



# Oregon

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### State Land Board

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## M E M O R A N D U M

June 9, 2015

**To:** Governor Kate Brown  
Secretary of State Jeanne Atkins  
State Treasurer Ted Wheeler

**From:** Mary Abrams, Director

**Subject:** Common School Forest Land Management  
Elliott State Forest Alternatives Status Report

### Elliott State Forest Alternatives Background

Planning for revision of the Elliott State Forest Management Plan (FMP) and an Elliott State Forest Habitat Conservation Plan (HCP) began in early 2000. After a long and unsuccessful process to develop a multi-agency HCP, the State Land Board approved an alternate FMP in 2012 that did not depend on an HCP to meet the Endangered Species Act (ESA) requirements and instead used endangered species surveys and protections for these individual resources (known as "Take Avoidance"). The primary driver for the alternate FMP was an attempt to provide ESA compliance without the cost and uncertainty of continued HCP development while allowing an annual timber harvest up to 40 million board-feet (mmbf). The FMP was designed by the Oregon Department of Forestry (ODF) with the intent of having them continue to manage the Elliott at an estimated annual return on asset value between 2.2% and 4.5%.

Litigation in 2013 resulted in the ODF revising the survey and protection measures for the marbled murrelet policies that support the FMP. This change in policies has caused a steep decline in timber harvest and associated revenues from the Elliott. This decline has resulted in a loss to the Common School Fund of over \$4 million since 2013.

The State Land Board (Board) is directed by Oregon's Constitution to manage the Common School trust lands (including approximately 84,000 acres in the Elliott) received from the federal government—also known as "Admission Act" lands—for K-12 public education. The mandate for these lands places a trust obligation on the Board to

maximize revenue to benefit multiple generations of K-12 students, and requires obtaining fair market value for any disposition of the Admission Act lands. Given that Common School trust lands are currently operating at a net loss to the Common School Fund, and future projections show the potential for this loss to increase in the future, it raises the question as to whether or not continuing to hold these lands as part of the Common School Fund land asset portfolio is consistent with the legal mandates the Board is required to meet.

In 2014, the Department undertook an extensive evaluation and public process around future options for the Elliott with the goal of informing the Board and seeking their direction on how to manage this asset of the Common School Fund. In December of 2014, the Department compiled the information into two reports for the Board's deliberation. Two consistent themes were heard from a wide range of stakeholders: 1) the model of relying on forest land management to generate school funding is outdated, and it is time to decouple or separate decision-making about how best to manage public lands from decisions about how best to generate revenue for schools; and 2) there are many public values associated with the Elliott State Forest, and most believe those values need to be protected regardless of what the Land Board decides about the future ownership and/or management of the Elliott.

On December 9, 2014, the Board directed the Department to pursue further due diligence on three possible scenarios for the Elliott: 1) reducing costs and increasing revenues by contracting with a different manager (other than the Oregon Department of Forestry), while also reducing risks to future revenues; 2) improving the predictability of future revenues by negotiating a Habitat Conservation Plan (HCP) that would allow for sufficient net revenue to make the Elliott an appropriate asset for the Common School Fund; and 3) changing Common School Fund ownership by divesting of some or all of the Elliott while retaining either public ownership or public protection of a broad range of public values currently provided by the forest. The Board also requested the Department investigate several legal questions around the state's trust obligations and alternatives for managing legal risk, particularly with the first scenario.

### **Current Information**

A summary of the current information on the three future options for the Elliott, as well as a summary of the state's trust obligations are presented below.

#### *Trust Obligations*

Article VIII of the Oregon Constitution designates the Board as trustee of the Common School fund trust lands for the exclusive benefit of public education. The beneficiaries of the trust include both current and future public schools in Oregon. Sound techniques of land management are important for maintaining the value of the land as an asset, even if it is unproductive today. The Board must balance the need for short-term revenue against the long-term value and potential future productivity of the land for

beneficiaries in the future, together with a thorough evaluation of alternative investments. Given the significant decrease in short-term revenues (and current net operating losses), the Board is appropriately considering whether the Elliott State Forest should remain as an asset of the Common School Fund.

*Current Status of Three Scenarios for the Future of the Elliott*

1. *Change of Manager* – Changing management to a private contractor has been presented as a way, potentially, to increase short term and long term returns, through decreased management costs, increased harvest levels, and shared legal risk. The Department completed preliminary information gathering on business interest, including legal risk tolerance of interested parties, and has summarized it below:
  - a. There is market interest in providing forest management services on the Elliott, but for managing the forest on a time and materials basis;
  - b. Private managers are interested in developing a Habitat Conservation Plan to reduce legal risk, but developing an HCP likely would increase the costs of this option;
  - c. It is unlikely that a private manager would agree to assume any significant legal liability for known risks around managing the property unless there was co-ownership;
  - d. A joint venture approach with co-ownership would limit participation to those forest managers with available capital and an ownership-type of business model;
  - e. Engaging a new manager would not result in any significant change in risk to the value of the forest for the Common School Fund; and
  - f. Because of the start-up costs and likelihood of early litigation, it is expected that net costs to the Common School Fund over the next five years would increase, not decrease, with this approach.
2. *Negotiating an HCP for the Management of the Elliott* – A Habitat Conservation Plan (HCP) could provide increased predictability concerning future revenues from the Common School Fund, while also leading to improvements in conservation values. An HCP approved by the federal regulatory agencies (National Oceanic and Atmospheric Administration (NOAA) Fisheries and the United States Fish and Wildlife Service (USFWS)), would include an Incidental Take Permit (ITP) under Section 10 of the federal Endangered Species Act (ESA). The primary issues with an HCP are what levels of net revenue would result, given required conservation measures and mitigation, and what levels of predictability are possible. In December, the Land Board supported continued exploration of the feasibility of a Habitat Conservation Plan for the Elliott, but expressed concern about the ongoing investment of Department resources. The Department continued discussions with the federal agencies, and has made the following preliminary assessment:

- a. Developing an HCP for the Elliott would be a highly complicated undertaking due to the nature of the species involved, the overlapping responsibilities of regulatory agencies, and the high likelihood of legal challenges.
  - b. The State has been pursuing HCPs on the Elliott since the northern spotted owl and marbled murrelet first were listed in the early 1990s.
  - c. One concept explored was to reduce the duration of an HCP to 10 years, and to develop conservation measures based on site-specific application of desired habitat outcomes. This approach, if successfully implemented, might allow harvest at an average level of between 23-27 mmbf/year for the ten-year period.
  - d. The estimated net revenue to the Common School Fund for a 23-27 MMBF level HCP, if achievable, would be \$2.0 – 6.1 million/year (0.6 – 1.7% return on asset value).<sup>1</sup>
  - e. This level of harvest assumes the GIS modeling used to predict harvest volumes is within a range of accuracy.
  - f. This level of harvest does not account for potential disruptions due to legal challenges to the HCP and subsequent management of the forest. Nor does it account for potential changes in the ESA status of species present in the forest.
  - g. There are continued legal risks even with an HCP that is developed, paid for, approved, and implemented – the federal agencies routinely are engaged in litigation to defend HCPs, including, for example, the 2008 suit challenging the previous Elliott HCP.
  - h. While there is some economic potential for operating under an HCP, consideration would have to include weighing the relative risk vs. reward potential for the greatest benefit for the schools.
3. *Change in Ownership* – At the December 9, 2014 meeting, the State Land Board expressed a strong interest in pursuing a transfer of ownership of some or all of the Elliott. The Board directed the Department to continue with further due diligence on this option, particularly around effective ways to separate timber harvest from education funding while retaining public ownership benefits. The Board also requested staff to involve a wide range of interests, including tribal entities, in the process. Staff moved forward on this option on three fronts: 1) assisting Oregon legislators at their request, in development of a possible trust land transfer tool; 2) issuing a Request for Information to gauge market interest and to inform, if needed, a subsequent transfer approach; and 3) developing a conceptual ownership transfer strategy in case the trust land transfer tool proved untenable or insufficient.

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<sup>1</sup> Based on a range of recent stumpage prices (\$325-425/MBF) and projected costs including implementation of an HCP at 25 MMBF (\$200 – 240/MBF).

- a. While receiving considerable legislative interest, it appears unlikely that the 2015 legislature will enact trust land transfer legislation.
- b. The response to the Request for Information was limited but provided the following information:
  - i. There is some market interest in acquiring the Elliott, including purchasers willing to maintain some form of public ownership or interest in the lands;
  - ii. Interest is in a significant portion of the property, but concerns were expressed about having to take on the entire 84,000 acres;
  - iii. A public auction would deter participation by some potential transfer partners;
  - iv. Potential transfer partners are interested in working together to come up with shared solutions; and
  - v. Tribal interest in a transfer exists.
- c. The Department believes there are ways to craft an ownership transfer of the Elliott that both meets the Board's trust obligation and protects public values of interest in the forest. The trust obligation could be addressed through an objective third-party determination of value, requiring that the Common School Fund be compensated for the full fair market value of the lands. With this condition established, the Board could then specify additional outcomes and public values that would have to be achieved by recipients for a transfer to occur (these outcomes and values would likely require finding public or private subsidy of some sort). The additional outcomes and values could include categories such as:
  - i. Supporting Local Economies / Mill Infrastructure;
  - ii. Preserving Public Recreational Access and Use;
  - iii. Protecting Key Watersheds for Coho Spawning;
  - iv. Prohibiting Mining;
  - v. Protecting Old Growth / Older Forest Stands; and
  - vi. Prohibiting Log Exports from the Elliott.

Since many of the concerns about public values vary across the range of stakeholders, combinations of interests may be the optimal way to achieve all of these desired outcomes.

4. *Public Auction* – the Board instructed the Department to put aside the possibility of a public auction of the Elliott, with the hope that another solution could be found that would meet their trust obligations as well as protect public values of interest in the forest. This option remains a last resort if none of the three alternate options listed

above prove successful in addressing the challenges of meeting the Board's trust obligation to the beneficiaries.

### **Next Steps**

The Department will take the information in this update, additional input from the Land Board, and complete the due diligence on these alternatives. While most of the work has been completed on alternatives (1) and (2), the details of an ownership transfer process for alternative (3) still need further work. The Department also will connect with stakeholders and interested parties before bringing final recommendations to the Board. The Department intends to return to the Board in August to seek direction on the preferred path forward for the Elliott.