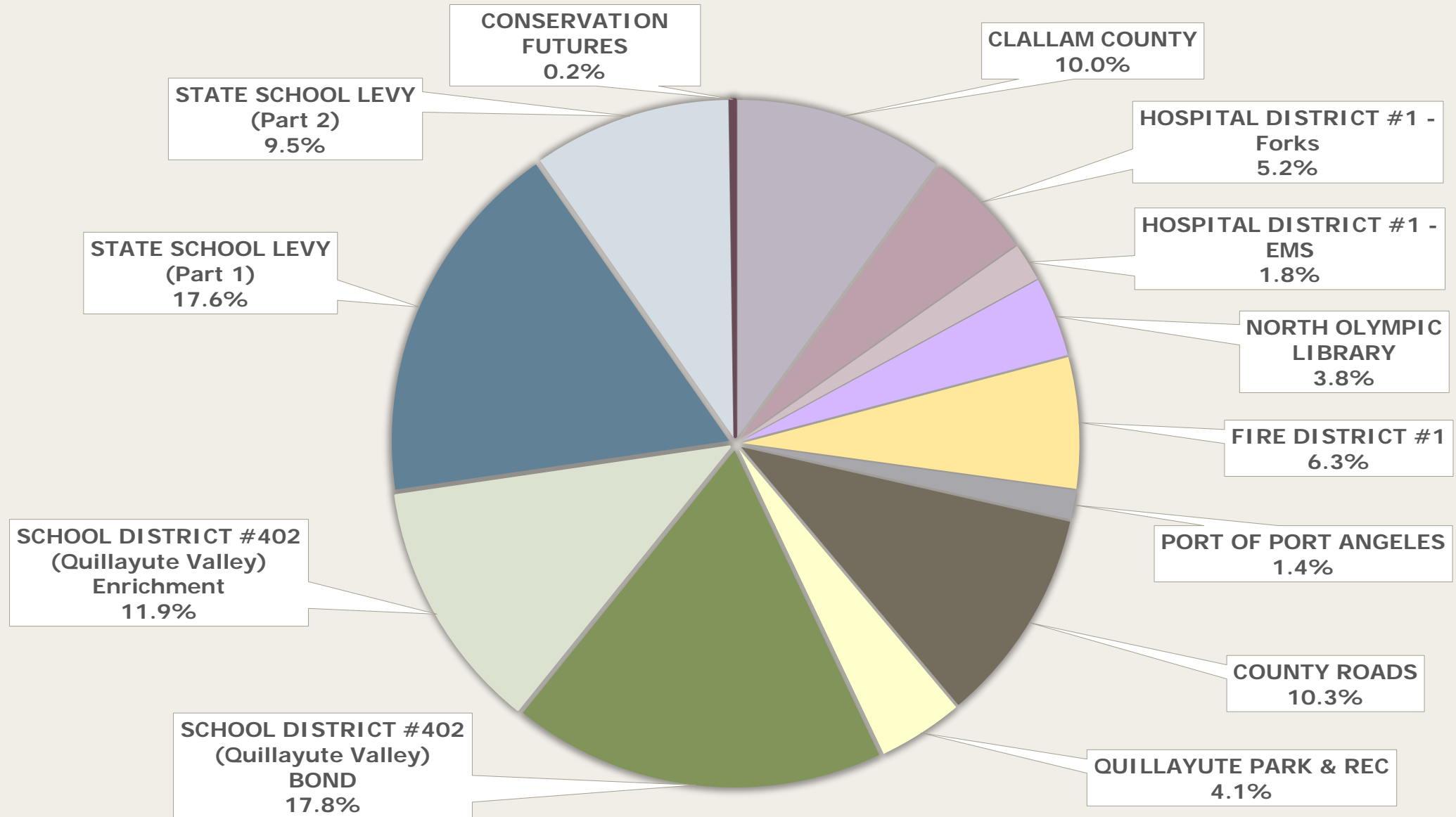
Typical Recipients of Funding



- County Services
- **School Districts**
- County Roads
- Ports
- Library Districts
- Fire Districts
- Hospitals
- EMS

Example – Clallam County Tax Area #503

Data Source: Clallam County Levy Rates Report for 2021



Board of Natural Resources

Board of Natural Resources shall establish policies ensuring land management is based on sound principles and designed to achieve maximum development and use of lands consistent with applicable laws

(summarized from [RCW 43.30.215](#))



Board Policies and Other Applicable Laws

Policy for Sustainable Forests

(Multiple state and federal laws)

- Economic Performance
- Forest Ecosystem Health and Productivity
- Social and Cultural Benefits
- Implementation

Multiple Use Concept

(Multiples Uses - RCW 79.10.120)

Sustainable Harvest Level

(Sustainable Harvest - RCW 79.10.300-340)

Habitat Conservation Plan

Endangered Species Act

(16 U.S.C. 1531 et seq.)



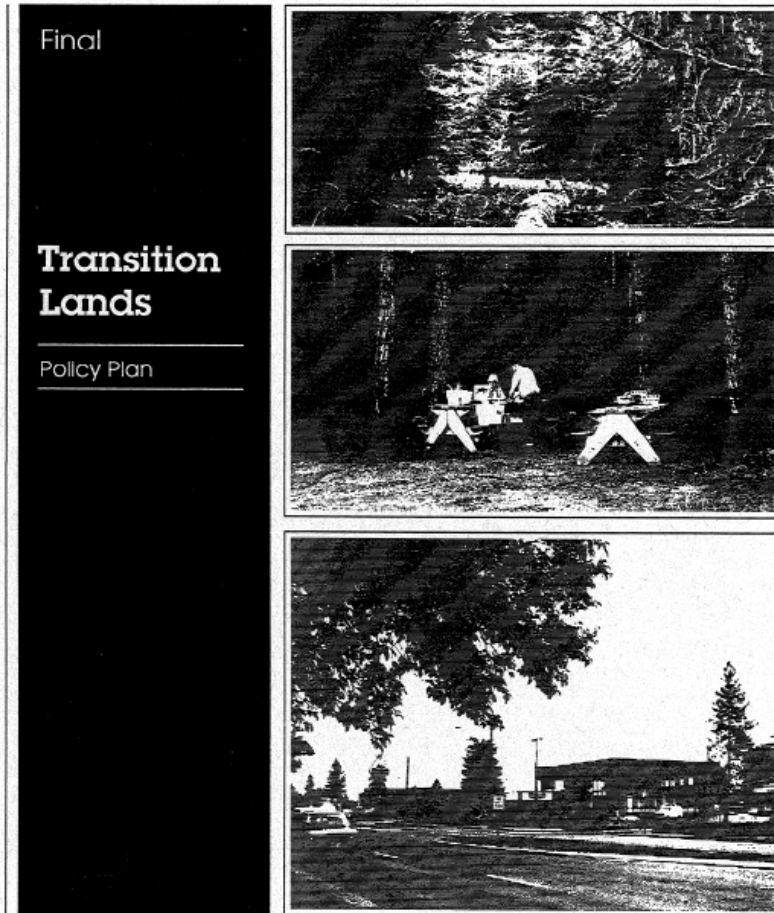
Transition Lands & Clean Energy Program



1988 Transition Lands Policy Plan

KEY GOALS

- Manage transition lands to optimize land value
- Manage land assets to achieve an optimum relationship between income and risk
- Increase the level of financial support to trust beneficiaries
- Further diversify sources of income to trust beneficiaries
- Balance the short- and long-term needs of the trust beneficiaries

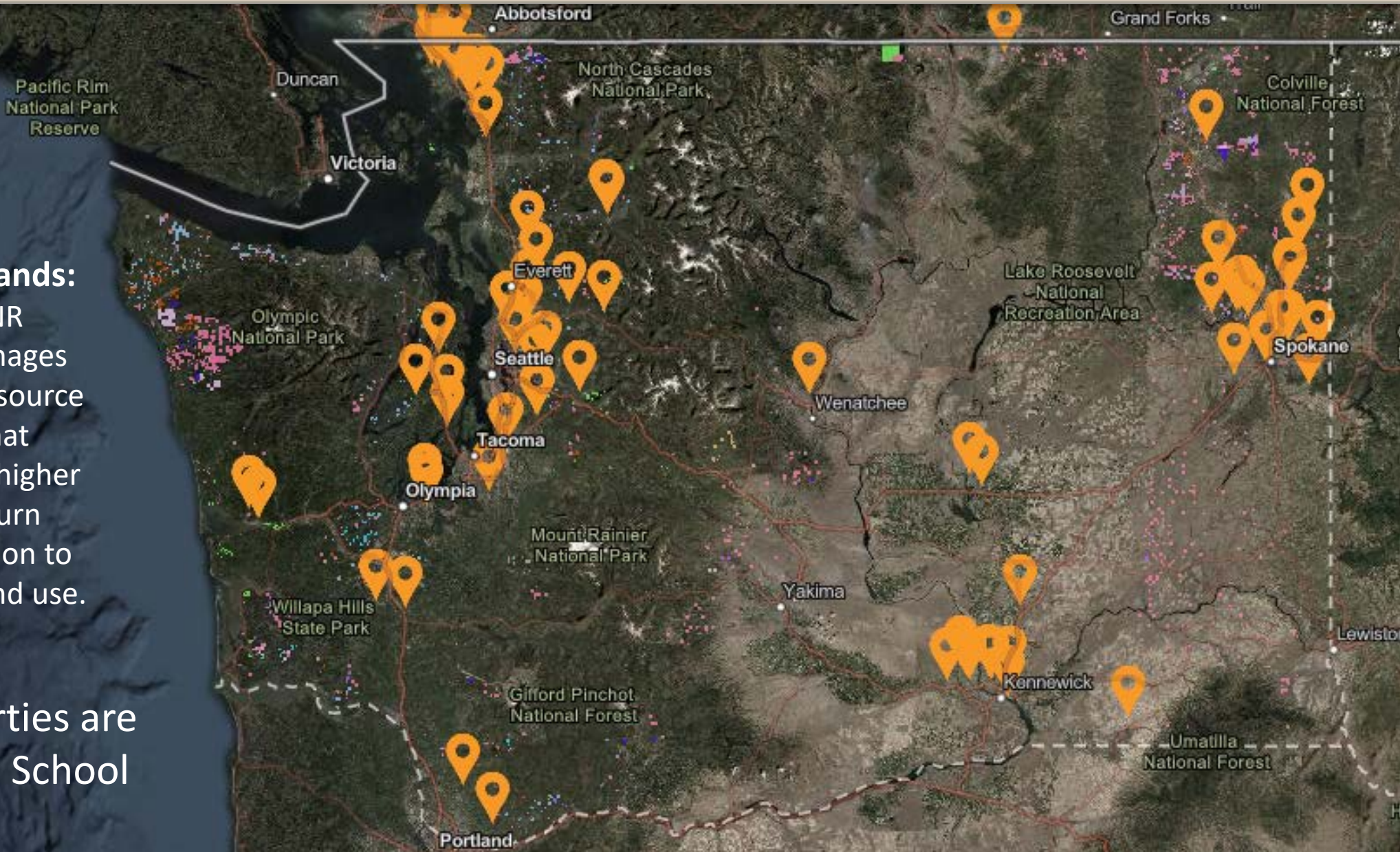


What are Transition Lands?

Transition Lands:

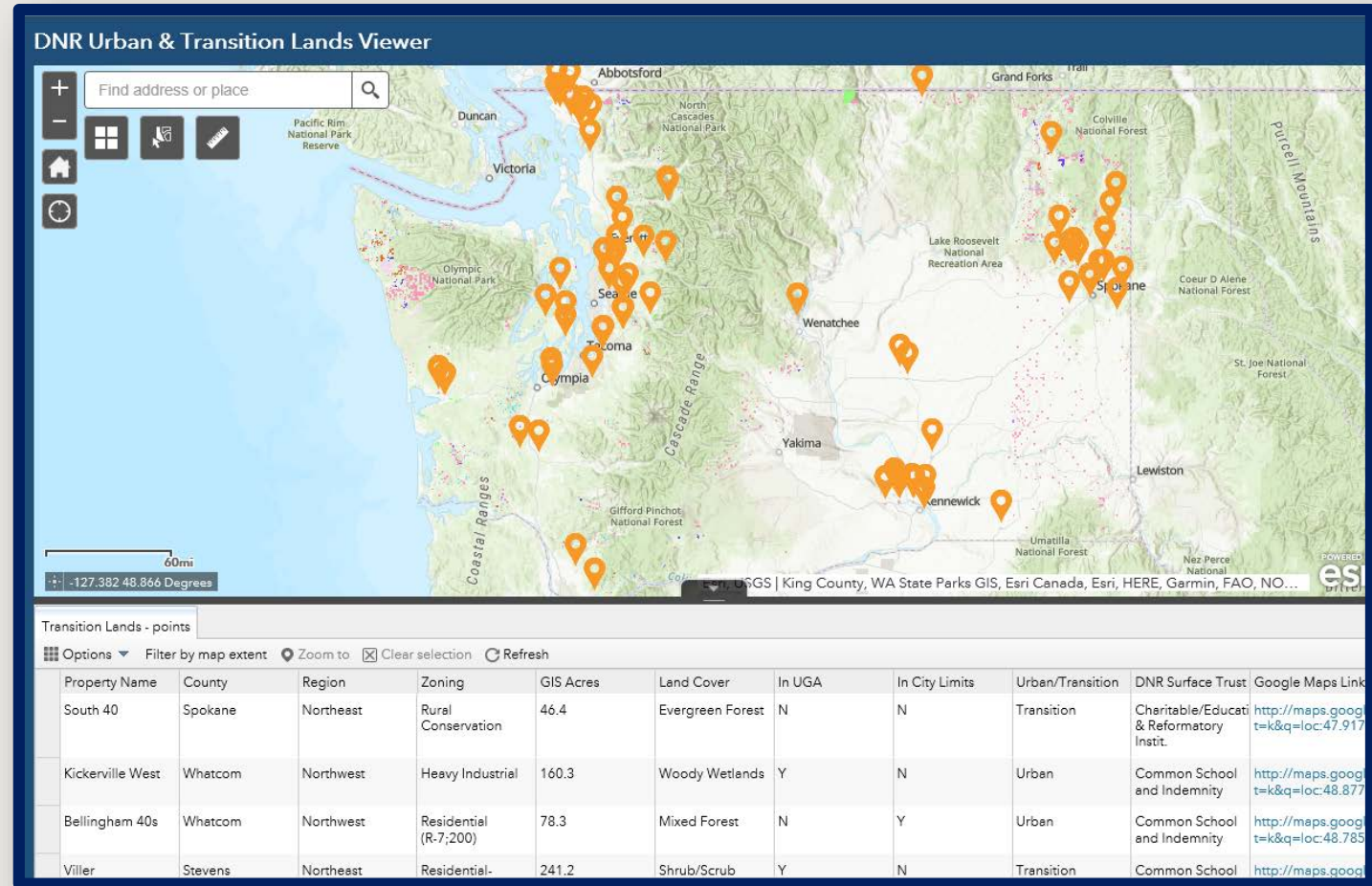
Areas that DNR currently manages for natural resource production that could yield a higher economic return from conversion to a different land use.

66 properties are
Common School



How do Transition Lands get identified?

- DNR Region staff and Commercial Real Estate Program staff conduct an annual review to identify new properties
- Updated list is brought to the Board



- Sites get added to map on DNR's website:

<https://wadnr.maps.arcgis.com/apps/webappviewer/index.html?id=47c463498d384e659c4b37ac02e840c8>

Clean Energy Program

Wind Energy

- 18 leases | ~15,000 acres
- ~\$1,242,000 Revenue (FY 2020)



Solar Energy

- 3 leases (FY 2021) | ~1,300 acres
- ~\$150,000 Revenue (FY 2020)





Clean Energy Program



Program focus:

- Goal of 500 megawatts of solar on DNR-managed lands by 2025.
- Currently working on identifying best sites for solar installations
- Looking at all opportunities:
 - Wind
 - Solar
 - Geothermal



More Information?



- DNR Annual Reports
- County Quarterly Income Reports
- State Forest Trust Lands within School Districts
- State Trust Lands Map

www.dnr.wa.gov/beneficiaries

Part 2 - Valuation Findings



- Budget Proviso
- Valuation:
 - ***Trust Land Performance Assessment – Trust Values and Returns***
Deloitte Transaction and Business Analytics
 - ***Non Market Environmental Benefits and Values***
Earth Economics
 - ***Charting a Course for the Future – Legislative Report***
Department of Natural Resources

The Commissioner's Priorities

Modernize state trust lands

Reform and enhance revenue programs with promise for immediate growth (*e.g.*):

- *Renewable energy*
- *Commercial real estate*

Optimize near- and long-term performance for *current and future generations*

Trust Lands Assessment Project

DNR partnered with the Legislature

(Proviso: ESSB 6095, Section 7015 in 2018)

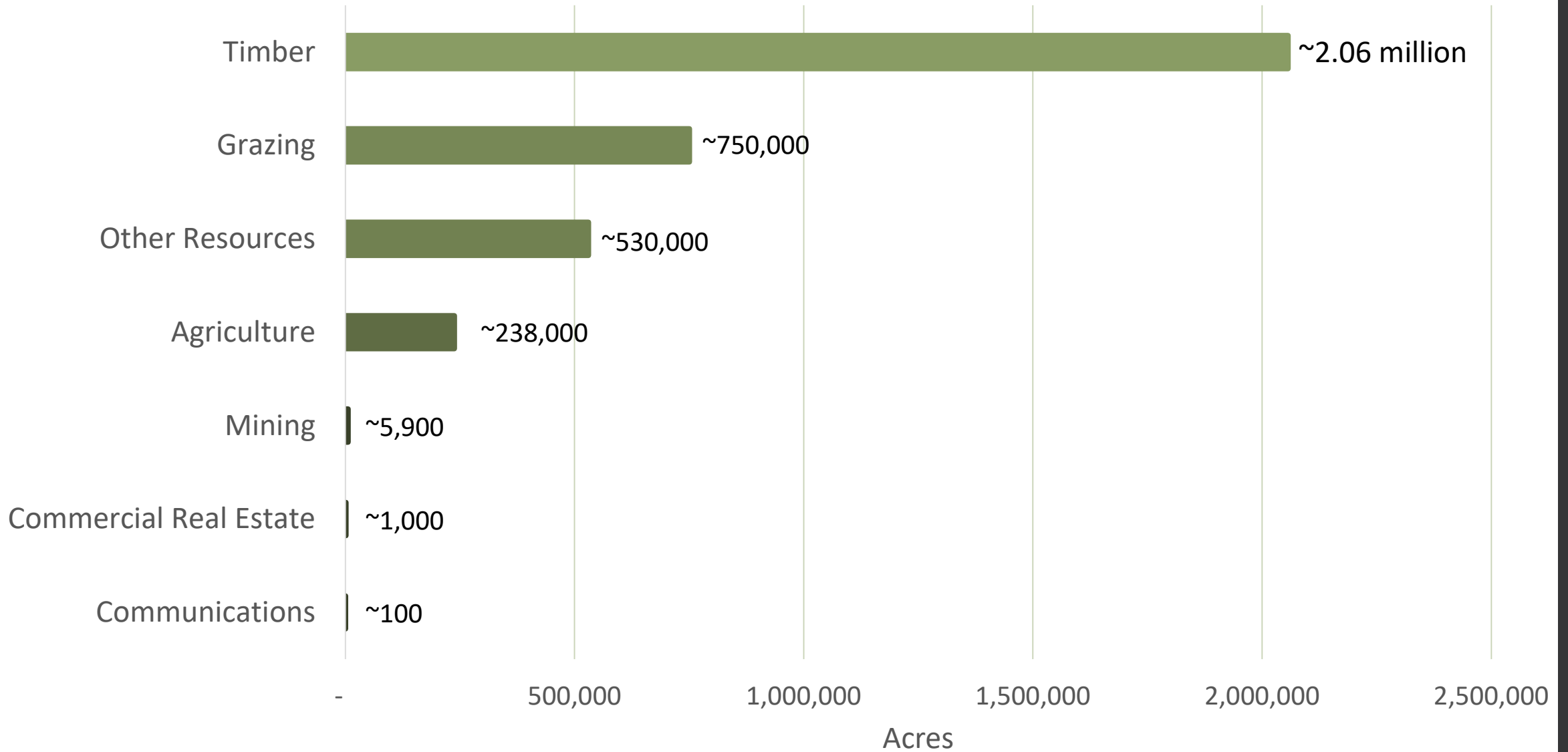
Shared funding for a comprehensive assessment of trust lands to include:

1. Estimate fair market value of the land
2. Gross & net income by asset class
3. Value ecosystem services & recreation
4. Recommendations for improvement

Asset Classes

- Timber
- Agriculture
- Grazing
- Commercial Real Estate
- Mining
- Communication Sites
- Other Resources
Includes wind energy, special forest products, rights-of-way, and special uses

Trust Land Acres in each Asset Class



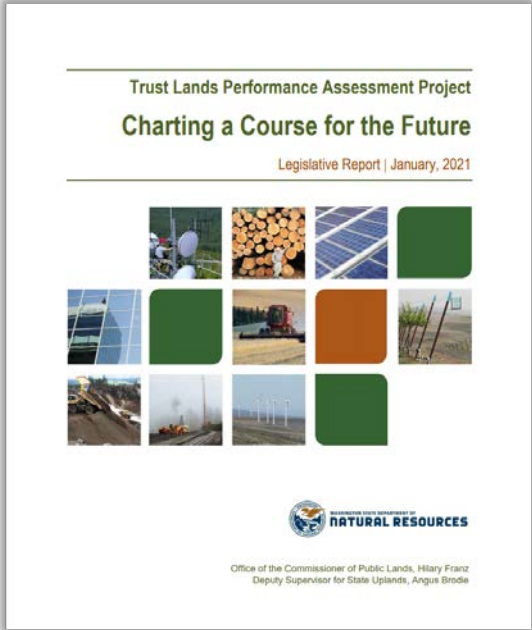
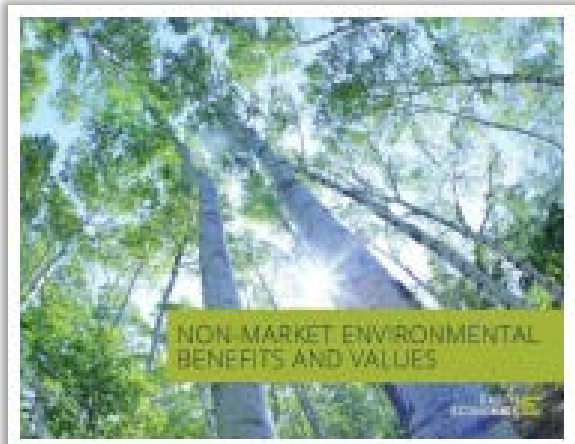
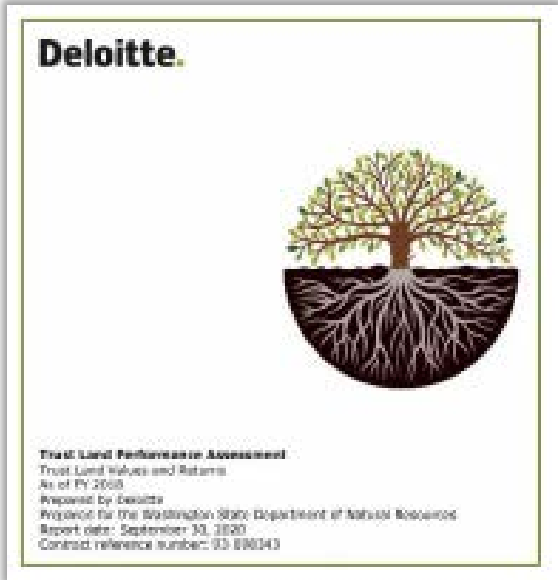
Other Resources: Wind Energy, Special Uses, Special Forest Products, Rights-of-Way

Acres may overlap into more than one asset class

Trust Land Performance Assessments

3

Reports



www.dnr.wa.gov/tlpa

Trust Land Portfolio Valuation Summary

Valuation performed by Deloitte Transactions and Business Analytics



- Beneficiaries are the audience

- Deloitte answers two key questions:



- How much is the land worth?

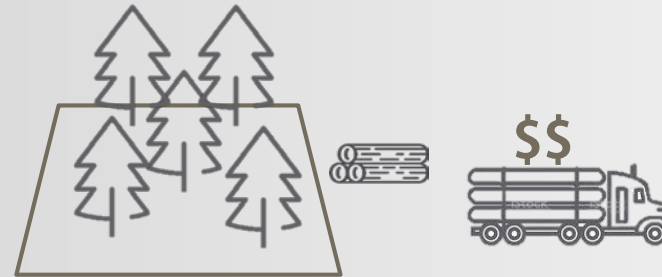
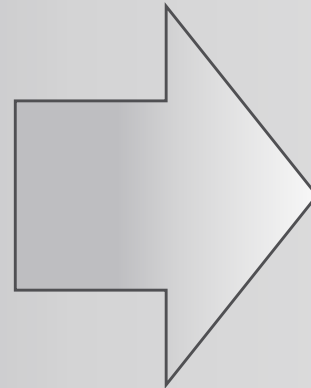


- What is the value of the revenue generated off the land?

Deloitte Concept: Fair Market Value vs. Trust Value

Fair Market Value

- Proviso - land valuation
- Value-in-exchange method
- **Reflects highest and best use of property**



Trust Value

- Deloitte - land valuation
- Value-in-use method
- **Reflects existing use of property** (*may or may not be highest and best use*)

Deloitte Concept: Trust Value

How are trust lands different from private lands?



The sale of trust lands is subject to limitations:

- Statutory
- Constitutional
- Enabling Act

Productivity and utilization of the lands subject to:

- Statutes
- Regulations
- Policies
- Management practices

Size of the asset portfolio

Deloitte Concept: Trust Value

~2.9
million
acres

Trust Land Portfolio Valuation based on:

- Under the **ownership and control of the State of Washington**, acting as a **trustee on behalf of defined beneficiaries**
- **Use and control limitations**, such as:
 - Significant **limitations upon sale of the trust lands**, and
 - Statutes, regulations, policies and management practices which are different than otherwise similar, privately-owned lands

Deloitte Concept:
Rate of Return vs. Cash Flow

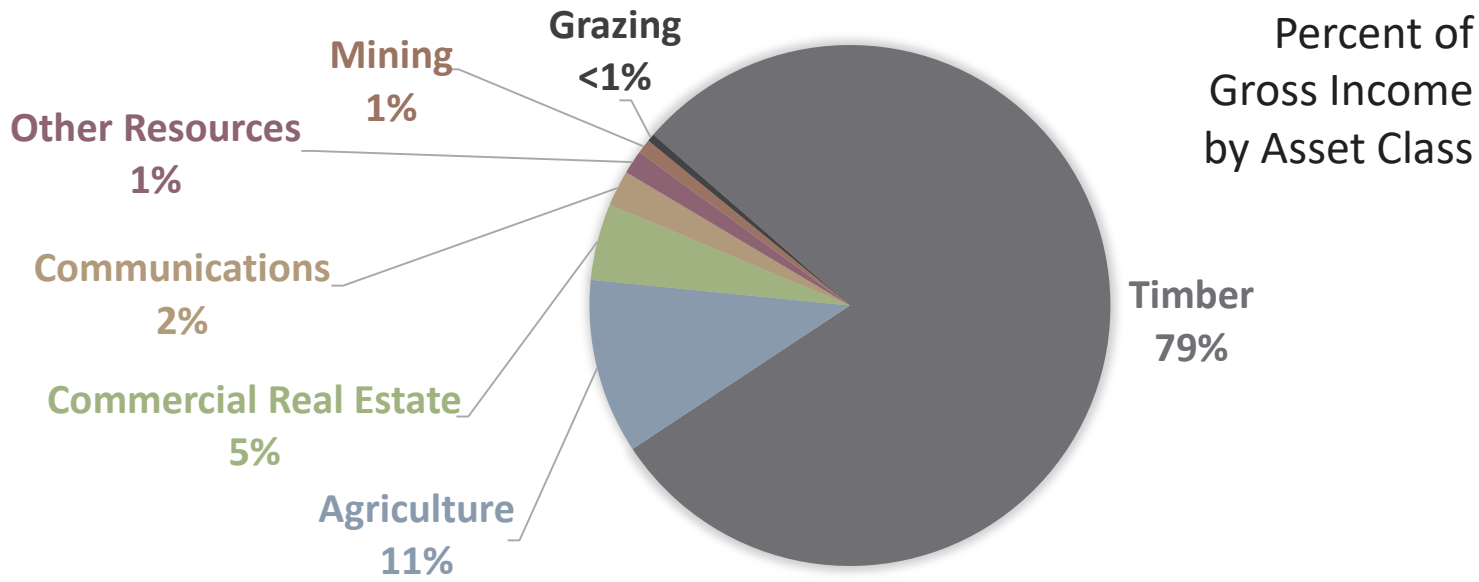


Rate of return has *very little utility* for the trust lands portfolio because:

1. Revenue distribution requirements
2. Restrictions on the sale of lands
3. It is difficult to change the trust manager

Deloitte Recommendation:

Focus on *Cash Flow to the beneficiaries* as the preferred metric of performance rather than rate of return.



Trust Land Portfolio Valuation Findings

*See Deloitte's report, Appendix D for State Forestland Trust Values

Summary of 2018 Asset Class Income and Trust Value*

Asset Class	Gross Income	Net Operating Income	Trust Value	Net Operating Income/Trust Value
Timber	\$171.7 million	\$123.6 million	\$2,136 million	5.79%
Agricultural Resources	\$23.5 million	\$16.7 million	\$238.3 million	7.00%
Commercial Real Estate	\$10.3 million	\$7.2 million	\$95.7 million	7.53%
Communication Resources	\$ 4.8 million	\$3.4 million	\$41.2 million	8.16%
Other Resources	\$3.2 million	\$2.2 million	\$20.3 million	11.03%
Mining Resources	\$1.9 million	\$1.3 million	\$16.6 million	7.99%
Grazing Resources	\$1 million	\$0.7 million	\$10.5 million	7.00%
Total	\$216.4 million	\$155.1 million	\$2,558.6 million	6.07%

Non-Market Benefits Valuation Findings

Deloitte Transactions and Business Analytics
hired Earth Economics
to fulfill a portion of the 2018 proviso direction.

“Estimates the value of ecosystem services and recreational benefits for asset classes that produce these benefits.”



Non-Market Benefits Valuation Findings

Annual Ecosystem Services Value and Social Cost of Carbon

Averaged by Land Cover and Asset Class (2018)

Asset Class	Asset Acres	Annual Ecosystem Services Value	Social Cost of Carbon (<i>One-Time Cost</i>)
Forested	2,170,070	\$1,231.64 million	\$16.56 billion
Cultivated	301,807	\$84.55 million	\$0.74 billion
Grazing	366,240	\$46.20 million	\$1.00 billion
Other	124,969	\$37.68 million	\$0.44 billion
Total	2,963,086	\$1,400.07 million	\$18.74 billion

Economic Value of Outdoor Recreation on State Trust Lands (2018)

Activities	Annual Value
All Recreational Activities	\$990 million

DNR Analysis

ESSB 6095
SL, p. 152

Options to:

- Improve rates of return
- Increase revenue reliability & possible enhancement
- Present and explain factors that either:

Define



Constrict



Define &
Constrict



**Factors considered
include:**
Statutory
Constitutional
Operational
Social

the department's management practices and revenue production

DNR Analysis

Challenge:
Decrease in Revenue

Differences in Net Revenue Between 1995 and 2018

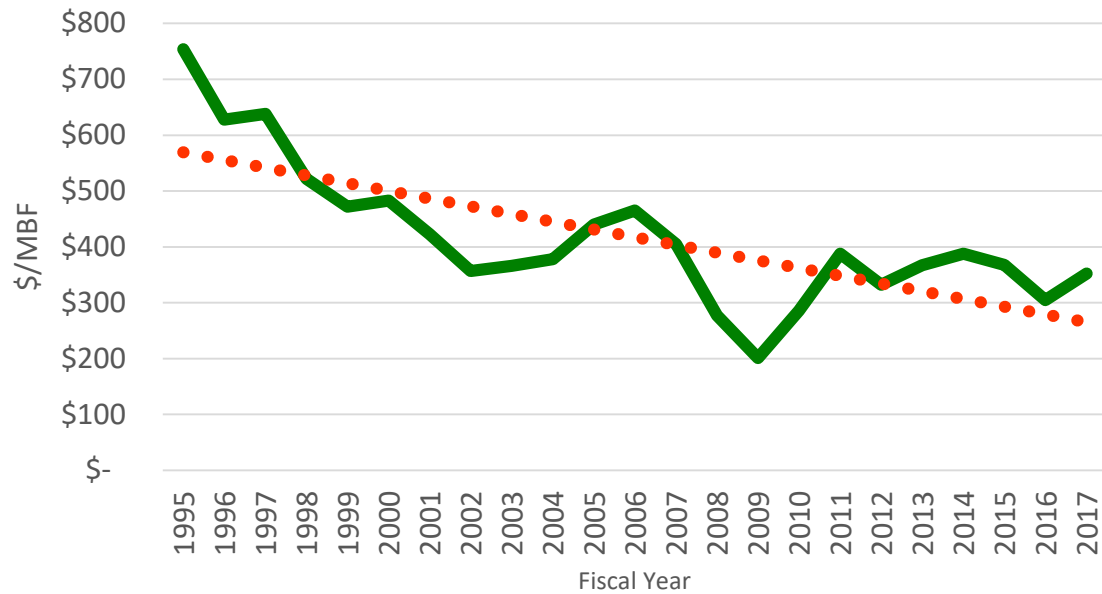
Asset Class	FY 1995 Net Revenue	FY 1995 Net Revenue in 2018 dollars	FY 2018 Net Revenue	Percent Change
Timber	\$139.83 million	\$224.34 million	\$123.62 million	-45%
Agriculture	\$3.9 million	\$6.3 million	\$16.68 million	166%
Commercial Real Estate	\$2.3 million	\$3.6 million	\$7.2 million	99%
Grazing	\$386 thousand	\$619 thousand	\$735 thousand	19%
Communication Resources	\$1.1 million	\$1.8 million	\$3.4 million	90%
Mining	\$1.1 million	\$1.7 million	\$1.3 million	-23%
Other Resources	n/a	n/a	\$2.2 million	n/a
TOTALS	\$148.56 million	\$238.36 million	\$155.18 million	-35%

All numbers are rounded

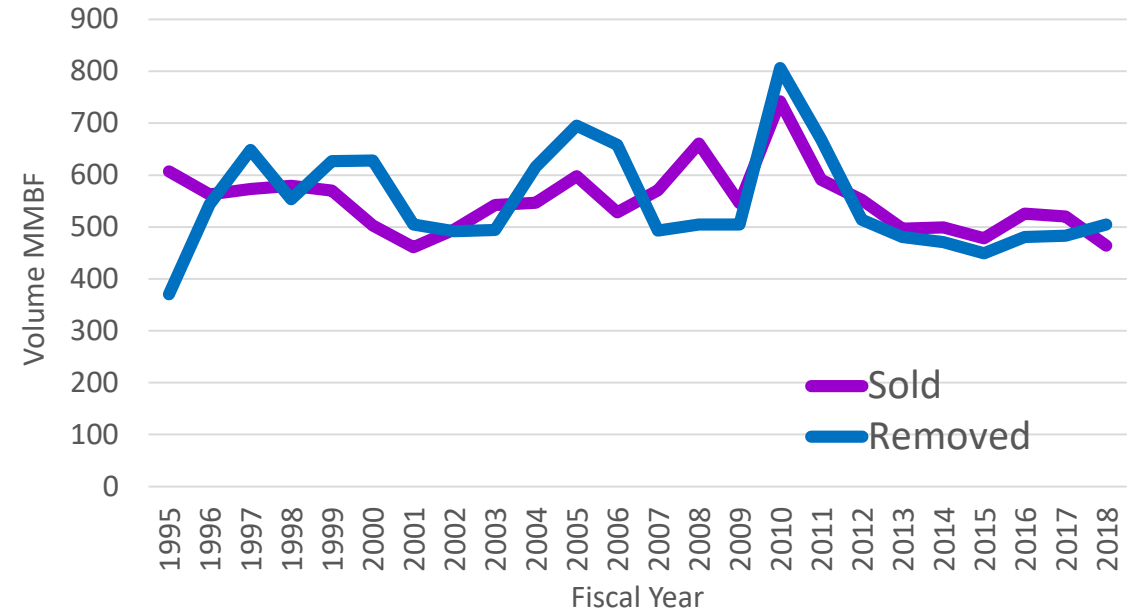
Draft - Subject to Change April 2021

DNR Analysis - Timber Revenue

Stumpage prices for state trust lands



Sold and removed volume from state trust lands

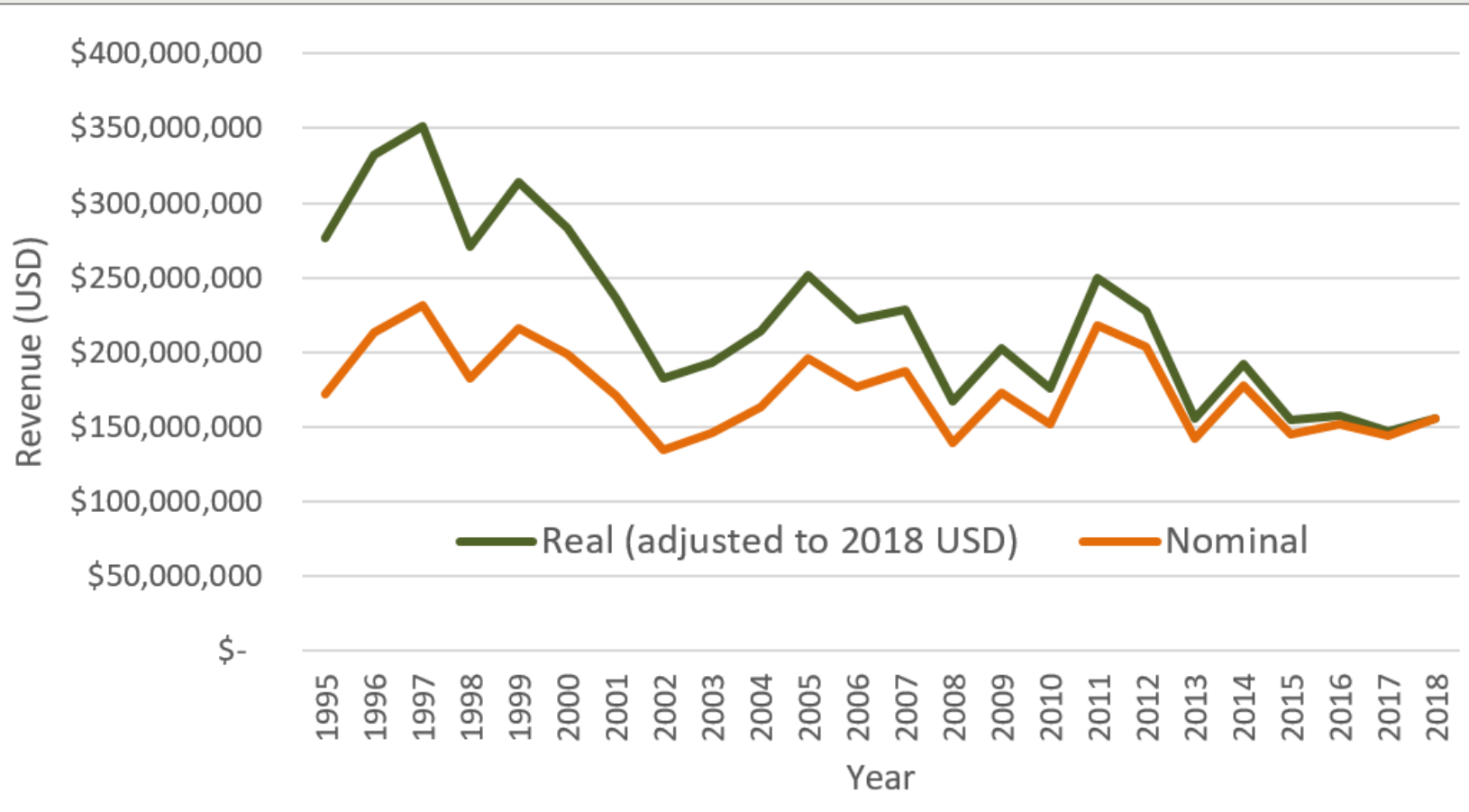


WHY?

1. Decline in stumpage price
2. Decline in operating base

DNR Analysis

Total Net Revenue Generated from State Trust Lands FY 1995-2018



Challenge:
Revenue
reliability

Part 3 - Initial Ideas for Moving Forward



- Project Scope



- Opportunities



- Initial Ideas



Scope

Need

DNR needs to increase the amount and reliability of the revenue it generates through the assets it manages on state trust lands into perpetuity.

Purpose

DNR will transform state trust land management:

- 1) Legislative proposals to increase amount and reliability of revenue
- 2) Changes to Board of Natural Resources policies to improve trust asset performance
- 3) Updated operational business practices to increase efficiency and effectiveness

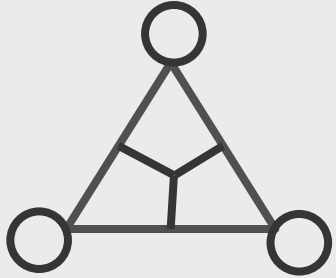
Scope



Objectives

1. Increase amount and reliability of revenue
2. **Sustain the natural resource lands**, while seeking opportunities to diversify
3. Maintain or enhance the social, environmental, and cultural benefits of state trust lands consistent with revenue generating purposes of the land
4. Feasible solutions

Opportunities



Improve Business Model and Systems



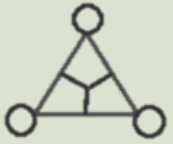
Increase Access to Capital



Greater Ability to Transact Lands



New or Revitalized Management Tools

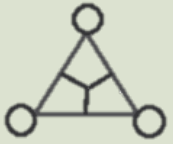


Improve Business Model and Systems

Initial Ideas

Idea	Summary	For more information
1	Improve financial systems to incorporate for-profit-enterprise practices	•Deloitte General Items: 1-4
2	Reliability Fund	•Deloitte General Item: 10 •DNR Leg Report, page 37
3	Smooth revenue distribution through loans Legislature could develop a program to borrow money to distribute to beneficiaries evenly over a period of time to reduce cash flow volatility	•Deloitte General Item: 14 •DNR Leg Report, page 38





Improve Business Model and Systems

Initial Ideas

Idea	Summary	For more information
4	Fund studies to compare DNR's approach to the Endangered Species Act compliance with others	•Deloitte Asset Class: Timber - T5
5	Compare services DNR provides to those of an external manager	•Deloitte Asset Class: Timber - T6
6	Pursue ways to monetize Ecosystem Services for Timber Asset Class	•DNR Leg Report, page 39





Increase Access to Capital

Initial Ideas

Idea	Summary	For more information
7	Borrowing authority	•DNR Leg Report, page 37
8	Capital expenditure funding options examples Increase investments in working forests to increase timber value and volume	•Deloitte General Item 8
9	Change trust land management and investments funding Legislature could reimburse DNR with actual management costs and liabilities instead of percentage set across all asset classes for each trust group	•Deloitte General Item 5 •DNR Leg Report, page 37





Greater Ability to Transact Lands

Initial Ideas

Idea	Summary	For more information
10	Statutory, Constitutional, or Enabling Act Improvements	<ul style="list-style-type: none">•Deloitte General Item 11•DNR Leg Report, page 38





New or Revitalized Management Tools

Initial Ideas

Idea	Summary	For more information
11	Funding sources for non-trust expenses	<ul style="list-style-type: none"> •Deloitte General Item 12 •DNR Leg Report, page 38
12	Trust Land Transfer	<ul style="list-style-type: none"> •DNR Leg Report, page 38
13	Trust Land Replacement Program	<ul style="list-style-type: none"> •DNR Leg Report, page 38



Summary of Initial Ideas Presented

Initial Ideas

Idea	Summary	Who?	Where?
1	Improve financial systems to incorporate for-profit-enterprise practices	Deloitte	GI 1-4
2	Reliability Fund	Deloitte	GI 10
3	Smooth Revenue Distribution through Loans	Deloitte	GI 14
4	Fund studies to compare DNR's approach to the Endangered Species Act compliance with others	Deloitte	T5
5	Compare services DNR provides to those of an external manager	Deloitte	T6
6	Pursue ways to monetize Ecosystem Services	DNR	p. 39
7	Borrowing authority	DNR	p. 37
8	Capital expenditure funding options examples	Deloitte	GI 8
9	Change trust land management and investments funding	Deloitte	GI 5
10	Statutory, Constitutional, or Enabling Act improvements	Deloitte	GI 11
11	Funding sources for non-trust expenses	Deloitte	GI 12
12	Trust Land Transfer	DNR	p. 38
13	Trust Land Replacement Program	DNR	p. 38

DNR Would Like Your Feedback

- Ideas proposed in all assessment reports
- New ideas
- Opportunities you see
- Concerns
- Gaps
- Recommendations on subject matter experts for advisory committee, with expertise in:
 - revenue generation
 - asset management
 - revenue distribution



What is DNR already doing?

- Improving the timber sale process

SB5201



- Extending the duration of commercial real estate leases

HB1430



- Replacing the contracts and revenue system (NatureE) for compatibility with One Washington

Operating budget proposal



- Creating silviculture jobs

Capital budget proposal



- Improving the tracking of financial information - chart of accounts

Next Steps





Public Webinar



April 28, 2021



Webinar Comments: April 28 – May 12, 2021

www.dnr.wa.gov/tlpa

Find out more
by visiting
dnr.wa.gov/tlpa

Trust Lands Performance Assessment

Charting a Course for the Future (DNR)

Trust Land Values and Returns (Deloitte)

Non-Market Environmental Benefits and

Values (Earth Economics)

