

*Annual Staff Report
on the
Management of State School Lands
Fiscal Year 2012-13*



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Submitted to

Edmund G. Brown Jr., Governor

*The California State Legislature
and
The State Teachers' Retirement System*

Note to the Reader

School Lands were granted to the State of California by the federal government under the Act of March 3, 1853 (10 Stat. 244) for the purpose of supporting public education in California, and consisted of the 16th and 36th sections of land in each township (with the exceptions of lands reserved for public use, lands taken by private land claims, and lands known to be mineral in character). A supplementary act in 1927 extended the grant of mineral lands to the State. No federal patents to the State were required under this grant. Title to the lands vested in the State upon approval of the U.S. Township Survey Plats (subject to the exceptions described above).

Indemnity School Lands (a.k.a. Lieu Lands) - In cases of preemption due to the exceptions described above (i.e., instead of a Section 16 or a Section 36), the State was given the opportunity to select replacement lands from the United States. For each transaction, the process involved several steps. First, the State filed a list with the federal government describing the lands lost to the State due to the exceptions described above. These lands were known as base lands. Then, the State filed a list with the federal government describing other federal lands selected in place of these base lands. When the list of selected replacement lands was approved by United States, a Clear List was issued to the State. The State's rights to the base lands were relinquished back to the federal government, and title to the selected lands became vested in the State. The Clear List was the document of conveyance and there are no patents issued by the federal government.

For the purposes of this Annual Report, the term *school lands* is used to describe both lands obtained under the Act of 1853 and indemnity school lands. References to annual revenues are for Fiscal Year 2012-13.

The **Annual Staff Report on the Management of State School Lands** is prepared pursuant to Public Resources Code Section 6477, which requires that the State Lands Commission report annually to the State legislature and the governor on the management of school lands.

CALIFORNIA STATE LANDS COMMISSION

**ANNUAL STAFF REPORT ON THE MANAGEMENT
OF STATE SCHOOL LANDS**

Fiscal Year 2012-13

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INTRODUCTION

The California State Lands Commission (CSLC), through its State School Lands Management Program (Program), manages approximately 468,600 acres of school lands held in fee ownership by the State of California (State), and the reserved mineral interests on approximately 790,000 acres of school lands where the surface estate has been sold. These interests are what remain of the 5.5 million acres granted by Congress in 1853. Most of the lands were sold by the State in the 19th century. Management of the Program is split between two CSLC divisions, the Mineral Resources Management Division (MRMD) and the Land Management Division (LMD). The MRMD is responsible for the Geothermal, Solid Minerals, and Oil & Gas Programs, which involve the leasing of school lands for geothermal resources development, mining activities, and oil and gas development. The LMD is responsible for the Surface Management Program under which all surface resources on school lands, with the exception of mineral activities, are administered.

School lands were placed into a statutory trust in 1984 when the State Legislature approved the School Land Bank Act (Act), created the School Land Bank Fund (SLBF), and designated the CSLC as trustee of the SLBF. The Act added Sections 8700 through 8716 to the Public Resources Code (PRC), which set forth the management guidelines for the Program. The Act directs that school lands be proactively managed and enhanced to provide for an economic base in support of the public school system. PRC Section 8702 spells out specific findings and declarations made by the Legislature, emphasizing the development of school lands into a permanent and productive resource base and requiring that all transactions, including exchanges, sales, and acquisitions, be implemented for revenue generating purposes.

Pursuant to PRC Section 6217.7, all net revenues, monies, and remittances from the sale of school lands are deposited into the State Treasury to the credit of the SLBF. PRC Section 6217.5 directs all net revenues derived from the use of school lands (i.e., royalties, rents, and interest generated from promissory notes) be deposited into the State Treasury to the credit of the Teachers' Retirement Fund, which benefits the State Teachers' Retirement System (STRS).

The CSLC's emphasis in administering the Program has been: 1) the maximization of revenues from school lands assets, 2) protecting the corpus of the trust, and 3) protection of the environment and compliance with the California Environmental Quality Act (CEQA).

Net revenue transferred to STRS during Fiscal Year (FY) 2012-13 was \$9,569,623.80, which represents an increase of 66% over the prior year net revenue. Management expenses for the Program in FY 2012-13 totaled \$1,029,532.93, which represents a decrease of 14% over FY 2011-12 expenses. The fiscal year-end balance of the SLBF was \$1,725,620.18 (not including a

\$59,000,000 loan to the General Fund). For a summary, see the table entitled "Financial Summary: Fiscal Year 2012-13" (page 35).

GEOTHERMAL, SOLID MINERALS, AND OIL & GAS PROGRAMS

The MRMD is responsible for the Geothermal, Solid Minerals, and Oil & Gas Programs, which involves the leasing and management of school lands for geothermal, mining, and oil & gas development. These programs strive to maximize royalty revenue while protecting the environment and ensuring public safety. Historically, the activities of MRMD staff (staff) have generated at least 95% of annual revenues to STRS from its management of the SLBF. For a summary of these revenues, see the table entitled “Summary of Revenue Generated from Geothermal, Solid Minerals, and Oil & Gas Programs – Fiscal Year 2012-13” (page 22).

FISCAL YEAR 2012-13 ACTIVITIES

GEOTHERMAL PROGRAM

Managing geothermal leasing and development programs on school lands requires staff involvement in several specialized areas. Processing applications and negotiating leases requires input from legal and environmental staff. Drilling proposals require a technical review by engineering staff. Drilling and production operations need to be documented by field inspection staff for surface compliance with the terms and conditions of State leases, and approved drilling plans. Production reports, royalty calculations, and payments, must be verified by staff with expertise in geothermal operations and lease terms.

At present, all revenue from the geothermal program is generated from royalties paid on the production of steam from State leases located at The Geysers geothermal field in Sonoma, and Lake Counties. Electricity generated from the steam is sold to the utility, and is the basis for determining royalty revenue paid to the State.

Geothermal adjusted revenue totaled \$4,819,346.45 for FY 2012-13, a 9.1% increase from the prior year.

Geothermal Leases at the Geysers

The Geysers has operated commercially for 53 years, and is still the largest geothermal energy project in the world. The field now generates 835 megawatts of electricity from approximately 28,000,000 pounds of steam, enough to supply over 900,000 homes. Steam production has been relatively stable since 1995, due to the consolidation of field operations and increased injection of water



into the reservoir. The injection water is piped to the field from reclamation plants nearby in Lake County and Santa Rosa.

The State owns a 100% mineral interest in 7,247 acres currently under lease at The Geysers, in addition to a 1/16th mineral interest in another 895 acres. Most of the state parcels were acquired from the Bureau of Land Management (BLM) as lieu lands in the 1940s, and also through the indemnity selection process in the 1980s. Geysers Power Company LLC, a subsidiary of Calpine Corporation, holds State leases PRC 4596, 4596 "A", 4597, 5206, 6422, 7845, and 7179. It also owns and operates 17 of the 22 electrical-generating units at The Geysers. State leases PRC 8556, 8844 and 8950 are held by a different Calpine subsidiary called CPN Wild Horse Geothermal LLC.



Electrical-generating unit at The Geysers

The CSLC approved one new drilling project during the year – a new injection well (LF-22) in PRC 4597. The converted producer on PRC 8844 began production in December 2012, and uses a new CPN Wildhorse pipeline to transport the steam. Three other producers drilled two years ago, on PRC 8556, remain idle pending the construction of another pipeline. Sonoma County granted approvals for two new generating plants, however, CPN Wildhorse may instead opt to send the newly developed steam to existing power plants.

During FY 2012-13, the CSLC Executive Officer, as authorized by the CSLC, approved Calpine's request that the 159 acres of PRC 4596 "Parcel A" be utilized

for injection rather than production, and accepted the increased annual rent of two hundred fifty dollars (\$250) per acre (\$39,750 per year). This is a significant increase compared to the prior year's rent of ten dollars (\$10) per acre (\$1,590 per year). Rent will continue at two hundred fifty dollars (\$250) per acre as long as injection is occurring in "Parcel A", in order to offset the potential loss of royalty revenue resulting from non-production.

In May 2013, Calpine applied to amend the Lease PRC 8556, regarding Parcel 3, to hold the lease by injection rather than production. Staff reviewed the application and requested additional engineering and financial information. Calpine intends to indicate that the injection of recycled water, acquired from the City of Santa Rosa, into the reservoir under Parcel 3 contributes to the production of state wells within the outlying State Lease PRC 8844, Parcel 1. Regarding PRC 8556, Parcel 4, staff has identified that the lease will terminate unless it is held through production by September 1, 2014. Calpine stated its intention to fork and extend the Aidlin 10 well, so that it penetrates and bottoms into Parcel 4. Engineering staff is currently reviewing the data for this project to ensure that STRS resources will be protected.

Geothermal Leasing Proposed in Imperial County (W40958)

In September 2011, NGP Truckhaven, a subsidiary of Nevada Geothermal Power (NGP), submitted an application for a negotiated lease on approximately 4,321 acres of school lands, and another 543 acres of lands owned by the California



Department of Parks and Recreation (Parks), in the Truckhaven area west of the Salton Sea in Imperial County. Much of the land is located within the Parks' Ocotillo Wells State Vehicular Recreation Area (SVRA). Pursuant to PRC Section 6924, staff must coordinate its leasing efforts with Parks, such that the exploration and development does not unreasonably interfere with the use of the lands for recreation.

Staff has attempted to have these lands explored and/or developed for years. Prospecting permits were issued for most of the lands during the early 1980s, followed by a geothermal lease in the late 1980s, but no drilling or development ensued. In 2001, applications for new permits were submitted, but the applicants failed to follow through. The lands have been nominated two times for lease by

competitive bid, the last of which, was in 2007. Both nominations were from Ormat Nevada, Inc. (Ormat), but each time, Ormat withdrew its nomination when requested to provide funding for an environmental review. In 2011, Ormat sold its private and federal lease interests to Iceland America Energy, which subsequently sold the leases to NGP. Staff believes that leasing or permitting by direct negotiation with NGP, rather than a competitive lease sale, may be possible given NGP's consolidated land position.

The State parcels are interspersed with federal and private lands. The BLM issued federal leases in the area in 2009, and required NGP and two other federal lessees to form a unit, or cooperative plan of development. NGP did not agree with BLM's designated unit area and appealed to the Interior Board of Land Appeals. They believed that the unit area was too big, and was not based on the geography of the geologic resource. In late 2012, NGP lost their appeal, and informed staff that they had been unsuccessful in entering into an Operating Agreement with the two other federal lessees. Unless such an agreement can be reached, the BLM may be compelled to cancel the geothermal leases for all three lessees.

In May of 2013, NGP informed staff of a new name change to Alternative Energy Resources Inc. (AER). AER currently has a negotiated lease application pending with the State. AER is also considering applying for a geothermal prospecting permit on the state-owned lands, and hopes to develop the subsurface geothermal resources in the near future to support their planned 15-45 MW power facility. Staff is awaiting action by AER and the BLM.

Geothermal Prospecting Permits

Deep Rose Development, LLC (PRC 8949)

In June 2013, the CSLC issued a two-year extension of PRC 8949, to Deep Rose Development, LLC (Deep Rose), to prospect for geothermal resources on a 640-acre parcel of school lands in Inyo County, near Coso Junction. Deep Rose is working on completing the last mile of an 8 mile road that will be used to construct a well pad for the drilling rig. They expect to be drilling in the first quarter of 2014. Rent escalates to \$25/acre for the third and fourth year of a geothermal prospecting permit. The State parcel is surrounded by the Haiwee Geothermal Leasing Area, a collection of federal parcels that may soon be offered for lease by the BLM. If the area contains geothermal resources in commercial quantities, development will likely require a project that combines State and federal lands.

Entiv Organic Energy (PRC 8998)

In June 2012, the CSLC approved a two-year permit (PRC 8998) for Entiv Organic Energy, LLC (Entiv), allowing them to deepen a water well located on a 520-acre parcel in Siskiyou County. The parcel was originally a fee-owned school land, but the federal government acquired the surface through a condemnation action in the 1940s to enlarge the Lower Klamath National Wildlife Refuge. The mineral interests were reserved to the State. In 2001, the U.S. Fish and Wildlife Service (USFWS) drilled a series of shallow wells on the refuge to locate fresh water for habitat improvement. Two wells on the State parcel encountered hot water (157-192 degrees Fahrenheit). In 2011, the USFWS allowed Entiv access to the test wells. The ultimate goal is to locate water at a sufficient temperature to generate electrical power that would be used on the refuge to pump water. Excess power could then be sold.

In December 2012, Entiv deepened well 9-A to a depth of 1220', and experienced temperatures of approximately 181 degrees Fahrenheit. Entiv is currently in the process of evaluating the well to determine if it possesses geothermal resources in commercial quantities. If the well is deemed commercial, Entiv has the right to apply for a preferential lease. Staff is currently working on obtaining the daily operation reports, well records/history, logs, and flow tests, as required by the permit.

High Valley LLC (PRC 9001)

The CSLC approved a two-year permit for High Valley, LLC, a subsidiary of U.S. Renewables Group (USRG). The permit (PRC 9001, effective December 1, 2012) includes 1,383 acres of school lands immediately north of The Geysers. High Valley plans to re-enter one or more wells previously drilled during the 1980s, or drill new wells, to confirm the presence of geothermal resources and evaluate its commercial potential. USRG has submitted applications for two other prospecting permits on lands further north in anticipation of successful drilling on the permitted lands. These applications were deemed complete in

2008. Staff is investigating why the requisite CEQA work has not been completed to date, so that the Commission can consider permit issuance.

SOLID MINERALS PROGRAM

Revenue from the Solid Minerals program totaled \$3,575,009.45 for FY 2012-13. This represents over a 900% increase from the prior year's revenue of \$328,756.10. This is the largest royalty revenue that the Solid Minerals program has ever generated within one year for STRS. The production on the State lease at the Mesquite Gold Mine is the primary reason for the marked increase in royalty revenue, although production on the aggregate leases has shown steady but slow improvement as the economy recovers.

Solid Minerals program staff manage four leases totaling 1,054 acres, one active 1/16th reserved mineral interest parcel totaling 560 acres, and three mineral prospecting permits totaling 1,910 acres. The CSLC approved an extension and amendment for one of the active mineral prospecting permits and issued two new permits, one of which has already been extended and amended for an additional year. There are two leases totaling 465 acres that were quitclaimed several years ago where site reclamation is ongoing. In addition to managing these mineral properties, staff continued processing applications for new permits and leases, while responding to mineral inquiries, and addressing abandoned mine hazards (liability reduction).

Mineral Extraction Leases

U.S. Borax (PRC 736)

U.S. Borax, Inc. has mined borates on state lands at the Gerstley Mine for more than 80 years. U.S. Borax, Inc. quitclaimed its 160-acre lease in 2006, and is continuing to work with Inyo County and the Department of Conservation's Office of Mine Reclamation (OMR), to reclaim the site. Mine openings were sealed for public safety in 2005 through the installation of bat-compatible gates at the two main portals, and grates anchored at two air shafts. During an inspection conducted in 2007, all remaining hazardous materials were removed from the underground workings. U.S. Borax has continued to work on reclamation involving re-vegetation and minor earthwork. Staff is awaiting the findings of a spring 2013 inspection by OMR and Inyo County that MRMD staff was unable to physically participate in.



Hanson Aggregates (PRC 7301)

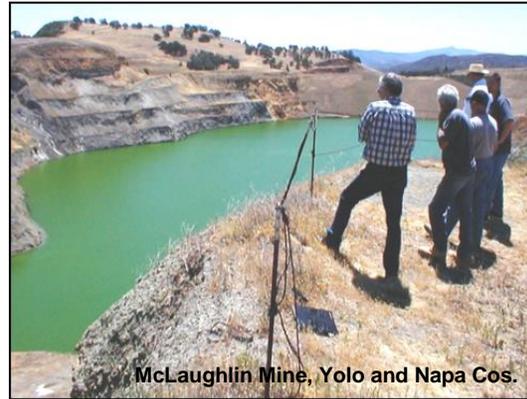
Hanson Aggregates (Hanson) holds a 102-acre lease near Lakeside in northern San Diego County called the Vigilante Aggregate Mine. Revenue from the lease totaled \$7,500.00, which is derived solely from the minimum annual royalty payment required by the lease, regardless of production. The mine



has not operated since 2009 due to the recession and downturn in housing and road construction/maintenance. On September 1, 2011, the CSLC renewed and amended the lease term through June 30, 2021. Hanson's new lease provides for a higher royalty rate of 6.5% of the gross sales.

Homestake Mining Company (PRC 7808)

Homestake Mining Company quitclaimed its 305-acre gold mineral extraction lease in 2002 after it was drilled and found to be non-economic. The lease is located at the McLaughlin Gold Mine in both Yolo and Napa counties. Staff conducted a field inspection in July 2012 in concert with Napa County, the SMARA lead agency, and concluded that the State parcel has been successfully reclaimed in accordance with the approved reclamation plan.



Western Mesquite Mines (PRC 8039)

In October 2002, Western Mesquite Mines, Inc. (WMMI) was issued a mineral extraction lease on 658 acres to expand their Mesquite Gold Mine complex northward, on the southern flank of the Chocolate Mountains of Imperial County. The lease was due to expire on September 30, 2012. The mine, idled in 2001 due to low gold prices, resumed operations in 2007 when gold prices escalated to over \$900 per ounce. Mining on the state parcel commenced in the fall of 2011 and the State received its first royalty production payment in January 2012.



On August 14, 2012, the CSLC approved the renewal and amendment of the State Mineral Extraction Lease through September 30, 2022. Through this amendment, the royalty increased the sliding scale to 6 to 9 percent of the gross depending on the price of gold.

Staff conducts periodic site inspections to verify the mining and production process and proper payment of royalty. The total revenue generated for this fiscal year is \$3,451,522.00. In the 2nd quarter of the fiscal year, the royalty percentage escalated to 7%, from 6%, due to the new sliding scale royalty rate and the high price of gold.

Mining on the State parcel is expected to be completed during the next fiscal year, but gold ore placed on the heap leach pad will continue to be recovered, and royalty paid. As monthly sales are made, the State is paid at a rate proportional to their ownership of the heap leach pad. After the State's ore is no longer added to the heap leach pad, the State ownership proportion will gradually decrease. However, the State should see revenues from the mine continue for many years.

Vulcan Lands, Inc. (PRC 8253)

Vulcan Lands, Inc. (Vulcan) holds a 160-acre lease at its Black Angel Quarry southwest of Barstow in San Bernardino County. Staff conducted a site inspection on January 2013 and observed a moderate amount of activity, and large stockpiles of sorted aggregate.



During this FY, Vulcan's production increased markedly and reflects increased economic activity in the economy of the high deserts of Victorville, Apple Valley and Barstow. Revenue generated this FY totaled \$81,602.70.

Granite Construction, Ludlow Pit (PRC 8272 - Expired)

The 80-acre lease held by Granite Construction Co. (Granite) near Ludlow, in San Bernardino County, expired in March 2011. The mine has been idle since 2004. Granite has advised staff that it plans to sell the quarry. Since the County's conditional use permit is still valid, staff monitored the site for any mineral production, but observed none.



Protech Minerals (PRC 8322 - Expired)

The 10-acre lease held by Protech Minerals, Inc., at the Pioneer Talc Mine in the Kingston Range of San Bernardino County, expired in April 2011. On March 7, 2013, staff inspected the site together with Steve Suitt of San Bernardino County, the CEQA lead agency, and OMR, to determine if reclamation was complete. While substantial reclamation has been achieved, the County identified additional grading necessary prior to the approval of final closure.



Hi-Grade Materials (PRC 8831)

Hi-Grade Materials Company (Hi-Grade) holds a 116-acre lease issued in July 2009, to extract sand and gravel at the Hesperia Quarry in the Lucerne Valley of San Bernardino County. Lease production began in July 2010 and revenue for FY 2012-13 increased nearly 50%, to \$36,106.00. Staff is awaiting consideration by San Bernardino County of the revision of their Conditional Use/Mining Permit and Reclamation Plan, which will permit the mining of all 116 acres of leased State school lands. This revision should allow mining to continue for several decades. Staff inspected the site on January 16, 2013 and found the lease and processing plant to be in good order.



Granite Construction, Palm Desert Pit (PRC 7945)

Granite extracts sand and gravel from a large open pit mine near Palm Desert in Riverside County. Included within the pit is a 560-acre parcel in which the State retains a 1/16th reserved mineral interest. The State's royalty rate is fixed at \$0.04 per ton of material mined and sold. Unfortunately, revenue from the parcel has decreased over 50%, equaling \$5,778.75 for the year, which according to Granite, was due to a weak economy.

Mineral Prospecting Permits

Bagdad Chase, Inc. (PRC 8917)

Bagdad Chase, Inc. (Bagdad) holds a prospecting permit covering a 640-acre parcel of fee-owned school land south of Ludlow in San Bernardino County, near the historic Bagdad Chase Gold Mine. The one-year permit was issued effective May 1, 2011. Under the permit, Bagdad conducts geologic mapping and rock chip sampling in the hopes of identifying a commercial aggregate deposit. On May 7, 2012, Bagdad



submitted an application for a permit extension and amendment to drill two holes on State lands to explore for precious metals. Staff conducted a site inspection on May 20, 2012, to witness drilling on Bagdad's private lands and discuss the details of the permit. On August 14, 2012, the CSLC approved Bagdad's Mineral Prospecting Permit Extension and Amendment to prospect for solid minerals and to drill two new exploration holes on state fee-owned school lands. The effective date of the permit is retroactive as of May 1, 2012, and will expire on April 30, 2014.

Robert G. Wetzel (PRC 9026.2)

On May 31, 2012, staff received an application from Robert G. Wetzel (Wetzel) to prospect for solid minerals on approximately 633 acres of State fee-owned lands. The parcel is described as Section 16, T15N,R10E, SBM, San Bernardino County, about 10 miles northeast of Baker. Wetzel proposes to conduct geologic mapping and hand sampling to help determine if the state parcel contains a commercial gold and/or silver deposit. On October 19, 2012, the Commission approved Wetzel's Mineral Prospecting Permit that was effective for one year starting on November 1, 2012.



Following favorable hand sampling results, on January 27, 2013, Wetzel submitted an application for an extension and amendment to the existing permit. Wetzel proposes to drill six holes projected underneath the section, all of which will be drilled from BLM land, with the exception of one being drilled directly on State lands. On June 22, 2013, the CSLC approved the permit amendment and extension through October 31, 2014. On December 19, 2012 and January 4, 2013, staff conducted site inspections, met the permittee, and reviewed the proposed drill sites.

Robert G. Wetzel (PRC 9027.2)

On June 20, 2012, staff received an application from Wetzel to prospect for solid minerals on 640 acres of State fee-owned school lands described as Section 36, T16N,R13E, SBM, San Bernardino County, about two miles south of the Mountain Pass Exit on 1-15. Wetzel's purpose for seeking a prospecting permit is to conduct geological mapping and hand sampling to help determine if the State parcel contains commercial base



(copper, iron, zinc) or precious metals (gold or silver). The parcel contains the Iron Horse Mine (last active during WWII) that was developed by two deep shafts, which staff has fenced for protection of the public. On October 19, 2012, the CSLC approved Wetzel's Mineral Prospecting Permit to prospect for solid minerals on State fee-owned school lands. The effective date of the permit is November 1, 2012, and will expire on October 31, 2013. Staff inspected the parcel on January 16, 2013, and found the fencing surrounding the shafts intact.

Mineral Extraction Lease Applications

Granite Construction, Liberty Quarry (W 40904)

In 2004, Granite Construction (Granite) applied for a mineral extraction lease on a 151-acre parcel south of Temecula in Riverside County. Granite plans to open a new mine, designated the Liberty Quarry, to extract granitic rock for aggregate. The proposed lease and an adjacent 160-acre parcel where the State owns a 1/16th mineral interest will be included in the project.



The Riverside County Planning Department, as the CEQA lead agency, completed an Environmental Impact Report (EIR) in April 2011. Staff wrote several letters to the County advising of the mineral interest that the CSLC manages for the economic benefit of STRS and the economic importance of the project. Additionally, when the City of Temecula attempted to annex the area that may have precluded the development of the project, staff again wrote several letters and testified at a public hearing advising of the possible negative impact that such an action could have. Annexation efforts were not successful. Numerous public hearings were conducted by Riverside County to discuss local concerns. In December 2011, the Riverside County Planning Commission denied the project by a 3-to-2 vote. Granite appealed their decision to the Riverside County Board of Supervisors, who also denied the project in February 2012. However, in May 2012, the Board of Supervisors approved the EIR. On November 14, 2012, Granite withdrew their lease application. Granite also advised the County of Riverside of the withdrawal of their land use applications. The Pechanga Band of Indians paid over \$3 million to purchase the surface rights to the property and over \$17 million for Granite to abandon the project. The land was considered sacred to the Pechanga Tribe. The project, if approved, would have provided a significant source of income to STRS, possibly several hundred million dollars over the proposed 50 year mine life.

Bureau of Reclamation (PRC 6735)

The U.S. Bureau of Reclamation (BOR) held a 90-acre lease from October 1, 1984, through September 30, 1994, at the Manchester Quarry in San Bernardino County near the California-Nevada-Arizona border. Operations ceased at the quarry in 1994, upon lease expiration. One month later, with passage of the California Desert Protection Act, the quarry was included in the Dead Mountains Wilderness Area. In



In 2001, the BOR submitted an application to renew the lease, along with an

application to the County to resume mining. The BOR proposed extracting 2.8 million tons of rock over a 25-year period to armor levees along the Colorado River to protect life and property.

After several years of inaction, staff met with BOR, San Bernardino County, and the OMR, in 2007 to discuss the project. In 2008, a draft CEQA document and a Mining and Reclamation Plan were completed. In 2009, an annual mine inspection by the County, revealed numerous violations and deficiencies and were deemed out of compliance with the Surface Mining and Reclamation Act (SMARA). After much discussion, the BOR recently agreed to either reclaim the parcel in accordance with SMARA, or mine it if permitted. Staff would prefer mining, as that would generate revenue for STRS and be a part of the necessary reclamation to decrease the existing mine slopes, rendering them safe.

On April 17, 2013, a meeting was convened at the BLM Needles office between the BOR, BLM, OMR, San Bernardino County and CSLC staff to discuss re-permitting or mine reclamation. BOR expressed their desire to reclaim but differed in the amount of reclamation that the County and OMR desire. Following the meeting, a field inspection was conducted by Steve Suitt of the County in accordance with SMARA. He determined that the mine remains out of compliance due to excessive pit slope angle and detrital fouling of the stream drainage. San Bernardino County is in the process of determining what form of permit exclusive of mining may be suitable for reclamation.

Mineral Exchange Application Kaiser Resources (W 40871)

In August 2002, Kaiser Resources applied to exchange the State's reserved mineral interest on a 467-acre parcel of school lands for a percentage interest in a nearby mineral estate. The parcel is located in the Eagle Mountain Mine Complex, a 3,000-acre area of open-pit iron mines in Riverside County. Kaiser held a 145-acre lease within the parcel from 1978 to 2002, but mining of iron ore ceased in 1982. In 1997, Riverside County issued an



approval to Mine Reclamation, LLC (a subsidiary of Kaiser Resources), for a Class 3 landfill at the site to serve the greater Los Angeles area, which was subsequently sold to the Los Angeles County Sanitation District for \$41 million. However, the sale was delayed due to litigation over a land exchange with the BLM. A series of State and federal court decisions ensued, culminating when the U.S. Supreme Court in March 2011, declined to review a negative decision by the U.S. Ninth Circuit Court of Appeals. Mine Reclamation, LLC, determined that resolution of the issues was unlikely and declared bankruptcy on October 30, 2011. Further discussion on the issue is pending resolution of the bankruptcy.

Eagle Crest Pumped Energy Storage Project (SCH #2009011010)

In 2010, the CSLC was asked to comment on the environmental review for the Eagle Crest Energy Company's Eagle Mountain Pumped Water Storage project which involves the east pit formerly leased to Kaiser. The basic proposal is to flood the upper and lower pits and pump water from the lower east pit to the upper pit at night when electrical usage is low. The water would flow through turbines to the lower pit during the day when electrical demand is high, generating up to 1,300 megawatts of electricity. Staff provided information regarding the State's 466.6 acre reserved mineral interest at the complex. In July 2012, staff sent comments to the State Water Resources Control Board (SWRCB) for a Draft Water Quality Certification for the project. In May 2013, staff reviewed the final draft EIR and sent comments to the SWRCB, which serves as the CEQA lead agency for the project, petitioning the Board not to certify the Environmental Impact Report due to cited deficiencies, and also because the State would be precluded from the ability to develop the iron ore resource on behalf of STRS.

With rapid escalation of iron ore prices and the reopening of several small iron ore mines in the southern California desert, the Kaiser Eagle Mountain Mine Complex is likely under review to determine whether resumption of iron ore mining is economically feasible.

Mineral Prospecting Permit Applications

Enigma Resources LLC (W 40949)

Enigma Resources LLC (Enigma) submitted an application for a mineral prospecting permit in July 2010 for a 480-acre parcel northeast of Bridgeport, in Mono County. A permit covering this parcel was previously issued to Enigma in March 2007, and then assigned to Cougar Gold LLC in April 2007. That permit, PRC 8742, expired in February 2010. Enigma plans to pursue the prospecting that Cougar Gold intended to carry out, to demonstrate commercial viability. Enigma's application remains incomplete at this time, pending application to Mono County for a drilling permit. Enigma is also working on a vehicle access agreement with the Flying M Ranch to the west, and the possible use of a helicopter to reduce prospecting impacts. On February 13, 2013, Enigma updated staff on their efforts to pursue the prospecting permit, which are centered on access negotiations with the Flying M Ranch.

Abandoned Mine Lands

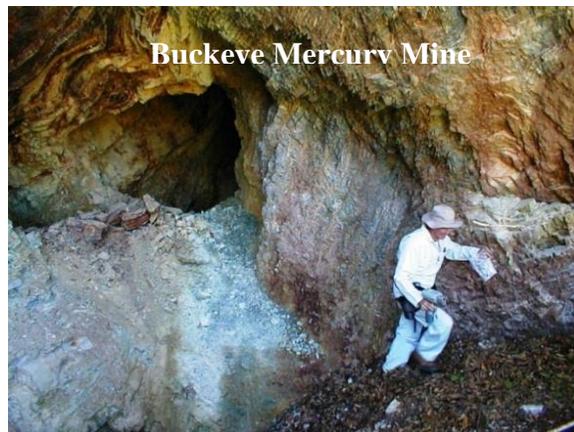
Staff continued its efforts to inventory and remediate abandoned mine features located on school lands. Staff participates in periodic meetings with local, county, State, and federal agencies, as well as contractors, environmental groups, and the public to share information.

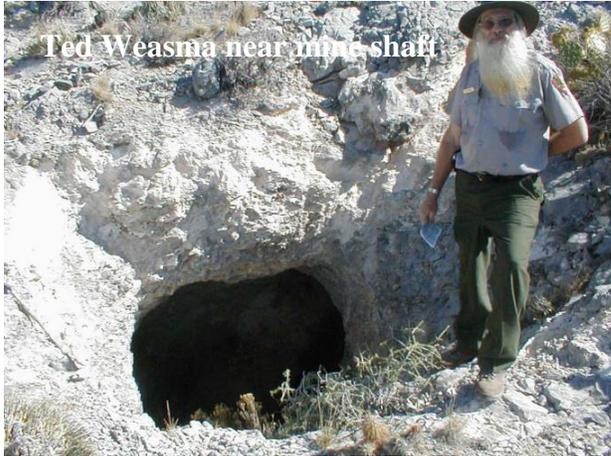
A 2009 report by the Natural Resources Agency summarized an inventory of chemical and physical hazards on lands managed by the State, including State school lands. The Resources Agency directed the OMR to prioritize and coordinate the remediation of the sites. The OMR and the Department of Toxic Substances Control (DTSC) determined that chemical hazards on lands managed by State Parks were of highest priority for remediation. The report states there are 1,213 abandoned mine features located on 143 school land parcels, five of which contain chemical hazards. Staff posted signs on those five parcels in 2009, warning that some form of chemical contamination from past mineral processing may be present.

During FY 2012-13, efforts were focused on the Buckeye Mercury Mine in Lake County, and the Pacific Fluorite Mine parcel in San Bernardino County.

Buckeye Mercury Mine:

In 2008, OMR contracted DTSC to sample mine tailings at the Buckeye Mercury Mine, to determine if they contained unacceptable concentrations of mercury. Results of the sampling indicated the mercury levels within relatively small tailing piles exceeded the Human Health Screening Criteria established by DTSC. In 2011, staff worked with DTSC to try and obtain a U.S. Environmental Protection Agency (EPA) Brownfield Grant for the Buckeye Mercury Mine in order to complete more studies to characterize the risk and level of contamination. The EPA denied the grant application, stating that sufficient information was gathered to make a determination as to whether the mine may qualify as a Superfund Site. In August 2012, the EPA issued a contract to Weston Solutions to conduct a Preliminary Assessment to determine if the site qualifies for the National Priorities List as a Superfund Site. Staff assisted Weston with essential background information. In September 2012, a site visit was conducted with the EPA, Weston Solutions, DTSC, OMR and CSLC staff. The EPA subsequently sent a letter on March 18, 2013, advising that the results of the Preliminary Assessment reveal that the site does not qualify for placement on the National Priorities List as a Superfund Site. AML warning signs have been posted at the mine and processing sites. Additional work remains to safeguard the physical hazards, including the adit shown above.





Ted Weasma near mine shaft

Pacific Fluorite Mine Area:

At the request of Mojave National Preserve Geologist Ted Weasma, an abandoned mine inventory was conducted in June of 2012 at the site of the Pacific Fluorite Mine in the Clark Mountains of San Bernardino County. Due to the large number of abandoned mine features from old silver and fluorite mines, and their geographic remoteness and rugged terrain, staff returned to the site on July 9 of

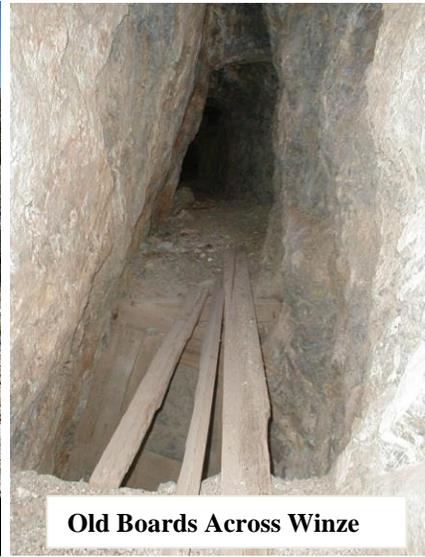
2012, and completed the inventory work which resulted in the compilation of over twenty shaft and adit features, which could pose a hazard to the public and wildlife. Staff returned to the site in December 2012, and again in January 2013, installing warning signs at each of these mine features. In addition, an abandoned steel pipe was cut off and removed that was sticking up and posing a hazard on the dirt road that traverses the parcel.



Abandoned Pipe



Rotted Wood Shaft Collar



Old Boards Across Winze

OIL & GAS PROGRAM



Round Mountain Oil Field

Revenue from the oil & gas program totaled \$1,981,011.65 for FY 2012-13, a 6% decrease from the prior year. Oil production from the two school lands parcels where the State has a 1/16th reserved mineral interest reached 3,275,778 bbls, which is less than a 0.1% decrease from the previous year. The price for the oil averaged \$102.33 per barrel, 5.8% lower than the prior year. Most of the revenue, \$1,979,603.93, came from the 160-acre Round Mountain parcel (VA 5310) located northeast of Bakersfield in Kern County. This parcel is part of a unit operated by MacPherson Oil Company. The balance of the revenue, \$1,407.72, came from the seven-acre Sulfur Crest parcel (LA 9252) located in the Ojai Oil Field in Ventura County, which is leased by the Termo Company.

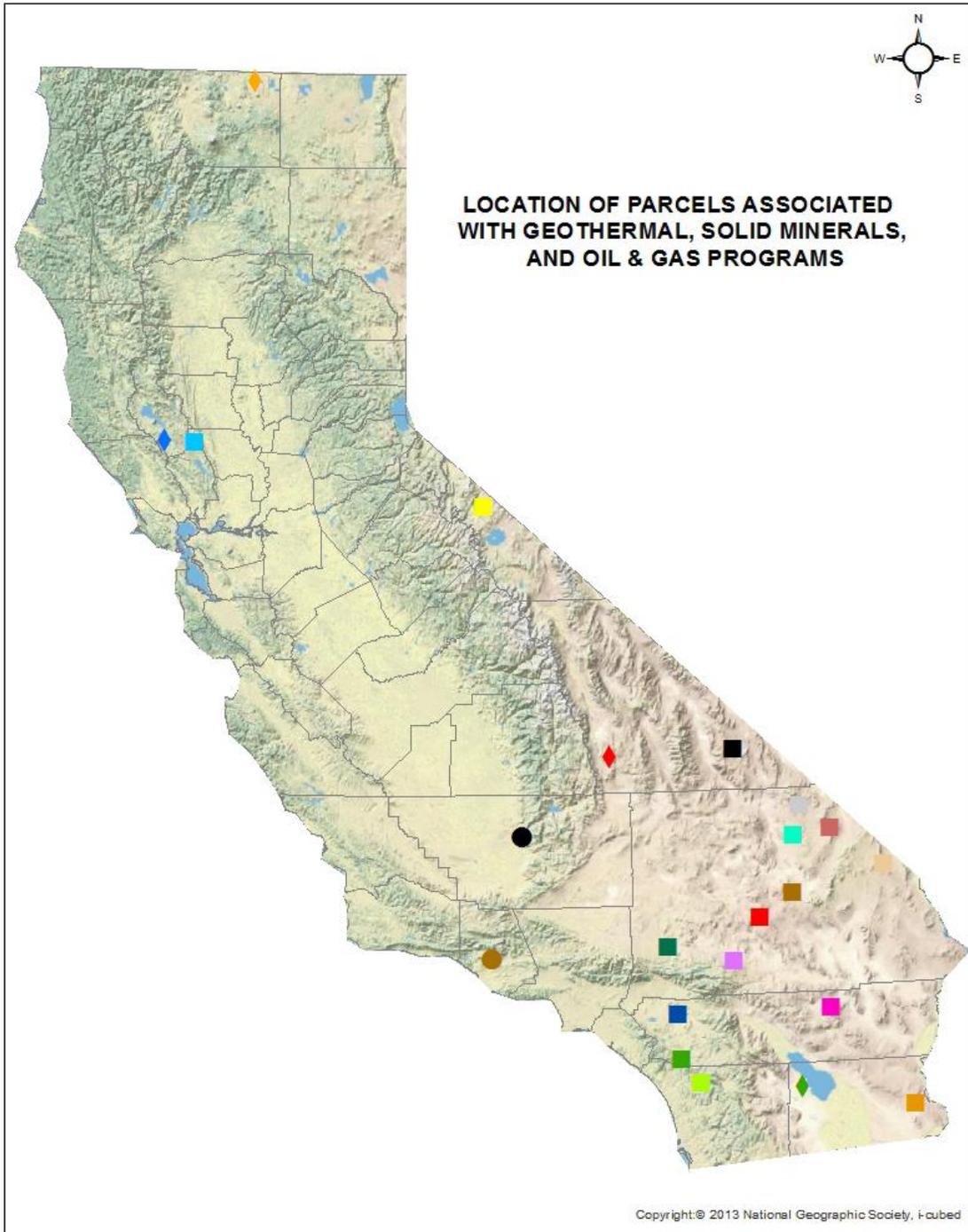
The designations VA and LA stand for the Visalia and Los Angeles land districts of the old California Surveyor General, a constitutional office until 1929. The sale of school lands was one function of that office, and transactions were typically identified with the district abbreviation and a number. After 1929, the functions of the Surveyor General were transferred to the Division of State Lands within the

Department of Finance, then again in 1938 to the California State Lands Commission.

AB 982/Desert Renewable Energy Conservation Plan

Staff's efforts in regards to AB 982 and the Desert Renewable Energy Conservation Plan (DRECP) are discussed in further detail in the Surface Management Program of this report. AB 982, which became law in 2011, directed the CSLC and the Department of the Interior to enter into a Memorandum of Agreement (MOA) designed to facilitate land exchanges to consolidate State school land parcels consistent with renewable energy development of the DRECP. CSLC staff provided input into the draft Environmental Impact Statement/Environmental Impact Report (EIS/EIR) that will guide land exchanges between the State and the Bureau of Land Management, for the purpose of protecting valuable biological and cultural resources in the desert while paving the way for renewable energy development. This initiative was enacted, in part, to facilitate the Governor's desire to achieve 33% renewable energy by 2020. During FY 2012-13, staff continued efforts to support the DRECP planning process by initiating a GIS database of land ownership, mineral resources, biological resources, historical resources, and renewable energy resources.

Under the MOA, the CSLC has provided a list of school lands it would be willing to exchange that are within the geographic boundaries of the DRECP. Likewise, the BLM will provide a list of lands to the CSLC that they believe would be desirable for acquisition by the Commission to facilitate renewable energy development, and subsequent revenue generation. In addition to this, the BLM will identify the school land parcels they would like to acquire in the exchange. Upon receipt of that list of lands, MRMD staff will evaluate the mineral potential of the desired school land parcels to determine if additional value is warranted in the appraisal process.



Legend

Geothermal

- ◆ Deep Rose Development, LLC: PRC # 8949
- ◆ Entiv Organic Energy: PRC # 8998
- ◆ Geothermal Leasing Proposed Project - Nevada Geothermal Power: WO # 40958
- ◆ The Geysers: PRC # 4596, 4596 "A", 4597, 5206, 6422, 7845, 8556, 8844, 7179, 8950, 9000

Oil & Gas

- MacPherson Oil Company: VA # 5310
- Termo Oil Company: LA # 9252

Solid Minerals

- Bagdad Chase, Inc.: PRC # 8917
- Bureau of Reclamation: PRC # 6735
- Enigma Resources LLC: WO # 40949
- Granite Construction, Liberty Quarry: WO # 40904
- Granite Construction, Ludlow Pit: PRC # 8272 - Expired
- Granite Construction, Palm Desert Pit: PRC # 7945
- Hanson Aggregates: PRC # 7301
- Hi-Grade Materials: PRC # 8831
- Homestake Mining Company: PRC # 7808
- Kaiser Resources: WO # 40871
- Protech Minerals: PRC # 8322 - Expired
- Robert G. Wetzel: PRC # 9026.2
- Robert G. Wetzel: PRC # 9027.2
- U.S. Borax: PRC # 736
- Vulcan Lands, Inc.: PRC # 8253
- Western Mesquite Mines: PRC # 8039

**SUMMARY OF REVENUE GENERATED FROM GEOTHERMAL,
SOLID MINERALS, AND OIL & GAS PROGRAMS -
FISCAL YEAR 2012-13**

STRS FUND

Geothermal Royalties:

Regular PRC Royalties: \$ 4,362,346.07

Supplemental PRC Royalties: \$ 258,731.99

Fractional RMI Royalties: \$ 198,268.39

Total PRC/RMI Royalties: \$ 4,819,346.45

Solid Minerals Royalties:

Royalties from leases: \$3,569,230.70

Royalties from 1/16th interest parcels: \$ 5,778.75

Solid Minerals Total: \$ 3,575,009.45

Oil & Gas Royalties:

Oil & Gas Total: \$ 1,981,011.65

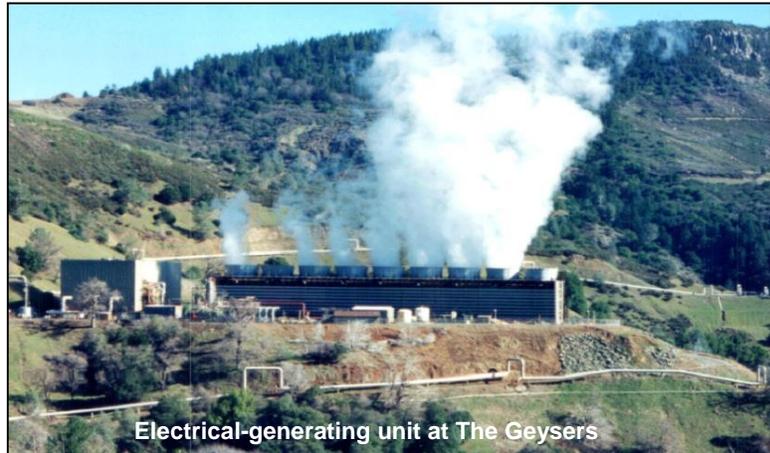
TOTAL GROSS REVENUE: \$10,375,367.55

FISCAL YEAR 2013-14 PLANNED ACTIVITIES

GEOTHERMAL PROGRAM

The Geysers

Staff estimates that revenue from school lands geothermal leases at The Geysers should remain in the range of approximately \$4.5 million during FY 2013-14. Steam production on developed leases is expected to decline slightly, while prices for electrical power –



underlain by those for natural gas - are expected to increase slightly. The scarcity of capital may compromise new exploration activity taking place in the near term, resulting in revenues that are unlikely to top \$5.0 million.

Geothermal Permits

Staff plans to monitor proposed exploratory drilling on Deep Rose's permit PRC 8949 in Inyo County, Entiv's permit PRC 8998 in Siskiyou County, and High Valley, LLC's permit PRC 9001.2 in Lake and Mendocino counties. Successful drilling and discovery of commercial geothermal energy could lead to proposed conversion of the permits into leases, subject to CSLC approval.

Geothermal Applications

Staff expects to seek CSLC approval of a negotiated lease, or a prospecting permit, with Alternative Earth Resources (AER), formally Nevada Geothermal Power Inc, in the Truckhaven area of Imperial County. AER's current leasehold interest covers approximately 4,027 gross acres of federal and private leases. AER's proposed Phase One will consist of a development plan to construct a 15 MW binary power plant to be built entirely on private land. If a permit or lease is issued, the state parcels will most likely be drilled during Phase Two.

Staff will continue to monitor, amend, and issue new geothermal leases. Staff encourages new applicants, and continually assists with answering any questions regarding geothermal development. Staff is currently working on IWP and AER's negotiated geothermal leases, and Calpine's application to amend PRC 8556, Parcel 3. Staff anticipates that these items will be considered by the CSLC in the coming fiscal year.

SOLID MINERALS PROGRAM

Mineral Lease Management

During the last FY, staff estimated that the revenue from solid mineral leases will likely exceed \$2.0 million. During FY 2012-13, royalty revenue exceeded staff's expectations, amounting to royalty revenue of \$3,575,009.45, with \$3,451,522.00 generated from WMMI at the Mesquite Gold Mine. Due to the commencement of precious metals mining by WMMI on the state parcel, the solid minerals program experienced the highest single-year royalty ever generated in solid minerals. For the FY 2013-14, staff anticipates a reduction of revenue to about \$1.5 million, primarily since mining of the state parcel is expected to be completed at the Mesquite Mine in FY 2013-14. As monthly sales are made at the Mesquite Mine, the State is paid proportional to their ownership of the heap leach pad. Once mining of State lands is concluded, State ore will no longer be added to the heap leach pad and the State's proportion will gradually decrease over time. The payments will be received within the 10-year lease renewal, as the State is paid when ounces are sold. The property was acquired under an exchange with the BLM as part of the California Desert Protection Act of 1994. The federal government under the MOU, will receive an equal value of state inholdings within park and wilderness areas for all royalty revenues received.

The slow economy continues to effect aggregate mines in southern California. The State currently only has three school land aggregate leases. While the Hanson mine in San Diego County remains idle, the Vulcan Black Angel Quarry and the Hi-Grade Lucerne Valley Pit, continue to show marked improvement in sales. Staff anticipates an increase in demand for aggregate for road construction and housing as we continue to recover from the recession.

Mineral Applications

Staff continues to pursue either a new Mineral Extraction Lease with the Bureau of Reclamation (BOR), for the Manchester Quarry, or site reclamation. Staff prefers the site be reclaimed via mining, as this work could potentially result in revenue in excess of \$5.0 million to the STRS over a 25-year project life.

Staff will continue to manage, extend, and issue, new mineral prospecting permits. Staff encourages new applicants to extend or amend their permits as required, and continually assists with new mineral inquiries to foster and encourage environmentally sound mineral exploration and development.

Staff plans to initiate discussions with Kaiser regarding their application for a mineral exchange, since it appears the landfill is unlikely to occur. With the reopening of other iron ore mines in the California desert, the Kaiser Eagle mine, with its large remaining resource, is sure to be considered. Staff is awaiting a response from the State Water Resources Control Board regarding their request to not certify the EIR for the Eagle Crest Pumped Water Storage Project, due to the adverse impact to future iron ore productions at Eagle Mountain.

Desert Renewable Energy Conservation Plan

Under the MOA the CSLC has executed with the BLM, Staff is awaiting the list of school lands BLM would like to acquire, and also a list of lands they are willing to exchange that are suitable for alternative energy development. The BLM does not appear to be willing to exchange lands with geothermal resource potential. During FY 2013-14, staff hopes to negotiate the first exchange that the CSLC could consider in FY 2014-15. Staff also anticipates the completion of the DRECP EIS/EIR that will guide the agencies in their exchange negotiations, such that the BLM acquires lands suitable for the preservation of biological and cultural values, and that the CSLC acquire lands suitable for alternative energy development.

Abandoned Mine Lands

Staff desires to continue work with the OMR on the inventory and remediation of hazardous mine features on school lands parcels. However, during the last several years, the OMR's contractual obligations with the BLM and the National Park Service to conduct abandoned mine land inventory and remediation project management substantially slowed mutual efforts with the CSLC. OMR has stated that their contract work is nearly concluded with the NPS and the BLM and that they look forward to renewed inventory and closure work with the CSLC starting in the first quarter of 2014.

With the completion of the inventory and signage at the Pacific Fluorite Mine parcel, staff plans to install fencing as well as a bat gate and cupola on at least one adit and shaft during the late summer of 2014, during the appropriate biologic window.

At the Leiser Ray Mine, staff intends to complete consultation with CDFG and SHPO so that the mines can be closed either during the summer, or fall, of 2014, such that bat maternity season can be avoided. Additional bat exit survey work on the two large shafts may permit their closure, along with ten smaller shafts, such that all of the closure work could be completed at one time.

Staff will continue to inspect the Crown Uranium Mine, and other mines that have received signage, fencing, bat gates, cupolas, backfills, or other protective measures, to ensure their continued integrity from adverse weather and/or vandals. Staff will continue to participate in quarterly abandoned mine meetings that OMR hosts in order to share information concerning AML efforts of local, State, and federal agencies.

OIL & GAS PROGRAM

Staff estimates that revenue from the two school lands oil & gas parcels is expected to decline slightly, but will remain close to \$2.0 million during FY 2013-14, as high levels of oil production continue, but prices drop under \$100/barrel due to increased domestic production.

SURFACE MANAGEMENT PROGRAM

The LMD is responsible for the Surface Management Program, which oversees all surface activities on school lands with the exception of mineral activities. These activities include land exchanges and sale of school lands parcels to public and private entities, acquisitions of lands to enhance the resource base, and the issuance of leases for various purposes such as the production of renewable energy, agriculture, grazing, and rights-of-way for roads, oil and gas pipelines, and electrical transmission lines. The objectives of the Surface Management Program are to manage surface uses to generate revenue, assure ongoing viability of the resource, protect the corpus of the trust, enhance local economic development, and protect the environment. These goals are accomplished through management and development techniques that maximize the economic return to STRS and the SLBF. For a summary of the revenues generated to STRS and the SLBF through the Surface Management Program, see the table entitled "Summary of Revenue Generated From Surface Management Program - Fiscal Year 2012-13" (page 30).

FISCAL YEAR 2011-12 ACTIVITIES

STATE TEACHERS' RETIREMENT SYSTEM FUND REVENUES

Surface Rental Income and Revenues

General surface leasing involves ongoing activities, including processing new applications, re-issuing expiring leases, processing lease assignments and amendments, conducting rent reviews, terminating old leases, and conducting other surface management activities. The majority of the 468,600± acres of school lands are isolated, landlocked parcels, with many being non-revenue generating desert lands. However, close to a quarter of the total school land acreage is leased for revenue-generating purposes.

Revenues deposited into the STRS fund from more than 100 revenue-generating surface leases in FY 2012-13 totaled \$223,789.18, which represented an increase of 19% from FY 2011-12. Surface rent rates are usually tied directly to land values, which have been in decline due to the recent recession. However, revenues from LMD surface leases actually increased in FY 2012-13 because several new right-of-way leases were completed. Also, some older leases from the 1960s expired and were renegotiated at current market rent rates.

SCHOOL LAND BANK FUND - LOAN TO THE GENERAL FUND, REVENUES, AND EXPENSES

Loan to the General Fund

In response to the State's severe budget crisis, the Legislature borrowed from numerous State funds during FY 2008-09, including \$59,000,000 from the SLBF. This loan to the General Fund was part of the Budget Act of 2008, as amended by Chapter 2, Statutes of 2009 Third Extraordinary Session. The loan is scheduled to be repaid no later than June 30, 2016. During the term of the loan, interest will accrue based on the rate utilized by the Pooled Money Investment Account (PMIA).

Bureau of Land Management CDPA Land Exchange (AD 556)

On October 31, 1994, the California Desert Protection Act (CDPA) was signed into law by the President of the United States (Public Law 103-433). The CDPA designated 3.6 million acres in southern California as wilderness to be administered primarily by the U.S. Bureau of Land Management (BLM), and designated an additional four million acres in southern California to be included in the national park system. The purpose of the CDPA is to preserve areas in the California desert to protect its natural, cultural, scenic, and historical values and to provide for public enjoyment. Four hundred forty-two parcels (approximately 251,000 acres) of fee-owned school lands and more than 100 parcels encumbered by the State's reservation of mineral interests were initially identified to be within the boundaries of the CDPA.

Section 707 of the CDPA provides for the exchange of school lands located within these designated areas for other federal lands located outside of these areas. The CSLC receives compensation for the exchange of its fee and mineral interests on a value-for-value basis as determined by fair market appraisals. Compensation for the State's assets may be made in various forms, including cash or exchange for other lands. To date, there have been five CDPA land exchange transactions completed with the BLM. These five exchanges have resulted in the transfer of more than 66,000 acres of school lands to the BLM and deposits totaling more than \$14.7 million into the SLBF.

During FY 2012-13, work continued on a sixth CDPA land exchange. Staff completed the negotiations on a Binding Exchange Agreement with the BLM, involving 69 parcels of school lands totaling approximately 38,434 acres. All of these properties are located within national parks, national monuments, or federal wilderness areas. It is hoped that the sixth CDPA land exchange will be completed in FY 2013-14, and will result in a total deposit of \$7,994,925 into the SLBF. As part of this transaction, a partial payment of \$56,492.29 was deposited into the SLBF during FY 2009-10. For more information on this exchange, see page 34.

Accrued Interest on the School Land Bank Fund

A total of \$4,886.29 in interest was generated by the PMIA to the SLBF during FY 2011-12. Interest accruals decreased slightly from the previous year due to the lower interest rates that resulted from the lower overall Fund balance.

Expenses Charged to the School Land Bank Fund

Expenses during FY 2012-13 totaled \$473,001.61. Of this amount, \$279,745.68 was charged to the Renewable Energy Program and \$174,753.93 was incurred by the Abandoned Mine Remediation Program. There was also a total of \$18,502 in charges to the Fund for statewide administrative services.

SUMMARY OF REVENUE GENERATED FROM SURFACE MANAGEMENT PROGRAM - FISCAL YEAR 2012-13

STRS FUND

Surface Rentals:

Surface Rentals:	\$ 233,789.18
TOTAL GROSS REVENUE GENERATED TO STRS FUND:	\$ 233,789.18

SCHOOL LAND BANK FUND

GROSS REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$ 4,886.29
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EXPENSES

Statewide Administrative Services (Pro Rata):	\$ -13,902.00
Statewide Administrative Services (Fi\$Cal):	\$ -4,600.00
Program 10 – Abandoned Mine Closure Program:	\$ -174,753.93
Renewable Energy Program:	<u>\$ -279,745.68</u>

NET REVENUE GENERATED TO SCHOOL LAND BANK FUND:	\$ -468,115.32
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FISCAL YEAR 2013-14 PLANNED ACTIVITIES

POTENTIAL STATE TEACHERS' RETIREMENT SYSTEM FUND REVENUES

Surface Rentals Income

Staff estimates that surface rentals from existing and new surface use leases on school lands parcels during FY 2013-14 will remain relatively unchanged from FY 2012-13.

Timber Harvests

There is potential for income from timber salvage and sanitation operations in FY 2013-14. These operations are conducted periodically due to losses from natural causes such as fire, high winds, insect infestation, and diseases. Because of the irregular nature of these operations, the amount of additional income from these sources is difficult to predict.

Renewable Energy Projects

With the passage of Assembly Bill (AB) 32, the increase in public awareness about climate change, and the rise in energy prices, staff expects more interest in the long-term leasing of school lands for renewable energy projects. Some of these projects will involve utilization of wind as an energy source. These projects require the installation and operation of wind turbines that, if installed, would generate electricity that would be placed into the State's electrical grid. Other renewable energy projects will utilize solar technology such as photovoltaic cells and solar-concentrating systems (troughs, towers, or dishes).

WIND

Staff plans to continue processing an application for a wind energy lease known as the Tule Wind Project, which was filed with the CSLC in 2007. This proposed project involves more than 12,000 acres of lands located in eastern San Diego County, including federal lands administered by the BLM, private lands, tribal reservation lands of the Ewiiapaayp Band of Kumeyaay Indians, and 640 acres of school lands.

The Tule Wind Project was analyzed in a joint Environmental Impact Report/Environmental Impact Statement (EIR/EIS) prepared by the California Public Utilities Commission (as the lead agency under CEQA) and the BLM (as the Lead Agency under the National Environmental Policy Act). In December 2011, the BLM issued a Record of Decision authorizing the portion of the project located on federal lands. But new transmission lines and access roads necessary for the project require separate authorization from the Bureau of Indian Affairs (BIA) for development on the tribal lands and by the CSLC for

development on the school lands. The BIA and the CSLC are separately analyzing the proposed project on their respective lands, particularly with regards to potential impacts on golden eagles. Staff also is consulting with the U.S. Fish & Wildlife Service on the project. If the project ultimately is approved by the CSLC and the lease is issued to allow construction and operation of the wind turbines, staff anticipates significant revenue from this lease beginning in FY 2014-15.

SOLAR

Staff will continue processing two applications for solar energy leases in San Bernardino County that together would cover almost 11,400 acres of school lands. The two proposed projects, Johnson Valley SEGS and Sorrel Solar Farm, will each be subject to environmental reviews under CEQA. Both of these projects are on temporary hold while the DRECP (see discussion below) is completed and new transmission line projects are reviewed and approved. If these two solar projects are successfully completed and the leases are issued, staff anticipates significant revenue from these leases beginning in FY 2017-18.

Desert Renewable Energy Conservation Plan/Renewable Energy Action Team (DRECP/REAT)

On November 17, 2008, Governor Schwarzenegger signed Executive Order S-14-08 (Order), establishing a Renewable Portfolio Standard (RPS) for California, whereby retail sellers of electricity must serve 33 % of their load with renewable energy by 2020. The Order directed State agencies to take all appropriate actions to implement this target in all regulatory proceedings, including siting, permitting, and procurement for renewable energy power plants and transmission.

Also on November 17, 2008, the California Energy Commission and the California Department of Fish and Game (CDFG, now California Department of Fish & Wildlife, CDFW) signed a Memorandum of Understanding (MOU) formalizing the Renewable Energy Action Team (REAT) to facilitate the planning and realization of this RPS. The Order, among other things, directed the REAT to create a "one-stop" process for permitting renewable energy generation power plants and to work with the BLM and USFWS to create a Desert Renewable Energy Conservation Plan (DRECP or the Plan) that, generally speaking, encompasses portions of the Mojave and Colorado deserts in California. The primary goals of the DRECP are to provide for the long-term conservation and management of sensitive species and the natural communities and ecosystems on which they depend, identify the most appropriate locations in the Plan area for renewable energy development, and provide a coordinated and standardized mitigation requirement strategy that creates a more efficient process by which project applicants may obtain the necessary regulatory authorizations.

On September 1, 2011, CSLC entered into an MOU with the REAT to facilitate coordination between CSLC staff and the REAT Agencies to ensure that REAT and DRECP goals for renewable energy development and environmental protection are accomplished in a manner that is consistent with and advances CSLC's management objectives for school lands in the DRECP Planning Area. The execution of this MOU, along with the passage of AB 982, discussed below, enhances the CSLC's role in the development of the DRECP and helps facilitate the exchange of lands between the CSLC and the BLM, resulting in the consolidation of land ownership patterns to the benefit of both agencies.

During FY 2013-14, staff will continue to actively participate in the DRECP for the purpose of improving the potential development of school lands for renewable energy projects involving both revenue-generation purposes and habitat mitigation and thereby maximize the value of the lands within the SLBF.

Land Exchanges to Facilitate Renewable Energy Projects – AB 982

During the 2011 legislative session, the Legislature passed and Governor Brown signed AB 982 (enacting chapter 2 of Division 7.7 of the Public Resources Code). The new law requires CSLC staff, with the cooperation of the Department of the Interior, to enter into a memorandum of agreement to facilitate land exchanges that consolidate school land parcels into contiguous holdings. AB 982 also provides that in preparing any land exchange proposal, priority must be given to exchanges that are best suited for renewable energy development projects and that are consistent with the DRECP. This law went into effect on January 1, 2012. Furthermore, the law requires that environmentally-sensitive lands and lands with extraordinary cultural or biological resources be identified, with the intent of consolidating these lands and providing for their long-term protection.

The CSLC and BLM staffs have already met to begin this process, and anticipate entering into a proposed land exchange agreement during the last half of FY 2013-14. There has been ongoing discussion between CSLC and the BLM regarding the need for appropriate compensation associated with the exchange of lands possessing mineral, biological, renewable energy, and historical resources. For more information, see the Addendum, *Report to the California State Legislature on the Status of School Land Consolidation Efforts in the California Desert*.

POTENTIAL SCHOOL LAND BANK FUND REVENUES AND ACTIVITIES

Applications for the following projects are currently under consideration and will be actively processed in FY 2012-13. Staff also anticipates new requests for land exchanges and land sales will be received during the year.

CDPA/BLM Land Exchange (AD 556)

Prior CDPA land exchanges between the CSLC and the BLM have resulted in an unequal balance between the values of the lands previously exchanged. Currently, the CSLC owes the BLM lands worth \$2,154,675. The BLM has available, through the General Services Administration, \$7,938,432.71 from surplus federal land sales designated for CDPA land purchases from the CSLC. Staff continues to work with BLM on a new proposed "Ledger Balancing Land Exchange" whereby the CSLC will transfer school lands of approximately \$10,149,600 in value to the BLM and National Park Service (NPS) to eliminate the outstanding balance and facilitate the completion of the terms of the original CDPA legislation. As part of the transaction, the NPS was already provided a payment of \$56,492.29 to balance the transaction (see page 23). Regardless, this transaction was stalled due to a federal audit by the General Accountability Office (GAO). Staff hopes to complete this transaction during FY 2013-14. However, the legal dispute between the GAO solicitor and the Department of the Interior solicitors is beyond the CSLC's control. It remains uncertain if and when this dispute will be resolved. When completed as proposed, staff anticipates a total of \$7,994,925 will be deposited into the SLBF from this exchange.

State Parks Land Sale (SA 5763)

The California Department of Parks and Recreation (Parks) submitted an application in FY 2005-06 to purchase 5,758 acres of school lands for a State Vehicle Recreation Area (SVRA). The land consists of nine full sections located in Imperial County west of the Salton Sea. Parks already completed an acquisition involving 4,000 acres of privately-owned land for the project, and the nine sections of school lands are arranged in a checkerboard pattern amid this previously acquired property. Since originally proposed, the purpose of this sale was modified. Parks now will obtain the School land property as part of a mitigation measure for a development project under construction by San Diego Gas & Electric (SDG&E). SDG&E will provide the funds for the transaction. Approximately half of the transferred school lands will be used by Parks to expand Anza Borrego State Park and the remainder will be used by Parks Off-Highway Vehicle Division for the SVRA. After lengthy delays, the sale is expected to be completed in FY 2013-14, and will add more than \$2,300,000 to the SLBF.

Heinz Ranch Land Exchange (W 26524)

Staff will continue to process an application for a land exchange that was received in December 2011. This project involves school lands located near Honey Lake in Lassen County. Under the proposed exchange, 2,745 acres of school lands will be exchanged for 2,876 acres of private lands located in the same area. The CSLC will also receive a cash payment of \$42,500, which will be deposited into the SLBF. The applicant currently is attempting to acquire mineral rights which will be required as part of the exchange agreement.

FINANCIAL SUMMARY: FISCAL YEAR 2012-13

STRS FUND

REVENUES AND EXPENSES

Revenues:

Surface Rentals	\$	223,789.18
Geothermal	\$	4,865,331.57
Solid Minerals	\$	3,575,009.45
Oil and Gas	\$	1,981,011.65
GROSS REVENUES	\$	10,645,141.85
Less: Geothermal Resource Development Account (GRDA) Deposits.....	\$	<45,985.12>
(Public Resources Code Section 3826)		
TOTAL	\$	10,599,156.73
EXPENSES: Net Management Costs		
Land Management.....	\$	388,707.93
Geothermal	\$	430,166.66
Solid Minerals	\$	221,968.21
Oil and Gas	\$	1,745.19
Ownership Determination	\$	121,451.63
GROSS EXPENSES	\$	1,164,039.62
Less: Reimbursement Recovery	\$	<134,506.69>
TOTAL EXPENSES	\$	1,029,532.93
NET REVENUE TO STRS	\$	9,569,623.80

SCHOOL LAND BANK FUND

Balance as of July 1, 2012 (<i>after year-end accounting adjustment</i>)	\$	1,725,620.18
SMIF Interest Earned Fiscal Year 2012-13.....	\$	4,886.29
Less: Expenses.....	\$	<473,001.61>
BALANCE OF FUND AS OF JUNE 30, 2013.....	\$	1,257,504.86

(Note: Does not include \$59,000,000 loan to General Fund, due 6/30/16)

ABBREVIATIONS AND ACRONYMS

AB	Assembly Bill
AD	Acquisition Disposition
AER	Alternative Energy Resources, Inc.
BIA	Bureau of Indian Affairs
BLM	U.S. Bureau of Land Management
BOR	U.S. Bureau of Reclamation
CDFG	California Department of Fish and Game
CDFW	California Department of Fish and Wildlife
CDPA	California Desert Protection Act
CDOGGR	California Division of Oil, Gas, and Geothermal Resources
CEQA	California Environmental Quality Act
CPX	CPX Uranium, Inc.
CSLC	California State Lands Commission
DRECP	Desert Renewable Energy Conservation Plan
EIR	Environmental Impact Report
EIS	Environmental Impact Statement
ENTIV	Entiv Organic Energy LLC
EPA	United States Environmental Protection Agency
FY	Fiscal Year
GIS	Geographic Information Systems
IAE	Iceland America Energy
IMP	Interim Management Plan
LA	Los Angeles (an old State Land Office land district designation)
LLC	Limited Liability Corporation
LMD	Land Management Division
MRMD	Mineral Resources Management Division
MOU	Memorandum of Understanding
NEPA	National Environmental Policy Act
NGP	Nevada Geothermal Power

NPS	U.S. National Park Service
OMR	California Department of Conservation, Office of Mine Reclamation
Parks	California Department of Parks and Recreation
PMIA	Pooled Money Investment Account
PRC	California Public Resources Code
REAT	Renewable Energy Action Team
RPS	Renewable Portfolio Standard
SDG&E	San Diego Gas & Electric
SLBF	School Land Bank Fund
SMARA	Surface Mining and Reclamation Act
STRS	State Teachers' Retirement System
SVRA	State Vehicular Recreation Area
USFWS	United States Fish and Wildlife Service
USRG	U.S. Renewables Group
VA	Visalia (an old Surveyor General land district designation)
WMMI	Western Mesquite Mines, Inc.

ADDENDUM

Status of School Land Consolidation Efforts in the California Desert - 2013

Introduction and Purpose

In September 2011, the Executive Officer of the California State Lands Commission (Commission), with authority from the Commission, executed a memorandum of understanding with the four agencies comprising the Renewable Energy Action Team (REAT)¹ expressing the agencies' intent to coordinate and cooperate on development of the Desert Renewable Energy Conservation Plan (DRECP or Plan) in the Mojave and Colorado Desert regions of the State. The goal of the DRECP is to provide for effective protection and conservation of desert ecosystems while allowing for the appropriate development of renewable energy projects. In addition to the REAT agencies and the Commission, the planning process involves several other state and federal agencies, including the California Public Utilities Commission, California Department of Parks and Recreation, National Parks Service, and the Department of Defense, as well as interested stakeholders including cities, counties, tribal interests, industry and utilities, and non-governmental environmental organizations.

Assembly Bill 982 (Skinner), enacted as Chapter 2 of the School Land Bank Act, Land Exchanges for Renewable Energy-Related Projects (Chapter 485, Statutes of 2011 and codified in California Public Resources Code §§ 8720-8723), builds on this ongoing cooperative relationship. Pursuant to the requirements of Chapter 485, Commission staff is submitting this report on its school land consolidation efforts in the California desert,² including the status of the memorandum of agreement (MOA) between the Commission and the United States Department of the Interior, Bureau of Land Management (BLM) described in subdivision (a) of section 8722.

Background

School lands were granted to the State of California by the federal government in 1853 and consisted of the 16th and 36th sections of land in each township. A supplementary act in 1927 extended the grant of mineral lands to the State. Today, the Commission manages approximately 468,000 acres of school lands held in fee ownership by the State, and the reserved mineral interests on approximately 790,000 acres of school lands where the surface estate has been sold.

School lands were placed into a statutory trust in 1984 when the State Legislature approved the School Land Bank Act, creating the School Land Bank Fund³ and designating the Commission as trustee of the Fund. In enacting the School Land Bank

¹ The REAT was established pursuant to a memorandum of understanding among the California Energy Commission, the California Department of Fish and Wildlife, the U.S. Department of Interior Bureau of Land Management, and the U.S. Fish and Wildlife Service, dated November 17, 2008.

² The "California desert" in this report means the California Desert Conservation Area as described in Section 1781 of Title 43 of the United States Code.

³ The School Land Bank Fund was created pursuant to section 8711 of the California Public Resources Code.

Act, the Legislature directed the Commission to “take all action necessary to fully develop school lands, indemnity interests, and attendant mineral interests into a permanent and productive resource base” to provide economic support of the public school system (California Public Resources Code § 8701). Today, all net revenue derived from the use of school lands (i.e., royalties, rents, and interest generated from promissory notes) must be deposited into the State Treasury to the credit of the Teachers’ Retirement Fund, which benefits the California State Teachers’ Retirement System.

The majority of the over 340,000 acres of school land under the jurisdiction of the Commission in the California desert are fragmented and isolated, and the size of the individual parcels is insufficient for development of renewable energy projects. In addition, significant portions of these parcels are located within national parks, preserves, monuments, and forests. Although these lands retain significant conservation value, their location and physical characteristics limit development potential.

Generally, the Commission’s objective in participating in the development of the DRECP is to ensure that DRECP goals for renewable energy and environmental protection are accomplished in a manner that is consistent with and advances the statutory responsibilities described above for management of school lands in the California desert area. Assembly Bill 982 supports this effort because it articulates the important role of land consolidation efforts in achieving a successful DRECP and improving revenue generation on school lands. Specific activities and accomplishments related to this objective and the provisions of Assembly Bill 982 are described below.

Memorandum of Agreement

The provisions of the School Land Bank Act enacted via Assembly Bill 982 direct the Commission to consolidate school lands through exchanges with the Department of Interior, represented by the BLM, in the California desert area, which includes the DRECP Plan Area. Section 8722, subdivision (a) requires the Commission to enter into an MOA with the BLM by April 1, 2012, to facilitate and prioritize these exchanges such that the resulting contiguous school land holdings are suitable for large-scale renewable energy projects. This MOA was signed by the Commission’s Executive Officer and the California Director of the BLM on May 21, 2012. The MOA formalizes the working relationship between the two agencies and provides a process for cooperation to prioritize, enter into, and complete one or more mutually beneficial land exchanges.

The MOA sets forth the objectives and commitments of the Commission and the BLM, including information sharing, minerals evaluation and appraisal, streamlining of the land exchange process, and commitments to prioritize completion of exchanges. As discussed below, through its participation in the DRECP development process, Commission staff is engaged in discussions with the BLM, California Department of Fish and Wildlife (CDFW), and other state and federal agencies that will assist in developing a successful land exchange proposal.

DRECP Development and CDFW consultation

The DRECP Planning Area contains extensive school lands under the Commission’s jurisdiction, and the development of the DRECP will affect these lands and the potential to generate revenue benefiting the State Teachers’ Retirement System. Commission staff

continues to actively participate in the DRECP planning process to ensure the Commission's interests and mandated school land development responsibilities are adequately represented in the Plan. As part of this effort, staffs from the Commission's Land Management and Environmental Planning and Management Divisions have participated in efforts to develop conservation actions, define development boundaries, ensure scientific integrity, and write and review draft material for consistency with the School Land Bank Act, the MOA, and other Commission policies and practices. Importantly, as required by Assembly Bill 982, participation on these groups provides Commission staff the opportunity to consult with CDFW staff to ensure land exchanges and subsequent development of school lands will be consistent with the proposed or adopted provisions of the Plan, either for their development potential or their conservation value. The exchange proposal discussed below reflects these coordination efforts and can be refined and adjusted as the DRECP moves forward to ensure this provision is satisfied.

The Commission's Mineral Resources Management Division staff has also provided expertise and guidance on the Commission's authorities and constraints related to mineral resources, including geothermal resources, that may exist in the California desert to ensure the DRECP and the land exchanges proceed in a manner consistent with Commission jurisdiction and revenue responsibilities. Finally, Commission Geographic Information Systems (GIS) and Title staffs have been able to refine and improve the Commission's mapping of school land parcels in coordination with GIS staffs from other participating agencies (see http://www.slc.ca.gov/GIS/GIS_Downloads.html). This improved mapping will not only benefit the School Land Bank generally, but will also assist in developing proposals for sale or exchange of parcels to consolidate school land ownership, consistent with the provisions of Assembly Bill 982.

Exchange Proposal

Assembly Bill 982, directed the Commission to prepare and submit, within 240 days from the execution of the MOA, "...a proposal for land exchanges that consolidate school land parcels in the California desert into contiguous holdings that are suitable for large-scale renewable energy-related projects." (Ca. Pub. Resources Code, § 8723, subd. (a)) Consistent with this direction, the Commission's Executive Officer submitted an initial proposal to the BLM on January 15, 2013. The proposal requested approximately 5,800 acres of BLM-owned lands generally located adjacent to or near existing school lands and with high potential for successful development (one parcel has an existing BLM right-of-way (ROW) authorizing use of the lands for renewable energy purposes, and several others have pending applications for renewable energy ROWs). The proposal also requested approximately 2,000 acres of BLM-owned lands in the eastern portion of the DRECP Planning Area that, while not adjacent to existing school lands parcels, are located within areas designated in the administrative draft DRECP as Development Focus Areas (DFAs) and with reasonable development potential due to low biological resource conflicts and access to transmission. Lastly, the proposal listed approximately 184,000 acres in 338 parcels of school lands and requested the BLM prioritize the list for acquisition in the exchange.

Throughout 2013, Commission and BLM staffs have been meeting regularly to refine the exchange and prioritize parcel selection. Also during this time, the design and content of the DRECP has continued to progress, allowing the exchange discussions to benefit from information related to biological resources (species, habitats, corridors), Department of Defense considerations, and access to existing or future transmission. As of December 2013, the BLM-owned “offered” lands, totaling approximately 20,000 acres, are being prioritized by Commission staff, while approximately 68,000 acres of school lands are being evaluated by BLM staff. Consistent with Assembly Bill 982 and the MOA, the BLM lands consist of parcels with a high likelihood of commercial-scale renewable energy development, and the school lands consist of the scattered inholdings located within federally protected areas, such as wilderness and national parks. The State parcels are also prioritized according to whether mineral resource evaluations have been conducted. Additionally, REAT staff has expressed a desire to include in the exchange school land parcels in areas of “high conservation priority” under the DRECP even where those parcels are not currently in wilderness designations. Commission staff anticipates these additional parcels will be added to the proposal once they are identified.

Commission and BLM staffs expect significant progress will be made in 2014 toward formalizing a binding exchange agreement. Several critical steps must be completed as part of this process, including the performance by BLM of a “value consultation” which would assess the general nature of the respective parcels and their values for feasibility, prior to moving forward with detailed environmental review and parcel appraisal. Barring unforeseen challenges or roadblocks, the exchange transaction could take place as early as 2015.

Staff resources and accounting

Assembly Bill 982 allows the Commission to use School Land Bank Fund monies for costs and expenses attributable to the exchange process and allows the Legislature to appropriate funds to reimburse the School Land Bank Fund from revenues derived from future project development. Staff coordinates with the BLM, CDFW, and other agencies as appropriate to ensure the completion of land exchanges in compliance with the new sections of the School Land Bank Act. For Fiscal year 2012-13, expenditures from the School Land Bank Fund attributable to developing the exchange proposal and conducting the necessary coordination with CDFW were \$279,745.68. Revenues resulting from leasing existing and consolidated school lands for purpose of renewable energy projects are expected to well exceed the initial costs to the School Land Bank Fund and would be deposited into the State Treasury to benefit the State Teachers’ Retirement Fund. Commission staff estimates DRECP completion in late 2014 or early 2015, and completion of the land exchange in 2015. Depending on the duration of any additional permitting and environmental review processes, within 5 to 7 years revenues benefitting the State Teachers’ Retirement Fund should realize a significant increase.