Trust Land Performance: Charting a Course for the Future

Public Webinar
April 28, 2021

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Lisa Anderson
Angus Brodie
Agenda

• Part 1 – State Trust Land Background Information

• Part 2 - Valuation Findings
  • Group Questions on Parts 1 and 2

• Part 3 – Initial Ideas for Moving Forward and Next Steps
  • Group Questions
Trust Manager

~2.9 million acres

of

State Trust Lands

in Washington
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
Federally Granted Trust Lands (Created in Enabling Act and Constitution)

- Present in all counties
- Revenue is generated from a variety of asset classes
- 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

*Includes Common School, Indemnity and Escheat.
State Forestlands
Created in Washington Statute

- 21 Counties-mostly in western Washington
- Revenue generated is primarily from the timber asset class
- Revenue distribution is tied to geographic locations
- Over 617,000 acres* (from Deloitte Report)

Typical Recipients of Funding

- County Services
- School Districts
- County Roads
- Ports
- Library Districts
- Fire Districts
- Hospitals
- EMS
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.)
Part 2 - Valuation Findings

- Budget Proviso
- Assessments
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
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

- Timber: ~2.06 million acres
- Grazing: ~750,000 acres
- Other Resources: ~530,000 acres
- Agriculture: ~238,000 acres
- Mining: ~5,900 acres
- Commercial Real Estate: ~1,000 acres
- Communications: ~100 acres

Other Resources: Wind Energy, Special Uses, Special Forest Products, Rights-of-Way
Trust Land Performance Assessments

Reports

www.dnr.wa.gov/tlpa
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)*
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:**

**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.
## Summary of 2018 Asset Class Income and Trust Value*

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

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

Draft - Subject to Change. April 2021
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)

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

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

<table>
<thead>
<tr>
<th>Activities</th>
<th>Annual Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Recreational Activities</td>
<td>$990 million</td>
</tr>
</tbody>
</table>
DNR Analysis

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

### Differences in Net Revenue Between 1995 and 2018

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Timber</td>
<td>$139.83 million</td>
<td>$224.34 million</td>
<td>$123.62 million</td>
<td>-45%</td>
</tr>
<tr>
<td>Agriculture</td>
<td>$3.9 million</td>
<td>$6.3 million</td>
<td>$16.68 million</td>
<td>166%</td>
</tr>
<tr>
<td>Commercial Real Estate</td>
<td>$2.3 million</td>
<td>$3.6 million</td>
<td>$7.2 million</td>
<td>99%</td>
</tr>
<tr>
<td>Grazing</td>
<td>$386 thousand</td>
<td>$619 thousand</td>
<td>$735 thousand</td>
<td>19%</td>
</tr>
<tr>
<td>Communication Resources</td>
<td>$1.1 million</td>
<td>$1.8 million</td>
<td>$3.4 million</td>
<td>90%</td>
</tr>
<tr>
<td>Mining</td>
<td>$1.1 million</td>
<td>$1.7 million</td>
<td>$1.3 million</td>
<td>-23%</td>
</tr>
<tr>
<td>Other Resources</td>
<td>n/a</td>
<td>n/a</td>
<td>$2.2 million</td>
<td>n/a</td>
</tr>
<tr>
<td>TOTALS</td>
<td>$148.56 million</td>
<td>$238.36 million</td>
<td>$155.18 million</td>
<td>-35%</td>
</tr>
</tbody>
</table>

Challenge: Decrease in Revenue

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

Revenue (USD)

$400,000,000
$350,000,000
$300,000,000
$250,000,000
$200,000,000
$150,000,000
$100,000,000
$50,000,000


Year

Reality: Revenue reliability

Challenge:
Group Questions
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

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

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

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<tr>
<td>4</td>
<td>Fund studies to compare DNR’s approach to the Endangered Species Act compliance with others</td>
<td>• Deloitte Asset Class: Timber - T5</td>
</tr>
<tr>
<td>5</td>
<td>Compare services DNR provides to those of an external manager</td>
<td>• Deloitte Asset Class: Timber - T6</td>
</tr>
<tr>
<td>6</td>
<td>Pursue ways to monetize Ecosystem Services for Timber Asset Class</td>
<td>• DNR Leg Report, page 39</td>
</tr>
</tbody>
</table>
## Increase Access to Capital

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<thead>
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<tr>
<td>7</td>
<td><strong>Borrowing authority</strong></td>
<td>• DNR Leg Report, page 37</td>
</tr>
<tr>
<td>8</td>
<td><strong>Capital expenditure funding options examples</strong></td>
<td>• Deloitte General Item 8</td>
</tr>
<tr>
<td></td>
<td>Increase investments in working forests to increase timber value and volume</td>
<td></td>
</tr>
<tr>
<td>9</td>
<td><strong>Change trust land management and investments funding</strong></td>
<td>• Deloitte General Item 5</td>
</tr>
<tr>
<td></td>
<td>Legislature could reimburse DNR with actual management costs and liabilities instead of percentage set across all asset classes for each trust group</td>
<td>• DNR Leg Report, page 37</td>
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### Greater Ability to Transact Lands

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</thead>
</table>
| 10   | Statutory, Constitutional, or Enabling Act Improvements | • Deloitte General Item 11  
• DNR Leg Report, page 38 |
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<tbody>
<tr>
<td>11</td>
<td>Funding sources for non-trust expenses</td>
<td>• Deloitte General Item 12</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• DNR Leg Report, page 38</td>
</tr>
<tr>
<td>12</td>
<td>Trust Land Transfer</td>
<td>• DNR Leg Report, page 38</td>
</tr>
<tr>
<td>13</td>
<td>Trust Land Replacement Program</td>
<td>• DNR Leg Report, page 38</td>
</tr>
<tr>
<td>Idea</td>
<td>Summary</td>
<td>Who?</td>
</tr>
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<td>DNR</td>
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Next Steps - 2021 Work Plan

Quarter 1: January - March
- Share Key Findings
- Collect input on:
  - Project scope
  - Ideas for change
- Host public webinar

Quarter 2: April - June
- Continue to collect input on:
  - Project scope
  - Ideas for change

Quarter 3: July - September
- Seek BNR support for project scope
- Develop potential proposals (e.g.):
  - Form Advisory Committee(s) and/or Work Group(s)

Quarter 4: October - December
- Continue to develop proposals
- Collect input on proposals

Quarter 1:
Quarter 2:
Quarter 3:
Quarter 4:

Quarter 1:
Quarter 2:
Quarter 3:
Quarter 4:

Quarter 1:
Quarter 2:
Quarter 3:
Quarter 4:

Draft - subject to change
April 2021
More Information?

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

www.dnr.wa.gov/tlpa
www.dnr.wa.gov/beneficiaries
Webinar Comments

If you’d like to submit comments online,
please go to:

www.dnr.wa.gov/tlpa

April 28 – May 12, 2021
Group Questions